

Decision No. 81221

ORIGINAL

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

The California Farm Bureau Federation,
a non-profit organization,

Complainant,

vs.

San Miguel Telephone Company of
California,

Defendant.

Case No. 8855
(Filed November 4, 1968)

In the matter of the application
of San Miguel Telephone Company of
California for authorization to
borrow \$1,225,000, issue notes
therefor and execute security instru-
ments in connection therewith.

Application No. 51582
(Filed December 29, 1969)

In the matter of the application
of San Miguel Telephone Company of
California for authorization to
borrow \$1,225,000, issue notes
therefor and execute security instru-
ments in connection therewith.

Application No. 53576
(Filed September 8, 1972;
amended December 18, 1972)

SECOND INTERIM OPINION

The Commission issued Decision No. 77208 dated May 12, 1970 in the consolidated proceedings, Case No. 8855, a service complaint of the California Farm Bureau Federation against San Miguel Telephone Company of California^{1/} and Application No. 51582,^{2/} wherein San Miguel

^{1/} Now Redwood Empire Telephone Company (Redwood).

^{2/} Decision No. 77208 was amended by Decision No. 77215 dated September 15, 1970 as it applied to Application No. 51582.

sought authorization to borrow \$1,225,000 from the Rural Electrification Administration (REA). The Commission's decision, among other things, authorized the borrowing from REA.

On September 8, 1972 Redwood filed an application for supplemental order^{3/} seeking authority to expend the funds authorized to be borrowed by Decision No. 77208 for purposes different than those authorized therein. Application No. 53576 is hereby consolidated with Case No. 8855 and Application No. 51582. In its application Redwood states that since issuance of the Commission's order in Decision No. 77208, it has experienced a significant increase in demand for local and toll telephone service, principally in the Sea Ranch central office area of its Northern Division. It further states that in addition increased costs of labor and materials due to inflation have seriously eroded the purchasing power of the funds available to it from the \$1,225,000 REA "D" loan authorized by Decision No. 77208. As a result, Redwood claims that the "D" loan funds will not permit completion of the projects originally contemplated.

In Exhibit A, attached to Application No. 53576, Redwood presents a new design construction program that it states can be accomplished with the funds available. The revised program contemplates reconstruction of the toll line linking Parkfield and San Miguel central offices together with taps and branches along the route of that toll line within the San Miguel exchange, reconstruction of all outside plant in the Parkfield exchange, construction of an additional central office building in the San Miguel exchange, and installation of central office equipment in that building as well as a number of projects in its Northern Division. The revised program

3/ Amended December 18, 1972.

would defer reconstruction of certain portions of the outside plant within the San Miguel exchange. Redwood states that because of certain recent improvements in outside plant, reconstruction of the balance of outside plant in the San Miguel exchange can be safely deferred until additional financing can be obtained in the future. Redwood states that, notwithstanding the proposed changes in its construction program, the expenditures of monies in its Northern and Southern Divisions will be the same amounts as originally proposed in its Application No. 51582.

In its amendment to Application No. 53576, Redwood asks for authority to proceed with the plans set forth in Application No. 53576 except for deferral of Parkfield outside plant reconstruction and the San Miguel/Parkfield toll line with local distribution taps in San Miguel exchange. Redwood further asks it be directed to withhold not in excess of \$200,000 of "D" loan funds in order to construct the deferred improvements referred to above at an appropriate time. San Miguel states that the deferral is requested because it has been unable to acquire the necessary easements to construct the portions of the telephone system which will link Parkfield and San Miguel central offices and to construct the Parkfield outside plant. It appears that the REA will not permit any expenditure of construction loan funds in either the Northern or Southern Division until all necessary easements have been obtained. Lacking the necessary easements, Redwood is unable to proceed with any construction. The REA has also informed Redwood that it could proceed with the use of "D" loan funds for the revised construction program only upon approval of this Commission.

By letter dated January 17, 1973, Mr. William Knecht, attorney for the California Farm Bureau Federation, complainant in Case No. 8855 and interested party in Application No. 51582, informed the Commission of his view that the public would be best served by the granting of Redwood's Application No. 53576 ex parte as requested by Redwood. However, he recommended that a number of conditions be attached to the authorization. His recommended conditions are as follows:

1. Grant Redwood Empire Telephone Company permission to draw down the funds allocated to it by REA;
2. Impound \$200,000 for the Southern Division;
3. Require immediate action on the construction of a new central office for San Miguel, holding or earmarking funds for that project;
4. Require Redwood to rescind and cancel any rights-of-way agreement in the Parkfield-San Miguel areas, upon demand of customers, for a period of 30 days after written notice to all landowners that such option is available;
5. Require Redwood to offer all landowners in the Southern Division a right-of-way agreement which includes provision that the Company will pay court-fixed attorney's fees and costs in connection with any litigation thereunder;
6. Require Redwood to engage a consulting engineer for not less than two days per month, to make review of all operating conditions, plant facilities, work orders, etc.; to give (not subject to countermand) recommendations for and maintenance orders;
7. To file copies of all said orders and recommendations with the CPUC and complainant; and
8. Require Redwood to file reports showing compliance with all orders, instructions and recommendations, initialed by the consulting engineer.

By letter dated January 24, 1973 from its attorney, Redwood objected to Mr. Knecht's suggestions 4 and 5.

On February 16, 1973, a staff report entitled "Redwood Empire Telephone Company Application No. 53576" was distributed. Mr. Knecht's letter will be Exhibit 15, Redwood's letter will be Exhibit 16, and the staff's report is received as Exhibit 17 in these consolidated proceedings.

The staff summarized its report as follows:

"SUMMARY

"The staff has no objection to Applicant amending its construction program as authorized in Decision No. 77208. It would serve no useful purpose to delay needed improvements in other portions of the system because of the inability to obtain rights of way in the Parkfield area.

"Some safeguards must be included in the decision to provide assurance that the management of Redwood Empire Telephone Company will carry out its responsibilities diligently. At the same time, we are aware of the fact that under a cost type of settlement with The Pacific Telephone and Telegraph Company, there is little incentive for economies or efficiencies. This is particularly true in this instance, where approximately 85% of Applicant's revenues are derived from toll settlements.

"Construction projects have repeatedly been revised or deferred due to a lack of available loan funds. Each time Applicant applies for and receives authorization for an REA loan, it appears that substantial portions of each succeeding loan are diverted to meet the excess of actual construction costs over estimated costs relating to the prior loan. Apparently the REA is not too concerned with these construction cost overrides since it keeps making additional loans to Applicant. Applicant has indicated that if the funds available under the existing 'D' loan are not sufficient to meet construction costs contemplated in its revised construction program it will attempt to obtain the additional sums required to complete its revised construction program from the REA by applying for a future 'E' loan.

"The Federal Government recently announced an increase in the interest rate on REA loans that in the future will more closely parallel interest rates in the commercial money market. No longer will Applicant be able to count on a spread of nearly 6% between the approximately 8% rate of return that it receives in toll settlements from PT&T and the 2% interest rate that it pays for REA funds. If Applicant fails to control costs, it is almost certain that the customers of Redwood Empire will be burdened with requests for new and higher rates in the future based on these additional construction costs, and higher cost of capital. For this reason it becomes even more important for Applicant to institute economies and efficiencies and to adhere closely to its cost estimates.

"We have no positive solution to these problems. If comparisons of budgeted construction costs are filed in a timely manner, the Commission will have an opportunity to become aware of cost overruns as they develop, but reports alone will not prevent these cost overruns from occurring.

"In the past Applicant's controlling shareholders have been reluctant to invest their own funds in the company, preferring to operate on borrowed capital to the fullest extent possible. We suggest, therefore, that Applicant be placed on notice that it will be required to finance with equity capital those portions of any future capital requirements reflecting cost overruns on prior loans. Such a requirement may give Applicant incentive to control costs more closely. The Commission also should prohibit Applicant from drawing down additional funds from REA 'D' loan at any time that Applicant is in arrears in supplying financial data and operating reports ordered by the Commission. Moreover, we recommend that Applicant be placed on notice that it is subject to contempt proceedings under Sections 2107 and 2111 of the Public Utilities Code for failure to comply with Commission orders and that future violations will cause the Commission to take punitive action."

Based on its report, the staff made the following recommendations:

"The following ordering paragraphs should be included in the decision:

"IT IS ORDERED that:

- "1. Redwood Empire Telephone Company is authorized to use 'D' loan funds in the amounts and for the purposes described in Exhibit A attached to Application No. 53576 filed September 8, 1972.
- "2. Applicant is placed on notice that in considering future loan applications the Commission will examine carefully the construction project costs under the 'D' loan authorization. If any future loan proceeds are earmarked to cover overrides in the 'D' loan, the Commission may require Applicant to finance such overrides with equity capital.
- "3. Applicant is reminded that it is required by Ordering Paragraph No. 5 of Decision No. 77208 to submit to the Commission copies of all correspondence, reports or other documents sent to or received from the REA during the immediate prior calendar quarter, within 60 days of the end of each quarter. Should Applicant fail to comply with this order, in a timely manner, Applicant is prohibited from making any further expenditures from its 'D' loan funds until compliance is effected."

Ordering Paragraphs 4, 5, and 7 of Decision No. 77208 ordered the following:

- "4. San Miguel Telephone Company of California shall file with the Commission a report, or reports, as required by General Order No. 24-B, which order, insofar as applicable, is hereby made a part of this order.

"5. Applicant shall submit to the Commission:

- a. Operating and capital expenditure budgets for a five-year period. In addition to showing dollar amounts expended on plant construction, the budget shall include a construction time schedule by exchange and by type of plant. These budgets shall be filed within 90 days.
- b. Quarterly financial statements (balance sheets, income statements, and capital expenditure statements, with supporting schedules) showing how closely the budget forecasts in dollar amounts and construction time schedules have been met, within 60 days of the end of each quarter.
- c. Quarterly reports showing the number of main stations, by exchange, within 60 days of the end of each quarter.
- d. Copies of all correspondence, reports or other documents sent to or received from the REA during the immediate prior calendar quarter, within 60 days of the end of each quarter.
- e. A quarterly payroll summary segregated between office, management and maintenance and operational employees, showing the amount of the payroll charged to operating expenses, plant accounts and other accounts, within 60 days of the end of each quarter."

"7. Applicant shall increase its common equity investment to a minimum of 10% of capitalization, and maintain this minimum percentage thereafter."

Decision No. 77208 became effective on June 1, 1970.

General Order No. 24-B which became effective on July 1, 1964 states:

"On or before the 25th day of each month, the following statements for the preceding month ...shall be filed with the Commission."

The records of this Commission show that Redwood's filings are consistently late and are not in the format required by the General Order.

Exhibit 15 shows that in regard to Ordering Paragraph 5 "...only a small portion of the correspondence and reports have been submitted to the Commission in compliance with the ordering paragraphs of the decision despite repeated requests for such material."

Section 581 of the Public Utilities Code states:

"Every public utility shall furnish to the commission in such form and detail as the commission prescribes all tabulations, computations, and all other information required by it to carry into effect any of the provisions of this part, and shall make specific answers to all questions submitted by the commission."

"Every public utility receiving from the commission any blanks with directions to fill them shall answer fully and correctly each question propounded therein, and if it is unable to answer any question, it shall give a good and sufficient reason for such failure."

Section 2107 of the Public Utilities Code states:

"Any public utility which violates or fails to comply with any provision of the Constitution of this State or of this part, or which fails or neglects to comply with any part or provision of any order, decision, decree, rule, direction, demand, or requirement of the commission, in a case in which a penalty has not otherwise been provided, is subject to a penalty of not less than five hundred dollars (\$500) nor more than two thousand dollars (\$2,000) for each offense."

Section 2108 of the Public Utilities Code states:

"Every violation of the provisions of this part or of any part of any order, decision, decree, rule, direction, demand, or requirement of the commission, by any corporation or person is a separate and distinct offense, and in case of a continuing violation each day's continuance thereof shall be a separate and distinct offense."

In Decision No. 77208 (mimeographed copy page 9) we said, "The Commission expects that defendant will proceed promptly, diligently and in good faith to carry out all of the orders enumerated above. If there is reason to believe that defendant has not been diligent in carrying out the above orders, the Commission will formally inquire into the circumstances for the purpose of determining whether or not defendant shall be held in contempt."

There are abundant reasons, as discussed above, to believe that Redwood has not been diligent in carrying out the orders of Decision No. 77208. Therefore, we have today instituted a formal investigation to determine whether or not Redwood should be held in contempt under Section 2113 of the Public Utilities Code which states:

"Every public utility, corporation, or person which fails to comply with any part of any order, decision, rule, regulation, direction, demand, or requirement of the commission or any commissioner is in contempt of the commission, and is punishable by the commission for contempt in the same manner and to the same extent as contempt is punished by courts of record. The remedy prescribed in this section does not bar or affect any other remedy prescribed in this part, but is cumulative and in addition thereto."

Findings

1. The money, property, or labor to be procured or paid for by the remaining proceeds of applicant's Rural Electrification Administration "D Loan" is reasonably required for the purposes specified herein, which purposes are not, in whole or in part, reasonably chargeable to operating expenses or to income.

2. Until Redwood has obtained necessary easements for construction of the San Miguel/Parkfield toll line with local distribution taps in the San Miguel exchange and of the Parkfield outside plant reconstruction or until further order of this Commission, applicant should withhold and reserve \$200,000 of "D" loan funds for these construction purposes.

Conclusions

1. The application should be granted.
2. A public hearing is not necessary.

The authorization herein granted is for the purpose of this proceeding only and is not to be construed as indicative of amounts to be included in proceedings for the determination of just and reasonable rates.

SECOND INTERIM ORDER

IT IS ORDERED that:

1. Redwood Empire Telephone Company (Redwood) may utilize the remaining proceeds of its Rural Electrification Administration "D Loan" for the purposes set forth in Exhibit A attached to Application No. 53576.

2. Redwood shall file with the Commission the reports required by General Order No. 24-B, which order, insofar as applicable, is hereby made a part of this order.

3. Until necessary easements have been obtained for construction of the San Miguel/Parkfield toll line with local distribution taps in the San Miguel exchange and of the Parkfield outside plant reconstruction or until further order of this Commission, Redwood is ordered to withhold and reserve \$200,000 of "D" loan funds for the foregoing construction purposes.

4. Applicant is placed on notice that in considering future loan applications the Commission will examine carefully the construction project costs under the "D" loan authorization. If any future loan proceeds are earmarked to cover overrides in the "D" loan, the Commission may require applicant to finance such overrides with equity capital.

5. Applicant is reminded that it is required by Ordering Paragraph No. 5 of Decision No. 77208 to submit to the Commission copies of all correspondence, reports, or other documents sent to or received from the REA during the immediate prior calendar quarter, within 60 days of the end of each quarter. Should applicant fail to comply with this order, in a timely manner, applicant is prohibited from making any further expenditures from its "D" loan funds until compliance is effected.

6. By the 15th of each month Redwood shall file a report for the preceding month informing the Commission as to its progress on each project enumerated in Exhibit A of Application No. 53576 filed September 8, 1972. Such reports shall include but not be limited to progress in obtaining easements, engineering design and staking, preparation of contracts and specifications, advertising and award of construction bids, construction progress, project completion, main stations in service, and held orders and regrade requests. The first such report shall be for the month of April 1973.

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

Dated at San Francisco, California, this 3rd day of APRIL, 1973.

Vernon L. Spurgeon
President
William J. Spurgeon
[Signature]
[Signature]
[Signature]
Commissioners