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Decision No. 58105

ORIGINAL

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of SUNLAND-TUJUNGA TELEPHONE COMPANY, a corporation, for an order of the Commission authorizing it to increase certain rates and telephone charges for telephone service.	Application No. 40385 (Amended)

Orrick, Dahlquist, Herrington & Sutcliffe, by Warren A. Palmer, for applicant.
T. M. Chubb, Chief Engineer & General Manager, Department of Public Utilities and Transportation of the City of Los Angeles, by M. Kroman and Robert W. Russell; J. J. Deuel, for California Farm Bureau Federation; Neal C. Hasbrook, for California Independent Telephone Association, interested parties.
William C. Bricca, Hector Anninos and James F. Haley, for the Commission staff.

O P I N I O N

Public hearings were held on this application before Commissioner Theodore H. Jenner and Examiner Grant E. Syphers in Los Angeles on November 5, 1958, and before Examiner Syphers on December 10 and 11, 1958. On these dates evidence was adduced and on the last-named date the matter was submitted. It now is ready for decision.

The applicant herein proposes certain increases in its present rates as set out in Exhibit 10, attached to the first amendment to the application, which applicant estimates will yield it a rate of return of 7.25 percent on its over-all operation. The present and proposed basic exchange rates are as follows:

Class and Grade of Service	Present Rates	Proposed Rates	Proposed Increase
Business Flat Rate Extended One-Party	$ 9.90	$12.50	$ 2.60
Business Flat Rate Extended Two-Party	7.85	9.80	1.95
Residence Flat Rate Extended One-Party	4.90	6.35	1.45
Residence Flat Rate Extended Two-Party	4.00	5.25	1.25
Residence Flat Rate Extended Four-Party	3.40	4.25	.85
Business Extensions	1.40	1.50	.10
Residence Extensions	1.10	1.25	.15
Semi-Public Coin Box	1.25 (plus .24 per day)	2.55 (plus .24 per day)	1.30

The present as well as applicant's proposed rates contemplate telephone service to over 11,000 users in the Sunland-Tujunga exchange, all of which service is on a direct subscriber dialed basis. The extended free calling access of these users totaled 202,354 stations as of May 31, 1958, and a direct subscriber toll dialing access to more than 2,000,000 telephones.

At the hearing the company presented testimony and exhibits through its accounting supervisor and its general manager. This testimony discloses that the present rates have been in effect without change for the past six years. During this period it was alleged that the applicant's construction and operating costs have steadily mounted. For example, the plant investment cost for each new station added in 1952 was estimated to be $444.25, compared with $725.98 for each new station added in 1957. Likewise, the operating expenses increased from $41.18 per telephone station in 1952 to $51.69 per telephone in 1957. It was also testified that taxes, wages, and other costs have continually increased.

During the past six years the growth of the company has necessitated increased capitalization. It was estimated that for the year 1958 the construction program approximated $391,000, and for 1959 it would be about $328,800.

Applicant asserts that its rate of return has continually declined, claiming that in the year 1957 its average rate of return was 6.20 percent, whereas in 1958 it would decline to 5.56 percent under existing rates. Applicant shows its net operating income was $224,303 in 1957 and estimates it will be $220,011 in 1958 under present rates for telephone service.

The proposed rate increase, according to applicant's computations, will result in an increase in gross revenue of $146,000 and in net revenue of approximately $67,000. Applicant's testimony was supported by Exhibits Nos. 1 through 13 and 18 through 21, which exhibits, among other things, set out the financial position of the company, its construction budget, capital structure, and its estimate of results of operations under present and proposed rates.

Likewise, the applicant presented testimony showing that the rates of interest it is required to pay are higher than those paid by the two major telephone companies in the area, The Pacific Telephone and Telegraph Company and the General Telephone Company of California.

Additional testimony was presented concerning taxes, stock dividends and depreciation expense. We shall note some of these estimates hereinafter.

A study was presented by a representative of the Department of Public Utilities and Transportation of the City of Los Angeles which tended to show that applicant's earnings on equity capital exceeded the average yield of seventeen other independent telephone companies, although applicant's equity ratio (the ratio between the amount of equity capital and the total amount of capital) was comparable to that of the seventeen companies, as also was the average dividend paid out. From Exhibit No. 15 of the City of Los Angeles and Exhibit No. 17 of the staff, the following capital structure of applicant, as of June 30, 1958, is noted:

	City of Los Angeles	Staff
Funded debt	$1,800,000	$1,800,000
Less: Unamortized discount	(8,700)	
Short term debt	84,000	
Reserve for federal income taxes due to accelerated depreciation	57,600	
Preferred stock	324,600	324,575
Equity capital	1,676,600	1,656,706
Total Capital	$3,924,100	$3,781,281

(Red Figure)

The City's figures result in a percentage of equity capital to total capital of 42.62 percent, the staff's of 43.8 percent. This same ratio for the seventeen companies was 42.3 percent.

The average amount of dividends paid out by the seventeen companies was 72 percent, while that of applicant was 71.2 percent in 1957. Of earnings of $164,352 in 1957 available for equity capital, the applicant paid out $117,000 in dividends.

It is noted that as of June 30, 1958, applicant had a funded debt of $1,800,000, which constituted 47.6 percent of its capital structure, and upon which it was obligated to pay interest charges of 4.28 percent annually, or a sum of $77,040. It also had outstanding preferred stock of $324,575, amounting to 8.6 percent of its capital structure, with an annual dividend cost of 5.25 percent, or a sum of $17,040.

The staff of the Public Utilities Commission presented a study relative to the operations of this company, which study showed somewhat different results from the conclusions of applicant.

A comparison of the staff and the company estimates relating to the year 1958 under present rates and using straight-line tax depreciation is set out hereinbelow:

	Total Company	Inter-Changed Message Toll	Multi-Message Unit	Remainder
Applicant - (Exhibit No. 3)				
Revenues	$1,159,900	$ 90,192	$ 396,911	$ 672,797
Expenses and Taxes	939,889	73,930	312,804	553,155
Net Revenue	220,011	16,262	84,107	119,642
Depreciated Rate Base	3,958,604	211,198	1,186,283	2,561,123
Rate of Return	5.56%	7.70%	7.09%	4.67%
Staff - (Exhibit No. 17)				
Revenues	$1,160,788	$ 87,788	$ 396,500	$ 676,500
Expenses and Taxes	929,402	71,862	311,315	546,225
Net Revenue	231,386	15,926	85,185	130,275
Depreciated Rate Base	3,942,000	206,831	1,201,486	2,533,683
Rate of Return	5.87%	7.70%	7.09%	5.14%

The showings of both the applicant and the Commission staff reflect interchanged toll revenues which yield to applicant its costs, including a rate of return of 7.7 percent on the plant devoted by applicant to interchanged toll operations.

Interchanged Message Toll - Interstate

Applicant's interchanged interstate toll service is outside and beyond the scope of this Commission's jurisdiction. Applicant should not expect to offset any deficiencies in interstate toll earnings by increases in local exchange rates. Toll rate revisions should be sought from the appropriate regulatory authority or by renegotiation of settlement contracts with the companies that handle the toll service.

Interchanged Message Toll - Intrastate

Applicant's interchanged California intrastate toll service is furnished at rates filed with this Commission by The Pacific Telephone and Telegraph Company. In Decision No. 56652, dated May 6, 1958, in Application No. 39309, in connection with the intrastate toll rates of The Pacific Telephone and Telegraph Company, we made the following finding:

> "Under an alternative set of toll rates, introduced by applicant at the request of the Commission staff, a toll revenue increase of about $8,766,000 would be produced and a rate of return of 7.7 percent would result from such business. In view of the evidence we find it to be fair and reasonable to authorize the latter.8/
>
> "8/ Applicant (Pacific Company) is the tariff filing utility for toll service generally throughout the state and accordingly has the obligation and responsibility of seeing that each of the connecting independent telephone companies receives its costs and a fair return on the plant devoted to the service. The increases in toll rates authorized herein apply both to the intrastate toll traffic of applicant and to the intrastate toll traffic interchanged between applicant and the connecting companios. Toll rates for traffic wholly over the lines of the independent companies, however, are in no manner changed by the order herein since the record contains no evidence respecting the cost of furnishing such service."

In view of that finding, and giving effect to the evidence in this matter, we now find that for this applicant a rate of return of 7.7 percent is fair and reasonable. The ensuing order will reflect such a rate of return.

Applicant should not expect to offset any deficiencies in intrastate toll earnings by increases in local exchange rates, but rather should obtain a fair and reasonable toll settlement. No such toll settlement contract was in effect on the date of submission of this matter. Under Section 766 of the Public Utilities Code, if utilities do not agree upon the division between them of joint charges, the Commission, after hearing, may establish such division by order.

Multi-Message Unit

The showing of both the applicant and the Commission staff reflects interchanged multi-message unit revenues which yield to applicant its costs, including a rate of return of 7.09 percent on the plant devoted by applicant to such multi-message unit operations. Applicant's multi-message unit service is furnished at rates filed with this Commission by The Pacific Telephone and Telegraph Company. By Decisions Nos. 55936 and 56652 this Commission, among other things, increased multi-message unit revenues by shortening the mileage steps, and found a settlement ratio of 7.09 percent on interchanged multi-message unit business to be within the zone of reasonableness. We find, as respects applicant herein, that the interchanged multi-message unit revenue to which applicant is entitled is applicant's costs plus at least a 7.09 percent settlement ratio. Looking to the future we will not burden exchange rates with any deficiency which may result from applicant's entering into a settlement contract that has not been specifically approved by the Commission.

Remainder (Principally Local Exchange)

There remains applicant's local exchange and miscellaneous operations to analyze to determine applicant's need and justification for rate increases. Both applicant and the Commission staff presented more detail of the earnings of applicant's exchange operations under present rates, and using straight-line tax depreciation, than previously shown. These may be summarized and compared as follows:

SUMMARY OF
EXCHANGE AND MISCELLANEOUS OPERATIONS
YEAR 1958, ESTIMATED

Item	Applicant Exh. No. 3	Staff Exh. No. 17	Adopted Results
Revenues			
Local Service	$ 593,513	$ 600,300	$ 600,300
Miscellaneous	79,563	79,200	79,200
Uncollectibles	(279)	(3,000)	(3,000)
Total Revenues	672,797	676,500	676,500
Expenses and Taxes			
Operating Expenses	272,724	262,254	262,300
Depreciation Expense	135,735	118,924	118,900
Taxes Other Than Income	89,502	88,845	88,800
Income Taxes	55,194	76,202	73,800
Total Expenses and Taxes	553,155	546,225	543,800
Net Revenue	119,642	130,275	132,700
Rate Base (Depreciated)	2,561,123	2,533,683	2,534,000
Rate of Return	4.67%	5.14%	5.24%

(Red Figure)

There is no significant difference between the two estimates as to revenues. The staff's estimate of revenues appears reasonable and will be adopted. As to operating expenses we note that the company's estimate included an allowance for vacation reserve and an estimated fee for a depreciation study by an outside consulting engineer. On the other hand, the staff did not make an allowance for these items. The evidence discloses no such depreciation study will be made during 1958 and, accordingly, this expense should not be allowed in this proceeding. As to the vacation reserve, it is the company's practice to charge an expense when an employee is on vacation. However, the evidence does not establish any justification for this charge inasmuch as no additional salaries are paid to employees when they are on vacation and no extra employees are hired for this reason. The staff estimate has made allowances to reflect a wage increase for the company employees which became effective on December 29, 1957, and an allowance for an additional central office repair man and a commercial engineer. Other increases, such as the postal rates, have been taken into account; likewise, the staff's estimate has recommended certain decreases due to a change in the system of accounts, and a change in the telephone directory publishing contract. In short, it appears that the staff estimate was based on more recent information and more recent trends than were the company estimates. A complete analysis of the two estimates leads us to now find that the staff's estimate as to operating expenses is reasonable, and, accordingly, $262,300 will be adopted for this proceeding.

In the matter of depreciation expense, the company's estimate for exchange operations exceeds that of the staff by $16,811. A large part of this difference is due to the fact that the company desires to charge higher depreciation rates on telephone equipment. It was testified that there is a present demand of subscribers for telephones of more modern shapes, and also of varied colors. These colored telephones have a much shorter life than the conventional black telephones due to obsolescence. The conventional black telephone may have a life of twenty years, whereas a colored telephone has a much shorter life because it is more likely to be replaced to conform to changes in the decorating scheme of the subscriber's premises. While this may be a real problem to the utility, it does not now appear to be a valid reason for allowing a higher depreciation rate on station equipment. There is no testimony to indicate that colored telephones are a technological advance. The demand for them appears to be one of luxury rather than necessity. This being so, it appears to us that the person who desires a colored telephone should bear the major part of the expense therefor. If the company discovers that frequent replacements of colored telephones become a major factor it should then make provision to cover this expense by appropriate increased installation or service connection charges. It should be added that the evidence in this proceeding discloses the company's efforts in advertising colored telephones are partly responsible for the increased demands. We make no criticism of this practice, but do observe in passing that it does not now appear equitable to increase the rates to the general subscriber in order to permit certain subscribers to have colored telephones. While the company has proposed to reduce the installation rate for colored telephones from $10 to $7.50, we find it more in keeping with the realities of the situation to maintain the higher installation cost. We find $118,900 for depreciation expense to be reasonable as to applicant's exchange operations for 1958.

There is no significant difference between the estimates as to taxes other than income, and we find an amount of $88,800 is reasonable for applicant's exchange operations for 1958.

As to income taxes, the applicant testified that it had been using so-called accelerated depreciation for the years 1954, 1955, 1956 and 1957. This practice has resulted in a reduction in federal income taxes of approximately $57,000 as of the end of 1957. It was the applicant's position that these tax savings resulting from this accelerated depreciation should be normalized by crediting these savings to a tax reserve. However, the company witness further stated that if the Commission did not allow this practice in these proceedings, applicant will file tax returns taking depreciation on a straight-line basis for 1958 and thereafter, pending the results of the Commission's general inquiry into this matter in pending Case No. 6148.

Until such case is decided, the applicant shall advise this Commission as to its election for the 1958 and 1959 tax years within 30 days after the effective date of this order, and yearly thereafter by January 1 of each year until final decision of this Commission in Case No. 6148, and the Commission will promptly move to adjust the rates herein authorized in such manner as may be found appropriate. For the purposes of this decision only, pending final decision by this Commission on the treatment to be accorded accelerated depreciation for rate-making purposes, the tax expense for rate-making purposes herein will be determined on the basis of straight-line depreciation after crediting to the Federal Income Tax Account interest calculated on the reserve for income taxes at the rate of return on applicant's rate base herein adopted. Since approximately 64 percent of this reserve, or about $37,000, is chargeable to applicant's local exchange and miscellaneous operations, the interest credit in this proceeding will be $2,400.

After giving weight to the revenues and expenses being adopted herein and the deferred tax reserve interest credit, an income tax figure of $73,800 is computed for the test year 1958 which is found to be reasonable and is adopted.

The difference in rate base is partly accounted for by the staff's lower allowance for working capital and for materials and supplies, as well as a difference in depreciation reserve. This difference is not substantial, and the staff's estimate is based upon established practices. Accordingly, we now find that on an average depreciated rate base of $2,534,000 for exchange operations as estimated for the year 1958, this company under its present rates will realize a rate of return of 5.24 percent. The evidence in this record indicates a level trend in rate of return.

Upon consideration of all of the evidence before us we find that applicant is entitled to an increase in the rates on its local exchange and miscellaneous operations, but not to the extent requested. The ensuing order will authorize an increase which will result in a rate of return of 6.51 percent on a depreciated rate base of $2,534,000 devoted to exchange and miscellaneous operations, which rate base is hereby adopted. This rate of return is estimated to result in a rate of return of approximately 6.75 percent on applicant's total depreciated rate base, after taking into consideration a rate of return of 7.7 percent on the portion of applicant's depreciated rate base devoted to interchanged toll and a rate of return of 7.09 percent on the portion of applicant's depreciated rate base devoted to multiple message unit service. The increase in rate of return herein granted is estimated to produce an increase of $70,400 in annual gross revenues, which increase is hereby found to be required. This is approximately 48 percent of the increase in revenues requested by applicant.

Spread of Rates

Of the $146,000 increase in revenues requested by applicant, approximately $134,100 is applicable to Schedule A-1, Individual and Party Line Service and the balance, or $11,900, is applicable to a number of miscellaneous services including semi-public coin box, mileage rates, suburban service, private branch exchange, key systems, joint user, directory listing, supplemental equipment, interexchange receiving service, and foreign exchange service.

We find an increase of $59,600 is justified for individual and party line service (Schedule A-1) segregated $17,700 for business service and $41,900 for residence service. With respect to applicant's miscellaneous services, we find an increase of $10,800 to be reasonable, and the order herein will so provide.

The increases in basic rates found justified at this time may be summarized as follows:

	Increase Per Month	
	Business Service	Residence Service
Individual line flat rate	$2.60	$0.50
Two-party line flat rate	1.95	.40
Four-party line flat rate	*	.40
Suburban	1.25	.50
Trunk rate	4.00	*

* Service not offered.

Inasmuch as the Commission is authorizing new foreign exchange rates for applicant, it follows that affected foreign exchange rates filed by connecting companies should be revised so as to be consistent therewith. Such connecting companies should request authority of this Commission, by advice letter procedures, to make the necessary tariff filings to reflect the increase authorized in the serving exchange by the order herein.

In the interest of providing a more equitable distribution of charges among small and large business users, as well as to improve service to residence users, applicant will be required by the order herein to prepare and place before the Commission, studies of the cost and revenue effects of providing business individual line and private branch exchange message rate service in lieu of business individual line, two-party line and private branch exchange flat rate service, as well as residence two-party message rate service in lieu of residence four-party flat rate service in Sunland-Tujunga exchange.

The Commission has carefully weighed all of the evidence of record and has considered the statements of the parties with equal care. The findings hereinabove set forth produce an over-all result which we find to be fair and reasonable and in the public interest. Further, we hereby find as a fact that the increases in rates and charges authorized herein are justified and that present rates and charges, insofar as they differ from those herein prescribed, for the future are unjust and unreasonable.

O R D E R

Sunland-Tujunga Telephone Company, a California corporation, having applied to this Commission for an order authorizing increases in rates and charges for telephone service, public hearings having been held, the matter having been submitted and the Commission having been fully informed thereon, the matter is now ready for decision based upon the evidence and the findings and conclusions contained in the foregoing opinion, therefore,

IT IS HEREBY ORDERED that applicant is authorized to file in quadruplicate with the Commission, on or after the effective date of this order, and in conformity with the provisions of General Order

No. 96, revised tariff schedules with rates, charges and conditions modified as set forth in Appendix A attached to this order and, on not less than five days' notice to the public and to this Commission, to make said revised tariffs effective for all service rendered on and after April 4, 1959.

IT IS HEREBY FURTHER ORDERED that within six months from the effective date of this order, applicant shall have prepared and properly filed with the Commission and shall have served copies thereof upon the appearances in this proceeding, a study or studies showing the cost and revenue effects of providing (1) business individual line and private branch exchange trunk message rate service in lieu of business individual line, two-party line and private branch exchange trunk flat rate service and (2) residence two-party message rate service in lieu of residence four-party flat rate service. Further, such study or studies shall include a proposal or proposals as to rate levels and a reasonable program for the introduction of such in-lieu services.

The effective date of this order shall be twenty days after the date hereof.

Dated at San Francisco, California, this 10th day of March, 1959.

E. L. Fox
President

Peter E. Mitchell

Matthew J. Dooley

Theodore H. Jenner

Everett C. McKeage
Commissioners

RATES

The presently effective rates, charges and conditions are changed as set forth in this appendix.

Schedule No. A-1
Individual and Party Line Service

The following monthly rates are authorized.

	Rate Per Month: Business Flat Rate Service	Rate Per Month: Residence Flat Rate Service
Each individual line primary station	$12.50	$ 5.40
Each two-party line primary station	9.80	4.40
Each four-party line primary station	—	3.80
Each extension station	1.50	1.15

Schedule No. A-3
Semipublic Coin Box Service

The following changes in rates are authorized.

	Minimum Charge Per Day	Monthly Rate *
Primary station rate:		
Each individual line coin box station	$0.24	$ 2.55

* In addition to minimum charge per day.

Extension station rate:	Monthly Rate
Each extension station without coin box	$ 1.50
Each extension station with coin box	2.25

Schedule No. A-4
Mileage Rates

The following changes in mileage rates are authorized.

	Rate Per Each One-Quarter Mile or Fraction Thereof Per Month
Primary and trunk lines:	
Each individual line primary station	$0.75
Each private branch exchange trunk line	.75
Each battery supply circuit	.75
Each ringing power supply circuit	.75
Each two-party line primary station	.50
Each four-party line primary station	.35

Off-Premises stations:
Change rate 4(a) 1.c. from $0.50 to $0.75 per month.
Change rate 4(b) from $0.50 to $0.75 per month.

Schedule No. A-5
Suburban Service

	Rate Per Month	
	Business Service	Residence Service
Each ten-party line station	$5.75	$4.15
Each extension station without bell	1.50	1.15

Schedule No. A-6
Private Line Service

Rate for each station is authorized to be increased to $1.50 per month.

Schedule No. A-7
Private Branch Exchange Flat Rate Service

The following changes in rates and charges are authorized.

	Installation Charge	Monthly Rate
Switchboard Rate:		
Each cordless type switchboard	$80.00	$12.00
Cord Type Switchboard:		
40 lines or less		20.00
41 to 80 lines		25.00
Over 80 lines		30.00
Trunk Rate:		
Each trunk line		18.75
Station Rate:		
Each station not located in hotel guest room		1.50
Each station located in hotel guest room		1.15
Each jack in lieu of PBX local station		1.50
Automatic Private Branch Exchange Service:		
Each trunk line		18.75

Schedule No. A-8
Telephone Answering Service

The monthly rate for each non-multiple cord type switchboard position arranged for not more than 80 secretarial lines is authorized to be increased to $25.00 and the monthly rate for each station is authorized to be increased to $1.50.

Schedule No. A-9
Key System Service

Revises "territory" to read:

"Within the base rate area of the Sunland-Tujunga exchange, as said area is defined on a map filed as part of the tariff schedules."

The following changes in monthly rates are authorized.

	Monthly Rate
Equipment and Station Rate:	
Relay equipment arranged for a system with a capacity of:	
2 lines, 4 stations	$ 7.50
2 lines, 7 stations	10.75
3 lines, 7 stations	12.00
4 lines, 7 stations	13.50
4 lines, 12 stations	14.50
Each station	3.25
Central Office Line Rate:	
Each central office line:	
Business	12.50
Residence	5.40

Schedule No. A-10
Public Air Raid Warning Siren Service

The monthly rate for each public air raid warning siren arrangement is authorized to be increased to $7.00.

Schedule No. A-13
Joint User Service

The following changes in monthly rates are authorized.

	Monthly Rate
Each joint user service in connection with:	
Business flat rate service	$5.00
Commercial PBX flat rate service	6.00
Semipublic coin box service	3.00

Schedule No. A-14
Directory Listings

All $.50 per month items are authorized to be increased to $0.75.
All $0.25 per month items are authorized to be increased to $0.40.

Schedule No. A-15
Supplemental Equipment

The following changes in monthly rates are authorized.

	Monthly Rate
Extension bell	$0.65
Extension gong	1.00
Buzzer circuit	.75
Additional buzzers	.30
Cam lever key Cut off	.45
Indoor booth	2.00
Amplifier Units	2.50 *
Industrial Signal	1.35
Hands-free telephone	5.00 *
Exclusion feature	.15

* In addition to regular charge for type of service furnished.

The installation charge of $3.00 for each retractile cord is to be canceled.

Schedules Nos. A-16, A-17 and A-20
Foreign Exchange Service

Primary Service Rates:

1. Primary rates for foreign exchange service served from Sunland-Tujunga exchange are to be adjusted to the extent required by the increases hereinabove authorized in primary rates and in addition are to be increased by 50¢ per month.

2. Primary rates for foreign exchange service located within Sunland-Tujunga exchange are to be adjusted to the extent required by the increases hereinabove authorized in directory listing rates.

Schedule No. A-21
Interexchange Receiving Service

The monthly rate is authorized to be increased to $6.00.