

Decision SS 02 046

FEB 24 1988

ORIGINAL

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of)
Pacific Bell, a corporation, for)
authority to increase certain intra-)
state rates and charges applicable)
to telephone services furnished)
within the State of California.)

Application 85-01-034
(Filed January 22, 1985;
amended June 17, 1985 and
May 19, 1986)

_____)
)
)

I.85-03-078
(Filed March 20, 1985)

And Related Matters.)
)
)

OII 84
(Filed December 2, 1980)

Case 86-11-028
(Filed November 17, 1986)

OPINION MODIFYING DECISION 87-12-067

Introduction

Subsequent to the issuance of Decision (D.) 87-12-067, our Second Interim Opinion on Pacific Bell's 1986 test year revenue requirement (the Phase 2 decision), Pacific Bell and the Division of Ratepayer Advocates (DRA) filed separate pleadings requesting certain modifications. This decision resolves the issues raised in these separate requests.

DRA's Request

On January 29, 1988, DRA filed a "Request for an Extension of Time Pursuant to Rule 43", seeking relief from certain directives contained in Ordering Paragraph 20 of the Phase 2 decision requiring DRA to select a consultant in connection with its evaluation of the outside plant utilization issue within 90 days of December 22, 1987 (the effective date of the Phase 2 decision). DRA states that the 90-day period we specified in the Phase 2 decision is both insufficient to complete

the necessary request for proposal (RFP) process, and unnecessary, given the fact that Pacific Bell apparently will not seek removal of the outside plant penalty (which we retained in the Phase 2 decision) in the near future. DRA maintains that the evaluation study should be conducted expeditiously, but only after Pacific Bell files its application seeking removal of the outside plant penalty.

We indicated in the Phase 2 decision that we envisioned the penalty removal study would involve two parts: (1) the initial study designed to determine whether to undertake a full-scale audit or a statistical audit, and (2) the primary audit designed to ascertain whether Pacific Bell has met the 67.6% standard justifying removal of the outside plant penalty (D.87-12-067, mimeo. pp. 169-171). Ordering Paragraph 20 required DRA to select the consultant who would perform the initial study within 90 days, and specified that the primary audit would be triggered by the filing of Pacific Bell's application seeking removal of the \$13.8 million underutilization penalty. (D.87-12-067, mimeo. pp. 332-333.)

However, DRA indicates in its Request that it intends to use the same consultant for both parts of the penalty removal study and the separate generic utilization study mandated in Ordering Paragraph 21 of the Phase 2 decision. Given the amount of time DRA believes is necessary to complete the RFP process, and the fact that there is no formal opposition to DRA's requested extension, we will modify Ordering Paragraph 20 to delete the reference to a 90 day time requirement. In its place we will specify a time limit of December 31, 1988, consistent with DRA's assertion that the RFP process and the required initial evaluation can be completed "during the course of 1988." (DRA Request, p. 1.)

Pacific Bell's Petition for Modification

On February 1, 1988, Pacific Bell filed a "Petition for Modification of D.87-12-067 and For An Extension of Time to Comply With Ordering Paragraph 15a of That Decision." On February 11,

1988, DRA filed its formal reply indicating agreement with the majority of Pacific Bell's request, but expressing opposition to one requested change: The use of a different billing base for calculating the surcharge adjustment.

Meanwhile, on February 5, 1988, the Executive Director acceded to Pacific Bell's request for a 7-day extension of time to comply with Ordering Paragraph 15a, in order to enable us to consider the requested modifications prior to the time certain advice letter filings are mandated under Ordering Paragraph 15a. This extension also applies to each exchange carrier required to make an Advice Letter Filing in compliance with Ordering Paragraph 15a.

1. The Zum Expansion Issue

As Pacific notes, the Zum Expansion issue which results in a \$15.088 million revenue requirement reduction, is properly keyed to an expansion actually implemented in the Sacramento, San Diego, Los Angeles, and Orange County Extended Areas. The Phase 2 decision mistakenly refers to the San Francisco-East Bay Zum Expansion Proposal submitted in the rate design portion of this proceeding. Pacific Bell properly notes that the San Francisco-East Bay Zum Expansion Proposal should not be decided until all rate design issues are decided, since that proposal has a revenue requirement impact that is not accounted for in the Phase 2 decision. Therefore it is appropriate to correct the discussion section, relevant findings of fact, conclusion of law, and ordering paragraph.

2. Corrections to Ordering Paragraph 15a

Pacific Bell, DRA, and the Commission Advisory and Compliance Division (CACD) agree that Ordering Paragraph 37 conflicts with Ordering Paragraph 15a's provision that no portion of the intraLATA SPF to SLU surcharge adjustment shall be applied to intraLATA toll, and recommend that Ordering Paragraph 37 be modified accordingly. ✓

If the Commission adopts this modification, the existing -9.080% billing surcharge on intrastate intraLATA access services will change to -8.611%. The existing -0.193% surcharge on intraLATA services would become disaggregated into the following two surcharges: 0.276% for intraLATA toll services, and -0.727% for intraLATA exchange services, as shown on Attachment A. Accordingly, we will make the change to Ordering Paragraph 37, and related changes to Findings of Fact 149 and 150 and the underlying discussion (at mimeo. pp. 295-296).

Similarly, there is consensus among Pacific Bell, DRA, and CACD that Ordering Paragraphs 15a and 37 should be modified to provide that the surcharge adjustment shall be administered on a bill-and-keep basis, consistent with prior Commission decisions in this docket. These changes will also be made.

Pacific Bell, DRA, and CACD also believe that Ordering Paragraph 15a must be clarified to specifically note that the conversion steps for intraLATA SPF-to-SLU also involve a step for direct assignment of WATS, consistent with the testimony of DRA Witness Poponce. (Exhibit 324.) This change will be made.

There is also agreement that a minor clarification is necessary to the Ordering Paragraph 15a references to "intraLATA toll," by modifying that reference to read "intraLATA toll inclusive of intraLATA toll private line." Pacific Bell believes this modification is necessary for consistent application of the surcharge adjustment by the exchange companies.

Pacific Bell requests that Ordering Paragraph 37 be modified to state that Pacific Bell's Ordering Paragraph 15a Advice Letter Filing should begin with the second step of the intraLATA SPF to SLU conversion, since Pacific Bell has already implemented these steps in compliance with Ordering Paragraph 37 of the decision. This change will also be made.

Finally, as noted previously, the Executive Director has granted a 7-day extension of time relative to the filing of Advice Letters under Ordering Paragraph 15a, to accommodate the changes made in this decision. Therefore, the new date for such filings is February 29, 1988.

3. Modifications to Ordering Paragraph 12
(SRV Building Construction Costs)

Pacific, DRA, and CACD agree that Ordering Paragraph 12 should be modified to delete reference to the \$230 million cap as the maximum amount to be "booked to plant in service". Pacific Bell believes that the restrictive use of the term "book to plant in service" in Ordering Paragraph 12 runs counter to Federal Communications Commission (FCC) Uniform System of Accounts (USOA) standards, which provide that the plant in service account is the proper place to book all construction costs that have not been expressly disallowed and which relate to plant that has been placed in service. Instead, there should be an indication that the maximum amount which Pacific Bell may recognize for 1986 test-year ratemaking purposes for SRV building costs is \$230 million. This proposed modification, which results in no additional costs being recognized for ratemaking purposes beyond those costs recognized in the Phase 2 decision, is appropriately made.

4. 1986 Customer Billing Base
Versus 1987 Billing Base

The one requested modification which is disputed by DRA is Pacific Bell's request that the Phase 2 decision be modified to use Pacific Bell's 1987 billing base, rather than the 1986 billing base used in the decision. The Phase 2 decision orders Pacific Bell's revenues reduced by \$194.5 million, and implements that reduction by applying a surcharge adjustment. However, Pacific Bell maintains that the 3.29% adjustment ordered in the decision actually reduces its revenue requirement by approximately \$217 million. This is due to the fact that the 3.29% adjustment was arrived at by dividing \$194.471 million by the 1986 customer

billing base rather than the latest available 1987 customer billing base. If the more current billing base had been used, a 2.94% surcharge adjustment would have been calculated to reduce Pacific Bell's revenues by the \$194.471 million ordered.

As noted, DRA opposes Pacific Bell's request on the grounds that the 1987 customer billing base is not in the record, and that any attempt to insert it in the record would have been inappropriate updating beyond the 1986 test year. According to DRA: "It is completely logical that the numerator and the denominator in the formula to derive the surcharge adjustment should reflect the same year--1986. If the 1987 billing base were to be used it opens the door to update other aspects of the record including the long overdue adjustment to the inordinately high 15% return on equity." (DRA Reply, p. 2.)

Pacific Bell acknowledges that the 1987 customer billing base was not formally entered into the record in this proceeding, because the parties expected that a rate design decision would be issued concurrently with the Phase 2 decision, thus eliminating the need for any interim billing surcharge. Pacific Bell believes that in other instances the Commission has approved use of the 1987 billing base to calculate its surcharge adjustments. It refers to Advice Letter 15325, filed in compliance with Ordering Paragraph 5 of D.85-06-115, Advice Letter 15215B (1987 attrition), and other proceedings involving Universal Lifeline Telephone Service and proceedings regarding handicapped services.

However, we believe Pacific Bell's arguments about recent advice letter adjustments obscure the fact that the Phase 2 reductions are premised on a 1986 test year, not 1987 or 1988 events. It is fully consistent with test year ratemaking principles to use the 1986 billing base. Therefore we will not make the requested modification.

Findings of Fact

1. Due to the time constraints of the Request For Proposal (RFP) process, and DRA's wish to use the same consultant for the studies outlined in Ordering Paragraphs 20 and 21 of D.87-12-067, it is reasonable to extend the 90-day time period set forth in Ordering Paragraph 20 to December 31, 1988.

2. The \$15.088 million revenue requirement reduction adopted in D.87-12-067 associated with Zum Expansion, relates to an expansion already implemented in the Sacramento, San Diego, Los Angeles, and Orange County Areas, rather than the San Francisco-East Bay Expansion proposal presented during the Phase 2 rate design proceedings.

3. Ordering Paragraph 37 of D.87-12-067 should be clarified for consistency with Ordering Paragraph 15a, to provide that the portion of the overall billing surcharge/surcredit adjustment applicable to intraLATA SPF-to-SLU shall not be applied to intraLATA toll services.

4. The surcharge adjustments to be implemented via Ordering Paragraphs 15a and 37 of D.87-12-067 were intended to be collected on a bill and keep basis, consistent with a related decision issued earlier in this docket.

5. Ordering Paragraph 15a of D.87-12-067 should be further clarified to specifically note that (i) the conversion steps for intraLATA SPF-to-SLU also involve a step for direct assignment of WATS, and (ii) "intraLATA toll" is inclusive of "intraLATA toll private line."

6. Ordering Paragraph 37 of D.87-12-067 should be modified to indicate that Pacific Bell's Ordering Paragraph 15a Advice Letter filing should begin with the second step of the intraLATA SPF-to-SLU conversion.

7. Ordering Paragraph 12 of D.87-12-067 should be modified to delete reference to the phrase "book to plant in service", and replace that phrase with an indication of the ratemaking treatment for SRV costs adopted in D.87-12-067.

Conclusion of Law

D.87-12-067 should be modified as more particularly set forth in the ordering paragraphs below.

ORDER

IT IS ORDERED that D.87-12-067 is modified as follows:

1. Ordering Paragraph 20 is modified to read:

20. On or before December 31, 1988, DRA shall select a consultant using competitive bidding practices for the purpose of evaluating the costs and benefits of a full scale versus statistical independent audit of outside plant utilization, in accordance with the terms of this decision. After this initial evaluation is complete, DRA shall select an independent auditor and manage the primary audit as more fully discussed in this decision. This primary audit shall be triggered by the filing of the Pacific Bell application seeking removal of the \$13.8 million penalty.

2. The first paragraph of the discussion at mimeo. p. 157 under the heading "C. Zum Expansion" is deleted and the following paragraph inserted in its place:

In response to previous Commission directives, Pacific Bell presented its study of the 1986 test year impacts of local calling area boundary changes and Zone Usage Measurement (ZUM) expansion in the Sacramento, San Diego, Los Angeles, and Orange County Extended Areas. The latest version of this so-called "Ordering Paragraph 16.a Study" was submitted on April 15, 1986, and was reviewed by DRA (Exhibit 6, NCL-4 to NCL-5).

3. Finding of Fact 99 is modified to read:

99. The revenue requirement impact of the Sacramento, San Diego, Los Angeles, and Orange County Zum expansion proposal is negative \$15.088 million.

4. Finding of Fact 99a is deleted.

5. Conclusion of Law 28 is modified to read:

28. The revenue requirement impact of the Sacramento, San Diego, Los Angeles, and Orange County Zum expansion project (a negative \$15.088 million) should be reflected in the Phase 2 results of operations.

6. Ordering Paragraph 17a is deleted.

7. Ordering Paragraph 17b is modified to read:

17b. The revenue requirement impact of the Sacramento, San Diego, Los Angeles, and Orange County Zum expansion project (a negative \$15.088 million) is hereby adopted.

8. Ordering Paragraph 15a is modified to read:

15a. Each exchange telephone company which is a party to this proceeding shall implement the transition in allocation of nontraffic sensitive (NTS) costs to intraLATA toll services prescribed in the foregoing Opinion, gradually converting from use of an allocator based on SPF to one based on SLU through six annual steps and a step for direct assignment of WATS, beginning in January 1986 and continuing in January of each year thereafter until and including January 1992, thus coinciding with the interLATA SPF to SLU transition. On or before February 29, 1988, each exchange carrier offering intraLATA WATS service shall make an Advice Letter Filing under the terms of GO 96-A to revise the appropriate tariffs to implement a flash cut conversion to direct assignment of closed end intraLATA WATS line costs and to implement an intraLATA billing surcharge on local exchange services, exclusive of intraLATA toll (inclusive of intraLATA toll private line) to offset the lost intraLATA toll settlement effects due to the SPF to SLU transition and

the WATS phase-down. Thereafter each exchange telephone company shall make an Advice Letter filing under the terms of GO 96-A in coordination with each annual adjustment in its NTS cost allocator, in order to establish or revise its billing surcharge on intraLATA services, excluding intraLATA toll (inclusive of intraLATA toll private line), using the newly effective NTS cost allocator. The revenues resulting from the billing surcharge shall be administered on a bill-and-keep basis.

9. Ordering Paragraph 37 is modified to read:

37. Within five days of the effective date of this order Pacific Bell shall file revised tariff sheets to reflect the incremental changes in billing surcharge/surcredit adopted in this decision. The effective date of the ordered revisions shall be January 1, 1988. Such filing shall comply with General Order Series 96-A. The portion of the overall billing surcharge/surcredit adjustment applicable to intraLATA SPF-to-SLU shall not be applied to intraLATA toll services. The revenues resulting from the surcharge adjustment for interLATA SPF-to-SLU shall be included in the intrastate access service revenue pool. The revenues resulting from the Phase 2 overall surcharge/surcredit adjustment shall be administered on a bill-and-keep basis. In view of the implementation of the first step of the intraLATA SPF to SLU conversion and the direct assignment of WATS step ordered herein, Pacific Bell's Ordering Paragraph 15a Advice Letter filing should begin with the second step of the intraLATA SPF to SLU conversion.

10. Finding of Fact 149 is modified to read:

149. As shown by Table 1 the reduction in Pacific Bell's revenue requirement for all other issues addressed in this decision for the year January 1, 1988 through and including December 31, 1988 is \$194,471,000, which changes the billing surcharge/surcredit adjustment for access services and intraLATA toll services by an increment of negative 2.821% and for intraLATA exchange services by an increment of negative 3.824%.

11. Finding of Fact 150 is modified to read:

150. Consolidating AL 15325 with this decision will reduce customer confusion in that only one change in billing surcharge/surcredit will occur on January 1, 1988. This new billing surcharge/surcredit for intraLATA toll services is 0.276%, for intraLATA exchange services is negative 0.727%, and for interLATA access services is negative 8.611%.

12. The second full paragraph of the discussion at mimeo. p. 295, continuing to mimeo. p. 296 is modified to read:

The present billing surcharge/surcredit on other than access services is 1.287% and on access services is negative 5.363%. The reduction of \$194.471 million results in a billing surcharge/surcredit adjustment for access services and intraLATA toll services by an increment of negative 2.821% and for intraLATA exchange services by an increment of negative 3.824%. The SPF to SLU shift results in a billing surcharge adjustment on other than access services by an increment of 1.81% and an adjustment in the billing surcredit on access services by an increment of negative 0.427%. Combining these two incremental changes, the net incremental change in the present billing surcharge/surcredit is negative 1.011% for intraLATA toll services, negative 2.014% for intraLATA exchange services, and negative 3.248% for access services, which yields a surcharge/surcredit on intraLATA toll services of 0.276%; on intraLATA exchange services of negative 0.727%; and on access services of negative 8.611%.

13. Ordering Paragraph 12 is modified to read:

12. Based on the record developed in Phase 2, the maximum amount which Pacific Bell shall book to plant in service for 1986 ratemaking purposes for building costs in connection with SRV is \$230 million, exclusive of land costs; ancillary IDC shall be derived in view of this cap on building costs. Pacific Bell shall retain all data associated with its prior tracking of SRV costs, until further order of this Commission.

14. Pacific Bell's request to implement the revised surcharge adjustments ordered herein concurrently with its Ordering Paragraph 15a Advice Letter compliance filing, is granted.

IT IS FURTHER ORDERED that, except as provided above, Pacific Bell's Petition for Modification of D.87-12-067 is denied.

This order is effective today.

Dated FEB 24 1988, at San Francisco, California.

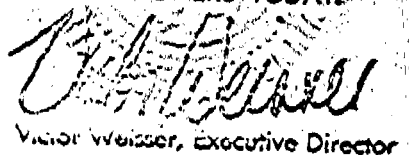
STANLEY W. HULETT
President

DONALD VIAL
JOHN B. OHANIAN
Commissioners

Commissioner Frederick R. Duda,
being necessarily absent, did
not participate.

Commissioner G. Mitchell Wilk,
being necessarily absent, did
not participate.

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


Victor Weisser, Executive Director

AB

Elimination of Technical Inconsistency Between O.P. 15A and O.P. 37
 (Application of IntraLATA SPF to SLU Revenue Requirement
 Adjustment to IntraLATA Exchange Only)

(\$ THOUSANDS)		INTERLATA ACCESS (A)	INTRALATA TOLL (B)	INTRALATA EXCHANGE (C)	TOTAL INTRASTATE D=A+B+C
CURRENT SURCHARGE CALCULATIONS	1. Surcharge A/O 12-31-87	-5.363	1.287	1.287	
	2. 1988 InterLATA SPF to SLU (AL 15325) (Consolidated with D-87-12-067)	-0.427	1.810	1.810	
	<u>D-87-12-067 ORDERING PARAGRAPH 37 PHASE II SURCHARGE CALCULATION</u>				
	3. 1986 Billing Base	\$1,080,724	\$2,089,830	\$2,746,416	\$5,916,970
	4. Adopted Revenue Requirement Adjustment	(35,521)	(68,685)	(90,265)	(194,471)
	5. Surcharge Adjustment (4/3)	-3.290	-3.290	-3.290	
6. TOTAL ADOPTED SURCHARGE/SURCREDIT (1+2+5)	-9.080	-0.193	-0.193		
PROPOSED MODIFICATION	<u>MODIFIED O.P. 37 PHASE II SURCHARGE CALCULATION CONSISTENT WITH O.P. 15A</u>				
	7. Revenue Requirement Adjustment (excluding IntraLATA SPF to SLU)	(30,478)	(58,954)	(77,482)	(166,914)
	8. IntraLATA SPF to SLU Revenue Requirement Adjustment			(27,557)	(27,557)
	9. Adopted Revenue Requirement Adjustment (7+8)	(30,478)	(58,954)	(105,039)	(194,471)
	10. Surcharge Adjustment - Basic (7/3)	-2.821	-2.821	-2.821	
	11. Surcharge Adjustment - SPF to SLU (8/3)			-1.003	
12. TOTAL MODIFIED SURCHARGE/SURCREDIT (1+2+10+11)	-8.611	0.276	-0.727		

1988, DRA filed its formal reply indicating agreement with the majority of Pacific Bell's request, but expressing opposition to one requested change: The use of a different billing base for calculating the surcharge adjustment.

Meanwhile, on February 5, 1988, the Executive Director acceded to Pacific Bell's request for a 7-day extension of time to comply with Ordering Paragraph 15a, in order to enable us to consider the requested modifications prior to the time certain advice letter filings are mandated under Ordering Paragraph 15a. This extension also applies to each exchange carrier required to make an Advice Letter Filing in compliance with Ordering Paragraph 15a.

1. The Zum Expansion Issue

As Pacific notes, the Zum Expansion issue which results in a \$15.088 million revenue requirement reduction, is properly keyed to an expansion actually implemented in the Sacramento, San Diego, Los Angeles, and Orange County Extended Areas. The Phase 2 decision mistakenly refers to the San Francisco-East Bay Zum Expansion Proposal submitted in the rate design portion of this proceeding. Pacific Bell properly notes that the San Francisco-East Bay Zum Expansion Proposal should not be decided until all rate design issues are decided, since that proposal has a revenue requirement impact that is not accounted for in the Phase 2 decision. Therefore it is appropriate to correct the discussion section, relevant findings of fact, conclusion of law, and ordering paragraph.

2. Corrections to Ordering Paragraph 15a

Pacific Bell, DRA, and the Commission Advisory and Compliance Division (CACD) agree that Ordering Paragraph 37 conflicts with Ordering Paragraph 15a's provision that no portion of the intraLATA SPF to SLU surcharge adjustment shall be applied to intraLATA toll,

and recommend that Ordering Paragraph 37 be modified accordingly. If the Commission adopts this modification, the existing -9.080% billing surcharge on intrastate intraLATA access services will change to -8.611%. The existing -0.193% surcharge on intraLATA services would become disaggregated into the following two surcharges: 0.276% for intraLATA toll services, and -0.727% for intraLATA exchange services, as shown on Attachment A. Accordingly, we will make the change to Ordering Paragraph 37, and related changes to Findings of Fact 149 and 150 and the underlying discussion (at mimeo. pp. 295-296).

Similarly, there is consensus among Pacific Bell, DRA, and CACD that Ordering Paragraphs 15a and 37 should be modified to provide that the surcharge adjustment shall be administered on a bill-and-keep basis, consistent with prior Commission decisions in this docket. These changes will also be made.

Pacific Bell, DRA, and CACD also believe that Ordering Paragraph 15a must be clarified to specifically note that the conversion steps for intraLATA SPF-to-SLU also involve a step for direct assignment of WATS, consistent with the testimony of DRA Witness Poponoe. (Exhibit 324.) This change will be made.

There is also agreement that a minor clarification is necessary to the Ordering Paragraph 15a references to "intraLATA toll," by modifying that reference to read "intraLATA toll inclusive of intraLATA toll private line." Pacific Bell believes this modification is necessary for consistent application of the surcharge adjustment by the exchange companies.

Pacific Bell requests that Ordering Paragraph 37 be modified to state that Pacific Bell's Ordering Paragraph 15a Advice Letter Filing should begin with the second step of the intraLATA SPF to SLU conversion, since Pacific Bell has already implemented these steps in compliance with Ordering Paragraph 37 of the decision. This change will also be made.

7. Ordering Paragraph 12 of D.87-12-067 should be modified to delete reference to the phrase "book to plant in service", and replace that phrase with an indication of the ratemaking treatment for SRV costs adopted in D.87-12-067.

Conclusion of Law

D.87-12-067 should be modified as more particularly set forth in the ordering paragraphs below.

ORDER

using a competitive bid process

IT IS ORDERED that D.87-12-067 is modified as follows:

1. Ordering Paragraph 20 is modified to read:

20. On or before December 31, 1988, DRA shall select a consultant for the purpose of evaluating the costs and benefits of a full scale versus statistical independent audit of outside plant utilization, in accordance with the terms of this decision. After this initial evaluation is complete, DRA shall select an independent auditor and manage the primary audit as more fully discussed in this decision. This primary audit shall be triggered by the filing of the Pacific Bell application seeking removal of the \$13.8 million penalty.

2. The first paragraph of the discussion at mimeo. p. 157 under the heading "C. Zum Expansion" is deleted and the following paragraph inserted in its place:

In response to previous Commission directives, Pacific Bell presented its study of the 1986 test year impacts of local calling area boundary changes and Zone Usage Measurement (ZUM) expansion in the Sacramento, San Diego, Los Angeles, and Orange County Extended Areas. The latest version of this so-called "Ordering Paragraph 16/a Study" was submitted on April 15, 1986, and was reviewed by DRA (Exhibit 6, NCL-4 to NCL-5).