GH

Decision No. 62893

ORIGINAL

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of GENERAL TELEPHONE COMPANY OF CALIFORNIA, a corporation, for authority to increase certain rates and charges applicable to the sale of advertising in its Telephone Classified Directories.	Application No. 43545 (Filed June 26, 1961)

Griffith & Thornburgh, by Laselle Thornburgh, and Albert M. Hart and John Robert Jones, for applicant.
Edward L. Abbott and Stanley T. Tomlinson, for City of Santa Barbara; Gerald Desmond, by Edward T. Bennett, and Henry E. Jordan, for City of Long Beach; R. W. Russell, by K. D. Walpert, for City of Los Angeles; interested parties.
Harold J. McCarthy and Paul Popenoe, Jr., for the Commission staff.

O P I N I O N

General's Request

General Telephone Company of California[1/] requests that the Commission authorize it to place in effect increased rates for classified telephone directory advertising service as set forth in Exhibit "G" herein. Under the proposed rates, General's directory advertising revenues would be increased by about $2,384,000, or by 26%, on an annual basis.

Public hearing on General's request was held before Commissioner George G. Grover and Examiner James F. Haley at Santa Barbara on September 11, 1961, and before Examiner Haley at Los Angeles on September 12, 13 and 15, 1961.

General alleges, that since its last directory advertising rate increase was placed in effect on January 5, 1953, it has been obliged to more than double its total directory circulation, with the

1/ General Telephone Company of California (General) is the largest independent telephone company in the United States. It provides telephone service to about 1,150,000 stations located in approximately 125 California communities within 34 exchange areas.

result that the value of advertising to the advertisers has been increased substantially.

According to General, the most comparable advertising medium to the classified directory is the newspaper, which is competing for the advertiser's dollar. General points out that during the period its present directory advertising rates have been in effect, taking into consideration increases in such rates due to reclassification of directories into higher circulation groupings, directory rates have increased by only 27%, as compared to an alleged increase in competing newspaper advertising rates of approximately 250%.

General also represents that the costs of issuing directories have increased since 1952. It cites increased directory production costs, including paper, printing, publishing salaries and wages, and sales salaries.

In Decision No. 57086, dated August 5, 1958, in Application No. 39465, General's last telephone rate proceeding, the Commission found a rate of return of 6.6% to be fair and reasonable for General's over-all operations and authorized increased telephone rates intended to produce that return. General contends that under present operating conditions such rates are now yielding only 5.86% in rate of return and that with the directory advertising rate increase sought herein it would realize only 5.99%.

In summary, it is General's position that its advertising rates for future directory issues should be increased because of: (1) the substantial increase in the value of service to directory advertisers; (2) increased directory publishing costs; and (3) the low level of earnings it is realizing on its over-all telephone operations.

Directory Publishing Arrangements

Twenty-five different directories are issued by General to cover the 34 exchanges it serves. Each of these directories contains an alphabetical section (white pages) showing all listed subscribers and a classified section (yellow pages) containing business listings and advertising. All of the 25 directories are published by an affiliate, General Telephone Directory Company (Directory Company), which is a wholly owned subsidiary of General Telephone and Electronics Corporation, the parent company of the applicant. The publishing is done according to the provisions of a contract between the two affiliates, a copy of which was introduced herein as Exhibit "M". The contract provides that the Directory Company shall sell advertising space and compile, proof-read and print the directories. For these services General currently pays the Directory Company approximately 51% of the directory advertising billing. The balance, or 49%, is retained by General, which does the billing and collecting for the advertising as an adjunct to performing such functions for other telephone services rendered.

In this proceeding the Commission's staff was concerned with the affiliated relationships between General and the Directory Company. The staff introduced Exhibit "L", which showed that the Directory Company received $4,173,969 from General's California operations and had associated expenses and taxes of $3,550,426 yielding a net return of $623,543 for the year 1960. Review of Directory Company balance sheet items indicated that $2,136,969 was invested in property and equipment, inventories and working funds allocable to General. Using these figures, the staff computed a rate of return of 29.2% on the Directory Company's operations for General. The staff indicated that a return of 7% to the Directory Company would require a net revenue of only $148,000 or $476,000 less than the actual net of $623,543 realized in 1960. This $476,000 is equivalent to approximately 90% of the $525,000 increase in net income which General would realize from the granting of this application.

In considering the staff's position, we take notice of the Commission's finding in Decision No. 57086, wherein the Commission stated:

> "The evidence discloses and the Commission finds that through the incentive factors contained in the contract and through the experience of the directory company, revenue results in favor of applicant are achieved that could not be realized through other means. Applicant contends that it cannot itself provide results as beneficial to it and to its ratepayers as it obtains through the directory service contract. There is no convincing evidence to the contrary. Further the application of a rate of return to the assets of a sales and service organization, such as a directory company, in our opinion, provides no realistic measure of the reasonableness of the charges for, or the value of, the service. In view of the evidence, we find said contract to be reasonable, therefore the adjustments made by the staff for this service will not be adopted herein."

In view of the Directory Company's high rate of return, it bears emphasis that the foregoing finding does not preclude further consideration of the Directory Company-General affiliated relationship in future rate proceedings, and General is hereby placed on notice that it will have the full burden of supporting the reasonableness of its contract in such proceedings. In addition, General is admonished to seek improvements in its settlement ratio with the Directory Company prior to any future rate application.

<u>Present and Proposed Rates</u>

The present directory rates in effect throughout General's service area are arranged for 14 circulation rate groups, the circulation being measured by the number of telephone stations in the largest exchange covered by a given directory. The rate groups range from the smallest, Group 1, covering up to 1500 stations, to the largest, Group 14, covering 195,001 to 240,000 stations. None of General's 25 directories now fall in either Group 1 or Group 14. Under General's proposal, present circulation rate groups would remain unchanged.

Increases are sought by General for all types of advertising in all of the circulation rate groups. The following tabulation compares certain present and proposed monthly advertising rates for directories having small, medium and large circulations:

	Circulation Rate Group					
	Group 2 (1501-2000)		Group 8 (30,001-40,000)		Group 13 (155,001-195,000)	
Type of Advertising	Pres.	Prop.	Pres.	Prop.	Pres.	Prop.
Regular type Listing	$ .25	$ .30	$ .55	$ .70	$ .80	$ 1.00
Bold type Listing	.50	.65	1.40	1.75	2.00	2.50
Trade Name Listing	.60	.75	1.65	2.10	2.20	2.80
Trade Mark Heading	2.00	2.50	5.75	7.20	9.50	11.90
Informational Inch	1.50	1.90	4.50	5.65	7.00	9.00
Display Advertising:						
1/4 Column	2.25	3.00	7.50	9.50	16.00	20.00
1/2 Column	4.50	6.00	15.00	19.00	32.00	39.00
2-1/2 Column	9.00	12.00	30.00	38.00	64.00	78.00

The present directory advertising rates of General are at levels generally in effect for most of the independent telephone companies throughout California. Although precise comparison is not possible between General's directory advertising rates and those of The Pacific Telephone and Telegraph Company (because of differences in circulation rate groupings), on an over-all basis General's present rates are at a higher level than Pacific's California rates.

Revenue Effects

Estimates introduced by General show that the proposed rates would produce a gross increase of $2,383,999.20, or an over-all increase of 26% in total billings to advertisers. General contends, however, that the impact of the rate increase would cause reductions and cancellations of advertising to such an extent that the realized increase in billing would be only 60% of this amount, or $1,430,399.52. After allowing for additional uncollectibles in the amount of $30,038.39, General would pay the Directory Company under the provisions of the current contract $238,061.39 of the increase, leaving General the remainder of $1,162,299.74. General's estimates are based on a repricing of the advertising items in its directories in service as of March 31, 1961, and do not, therefore, reflect any allowance for the acquisition of new advertisers through growth.

Value of Service

One of applicant's bases of justification for the proposed directory advertising rate increase rests upon the value of service concept. General points out that, since December 31, 1952, its total directory circulation has increased by 111.4%, thus making the value of the service proportionately greater to its advertisers. As of December 31, 1952, total directory circulation was 514,515, whereas on December 31, 1960, the total circulation was 1,087,838, an increase of 573,323.

In advancing this value of service concept, General overlooks the fact that during this period there have been a substantial number of rate increases placed in effect for individual directories as a result of the greater circulations which have accompanied station growth in General's exchanges. This process of raising the rate grouping of each directory as its circulation grows follows the corresponding increase in value of service, and thus the advertiser is already paying for the higher value of service realized through greater circulation. During the period in which General's total directory circulation increased by 111.4%, total billings to General's directory advertisers increased by 267.1%, from $2,211,322 to $8,118,048.

The Commission's tariff records show that, since January 5, 1953, the advertising rate levels of all but one of General's directories have been increased by at least one circulation rate group, and that eight directories have been increased by two levels, five directories by three levels, and one directory by five levels. The tabulation below shows the circulation rate group placed in effect for each directory concurrently with the January 5, 1953 rate increase and the circulation rate group now in effect for each directory:

	Circulation Rate Grouping		
Directory	1/5/53	Present	Increase
Arrowhead	1	2	1
Carpenteria	1	2	1
Covina	6	11	5
Downey	8	11	3
Fowler	1	2	1
Huntington Beach	3	6	3
Laguna Beach	4	5	1
Lancaster	3	6	3
Lindsay	3	3	0
Lompoc	2	4	2
Long Beach	12	13	1
Malibu	1	3	2
Ontario	6	8	2
Oxnard	5	7	2
Pomona	7	9	2
Redondo	7	10	3
Reedley	2	3	1
San Bernardino	8	9	1
Santa Barbara	7	9	2
Santa Maria	4	6	2
Santa Monica	10	12	2
Santa Paula	3	4	1
Santa Ynez	1	2	1
West Los Angeles	9	10	1
Whittier	8	11	3

There is every reason to believe that, as station development continues in General's exchanges, further raising of the circulation groupings of the individual directories willyyield General additional increases in directory advertising revenues.

Publishing Costs

In Exhibit "D", General presents a comparison of the directory publishing expenses of the Directory Company for the year 1952 compared with the year 1960. According to General, during that period unit printing costs increased by 29%; the price per pound of white paper by 6.3%; yellow paper by 6.6%; cover paper by 17.4%; daily rate publishing salaries and wages by 42.9%; and daily rate sales salaries by 36.7%.

Exhibit "N", which was introduced by General at the request of the examiner, shows that, for the year 1952 compared with the year 1960, the total payments received by the Directory Company from General increased from $1,331,112 to $4,173,969, or by 213.6%, and that the Directory Company's net income relating to business from General increased from $206,893 to $623,543, or by 201.4%.

Level of Earnings

As its Revised Exhibit "B", General introduced a summary of earnings on its over-all telephone operations for the 12-month period ending April 30, 1961, as recorded and as adjusted by General to reflect its estimate of the effects of present operating conditions. The rates of return shown on that summary of earnings are tabulated below in the column headed "Applicant". The staff introduced the related Exhibit "K", which shows General's adjusted figures for rate of return modified to reflect incrementally: (1) the rate-fixing adjustments used by the Commission as the basis for Decision No. 57086 in Application No. 39465, and (2) the adjustments for transactions with manufacturing, service, sales and directory affiliates recommended by the staff in Application No. 39465 but not therein adopted by the Commission. The rates of return developed in Exhibit "K" are tabulated below under the heading "Staff".

RATE OF RETURN

12 Months Ending April 30, 1961	Applicant	Staff: Dec. 57086 Basis	Staff: Basis Adj. for Affiliates
Recorded Basis	6.06%	--	--
Adjusted Basis, Present Rates	5.86	6.12%	6.52%
Adjusted Basis, Proposed Rates	5.99	6.25	6.65

In the light of the magnitude of the requested rate increase, the evidence on results of operations presented by General was somewhat abbreviated. We find that General's recorded figures represent a more significant starting point for approximating the present level of earnings than do General's adjusted figures, because, among other reasons, the adjusted figures reflect certain expenses associated with increased plant but do not correspondingly reflect the increased revenues which the greater plant would produce. Beginning, then, with the recorded results and applying the principles of the rate-fixing adjustments used in Decision No. 57086, we have determined that General's rate of return is, at the very least, at the level of 6.3%. There is no evidence in this proceeding upon which we could base a finding that such a rate of return is unreasonable. Moreover, the figure of 6.3% assumes the reasonableness of all of the expenses and investments which stem from applicant's transactions with its affiliates, and there is no basis provided by this record for that assumption.

Decision No. 57086 declared that applicant bears the burden of proving that its ratepayers are not burdened with the payment of unreasonable amounts to affiliates, and that it is essential that the Commission have before it information upon which it may appraise any unreasonableness in charges which may result from utility-affiliate relationships. Inasmuch as General relies upon the level of its over-all earnings in justification of the proposed directory advertising rate increase, the scope of General's burden of proof cannot be limited to its directory publishing affiliate alone, but must also encompass its transactions with its manufacturing, service and sales affiliates. General's showing herein does not meet this basic requirement.

Findings

The record in this proceeding will not permit us to make a finding that the requested increase in rates is justified. Necessarily, therefore, we find that the application should be denied.

O R D E R

General Telephone Company of California having applied for an order authorizing increases in directory advertising rates, public hearing having been held, the matter having been submitted, and the Commission having found that the application should be denied,

IT IS ORDERED that Application No. 43545 is hereby denied.

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

Dated at Los Angeles, California, this 5th day of December, 1961.

Everett C. McKeage
President

George G. Grover
Frederick B. Holoboff

Commissioners

Commissioner Peter E. Mitchell, being necessarily absent, did not participate in the disposition of this proceeding.