

Letter of Comment No: 49  
File Reference: 1200-400  
Date Received: 4/13/04

April 13, 2004

Mr. Lawrence W. Smith  
Director of Technical Application and Implementation Activities  
Financial Accounting Standards Board  
401 Merritt 7, P.O. Box 5116  
Norwalk, Connecticut 06836-5116

RE: File Reference No. 1200-400

Dear Mr. Smith:

PG&E Corporation is pleased to comment on the Financial Accounting Standards Board's (FASB) Exposure Draft, "Accounting Changes and Error Corrections - a Replacement of Accounting Principles Board Opinions (APB) No. 20, Accounting Changes, and Financial Accounting Standards Board's (FASB) No. 3, Reporting Accounting Changes in Interim Financial Statements" (the proposed Statement).

PG&E Corporation is an energy-based holding company with approximately \$10 billion in revenues in 2003, and approximately \$29 billion in assets at the end of 2003. It conducts its business principally through Pacific Gas and Electric Company, a utility that delivers natural gas and electricity service in Northern and Central California.

We recognize that the FASB and the International Accounting Standards Board (IASB) are committed to converge the accounting standards of their respective jurisdictions through a long-term plan in order to achieve more comparability in cross-border financial reporting. As part of the plan, the FASB and the IASB have undertaken a short-term project to eliminate certain differences between the accounting pronouncements of the IASB and those of the FASB. Under the short-term project, the reporting of accounting changes has been identified as an opportunity for convergence. Although the provisions of this proposed Statement are consistent with both the FASB's and IASB's goal of promoting international convergence of accounting standards, we are concerned that retrospective changes to historical financial statements may actually detract from the quality of financial reporting in the United States by causing unease amongst investors resulting from the constant revision of historical financial results.

We agree with the FASB in adopting the IASB's conclusion that a change in depreciation method should be treated as a change in estimate effected by a change in accounting principle. Changes in a depreciation method are often related to the continuing process of obtaining additional information and revising estimates, and therefore, are considered changes in estimates. Furthermore, we concur with the FASB's decision to require disclosure of the justification to support the change to a new accounting principle.

We support the FASB's position in the proposed Statement to carry forward, without reconsideration, the provisions for correction of an error from paragraphs 13, 36 and 37 of APB 20. As errors consist of mathematical mistakes, mistakes in applying accounting principles, and

oversight or misuse of facts that existed at the time the financial statements were prepared, it is appropriate for an entity to restate its financial statements in order to correct an error.

We also agree with the FASB's position to carry forward the guidance in APB 20 to account for a change in accounting estimate (or a change in accounting estimate effected by a change in accounting principle) prospectively, and a change in the reporting entity by restatement, and to disclose the justification for a change in accounting principle. Furthermore, we support the proposed Statement to carry forward the guidance in SFAS No. 3 on reporting accounting changes in interim financial statements.

However, we do not agree that reporting a change in accounting principle by retrospective application would improve the quality of the financial statements by enhancing the inter-period comparability or consistency of financial information. We believe that APB 20 currently provides the appropriate accounting guidance in accounting for a change in accounting principle. Under APB 20, most changes in accounting principles are recognized by including the cumulative effect of changing to a new accounting principle on the income statement and in retained earnings at the beginning of the period in which the change is made. The financial statements for prior periods included for comparative purposes should be presented as previously reported. As discussed below, pro forma disclosure of prior year results could be required if called for in specific instances, and comparison is warranted.

We believe that investors should be able to rely on historical financial statements. However, reliability will be disrupted by continually changing financial statements resulting from retrospective application of accounting principles. For example, prior period financial statements would have been modified at least quarterly based upon the numerous modifications to SFAS No. 133. Although disclosures can help investors understand the changes, constant re-casting of historical results can lead to confusion, frustration and a general lack of integrity in the quality of the historical information being provided. Further treating the correction of accounting errors and changes in accounting principles similarly will tend to eliminate the distinction between the two. We continue to believe that the corrections of accounting errors and changes in accounting principles are very different. Therefore, we believe that investors' confidence would be weakened as a result of retrospective application of changes in accounting principles. Our belief is consistent with the discussion in paragraph 14b of APB 20, which states: "Restating financial statements of prior periods may dilute public confidence in financial statements and may confuse those who use them. Financial statements previously prepared on the basis of accounting principles generally accepted at the time the statements were issued should therefore be considered final except for changes in the reporting entity or corrections of errors." An alternative to retrospective application is to enhance the cumulative effect disclosures in the financial statements. The cumulative effect disclosures demonstrate comparability between periods by presenting financial results prior to a change of accounting principle, and financial results as a result of the recent guidance. We believe that disclosure of the pro forma effects on earnings resulting from the accounting change may also help with comparability and could be included in the cumulative effect disclosures.

We believe that the lack of specific requirements on retrospective application would result in variability in practice. The proposed Statement calls for judgment in determining what an entity

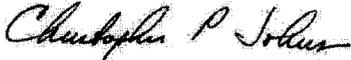
would consider practical. Under the proposed Statement, retrospective application would be utilized unless it is impracticable to determine the period-specific effects of an accounting change on one or more individual prior periods presented, or the cumulative effect of applying a change in accounting principle to all prior periods. In an attempt to enhance application consistency, the FASB provides guidance that limits the use of the impracticability exception. The FASB concludes that retrospective application would be considered impracticable if the effects are not determinable, application would require assumptions about management's intent in a prior period, or application would involve significant estimates made as of a prior period. However, in deciding whether retrospective application is impracticable, we believe that a high level of judgment and subjectivity would be involved. Accordingly, the earliest period for which retrospective application is practicable or the earliest date for which the change is made prospectively would vary widely in practice.

In addition, retrospective application will potentially create an administrative burden on companies. In our view, Sarbanes-Oxley Section 404 requires that financial statements be based upon a ledger that is supported by schedules and work papers, and it requires timely reconciliation of a company's accounts. These schedules and work papers also support other financial reporting requirements, such as preparation of the company's tax returns. We believe retrospective application of changes in accounting principles will require companies to reopen prior period books and records and to adjust prior year work papers and schedules. This will be a burden to companies regardless of their size and the sophistication of their accounting systems.

In the event that the FASB decides to proceed with its plans to report a change in accounting principle by retrospective application, we recommend that the FASB provide additional guidance in the following areas: (1) how to decide the effects of retrospective application are not determinable, (2) how to objectively determine what constitutes a "significant estimate," and (3) how many accounting periods back retrospective application should be applicable. Without explicit guidance in these areas, we believe that there would be a lack of consistency in application and comparability between companies. This would not aid investors in their assessment of a company's financial position and would likely result in more confusion. If the FASB insists on retrospective application, we also recommend that the FASB consider a requirement to include an affirmative statement in the financial statements in regard to the time period over which the financial statements are reliable. With the frequency and number of changes in accounting principles, a company would be expected to restate its prior results regularly. It would be difficult for investors and other users of the financial statements to keep abreast of changes in accounting principles and to know whether they render the financial statements they are using obsolete. Accordingly, the affirmative statements would allow investors and potential investors to know when to expect the next revised version of the financial statements and disregard the previous version. Furthermore, the FASB should implement a set of rules to identify the types of financial documents and data (such as Regulations S-K, S-X, tax returns and financial ratios) that utilize historical financial information that also require restatement due to retrospective application of new accounting principles.

We would be pleased to discuss our comments with the Board or its staff at your convenience.

Sincerely,



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Senior Vice President and Controller

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