

ORIGINAL

Decision No. 53319

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of)
THE PACIFIC TELEPHONE AND TELEGRAPH)
COMPANY, a corporation,)
for an order authorizing it (a) to)
issue and sell \$78,000,000 principal)
amount of Thirty-two Year _____%)
Debentures due August 15, 1988,)
(b) to execute and deliver an)
Indenture to be dated August 15, 1956,)
and (c) to issue 1,562,267 common)
shares for subscription and sale)
for cash at \$100 per share to the)
holders of its preferred and common)
shares.)
-----)

Application
No. 38078

Arthur T. George, for applicant; Donald E. Hall,
for Washington Public Service Commission,
interested party; Dion R. Holm, City Attorney,
and Paul L. Beck, Chief Valuation and Rate
Engineer in the City Attorney's office, by
Paul L. Beck, for the City and County of
San Francisco, interested party.

O P I N I O N

The Pacific Telephone and Telegraph Company has filed the
above-entitled application for authorization (1) to issue and sell
\$78,000,000 principal amount of debentures, (2) to execute and deliver
an indenture creating such debentures and defining the terms thereof,
and (3) to issue and sell 1,562,267 shares of common stock of the
aggregate par value of \$156,226,700.

The application was filed on May 31, 1956. A public hear-
ing was held before Commissioner Dooley and Examiner Coleman in
San Francisco on June 19, 1956, at which time the matter was taken
under submission. The Commission has received no protests in the
proceeding.

This company has come before the Commission on numerous occasions, in applications similar in form to the one now under review, for authorization to issue and sell debentures and common stock to finance the cost of property. At this time, it once again seeks to employ the same methods it has used successfully in the past in disposing of its securities and it proposes, upon receiving the requisite regulatory approval, to put up its debentures for sale at competitive bidding, the winning bid to determine the interest rate, and to offer the common shares to the holders of its presently outstanding shares of preferred and common stock, pursuant to their pre-emptive rights, for subscription and sale, at par for cash, on the basis of one new share for each six standing in the name of each shareholder of record on the stock books of the company at the close of business on a date hereafter to be selected by applicant's board of directors.

The purpose of the proposed financing is to reimburse applicant's treasury for moneys actually expended from income, and other treasury funds, for the acquisition of property and for the construction, completion, extension and improvement of its facilities and of those of Bell Telephone Company of Nevada, its wholly owned subsidiary. The record shows, in Exhibit E, capital expenditures of \$521,402,566 as of April 30, 1956, which had not been paid or provided through the issue and sale of permanent securities but which had been financed, in general, with moneys represented by reserves, retained earnings and current accounts.

As to the necessity for the replenishing of the treasury in the amounts now requested, applicant reports that it, and its subsidiary, had outstanding short-term loans aggregating \$120,000,000 on April 30, 1956, that it is expected that such loans will increase to \$189,000,000 by the end of August, when the debenture proceeds will become available, and that thereafter additional borrowings will be made. It is estimated that the stock proceeds will

be received during September and will be utilized to discharge the remaining loans existing at that time but that, even so, there will be additional loans which applicant will be required to make during the last two months of the year which will amount to \$42,000,000. Applicant asserts that a continuation of its policy of financing through the medium of short-term loans is necessary, if it is to have an uninterrupted flow of money to meet its capital requirements. In this connection, it shows, in Exhibit 4, estimated gross construction expenditures of \$408,453,000 in 1956 and \$451,943,000 in 1957, and it estimates that only about \$150,000,000 to \$175,000,000 annually of the funds thus required for these purposes will be available from internal sources.

In presenting this matter to the Commission applicant has filed a financial statement showing its assets, liabilities and capital as of April 30, 1956. A summary of the statement is as follows:

Assets

Telephone plant, less reserves		\$1,709,515,214
Other investments		400,557
Current assets -		
Cash and deposits	\$17,474,738	
Accounts receivable	79,929,881	
Materials and supplies	<u>32,256,244</u>	
Total current assets		129,660,863
Prepayments		23,445,281
Deferred charges		<u>10,101,719</u>
	Total	<u>\$1,873,123,634</u>

Liabilities and Capital

Debentures		\$ 582,000,000
Advances from A.T. & T. Co.		24,000,000
Current liabilities -		
Notes payable	\$96,000,000	
Accounts payable	80,214,940	
Accrued liabilities	<u>71,534,163</u>	
Total current liabilities		247,749,103
Deferred credits		6,389,564
Preferred stock		82,000,000
Common stock equity		
Common stock	\$855,360,200	
Surplus	<u>75,624,767</u>	
Total common stock equity		<u>930,984,967</u>
	Total	<u>\$1,873,123,634</u>

The outstanding short-term borrowings at the date of the balance sheet were represented by \$96,000,000 of 3-1/2% notes issued to banks in the service area and \$24,000,000 obtained from American Telephone and Telegraph Company at 3-1/4%. Since April the bank interest rate has risen to 3-3/4% and the American Telephone and Telegraph Company rate to 3-1/2%.

The outstanding \$582,000,000 of debentures consist of nine issues, sold during the years 1945 to 1955, inclusive, which mature during the years 1978 to 1991, inclusive, and carry interest at rates ranging from 2-3/4% for the 1945 issue to 3-5/8% for the 1955 issue.

The outstanding shares of stock consist of 820,000 shares of 6% cumulative preferred stock and 8,553,602 shares of common stock, a total of 9,373,602 shares, all of the par value of \$100 each. The common shares had a book value of \$108.21 on the basis of the balance sheet figures of April 30, 1956, and a current market value, on or about the date of the hearing of this application of about \$138. For a number of years annual dividends of \$7 have been paid on each of the common shares. The record shows that American Telephone and Telegraph Company owns 8,398,946, or 89.60% of the outstanding shares and that others, 12,435 in number, own 974,656 shares, or 10.40% of the total.

According to the evidence, the company has endeavored, by alternating debt and stock financing, to maintain a capital structure with a debt ratio at a level considered by it as prudent in view of its consistently large volume of construction. Its capital ratios, according to Exhibit 5, are as shown in the following tabulation:

	<u>Dec. 31, 1955</u>	<u>Pro Forma Dec. 31, 1956</u>
Debt	37.9%	37.3%
Preferred stock	5.1	4.3
Common stock equity	<u>57.0</u>	<u>58.4</u>
Total	<u>100.0%</u>	<u>100.0%</u>

Applicant has long been an exponent of par offerings to its shareholders. Exhibit 7 shows that there have been 12 such offerings in the past, which have produced in excess of \$847,000,000 of equity money, and it is apparent that applicant will be required to go to its shareholders from time to time in the future for additional funds. It is applicant's position that it is desirable for the minority shareholders to continue their participation in the company and that a par offering is a means to insuring such continued participation. Applicant points out that the amount of paid-in capital would be the same if the 1,562,267 shares were to be sold at par or a lesser number at a price higher than par. Its vice president and comptroller testified that the sale of stock at par when the market is substantially above par does not affect the rate of return which the company is entitled to receive on its investment in operative property and hence does not affect the rates which customers would be asked to pay for service.

Upon a review of the evidence it is clear that applicant has had unreimbursed capital expenditures well in excess of the proposed security issues, that it is entitled to and has need for the reimbursement of its treasury in the amounts now requested in order to liquidate its short-term borrowings, to improve its cash position and to enable it to proceed with the expansion of the telephone facilities. When consideration is given to the large volume of construction work which applicant will be required to perform in order to meet its service requirements, it is obvious that it must maintain a capital structure sufficiently flexible to permit it to obtain additional capital under favorable terms when and as needed under whatever market conditions may prevail in the future.

The record in this proceeding warrants the making of an order approving applicant's requests. In making such an order we reiterate the position we have taken in the past, that we do not regard the dividends paid on the shares of stock as determining or fixing the rate of return applicant should be allowed to earn on its rate base. The authorization herein granted is for the issue of securities only and is not to be construed as indicative of amounts to be included in a future rate base for the purpose of determining just and reasonable rates.

O R D E R

A public hearing having been held on the above-entitled matter and the Commission having considered the evidence and being of the opinion that the application should be granted, as herein provided, that the money, property or labor to be procured or paid for by the issue and sale of the debentures and shares of stock herein authorized is reasonably required by applicant for the purposes specified herein, and that such purposes, except as otherwise authorized, are not, in whole or in part, reasonably chargeable to operating expenses or to income, therefore,

IT IS HEREBY ORDERED as follows:

1. The Pacific Telephone and Telegraph Company, on and after the effective date hereof and on or before December 31, 1956, may execute and deliver an indenture to be dated August 15, 1956, in substantially the same form as that filed in this proceeding as Exhibit C, and may issue and sell \$78,000,000 in principal amount of Thirty-two Year Debentures due August 15, 1988, at competitive bidding at the price which will result in the lowest annual cost of money to applicant.

2. The Pacific Telephone and Telegraph Company, on and after the effective date hereof and on or before December 31, 1956, may offer to the holders of its preferred and common shares 1,562,267 shares of its common stock for subscription and sale, for cash at \$100 a share, in the proportion of one new common share for each six preferred and/or common shares standing in the name of each shareholder of record on the stock books of applicant at the close of business on a date hereafter to be fixed and, upon receipt by applicant of subscriptions properly executed, together with the necessary funds, to issue certificates for the appropriate number of shares.

3. The Pacific Telephone and Telegraph Company shall use the proceeds to be received from the issue and sale of said shares of stock and debentures, other than accrued interest, for the purposes set forth in this application. The accrued interest may be used for such purposes or for general corporate purposes.

4. Immediately upon awarding the contract for the sale of said \$78,000,000 of debentures, The Pacific Telephone and Telegraph Company shall file a written report with the Commission showing, as to each bid received, the name of the bidder, the amount of the bid, the interest rate and cost of money to applicant based upon such price and interest rate, and the name of the bidder to whom the contract for the sale of the debentures was awarded.

5. Within 30 days after the issue and sale of the debentures under the authorization herein granted, The Pacific Telephone and Telegraph Company shall file a report with the Commission showing the date on which such debentures were sold and the consideration received, and within 30 days after the closing date of subscriptions for the shares of stock herein authorized to be issued, applicant shall file with the Commission a report showing the number of shares

of stock subscribed for by American Telephone and Telegraph Company, the number of shares of stock subscribed for by others, the consideration received, and the purposes for which the proceeds were expended.

6. As soon as available, The Pacific Telephone and Telegraph Company shall file with the Commission three copies of its prospectus.

7. The authority herein granted to issue debentures will become effective when applicant has paid the fee prescribed by Section 1904(b) of the Public Utilities Code, which fee is \$22,500. In other respects the authorization herein granted will become effective on the date hereof.

Dated at San Francisco, California, this 5th day of July, 1956.

[Signature]
President
Justice F. Calves
Paula Intermei
[Signature]
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Commissioners

PUBLIC UTILITIES COMMISSION
STATE OF CALIFORNIA
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BY [Signature]