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ORIGINAL

Decision No. 76560

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of THE WESTERN UNION TELEGRAPH COMPANY, a corporation, for an order authorizing it to revise certain intrastate rates and charges applicable to telegraph and other services within the State of California.	Application No. 50722 (Filed December 4, 1968)

Noel Dyer, W. E. Seward, T. R. Matias, Counsel for applicant.
Sesto F. Lucchi, for the Commission staff.

OPINION

By this application, The Western Union Telegraph Company, a New York corporation, seeks authority to increase its rates and charges for public message, press message, money order, commercial news and public facsimile services within California. On the basis of applicant's test-year 1967 operations in California, applicant's rate increase proposals would produce increased gross revenues of $814,400, an overall increase of slightly more than ten percent.

Public hearings in the matter were held before Examiner Emerson on April 29, April 30, May 1 and May 2, 1969 at San Francisco. On the latter date submission was taken subject to the filing of a brief which the Examiner directed to be submitted by applicant not later than 30 days following receipt of the reporter's transcripts. On July 1, 1969, applicant petitioned to reopen the proceeding for presentation of additional evidence. By Decision No. 75935, issued July 15, 1969, said petition was granted and an additional day of hearing was held on July 31, 1969, a date convenient to applicant's eastern counsel and witnesses. Submission, without briefing, was taken on July 31, 1969.

The record consists of 14 exhibits and the testimony of eight witnesses, six on behalf of applicant and two on behalf of the Commission staff.

The application recites substantially the following respecting applicant's need for increased revenues:

1. Applicant's system-wide rate of return for the 12 months ended December 31, 1967, was 4.8 percent.

2. New labor contracts, effective June 1, 1968, will result in increased costs of $4,600,000 in 1968, $13,100,000 in 1969 and $21,700,000 in 1970. A revised pension plan will result in additional costs of $2,400,000 per year for the period July 1, 1969 through 1972. These amounts are for the total system.

3. System-wide operating results for 1968, including that portion of the new labor contract costs for such year are projected to produce a rate of return of 4.5 percent.

4. The combined effect of the proposed interstate and intrastate rate revisions (applicant is seeking to make effective identical rates in all other States) is to increase the projected 1968 system-wide rate of return to 4.9 percent and to increase the 1968 results adjusted for 1969 effect to 5.0 percent.

5. The successful implementation of applicant's modernization plans requires the maintenance of its earnings at the level projected to result from the proposed rate increases.

6. In California, applicant's intrastate operations for the year 1967 show a loss of $1,368,146. After reflecting the increased revenues to be produced by the proposed rates and to reflect the effect of the new labor contracts and pension plan, intrastate operations in California would still produce a loss.

Applicant's Vice President of Revenue Requirements testified that applicant does not consider this proceeding as being one concerned with rate of return and gave as the two major factors involved in applicant's rate increase proposals (1) the need to raise additional revenues to permit applicant to have sufficient borrowing capacity to meet the requirements for its modernization program and (2) that the type of rate structure related to message telegram service is too complex to permit customers to easily understand the charges or to make comparisons between the cost of telegram service and the cost of other alternative methods of communications.

Applicant provides three major types of service offerings: message telegram service, private leased-wire systems, and measured services presently consisting principally of Telex service. Applicant faces competition, either directly or indirectly, in each.

The rate proposals put forward by applicant in this proceeding fall into two categories. The first category concerns rate revisions to reflect increases heretofore placed into effect (May 5, 1968) for interstate service. These increases were (a) from 5.3 cents to 10 cents for messages picked up by messenger or filed by telephone (b) from 10 cents to 15 cents for collect messages and (c) a 10 percent increase in money order charges.

The second rate increase category concerns a number of items among which are a simplified rate structure providing for (a) a single rate step (instead of the present five zone mileage steps) with a uniform basic rate of $1.70 for day-time telegrams and (b) a uniform basic rate of $1.30 for over-night telegrams. Further, money order service would be restricted to full-rate telegram handling ($1.70 minimum rate). A new charge of 75 cents is proposed for physical delivery of messages. Overnight telegrams would no longer be accepted after midnight. Delivery of messages to trains, motor-buses, airplanes and boats would no longer be undertaken and delivery of domestic messages could be made by telephone, tie-line or messenger at the option of applicant. Day-letter service would be eliminated.

The increased revenue estimated to be produced in California from applicant's rate proposals is summarized as follows:

Item Increased	Annual Revenue Amount
Public Message Service	$617,400
Acceptance and Collect Charges	47,300
Physical Delivery	84,800
Money Order Premium Charges	64,900
Total	$814,400

Western Union operations are unlike those of any other public utility in a number of respects, but primarily because its system constitutes a network with no self-contained or independent units within it. For example, all public messages are transmitted to a central office known as the Reperforator Center which routes the telegram. There are now only eleven such reperforator centers in the United States. One of the larger centers is in Los Angeles and it handles originating and terminating message traffic for Western Union offices in California, Arizona, New Mexico and Clark County, Nevada. Another reperforator center is in Portland, Oregon and, for applicant's own convenience, part of the traffic from its San Francisco offices is handled through Portland. Thus, telegrams between points in California may or may not be transmitted within the State and in any event pass through centers handling inter- as well as intra-state traffic. The company presently has but three auditing centers in the United States and plans to combine these into one center at Minneapolis. There are two comptroller offices (New York and Dallas) which receive information from the auditing centers and forward such data to the general office in New York. Thus, it is seen that the company's accounting as well as its traffic handling operations are highly centralized. In fact, nearly all phases of Western Union's operations are directed and supervised from its New York headquarters offices.

Because of the various regulatory jurisdictions and the various taxing authorities under which this network operates, its plant, revenues and expenses are "separated" or allocated in accordance with procedures which it itself has set forth in a "Manual of Instructions, State Separation Studies" which it is continuously revising by means of supplementary memoranda to certain of its employees. It characterizes these studies as "a series of analytical, engineering and accounting processes having for its ultimate purpose a division of joint operating revenues and related expenses between interstate and intrastate jursidictions". Insofar as intrastate operations are concerned, these studies have three main purposes: (1) to provide a basis for state tax reports, (2) to provide data supplementary to the annual reports filed in state jurisdictions and (3) to provide basic data for state rate cases.

To one knowledgeable in the utility regulatory field, it is abundantly clear that separations methods and procedures and the manipulations possible therein can be so used as to produce nearly any desired end result. Because of such possibility, "separations" become suspect in rate cases and should receive close scrutiny. In addition, the overall results of "separations", by which the rate burdens to be placed upon various classes of customers or types of services are determined and assigned, must be reasonable, for it is fundamental that no undue rate discrimination should either be created or, if discovered, be permitted to continue.

In the last twenty years, applicant has been before this Commission, in no fewer than 14 rate increase proceedings. In each one, it has informed this Commission that its California operations have been at a loss and that such operations would continue at a loss even after the requested increases. In no proceeding has it ever disclosed a positive net revenue in more than two states (in one proceeding it claimed that its "profit" in one state was only $275 for the entire year concerned). In each proceeding, however, its overall operations have been shown to be profitable. Repeatedly, and primarily because Western Union's applications have in nearly every instance pertained only to portions of its service offerings, or have been for relatively modest rate increases, this Commission has foregone a complete examination of its separations methods. Repeatedly, in its decisions, the Commission has in a critical vein discussed Western Union's separations methods and time after time has indicated that the methods would be left open for further study and that further experience might show that changes or refinements might be justified. Western Union having in no meaningful way responded to such forewarnings, this Commission in its Decision No. 74283, issued June 25, 1968, placed Western Union on notice that if it seeks further rate increases for California intrastate services "it will be necessary for the utility to <u>support fully its methods</u> of determining California intrastate operations <u>including all of its separations and cost allocation procedures and to fully justify the reasonableness of them.</u> It will also be necessary for Western Union <u>to demonstrate and prove</u> that its public message service rates are not necessarily burdened by other private line, computer, or data handling services it offers". (Emphasis added). The instant rate increase application was filed some five months later. Neither the application nor the testimony of applicant's witnesses having satisfied such notice, applicant was directed to file a brief in which it would specifically point out wherein the record made was in response to such notice. No brief was forthcoming. Indeed, the task could not have been accomplished for the record was substantially deficient in such respect. Instead of filing the brief applicant petitioned for a reopening of the proceeding for the purpose of presenting evidence in such regard and, as hereinabove recited, applicant's witnesses returned to California in order to present this additional evidence.

Applicant's "Manager of Regulatory Allocations" testified respecting the company's balance sheets and income statements, capital structure, capital requirements and its desires respecting increased earnings. His only testimony respecting intrastate allocation or separation data was a passing reference to Western Union's "Annual Jurisdictional Separations Study" for the year ended December 31, 1967 (not presented in evidence) and the introduction into evidence of the company'a latest manual of instructions respecting separations. This manual consists of three parts: (1) a General section which states some of the reasons for separations and emphasizes the company's position respecting the "utter impracticability" of maintaining complete accounts and records, (2) a Field Office Instructions section, effective for data submitted for the year 1949 and (3) a Home Office Instructions section which includes changes or amendments in Home Office procedures up to January 1, 1961. The manual reflects no changes made since 1949 or 1961, as the case may be. For example, it still is based on the once-existent fifteen reperforator centers (there are now only eleven) and five-state reperforator areas (there are now only three). On bringing apparent discrepancies to the attention of the witness, he testified, among other things, that "Western Union is well aware of the need for the revision of this manual". He also testified that letter instructions were used in making continuing revisions in procedures. None of these were placed in evidence or otherwise explained. With respect to the relationship of public message service to other services, the witness testified that on a system-wide or overall basis the company does measure return by service categories but that on an intrastate or jurisdictionally separated basis, company records and procedures do not lend themselves to the determination of such return relationships. There the matter rested insofar as the company was concerned. The testimony of applicant's Vice President of Revenue Requirements offered in supplement to the testimony of the Manager of Regulatory Allocations was so dependent upon expressions of conjecture as to lend no meaningful support thereto. If this manual and such testimony constitutes a response to the hereinabove quoted portion of Decision No. 74283, the Commission can only conclude that applicant's response was woefully deficient.

Applicant's "additional evidence" presented on reopening of the proceeding was directed solely towards a demonstration that public message service rates in California are not burdened by its other services. Presented were the results of a study made to separate the California intrastate public message revenue, expense and investment and to measure rate of return earned on public message service. The exhibit showing these results (Exhibit No. 13) purports to show "Actual Intrastate California Operating Results" for the year ending December 31, 1967 and such results after modification to reflect revenues from increased rates and presently known increased expenses such as wages and pension costs.

In reality, no actual results are shown, however, for nearly all items are in fact no more than further allocations of previously allocated amounts. They are subject to the same infirmities hereinabove commented upon, since they are but extensions of such basic separations. Be that as it may, the exhibit serves to show the relative earnings of applicant's California intrastate public message services and its other California services. After correction of admitted errors in the exhibit, the exhibit shows that under existing rates applicant's intrastate public message service is operated at a loss of $602,747 while its other intrastate services earn $172,836 and a 9.4 percent rate of return. On the assumption that increased rates and expenses are applicable for the same 12-months' period, the exhibit further shows that public message services would be operated at a loss of $621,021 while other services would produce earnings of $141,145 and 7.7 percent rate of return. The exhibit also shows that applicant's total intrastate operations produce a loss of $429,911 at present rates and a loss of $480,876 under the new rates and increased expenses. The greater loss (under increased rates) in the public message category results primarily from the assignment of nearly all of the wage increase effects to such category. While this exhibit demonstrates that intrastate public message service may not be burdened by other services, it also demonstrates that the other services are burdened by the public message service. Applicant claims that no such burden exists, however, because in the opinion of applicant's witness applicant should earn a rate of return in the range of 10-10.5 percent overall.

The evidence and testimony presented in this proceeding by the Commission staff included a report on a "separated" results of operations study. While the report contained the statement "The staff believes that the separations procedures are reasonable and do not burden this state with unreasonable expenses", cross-examination developed the fact that the staff was wholly reliant upon information which the company had supplied and had been unable to make an independent analysis. The staff witness testified that there were certain "gray areas" involved. In particular, he testified that he did not agree with the company's allocation factors or separation principles regarding separations of expenses on the basis of allocated revenues nor did he agree with money order bureau allocations based upon revenues instead of volume of traffic. Neither did he agree that separation of revenues between interstate and intrastate on the two-to-one message handling factor used by the company was acceptable because it ignores the time involved in handling the traffic. Since no study had been made respecting message handling he was unable to accept the company premise as being a proper one. The staff was unable to develop any separations between types or classes of service in California because, as the witness explained, the staff had requested cost of service data for intrastate services but the company had not responded to such request.

From the record the Commission concludes that neither the applicant nor the staff has fully supported the company's methods of separations between interstate and intrastate operations or the reasonableness of such separations. The respective showings pertaining to intrastate earnings are unreliable. The methods used appear to saddle California intrastate operations with a disproportionate share of system operating costs, thereby favoring interstate operations at the expense of California intrastate operations.

As above noted, the burden of fully supporting its separations was a condition precedent to increased rates placed upon Western Union by this Commission's Decision No. 74283. Applicant has not satisfactorily met such burden. The full burden remains. In view of such situation the Commission concludes that the application herein should be denied.

In summation, the Commission makes the following finding of fact and conclusion of law:

Finding of Fact

Applicant has not met its burden of proof, respecting the reasonableness of its separations and cost allocations as required by this Commission's Decision No. 74283.

Conclusion of Law

The Commission concludes that the application herein should be denied.

ORDER

IT IS ORDERED that the application of the Western Union Telegraph Company herein (Application No. 50722) be and it is hereby denied.

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

Dated at San Francisco, California, this 16th day of DECEMBER, 1969.

William Symons Jr.
President

Augustus

Thomas Moran

Vernon L. Sturgeon
Commissioners

I abstain
J.P. Vukasin Jr.