

Decision 84 04 104 APR 12 1984

ORIGINAL

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application)
of THE PACIFIC TELEPHONE AND)
TELEGRAPH COMPANY, a corporation,)
for authority to increase certain)
intrastate rates and charges)
applicable to telephone services)
furnished within the State of)
California due to increased)
depreciation expense.)

Application 82-11-07
(Filed November 4, 1982)

In the Matter of the Application)
of THE PACIFIC TELEPHONE AND)
TELEGRAPH COMPANY, a corporation,)
for authority to increase certain)
interstate rates and charges)
applicable to telephone services)
furnished within the State of)
California.)

Application 83-01-22
(Filed January 17, 1983)

Investigation on the Commission's)
own motion into the rates, tolls,)
rules, charges, operations, costs,)
separations, inter-company settle-)
ments, contracts, service, and)
facilities of THE PACIFIC)
TELEPHONE AND TELEGRAPH COMPANY,)
a California corporation; and of)
all the telephone corporations)
listed in Appendix A, attached)
hereto.)

OII 83-04-02
(Filed April 20, 1983)

In the Matter of the Application)
of THE PACIFIC TELEPHONE AND)
TELEGRAPH COMPANY, a corporation,)
for authority to adopt intrastate)
access charge tariffs applicable)
to telephone services furnished)
within the State of California.)

Application 83-06-65
(Filed June 30, 1983)

TELEPHONE ANSWERING SERVICES
OF CALIFORNIA,

Complainant,

vs.

THE PACIFIC TELEPHONE AND
TELEGRAPH COMPANY,

Defendant.

Case 82-10-09
(Filed October 28, 1982)

In the Matter of the Suspension and
Investigation on the Commission's
own motion of the tariff schedules
to offer interLATA telecommunica-
tions services filed under Advice
Letter 1 of AT&T Communications.

(I&S) Case 83-11-06
(Filed November 22, 1983)

In the Matter of the Suspension and
Investigation on the Commission's
own motion of tariffs to reflect
corporate divestiture and the Tariff
Information Management System filed
under Advice Letter 14641 of The
Pacific Telephone and Telegraph
Company.

(I&S) Case 83-11-07
(Filed November 22, 1983)

ORDER MODIFYING DECISION 83-12-025
AND DENYING REHEARING

On December 7, 1983, the Commission issued Decision (D.)
83-12-025, which authorized a \$445,450,000 interim general rate
increase to the Pacific Telephone and Telegraph Company, now
Pacific Bell (Pacific), to be collected through a 10.30% surcharge
on present rates. The American Telephone and Telegraph Company
(AT&T) and Toward Utility Rate Normalization (TURN) have filed
applications for rehearing of this decision. We have carefully
considered all of the allegations raised in these applications,

and are of the opinion that sufficient grounds for granting rehearing have not been shown. However, our further review has led us to modify several areas of the decision, as indicated below, to more clearly express our rationale and intent.

We first note that AT&T's application also seeks rehearing of D.83-12-024, wherein we authorized Pacific to establish and collect access charges from long-distance carriers for the provision of exchange access service enabling placement of intrastate toll calls. We will treat AT&T's application in connection with our disposition of the other applications and petitions protesting D.83-12-024, and do not address it in this order.

Our first modification concerns the subject of underutilized plant. We have decided not to change our determination that Pacific may continue to earn 50% of the return applicable to that plant; however, upon further consideration, we do not feel it appropriate that Pacific should file for relief from this penalty between general rate cases. We will modify our discussion and finding accordingly.

Secondly, we are persuaded that as a policy matter we should reverse our decision to eliminate the imputation of a 6% cost to \$82 million of Pacific's common equity. While insignificant from a rate of return perspective, our earlier decision to impute this cost was done for the explicit purpose of protecting Pacific's ratepayers from having to absorb a cost Pacific incurred solely because of the way it chose to reorganize with AT&T. While the onset of divestiture might set the appropriate stage for discontinuing this imputation, D.83-12-025 was to assess the "business as usual" situation. For these reasons, we will continue the imputation for the present, but will consider the issue further in Phase 2.

We finally address TURN's contention that we have improperly disregarded the decrease in the California Corporation Franchise Tax (CCFT) rate applicable to Pacific as of January 1, 1984. We disagree with this contention. It is true that the Commission has on several occasions provided for yearly tax adjustments to be made between general rate cases, or set rates subject to refund pending determination of the correct tax to be applied where federal tax laws had undergone a major modification. We do not dispute the argument that we have the authority to have done the same in the present situation. However, for reasons already stated in D.83-12-025, we do not consider such a course to be necessary or desirable.

The basic principle underlying our rate setting authority is that of test-year ratemaking. Under that principle, it is not appropriate to go beyond the test year to adjust either revenues or expenses except in exceptional circumstances. This case presents one of those circumstances; namely, divestiture of Pacific from AT&T. In order to enable consideration of what were predicted to be divestiture-related financial impacts of substantial magnitude, we divided the rate case into pre- and post-divestiture phases.

In theory, financial impacts caused by divestiture were not to be considered until the post-divestiture phase. In practice, our knowledge that divestiture was pending was a factor in Phase 1, to the extent that it influenced certain value judgments to be made -- the best example of this being our rate of return determination. But where specific items of expense or revenue were concerned, we have tried to carefully separate pre- and post-divestiture effects, to be consistent with the test-year ratemaking concept and the important exception necessitated in this case by divestiture.

We think our treatment of the CCFT rate satisfies the above. The correct application of the decreased rate is being considered in Phase 2 and will be applied beginning with the decision in that Phase, expected this May. If the alternative had been to postpone its application until a decision in Pacific's next general rate application, we might well have decided to provide for an earlier adjustment. But by providing for its consideration in Phase 2, we have in effect accomplished the same result.

IT IS THEREFORE ORDERED that D.83-12-025 is modified as follows:

1. The sentence beginning on the last line of page 123 and continued on page 124 is changed to read:

"We will consider a normal rate of return on this plant if, in the course of future general rate application proceedings, PT&T can show that it is in use."

2. The last paragraph on page 145 is changed to read:

"It is true that the impact of the 6% imputation could easily be absorbed into our rate of return determination, considering the relative lack of precision in making that determination. It is also desirable that PT&T should embark upon divestiture as cleanly as possible. However, regardless of these factors, the 6% imputation was done for the very important reason of protecting PT&T's rate-payers from the burden of a cost the Commission decided was more equitably borne by the shareholders. We do not see sufficient reason to eliminate that imputation today, although we will review the matter again in Phase 2, along with numerous other divestiture issues."

3. Finding of Fact 8 is changed to read:

"A reasonable rate of return to be applied to PT&T's California intrastate rate base is 12.64%."

4. Finding of Fact 9 is changed to read:

"A 12.64% return on that portion of PT&T's capitalization ascribed to the California intrastate rate base adopted in this decision would yield approximately 16.0% on California ascribed common equity."

5. Finding of Fact 10 is changed to read:

"PT&T's rates subject to the jurisdiction of this Commission should be increased by \$373,110,000, which increase, excluding the underutilized plant adjustment, should produce a 12.64% rate of return on PT&T's California intrastate rate base for the estimated test year 1983."

6. Finding of Fact 11 is changed to read:

"A 12.64 % rate of return on California intrastate rate base would provide an interest coverage of 4.27 times before taxes on income, and 2.72 times after taxes."

7. Finding of Fact 26a is added to read:

"It is appropriate to review Pacific's tax liability under the applicable post divestiture CCFT rate in the second phase of this proceeding."

8. Finding of Fact 32 is changed to read:

"In its next general rate case, PT&T may apply to have the rate of return on the underutilized plant changed, based on the usage of that plant."

9. Finding of Fact 37 is changed to read:

"The imputation of a 6% cost to \$82 million of common equity required by D.82-05-007 should be continued."

10. Finding of Fact 38 should be changed to read:

"On a recast three basis, gross revenues should be increased by \$434,116,000 after adjustment for underutilized plant."

11. Conclusion of Law 1 should be changed to read:

"Based on the foregoing findings of fact and under PU Code §§ 451 and 454, the Commission should grant PT&T the authority to apply surcharges to its present rates as provided in the following order to enable PT&T to earn additional revenues of \$373,110,000."

12. Conclusion of Law 3 should be changed to read:

"The above \$373,110,000 increase is in addition to the \$61,006,000 previously authorized in D.83-08-031."

13. Ordering Paragraph 3 is changed to read:

"PT&T and the staff should continue to impute a 6% cost to \$82 million of common equity as required by D.82-05-077."

14. New Ordering Paragraph 4 is added to read:

"The 1984 test year revenue requirement adopted in Phase 2 of the PT&T rate case will be reduced by the product of (1) the reduction in 1983 test year revenue requirement resulting from Ordering Paragraph 3, multiplied by (2) the ratio of the number of days in 1983 during which the Phase 1 rates are in effect to the total number of days in the test year."

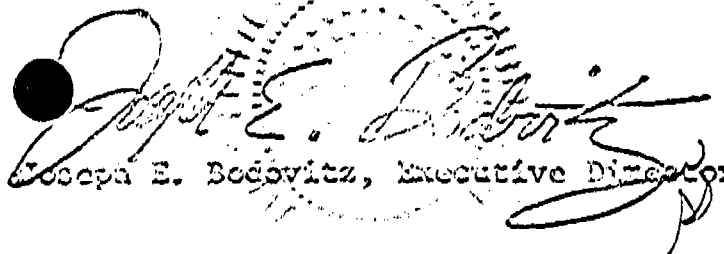
This order is effective today.

Dated APR 18 1984, at San Francisco, California.

I CERTIFY THAT THIS DECISION WAS APPROVED BY THE ABOVE COMMISSIONERS TODAY.

LEONARD M. GRIMES, JR.
President

VICTOR CALVO
FRISCILLA C. GREW
DONALD VIAL
WILLIAM T. BAGLEY
Commissioners


Joseph E. Bodovitz, Executive Director

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