

LSC

Decision No. 83809

ORIGINAL

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of)

CONTINENTAL TELEPHONE COMPANY)
OF CALIFORNIA, a California)
corporation,)

for an order authorizing it to issue)
and sell \$25,000,000 Principal Amount)
of its First Mortgage Bonds, Series K,)
and exempting the issuance and sale)
of said Bonds from the requirements)
of the Commission's Competitive)
Bidding Rule.)

Application No. 55302
(Filed November 7, 1974)

Orrick, Herrington, Rowley & Sutcliffe, by James F. Crafts, Jr.,
Attorney at Law, for applicant.
Sidney J. Webb, for the Commission staff.

O P I N I O N

Continental Telephone Company of California, a California corporation, seeks authority to execute and deliver a Fifteenth Supplemental Indenture, and to issue and sell \$25,000,000 principal amount of its First Mortgage Bonds, Series K, through negotiations which may be conducted outside of California and in the State of New York.

After due notice, a public hearing in the above-entitled matter was held before Examiner Tomita in San Francisco on November 27, 1974, at the conclusion of which the matter was taken under submission. The Commission has received no protests in the proceeding.

Applicant furnishes local and toll telephone service in portions of Arizona, California and Nevada. It is a subsidiary

A. 55302 LSC

of Continental Telephone Corporation, a Delaware corporation. For the 12 months ended September 30, 1974, applicant's reported total operating revenues and net income amounted to \$78,200,512 and \$12,729,083, respectively.

The reported capitalization ratios of applicant at September 30, 1974, and as adjusted to give effect to the proposed bond issue, are summarized from the application, as follows:

| | <u>September 30, 1974</u> | <u>Pro Forma</u> |
|-----------------|-------------------------------|----------------------|
| Long-term debt | 50.29% | 55.12% |
| Preferred stock | 7.84 | 7.08 |
| Common equity | <u>41.87</u> | <u>37.80</u> |
| Total | <u>100.00%</u> | <u>100.00%</u> |

The utility proposes to negotiate the terms of the new bonds with a nationwide group of underwriters. The bonds would be secured by an existing indenture as heretofore amended and supplemented and as to be further amended and supplemented by a proposed Fifteenth Supplemental Indenture.

Applicant's construction program for the year 1974 amounts to approximately \$31,872,000, of which it has financed a portion by selling \$5,000,000 principal amount of debentures authorized by Decision No. 82914, dated May 29, 1974, in Application No. 54864. The company reports \$17,000,000 of outstanding short-term bank loans incurred to finance temporarily its construction program, and that such loans will be increased before the proceeds of the new bonds are received. In addition to retiring short-term bank loans said proceeds will be applied toward paying the cost of additional facilities under the utility's 1975 construction program.

The only material issue for the Commission to resolve in this proceeding is whether or not the sale of the proposed bonds should be required to be through competitive bidding. In addition, applicant specifically requests certain findings and authorizations due to the existence of the California Usury Law, which we have held on several recent occasions does not apply to security issues authorized by this Commission.

Applicant's reasons for requesting exemption from the competitive bidding requirements are set forth in the application as follows:

"Although applicant has been able to sell its its Series I First Mortgage Bonds and Series J First Mortgage Bonds at competitive bidding in 1971 and 1973, respectively, the marketing of utility bonds with a rating lower than AA has continued to constitute a problem for underwriters. This situation has been compounded in the last six months due to the extremely tight money conditions which have prevailed. For these reasons, sales of lower-rated bonds at competitive bidding in recent months have not only been made at higher underwriting discounts but have also, on the average, resulted in higher interest costs to the issuers. In addition, the ability of underwriters to market bonds is greatly enhanced if the timing of the issue can be adjusted to meet short-term fluctuations in interest rates and in the volume of offerings. Since the date for a sale of bonds at competitive bidding must be selected well in advance and it is difficult to change a bidding date once selected other than by a substantial postponement, applicant is seeking herein an exemption from the requirements of the competitive bidding rule for the sale of the new bonds. . . A negotiated transaction permits the underwriters to develop advance interest in the issue prior to the offering and a more sensitive adjustment of the terms of the offering to current market conditions."

The evidence adduced at the hearing persuades us that the present unsettled market conditions justify negotiated offerings of the securities. Although a negotiated sale may allow more flexibility in marketing the proposed bonds and facilitate the sale with less cost to applicant, a negotiated sale is not always necessarily in the public interest. This decision is not intended to modify the competitive bidding rule as initially set out in Decision No. 38614 (46 Cal.R.C. 281 (1946)).

The utility seeks authorization to situate and structure the proposed issuance and sale of such bonds outside California, in the State of New York; however, it does not intend to restrict the market for the bonds to areas outside of California. Inasmuch as applicant's proposal does not operate to restrict the potential bond market to the detriment of applicant or its ratepayers, we are not opposed to such structuring and situating of the proposed issuance and sale. In this connection recent Decisions Nos. 83411, 83504, 83598 and 83600, among others, hold that this Commission in exercising its authority to regulate public utility debt securities is not restricted by the California Usury Law and its ramifications. We reaffirm this holding and conclude that if the interest limitation of the California Usury Law is exceeded but it is determined that the transaction, whether negotiated or by competitive bid, is the best the utility can obtain because of market conditions, then the public interest requires this Commission to authorize the issuance and sale of the debt instruments.

After consideration the Commission finds that:

1. Applicant is a California corporation operating under the jurisdiction of this Commission.
2. The proposed bonds would be for proper purposes.
3. The proposed documents would not be adverse to the public interest.
4. Applicant has need for external funds for the purposes set forth in this proceeding.
5. The sale of the proposed bonds should not be required to be through competitive bidding.

6. The money, property or labor to be procured or paid for by the bonds herein authorized 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.
7. Underwriters will not be restricted from offering or selling applicant's Series K bonds in California.
8. The security for applicant's Series K bonds would consist mainly of California property.
9. Prevailing market conditions may necessitate that applicant's proposed bonds will be issued and sold with a rate of interest exceeding the limitations provided in Article XX, Section 22 (Interest Rates) of the California Constitution.
10. Pursuant to plenary powers granted to the Legislature by Article XII, Section 5 of the California Constitution, the Legislature is authorized to confer such additional consistent powers upon this Commission as it deems necessary and appropriate, unrestricted by any other provisions of the California Constitution.
11. The Legislature has conferred upon this Commission the authority to regulate the issuance of public utility securities, including evidences of indebtedness, and to prescribe restrictions and conditions as it deems reasonable and necessary (Sections 816 et seq. of the Public Utilities Code).
12. Pursuant to the plenary powers granted to the Legislature in Article XII, Section 5 of the California Constitution, it conferred upon this Commission comprehensive and exclusive power over the issuance of public utility securities, including evidences of indebtedness, and the California Usury Law cannot be applied as a restriction on this Commission's regulation of such issuances of public utility securities, including the establishment of a reasonable rate of interest.
13. In addition to the plenary powers granted to the Legislature by the California Constitution pursuant to which the Legislature conferred upon this Commission exclusive authority to regulate the issuance of bonds by public utilities (Sections 816 et seq. of the Public Utilities Code), irrespective of the Usury Law, judicial interpretation of the California Usury Law has exempted corporate bonds of public utilities from operation of the Usury Law.

14. If the usury limitation contained in Article XX, Section 22 (Interest Rates) of the California Constitution and the Usury Law Initiative Act is exceeded, but the transaction is authorized by this Commission and is the best applicant can obtain because of market conditions, applicant utility, its assignees or successors in interest, will have no occasion to and cannot assert any claim or defense under the California Usury Law; further, and necessarily, because of lawful issuance by applicant of bonds in compliance with authorization by the Public Utilities Commission, persons collecting interest on such authorized bonds are not subject to the Usury Law sanctions.
15. The Commission does not find objectionable applicant's proposal to situate and structure the proposed issuance and sale of said bonds in the State of New York, since this proposal does not restrict the potential bond market to areas or purchasers outside California.

On the basis of the foregoing findings we conclude that the application should be granted. As set forth in said Decisions Nos. 83411, 83504, 83598 and 83600, among others, we further conclude that the usury limitations on interest contained in Article XX, Section 22 of the California Constitution and the Usury Law Initiative Act do not apply to the issuance of public utility securities, including evidences of indebtedness, lawfully authorized by the Public Utilities Commission. 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.

Applicant is hereby placed on notice that, if the Commission believes that the negotiated price or interest rate pertaining to the proposed bond issue will result in an excessive effective interest cost, it will take into consideration in rate proceedings only that which it deems reasonable.

O R D E R

IT IS ORDERED that:

1. The sale by Continental Telephone Company of California of not exceeding \$25,000,000 aggregate principal amount of its First Mortgage Bonds, Series K, is hereby exempted from the Commission's competitive bidding rule set forth in Decision No. 38614, dated January 15, 1946, as amended, in Case No. 4761.
2. Continental Telephone Company of California may execute and deliver a Fifteenth Supplemental Indenture in substantially the same form as Exhibit B attached to the application.
3. Continental Telephone Company of California may issue and sell not exceeding \$25,000,000 aggregate principal amount of its First Mortgage Bonds, Series K, on terms and conditions to be negotiated in accordance with the record in this proceeding.
4. Continental Telephone Company of California may situate and structure the proposed issuance and sale of its First Mortgage Bonds, Series K, outside California, in the State of New York.
5. An interest rate for Continental Telephone Company of California's First Mortgage Bonds, Series K, may exceed the maximum annual interest rate otherwise permitted under the California Usury Law, as contained in Article XX, Section 22 (Interest Rates) of the California Constitution and the Usury Law Initiative Act, if market conditions so require.
6. Neither Continental Telephone Company of California, nor anyone purporting to act on its behalf, shall at any time assert in any manner, or attempt to raise as a claim or defense in any proceeding, that the interest on its First Mortgage Bonds, Series K, exceeds the maximum permitted to be charged under the California Usury Law or any similar law establishing the maximum rate of interest that can be charged to or received from a borrower.

7. Continental Telephone Company of California shall use the proceeds from the sale of said bonds for the purposes referred to in the application.

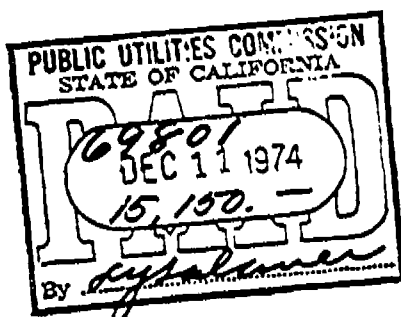
8. Upon determining the maturity date, price and interest rate pertaining to the bonds herein authorized, Continental Telephone Company of California shall notify the Commission thereof in writing.

9. As soon as available, Continental Telephone Company of California shall file with the Commission three copies of its prospectus pertaining to said bonds.

10. Within one month after issuing and selling the bonds herein authorized, Continental Telephone Company of California shall file with the Commission a statement, in lieu of a report under General Order No. 24-B, disclosing the purposes for which it used the bond proceeds.

11. This order shall become effective when Continental Telephone Company of California has paid the fee prescribed by Section 1904(b) of the Public Utilities Code, which fee is \$15,150.

Dated at San Francisco, California, this 10th day of December, 1974.



Vernon L. Sturgeon
President
William J. Symon
Thomas Moran
Robert E. Myland
Commissioners