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ECONOMICS DIV.
EXH. 44

Exhibit No. _____
Application No. 59351
Witness: R. Cadenasso
ALJ: J. Haley
Date: _____

CALIFORNIA ASSOCIATION OF UTILITY SHAREHOLDERS

Prepared Testimony

and

Exhibits

of

Ross J. Cadenasso

for

Southern California Edison Company

General Rate Case

8108110704

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CALIFORNIA ASSOCIATION OF UTILITY SHAREHOLDERS

PREPARED TESTIMONY OF ROSS J. CADENASSO

1 Q. Please state your name and business address.

2 A. My name is Ross J. Cadenasso and my business address is 44
3 Montgomery Street, San Francisco, California.

4 Q. Please state your educational and professional qualifications
5 as they relate to the testimony you are about to give.

6 A. I received a Bachelor of Science degree from the University of
7 California at Berkeley, majoring in Business Administration and
8 a Master of Business Administration degree, also from the
9 University of California at Berkeley, majoring in Corporate
10 Finance and Accounting. After graduation I practiced as a
11 Certified Public Accountant for four years. I then joined the
12 investment banking firm of Blyth & Co., Inc. initially as a
13 security analyst. After one year I transferred to the Corporate
14 Finance Department of Blyth and for the next sixteen years I
15 was engaged in various corporate finance activities for that firm.

16 Q. What did you do in the Corporate Finance Department?

17 A. The last eight years I was a vice president and a first vice
18 president in the Corporate Finance Department in San Francisco.
19 My investment banking experience included working with the firm's
20 corporate clients in the raising of capital through public
21 offerings of stocks and bonds, private sales of securities to
22 institutional investors, mergers and acquisitions, and appraisals
23 of corporations. Blyth & Co., Inc. was heavily engaged in the
24 underwriting and financing of public utilities in the United
25 States and had a number of important utility clients on the
26 West Coast.

27 Q. Did you ever work on offerings of public utilities?

- 1 A. I have worked on financings for the Pacific Gas and Electric
2 Company on many occasions over a fifteen year period. I
3 worked on the initial financing of the Pacific Gas Transmission
4 Company, the pipeline company which brings natural gas to
5 California from Canada. I have also been involved in financings
6 for Portland General Electric, San Diego Gas and Electric
7 Company, Telephone Utilities Company and Alaska Electric Light
8 and Power Company.
- 9 Q. What have you done since leaving Blyth?
- 10 A. Since May of 1973 I have practiced as a Corporate Financial
11 Consultant. My activities have involved advising corporate
12 clients on matters pertaining to long term financing and
13 appraising corporate securities for various purposes.
- 14 Q. Are you a member of any professional organizations?
- 15 A. Yes. I am a member of The Security Analysts of San Francisco
16 and the Financial Analysts Federation. I am also a member of
17 the California Society of Certified Public Accountants. I
18 served as an officer and a member of the Board of Directors of
19 The Security Analysts of San Francisco.
- 20 Q. Have you had any articles published in the field of public
21 utility regulation?
- 22 A. Yes. I presented a paper before the Pacific Coast Gas Associ-
23 ation entitled "The Return Allowance" which was published in
24 the proceedings of the Association.
- 25 Q. Have you appeared as a witness in court or in administrative
26 proceedings?
- 27 A. Yes. On a number of occasions I have appeared before courts
28 and administrative agencies. I have been a witness on rate of
29 return matters before the California Public Utilities Commission

1 on behalf of The California Association of Utility Shareholders
2 in the Pacific Gas and Electric Company general rate case
3 (Application nos. 57284, 57285), San Diego Gas and Electric
4 Company general rate case (Application no. 58067) and Pacific
5 Telephone general rate case (Application no. 58223) and before
6 the Alaska Public Service Commission on behalf of the Alaska
7 Electric Light and Power Company. I have appeared as an expert
8 witness on valuation before the California Corporations Commission
9 and in the United States District Courts, the Northern District
10 of California, the State of Nevada and the State of Oregon and
11 in the Oregon Tax Court and the United States Tax Court.

12 Q. For whom are you appearing in this matter?

13 A. I am appearing for the California Association of Utility
14 Shareholders in these proceedings. Many of the Association's
15 members are shareholders of Southern California Edison Company
16 (SCE) and the Association is also a shareholder of SCE.

17 Q. Could you describe the Association for us?

18 A. The Association is a nonprofit corporation whose members are
19 shareholders of California public utility companies. The
20 Association was organized in June of 1976 and now has a member-
21 ship in excess of 9,000. The purpose of the Association is to
22 give voice to utility shareholders before regulatory agencies,
23 the State Legislature and Congress and in the news media. Our
24 aim is to see that shareholders are treated fairly by government
25 and regulatory authorities and that the interests of the share-
26 holders are protected.

1 Q. Do you hold any office in the Association?

2 A. Yes. I am president of the Association, a member of the
3 board of directors.

4 Q. What is the interest of the Association in this present
5 proceeding?

6 A. The Association is vitally interested in this Southern
7 California Edison Company general rate case. We believe that
8 SCE shareholders have suffered greatly during the past seven
9 years from unjust and inequitable treatment in previous rate
10 cases. We intend to bring before the Commission in these
11 proceedings a stockholder perspective which we hope will help
12 the Commission to arrive at a just and fair decision in this
13 case.

14 Q. Can you tell us how many shareholders own SCE shares?

15 A. The Company had about 180,000 shareholder accounts at December 5,
16 1979 including 33,000 preferred shareholders and 147,000
17 common shareholders. Of these accounts 46,000 were joint
18 accounts representing at least two shareholders. Small
19 shareholders, those owning less than 500 shares accounted for
20 91% of shareholders. (500 shares of SCE common has a current
21 market value of only \$11,000).

22 Q. Mr. Cadenasso, as a potential investor, what do you expect
23 when you make an investment in an electric utility company
24 common stock?

25 A. I would expect the company to be able to earn a fair return
26 on the stockholders' investment, a return which would be equal
27 to the return earned on stockholders' investments in other

1 enterprises of corresponding risk. I would also expect the
2 company to be able to maintain a sound capital structure and
3 a sound credit rating. If the company had to raise additional
4 equity capital to finance necessary expansion, I would
5 expect it to be able to raise capital through the sale of
6 additional shares of common stock at prices that would not dilute
7 my interest in the company.

8 Q. What gives rise to those expectations?

9 A. An electric utility company is granted a franchise by governmental
10 bodies to provide an essential public service. As a natural
11 monopoly its rates are regulated by the State. A utility is
12 permitted the opportunity to earn a fair and reasonable return
13 on its investment in utility properties under state and
14 federal statutes and under the provisions of the United States
15 Constitution. Over the years the Supreme Court of the
16 United States has laid down certain definitions of a
17 fair and reasonable return. I might quote here some of the
18 key portions of the landmark Supreme Court cases dealing with
19 fair and reasonable return: In the Southwestern Bell Telephone
20 case of 1923 the Supreme Court stated "The compensation which the
21 Constitution guarantees an opportunity to earn is the reasonable
22 cost of conducting the business. Cost includes not only
23 operating expenses, but also capital charges. Capital charges
24 cover the allowance, by way of interest, for the use of capital,
25 whatever the nature of the security issues therefor; the
26 allowance for risk incurred; and enough more to attract

1 capital." In the Bluefield Water Works case, also in 1923,
2 the Court added several more measurements of reasonableness.
3 It stated that the rate should permit a return "equal to that
4 generally being made at the same time and in the same general
5 part of the country on investments in other business under-
6 takings which are attended by corresponding risks and un-
7 certainties...The return should be reasonably sufficient to
8 assure confidence in the financial soundness of the utility and
9 should be adequate under efficient and economical management,
10 to maintain and support its credit and enable it to raise the
11 money necessary for the proper discharge of its public duties."

12 Q. Those cases were decided in 1923. Has the Supreme Court consid-
13 ered the issue since then?

14 A. Yes. In 1943 in the Hope Natural Gas case the Court reiterated
15 that "the return to the equity owner should be commensurate
16 with the returns on investments in other enterprises having
17 corresponding risks", and that "the return should be sufficient
18 to assure confidence in the financial integrity of the enter-
19 prise, so as to maintain its credit and to attract capital..."
20 These decisions continue to be recognized today as laying down
21 the three important guidelines to be used in the determination
22 of a fair and reasonable return to the owners of public utility
23 property. These are (1) the owners should be allowed an oppor-
24 tunity to earn a return which is commensurate to returns on
25 investments in other enterprises having corresponding risks,
26 (2) the return should be sufficient to maintain the financial
27 integrity and credit of the utility and (3) the return should
28 be sufficient to allow the company to attract capital.

1 Q. How much reliance do you put on the Southwestern Bell
2 Telephone, Bluefield and Hope Natural Gas cases?

3 A. I place a great deal of reliance on these landmark Supreme
4 Court decisions. The stockholders of Southern California
5 Edison Company and any other utility look to public utilities
6 commissions to fairly balance the interests of consumers and
7 investors. If a fair balance is not maintained, consumers
8 may be injured by being forced to pay higher than necessary
9 rates for public services, or shareholders of the utility
10 company can be harmed by not allowing them to earn a fair
11 return on their investment and by creating a situation that
12 results in a loss of their investment through the forced
13 dilution or confiscation of a portion of their investment.

14 Q. Why is it important to you as a shareholder that a utility
15 company be able to maintain its financial integrity and
16 credit rating?

17 A. If a utility cannot maintain its financial integrity and its
18 credit rating, the shareholders can be severely injured. In
19 the even of a default on a senior security of the company,
20 the stockholders' investment could be wiped out. Even a less
21 severe situation such as a downgrading of the quality of
22 the company's bonds and preferred stock can have an adverse
23 impact on the market price of the company's common stock to
24 the detriment of common shareholders. Obviously, any deter-
25 ioration in a company's financial position and financial
26 integrity increases risks to the common shareholder who is the

1 low man on the totem pole. It is the common shareholder
2 who has the value of his investment eroded first in a
3 deteriorating situation.

4 Q. Why is it important to a shareholder that a utility be able to
5 attract capital?

6 A. A utility company has an obligation to satisfy its customers'
7 demands for service. This means that the company must expand
8 its facilities to provide additional capacity to satisfy
9 consumer needs at all times irrespective of what conditions may
10 currently exist in the securities market. If returns are in-
11 adequate to maintain a market price at least equal to the
12 investment of existing shareholders, then new capital can only
13 be attracted by selling shares at a price below the value of the
14 existing shareholders' investment in the company. The effect
15 is that existing shareholders are compelled to give up a portion
16 of their investment to entice new shareholders to contribute
17 their money to the enterprise. This is a dilution of existing
18 shareholders interests and is brought about when the return to
19 common shareholders is inadequate in relation to risks borne
20 by shareholders.

21 Q. Is the balancing of rewards and risks an important part of
22 the regulatory process?

23 A. Yes, it is the heart of the process. If risks increase and
24 returns (another word for rewards) do not also increase
25 commensurately, the price of the stock will fall in the market-
26 place. When the price falls below the book value of existing

1 shareholders' investment per share, the utility is no longer
2 capable of attracting equity capital except on a basis which
3 is confiscatory to existing shareholders.

4 Q. How has the high rate of inflation in recent years affected
5 the risk/reward balance you speak of?

6 A. Inflation is the root cause of many critical problems facing
7 utilities in recent years. Inflation has had a major impact
8 on investors and on security values. Investors react to
9 increasing rates of inflation by demanding higher returns
10 to help compensate for the loss of real purchasing power of
11 their capital and income. This evidences itself in the decline
12 of security prices in anticipation of rising inflation. Inflation
13 also affects the earnings of companies. A regulated utility
14 is at a great disadvantage during an inflationary period
15 because it is not free to raise its prices to compensate for
16 higher costs. Its earnings fall until new higher rates are
17 authorized and put into effect. Where regulation is slow and
18 unresponsive, utility investors can be greatly harmed, not
19 only by lower rates of earnings on investment but also from
20 the dilution of their investments when new shares are sold
21 below book value. This becomes a vicious circle.

22 Q. Can you explain how this vicious circle works?

23 A. It works like this:

- 24 1. Inflation causes costs to rise. With fixed rates this
25 means that the rate of earnings on common stock falls.

- 1 2. Inflation also causes investors to demand higher returns
2 from stocks and bonds.
- 3 3. As a result of lower earnings and the demands of investors
4 for higher returns, utility stock prices drop sharply to
5 prices well below book value.
- 6 4. Inflation escalates the costs of new plants which a
7 utility is required to build to satisfy customers'
8 demands for service.
- 9 5. Internal generation of funds -- retained earnings and
10 depreciation -- provide a smaller portion of funds for
11 new plants thus requiring the sale of greater amounts of
12 stocks and bonds.
- 13 6. The sale of large amounts of bonds and preferred stocks
14 at the higher interest and dividend rates demanded by
15 investors in the marketplace causes imbedded costs of
16 senior capital to rise and correspondingly reduces the
17 return flowing to the common stock.
- 18 7. To maintain its financial integrity and credit rating,
19 the utility must sell large amounts of common stock.
20 Since common stock prices are well below book value, many
21 more shares must be sold to raise a given amount of
22 equity capital. This reduces book value and earnings
23 per share and increases downward pressure on the price
24 of the common stock. Thus the vicious circle continues.
- 25 Q. How do investors react in these circumstances?

- 1 A. First, investors tend to favor industrial stocks or other
2 forms of investment over utility stocks since in an inflationary
3 environment they perceive much greater risks associated with
4 utilities, particularly regulatory risks.
- 5 Q. What do you mean by regulatory risks?
- 6 A. This is the risk that regulatory authorities may be slow or
7 unresponsive to the changes brought about by inflation,
8 and as a result, returns to shareholders will drop to un-
9 satisfactory levels.
- 10 Q. How do the different types of investors react in an inflationary
11 environment?
- 12 A. Sophisticated investors tend to move out of utility stocks
13 and prices decline relative to industrial stocks. When
14 utility prices drop enough to compensate for the higher risks
15 associated with inflation and regulation and the lower rate
16 of earnings, the dividend yield becomes attractive to buyers,
17 particularly small investors who need higher yields to cope
18 with inflationary pressures. Thus utilities have been able to
19 sell large amounts of common stock primarily to unsophisticated
20 investors who are seeking high current yields even though the
21 rate of earnings on equity has been at depressed, low levels
22 for years. But this equity financing has been done at
23 tremendous cost to existing shareholders as I will discuss in
24 detail later in my testimony.
- 25 Q. What you are saying is that the high rate of inflation since
26 1972 has had an impact on the risk/reward relationship for

1 utilities. Is that correct?

2 A. Yes, a massive impact as risks have skyrocketed while returns
3 for many utilities have not increased significantly and, in
4 fact, at times have fallen precipitously where regulation
5 has not been responsive to these changed conditions. Such
6 situations have been a disaster for utility shareholders.

7 Q. How can this vicious circle which you described be broken
8 and a fair balance between investors and ratepayers be
9 restored?

10 A. The only way it can be broken is for returns to increase
11 significantly and for risks to diminish so that investors
12 again will be willing to buy utility stocks at prices at
13 least equal to existing shareholders' investment in the
14 enterprise, that is book value. The most important thing
15 that regulatory commissions can do is to recognize the true
16 cost of equity capital today and increase the allowed
17 rate of return on common equity by 200 to 400 basis points --
18 (2% to 4%). Commissions can also reduce risks by (1) pro-
19 viding for rate adjustments to effectively offset both financial
20 and operational attrition so that the allowed return can
21 actually be earned and (2) improving the quality of earnings
22 and cash flow by permitting the normalization of income
23 taxes and incorporating CWIP in rate base.

1 Q. You have described in general terms what has taken
2 place in recent years. Can we now get more specific with
3 respect to SCE's situation; have you made a study of
4 Southern California Edison Company's operating results
5 and the impact of these results on common stockholders?
6 A. Yes, I have prepared a number of tables and charts, all
7 of which are included with and which support the testimony
8 I am presenting. Table 1, page 39, is a ten year summary
9 of financial data of the Company and other factors
10 impacting determination of allowed return.
11 Q. Can you describe this summary and discuss the importance
12 of the data shown therein?
13 A. The tabulation first shows on lines 1 through 5 the
14 important per share financial data on the Company's
15 common stock -- average price, earnings, dividends
16 and book value. The second set of data on lines
17 6 through 8 shows the return on average common equity.
18 Line 6 shows the return found reasonable by the
19 California Public Utilities Commission in rate cases
20 since 1970. On line 7 is the actual rate of return
21 earned before adjustment for dilution. Line 8
22 shows the return adjust for dilution.

1 Q. Would you explain how the return adjusted for dilution
2 has been determined?

3 A. Yes. In computing the return adjusted for dilution, I
4 have taken into account the change in book value per share
5 caused by the sale of additional shares. When additional
6 shares are sold below book value as they have been in 1980
7 and each of the previous four years, there is a loss of
8 existing shareholders' investment in the Company. *This
9 is a very real loss which will result in lower earnings
10 and dividends in the future. This loss should be reflected
11 in his return in the year in which it occurs. You will note
12 that the difference between the adjusted and unadjusted figures
13 was insignificant up until 1974 and since then the shareholders
14 have suffered /every year except in 1975. I will discuss the
15 magnitude of dilution later in my testimony. This adjustment
16 has had the following impact on the return on average common
17 equity:

	<u>As Reported</u>	<u>Adjusted for Dilution</u>	
18			
19	1974	9.8%	6.0%
20	1975	9.8%	9.7%
21	1976	12.6%	9.0%
22	1977	12.1%	11.7%
23	1978	10.9%	7.9%
24	1979*	13.6%	7.4%*

25 * Includes dilution from sale of 7 million shares in
26 February, 1980.

1 Q. Mr. Cadenasso, would you continue to describe the material
2 shown on Table 1?

3 A. Yes. On lines 9 through 15 I show some key measurements of
4 risks. First, shown on line 9 is the average SCE common
5 stock price as a percent of average book value. This percent
6 has dropped from 116% in 1970 to 61% in 1974, increased to
7 77% in 1977 and 1978 and as of April 1980 had fallen sharply
8 to 68%. The important fact is that SCE stock has continuously
9 sold below book value since the beginning of 1973 -- over seven
10 years. When a stock sells below book value, the risk of
11 dilution when new shares are sold is great and almost certain
12 to occur. Line 10 shows the number of times interest has
13 been earned before income taxes. This ratio declined
14 from 3.1 times in 1970 to 2.7 times in 1975 and has
15 since recovered to 3.0 times in 1979. The combined after
16 tax coverage of interest and preferred dividend requirements
17 showed a drop from 2.2 times in 1970 to 1.8 times in 1974 and
18 1975 and rose to 2.1 times in 1979. Line 13 shows that the
19 Company's effective income tax rate has risen from 24% in
20 1970 to 30% in 1974 and then declined to 18% in 1979. Lines
21 14 and 15 show a significant drop in the quality of earnings
22 and the internal generation of funds to pay for construction.
23 AFDC, a noncash credit to earnings, as a percent of common
24 earnings has risen sharply from a low of 6% in 1972 to 41%
25 in 1979. Internal cash generation as a percent of construction
26 has fallen from a high of 55% in 1972 to 27% in 1979.

1 Lines 16 through 19 show other factors which impact the
2 determination of allowed return, such as, rate of inflation,
3 long term interest rates and return on equity and price/book
4 value ratios for industrial common stocks. These factors
5 will be discussed later in my testimony.

6 Q. How have SCE shareholders fared in recent years?

7 A. Very poorly. In Table 2 I have shown the total return, that
8 is dividends received and change in price of the stock, for
9 SCE shareholders who have held their shares for the past
10 2, 5, 10 and 15 years. The investor who invested his
12 retirement funds in SCE stock in 1964 has received a total
13 return of only 2.1% annually over the past 15 years.

14 After the average inflation of 6.2% annually over the 15 year
15 period is taken into account, the shareholder has had a
16 negative real return of 4.1%. The same poor results were
17 achieved by the person owning SCE stock for the past 10 years.
18 His total return was 1.4%, with an inflation rate of 7.2%
19 he ended up with a negative return of 5.8% annually. A buyer
20 of the stock in the dark days of 1974 when SCE was selling
21 at an average discount of 39% from its book value received a
22 17.5% return over the past five years when inflation averaged
23 9.2% or a positive real return of 8.3% annually. A buyer
24 of the stock in 1977 has received a total return of 7.2%,
25 but after deducting the inflation rate of 8.2% he again had
a negative return of 1.0% annually.

26 When appraising these returns, keep in mind that SCE was
27 not a dying, obsolete company but an expanding company with

1 a huge appetite for money to finance its customers' demands
2 for service -- a company that must continue to attract
3 capital to survive.

4 Q. In view of the poor returns earned by SCE shareholders, how
5 has the Company been able to attract the equity capital it
6 has required?

7 A. The Company has been able to attract equity capital by
8 selling its stock substantially below the book value of its
9 existing shareholders' investment in the Company. Over the
10 past five years new investors have received \$1.40 of book
11 value in the Company's equity for each one dollar of new
12 equity money invested. Thus by the simple expedient of
13 selling new shares at whatever price the market dictates,
14 the Company's inadequate returns have been transformed into
15 returns high enough to attract new equity capital.

16 Q. Does not selling stock below book value hurt existing
17 shareholders?

18 A. Of course it does. Table 3 shows the dilution of existing
19 shareholders' investment from the sale of new stock below book
20 value over the past five years. The Company has sold a total
21 of 23,033,000 shares in this five year period or 49% of the
22 total shares outstanding at the beginning of the period.
23 These shares were sold for \$542 million or 28.5% below their
24 book value. The total dilution suffered by existing shareholders
25 was \$216 million which equalled 14.5% of the total common
26 stockholders' equity in the Company at the beginning of this

1 five year period. In other words, the old shareholders had
2 \$216 million taken away from them and given to new shareholders
3 to entice them to buy stock in the Company which was earning
4 inadequate profits.

5 Q. How has SCE met the Supreme Court's attraction of capital
6 test over the past five years?

7 A. It has not. The Company could not sell one single share of
8 its stock for a price equal to the investment in the Company
9 of its existing shareholders at any time over the past seven
10 years. It could only sell its shares at discounts ranging
11 from 22% to 35% below book value, and it is these discounted
12 prices which attracted the equity capital, not the so-called
13 "fair" return it was earning.

14 Q. Some people say that as long as a company can sell its
15 shares, regardless of price, it is meeting the attraction
16 of capital test. Do you agree?

17 A. No, but I have heard even public utility commissioners make
18 such statements. That reasoning in my opinion, is a complete
19 perversion of the Supreme Court's attraction of capital test --
20 it makes the test meaningless.

21 Q. Have not the regulators justified their allowed returns on
22 equity by claiming they are balancing the interests of
23 customers and shareholders?

24 A. Yes, when the hard evidence is ignored and allowed returns
25 are rationalized under the guise of balancing customer and
26 shareholder interests almost any return can be justified.
27 Such ignorance of hard evidence can result in ridiculous
28 situations. For example, in the recent Pacific Telephone

1 general rate case decision, the Commission, giving weight to
2 the Staff's and GSA's expert testimony, allowed a 12.25%
3 return on equity. Within seven months after the decision,
4 the company sold its senior bonds at a 15.7% cost, to the
5 company -- nearly 350 basis points higher than the allowed
6 return on its common equity!

7 Q. Do you have any hard evidence which has a bearing on the
8 balancing of customer and shareholder interests?

9 A. Yes. Chart 1 shows six pertinent factors which illustrates
10 how SCE customers' and shareholders' interests have been
11 balanced since 1970. The cost of living, which affects
12 both customers and shareholders, has risen 84% since 1970.
13 Californians have been able to more than keep up with this
14 inflation. Their per capita disposable personal income has
15 risen by 125% since 1970 and after adjusting for inflation,
16 it has risen 21% in real terms. SCE shareholders have not
17 been so lucky. Their dividends have risen 81% since 1970,
18 or only 3% below the increase in the cost of living. This
19 is a good performance when considered alone. Increased
20 dividends, however, were due, in part, because of a higher
21 dividend payout policy in recent years. This is evidenced
22 by earnings increasing only 59% or a decline of 8% in real
23 terms and book value increasing only 34% or a decline of
24 27% in real terms. While higher dividend payments caused a
25 lesser increase in book value than in earnings, the major cause
26 was dilution from the sale of a huge number of shares below

1 book value.

2 The price of SCE stock has declined about \$5.50 per share or
3 19% since 1970 in absolute terms but when adjusted for
4 inflation the decline is a staggering 56%! This large decline
5 in market value is due in large measure to the sharp rise in
6 returns demanded by investors in the market place because of
7 accelerating inflation. When returns earned by a company
8 on its equity do not increase in line with the higher cost
9 of equity capital, stock prices decline. The market is the
10 mechanism by which a purchaser of SCE stock today is able to
11 achieve the going market rate on his investment because he
12 acquires about \$1.50 of book value in the Company for each
13 dollar he invests. Thus his return is 1.5 times the return
14 the Company is earning on its shareholders' investment.

15 It is this tremendous gap between the returns demanded by
16 the market and the returns actually earned by the Company
17 that must be closed before we can end the present seven year
18 era of dilution and confiscation.

19 I think these figures clearly show that there has been a
20 great imbalance between customers' and shareholders' interests
21 in recent years and as a consequence, shareholders of SCE have
22 suffered tremendous losses that can never be recouped.

23 Q. How can this imbalance be corrected and a fair balance
24 established between customers' and shareholders' interests?

25 A. The imbalance can be corrected if we acknowledge the
26 realities of the high inflation environment we are in now,
27 have been in since 1973 and undoubtedly will be in during the
28

1 period in which rates established in these proceedings will
2 be in effect. That means that we must look at the hard
3 evidence of the past seven years -- not the soft evidence of
4 some Staff member's opinion supported only by an allegation
5 that customer and shareholder interests are balanced; not by
6 wishful thinking that inflation will some how disappear; not
7 by looking at a mass of comparative data on other utilities
8 whose shareholders have suffered fates similar to those
9 suffered by SCE shareholders.

10 Q. What sort of hard evidence should we be looking at?

11 A. First, we must consider the historical inflation rate and
12 its impact on the returns investors demand in the marketplace
13 and how the CPUC has responded to these changes in the past.
14 Charts 2 and 3 show that since 1970 the rate of inflation
15 has risen 120%, long term bond yields have risen 69%, and
16 investors have demanded 101% to 128% more earnings on their
17 common stock investments as measured by earnings/price
18 ratios. The earnings/price ratios of SCE common stock has
19 increased 110%, Moody's Electric Stocks 101% and S & P 400
20 Industrial Stocks 128% since 1970. Contrast this to the
21 14% increase in the CPUC allowed return on equity to SCE
22 from 11.79% in 1970 to 13.49% in 1980. This tremendous
23 disparity is the prime reason why SCE common stock is currently
24 worth only 68% of shareholders' investment in the Company and
25 why the stock has sold continuously below book value since 1972.
26 It should be obvious that the allowed return must be increased
27 substantially to make up for the past inadequacies.

1 Nevertheless, the staff has recommended a 13.6% allowed
2 return in this case which is slightly above the 13.49% rate
3 of return allowed in the last general rate case -- a return
4 which has proven so inadequate in the 1979 test year of that
5 case.

6 Q. It has been said that the CPUC does not control the market
7 price of the stocks of companies it regulates; their concern
8 is with the return earned on investment in utility properties.
9 Do you agree?

10 A. No, the CPUC has a tremendous influence on the market price
11 of the stocks of companies it regulates. Market price is
12 primarily determined by the return earned on investment and
13 this is under the control of the CPUC. In addition, the
14 CPUC has a responsibility to see that the utility is able
15 to attract capital on a reasonable basis (nonconfiscatory
16 basis) to enable it to discharge its franchise obligations.
17 Thus the market price of a utility's stock should be of central
18 concern to public utility commissioners. When a utility's
19 stock starts to sell below book value, a regulator should
20 recognize this as a serious problem and respond by taking
21 actions to correct such a situation. Unfortunately for
22 California utility shareholders, the CPUC response has been
23 consistently too little, too late and as a consequence all
24 of California's major utility stocks have sold below their
25 book values continuously since early 1973.

26 Q. How have utilities fared in other jurisdictions?

1 A. While some other states have had records similar to California,
2 in many states utility stocks have sold above book value at
3 various times since 1973 and some equity financing has been
4 done on a nonconfiscatory basis. At the present time, however,
5 there is practically no utility in the entire nation that
6 can raise equity capital on a nonconfiscatory basis.

7 The only exceptions are where the utility has nonregulated
8 earnings from oil and gas production or some other source.
9 This is why using returns of comparable utilities to establish
10 allowed returns is meaningless at this time except to explain
11 why utility stocks are selling below book value. We must
12 study the returns earned by nonregulated companies and
13 companies whose stocks are selling above book value in order
14 to arrive at a fair return for utility shareholders.

15 Q. How have allowed returns and returns earned by SCE compared
16 with those of nonregulated companies during the inflationary
17 period since 1970?

18 A. Chart 4 shows the return on average common equity earned by
19 SCE and S & P Industrial Companies and compares these to the
20 return allowed SCE by the CPUC. In 1979 industrial companies
21 increased their average return to 16.8%, a 62% increase over
22 1970. SCE's return increased 21% since 1970 to 13.6% last
23 year. When dilution from the sale of 7 million shares in
24 early 1980 is recognized, the true return in 1979 to SCE
25 shareholders was 9.4% or 44% below the average return earned
26 by the S & P 400 Industrial Companies and 30% below the
27 CPUC's allowed return. The allowed return increased only
28 14% since 1970 and was 20% below the return on industrial
29 stocks in 1979.

1 Q. You have just reviewed the returns earned on equity and the
2 returns demanded by investors in the marketplace since 1970.
3 How do you tie these two factors together?

4 A. They are tied together by the price/book value ratio where we
5 relate the price of a stock with its book value. This is
6 a key ratio since it is influenced by the rate of earnings
7 on equity and by the returns demanded by investors in the
8 marketplace. Chart 5 shows price/book value ratios since
9 1970 for SCE, Moody's Electrics and the S & P 400 Industrial
10 Companies. The average price of SCE stock in 1970 was
11 116% of book value, it declined to 103% in 1972 and then
12 plunged steeply below book value beginning in 1973 and has
13 remained there ever since. Between 1974 and 1980 the stock
14 has fluctuated between 61% and 77% of book value and currently
15 is at 68% of book. The price/book ratio of Moody's Electrics
16 showed a similar pattern; however, it was slightly higher than
17 SCE from 1970 through 1978 and has been slightly lower in 1979
18 and 1980. While the price/book value ratio of industrial
19 companies has also declined, it has remained over book value
20 and is currently at 116% of book value. This indicates that
21 investors are willing to pay more than book value for the
22 average industrial company stock because earnings have risen
23 along with inflation. So even though investors have demanded
24 a higher return (as witnessed by rising earnings/price ratios)
25 because of inflation, the average industrial company has been
26 able to increase its earnings sufficiently to give the investor
27 this higher return at stock prices above book value. On the
28 other hand, SCE and almost all other utilities have not been

1 able to increase returns sufficiently to satisfy investors'
2 demands for a higher return, and, therefore, investors will only
3 pay an average of less than 70 cents on the dollar for SCE and
4 electric utility common stocks generally today.

5 Q. Would a return equal to the return earned by S & P 400
6 Industrial Companies in 1979 be enough to make investors pay
7 at least book value for SCE common stock at this time?

8 A. No, at the present time, I do not think a return of 16.8% would
9 be enough to make SCE stock sell above book value. If we
10 look at Chart 3, you will notice that investors have consistently
11 demanded higher returns from utility stocks since 1970
12 because they perceive greater risks associated with ownership
13 of utility stocks than with the ownership of the average
14 industrial stock.

15 Q. Have investors always considered utility stocks more risky
16 than the average industrial stock?

17 A. No, back in the late 1950's and early 1960's when inflation
18 was at a low level, investors at times paid higher prices
19 for utility stocks than for industrial stocks, but this
20 changed when inflation accelerated in the last half of the
21 1960's and during the 1970's. Investors have rightly
22 appraised the relatively greater risks of utility stocks
23 in recent years. During inflationary periods, utilities
24 are highly risky businesses. Consider some of the risks
25 unique to electric utilities which their shareholders must
26 bear at this time:

27 1. Regulatory lag and attrition which have prevented
28 utilities from earning their allowed returns during the
29 past five to seven years.

- 1 2. Inability of utility managements to increase rates of
2 return to compensate for inflation except to the extent
3 relief may be granted by governmental bodies subject
4 to all sorts of political pressures from hard pressed
5 consumer groups.
- 6 3. The risk of being forced to raise capital to finance
7 franchise obligations when the utility's stock is selling
8 below book value thereby confiscating a portion of
9 existing shareholders' investment in the company.
- 10 4. The financial risks associated with nuclear plants.
11 These huge projects which involve a substantial portion
12 of stockholders investment, may be subject to long
13 delays before being placed into service and once in
14 service may be removed from service at any time for
15 modifications because of changing technical, political,
16 environmental and economic considerations. When such
17 changes take place there is great political pressure
18 to make shareholders absorb losses even though they have
19 never been compensated with higher returns to assume the
20 unusual risks associated with these huge projects.

21 Q. How can the CPUC reduce the unusual risks now being borne
22 by utility shareholders?

23 A. These unusual risks can be reduced by:

- 24 1. Putting in place a regulatory system that can cope with
25 today's fast changing inflationary environment -- a system
26 that can adjust rates quickly to cover swiftly rising
27 costs so that the utility will be able to recover from

1 ratepayers the legitimate costs of providing service
2 including the return allowed on shareholders' investment.

- 3 2. Allow returns to rise to the level necessary to make
4 utility stocks again worth as much as shareholders'
5 investment in them. In other words, increase returns
6 on equity so that the shares will be selling above book
7 value and thereby put an end to the seven year period
8 of dilution and confiscation which has plagued the
9 industry, especially in California.

10 Q. Are you advocating reducing risks to utility shareholders to
11 below the level of risks borne by the shareholders of
12 the average industrial company?

13 A. No, I am suggesting that the unusual risks unique to utilities,
14 which are related to inflation, be lowered. Such risks as
15 regulatory lag, attrition and forced dilution are not borne
16 by industrial company shareholders.

17 Q. Assuming your suggestions to reduce risks are implemented,
18 what rate of return on common equity must SCE have to meet
19 the Supreme Court's criteria of a fair return?

20 A. A return on common equity of between 17% and 18% would be
21 required to meet the Supreme Court's comparative earnings
22 standard if we make the assumption that common shareholders
23 of the average industrial company and SCE shareholders are
24 bearing corresponding risks. I believe it is safe to say
25 that SCE shareholders bear at least as much risk as the
26 average industrial company shareholder. Chart 3 indicates
27 that investors have consistently demanded higher earnings

1 returns from SCE and electric utility stocks generally than
2 from industrial company stocks since 1970. These investors
3 have, in fact, perceived greater risks to electric utility
4 shareholders in recent years. But to be conservative, let
5 us assume the risks are equal. SCE shareholders, therefore,
6 should have an opportunity to earn as much on their investment
7 as the average industrial company shareholder in order to
8 meet the comparative earnings standard set forth in the
9 Hope case.

10 The average return on common equity of nonutility corporations
11 was 17.4% in 1979. The March 17, 1980 edition of Business
12 Week (page 116) reported average returns on common equity of
13 16.6% for 1,200 corporations in 1979. This tabulation
14 included 83 utilities with average returns of 12.8%. If
15 the utilities are removed from the total, the average return
16 for the remaining 1,117 nonutility corporations was 17.4%
17 on common equity in 1979.

18 It should also be noted that this Business Week tabulation
19 clearly shows the grave national problem facing utilities.
20 Average returns of utilities were 26% below those of non-
21 utility companies in 1979. Nevertheless, utilities must
22 compete in the capital markets for huge amounts of equity
23 capital. The only way this capital is being obtained today
24 is by massive confiscation of utility shareholders' investment.
25 We cannot expect this situation to continue indefinitely.
26 We are asking the CPUC to take leadership in solving this
27 national problem, and they can by their decision in this case

1 and in the pending Southern California Gas Company general
2 rate case.

3 Q. What return is required to meet the Supreme Court's
4 attraction of capital test?

5 A. In general terms it is a return which would make SCE common
6 stock attractive enough to investors to make them want to pay
7 at least book value for the shares during the period in
8 which the rates set in this case are to be in effect. If
9 the price of the Company's stock does not increase to book
10 value, then dilution will continue through 1982, and we will
11 have witnessed a full decade of dilution and confiscation.
12 The Company will, no doubt, continue to attract equity capital
13 but only by the discounted price at which it will sell its
14 shares, not because of a "fair return" earned on its equity.

15 Q. How do we get the price of its shares up to book value?

16 A. By increasing the return on equity substantially above the
17 present allowed level which has proven to be woefully
18 inadequate this past year as inflation has accelerated and
19 returns on stocks and bonds in the marketplace have risen
20 sharply.

21 Q. What rate of return on equity is necessary today for SCE stock
22 to sell for book value?

23 A. I would estimate that a return of around 20% would be required.
24 The earning/price ratio for the Company's stock is presently
25 20%. The Company just sold its first mortgage bonds at a
26 cost of 15.36% and if we add the 5% to 6% risk premium for
27 common stock, a cost of equity to the Company of between

1 20% and 21% is indicated. With SCE stock now selling at
2 68% of book value, investors are acquiring \$1.47 of book equity
3 for each \$1 invested. Their return based on the 13.6%
4 actually earned on equity in 1979 is 20% ($1.47 \times 13.6\%$).

5 Q. Does not the current market represent an extreme high point
6 in interest rates and stock returns historically?

7 A. We have witnessed a dramatic acceleration in the inflation
8 rate in recent months and it is now approaching 20% annually.
9 Investors have raised their long term inflationary expectations
10 sharply as witnessed by the steep rise in long term bond
11 yields to the 14% to 16% area. Bank prime lending rates are
12 now 20%. All of these rates are at all time highs. Who
13 can say what rates will be in 1981 and 1982 when the rates set
14 in this case will be in effect. We are in uncharted waters.
15 As one student of the money market recently remarked: "We
16 have never played this ballgame before." In the past the
17 Commission and Staff have tended to assume rates will retreat
18 to lower historical levels. Such wishful thinking has proven
19 incorrect as the trend of each cycle has been higher than
20 the previous one. I don't believe we can again deprive
21 shareholders of a fair return by wishfully thinking that rates
22 are going to go back to the levels of several years ago.
23 There is, of course, the possibility of a decline from current
24 levels. There is also the possibility of further increases.

25 Q. Are you suggesting that current market conditions be used
26 to determine the fair rate of return in this case for test
27 year 1981 and 1982?

1 A. While I have no basis for predicting a substantial drop in
2 long term interest rates and return on equity expected by
3 investors, I am, nevertheless, basing my recommended allowed
4 return in this case assuming a substantial reduction in the
5 rate of inflation and long term interest rates from present
6 levels, and not on the higher returns that have prevailed so
7 far in 1980. This may prove to be an entirely too optimistic
8 assumption as far as shareholders are concerned, but I
9 believe this assumption will definitely not be unrealistically
10 high at the time a decision must be made in this case

11 Q. How did you determine that a 17% return is necessary for SCE
12 to meet the attraction of capital test?

13 A. The 17% return figure is supportable on the basis of the
14 current earning level of nonutility companies referred to
15 previously. With industrial stocks earning this rate of
16 return, investors are currently paying on average more than
17 book value for their shares. Unfortunately all electric
18 utilities are now selling below book value and earning less
19 than 17% on equity. Therefore, we cannot test the adequacy
20 of a 17% return for utilities in today's market. Investors
21 have consistently demanded higher returns from utility stocks
22 than from industrial stocks over the last decade and this
23 indicates that a return higher than 17% would be required.
24 I am anticipating, however, some improvement in the capital
25 markets from present levels and believe such improvement would
26 permit a utility stock to sell above book next year if it

1 earned a 17% return.

2 With respect to SCE we must recognize that investors
3 perceive more risk in this stock than in the average electric
4 utility stock because of SCE's current and future heavy
5 dependence on nuclear power generation. Since the Three
6 Mile Island problem, which commenced March 30, 1979,
7 investors are demanding greater returns from nuclear utilities
8 to compensate for greater risks. This shift in investors'
9 attitudes shows up clearly when we compare SCE's price/earning
10 ratios to those of the average electric utility since the end
11 of 1978. This is shown below:

12 Price/Earnings Ratios

13		<u>Median</u> <u>100 Electrics (a)</u>	<u>SCE</u>	<u>SCE as %</u> <u>of Median</u>
14	12/29/78	7.4x	8.1x	109%
15	3/30/79	7.4x	7.5x	101%
16	6/29/79	7.3x	6.3x	86%
17	9/28/79	6.9x	6.3x	91%
18	12/31/79	6.5x	5.4x	83%
19	2/29/80	5.9x	4.7x	80%

20 (a) Source: Electric Utility Common Stock Market Data,
21 Salomon Brothers.

22 So when I recommend a 17% return on equity for SCE, I am
23 clearly anticipating a very significant improvement in capital
24 markets from current levels. Of course, inherent in the
25 assumption that interest rates are going to fall is also the

1 assumption that a recession will hit our economy. This
2 could hurt SCE earnings since revenues are likely to fall
3 faster than expenses during a recession.

4 Q. Suppose long term interest rates drop 300 to 400 basis
5 points and suppose SCE were granted an allowable return of
6 17% on common equity. Would the price of its stock sell
7 way above book value?

8 A. If rates in fact decline 300 to 400 basis points and SCE were
9 to actually earn 17% on equity, I doubt that during the time
10 new rates are in effect in 1981 and 1982 the price of SCE
11 stock would be significantly above book value. Investors
12 will first want to be shown that the Company can actually
13 earn an allowed rate of 17%. If this is achieved in 1981,
14 investors then will want to see if the Company will get rate
15 adjustments at the start of 1982 to offset attrition so that
16 17% can actually be earned in the year following the test
17 year. At that time, if investors feel fairly confident that
18 17% will be earned in 1982, the stock may well sell above
19 book value assuming the 300 to 400 basis points decline in
20 long term bond yields.

21 Q. If that were the case, would it not be unfair to ratepayers?

22 A. If such a situation materialized, I do not think any fair
23 minded person could reach that conclusion. After SCE's
24 common stock has sold continuously at discounts of 20%
25 to 40% below book for the past seven long years, when share-

1 holders have suffered massive dilutions of their investment.
2 a brief period when the stock sells above book could hardly
3 be considered an undeserved windfall to shareholders.

4 Q. What is your recommended return on average common equity
5 for SCE in this case?

6 A. I recommend that the allowed return on average equity be
7 not less than 17%, provided that provision is made to
8 adjust rates at the beginning of the year following the
9 test year for financial and operational attrition, so that
10 the Company will have a fair opportunity to actually earn
11 this allowed return in 1982.

12 Q. Your 17% recommendation represents a big jump from the present
13 allowed rate of 13.49%, the Staff's recommended rate of
14 13.6% in this case and even from the Company's requested
15 rate of 15% in this case. Why are you recommending a rate
16 so much higher?

17 A. Anything less would not meet the standards set by the
18 Supreme Court in my opinion and would assure that the con-
19 fiscation of existing shareholders' equity would continue
20 for another three years. The present 13.5% allowed rate
21 has been proven entirely inadequate. The Company actually
22 earned slightly more than 13.5% in 1979, the test year for
23 their last rate case, however, the price of its stock has
24 never sold above 83% of its book value since the last
25 general rate case decision was handed down in December 1978.
26 Experience and hard evidence in the marketplace have proven
27 that the 13.5% allowed return in the last rate case should

1 have been at least 15% and probably higher. My 17%
2 recommendation reflects the worsening inflation rate since
3 the previous rate case decision.

4 The Company's requested return of 15% was developed in
5 the fall of 1979 before the recent sharp acceleration in
6 inflation and the big jump in long term interest rates and
7 long term inflationary expectations. The Company's 15%
8 request was based on an analysis of conditions prevailing
9 from 1974 through 1978. At this time, in my opinion, it is
10 not realistic to expect that during test year 1981, inflation
11 rates and the money and financial markets will return to
12 the average of levels prevailing in the 1974-78 period.

13 Q. What would the composite cost of capital be to SCE in 1981
14 using your 17% recommended return on common equity?

15 A. The composite cost of capital would be 12.02%. Table 4
16 shows the computation of this figure. It is based on the
17 capital ratios contained in the Company's and Staff's cost
18 of capital studies and the estimated cost of senior capital
19 for 1981 contained the testimony of H. Fred Christie on
20 April 2, 1980.

21 Q. What is the total interest coverage under your recommended
22 composite cost of capital?

23 A. 2.90 times for test year 1981.

24 Q. Is 2.90 times an adequate coverage ratio?

25 A. I believe it is if the Commission makes an adequate provisions
26 for attrition in its decision so that the Company will have

1 an opportunity to actually earn its authorized return in
2 1982. In other words, I believe my recommended rate of
3 return will meet the Supreme Court's third test of a fair
4 return, that is, a return which will be sufficient to maintain
5 the financial integrity and credit of the Company.

6 Q. What would be the cost to ratepayers of providing a 17%
7 return on equity compared with the 13.6% recommended by the
8 Staff?

9 A. Approximately \$135 million which would represent a 3.6% increase
10 in CPUC jurisdiction revenues. This would increase the
11 average customer's bill by approximately \$1.80 per month.
12 A small price to pay for reestablishing a fair balance
13 between ratepayers and shareholders -- a balance which has
14 not existed for eight years.

15 Q. How do you suggest attrition be handled?

16 A. In the three previous general rate cases we have participated
17 in, we have called attention in our prepared testimony
18 to the need to provide for attrition in the year following
19 the test year. The two year cycle for general rate cases
20 under the Commission's Regulatory Lag Plan makes this necessary
21 particularly in our inflationary environment. In the PG&E
22 Decision No. 89316, dated September 6, 1978, the Commission
23 did not discuss our suggestion for handling attrition. In
24 subsequent decisions it has given partial recognition to
25 attrition and in the most recent PG&E decision we were
26 pleased to read Mr. Bryson's opinion urging the Commission

1 to focus on the problem of both financial and operation
2 attrition. We are also pleased to see that Staff has recommended
3 an attrition adjustment to curve both financial and operational
4 attrition to be effective at the beginning of 1982.

5 In a period such as the present when we are witnessing
6 accelerating inflation and swiftly rising cost of senior
7 capital, it is imperative that any general rate decision
8 be based on the most current data and fair and reasonable
9 estimates of test year expenses and must provide for ad-
10 justments to rates to cover attrition at the beginning of
11 the year following the test year. I believe it is preferable
12 to have an interim adjustment based on conditions prevailing
13 at the end of the test year than to try to guess the impact
14 of attrition in 1982 at the time a decision is rendered on
15 this case in the latter part of 1980.

16 In this regard, I do not agree with the Staff's proposal to
17 place a ceiling on the attrition allowance. To do so is
18 dangerous in these fast changing times and may tend to defeat
19 the purpose of the adjustment, that is, to give the Company a
20 fair opportunity to earn its allowed return. Who can
21 accurately estimate attrition two years ahead when inflation
22 is currently raging at nearly a 20% annual rate?

23 If we can agree that fair treatment of shareholders requires
24 that rates be adjusted at the beginning of the year following
25 the test year so that the Company will have a reasonable
26 opportunity to earn its allowed return in 1982, I think
27 that is sufficient. The Commission should clearly state

1 in its decision that it intends to adjust rates at the
2 beginning of 1982 so that the Company will have a fair
3 opportunity to earn its allowed return in 1982. This would
4 have a beneficial impact on the Company's stock.

5 Q. Does this conclude your testimony?

6 A. Yes.

TABLE 1
SOUTHERN CALIFORNIA EDISON COMPANY
TEN YEAR RECORD OF COMMON STOCK DATA
AND FACTORS IMPACTING DETERMINATION OF ALLOWED RETURN
1970-1980

LINE NO.		1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	April 1980
<u>PER COMMON SHARE DATA</u>												
1	Average of high and low price	28.00	30.49	27.45	22.90	17.25	19.15	21.00	24.20	24.95	25.44	22.62
2	Earnings	2.70	2.46	2.51	2.67	2.80	2.86	3.30	3.60	3.52	4.56	
3	Dividends declared	1.50	1.515	1.56	1.56	1.68	1.68	1.68	2.06	2.30	2.60	
4	Book Value, year end	24.72	26.20	27.14	28.46	28.50	29.64	30.67	32.30	32.57	34.22	33.07b
5	Book Value, average begin & end of year	24.13	25.46	26.67	27.80	28.48	29.07	30.16	31.49	32.44	33.40	
<u>RETURN ON AVERAGE COMMON EQUITY</u>												
6	Found fair & reasonable by CPUC (weighted average) Actually earned, per share:	11.79%	11.79%	11.9%	12.25%	12.25%	12.25%	12.65%	12.65%	12.65%	13.49%	
7	Before adjustment for dilution	11.2%	9.7%	9.4%	9.6%	9.8%	9.8%	12.6%	12.1%	10.9%	13.6%	
8	After adjustment for dilution (a)	11.2%	11.5%	9.4%	9.6%	6.0%	9.7%	9.0%	11.7%	7.5%	9.42b	
<u>MEASUREMENTS OF RISK</u>												
9	Average common price as % average book value	116%	119%	103%	82%	61%	66%	70%	77%	77%	76%	68%
Coverage ratios:												
10	Times interest earned before taxes	3.1X	3.0X	3.0X	3.0X	3.0X	2.7X	2.9X	2.9X	2.7X	3.0X	
11	Times interest earned after taxes	2.6X	2.5X	2.5X	2.5X	2.4X	2.4X	2.6X	2.6X	2.4X	2.7X	
12	Times interest and pref. div. earned after taxes	2.2X	2.0X	2.0X	1.9X	1.8X	1.8X	2.0X	2.0X	1.9X	2.1X	
13	Effective income tax rate	24%	24%	25%	25%	30%	20%	19%	18%	17%	18%	
14	AFDC as percent of common earnings	15%	15%	6%	9%	13%	20%	26%	29%	39%	41%	
15	Internal cash generation as % construction (c)	43%	45%	55%	47%	46%	39%	36%	35%	26%	27%	
<u>OTHER FACTORS IMPACTING DETERMINATION OF ALLOWED RETURN</u>												
16	Inflation rate	5.9%	4.3%	3.3%	6.2%	11.0%	9.1%	5.8%	6.8%	7.7%	8.9%	13.0%
17	Long Term interest rates (Moody's Util.AA)	8.52%	8.00%	7.60%	7.72%	9.04%	9.44%	8.92%	8.43%	9.10%	10.77%	14.44%
18	S&P 400 Industrials - return on avg. common equity	10.4%	11.2%	12.0%	14.6%	14.8%	12.3%	14.5%	14.7%	15.3%	16.8%	
19	S&P 400 Industrials- Avg. stock price as % avg.book value	171%	199%	216%	196%	139%	133%	150%	138%	125%	123%	116%

(a) Dividends paid plus net change in book value per share as percent of average common equity.

(b) Reflects sale of 7 million shares on 2/5/80 at 34.5% discount from book value.

(c) Net income to common plus depreciation minus AFDC minus common dividends divided by construction expenditures.

TABLE 2
 TOTAL RETURN TO SOUTHERN CALIFORNIA EDISON SHAREHOLDERS
 OVER LAST 15 YEAR, 10 YEAR, 5 YEAR AND TWO YEAR PERIODS

LINE NO.	Holding Period			
	1964 to 4/80 (a)	1969 to 4/80 (b)	1974 to 4/80 (c)	1977 to 4/80 (d)
1	15	10	5	2
2	\$34.50	\$34.40	\$17.25	\$24.20
3	22.62	22.62	22.62	22.62
4	(11.88)	(11.78)	5.37	(1.58)
5	25.44	18.82	11.00	5.58
6	1.67	1.84	2.10	2.48
7	Total average annual return to shareholders:			
8	(2.7%)	(4.0%)	5.3%	(3.0%)
9	4.8%	5.4%	12.2%	10.2%
10	2.1%	1.4%	17.5%	7.2%
11	6.2%	7.2%	9.2%	8.2%
12	(4.1%)	(5.8%)	8.3%	(1.0%)

(a) Average of high and low price for year.

TABLE 3
SOUTHERN CALIFORNIA EDISON
DILUTION INCURRED BY SALE OF COMMON STOCK BELOW BOOK VALUE
1976-1980(a)

LINE NO.	1976-1980(a)					TOTAL	
	1976	1977	1978	1979	1980	1976-1980 (a)	
1	Number of shares sold (000)	5,644	966	7,472	1,951	7,000	23,033
2	Net proceeds (000)	\$123,951	\$23,742	\$188,842	\$48,174	\$156,975	\$541,683
3	Book Value per share before offering	\$31.25	\$31.49	\$32.87	\$33.40	\$34.22	
4	Net proceeds per share	\$21.96	\$24.58	\$25.27	\$24.69	\$22.39	
5	Dilution per share (3) - (4)	\$9.29	\$6.91	\$7.60	\$8.71	\$11.83	
6	Total dilution (000)	\$52,432	\$6,677	\$56,787	\$16,993	\$82,800	\$215,689
7	Net proceeds percent below Book Value	29.7%	21.9%	23.1%	26.1%	34.6%	28.5%
8	Additional shares sold because of dilution:						
9	Percent	42.3%	28.1%	30.1%	35.3%	52.6%	39.9%
10	Number (000)	1,678	212	1,727	509	2,413	6,539

(a) Through February 1980.

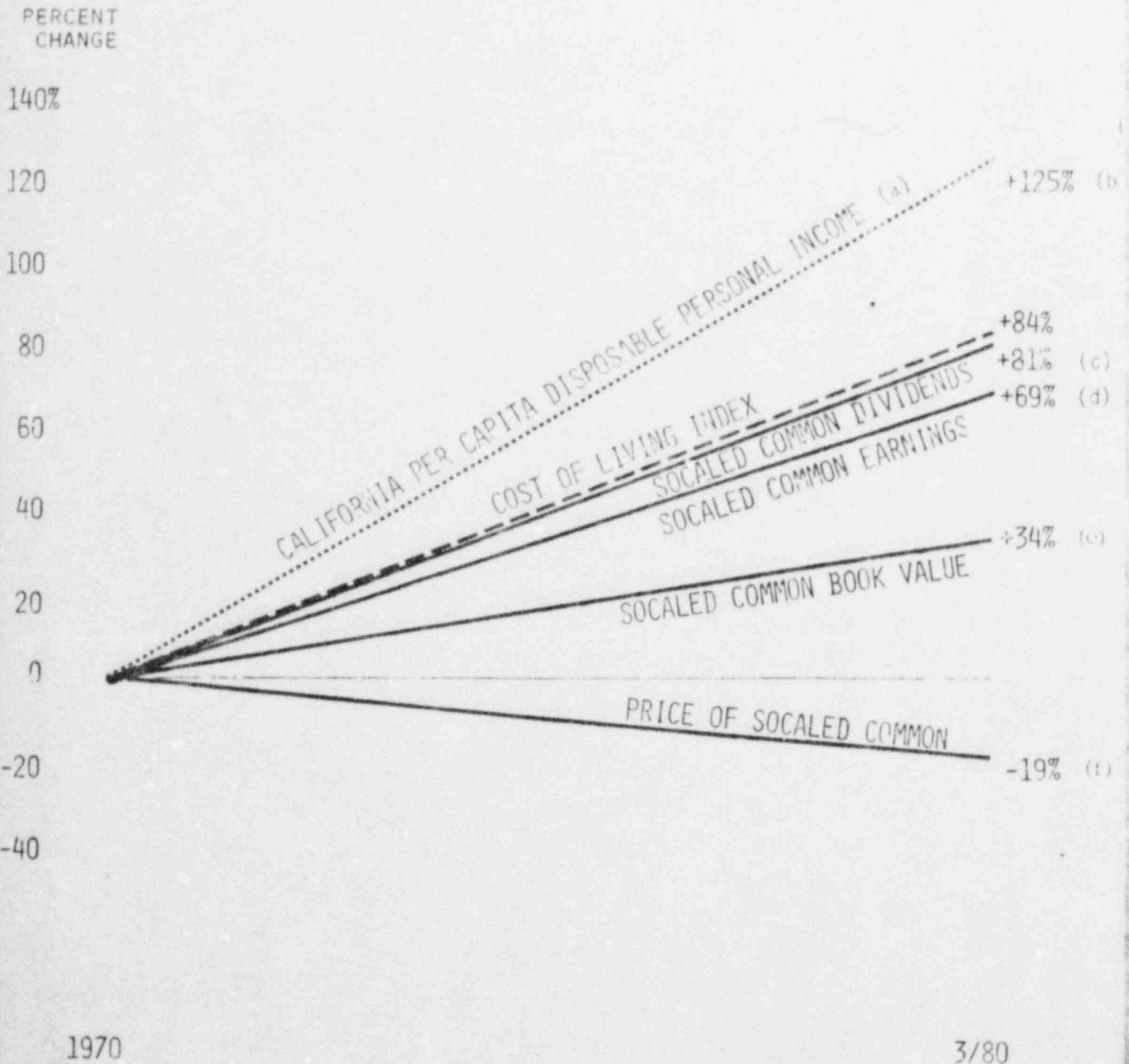
TABLE 4

COMPOSITE COST OF CAPITAL BASED
ON RECOMMENDED RETURN ON COMMON EQUITY
TEST YEAR 1981

(a)	Capital Ratio	Cost Rate	Return Component
	(b)	(c)	(d)
1. Long-term debt	47.0%	8.82%*	4.15%
2. Preferred stock	13.0	8.21*	1.07
3. Common equity	40.0	17.0%	6.80
4. Total capital	<u>100.0%</u>		<u>12.02%</u>
5. Times interest earned			2.90X

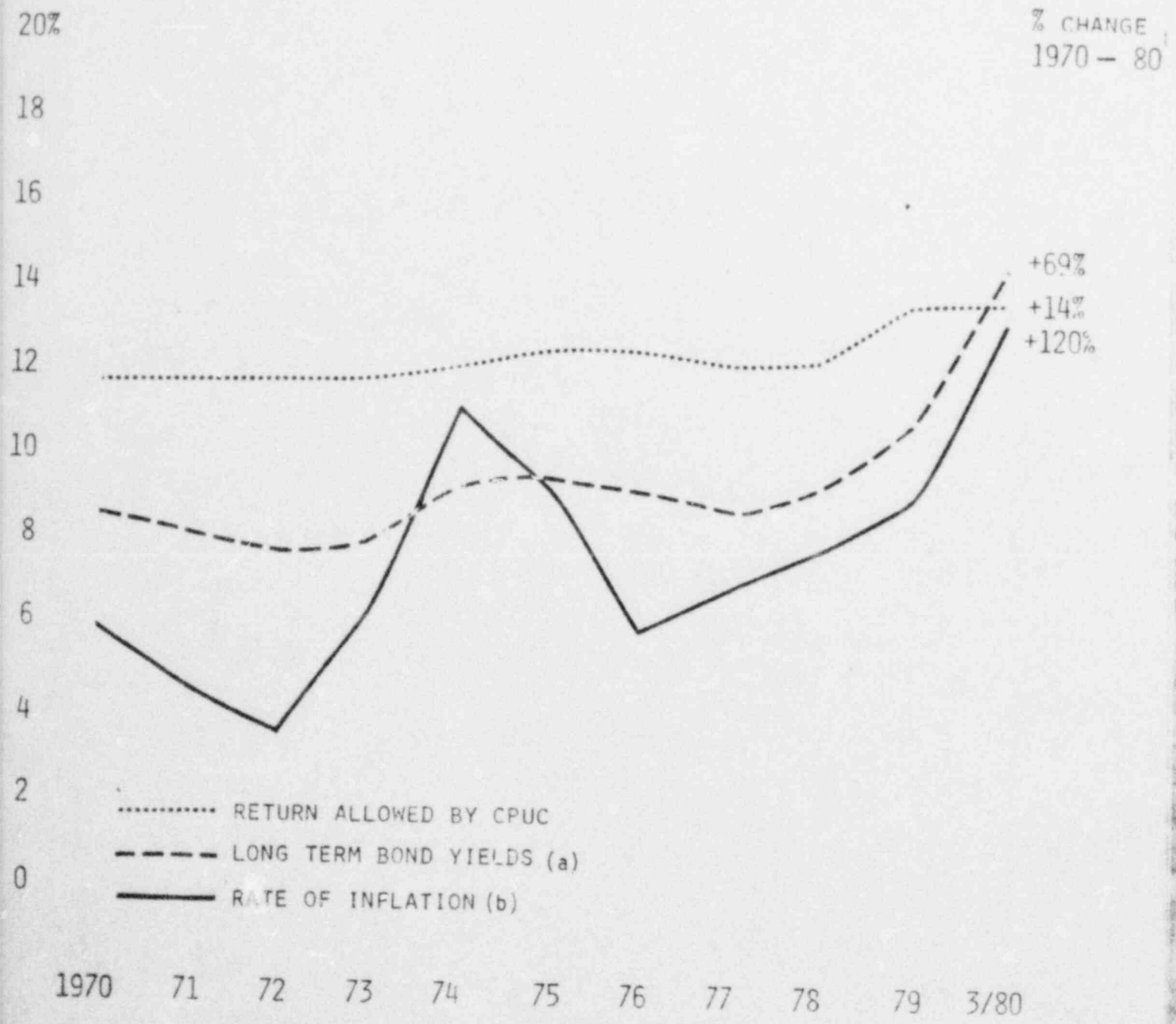
*Per testimony of H. Fred Christie, April 2, 1980. Imbedded cost of long term debt includes actual cost of 15.36% for debt sold April 1980, and estimates of 14%, 12% and 11% for issues to be sold in 1980, 1981 and 1982, respectively, and estimated costs of preferred stock to be sold of 13%, 11% and 10% in 1980, 1981 and 1982, respectively.

CHART 1
 SOUTHERN CALIFORNIA EDISON
 MEASUREMENTS OF THE BALANCE OF CUSTOMER
 AND SHAREHOLDER INTERESTS



- (a) After Federal and State income taxes; 1979 estimated.
- (b) 22% increase in real terms after adjusting for inflation.
- (c) 2% decline in real terms after adjusting for inflation.
- (d) 8% decline in real terms after adjusting for inflation.
- (e) 27% decline in real terms after adjusting for inflation.
- (f) 56% decline in real terms after adjusting for inflation.

CHART 2
 SOUTHERN CALIFORNIA F
 ALLOWED RETURN ON EQUITY, INFLATION RATE
 AND LONG TERM INTEREST RATES



(a) Moody's AA rated utility bonds
 (b) Change in cost of living index

CHART 3
 SOUTHERN CALIFORNIA EDISON
 EARNINGS/PRICE RATIOS

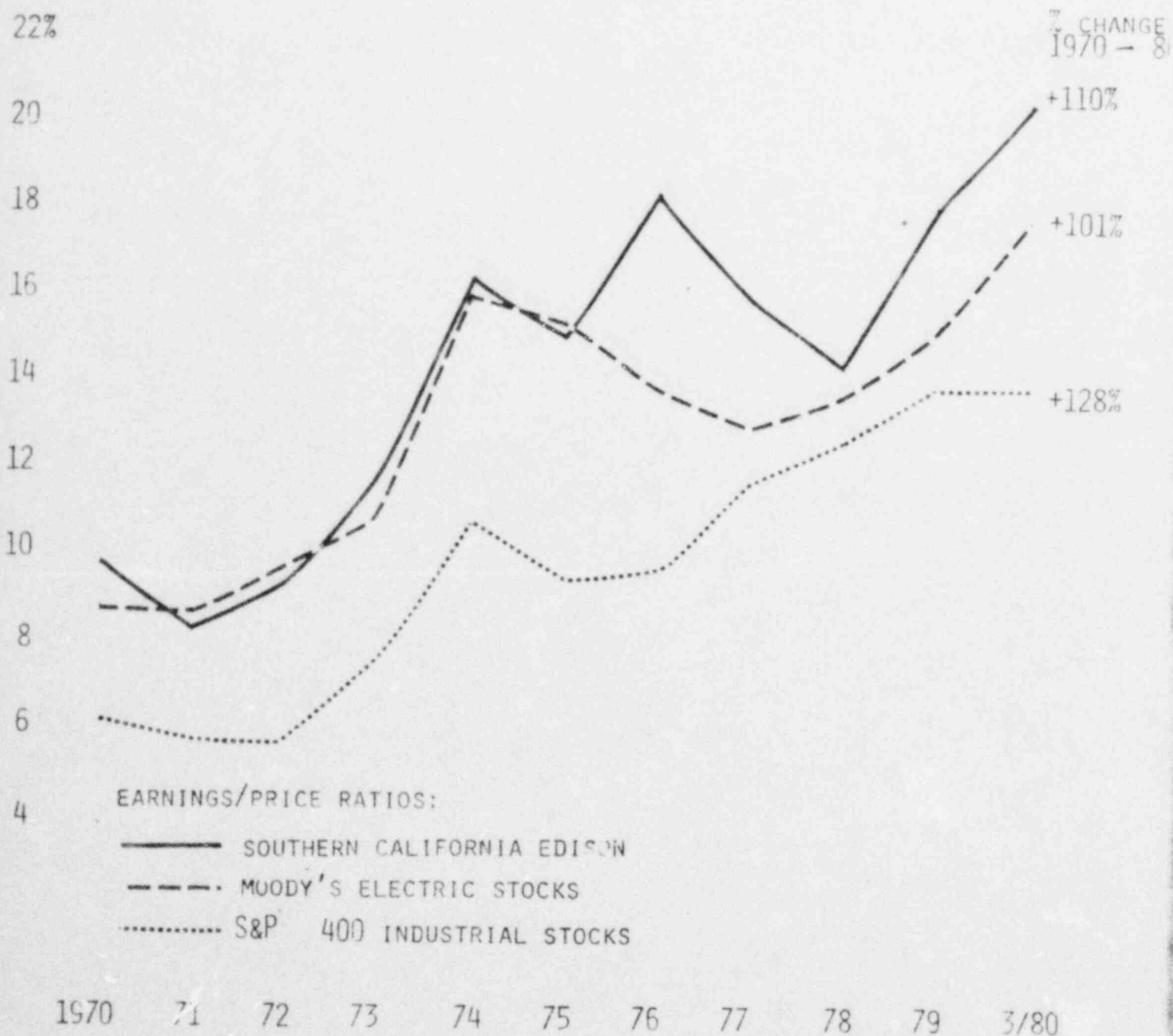
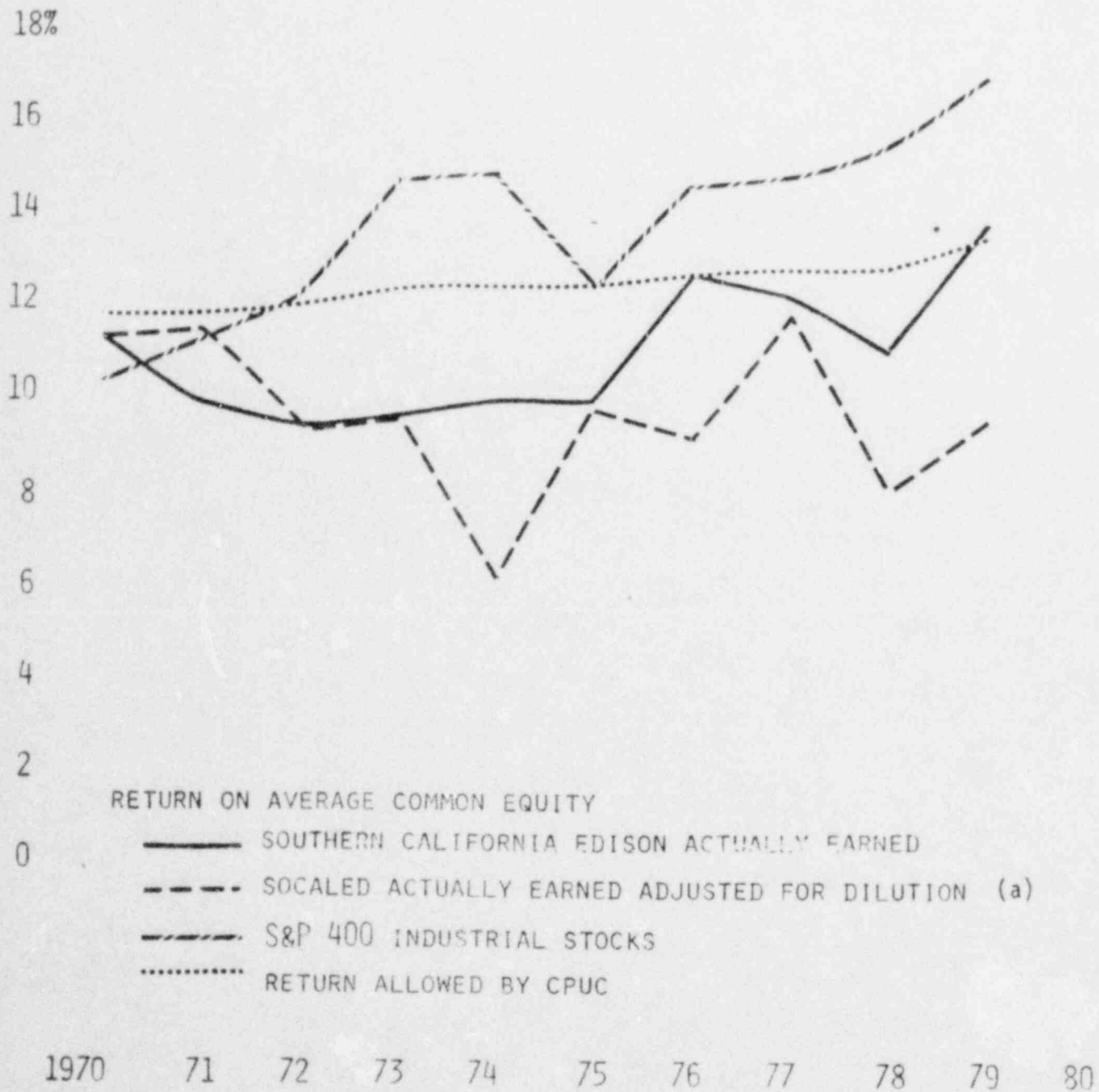
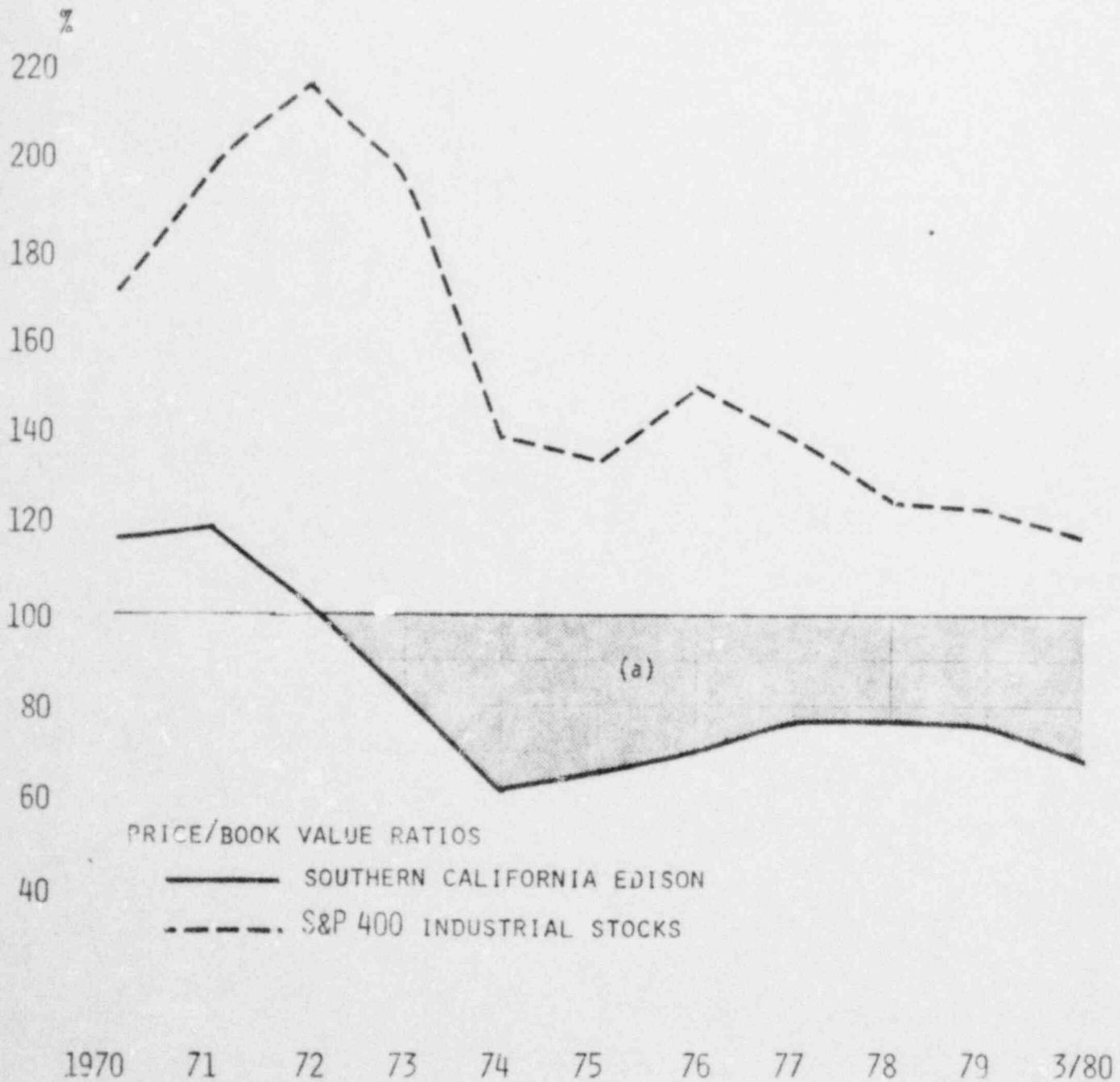


CHART 4
SOUTHERN CALIFORNIA EDISON
RETURN ON AVERAGE COMMON STOCK EQUITY



(a) Equals dividends paid plus net change in book value per share as a percent of average common stock equity per share.

CHART 5
SOUTHERN CALIFORNIA EDISON
PRICE/BOOK VALUE RATIOS



(a) Shaded area represents period when company has been unable to raise new common equity except on basis confiscatory to existing shareholders.