

PG&E Corporation Fourth Annual

Corporate Responsibility Report



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	On the cover
	Tom King, CEO of Pacific Gas and Electric Company, secures solar panels on the roof of a new home being constructed as part of our Solar Habitat program and partnership with Habitat for Humanity.

This Corporate Responsibility Report and letter from the Chairman contain forward-looking statements that are necessarily subject to various risks and uncertainties, the realization or resolution of which are outside of management's control. These statements are based on current expectations and projections about future events and assumptions regarding these events, and management's knowledge of facts at the date of this report. Actual results could differ materially from those expressed or implied in the forward-looking statements. Please see our reports filed with the Securities and Exchange Commission for a discussion of some of the more significant risks and uncertainties, the resolution of which could materially affect actual results.

Letter From the Chairman and CEO

To Our Stakeholders:

Our business today operates in a world of relentless and real-time change as we approach the second decade of the 21st century. From shifts in the global climate to evolving economic and demographic trends in our local communities, we live and work in an environment that constantly challenges us to think anew about our customers, communities and responsibilities as a company.

We embrace these changes. As a company that aspires to be the leading utility in the United States, our long-term success depends on us staying on top of—or ahead of—these transformative waves, which roll in each and every day. We do this, in part, by always reminding ourselves that true leadership has to be sustainable leadership.

To us, sustainable leadership means doing the big things, small things—and the right things—that will help ensure that PG&E remains relevant, vibrant and connected to all of our stakeholders for the next quarter of a century, not just the next quarter.

Our report this year illustrates some of the many ways we are thinking and working outside of the box, and outside of our northern and central California service area, as we strive to fulfill global responsibilities and meet our ethical obligations to take care of the world around us.

This accountability starts with our 15 million customers, nearly 20,000 employees, investors, regulators, partners and communities within California, which is now the sixth-largest economy on the planet. It ultimately extends to everyone who shares PG&E's interest in ensuring a clean, secure energy future—from national policymakers to industry peers at home and even overseas.



Peter A. Darbee

As a utility, we also believe strongly that our stakeholders are entitled to high expectations of us. We enjoy a unique relationship with customers and communities by virtue of our franchise to serve a given area and the promise of an opportunity to earn a fair return for our investors. This is a privilege, and we accept that it requires a readiness to be held to a higher standard than other companies who operate in a different environment.

Even as we accept this responsibility and willingly confront the issues that are most critical to us and our stakeholders, it is clear we can't resolve every challenge on our own. That's why, wherever possible, we seek solutions together with partners who are as passionate and committed as we are.

Last year, for example, PG&E accepted an invitation to be a member of Ceres, a leading national network of investors, environmental organizations and other public interest groups working to address sustainability challenges such as global climate change. More recently, we joined a handful of the nation's leading companies and environmental organizations to form the U.S. Climate Action Partnership and call for federal action to reduce greenhouse gas emissions.

Other examples of partners include Habitat for Humanity, with whom we work to install solar energy systems in affordable housing, or the Red Cross, which is working with PG&E to prepare communities in the Bay Area to weather a natural disaster. Without partners like these, we'd be far less effective in achieving our long-term goals as a company.

The basis for all of our partnerships is shared values. We may operate in a complex world today, but at PG&E we believe the bottom line isn't that complicated; if we live by our values, we'll create real value for employees, customers, communities, partners and investors.

Examples of this are abundant across our business. Our values are driving new investments in our communities, through increased charitable support, which reached its highest level ever last year. They are driving us to significantly improve our performance in areas like supplier diversity, where in 2006 we exceeded our target for the first time since 2002. They are driving increased transparency around corporate governance, where third-parties consistently rank us among the best in the industry.

They are also driving us to be more aggressive than ever in our efforts on behalf of the environment.

Over 50 percent of the electricity we deliver to customers today comes from sources that emit no greenhouse gases. We have also helped Californians become the most energy efficient consumers in the nation. A leader in energy efficiency since the 1970's, we've worked with our customers to achieve significant cumulative lifecycle energy and cost savings, on the order of

\$9 billion, and prevent approximately 125 million tons of carbon dioxide from entering the atmosphere. In 2006, PG&E began a new chapter by launching a three-year, \$1 billion customer energy efficiency commitment—the largest such program of its kind by a U.S. utility.

By continuing to succeed in these efforts, we'll be able to generate greater environmental and economic security for our customers and communities—another way we define corporate responsibility.

With that in mind, we are investing prudently and significantly in this new energy economy. Among other efforts, we're working with technology companies and entrepreneurs on innovative strategies to advance and commercialize energy efficiency, renewable energy technologies and the "smart grid"; we're actively hiring a diverse group of the best and brightest to work on these challenges; we're engaging with the transportation sector through our support of plug-in hybrid electric vehicles and other clean air vehicle strategies; and we're partnering with companies in the manufacturing and retailing sectors to establish and promote energy-efficiency standards.

These efforts are not only the right thing for customers, they are keys to achieving our vision of sustained and sustainable leadership in the industry.

As we have acknowledged, as proud as we are of the progress we are making, we are not there yet. This report is as much an opportunity for us to openly and honestly assess the areas on which we need to continue working as it is to highlight accomplishments. In that spirit, we are redoubling efforts in areas like employee safety, where our performance falls short of where we aim to be. We're also continuing to focus on fostering diversity within our leadership.

Lastly, we need your engagement and feedback in order to have an open and two-way dialogue. Please let us know what you think of this report and our overall performance. Speaking up in the name of continuous improvement is your responsibility; delivering on the promises we've made is PG&E's responsibility. Together, I am confident we can make the world better for all of our stakeholders.

Sincerely,

A handwritten signature in black ink, appearing to read "Peter A. Darbee". The signature is fluid and cursive, with a long horizontal stroke at the end.

Peter A. Darbee
Chairman of the Board, CEO and President, PG&E Corporation

Global Reporting Initiative Linkages and Stakeholder Engagement

PG&E is committed to continuous improvement when it comes to how we report our impacts and sustainable business strategies. The table below shows how this report aligns with the Global Reporting Initiative (GRI) Performance Indicators, which we use as an important guide and reference point. While we are working toward meeting the GRI reporting protocols, for several indicators below, we currently only partially meet the recommended standard.

In developing and writing our Fourth Annual Corporate Responsibility Report, PG&E engaged with Ceres and a team of external stakeholders, which was selected by Ceres¹. The Ceres stakeholder team is an independent group of individuals drawn primarily from the Ceres coalition and represents a range of constituencies that have expertise in environmental, social and governance issues. In reviewing this report, the team considered whether the company adequately reported on its sustainability performance and key impacts, including goals, targets, systems, data and initiatives. Through this review process, the Ceres stakeholder team provided extensive feedback to PG&E, which was considered in the preparation of the final version of this report.

Indicator	Description	Report Section(s)	Page(s)
Strategy and Analysis			
1.1	Statement by the CEO	Letter from the Chairman and CEO	1-3
Organizational Profile			
2.1	Name of the organization	Cover	Cover
2.2	Primary brands, products, and/or services	Company Overview	9
2.4	Location of organization's headquarters	Company Overview	9
2.5	Countries in which the company has operations	Company Overview	9
2.6	Nature of ownership and legal form	Company Overview	9
2.7	Markets served	Company Overview	9
2.8	Scale of the reporting organization	Company Overview	9-10
2.10	Awards received in the reporting period	Recognition for Diversity; Environmental Awards	24; 77-78
Report Parameters			
3.1	Reporting period	Summary Statement	5
3.2	Date of most recent previous report	Summary Statement	Website
3.3	Reporting cycle	Cover	Cover
3.4	Contact point for questions regarding the report	Summary Statement	5
GRI Content Index			
3.12	Table identifying the location of the Standard Disclosures in the report	Global Reporting Initiative Linkages	4
Governance			
4.1	Governance structure of the organization	Corporate Governance	14-15
4.2	Indicate whether the Chair of the highest governance body is also an executive officer	Letter from the Chairman and CEO	1
4.5	Linkage between organization's performance and executive compensation	Corporate Governance	15
4.8	Corporate mission and values	High Standards and Clear Values Form the Foundation of Leadership	25-27
4.12	Externally developed economic, environmental, and social charters	Working Collaboratively and Creatively to Address Climate Change	55-59
4.13	Memberships in associations	Partnerships	74-77
4.14	Stakeholder groups engaged by the organization	Letter from the Chairman and CEO; Partnerships	1-3; 4; 74-77
4.15	Identification and selection of stakeholders	Letter from the Chairman and CEO	1-3
4.16	Approaches to stakeholder engagement	Letter from the Chairman and CEO	1-3
4.17	Key topics and concerns raised through stakeholder engagement	Letter from the Chairman and CEO	1-3

¹ Ceres is a network of investors, environmentalists and other public interest groups that works with companies and investors to address sustainability challenges (see www.ceres.org for more information).

Indicator	Description	Report Section(s)	Page(s)
Economic			
EC1	Direct economic value generated and distributed	Company Overview; Corporate Philanthropy	9; 31-34
EC2	Financial implications and other risks and opportunities for the organization's activities due to climate change	Working Collaboratively and Creatively to Address Climate Change	55-59
EC6	Policy, practices, and proportion of spending on locally-based suppliers	Environmental Justice	42-43
EC7	Procedures for local hiring at locations of significant operation	Environmental Justice	42-43
Environmental			
EN3	Direct energy consumption by primary energy source	General Utility Production Statistics; Electric Power Mix Delivered to Retail Customers; Environmental Performance Summary Tables	10; 50; 80
EN4	Indirect energy consumption by primary source	General Utility Production Statistics; Electric Power Mix Delivered to Retail Customers; Environmental Performance Summary Tables	10; 50; 80
EN5	Energy saved due to conservation and efficiency improvements	Putting Efficiency First; Environmental Performance Summary Tables	48-49; 80
EN6	Initiatives to provide energy-efficient or renewable energy based products and services, and reductions in energy requirements as a result of these initiatives	Putting Efficiency First; Planning for California's Clean Energy Future; Partnering to Accelerate Innovation; Environmental Performance Summary Tables	48-55; 80
EN13	Habitats protected or restored	Promoting Stewardship of California's Natural Resources	59-63
EN14	Strategies, current actions, and future plans for managing impacts on biodiversity	Promoting Stewardship of California's Natural Resources	59-63
EN16	Total direct and indirect greenhouse gas emissions by weight	Working Collaboratively and Creatively to Address Climate Change	56
EN18	Initiatives to reduce greenhouse gas emissions and reductions achieved	Putting Efficiency First; Planning for California's Clean Energy Future; Partnering to Accelerate Innovation; Working Collaboratively and Creatively to Address Climate Change; Environmental Performance Summary Tables	48-59; 79-80
EN20	NO _x , SO _x , and other significant air emissions by type and weight	Planning for California's Clean Energy Future; Environmental Performance Summary Tables	51; 79
EN22	Total weight of waste by type and disposal method	Environmental Performance Summary Tables	81
EN26	Initiatives to mitigate environmental impacts of products and services, and extent of impact mitigation	Our Environment	48-73
EN28	Monetary value of significant fines and total number of non-monetary sanctions for non-compliance with environmental laws and regulations	Operational Performance; Environmental Performance Summary Tables	73; 81
EN29	Significant environmental impacts of transporting products and other goods and materials used for the organization's operations, and transporting members of the workforce	Working Collaboratively and Creatively to Address Climate Change; Innovative Transportation Solutions and Technologies	56; 66
Social Performance			
LA1	Total workforce by employment type, employment contract, and region	Company Overview	9
LA7	Rates of injury, occupational diseases, lost days, and absenteeism, and number of work-related fatalities by region	Working Safely and Staying Healthy	20
LA11	Programs for skills management and lifelong learning	Employee Development and Learning	24-25
LA13	Composition of governance bodies and breakdown of employees per category according to gender, age group, minority group membership, and other indicators of diversity	Workforce Diversity and Initiatives	22-23
SO1	Nature, scope, and effectiveness of any programs and practices that assess and manage the impacts of operations on communities, including entering, operating, and exiting	Environmental Justice	42-43

This Fourth Annual Corporate Responsibility Report provides information on performance metrics and activities occurring in calendar-year 2006, except when otherwise noted. The complete report, as well as a Summary Report, can be viewed and downloaded at www.pgecorp.com, where stakeholders can contact us to solicit additional information and also offer comments and suggestions on this and future reports. Stakeholders can also access information at www.pge.com on tips to improve the energy efficiency of their homes and businesses and reduce their carbon footprint.



PG&E seeks success on behalf of our 15 million customers each and every day as we provide them with natural gas and electricity to fuel their businesses and live their lives. Together, we ask if we can slow global climate change, if we can build energy sustainability into our communities, if we can harness the next generation of renewable energy, and if we can leverage energy efficiency to transform the economy and the environment. These are crucial questions worth exploring and we are working with dynamic employees and community and business partners to generate answers. We are managing for today and planning for tomorrow; and, as we shape the utility of the 21st century, our business will always do "The Big Thing," "The Difficult Thing," as long as it is "The Right Thing."

Our Business

Bringing Energy Efficiency to Silicon Valley—and Our Customers

As a leader in the utility industry, PG&E works with a number of companies to help them advance energy-efficient products and services. One of our most fruitful partnerships has brought us together with Sun Microsystems. Last year, we certified Sun's new energy-efficient servers and created a purchaser rebate plan for the computers. This innovative program has helped spur sales for Sun's cutting-edge servers, reduced energy use in technology data centers and motivated other major computer manufacturers to embrace energy efficiency—which will ultimately benefit PG&E's customers, California's and the country's economy and the environment.

Mark Bramfitt, a principal program manager at Pacific Gas and Electric Company, is responsible for the breakthrough relationship with Sun. He also reaches out to three key industries—high-technology, healthcare and biotechnology—in an effort to design and develop energy-efficiency programs that will make a real difference for our customers.

Dave Douglas, Vice President for Eco Responsibility at Sun, joined forces with PG&E and oversees the computer maker's environmental and sustainability efforts.



Mark Bramfitt



Dave Douglas

Is the technology sector gobbling up a disproportionate share of energy?

Bramfitt: Information technology is still growing rapidly and the data centers are crowded with computers. There's not a lot of cooling or air flow in these critical places and the power capacity is being stretched significantly. PG&E serves Silicon Valley. We wanted to offer technology executives some sort of help here. Our customers need our best solutions.

Douglas: The technology industry is in an interesting spot today. Our products are essential to economic growth—whether they help optimize supply chains, stimulate productivity or enable e-business. But computers use lots of energy. So we are part of the solution and part of the problem. At Sun, our goal is to maximize technology's possible uses and minimize its negative impacts. Energy reduction is a big part of that. And that's why we initially raised awareness about the importance of energy efficiency in late 2005. We've tried to carry this through to our products since then.

What does the PG&E-Sun partnership really mean?

Bramfitt: Sun is clearly a leader. They saw these issues early and began designing an energy-efficient server. This has changed the way the technology industry thinks. It's changed the standards. Before, it was how fast and how big the computer was. Now, it's how fast, how big and how energy efficient. People are thinking about cooling and capacity today because of Sun.

Last year, we certified Sun's new energy-efficient servers and created a purchaser rebate plan for the computers. This innovative program has helped spur sales for cutting-edge servers, reduced energy use in data centers and motivated other major computer manufacturers to embrace energy efficiency—which will ultimately benefit PG&E's customers, California's and the country's economy and the environment.

Douglas: PG&E has tremendous vision and has exercised tremendous leadership on the energy-efficiency issue. We couldn't do this alone. Mark and his team are using incentives to steer people toward technology products that make sense in today's environment. Our Sun Fire T1000 and T2000 servers are powered by our Ultra SPARC T1 processor. This combination means the servers can do a lot at once, operate even faster and still burn less power.

In terms of energy efficiency, is Sun influencing the technology industry the way Toyota seems to be doing in the automotive world?

Douglas: Toyota and Sun are both investing in innovation to help address the energy-efficiency issue.

It's early, but are there any results stemming from the PG&E-Sun alliance that we can report?

Bramfitt: At this point, we're running more than four times ahead of projections for data-center energy savings. That's incredibly encouraging.

Douglas: Our server line is selling really well. We hit approximately \$400 million in Sun Fire T1000/T2000 sales for the last four reported quarters. And our relationship with PG&E has led to a number of dialogues with other utilities around the country.

Company Overview

PG&E Corporation is an energy-based holding company whose core business is Pacific Gas and Electric Company. Pacific Gas and Electric Company, or the Utility, delivers safe, reliable and responsive gas, electric and customer service to a population of approximately 15 million people throughout northern and central California. PG&E had approximately \$34.8 billion in assets as of December 31, 2006, and generated revenues of approximately \$12.5 billion in 2006.



Headquarters' Location
San Francisco, CA

Service Area
70,000 square miles in northern and central California

Service Area Population
15 million people (or about 1 of every 20 Americans)

Electric Distribution Customer Accounts
5.1 million

Natural Gas Distribution Customer Accounts
4.2 million

Revenue
\$12.5 billion

Assets
\$34.8 billion

Earnings per Share
\$2.76

Number of Common Shareholders
93,170

Number of Common Shares Outstanding
374,181,059

Employees
Approximately 19,700

Approximately 12,700 are covered by collective bargaining agreements with three labor unions:

- International Brotherhood of Electrical Workers (IBEW), Local 1245
- Engineers and Scientists of California/ International Federation of Technical and Professional Employees (ESC/IFTPE), Local 20
- Service Employees International Union/ International Union of Security Officers (SEIU/IUSO)

System
158,689 circuit miles of electric transmission and distribution lines and 46,259 miles of natural gas transmission and distribution pipelines; approximately 6,000 megawatts of generation, including the Diablo Canyon nuclear power plant and one of the largest hydroelectric systems in the country

Examples of Customer Groups
Residential, Small Business, Retail, Agriculture, Education, Heavy Industry and Manufacturing, Government, Medical, Distillers, Hospitality, High-Technology, Food Service, Biotechnology, Large and Small Commercial Enterprises

Selected Examples of Major Customers
Albertsons, Inc., Bank of America, Chevron, Fetzer Winery, Intel, Lockheed Martin, New United Motors Manufacturing, FedEx, Safeway, Inc. and Sun Microsystems

General Utility Production Statistics

	2004	2005	2006
Total Electricity Generated (GWh gross)*	27,396	32,680	34,086
Fossil Plants (GWh gross)	996	1,139	629
Hunters Point (GWh gross)	601	677	187 ¹
Humboldt (GWh gross)	395	462	442
Other plants (GWh gross)	26,400	31,547	33,457
Diablo Canyon (GWh gross)	15,210	18,592	18,421
Hydro Facilities (GWh gross) ²	11,191	12,955	15,035
CA-Eligible Hydro (GWh gross)**	1,267	1,397	1,439
Electricity Purchased (GWh)	34,553	25,990	29,104
Other Electric Supplies (GWh)***	21,971	23,275	19,585
Electricity Delivered (GWh)	82,936	81,626	84,310
Electricity Purchased by Our Customers (GWh)	73,616	72,727	76,692
Total Natural Gas Throughput (million cubic feet or MMcf)	877,760	844,068	828,550 ³

* One GWh, or gigawatt-hour, is one million kilowatt-hours, enough to power one million homes for one hour.

** Electricity generated by hydroelectric facilities with a capacity under 30 MWs.

*** Represents contract energy from the California Department of Water Resources, which the Utility neither purchases nor takes title to but which is delivered to the customer.

¹ Hunters Point ceased operation in May 2006.

² Hydroelectric generation can vary year-to-year due to variability in precipitation.

³ The largest factor causing the decline in throughput from 2004 to 2006 is the decline in off-system market throughput.

Establishing Priorities to Transform Our Business and Achieve Our Vision

Establishing a clear set of priorities is paramount to achieving our vision of becoming the leading utility in the United States. Employees must have a solid

understanding of what is expected of them and how what they are doing supports the company's overall efforts. At the same time, our shareholders, our regulators and our customers must understand and support the steps the company is taking to better provide our products and services and position

us well for the future. The priorities PG&E established for 2006 were shared broadly and tie directly to our goals of delighting our customers, rewarding our shareholders and energizing our employees.

For 2006, our priorities included:

- **Advance business and culture transformation.** Moving transformation ahead is essential for PG&E to successfully achieve its vision.
 - By the end of 2006, more than 40 transformation initiatives were fully or partially deployed; they achieved approximately \$175 million in savings during 2006.
 - These initiatives included opening all seven new Resource Management Centers and centralizing and streamlining work previously done in 70 different locations.

We are passionate about meeting our customers' needs and delivering for our shareholders.

PG&E Settles 10 Years of Litigation Related to Chromium

In February 2006, PG&E announced a \$295 million legal settlement that effectively ended 10 years of litigation related to our use of chromium in PG&E's gas compressor operations during the 1950s, '60s and '70s. PG&E used chromium (a rust inhibitor) in cooling towers at three of its gas compressor stations in remote parts of our service area. The company placed wastewater containing chromium in unlined ponds at those stations. These practices were both common and legal.

Over time, chromium eventually reached groundwater in these areas. Some PG&E employees became aware of this in the 1960s, but regrettably, the facts suggest that they did not share that information with others in the company or the public. This situation should never have happened—and we are sorry that it did. It is not the way we do business.

In 1987, these facts came to light again during a routine environmental audit. When PG&E discovered that years ago the information had not received the proper attention, we immediately notified residents, state and local officials and the media. PG&E provided drinking water to nearby residents and arranged for medical exams for those who wanted them. PG&E also began cleaning up the groundwater contamination, in cooperation with state and local officials. That work continues today.

In the 1990s, lawsuits were filed. A portion of these claims were settled in 1996 for \$333 million. The settlement which occurred in February 2006 resolves substantially all of the remaining claims.

These events have long been public and they are well understood by all the parties. The differences between PG&E and the plaintiffs have centered on opposing views of the health science on chromium. Although the settlement does not resolve these differences, PG&E believed it best to move forward.

An essential part of our company vision is our values. Two that are especially relevant for this situation: "We act with integrity and communicate honestly and openly" and "We are accountable for all of our own actions: these include safety, protecting the environment and supporting our communities." As PG&E pursues its goal of becoming the leading utility, a fundamental part of that success will be continuing to ensure that our actions align with our values. This settlement is a reminder that every employee at PG&E must take this responsibility very seriously. It's the right thing for the company—and it is the right thing, period.

Innovative Partnerships With the High-Tech Industry

Many regions across the U.S. are experiencing huge new demands for electric infrastructure as data-center operators construct new facilities. Nationwide, existing data centers are experiencing space, cooling and energy-capacity issues. With that in mind, PG&E is offering energy-efficiency programs to help customers live within their existing data centers, and to moderate the energy impact of new ones. Data centers can use up to 100 times the energy per square foot of typical office space, so the energy-efficiency opportunities are significant.

PG&E worked with Sun Microsystems to develop an incentive program for energy-efficient servers, garnering attention from a growing number of other major computing equipment manufacturers, who are also qualifying their premium performance equipment for the program.

PG&E also announced the first-ever utility financial incentive program for virtualization projects in data centers. Virtualization technology enables customers to consolidate IT workloads and use less equipment and energy. One major software firm, for example, was able to consolidate workloads that were running on 230 servers onto just 13, capturing tens of thousands of dollars in energy savings.

And, more recently, we helped form a nationwide coalition of utilities to discuss and coordinate energy-efficiency programs for the high-tech sector, focusing on data centers.

We have already undertaken coordination efforts with Southern California Edison and San Diego Gas & Electric so that program offerings are consistent across the state, and are now reaching out to utilities in key markets across the country. The Northwest Energy Efficiency Alliance (NEEA), TXU Electric Delivery, Austin Energy, New York State Energy Research and Development Authority (NYSERDA) and NSTAR have all joined the coalition.

- We also implemented our PG&E Tomorrow program, which brought management into the field to meet employees and talk about our transformation initiatives; more than 18,000 of our approximately 20,000 employees have now had the opportunity to visit with management.

- **Provide attractive shareholder returns.** A utility whose finances are healthy and sound, and is meeting—or exceeding—shareholder expectations is in the best position to do the right things for its customers, its communities and society as a whole.
 - In 2006, PG&E Corporation exceeded its earnings per share estimate. Earnings per share from operations for 2006 grew by nearly 10 percent compared with 2005. This surpassed our projected growth rate of 7.5 percent. We expect to continue growing earnings on a trajectory that is one of the strongest among comparable utilities.
 - PG&E's strategy and outlook continue to resonate with the market. Our stock price ended 2006 just below the all-time peak it hit in December 2006. For shareholders, the growth in stock price, plus four quarters of steady common dividend, added up to a total annual return of approximately 31 percent. PG&E's returns beat the S&P 500, the S&P Electrics, and the S&P Multi Utility Index.
- **Increase investment in utility infrastructure.** Similar to many utilities, PG&E is making major capital additions to its infrastructure in order to support growth and improve existing service. This benefits the homes and businesses we serve. It also provides corresponding opportunities for shareholders to earn additional returns. And it allows us to transform our system to one which will be able to support, leverage and provide the advanced energy solutions necessary to create a sustainable energy future.
 - In 2006, infrastructure investments in electric and gas distribution and transmission and electric generation totaled \$2.4 billion, up from \$1.9 billion in 2005.
 - We have received regulatory approval for revenues that will support ongoing capital investments averaging \$2.8 billion annually between 2007 and 2011; in 2008 and 2009, this figure is expected to rise to more than \$3 billion annually.
 - We have also received regulatory approval for a total capital investment of \$1.4 billion between 2006 and 2010; this capital will support our SmartMeter™ initiative, and we have already begun deploying these funds. These meters will help to facilitate demand response, the next generation of "smart" end use technologies, and plug-in hybrid electric vehicles.
 - Finally, we have received regulatory approval for a total capital investment of \$1.3 billion between 2009 and 2010; this capital will be used to construct new PG&E-owned electric-generating facilities, which will use some of the most advanced and efficient technologies available.

- **Implement an energy procurement plan.** Rejuvenating California's energy supply and infrastructure is one business driver. Another is laying the groundwork for a sustainable energy future that reduces the overall carbon intensity of our economy and ensures a diversity of reliable and affordable energy choices.

PG&E's energy procurement efforts are modeled on California's Energy Action Plan, which prioritizes energy efficiency and demand response, renewable generation and low-emitting conventional energy resources. We are leveraging smart, sustainable resource planning to facilitate the development and deployment of cleaner, more efficient technologies.

- In 2006, more than 50 percent of the electricity we delivered to our customers came from resources that produce no or low amounts of greenhouse gas emissions.
- We exceeded the aggressive energy-efficiency targets established by the California Public Utilities Commission, avoiding the need to secure an additional 142 MW of peak power for our customers. And our electric and natural gas customer energy-efficiency savings for 2006 prevented the release of 489,000 tons of carbon dioxide (CO₂) into the atmosphere.
- We also signed more than a dozen contracts for new supplies of California-eligible renewable generation, with the potential to provide more than 500 MW of capacity fueled by biomass, geothermal, biogas and other renewable resources.

Enterprise Risk Management

PG&E is taking an integrated and coordinated approach to risk management to the benefit of our shareholders and customers. We are engaged in an enterprise-wide effort to identify the most significant risks facing our business and establish a sustainable process for managing these risks into the future. Enterprise Risk Management (ERM) is a process used by companies to ensure they are effectively managing major risks to achieve their business objectives. PG&E's ERM program:

- is designed as an ongoing process rather than a one-time project;
- supports the company's vision, goals and strategies;
- provides a portfolio view of risk and facilitates a coordinated risk response across the enterprise;
- identifies significant risks and ensures they are being managed within the company's risk tolerance;
- ensures a systematic process for identifying and evaluating risks;
- improves the understanding of key risks and their potential interdependencies;
- enhances the ability to manage the probability of occurrence and/or consequence of risks;
- improves the allocation of resources used to manage risk; and
- defines clear roles and responsibilities for risk-management activities, including the creation of a senior officer risk committee, which is responsible for prioritizing risks and reviewing the evaluations and plans for the top risks.

Making Energy Bill Payment Fast, Easy, and More Resource-Efficient

PG&E is providing customers with more options and better services, while also finding ways to protect and enhance the environment. Our paperless e-Bills program is one such example.

With e-Bills, customers receive e-mail notifications when bills are ready to view at www.pge.com—using a secure, password-protected login. While online, they can also make automatic payments. The service is free.

More than 660,000 customers no longer receive paper bills. In 2006 alone, PG&E sent 6.5 million e-Bills to customers. This provided not only convenience to our customers, but also significant paper and solid waste savings. PG&E avoided the use of more than 165 tons of paper, which equals approximately 2,800 trees and 160 tons of solid waste. Environmental impact estimates were made using the Environmental Defense Paper Calculator. For more information, visit www.papercalculator.org.

PG&E is also reducing impacts to the environment by printing double-sided bills on 30 percent post-consumer content recycled paper. So, whether customers go paper or electronic, we're committed to being customer- and environment-friendly. And that is a very good place to be.

Consistent with best practices, PG&E is taking both a “bottom-up” and “top-down” approach to risk management. A structured “bottom-up” approach was used to identify key risks and provide a high-level evaluation of these risks. Subject matter experts within PG&E were interviewed to define the nature and potential impact of key risks as well as existing mitigation activities. An outside expert on global trends then reviewed this work and provided additional suggestions.

As a result of this process, approximately 30 significant risks to PG&E Corporation and the Utility were identified. They include a wide variety of risks, such as commodity risk, strategic business risk, operational risk, natural hazards, political risk, regulatory risk, economic risk and environmental risk, including climate change. A structured “top-down” approach was then used to prioritize key risks. Risk assessments and mitigation plans to address the risks identified are being developed and put into effect, and will be reviewed and updated annually to take into account changing market, regulatory and other dynamics.

An outgrowth of the ERM process was establishing an integrated way in which to identify key stakeholders for the company, assess stakeholders’ areas of interest and concern and better understand how these stakeholders perceive the issue of risk as it pertains to our business. We are currently undertaking a structured effort to reach out to these stakeholders and engage in constructive dialogue to develop a shared sense of the major issues of concern as well as a common understanding of the major issues facing PG&E going forward; we are also enhancing existing, and in some cases establishing, working relationships with stakeholders to mitigate these issues.

Corporate Governance

At PG&E, our long-standing conviction is that integrity is fundamental to our success and that transparency is critical to allowing investors and others to make informed decisions about our company. Integrity and transparency create the basis for the trust between our company and the many stakeholders on whom our business depends, including our employees, our shareholders, our customers, our communities and our regulators. Because we believe this trust is essential, we

consistently strive to hold our conduct to the highest standards of integrity and to provide timely and meaningful disclosures about our business and its operations. Not only is this approach necessary in today’s business world, it is the right thing to do.

We act with integrity and communicate openly and honestly.

This belief is one of the key reasons why PG&E has placed significant emphasis on our corporate governance policies and practices and decided to highlight them in this report. Some examples of 2006 activities include the following:

- In response to new Securities and Exchange Commission (SEC) requirements for the 2007 proxy season, PG&E enhanced a number of its disclosures regarding director and executive compensation, related party transactions and general corporate governance in 2006. These enhancements include:
 - Providing a new narrative section in the 2007 Joint Proxy Statement of PG&E Corporation and Pacific Gas and Electric Company called the “Compensation Discussion and Analysis,” which explains the material elements of executive compensation and provides additional information regarding compensation policies and decisions.
 - Adopting a new policy governing Audit Committee review of transactions that involve company directors or officers, or entities that own more than 5 percent of either company’s securities.
 - Amending the Charter of the PG&E Corporation Board of Directors’ Nominating, Compensation and Governance Committee to reflect the new SEC rules.
- To more closely align the interests of directors and shareholders, in 2006, both PG&E Corporation and the Utility adopted director stock ownership guidelines. These guidelines encourage directors to own a significant equity interest in PG&E Corporation within a reasonable time after election to the Board. The stock ownership target is \$200,000, which is measured at the time the stock is acquired or on the first business day of 2007, whichever is later. The time period for directors to achieve this target is five years from the date of election to the Board or five years from December 20, 2006, which is the adoption date of the guidelines. Senior officers of PG&E Corporation and the Utility have been subject to stock ownership targets since 1997.
- To reflect the growing importance of climate change, we amended the Charter of the PG&E Corporation Board of Directors’ Public Policy Committee to include specific oversight of climate change-related issues. This committee has oversight for many areas addressed in this Corporate Responsibility Report, including, but not limited to, corporate philanthropy, supplier diversity, workforce diversity and environment.

Our Corporate Governance Guidelines are published annually in PG&E’s Joint Proxy Statement and are also posted at www.pgecorp.com, along with our Board Committee Charters, director and employee codes of conduct and PG&E Corporation Disclosure Policy. For additional information on directors and Board Committees, please see pages 176 to 179 of our 2006 Annual Report to Shareholders.

Corporate Governance Rankings

PG&E’s corporate governance practices have been evaluated and rated by several institutional shareholder groups and corporate governance organizations. We have received ratings that are well above average compared with other utility companies, as well as general industry companies.

For example, as of the beginning of April 2007, based on the Institutional Shareholder Services (ISS) Corporate Governance Quotient (CGQ) rating system, PG&E Corporation outperformed 100 percent of the utility companies in the S&P 500 index and 98.1 percent of all companies in the S&P 500. ISS is a leading provider of proxy voting and corporate governance data services.

In addition, in February 2007, Governance Metrics International (GMI), a corporate governance research and ratings agency, gave PG&E Corporation GMI’s highest rating (10.0 out of 10.0) in the areas of shareholder rights and remuneration, as well as a very high overall governance rating (9.5 out of 10.0).

The governance ratings issued by ISS and GMI are updated periodically and are determined relative to other utility and general industry companies rated by those organizations. Thus, PG&E Corporation’s ratings may change during the course of the year as a result of changes in those other rated companies’ governance practices, as well as changes in our own governance practices.



PGE is powered by its nearly 20,000 employees, and we must attract, nurture and retain the very best talent if we are going to help our customers and communities flourish in the 21st century, just as we did in the 20th century. As we construct this new future, we are blending the world-class experience and expertise we now have with new talent that comes from outside PG&E. But talent is nothing without a guiding set of values, such as integrity, respect, accountability and honesty. We discount success if it is not earned fairly or does not provide an example of how business should be conducted. We also know that collaboration is crucial to achieve our goals. PG&E shines brightly, but it is a corporate constellation, not a cluster of stars. Looking ahead, we will continue to listen and learn wherever and whenever we can. In the end, that is the best—and only—way to delight customers and energize employees.

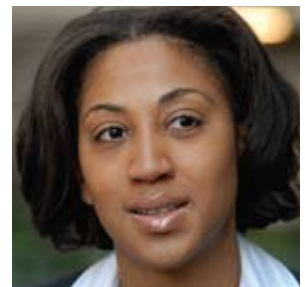
Our Employees

Bringing the Best and Brightest Talent Together

After 100 years in business, PG&E is in the process of creating a new type of utility. To do that, we must be willing to embrace different and nontraditional perspectives. That's why our MBA Leadership Program, in place since 2000, is so valuable. Each year, we try to bring aboard several of the best and brightest young leaders of tomorrow and give them the tools and attention to succeed today. If they thrive, our company and our customers and communities prosper as well.

Kim Webb, a manager in PG&E's Business Transformation Program Management Office, joined the company as part of the MBA Leadership Program.

Won Park, an MBA associate at PG&E, is a project leader on the company's innovative new ClimateSmart program, which enables customers to become "climate neutral" on a voluntary basis. (See page 58 for additional details on ClimateSmart.)



Kim Webb



Won Park

Why is the MBA Leadership Program so crucial to PG&E and its customers?

Webb: I think people are starting to see that the energy sector is in a very dynamic state today. It's where some of the most complex and challenging problems that currently face our society are being addressed and solved. To accomplish this requires great minds, great passion and great people. The MBA Leadership Program gives us a real advantage when it comes to recruiting and retaining talented folks who can break through and make a difference.

Park: A lot of the MBAs have really fresh ideas about how to help the environment, and they want to work with us at PG&E because we are seriously focusing on issues like climate change and energy efficiency and trying to lead the way. We're all determined to do something about global climate change—to take responsibility and help identify and implement the innovative solutions that will be needed both here in California and throughout the world.

What kinds of programs do the MBAs actually get to work on at PG&E?

Webb: Our core jobs could involve anything from work on business transformation to innovative human capital strategies to managing our portfolio of assets; most of us also volunteer for project opportunities that allow us to learn as much as we can about the business.

Park: I've been working on ClimateSmart, which we think can remove at least 2 million tons of CO₂ from the atmosphere over its three-year demonstration period. That's the equivalent of taking 350,000 cars off the road for a year. ClimateSmart provides our customers with the opportunity to take action on global climate change, while also enhancing California's natural environment. What is really exciting about ClimateSmart is that it was developed by employees who care about the issue, understand that our customers do too and thought creatively about how to take a concept and turn it into a workable program. It's these types of activities and innovation that our culture fosters; and it provides great opportunities for folks that work at PG&E.

Do you see yourselves as the next-generation leaders of companies like PG&E?

Webb: Well, we have a long way to go and a lot to learn. But PG&E employees are a great team of people to learn from. And, if we can find some of the solutions, then PG&E's customers will benefit, our communities will benefit and society at large will benefit as well.

Park: We're thinking globally but acting locally at PG&E. This is a good model for the utility industry.

Working Safely and Staying Healthy

Creating a safe and healthy workplace requires designing and maintaining hazard-free workspaces, developing and implementing safe work processes and investing in the appropriate training and equipment to protect our team members. The Utility's multifaceted Safety and Health Program is designed to achieve these goals. The program ensures that we have a systematic means to identify potentially unsafe or unhealthy situations, evaluate alternatives for corrective action and track our progress in avoiding and remedying these situations.



A new climbing technique requires linemen to use a safety belt while climbing. In the past, linemen would not "belt on" until they reached the point where they would be working.

In 2006, the Utility enhanced its Safety and Health Program in the following ways:

- Developed and implemented a new and innovative Safety and Health Management Program, called "Zero-In on Safety," which includes new tools, training and initiatives that are designed to lead the company toward zero injuries.
- Restructured the company's Safety and Health organization, leading to a centralized structure that will result in a more effective and consistent approach to incident prevention and management.
- Implemented a formal Driver's Training Program for employees, focused on reducing the number of motor vehicle incidents involving Utility employees.

The Utility's statistical performance improved significantly in 2006. For example, we reduced our OSHA Recordable Rate by 13 percent, compared to 2005, and cut our Lost Workday Case Rate by more than 14 percent. We also realized continued

Serving Customers Over an Area of 70,000 Square Miles, with a Focus on Safety

Combining safety discussions, vehicle mechanics and a little science, PG&E's "What Happens Next?" program looks at the root causes of large-vehicle accidents and offers practical tips for preventing such accidents.

At a program meeting in 2006, more than 50 Kern Division linemen and troublemen attended a lively and interactive safety tailboard aimed at reducing large-vehicle rollover and raising driver awareness about other issues that can cause accidents such as road conditions, driver distraction, the vehicle's center of gravity and vehicle speed.

Participants reviewed the company's Daily Inspection Report and watched a remote control vehicle demonstrate diverse driving conditions. Doug Rodrigues, Area 3 safety program coordinator, described the aim of the program: "Our goal is to help employees become better professional drivers so they can better serve our customers and safely return to their families at the end of the day."

A Safe Work Environment Fosters Dedicated Employees and Ensures Reliable Service

Delivering electricity and natural gas is a 24/7 operation that—by the nature of the services and the work required to deliver them—inherently presents safety risks and hazards. We aim for an injury- and illness-free work environment for the benefit of our employees, our customers and our communities. Our Safety and Health Policy forms the foundation for the programs PG&E uses to achieve this goal.

This policy requires that

- employees do their jobs with the goal of creating a work and business environment free from injury, illness and property damage for the benefit of employees, customers and the general public;
- employees (1) perform work in a way that protects and promotes the safety and health of themselves, co-workers and the public, and (2) comply with all applicable health and safety laws and regulations; and
- each officer manages effectively the occupational and public safety and health matters concerning business activities for which he or she is responsible.

success in reducing the total number of Lost Workdays, ending 2006 with nearly 8 percent fewer Lost Workdays than 2005. The table below provides complete safety statistics for 2004 through 2006. And while we have made progress over the years, we recognize that zero incidents is our ultimate goal, and we are committed to moving aggressively toward achieving it.

Safety Results for 2004 through 2006

	2004	2005	2006
Total Lost Workdays ¹	60,766	42,639	39,343
Total Lost Workday Cases ²	284	196	177
Total Lost Workday Case Rate ³	1.48	1.04	0.89
Total OSHA Recordables ⁴	1,365	1,142	1,048
OSHA Recordable Rate ⁵	7.09	6.08	5.29

¹ Total Lost Workdays is an internal PG&E metric that counts the number of workdays lost due to occupational injury or illness.

² Total Lost Workday Cases is the number of nonfatal occupational injury and illness cases that (1) satisfy OSHA requirements for recordability, (2) occur in the current year and (3) result in at least one day away from work.

³ The Lost Workday Case Rate measures how frequently new Lost Workday Cases occur for every 200,000 hours worked, or for approximately every 100 employees.

⁴ Total OSHA Recordables is the number of injuries and illnesses that meet OSHA requirements for recordability, i.e., (1) are work-related, (2) are new cases and (3) meet one or more OSHA general recording criteria.

⁵ The OSHA Recordable Rate measures how frequently occupational injuries and illnesses occur for every 200,000 hours worked, or for approximately every 100 employees.

In 2007, we plan to provide safety statistics for PG&E Corporation, in addition to the Utility. We also plan to include data benchmarking our safety performance against others in our industry.

Workforce Diversity and Initiatives

PG&E operates in the most diverse state in the nation. It is our fundamental belief that the remarkable range of backgrounds and life experiences of California's citizens has made it one of the most innovative economies in the world and a leader on the important business, social and environmental matters of the day. And it is this belief that inspires us to foster rich diversity among our employee team; meaningful diversity allows us to achieve our vision of being the leading utility in the United States.

In 2006, PG&E's senior management team reviewed our overall approach to securing the most capable, highly skilled and diverse workforce possible. We recognize that for us to become the company we want to be, we will need an employee team that is composed of individuals who have the confidence and capabilities to work anywhere, do anything and yet choose to be at PG&E. Attracting and nurturing this kind of talent requires the creation of a culture and environment that encourages employees to realize their full potential and produce results beyond expectations. Pursuing a strategy that enhances, fosters and celebrates diversity is critical to realizing this vision.

The strategy developed by our senior management team is based on five key drivers:

- **Market:** The diversity of our customer base is increasing rapidly; our workforce must reflect the marketplace.

- **Talent:** There is an increasing “war for talent” with other utilities, companies and industries; attracting and retaining a diverse, high-quality workforce is critical.
- **Innovation:** Leveraging our diversity to develop breakthrough solutions that will address customer service, distribution and operational challenges is essential.
- **Reputation:** Our reputation and relationship with the diverse communities we serve is crucial to our future growth, profitability and overall viability.
- **Values:** Our behaviors in the workplace must be aligned with our corporate values.

To support this strategy, we are developing and implementing programs and policies to maintain and enhance diversity at PG&E, in all facets of the organization; ensure that all members of our employee team recognize the importance of a diverse

workforce and understand how they contribute to realizing this goal; and prepare the workforce of tomorrow. And, we are communicating our vision and values widely so that all prospective candidates understand the opportunities available at PG&E. For example, PG&E was honored to participate in the 2006 Net Impact conference, hosted by the Kellogg School of Management. The Net Impact conference brings together approximately 1,000 MBA students from over 90 MBA programs to hear from leading businesses, academics and nongovernmental organizations about corporate responsibility in today’s workplace. PG&E provided insight into how our renewable energy programs help to create a sustainable energy future for both California and the nation, as well as the responsibility companies have to ensure that the communities they serve are both healthy and vibrant.

Some other examples of programs, policies and initiatives to foster a diverse workforce include:

- **MBA Leadership Program.** PG&E’s MBA Leadership Program recruits graduates from MBA programs at top business schools that are not only academically distinguished, but also are known for their diverse student bodies. The program puts MBA graduates on an accelerated track, developing them through a series of rotational assignments within PG&E that give them a broad base of experience and knowledge about our business. In 2006, 35 officers and directors, including the Chairman and CEO of PG&E Corporation, visited 5 campuses and met with more than 100 MBA candidates. Seven MBA hires will be joining PG&E in the fall of 2007. These recruits will join the 18 current and graduating members of this program currently working as part of our team.
- **Apprentice Training Programs.** We also cultivate diversity through external partnerships with programs and organizations that work with minorities and women. For example, our partnership with the Center for Training and Careers in San Jose helps prepare and train women for careers in nontraditional occupations at PG&E. Currently nine graduates are working in career-oriented positions.
- **Math Engineering and Sciences Achievement Program (MESA).** In 2005, PG&E agreed to underwrite three MESA postsecondary student leadership conferences through 2008. MESA is a recognized leader in developing

**We respect each other and
celebrate our diversity.**

tomorrow's engineering, technology and management leaders from California's educationally disadvantaged student populations. These events will provide more than 300 math, science and engineering students from community colleges and four-year universities throughout northern California with the opportunity to immerse themselves in leadership and career-building activities. Our collaboration with MESA serves as an outstanding industry-education model. It ensures an improved quality of education for California's diverse student community, and it expands the pool of talent from which PG&E can draw. And, in 2006, PG&E worked in coordination with other members of the California Utility Diversity Council to provide a three-year grant totaling more than \$1.2 million to support internships for MESA students.

- **Sexual Harassment Prevention Training Program.** In 2006, all company officers, directors and managers completed an interactive online Sexual Harassment Prevention Training program consistent with California's aggressive sexual harassment training requirements. The program helps ensure that all company leaders know how to prevent unacceptable harassment from occurring in the workplace and also provides tools to help them communicate with their staff about sexual harassment.

This strategic approach to creating and maintaining a diverse, highly skilled workforce increases our success in representing the communities we serve. As of the end of 2006, PG&E employed approximately 19,700 people. Using Equal Employment Opportunity Commission (EEOC) definitions, PG&E's workforce statistics for 2004, 2005 and 2006 are presented in the following table. The statistics for 2006 are generally consistent with those from 2005.

Representation of Women and Minorities in PG&E's Workforce, 2004–2006

EEOC Category	2004	2005	2006
Women	26%	26%	26%
Officials and Managers	26%	27%	27%
Professionals	35%	35%	36%
Technicians	16%	15%	16%
Minority	35%	35%	36%
Officials and Managers	23%	25%	26%
Professionals	36%	38%	39%
Technicians	31%	32%	32%

Comparison of PG&E's Representation of Women and Minorities to the National Utility Average

Category	PG&E	National Utility Average ¹
Women	26%	25%
Minorities	36%	20%

¹ All U.S. utility companies.

With respect to individual minority representation, PG&E's workforce statistics for 2004, 2005 and 2006 are provided in the table below.

Workforce Representation

	2004	2005	2006
Asian	13%	13%	14%
Black	7%	7%	7%
Hispanic	13%	14%	14%
Native American	2%	2%	2%

Monitoring Results

PG&E is committed not only to putting in place the appropriate policies and networks to attract and retain a diverse workforce, but also to ensuring that implementation of its programs and policies is working. Both internal and external oversight help ensure that PG&E achieves its goal of encouraging diversity.

Internal Monitoring

PG&E has a long-standing commitment to maintain employment policies and practices that meet the highest legal and ethical standards of excellence. Review of our equal employment opportunity and affirmative action policies and performance is one of the roles of the Public Policy Committee of PG&E Corporation's Board of Directors. Ongoing internal oversight that results from the monitoring of our employment practices and procedures helps ensure that our actions are aligned with our high standards of ethical behavior. Reviewing our affirmative action progress, action-oriented programs and good-faith efforts provides key indicators of our compliance—not only with legal requirements but also with our own expectations. For example, PG&E develops and reviews more than 40 Affirmative Action Plans (AAPs) each year to ensure that we are pursuing the appropriate policies and programs to attract and maintain a workforce that is reflective of the communities we serve.

External Monitoring Through Government Audits

The U.S. Department of Labor's Office of Federal Contract Compliance Programs (OFCCP) is responsible for auditing the AAP results of federal contractors, such as the Utility. The company's more than 40 AAPs are subject to potential audits by the OFCCP in any given year. In 2006, the OFCCP initiated audits of six of these AAPs. We have received satisfactory closures on all six of these compliance reviews.

Helping Employees Take Control of Their Careers

To assist employees who may be susceptible to changes in the company, PG&E worked with IBEW Local 1245, which represents nearly two-thirds of our workforce, to develop and implement a job-bidding system. This system first attempts to fill vacancies internally. Employees can submit a pre-bid (name and years of service with the Utility) online where they categorize themselves as an "A-bidder," looking for a job within the same department, or a "B-bidder," looking in another department for a position. In the bidding process, employees can express interest in bargaining-unit positions by submitting transfers for entry-level positions and pre-bids for positions that are above entry-level.

As an example, two meter readers from northern California who were likely to have their positions impacted by the SmartMeter program became proactive and found new roles in the company. Santa Rosa's Steve Kingwell and Petaluma's Joe Cunha took advantage of the company's job-bidding system and were placed in new crews where they received on-site training. Kingwell now works as a fieldman and Cunha is an apprentice welder. The former meter readers appreciate the opportunity to move into a new role and the support PG&E provided.

Recognition for Diversity

As a result of our efforts and achievements in creating and maintaining a diverse workforce and making PG&E a great place to work, we received the following awards and recognition in 2006:

- 30 Best Companies for Diversity — Black Enterprise magazine
- Top 30 Companies for Minorities — Fortune magazine
- Corporate 100 Best Places to Work for Latinos — Hispanic magazine
- Top 50 Companies for Hispanics — Hispanic Business magazine
- Best Places to Work for GLBT Equality — Human Rights Campaign Foundation

Employee Development and Learning

To achieve our vision of being the leading utility in the United States, we must have energized employees, delighted customers and rewarded shareholders. Having a team committed to excellence and innovation—and providing that team with opportunities, skills and support—is essential. We recognize that our people are our greatest asset and that to delight our customers and reward our shareholders, we must energize our employees by investing in their development and well-being with a continuous learning environment that is aligned with rapidly changing business needs. We also must provide a clear indication to our employees of their accountability and our overall expectations, and we must develop and implement programs to retain employees over the long term. Some examples of programs and initiatives enhanced or implemented in 2006 include:

- **Performance Management Program**, which ensures that employees have a clear understanding of their goals and expected behaviors and how those are linked to the company's goals and aligned with our vision and values. Additionally, the program focuses on employee development to ensure that every employee is continually learning and developing to position themselves for future business challenges.
- **Leadership Academy**, which is designed to provide directors, managers, superintendents and first-line supervisors with high-quality workshops dedicated to enhancing their leadership skills. Many of the workshops are led by PG&E officers, and the curriculum is progressive, allowing for the introduction of new workshops as needs are identified.
- **Leadership Coaching**, which is an ongoing partnership designed to help employees throughout the company produce fulfilling results in their professional lives. Through the process of coaching, employees deepen their learning, improve their performance and enhance their quality of life.

We are also working closely with our three labor unions on workforce planning and training. There are regular meetings with the IBEW Local 1245, ESC/IFTPE and SEIU/IUSO to discuss staffing levels, including the filling of new positions and employee training.

We work together as a team and are committed to excellence and innovation.



Tyler Davidson, a former electrician, went through a challenging three-year on-the-job training program to secure his job with PG&E.

One way we are addressing future staffing needs is through an aggressive effort to place employees into apprenticeships which we jointly developed with IBEW Local 1245 and ESC/IFTPE. PG&E currently has 800 employees participating in state-certified programs. Most apprenticeship programs are three years and include both classroom and on-the-job training.

As we anticipate replacing thousands of retiring employees in the years ahead, a critical challenge is ensuring a transfer of knowledge from our existing workforce to our next-generation employees. In response, PG&E has developed a knowledge transfer toolkit and supporting methods aimed at ensuring that, at a minimum, plans are in place for transferring valuable employee know-how to our next generation of employees. We are also looking at ways we can embed knowledge transfer in our daily work activities, giving us another powerful approach to eliminating the risk of knowledge loss, and ensuring service continuity and safe operations.

High Standards and Clear Values Form the Foundation of Leadership

Integrity is the foundation of a responsible company, and a clear commitment to compliance and ethics is an essential element of corporate integrity. PG&E is committed to acting with integrity and aims to set the industry standard for complying with the laws and regulations that govern our business. To achieve this, PG&E has an integrated compliance program that works with all of our operating groups. This is facilitated by the Compliance and Ethics department, which reports to PG&E Corporation's Chief Risk and Audit Officer.

Teamwork, Commitment, Excellence, and Accountability: Employees Exemplify Our Values and Recognize We're Part of the Community

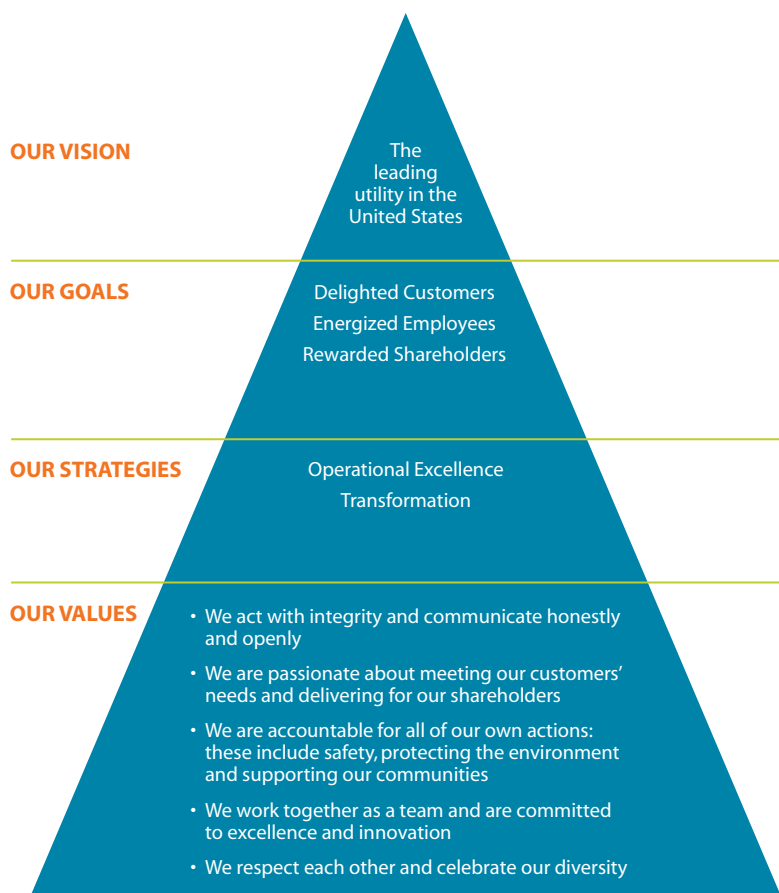
Troubleman Tim Broderius was on-call on December 9, 2006, when the alert came in around 2 a.m. that customer Queena Izzo's power was out. Broderius quickly determined that Ms. Izzo had two broken fuses in her house and replaced them. He explained, "She's 92 years old and was in pain from a recent fall, which broke her wrist. I told her, 'If there's some way I can help you out, I will.'"

Broderius explored assistance options for Ms. Izzo and teamed up with public affairs associate Kathy Lavezzo, who made calls to two PG&E programs for low-income households, CARE and Energy Partners. CARE offers a 20 percent monthly discount and Energy Partners provides no-cost energy-efficient appliances, equipment and weatherization to qualifying customers.

Broderius went back and checked on Ms. Izzo's power, and she mentioned that she had problems getting a flu shot for the winter. Broderius arranged for someone at the San Mateo County Department of Health to come out and give Ms. Izzo a vaccination.

PG&E installed a brand-new heating system, provided free weatherization services and certified Ms. Izzo for CARE. She expressed her thanks: "Tim has been so helpful...I don't know what I could have done to survive without him."

Our Vision and Values



The Compliance and Ethics department provides an infrastructure that enables PG&E's employees to fully comply with all applicable laws, regulations and PG&E policies and standards, and to adhere to high ethical standards in every business decision. In concert with other departments and leadership throughout the company, Compliance and Ethics is providing employees with a clear sense of the values and behaviors critical to achieving PG&E's vision of being the leading utility in the United States. PG&E's values are presented above and featured throughout this report.

Senior leaders at PG&E introduced the values in 2005 through an extensive outreach program with employees. Personal conduct expectations are communicated through our values and annual compliance and ethics training. Our Compliance and Ethics department develops new training each year to address our employees' needs and to respond to their suggestions. In 2006, almost 100 percent of employees completed the annual compliance and ethics training, and nearly 95 percent of those targeted to complete our Business Conduct Questionnaire (BCQ) did so.

PG&E's annual compliance and ethics training is typically conducted in small groups so as to stimulate discussion and share experiences. The trainings are facilitated and are supported by a video created by the Compliance and Ethics department that portrays various compliance or ethical dilemmas that employees may face.

The annual completion of the BCQ is one way in which employees support the company's commitment to ensure that our business decisions and practices reflect high ethical and safety standards, follow our policies and comply fully with all applicable laws and regulations. The BCQ has questions that relate to employee conduct standards in the Code of Conduct Handbook. Completing the BCQ is mandatory for all management employees.

In addition, PG&E's Compliance and Ethics department has produced handbooks on major topics that require detailed knowledge with regard to how to act and work responsibly. Examples include:

- *Code of Conduct: Standards for Personal Conduct and Business Decisions*
- *Protecting the Environment: An Overview of Environmental Laws*
- *Insider Trading: An Overview of Laws and Corporate Policies*
- *Working With Government Officials: Compliance with Political Laws*

In 2006, we revised our Code of Conduct Handbook, which was provided to employees in 2007 and is available at www.pgecorp.com. The handbook outlines our core values, describes our standards of conduct and addresses key regulatory and compliance requirements.

Just as we are committed to ethical business conduct and compliance with applicable laws, regulations and policies, we appreciate and expect equal commitment from our vendors and contractors. For additional information, please visit www.pgecorp.com to view PG&E's Contractor, Consultant and Supplier Code of Conduct.

In addition to these publications, PG&E has identified a person or persons with expertise in each area who is responsible for ensuring compliance with all applicable laws and regulations as they pertain to each issue. For example, PG&E has a manager for political resources, who has the expertise to answer questions and provide guidance to other employees and who is responsible for ensuring that PG&E is in compliance with all state and federal laws surrounding political contributions and management of the company's EnergyPAC.

Finally, we provide opportunities for employees to ask questions and report questionable activities. PG&E's Compliance and Ethics Helpline is available to employees, contractors and customers 24 hours a day. It handled 461 calls in 2006, which is up slightly from approximately 450 in 2005. Calls are handled confidentially, and callers can remain anonymous.

**We act with integrity and
communicate honestly and openly.**



PG&E is woven into the fabric of the communities we serve. And we are working hard to help make those communities—our communities—become thriving examples of the new clean and green ecosystem. This means building connected communities with diversified economies that provide good jobs and good schools and are prepared for the unexpected. It means more sustainable communities with more energy efficiency, more resource efficiency and more innovative solutions that boost the quality of life. Our focus is on California: in its research parks and state parks, its homes and businesses, its schools and conference halls, because that's where our customers, and our employees, live and work. But we believe we can have an immeasurable impact on the rest of the country—and the world, too—because sustainability can improve communities everywhere.

Our Communities

Bringing Energy-Efficient Housing to Our Neighborhoods

PG&E can't develop the sustainable community of the future on its own. We need partners. And since 2005, we have been partnering with Habitat for Humanity. Together, we initiated and implemented the Solar Habitat Program, which provides local Habitat for Humanity chapters with PG&E's charitable grants to cover costs for solar-powered systems on houses they build. This reduces the electricity bills of Habitat's low- and moderate-income homeowners by providing them with the latest solar technology and equipment. In addition to funding and technical expertise, PG&E contributes employee volunteers, who help build the homes. The Solar Habitat Program is part of PG&E's commitment to vibrant, innovative 21st-century communities that resonate with true resourcefulness.

Daryl Lee, the corporate relations officer for Habitat for Humanity's East Bay region, is responsible for the innovative relationship with PG&E.

Vickie Malone, a bakery manager and mother of two, is the new owner of a solar-powered home in the East Bay that has resulted from the PG&E-Habitat for Humanity partnership.



Daryl Lee



Vickie Malone

Why is the PG&E-Habitat for Humanity program so important?

Lee: The partnership between PG&E and Habitat for Humanity not only helps low-income families keep utility costs down, it also helps make more and better energy available to communities and lessens greenhouse gas emissions for everyone. That's really good for the environment. An added benefit we get from PG&E's solar-powered systems is that during the day, they're like mini power plants because they feed energy back into the grid. It's part of building sustainable neighborhoods, communities, cities and nations.

Malone: I have always taken care of my responsibilities, and that's just what I'm doing now. Owning a home is big. If you own your home, you can do anything. I definitely want to be part of the community and help it in any way I can. We all live here together in this environment, so we all have a responsibility to take care of it and make sure it's healthy for everyone.

When you look at Vickie's new house, you realize that this is a real environmental accomplishment, isn't it?

Lee: Absolutely. We're developing 26 solar homes, including Vickie's, on what was an automobile salvage yard. There used to be burned oil tanks, tires, and car batteries all over the ground. We had to dispose of these environmental eyesores and remove 300,000 yards of soil before we could build and before we could even think about PG&E's solar panels or clean energy.

Malone: My aunt, who raised me after my mother died, always said that you get where you need to go if you take it one mountain at a time. I think we're doing that by building these houses, one at a time, and by helping our communities, one at a time.

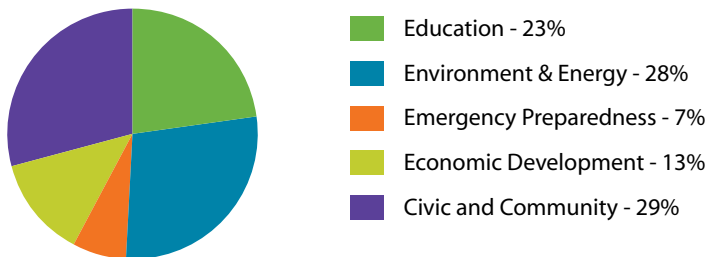
Where does this program go from here? What are the expansion plans?

Lee: PG&E has demonstrated huge support for what we're doing, and has even increased its commitment. We're grateful for that. And all the affiliates of Habitat for Humanity in PG&E's service area can take advantage of this program. Ultimately, we can have a deep impact on many communities. That means helping families with affordable housing and affordable energy—and also helping the environment by using clean solar power that adds significantly to sustainability.

Corporate Philanthropy

By being active members of our communities and supporting organizations and initiatives that create neighborhoods with robust businesses, plentiful jobs, vibrant schools, great parks and a healthy citizenry, we are contributing to a more sustainable society. We give money, time, advice—and technology—to make a difference and improve the quality of life.

2006 Corporate Contributions



In 2006, PG&E increased its shareholder-funded charitable contributions to nearly \$14.7 million from approximately \$12 million in 2005, achieving our goal of contributing 1 percent of pre-tax earnings from operations. And we did it in a way that was responsive to the needs of both the communities and constituencies we serve and provides support for a better environment and more sustainable future. PG&E provided cash grants, in-kind contributions, and other forms of support to nonprofit organizations and government agencies throughout northern and central California; we also contributed to statewide and national organizations. To do this, we worked with communities and local organizations to identify community needs and develop programs that delivered targeted contributions. In 2007, PG&E plans to make charitable contributions of \$18.3 million or 1.2 percent of pre-tax earnings.

In 2006, we targeted five broad areas for charitable giving: education, environment and energy, emergency preparedness, economic development, and civic and community. The chart above provides an overview of the percentage of contributions in each area in 2006.

Within these categories, we directed a significant portion of the contributions to support organizations working in underserved communities. For example, in 2006, approximately 71 percent of our corporate contributions went to organizations supporting low-income communities, people of color, senior citizens, the disabled, the homeless, the working poor and unemployed and the GLBT community. This is an increase of 6 percentage points from 2005. In addition, 21 percent of our

We are accountable for all of our own actions: these include safety, protecting the environment, and supporting our communities.

corporate contributions went to organizations with minority leadership, up from 17 percent in 2005. Going forward, we intend to increase the contributions directed toward assisting the most vulnerable members of our communities.

Examples of PG&E's 2006 contributions include:

- ***Helping California's Schools Use Technology to Reduce Their Environmental Impact and Save Money.*** California's schools face unprecedented challenges—including increased operating costs, reduced funding and pressures to improve the overall educational environment for students. Recognizing this



Students at Evergreen 6th Grade Academy in Paradise, Calif., celebrate their participation in PG&E's Solar Schools program.

challenge, we launched the Solar Schools Program in 2004; this is a shareholder-funded initiative that reinforces PG&E's commitment to renewable energy, education and the need to address climate change in a way that benefits underserved schools, students and the community at large.

The largest program of its kind, Solar Schools provides participating schools throughout northern and central California with a free 1.3-kW solar energy installation and supporting educational materials that help each participating school meet the California Department of Education's standards for science, social studies, math and English. In 2006, we facilitated the installation of solar arrays in 30 schools, trained more than 600 teachers in a solar sciences curriculum and made grants of \$225,000 in support of these efforts. As a result, more than 77,000 students will gain first-hand knowledge of the potential of solar energy and, hopefully, be inspired to pursue educational opportunities in science. In recognition of the success of this program, in 2006, PG&E received the prestigious California Governor's Environmental and Economic Leadership Award.

- ***Contributing Our Expertise and Deploying Advanced Technologies to Help Make Energy More Affordable.*** PG&E's Solar Habitat Program, a partnership between PG&E and Habitat for Humanity, is helping to reduce energy bills for low-income homeowners and making a real contribution to improving air quality and mitigating climate change. Through this program, PG&E is providing expertise, volunteers and charitable grants to help build energy-efficient homes and install roof-top solar-powered systems. This means that these homeowners need to buy less power to meet their basic energy needs, which saves them money and protects the environment.

In 2006, PG&E supported solar installations on 51 homes throughout our service area. These solar panels will each generate nearly 300 kWh of clean, renewable energy from sunlight each month, saving the families approximately \$500 a year; each panel will also help avoid the release of more than 132,000 pounds of carbon dioxide (CO₂) to the atmosphere over the 30-year life of the system. In 2007, this program will be expanded to at least 18 Habitat for Humanity chapters in our service area in northern and central California.

- ***Ensuring Our Customers and Communities Are Prepared for Disasters.*** As an outgrowth of the commemoration of the 1906 San Francisco earthquake, PG&E partnered with the U.S. Geological Survey (USGS), New American Media, the Asian Pacific Fund and the California Earthquake Authority

to translate and distribute culturally appropriate, non-English versions of the USGS document “Putting Down Roots in Earthquake Country”—a primer on how to prepare your family and your home for the next big Bay Area earthquake. In addition, PG&E is hosting a series of town hall meetings with our partners to provide enhanced emergency preparedness information for community-based organizations whose clients are primarily from underserved populations. PG&E is also hosting and contributing its expertise to a series of training sessions for ethnic media outlets so that they are better informed about both how to prepare for an earthquake and how to communicate to their audiences after one strikes.

This effort is an extension of our three-year commitment of over \$1 million to Red Cross Chapters in Northern California to support their preparedness activities for vulnerable populations.

- ***Supporting Our Communities So They Can Build for the Future.*** For the fifth consecutive year, PG&E sponsored its Local Economic Development (LED) grants program, which distributed almost \$400,000 in grants to 62 community-based and governmental organizations to assist in their efforts to build more economically viable communities. These grants were used for a variety of economic and community development initiatives, including business retention, business recruitment, infrastructure planning, downtown improvement, training, Web sites, marketing materials and green business development. Over the past five years of this program, PG&E has provided more than \$1.3 million to 248 LED projects.
- ***Partnering to Educate Tomorrow’s Leaders about the Importance of a Healthy Environment.*** In partnership with the National Fish and Wildlife Foundation (NFWF), PG&E formed the Nature Restoration Trust (NRT) in 1999 to provide grants to community-based organizations and schools for high school environmental education projects. As part of the program, students from participating schools perform hands-on habitat restoration around their communities. In 2006, PG&E and NFWF held the first NRT Conference, which brought together grantees for a series of seminars, panel discussions and “best practices” discussions. California Secretary for Resources Mike Chrisman opened the conference and reinforced that hands-on environmental education at the K-12 level is critical to ensuring a healthy environment for the future.
- ***Partnering with Our Employees to Provide Educational Opportunities for Underserved Youth.*** PG&E partners with its seven Employee Associations to provide opportunities to underserved youth from diverse communities so they can further their education. In 2006, these associations awarded a total of \$136,750 in scholarships, an increase of more than 25 percent from 2005. These scholarships enabled more than 100 youth from throughout our service area to pursue educational opportunities at the college level.
- ***Providing Seed Funding to Audubon California to Support Educational Programs and Habitat Restoration at the 6,800-acre Bobcat Ranch.*** Home to important blue oak, chaparral and riparian habitat, the Bobcat Ranch also connects to the 750,000-acre Blue-Ridge Berryessa Natural Area, a large area of oak woodland and grassland habitat unique to

A bird box is installed with the help of a local student, as part of Audubon California’s large-scale restoration effort at the Bobcat Ranch.



Photo: Audubon California Landowner Stewardship Program

PG&E Helps Establish Northern California as a Leader in Energy Efficiency Research and Technology

In April 2006, PG&E announced that it will give \$500,000 in shareholder-funded contributions to support various programs and projects aimed at commercialization of energy-efficient technologies through a newly created Energy Efficiency Center at the University of California at Davis.

Plans for the establishment of the center were unveiled by the California Clean Energy Fund (CalCEF), which then solicited proposals from universities in northern California to create the world's leading university-based center to advance the efficient use of energy.

PG&E will donate \$100,000 per year over the next five years to the new Energy Efficiency Center. This leadership gift will help launch the Center's aggressive, five-year fund-raising plan and strengthen its ability to support energy-efficiency advances throughout California.

Our contribution will be used to support fellowships to attract a new generation of engineers and entrepreneurs. These fellows will work on emerging technology commercialization partnerships, and support the Center's conferences and outreach efforts. Each year, PG&E will work with UC Davis to target the funds based on its emerging technology successes and the agreed-upon goals of the Center.

Northern California. In 2007, PG&E will be participating with Audubon's Landowner Stewardship Program to enhance native riparian vegetation at the company's natural gas storage facility, located in close proximity to Bobcat Ranch.

- **Supporting the Center for Advanced Research and Technology.** We have helped in efforts to equip high school juniors and seniors from the Fresno and Clovis Unified school districts with the tools necessary to solve local environmental problems. Students collaborated with research and regulatory organizations to restore native habitat, research the effects of temperature and chemical fluctuations on coral, and collect and analyze water quality samples to assess the health of local water bodies.
- **Expanding Employee Giving to More Community Organizations.** In addition to the nearly \$14.7 million in shareholder-funded contributions granted in 2006, PG&E's employees again demonstrated a great commitment to nonprofit organizations in their communities through the company's Campaign for the Community. PG&E expanded its campaign effort with new incentives for employees and increased support from senior management. Donations pledged in 2006 exceeded \$3.2 million, compared with \$2.7 million in 2005. These donations, made by nearly 7,150 employees and retirees, will help support more than 3,000 organizations throughout our service area and beyond.

Volunteering and Demonstrating Community Commitment

PG&E's employees demonstrate commitment to improving the health and well-being of the communities they serve every day, through their actions both on and off the job. Not only do they donate generously to nonprofit organizations, they also give generously of their time. At all levels of the company, we encourage employees to volunteer their time and expertise to support our communities and lend a helping hand. We do this by organizing volunteer events and opportunities, recognizing employees for exceptional commitment and services, and communicating the importance of community service and involvement through our values.

In 2006, we initiated some new programs and enhanced others to better facilitate volunteerism among our employee team, including:

- **Implementing a Web-based program to notify employees and retirees of upcoming company-sponsored volunteer opportunities and allow them to sign up for participation.** This Web site also provides the opportunity for employees to recruit their colleagues to join them in supporting the community.
- **Working with departments throughout PG&E to create volunteer events for employees that build on their interests in specific community needs, and that provide team-building opportunities.** For example, several departmental teams served meals to the homeless at San Francisco's Glide Memorial Church. Also, several PG&E volunteer-teams installed solar panels on Habitat for Humanity homes in support of PG&E's Solar Habitat Program.
- **Supporting PG&E's seven employee associations by providing financial and other forms of support.** The associations banded together in 2006 to promote employee involvement in the 20th Annual AIDS Walk San Francisco. More than 100 PG&E employees participated in a walk that raised \$3.77 million to benefit

Helping Our Customers Manage Energy Costs



Frances Thompson, a supervisor in the Utility's Low-Income Energy Efficiency program, performs an energy audit.

P G&E recognizes that managing energy costs is not easy for all our customers. Competing needs, including food, housing and other essentials, make it difficult for some of our customers to pay their bills, while others are seeking ways to merely reduce the amount they pay for electric and gas service. In addition to the various energy efficiency, demand response, balanced bill payment, weatherization and other cost and energy management options we offer, for the second consecutive year, PG&E provided customers who successfully took steps to cut their natural gas usage during the winter with a rebate on their spring bills.

Customers who qualified for the company's 2006-2007 10/20 Plus Winter Gas Savings Program received bill credits expected to total approximately \$50 million in spring 2007. An estimated 42 percent of eligible residential and business customers qualified for the credit. Qualifying residential customers are expected to receive an average credit of \$20, compared to \$109 for small commercial customers and \$4,537 for large commercial customers.

To earn the 10/20 Plus Program credit, qualifying customers had to reduce their cumulative natural gas usage during January and February below the three-year historical average at their home or business. For every 1 percent decrease in usage, customers received a 1 percent credit up to 9 percent. Customers who reduced their usage by 10 percent or more received a 20 percent bill credit. PG&E is also helping customers reduce their energy use, through conservation and energy-efficiency programs,

including rebates for energy-efficient appliances, on-line energy audits and through programs to help low-income households.

In addition to our 10/20 program, PG&E continued to promote and work with community-based organizations to reach and sign up customers for:

- **California Alternate Rates for Energy (CARE) Program.** This allows income-qualified households to save 20 percent on their utility bills.
- **Relief for Energy Assistance through Community Help (REACH) Program.** This is an emergency assistance program sponsored by PG&E and administered by the Salvation Army that provides financial assistance to low-income customers who experience a sudden or uncontrollable change in their ability to pay their utility bill.
- **Energy Partners.** This is a program offered by PG&E and administered by PG&E-approved contractors that provides eligible low-income households with free weatherization to make their homes more energy efficient.
- **Low-Income Home Energy Assistance Program (LIHEAP).** This program provides financial assistance with energy bills and weatherization projects through local government offices and nonprofit organizations. PG&E is also working with national organizations and elected officials to secure full federal funding for the LIHEAP program so that it can service all those in need of assistance.



Members of PG&E's Employee Associations, colleagues, friends and family participate in AIDS Walk San Francisco.

the San Francisco AIDS Foundation and 43 HIV/AIDS organizations throughout the Bay Area. In addition, the Asian Employees Association, with financial support from the company, participated in San Francisco's annual Chinese New Year's parade—the largest event of its kind outside of Asia, attracting as many as 500,000 people, with another one million watching it on TV.

- ***Providing information on and training for senior management to participate on nonprofit boards.*** By the end of 2006, nearly 80 percent of the company's officers were serving on a nonprofit board or were in discussions about joining one. Moreover, the company's directors were polled about their community interests so that they could be trained about nonprofit board service and nominated to the boards of local nonprofits. The company expects to have at least half of these directors lending their expertise and time to nonprofits by the end of 2007.

Some examples of coordinated efforts currently under way at PG&E to encourage and enhance employee volunteer efforts include:

- ***Partnering with Junior Achievement.*** For four years, PG&E employees have been actively involved with Junior Achievement's Elementary School Program, which provides a first look at how education and economics play a role in the workplace. During the 2005-2006 school year, more than 300 PG&E volunteers spent nearly 2,200 hours in 244 classrooms throughout the Bay Area. These efforts reached 14 different schools and more than 5,600 students.
- ***Protecting and improving the environment.*** Through our Volunteer Program, we work with environmental restoration groups to help identify and coordinate opportunities for employees and their families to take part in



Joined by family, a PG&E employee volunteers at Año Nuevo State Reserve on Earth Day.

projects that help clean up their communities and protect and enhance the environment. In 2006, more than 4,800 employees and their family members participated in various PG&E-sponsored projects, including an Earth Day event in partnership with the California State Parks Foundation. Nearly 900 PG&E volunteers spent Earth Day helping to clean up and restore habitat at 12 California State Parks throughout our service area. Other notable events involved more than 100 employees planting trees in a previously shade-free stretch of San Francisco's Bayview-Hunters Point neighborhood and the more than 250 employees who eagerly descended upon San Francisco's Golden Gate Park to participate in various park restoration projects as part of team-building projects.

- ***Recognizing exceptional commitment and service.*** In 1986, PG&E established the Frederick W. Mielke, Jr., Award, which recognizes employees for outstanding community service and provides organizations selected by the winners with a \$5,000 charitable contribution from the company. In 2006, six employees won this award (see page 37 for details on award winners).

Over the next several years, PG&E intends to implement additional programs and initiatives that will help organizations that can benefit from PG&E volunteers; we will also keep encouraging employees to donate their time, and we will make it easier for employees to do so.

Recognizing Outstanding Community Service

Building better communities is a core value of the six recipients of the 2006 Frederick W. Mielke, Jr., Award. The Mielke Award, established in 1986, recognizes outstanding community service by the company's employees. It is named in honor of Frederick W. Mielke, Jr., who served as Pacific Gas and Electric Company's Chairman and CEO from 1979 to 1986 and was known for his efforts to encourage employees to give back to the communities that PG&E served.

Beginning in 2005, PG&E also partnered with the American Institute for Public Service of Wilmington, Del., to confer the Institute's Jefferson Awards on each of the Mielke Award winners.

In 2006, six employees won the Mielke Award and were also presented with the Jefferson Award for Public Service. These employees epitomize a spirit of partnership, community service and giving.



Jesse Cottonham, a troubleman in Daly City, and his wife, **Pally Cottonham**, a senior compliance consultant in San Francisco. Together, they volunteer at St. John Missionary Baptist Church in Bayview-Hunters Point where they mentor kids through the church's Champions Youth Ministry. Jesse and Pally teach bible study, coach basketball, plan field trips, hold workshops and work with the children's families.



Irene Degl'Innocenti, a senior consulting gas engineer in San Francisco. Outside of work, Irene has devoted herself to the Girl Scouts of America as a troop leader, parent volunteer and leader at the association level for the past 30 years. She teaches the girls to maintain a 50-foot power boat, counsels them on careers in nontraditional jobs at PG&E and prepares them for the annual Redwood City Christmas and Fourth of July parades.



Fred Flint, a geologist in environmental services in San Ramon, acts as coordinator of the Walnut Creek Little League Challenger Division, which works with children with disabilities. Fred prepares newsletters, forms teams, creates schedules, distributes equipment, organizes special events, raises funds and recruits, coaches and manages a baseball team.



John McDougal, a senior land surveyor in technical and land services in Fresno, volunteers with the Children's Hospital of Central California in Madera. After his daughter passed away from a heart condition, John and his wife, Jennifer, were spurred to action. They founded and oversee "An Evening Under the Stars," a dinner-dance that has raised more than \$120,000 for the hospital's heart center.



Mark Rasmussen (third from left), a General Construction electric supervisor in Stockton, whose volunteering efforts benefit the Hospice of San Joaquin. Mark coordinates a holiday fundraiser known as "The Tree of Lights," during which, for the past 18 years, he and other PG&E volunteers have strung thousands of lights around a tree at Delta College.

Creating Successful Partnerships With Diverse Suppliers to Better Serve Our Customers

PG&E’s Supplier Diversity Program helps support local businesses of all sizes and contributes to the overall economic growth and development of California. We partner with our suppliers by providing them with training and networking opportunities that support the development of their businesses.

Since 2004, PG&E has done business with World Wide Technology, Inc. (WWT), a minority-owned business enterprise that works on systems integration of technology solutions and computer hardware. In 2006, PG&E spent more than \$11 million with WWT, which assisted PG&E engineers in designing and deploying the network infrastructure at our new Resource Management Centers (RMCs).

The RMCs have enabled PG&E to centralize and consolidate multiple job functions, including: forecasting, planning, designing, estimating and scheduling. Through our partnership with WWT, PG&E will be better equipped to meet our customers’ needs.



Supporting Economic Vitality Through Supplier Diversity Initiatives

As a major purchaser of goods and services, PG&E has a significant potential to help diverse businesses grow and to strengthen the state and local economies in the communities we serve. PG&E is committed to providing women-, minority-, and service-disabled-veteran-owned business enterprises (WMDVBE or diverse enterprises) with the economic opportunities to supply products and services required by the Utility. In an effort to achieve these goals, PG&E enacted a Supplier Diversity Program in 1980.

In 2006, PG&E achieved its highest level of diversity spending in the 26-year history of the program—\$491.9 million, a \$133.4 million (or 37 percent) increase over 2005. PG&E’s WMDVBE purchases in 2006, as a percentage of overall purchases, were 21.7 percent, compared to 19.4 percent in 2005. And, in 2006, PG&E met the target established by the California Public Utilities Commission (CPUC) for procurement from diverse firms for the first time since 2002.

Most notably, significant improvement was achieved in spending with minority-owned business enterprises (MBEs). The 2006 total of \$333.8 million, or 14.8 percent of our overall spending, represented a \$97.9 million (or 42 percent) increase over 2005. The largest increase in MBE spending went to business enterprises run by minority men. Spending with this group in 2006 totaled \$259.9 million, a \$98.8 million (or 61 percent) increase over 2005. Spending with business enterprises run by women in 2006 also expanded, totaling \$137.2 million, or 6 percent of our overall expenditures. This represents a \$35.7 million (or 35 percent) increase over 2005.

Diverse Supplier Spending Targets

Category	CPUC Target (%)	PG&E’s 2006 Results (%)
Minority Men	12	11.4
Minority Women	3	3.3
Minority Business Enterprise (MBE)	15	14.8
Women Business Enterprise (WBE)	5	6
Subtotal Women, Minority Business Enterprise (WMBE)	20	20.8
Service-Disabled-Veteran Business Enterprise (DVBE)	1.5	0.9
Total WMDVBE	21.5	21.7

PG&E’s success in meeting our diverse supplier spending targets was the result of an outreach strategy, the foundation of which rests on targeted partnerships with our communities. For example, we work collaboratively with community organizations to increase training, certification and contracting opportunities for diverse suppliers. To facilitate this, PG&E added six members to the supplier diversity department in 2006. And, while we initiated new efforts, we continued our work with key organizations that foster and support the growth of WMDVBE suppliers, such as the California Hispanic Chamber of Commerce, the United States Pan Asian Chamber of Commerce, the California Black Chamber of Commerce, the American Indian Chamber of Commerce, the Women Business Enterprise National Council and California Disabled Veteran Business Enterprise Alliance.

Partnering for a Greener San Francisco



In 2006, PG&E proposed an unprecedented and far-reaching partnership with the city of San Francisco to develop alternative energy sources, reduce greenhouse gas emissions and foster sustainability. The partnership relies on six key points to enhance the city's energy future:

- Expanding PG&E's Solar Schools and Solar Habitat Programs by investing at least \$2.5 million in San Francisco by 2010;
- Investing at least \$5 million for new solar installations in the city, including PG&E's own service center;
- Working with ocean-power innovators to explore the use of natural tidal resources as another source of clean, renewable energy;
- Supporting economic development efforts to promote green businesses and clean-energy technologies in San Francisco;

- Enabling our customers to become "climate neutral" through ClimateSmart, propelling the city toward its greenhouse gas reduction goals; and
- Turning Treasure Island and Hunters Point into model sustainable urban communities.

PG&E's goal is to provide innovative solutions to help make San Francisco the greenest city in the nation. In San Francisco alone, PG&E has helped interconnect almost 500 customer-owned solar systems. PG&E is also collaborating with San Francisco to bring an enhanced, multi-year energy-efficiency program worth \$11.5 million to the city and our energy customers.

To complement these efforts, PG&E introduced a new outreach initiative, "Let's Green This City," to serve as a community resource detailing the many ways that residents can contribute to San Francisco's greening efforts. While we have started in San Francisco, we will be expanding our efforts to help the other communities we serve become even more sustainable.

Overall, in 2006, PG&E participated in 103 outreach events and partnered with 25 organizations to promote opportunities for diverse suppliers and increase the pool of qualified diverse suppliers available to PG&E and other businesses in California. These events and partnerships resulted in PG&E awarding a multi-year contract to Twining Laboratories, a disabled-veteran business enterprise located in Fresno. PG&E also awarded a multi-year contract to Stillwater Sciences, a woman-owned business that provides environmental studies, licensing of hydroelectric projects and biological consulting for endangered species.

Looking ahead, PG&E has worked with a woman/minority-owned firm with extensive supplier diversity program development, education, implementation and outreach experience to develop a revitalization strategy for 2007 and beyond, focused on the economic development benefits of supplier diversity. Key components of the strategy include: executive leadership and commitment, employee engagement, an effective communication plan and targeted outreach in areas where diverse procurement performance is underutilized.

PG&E will hold internal training for directors and managers in 2007 to ensure that all decision-makers understand the business case for supplier diversity. In addition, Supplier Diversity will launch focused legal and financial efforts to increase procurement opportunities for diverse suppliers.

Through these efforts and initiatives, we hope to increase our supplier diversity to 25 percent of total procurement by the end of 2007 and 30 percent by 2010.

Keeping Our Communities Safe

Creating a safe environment for our customers and communities is as important to us as the safety of our employees. PG&E continues to have a comprehensive Public Safety Information Program that focuses on increasing awareness about the safe and proper use of gas and electricity, as well as helping to keep those working around utility lines safe from harm.

This program distributes user-friendly materials in multiple languages to convey important safety messages. We also identify creative and attractive ways to provide these materials to our target populations.

Some examples of our programs and 2006 activities include:

- **SafeKids School Safety Program.** Over the past seven years, PG&E has provided free safety education materials to teachers in more than 85 percent of the schools in our service area. This past year alone, more than 800,000 students in almost 5,300 elementary and middle school classrooms received our materials. Teachers regularly comment that the materials are fun and effective in helping them teach their students the importance of gas and electric safety.
- **Contractor and Agricultural Worker Outreach.** PG&E continues to provide safety training materials to contractors and agricultural workers throughout our service area. These materials include bilingual brochures, posters and videos. Over the past five years, more than 140,000 contractors and 60,000 agricultural

Providing Nuclear Power Safely and Reliably for the Benefit of Our Customers



Located in San Luis Obispo County, Calif., PG&E's Diablo Canyon Power Plant (DCPP) provides approximately 24 percent of the electricity used by PG&E's customers and fulfills roughly 12 percent of the state's power requirements.

DCPP generates electricity safely and reliably. It also provides an affordable source of non-greenhouse gas-emitting power, which will help PG&E meet its climate change goals. With high safety and performance ratings from the Nuclear Regulatory Commission and the Institute of Nuclear Power Operations, DCP continues to be a safe and efficient nuclear power plant. In 2006, DCP had a 94.8 percent capacity factor (actual energy produced versus maximum plant capacity).

PG&E and DCP employees are committed to protecting public health and safety. A highly trained and well-armed security force guards the station using sophisticated electronic security and surveillance systems. Employees provide training and support to the San Luis Obispo County Office of Emergency Services, which led to the installation of battery back-up systems on the county's early warning sirens to ensure appropriate notification in any emergency situation the county may face. To ensure continued safety and reliability, PG&E is investing more than \$1 billion to install new steam generators, reactor vessel heads and a dry cask waste storage system at the plant.



DCPP employs 1,400 full-time workers that support the local community and environment. Employees contribute nearly \$500,000 every year to local charities and other nonprofit organizations, and the plant adds more than \$700 million annually to the local and state economies. DCP maintains 12,000 acres of land that is home to many species of plant and animal wildlife, and employees participate in Earth Day, coastal cleanup, the annual migratory bird count, tidal pool studies and other similar initiatives.

Looking ahead, DCP is addressing the challenge of the storage and disposal of nuclear waste. PG&E is constructing an on-site, dry cask system at DCP to safely store used fuel until the federal government opens a permanent storage facility. The issue is undergoing review at the Nuclear Regulatory Commission.

For additional information on waste storage and other issues, please see page 106 of our 2006 Annual Report to Shareholders.

workers have received these materials through their employers. In addition, PG&E continues to work with trade associations and safety groups statewide to help distribute safety information directly to their members.

- **Emergency Preparedness.** PG&E works closely with organizations like the Red Cross and local city emergency preparedness councils to provide brochures and other materials that help explain how to prepare for an earthquake, how and when to shut off utilities, and why it's necessary to have an emergency kit beforehand. These efforts have been highly valued by the organizations, as well as by the people, receiving the information.

For our efforts, PG&E continues to be identified by regulators and our peer utilities as having a "best-in-class" public safety information program.

Environmental Justice

In order to be responsive to our customers and communities, we must first understand their concerns and they must understand our intentions. Producing, transporting and distributing natural gas and electricity to more than 15 million people over 70,000 square miles requires power plants, thousands of miles of pipelines and transmission and distribution wires, thousands of vehicles and other equipment necessary to maintain this infrastructure and deliver this service.

The facilities used to serve our customers are often close to population centers to ensure reliable power and efficient service. Our goal is to balance the need to maintain and enhance these facilities for customers with the responsibility to understand and respect the needs of our neighbors. Our efforts to strike this balance are guided by a formal environmental justice policy and program. This policy and program requires that we seek meaningful involvement from stakeholders, train and educate employees on environmental justice and related issues, and focus on managing facilities in an environmentally responsible manner, in compliance with all laws and regulations, and in a way that minimizes impacts on adjacent communities.

PG&E's pledge to corporate responsibility includes a continuous effort to work more effectively with our customers and communities and to make a positive difference.

Examples of our environmental justice policy in action during 2006 included the following:

- ***The closure of PG&E's Hunters Point Power Plant after years of collaborative work with the local community.*** PG&E invested more than \$300 million to complete nine transmission projects to facilitate closure of the plant. The California Independent System Operator (CAISO) determined that these transmission upgrades were necessary to ensure electric reliability for our customers in San Francisco and the greater Bay Area. Once the CAISO determined that the plant was no longer necessary to maintain electric reliability, it ceased operation. PG&E voluntarily committed that it would demolish the plant and remediate the site to meet standards for residential use, becoming one of the first utility companies in the country to make such a commitment.



(From left) Pacific Gas and Electric Company CEO Tom King and San Francisco Mayor Gavin Newsom “shut off” the Hunters Point plant at a community ceremony.

As part of our continued commitment to the local community, PG&E and its prime contractor, TRC Solutions, are hiring local residents and providing them the necessary training to dismantle the facility. In addition, PG&E joined San Francisco’s CityBuild program, a workforce training initiative designed to provide construction-related job training and employment to city residents. As of the end of 2006, 47 percent of PG&E’s contractor dismantlement team were graduates of CityBuild and lived in the neighborhoods surrounding the plant. In addition, 30 percent of the contract value, approximately \$7 million, will be spent with diverse suppliers, and seven of the subcontractors on the dismantlement team are local companies.

Finally, this work is being augmented by a community outreach effort, spearheaded by a Project Advisory Committee that includes approximately 30 neighborhood and community leaders and meets monthly with the project team to obtain firsthand information and discuss issues of importance to the community.

- ***PG&E reached an unprecedented agreement with the Fort Mojave Indian Tribe, which was publicly shared at a historic gathering.*** PG&E expressed regret for the spiritual consequences to the Tribe when it built a wastewater treatment plant near the Topock Compressor Station in the Mojave Desert. The treatment plant, built by PG&E at the direction of state environmental regulators, serves as an interim protective measure to ensure that a chromium plume does not reach the Colorado River (see page 63 for details).

The treatment plant is located within a larger area of unique spiritual value to the Fort Mojave Indian Tribe. As part of the agreement, the Tribe dropped its lawsuit against the Utility, and PG&E promised to be more sensitive to tribal cultural and spiritual values. The company also agreed to remove the treatment plant and restore the site upon implementation of a final remedy to address groundwater contamination. PG&E will also transfer the property on which the plant is now located to the Tribe and pledged to consult with the Tribe on all aspects of the site investigation and remedy development and implementation process. PG&E also agreed to educate all workers and contractors on the site as to the Tribe’s spiritual concerns regarding the area in which they work.





Combating climate change, conserving habitat and cleaning up our air and waterways are issues that demand prudent but forceful action. They are also issues that demand innovative thinking, doing things differently and working constructively and collaboratively with others. We recognize this, and that is why we work with a host of partners in government, industry, academia and the environmental community to find the solutions to achieve these goals. The results have been rewarding: we provide our customers with some of the lowest-emitting electricity in the country and we continue to find new and innovative ways to maintain and expand our infrastructure while minimizing our impact on the environment. Looking ahead, we are determined to keep growing our business while developing the environmental solutions that will sustain our communities and society.

Our Environment

Bringing Our Leadership to Bear in a Low-Carbon Economy

PG&E is committed to being transparent and open in all its dealings on the environment. We also seek a variety of viewpoints on this complex and challenging issue. Our relationship with Ceres—a national network of investors, environmental groups and other public interest entities working with companies to address sustainability challenges such as global climate change—is one of the ways we achieve this. We believe in continuous learning and improvement, and we have learned a lot from Ceres on how to keep raising the bar, as the following conversation shows.

Mindy Lubber is president of Ceres. An environmental lawyer for 28 years, Lubber has built public interest groups, served as an environmental litigator, ran a socially responsible investment firm and worked for the U.S. Environmental Protection Agency.



Mindy Lubber

What is your mission at Ceres?

Lubber: I've been a change agent, and my sense of how we most effectively make change right now is by bringing different players to the table, working collaboratively, looking for unique solutions and getting to "yes"—and that's what we do at Ceres. Ceres is an organization that strives to build sustainability ethics and practices into the largest corporations in the world.

How do you define sustainability?

Lubber: Sustainability means the ability to keep building our planet—and I don't mean this only from an environmental perspective. It means having the resources we need to move forward. It means using our resources smartly. It means developing sustainable companies that take into account environmental justice and worker rights and safety. It means being able to build a future economy—as well as a future environment—that can sustain the kind of work and businesses we want to run.

What does it take to translate this into action?

Lubber: When I hear PG&E Corporation's CEO, Peter Darbee, talk about the fact that his leadership on global warming has motivated his workforce at PG&E to go above and beyond their job performance, that's about building a sustainable and smart corporation.

The challenge is to ensure that this is ingrained in all parts of the organization and is used to drive innovation and creative thinking going forward.

You often talk about sustainability as a corporate governance issue.

What do you mean?

Lubber: It's very clear to the board members of hundreds of companies that there are huge financial implications involved with taking on, and being part of, solutions for global warming, water shortages and loss of biodiversity—all of which have a profound impact on whether businesses can keep growing. For years, the climate issue was viewed as only a scientific and environmental imperative—not one of shareholder value or financial transparency. And disclosure is critically important, as is finding ways to articulate your position clearly; both enhance credibility and provide opportunities for new partnerships and joint ventures.

What caused the "tipping point" on climate change? Why do so many people care about this issue now?

Lubber: I believe we are now at critical mass in word—not deed. I still don't feel like the world is acting fully on ways to bring down our carbon footprint by 70 percent. But we have acknowledged the problem and there is awareness and clarity around the issue. How did it crystallize? I think part of it was just time. I also think Hurricane Katrina was a horrible marker in our lifetime, particularly when scientists were saying that storms are more intense because of global warming and the change in our ocean temperatures. Other things—like a heat wave in Europe that killed more than 20,000 people four years ago and a slew of forest fires in California that cost

people their homes—were very vivid. They made people realize what the real-life consequences of this are and could be. And, I think “An Inconvenient Truth,” Al Gore’s film, was very influential. It has worked its way into the modern-day media and is being discussed by kids and lay people who are not scientists.

What should the utility industry be doing to make a difference?

Lubber: The utility sector needs to be looking at every opportunity that can be gained from energy efficiency and demand management. PG&E is really leading here. People should use energy smartly and use less of it. We are a long way from having maximized our energy-efficiency capability.

When it comes to the environment, how do you see the relationship between companies and communities?

Lubber: We have a long history in our country of putting our environmental problems in the communities of the people who could least afford them. PG&E’s willingness to tackle environmental justice issues, set goals and look at what the company is doing and the impact it has on communities speaks to its leadership—not only on climate change, but from a broad sustainability perspective.

What would you like to see from PG&E going forward?

Lubber: I think it is important for PG&E to clearly identify its goals and targets for things like customer energy efficiency, renewable power and greenhouse gas reductions. And, it is extremely important to quantify the business benefits and growth opportunities of achieving these objectives. There is a real opportunity to support and advance the linkage between economic growth and environmental protection. I think it has been borne out in a lot of what PG&E has done; sharing this information more widely will drive others to follow.

Bringing Energy-Efficient Technologies to Market

In addition to maximizing energy savings today, PG&E is actively working to identify the next generation of energy efficient technologies—helping to accelerate the spread of promising new innovations in the market. PG&E's goal is to move new products through the "pipeline," so they can quickly be commercialized with rebates and incentives for residential and business customers.

With an annual Emerging Technologies program budget of \$3.7 million, PG&E is targeting more than 60 technologies in various stages of development and deployment. Each technology is carefully evaluated to confirm that it will save energy as claimed and be accepted by our customers.

Several emerging technologies were deployed in 2006, including stairwell light fixtures that have two different illumination levels. This energy-efficient lighting is designed to replace conventional stairwell lighting, which runs constantly and wastes energy illuminating stairs, alcoves and landings that are often unoccupied. The bi-level lights operate at a low standby mode and use motion sensors to instantly activate to full lighting levels when someone enters the stairwell. Using new PG&E rebates in 2006, the University of California and California State Universities ordered more than 1,000 of the fixtures for campus buildings, for an expected energy savings of 245 MWh per year of operation.

Other emerging technologies now entering PG&E rebate and incentive programs include energy-efficient desktop computer power supplies, high-performance lighting for classrooms and energy-saving cooling systems for computer data centers.

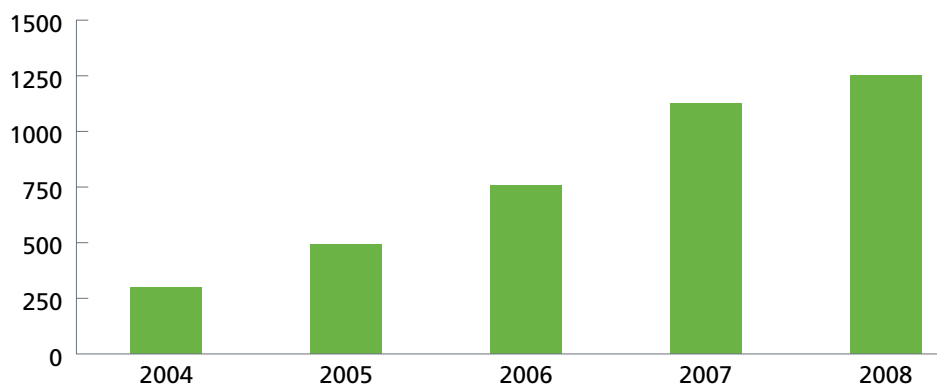
As a provider of electricity and natural gas to approximately 40 percent of Californians and one in 20 Americans, we recognize that the way we produce and deliver our products and serve our customers has a direct impact on the environment.

A healthy environment is necessary for the well-being and vitality of our customers, employees and the communities we serve—as well as society at large. That is why our environmental commitment extends beyond compliance; it requires that we raise the bar for ourselves and that we work with others to do the same. With this challenge comes many exciting opportunities, including further securing America's long-term economic prosperity, reducing our dependence on unstable parts of the world and fostering innovative new technologies.

Putting Efficiency First

Using energy more efficiently is the fastest, most cost-effective way to reduce greenhouse gas emissions. And, in 2006, PG&E celebrated our 30th anniversary of helping customers and communities do just that, saving them money at the same time. Over this time period, PG&E's customer energy-efficiency efforts, both electric and natural gas, have achieved significant cumulative lifecycle energy and cost savings, on the order of \$9 billion, and prevented approximately 125 million tons of carbon dioxide (CO₂) from entering the atmosphere.

Customer Energy Efficiency¹ Gigawatt-Hour Savings: Historic and Target²



¹ We expect to meet approximately half our demand growth through Customer Energy Efficiency.

² Our Customer Energy Efficiency programs and other efforts have helped keep California's per capita electric consumption essentially flat for 30 years, while per capita electric consumption nationally increased 50 percent.

In 2006, we also began a new chapter by launching a \$1 billion commitment that will extend until 2008—the largest energy-efficiency effort of its kind by a U.S. utility company. We were spurred by the CPUC, which challenged PG&E to reach record-high energy savings targets for this ambitious customer program.

To meet the aggressive 2006-2008 targets, PG&E undertook a new, forward-thinking business model that focused squarely on the customer experience. Our approach

employs a strategy successfully used by financial planners as they work to understand their clients' individual financial goals, resources, needs and limitations.

Using an integrated portfolio strategy, PG&E worked with our customers and partners to not only meet but exceed the aggressive 2006 energy savings targets agreed upon with the CPUC. Targeting customers in naturally occurring market segments is a key element of the strategy.

2006 Energy Efficiency Portfolio Savings

	2005 Actual Savings	2006 Goal	2006 Actual Savings ¹	2006 % of Goal
Megawatts	115	132	142	107
Gigawatt Hours	459	677	777	115
Million Therms	5.6	10.16	10.69	105

¹ PG&E's actual energy savings are on file with the CPUC in our Dec. 2006 Monthly Report (Revised March 2007).

PG&E's energy-efficiency portfolio mix includes a diverse array of rebate programs, financial incentives, training and education, emerging technology projects, development and advocacy of codes and standards for buildings and appliances, marketing and outreach, and program evaluation activities. This allows PG&E to reach customers in many ways—through rebates on purchases of energy-efficient appliances as well as through partnerships that focus on providing specific energy-efficiency services to targeted customers.

We are working through our Pacific Energy Center in San Francisco, Energy Training Center in Stockton, and Food Service Technology Center in San Ramon to promote new technologies and educate our customers on the latest energy efficiency options.

Highlights from 2006 included:

- Making the connection between energy efficiency and climate change through the Sonoma County Energy Watch Partnership, one of 22 innovative partnerships with local governments and state entities throughout our service area. The goal of the Partnership is to realize significant energy savings by leveraging Sonoma's ambitious commitment to reduce greenhouse gas emissions throughout the county.
- Working directly with manufacturers and retailers to promote and increase sales of ENERGY STAR® qualified compact fluorescent lamps, which use 66 percent less energy than traditional incandescent lamps.
- Joining 15 other California electric and gas utilities, state policymakers, and key stakeholders in support of the National Action Plan for Energy Efficiency. If implemented, the plan's recommendations could help avoid greenhouse gas emissions equivalent to over 35 million vehicles.
- Contributing \$500,000 in shareholder funding to a new Energy Efficiency Research Center at the University of California at Davis. (See page 34 for details.)

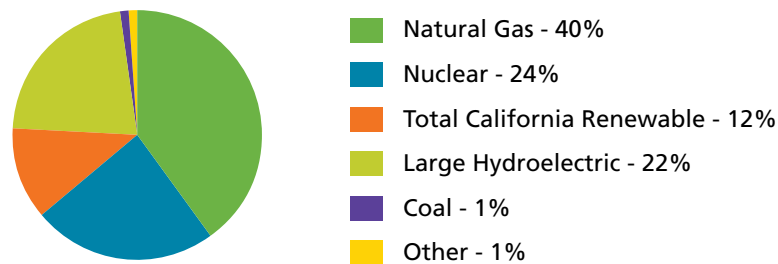
Planning for California's Clean Energy Future

Following California's Energy Action Plan, PG&E has designed a broad energy strategy to meet its customers' future power needs in as environmentally responsible a manner as possible. The strategy relies first on an aggressive expansion of customer energy-efficiency and demand-side management programs; then it looks to secure additional renewable power resources; and, finally, it seeks to fill the remainder of customers' energy needs through traditional, but ever more efficient, generation sources.

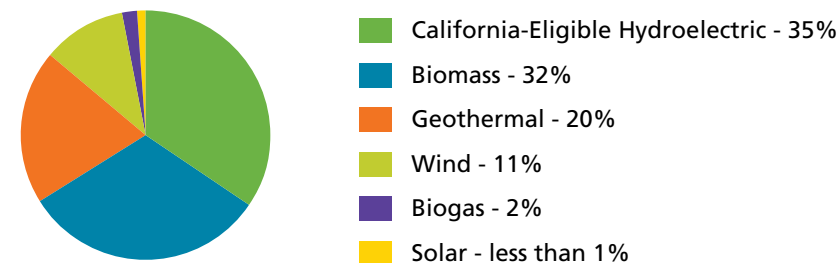
Meeting Our Customers' Electricity Needs

To meet the needs of our customers, we generated more than 34,000 GWh of electricity from PG&E-owned natural-gas, hydroelectric and nuclear facilities in 2006. To supplement our owned generation, PG&E procured power from a variety of sources to satisfy a total customer demand of nearly 76,700 GWh.

PG&E's 2006 Electric Power Mix Delivered to Retail Customers



PG&E's 2006 California-Eligible Renewable Resources



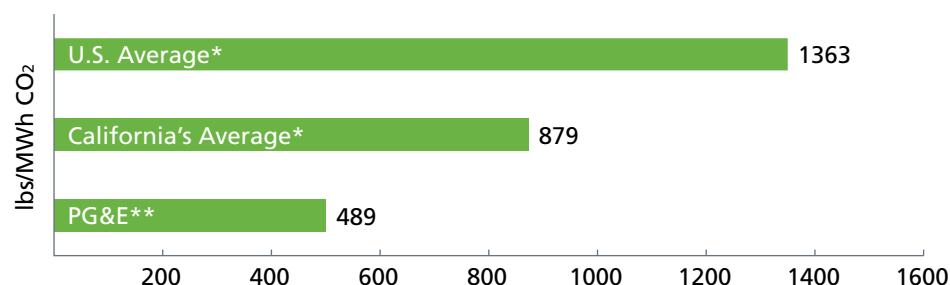
As defined in Senate Bill 1078, which created California's renewable portfolio standard, an eligible renewable resource includes geothermal facilities, hydroelectric facilities with a capacity rating of 30 MW or less, biomass, selected municipal solid waste facilities, solar facilities and wind facilities.

As the chart indicates, more than half of the electricity we delivered to customers comes from sources that emit no or low amounts of greenhouse gases; a significant amount comes from large hydroelectric power stations (which, under California law, do not qualify as an eligible renewable resource). When these facilities are factored into the power used to serve our customers, PG&E's sales of California-eligible renewable resources—plus large, noneligible hydroelectric—were approximately 34 percent in 2006.

Delivering Some of the Nation's Cleanest Power

PG&E delivers some of the cleanest electric power of any major electric company in the United States. In 2005, the carbon dioxide (CO₂) emissions rate of our owned electric generation was 44 pounds per megawatt-hour (lbs/MWh), while the independently certified CO₂ emissions rate associated with the power we sold to customers was 489 lbs/MWh. By comparison, the national average CO₂ emissions rate for all power generation was approximately 1,363 lbs/MWh, while the California average CO₂ emissions rate was approximately 879 lbs/MWh.

Benchmarking Greenhouse Gas Emissions for Delivered Electricity



* Source: U.S. Environmental Protection Agency eGRID Version 2.1 (updated April 2007 and based on 2004 data).

** 2005 emissions rate for our delivered electricity was independently certified and registered with the California Climate Action Registry.

For our owned generation, PG&E's nitrogen oxide (NO_x) emissions rate was 0.06 lbs/MWh in 2006, compared to an estimated national average of 1.99 lbs/MWh; our 2006 sulfur dioxide (SO₂) emissions rate was 0.00388 lbs/MWh, compared to an estimated national average of 5.22 lbs/MWh. We had no reportable mercury emissions.

We also continue to work to minimize the emissions associated with the transmission and distribution of electricity. Sulfur hexafluoride (SF₆) is an extremely potent greenhouse gas, approximately 22,200 times as potent as CO₂. It is used as an insulating material in high-voltage circuit breakers.

In 2006, PG&E significantly reduced our SF₆ emissions through a variety of innovative techniques and process improvements, including piloting the use of X-ray technology to more efficiently inspect the internal components of circuit breakers; implementing a program to reduce the low SF₆ alarm threshold on our circuit breakers, which allows us to identify leaking units much sooner; verifying SF₆ levels in our circuit breakers on a monthly basis to more quickly flag potential leaks; and evaluating a new 72 kV circuit breaker that contains no SF₆ gas, which could potentially replace more than 360 breakers currently in service, each containing 20 pounds on average of SF₆.

Since 1998, we have reduced our SF₆ leak rate by 84 percent and our absolute emissions by 76 percent. To achieve these reductions, we worked in partnership with the U.S. Environmental Protection Agency (EPA) and others through the U.S. EPA's SF₆ Emission Reduction Partnership, of which we were a Charter Member.

Renewable Portfolio Standard—Contracts Signed in 2006

Project	Location	Technology	MW	GWh/Year (low)	GWh/Year (high)
HFI Silvan	La Pine, OR	Biomass	20 to 40	71	142
Liberty Biofuels McCarthy Family Farms	Lost Hills, CA	Biofuels	5 to 10	35	70
Bottle Rock USRG	Ukiah, CA	Geothermal	17 to 55	119	385
IAE Truckhaven	Salton Sea, CA	Geothermal	49	366	366
Global Common– Chowchilla	Chowchilla, CA	Biomass	9	72	72
Global Common– El Nido	El Nido, CA	Biomass	9	72	72
Northwest Geothermal– Newberry	Newberry, OR	Geothermal	60 to 120	420	840
Calpine Geysers ¹	Sonoma and Lake Counties, CA	Geothermal	200	922	922
Tunnel Hydro	El Dorado County, CA	Hydro	0.6	2.1	2.1
Buckeye Hydro	El Dorado County, CA	Hydro	0.4	1.4	1.4
Eden Vale Dairy	Kings County, CA	Biogas	0.15	1.3	1.3
Bio Energy LLC	Fresno, CA	Biogas	2 to 44	15	350
Microgy	San Joaquin Valley, CA	Biogas	4 to 44	35	350
Palco	Scotia, CA	Biomass	7	36	36
Total			383 to 588	2,168	3,610

¹ Part of the Geysers contract replaces 722 GWh of the Calpine 2002 contracts for a net of 922 GWh.

In 2006, PG&E began delivering clean, renewable wind energy from a PPM Energy site in Solano, Calif.



Photo courtesy of PPM Energy

Securing Renewable Power Resources

In 2006, PG&E made significant progress toward meeting our renewable energy goal of supplying 20 percent of our customer needs with qualifying renewable resources, consistent with California's renewable portfolio standard (RPS). In 2006, more than 9,100 GWh of the power we delivered to customers came from California-eligible renewable resources (including eligible hydroelectricity that we own); this represented approximately 12 percent of our total retail sales.

PG&E is actively adding renewable electric power resources to our supply of delivered power. We secured more than a dozen contracts in 2006 with the potential to provide more than 500 megawatts of renewable resources. We are finalizing negotiations from our 2006 Request for Offers (RFO) and launched the 2007 RFO (our fifth solicitation) in March 2007.

We are also aggressively pursuing the most promising next generation of renewable energy technologies, and are dedicated to accelerating their development. We see a lot of potential for solar energy, with new, lower-cost, higher-volume solutions being developed worldwide. Additionally, PG&E launched a new initiative to generate significant amounts of renewable energy from animal waste. And, we are working on projects to convert abundant California agricultural and forest trimmings to clean energy.

Wave power also holds great potential, as PG&E's service area borders approximately 600 miles of Pacific coastline. We are evaluating many different promising technologies that could cost-effectively convert the energy of the oceans into electricity over the next decade. The next generation of renewable energy offers many possibilities.

Seeking to build on these efforts, PG&E proposed a \$30 million Emerging Renewable Resources Program to the CPUC in our 2006 Long-Term Procurement Plan. If approved, this program would enable PG&E to ramp up efforts to identify and support new technologies and resources, and assist promising technologies in overcoming developmental barriers with the goal of expanding renewable supplies and reducing costs over the long term.

Investing in Cleaner Conventional Sources

PG&E is also investing in state-of-the-art, cleaner sources of fossil fuel-based power to meet growing demand. In 2006, we unveiled a comprehensive investment strategy in electric infrastructure to ensure years of clean, reliable future electricity supplies for our customers. PG&E reached a key milestone by executing agreements to purchase 2,096 megawatts of new, highly efficient electric power generation for operation in 2009 and 2010.

In addition, PG&E will build, own and operate the new 530-megawatt natural gas-fueled Gateway Generating Station—the first new power plant we have constructed in nearly 20 years. The facility offers a number of environmental advantages, including a “dry-cooling” technology to avoid use of river water for cooling purposes. Also, the combined cycle technology will decrease fuel use and greenhouse gas emissions in comparison to conventional fossil-fuel power plants. Compared to older plants, the new plant will yield 35 percent less CO₂ for every megawatt-hour of power produced.

PG&E also plans to repower its existing Humboldt Bay Power Plant with a new, environmentally superior generation facility. PG&E will own and operate the new 163-megawatt power plant upon completion of construction, which is expected in mid-2009. The modern technology selected will allow the new power plant to provide a flexible and reliable supply of electricity for local residents that will be 35 percent more efficient and produce 90 percent fewer ozone precursors than the existing plant, while eliminating the need for once-through ocean-cooling utilized by the existing plant.

Delivering Natural Gas

PG&E's 4.2 million natural gas customers consumed approximately 828,550 million cubic feet (MMcf) in 2006. Natural gas is a clean-burning fuel that is used in a wide variety of applications, including heating homes, cooking meals and driving manufacturing processes.

With more than 40,000 miles of natural gas distribution pipelines and 6,000 miles of transmission pipelines, PG&E operates one of the largest natural gas distribution networks in the country and takes seriously our responsibility to ensure its safety and integrity. As part of this commitment, PG&E is working to reduce greenhouse gas emissions associated with the delivery of natural gas.

“Got Gas?”—California's Dairy Farms Offer Opportunities for New, Environmentally Responsible Forms of Energy

Energy from animal waste is one of the newest and most innovative ways PG&E is realizing its renewable energy goals. Through a cutting-edge initiative, bio-methane from dairy manure will be sent through California's natural gas pipelines. Doing so will provide renewable energy and produce important climate benefits by preventing methane from escaping to the atmosphere.

This innovation holds significant promise for PG&E because California is the nation's largest dairy producer and largest energy consumer. It is also a step toward developing an important renewable energy source from California's vital agricultural sector.

In 2006, PG&E achieved a major milestone by signing an agreement with Microgy, Inc., to supply up to 8,000 mcf of pipeline-quality renewable natural gas daily; all the gas will be generated by facilities in California. Microgy plans to construct four state-of-the-art production facilities on the site of large dairy farms in California and interconnect those systems to PG&E's extensive gas pipeline network. PG&E also signed an electricity purchase agreement with a dairy bio-digester to take electricity generated onsite.

Both agreements illustrate PG&E's commitment to explore a number of options to provide project developers maximum flexibility and PG&E's customers maximum benefits.



Natural gas contains more than 95 percent methane, a powerful greenhouse gas that is 21 times more potent than CO₂. As an active member of EPA's Natural Gas STAR Partnership, PG&E has continued to reduce the methane leak rate from our natural gas pipeline operations, preventing the release of more than 670 tons of methane or approximately 14,066 tons of CO₂-equivalent in 2006. This compares to an avoided release of more than 1,000 tons of methane in 2005—a reflection of PG&E's continued improvements and the fact that the largest opportunities for reductions have already been captured.

In addition to replacing pipelines, PG&E reduces methane emissions through cross compression, a process by which natural gas is transferred from one pipeline to another during large pipeline construction and repair projects. Cross compression reduces the amount of natural gas vented to the atmosphere by 85 to 90 percent. In 2006, PG&E used the cross compression technique five times throughout our system. And finally, PG&E is looking at alternative sources of "natural gas" for our customers by pursuing opportunities to utilize bio-gas in our system. PG&E's service area is one of the richest in the country in terms of the potential for bio-gas, and we have entered into an agreement with Microgy, Inc., to tap this vast resource.

Partnering to Accelerate Innovation

PG&E leads the nation with the largest number of customer-owned and connected solar power systems. In 2006, PG&E interconnected more than 4,300 of these systems to the electric grid, bringing the total to nearly 15,000—another way we partner with our customers to keep California a world leader in clean, renewable energy.

PG&E also welcomed the adoption of the California Solar Initiative by the CPUC, an ambitious program designed to boost the amount of customer-installed



Located in West Sacramento, Tony's Fine Foods features the largest privately owned solar power system in northern California.

solar capacity in California. The goal of the statewide program is to install 3,000 megawatts by 2017. PG&E began administering the program in 2007.

The California Solar Initiative greatly expands upon another existing program—PG&E’s Self-Generation Incentive Program—which offers financial incentives to help customers offset much of the cost to install clean and/or renewable distributed generation projects; this includes solar, wind, fuel cell, or cogeneration systems 30 kW or larger. Through this program, in 2006, nearly 130 customers received incentives of more than \$69 million for clean and renewable technology projects totaling more than 37 MW.

Demonstrating a commitment to the community, Tony’s Fine Foods in West Sacramento sought an innovative technology to hedge future energy bills, maintain the quality of its perishable food, and provide a clean energy source. Working closely with PG&E, the deli and bakery product specialist exceeded this goal by installing a 1 MW photovoltaic system and applying more than \$3.5 million in PG&E rebates to create the largest, privately owned solar power system in northern California. Over its 30-year projected lifetime, the system will generate enough solar electricity to meet more than half the company’s electric needs while avoiding the release of 10,000 tons of CO₂ emissions to the atmosphere.

In addition, PG&E was a major sponsor of the California Clean Tech Open, a business-plan competition designed to accelerate the creation of clean technology companies in California. PG&E pledged to provide \$15,000 toward the Energy Efficiency prize, energy system testing services from its world-class Technical and Ecological Services laboratory, as well as 4,000 square feet of office space for the energy efficiency and renewable prize winners.

And finally, through PG&E’s first-of-its-kind Agricultural Internal Combustion Engine Conversion Incentive Program (AG-ICE), we continued to help improve air quality, reduce greenhouse gas emissions and enhance the quality of life for a growing number of communities in the San Joaquin and Sacramento valleys. During 2006, interest in the program—which encourages agricultural customers to convert from diesel-powered irrigation pumps to electric pumps—continued to grow. In total, PG&E received more than 1,400 AG-ICE applications, which, over the useful life of the systems, has the potential to reduce more than 750,000 tons of CO₂ emissions. PG&E’s innovative AG-ICE program won California’s prestigious Governor’s Environmental and Economic Leadership Award in 2006.

Working Collaboratively and Creatively to Address Climate Change

Our Climate Change Commitment

PG&E is committed to leading by example when it comes to climate change. That means more than just minimizing the greenhouse gas emissions from our operations. It also means maximizing the opportunity we have to establish responsible policies and programs that address global climate change.

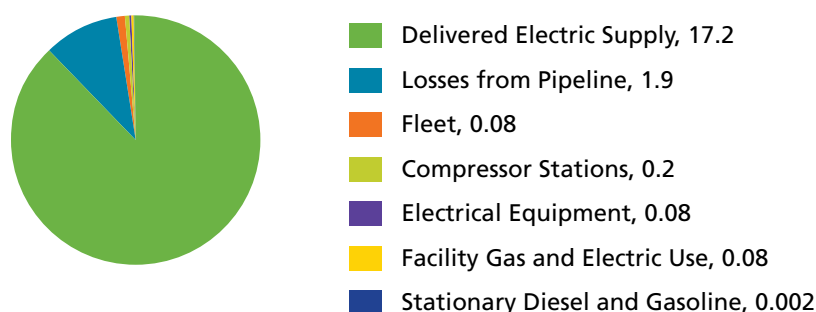
Putting Our Climate Change Commitment Into Action

We recognize that climate change threatens to significantly alter the physical environment for this and future generations. We also recognize that the electric and natural gas industry is a significant contributor to greenhouse gas emissions and has a responsibility to find solutions and take action. This approach to climate change was a driver in 2006, when we took the following actions:

Understanding Our Greenhouse Gas Emissions and Being Transparent

We believe that investors, policymakers, stakeholders and customers need to understand how we view the issue of climate change and the steps we are taking to mitigate our emissions and identify emerging business trends; this will allow them to make informed decisions about PG&E. Toward that end, we continued

Total 2005 Greenhouse Gas Emissions by Source Category (Total: 19.5 Million Metric Tonnes CO₂-e)



our participation in the California Climate Action Registry (Registry) and, in 2006, became the state's first investor-owned utility to certify our entity-wide greenhouse gas emissions for all six greenhouse gases (CO₂, methane, SF₆, N₂O, HFCs, and PFCs). (Please see the chart above for greenhouse gas emissions by source category.) Also, in 2006, we certified the CO₂ emissions rate associated with our 2005 electric delivery mix—489 lbs CO₂/MWh.

PG&E also worked cooperatively with the Registry to develop a protocol for measuring and reporting emission reductions associated with various types of forestry projects. These protocols will be used to support PG&E's ClimateSmart program, which provides our customers with the opportunity to make their energy use climate neutral. PG&E also began work with the Registry to develop a protocol for measuring and reporting on emission reductions associated with the capture and use of methane from dairy cattle manure. Methane from dairy cattle manure provides significant promise as a form of bio-gas for use in our pipeline system.

In addition to understanding and reporting our emissions sources to the Registry, we also took steps to more broadly articulate our approach to climate change. For example, PG&E received an invitation from the Carbon Disclosure Project (CDP) in 2006 and was pleased to provide a submission. The CDP serves as an information

clearinghouse on what companies are doing to mitigate the risk associated with climate change as well as to identify emerging business opportunities. PG&E plans to participate again in 2007.

Finally, PG&E developed and released a document discussing our views on climate change, the process we undertook in developing these views, and our proposals for moving the U.S. forward and into a leadership role on this issue. The document, *Global Climate Change: Risks, Challenges, Opportunities and a Call to Action*, was made available on our Web site (www.pgecorp.com), mailed to all our employees and distributed broadly to our stakeholders—including elected officials, regulators, customers, investors, community leaders and other interested parties.

Proactively Reducing Our Greenhouse Gas Footprint

PG&E has one of the cleanest electric-generation operations in the industry. By making cost-effective energy efficiency a priority, we first look to meet our customers' energy needs by utilizing the ultimate emissions-free resource. Also, with significant hydroelectric and nuclear resources, the CO₂ emissions rate for our generating operations is now among the lowest of any utility in the country. When factoring in the power we purchase from other sources—a growing portion of which comes from California-eligible renewable resources—the emissions rate associated with the electricity we deliver to our customers is approximately 60 percent less than the average among utilities nationwide.

In addition to the steps we are taking to ensure some of the lowest greenhouse gas emitting power in the country, we are also working to reduce our overall emissions footprint.

Here are some of the actions that PG&E is now taking; we believe these actions will continue to yield benefits in combating climate change and reducing energy consumption.

- Continuing our participation in EPA's SF₆ Emission Reduction Partnership; this program has helped us reduce our SF₆ absolute emissions by more than 76 percent since 1998.
- Continuing our active participation in EPA's Natural Gas STAR Partnership; this program has helped us reduce the methane leak rate associated with our natural gas pipeline operations and enabled us to avoid the release of more than 14,000 tons of CO₂-equivalent in 2006. As part of this program, we are sharing best practices associated with cross compression, a process by which natural gas is transferred from one pipeline to another during large pipeline construction and repair projects.
- Leveling the playing field for low-emissions sources by analyzing the greenhouse gas emission implications of competitive bids for long-term electric contracts. This approach monetizes the emissions associated with the electricity so we can determine the relative financial risks associated with the greenhouse gas emissions from various generation sources.

Finally, in addition to these activities, PG&E is currently assessing the impacts of California Assembly Bill 32 (AB 32), the Global Warming Solutions Act, on our current

Closing the Loop With Biomass

PG&E's sustainable forestry efforts on more than 52,000 acres of company-owned watershed lands are helping to achieve both business and environmental goals. Through timber harvesting, thinning, and forest restoration projects, PG&E generates significant quantities of biomass—treetops, limbs, cull logs and brush—that cannot be made into lumber.

An important resource, this biomass is helping PG&E meet its renewable energy goals. We are closing the loop by sending wood chips, cull logs and other biomass to co-generation plants that generate renewable power for the state's electricity grid. Two of PG&E's 2006 timber harvests in the Pit River area produced enough biomass to meet the electricity needs of more than 4,000 average-sized homes for a month.

Removing biomass from PG&E's timberland also reduces the risk of wildfires and helps create a vigorous, healthy forest. Biomassing promotes growth and vitality on the remaining trees, benefits forest ecological systems by improving biodiversity and finds a productive use for woody material that would otherwise be left in the forest to decay.

Through proper forest stewardship, PG&E aims to break even on its biomass management efforts, and did so in 2006. Looking forward, PG&E will continue to utilize biomass as part of an integrated sustainable forestry strategy, which factors economic, community and environmental considerations into every decision we make.



PG&E's sustainable forestry operations near the Pit River generate biomass, a source of renewable electricity.



Tom King, CEO of Pacific Gas and Electric Company, joins (from left) California Governor Arnold Schwarzenegger, San Francisco Mayor Gavin Newsom and former New York Governor George Pataki at an AB 32 signing ceremony in San Francisco.

and future electric delivery mix, as well as other aspects of our business. AB 32 requires California to reduce statewide greenhouse gas emissions to 1990 levels by 2020. PG&E is actively participating in AB 32's implementation process and will take the necessary steps to meet the reduction targets established by the legislation.

Empowering Our Customers to Take Action

In 2006, PG&E received approval to implement ClimateSmart—a new and innovative voluntary program that will provide customers with the option to neutralize greenhouse gas emissions associated with their energy use, thereby protecting California's environment and contributing to state and local efforts aimed at fighting climate change. ClimateSmart is scheduled to launch in summer 2007. Conceived and developed by a team of PG&E employees to provide additional, environmentally responsible products for our customers, ClimateSmart allows residential and business customers to sign up voluntarily and pay a small amount on their monthly utility bill based on energy usage; the payment will fund environmental projects aimed at removing CO₂ from the air. The amount removed from the air will equal the amount of greenhouse gases associated with the customer's energy use, thus making them "climate neutral."

PG&E anticipates that ClimateSmart will receive approximately \$20 million in its first three years, and the goal is to remove two million tons of CO₂ from the atmosphere. This reduction would be the equivalent of taking 350,000 cars off the road for one year. PG&E will invest in a range of emission reduction projects, including conserving and restoring California's forests, and all reductions will be certified using rigorous criteria established by the Registry.

Working With California and Federal Officials on Responsible Policies

While we have worked cooperatively with local, state and federal partners to achieve significant greenhouse gas reductions and avoid emissions, we recognize that voluntary initiatives alone will not be enough. PG&E believes that effectively combating global climate change will take sustained and coordinated international action, cooperation and investment over the long term. To accomplish this, we believe that it is critical for the United States to take a leadership role and enact

mandatory climate change legislation that is both environmentally effective and economically sustainable.

For example, PG&E is an active member of the Clean Energy Group, a coalition of progressive energy companies advocating a national, mandatory and market-based program to reduce greenhouse gas emissions. In the 109th Congress, the Clean Energy Group supported the Clean Air Planning Act, which would have established mandatory limits on CO₂ emissions from the power sector. Also, in 2006 PG&E participated with 10 other leading businesses and four leading environmental nongovernmental organizations as part of the U.S. Climate Action Partnership to develop a set of policy principles and a legislative framework for a federal, market-based, mandatory climate change program.

And, while we prefer a national approach to addressing climate change, we also recognize the important role that states can play—in terms of acting as a catalyst for federal legislation, bringing forth innovative ideas and approaches to tackle the complexities of the issue, and making progress toward combating climate change. That is why we worked constructively with the California legislature and the Administration to enact AB 32, the Global Warming Solutions Act, and were the first major utility to support its passage. We also supported passage of SB 1368, which requires that all power sold to utilities in the state under long-term contracts meet a greenhouse gas emissions performance standard that is equivalent to that of an efficient, combined-cycle natural gas plant. Implementation of these two pieces of legislation will ensure that California continues on a path of reducing its overall carbon footprint and challenging its businesses to do the same.

PG&E is working cooperatively with the CPUC, the California Air Resources Board and the California EPA to implement these groundbreaking pieces of legislation in a way that maximizes environmental effectiveness, minimizes costs, provides for economic opportunities and serves as a model for federal legislation.

Identifying Potential Impacts of Climate Change on Our Business

As part of PG&E's Enterprise Risk Management strategy, we plan to take an integrated, structured approach to evaluating the projected impacts of climate change on our business and the communities we serve—from the threat of more frequent and intense heat waves to reductions in summer snow pack in the Sierra Nevada mountain range, which supplies the state's hydroelectric system. This analysis will be incorporated into our overall risk management program, which is managed by PG&E Corporation's Chief Risk and Audit Officer.

Promoting Stewardship of California's Natural Resources

As one of California's largest landowners, we take the quality and stewardship of the region's water, land and other natural resources to heart. We strive to exceed stringent legal requirements by protecting lands for future generations, preserving habitat for wildlife and providing opportunities for responsible recreation on our lands.

As its sole funder and an active member on the Board of Directors, PG&E is partnering with the Pacific Forest and Watershed Lands Stewardship Council

Conserving Water through Alternative Cooling Systems

Traditionally, many power plants have employed once-through or other “wet” cooling technologies using water from sources such as ground water, municipal water, rivers and oceans to cool excess heat from the power generation process. In addition to placing pressure on limited available water resources, wet cooling can also impact local water quality and aquatic species and habitats.

In 2006, PG&E operated three facilities that use seawater for once-through cooling: Diablo Canyon, Hunters Point, and Humboldt Bay. Hunters Point was closed in May 2006. And PG&E plans to repower its Humboldt Bay Power Plant by 2009 with a new state-of-the-art generation facility, which, among other benefits, will eliminate the need for once-through ocean cooling utilized by the existing plant.

In contrast to wet cooling, dry-cooled power plants use air to cool and condense process-related steam. By evaluating the use of alternative cooling systems, such as “dry” cooling, for new facilities, PG&E can provide sufficient capacity to meet California’s growing electricity needs without impinging on local water supplies.

In 2006, PG&E announced plans to employ dry-cooling technology at the Gateway Generating Station, a new highly-efficient 530-megawatt combined cycle natural gas-fueled power plant to be built, owned, and operated by PG&E. The dry-cooling technology will use 97 percent less water and produce 96 percent less discharge than a conventional water cooling system, avoiding the use of river water for cooling purposes.

PG&E has also contracted to construct the Colusa Generating Station, a dry-cooled 660 megawatt combined-cycle natural gas-fueled power plant. This plant will be owned and operated by the Utility.

PG&E also established a 10-year contract to purchase power generated at a plant relying on secondary effluent (waste water) supplied by the City of Hayward’s Water Pollution Control Facility, located across from the plant site. To close the loop, cooling waste water from the power plant will subsequently be returned to the city’s facility for reuse.

PG&E is evaluating a variety of alternative cooling options for its new power plants, recognizing that there can be tradeoffs for different technologies in different applications. For example, some dry-cooling systems may reduce overall plant efficiency, unless other modifications are adopted. However, taken as a whole, these new technologies will continue to offer benefits to PG&E, our customers, and the environment for years to come.



PG&E’s state-of-the-art Gateway Generating Station will feature dry cooling technology, among other environmental advantages.

to permanently protect more than 140,000 acres of watershed lands associated with our hydroelectric system and the 655-acre Carizzo Plains in San Luis Obispo County. Significant progress was made in 2006 on a Land Conservation Plan for the property, which the Council is expected to adopt in 2007. Additionally, the Council piloted a set of Youth Investment Grants, awarding \$2.25 million to 57 organizations that serve more than 38,000 young Californians; among the grants was a \$150,000 award that helped the Daly City Parks and Recreation and Jefferson Unified High School District purchase alternatively fueled eight-passenger vans to transport youth to school programs and also help them access outdoor experiences.

Responsibly Managing Our Land and Hydro Facilities

Over the last six years, PG&E has received and implemented new federal licenses for six of its hydroelectric generation facilities located in the Sierra Watershed, with up to six more expected by 2008. Implementation of terms and conditions contained in these new licenses, as well as PG&E's ongoing environmental stewardship actions, has had a profoundly positive effect on water quality and temperature, sensitive species habitats and other natural resource attributes.

Examples of stewardship activities in 2006 include:

- ***Working toward the recovery of the endangered Shasta crayfish*** through a cooperative effort with the U.S. Fish and Wildlife Service and others. The project, conducted in association with PG&E's Pit 1 and Hat Creek Project federal licenses, removed more than 1,500 non-native signal crayfish during 2005 and 2006; this moved us closer to the goal of eradicating all non-native crayfish from a designated set of ponds and enhancing populations of endangered Shasta crayfish.
- ***Working at Butte Creek in close collaboration with resource agencies and others*** to successfully protect record numbers of threatened salmon and steelhead through the July heat storms, part of a larger salmon restoration effort.
- ***Surveying more than 50 bald eagle nesting territories*** as part of a long-term statewide effort to monitor our national symbol, a threatened and endangered species. For the past 25 years, PG&E has led various conservation initiatives, including developing tailored nest territory management plans, to protect bald eagles at our facilities. Today, PG&E's hydroelectric facilities support about one-quarter of the state's entire breeding population of bald eagles and our work has significantly contributed to the U.S. Fish and Wildlife Service's consideration of de-listing this important species.
- ***Contributing \$30,000 to help fund a study to find the best ways of removing fish barriers and restoring water flows on Alameda Creek***, with the goal of someday restoring steelhead runs on the creek and its tributaries. PG&E has pledged to also make its natural gas line crossing passable to fish as part of a comprehensive plan to restore the riparian habitat of Alameda Creek.
- ***Partnering with the Solano Land Trust*** to prepare a natural resource baseline report for 2,315 acres of the Eastern Swett and Vallejo Swett Ranches. These studies included the red-legged frog, burrowing owl, sensitive vegetation, public access and grazing that will be used to prepare detailed management plans and habitat enhancement projects.



Breeding bald eagles in California have increased from a low of only about 30 pairs in the early 1980s to over 200 pairs today.

- **Supporting California Proposition 84** and contributing \$25,000 toward the voter-approved bond measure that will invest in the state’s natural resources—benefiting our customers and employees. Consistent with our environmental values, the measure will provide critically needed funds to ensure the availability of safe drinking water, improve local water supply reliability, strengthen flood protection and preserve California’s natural landscapes.

With the largest privately run hydroelectric operation in the nation, there are some challenges as well. PG&E’s 9-megawatt Potter Valley Project requires an ongoing balance of competing water demands for fisheries, agriculture and water supply on the Eel and Russian rivers. For nearly 100 years, the project has diverted water from the Eel River to the East Branch Russian River. Many people have come to rely on this water diversion for agricultural and water supply needs.

In 2004, the Federal Energy Regulatory Commission (FERC) amended PG&E’s license to keep more water in the Eel River to benefit endangered salmon and steelhead. Initially, PG&E misinterpreted the amended license and diverted more water to the East Branch Russian River than specified in the license. We fully reported these over-diversions to FERC and have taken steps to ensure our operators precisely comply with the license, which will leave water users on the East Branch Russian River with less water than originally anticipated. PG&E will comply with the project license while continuing to work with all resource agencies and Eel and Russian river interests to try to minimize impacts on any particular stakeholder.

Migratory Bird Protection Program

The goal of PG&E’s Migratory Bird Protection Program is to protect migratory birds and threatened and endangered birds to the greatest extent possible, while reducing outages and increasing reliability for our customers. As part of the program, PG&E has documented and mapped Raptor Concentration Zones throughout our service area.

Since 2002, PG&E has retrofit more than 10,000 existing utility poles with “bird-safe” equipment; we have also retrofit thousands more poles in high-risk areas where we have experienced a bird incident or outage. All new poles and replacement poles in the Raptor Concentration Zones are also built “bird safe.”

Bird Protection Program (Bird-Safe Retrofits)

	2004	2005	2006
Poles Planned	2,000	2,050	2,075
Poles Completed	2,023	2,073	2,117
% Poles Completed	101%	101%	102%

Using helicopters, PG&E is also doing cutting-edge work to protect the endangered California condor. Through long-lining helicopter techniques, PG&E is installing bird flight diverters in Big Sur—one of the largest applications of its kind on the West Coast. The procedure, developed by PG&E in conjunction with IBEW Local 1245 and approved by the California Occupational Safety and Health Administration, is one of the most innovative techniques some PG&E employees



Demonstrating the latest best practices, PG&E is using helicopters to install measures to protect the California condor in hard-to-reach coastal locations.

have seen in 20 years. It allows PG&E to mark high-risk collision lines for condors in hard-to-reach areas of California's Central Coast. Monterey County, Ventana Wildlife Society, California State Parks and the U.S. Fish and Wildlife Service partnered with PG&E on this innovative effort.

Water Consumption and Management Practices

Fresh water is a finite resource and requires care in California—from the management of storm-water runoff to the design of alternative cooling water systems at power plants. At PG&E, we are making strides to protect and conserve this valuable resource by implementing a variety of water conservation activities and storm-water best management practices programs.

For example, in 2006, PG&E began using "portable" bridges to allow trucks and equipment to cross rivers and streams for PG&E's timber management program; we are one of the first utilities to implement such an approach. By using the portable bridges instead of culverts or earthen fill, PG&E is reducing the amount of sediment going into the watercourses, thus protecting water quality and fisheries' habitat. Moving forward, the bridges will be made available to other company departments for use during construction projects where watercourses need to be crossed.

Storm-Water Management

In California, storm-water runoff is a serious problem, with rainwater "running off" the landscape into nearby lakes, rivers, wetlands and coastal waters (as well as groundwater)—potentially transporting pollutants along the way. Recognizing the importance of this issue, in 2006, PG&E rolled out a storm-water best management practices (BMP) program for our service centers; the goal of the program is to reduce and eliminate pollutants such as sediments, oil, grease and trash from entering storm drains, culverts and waterways. The BMPs were developed based on a detailed assessment of our service center operations and involved input from numerous lines of business.

PG&E's Topock Compressor Station

PG&E's Topock Compressor Station is located in San Bernardino County, about a half mile from the Colorado River. Consistent with industry practice at the time, hexavalent chromium was used at Topock in the cooling towers to prevent corrosion. Beginning in 1951, untreated wastewater from the cooling towers was discharged into a nearby dry wash prior to implementation of a treatment system in 1964. Over time, the previously discharged hexavalent chromium reached and contaminated the groundwater aquifer. PG&E's monitoring program continues to show no presence of hexavalent chromium in the Colorado River.

PG&E has been monitoring the groundwater plume for several years and has been working cooperatively with state and federal regulators and other interested parties to evaluate and remedy this groundwater contamination. In early March 2004, state regulators required PG&E to begin operating a ground water extraction system as an interim protective measure to ensure that the chromium plume is hydraulically controlled so it does not reach the Colorado River. In July 2004, PG&E initiated treatment of the hazardous groundwater prior to offsite disposal and, subsequently, expanded the groundwater extraction and treatment system. That expansion was completed in July 2005 and includes a treatment plant, which cleans the extracted groundwater so it can be re-injected into the groundwater aquifer.

There are several potential options for a long-term remedy, including expanding the groundwater extraction system and using in-situ treatment to remove hexavalent chromium from groundwater in place. PG&E is working with state and federal regulators and key stakeholders to complete the evaluation of contamination at Topock and develop alternatives for the final remedy in an expedited manner.



Portable bridges, like this one crossing the Stanislaus River, minimize impacts to water quality and habitat from PG&E sustainable forestry operations.

To help raise awareness about the program, PG&E provided training for more than 8,500 fleet, construction and operations staff—highlighting steps they can take in everyday operations to protect water quality. In parallel with the program, we launched a storm-drain stenciling campaign—where storm-drains at the company’s 172 service centers were stenciled to provide a visible reminder for employees.

Linking Energy Efficiency and Water Conservation

At certain PG&E customer facilities—such as food processing plants and wineries—saving water can also reap huge energy and cost-saving rewards. Every gallon conserved through an industrial process improvement can save energy through a reduction of water pumped, water heated and water treated prior to discharge.

In 2006, PG&E worked closely with Sonoma Wine Company on its plans to double production at an existing custom bottling facility. The integrated design recommendations being implemented by the company will earn \$260,000 in energy efficiency incentives, save \$266,000 on gas and electricity each year, and save enough water to eliminate the customer’s need to build additional treatment ponds and apply for additional water discharge permits.

Such projects reduce both water and energy use, and PG&E is developing a pilot to expand upon existing programs to save the energy “embedded” in water. For example, a significant amount of energy is used to collect, treat and distribute water to customers, and then to collect and treat the wastewater. More efficient appliances and fixtures, such as low-flow showerheads, high-efficiency clothes washers and low-flow pre-rinse spray valves help customers save money, water and energy; these appliances and fixtures also reduce the amount of natural gas used to heat water.

To target water-embedded energy savings, PG&E is partnering with East Bay Municipal Utility District, Santa Clara Valley Water District and Sonoma County Water Agency.

In addition to insulating their wine tanks, a planned roof above Sonoma Wine Company’s tank farm will catch and divert rainwater from their treated waste stream.



Photo courtesy of Sonoma Wine Company.

Driving Innovation With Plug-In Hybrid Vehicles



Demonstrating leadership, PG&E took significant steps to promote plug-in hybrid vehicle (PHEV) technology in 2006. Not yet commercially available, these innovative vehicles differ from conventional hybrids because they contain a much larger battery that can be “plugged in” to a standard outlet; as a result, they gain increased fuel efficiency and reduce greenhouse gas emissions.

We are proud to be a founding member of Plug-In Partners, a national organization committed to the commercialization of PHEVs, and we are joining with our customers to demonstrate demand for these vehicles. That’s why we sent all 5.1 million PG&E electric customers a bill insert encouraging them to pledge their support for PHEV technology at pluginpartners.com. We are also working with auto manufacturers to bring plug-in hybrid vehicles to market on a production scale, which will reduce costs and make them more available.

As a key step, PG&E is assessing the new technology in our own fleet. In 2006, we took delivery of a Plug-In Prius. Achieving 100 miles per gallon when fully charged, the vehicle can be plugged in at night when excess renewable power is available from the grid. Raising awareness, PG&E showcased the vehicle to customers and other stakeholders during 2006 at community events, environmental fairs, electric vehicle association meetings and other venues.

PG&E also signed on as one of 14 U.S. utilities to test a new hybrid utility service truck; we placed the vehicle into service in San Francisco, where it helped perform routine and emergency overhead line work. PG&E is also partnering with the Electric Power Research Institute to conduct a plug-in pilot project for an F550 Super Duty Trouble Truck and a field trial of two DaimlerChrysler plug-in hybrid Sprinter vans. Both the service truck and trouble truck offer a unique benefit—the ability to operate the boom, lights and other auxiliary power from a battery versus generating diesel emissions. This way, the trucks can operate quietly—and emissions-free—at neighborhood job sites.

Looking to the future, we are also exploring a vehicle-to-grid program where the stored energy in plug-in hybrid vehicle batteries could be uploaded back to the grid to help reduce peak energy demand on the system. If fully implemented, the vehicle-to-grid concept could significantly alter the energy utility business.

Innovative Transportation Solutions and Technologies

For nearly two decades, PG&E has helped advance cleaner, more efficient vehicle technologies for our customers. With the largest natural gas utility fleet in the nation, we also continue to demonstrate leadership with our own vehicles.

Last year, through the 36 compressed natural gas (CNG) fueling stations we own and operate, we supplied natural gas to more than 200 commercial and private fleets, improving air quality in northern and central California communities.



PG&E's fleet includes a hybrid-electric service truck (left) and hydrogen fuel-cell vehicles (above).

We also helped our customers qualify for more than \$25.9 million in air district, state, and federal grants—up from \$6.6 million in 2005. This included organizing a consortium of 19 school districts that received more than \$12 million in grants to fully fund 70 natural gas school buses. PG&E also provided extensive support to a Port of Oakland-based trucking firm, which applied for state funding for 30 new CNG trucks and 30 more conversion systems; in doing this, we also helped an underserved community achieve its clean air goals.

PG&E also expanded its leadership role by agreeing to test three hydrogen fuel-cell vehicles made by DaimlerChrysler. Through daily use, PG&E is obtaining the operational experience and technical data needed to help improve the next generation of fuel-cell vehicles. PG&E was also awarded a \$1.2 million grant to co-fund a state-of-the-art demonstration project to further the hydrogen highway network. Based in San Mateo County, the project will enhance natural gas-to-hydrogen reforming technology and incorporate hydrogen-fueling capability into an existing natural gas station.

In 2006, we also purchased 275 new CNG vehicles, giving PG&E a fleet of more than 1,180 vehicles that run either entirely on CNG or have bi-fuel (gasoline with a separate CNG system) capability. We also successfully tested a 3,000 gallon liquefied natural gas (LNG) tanker trailer that can be placed strategically throughout PG&E's system as a temporary LNG fueling station. This was part of an ongoing effort to document safe and effective fueling procedures before placing the trailer into full operation.

As a result of these efforts, as well as vehicle natural gas used by our customers, we avoided the use of more than 15.7 million gallons of petroleum and the emission of approximately 670 tons of NO_x, 43 tons of particulate matter and 28,630 tons of CO₂.

Minimizing the Environmental Impact of Our Facilities

We are committed to reducing waste streams and water consumption, maintaining high waste recycling rates, modeling sound energy-efficiency practices and minimizing the use of toxic and chemical substances in our buildings and facilities.

Greening Our Own Buildings

By making our own buildings “green,” PG&E is demonstrating the value of protecting the environment to our employees and the local community.

In 2006, PG&E incorporated a variety of energy efficiency and sustainable building concepts into the development of our Concord Resource Management Center (RMC), using LEED™ criteria as our guide. Key features included low-flow plumbing fixtures, lighting that automatically dims near windows during the day, cubicle sensors that control energy demand when employees leave their work stations, sustainable wood products, and ENERGY STAR-labeled refrigerators, microwave ovens, copiers, and other office appliances and equipment. PG&E’s new program, “Earth & Art,” helped to furnish the building with artwork from area high schools. PG&E also incorporated many of these green building features at the new Fresno RMC.

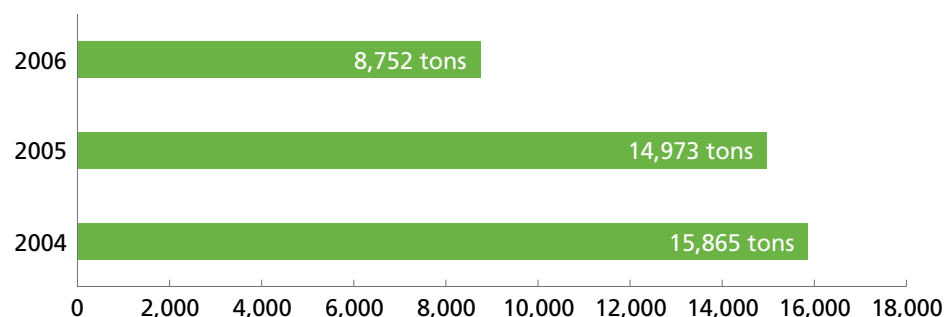
These and other efforts have helped build momentum for an emerging green building initiative, which is designed to leverage enterprise-wide opportunities and improve the environmental performance of PG&E’s new and existing facilities.

Waste Minimization

In 2006, PG&E partnered with Omega Waste Management to pilot a new approach that would boost recycling and waste reduction efforts at 50 PG&E facilities throughout a 19-county area. By successfully consolidating 44 different recycling and waste management contracts into one, Omega was able to achieve economies of scale, improve recycling procedures and right-size PG&E’s trash service to dramatically reduce the amount of waste being disposed. The end result was a resounding success: PG&E more than doubled the amount recycled at these sites in 2006.

In the course of operations, PG&E also generates hazardous wastes regulated by the federal government and the state of California. Federal regulations include the Resource Conservation and Recovery Act (RCRA) and the Toxic Substances Control Act.

Federally Regulated Hazardous Waste



California-regulated (non-RCRA) wastes are not regulated by the federal government but under more stringent California requirements. (These include non-PCB used oil, oil saturated solids and debris with metals at lower thresholds than federal standards.)

These wastes are generated by routine gas and electric operations, equipment maintenance and overhauls, and facility construction and demolition. Waste is also generated by remediation and cleanup of historic legacy sites. All waste generated by PG&E is managed and minimized in accordance with applicable federal and state regulations.

Other examples from 2006 include:

- *Continuing to achieve environmental benefits and cost savings by receiving a growing portion of our primary underground electrical cables on returnable steel reels*—versus one-time-use wooden reels. Since we began this effort in 1998, PG&E has received shipments of nearly 8,900 reusable steel reels, avoiding the use of more than 5.8 million pounds of wood, which translates into approximately 33,000 trees. PG&E has also saved a total of \$2.8 million in avoided purchasing and material handling costs, and the savings continue to grow.
- *Recycling and reusing our “e-waste,”* including approximately 3,660 CPUs, 6,530 monitors, 1,220 printers and 90 servers. It is PG&E’s practice not to allow our e-waste to be shipped overseas for processing.
- *Recycling or reusing 33,951,630 pounds of scrap iron, aluminum and copper from conductors, meters and miscellaneous infrastructure from our waste stream.* We also recycled more than 100,000 pounds of plastic piping as well as used hard hats.

Taking Responsibility for Our Historical Impacts

At PG&E, we are accountable for all our own actions. One recent event truly exemplifies this: the 2006 settlement that effectively resolved 10 years of litigation related to our use of chromium decades ago. In our announcement, we took responsibility for PG&E’s actions in the 1950s, 60s, and 70s, and we unequivocally affirmed the critical importance of ensuring that our conduct always aligns with our values.

PG&E has been delivering power to our customers for more than 100 years. As a result, we generated waste products that were disposed of in ways that were acceptable in their time, but ultimately created the need to clean up or isolate these wastes to protect human health and the environment.

We have taken responsibility for cleaning up historic or “legacy” contamination from past operations. For example, PG&E successfully led a multi-year effort to clean up a geothermal waste facility in Lake County, Calif., with oversight from the California Regional Water Quality Control Board and several other agencies. The facility was abandoned by its operator, and PG&E and numerous other companies were left with responsibility for securing the site and completed the effort in 2006. Key milestones included excavating and solidifying 186,000 cubic yards of waste, evaporating 21 million gallons of wastewater and planting 32 acres of trees, which are helping to lower the groundwater table, protecting it with contact from

Revising Our Environmental Policy and Governance Structure to Ensure All Employees Understand Their Contribution and Its Importance



For the nearly 20,000 men and women of PG&E, protecting the environment is a shared value and a top priority.

PG&E undertook an extensive effort to review our environmental policy in 2006; we revised it to make it more dynamic, action-oriented and stakeholder-driven. To highlight the value we place on environmental stewardship as we attempt to become the leading utility in the United States, we included an overall commitment statement with our policy. We also established tangible goals and initiatives to monitor our environmental efforts and performance and help our employees translate this policy into their everyday actions. Included here is our Environmental Commitment and broad Environmental Policy. For more information on environmental goals and initiatives as they relate to policy implementation, as well as our environmental governance structure, please visit www.pge-corp.com.

Environmental Commitment

At PG&E, we are committed to being an environmental leader and demonstrating this through our actions. We pledge to think creatively, work cooperatively and be results-oriented in our environmental stewardship efforts.

Environmental Policy

Our environmental policy reflects our environmental commitment and challenges us to find ways to produce, deliver and use energy as sustainably, responsibly and efficiently as possible. It is our policy to:

- Comply fully with the letter and spirit of all applicable environmental laws and regulations.
- Seek opportunities to exceed current standards of environmental protection, including pollution prevention, climate protection, and habitat and species protection.
- Lead efforts to craft and reform laws and regulations that create more effective policies and greater environmental benefits.
- Improve management programs and standards that foster environmental excellence and innovation and reduce our impact on the environment.
- Ensure that regular independent reviews of all environmental aspects of our business are conducted through a risk-based audit plan and corrective-action program.
- Enhance our transparency with regard to environmental progress and performance, and provide this information to the public.
- Maintain a constructive dialogue with our customers and stakeholders on environmental matters, and seek out partnerships to achieve results more effectively and efficiently.
- Educate all employees about applicable environmental requirements and the importance of environmental leadership in achieving our vision, and ensure that there is accountability for, and recognition of, actions.
- Strive for continual improvement in our environmental performance.

solidified waste. PG&E even enlisted 900 goats for weed abatement, and we created and are managing a 40-acre conservation easement containing three acres of new wetlands on the property. PG&E has also committed to long-term monitoring and maintenance to ensure the property's ongoing stable management and security.

Monitoring and Measuring Our Performance

PG&E continuously seeks ways to reduce its environmental footprint. Through our policies, management systems, review processes and programs we ensure that our operations first meet all applicable environmental requirements; we then seek to elevate our performance above and beyond the legal and regulatory requirements.

Our experience shows that striving to outperform and advancing innovative processes and ideas year after year not only improves performance but also strengthens our position within our industry by driving positive change and efficiency.

Environmental Management Systems

We took steps in 2006 to further develop and enhance our environmental management system (EMS), which is a comprehensive, systematic approach to managing our impacts on the environment and reducing potential environmental risks. Our EMS is the system that provides the mechanism to implement our Environmental Policy. Our EMS is a framework that defines how we:

- Develop strategic plans and programs;
- Establish corporate objectives and targets;
- Institute operational controls and train employees;
- Assign accountability and track performance;
- Increase employee and public awareness of environmental activities;
- Engage management in all aspects of our environmental performance; and
- Implement sustainable continuous improvement processes.

We obtained third-party verification in 2006 that our EMS framework is ISO-14001 compliant. To further strengthen our program, we:

- Applied a rigorous risk-management process to our program to identify and mitigate any significant risks and prioritize them among all company risks;
- Developed draft Environmental Management Plans to address environmental risks from a programmatic level;
- Obtained concurrence from line-of-business partners to set aggressive targets and objectives that reduce environmental risks; and
- Implemented an Environmental Scorecard to raise environmental awareness and accountability.

We will refine and implement our Environmental Management Plans in 2007. These plans address existing and proposed legal and regulatory changes, resource planning,

compliance issues, management strategies, overall accountability and other issues. In addition, they specify key actions required to improve or sustain performance. Metrics from these plans will be reported to senior management on a regular basis.

E-Screen

PG&E rolled out a new procedure called “Environmental Screening and Best Management Practices” in 2006. Otherwise known as “E-Screen,” these tools will help ensure that maintenance and construction activities receive the appropriate environmental reviews to protect the environment and mitigate potential environmental risks. Key milestones in 2006 included training 4,500 construction-related employees and 1,650 employees with engineering, design and project management duties. Together, the E-Screen tools will help PG&E reduce the risk of noncompliance with environmental laws and regulations, minimize work stoppages or re-work, improve job scheduling and budgeting, and improve relations with neighbors, customers and regulators. Moving forward, we will continue to further integrate E-Screen into the company’s work management processes.

Auditing Our Performance

Our environmental policy requires that we develop and implement a risk-based audit plan to ensure periodic independent review of all aspects of our environmental performance.

We performed 59 formal audits in 2006 to assess compliance of our facilities, operations and vendors with regulatory standards for air and water quality; management of polychlorinated biphenyls (PCBs), hazardous materials, and hazardous waste; and protection of endangered species. All audit findings were reported to the applicable operations officer and were required to be corrected in a timely manner. The program also utilized a cross-business unit, officer-appointed steering committee to review annual audit plans and enhance program processes and communication.

In addition to the formal audits discussed above, PG&E environmental personnel conducted 1,868 compliance assessments, which provided valuable information to operations employees that allow process changes to be identified to prevent compliance issues.

Operational Performance

PG&E’s environmental policy requires that we track and report annual environmental performance across a broad spectrum of areas. This section details our performance results for 2006.

Reported Releases and Permit Exceedances

The Utility reported to various government agencies a total of 324 releases to the environment and/or permit exceedances, an 18 percent increase from 2005. The increase is attributable, in part, to a major heat storm during July and August. Our crews and outside contractors respond to all spills—even those with only trace amounts of material—and perform cleanup and reporting in accordance with all

Recognizing Employee Leaders: Clarke Awards



Climate Protection Team members (from left) Sid Dietz, Greg Backens, Jan Berman, Jay Luboff, Greg San Martin, Jasmin Ansar, Gail Slocum. (Not pictured: Jon Forrester, Tom Jarman, Yvonne Rumbaoa, Chenoa Thomas, Jim Turnure, Christy Dennis)

San Joaquin Valley Habitat Conservation Plan Advisory Team members (from left) Steve Scialabba, Tom Cooper, Lori Austin, Raj Beasla, Bruce Wessels, Dick Benefiel, Greg Parker. (Not pictured: Lynn Cullen, Chris Damianakes, Rod Goodwin, Gus Quiroz, Wayne Yamagiwa)



P G&E celebrated the fifth anniversary of the Richard A. Clarke Environmental Leadership Award—an annual award that honors employees whose work embodies PG&E's commitment to environmental excellence. Since its inception in 2002, PG&E employees have submitted more than 110 nominations representing the environmental leadership efforts of more than 600 employees. Interest continues to grow; in 2006, more than 180 employees were nominated for an individual or team award, exceeding the prior years' average by nearly 80 percent.

Each year, PG&E has made a financial contribution to the winner's organization of choice; in the past, we've supported groups as diverse as the Golden Gate Audubon Society, Sierra Club's Inner City Outings and the American Council for an Energy-Efficient Economy.

This year, two teams received the prestigious Clarke award:

The Climate Protection Team proposed and received approval from the California Public Utilities Commission (CPUC) on ClimateSmart, a voluntary climate protection program. Starting in the summer of 2007, PG&E

customers can choose to pay a small amount on their monthly utility bill. This will fund new environmental projects aimed at removing an equal amount of CO₂ from the atmosphere—making the customer's energy use "climate neutral." On behalf of the team, PG&E made a \$5,000 contribution to the Pacific Forest Trust.

The second award was received by a team of PG&E employees that pioneered an innovative approach to meeting state and federal protection requirements for endangered plants and animals. The team developed a multi-species, 30-year **Habitat Conservation Plan (HCP)** for the San Joaquin Valley. Rather than taking a project-by-project approach, the comprehensive plan allows for ongoing infrastructure maintenance while providing long-term commitments for sensitive species and habitat protection. This HCP is the first in a series of six that will cover PG&E's service area; it continues to serve as a model for resource agencies working with other utilities. In 2007, PG&E expects to implement the San Joaquin Valley HCP, following extensive training of our field crews and managers. On the team's behalf, PG&E made a \$5,000 contribution to the San Joaquin River Parkway and Conservation Trust.

applicable laws and regulations. The majority of the releases were minor, involving small amounts of material, and more than half were either weather-related or caused by third-party accidents.

Agency Inspections

Government agencies conducted 517 routine inspections of the Utility's facilities in 2006, up from 513 inspections in 2005. Certified uniform program agencies—such as environmental health departments and fire departments—performed the majority of the inspections and are generally responsible for enforcing hazardous waste and hazardous materials requirements.

Enforcement Actions—Notices of Violation (NOVs)

The Utility received a total of eight NOVs from government agencies during 2006, a decrease from nine NOVs received in 2005. The rate of NOVs in 2006 continued a downward trend, as well. There were 1.55 NOVs per 100 agency inspections in 2006, compared to a three-year average of 1.83.

Of the eight NOVs received during 2006, four involved air quality regulations. One NOV was issued for not complying with air district permit conditions by exceeding daily average particulate matter limits at a site remediation project. Another involved incomplete records retention for the California Air Resources Board's Smoke Check Program for heavy-duty diesel vehicles. The third air-related NOV was for improper maintenance of a hose at a fueling station. And an NOV was received for exceeding air emissions limits during a source test at PG&E's Hinkley Compressor Station.

Three NOVs involved water quality regulations, including one issued by a local environmental health department for failure to prevent a hazardous waste release. A small amount of diesel fuel from an above-ground storage tank leaked into concrete containment, which failed to contain the fuel due to recent rain and possible fractures of the secondary containment. An NOV was issued by a Regional Water Quality Control Board when an annual certification of a storm water pollution prevention plan for a substation construction project was not submitted in a timely manner. And an NOV was received for late submittal of a progress report for a remediation pilot program at the Hinkley Compressor Station.

The Utility also received an NOV for a minor hazardous waste record-keeping issue at our Diablo Canyon Power Plant.

2006 Enforcement Penalties and Settlements

In 2006, the Utility received a total of one NOV resulting in monetary penalties and paid penalties on three other NOVs received in 2005. The penalties totaled \$6,800 and all involved air quality regulations. The penalties were \$1,000 for exceeding an emissions limit during a source test, \$1,000 for failure to properly cover a contaminated soil pile and two separate fines of \$2,400 for not submitting Emission Control Plans by the due date.

In response, PG&E swiftly resolved all of these issues by taking appropriate corrective actions and is developing processes to help prevent a future recurrence.

Partnerships

PG&E believes in collaboration, and we continue to work with a host of partners—environmental stakeholders and businesses. These partnerships embody several of our core values: transparency, open and honest communications, and taking responsibility for our actions. Engaging in trusted relationships is the right way to make progress on the key environmental issues that confront us all.

Environmental and Conservation Groups

Audubon California

Audubon California's mission is to conserve and restore California's natural ecosystems, focusing on birds, other wildlife, and their habitats for the benefit of humanity and the earth's biological diversity.

California Climate Action Registry (Registry)

Established by California statute as a nonprofit voluntary registry for greenhouse gas (GHG) emissions, the Registry helps companies and organizations with operations in the state establish GHG emissions baselines and record their GHG emissions inventory.

California Environmental Dialogue (CED)

CED's mission is to engage California business, government and environmental leaders collaboratively to improve public and private environmental policy.

California Environmental Protection Agency (EPA) Advisory Committee on Environmental Justice

This group was created to assist the California EPA Interagency Working Group with implementing an environmental justice agenda.

California League of Conservation Voters (CLCV)

The CLCV is the nonpartisan political action arm of California's environmental movement. Its mission is to protect the environmental quality of the state by increasing public awareness of the environmental performance of all elected officials, working to elect environmentally responsible candidates and holding them accountable to the environmental agenda once elected.

California State Parks Foundation (CSPF)

Dedicated to preserving California's 278 state parks, the CSPF works with citizens, lawmakers, and community and business leaders to secure adequate funding and protection of the resources that help California's parks thrive. CSPF also supports environmental education, wildlife and habitat preservation, volunteerism and sound park policy.

Center for Natural Lands Management (CNLM)

As a leader in the planning and management of mitigation and conservation lands, the CNLM manages more than 49,000 acres of conservation lands throughout California and facilitates the successful implementation of federal, state and local statutes designed to protect our natural heritage.

**Central Valley Salmon and Steelhead Recovery Assessment Project/
California Trout**

California Trout's mission is to protect and restore wild trout, salmon and steelhead and their waters throughout California. PG&E and California Trout collaborated with agency, industry, nongovernmental and academic representatives to identify and prioritize recovery opportunities and actions for endangered salmon and steelhead across the Sacramento/San Joaquin River.

Ceres

Ceres is a leading national coalition of investment funds, environmental organizations and other public interest groups working with companies to tackle environmental and social challenges, including climate change. PG&E is a member.

Ducks Unlimited

Ducks Unlimited conserves, restores and manages wetlands and associated habitats for North America's waterfowl.

National Arbor Day Foundation

The foundation is a nonprofit, environmental education organization of nearly one million members, with a mission to inspire people to plant, nurture and celebrate trees.

The Nature Conservancy (TNC)

Since 1951, TNC has worked with communities and businesses to protect more than 117 million acres around the world. PG&E is currently working with TNC and the Sacramento National Wildlife Refuge to restore and protect wildlife habitat along the Sacramento River for the federally protected Valley Elderberry Longhorn Beetle. Projects are expected to be completed in 2008.

San Francisco Bay Joint Venture

This is a partnership of public agencies, environmental organizations, the business community, local governments, the agricultural community and landowners working cooperatively to protect, restore, increase and enhance wetlands and riparian habitat in the San Francisco Bay.

Save San Francisco Bay Association

This organization seeks to preserve, restore and protect the San Francisco Bay and Sacramento/San Joaquin Delta Estuary as a healthy and biologically diverse ecosystem essential to the well-being of the human and natural communities that it sustains.

Solano Land Trust

Solano Land Trust's mission is to preserve agricultural lands, open space and resources through the acquisition of land and conservation easements, education and land management.

Sustainable Silicon Valley (SSV)

SSV is a collaboration of businesses, governments and nongovernmental organizations that are identifying and addressing environmental and resource pressures in Silicon Valley.

Trust for Public Land

As part of our overall species protection plan, PG&E partnered with the Trust for Public Land and the Sierra Foothill Conservancy (SFC) to protect 719 acres of high-quality habitat around Fine Gold Creek for the Valley Elderberry Longhorn Beetle, a federally protected species. Managed by SFC and the California Department of Fish and Game, this important habitat is also home to the western pond turtle, the foothill yellow-legged frog, and other sensitive bird and plant species. The Wildlife Conservation Board and the Bureau of Reclamation co-funded the project.

Business Community Partners

Alliance to Save Energy

The Alliance promotes energy efficiency worldwide to achieve a healthier economy, a cleaner environment and energy security. Corporations and business trade associations work together through the Alliance to promote greater investment in cost-effective energy efficiency.

California Council for Environmental and Economic Balance (CCEEB)

CCEEB is a coalition of California business, labor and public policy leaders who work together to advance collaborative strategies for a sound economy and a healthy environment.

California Fire Safe Council (CFSC)

CFSC's mission is to preserve and enhance California's man-made and natural resources by providing leadership and support that mobilizes all Californians to protect their homes, communities and environment from wildfires.

California Fuel Cell Partnership (CFCP)

The CFCP is a unique collaborative of auto manufacturers, energy companies, fuel cell technology companies and government agencies committed to promoting fuel cell vehicle commercialization as a means of moving toward a sustainable energy future.

California Natural Gas Vehicle Coalition (CNGVC)

CNGVC is devoted to ensuring that the state continues to set the pace in adopting this clean-burning transportation technology.

Clean Energy Group (CEG)

A coalition of national energy companies, CEG is dedicated to promoting environmentally progressive policies at the national and regional levels. CEG is actively engaged at the federal level in promoting national mandatory standards for reducing emissions of NO_x, SO₂, mercury and CO₂.

The Climate Group

PG&E joined other industry leaders, as well as Prime Minister Tony Blair and Governor Arnold Schwarzenegger, in a Roundtable convened by The Climate Group to discuss how business and government can deploy clean energy and clean technologies to accelerate the transition to a low-carbon economy. The Climate Group is an independent, nonprofit organization dedicated to advancing business and government leadership on climate change.

National Hydropower Association (NHA)

NHA is a national nonprofit association that seeks to secure hydropower's place as an emissions-free, renewable and reliable energy source that serves national environmental and energy policy objectives.

Natural Gas Vehicle Coalition (NGVC)

A national organization dedicated to the development of a growing, sustainable and profitable natural gas vehicle market, NGVC represents more than 100 natural gas companies; engine, vehicle and equipment manufacturers; service providers; environmental groups; and government organizations.

Pew Center on Global Climate Change: Business Environmental Leadership Council

A project of the Pew Center, the Council represents a group of leading companies worldwide responding to the challenges posed by climate change.

Environmental Awards

- ***American Council for an Energy-Efficient Economy—Champion of Energy Efficiency.*** Granted to PG&E's Food Service Technology Center for excellence in the categories of research and development, energy policy, implementation and deployment, and leadership.
- ***Association of Energy Services Professionals—Outstanding Achievement in Energy Program Design or Implementation—Honorable Mention.*** Granted to the California Statewide Multifamily Energy Efficiency Rebate Program, which PG&E and the other state investor-owned utilities administer. The Association of Energy Services Professionals is a nonprofit organization dedicated to advancing the professional interests of individuals working to provide value through energy services by sharing ideas, information and experiences.
- ***Breathe California—Clean Air Award.*** Recognized PG&E and numerous community groups for the collaborative efforts that led to the closure of the Hunters Point Power Plant.
- ***Building Owners and Managers Association (BOMA)—San Francisco: Commercial Recycler of the Year Awards—Runner-Up for "Large Buildings" Category.*** For our commitment to recycling at our General Office complex in downtown San Francisco.
- ***California Inland Fisheries Foundation, Inc. (CIFFI)—Corporate Community and Environmental Stewardship Award.*** Recognized PG&E's environmental stewardship of California's watersheds, integrating hydro-power operations while providing recreational and fishery benefits to Californians. Also commended PG&E's commitment to the communities it serves, including support of CIFFI's youth derbies and educational programs.
- ***California Governor's Environmental and Economic Leadership Award.*** PG&E won this award for two of its programs: Solar Schools (under the "Children's Environmental Education" category) and "AG-ICE" (under the "Environmental and Economic Partnerships" category). The award is the State of California's highest and most prestigious environmental honor, recognizing individuals, organizations and businesses that have

demonstrated exceptional leadership and made notable contributions in conserving California's precious resources, protecting and enhancing our environment, and building public-private partnerships.

- **California State Parks Foundation—Golden Poppy Award.** Honored the dedicated employees of PG&E, who have worked countless volunteer hours during the California State Parks Foundation's annual Earth Day Restoration and Cleanup event.
- **Interstate Renewable Energy Council—Annual Innovation Award.** Recognized PG&E's Solar Schools Program for its innovative role in promoting and accelerating the adoption of renewable energy technologies.
- **Keystone Center—Leadership in Industry Award.** Honored PG&E's accomplishments across a range of environmental areas, notably our leadership in developing initiatives in energy efficiency, renewable energy and global climate change.
- **National Arbor Day Foundation—Tree Line USA Award.** For the 12th consecutive year, recognized PG&E as a Treeline USA Utility for the company's environmental leadership in caring for the health of trees while providing safe and sound vegetation management along gas and electric lines.
- **Pacific Forest Trust—2006 Outside-the-Box Award.** Honored PG&E for its innovative ClimateSmart program, which will give customers the option to make their energy use "climate neutral" by investing in forest conservation and restoration projects that remove an equivalent amount of carbon dioxide from the atmosphere. The company was also recognized for its exemplary history of managing its watershed forestlands utilizing sustainable stewardship practices.
- **Peak Load Management Alliance—Demand Response Award.** Recognized PG&E and The Energy Coalition for founding the Business Energy Coalition, a voluntary cooperative program between PG&E and more than 30 major San Francisco business and civic leaders.
- **San Francisco Business Times—Education Innovator of the Year.** For designing and implementing the highly successful Solar Schools program to train teachers, inform students and generate interest in the critical role that renewable resources play in meeting California's energy needs.
- **Solar Electric Power Association—Public Awareness and Industry Leadership Award.** In recognition of PG&E's ongoing solar outreach, policy support and leadership.
- **U.S. Environmental Protection Agency—ENERGY STAR Sustained Excellence Award.** For continued outstanding achievement in our energy efficiency program targeting residential new construction. For the fourth year in a row, PG&E and California's other investor-owned utilities won recognition from ENERGY STAR for the residential new construction program.
- **U.S. Environmental Protection Agency—WasteWise Organic Material Reduction Gold Achievement Award.** For outstanding composting and waste reduction efforts at our San Francisco headquarters and Pacific Energy Center.

Environmental Performance Summary Tables (2004-2006)[†]

Emissions Statistics (for Utility-retained generation only)*

	2004	2005	2006
Total NO_x Emissions (tons)	942	1,084	982
Hunters Point**	108	133	39
Humboldt	834	951	943
NO_x Emissions Rates (lbs/MWh)			
Hunters Point**	0.36	0.39	0.38
Humboldt	4.23	4.10	4.08
Fossil Plants	1.89	1.90	2.94
All Plants	0.07	0.06	0.06
Total SO₂ Emissions (tons)	7.43	6.77	66***
Hunters Point**	3.06	3.33	1
Humboldt	4.37	3.44	65
SO₂ Emissions Rates (lbs/MWh)			
Hunters Point**	0.0102	0.0098	0.01
Humboldt	0.0221	0.0149	0.28
Fossil Plants	0.0150	0.0119	0.2000
All Plants	0.00054	0.00041	0.00388
Total CO₂ Emissions (tons)	657,376	751,530	474,115
Hunters Point**	357,646	409,766	124,443
Humboldt	299,730	341,764	349,672
CO₂ Emissions Rates (lbs/MWh)			
Hunters Point**	1190	1210	1218
Humboldt	1519	1479	1511
Fossil Plants	1320	1319	1421
All Plants	48	44	39

Other Emissions Statistics

SF₆ Emissions	2004	2005	2006
Total SF ₆ Emissions (pounds)	11,552	7,396	5,539
Total SF ₆ Emissions (tons CO ₂ -equivalent)	138,046	88,382	66,191
SF ₆ Emissions Leak Rate	4.2%	2.6%	1.9%
Methane Emissions			
Total Methane Emissions (tons)	N/A	98,772****	N/A
Total Methane Emissions (tons CO ₂ -equivalent)	N/A	2,074,217****	N/A

[†] PG&E does not trigger threshold reporting levels for those substances reported under the Toxic Release Inventory.

* PG&E's Utility-retained generation comprised approximately 40 percent of our delivered electricity in 2006.

For comparison to national average emission rates, see page 51.

** PG&E's Hunters Point Power Plant ceased operations on May 15, 2006.

*** This increase was due to temporary fuel oil combustion at PG&E's Humboldt power plant during a period of natural gas curtailment.

**** 2005 was the first year PG&E certified all six of its greenhouse gas emissions, including methane.

Greenhouse Gas (GHG) Emissions Avoided (Tons CO₂-equivalent)

	2004	2005	2006
Total GHG Avoided	3,393,981	3,400,849	4,298,066
CO ₂ Avoided (Lifecycle Customer Energy Efficiency Savings)	3,390,000	3,378,000	4,284,000
Methane Avoided	3,981	22,849	14,066

Annual¹ Energy Savings and Emissions Avoided

(Customer Energy Efficiency Programs)

	2004	2005	2006
Energy Savings			
Megawatt (peak)	77	115	142
GWh (total)	332	459	777
Million Therms	14	5.6	10.69
Emissions Avoided (Efficiency)			
CO ₂ Avoided (tons)	264,000	285,000	489,000
NO _x Avoided (tons)	23	32	54

¹ Annual energy savings refer to the *first year impacts* associated with installed customer energy efficiency projects.

Lifecycle² Energy Savings and Emissions Avoided

(Customer Energy Efficiency Programs)

	2004	2005	2006
Energy Savings			
GWh (total)	3,940	5,294	6,364
Million Therms	210	80	135
Emissions Avoided (Efficiency)			
CO ₂ Avoided (tons)	3,390,000	3,378,000	4,284,000
NO _x Avoided (tons)	276	371	445

² Lifecycle energy savings refer to the estimated energy efficiency savings over the *expected lifetime* of the installed customer energy efficiency projects.

Energy Consumed by Pacific Gas and Electric Company

	2004	2005	2006
Electricity Consumed (GWh)*	87	90	84
Natural Gas Consumed (MMcf)*	131	142	137
Energy Intensity (kWh/per sq. ft)*	15.1	15.6	14.7
Petroleum Consumed by PG&E Fleet (gallons)	8,943,199	8,347,899	10,277,615

* These figures represent electricity and natural gas usage at the 179 facilities managed by the Utility's Corporate Real Estate department.

Clean Air Transportation Program (Customer Savings)

	2004	2005	2006
Avoided NO _x Emissions (tons)	580	603	649
Avoided PM Emissions (tons)	37	39	42
Avoided CO ₂ Emissions (tons)	24,833	25,810	27,773
Equivalent Petroleum Gallons Displaced (x1,000)	13,637	14,174	15,252

Compliance Data

	2004	2005	2006
Notices of Violation (NOVs)	10	9	8
Rate of NOVs (per 100 inspections)	2.19	1.75	1.55
Releases/Exceedances	255	274	324 ¹
Penalties Paid	\$43,049	\$9,230	\$6,800
Agency Inspections	455	513	517
Formal Audits Performed	59	62	59
Compliance Assessments Performed	1,710	1,872	1,868

¹ Figures include both PG&E- and non-PG&E-caused releases/exceedances. In 2006, for example, 58 percent were either weather-related or caused by third-party accidents.

Hazardous and Non-Hazardous Waste

	2004*	2005*	2006
PCB Waste >50 ppm PCB			
Total (kilograms)	1,153,176	738,680	832,377
Incineration	556,513	326,423	267,710
Landfill	168,505	75,157	334,857
Recycled	428,158	337,100	229,810
% Recycled	37%	46%	27%**
PCB Waste <50 ppm PCB			
Total (kilograms)	7,872,346	7,840,415	7,154,148
Incineration	406,655	510,218	354,555
Landfill	94,344	201,658	547,095
Recycled	7,371,347	7,128,539	6,252,498
% Recycled	94%	91%	87%**
Low-Level Radioactive Waste (Disposed)			
Diablo Canyon (cubic feet)	1,672	3,881	1,159
Humboldt Bay Power Plant (cubic feet)	3,610	N/A***	N/A***
RCRA Hazardous Waste (Generated)			
Total (tons)	14,597	14,160	7,836
Recycled (tons)	14,327	221	23
% Recycled	98%	2%	<1%
Universal Waste (Generated)			
Total (pounds)	169,122	345,239	233,429
Recycled (pounds)	169,122	345,239	233,429
% Recycled	100%	100%	100%

* Values for 2004 and 2005 revised based on improved reporting procedures.

** Increases in the quantities of PCB waste generated in 2006 were due to additional site remediation and cleanup activities. These activities resulted in a proportional increase in PCB contaminated soil and debris that could not be recycled under applicable regulations. Thus, the percentage of PCB waste recycled decreased relative to prior years.

*** Low-level radioactive waste was generated and is currently being stored on site.

In producing this report, we took steps to minimize environmental impacts, promote supplier diversity, and support businesses in our Utility service area. With these goals in mind, we selected the following products and vendors:

- Low-VOC soy-based inks and process chlorine-free paper manufactured from 100% post-consumer waste. This paper is produced using wind-generated energy and is certified by Green Seal and by SmartWood, an affiliate of the Rainforest Alliance.
- A printer and graphic designer that are WMDVBE-certified businesses.
- An environmentally sensitive printer that is a Pacific Gas and Electric Company gas customer.



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