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Decision 88 07 022 JUL 8 1988

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 intrastate 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)
And Related Matters.	I.85-03-078 (Filed March 20, 1985) OII 84 (Filed December 2, 1980) C.86-11-028 (Filed November 17, 1986)

(See Decisions 85-08-047, 86-01-026, and 87-12-067 for appearances.)

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OPINION ADOPTING A RATE DESIGN FOR PACIFIC BELL

I. Summary of Decision

In this rate design portion of Phase II of Pacific Bell's (Pacific) general rate case it was our initial intent to reflect the revenue requirement decrease of $86.435 million which we adopted in Decision (D.) 87-12-067 as modified by D.88-02-046, and D.88-03-064 by eliminating most positive or negative surcharges and adjusting rates to incorporate those amounts. Instead, this decision finds that because this proceeding is limited to 1986 projected volumes and cannot distribute that portion of Pacific's surcharges which became effective after 1986, following such a plan would likely result in rate increases now which would be followed by rate decreases in a short while when we conduct the supplementary rate design hearings in the present docket. Therefore, this decision retains the presently effective surcharges, with some modification, and only redistributes revenues presently collected in rates, including a shift out of toll rates and toll related services of about $71 million which was authorized in the Assigned Commissioner's Ruling in this proceeding dated April 1, 1986, and a shift of $11 million from Special Access rates to nonaccess rates which we authorized in D.87-08-048, with implementation put over to the present proceeding.

This rate redesign recognizes the impact of recent changes in the telephone marketplace, chief among which is the need for substantial reductions in rates for toll service, in order to position Pacific to better deal with potential direct intraLATA toll competition as well as indirect competition. Thus, for example, we adopt the proposal of the Division of Ratepayer Advocates (DRA) for a shift from the present subscriber plant

factor (SPF) means of allocating nontraffic sensitive costs of the local network to toll to the subscriber line usage (SLU) allocation factor.

Based on detailed and voluminous service cost studies we conclude that private line rates fall far below costs. We therefore increase Pacific's private line service recurring rates by up to 50%, and its nonrecurring private line charges by up to 100% of present levels, resulting in an overall private line revenue increase of $67.020 million. This increase is only for the test year. We do not grant the three-year incremental rate increases Pacific proposes, nor do we adopt any proposal for deaveraged local loop rate schedules or for separate alarm transport tariffs. We do adopt the disaggregated installation charges for secretarial lines proposed by Telephone Answering Services of California, Inc. (TASC), but decline to adopt certain other changes they propose.

While we continue to set basic residence and business rates residually for now--partly in recognition of the fact that Pacific's cost data, even if it is accurate, does not necessarily reflect the <u>most efficient</u> costs of service,--we do adopt increases which have the purpose of moving these rates, except for Lifeline rates, gradually toward costs. Thus, we increase recurring basic residence and business rates by approximately 1%, and service connection charges by the same approximate percentage (These rates are rounded to the nearest $0.05 and adjusted where necessary to meet the overall revenue requirement). We make no change in the usage rates for local service. We reject Pacific's 130 Call Allowance Plan and retain the present service offerings, but we expand the Lifeline options as Pacific proposes. The overall effect of these basic exchange changes is a revenue increase of $10.798 million which includes the effects of increasing FEX access rates by the same amounts as basic residence and business service rates.

Recognizing that a PBX line equipped with Direct Inward Dialing (DID) competes with Centrex, which is designed to provide a contribution over cost, this decision adopts an increase of 48.48% for measured rate trunk access and 33.53% for flat rate trunk access, contingent on Pacific developing a set of unambiguous design parameters describing when a designed circuit (PBX line equipped with DID) rather than a regular business line is required from the serving central office. These changes increase PBX revenues by $20.554 million which includes the effects of increasing FEX trunk rates by the same amount as PBX trunk rates.

We also authorize a number of changes in Centrex service including the unbundling of the primary station line charge, an increase in the Centrex trunking charge from $.85 to $1.25, the addition of new optional service features, and a simplification of charges for optional services. Together the adopted changes in Centrex service result in a revenue decrease of $0.912 million. At the same time, we authorize a separate trunk sensitive circuit termination rate element for DID which treats all blocks of 100 station numbers the same, rather than charging more for the first 200, and results in lower cost to the customer than present rates until the customer reaches about 600 station numbers. This design benefits telephone answering service (TAS) users, while slightly increasing the DID rate component for very large users. This change results in an overall revenue decrease of $1.870 million.

The decision does not change coin telephone rates, but does increase access rates and service connection charges for semi-public coin service to approach costs, and does increase the access and installation rates for coin operated public telephone (COPT) service by the same percentages as basic service. These new rates will increase revenues for semi-public service by $9.005 million, and revenues for COPT by $.019 million.

We leave the rate for nonpublished service at $.30 per month and adopt Pacific's proposal for a new service, Directory

Assistance Listing, which permits the customer to be unlisted in the telephone directory, but makes the customer's name, address, and telephone number available in the directory assistance data base. The adopted rate for this service is $.15 per month. Rates for Touchtone service remain unchanged for lack of any evidence to justify other action, but Pacific is directed to provide cost and revenue data about this service in the supplementary rate design proceedings. The charge for Verification Interrupt remains unchanged as do the rates for Remote Call Forwarding.

The rates for Message Toll Service (MTS) and related optional calling plans are modified by this decision to produce a revenue decrease of $68.166 million. The modifications include a reduction in the number of MTS rate bands and a slight reduction in usage rates for MTS "additional minutes of use." The optional calling plans are all retained in their present forms, but their revenues are affected by the changes in MTS usage rates. WATS and 800 Service will remain unchanged, but changes in other rates will produce a slight reduction, $0.527 million, in revenues from WATS.

Turning to ZUM, we adopt Pacific's proposal to expand ZUM on the periphery of the San Francisco-East Bay Extended Area, resulting in a revenue reduction of $6.252 million. We do not adopt the proposals to change the ZUM Zones 2 and 3 boundary definitions, but we adopt rate reductions for usage rates which are analogous to the usage rates we adopt for MTS. The result is a revenue reduction of $30.531 million. The proposal of TURN for a flat rate metropolitan plan and the elimination of ZUM and optional toll calling plans is rejected, as is General Telephone's request for ZUM expansion. However, we do authorize the parties to study the feasibility of General's ZUM expansion proposal.

This decision denies Pacific's request to restrict Foreign Exchange (FEX) service to present customers, adopts an FEX rate design disaggregated into an access component which mirrors recurring basic exchange rates and a separate FEX increment component set at the rate presently attributable to this increment. Nonrecurring charges for FEX are increased by 100%. We also authorize the parties to study meet-point bill and keep billing of FEX services and to present this Commission, after staff review and approval, with a proposal for its implementation. The revenue impact of these authorized nonrecurring FEX changes is an increase of $12.751 million.

We authorize the small Independent Telephone Companies (ITCs) to recover any revenue shortfall caused by the adopted rates and charges by a uniform increase capped at 100% in their basic exchange rates and FEX services, followed by a bill and keep surcharge on intraLATA services where necessary. We authorize General to recover any revenue shortfall by a bill and keep billing surcharge on intraLATA services. The net settlement effects for each ITC of the adopted rate design and the intraLATA SPF to SLU phase-down in compliance with ordering paragraph 15A of D.87-12-067, (which have been placed into a memorandum account as required by D.88-03-064), are shown in Appendix C. Appendix D sets forth the adopted 1986 customer and FEX service volumes for each ITC. Appendix E shows each ITC's adopted 1986 customer billing base and the effects on its billing base of the adopted toll and toll private line rates and the adopted ZUM rates. We deny the motion of customers of Citizens Utility Company that we find that notice of changes in rates of the ITCs occasioned by this Pacific rate design did not meet statutory requirements. We adopt the intraLATA High Cost Fund proposed by DRA and the ITCs.

Additionally, this decision revises Pacific's present billing surcharges to reflect the change in customer billing base due to the adopted rate design. The present billing surcharge is revised from -2.52% to -2.616% for intraLATA toll and toll-related services; from -2.989% to -2.916% for local exchange service; and from -11.407% to -11.552% for access service. Should we not order any additional revenue requirement changes before January 1, 1989, the surcharges applicable from that day forward shall be 2.176% for intraLATA toll and toll-related services, 1.446% for local exchange service, and -6.882% for access service. These authorized billing surcharges are set forth in Appendix A. The development of these revised billing surcharges is contained in Appendix F.

The following Table 1 is a summary of the changes in 1986 customer billings and revenues generated by the adopted rate design. The changes in revenues reflect the settlements factors resulting from the Phase 2 Results of Operations decision, D.87-12-067 as modified.

Table 1

Summary of Changes in 1986 Customer Billings And Revenues at Adopted Rates and Charges ($000)

	Item	PACIFIC BELL Change in Billings	PACIFIC BELL Change in Revenues
1.	PBX (Incl. FEX recurring)	$21,415	$20,554
2.	Remote Call Forwarding	0	0
3.	Centrex	(950)	(912)
4.	Direct Inward Dialing	(1,948)	(1,870)
5.	Directory access listing	(118)	(113)
6.	Foreign area serv. - nonrecurring	13,285	12,751
7.	Local usage - Lifeline	(376)	(361)
8.	MTS	(61,031)	(56,478)
9.	Call Bonus	(1,735)	(1,150)
10.	Operatory - Busy verify	0	0
11.	Optional calling plans	(11,314)	(10,538)
12.	Private Line (incl. exp. savings)	73,647	67,020
13.	Semi-public (incl exp. savings)	9,671	9,005
14.	WATS	(660)	(527)
15.	800	0	0
16.	ZUM	(32,474)	(30,531)
17.	ZUM Expansion - LCAR	(12,671)	(6,252)
18.	Implementation	(1,130)	(800)
19.	Decrease in Access Charges	(11,000)	(10,615)
20.	Subtotal, Lines 1 - 19	(17,389)	(10,817)
21.	COPT	20	19
22.	Service Connection	1,194	1,146
23.	Basic Exchange Svc. (incl recur. FEX)	10,056	9,652
24.	Subtotal (lines 21 - 23)	11,270	10,817
25.	TOTAL	(6,119)	0

(Negative Amount)

Finally, we address the quality of Pacific's private line service and find it to be in compliance with the requirements of General Order (GO) 152.

The Administrative Law Judge's (ALJ) Proposed Decision in this rate design phase was filed and mailed to the parties on May 20, 1988. Pursuant to Rule 77.3 of this Commission's Rules of Practice and Procedure (Title 20, California Administrative Code, Section 77.3) the following parties filed timely comments, and/or replies to the comments of other parties: Pacific, General Telephone, AT&T, Continental Telephone, the Smaller Independent Telephone Companies, Sprint, the Federal Executive Agencies, Carlos E. Benemann and David Kilmer, CBCHA/TCA, WBFAA, API, TASC, TURN, and Bay Area Teleport. Additionally, Pinnacles Telephone Company submitted late-filed comments after discovering a computational error. That filing was reasonable and is accepted. These comments, to the extent they focused on alleged factual, legal, or technical errors in the Proposed Decision, were carefully considered in arriving at this final decision.

II. Introduction

A. Procedural and Policy Considerations

1. Procedural History of this Matter

It is our purpose in the present decision to adopt a new rate design for Pacific Bell, but the scope of the revenues that should be included in this rate design is somewhat problematic.

On June 25, 1986 Pacific filed its final rate design testimony in the present matter. It purports to make no change in total annual revenues, except to redesign rates in a way which will allow the elimination of the 2.48% billing surcharge in effect at the time by incorporating the net revenues derived from that surcharge into rates. The rate design proposed by DRA proposes to spread the same surcharge, but also suggests alternatives should we wish to consider later surcharges. Additionally, both these rate designs attempt to comply with the Assigned Commissioner's Ruling issued on April 1, 1986 which is discussed below.

From our issuance of D.85-03-042 in March of 1985 to our issuance of D.87-12-067 as modified by D.88-02-046 in February, 1988 and D.88-03-064 in March, 1988 we have imposed a number of positive and negative surcharges on Pacific's rates to adjust for reductions we ordered in access revenues and for attrition or rate case adjustments. Since the time of Pacific's filing this intraLATA portion of Pacific's billing surcharge was increased to 4.13% effective January 1, 1987 (see Resolution T-11091 (December 22, 1986)), and was then decreased to 1.287% effective May 1, 1987 (see Resolution No. T-12007 (March 25, 1987)). It was slightly decreased again by D.87-04-024, effective June 7, 1987 and was again decreased to -0.193% effective January 1, 1988 as a result of D.87-12-067. Then, by Advice Letter 15356 filed in compliance with Ordering Paragraph 15A of D.87-12-067 as modified by D.88-02-046 and D.88-03-064, different surcharges were established for intraLATA toll and for intraLATA exchange services effective April 10, 1988. The latter remains at -0.193%, while the former is 0.276%. Subsequent to the mailing of the ALJ's proposed rate design decision we adopted yet another change in response to Advice Letter 15377A, filed in compliance with Ordering Paragraph 1a of D.88-01-064, dated February 2, 1988, modifying D.88-01-061, dated January 28, 1988. This change reduced the surcharge for intraLATA toll to -2.520% and for intraLATA exchange services to -2.989%. These latest surcharge revisions are reflected in Appendices A and F.

Now that we have the rate design proposals and comments of the various parties before us for this general rate case, two problems have become clear. The first is that we are necessarily confined to the 1986 estimated billing base, which means that any increases will be spread under the assumption of a lower volume than likely exists today, thereby magnifying the impact of rate increases on ratepayers. The second is that if various components of the surcharge are spread in rates today, a rate increase followed quickly by a rate decrease would likely result. The surcharge in place through 1986 plus the direct assignment of WATS closed end costs as of January 1, 1987, and the 1988 interLATA SPF to SLU phase-down which had been authorized prior to 1986 all require a rate increase. They are currently being offset by the revenue requirement reductions which were adopted subsequent to 1986. But since those reductions result from proceedings which assume a post-1986 billing base, the reductions could not be used to offset the revenue increases if those increases are spread in rates.

In Order Instituting Investigation (OII) In the Matter of Alternative Regulatory Frameworks for Local Exchange Carriers, issued November 25, 1987 we stated that Pacific should accumulate revenue requirement changes occurring subsequent to its general rate case Phase 2 decision (D.87-12-067, as modified) in a memorandum account. Further, we noted that "[t]he net effect of several upcoming revenue requirement changes...will probably be a reduction in total revenue requirement." We added, "[w]e see these supplementary rate design hearings as providing an opportunity to move rates downward for services currently priced above cost without necessarily having to adjust rates upward for basic services that are priced below cost."

Because of the unnecessary rate fluctuation which we now recognize as the likely outcome of spreading some, but not all, of the billing surcharges which have already been adopted, we believe it is preferable to address the appropriate spreading of all billing surcharges ordered for services other than access since D.85-03-042, along with the surcharges and other rate changes which will be addressed in the supplemental rate design hearings. To assure the most accurate rate design possible in disposing of these surcharges, we will direct Pacific and the other parties, including the ITCs, to file testimony using 1988 and 1989 projected billing base data for use in the supplementary rate design phase of the present proceeding. Until then we will keep in place the existing billing surcharge/surcredit.

The result of our adopting this position is that rather than considering how to spread about $118 million which includes the surcharge revenues plus revenue requirements which we have ordered to be adjusted or shifted among Pacific's service offerings, this decision will address only the spreading of revenue from the latter source, which comes to about $82 million.

2. <u>The Regulatory Context of the Rate Design</u>

It is our intent that this decision continue an evolution in rate design reflected in various Commission decisions since the AT&T divestiture which we cite above. More significantly, with this rate design we establish a baseline for moving ahead with any further changes which may be made in conjunction with our investigation into alternate regulatory frameworks in I.87-11-033. Before proceeding with the discussion of specific issues therefore, we briefly review some fundamental principles which are and will continue to be important considerations for this Commission.

For a variety of economic efficiency reasons, we are guided by the same desire voiced by most of the parties to this proceeding, to move rates over time toward economic costs. Among other benefits, moving toward economic pricing promises to improve efficiency in both the provision and consumption of telecommunications services. Economic pricing can help promote uses for which value exceeds the "true" cost of providing service. It can also discourage the allocation of utility resources toward uneconomic uses and prevent a misallocation of society's resources in facilities which unnecessarily duplicate those of the utility.

The long-run sustainability of large contribution flows from usage rates to support low basic exchange access rates is also a central concern--not only in this proceeding but in the regulatory framework OII as well. As we have previously noted, short-run competitive threats do not appear to be nearly as catastrophic as sometimes has been suggested. We have the time to plan an organized, deliberate course to implement "rationalized" rates based much more closely on economic costs. In this instance, the inertia and the caution of business users in making substantial investments in private networks weighs in the Commission's favor.

As a specific target of our continuing rate design policy we hope to minimize the potential for uneconomic bypass of the public telecommunications network. In D.85-06-115 we established an initial series of steps aimed particularly to achieve this end by ordering the interLATA SPF to SLU transition. In doing this we effectively cut in half the burden of non-traffic sensitive costs borne by interexchange carriers which pay access charges, shifting it to intraLATA services. In our recent decision on Pacific's revenue requirement, D.87-12-067, we indicated that the SPF to SLU methodology for allocating non-traffic sensitive costs would be applied to intraLATA toll service, thus reducing the costs of intraLATA usage as well. We intend to continue the clear signaling of our long-run direction, as manifested by our SPF to SLU decisions, D.85-06-115 and D.87-12-067, to forestall uneconomic bypass decisions.

Continuing market, technological and federal regulatory changes may very well accelerate the bypass threat in the future. This Commission must be prepared with a consistent and continuing long-term strategy for rate design so that it <u>can</u> phase in significant changes gradually and so that the process can be implemented in the most effective and least disruptive way possible should an accelerated threat materialize.

In large part, these adjustments to rates will lower the price of using the public network, while raising the price of obtaining access to the network to levels which more closely reflect the costs of service.

Our course toward economic pricing has been a moderate one and it is the intent of this decision to continue to balance efficiency benefits with the equally important goal of maintaining affordable basic service for all Californians. We must proceed cautiously because the evidence of marginal costs, which would greatly assist us in basing rates on economic costs, is incomplete. Given our commitment to economic usage pricing, we must guard against overreacting to the need for pricing adjustments by shifting too high a percentage of fixed costs to basic service rates. Such a tendency might result from the fact that basic residential and business service charges and rates are priced residually after other services have been priced to recover as much of the utility's fixed costs as feasible.

As the utility responds to more concrete evidence of the bypass options of large users and to competitive forces, we should resist the abuse of residual pricing to pursue economic efficiency objectives that are still in the formative stages of development. At this point the shifting of fixed costs from usage to basic exchange services is still fraught with many value judgments. The technological imperative is that we give greater weight to economic pricing. This acknowledgement of alternatives to the utility system does not require us to ignore other noneconomic policy objectives. In fact, we have no intention of abandoning those consumers who are most subject to monopoly power and who are most in need of the Commission's protection, nor do we believe that we must choose between efficiency and affordable service. The decision below reflects these principles.

B. The Source of Remaining Revenue Requirement Changes

1. Centrex Service Feature Changes

On May 13, 1987, we issued Resolution T-12023, effective that same date, which authorized Pacific to offer 25 new Centrex service features from certain central offices, pursuant to Pacific's Advice Letter 15243. Seven of these features were included in the rate design Pacific submitted in the present proceeding. Five of these seven, however, are set at higher rates than those proposed in this rate proceeding. The resolution found that the newly approved rates for these five services would produce an additional $58,932 over the annual revenues proposed by Pacific in its filing in this present proceeding. Therefore, the resolution directs that this rate effect be taken into account in the present decision. Our accounting for this revenue effect can only be prospective from the effective date of this decision.

2. **Private Line Revenue Requirement Reduction**

In D.87-08-048 issued August 26, 1987, we found Pacific's special access (private line and private line-like services) revenue requirement should be reduced, this time by $11 million. And again, we necessarily found that that reduction should be offset by an increase in nonaccess service rates, chief among which are basic local exchange services. Because D.87-08-048 was issued shortly before the expected date of this decision, we directed that comments on the appropriate rate design for these changes should be filed for consideration and disposition in the present proceeding and that implementation of these revenue requirement shifts should occur in the context of this proceeding in order to avoid the adverse effects of short-term billing changes. Therefore, in this decision we are ordering Pacific to shift $11 million in revenue from its special access rates on a prospective basis. The appropriate special access rate design after removing this $11 million and the impact of this shift on other telephone companies are discussed below.

3. **The Assigned Commissioner's Ruling**

The final action governing the extent of rate changes is the Assigned Commissioner's Ruling issued in this proceeding on April 1, 1986. The Ruling states at Ordering Paragraph 2:

> "Pacific's rate design proposal shall be heard by the Commission except that the rate shift presented shall not be greater than that recommended by PSD [Public Staff Division, now called Division of Ratepayer Advocates or DRA] in the compromise proposal filed in its motion

> of February 7, 1986, adjusted solely to account for changes caused by D.86-03-049, unless a hearing on a greater revenue shift is permitted by order or ruling after the Commission has more information as to long-range rate projections."

At the time this Ruling was issued Pacific had a proposal before this Commission which included a shift of over $400 million in revenue from intraLATA toll service to local exchange rates. The DRA proposal mentioned reduced rates for message toll service (MTS) and MTS-related service by $71 million to reflect its proposed intraLATA SPF to SLU transition. The subsequent proposal filed by Pacific increases residence basic service revenue by $71.3 million. We consider that some or all of the $11 million shift which we ordered in D.87-08-048 as well as this $71 million SPF to SLU change could be shifted to local basic exchange rates. Therefore, we are bound to keep any prospective increase in the total revenue requirements for local exchange rates within a maximum of about $82 million prospectively, and about $71 million for the test year.

C. Rate Design Objectives of Pacific and DRA

At the same time that Pacific has been experiencing an overall reduction in its revenue requirements, there have been pressures tending to push the revenue requirement for some end user services, notably basic exchange services, upward. This is due in part to the entry of competitors into the interstate long distance market following the divestiture of AT&T's monopoly of those services, and the impact of that competitive force on the rates Pacific is authorized to charge those competitors for such things as access to the local network. Thus, for example, in D.85-06-115 we authorized changes in the methods used to calculate Pacific's revenue objective for access services which resulted in reducing Pacific's access charges by about $140 million. We offset that reduction with a complementary billing surcharge on most of

Pacific's end user services--many of which are basic exchange services. Another pressure comes from the possibility of competition in the intraLATA MTS market which we will address in Phase III of I.87-11-033.

Based on an overall rate design meant to eliminate the 2.48% surcharge on nonaccess services in effect after our Phase I interim decision in this proceeding, D.86-03-049, which ordered a revenue decrease of $120.649 million, and to redesign some rates so as to redistribute revenue while remaining revenue neutral overall, and taking note of the rate pressures referred to above, Pacific proposes to deal with them by decreasing MTS rates and certain other service rates and offsetting these decreased revenues by increasing basic residence service rates, private line rates, and business rates. Pacific's rate design testimony emphasizes its belief in the necessity of our authorizing rate-setting principles which target basic residence service at subsidized rates and which assure that other rates are set to move toward costs. Pacific asks us to move away from a focus on average historical costs and toward a focus on economic costs, giving consideration to such issues as geographical cost differences, cost differences due to usage variations among types of customers, perceived value or demand balanced against the availability and prices of substitute services, and efficient network utilization.

DRA has proposed two rate designs, one based only on spreading the 2.48% surcharge in effect in 1986 as a result of the $120.649 million reduction in revenue requirement adopted in D.86-01-026, and another which assumes a total 1986 test year revenue requirement reduction of about $300 million based on DRA's recommendations in the Results of Operations phase of this proceeding.

In the first design DRA witness Shantz proposes reducing MTS revenue by $47.428 million, increasing business and residence basic exchange service rates by a uniform percentage amount to recover an additional $101.825 million, increasing rates for private line and private line-like services by about $67.5 million, and increasing service connection charges by about $7 million. (See p. 1 to attachment to Exhibit 351.)

His second rate design, filed subsequent to Pacific's June 25, 1986 rate design and based on a reduction in revenue requirement of about $300 million, proposes reducing MTS and MTS-related services by about $125 million, reducing basic exchange rates by nearly $88 million and retaining most of the other proposed rate revisions. (See Exhibit 352, p. DMS-3.)

DRA presents yet a third rate design in its opening brief. This design proposal addresses spreading about the same $300 million revenue reduction; however, it includes spreading an additional amount which recognizes the increase in the billing surcharge which became effective on January 1, 1987 to account for a reduction in the revenue requirement for interLATA access services. This third rate design proposes decreasing MTS rates by about $26.7 million, very slightly changing the previously proposed increase for private line and private line-like services (from $67.54 million to $68.165 million), leaving the increase in service connection charges the same, and continuing to decrease basic local service rates but by the much smaller amount of about $19 million. DRA advocates spreading this basic exchange rate decrease uniformly across all basic service rates.

D. Rate Design Objectives of Other Parties

In the principal decision in Pacific's previous general rate case we described our rate-setting process as follows:

> "Generally speaking, we set rates for a particular service based on one of three distinct models: (1) setting rates to recover the full costs of service, including an appropriate factor for return on invested capital; (2) setting rates to recover the full costs of service plus an additional contribution toward common costs or the costs of other services; and (3) setting rates

> residually to recover revenue requirement not achieved from other services. The first model of fully cost-based rates is our general standard. We apply the second model to optional, discretionary services where considerations of demand elasticity, value of service, and historical rate relationships justify setting rates above cost. The third model, residual pricing, is reserved for basic exchange services and related essential services which the Commission historically has sought to protect from the impact of drastic rate increases, in the interest of promoting the goal of universally affordable telephone service." (Pacific Tel. & Tel. Co. (1984), D.84-06-111, mimeo. at 142-143.)

The parties to this present rate design proceeding differ in their views of how costs should be measured, how we should determine which of the above models to apply to a particular rate, and how we should determine the appropriate amount of contribution to assign to rates for those optional or discretionary services which are set according to the second model.

Further, three parties, the California Bankers Clearing House Association and the Tele-Communications Association, herein jointly referred to as CBCHA/TCA, and sometimes called the Users Group, a group comprised of the United States Department of Defense, the General Services Administration, and all other Federal Executive Agencies, herein jointly referred to as FEA, and the Western Burglar and Fire Alarm Association (WBFAA) prefer that there be no rate design at all, and that we simply reflect the changes in Pacific's revenue requirements by adopting a uniform surcredit or surcharge to be applied to all services.

CBCHA/TCA argue that the Commission should wait to adopt a rate design "until the revenue requirement is more certain and the cost study support more accurate." However, they ask that in the event we do adopt a new rate design, that we reject Pacific's and adopt the one which they offer. The key feature of CBCHA/TCA's proposal is its elimination of most residual rate-setting and covering a far greater portion of costs through access rates, thereby reducing usage rates.

It is FEA's position that rates should be set for each particular service at least as high as the incremental cost for providing that service, and then any augmentation in the price/cost margin should be set on the basis of market conditions, with lower price/cost margins for services with a relatively elastic demand curve and higher price/cost margins for services with a relatively inelastic demand curve--with certain narrow exceptions where subsidies are maintained for "those customers who are truly in need." However, FEA maintains that Pacific could not set prices in this way because it has not produced incremental cost studies for each specific service category. FEA concludes that this constitutes a failure to comply with this Commission's prior decisions and the recommendations of Pacific's own pricing policy witness, Dr. Harris, and therefore requires that Pacific's rate proposals be rejected.

WBFAA finds Pacific's cost studies to be "uncertain," its revenue projections to be "unclear," and its view of the future to be "murky," and asserts that the result might be "unanticipated and undeserved revenues [for Pacific], and irreparable harm to the ratepayers." WBFAA therefore urges that the present surcharge remain in place or that all rates be adjusted by the amount of the surcharge. Though WBFAA does not address other revenue shifts, we assume that it prefers that any rate shift be spread across all services on the same percentage basis.

Further, Telephone Answering Services of California, Inc. (TASC) also argues that Pacific's cost studies are unreliable and supports this Commission's rejection of the Pacific cost studies and adoption of the motion filed in February, 1986 by DRA and the subject of the Assigned Commissioner's Ruling mentioned above, which proposed setting the then-current billing surcharge to zero, reducing MTS rates by $71 million to reflect DRA's proposed intraLATA SPF to SLU transition, realigning certain ZUM rates in the San Francisco Bay area, and applying the remaining revenue requirement (about $201 million) as a uniform increase across all service categories except Coin, Lifeline, and Centrex.

We agree with CBCHA/TCA, FEA, WBFAA, and TASC that problems with cost studies as well as other issues these parties raise have made our rate design efforts more difficult; however, Pacific and its ratepayers have a right to the rate design they seek rather than continued across-the-board additions and subtractions to rates which may deserve different treatment or may deserve to be supplanted with new or different rate elements. The issues these parties have raised are not insurmountable. There is always some imprecision in this process. We do not believe it is so great in this record that we must forego a review of Pacific's rate design proposals altogether.

III. Basic Residential and Business Service

A. Residential and Business Rates

1. Pacific's Basic Residence Access and Usage Proposal

Pacific proposes a new billing disaggregation for basic residence exchange service which distinguishes between that portion of exchange service which is common to all customers and not usage sensitive, which it designates as access, and that portion of exchange service which is usage sensitive. Pacific proposes setting the residence access line rate at $4.45 per month for all its residence offerings. Its cost witness, Mr. Scholl, claims the average historical cost for access is $25 per month.

Pacific then proposes three usage offerings, also targeted at rates requiring subsidy. The plans include a continuation of the present "Unlimited Calling Plan" within the local (ZUM Zone 1) area, and the "Measured Call Plan" designed for those whose local usage needs are minimal, and the establishment of a new "Call Allowance Plan."

The Unlimited Calling Plan would be set at a flat rate of $5.55, so that with the addition of the access charge the total cost for unlimited usage would become $10 rather than the $8.25 presently authorized.

The Call Allowance Plan would be set at $3.80 per month in addition to the access charge and would permit 130 untimed local messages per month with each local message thereafter being charged at $.08 per message, up to a maximum of $1.75. Thus, this plan would also be capped at $10 per month, but those customers accumulating no more than 130 local messages would pay only $8.25 per month, the same as the presently authorized unlimited calling rate. Pacific states that about 65% of today's residence customers make fewer than 130 local calls per month and that this plan would, therefore, meet their needs. Pacific's rate design witness Sullivan testified that this plan would keep most customers' rates at their present level and would cost Pacific $8- to $10 million to implement. Further, according to Exhibit 345 Pacific proposes to notify its customers that their service will automatically be converted to the 130 Call Allowance Plan unless they request a different service.

The Measured Call Plan would not change except for the names of the rate elements. It is set at the access rate plus $.04 for the first minute of usage and $.01 for each additional minute. Additionally, customers of this service would receive a $3.00 monthly allowance against their local and ZUM Zone 2 usage. That comes to 37 1/2 5-minute local calls per month. Sullivan asserts that about 20% of Pacific's present residential customers could subscribe to this plan, continue their present calling patterns, and pay no more than the $4.45 access charge each month.

As for Universal Lifeline Telephone Service (ULTS or Lifeline) Pacific proposes to leave the rate for measured service at $1.48, which is computed as 50% of the measured access rate less $.75 Customer Premises Equipment (CPE) rental credit. Lifeline measured rate service continues to provide a call allowance of 60 local calls (as contrasted with $3.00 worth of measured local usage for non-Lifeline measured service) and proposes reducing the additional charge to $.08 for all calls rather than the present rates of $.10 for 61 to 70 calls and $.15 for all calls after the 70th.

Sullivan testified that Pacific wishes to make Lifeline service more valuable to those who qualify for it by also offering a discounted 130 Call Allowance Plan and the Unlimited Calling Plan so that economically disadvantaged customers can have the same options as other customers. Initially Pacific proposed a $2.00 monthly discount for the 130 call plan and the unlimited call plan for Lifeline customers; however, with the intervening passage of AB 3288 on September 23, 1986 amending Public Utilities Codes § 739.2, Pacific asks that these services be offered to Lifeline customers on the same 50% tariff rate basis as basic measured service. Pacific requests that it be permitted to recover the discounted Lifeline amounts for these optional services from the Universal Telephone Service Fund.

Pacific also proposes that the charge for installation or service on individual business lines be raised from $70 to $100 for the first line, but stay at $70 for each additional line. Further, it proposes to give customers 90 days from implementation of these new rates to choose a new service (or, presumably, to choose not to be transferred to the 130 Call Allowance Plan) without being subject to a charge for the change.

2. Criticism and Alternatives to Pacific's Residence Proposal

a. CBCHA/TCA

The CBCHA/TCA proposal agrees with the concept of separate charges for residential access and usage; however, as their witness Dr. Selwyn testified, they believe that Pacific's proposal detrimentally perpetuates an unnecessarily high annual subsidy to basic exchange access lines of about $2 billion (the amount by which costs Pacific assigns to local access exceed revenues), and consequently, excessive rates for other services such as intraLATA usage, intrastate interLATA access, and interstate access. Selwyn testified that this policy results in suppressing demand and giving customers incentive to bypass. He argues that the goal of universal service can be met at a far lower cost through a targeted subsidy program for Lifeline customers while moving access line rates for all other residential exchange access toward cost.

Citing a study performed by the staff of the Florida Public Service Commission, Selwyn claims that residential demand for local service is highly price inelastic, and concludes that the Lifeline mechanism already provided for in California is all we need to assure the universal availability of basic telephone service. He therefore proposes to reduce, and eventually eliminate the subsidy to non-Lifeline residential ratepayers.

As a first step CBCHA/TCA proposes a plan with three basic options for residential customers. All customers would pay $5.00 monthly for access. Under the first service option the customer would pay an additional $2.10 which would include a $3.00 usage allowance. Additional calls would be $.04 for the first minute and $.01 for each additional minute. Thus, this option would cost $7.10 for up to $3.00 of usage. The second option, untimed measured service would be priced at the access rate plus $4.25 per month for up to 130 untimed calls. Additional calls would be priced at a flat $.07, with no usage cap. Thus this option would cost $9.25 for up to 130 untimed calls per month. The third option is for flat rate service at $9.00 per month plus the $5.00 access charge, or a total of $14.00 per month. Each service would be discounted by 50% plus the $.75 equipment credit for

Lifeline customers. Selwyn's minimal reliance on local measured calls arises from his concern that, at an average cost increment of $.08 more than a local flat rate call, measured calls are of dubious value.

Selwyn asserts that the combination of his exchange rate proposal and his ZUM proposal discussed below will stimulate calling and create a better balance between rates and costs for both access and usage.

Pacific responds to the proposal of CBCHA/TCA by noting that the existing subsidy requirement "can and should be substantially reduced by eliminating, over a reasonable period of time, the subsidies which many business services currently enjoy." Pacific claims that its proposals will more effectively accomplish that goal and will also appropriately reflect the variances in the magnitude of revenue-to-cost shortfalls among services.

DRA urges this Commission to reject Selwyn's proposal as an unjustified departure from our traditional policy of setting residential rates on a residual basis. It also claims that Selwyn's proposal would only spread the benefit of reduced revenue requirement to business customers when both business and residential customers should share the benefit.

b. FEA

The FEA assert that traditional rate structure must be changed by reducing price/cost margins for those services which are sensitive to price and subject to competition. FEA claim that this should be accomplished by assuring that any subsidy to local exchange customers goes only to those who are truly in need. Thus, FEA propose moving pricing for services with relatively inelastic demands, presumably including basic residential service to those who are not truly needy, to incremental cost, plus whatever further amount basic demand considerations will permit. Recognizing that customers with relatively inelastic demands for particular services will resent an immediate doubling or tripling of prices, FEA suggest that the change be made by degree and not all at once.

FEA argue that this measure is necessary to circumvent bypass by large users, including FEA which will occur because alternative suppliers and new technologies [are] driving down cost. FEA claim that loss of business from these large users would result in stranded investment and increase the revenue requirement on basic exchange service even further. FEA add that offering volume discounts will also encourage these high volume business and government customers not to bypass.

Further, FEA assert that incremental or marginal cost information is crucial to determining appropriate rates, and point out that we ordered Pacific to submit such information in this proceeding. FEA claim that Pacific should have provided incremental cost data by service category, and that the data provided is insufficient since it only relates to three broad categories of plant: local loop, interoffice facilities and switching equipment. FEA add that since both their witness, Dr. Baughcum, and Pacific's expert witness on pricing policy, Dr. Harris, testified that incremental cost is the proper cost methodology this Commission should require Pacific to submit incremental cost data by service category in its next rate case.

As for the present, FEA argue that we should reject Pacific's rate design proposals because they are based on estimates of embedded costs which FEA's Baughcum describes as having little to do with economic or market value. He cites with approval the testimony of Harris that in a competitive environment, setting prices on the basis of historic costs will cause substantial allocative and technical inefficiencies. (Ex. 316, pp. 30-31.)

c. <u>TURN</u>

TURN's witness, Sylvia M. Siegel, argues that Pacific's residential customers are entitled to a share of the revenue requirement reduction by way of reduced rates for basic service. She proposes a "Residential Rate Simplification Plan" under which local measured service (LMS) would be eliminated altogether in favor of universal flat rate service and flat rate lifeline service. Siegel proposes offering this flat rate service at $6.00 per month, with lifeline set at $2.25 (one half the normal rate less $.75 to offset telephone equipment costs). Further, she testified that based on Pacific's workpaper volumes she estimates that a revenue neutral universal flat rate would be $7.73 per month and that her proposal would reduce annual revenues by roughly $128 million.

TURN urges this Commission to reject Pacific's 130 Call Allowance Plan for being priced specifically to make flat rate service uneconomical for each and every residence customer, despite any considerations of costs and revenues. TURN points out that Pacific's costs of serving customers who switch from flat rate to this measured service would rise by the cost of measuring the calls. TURN states that if 58%, or 3.7 million, of Pacific's residential customers switch to the new 130-call plan, as Pacific's workpapers suggest, and if Scholl's estimate of $.004 per message for measuring is accurate, and if it is assumed that each customer averages 100 calls per month (a figure which appears low to TURN), then the additional annual cost for measurement would be $17.76 million. TURN concludes that the 130-call plan is a loss-leader for Pacific under which every customer will pay less than the flat rate, while every customer will actually create higher costs of service than do flat rate customers.

TURN also opposes Pacific's efforts to separate basic service into access and usage components, reminding this Commission that we rejected a similar proposal in our last Pacific rate design decision, D.84-06-111, which, among other things, found that the proposed distinction was more didactic than practical. TURN asserts that the proposal is purely a marketing tool that attempts to redefine existing services in ways that would slant Commission and public attitudes toward the Utility's repricing schemes. TURN alleges that nothing has changed since we made the observation in D.84-06-111, that "PacBell does not actually propose unbundled rates but merely uses the access/usage dichotomy to explain the relationship between its proposed rates and its calculated costs." (D.84-06-111 at 275). Further, TURN alleges that the policy is illegally discriminatory in that a residential flat rate customer would pay $4.45 for access alone, while an LMS customer would receive access plus $3 worth of free usage for the same amount.

CBCHA/TCA expresses agreement with TURN that Pacific's measurement of local calls improperly inflates the cost of providing residential exchange service, but does not agree with TURN's rate proposal, since it contends that even Pacific's proposal prices local access too far below cost.

Pacific is also critical of TURN's proposals, claiming that it is necessary to narrow subsidy targets to residence access and a reasonable amount of usage and service connection, in this period of diminishing sources of subsidy. Pacific argues that TURN's proposal would decrease rates for customers who generate the greatest costs, the residence flat rate customers, while increasing rates for the measured service customers who generate the least costs, and adds that the 130 Call Allowance Plan together with its other proposed local offerings more appropriately provide the Commission with the means to direct subsidy flows to achieve its policy objectives in the most efficient manner.

d. Brylawski

Dr. Robert E. Brylawski testified on his own behalf about Pacific's residential basic exchange service proposal. His testimony agrees with that of Siegel that Pacific has not provided cost support to justify increasing flat rate service rates as proposed while leaving measured service rates unchanged. He further asserts that Pacific's cost studies suggest that current relative prices of the two services are reasonably in balance from a revenue/cost standpoint.

Brylawski bases his testimony on a comparison of Scholl's testimony and related workpapers, Exhibit 293, a customer usage study done by Pacific, and portions of Sullivan's testimony and workpapers which, he states, together lead him to conclude that there are several errors in Scholl's data input which distort the revenue and cost figures Pacific adopts for residential basic exchange service.

As shown in Table 2 to Exhibit 379, Brylawski's calculations conclude that the revenue shortfall is fairly similar for either flat or measured service based on either Scholl's data or Exhibit 293, but that the revenue to cost ratio revealed that in both instances flat rate service contributes proportionally more to meet its costs than measured service. Based on this finding and his contention that revenue shortfall is a more reasonable basis for comparing alternative services in the same service class, he recommends preserving the present balance by spreading the new revenue requirement for residential basic exchange service between flat and measured services by raising or lowering the rates for both services by essentially equal dollar amounts.

Brylawski is opposed to the 130 Call Allowance Plan, claiming that support data for both costs and revenues are woefully inadequate and cautioning that the data available suggest that it is designed primarily to draw customers away from flat rate service and raise a distinct possibility that this plan may actually produce incremental costs in excess of incremental revenue. He also objects to the plan on policy grounds, claiming that it will further complicate the customer's choice of basic service and require them to be dependent on Pacific's representatives for advice. Brylawski points out that flat rate service would become superfluous under Pacific's proposal and expresses the suspicion that it is designed to drive flat rate service out of existence.

Brylawski asserts that there is no discussion of the incremental costs of this plan when compared to the status quo, but claims that there will at least be a cost for service regrades for the 4.2 million customers who will switch to the service. Suggesting the "modest" assumption of $30 per regrade, he calculates this nonrecurring cost to be $125 million. Brylawski also claims there will be a new cost of measuring and billing for local calls that are currently unmeasured under flat rate. He estimates this as ranging between $2.5 and $7.5 million annually, depending on the call volume estimate used and the measuring cost per call used, and points out that adding this additional cost to the incremental revenue of $4.5 million which Pacific projects will result in something between a $2 million increment and a $3 million loss.

e. DRA

DRA's Exhibit 329 critiques Pacific's various cost studies. It agrees that Pacific's methodology for establishing the cost of service connection for residence and business services is sound and produces acceptable results, but expresses skepticism of the accuracy of Pacific's bottoms-up studies of subscriber access lines and local usage.

DRA agrees with Pacific's conclusion that costs of subscriber access are likely to exceed revenue from present rates, but does not accept Pacific's estimates because they are not based on a true bottoms-up cost study. Specifically, DRA criticizes the major component of the access cost study, the local access line loop study, for not using a larger sample size. DRA argues that Pacific's precision level of plus or minus 13% for residence loop length and plus or minus 16% for business loop length at a confidence probability of 95% is inadequate and that the precision level should be plus or minus 5%. DRA also criticizes as unscientific some of the assumptions Pacific made about various quantities of outside plant not included in the loop study which result in more than doubling the total loop length. DRA also objects to Pacific's use of booked investments for outside plant to distribute investment dollars to the loop footage, arguing that this is inappropriate to a true bottoms-up study.

DRA addresses the reasonableness of the methodology of Pacific's bottoms-up local usage study, finding the methodology Pacific uses to determine costs of two of the three equipment categories to be appropriate, but the third to be inconsistent. The first two give embedded cost output. The third provides incremental costs, to which Pacific has added an "embedding factor." DRA points out that this inconsistency "casts doubt on the likelihood that the switching cost component represents an average embedded bottoms-up cost." (Exhibit 329, 10-4.) Further, DRA points out that since the usage costs are not current, but embedded, they are of very limited use in evaluating bypass potential or other competitive pressures or in analyzing pricing proposals in the present environment.

With these reservations in mind, DRA has relied little on Pacific's cost studies and has instead emphasized the importance of making rate design changes which address its policy goals by making rate changes which protect basic service rates. DRA states that its primary goals are to eliminate the billing surcharge and decrease MTS rates. DRA witness Shantz suggests that a first priority for accomplishing that is an increase in rates and charges for private line and private line-like services and possibly a slight increase in basic local residence and business services rates.

DRA proposes increasing the rates for service connection charges, but slightly decreasing basic exchange service rates. In his pre-filed testimony of July 10, 1986, (Exhibit 351), Shantz explains DRA's rationale for increasing service connection charges. He states that the present service connection charges were established in mid-1984 and that "DRA does not believe that the charges for these labor intensive activities should remain unchanged for as long as five years." Nonetheless, DRA does not agree with the imposition of a large increase in this rate. Rather, this initial testimony of Shantz proposes a uniform percentage increase of about 5% for each service which can be characterized as a form of access lines. This, he asserts, will reflect the labor intensive nature of these services while excluding increases for services which were the subject of our investigation into Pacific's marketing practices such as Touchtone and optional calling plans.

DRA opposes Pacific's unbundling of residence rates into access and usage components, stating that it will lead to customer confusion and makes no sense when discussing a flat rate service. DRA also opposes the 130 Call Allowance Plan and the automatic conversion to this plan which Pacific proposes, arguing that the similarity between this and the proposed flat rate service will lead to customer confusion and could mislead customers into believing that the 130-call plan is the same as flat rate service. DRA therefore advocates leaving the residential service choices as-is. Further, DRA points out that this Commission has traditionally set residential rates on a residual basis, and concludes that there is no justification for abandoning that policy as some of the parties have suggested.

Although DRA initially opposed Pacific's proposed flat rate lifeline offering, it now contends that the proposal is supported by the January, 1987 amendment to Public Utilities Code § 739.2.

CBCHA/TCA criticize DRA's residual pricing argument as simply a characterization of past Commission practice which has no place in a post-divestiture environment where competitive and potentially competitive services ought to be priced to reflect economic costs of providing them except in those limited areas where subsidy is required to ensure universal service. CBCHA/TCA adds that absent some valid public policy rationale the subsidy to residential basic exchange service which DRA advocates is unreasonable and discriminatory in violation of Public Utilities Code §§ 451 and 453.

FEA criticize DRA's proposal because of the significant risk of stranded investment and ultimately higher basic exchange rates which arise from not following marginal cost-based or market-based pricing policies.

Pacific also criticizes DRA's proposal for disregarding the competitive threats to the services which help subsidize basic exchange service in order to achieve a minimal reduction in basic exchange rates (e.g. DRA's proposed reduction of $.15 in the monthly rate for Individual Line Measured Rate Residence Service with a $3.00 usage allowance and its $.05 proposed reduction for Individual Line Measured Rate Business Service). Furthermore, Pacific defends against DRA's criticism of its local usage cost study and its access line loop study precision factor pointing to DRA witness statements which it claims support Pacific's conclusions.

3. Discussion of Residence Rate Proposals

The importance of taking account of economic costs of service and setting rates that promote efficient use of the network will be growing as our economy becomes increasingly dependent on communications networks for transaction and information services. Large applications in particular may be greatly affected by uneconomic usage rate design, and such rate design will probably aggravate other tendencies toward private networks. At the same time that we recognize this future scenario we also recognize the need to provide rate subsidies for those who truly need them through the Lifeline program. Outside this focus, however, it is our intent that basic exchange rates should gradually but continually move toward a closer relationship with efficient economic costs of service.

This is different from the abandonment of residual pricing of basic residence services as proposed by CBCHA/TCA or FEA with only a targeted subsidy for Lifeline customers. Both base their argument for this policy change, as at least in part, on the bypass threat. We recognize that bypass is a problem facing Pacific; however, we believe that the presently authorized interLATA SPF to SLU phase-down, along with the intraLATA SPF to SLU phase-down which we authorized in D.87-12-067 will provide a sufficient signal of our continued intent to limit incentives for uneconomic bypass without the need for the sort of dramatic shifts in basic rates they advocate.

As we have pointed out before in proceedings addressing this question of how to deal with the costs of the local network, the great bulk of the nontraffic sensitive (NTS) costs at issue here are capital-related costs such as earnings on capital investment, income taxes on those earnings, depreciation charges, and property taxes. The magnitude of these capital costs is attributable to the method of accounting for subscriber plant costs over the years which was designed to keep the costs of becoming a subscriber to telephone service low in keeping with the national (and Bell system) telecommunications policy goal of universal telephone service. The costs of these local facilities were not charged to the local subscribers whom they were built to serve. Often the facilities were built to meet anticipated future need so there were no subscribers to charge. The ubiquitous nature of the resulting telephone network benefits all users. The logic of these accounting practices and the shared benefits that resulted from them seem to this Commission to mandate that the costs of that network should be shared and not now thrust solely upon the shoulders of the local users. At the same time, however, in response to the emergence of technological alternatives to the local network, we give greater recognition to the economic pricing of usage. We believe that the transition from SPF to SLU cost allocation accomplishes these goals.

Further, we expect basic exchange rates in the long-run to approach the most efficient costs of service. We explicitly make no endorsement that, even assuming their accuracy, the costs currently reflected by Pacific as the cost of basic access lines, for example, are those most efficient costs. Observers should not mistake the willingness and even the desire to accommodate increases in basic exchange access rates as any relief from this Commission's will to apply continuing regulatory pressure on corresponding costs.

Indeed, one of the Commission's challenges as it considers changes in regulatory mechanisms in I.87-11-033 will be to find more effective ways to keep pressure on exchange carriers to minimize the cost of basic exchange access lines. Basic exchange access is perhaps the service least subject to competitive pressures for cost reduction and most susceptible to the "goldplating" and lack of managerial attention popularly and frequently cited as one of the primary rationales for reexamining the effectiveness of rate of return regulation.

Considering the questionable reliability of the available cost information the fairest means of instituting a rate increase for local exchange services is to adopt an increase spread across all recurring local service rates as uniformly as possible, as DRA suggests. For this reason we find no merit in TURN's proposal to simply reduce flat rate service rates to $6.00 per month. There is no reason to exempt any service, including the measured call plan, from this spread. We will not adjust rates for message units in this process. As Pacific's rate design indicates, these rates should remain at their present levels.

Pacific proposes increasing its service connection charge for installation of an initial business line from $70 to $100. We agree with DRA that service connection charges should be moderately increased to take increasing labor costs into account. However, there is no more basis in the record for authorizing an inconsistently large increase in a charge which impacts the residential customer's ability to establish basic service, than there is for authorizing a large increase which impacts that customer's ability to maintain basic service. Therefore, we will adopt the same uniform percentage increase for this service that we adopt for other residence rates.

Turning to the specific service categories of Pacific's residence rate design proposal, we find the pricing structure of Pacific's proposed 130 Call Allowance Plan troubling. As DRA, TURN, and Brylawski point out, the Plan would make the proposed flat rate service uneconomical and therefore essentially eliminate the flat rate service option. The 130 Call Allowance Plan proposal would simply confuse ratepayers and obscure the distinct difference between flat rate plans and measured call plans which exists today. Flat rate service is less costly to administer than measured rate service. The record demonstrates no basis for eliminating it. Flat rate service should continue to be an option. Therefore, we reject Pacific's 130 Call Allowance Plan. Obviously, Pacific's claimed implementation expense of $9.394 million for this plan is also rejected.

We are likewise not persuaded by TURN's argument that the present measured call plan should be eliminated. Pacific shall continue to offer its two present basic services to residential customers--individual line measured rate service with a usage allowance presently set at $3.00, and individual line flat rate service.

As for Pacific's proposal to create two separate rate elements for residence service, access and usage, we find such a step adds terminology which implies rate policies which are inconsistent with the use of residual pricing of residential basic rates which we follow in this decision, and which are also inconsistent with flat rate pricing. Therefore, we will not adopt the proposed separate rate elements for residence service at this time.

In our efforts to promote efficient use of the local telephone system, we have authorized tariffs which charge separately for access and usage and are known as "measured rates." However, as noted above, Pacific's proposal to charge each subscriber an access fee plus an additional usage fee, regardless of whether the usage rate is flat or measured, is not acceptable.

The concept of measured rates intrigues industry pundits, since such pricing might give a more accurate signal of the cost of service to the telephone customer. Ideally, calls should be priced at no more than marginal cost so that incremental usage will not be overpriced to the extent that uneconomic bypass occurs. Given rates that reflect the cost of service, the consumer presumably will tailor his or her demand in such a way that increases in the capacity of the phone system will be required only when consumer demand justifies additional investment by the phone company.

So far as we know, however, the variation in customer demand may make it infeasible to tailor measured rate pricing periods to give consumers the appropriate signals which will assure such efficient usage. If that is the case, the concept propounded by TURN in its proposal for a metropolitan flat rate, if priced properly, may have substantial merit. On the other hand, it may be that Pacific's customers do exhibit a pattern of demand that can be mirrored by appropriate pricing periods. While Pacific has presented some evidence of incremental costs, the present record does not give us sufficient information to either ascertain the marginal cost of basic service with a high level of confidence or to determine whether our goal of promoting economic efficiency would be realized and not frustrated by the TURN proposal. Without such information we are unwilling to depart very far from either the present rate design or the present relationship among rates for local recurring services.

We believe, however, that the possibility of improving economic efficiency in the provision of local service warrants further examination of Pacific's customer and cost data to determine whether measured rates for such service actually promote or hinder such economic efficiency. Therefore, we will direct Pacific to introduce further evidence of the incremental costs of basic exchange service in the supplemental rate design proceeding. In order to explore the implications of TURN's alternative proposal, which extends to ZUM zones, we will also direct Pacific to present distinct evidence of incremental costs of calls within its ZUM areas as well. The evidence may persuade us to amend the terms and conditions of service priced at measured rates in our supplemental rate design proceeding. As for Scholl's recommendations about the level of detail this Commission should require in Pacific's future cost studies, we agree with the comments of DRA that such determination should be made on a case-by-case basis.

Turning to Lifeline, we see that the program must be "filled out" to provide completely for the protection of ratepayers with limited means. We agree with Pacific's conclusion that Lifeline would better serve the varying needs of those who qualify by offering the same plan options that are offered to other customers. In fact, with the implementation of AB 3288, the flat rate Lifeline option with unlimited local calls has begun. We will continue to authorize it at one-half the adopted flat rate less $.75 for telephone set rental and less $.25 for inside wire maintenance. We will also authorize a continued Lifeline measured access rate at 50% of the regular measured rate less the inside wire and rental amounts, and we will adopt Pacific's unopposed proposal to reduce the charge for additional calls after the 60-call allowance to $.08. We will also continue to authorize Pacific to recover the amount of discount it provides to Lifeline customers for these services from the Universal Telephone Service Fund. Today's economic climate suggests that further expansion or refinement of the scope of this program may be required as Lifeline takes on an even more important role than it bears today.

4. Pacific's Business Rate Proposal

Pacific proposes increasing the charge for the initial minute of business usage from $.04 to $.043, and measured line business access rates from the present $8.25 to $10.75. This access rate increase is just over 30%. It proposes increasing the rest of its business line access rates by over 48%. Citing the additional cost of providing trunks (also called Private Branch Exchange or PBX trunks), and Pacific's belief that customers will use the network more efficiently and avoid ordering designed circuits when they are not necessary if there is a price differential between regular business lines and trunks, Sullivan initially also proposed a new separate measured trunk rate at $16.00, a 93.93% increase, and an increase for the flat trunk rate from $25.65 to $38.00. The measured trunk rate is not presently differentiated from the business line rate of $8.25. Further, as with residence service, Pacific's proposed tariffs would raise the charge for installation or service on the first business line from $70 to $100, and leave the charge for each additional line at $70. It proposes charging even more for the installation of trunks, raising the charge from $70 to $175.

5. Other Parties' Positions On Business Rates

CBCHA/TCA do not comment on Pacific's proposal to increase measured line business rates, except insofar as they propose extending ZUM calling to distances up to 30 miles as the first step toward establishment of metropolitan-wide "community-of-interest-wide flat rate local calling." The proposal encompasses consolidation of ZUM Zones 2 and 3 and creation of a new Zone 3 to cover distances between 17 and 30 miles. It also includes day rates set at $.13 for the first minute and $.07 for each additional minute for this new Zone 3 rather than Pacific's proposed toll rates for that distance of $.25 and $.16. As we explain in our discussion of ZUM, below, we reject this ZUM rate consolidation plan.

As we have stated above, CBCHA/TCA also generally support cost based local calling rates, and Selwyn expresses a preference for flat rate local service, asserting that measured service unnecessarily increases local costs.

CBCHA/TCA do not approve of Pacific's proposals for increases in rates for trunk lines. They argue that the fact that PBX trunks have to be "designed" should not determine the pricing policy since many users of trunks select them not because of their design features, but because of customer distance from the servicing central office, the gauge of the wire Pacific chooses to use for the access lines, the number of splices or connection points, or the routing of the cable to the central office. They claim that each of these things can affect the quality of a normal business line in such a way that the customer must use trunk lines instead. CBCHA/TCA also argue that trunks are less costly and more profitable than business lines in that costs of billing and collections may be lower on a per-line basis since they are normally utilized by customers who require many lines. They also claim that the rate of call completion is higher for PBX trunks than for regular business lines. Based on this analysis CBCHA/TCA recommend that Pacific raise its PBX trunk rate from $8.25 per month to $10.75 per month, the same amount proposed for the regular business lines.

DRA recommends rejecting both Pacific's measured PBX trunk rate and its flat PBX trunk rate. DRA argues that the measured rate discriminates against customers and appears to be set to "better position the price of Centrex service to the price of PBX trunk service." Like Selwyn, DRA also argues that there are no unambiguous criteria which a customer can use to determine whether it needs designed PBX trunks rather than nondesigned business lines. Citing D.93367 at 6 CPUC 2d 441, DRA claims that this fact led the Commission to establish identical rates for measured business service and measured trunk service in the first place. Both DRA and CBCHA/TCA point out that this ambiguity leaves Pacific with too much discretion and could result in abusive marketing practices. DRA again argues that the objective of this rate design proceeding "should be to eliminate Pacific's surcharge, and not to reflect an increase in the revenue requirement." With this in mind, DRA suggests that a 50% increase for any BEAL (Basic Exchange Access Line) service should be the maximum, but it recommends a uniform percentage decrease for all business BEAL service based on the adopted revenue requirement decrease.

As with residential service, DRA agrees that service connection charges should be increased, but objects to Pacific's proposal and instead asks us to adopt the same percentage increase it advocates for residential service connection charges.

6. Pacific's Rebuttal and Alternative PBX Proposal

Pacific's Sullivan responds to criticism of its PBX trunk pricing proposal by asserting that Pacific's primary reason for proposing higher rates for trunks than for business lines is that trunks cost more to provide and they are more valuable to the customer because they support greater usage. Pacific also asserts that PBX trunk line service is not an economical alternative to Centrex service, but that in California Centrex rates are set high enough so that PBX trunk line service is used to bypass Centrex. This, contends Pacific, is an example of the sort of uneconomic bypass this Commission has repeatedly stated it wishes to prevent.

Further, in his rebuttal testimony Sullivan makes an alternative proposal for Pacific's PBX trunk pricing based on the opposition of so many parties to its initial proposal. The alternative is to increase the PBX measured trunk line rate by $4.00 per month to $12.25 rather than increasing them to $16.00. Sullivan states that this will accomplish the same 12% increase in cost coverage which Pacific's proposed individual business line rate increase will accomplish. He goes on to claim that this rate would result in a $19 million net revenue shortfall which could be recovered through increasing the business local usage rate from $.04 to $.047 rather than to the originally proposed $.043. Further, he claims that while Centrex customers pay rates that recover its costs, PBX customers presently pay Pacific less than half of the cost of their trunks. Pacific argues that if this anomaly in pricing is not corrected, residential ratepayers will bear the burden of the lost Centrex revenues while underpriced PBX trunk service will continue to absorb large quantities of scarce subsidy.

7. Discussion of Business Rate Issues

We have already stated that the evidence in this record does not warrant total abandonment of our present policy and an immediate shift to cost-based rates for all local services except for a narrowly defined subsidy as FEA and CBCHA/TCA advocate. This holds true for basic business service as well as residence service. In order to continue the present policy it is appropriate to apply the same residual pricing model to basic business service that we apply to basic residence service. Likewise, we are unconvinced of the wisdom of Selwyn's related recommendation of significant reductions in minutes of use rates, offset by higher access rates for all local service. Therefore, we will follow the general recommendation of DRA and adopt the same percentage increase for business services that we have adopted for the residence services. Furthermore, Pacific's rationale for increasing the initial minute rate for business usage goes unexplained. We will authorize no increase in local usage rates.

Contrary to DRA's claim, our decision to keep trunk rates and individual business line rates the same in D.93367 was the result of monitoring difficulties which Pacific would have had at a time prior to the deregulation of customer premises equipment. The rationale does not apply today. Furthermore, there is nothing inappropriate in Pacific attempting to reconcile PBX trunk and Centrex pricing, so long as both remain at justifiable levels. We agree with Pacific that it is reasonable for PBX trunk rates to be raised to a level closer to costs. Unlike basic residence and business services, a PBX line equipped with Direct Inward Dialing (DID) is in competition with another service, Centrex, and Centrex is designed to provide a contribution over costs as defined by Pacific in Exhibit 260, p. 4.2. Obviously, if we require this combination of services, PBX and DID, to be priced below cost, the contribution from Centrex will be diminished and efficient use of the network will be reduced to the disadvantage of Pacific and consumers of basic services.

On the other hand, the ambiguities in determining when a PBX trunk is needed rather than an ordinary business line lead us to conclude that it is inappropriate to approve rates which are totally competitive with Centrex at this time. Thus, we agree with the critics that the 94% increase in trunk access rates initially proposed by Pacific is not reasonable. The compromise proposed by Sullivan, which increases the measured trunk access rate by 48.48% and the flat rate trunk access rate by 33.53%, is more appropriate under the circumstances. We will authorize its adoption contingent on Pacific developing, as a part of its tariffs a set of written criteria setting forth design parameters for PBX, and explaining when a designed circuit is required from the central office serving that customer. After its submission by an advice letter and approval by the Commission by Resolution, Pacific shall provide a copy of this tariff to each customer seeking to establish PBX service.

Finally, seeing no justification to depart from our policy with regard to service connection charges, we will authorize the same percentage increase here that we have authorized for residence service connection charges.

8. **The Revenue Increase to be Spread Over Basic Residence and Business Services**

Based on the considerations described above we will authorize adoption of a rate design which spreads the test year residual revenue requirement using a percentage increase, as uniform as possible, for all recurring local business and residence service rates and service connection charges, except that business trunk rates shall be increased by the amounts set forth above. For clarity and customer ease basic rates will be rounded to the nearest $.05 and service connection charges will be rounded to the nearest $.25. The average increase for these services is about 1%; however, in order to set basic rates at 5-cent increments and still meet the revenue requirement, it is necessary to make slight adjustments to the average percentage increase to some services. Rates thus derived are set out in Appendix A to this decision.

B. Centrex Service

1. Pacific's Proposal

Centrex is a service provided from a Pacific central office which allows intercom calling at the customer's premises, access from these telephone sets to Pacific's network, the ability to transfer calls among telephones at the customer's premises, and various additional optional features such as call forwarding, speed calling, and call waiting. Pacific proposes to restructure Centrex rate elements and to change the way these rate elements are offered to the customer as well as the prices for certain of the the offerings.

The most significant changes proposed are the unbundling of the present Centrex primary station line charge into two elements, Centrex switching and Centrex access; charging two different rates for the new access element to offset the difference in the two End User Common Line (EUCL) charge rates the Federal Communications Commission (FCC) has mandated for service commenced pre-July, 1983 and post-July, 1983; reducing the rates for tie line termination (private network access); including single digit dialing as an element of basic Centrex service; increasing the Centrex Exchange Access Trunking charge to $1.60 to "reflect" Pacific's proposed $16 PBX business measured trunk rate;[1] adding new optional service features; and simplifying charges for optional services by charging one or the other of two rates depending on whether the service has been classified as "high demand, low cost" or "low demand, more complex."

According to Sullivan this proposal will result in an overall revenue decrease of $3.176 million for the 1986 test year. However, as we mentioned above, since the time Pacific's proposal was filed this Commission has issued Resolution T-12023 authorizing 25 additional optional Centrex service features and authorizing rate increases for some of these services which would produce $58,932 more than the annual revenues which would be produced by Pacific's proposal as filed.

Further, since the time Pacific's proposal was filed the FCC has raised the pre-1983 EUCL by $1 per month, from $2 to $3 in its apparent plan to phase out the differential between the two EUCLs.[2] The result is that Pacific's proposed pre-July, 1983 and

1 This is considered a "reflection" because it is generally assumed that one PBX trunk is the equivalent of ten Centrex lines.

2 In April, 1987, the FCC adopted rules that set the pre-July, 1983 EUCL at the lesser of actual cost or $3 per line per month only until June 30, 1987. Then, subject to the same "actual cost"

(Footnote continues on next page)

post-July, 1983 rate parity would be lost or else it would be necessary to adjust rates to take cognizance of this change. Sullivan cites the language of Pacific's proposed tariff Schedule CPUC No. A 9.1.1.A. 1.i. which, in anticipation of such an FCC change, states:

> i. Any change (increase or decrease) in the End User Common Line Access Charge (EUCL) stated in Tariff F.C.C. No. 128, will be offset by a change in the Centrex Line rate in the same amount. The revenue requirement associated with the change will be recovered within the Centrex category as determined by the Utility with at least 30 days notice to the CPUC.

Since the EUCL change was effective on June 1, 1986, Pacific could not offer any evidence in this proceeding on its revenue requirement impact. Therefore, at least until such time as the recovery contemplated by the above tariff language became effective Pacific's pre-1983 customers would actually be paying a minimum of $1 more for basic Centrex service than its post-1983 customers, rather than $2.54 less as is now the case.

In discussing reasons for setting prices to offset the different EUCL rates, Pacific argues that the present rate difference is not cost-based and establishes an artificial cost barrier which keeps customers from adding new Centrex lines or commencing Centrex service, either of which would benefit Pacific's general body of ratepayers by providing a contribution of revenues

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(Footnote continued from previous page)

limitation, the charge was increased to $4 per line per month and will increase again on December 1, 1988 to $5 per line per month. The final increase will be to $6 per line per month on April 1, 1989. (CC Dockets 78-72; 80-286; 87-133: Adopted April 16, 1987; Released May 19, 1987.)

over costs. Sullivan adds that Centrex customers make a relatively greater contribution of revenues over costs than do PBX type customers because Centrex customers buy more features and usage, apparently implying that more customers would choose Centrex instead of PBX or move from PBX to Centrex and would spend more money for features and services if this barrier were removed.

2. Positions of the Other Parties

CBCHA/TCA oppose Pacific's Centrex proposal as simply another element of PacBell's marketing efforts to enhance the competitive position of Centrex versus PBX. CBCHA/TCA cite with approval the opinion testimony of DRA's Shantz that this price positioning by Pacific, where it proposes reducing new Centrex service from $18.68 to $16.00 while increasing PBX trunk rates from $8.25 to $16.00, "is akin to the unethical and abusive marketing practices for which Pacific has already been partially reprimanded by the Commission." (Ex. 351, p. 4.) CBCHA/TCA also argue that the effect of Pacific's proposal is to circumvent the actions of the FCC by causing customers to pay more for their pre-July, 1983 Centrex lines than for their post-July, 1983 lines. CBCHA/TCA conclude that this Commission should reject the proposal and leave the present Centrex rates in effect.

Besides the above-cited statement by Shantz, he also expressed concern about Pacific's motivation in moving from its May, 1986 rate design proposal which would have produced a $2.5 million Centrex revenue increase, and its June, 1986 final proposal which would produce a $3.176 million decrease. He proposes instead that Pacific be authorized to adopt a provisional Centrex offering, applicable to new service only, while retaining the present rate design for service already in effect and changes to such service. He also proposes that while the provisional offering is in effect, each customer subscribing to it sign a statement which puts that customer on notice that the offering is provisional and subject to change. DRA's proposed provisional offering is the same as

Pacific's proposal except it does not include Pacific's proposed reduction from $92.75 ($88 plus a 5.4% surcharge) per month to $55 for tie line terminations because Shantz regards this rate change as intended to improve the price position of Centrex service at the expense of non-Centrex services. Shantz testified that the DRA provisional offering proposal should remain in effect until this Commission addresses the appropriate rates and charges for Centrex services and PBX BEAL services in a separate proceeding after which this Commission would establish permanent rates for all Centrex customers and eliminate the interim provisional offering. Meanwhile, since the provisional offering only applies to new systems, DRA believes that there will be no change in annual test year revenues.

The basis for Shantz' recommendation seems to be a letter which he quotes in his testimony (Exhibit 351). It was sent by the Commission's Advisory and Compliance Division (CACD) to Pacific in December, 1985 refusing to process any more contracts for Centrex services and recommending that Pacific file an application, apparently offering tariffs to cover the services then being offered by contract. The letter criticized Pacific for failing to adhere to Commission procedures in handling these contracts. Shantz seems to take the position that the tariff revisions filed by Pacific in this proceeding, and its failure to file an application as directed by CACD are inappropriate in that they make it impossible for this Commission to give the careful consideration necessary to this question of the wisdom of altering the rate relationship between Centrex service and PBX trunks equipped with DID service.

3. Discussion

We view Centrex as a service which can provide a contribution to Pacific's basic rates. Thus, it is appropriate for Pacific to set rates to maximize this contribution so long as they remain reasonable. PBX rates and DID rates must also be set at reasonable levels. We set those rates above based on their independent merit, but with consideration given to the fact that they compete with Centrex.

Much of DRA's concern about Pacific's Centrex proposal relates to our investigation of Pacific's abusive marketing practices and DRA's concern that such practices have extended into Pacific's business services and may be in operation here. DRA, concerned with the need to further investigate the appropriate relationship between Centrex and PBX services, but wanting Pacific to be able to offer the new digital services in its proposal, contends that we should adopt Pacific's new proposed rates with one exception on a provisional basis for new Centrex service only, applying the existing tariffs to systems in service and growth additions or supersedures to them. We do not believe that the record before us requires the further investigation DRA requests;[3] however, we agree with DRA that Pacific's customers should have the benefit of a rate design which includes its new digital offerings.

Some aspects of appropriate Centrex rate design are clear. For example, hearing no argument to the contrary, we will continue to assume that ten Centrex lines are the equivalent of one PBX trunk. Since we have adopted a PBX trunking rate of $12.25, a consistent Centrex trunking charge would be $1.25 (we round to the nearest $.05), rather than the $1.60 which Pacific proposes based on its $16 PBX trunking rate proposal. This change alone would reduce Centrex revenue by about $3 million.

3 We note that Centrex pricing in relation to PBX pricing, for reasons other than that underlying DRA's concern, may be revisited in the upcoming I.87-11-033 Supplemental Rate Design proceeding. Our conclusions about Centrex pricing here, however, are appropriately based solely on the present record.

On the other hand, this record provides no information on which to determine the reasonableness of the one very large rate change that Pacific proposes - the reduction in tie line charges from $92.75 per month to $55. In fact, its initial proposal did not make such a shift. Furthermore, we have very little information on the relative costs for meeting any particular user's needs via PBX trunks versus Centrex service should these proposed changes be implemented. Thus, while there is no evidence of marketing abuse with respect to the marketing of Centrex vis-a-vis PBX trunk lines equipped with DID service, the evidence available is inadequate to warrant a rate design which would amplify the revenue effects of the reduced trunking charge by incorporating this further rate reduction.

According to Pacific the revenue difference between its earlier Centrex proposal and the June 25, 1986 final proposal is about $5.676 million. Leaving the single tie line monthly rate element at its present $92.75 level, rather than the proposed $55, adopting the $1.25 trunking rate, and adopting the rest of Pacific's final proposal, excluding the five features adopted by Resolution T-12023, results in a $0.968 million revenue decrease. When we include the additional revenue from Resolution 12023 the total Centrex revenue effect is a negative $0.912 million, which still provides a contribution over cost (at least as Pacific defines cost at p. 4.2 of Exhibit 260).

These changes leave a rate design which incorporates the new digital offerings and also achieves a reasonably small revenue change in a relatively straightforward manner. Therefore, Pacific is authorized to adopt its final proposed rate design for Centrex except that the tie line termination charge shall remain at its present $92.75 and the Centrex Exchange Access Trunking Charge shall be set at $1.25. These new rates shall apply to all Centrex customers.

C. Direct Inward Dialing (DID) Service

1. Background

DID is a service which allows a caller to call directly to a telephone number which is on a PBX or telephone answering service (TAS) or similar service without having to be answered by an attendant. This is done by an arrangement in the central office serving the PBX or TAS customer which sends the call from the local network to the PBX or TAS dial switching or number identifying equipment, which then relays it to the appropriate telephone set. The DID capability is also a part of Centrex service, however in that case the individual telephone line terminates at a "port" on Pacific's central office switching machine rather than on equipment at a user location.

During hearings in Pacific's last general rate proceeding Telephone Answering Services of California (TASC) objected to Pacific's present DID rate structure which bases charges on the volume of telephone numbers without a separate trunk charge. TASC argued that because call holding times for TAS are shorter than they are for PBX systems where full length conversations transpire, TAS customers require fewer trunks for a given quantity of telephone numbers than PBX customers do, and so impose less trunking costs on the utility. In effect, they argued, they are being charged for trunks they do not use. TASC therefore urged disaggregation of charges for DID numbers and trunks. In D.84-06-111 we found that TASC had not sustained its burden of proving the unreasonableness of Pacific's DID rates but at Ordering Paragraph 16.c. we ordered Pacific to conduct and file in the present general rate proceeding, a study of DID costs and, if appropriate, a rate proposal addressing these issues.

2. Pacific's Study and Proposal

Pacific conducted the study (Exhibit 264) and determined that its DID rate design should be changed. It proposes three changes; the first two essentially do away with the present declining block pricing by decreasing the charge for the first two blocks of 100 DID station numbers from $200 to $60, and increasing the charge for additional blocks of 100 DID station numbers from $35 to $60, making each block the same. The third change is to add a trunk-sensitive monthly circuit termination rate element of $8 per trunk. The effect of such a change, of course, is to reduce the rates for users of fewer than 200 station numbers but to increase rates for the largest customers of DID service such as large PBX users. Pacific claims that its new rate structure strikes a more equitable balance between the PBX and telephone answering service markets than the existing rate structure. The annual revenue effect for the 1986 test year is an additional $38,000.

3. <u>Positions of Other Parties</u>

DRA reviewed Pacific's study and concluded that the cost study is inadequate in several respects. The review finds that rates for trunks and numbers should be separated, but DRA's Shantz cautions that without an adequate cost study it is not appropriate to reduce the aggregate customer billing from DID service because of its similarity, when used in conjunction with a PBX, to Centrex service. Nonetheless, Shantz testified that DRA supports Pacific's proposed rate revisions and recommends their adoption because they address the need for restructured rates and result in a small change in aggregate customer billing.

TASC generally supports the Pacific rate proposal. However, pointing out that Pacific's work papers show a revenue to cost (R/C) ratio of 1.25 for the proposed DID station number charge, while Centrex is proposed to be priced at 1.0, TASC argues that since these services compete, they should both be priced at the same 1.0 R/C ratio. Further, TASC asserts that since the trunk charge proposal will have differing effects on customers depending on how long their calls tend to be, the fairest way to price it is to adopt the same R/C ratio for it as for the station number charge.

In addition TASC requests that we do away with Pacific's Basic Termination Charge (BTC) which is assessed for terminating service prior to the 3-year minimum period provided for in the DID tariff. It is set at $6,500 per 100 numbers for the first 200 DID numbers and $1100 per 100 numbers thereafter. TASC points out that if Pacific's new rate proposal is adopted and a hypothetical TAS customer with 400 DID numbers, paying a recurring charge of $240 per month, discontinues service after one year that subscriber will be obligated to pay Pacific 2/3 of $15,200 for the 400 numbers, or $10,133. However, if the customer simply continues paying the monthly payments for the next 24 months and leaves the service idle, its payments will total only $5,760. TASC claims that the nonrecurring charge at the time of installation is supposed to cover both installation and removal charges, and questions what cost is left that requires this payment. Further, TASC asserts that there is no similar charge for Pacific's Centrex service.

FEA claim they generally support the unbundling of rate elements, but oppose Pacific's proposed $8 per month trunk termination charge, claiming that it would cause rate shock when considered in conjunction with the increased PBX trunk rate Pacific has proposed. This concern is based on the assumption that we will adopt Pacific's proposed $16 measured trunk rate.

CBCHA/TCA, oppose adoption of Pacific's DID rate design. They assert that while small PBX customers would receive a rate reduction under the proposal large customers would be unfairly burdened with increases of up to 100%. They argue that these rates will have an anticompetitive impact on PBX service, that Pacific's own cost study shows that the rates exceed costs by 156% to 176%, but that this cost study is flawed and unreliable. Selwyn expressed several concerns about the cost study including lack of detail as to assumptions Pacific employed in undertaking the study including what type of central office equipment it examined, what level of utilization of the central processor it assumed and why, how consistent these costs are with those parallel costs developed for Centrex - e.g., allocation of fixed central office processor capacity costs, and the lack of consideration given to economies of scale. Selwyn concludes that Pacific's cost study probably overstates costs, but that it would be fair to set rates at precisely the level of cost that the cost study shows. He finds this to be $25 per 100 DID station numbers for all 100 number blocks and $8 per DID trunk.

Pacific cites the rebuttal testimony of Scholl (Exhibit 402) as well as other exhibits to defend against almost every item of criticism leveled at its cost study by DRA and Selwyn.

4. Discussion

None of the criticism of Pacific's DID pricing proposal disputes the need for disaggregating rates to provide a separate trunk sensitive circuit termination rate element. Only FEA object to the amount Pacific proposes to charge, on the ground that this rate in conjunction with the $16 measured trunk rate Pacific proposes for PBX service would produce rate shock.

In fact, this decision adopts a lower measured trunk rate of $12.25. When added to the termination charge the new rate per trunk would be $20.25. The present rate, which has no termination charge, is $8.25. However, this comparison does not consider the monthly reduction proposed for the first 200 DID station numbers. If we accept Pacific's estimate that on average one trunk will support 18 PBX numbers (and 30 TAS numbers), then a PBX customer would pay about $342.75 for the first 200 DID station numbers under the new proposal with the newly adopted PBX trunk rate, as compared with $490.75 under the present rate design. On the other hand, the second 200 numbers would cost the same $342.75 under the proposed plan, but only $160.75 under the present rate design. Thus, the average PBX customer will begin to see a slight ($34.00) rate disadvantage under the new proposal at the 400 station number level, and that disadvantage will average about $182 or 107% for each additional 200 DID station numbers.

Comparing just the DID rates rather than combined with the PBX trunk rate, shows that charges under the new rates do not exceed charges under the present rates until a customer reaches the station number level of about 500, at which point DID charges under the proposed rates are about $17 higher per month than under the present rates. From that point on the disparity continues to grow as the old rates increase by $35 per month per 100 numbers while the new rates increase by about $104 per 100 numbers, with rates under the new proposal becoming double that under the present design at about 1,900 lines.

These calculations indicate to us that the rate increases to large PBX users under this proposal do not outweigh the more equitable treatment of TAS users provided by a separate trunk sensitive rate element for DID service. TASC, DRA, and CBCHA/TCA agree that it is appropriate to adopt this element, and we agree.

Although there are some questions about the accuracy of data Pacific relied upon in arriving at its costs, we are confused by DRA's criticism of the major features of Pacific's DID cost study. For example, DRA's witness Singh criticizes Pacific because its estimates of investments and expenses come from Pacific's Results of Operation report which is based on tops-down, not bottoms-up study methodology. He also faults Pacific for allocating these investments and expenses to DID services using Functional Accounting methodology. Singh does not criticize the results of Pacific's tops-down studies. We do not know if DRA finds that they are, in fact, inadequate or not. Likewise, even assuming Pacific did use Functional Accounting, Singh's only comment is that it "has not been recognized by this Commission as a proper method of accounting for rate making purposes." We do not know whether he views it as a reasonable method or not. In any case, Pacific argues that a bottoms-up study was not required for DID, and Scholl adds that Pacific did not derive unit investment costs from its books of account, but relied on current prices charged by the manufacturer to determine costs (apparently costs for switching equipment). Further, Pacific is correct about cost studies. Ordering Paragraph 16 d. of D.84-06-111 only ordered bottoms-up studies for service categories where Pacific "proposes rate increases substantially greater in percentage terms than the proposed increase in total revenues."

We do agree with DRA's uncontroverted claim that the variables used in the SCIS model which was used to assign costs between touchtone and dial pulse were not demonstrated to be valid. We are further concerned about the issue raised by Selwyn regarding the comparability of cost assignment between Centrex and DID, since DID is a component of a service used in competition with Centrex. Scholl asserts in his rebuttal testimony (Exhibit 402) that costs were assigned to both in the same way, but cites no documentation which demonstrates this.

Since we find it reasonable to adopt a disaggregated rate element for the trunk component, we must now arrive at a reasonable rate for station numbers. Pacific's cost study shows that there is no basis for differentiating between the first two blocks of 100 numbers and subsequent blocks. Therefore, we will adopt a rate which treats each block the same. We are not confident enough in the accuracy of Pacific's cost study, however, to adopt the $60 rate it suggests. A lower rate would more certainly protect PBX customers from rates set too high when considered in relationship to competitive Centrex service rates.

It appears to us that TASC's recommendation of setting this rate at a R/C ratio of 1.0, based on Pacific's cost study is a reasonable means of achieving these goals. The appropriate rate thus defined is $45 per each 100 DID station numbers rather than the $60 Pacific has proposed. Charges reach the same amount under this rate design and under the present rates at about 600 lines. Rates do not double in comparison to present rates until a customer reaches nearly 2,900 lines. This change along with the adopted trunk sensitive termination rate element will reduce Pacific's proposed DID revenues by $1.870 million.

We are sympathetic with TASC's request that the termination of service charge for DID be removed. TASC's assertions make the validity of the charge seem quite dubious. There has been no opportunity in this proceeding, however, for Pacific to provide its rationale for continuing the charge. Therefore, we will take no action on the TASC request, but we will order Pacific to address the reasonableness of continuing this charge, including a showing of costs which it is designed to cover, in its next general rate proceeding.

D. Coin Services

1. Coin Telephone Rates

Pacific proposes no change in its local coin telephone rates; however, TURN's witness Siegel proposes that the rates be reduced from $.20 to $.10, based on the results of the cost study presented by a TURN witness in Pacific's last general rate proceeding. We considered that study and adopted the present rate in D.84-06-111. No new evidence convinces us that we should now revert to the coin rate level which we adopted in 1952. We also find no basis in the record for adopting TURN's alternative recommendation that the coin rate be reduced to $.15. We will deny TURN's request.

2. Semi-Public Coin Service

a. The Service and Pacific's Proposal

As Sullivan explained on cross examination, semi-public coin service is a service provided to a business customer which allows the features of a regular business service, including directory listing, but gives the customer a coin telephone for the use of employees, the transient public or the like, which assures that the caller pays for his or her own call. Such service is common in dormitories and sorority and fraternity houses as well as business locations. Exhibit 287 shows that Pacific projected 77,553 semi-public in-service access lines in 1986.

Pacific proposes increasing its access rate for semi-public coin service by 55% from $20 to $31. It also proposes changing extended area service (EAS) and Special Rate Area (SRA) rate increments for semi-public rates, and increasing the service connection charge by 37.14% from $175 to $240. Sullivan testified that Pacific wishes to relate its price more closely to the cost of providing the service, and also stated Pacific's position that this service should cover its own costs. In addition to these rate increases Pacific proposes that it be entitled to require a deposit equal to the replacement cost of the instrument and associated equipment when service is requested in locations Pacific deems to be not secure. The proposed tariff gives examples such as construction sites and temporary structures. Sullivan testified that the purpose of this provision is to assure that general ratepayers are not burdened with the cost of lost equipment. He stated that he believed the charge would be in the range of $400 to $500 and that Pacific did not expect it to diminish the ordering of semi-public service. There appears to be no offset for this expense savings in any cost calculation.

Cost witness Scholl's original testimony (Exhibit 260) shows a revenue to cost ratio for monthly service at present rates, based on average historical cost, of .5 and for service connection of .4. Scholl's later testimony, Exhibit 261, shows that in order to reflect the results of operations this Commission actually adopted in D.86-01-026 the costs of these services should be reduced by the appropriate scaling factor. In the case of the recurring charge, the factor is 90%. It is 93% for the nonrecurring charge. Thus Pacific acknowledges that its revenue to cost ratios overstate the amount by which average historical costs exceed revenues by 10% and 7% respectively.

b. Positions of Other Parties

DRA advocates applying the same percentage adjustment for the access rate for this service that is adopted for recurring business and residence services. On behalf of DRA Shantz testified that DRA opposes any change in EAS rates on the grounds that Pacific has not provided any basis for increasing EAS, that these increments are generally intended to represent the loss in message toll revenue that results when message toll routes are converted to local (EAS) routes and that little attention has been given to sustaining the relationship between the EAS increments and the message toll rates in recent years. While DRA does not specifically address the extension of EAS or SRA rate increments to services to which they have not previously been applied, we take this statement to indicate that DRA contends that such extension should be denied except upon a specific showing of the relationship between the increments and message toll losses.

c. Discussion

If it is the case that we need to reset EAS rates so that they better reflect the difference between message tolls previously collected and local rates, then we will do so when we are presented with evidence of the problem. However, since we are not adopting the toll zone consolidation Pacific proposes it does not appear that any change in EAS or SRA rates is necessary at this time. Therefore, we will not grant Pacific's proposal to change EAS and SRA rate increments for semi-public rates.

Pacific's cost evidence indicates that access costs would match revenue if a 45% increase were granted, yet it asks for a 55% increase. This service is not one which we consider to be primarily a basic service, although it may be a substitute for basic service for many users. Because it is not a basic service it is reasonable that revenues cover costs. On the other hand, the service is not the sort from which the subscriber gains any direct benefit. We are therefore reluctant to permit rates which might discourage subscribers from continuing to provide this service to its employees or residents who rely upon it. This is not a service which ought to subsidize basic service rates. Therefore, we will permit a rate increase of 45%, which raises access rates from $20 to $29. Based on the same rationale, we find Pacific's proposal to increase the service charge to $240 to be appropriate, and will adopt it.

We are sympathetic to Pacific's desire to prevent burdening general ratepayers with costs for equipment loss. Requiring a deposit from certain types of customers may be a reasonable way of accomplishing this end. However, the language of Pacific's proposed tariff is too broad. It could be used discriminatorily. It could have been drafted in more specific terms. Had Pacific chosen to do so, we may have found it acceptable, but in the form presented it must be rejected. Furthermore, while the cost saving is likely to be small, if Pacific chooses to propose such a provision in a future proceeding, it should at least address that cost savings.

The rate changes we adopt for Semi-public Coin Telephones, including expense savings, provide a test year revenue increase of $9.005 million.

3. Customer-Owned Pay Telephone (COPT)

a. Pacific's Proposal

A COPT telephone is similar to a semi-public telephone except that the COPT customer owns and operates the telephone instrument, the proceeds of the coin box belong to the COPT customer and the service is not confined to business premises. Exhibit 287 shows a Pacific projection of about 4,500 COPT access lines in service for 1986. Pacific proposes increasing measured access line rates for COPT by 29.4% from $17 to $22, and flat access line rates from present rates between $27 and $43 to new rates between $32 and $48, and increasing the allocation of message units for the initial minute of measured service by 5% from $.06 to $.063. Sullivan changed this message unit figure in his rebuttal testimony to an 11.7% increase from $.06 to $.067. Subsequent minutes remain at $.01. Additionally Pacific proposes increasing the installation charge from $110 to $175 and the charge for converted service from $75 to $115.

Sullivan described these proposed rates as an attempt to achieve movement toward coverage of costs and also testified that the proposed access rate increases are meant to mirror the percentage changes Pacific is proposing for business line access rates. Sullivan testified that this is consistent with Ordering Paragraph 11 of D.85-11-057 which states that rates and charges for COPT service should be "subject to adjustment in the rate design phase of Application (A.) 85-01-034 only for the purpose of maintaining consistency with rates for comparable services." He further testified that his originally proposed rate for an increase in the initial message unit is meant to reflect corresponding proposed changes in MTS rates and thus to maintain the present relationship between toll rates from coin phones and toll rates from dial stations. The change to this rate that he proposed on rebuttal is to account for the increase in message unit charges for business services which adjusts for Pacific's proposed alternative rate for Centrex service. He also testified about Exhibit 301 which projects that the new rates would cause a repression rate of 15% in station growth due to nonrecurring rate increases and 5% due to recurring rate increases, producing an overall revenue increase of about $226,000 or about 13%, over the baseline total at current rates of about $1,719,000.

Scholl testified that his service cost studies did not address COPT service because COPT was not yet a Pacific offering at the time his cost exhibits were being prepared.

b. Positions of Other Parties

DRA again advocates applying the same percentage adjustment to recurring rates for this service that is adopted for business services, and the same lower rate increase for the installation charge that is advocates for all service connection charges. Shantz testified that DRA does not propose a change for the $75 charge for conversion of service.

California Payphone Association (CPA), whose 35 members conduct private payphone businesses in California, presented the testimony of its President, John Cunningham, who is also an officer of a company which owns, installs, and operates private payphones in Pacific's service area. He testified that at present rates the COPT operator must generate revenues of $349 per month on an annual basis in order to stay in business, assuming that the COPT operator charges the maximum allowable $.25 per local call, that capital costs per COPT are $2,500 with a 5-year depreciation life for installation, that 20% of the operating profit will be paid as a commission to the location owner or manager, that operating and maintenance expenses plus administrative and general expenses for the operator are about $55 per month per station, and that a 14% annual return on investment is the minimum reasonable return.

He claims that fewer than 15% of the public telephones in Pacific's service area can generate that much revenue and that COPT operators must concentrate their services in these high usage market locations. At Pacific's proposed rates (without Sullivan's last increase in the initial minute rate) Cunningham estimates that the return from a COPT generating $349 per month would be reduced to 11.8% and that the COPT would have to generate $365 per month to produce a 14% return, thereby reducing even further the selection of COPT locations. To this he adds other inherent competitive disadvantages in COPT operations which he says lead him to conclude that the proposed rate increase could lead to an end to the long-term viability of the private pay telephone market in California. These unquantified disadvantages include the COPT's "need" to charge the allowable maximum of $.25 rather than Pacific's $.20 rate, the "need" of COPTs to limit calls to 15 minutes, the COPT's inability to derive much revenue from nonlocal calls, and its inability to receive any share of "nonsent paid toll revenues" or access service revenues for interLATA calls made from COPT stations. We put the word "need" in quotation marks because these practices are not tariff requirements, but business decisions.

CPA asserts that the increased revenue Pacific expects to generate from its proposed COPT rate changes is miniscule by PacBell's standards, but very ominous to the small businesses which comprise CPA's membership. Although there are no cost studies specifically addressing COPT in this record, CPA states that the information about coin services in the cost studies Pacific sponsored show revenues approximately equal to cost for coin access lines, local usage and sent-paid toll. CPA goes on to claim that there is insufficient detail to identify not-sent-paid (i.e., credit card or operator assisted) toll revenues and access charge revenues related to coin service. Citing the analogous 2.8 revenue to cost ratio for intraLATA MTS set out in Scholl's testimony, Exhibit 260, CPA claims that these two revenue categories are among the most profitable to PacBell, and concludes that Pacific's coin services as a general class produce revenues well in excess of costs. Based on this conclusion CPA argues that there is no basis in the record for presuming that subscribers to COPT do not, likewise, pay rates which fully cover the costs of those services which PacBell provides to them.

CPA adds that D.85-11-057 does not <u>mandate</u> a rate adjustment for COPT in this proceeding, it merely "place[s] a <u>ceiling</u> on the degree to which COPT service rates might be adjusted in this proceeding" (emphasis in original). Further, CPA points out that the present monthly rate for measured COPT service was developed based on Pacific's own cost estimates and the cost study which provided the firmest basis for the COPT line rate we adopted is the cost study for a measured business line which was prepared by Pacific and sponsored by Scholl in this current rate proceeding. (See D.85-11-057, mimeo. at 45-50, Finding 24, at 114; D.86-01-059, mimeo. at 4.) CPA concludes that our prior decision does not absolve Pacific of its obligation to provide adequate evidentiary support for these rate change proposals.

CPA argues that we should deny the COPT increases Pacific seeks because the competitive inroads private operators have made into the public telephone services market are small and their profit margins are already narrow. It adds that adoption will imperil the vitality and the future of the private payphone industry as well as the services which that industry could offer to the general public.

c. Discussion

We stated our priorities for the setting of COPT rates quite clearly in D.85-11-057. We said:

> "We need not evaluate the business prospects of COPT operators in detail, because we conclude that the viability of the business potential for COPT operators is at most a consideration of secondary importance in our setting rates for COPT service. Our primary concerns are to assure that COPT rates are set at levels which do not seriously impair Pacific's net revenues and are reasonable in relation to Pacific's service costs and its rates for comparable services. We agree with TURN that if, having analyzed and weighed these relevant factors, we adopt rates which offer only a narrow window of business opportunity in especially high volume locales, that may disappoint prospective entrepreneurs but will nonetheless serve the interests of the general body of ratepayers. If the adopted rates are low enough to foster widespread COPT operations in California, that will be

> so much the better. Thus, in setting rates for COPT service, we shall direct our attention to the interests of the general body of ratepayers rather than to those of the potential COPT operator. On the other hand, we recognize that Pacific will be a competitor with COPT operators as well as a provider of services to them. We therefore intend to assure that the rate structure and rate levels adopted for COPT service do not unduly or unnecessarily discriminate against the COPT operator in relation to Pacific's own pay telephone services." (D.85-11-057, mimeo. at 34-35.)

Keeping this in mind we evaluated the various proposals before us. Pacific's proposal for the access line rate was based on its costs of providing measured business (1MB) lines, which have cost characteristics similar to COPT lines. The accuracy of this proposal was corroborated during the hearing in that proceeding, with one slight adjustment, by Scholl based on cost study data which had been prepared for, but not yet presented in, the present proceeding. We further adjusted Pacific's figure to account for the appropriate rate of return, the proper attribution of the interstate Customer Access Line Charge (CALC), the adopted revenue requirement, the value of the 411 directory assistance allowance included in the COPT service, and continuing administrative costs. We found that the cost of an average call was very close to the then-effective ZUM Zone 1 rates, and concluded that simplicity of rate design, ease of future adjustment, and consistency with Pacific's service costs as well as alleviation of any incentive for customers to connect COPTs improperly to ordinary business lines by setting this rate at the same level as those business lines, made it reasonable to set the rates for local COPT calls at the ZUM Zone 1 rates as DRA recommended.

Since no new cost evidence has been presented and the amount of time since we authorized Pacific's present COPT rates is relatively short, we assume that the cost of an average COPT call is still very close to the ZUM Zone 1 rate. The advantages we cited in D.85-11-057 for using this same rate for COPT service still hold true. At the time we adopted the present COPT rates residence and business usage rates were the same for ZUM Zone 1. That fact is not changed by this decision. Since COPT costs have characteristics similar to measured business lines it is appropriate for Pacific's COPT rates to continue to reflect those rates. Therefore, Pacific's COPT access rates should be increased by the same percentage as business access rates and COPT usage rates should remain at present levels.

We see no reason in this record to deviate from the across-the-board percentage increase for installation and repair that we have adopted for business and residence services. Pacific should adopt the same increase. Furthermore, since conversion of service is just as "labor intensive," as DRA put it, as installation or repair, that cost should reasonably be expected to increase by the same percentage. Therefore, we will permit Pacific to adopt the same increase factor for conversion as for new installation.

Clearly these rate changes will have less impact on the COPT operators than the changes Pacific proposes. The impact that the changes do cause are reasonably related to costs and protect the general ratepayer from subsidizing this service. While this decision may reduce their rate of return to something less than 14%, and perhaps cause them to reconsider contemplated new services, it is certain that these changes will not deprive CPA members of their ability to operate.

The COPT rates and charges we adopt in this decision will produce a $0.019 million revenue increase for the test year.

IV. Incidental Services

A. Nonpublished Service

Pacific presently provides nonpublished service to its customers for $.30 per month. This service allows a customer to be unlisted in both the telephone directory and with directory assistance. Sullivan testified that Pacific's market studies show that this service is grossly underpriced in relationship to the value many customers place on it. Based on this he recommends increasing the monthly rate by 83.33% to $.55.

Additionally, Sullivan described a new service which Pacific proposes to call Directory Assistance Listing (DAL). This service permits the customer to be unlisted in the telephone directory, but includes that customer's name, address, and telephone number in the Directory Assistance Service data base, so that a caller who knows the name and location of the customer can get his or her number from Directory Assistance, but the customer can avoid random solicitations and nuisance calls. Pacific proposes pricing this service at $.30 per month. Taken together Pacific projects that these services as proposed will generate an additional $7.443 million in the test year.

DRA supports both these proposals but argues that the rates for nonpublished service should remain at their present $.30 level and that rates for DAL should be set at half that price, $.15 per month. DRA's rationale for its rate proposals is Shantz' testimony that it is inappropriate to increase rates for this service on a value of service basis in a period of declining overall costs for Pacific. DRA calculates that its rate proposal results in a revenue decrease of about $113,000 to Pacific.

TURN also objects to any increase for nonpublished service, arguing that ratepayers have a right to protect their privacy and should not have the cost of this privacy nearly doubled.

We believe that Pacific's new offering is a useful addition to its nonpublished service offering, and will adopt it. Some customers object to paying anything over cost for unpublished service. We recognize that many people believe it is important to keep their numbers private, but we think this is the sort of nonessential service which ought to continue to provide some subsidy to basic service. On the other hand, we agree with DRA that it is inappropriate to increase the rates for existing nonpublished service when the rates are already set well above costs.

It seems intuitively likely that DAL service would have higher per-unit costs than nonpublished service, and its costs ought to be set to reflect that fact. However, we can find nothing in the record to verify this, and both Pacific and DRA endorse setting DAL rates at between 50% and 55% of the nonpublished service rates. We will keep rates at this same ratio. Thus, we have kept the $.30 rate level for nonpublished service, we will also adopt DRA's proposed $.15 level for DAL service. The small revenue reduction which results from DRA's proposal is too small to have a noticeable effect on the overall revenue contribution of these services.

B. Touchtone Service

Pacific's initial proposal suggests no change in its Touchtone service rates. In his rebuttal testimony, however, Sullivan proposed reducing rates for three services if the revenue requirement we adopt in this proceeding is lower than what Pacific proposed. Making Touchtone a standard rather than an optional offering was the third of these proposed rate changes. Sullivan points out that since the Touchtone function is necessary to many new telephone products and services, such treatment would guarantee the broadest possible availability of new offerings to Pacific Bell customers. Pacific's closing brief adds that Touchtone service generates approximately $80 million in annual revenues, but fails to cite any reference in the record which yields such information.

DRA does not comment on this proposal; however, TURN does. TURN recites the arguments it made in Pacific's previous general rate proceeding for the elimination of additional charges for Touchtone service. It states that Touchtone service automatically becomes available, without any extra cost to Pacific, in areas where Pacific installs electronic switches; that calls made with Touchtone should cost less than rotary-dialed calls due to shorter set-up times; and that the overwhelming majority of residential customers now have Touchtone phones, so that this former luxury is now a near-universal element of basic service. TURN urges that such a rate change is an equitable alternative for spreading part of the rate reductions which it contends are due residential customers.

In the past it has been our position that Touchtone service was an appropriate demarcation line between basic service and access to the optional features and information services which ought to cover their own costs and, where possible, provide a contribution to basic service. The Touchtone rates have remained at their current levels, $1.20 for residence lines and $1.70 for business lines, since they were first authorized in 1967. Of course, they have become increasingly more useful since that time as the number of services available through them has continued to increase.

It is reasonable to argue that Touchtone should be offered at no premium since its broad availability does not result in extra direct costs to Pacific, but might encourage more customers to buy additional optional services which are priced to subsidize basic service. We are not averse to considering the elimination of extra charges for Touchtone service. However, we cannot do so in this proceeding since Pacific's cost and revenue witness did not address this particular service and we have no evidence of the revenue impact of such a change. The statement in Pacific's closing brief is not evidence. Even if this statement could be regarded as evidence we note that Pacific projected Touchtone revenues of about $107 million in 1984, in contrast to the $80 million figure which Pacific now claims, apparently as a 1986 figure. (See D.84-06-111, mimeo. at p. 201.) This large discrepancy alone makes reliance on Pacific's unsubstantiated claim unreasonable. For these reasons we will leave Pacific's Touchtone rates as-is for the present, but we will direct Pacific to provide cost and revenue data for Touchtone service in the supplementary rate design proceedings.

C. <u>Verification Interrupt</u>

This is a service by which toll operators may verify that a line is actually busy at the request of a calling party. Sullivan testified that Pacific wishes to increase the charge from $.50 to $.75 in order to bring the rates more in line with the cost of handling this type of service. DRA opposes the increase.

Scholl's testimony, Exhibit 260, does not specifically indicate the cost of providing Verification Interrupt service. It divides operator services between two categories, directory assistance (DA) and "other." In this "other" subcategory, to which Verification Interrupt service would belong, Scholl shows an overall revenue to cost ratio of 0.7. Applying the 82% adjustment factor to the costs for this subcategory brings that ratio to about 0.9. In Exhibit 351 Shantz points out that Pacific has projected an annual revenue increase of $247,000 for this service in the test year based on calculations using a unit cost of $.27, and assuming adoption of the proposed rate increase. Shantz argues that this unit cost figure is well below the present rate already and does not seem to justify a further increase. We agree. There is no clear basis in this record for raising the Verification Interrupt rate. We will leave it as-is.

D. Remote Call Forwarding

Remote Call Forwarding (RCF) is an optional service allowing customers a local telephone number identity in a remote location without actually maintaining an office there. Incoming calls to this remote number are automatically forwarded to the telephone number where the customer is actually located. The calling party is billed for the call to this remote telephone number, while the subscribing customer is billed for the remaining portion.

The present monthly rate for this service is $18 per access path. Pacific proposes to retain the same rate for initial access paths, but to reduce the charge for the second and third access paths to $10 and to reduce the charge for the fourth and further access paths to $5. Sullivan testified that such pricing would produce usage stimulation thereby producing optimum revenue. He added that this service is a partial substitute for FEX. Despite the rate reduction, Pacific projects a revenue gain of $1.143 million with this rate change due to the growth it estimates will take place in RCF access paths.

DRA opposes any change in RCF rates, pointing out that the revenue gain Pacific projects is the result of its proposed limitation on Foreign Exchange Service to existing customers, which DRA also opposes. DRA also opposes the proposal on the ground that RCF is a type of basic exchange service and that it would be improper to permit a decrease in this rate if we are adopting increases in other basic exchange service rates. Finally, DRA also objects to this proposal because RCF was one of the services which was the subject of our marketing abuse findings. DRA argues that we should not permit changes in rate structures for any such service "until the effects of the unethical and abusive marketing activities have been corrected and eliminated."

We agree with DRA that RCF rates should not be reduced in this decision. The basis for Pacific's projection of a revenue gain is the grandfathering of its FEX service. Elsewhere in this decision we explain why that grandfathering proposal is not reasonable. This being so, the revenue effect of Pacific's proposed changes in RCF rates is not likely to be the increase which it has projected. We will authorize no change in RCF rates.

V. Message Toll Service (MTS) and MTS-Related Services

A. Introduction

Pacific proposes various rate changes for Message Toll Service (MTS) and related services. The related services are Call Bonus Wide Area, Community Calling Plans, Circle Calling, Optional Calling Measured Service (OCMS), Wide Area Telephone Service (WATS), and 800 Service. Pacific says that the MTS and MTS-related services rate design which it proposes will produce a test year revenue decrease of $51.718 million for these services. With parentheses denoting negative revenue effects, this breaks down as follows:

MTS:	($36.719 million)
Call Bonus Wide Area:	(5.521 million)
Community Calling:	0.661 million
Circle Calling:	(1.327 million)
OCMS:	0.739 million
WATS:	1.516 million
800 Service:	(11.067 million)

DRA's revenue neutral proposal for the same time frame would decrease revenues from this source by a slightly larger amount, $54.010 million. It breaks down as follows:

MTS:	($46.860 million)
Call Bonus Wide Area:	(0.568 million)
Community Calling:	(2.719 million)
Circle Calling:	(2.925 million)
OCMS:	(0.460 million)
WATS:	(0.478 million)
800 Service:	0.0 million

In DRA's alternative rate design to reflect its later revenue requirement proposal, the portion for MTS and MTS-related services comes to a negative $166.212 million, and in the rate design proposal in its Concurrent Opening Brief, which is based on the total revenue reduction of $181.557 million, (which includes DRA's calculations for a revenue neutral outcome plus an additional revenue requirement decrease of $79.6 million to reflect the direct assignment of closed end WATS costs on January 1, 1987 as shown in DRA's latest proposal in the Results of Operations Phase) DRA proposes reducing MTS and MTS-related services by only $33.295 million. The details of Pacific's proposal as well as DRA's alternatives and the suggestions and comments of other parties are addressed below.

B. Message Toll Service (MTS)

1. Pacific's Rate Band Proposal

Pacific proposes re-pricing and simplifying its MTS service. Under the plan intraLATA message toll rate bands would be reduced from seventeen to four. Pacific would consolidate the first two of these bands into one larger zone encompassing the area from beyond the 8-mile local calling area up to 16 miles. (Pacific proposes the same change in major metropolitan areas where these two zones are known as ZUM Zones 2 and 3 and their rates are set below toll rates to recognize the differences in costs and calling needs in highly urbanized areas. Pacific's plan for the ZUM zone consolidation is discussed along with other ZUM proposals below.)

The remaining 15 message toll rate bands, which account for calls in mileage increments from 16+ miles up to 245 miles, with the last band being for calls of over 245 miles, would be consolidated into three bands: 16+ to 30 miles, 30+ to 50 miles, and over 50 miles. Pacific then proposes setting rates for its consolidated first rate band at $.59 for a five-minute call. This contrasts with the present rate of $.49 for a five-minute call in the 9-12 mile mileage band, a 20% increase, and $.64 for a five-minute call in the 13-16 mile mileage band, an 8% decrease. Additionally, Pacific proposes rate decreases in the consolidated longer mileage bands, with the most expensive five-minute call decreasing from $2.42 to $1.50. However, these rates would still result in a rate increase for one more of the present rate bands, the 16+ to 20 mile band, by about 12%. Pacific projects the overall test year revenue effect of these changes to be a reduction of $36.719 million.

Pacific's Scholl points out that the proposed MTS rate restructuring still results in revenues which exceed projected historical costs for every mileage band although the revenue to cost ratio will be greater than it is now for short-haul mileage bands and less than it is now for the longer-haul bands. He adds that the new rate design would bring these ratios into a much tighter range. (Exhibit 402, p. 137.) In other words, the profit margins would become more similar among the bands. Pacific's Sullivan cites the following objectives for proposing these changes: to stimulate usage on the most profitable longer-haul routes, to protect against bypass, and to continue the revenue contribution to provide a sustainable means of sustaining the support of Residence Exchange Telephone Service. (Exhibit 283, pp. 10-11.)

Pacific adds that in the face of ever-increasing competitive pressures underpriced business services rates should be increased thereby facilitating toll-related rate decreases as a first line of defense of the basic residence service subsidy. Further, Pacific argues that longer-haul calls tend to have the highest revenue-to-cost ratios and therefore are most vulnerable to bypass. It makes sense, adds Pacific, to focus rate reductions on such calls, partly because the per-mile costs of such calls are less than for shorter-haul calls.

Finally, Pacific suggests that if further revenue requirement reductions are required, MTS services should be given first priority for such reductions, and those (longer-haul) mileage bands with the highest revenue to cost ratios should be reduced first.

2. DRA's Rate Band Proposal

DRA's witness, Karen L. Miller, testified about DRA's revenue neutral rate design proposal, which she designed based on the instruction of Project and Program Supervisor, Shantz, that the level of revenue decrease for these services should be about $50 million for the test year.

Miller testified that DRA proposes reducing the number of MTS rate bands from 17 to 9 by combining all the rate bands from 71 miles and greater into one band, consolidating the message toll coin rate bands to be consistent with this regular MTS rate band proposal, and reducing the rates for the initial minute of service for each of these remaining bands. Miller testified that DRA's proposal would reduce rates in each rate band by $.01 out to 71+ miles where, because the rest of the bands are consolidated, the rate reduction effectively increases with distance. She claims that consolidation of these longest-haul rate bands makes sense because, as a result of divestiture traffic over these routes has become small compared to the shorter-haul rate bands.

Shantz testified that it is DRA's position that these intraLATA message toll-type services should reflect the shift in revenue requirement brought about by implementation of DRA's proposed intraLATA SPF to SLU transition and the direct assignment of costs for closed end intraLATA WATS which we adopted in D.87-12-067. Shantz also cautioned Commission against "dipping into the toll pot...in lieu of raising basic rates." He added, "[W]e must be very careful that the subsidy be made smaller so that if there is intraLATA competition authorized and the golden egg completely disappears you do not suddenly see very large increases in basic rates."

3. <u>US Sprint's Position</u>

US Sprint Communications Company (US Sprint) supports DRA's MTS rate design because it reduces rates in <u>all</u> mileage bands, and allows end users to share approximately equally in the benefits for reduced intraLATA toll rates, and because the DRA proposed rate design more closely reflects cost causation.

US Sprint asks us to reject Pacific's proposed revisions to MTS rates. It claims that the proposal has no basis in cost causation and is anticompetitive in that it is an attempt to position Pacific for potential intraLATA toll competition and to disadvantage potential competitors by attempting to set relatively low prices for the longer haul intraLATA toll routes which are most vulnerable to potential competition while increasing rates on short-haul intraLATA toll routes which are in Pacific's view least vulnerable to competition. US Sprint also claims that Pacific's proposal requires the users of short-haul and long-haul toll to pay disproportionate amounts in relation to the cost of service and adds that interexchange carriers (IECs) pay more to use the same facilities.

4. <u>CBCHA/TCA's Position</u>

In the event this Commission chooses to go forward with a rate design, CBCHA/TCA's witness Selwyn offers a proposal for

ZUM[4] expansion which increases the scope of applicability of ZUM rates, and thus decreases the scope of applicability of MTS rates and the revenue from toll-related services. Selwyn proposes that we adopt Pacific's proposal to consolidate ZUM Zones 2 and 3 but that we create a new ZUM Zone 3 for the 17-30 mile distance band. He adds that he does not object to Pacific's toll rate restructuring and toll rate reductions if his additional ZUM zone is adopted and the same rate differential which exists between Pacific's proposed consolidated 9-16 mile ZUM zone and the corresponding MTS rates is maintained between the additional 17-30 mile ZUM zone and corresponding MTS rates. Selwyn states that his proposal will more appropriately reflect the lower costs associated with metropolitan area calling and the traditionally lower levels of contribution expected from these fundamentally local messages, and will allow Pacific to more directly target its policies at reducing the potential for uneconomic bypass of the Company's message services. He states that the potential competitive threat to long-haul and nonurban intraLATA toll routes, (which US Sprint addresses), is minimal when compared with the potential for customer-specific alternatives within the more concentrated metropolitan areas. He adds that this conversion from MTS to the 30-mile extended ZUM zone would result in a net revenue reduction, before settlements, of $250 million. He claims that this figure should be lowered to $206 million to account for net revenues derived from the additional calling which this plan would foster.

5. Discussion

We agree with both Pacific and DRA that a reduction in the number of MTS rate bands is appropriate. Consolidation of the longer-haul mileage bands produces the simplification which Pacific

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4 Zone Usage Measurement, or ZUM is a discounted metropolitan toll plan discussed in detail in Section VI, below.

describes, and the flattening of rates for those bands should also produce usage stimulation. Scholl's Exhibit 260, Part 2, p. 7-10 shows projected MTS usage revenues exceeding costs by $740 million. It is clear that the proposals of DRA and Pacific will continue to provide a substantial contribution over cost, and it appears that the proposal of CBCHA/TCA's Selwyn would too.

Not being convinced of the equity of increasing short-haul toll so disproportionately to long-haul toll, we are not willing, however, to adopt the rate band consolidation which Pacific advocates and which CBCHA/TCA's proposal is premised upon. As we explain in our discussion of ZUM service, below, we wish to retain a distinct transitional rate zone between local service rates and toll rates. Pacific's proposal averages rates. While this is appropriate for some lower volume long-haul rate bands, it will make it more difficult to maintain ZUM rates distinct from local and toll rates, and it will not provide the users of the higher volume short-haul routes with the same level of control over their toll bills that they presently have. Such control includes choosing an optional calling plan best tailored to the customer's calling patterns as well as adjusting calling patterns. For these reasons we find Pacific's mileage zone consolidation unacceptable.

Nor are we convinced that it would be appropriate to shift revenue requirement from usage to access rates and from toll to local service in the manner proposed by CBCHA/TCA. Although much of our focus to date has been on the need to reduce toll rates to mitigate the potential for bypass, we wish to make it clear that our objective is not merely to craft a defensive strategy, but to achieve the broad range of benefits accruing from economic efficiency. Further, although the SPF-to-SLU reallocations reduce the revenue requirements attributed to toll services in particular, our concern is more generally focused on bringing all usage rates more into line with economic costs.

One sometimes forgets that even small consumers can benefit from reductions in usage rates which in large measure may offset increases in residence access line rates. In order for this to happen, however, the movement of rates toward economic costs must not be limited to those with bypass alternatives as is the CBCHA/TCA proposal, for a preoccupation with meeting competitive threats will leave out small users. Captive consumers are also entitled to the benefits of economic pricing.

As applied specifically to this proceeding, economic efficiency favors bringing rates more in line with economic costs for all usage rates, not merely long-haul toll usage rates. Particularly high contribution margins on long-haul toll routes may open such traffic to indirect bypass pressure even in the face of our intraLATA ban and may indicate a strategic need to adjust those rates. Aside from bypass threats, however, efficiency losses--that is, foregone benefits of calling in excess of the "true" costs of that calling--as a result of call suppression due to over-priced usage rates are of equally fundamental concern.

As we have acknowledged by our adoption of an intraLATA SPF to SLU transition plan, it is important to track intraLATA toll costs and one important reason is that such information will assist in setting rates which will allow Pacific to be in a position to compete should intraLATA toll competition be permitted in the future. At the same time, as US Sprint reminds us, it is important in any future competitive environment that Pacific not have an unreasonable advantage over its competitors. DRA's proposal, both for rate band consolidation and for rates, is fair in that respect. The principal appeal of this proposal so far as it goes, however, is not the fairness of its effect on potential future competition, but the fact that this proposal cuts the number of rate zones by nearly half, retains most of the present revenue to cost ratios, and still provides a zone configuration which will promote increased usage without disadvantaging today's short-haul customers.

While CBCHA/TCA's Selwyn advocates a policy based on economic pricing of MTS service, his proposal fails to consider the broader application of economic pricing which we believe is essential. In his recommendations for ZUM service Selwyn proposes moving toward more economic pricing by reducing the usage rates for ZUM service. As we discuss in Part VI below, we find some merit in this concept. Moreover, we believe that policy should also be applied to the analogous shortest MTS rate bands, those for 9 to 12 miles and 13 to 16 miles, in recognition of the policy concerns we have described above. With the knowledge that usage within these rate bands provides a substantial contribution, but absent more precise cost data, we conclude that it is reasonable to achieve these policy goals by adopting a modification of DRA's pricing proposal.

DRA had proposed only \$.01 reduction to the initial minute of MTS usage. This is but a token reduction in rates, as a 5-minute call in band 9-12 at current rates costs \$.49, but would only be reduced to \$.48 under DRA's proposed rates. A much more significant savings would be achieved by leaving the initial minute rate for toll bands 9-12 and 13-16 as-is and reducing the rates for <u>additional</u> minutes per call by \$.01. Under this rate design the band 9-12 call would cost \$.45.

We calculate that the application of this modest reduction in the rates for additional minutes of use will increase Pacific's revenue reduction for MTS from the \$46.860 million initially projected by DRA to about \$56.478 million if we adopt DRA's proposed rates for the remaining rate bands. Such a rate design provides an equitable way for Pacific to recognize the economies inherent in MTS service in the shortest, most heavily used rate bands, while benefiting all MTS users.

For all the reasons set forth we will adopt DRA's mileage zone consolidation proposal and we will adopt the rates set forth in its MTS rate band rate proposal shown in Appendix A, sheet 1 of 1 of Exhibit 348 (as amended to remedy a transcriptional error by Wilson by a letter to all parties dated February 18, 1987) except that we will retain the present rates for the initial minute of use for the 0 to 8, the 9 to 12, and the 13 to 16 mile rate bands and reduce the rates for additional minutes of use for these three rate bands by one cent.

C. Optional Toll Discount Plans

1. Pacific's Proposals

Pacific presently offers four optional calling plans which provide discounts for short-haul intraLATA usage services, both ZUM and MTS, for residence one-party customers. The first three, referred to as the Call Bonus Plans, are the Community Plan and the Circle Calling Plan which are limited to areas within 40 rate miles of the customer's home exchange and which were previously referred to as ORTS, and the group of Wide Area Plans which apply to toll calls throughout the customer's LATA. The fourth usage discount plan is called OCMS. It is also limited to a 40-mile radius of the customer's home exchange. Pacific proposes various changes to these services which it claims will result, on a test year basis, in a revenue decrease of $5.521 million for the Wide Area Plans and an overall revenue increase of $73,000 for the rest of the plans.

a. The Community Plan

For a monthly charge ranging from $3.60 to $8.55, depending on the rate mileage (9 to 40 miles), the Community Plan allows the subscriber to choose up to four communities in toll or ZUM areas within 40 miles of his or her premises (actually the home exchange or district area) to which discounted measured intraLATA toll rates plus a dollar amount allowance between $7.20 and $17.10, again varying with the rate mileage, will be applied. The customer may subscribe for double or triple allowances at comparable charges.

The mileage "Rate Steps" for both the Community Plan and the Circle Calling Plan correspond to the first six present MTS mileage bands (and the ZUM zones). The measured rate discount is 30% of the regular MTS rates.

The allowance for the Community Plan is double the flat monthly charge for the service. It is deducted from the discounted charges accumulated for calls to that exchange (or community) during the billing cycle. Thus, for example, a customer subscribing to a Community Plan for a community 18 miles from his or her exchange will be billed an additional $5.50 per month, for the 17 to 20 mile Rate Step, and will receive a 30% rate discount on calls to that community and an $11 allowance applied to those discounted charges.

Sullivan testified that Pacific proposes to keep the basic allowance at double the monthly rate and the discount at 30%, but to consolidate the Rate Steps into three steps, the last of which ranges from 31 to 50 miles, to be consistent with Pacific's proposed MTS mileage bands. Since this plan is restricted to communities listed in the tariffs and none of Pacific's routes is beyond 40 miles, this does not extend available service. Pacific also proposes deducting the allowance from the accumulated charges before the discount is applied, as is the case with Wide Area Plans. With these revisions Pacific projects a test year revenue increase of $661,000.

b. <u>The Circle Calling Plan</u>

For $4.75 per month the Circle Calling option provides the same 30% discounted measured intraLATA toll rates as the Community Plan, but without a usage allowance. However, the discount is applied to all toll/ZUM calls within the 40 miles (with certain exceptions such as where reciprocal availability is required). Sullivan testified that Pacific proposes reducing the rate for this service to $4.25 and also increasing the available radius from 40 to 50 miles to be consistent with the proposed rate band consolidation. Pacific projects a revenue decrease of $1.327 million due to these changes.

c. Optional Calling Measured Service

OCMS is a service which combines the time of day restrictions of the Wide Area Plan, below, the specific community restriction of the Community Plan, with unlimited free calling to the selected exchanges or district areas (communities) between those off-peak hours (8 p.m. and 8 a.m. on weekdays and all day Saturday and Sunday), and an allowance of one, two, or three hours of calling to that community at other times for a flat monthly rate (based on the Rate Step and time allowance selected and ranging from $4.50 to $27.00 per month). Peak hour calls to the selected communities beyond the subscribed-for allowance are charged at an overtime charge which is the same as the regular MTS rates for additional minutes. Other toll calls are charged under the regular MTS tariff. Only one OCMS service may be subscribed to for any particular service area, but the customer may subscribe to the service for several service areas. Customers in service areas where OCMS is available may also subscribe to a regular Call Bonus-Community Plan, but may not subscribe to the Circle Calling Plan.

Sullivan testified that OCMS is a form of Community Plan and stated that Pacific proposes withdrawing this service option and providing the present subscribers with Community Plan service instead. Pacific claims that withdrawal of this plan will result in a test year revenue increase of $739,000, which Sullivan seems to attribute to expense savings.

d. The Call Bonus Wide Area Plan

There are six permutations to the Call Bonus Wide Area Plan. Each is designed to provide a discount and two also provide a monetary allowance for all toll (and ZUM Zones 2 and 3) calls within the LATA so long as the calls are placed within the designated time frames. The allowance is applied to charges for calls placed within the designated time frames at undiscounted rates. There are two possible time frames, the first is for off-peak calls only. That is, calls placed between 11 p.m. and 8 a.m. weekdays (and all day Saturday and Sunday). This is called a basic hour plan. The second is for these off-peak times plus calls placed between 12 noon and 2 p.m. and between 9 p.m. and 11 p.m. on weekdays. This is called an extended hour plan. Thus there are three possible basic hour plans and three possible extended hour plans.

Sullivan testified that less than 7% of Wide Area Plan customers subscribe to the three basic hour plans, and he therefore proposes withdrawing those three plans and converting the customers to the comparable extended hour plans. He also proposes reducing the recurring charge for these three plans to the level of the basic hour plans (to $2.00, $4.00, and $6.00, from $2.75, $4.75, and $6.75) and changing the allowance for the $6.00 plan (the only plan which includes an allowance) from $8.50 to $8.00. The percentage discounts would stay the same. Based on its rate band consolidation and rate proposals Pacific projects the revenue impact of these changes for the test year to be a $5.521 million decrease.

2. DRA's Proposals for Optional Toll Discount Plans

Miller testified that DRA opposes all of the revisions to discounted ZUM/toll rates proposed by Pacific. Her testimony expresses a general opposition based on the fact that these services were the subject of our investigation of Pacific's marketing abuses. In addition to this general opposition Miller also expresses a specific objection to changes proposed for one of the optional toll discount plans, Circle Calling. Specifically she objects to the expansion of Circle Calling to 50 miles because the service is not available to all residence customers and is not available to any business customers. Miller contends that increased benefits should, wherever possible, be directed to all ratepayers rather than a selected few.

Miller argues that Pacific's proposal to withdraw its OCMS plan must be denied because this Commission specified, at Ordering Paragraph 14.b. in D.84-06-111, in Pacific's last rate proceeding, that future decisions concerning this service would be based upon the results of Pacific's study of subscriber usage of ORTS and OCMS and the degree to which these services merely divert usage from MTS rather than generating additional usage which otherwise would not occur. She asserts that the study Pacific submitted does not fulfill the requirements of D.84-06-111 necessary to the withdrawal of OCMS.

Although DRA's revenue-neutral scenario proposes no changes in Pacific's discounted ZUM/toll services, Miller testified that the changes it proposes in Pacific's MTS rate schedule would reduce annual revenue from the Wide Area Plan by $568,000 and would reduce revenue for the rest of these services by about $6.104 million based on DRA's assumption that the measured rate discount for the Community Plan and the Circle Calling Plan would be set at 30% of the effective MTS rate schedule, as is now the case. Miller's revenue figures are also based on our adoption of the DRA proposed MTS rates which we did adopt with one modification, above.

3. General Telephone's Position

As a general proposition the independent telephone companies (ITCs) do not have independent rates for intraLATA toll and toll-related services. Instead, they concur with Pacific's tariffs. For that reason these tariffs are of some interest to the ITCs. General Telephone Company of California presented John Jensik to address Pacific's rate design proposals, including optional toll discount plans.

Jensik states that Pacific's proposal for call bonus plans is an improvement over the existing plans. He endorses Pacific's proposal to eliminate OCMS and says that Pacific's proposal to reduce the amount of discount for the Community Calling Plan moves in the right direction, but he adds that General recommends withdrawing both OCMS and Community Calling, leaving Circle Calling as the only optional discounted toll plan. He bases this position on General's response to Ordering Paragraph 14.b. of D.84-06-111, which, he claims, shows that Community Calling Plans have been excessively discounted. He points out that under Pacific's present proposal Community Calling is still discounted more than Circle Calling. General argues that DRA's proposal promotes customer confusion caused by too many similar choices and retains excessive discounts for Community Plan subscribers at the expense of other customers.

4. TURN's Position

TURN contends that all Pacific's optional toll discount plans should be eliminated along with ZUM service and replaced with an optional flat rate metropolitan service. As explained elsewhere in this decision, we do not adopt the flat rate metropolitan plan at this time. Therefore, TURN's proposal for these other services is not addressed below.

5. Discussion

Pacific proposed the essential elimination of OCMS in its last rate proceeding and suggests it again here. In our decision in that last case we expressed our concern about the dwindling sources available for contribution toward the maintenance of low basic rates and our concern about the adverse impact on toll separations arising from our recognition of higher depreciation costs for Pacific, and concluded that it was necessary to diminish the preference in rate levels which has been allowed to ORTS and OCMS subscribers. We did so through the adopted rate design. However, we determined that it was inappropriate to discontinue the

OCMS offering at that time. Instead, we ordered Pacific and General to study subscriber usage of both OCMS and ORTS "toward the goal of determining to what degree each of these services merely diverts usage which otherwise would be priced at higher MTS rates and to what degree each service generates additional usage which otherwise would not occur, and also to determine the effects of each service on intercompany settlements and separation of revenues." (D.84-06-111, mimeo. at p. 224.)

Pacific admits that the sample size of its study, as to Circle Calling and OCMS at least, cannot represent a valid sample. Nonetheless, Pacific asks us to authorize the discontinuance of OCMS. In his rebuttal testimony Sullivan asks that we rely on a different study which shows that 81.85% of Pacific's OCMS subscribers would benefit from being reassigned to Community Calling Plans. He also asserts that the number of OCMS plans in service has decreased from 85,000 to 35,000 in less than three years. What he does not testify about, and what we still do not know, is what part of this OCMS usage is usage diverted from MTS and what part would not exist but for the existence of OCMS. Nor do we know what effect reassignment would have on these usage patterns. That is the information we asked Pacific to provide. Since it was not provided we will not grant its request to eliminate OCMS at this time. However, we invite Pacific to provide the information we requested in D.84-06-111 in our next review of its rate design, if it wishes further consideration of this proposal.

Pacific asks that the Community Plan monthly allowance be deducted from an <u>undiscounted</u> sum of charges to the selected community, rather than a <u>discounted</u> sum as is now the case. Pacific argues that this change will not result in a rate increase as DRA claims, but only a more rapid exhaustion of the allowance. That is true, it would be worth 30% less. That would mean that subscribers who now exhaust their allowance each month would either curtail their calling or continue their same calling behavior and pay more. Pacific has not studied the impact of such possibilities. The only basis for such a move that Pacific gives is consistency with the treatment of the allowance for the Wide Area Plan. We concur with DRA that the proposed change is inappropriate in the context of attempting to decrease MTS rates, and we are further concerned that its adoption might produce additional revenue which Pacific has not included in its revenue calculations. Therefore, we decline to adopt it. Obviously, we find even less merit in General's proposal to do away with the Community Plans altogether. General produced no evidence in this proceeding to support its proposal. The Community Plan rate design will remain unchanged.

Turning to Circle Calling, the question of whether to extend it to 50 miles is mooted by our decision not to adopt Pacific's rate band changes. There is no explanation of Pacific's proposal to decrease the monthly rate for this plan. Therefore, we will authorize no change in rate design for Circle Calling.

As with its OCMS proposal, there is some missing data in Pacific's Call Bonus Wide Area Plan proposal. It appears that reducing the choices from six to three in conjunction with the proposed rate reduction might reduce administrative costs and possibly benefit consumers. What we have not been provided, however, is information about the percentage and total number of customers who would be affected by having their allowance reduced from $8.50 to $8.00. Although it might be that the rate reduction of $.75 would compensate for that loss, the fact that this service was the subject of our marketing abuse investigation taken together with the paucity of data to support the Pacific proposal leads us to conclude that the Call Bonus Wide Area Plan rate design should remain in its present format. We will authorize no change in rate design.

Since we have adopted no changes in the Community Plan, Circle Calling, OCMS, or Call Bonus Wide Area Plan but have adopted the DRA proposal for rate bands and a modified form of its proposed usage rates, as well as decreases in ZUM rates, the revenue effect for these services will be a $11.688 million revenue reduction in the test year.

D. <u>WATS and 800 Service</u>

800 Service provides a reverse billing capability, so that calls of business customers to the subscribing business are charged to the business and not the customer. There are three plans. Full State and Half State plans are offered in conjunction with an IEC. The Metro plan is offered by Pacific and other local exchange carriers. Pacific's Sullivan testified that 800 service is priced above cost, but that the access and nonrecurring rate elements are priced below cost and supported by the hourly usage rate. Therefore, he recommends increasing the monthly access rate by 50% from $20 to $30 and also increasing the nonrecurring charge by 50% from $70 to $105. He further recommends reducing the Rate Group 1 (peak hour) hourly usage rates for Half State by 1.32%, from $15.20 to $15.00; for Full State by 30.23% from $21.50 to $15.00; and for Metro service by 20% from $12.50 to $10.00. Pacific would reduce the Rate Group 2 rates (off-peak hours: 9 p.m. to 9 a.m.) by the same percentages. The amounts corresponding to those above would be $6.08 to $6.00, $8.60 to $6.00, and $5.00 to $4.00. Pacific estimates that these rate changes will result in a revenue reduction of $11.067 million for the 1986 test year.

Pacific proposes rate changes in Outward WATS rates too. The proposals are for an increase from $25 to $30 in the access rate and a decrease in the first two steps of the four-step average hourly usage schedule. Thus Rate Group 1, for 0 - 5 average hours of use would be reduced by 9.09% from $11 to $10, and Rate Group 2, for 5.1 - 15 average hours of use would be reduced by 2.56% from

$9.75 to $9.50. Group 3 for average hours between 15.1 and 30 would remain at $9.00 and Group 4 for average hours over 30 would remain at $8.25. Pacific would also increase nonrecurring costs by the same amount as for 800 Service. Pacific projects that these changes would result in a $1.516 million revenue increase for the test year.

On behalf of DRA, Miller expressed opposition to any change in WATS rates or 800 Service rates, on the grounds that a rate increase in MTS and related services is inappropriate in the atmosphere of an overall revenue decrease. She also states that repression due to DRA's proposed changes in MTS rates under its revenue neutral proposal would decrease annual WATS revenue by $.478 million in the test year, but would have no effect on 800 Service revenues.

In his testimony General's Jensik states that General agrees with the direction chosen by Pacific regarding MTS and ZUM rate structure, noting that the proposed rate structure is easier to understand.

Pacific's Exhibit 260 lumps 800 Service and WATS together in its illustration of recurring access cost and revenue data and nonrecurring cost and revenue data projected for the test year, showing total recurring revenues of $39 million and recurring costs of $37 million, for a $2 million contribution; and nonrecurring revenues of only $2 million as opposed to costs of $15 million, for a net contribution of ($13 million).

Usage figures are separated for each service. They show 800 Service usage revenue at $110 million with costs of $34 million for a contribution of $76 million, and WATS usage revenue of $63 million with costs of $41 million for a $22 million contribution.

We agree with the principle of setting rates for both these services so that the access and nonrecurring charges cover their costs, assuming we know what those costs are. It appears that access is covering its costs, and that nonrecurring rates probably are not. However, we do not know how these recurring access costs and revenues and these nonrecurring costs and revenues are divided between the two services. Nor have we been informed of the rationale for the rate change proposals and how they will alter the revenue to cost ratios for these cost components.

Assuming that the 800 Service usage contribution of $76 million is in the ballpark, a revenue reduction of $11.067 million seems reasonable when reducing revenues is a goal. However, we are concerned that the focus of Pacific's rate reductions be to benefit the general body of ratepayers to the greatest extent possible. 800 Service rates do not directly benefit most consumers of toll-related services. Therefore, without a showing that such a revenue reduction is necessary to the viability and reasonable growth of this service, the present contribution level should remain. The record offers no suggestion why that contribution should be reduced. Further, there is no explanation for the rate design which essentially eliminates the category of Half State. For these reasons we agree with DRA's position that 800 rates should not be changed at the present. We will deny Pacific's 800 Service rate proposal. The adopted 800 Service rate design will result in no revenue effect.

Pacific's witnesses also offer no explanation for its proposal to change its WATS rates. As we have pointed out, so far as we can ascertain from the joint data, recurring rates already produce revenue to cover costs. We are not inclined to authorize this WATS proposal without some justification on the record. The WATS proposal is denied. The effect of the adopted MTS rate design, however, will be a $0.527 million WATS revenue reduction.

VI. Other Toll-Related Services

A. Pacific's Proposed ZUM Expansion and Other Changes

ZUM is a measured rate plan which is provided to all customers in designated metropolitan areas. It provides rates for two mileage bands beyond the local calling area which are set at about half the rates for message toll service (MTS) calls to analogous rate bands, i.e. the 9-12 and the 13-16 mile zones. In ZUM parlance these zones are respectively designated ZUM Zone 2 and ZUM Zone 3. ZUM service is designed to recognize the economies of volume which exist in these high density areas. It further recognizes that the very urbanization which is exemplified by these economies of volume is also exemplified by communities which spread from their centers and merge with adjacent communities thereby increasing the likelihood that the customer will utilize basic services within a wider area than the local calling area. In other words the customer's community of interest is no longer restricted to the area that forms her or his local exchange. Thus, the goal of ZUM service is to allow customers in urban areas to communicate with others in their more extensive community of interest at an affordable rate.

1. ZUM Expansion

Pacific proposes to expand its ZUM rate plan on the periphery of the San Francisco-East Bay Extended Area to add 12 exchanges. In addition Pacific proposes structural changes in the 39 exchange or district areas affected by this expansion. These changes include one consolidation, two divisions, relocation of six rate centers, and the elimination of two district area designations. The result of these changes will be that eight local routes will become nonlocal and seven nonlocal routes will become local. DRA supports Pacific's ZUM expansion proposal. No other party takes a position on this issue. We agree that the criteria

Pacific used to determine the applicability of ZUM to these new areas was appropriate and the characteristics of the areas warrant ZUM expansion. We will authorize the adoption of Pacific's proposed ZUM expansion.

Based on its proposed rates and charges Pacific claims that this ZUM expansion would result in a revenue reduction of $4.521 million in the test year. Considering the rates which we have actually adopted in this decision, the test year revenue effect of this ZUM expansion is a negative $6.252.

In addition to the ongoing revenue effects of this ZUM expansion, Pacific has asked this Commission authorize a one-time implementation cost of $1.13 million for the test year. DRA's Shantz opposes the request, explaining that the costs of [implementation] activities such as bill inserts and order processing are embedded in the historical data upon which the adopted results of operations is based. He adds that these activities normally occur as a part of the implementation of the rates and charges adopted by the Commission in a major rate proceeding. We find no support for this proposition. We will authorize adoption of Pacific's $1.13 million ZUM expansion implementation costs (which equates to $.8 million in revenue).

2. **ZUM Zone Boundary and Rate Change Proposal**

According to Pacific's rate design witness, G. J. Sullivan, Pacific proposes doing away with separate ZUM Zones 2 and 3 and replacing them with a single designation and a single rate. This is parallel to the MTS rate band consolidation proposal which we discuss in Part V, above. Presently in the areas where ZUM service is provided ZUM Zone 2 rates are charged for calls between 9 and 12 miles and ZUM Zone 3 rates are charged for calls between 13 and 16 miles. (The Zone 3 tariff is applied to calls between 12 and 13 miles.) Pacific proposes consolidating these zones and charging a new tariff for all ZUM calls between 9 and 16 miles.

Presently a 5-minute Zone 2 call costs $.20 and a 5-minute Zone 3 call costs $.30. Under Pacific's proposal either call would cost $.21. In addition, Pacific proposes distinguishing between business and residence rates for local calls (ZUM Zone 1) in areas where ZUM rates are in effect. The result is that a local call which is now measured at 4 units for the first minute and one unit for each additional minute would continue to be measured the same way for residential service, but would be counted as 4.3 units for the first minute and one unit for each additional minute for business service. No such distinction is proposed for calls between 9 and 16 miles, i.e. the new consolidated Zone 2.

DRA's Shantz describes Pacific's proposal as an attempt to subject the short-haul user to unreasonable increases in short-haul usage charges consistent with Pacific's past proposals to change the ZUM concept of providing a rate transition from local usage to message toll usage. DRA is concerned that this ZUM zone change is the first step in an attempt to do away with the concept of ZUM as a transitional phase with rates set at levels between local and toll rates. This is part of a plan, as DRA sees it, for Pacific to increase short-haul toll rates in order to decrease long-haul rates to be more competitive in the event this Commission permits intraLATA toll competition in the future.

As described in our discussion of MTS rates, above, CBCHA/TCA's Selwyn supports the consolidation of ZUM Zones 2 and 3 but urges that a new Zone 3 be established to cover distances between 17 and 30 miles. CBCHA/TCA argue that California does not recognize the fundamental distinction between calling within a metropolitan area, with its economies of volume, that it ought to recognize. As a consequence, they argue, much "local" calling in metropolitan areas, most of which is usage, is priced at toll rates. Since toll rates have historically been a source of subsidy to basic exchange service, local <u>usage</u> is, in their view, inappropriately subsidizing the cost of local <u>access</u>. According to

CBCHA/TCA's witness, Nancy J. Wheatley, their proposal would result in a net reduction in MTS revenue of about $206 million. CBCHA/TCA argue that implementation of this proposal "would provide a healthy stimulus to the use of the network by local subscribers." Much of this shortfall would be recovered from the increases CBCHA/TCA propose for basic exchange rates which are discussed above.

Selwyn used various Pacific workpapers to produce calculations which he claims indicate that the total annual cost for measurement and the provision of detailed billing of measured local and ZUM Zone 1 calling is $77.5 million. He goes on to state that the total annual cost for these measured services, based on Pacific's workpapers, is $447.1 million, but that it would be only $369.6 million if Pacific did away with measurement and simply provided flat rate service. Using rather speculative data Selwyn also calculated that the costs of detailed billing and measurement of ZUM Zones 2 and 3 calling is $37.9 million out of a total cost of $157.8 million. He concludes that the cost Pacific incurs to measure local calls and to provide detailed billing for local and ZUM calls may be impeding greater use of the network, and he therefore additionally urges this Commission to scrutinize this question of the propriety and value of local measured service.

Pacific opposes Selwyn's proposed ZUM mileage band expansion, stating that it seems out of harmony with the Commission's policy objectives and claiming that its own proposal is the most balanced and represents the greatest benefit to the general body of ratepayers. Based primarily on its study of savings which would result through offering detailed billing of ZUM messages only as an optional service in response to Ordering Paragraph 15.c. of D.84-06-111, Pacific also opposes Selwyn's proposal to eliminate detailed ZUM billing, stating that his cost figures are highly exaggerated as a result of his assumption that difference between the cost of a flat rate day period call and a similar measured call is due entirely to the measurement costs of a measured call. Scholl testified that this difference is largely due to time of day distribution, rather than measurement costs. Further, Scholl pointed out that his workpapers show measurement costs to be less than half that estimated by Selwyn. Finally, Pacific argues that detailed ZUM billing assists customers in understanding and controlling their telephone charges and allows customers with low usage to receive service at less than the flat rate.

DRA states that adoption of Selwyn's proposal would be unfair to rural, nonmetropolitan customers and would unjustly provide exchanges in the San Francisco-East Bay Extended Area and certain exchanges in the Los Angeles Extended Area with rates which are inequitable when compared to the exchanges in the Orange County Extended Area and the San Diego Extended Area.

3. *Discussion*

While the pricing structure Pacific proposes for its simplified ZUM configuration has some appeal, we must agree with DRA that this scheme moves in the direction of obscuring the transitional quality of ZUM. We agree with DRA and CBCHA/TCA that it is important to retain a clear pricing distinction between local and toll calls of similar distances. As we said in our last Pacific Bell rate decision:

> "[T]here are significant differences between ZUM service provided in a metropolitan area and short-haul toll service provided elsewhere in PacBell's service area. The differences are matters of averages: The typical ZUM route is denser and provides service more efficiently than the typical MTS route." (D.84-06-111, mimeo. at p. 246.)

We do not agree with CBCHA/TCA, however, that it is reasonable to consolidate the present ZUM zones and add a new one thereby decreasing revenues by over $200 million in order to redefine the community of interest of callers in high density urban areas. In actuality a community of interest clearly differs from customer to customer. The scope of the ZUM discount does not coincide precisely with the calling patterns of all callers in these highly urbanized areas, nor should it. Our ZUM policy attempts to strike a balance in setting rates which will provide the ratepayer with a reasonably defined calling area for meeting his or her basic local calling needs at relatively low rates. That is what we mean by "community of interest." There are clearly many ratepayers in urban areas who regularly make calls well beyond 16 miles. It cannot be stated without qualification that none of these calls should be regarded as the type which ought to constitute basic local service. Selwyn's proposal, however, would adversely impact on other important policies, such as keeping basic service prices at reasonable levels, by unduly burdening rates for the basic area of local service in order to increase the benefit to ratepayers making calls to farther points. Therefore, we conclude that the present ZUM boundaries ought to be retained. We decline to adopt Selwyn's proposal to extend ZUM boundaries or Pacific's proposal to consolidate ZUM Zones 2 and 3. We will direct Pacific to maintain its present ZUM zone definitions.

Turning to the issue of economic pricing raised by Selwyn, we agree that the underlying costs of providing local and metropolitan service can be kept lower than the costs for comparable nonmetropolitan service, due to increased traffic-handling efficiencies. The reduction in the cost of ZUM rates is an equitable step which should be taken now both to recognize this cost advantage and to recognize the decrease in the value of basic exchange service due to urbanization. However, as we said above in our discussion of MTS rates all consumers should benefit from reductions in usage rates. Selwyn's proposal provides a disproportionate benefit to large users, and a disproportionate basic rate increase to small consumers.

It is appropriate to recognize both the lower relative costs and the community of interest for the majority of metropolitan callers but neither Pacific's nor CBCHA/TCA's proposals equitably distribute cost savings in the context of a reasonable reduction of usage rates. Adoption of the same moderate usage rate reduction for additional minutes of use for ZUM Zones 2 and 3 that we have adopted for the analogous toll rate zones would accomplish this policy goal and continue to allow Pacific's ZUM service to provide a contribution. In fact, a reduction in these usage based rates also have the potential for greater revenues, as lower rates may cause a relaxation of usage suppression. Under such a rate design a ZUM Zone 2 call would cost $.26 rather than $.35 for a 10-minute call. Therefore, we will direct Pacific to retain its present ZUM pricing schedule, except that the rate for additional minutes of use will be treated analogously with that we have adopted for the first two MTS rates bands. We calculate that this change will decrease ZUM revenues by $30.531 million in the test year. We are not convinced of the need for different ZUM rate treatment for business and residence service as Pacific requests, and will therefore not adopt it. The rates we adopt here will apply to both business and residence ZUM.

We are satisfied with Pacific's Ordering Paragraph 15.c. study results and conclude that the costs of ZUM measurement are not so great as to outweigh the benefit to customers. Therefore, we will not adopt Selwyn's proposal to eliminate ZUM measurement.

B. <u>General's ZUM Expansion Proposal</u>

General's witness Jensik testified that General disagrees with Pacific's proposed ZUM expansion to the extent that Pacific has failed to propose expansions to many areas in LATA 5 and LATA 1, specifically as it affects General's customers in the San Bernardino, Redlands, Thousand Oaks, and Oxnard regions. Therefore, Jensik asks that the Commission order Pacific and General to file a plan to expand ZUM to include certain Pacific and General exchanges shown in Attachment 1 to Exhibit 384. He makes this proposal because General cannot file for ZUM expansion unilaterally in most locations since the ZUM tariff is a Pacific tariff in which General concurs and since Pacific must be involved to assure customer benefits and acceptance by keeping calls priced equally in both directions over common routes.

DRA responds to General's request by noting that at least three of the exchanges included in General's proposal are Continental Telephone Company of California (Continental) exchanges which therefore require Continental's participation, and by raising the issue of providing notice and an opportunity to be heard to affected ratepayers. DRA concludes that the issue should be heard in Pacific's next general rate proceeding. Pacific suggests that the appropriate forum should not be its next rate proceeding, but a separate application by any of the affected telephone utilities. Pointing out that General's recommendation encompasses several nonmetropolitan areas, which have not previously been deemed appropriate for ZUM expansion and also encompasses an alteration in ZUM availability criteria, Pacific adds that a proper analysis of the relevant issues will take 8 to 12 months. Pacific also claims that the parties should not be limited to evaluating General's proposals, but should be free to propose alternatives. General argues that Pacific's time estimate is greatly exaggerated, that the investigation and analysis, including that for the small number of Continental's affected exchanges, could be completed in 90 to 120 days, that the proposals of these other parties will unnecessarily delay needed beneficial changes, and suggests that the matter be taken up in General's ongoing general rate proceeding, A.87-01-002. In the alternative General supports the Commission's filing in the near future an OII with regard to ZUM expansion.

Since these arguments were presented General has unsuccessfully attempted to add this issue to A.87-01-002, its pending general rate proceeding. The denial of that further issue was appropriate. We believe that the issue is best raised in an

OII. It need not be a new one, however. Since I.87-02-025, which has been consolidated with A.87-01-002, is already open and all the relevant parties are respondents to it, a later phase of that proceeding will provide an appropriate forum to address this issue. Before that phase commences, however, the parties must have an opportunity to study General's proposal, notify potentially affected customers, and prepare alternative proposals. Therefore, we will order that this issue be heard in a later phase of I.87-02-025. The burden of proof of the feasibility of this proposal will not be altered by the forum in which it is to be heard. It will lie with the plan's proponent. The timing of this proceeding should be worked out by the parties in a prehearing conference.

C. TURN's Metropolitan Flat Rate Proposal

1. The Costs and Benefits Study

TURN proposes the addition of an optional metropolitan flat rate service and the elimination of ZUM (and other metropolitan rate options discussed in Part V of this decision). In making this proposal, TURN refers to Exhibits 294 through 296 which describe the results of the cost and benefit study regarding the establishment of residence flat rate metropolitan calling plans offering unlimited residential calling without charge in all or portions of the San Francisco-East Bay Extended Area or the Los Angeles Extended Area, which we required Pacific to conduct by Ordering Paragraph 16(b) of D.84-06-111.

Pacific's study involved offering one of three plans to different customers in selected prefixes in each of the extended areas between May 1 and December 31, 1985. Plans 1 and 2 each offered a choice of Metropolitan ZUM, which allowed residence customers unlimited usage on their ZUM Zones 2 and 3 routes for a fixed monthly rate, or Metropolitan Extended Area (EA), which offered unlimited usage throughout a wider extended area. Plan 3 only offered the ZUM choice. Pacific defines an extended area as an aggregation of exchanges within a geographical area that has ZUM. (Exhibit 295, part 2, p. 1.) The plans and price options were as follows:

<u>Flat Rate Plans</u>

	ZUM Option	EA Option
Plan 1		
8:00 am - 5:00 pm	$10.00	$35.00
5:00 pm - 8:00 am	5.00	25.00
24 hours	15.00	60.00
Plan 2		
8:00 am - 5:00 pm	$15.00	$45.00
5:00 pm - 8:00 am	10.00	35.00
24 hours	25.00	80.00
Plan 3		
8:00 am - 5:00 pm	$15.00	N/A
5:00 pm - 8:00 am	10.00	N/A
24 hours	25.00	N/A

2. <u>Pacific's Findings</u>

Pursuant to D.84-06-111 Pacific's study contains findings on the issues set out below.

a. <u>Extent of Subscriber Interest</u>

Exhibit 295 states that the flat rate trial plan was offered to over 91,500 residence customers and that over the eight months of the plans' existence 302 customers purchased one of the ZUM plans and 274 purchased one of the extended area (EA) plans. This breaks down to a net subscription rate of .88% or about 9 subscribers per 1,000 customers offered the plans. The subscription rate for EA was somewhat higher, at .50%, than the subscription rate for ZUM plans at .38%. Further, the study shows that price level significantly influenced both the EA and the ZUM plan subscription levels. The ZUM subscription rate for the higher priced plans was approximately 20% of that for the lower priced plans, and the EA subscription rate for the higher priced plan was approximately 75% of that for the lower subscription rate plan. Still, the subscription rates disaggregated by price are only 1.22% for lower priced offerings and .57% for the higher priced offerings.

Pacific's Sullivan argues that the rate of subscription to the trial plan was so low as to suggest that there is no significant unmet consumer need, and adds that the Circle Plan already offered by Pacific has similar geographic boundaries to the metro plan. He also argues against the implementation of such a plan based on the findings of the the post-trial survey of about 300 of the trial plan's purchasers, the results of which are set out in Attachment 4 to Exhibit 400, which shows that they are different from Pacific's typical customers in that they are older, have a higher level of education and income, are more often self-employed, are more likely to have more than one telephone number in their homes, are more likely to own personal computers with modems, and are more likely to conduct business-related or paid work from their homes.

b. Effects on Pacific's Revenues and Costs of Service

The study found that customers subscribing to EA plans increased their usage by 317.5% with 24-hour EA subscribers increasing their usage most at 468.8%, while ZUM subscribers increased their overall average usage by 31.5%, with a high of 36.8% for the daytime plan. Pacific's final report on this study states that during March 1985 trial participants used 100% more minutes, initiated 80% more messages, and generated 47% more revenue for Pacific Bell than did typical customers. (Exhibit 400, Attachment No. 4 at p. 23.)

The study compared the cost of subscribers' pretrial usage to Pacific's revenue breakeven point for ZUM and EA services and found that 79.9% of EA subscribers were, pretrial, below the breakeven point and that 58.6% of ZUM plan subscribers were below. The study then compared usage during November of the period and found that only 31.6% of EA subscribers were below the breakeven point, but the percentage of ZUM subscribers rose to 68.2%.

With such levels of subscription, Pacific projects an overall change in revenue requirement for 1987 ranging from a decrease of $19.12 million for the ZUM Plan 1 option to an increase of $9.28 million for the EA Plan 2 option.

Although its study shows that implementation would generally increase revenue and encourage increased metropolitan usage, in assessing long-term risk Pacific claims that the profitability of flat rate plans depends on a balance of subsidy flow among subscribers below and above breakeven points, and that the study indicates that low-end users who provide the subsidy increase their calling the most, thereby generating both incremental revenue and the majority of costs so that the subsidy from these subscribers decreases.

Pacific reports that the trial showed a trend for customers below the breakeven point to drop their plans (17.4% of total subscribers), and also claims that flat rate plans are riskier than Call Bonus plans based on allowances and discounts because costs under flat rate plans increase substantially since calling increases, but revenues do not increase proportionately. Thus, Exhibit 295 shows lower revenue to cost ratios for both Plans 1 and 2 than would exist without the plans.

In his rebuttal testimony, Exhibit 400, Sullivan asserts that the flat rate structure of this plan is inherently unfair, because it divides subscribers into two distinct groups - one which subsidizes the other. He states that the resulting profitability thus becomes dependent upon customers who do not benefit subsidizing those who do.

c. <u>Appropriate Rate Levels to Avoid Diminution in Net Revenues</u>

We issued a Supplemental Opinion, D.85-02-030, after the issuance of our last Pacific Bell general rate decision, in order to review Pacific's plans for conducting certain cost studies which we had ordered, including the optional metropolitan flat rate study. We explained that it was not our intention to approve the precise terms of the various study plans, but to address criticisms which went to the heart of the study plans, raising questions whether the studies as proposed to be conducted would provide at all the sorts of information which the Commission sought by Ordering Paragraph 16 [of D.84-06-111]. In that cost study review proceeding TURN urged us to require Pacific to set the total price for 24-hour metropolitan calling plans to begin at no more than $25. We found that such a price ceiling apparently is inconsistent with the avoidance of net revenue loss, and is therefore inappropriate. The lowest price offered for 24-hour EA service in this study is $60 per month.

Pacific's Exhibit 295 does not explain how it arrived at the prices it selected for this study. It merely states what prices it chose to test. According to Table A2.1, the total amount of revenue generated by implementation of the plans was $5,072 per month. This revenue results from gains of $5.01 or 67.9% per month from the average ZUM subscriber and $22.62 or 127.8% from the average EA subscriber, and these figures average the much higher subscription rate of Pacific's lower priced Plan 1 offerings with the lower subscription rates of its higher priced Plan 2 and Plan 3 offerings.

d. <u>Effects on Separations and Settlements Arrangements</u>

Pacific's study includes the projected results of the effects of the plans for 1987, 1988, and 1989, including effects of the plans for the intrastate revenue requirement after settlements with the independent companies. It indicates that the intrastate revenue requirement would range in 1987 from a decrease of $12.49 million for ZUM Plan 1 to an increase of $5.88 million for EA Plan 2.

e. **Cross-elasticities of Demand With Other Optional Discounted Services**

The final report found that trial participants were much more likely to have an optional calling plan before the trial than were typical customers. For example, 46% of trial participants had some optional calling plan while only 28% of typical customers had one, and 15% of trial participants had circle calling while only 2% of typical customers had it. By far the greatest predictor of participation in this trial was heavy pretrial usage.

3. TURN's Position

TURN points out that Pacific's exhibits show that virtually every version of the flat rate metropolitan service made money for the utility, while encouraging customers to increase their metropolitan calls and that Pacific found that the 5:00 p.m. to 8:00 a.m. extended area plan was the most popular among customers. TURN concludes that flat rate metro plans can be a profitable way to increase calls during the relative slack evening hours. TURN's witness Siegel recommends that an EA-wide service plan available from 12:00 noon to 8:00 a.m. weekdays and all Saturday and Sunday at $15 per month should be implemented.

TURN argues that service enhancements such as the flat rate metropolitan plan increase absolute usage and thus Pacific's revenues, and sees arguments about which customers pay what portion of the revenue increase as irrelevant since according to the data correlating existing optional calling plans with income such service enhancements are targeted to well-heeled customers as a way to attract more of their disposable income to profitable telephone services. TURN disputes Pacific's interpretation of the significance of the subscriber interest statistics Sullivan cites and concludes that the response to the metropolitan plan does show an unmet need.

4. Discussion

TURN's proposal for a trial metropolitan flat rate is apparently intended to safeguard residential ratepayers from our increased loading of marginal costs onto the monthly rate. However, its flaws cannot be overlooked. Pacific's cost study clearly demonstrates that revenue to cost ratios for the plans are much lower than the revenue to cost ratios for present discounted toll options, thus exposing Pacific to more risk of revenue shortfall from these plans, especially if those subscribers below the breakeven point continue to drop their plans.

Further, while we are not particularly concerned to learn that this service is more appealing to people who are better educated and make more money than the average subscriber, we are concerned with the fact that the cross-elasticity of demand between flat rate metropolitan service and present optional calling plans, particularly circle calling, is very high. If significant numbers of customers were to simply switch from another optional calling plan to this one the overall revenue increase would be eroded considerably.

We are also concerned with the possibility, as indicated at page 14 of Pacific's final report, that 36% of the trial customers, but only 14% of typical customers do paid work or business at home frequently or occasionally; and the further indication that 52% of this subgroup of trial customers use the telephone frequently while working at home. These statistics seem to support Pacific's concern that this plan might be used in place of basic business service and thus negatively impact Pacific's revenue from business services.

While it is true that Pacific's study indicates that a flat rate metropolitan plan could increase Pacific's overall revenue, at least in the short run, the limited appeal of the offering coupled with the strong likelihood that the plan will lead to a reduced subsidy source, the fact that the overall subscriber interest is lower than that for the present discounted toll options, and the fact that the particular flat rate metropolitan plans with the highest subscriber interest show projected overall revenue requirement increases, lead us to conclude that the risks of adopting a flat rate metropolitan plan at this time exceed the benefits to ratepayers and are not a reasonable way to recognize the economies of scale stemming from heavy users of the shorter range intraLATA long distance services while assuring that the program for recognizing those economies continues to provide a contribution over costs. Our adoption in this decision of usage rate decreases for MTS and ZUM services already accomplishes this goal with less risk. We will deny TURN's proposal.

D. Foreign Exchange Service (FEX)

FEX Service is telephone service which has dial tone and access to the network provided from an exchange or district area other than the one in which the customer's premises are located. It consists of a basic exchange access line plus network facilities connecting the customer's home central office to the remote central office of the customer's choice. There are three different ways that Pacific can provide this service. It provides each subscriber with service using whichever method it deems to be least costly.

The most common is called the Line Haul method. It uses a private line channel to connect the subscriber's serving central office to a central office in the desired distant exchange. The second method is the Dedicated Prefix method in which an office in one exchange is made to appear as though it were in another exchange through a billing arrangement (often referred to as a Dedicated NNX) and no private line channel is required. Dedicated prefixes exist only in central offices where Pacific has experienced a large enough demand for FEX service to another specific exchange to justify the dedication of a substantial portion of a central office switch and a large block of telephone numbers to that service. The third method is called the Cross Boundary arrangement. It connects a customer's premises directly to a central office in a contiguous exchange. This is a very infrequently used method which requires that the customer location be close to the exchange boundary. Additionally, there is one permutation with characteristics of both the Line Haul method and the Dedicated Prefix method, called the Hybrid Line Haul. In this configuration the customer's serving central office is not a Dedicated NNX office, but there is one close by, then a private line channel is installed from the serving central office to the Dedicated NNX office.

1. Pacific's FEX Proposal

At present FEX subscribers pay a specified rate for FEX service which varies based on whether they are residence or business subscribers, whether their business service is measured line or trunk, whether their residence service is flat, measured or party-line, whether the service is to a noncontiguous location, and, in some instances, whether service is in exception rate areas. Pacific proposes retaining these distinctions, but unbundling rates so that each rate has the same access component and usage component as basic local residence or business service plus a new FEX increment component.

Sullivan proposes setting the residence flat FEX increment at $6.75 per month, the measured residence increment at $4.05, and the business increment at $11.25. He also proposes continuing the present policy for determining the mileage used in setting certain rate levels. He explains that the proposed FEX rate elements are not increases, but simply the difference between the current FEX rate and the current rates for flat and measured service. When they are added to the access and usage rate increases Pacific has proposed for basic local residence and business service, the overall effect is an increase in rates for FEX subscribers.

In its last general rate case Pacific proposed limiting or "grandfathering" the offering of FEX service to existing subscribers. In addition to the described unbundling of rates in the present proceeding, Pacific again proposes grandfathering this service, for both residence and business FEX customers by limiting it to existing subscribers at their existing premises and existing class of usage service. In explanation of this aspect of its proposal, Pacific contends that the ratio of revenues to historical costs of FEX access, service connection, and mileage will show huge shortfalls in the test year. Sullivan cites examples ranging from 10% to 40% at current rates.

Pacific asserts that the extent of FEX demand is attributable to the inordinate discount it provides over toll services; and goes on to claim that stimulation of that demand in light of the poor financial performance of FEX is not sound ratemaking policy. Sullivan explains that it is Pacific's objective to ultimately replace this service with software-based services priced at compensatory levels. He contends that the proposed grandfathering is reasonable because there are enough optional calling plans and other substitutes for FEX available to new subscribers so that the growth of FEX can be eliminated. By way of example he points to ZUM expansion in the San Francisco-East Bay area which will eliminate some FEX needs, and to possible boundary realignments. Pacific also mentions Call Bonus plans and Remote Call Forwarding (RCF) as possible solutions for residence customers, and 800 Service and WATS for business customers. Pacific claims that RCF is a complete substitute for incoming FEX calling, but acknowledges that while there are means of achieving substantial toll discounts, there is not yet a direct substitute for all the outgoing calling components of FEX. It contends, however, that utilization of the available alternatives are preferable to FEX service at the extremely large price increases which Pacific's cost evidence demonstrates would be necessary to make them fully compensatory.

2. Positions of Other Parties

No other party which addressed the FEX issue disagrees with Pacific's proposal to unbundle FEX rates, but every other party which addressed the issue disagrees with its grandfathering proposal.

a. General

General's Jensik testified that General and other local exchange companies in California concur in Pacific's tariffs for FEX service. He objects both to Pacific's grandfathering FEX service and to its freezing rates at present levels. Instead, General proposes continuing the FEX offering, but moving prices toward cost. Jensik does not address residence FEX service, only business FEX service.

Claiming that all FEX service requires connecting a private line from a location in one exchange to a dial tone in another, he recommends that FEX rates should be consistent with the rates for private lines, plus dial tone [access] rates for business. Based on this model he goes on to recommend that a local channel termination rate be charged at the local loop end and usage be charged at the dial tone end. He states that where measured service is not available at the dial tone (open) end that the difference between the individual business line flat rate and the individual business line measured rate be charged.

Jensik added that his proposal arises in part from the incompatibility of Pacific's private line tariff structure with the one General has proposed in its pending general rate proceeding, and in part from General's view that the emerging competitive telecommunications marketplace makes it more necessary for these companies to be independent of one another in their pricing and selling of local exchange services. Intercompany settlements procedure for private line, including FEX, would be replaced by a "bill and keep" approach. Further, he proposes that for intercompany FEX service the companies use meet point billing to bill for the interoffice private line, i.e. the portion in General's territory would be billed at General's rates and the portion in Pacific's territory would be billed at Pacific's rates.

b. CBCHA/TCA

Selwyn opines that in addition to there being no direct substitute for FEX outward calling, as Pacific acknowledges, neither 800 Service nor Remote Call Forwarding provides an adequate substitute for inward business FEX service, i.e., service which provides a means for a caller from the distant exchange to place a local call to the FEX business subscriber. He explains that 800 service does not allow a business to create a "presence" in a distant market area in that it implies to the customer that wherever it was that they were calling was located at some distance from their own community.

Selwyn's only objection to Remote Call Forwarding as a substitute is that the MTS charges associated with the use of the service would be much higher than the access line and mileage charges for FEX service, assuming that there is some reasonable level of traffic to the remote location.

Selwyn asserts that the need for the magnitude of the loop costs which Pacific assigns to FEX service is questionable at best. He states that about $35 of the monthly loop expense for business FEX circuits which Scholl's workpapers set at $85 is associated with design and testing costs. He states that these design costs are associated with the claimed need to provide additional circuit equipment in order to achieve adequate transmission characteristics on the circuit and argues that there is little need for such "design" of FEX lines since the nature of FEX line usage is more likely to be limited to the immediate area around the exchange where dial tone is provided, with little if any use of toll or other long-haul connections where transmission losses in the line would be expected to have the greatest adverse effect. He also argues that FEX subscriber loops are not longer than average subscriber loops, but that since the need for design of a loop is associated with loop length, the costs Pacific attributes to these loops are too high. Selwyn also claims that Pacific's FEX testing costs are entirely unreasonable.

Finally, stating that Exhibit 287, Pacific's revenue impact workpapers, show no offsetting revenue increase for other services resulting from stimulation due to the grandfathering of FEX, Selwyn asserts that Pacific has either materially understated the revenue effect of its FEX proposal or else it is the case that there are no present alternatives to FEX service and the functions now provided through FEX will no longer be available to new customers. He concludes that Pacific's grandfathering proposal must be denied or at least this Commission must impute offsetting stimulated revenues equaling the $47 million revenue loss Pacific claims will be due to FEX grandfathering.

In his rebuttal testimony Pacific's Scholl testified that Selwyn's assertion that FEX loop length indicates that the need for "designed" access lines (i.e., lines with additional transmission equipment) is overstated is premised on a false assumption, and that while the PBX loops to which Selwyn compares this cost element are only designed when loop resistance is great, FEX service requires designing whenever an interoffice facility is required to provide the service (e.g., whenever the 'line haul' serving arrangement is required). He adds that this is the case for 67% of FEX lines. Scholl specifies that the elements of this design process are the assignment of the interoffice facility and the associated central office service area transmission equipment. Thus, Scholl asserts that the recurring costs for designed circuits which Pacific assigns to FEX are not overstated.

c. Centex

Centex describes itself as a communications manager for small and medium sized businesses which assists its clients in forming joint user groups, which enables them to qualify for service options not otherwise available to business customers of their size. Centex explains that its interest in FEX service is based on its clients' use of the service for outward calling.

Centex presented the testimony of Stephen E. Siwek, a telecommunications consultant, with degrees in economics and business administration. Siwek asserts that Pacific's grandfathering proposal should be rejected because its arbitrary customer disaggregation will stimulate inefficient consumption patterns and fails to let the mechanism of market selection function, leaving customers and the company less well off. (See generally Exhibit 370.)

Centex concurs with Shantz and Selwyn that there are no adequate alternatives for business FEX service, particularly outward calling. Centex cites Exhibit 403, the final report of Pacific's Special Services Administration Task Force (SSA Task Force), which was received into evidence very late in this proceeding. The document describes possible alternative FEX provisioning to reduce costly line haul. These include creating additional dedicated prefixes, where cost justified, creating shared dedicated prefixes, and the use of 2-Number FX.

Centex points to Scholl's testimony that shared dedicated prefixes have the advantage of permitting the assignment of just 1,000 calling numbers to a particular central office, rather than the dedication of a block of 10,000 numbers which the present dedicated prefix requires. Scholl also testified that Pacific was having difficulty in interfacing such a plan with interexchange carriers. The report explains that 2-Number FX would use a combination of Remote Call Forwarding and a redesign of Pacific's present billing system, called Front End Guide, which would allow the provision of both FEX service and conventional local service on a single line.

Centex asserts that the possibilities for Pacific provisioning FEX service more efficiently and in a less costly manner in the future as described in the SSA Report underscore the unreasonableness of permitting this service to be grandfathered and, like Selwyn, urges that we concentrate instead on appropriate pricing.

In its concurrent opening brief Centex moves for the admission, as a late-filed exhibit, of a Response to Transcript Request which it received after these hearings had concluded. Centex asserts that the document describes the 2-Number FX service and Front End Guide concepts more fully than Exhibit 403. Centex apparently offers this document to show that Pacific has studied technologically feasible ways of provisioning FEX service which do not require line haul configurations. The alleged contents of the document would merely be cumulative in supporting such a proposition. The description of these services in Exhibit 403 is adequate. We will therefore deny the motion.

Siwek supports the concept of unbundled FEX rate elements, but differs with Pacific on what the rates should be. In his analysis of Pacific's FEX cost studies, he cites Scholl's testimony that FEX access costs for Centrex customers would probably be less expensive to provide than a simple line haul service because, although there would be some additional switching-type costs, access line costs would be eliminated. (See Tr. 10051-10052.) Siwek argues that since Pacific has not quantified the savings associated with FEX service to Centrex customers, as an interim measure pending new company cost studies, this Commission ought to recognize the difference by applying Pacific's proposed increases in FEX access rates only to customers requiring access lines, maintaining access rates at current levels for customers who avoid the use of FEX access lines. On redirect examination Siwek was asked whether he would agree with Shantz' suggestion for setting an appropriate recurring monthly charge for customers who use FEX service in conjunction with Centrex service, which the questioner characterized as being the sum of an FEX rate increment applicable to all business FEX service plus the Centrex exchange trunking charge. Siwek stated that he did agree with such an approach in concept.

Siwek states that Pacific's decision not to increase FEX mileage rates seems consistent with its cost studies, which show these rates to be reasonably in line with 1986 costs, but adds his opinion that as Pacific's use of fiber optic plant increases incremental cost will decrease, thereby producing future revenue excesses which can be used in the future to offset any shortfalls from nonrecurring FEX charges.

Turning to nonrecurring costs, Siwek contends that the cost study portrayed in Pacific's data response Exhibit 276 which shows the nonrecurring cost per FEX business connection at $1,378 is so much higher than the total unit cost expense saving it shows for grandfathering FEX service in its transcript request Exhibit 303 ($541), and the estimated service connection costs it estimated in its 1984 rate proceeding ($333 for the 83% of service that is to contiguous areas and $573 for the 17% to noncontiguous areas--the weighted average is $374) that the accuracy of these studies is questionable.

Siwek adds the connect and disconnect savings figures from Exhibit 303 plus two times Pacific's claimed record costs to represent two service orders, plus Pacific's calculation for investment-related, nonrecurring FEX costs to arrive at his $895 proposed connection rate for new business customers. He cautions that this figure is probably high because the disconnect figure is somewhat overstated and because no cost adjustment factor has been applied to it to reflect Pacific's 1986 authorized revenue requirement. Later, based on Scholl's rebuttal testimony, Centex concluded that the two "record" service order inclusions in Siwek's calculation are inappropriate, so that the total should be reduced to $833. In any case Siwek goes on to state that we should not authorize even his proposed increase all at once, but should limit any connection rate increase to 100% above current rates in keeping with what he understands to be Commission policy regarding nonrecurring rate increases. Current rates are $190 for business connections for service between contiguous exchanges and $290 for service between noncontiguous exchanges. The weighted average would be $188.

Citing Selwyn's criticism of Pacific's allocation of design and testing costs to recurring FEX service rates, Centex' opening brief claims that comparable allocations were made to the nonrecurring cost categories on which Scholl's $1,378 estimate was based, and suggests that Pacific's failure to produce a bottoms-up cost analysis of nonrecurring FEX services is justification for authorizing no increase at all in these charges, or alternatively, for limiting them to the across-the-board 5% increase which Shantz proposed in his original testimony for all service connection charges.

Furthermore, Centex contends that the ratio of service connections to disconnections shown in Appendix B to Scholl's rebuttal testimony (Exhibit 402), which is based on the assumption that the grandfathering proposal is not adopted and that there are no rate changes in the test year, is unrealistically low when compared to the 1984 volumes. Centex asserts that if these figures were brought more in line with recorded figures for 1985 the allocation of nonrecurring costs to business FEX service would have produced a much smaller indicated cost per service connection.

Centex also suggests that there are two possibilities for unbundling FEX rates. One is to calculate rates which are revenue neutral with respect to the combined FEX rates for any particular customer, the other, which Centex recommends, is to establish a uniform FEX increment and allow the total rates paid by particular customers to vary, depending on the choice of access line.

Replying to Siwek's claim that the difference between Pacific's $1,378 total FEX nonrecurring cost figure and its $541 calculation of test year expense savings raises the question of the reliability of Pacific's projections, Scholl explained that the former figure is an average of all business FEX nonrecurring inward movement costs, including connects, disconnects, change orders, and record orders, while the latter is only the average connection cost of a business FEX access line. Scholl also explained that this $541 projected test year business FEX connection cost and the costs estimated in its 1984 rate case ($573 and $333) are not exactly comparable since the 1984 costs represent a composite average cost of service connection for both residential and business FEX while the cost projections presented in the pending matter are separated for business and residential. In response to Centex' skepticism about the number of inward orders (installations) Pacific projected for the test year, Scholl testified that he went back to the project management people who developed these numbers, and learned from them that business FEX would decline because of the growth of some cross-elastic services. He further learned that the tracking results through November, 1986 (the month before his testimony) had indicated that FEX did, in fact, decline throughout 1986. (TR at 19083-19084.)

d. DRA

DRA takes the position that Pacific's grandfathering proposal should be rejected because there are no adequate substitutes for this service, and adoption of it would thus be repressive. Shantz also contends that it would be inappropriate to drive more customers toward Remote Call Forwarding, as Pacific's plan would presumably do, when RCF has been the subject of this Commission's investigation of Pacific's marketing practices. DRA recommends that we require Pacific to file a tops-down and bottoms-up study of FEX service before considering granting any service discontinuance.

As an alternative to Pacific's grandfathering proposal, DRA's concurrent closing brief proposes decreases for FEX services in direct relationship to the decreases DRA proposed for residence and business BEAL services. When Shantz testified he was proposing service rate increases, the decreases are set forth in DRA's final rate design which was incorporated into the concurrent closing brief. The revenue effects of this change are factored into DRA's revenue effects for basic services and service connection changes.

DRA does support Pacific's proposed tariff structure, but stated that DRA did not have time to develop tariff revisions, and recommended that we authorize Pacific to file an advice letter setting forth an incremental FEX tariff structure, subject to review by CACD and final approval by Commission resolution. Shantz does not agree with Siwek's proposal to charge FEX subscribers who have Centrex service (and therefore do not need a line haul access line) only the FEX increment but no FEX access rate element. Shantz asserted that there are access costs which such a subscriber should cover and agreed with his cross-examiner, Mr. Mattes, that it would be equitable to set this rate element at the one to ten ratio that is used for Centrex exchange access trunking charges as compared to PBX trunking charges. Shantz further states that the FEX increment should be set at a level designed to generate zero revenue effect in relation to the prior unbundled service.

3. <u>Discussion</u>

a. <u>The Grandfathering Proposal</u>

Selwyn's assertion that Pacific's failure to show offsetting revenue increases for other services as a result of its grandfathering proposal indicates either understated revenue effect or a situation where no alternatives exist is well taken. While it appears that there are adequate substitutes for most residence FEX service requirements and that there has been a steady decline in residence FEX service subscription since Pacific's last rate decision was issued, Pacific acknowledges that there is no complete substitute for business FEX service and that subscription is increasing. This fact dictates that Pacific's grandfathering proposal only be authorized where the inequities of any other possible solution are beyond doubt.

Though Pacific's costing methodology seems appropriate and it has reasonably explained the points of it that have been criticized by various parties, we must agree with DRA that the marketing practices Pacific followed with respect to such options as Remote Call Forwarding may well have influenced the growth rate of this service in the recent past in a way which may not be characteristic of future growth. Further, although Pacific is correct that Ordering Paragraph 16d of D.84-06-111 only requires bottoms-up and tops-down cost studies for service categories where Pacific is proposing greater than average rate increases, the import of our order was that any plan to significantly alter an element of rate design should be based on cost data which allows a comparison of methodologies, and allows more precise cost allocation than tops-down studies alone can provide.

It may or may not be possible to bring FEX revenues to the level of costs. Nonetheless, it would be unreasonable to deny FEX service to future businesses seeking it based only on the record before us. This conclusion is reinforced by the suggestion of Pacific's SSA Task Force Report and the testimony of Sullivan that there are less costly alternatives to present FEX provisioning which are already technically possible. Perhaps our denial of this grandfathering proposal will spur Pacific to develop a means of implementing FEX innovations. In any case, we agree with General, Centex, Selwyn, and Shantz that a pricing solution is the most appropriate means of addressing FEX revenue shortfall at the present. We will not grant the grandfathering proposal. If Pacific wishes to offer the proposal again in a subsequent rate proceeding, it shall present both bottoms-up and tops-down cost studies to justify it.

b. Unbundled Rates

The concept of unbundled rates is one which we generally endorse. Although most FEX connections are presently made using a private line channel between central offices, the customer does not receive private line or private line-like service. Therefore, we see no merit in General's proposal to set FEX rates to be consistent with private line rates. Nor is Pacific's model for unbundling FEX rates entirely appropriate since we have already denied its proposal to unbundle basic rates into an access and a usage component. We will instead adopt a modification of Pacific's proposal which is disaggregated into a single rate encompassing both access and usage and a new FEX increment component for FEX services with dial tone from a Pacific central office. As we explain below we will authorize Pacific to set the access component at the same level as local service, and add a new FEX increment component. We adopt Pacific's proposal for the FEX increment component for FEX services with dial tone from a Pacific central office.

(1) Recurring Rates - Mileage and Access

We do not find convincing Selwyn's assertions about the impropriety of the assignment of design and testing costs for loops, the only recurring cost criticized. Scholl's explanation of the need for designing circuits whenever line haul is used seems reasonable. On the other hand, it is clear that such assignment could be lowered significantly if Pacific were able to implement any of the alternative FEX delivery systems described in Exhibit 403.

We agree with Siwek, who apparently does not dispute its accuracy, that the .9 revenue to cost ratio shown at

p. 7-127 of Exhibit 260 (to which no scaling factors have been applied) indicates that present FEX business mileage rates are reasonably close to 1986 costs. The ratio for residence measured service though, at .7, is somewhat low, even if cost is reduced by a factor in the range of 82% to 90% which is the range of all but one of the adjustment factors in Pacific's Exhibit 261. Nonetheless, it appears that mileage rates are close enough to cost that it is unnecessary to adopt an FEX mileage rate which differs from the present rates which we have retained. Furthermore, adoption of such rates may prod Pacific to act with more dispatch in attempting to institute alternative methods for providing FEX service.

There is no doubt that overall FEX service revenue is less than cost. Setting rates for access to the exchange to mirror those for basic service will not affect this picture, and it will provide a rate scheme which is easier for the customer to understand and easier for the utility to administer. No FEX customer should be exempt from exchange access charges; however, we agree with Siwek and Shantz that it is equitable to mirror Centrex exchange access trunking charges when providing FEX service to Centrex subscribers.

No party, however has presented us with a specific proposal for implementation of this concept. We will therefore order the filing of an advice letter which implements this concept. The advice letter should contain the tariff revisions necessary to implement the mirroring of the Centrex exchange access trunking charges when providing FEX service to Centrex subscribers; the estimated 1986 annual billing and revenue effects associated with the implementation of such tariff revisions; and revisions to the customer billing surcharge to reflect the annual revenue effect of implementing such tariff revisions for Centrex service. The advice letter shall be subject to Commission authorization by resolution before becoming effective.

(2) Nonrecurring Charges

Even with its doubts about tops-down cost study reliability and Pacific's $1,378 figure, Centex is willing to assert that FEX business connection costs could be $833 per connection if we assume, as we do, that allocation of design and testing costs to recurring service rates is appropriate and that the ratio of service connections to disconnections which Pacific used is appropriate. Charges are presently $170 for contiguous service to a Centrex line, $190 for all other contiguous service, $270 for noncontiguous service to a Centrex line, and $290 for all other noncontiguous service. Clearly, these charges would still be priced below cost even at 100% increase which Centex would prefer as a maximum. Looked at in this light, DRA's proposal would require Pacific to continue to heavily subsidize this rate element from other sources. FEX is not a basic service and ought not to be the recipient of large subsidies. On the other hand, it has been our policy to ameliorate the effects of rate shock by limiting individual nonrecurring charge increases to 100%. It is clear that such an increase, for both business and residence nonrecurring FEX charges, is reasonable now. We will authorize adoption of such charges.

(3) FEX Increment

As we understand it, General advocates setting the FEX increment at the channel termination rate for private line service. While 67% of FEX service is provided over lines that are similar to private lines, the remainder is not. The proposal ignores the treatment of residence service. Further, since we do not adopt General's private line costing model, it makes little sense to set the FEX increment to be consistent with the model.

Pacific does not propose a change in the portion of its FEX rate which is attributable to the FEX increment. There is no reason for this Commission to adopt a different result. We will authorize Pacific to set its FEX rate increments at the rates Sullivan has proposed for FEX services with dial tone from a Pacific central office. The increase realized from this adopted rate design will be far below any estimate of the difference between revenues and costs.

(4) Revenue Effect

The overall test year revenue effect for changes in FEX nonrecurring charges will be an increase of $12.751 million. The revenue effect for FEX recurring access rates is reflected in our discussion of basic exchange service revenues.

c. Bill and Keep Billing

It makes sense to move the billing structure for FEX services to a structure in which a customer receives a bill for the services which are provided from the particular utility which provides the service. In order to implement the meet-point billing proposal which General advocates, however, it is necessary to develop and adopt billing policies in the form of tariff provisions applicable to each carrier which provides intercompany FEX services, which assure that customers are not double-billed for any portion of their service. We must also ensure that each carrier which provides intercompany FEX services notifies its customers of the change in order to mitigate the confusion which might otherwise result upon the customer's receipt of separate bills from two local exchange carriers.

Detailed specific tariff provisions and customer notice provisions were not addressed in this proceeding. It is not possible to implement the meet-point billing concept for FEX services until such specific tariff provisions and customer notice provisions have been provided. Therefore, we will require Pacific and the other local exchange companies (LECs) to jointly study this proposal and then file with CACD for review and approval, either jointly or separately, the study results, detailing the means of achieving meet-point billing for intercompany FEX service pursuant to a bill and keep plan.

The joint study should address the type and methods of customer notice to be used as well as the conversion of each local exchange company's FEX tariff rate structure to a structure which will facilitate the implementation of the meet-point billing concept for FEX service. Further, in those instances where the implementation of the meet-point billing concept for FEX service will result in an increase in a utility's annual revenues, the advice letter filing should include a revision to the utility's customer billing surcharge applicable to intraLATA services to counterbalance that increase.

Once CACD approval has been received the LECs may make an advice letter filing for Commission authorization of the approved plan.

VII. Private Line and Private Line-like Services

A. Introduction

Scholl describes private line services as connections between two or more customer locations which do not utilize the public switched network, but are fixed or dedicated in nature. Pacific claims that with no rate changes its test year private line revenue will fall short of costs by about $400 million, the shortfall for its recurring costs being about 50% of the test year average historical costs or $300 million and the shortfall for its nonrecurring costs being about 70% or $95 million.

To reduce this shortfall Pacific's revenue neutral rate design proposal of June 25, 1985 proposes increasing test year revenue from private line services by $29.127 million which becomes $26.569 million after settlements, a 22.4% overall increase. Additionally, Pacific calculates that its proposed rate design will result in an expense savings from repression of $4.237 million. No proposed recurring rate is set more than 100% above present rates. Proposed nonrecurring rates are set at one quarter of the difference between present rates and cost coverage. In order to come closer to cost coverage while continuing to moderate the impact, Pacific also proposes phasing in some further private line increases over the two years following the test year, targeting these increases to cover revenue shortfalls created by reductions in carrier access charges and shifts in intraLATA NTS costs. These automatic step increases would result in additional revenue increases of $41.180 million for the second year and $36.293 million for the third year. Since these revenue increases are cumulative, total revenue increase in the third year would be $106.6 million, and the total revenue increase for the three years, excluding expense savings, would amount to $206.034 million.

Besides rate revisions for local loops, Associated Channel Equipment, intraLATA interoffice mileage and channel terminations, Pacific's proposed rates include some restructuring. For one thing, Pacific proposes deaveraging local loop rates by establishing two tariff schedules which recognize the different cost characteristics of serving wire centers with respect to loop length, age of plant, type of facility and structures, and density of development and to base rates on the ratio of average wire center loop investment compared with the statewide average loop investment. About 76% of all local loops would be charged under the lower priced Schedule I rates, and the remainder under the Schedule II rates. Another rate restructure Pacific proposes is making Alarm Transport a separate private line subcategory with smaller rate increases than the rest of private line services in order to recognize "differing market characteristics and different service alternatives that are emerging." This entails establishing a new tariff schedule for Alarm Transport. Further, Pacific proposes raising secretarial line rates somewhat less than other rates to avoid an excessive increase in one year. Finally, it proposes that certain telegraph private line services be limited to those customers currently receiving the services, on the ground that terminal equipment for the services is no longer being manufactured and new demand is therefore virtually non-existent.

B. <u>Pacific's Cost Studies</u>

1. <u>Overview of Pacific's Methodology</u>

Pacific conducted various cost studies to support its private line rate proposals. Separate studies were conducted for recurring and for nonrecurring private line costs. Ordering Paragraph 16.d. of D.84-06-111 required Pacific to conduct and file, as a part of this rate application, detailed bottoms-up as well as tops-down cost studies for any major service category for which PacBell proposes rate increases substantially greater in percentage terms than the proposed increase in total revenues. Thus, both tops-down and bottoms-up methodologies were used.

Pacific's basic cost study is the category analysis, which uses a tops-down methodology to disaggregate projected 1986 average historical (embedded) costs into 16 broad categories of service, one of which is private line. Pacific's category analysis studies were conducted in 1984 and early 1985 and the projected 1986 dollar amounts in each revenue, expense, and investment subaccount which these studies allocated to the various categories are the ones used in Pacific's Results of Operations (R/O) presentation.[5]

Pacific has changed its category analysis since its last rate proceeding by translating and regrouping its investment dollars from the Uniform System of Accounts (USOA), which identifies plant investment by type, to a Functional Accounting system which identifies plant investment by function. Pacific claims that this reorganization and the consequent further disaggregation of cost information allows investment-related costs to be assigned to service categories much more precisely. Thus, Scholl explained that where the accounting system provided sufficient detail, Pacific's investment-related costs and expenses were directly assigned to one of the service subcategories or to one of the cost components. Where this was not possible, Pacific used cost causative attribution methods to assign the costs.

Pacific's allocation rules are described by Kenneth G. Docter, a Price Waterhouse Certified Public Accountant, and Pacific witness, as being more detailed and complex than commonly used by major firms. Docter testified that he concluded that Pacific's information regarding the relative costs of categories of service was reliable after examin[ing] the major inputs to the embedded

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5 Subsequently, in response to D.85-09-018, Scholl also provided cost adjustment factors for each of the studied categories in order to reconcile costs with the reduced R/O adopted in D.86-01-026 as modified by D.86-03-049. The adjustment factor for private line recurring costs is 89%.

analysis, review[ing] allocation rules and verif[ying] calculations for the major inputs. He explained that this process included tests of the processes Pacific used for accumulating costs and investments and allocating to the service categories, as well as tests of reconciliation to the projected 1986 books of account at the account level, the total Company level and the category level. He added: "We tested the computerized model to ensure that it functioned as described and followed the allocation logic which we had reviewed. In addition, we reviewed development of input ratios and the control processes in place in [Pacific's] Service Costs [department] to ensure input and processing integrity." See Exhibit 275, pp. 5-6.

Pacific's category analysis for private line shows total projected test year costs of $720 million and revenues of $320 million producing a negative $390 million contribution, an overall 0.4 revenue to cost ratio, a revenue to cost ratio for recurring rate services of 0.5, and a revenue to cost ratio for nonrecurring rate services of 0.3. See Exhibit 260, pp. 7-17.

Pacific conducted two studies of private line costs which, according to Pacific, incorporate the bottoms-up methodology as we required in D.84-06-111. One of these studies was for recurring costs and the other was for nonrecurring costs. In its brief Pacific asserts that its bottoms-up studies offer a valid and worthwhile comparison between "identifiable bottoms-up costs" and tops-down accounting costs adding that it is not reasonable to anticipate that a bottoms-up study process would capture each and every cost of a given service. Rather, the extent of any difference is a measure of the reasonableness of the tops-down results. Pacific concludes that the accuracy of its projected unit costs for both recurring and nonrecurring private line costs is demonstrated through its tops-down/bottoms-up reconciliation. The reconciliation shows a difference for total loop investment of $300 million, or less than 5% of total. By way of comparison, the difference in these two loop investment figures in Pacific's last general rate proceeding was $2.6 billion. See D.84-06-111, mimeo., at 167.

2. Specific Cost Studies

a. The Recurring Cost Study

Scholl describes the recurring cost study for private line as being an average historical cost analysis with additional information complying with D.83-04-012. The recurring study begins by identifying the station designs and central office equipment associated with each private line service offering. Eight private line cost elements were thus identified. They are:

* loop (sometimes called channel),
* central office service area transmission equipment (CO SAT),
* station service area transmission equipment (station SAT)[6],
* channel terminations, and
* interoffice trunk equipment (line haul and outside plant components),
* bridging,
* signaling, and
* conditioning.

The cost study identifies end channel termination investment per termination. Interoffice equipment investments are identified on a per mile basis within mileage bands. Investments in the remaining items are identified per local loop.

Pacific relied on its Facilities System data base for information about station designs and central office equipment.

6 Together, station SAT and CO SAT are sometimes referred to as Associated Channel Equipment or ACE.

Then it developed a current unit investment for equipment associated with each station design and an average historic unit investment for each piece of central office equipment. Its Continuing Property Record data base provided the information Pacific used to develop these bottoms-up unit investment figures. These unit investments were multiplied by their occurrences (volumes) at each type of service offering to determine total investment by service offering. Then these total investments per service offering were divided by the number of local channels in that service offering (also identified from the Facilities System data base) to develop a weighted average unit investment per local channel (loop) per service offering for CO SAT and station SAT.

In a separate bottoms-up study the Facilities System data base provided identification of channel terminations and circuit mileage, tracking the transmission medium; i.e. cable, analog carrier, digital carrier, or broadband; thereby allowing a determination of the number of end channel terminations, intermediate channel terminations, route miles, and equivalent air miles for specified mileage bands per service offering, per transmission type. These volumes were multiplied by the average embedded unit investment for channel terminations, and by the average embedded investment per mile for each transmission type (determined in yet another bottoms-up study giving average line haul, interoffice outside plant, and channel termination investments for each type of transmission technology). The results show channel termination investment, line haul investment, and interoffice outside plant investment per mileage band for each service offering.

Scholl testified that these total bottoms-up investments in each mileage band for each service offering were then divided by the total number of end channel terminations and by the total mileage to yield a weighted average investment per mile in each mileage band for line haul and interoffice outside plant and a weighted average investment per channel termination in each mileage band.

Pacific also derived a weighted average investment per loop. The separate loop cost study is described below.

Pacific's next step was to multiply these weighted unit investments by loading (or investment allocation) factors, computed individually for each cost element, to load for "secondary gross investments,"[7] producing a loaded unit investment for each of these cost elements.

To close the bottoms-up investments to the tops-down total gross investments, the loaded unit investments for line haul, outside plant, and channel terminations were then multiplied by facility system miles and channel terminations projected for the test year, and the loaded unit investments for station SAT and CO SAT were multiplied by billing record service quantities. The total of all service offerings thus derived yielded what Scholl describes as total bottoms-up loaded investment figures for these cost elements. A similar process was applied to loaded loop unit investment to obtain a total loaded investment figure.

Finally, the gross investment identified by the category analysis for each cost element was divided by the corresponding bottoms-up loaded total investment for that cost element. This produced the scaling factor for each cost element by which each corresponding bottoms-up loaded unit investment was multiplied to yield an Average Original Investment (AOI) for each cost element.

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7 Scholl explained that these loading factors were derived by dividing the gross investment determined by the category analysis model by the principle investment without any loadings, also determined through the category analysis process. Ex. 260, p. 5-46. The secondary gross investment would load for costs incidental to providing the particular service, such as office space, which would not be included in the annual cost factors described below.

Annual cost factors determined separately for each subcategory of service offerings and for each cost element within the subcategory were then applied to the AOI to determine the annual recurring cost of private line services. These cost factors were for return and taxes, maintenance, commercial and marketing, depreciation, general expense, and other taxes and charges.

Pacific's cost exhibit shows the ratio of total tops-down to total bottoms-up investment costs for all of private line, including loop, to be 1.03. (Exhibit 260, pp. 7-111.)

b. The Local Loop Component of Recurring Costs

Local loop makes up a significant portion of the recurring private line costs. Thus, one of the building blocks used to obtain the private line recurring costs above was input on local loop costs. According to Scholl, this input was derived from the separate service-specific bottoms-up loop study which depicts the average subscriber loop plant investments associated with each of the eight service classes studied. Five of these eight studies relate to private line. They are: telephone answering service (TAS), alarm central station, alarm patron, Voicegrade Data, and exchange-related private line. Scholl testified that the sampling approach Pacific used resulted in all private lines having an opportunity to be selected. Thus, these five functional service classes are designed to include all of the services provided in each of Pacific's private line service subcategories.

Using what Scholl describes as a bottoms-up technique the loop studies derived universe listings for each of the subcategories of private line service from certain existing mechanized data bases which contain all statewide working lines which Pacific bills.

A random sample of lines was selected for each of these service groupings, the cable and pair associated with each line was identified, and field engineers identified specific loop characteristics (cable gauge, plant account (aerial, buried or underground), and length) for each of these samples. This data was entered into a computer program called "Loop Category Analysis" which calculates the length of each loop by plant account (buried, aerial or underground) then totals all loops sampled for each service offering and gives a statewide average loop length for working plant for each service offering by plant account. The statistician refined these figures to produce final results of average length by account.

These average lengths for working plant for each plant account per service group together with overall total working plant length by account were used to create an allocation factor for each service offering. The allocation factors were then applied to total investment in booked outside plant and to drop and pair feet to determine total working plant investment per service offering.

Next, Pacific conducted what Scholl describes as a tops-down to bottoms-up reconciliation by assigning the results of Pacific's Ready-to-Serve (RTS) analysis in proportion to the average relative lengths of in-service loop for each service offering. See Exhibit 260, p. 5-25. The RTS is a separate tops-down loop study. Its purpose was to identify Pacific's entire investment in subscriber outside plant (i.e., loop) by putting a dollar value on the investment in that portion of plant which is not currently working, but is ready to serve, and is, according to Pacific, a reasonable and economic reserve. Assignment of the RTS results to the working plant investment produced what Scholl calls the embedded unit investment for the service offering.

To the embedded loop unit investment figure thus derived, Pacific then added annual loop plant category charge factors (for depreciation, return, taxes, maintenance, etc.) developed from the tops-down category analysis, thus identifying annual cost for the loop portion of each service offering.

c. The Nonrecurring Cost Study

Pacific's bottoms-up nonrecurring private line study identifies the following types of private line investment:

* service order costs
* channel connect costs

Service order costs are defined by Scholl as those costs associated with the receipt, negotiation, processing and completion of a customer's request for private line service. Channel connect costs are those costs associated with the physical wiring and testing of a requested private line circuit or circuitry. The study produced unit costs by service offering and total cost by service offering. These service order and connection costs were derived by identifying the work components associated with these two activities and relying on panels of estimators with expertise in the areas to identify tasks required for various private line services and to provide average low, usual, and high work times for those tasks. These time estimates were used to compute average work times which were then multiplied by loaded labor rates to derive bottoms-up unit costs. Pacific provided data for 1984 actuals and projections for the test year using this methodology. Because we criticized the lack of explanation for the large discrepancy between Pacific's tops-down and bottoms-up results for nonrecurring costs in D.84-06-111, Pacific's filing this time includes a reconciliation for 1984 actuals which shows a closure factor of 1.2, and a 1986 projected closure factor, using the same methodology of 1.09. Scholl testified that a 94% adjustment factor should be applied to Pacific's nonrecurring cost projections for the test year to conform to the R/O adopted in D.85-01-034.

d. Incremental Cost Study

In D.84-06-111 (mimeo. at 294) we stated that we wished Pacific and other parties to address whether marginal cost analysis might be used as a basis for rate design decisions. To that end, Ordering Paragraph 16g ordered Pacific to file in the present proceeding an analysis of the relationship between incremental capital costs in the local network and incremental service demand for various services on a recent historical and prospective basis.

When we reviewed Pacific's incremental cost study plan in D.85-02-030 we clarified what we expected Pacific to produce in compliance with Paragraph 16g and we further found that the Paragraph 16g study was not likely to generate the sort of data on the incremental costs of providing particular services that we had hoped for. Therefore we required Pacific to submit a further incremental cost filing in this proceeding which would include: (1) an appropriate method for defining Pacific's incremental service costs for major service categories; (2) numerical estimates, to the extent available, of incremental costs defined by service category, calling characteristics (e.g., time of day), and subscriber density; and (3) for competitive or potentially competitive services, estimates of the relationship between Pacific's incremental service costs and the costs of competitive entry, with assessment of the relevance of these factors to rate design.

Pacific submitted its 16g study as ordered. The further study was filed as a part of Scholl's testimony in Exhibits 260 and 261. Exhibit 260 explained the three incremental cost methodologies used to look at the incremental capital costs associated with these major investment components of telephone plant: (1) customer loop plant, (2) interoffice facilities and equipment, and (3) switching equipment. Scholl testified that he used the engineering construct method for loop plant costs, the project or budget analysis technique for identifying the incremental capital costs of interoffice facilities and equipment (to be used as a building block for determining private line and usage services), and the statistical or regression technique for investigating the incremental capital costs of switching plant. Scholl explained that he chose to study only the loop plant portion of residential access service because that represents the greatest concentration of capital costs associated with residential access service. He does not state whether the same rationale was responsible for his decision to study the loop plant portion of business access service. However, it appears that private line loop is treated as a component of the business loop study.

The costs associated with loop plant were broken down both by residence and business categories, and by six density zones within each category. Exhibit 260 however, addressed only total plant level costs within each cost category, with some information about residence costs, but no specific business cost data.

Exhibit 261 provides supplemental incremental cost data for the loop portion of the Exhibit 260 study, at both the plant element level and the more disaggregated customer type level (business or residence) and the six subscriber density zones per customer type. The plant level estimate used a sample of about 5000 working loops to determine loop characteristics, including type of construction used and loop length. These characteristics were used to calculate the average statewide investment required to construct new loops. Then average customer loop incremental investments were calculated for each of the six density zones and a statewide weighted average incremental loop investment was calculated from the investments within each zone. Additional incremental capital costs for return, income tax and depreciation factors were applied to these investments to determine the capital costs associated with them. The results of this study varied somewhat from the results of the Exhibit 260 study, but still showed that subscriber loop incremental costs are considerably higher than embedded costs.

The same 5000 loop sample which was used in the studies above was disaggregated into residence and business components and each of these was further stratified into the six density zones in order to produce residence- and business-specific loop characteristics for each density zone. From these characteristics incremental customer specific loop investments were calculated, and this figure was used, as described above, to calculate a customer group specific statewide weighted average incremental investment for each density zone.

Scholl testified that the incremental capital costs were calculated using the same methodology as that described for the loop investments described above.

Based on this methodology Scholl's Exhibit 261 at p. 4.3 shows an average incremental loop investment per working business loop of $600 (residence is more) and an average incremental monthly capital cost per working business loop of $9 (residence is more). His statewide average figure for capital costs in Exhibit 260 was different (over twice as high) from the figure in Exhibit 261 ($10), but he testified that the latter study figures are more precise. Exhibit 261 does not show much cost variation for business service incremental capital cost based on density zone. The bar graph at p. 4-4 shows a range of between about $7.50 and $11, while the residence range is between $5 and $25. No figures are presented for the range of incremental investment for business service by density zone.

Private line was not a service which Pacific treated as competitive or potentially competitive. Thus it made no estimate of the relationship between its private line incremental service costs and the costs of competitive entry. Further, Pacific did not use its incremental cost studies as the basis for any of its pricing proposals.

C. DRA's Critique and Its Own Private Line Rate Design Proposal

1. Recurring Costs

In Chapter 11 of DRA's cost of service report, Exhibit 329, Shankey, DRA's private line witness, stated that DRA did not have the resources to review Pacific's tops-down recurring cost studies, and was only commenting on Pacific's methodology for determining these investment-related recurring costs. He testified that DRA supports the methodology Pacific used to derive its tops-down unit investments, but objects to Pacific's use of the Functional Accounting system rather than the USOA for determining costs.

Shankey explained the accounting format objection on two grounds. First, he stated that this Commission does not recognize the Functional Accounting format. Second, he seems to say that DRA would not object if the bottoms-up cost studies were truly stand alone studies, but asserts that because the investment-related costs allocated to private line services were allocated based on ratios with tops-down studies, which DRA did not have the resources to review, DRA cannot be sure of their accuracy. Further, Shankey added that this use of the Functional Accounting format is inconsistent with all Pacific's other filings, and for that additional reason prevents comparison and tracking for accuracy.

Shankey went on to note that in lieu of a conversion of Pacific's cost study results into a USOA format DRA had met with Pacific and agreed to consider two sets of adjustment factors provided by Pacific to adjust Pacific's cost studies. One was to reflect Pacific's R/O as set forth in the joint R/O comparison exhibit, and the other was to reflect DRA's R/O from the comparison exhibit. In later testimony, however, Shankey testified that DRA found the methodology Pacific used to develop the adjustment factors to be unacceptable because it used Functional Accounting translations which could not be reviewed and tested. Shankey added that it would be inappropriate to apply Pacific's cost adjustment factors across the board in the individual service cost studies because the quality of Pacific's cost analysis was not consistent. Instead, DRA applied an across-the-board adjustment factor of 85% to Pacific's figures. Shankey explained that factor represents the approximate difference between the aggregate costs which Pacific estimated for test year 1986 and the level of aggregate costs found reasonable by the Commission in D.86-01-026 (as modified by D.86-03-049). (Exhibit 330, pp. 8-9.)

Shankey also criticized Pacific's recurring service volume information for relying on information from only two points in time, June 1982 and June 1983. He claims that DRA's volume calculations based on five quarterly reports from Pacific's Private Line History File 9PLHF) are more representative of in-service volumes which can be expected for the test year.

In his rebuttal testimony, Exhibit 412, Shankey offers his opinion that Pacific's cost studies are in compliance with the Cost Manual guidelines. He explains that this Commission found tops-down allocation of some expenses to be proper in a bottoms-up cost development, and states that it is therefore up to Pacific to show that it has used those allocations properly. It is up to the Commission to decide to accept or reject Pacific's explanation. (Exhibit 412 at p. 2.)

DRA's opening brief advances this same position, adding that DRA agrees with Scholl's rebuttal testimony that Pacific did conduct a bottoms-up investigation of private line investment and that Pacific's tops-down cost study is validated by its reconciliation with this recurring bottoms-up cost study. In fact, DRA states that Pacific's bottoms-up study was an extensive and thorough study and adds that Pacific has made great strides in improving its private line cost study. The focus of DRA's concern with Pacific's cost studies is Pacific's use of the Functional Accounting format, and DRA's inability to analyze expense allocations derived from this format. DRA suggests that it had hoped Pacific's adjustment factors would be developed in a way that would allow their application to individual service accounts reported in the Functional Accounting format. When that proved not to be true DRA decided, as Shankey testified, that it would be more reasonable to rely on Pacific's overall adjustment factor than the one it developed specifically for private line.

2. Nonrecurring Costs

DRA developed its own nonrecurring private line cost projections. They are set out in Chapter 11 of Exhibit 329, DRA's cost of service report. Chapter 11 was prepared by Shankey. In that report DRA supports Pacific's nonrecurring cost study methodology, but finds the costs to be overstated. DRA's analysis of nonrecurring costs focuses on the activity times which Pacific used in its nonrecurring cost calculations. Shankey made field inspections at Pacific's facilities and observed the activities of Pacific personnel involved in the provisioning of private line services. He decided to conduct time and motion studies of work times for major tasks from a representative service offering in order to assess the reasonableness of Pacific's activity times, since his casual observations of the work groups' activities lead him to believe that significant reductions in personnel were possible. The 3002 4-wire voice grade (3002 4WVG) circuit was selected as the representative circuit. The time and motion studies were conducted on employees in each of the ten major work groups involved in provisioning 3002 4WVG service.

The studies eliminated nonproductive time and then added a standard allowance of 15% to account for personal, fatigue and delay time. The times DRA computed were then compared to the times recorded by Pacific to derive a ratio. The ratio was applied to Pacific's total activity time. The activity times thus adjusted were then multiplied by the fully assigned labor rates which Shankey adjusted by the ratio of the staff wage escalation factor as presented in DRA's R/O showing, to Pacific's wage escalation factor, to produce adjusted unit costs for the representative channel connect activity and the representative service order activity. The ratio between these DRA-adjusted unit cost and Pacific's unit costs were used as overall private line adjustment factors to be applied to Pacific's projected nonrecurring costs. The adjustment factor derived for channel connect activity was 0.798, that for service order activity was 0.486.

DRA contends that Pacific's proposed 25% increase in nonrecurring charges is much too low in light of its very low revenue to cost ratio (0.3 according to Pacific's cost studies). Therefore, DRA proposes increasing nonrecurring rates by 100% or to DRA estimated cost, whichever is less. No increases are proposed for new services such as DDS and HiCap transport service because they are, according to Shankey, new and therefore do not have as low a revenue to cost relationship.

In Exhibit 329, Shankey reported that DRA was unable to clarify the source of Pacific's forecasted 1986 nonrecurring volumes. DRA used different volumes, as described below. The overall effect of DRA's proposal, even with application of the cost adjustment factor, and different volume projections is a revenue increase for nonrecurring services of about $20 million for the test year.

3. <u>DRA's Position</u>

Even with its change in the adjustment factor, its reduction of the activity cost estimates in Pacific's recurring cost study, which resulted in a reduction of about $24 million from Pacific's recurring cost estimates, and its adjustments to Pacific's nonrecurring cost study, DRA argues that it is reasonable to authorize a large private line rate increase. In fact, as shown in Appendix A to Exhibit 330, DRA proposes a larger total test year rate increase than Pacific, at $67.540 million. However, since it does not propose incremental increases for the following two years, the result at the end of three years is that DRA's proposal would continue to produce revenues $67.540 million higher than present revenues while Pacific's rates would produce revenues $106.600 million higher than present. In its post-hearing brief, DRA sets the projected private line revenue increase from its proposed rate design a little higher, at about $68.1 million.

DRA's proposed rates were devised by establishing a revenue to cost ratio, after adjusting Pacific's rates as described above, for each private line cost element and service offering. Where the overall ratio was found to be greater than 1.0, no rate change was proposed. Further, DRA's proposed rates rely on in-service volumes for 1986 based on third quarter 1985 actual data from the PLHF report grown to mid-year 1986, and the inward movement volumes are based on recorded activity for the first nine months of 1985 grown for 1986.

DRA opposes Pacific's proposal to deaverage local loop rates into two subcategories based on geographical cost differences. For one thing, DRA asserts that it is unlikely that the cutoff point of 76% of loops being placed in the low cost Schedule I category will remain constant, and adds that the ratio has little validity on a per-service-offering basis. For another, DRA notes that loop costs are driven primarily by loop length, and Pacific's proposal would inequitably charge customers served from a high cost wire center at the premium rate no matter what their distance from the wire center might be. Shankey also claims that Pacific's private line volume data have been too inaccurate in the past to allow for reasonable reliance on such a classification of wire centers. And, DRA claims that such a scheme violates Section 453(c) of the Public Utilities Code by discriminating unreasonably among users. Instead, DRA proposes increasing local loop recurring rates by 50% or to DRA's estimated cost, whichever is less. The outcome is that DRA's rate design raises most local loop rates by 50%.

Noting that services utilized to provide telephone answering service were exempted when this Commission ordered the restructuring of private line and private line-like services mileage sensitive rate elements from rate center to rate center pricing to wire center to wire center pricing, Shankey testified that if the exemption were removed now DRA's proposal would increase recurring rates by more than 50%. Therefore, DRA's rate design leaves the present pricing structure, raises recurring rates by 50% for secretarial lines and concentrator-identifier lines, and recommends that Pacific be ordered to submit a study of the revenue impacts of restructuring the mileage sensitive rate elements applicable to TAS services to a wire center to wire center rate structure. DRA adds that it still supports a single averaged rate for the service charges for designed and nondesigned secretarial lines, but if the Commission permits the establishment of two separate rates, the 100% increase limitation should be disregarded and both rates should be set at cost. However, Shantz stated that the tariff should leave the final decision about the most economical manner for providing the service with Pacific.

DRA opposes adding a new tariff schedule for Alarm Transport services, arguing that it offers preferential treatment to alarm services which unreasonably burdens the general body of ratepayers. Shankey also argues that adding a new rate schedule further complicates Pacific's ability to properly and accurately render bills and to track in-service and inward movement data. He states that leaving Alarm Transport services in their present schedules will assist Pacific in developing better volume data for forecasting and analysis purposes and more accurate billing.

As a final note, DRA reminds us that several ITCs in California concur in Pacific's private line and private line-like tariffs. Thus, we must consider the impact on customer billing for those utilities as well.

D. The Critique and Proposal of CBCHA/TCA

CBCHA/TCA oppose both Pacific's and DRA's private line proposals on the ground that there is no adequate cost support to show that private line is underpriced at present. In explanation, CBCHA/TCA point to the fact that Pacific's cost studies were conducted using the revenue requirement which it projected before our R/O decision, D.86-01-026, which reduced that test year revenue requirement proposal by about 12%. CBCHA/TCA argue that the adjustment factors we ordered Pacific to develop are insufficient to assure accurate rates because developments in Phase II of the R/O proceeding, and other Pacific cases, including the 1987 attrition decision, D.86-12-099, have or will change the revenue requirement again. Further, CBCHA/TCA's Selwyn contends that Scholl's claim that the adjustment factors are only accurate at the service category level is preposterous, and CBCHA/TCA add that if we do adopt Pacific's 89% adjustment factor for private line, we should, at a minimum, do it by reducing each of the cost elements by 11% as Selwyn illustrated in Table 10 to his testimony, Exhibit 361.

CBCHA/TCA also assert that Pacific's application of average unit investment figures based on its books of account to, for example, the bottoms-up derived average number of feet by plant type in its private line loop study make that study a tops-down study, not a bottoms-up study as this Commission ordered. Further, they argue that Pacific's AOI fails to reflect the age of the facilities, and therefore may reflect incremental or replacement cost rather than embedded historical cost. Also, CBCHA/TCA's post-hearing brief faults Pacific's study for simply adding an amount to reflect nonworking facilities, without determining the actual spare capacity required to provide the particular service in question. They add that this step also converts the cost study into a tops-down study. Finally, CBCHA/TCA argue that Pacific's reconciliation of its cost study calculations to its tops-down assigned expenses makes its use of factors to calculate recurring costs flawed, and makes the factoring process inherently a tops-down study. Because of each of these perceived flaws CBCHA/TCA state that any increase in Pacific's private line rates must be very moderate.

Turning to specific costs, CBCHA/TCA dispute Pacific's assignment of its Switched Access Remote Testing System (SARTS) investment and related costs exclusively to private line. Claiming that labor expense savings which result from not needing the frame technician and field repairman when SARTS is used are not likewise being assigned solely to private line, Selwyn argues that if this cannot be done then that savings is being unfairly spread across all services and the only fair solution is to likewise spread the cost of SARTS across all services. He calculates that this reduces annual cost for CO SAT, after applying the .89 rate case scaling factor, from $250 to $134. (Before applying the scaling factor, the figure is about $150.)

While asserting that they do not know precisely what private line service costs are, CBCHA/TCA concede that the revenue to cost ratio is probably less than 1.0 presently. They therefore acknowledge that a moderate rate increase may be in order. However, they further argue that any such increase must take into account the differences in cost between private line services in dense metropolitan areas and in spread-out suburban and rural areas as well as the differences created by the size or amount of service at a given location and by the length of the commitment of the customer to the service as discussed by Selwyn. CBCHA/TCA add that average rates expose Pacific to the risk of uneconomic bypass in that the customer may obtain service at a rate below Pacific's averaged rate, but in excess of its actual cost. CBCHA/TCA do not find Pacific's dual rate plan for loop rates is a good way to accomplish this. Instead Selwyn suggests concentrating on the six Pacific wire centers which contain 10% of all private line loops and have costs less than 50% of the statewide average, and making them one group for rate purposes. He proposes a second group of wire centers representing another 27% of loops, which exhibit loop costs between 50% and 75% of the statewide average. Selwyn's proposed rate design applies the cost factors for each of these three schedules, and the .89 rate case scaling factor, as well as his assumption that 4-wire loop is not twice the cost of 2-wire loop to arrive at the loop rate proposal set out in Table 13 to Exhibit 361. CBCHA/TCA recommend adopting the other private line rate elements proposed by Pacific for the first year, but they oppose any further increases in years 2 and 3 on the grounds that the cost studies are too defective and the revenue requirement is too unsettled.

Finally, citing DRA's failure or refusal to evaluate critically the PacBell cost studies, and citing what it describes as an inconsistency between DRA's criticism in Exhibit 329 (distributed in December 1985) of Pacific's use of ratios based on tops-down studies in its bottoms-up study, Pacific's use of the Functional Accounting format, and Pacific's use of forecasted service volumes in its cost study, with DRA's July 1986 rate design testimony, Exhibit 351, advocating large private line increases, CBCHA/TCA submits that DRA's position must be rejected.

E. The Critique of API

API Alarm Systems, Inc. (API) criticizes Pacific's recurring and nonrecurring cost studies as they affect the provision of alarm circuits as well as DRA's private line rate recommendations. It concludes that all services, including alarm services should benefit from revenue requirement reductions which have occurred and will occur as a result of this proceeding.

1. Pacific's Recurring Cost Study and Incremental Cost Analysis

Like CBCHA/TCA, but focusing on 3002 private line alarm transport services, API argues that Pacific's recurring cost studies overstate costs by directly assigning investment and expenses for SARTS testing technology to certain private line services while spreading the related savings to all service categories. API's witness, W. Kenneth Edwards, testified that he believed that Pacific's rate and cost personnel have improperly allocated SARTS investment. He points, for example, to Exhibit 273 which contains work papers showing the assignment of testboard investment for SARTS and SMAS (Switched Maintenance Access System) used to determine loaded unit investment for CO SAT. That exhibit shows no assignment to 3002C-type circuits for SARTS/SMAS, but does show it for other circuits, including 3002A/B. Edwards testified that it was widely known that SARTS/SMAS is used to test 3002C service, and he went on to note that Pacific did assume wiring of SARTS/SMAS access points to 3002 service in developing its nonrecurring costs. API acknowledges that Scholl testified in rebuttal that there should have been a SARTS investment assigned to 3002C service and that doing so would produce an annual unit CO SAT cost of $260 per 3002C circuit rather than the $180 identified in his cost exhibit, Exhibit 260.

Edwards states that Pacific's failure to show a reduction in the maintenance carrying charge for the offerings to which the SARTS/SMAS technology is assigned also causes an overstatement of costs. API's closing brief suggests that Scholl should have assigned maintenance savings to the 3002C service when he calculated the SARTS investment.

API also endorses Selwyn's claim that Pacific's labor savings have not been appropriately assigned to private line and his proposal for reducing total testboard investment for all private line services. API further asserts that there is no evidence that the Pacific private line customers who are paying for SARTS have received any other consequential benefits from their expenditures. API concludes that this Commission should either adjust the allocation of SARTS investment and savings as Selwyn recommends or disallow some or all of the costs of the SARTS program and remove those costs from all rate elements to which they have been assigned as Edwards recommends.

According to Edwards' calculations, Pacific's annual testing labor expense savings due to SARTS use is $96.6 million. He added that one could effectively and reliably double this amount of savings to reflect other savings that would emanate from implementing SARTS testing. He opined that Pacific has thus saved a minimum of $193 million on a service category-wide basis. Edwards apparently proposes spreading this expense over Pacific's service categories as an alternative to Selwyn's proposal. API goes on to note that Scholl identified hypothetical savings for 1986 which had resulted from implementation of the SSIMS project, of which SARTS is a component, at about $33 million.

API asserts that Ordering Paragraph 17 of D.86-01-026 which ordered Pacific to continue preparing its Report on the Results of Operations in the same general format employed in the R/O phase of this proceeding (i.e., using USOA accounting), and Shankey's testimony that Pacific's use of Functional Accounting created problems in tying Functional Accounting investments and allocations back to the R/O expenses, are reasons to reject the accuracy of Pacific's allocation of SARTS savings to the private line category through its use of Functional Accounting. API also cites what it claims to be contradictory statements by Scholl about whether SARTS is really only used for private line testing, and adds that these recurring cost studies are also affected by wide discrepancies in volumes.

For all these reasons, API urges this Commission to reject Pacific's private line recurring cost studies.

Turning to Pacific's incremental cost information, API takes the position that Pacific's incremental cost conclusions should be rejected because they fail to consider cost-reducing effects of derived channel service, i.e., Pacific's Poll Star alarm service technology, which Pacific used for the first time during the test year, and because Pacific's subscriber loop incremental cost study erroneously assumes no utilization of existing plant to satisfy additional demand, and uses inconsistent fill factor assumptions to account for spare capacity requirements.

2. Pacific's Nonrecurring Cost Study

API also urges that none of Pacific's nonrecurring rate increases be granted on the ground that discrepancies in Pacific's loading of labor rates, its time estimates for nonrecurring tasks, its recognition of efficiencies as identified in Exhibit 403, and its volume projections make the cost study unreliable.

With regard to labor rates, API points to three specific items which it believes to be unreasonable. First is the loaded labor rate element. In Pacific's example in Exhibit 334, it provides for $3.56 for paid absence and productive wages and salaries of $11.22 for a given employee. Edwards asserts that the paid absence amounts to 31% of wages, which he claims translates to an unreasonable 16 weeks of vacation or nonproductive time.

Within the same exhibit is reference to average work time hours/day of 4.55. Edwards testified that the methodologies used to calculate these labor rates would mean that rates per hour range from $37.52 to $61.54 and that Pacific was therefore spending from $78,000 to $120,000 on these employees, making the loads on actual wages three to four times the wage in many cases. API states that this is also unreasonable since, if it were correct, Pacific would have been operating with a negative cashflow.

Based on the personal observations of Edwards and the observations and experience of API's witness, Diane Martinez, API asserts that Pacific's panel of estimators overstated the frequency of occurrence of certain tasks. Martinez argued that Pacific's cost study overstates the costs of provisioning 3002C 2-wire bridged alarm private line service by at least 50%. Martinez based this opinion on her work at Pacific where she worked as an alarm service representative and, for a time, trained others to do that job. She apparently left Pacific something over one year before her testimony was prepared.

In support of her opinion she claims in Exhibit 354 that Pacific's Exhibit 271 overstates both the amount of time necessary to do certain tasks and the need for certain work groups to be involved in the task at all. She states that activity times designated for service representatives in Exhibit 271 do not reflect the streamlining mechanization or automation of the operation that has taken place in recent years. For example, she claims that order writers as a result of mechanization or automation no longer perform any tasks with respect to any private line alarm service order. Further, she states that the MA or "marketing administrator" virtually is never involved with respect to the provisioning of 2-wire private line alarm services. She concludes that the combined times of up to 74.4 minutes shown for the service representative, order writer, and marketing MA for processing a 3002C order ought to be 5 to 10 minutes. She also asserts that the activity time of 12.9 minutes for the NTEC to review order is unreasonably high.

As another example, Martinez suggests that task code 204, "update force mgmt sys," should not have an occurrence factor of 100% since it is apparently only done when there is a cancellation or due date change to the information already in the force management system.

API makes reference to Exhibit 403, Pacific's Special Services Administration Task Force Report (SSA Report), which, because it was prepared between one and two years after Pacific's nonrecurring costs were developed by its panel of estimators, identifies many instances where both recurring and non-recurring private line ("Special Services") provisioning has been streamlined resulting in concrete savings of many millions of dollars in the test year. API suggests that this report dooms the accuracy of the study results Scholl presented.

API also points out that the testimony of J. M. Swenson, filed in the utilization phase of this proceeding, stated that Pacific would process over three million inward service orders for residence and single line business customers in the test year, and that the annual capital cost for its 25 million idle assigned pairs would produce a savings of $84 million in expense by eliminating the need for installation visits and additional assignment costs. Exhibit 577, p. 19. Edwards states that Swenson's figures produce a cost of $28 for the assignment and installation of residence and single line business customers, while the nonrecurring cost study shows just the assignment cost for 3002C 2-wire loops to be $49 and the installation cost to be another $200. Based on these differences API argues that Swenson's testimony tends to discredit Scholl's cost of service claims relatively more than Scholl's studies discredit Swenson's claims, because of Swenson's greater familiarity with the plant itself. Swenson is Pacific's division staff manager in charge of engineering.

Turning to volume projections API asserts that Pacific's cost studies show inconsistencies. Edwards noted, as an example, that Exhibit 273 identifies 745 type 3002C channels, and that Pacific work papers assume approximately three local channels per circuit, but that another work paper showed 745 channels and 19,608 circuits, a phenomenon, which API describes as a physical impossibility. Further, Edwards testified that Sullivan's Exhibit 267 shows 14,000 type 3002C loops as opposed to the 745 shown in Exhibit 273 and the 14,041 shown in Exhibit 332. API states that the use of "internally consistent" incorrect volumes does not result in a wash as the Company brief apparently contends. Instead, asserts API, the result will be an "internally consistent" incorrect rate and incorrect earnings level--and not a correct development of rates.

3. DRA's Private Line Rate Recommendations

API urges this Commission to reject DRA's private line proposal as not being the result of independent analysis, and being the result of impaired objectivity brought on by either Shankey's excessive reliance upon, or erroneous interpretation of, prior Commission orders. API claims that Shankey's testimony demonstrated uncritical acceptance of Pacific's recurring costs which merely adjusted these costs to reflect the R/O decision. Edwards claims that such factoring adjustments will replicate the Pacific cost study discrepancies about which he testified.

API finds DRA's review of Pacific's nonrecurring costs to be better, but Edwards testified that Shankey improperly adjusted labor times by a factor that resulted in a double count. API also finds it inappropriate that Shankey's projected volumes were primarily the result of using Pacific's PLHF data, together with an adjustment factor jointly developed by Shankey and the Company.

Likewise API asserts that Shankey should not have accepted Pacific's loaded labor rates, and then only applied the R/O factor and his own factor to account for nonproductive time.

API states that Shankey's approach to Pacific's cost studies was result-oriented and therefore not as objective as it should have been in that he began with the notion that private line services were priced below costs. Further, API notes that Shankey was unaware of the results of the "Robin & Dackerman Report," Exhibit 401, or the SSA Report, Exhibit 403, and that this later information is another factor which reduces the value of DRA's recommendations for alarm services increases.

4. Import of the Robin & Dackerman Report and the SSA Report

These two reports, Exhibits 401 and 403, were received during the rebuttal phase of this proceeding. API contends that the former provides important evidence that both Pacific Bell personnel and its outside consultants viewed its private line cost studies as suspect and biased. Further, it submits that the SSA Report shows that approximately $160 million in savings have been and will be achieved in future years. API concludes that together these reports confirm the contradictions of Pacific's private line cost study.

F. The Critique of WBFAA

1. Introduction and Background

Like CBCHA/TCA the preference of Western Burglar and Fire Alarm Association (WBFAA) is that rate design be foregone until Pacific's next general rate case and, in the meantime, the surcharge now in place be continued, so that all ratepayers can benefit equally from Pacific's revenue requirement reduction. WBFAA opposes rate design changes because Pacific's uncertain cost studies, unclear revenue projections, and murky view of the future might, in its opinion, result in Pacific realizing unanticipated and undeserved revenues, and irreparable harm to the ratepayers. Should we choose to adopt a new rate design, WBFAA urges this Commission to adopt Pacific's proposal to separately tariff alarm transport services, its proposal to create two private line local loop rate schedules, and its test year recurring rate design for alarm transport services, but to reject Pacific's nonrecurring rate design for alarm transport services and its proposal for further alarm transport services in the second and third years, as well as DRA's proposals for recurring and nonrecurring rates for alarm transport services. WBFAA also asks that we refuse to consider any further private line rate increases until Pacific demonstrates that it can and will comply with the costing methodologies prescribed in the Cost Manual.

WBFAA is an association representing over 500, mostly small, burglar and fire alarm companies and equipment manufacturers in California. Rod Uffindell, current president of WBFAA and the owner and president of an alarm company, testified that the private line services utilized by the alarm industry include 1009, 3002C, 3007, 3009, DSAS, and Poll Star. He added: DSAS and Poll Star are already separately tariffed services. It makes sense to use the same treatment for those private line services that are unique to alarm services. (Exhibit 367, p. 16.) He explained that Poll Star is a derived channel or quasi private line service which is piggy-backed onto the customer's regular telephone service. He went on to note that 1009 services, including 1009A direct wire service and 1009B/C McCulloh service, are used exclusively by the alarm industry. He pointed out that, in addition to these alarm circuits, alarm companies also transmit alarm signals using either ordinary business lines or 800 service, and to a very limited extent, cable TV facilities and long range radio.

He explained that most alarm service subscribers use 1009 service but that many companies have installed multiplex receiving equipment which utilizes the voice grade 3002C bridged alarm service. He further stated that he was reluctant to make the investment necessary to use Poll Star because some Pacific employees have told him that Poll Star will be replaced with other technology and he fears he may end up with stranded investment.

2. Pacific's Recurring Cost Study

Central to WBFAA's criticism of Pacific's recurring cost study is its assertion that Pacific's volume information is not reliable. Choosing one of the private line services which it utilizes, 3002C, WBFAA asserts that the volumes used in Pacific's recurring cost studies and presented by Scholl in Exhibit 260, shows both a lack of understanding of how the service is used, and Pacific's failure to verify the information it presented. WBFAA points out the inaccuracy in the volume used for 3002C patron loops which Scholl acknowledged in his rebuttal testimony, Exhibit 402. WBFAA argues that the revisions Scholl submitted in Exhibit 402 also have volume errors since they show 11,382 full duplex (FDX) patron loops, and only 2,216 half duplex (HDX) patron loops though

Scholl acknowledged that the predominance of patron loops are HDX, which is less costly than FDX.

WBFAA also points out that Scholl's count of local loop volumes was 14% higher than the loop counts used by Sullivan. According to the testimony of WBFAA's economic consultant, Charles W. King, since Scholl allocated 80% of private line recurring cost and 95% of alarm private line recurring cost based on his overstated local loop count, an extra $72.3 million in investment costs was assigned to private line service that would not have been assigned using Sullivan's counts.

In response to Scholl's testimony that volume differences do not matter because both revenues and costs would change correspondingly and financial performance is a function of the relationship between unit costs and rates rather than the value of the category totals, WBFAA asserts that since aggregate investment was determined by multiplying unit costs by overstated unit volumes, Pacific's bottoms-up investment was overstated. Further, WBFAA contends that because tops-down investment is based on the proportion of private line local loops relative to total working loops for all service categories and since private line loop count was overstated by 14%, the allocation of most central office and all subscriber outside plant to private line would be correspondingly overstated, thus overstating tops-down investment too. Likewise, WBFAA claims that Pacific's revenue to cost ratios, which were developed by comparing these tops-down costs allocated among services based on overstated unit counts with actual revenues, are understated.

3. Tops-Down and Bottoms-Up Reconciliation

It is WBFAA's position that Pacific's bottoms-up studies are not true bottoms-up studies and therefore, there can be no real tops-down and bottoms-up reconciliation as our Cost Manual requires. Noting that Pacific's 1983 bottoms-up loop study for developing unit cost, identified the primary cost-causing characteristics of cable size, gauge, year of placement, and fill factor for each section of the cable, including the bridge tap, and that a computer program then applied unit capital cost dollars per pair foot by cable type, cable size and gauge for each of the loops, King asserts that the later loop study Pacific conducted for this proceeding has abandoned the procedure of synthesizing investment cost from actual, identified loop plant facilities which Pacific used in the 1983 loop study, for a plan which uses bottoms-up data from the sampled loops for the purpose of developing allocators to distribute the tops-down totals of subscriber access outside plant by primary plant account. He goes on to state: The synthesis of actual facilities costs is limited to central office equipment and interoffice outside plant. Loop plant is allocated from investment totals. (Exhibit 365, p. 9.) King argues that this is not a true bottoms-up cost study, and fails to meet the bottoms-up study criteria we set forth in D.85-02-030. WBFAA concludes that these facts justify our rejection of Pacific's rate design proposals.

4. Unexplained Loop Investment

WBFAA also argues that just as it did in the last rate case, Pacific has a great deal of unexplained subscriber loop investment. Via different sorts of calculations King suggests that this amount might be $3 billion, $2 billion, or $1.82 billion. The first figure is calculated by first comparing what he describes as Scholl's tops-down average loop cost of $515 to the 1984 tops-down amount of $441, and then applying the percentage difference to the 1984 bottoms-up unit cost and multiplying the difference between these two figures by 13.1 million, the number of working loops in Pacific's system.

WBFAA dismisses Scholl's explanation that the 1984 study did not properly account for ready-to-serve plant, by asserting that the 1984 study did include an allowance for RTS, and that the only use made of the RTS study in the present case is to inflate the kilofeet assigned to each service. WBFAA adds that even if it assumes Scholl is correct and adjusts its trended bottoms-up cost by 10% to reflect the failure of the earlier study's fill factor to include Pacific's estimate of "restricted" cable, there is still $2 billion unaccounted for.

Citing, as did API, the testimony of J. M. Swenson in the utilization phase of this proceeding (Exhibit 578), WBFAA adds the amount his testimony shows for investment per additional loop added from 1982 to 1985 related to feeder cable, and the amount of additional distribution cable, and dividing that sum by the number of available pairs added during those years arrives at an incremental investment per cable pair. Using that figure, WBFAA derives an average embedded cost per cable pair to which it then applies an outside plant utilization factor of 66.3% from Exhibit 412. The shortfall thus derived is then multiplied by the number of Pacific's loops to obtain the unexplained investment figure of $1.82 billion.

WBFAA also claims that Pacific's idle distribution loop plant quantities result in private line costs with unproven and probably unreasonable overheads. WBFAA suggests that it might be appropriate to allocate the cost of particular idle distribution to particular service, and states that since private lines are most often placed in high density locations it is likely that their requirement for redundant distribution cable pairs is significantly less than business and residence exchange lines.

5. Pacific's Nonrecurring Cost Study

Again WBFAA points to the discrepancies between the volumes in Scholl's studies and in Sullivan's work papers for 3002C service for the purpose of discrediting the service order volume projections proffered by Pacific. WBFAA pointed out that there are 26 patron loops for every sponsor loop. Uffindell testified that it was thus not credible for Pacific to attribute the same factors for patron and sponsor loop provision. Further, WBFAA asserts that Pacific's attribution of loop provisioning should trend downward because as the network expands and bridges are installed it is more likely that the simplest design loops will be provisioned.

Based on various calculations made by King, WBFAA states its belief that Pacific's nonrecurring costs were overstated by 28% or at least $30 million. It specifies that the cost study's 57M circuit central office equipment moves and changes costs and PADS (Pacific Administration Design Services) costs were overstated by 34% each due to Scholl's count of channel connections being 34% higher than Sullivan's, and that the other major item, inside wire costs were overstated by 60%, or $17.1 million, as a result of the FCC's detariffing of inside wire which became effective on January 1, 1987. (The FCC decision was issued after Pacific's studies were done). Altogether, WBFAA's claims of overstated costs would reduce Pacific's tops-down nonrecurring costs from $110.3 million to $79.9 million.

WBFAA also asserts that the company's work times were exaggerated and inaccurate, e.g. simple designs for a service had higher work times than more complex designs for the same service, work activity time for taking a patron loop order was erroneously assigned to an employee who was not involved in the process, travel times for going to the same account premises were different for different tasks. Further, WBFAA claims that Pacific's labor costs are excessive in that they have risen disproportionately since Pacific's last rate proceeding, and they show unreasonably low ratios of productive to nonproductive time.

6. DRA's Cost Review

WBFAA argues that Shankey's review of Pacific's nonrecurring costs should not be adopted because it only looked at one service and then applied the same findings to the remaining 62 services. WBFAA states that such an approach frustrates the very concept of disaggregation. WBFAA also claims that because rates for private line have increased much faster than inflation, and faster than exchange rates since 1979, DRA's goal of focusing on private line rates is unjustified.

7. Rate Design Proposals

WBFAA maintains that it makes sense for Pacific to separately tariff alarm transport services because Poll Star and DSAS are separately tariffed and telephone answering services are separately tariffed, and because it is consistent with the manner in which cost studies are performed, and will assist in the implementation of General Order 152 regarding service standards for the alarm industry. WBFAA claims that it makes sense to adopt dual loop schedules because it is logical to disaggregate rates just as costs for loops have been disaggregated.

Turning to nonrecurring rates, WBFAA claims that 1009 service demand is already on the decline due in part to prior increases in the nonrecurring charge for this service. Therefore, it urges caution in granting any further increases for 1009 service. It asserts, however, that the increase proposed for 3002C service from $179 to $275 plus the $14 bridging charge is more significant. WBFAA points out that this service cost $40 in 1979, and argues that nonrecurring costs are dropping, and that cost studies do not validate these rates.

WBFAA states that Sullivan's rate proposal for 3002C service would cause rate shock for alarm companies and require them to raise their customer's rates by large percentages. Uffindell testified that he would have to raise his rates to 3002 customers from $45 per month to $60.75 per month to recover the DRA-proposed recurring rate increases and maintain the same gross profit margin. WBFAA argues that granting these requested increases will result in a stranding of the alarm companies' investment in their 3002C receiving equipment and in Pacific's existing bridged alarm network. WBFAA also argues that DRA's proposal would increase rates beyond what AT&T charges for the same service on an interLATA basis.

As for Pacific's proposal for second and third year private line increases, WBFAA urges that they be denied due to the probability that Pacific's revenue requirement will decrease in the future, and Pacific's inability to reasonably approximate its costs and revenues for the future.

G. FEA's Position

FEA claims that Pacific's data on the price elasticity of demand for private line services, as shown in the addendum to Baughcum's testimony, Exhibit 360, show that rate increases of the magnitude proposed by Pacific and DRA will adversely impact private line users, cause a reduction in volumes of up to 11.38%, and result in self-supply or bypass by many private line customers. FEA points to Pacific data showing that private line service is nearly ten times as price elastic as residential access, which, it asserts, means that private line service must be priced in light of competitive alternatives. FEA also argues that Scholl's studies are based on embedded historical costs, not incremental costs, and thus rates may already be set at or above the appropriate economic costs.

FEA adds that Pacific's failure to provide incremental cost data by service category ignores "earlier Commission edict," specifically the Commission's statement in D.84-06-111 that the parties should address whether incremental or marginal cost analysis should be used as a basis for rate design decisions. For this failure, FEA recommends that Pacific's and DRA's rate proposals should be rejected.

H. General's Position on Private Line

General and other local exchange companies concur in Pacific's private line rates. Existing settlements agreements describe how the revenue from these rates is distributed among the concurring companies. General's witness, Jensik testified that the rates are based only on Pacific's costs. He asserts that all parties would benefit if the present scheme were eliminated in favor of access charging arrangements between exchange carriers. Jensik favors replacing private line settlements with bill and keep charges for jointly provided private lines. General would bill its customers its own rates for the portions of jointly provided services that it provides and would charge its customers Pacific's rates for the portions provided by Pacific. Jensik refers to this as "meet point billing."

Jensik also testified that adoption of Pacific's proposed deaveraged local loop rates would negate the administrative advantage and customer satisfaction General has experienced as a result of discontinuing charging suburban mileage on local loops pursuant to our order in D.84-07-108.

I. TASC's Position on Secretarial Line Charges

Secretarial line is one of the services which this Commission designates as "private line-like." Technically the service is not provided under Pacific's private line tariffs, but under its Network and Exchange Services tariffs. Nonetheless, the service has the characteristics of private line service and is appropriately addressed in conjunction with private line services. Pacific's opening brief explains that there are three types of secretarial line service. Type 6A service extends from the termination of the subscriber's loop in the central office serving the subscriber to the telephone answering service (TAS) premises; type 6B service extends from the end of the subscribers loop in the central office serving that subscriber to a concentrator located in the same central office; and type 27B service extends from the end of the subscriber's loop in the central office serving that subscriber to a concentrator not located in the central office.

Pacific also explains that each of these types of secretarial line service may be provided using one of five distinct circuit designs depending upon the number of of central offices and the type of facilities used to provide the circuit. Ninety percent of the service, however, is provided using two of these circuit designs and another nine percent is attributable to a third design.

Telephone Answering Services of California, Inc. (TASC) represents the interests of TAS operators. TASC continues to prefer the rate design propounded in DRA's motion of February 7, 1986, which removed the then-current surcharge, reduced message toll rates by $71 million and expanded certain ZUM zones in the San Francisco Bay area. TASC offers an alternative in the event this Commission chooses not to adopt the described DRA proposal.

1. <u>The TASC Proposal and its Rationale</u>

TASC's alternative proposes the following: (1) Adoption of two installation charges, one for secretarial line connections in which the TAS and its subscriber are served from the same central office (CO) and one where they are served out of different COs. TASC calls these single-CO and multi-CO lines and proposes that the charges be set at Pacific's cost of installation and removal (i.e., the in and out costs) except that no charge should exceed 100% of the existing $92 charge; (2) Adoption of an expanded definition of the charge for a "move" which would not be limited to moves occurring at the same premises, and which would be set at 50% of the new connection charge; (3) A study of the feasibility of a new tariff for bulk moves. TASC proposes that this tariff should reflect the economies of scale inherent when a TAS moves a large number of secretarial lines at once, and proposes that the tariff include an alternative payment arrangement based solely on the labor costs for the specific project so that there will be no dispute over whether the charges paid by the TAS did or did not cover Pacific's costs. TASC also proposes that Pacific be required to submit a proposal for such a tariff to CACD and to TASC for review.

In addition, claiming that the use of concentrators can obviate the need for more expensive multi-CO service instead of single-CO 6B or 27B service, TASC proposes that this Commission order Pacific to permit customer-owned concentrators to be placed in Pacific's central offices, or to order Pacific to participate in a joint endeavor with TASC to develop a program to accomplish such a goal.

In explaining why this Commission should not treat secretarial line service as a discretionary service which is undeserving of protection from rate increases, TASC asserts that there is no reliable substitute for secretarial line service, explaining that, for example, the possible alternatives of call forwarding or delayed call forwarding (DCF) to a DID number require programming of the telephone each time the service is enabled or disabled and/or are not universally available because the TAS subscriber CO must have call forwarding or DCF capability and the TAS CO must have DID capability.

Based on that premise, TASC goes on to explain that the point of its two-tier installation charge proposal is to provide an incentive for TAS subscribers to employ single-CO facilities while not prohibitively pricing the multi-CO lines for those who, for one reason or another, elect to employ them notwithstanding the higher rate. TAS points out that nearly all (over 99%) single-CO lines are non-designed, and that the cost of installing a single-CO line is several times the cost of installing a non-designed secretarial line. Table 2.1 of Pacific's Exhibit 402 shows the single-CO line installation cost to be $125 for 6A, $63 for 6B, and $126 for 27B, while TASC's witness Krause set the costs at $48, $44 and $49, respectively. See Exhibit 405, p. 19, Table 2.1. TASC points out that this single line service represents over 60% of all secretarial lines. Pacific's same table 2.1 shows multi-CO line installation costs to be $805 for 6A, $744 for 6B, and $811 for 27B, while Krause's Table 2.2 shows these three multi-CO services to have an average installation cost of $275. Thus, the effect of TASC's proposal with its 100% cap would be charges of a maximum of $126 for single-CO service and $184 for multi-CO service. Using Krause's figures, the charges would be $46 and $184. Pacific proposes an aggregate charge of $160, while DRA proposes an aggregate charge of $184.

One of the reasons TASC offers for limiting multi-CO service charge increases to 100%, aside from the fact that that has been a Commission policy, is that the alternative to multi-CO 6A service, single-CO concentrator service (6B/27B), is not always available. Another reason is that application of this cap will render moot, at least for purposes of this proceeding, the considerable controversy that exists with respect to the actual cost of installing multi-CO secretarial line connections.

2. TASC's View of Cost Estimates

Should we choose to consider Pacific's secretarial line nonrecurring cost estimates, TASC argues that Pacific's service order and channel connect costs are overstated. While maintaining its preference for our adoption of the charges recommended by Krause, described above, TASC urges that we at least apply the following considerations in designing secretarial line nonrecurring charges: (1) setting the same charge for all three types of single-CO lines for ease of administration; (2) reducing the existing aggregate charge as to single-CO service; (3) applying a 100% charge cap on multi-CO charges; (4) requiring Pacific to develop service order change costs based on TASC's broader definition of a change order; (5) requiring Pacific to file interim tariffs that establish the move charge for secretarial lines at 50% of the "new" installation charge until this Commission has adopted charges based on Pacific's newly developed costs; (6) requiring Pacific to submit a proposal for a bulk move tariff to CACD and TASC for review.

J. Discussion

1. The Tops-down Category Analysis

DRA's Shankey criticizes Pacific's use of Functional Accounting rather than the Uniform System of Accounts (USOA) in its category analysis for the disaggregation of its projected 1986 average historical costs. We are troubled by DRA's inability to verify the reconciliations Pacific claimed between its tops-down and its bottoms-up studies due to this change in investment definitions. However, it appears that the Functional Accounting system allows much more precision than the USOA in assigning costs to specific service categories, or even to subcategories. That being the case, we are unwilling to reject Pacific's use of Functional Accounting in this category analysis. What was lacking in the present instance was a ready means for the other parties to verify the "translation" from USOA to Functional Accounting. Such information was apparently available to Docter, but as he testified, he and his associates spent a great deal of time checking the logic and integrity of Pacific's Functional Accounting system. In the present instance the parties did have an opportunity to review Docter's report and cross-examine him. However, we are sympathetic with the difficulty of that endeavor leading to a careful evaluation and full understanding of the process in light of the enormous number of issues which this proceeding has presented.

The USOA which we refer to here is the system of accounting adopted by the Federal Communications Commission (FCC) in 1935. In 1987 the FCC issued Part 32, Uniform System of Accounts for Telephone Companies, which became effective January 1, 1988. Part 32 uses functional accounting. We issued an order instituting investigation, I.87-02-023, to determine if the Part 32 system should be adopted for companies subject to this Commission's jurisdiction. We concluded in D.87-12-063 that it should. During those hearings DRA recommended that the major telephone companies implement a data continuity mechanism for converting new data into the old USOA format. These companies all agreed to do so. This fact alleviates the major concern raised by DRA, at least as to future reliance on functional accounting. As for the present, while the use of Functional Accounting has added one more variable to this record, we are satisfied that Docter's assessment of its reliability is reasonably accurate, and that Pacific's use of Functional Accounting to distribute test year revenue, expense and investment has improved the reliability of Pacific's tops-down cost allocations to private line.

2. <u>Pacific's Recurring Cost Studies</u>

a. <u>Cost Manual Costing Procedures</u>

Attachment A to D.83-04-012 sets forth procedures to be used in the development of general customer premises equipment service costs and Attachment B sets forth procedures to be used in the development of private line service costs. These attachments are generally referred to as our "Cost Manuals." The cost element detail which Pacific's cost studies provide is basically in accord with Cost Manual requirements.

Scholl's Exhibit 260 provides Cost Manual unit cost values at pages 7-49 through 7-79. However, Pacific does not use the values derived using Cost Manual methodology as a basis for the cost projections on which it bases its revenue and rate proposals. Instead, its projections are based on average historical costs. At page 4-32 of his prepared testimony, Exhibit 260, Scholl states:

> "The average historical costs differ from the cost manual values in that the net plant factors are different from the depreciated investment factors, the return and income tax factors (R.I.T.) are different, and the depreciation rates are different. The effects of these differences vary by cost element. In general, cost manual numbers are lower than the average historical costs--largely due to a representation of depreciation expense

which is lower than that identified in the results of operations."

In D.83-04-012, we recognized that adoption of the Cost Manual procedures would result in costs that understate Pacific's net booked investment for particular product lines and services. We explained that this result is due to a rather substantial amount of stranded investment (which Pacific calls reserve deficiency) in Pacific's books of account. We were concerned that unless something was done to change depreciation practices this undepreciated investment would simply continue to grow. We concluded that our adoption of the Cost Manual procedures as recommended by the ALJ would bring that stranded investment into focus and allow some estimate of its size to become available. We noted that our adoption of these costing methods did not stop Pacific from proposing "anything it wants in the way of rates which would bring the revenues derived from such rates to the overall revenue requirement found reasonable by the Commission." (D.83-04-012, mimeo. at p. 8.)

Pacific has complied with this Cost Manual requirement. We can compare its Cost Manual results with its annual historical costs. For example, Exhibit 260 shows 3002C total test year 1986 annual Cost Manual costs to be $4.8 million (p. 7-59), while it shows average historical costs for the same service to total $5.0 million (p. 7-18); and, it shows Cost Manual costs for 1009C service to be $400,000 (p. 7-54), while average historical costs for that service are shown to be $410,000 (p. 7-23).

b. Recurring Cost Study Methodology

In our review of Pacific's various cost study proposals in D.85-02-030, we stated:

"We wish to make clear that we envision proper bottoms-up cost studies as filling at least two important functions: (1) to facilitate the further disaggregation of tops-down accounting costs on a service-specific basis and (2) to reveal the extent of inconsistency between tops-down accounting costs and identifiable bottoms-up costs of plant and operations, thus compelling the sort of reconciliation of differences which the Cost Manual prescribes. . . .

"We do not accept Pacific's assertion that 'true' bottoms-up cost studies are impossible. Of necessity, recourse must be had to Pacific's accounting books to establish investment values for items of plant employed to provide service, and so there may have to be a 'tops-down' element to any bottoms-up study of recurring costs. However, it appears that Pacific intends to substitute such tops-down allocations for any meaningful bottoms-up assembly of service costs." (D.85-02-030, mimeo. p. 13.)

CBCHA/TCA and WBFAA both take the position that Pacific has not complied with the intent of the above-cited statements. These parties take exception to the bottoms-up study's application of investment allocation factors, especially in the loop study. Loop investment is a significant portion of private line investment. A computation of the figures presented on p. 7-111 of Exhibit 260 shows it to be about 29% of Pacific's recurring private line investment.

Obviously our statement quoted above contemplated the need for <u>some</u> tops-down input into bottoms-up costs. The question is whether the use Pacific has made of allocation factors is reasonable.

For recurring costs other than loop costs, Pacific has used the allocation factors only to distribute certain tops-down derived secondary gross investments onto the indisputably bottoms-up derived weighted unit investment figures. The methodology Pacific has used to determine bottoms-up recurring costs for line haul, interoffice outside plant, CO-SAT, and Station SAT equipment is thorough and reliable. It certainly comports with this Commission's desire for the development of bottoms-up cost data.

c. Loop Study Methodology

Pacific's 1983 bottoms-up loop study, which WBFAA and CBCHA/TCA seem to regard as superior to the present effort, identified cost-causing characteristics (cable size, gauge, year of placement, and fill factor) for each portion of cable and calculated a unit capital cost per pair foot by cable type, size and gauge for each loop. Pole and conduit costs were separately determined and assigned. In the present loop study, Pacific skipped the step of building bottoms-up unit costs based on calculated costs of the various cost-causing loop characteristics. Instead, it simply calculated a statewide average loop length for in-service plant for each of its service offerings by plant account, and then allocated tops-down derived costs to the service offerings using the average relative loop lengths as allocation factors. CBCHA/TCA and WBFAA assert that this procedure prevents the loop study from being a bottoms-up study and therefore prevents the reconciliation between it and the tops-down category analysis from being credible.

Scholl disagrees with the critics, claiming that the loop study is a statistical analysis of bottoms-up determined loop characteristic information, and that the comparison between Pacific's tops-down total loop plant determined from the Company's records with the private line loop plant determined in the service specific loop study was a true bottoms-up/tops-down reconciliation as required by this Commission.

The application of allocation factors developed through bottoms-up studies is a proper means of further disaggregating tops-down costs. However, in order to judge the reasonableness of these allocation factors, we must have a sense of the reasonableness of the bottoms-up costs which underly them. The problem with Pacific's loop study is that so far as can be discerned from the evidence the only statistical analysis that Pacific makes of its bottoms-up determined loop characteristic information is to count the number of feet by plant account for each service offering. There is no indication that information about cable gauge was used in the analysis nor, as Selwyn pointed out, is there any indication that Pacific considered year of placement. The absence of consideration of these factors casts some doubt on whether the costs thus derived are truly historical costs. As a consequence it might be expected that the resultant allocation factors would be less precise and less reliable than those derived in the last general rate proceeding.

On the other hand, the 1983 study did not separately analyze costs for in-service and RTS plant--a fact which Scholl cites as a major reason for the large discrepancy between tops-down and bottoms-up costs in that proceeding. Pacific's decision to evaluate RTS plant on a separate basis from in-service plant seems to be reasonable. However, even if it is true, as Scholl asserts, that there is no truly bottoms-up unit cost value which could be appropriately applied to both working and RTS plant using this scheme of evaluation, we do not understand Scholl's position that Pacific could not use actual bottoms-up costs, at least for in-service plant, as input into its bottoms-up study, but had to rely on the tops-down analysis for this portion of the input.

We find no fault with the methodology Pacific used in gathering the bottoms-up data it did gather for this loop study. Length is clearly the most significant factor in determining loop cost and the source of Pacific's loop length data seems quite reliable. However, while it appears that Pacific's loop cost study reasonably portrays loop cost distribution among Pacific's service offerings, its reliability is reduced by its failure to allow a determination of the extent of inconsistency between tops-down and bottoms-up cost data as intended by D.85-02-030.

d. RTS Cost Development

The most significant impact of the RTS study is due to Pacific's decision to treat the cost of spare capacity as an incremental cost. This treatment, according to Pacific, lowers the cost attributable to RTS from the $2.6 billion figure referenced in its last rate proceeding to $1.038 billion. No party takes issue with the cost methodology used to arrive at this RTS cost.

Selwyn maintains that Pacific neither attempts to associate the nonworking capacity with private line service nor to justify the aggregate level of nonworking plant. He is correct that the cost study assumes that the distribution of spare capacity should be proportional to the distribution of working plant. Scholl's justification of its RTS plant levels is that the determination of how much subscriber loop plant to place is based on demand forecasts. He concludes that the RTS cost study "showed that building excess capacity to provide for the uncertainty of service demand locations, is the most economic long term design." (Ex. 260, p. 5-26.) In D.87-12-067 as modified we considered the possibility that Pacific is maintaining excess levels of plant for which ratepayers are receiving no benefit, and concluded that we would take no further action on the question until Pacific's modernization audits were completed. Obviously the reasonableness of Pacific's cost allocations would have been enhanced if Pacific had provided some showing that its present level of spare capacity is necessary. This issue presents one more item of imprecision which must be considered in evaluating overall rate changes.

As for appropriate distribution of total RTS plant among the various service offerings, Pacific's cost study distributed RTS in two ways, the first, which Pacific opted to use, was by in-service proportions. The second was by inward movement proportions. The two distributions are set forth in parallel columns at p. 46 of Exhibit 402. The variation is not great, nor has this record been apprised of any reason why one should be preferred to the other. In fact, the number of variables which must be calculated and then weighted in order to come up with a total inward movement proportion makes distribution by in-service proportion preferable absent some showing of prejudice, since the in-service proportion is less problematic.

e. Service Volumes

Turning to service volumes, we note that Pacific's cost studies were prepared based on projections from 1982 and 1983 data. Scholl testified that introducing later volume data does not invalidate Pacific's cost projections or proposed rates because total service costs and revenues would also change if quantities were to change, so that the revenue to cost ratio and the unit costs of providing the service would remain constant. This position assumes, of course, that volumes are relatively accurate in relationship to one another. As Edwards pointed out there is the possibility of volumes fluctuating while the revenues remain constant. He suggests that that is what the differences in the volume claims for 3002C alarm service between Scholl and Sullivan seem to do, and suggests that an internally consistent revenue and rate are not supported by such volumes.

In his rebuttal testimony, Scholl acknowledged that the volume figures Sullivan used employed a more accurate view of 3002C volumes. (Exhibit 402, p. 21.) He went on to assert that using Sullivan's volume figures rather than the ones he employed in Exhibit 260 results in absolutely no change in the identified unit cost of any of the local channel cost elements (loop, central office SAT, station SAT, bridging, signaling and conditioning), changes unit channel termination costs in only two mileage bands (by 2% and 6% respectively), and only makes a noticeable change in interoffice trunk costs--all of which are less than 9%. Further, on cross-examination Scholl explained that the study analysis performed to illustrate this fact (Exhibit 402 pp. 22-24), applied two-wire and four-wire proportions uniformly to 3002C service because the data base did not provide information from which it could be determined which were actually patron loops and which were sponsor loops. This accounts for the discrepancy between the proportions of sponsor and patron loops for full- and half-duplex 3002C service which WBFAA pointed out.

Sullivan's rebuttal (Exhibit 400) adequately explained the different volume figures Edwards cited, stating that the 14,041 figure referred to by Edwards is a total quantity for 1985 while 13,991 is a 1986 volume for half duplex only. He also testified that volume changes in his revenue impact calculations reflect the clean-up of Pacific records which Shankey referred to in his testimony. (Exhibit 330, p. 10.) Shankey testified that DRA's development of revenue effects used in-service and inward movement volumes based on Pacific's PLHF report. In cross-examination, Shankey expressed confidence that Pacific's PLHF volumes allowed DRA to be at the point where we feel that the volumes are accurate enough that we can now go forward and develop some kind of a trend. (90 Tr., 10822.)

We are well aware that Pacific has had difficulty in establishing accurate private line volumes in the past and the criticism of intervenors point up a continuing difficulty. However, we are satisfied by the testimony of Shankey as well as the explanations of Scholl and Sullivan that overall, Pacific's volume estimates were consistent enough so that cost attributions among the various private line services, while far from perfect, may be regarded as providing a generally accurate portrayal of relative volumes. Further, it appears that Pacific's PLHF program may well end the difficulty Pacific has experienced in the past in providing accurate volumes.

f. Assignment of SARTS to Recurring Costs

The appropriate allocation of SARTS costs was a major issue in this proceeding. Pacific describes SARTS as a system which permits the remote testing of voice grade special services, interoffice trunks and facilities more efficiently than certain other testing methods, thereby reducing maintenance testing expense. Selwyn and others claim that Pacific has assigned the costs of SARTS to specific private line services but has not determined the expense savings due to the SARTS investment. They assert that these expense savings are not being likewise assigned only to the services which are assigned the SARTS costs, and that this is the case because the labor expense for central office and field craftspersons are assigned to the various service categories and rate elements without a distinction as to the use or nonuse of SARTS. Scholl argues that this is not the case, and that the Functional Accounting system has separate function code accounts for specific labor expenses charged to various services, including interoffice trunks associated with in-service intraLATA voice special services, and that this results in the labor expense and savings resulting from the SARTS testing program to be assigned specifically just to those services which use it.

Of course to the extent the reasonableness of the Functional Accounting system is in question, so too is the reasonableness of these allocations in question. Assuming, as we have, that Pacific's use of Functional Accounting is reasonably reliable, its description of the manner in which testing costs and labor expenses for testing of interoffice trunks were specifically assigned to particular private line services under the Functional Accounting system make it clear that the methodology was appropriate, and that the concerns of Edwards and Selwyn that Pacific failed to appropriately account for cost savings arising from the use of the SARTS technology are not well founded.

The level of confidence which can be placed on the accuracy of these allocations is somewhat reduced by Pacific's failure to assign SARTS to 3002C service and later acknowledgment that this service did use SARTS testing.

3. Pacific's Nonrecurring Cost Study

Pacific incorporated a number of changes into its nonrecurring cost study in response to D.84-06-111, which improved the methodology substantially. Nonetheless, while no one has suggested a better means of producing bottoms-up nonrecurring costs, reliance upon panels of estimators naturally results in a degree of subjectivity which opens the study to criticism.

One of the major areas of criticism was that time estimates for labor activities were overstated. We agree that Pacific's nonrecurring labor cost projections are overstated. Scholl has acknowledged some of the errors pointed out by intervenors, such as the inappropriate inclusion of task assignments to market administrators and order writers cited in the testimony of Uffindell and Martinez, but Scholl's explanation of the duties inherent in such functions as the NTEC task of reviewing an order, the basis for identifying 57M and PADS expenses associated with nonrecurring costs, and his provision of such information as the fact that only 13% of Pacific's Loop Assignment Centers have been mechanized, lead us to disagree with the estimates of the magnitude of the overstatement of nonrecurring charges proposed by King, Uffindell, Martinez, O'Brien, or Edwards. We also reject WBFAA's contention that Pacific has overstated the costs of inside wiring. Scholl explained on cross-examination that the term was used to describe costs of the installation of wiring on the <u>network side</u> of the standard network interface. (Exhibit 402 at 50.) That being the case, the FCC's detariffing of inside wiring has no impact on Pacific's cost projection.

API supports the nonrecurring study conducted by DRA, but API's Edwards asserts that DRA should not have made a 15% adjustment for nonproductive labor time because such an adjustment was already included in Pacific's loaded labor rates, and therefore the nonproductive time was double counted. Shankey and Scholl both responded that API had misunderstood Pacific's loaded labor rate calculations, which, he stated, do not include allowances for personal, fatigue and delay factors. Shankey therefore stands by his adjustment.

Scholl states that Shankey's observed labor times were lower than those of the panel of estimators because he "stopped the watch" whenever there was a difficulty rather than considering a weighted average of work times and because Pacific's estimates include a weighting for those instances where a second work location is involved.

We recognize that Pacific's nonrecurring cost studies used rather old volume estimates and overstated work times. We do not agree with the critics that these studies are replete with drastic errors or omissions and are so grossly overstated as to be useless. Nor are we persuaded by the evidence about overstated task frequency of occurrence figures. Nonetheless, we agree that a moderate downward adjustment to Pacific's estimates is in order. The across-the-board adjustment proposed by DRA presents the sort of reasonable and moderate adjustment which is appropriate under these circumstances.

4. <u>Impact of Pacific's Other Reports</u>

WBFAA claims that the statement of the Robin & Dackerman report that it should cost Pacific Bell less to provide 3002 private line services for alarm circuits than to provide 3002 data circuits supports the proposal for a separate tariff for alarm transport services, and that accordingly, this service should be distinguished from 3002 data lines and offered at a lower price (Exhibit 401, p. 9.) API claims that the Robin & Dakerman report is important evidence that both Pacific Bell personnel and its outside consultants viewed its private line cost studies as suspect and biased. The apparent fact that Pacific paid Robin & Dakerman to produce this report does not alter the fact that the report provides the reader with no hint of any factual underpinning for its conclusions or the opinions of the Pacific and API employees which apparently provided input for these conclusions. Therefore, the document has no probative value as to either the validity of Pacific's cost studies or the cost characteristics of 3002 alarm circuits and data circuits, and we accord no weight to its conclusions.

As for Pacific's SSA Report, Exhibit 403, API asserts that it shows that Pacific's private line cost study and rate design is significantly overstated, adding that the amount of achieved savings described in the report comes to $23.8 million and the amount of future savings comes to $134.8 million. Of this latter amount, about $23 million is clearly projected as annual savings. WBFAA does not claim that Exhibit 403 invalidates Pacific's cost study, but asserts that the issues addressed by the report show that Pacific is improving its provisioning of private line services, and that the realization of those improvements will reduce the future costs of private line provision, thereby making the granting of rate increases unwarranted.

We agree with Pacific's position that its SSA Report does not have any bearing whatsoever on Pacific's cost data. The document was not completed until November 1986--well after Pacific's cost studies were completed. Pacific's decision to look for ways to improve the provisioning of its special services, of which private line is one, is to be commended. The report indicates Pacific's belief that if all goes well, Pacific may see an increase in profitability in areas the report targets. However, it does not provide this Commission with reason to adjust or ignore the projections of Pacific's cost studies.

5. <u>Deaveraged Local Loop Rates</u>

The division point for the Schedule I and Schedule II local loop rates which Pacific proposes is set so that about 76% of all private line loops will be included in the definition of the lower priced Schedule I serving wire centers. Pacific does not specify what the cutoff point is in terms of ratio of average cost for Schedule I wire centers to statewide average cost, but it is certainly greater than 75%. Selwyn would provide lower rates in two tiers, but only include about 37% of the local loops altogether, with the first tier being for the six urban wire centers with average costs less than 50% of the statewide average and containing about 10% of all local loops and the second tier being for an additional 27% of customers served by wire centers with costs between 50% and 75% of the statewide average.

We are not inclined to authorize any deaveraging plan for private line local loop rates. The tradeoff, as we see it, is between lowering the rates for the largest urban users, while increasing the rates (at least proportionately) for smaller, more rural users. The fact that these users are businesses rather than residential users does not detract from our underlying concern that telephone service be universally available. To the extent that we permit deaveraged rates which disadvantage the small consumer, we are working against that principle. Furthermore, we agree with DRA that since loop costs are driven primarily by loop length, this proposal would inequitably charge customers in the high cost wire centers who happen to have short loops. We believe such a plan is only justifiable where there is strong evidence that alternative rates will disadvantage ratepayers generally in the long run. That is the argument that the parties make here, but it is not supported by the evidence. We remind the parties that our concern is with <u>uneconomic</u> bypass. So far as we can ascertain from the record before us, there is no imminent threat of uneconomic bypass should

Pacific retain a single local loop rate. We will not authorize deaveraged local loop rates.

6. Separate Alarm Transport Tariff

Pacific's proposal for a separate alarm transport tariff would increase nonrecurring charges for alarm transport customers by only 20% rather than the 25% Pacific proposes for other private line customers, smaller loop rate increases, and, where bridging is used, a small decrease in the rates for associated channel equipment and bridging. Sullivan's explanation of this proposal is baffling. He states: "We believe that the combination of increased prices and the availability of service alternatives will result in a reduction and ultimately the elimination of any perceived subsidy in this market." (Exhibit 283, p. 21.) Perhaps the meaning of Sullivan's cryptic statement will become clear in the future, but for now we perceive a subsidy, and one which would be larger for alarm transport services than for other private line services. We do not perceive a continued need to shield alarm transport customers from bearing their fair share of the costs of providing service to them. Since we see no need to distinguish alarm transport service rates from other private line rates and since we are not convinced by the parties' arguments favoring separate tariffs, we will not grant either separate rates or separate tariff treatment.

7. Secretarial Line Rates

TASC's assertions about secretarial lines seems to assume that this Commission's rate design policy does not recognize the importance of secretarial lines, and attempts to convince us that secretarial line service is, indeed, important. We do not doubt that fact. However, it does not give rise, as TASC would apparently like us to find it does, to the conclusion that we must treat secretarial line rates in the same way in which we treat rates for basic residence service. Our conviction about the need to preserve universal telephone service does not encompass the notion that secretarial line service must be set at rates which will assure universal availability. To the extent possible and reasonable secretarial line rates should be set to at least recover costs.

Since it is not our intent to adopt the across-the-board rate changes which TASC prefers, we therefore address below the secretarial line proposals presented.

a. Disaggregated Installation Charges

TASC proposes two separate secretarial line installation charges instead of one in order to recognize the difference in costs between installation of designed lines and nondesigned lines. Shankey testified that DRA's opposition to such a rate design is based on the same reason as its opposition to Pacific's proposal for two local loop rates. There is no dispute that a designed line displays significant differences from a nondesigned line, or that the very, very low incidence of designed single-CO line service makes it possible to accomplish charge disaggregation by setting one charge for single-CO line service and another for multi-CO line service, each charge being based on its disaggregated average costs. Were that the only consideration it would appear that DRA's main criticism of Pacific's loop rate proposal--its arbitrary cut-off point, and the small difference in average costs between the two groups--would be inapplicable to TASC's proposal.

It is clear that TASC's proposal would result in a much lower overall revenue recovery than would a single charge based on aggregate costs. Pacific proposes increasing this aggregated service charge element from its present $92 to $160. DRA proposes an aggregate increase to $184, but TASC would increase charges to $184 for only about 38% of subscribers while setting it for the other 62% of subscribers at somewhere between $126 (if we were to adopt Pacific's cost figures), and $46 (if we were to adopt Krause's cost figures).

We can distinguish the issue of deaveraging secretarial lines from the issue of deaveraging local loops. Not only are designed and non-designed secretarial lines different enough physically and in their costs as to impose different installation charges, the secretarial line customer in most cases has service alternatives that would enable him to avoid the purchase of designed lines.

As TASC properly pointed out, price averaging removes the incentive that a customer might have to use a less expensive configuration. Given that the rate for a designed line is now well below any estimate of its cost, the general body of ratepayers are made worse off each time a designed line is ordered. While it also may be true that customer and TAS choices about whether to use a designed line may be limited by accidents of location or Pacific's available technology, a more proper pricing differential will give TASs the incentive to locate so as to minimize not only their own costs but those of Pacific as well. Similarly, a price increase for averaged secretarial line service sufficient to make up a substantial portion of the deficit from designed lines would necessarily price non-designed lines far above their cost. This would harm TASs and their customers who would like to use the lower-cost non-designed lines but might be priced out of the market so that designed lines could be cross-subsidized.

A final consideration is that TASs operate in a competitive voice messaging market that features several alternatives. Indeed, Pacific has made public announcements as to its intent to provide voice mail, a service that would compete with answering services. As another example, inexpensive and reliable answering machines are widely available. Given the significance of secretarial lines for the provision of one of these competitive alternatives, it is important that we price them as near to cost as is feasible. In particular, the overpricing of non-designed lines so as to subsidize designed lines would hinder TASs that were attempting to use the most economical available technology to provide their service in this market.

In attempting to determine the appropriate charges for secretarial line installation, we note that Krause's calculations suggest that a charge of $133 would achieve cost coverage for the aggregated installation charge, while Pacific and DRA assume the costs are far more than 100% of present charges. DRA chooses to cap the charge at a 100% increase while Pacific chooses to increase this charge by about 75%. Sullivan testified that Pacific's private line rate design treats secretarial lines separately to avoid an excessive increase in one year. On this same theme of the impact of increases, TASC argues that secretarial line subscribers should be protected from large increases because the service is not discretionary, in that some TAS subscribers cannot make use of secretarial line alternatives such as call forwarding and DCF because their CO doesn't have that capability and/or the TAS CO doesn't have DID capability.

The first question we must answer is whether the cost studies support charges as high as Pacific and DRA propose. Then we must determine what constitutes reasonable charges for this service.

TASC claims there are several errors in Pacific's nonrecurring charge studies, as they apply to the installation of secretarial lines. It claims an error in the time a service representative needs to process a service order, and based on the testimony of Gladstone, and Martinez reduces Pacific's estimate from 19 minutes to 3 minutes. This change (along with TASC's elimination of any allocations for marketing) is the primary basis for TASC's reduction of Pacific's estimated overall cost of $29.37 to $8.14, though TASC's conclusion that Pacific's claim of marketing costs attributable to these services is implausible and TASC's deletion of any allocation for it is also a factor.

TASC also criticized other aspects of Pacific's cost projections. First, it points out that Pacific misplaced a decimal point and showed an occurrence factor for certain "IMF and I&M" work activities which Pacific later acknowledged was ten times higher than it should have been, and also acknowledged that it had miscalculated an input for the 6A2 line which resulted in a reduction of that input from $442 to $276. It also cites several instances of incredible ranges of time estimates from the panel of estimators. It goes on to suggest that Pacific's reassessment of the multi-CO secretarial line costs and its adjustments that reflect new subjective determinations by one member of the panel of estimators had the effect of partially offsetting the "premise occurrence" and "calculation error" adjustment which TASC had criticized, and is unreliable.

TASC further finds fault with Pacific's choice of weighting the high, usual and low time estimates on a 1:4:1 basis, asserting that such weighting presumes that everything goes right too infrequently, and claims that the confusion in the record about Krause's use of Shankey's observed work times, and Scholl's criticism of that use is another example of why this Commission cannot confidently set a NRC for multi-CO lines. Finally, TASC claims that Pacific could achieve cost reductions if it would employ the SLC-96 as an alternative to a standard concentrator.

There is no doubt that Pacific's cost studies are imperfect. Cost studies encompassing so much material could hardly be otherwise. Aside from simple mathematical errors, there are hundreds of points where choices must be made, and there are generally arguments which can support choices different from the one selected. We do not find Pacific's methodology to be so sloppy or ill-conceived that its cost studies deserve to be ignored. Still, we are convinced by the anecdotal testimony as well as

Shankey's survey that the nonrecurring cost figures derived from the panel of estimators are most likely overstated in many instances. We do not find Krause's worktime estimates for secretarial orders to be appropriate either. They minimize or delete costs to an unreasonable degree. While it may not be possible to derive an exact amount, we do not doubt that overall secretarial line installation charges are presently less than half the costs for that service.

It has been our policy in recent times to restrict nonrecurring charge increases to no more than 100%, where costs would justify more, in order to ameliorate rate shock. Pacific would have us adopt a lesser increase for secretarial line installation. The tradeoff for reduced increases, of course, it that someone else must pay. We are not convinced of the necessity of following Pacific's proposal in this matter. We will adopt a 100% increase in secretarial line installation charges as proposed by DRA.

We will apply this increase to the revenue allocation for the class of secretarial line service before disaggregating rates into separate charges for designed and non-designed installation. As the previous discussion indicates, we will use Pacific's cost study showing that a non-designed line costs $125 to install; we will set the non-designed installation rate at that level. Given this, we will set the designed line installation charge at $277 to achieve the 100% class revenue increase. While we acknowledge that this is an especially large increase for designed lines, we note that even TASC's Krause calculated a designed-line installation cost of $275; by contrast, Pacific's estimates were over $500 higher.

Appropriate tariff language is needed to distinguish designed from non-designed secretarial lines. We do not have such language before us for adoption in this decision, so we should order Pacific to file an advice letter containing this tariff language. Non-designed lines should be distinguished from designed secretarial lines based on the single versus multi central office description that TASC developed on the record. The deaveraged secretarial line installation rates that we order in this decision will take effect upon approval of this advice letter.

b. Move and Bulk Move Charges

TASC claims that there is no justification for Pacific charging for a new installation any time a TAS subscriber moves from one premises to another in the same or a different building. It takes the position that the language of the present tariff is overbroad, and asserts that the present charge for the relocation of the end of a channel at the existing customer premises should be expanded to include any relocation which does not alter the design, operation or function of the secretarial line service so long as both premises are served by the same central office. TASC contends that the cost study's failure to differentiate between work activity costs which occur only upon the initial installation of a new secretarial line connection, and those that are required for both a move and a new installation result in an overstatement of "channel connect establish" and "channel connect out" costs for moves in the category it has described. TASC urges that we adopt a new "move" charge for secretarial lines at 50% of the new installation charge until we have better cost information. We are not persuaded by TASC's arguments. We agree with Pacific that the definition of a move charge which TASC proposes is inconsistent with Pacific's cost studies as well as the tariffs. We will deny TASC's proposal. Similarly, there in not sufficient evidence in this record to warrant our requiring Pacific to submit a proposal for a bulk move tariff as TASC requests.

We will also deny TASC's request that we order Pacific to permit outside parties to place concentrators in

Pacific's central offices. In light of the considerable questions of liability, safety, protection of property, etc., there was not a sufficient evidentiary showing of reasonableness.

8. **Miscellaneous Private Line Issues**

Pacific has requested that certain telegraph private line services be limited to those customers currently receiving the service. We will grant that request. It appears that there is no longer a demand for these services.

FEA requests that we reject Pacific's cost proposals for failure to provide sufficient incremental cost data. We decline to do so. Pacific's incremental cost study complies with the requirements of D.84-06-111.

9. **Appropriate Private Line Rates**

Applying allocation factors to the tops-down data (booked outside plant investment) assures that this element of the cost study will achieve closure with the tops-down study. Such a practice gives the appearance of a much improved reconciliation between total tops-down and bottoms-up data. However, we have no way of judging how reliable this information might be. We are certainly not confident of the accuracy of the 5% discrepancy Pacific suggests. We are confident, however, that the refinements to the category analysis and to the non-loop components of the recurring cost study have improved the reliability of those two studies, and that fact suggests the likelihood that Pacific's bottoms-up studies do, in fact, account for many of the costs which went unidentified in the last rate proceeding.

One of the benefits of a bottoms-up cost study is that it provides a way of further disaggregating tops-down costs. Docter's testimony makes it clear that the category analysis process by which Pacific assigned costs to the private line service offering in this proceeding was much more refined and much more reliable than previous tops-down analyses. Further, the category analysis itself provided some disaggregation of private line costs.

As we said in D.84-06-111, the purpose of the bottoms-up studies is not to validate the category analysis but to carry it one step further through cost-based apportionment of the category costs to specific service offerings.

Therefore, Pacific's flawed tops-down to bottoms-up cost study reconciliation does not discredit the category analysis results. It simply compels caution in setting rates based on those results. The cost studies do not permit this Commission to set rates for private line services upon a precise cost basis, but these cost studies, for the most part, have once again shown progress in moving toward a more accurate and finely disaggregated tops-down analysis on the one hand, and the development of bottoms-up studies which will facilitate differential pricing of specific private line services on the other.

As with the studies for recurring costs, Pacific's nonrecurring cost study displays many imperfections. Nonetheless, the study is an admirable effort to provide better information about the costs of provisioning activities for private line service offerings. Application of the reasonable but moderate downward adjustment to these costs which DRA proposes, and even application of Scholl's private line nonrecurring cost scaling factor of .94 still reveals an unacceptably low revenue to cost ratio.

Together, Pacific's cost studies show a clear need for substantial rate increases. When weighed against the possibilities for error, especially in the recurring rate bottoms-up studies, we find it reasonable to provide private line rate increases for one year rather than incremental increases over three years as Pacific proposes.

Considering that the shortfall for nonrecurring private line charges will have to be collected from other customers, we see no reason to adopt Pacific's proposal for nonrecurring rate increases of only 25%. The shortfall is too large and the evidence of customer hardship insufficient to justify such a departure from our usual rate policies with respect to services for which rates are being moved toward costs. We will adopt the nonrecurring rates proposed by DRA.

Nor do we intend to set recurring rate increases at the rates Pacific proposes for the first year of its 3-year proposal, ignoring the effect of the proposed increases for the second and third years. The cost studies justify a much greater increase than that. Thus we will adopt the DRA proposal, which provides a substantially lower cumulative revenue increase (about half), but a larger increase for the test year than Pacific proposes.

Adoption of these rate proposals will result in a test year revenue increase for private line services of $67.020 million.

VIII. Settlements Effects

In March, 1985 we issued I.85-03-078, making all California independent telephone companies (ITCs) which interconnect their facilities with those of Pacific respondents for the purpose of investigating the effect of rate revisions to be granted to Pacific in the present general rate proceeding on separations procedures and intercompany settlements and revenues as related to intrastate toll and private line rates concurred in by these ITCs and related matters. We held five days of hearings on these issues in September and December 1986. The parties which participated in this phase all briefed the settlements effects issue in concurrently filed opening and closing briefs.

A. Background

As a result of decisions by the federal courts and the Federal Communications Commission (FCC) which restructured the Bell System and allowed entry of competition into the interstate and intrastate, interLATA long distance marketplace at the beginning of

1984, the traditional system of cost allocation, division of revenues, and ratemaking for long-distance telecommunications (toll) services was replaced with a system of exchange access charges and interexchange transmission charges to compensate local exchange carriers for the origination and termination of interstate traffic. This Commission opened a proceeding to determine access rates and related matters.

The ITCs were joined as parties to the access proceeding by an Order Instituting Investigation (OII). Under the jurisdiction established by that OII we approved the concurrence of ITCs in Pacific's access services tariffs along with their agreement with Pacific to pool all costs and revenues associated with access charges. At the same time we recognized that although there were serious time constraints imposed by the federal court as well as limitations on our staff's ability to review additional rate proposals, any ITC opting for a "bill and keep" approach to access charges and establishing its own access tariffs reflecting its own costs of offering access services had the right to do so, so long as it did not disadvantage the general body of ratepayers or impose inordinate administrative burdens on our staff. (D.83-12-024 at 137.) General and its affiliate West Coast Telephone Company chose to establish their own "bill and keep" access tariffs. The others adopted concurring tariffs.

A major purpose of this new system of separate access charges was to reduce the allocation of costs to toll services by relieving them of some of the burden of overallocated local network costs which they then bore. We did so as we have explained above by adopting a policy of gradual and moderate reductions in tariffs for intrastate, interLATA access services. This policy came to be known as "SPF to SLU," referring to a gradual shift in cost allocation factors from the use of a subscriber plant factor to the use of a subscriber line usage factor.

As a result of adopting the SPF to SLU policy as well as other rate changes D.85-06-115, our next major decision in the access proceeding, significantly reduced Pacific's intrastate access charges. To make the effect of the change revenue neutral to Pacific it was necessary to authorize an increase in the existing billing surcharge applied to most of Pacific's nonaccess rates.

Since smaller ITC rates have normally been set on a residual basis after taking account of the contribution of toll settlements (now including settlements from the intrastate access revenue pool), and since access revenues are a relatively high proportion of total revenues for most ITCs, the adopted reduction in Pacific's access revenue objective would have reduced the pool on which the ITCs could draw thereby potentially causing the ITCs to institute relatively high (as compared with Pacific) percentage increases on their basic local rates to meet their revenue requirements. Therefore, a number of the small ITCs which concurred in Pacific's access rates asked that we protect them from such disproportionate impacts.

Recognizing that while PU Code § 728 does not mandate the same or similar rates it does require that comparability of rates between similar neighboring service areas be considered in setting rates for exchange carriers, and also recognizing that we had authorized a similar equitable principle, that of rate averaging, to allow the rates of Pacific's rural ratepayers to be similar to those of its urban ratepayers, we determined that it was reasonable to apply a comparability test to the relationship between Pacific's basic exchange rates and basic exchange rates of interconnected ITCs concurring in Pacific's access rates. We concluded that the disproportionate impact of the Pacific access charge changes warranted, as an interim measure, the provision of a means of compensating for the total diminution in ITC access services revenues. We accomplished that end by ordering an interim surcharge for Pacific and all the ITCs and ordering that the revenue from this surcharge increase would be included in the access services revenue pool. The order stated that Pacific and the ITCs were to make advice letter filings pursuant to General Order (GO) 96-A to amend their tariffs to implement this additional billing surcharge.

Since we intended this surcharge to exist only until a new rate design was authorized for Pacific in the present rate proceeding, and since the new interstate High Cost Fund (HCF) would, when fully implemented in 1991, protect the ITC's customers against unreasonably burdensome local exchange rates, D.85-06-115 also authorized as a longer term interim solution an intrastate HCF which would draw upon the intrastate carrier common line charge (CCLC) revenues from Pacific and those ITCs which concur in its access services tariff and in the associated revenue pool to assure that ITC exchange rates remain within a reasonable range of comparison with Pacific's exchange rates in comparable neighboring exchanges.

The interstate HCF, when and if fully implemented will allow exchange carriers with fewer than 50,000 access lines to recover, from a fund financed by interstate CCLCs, 100% of that portion of their local loop NTS costs exceeding 150% of the national average local loop costs, and 75% of such NTS costs within the range of 115% to 150% of the national average. Larger IECs will recover somewhat less from the interstate HCF.[8] As we pointed out in D.85-06-115 the effect of this assignment of high

8 As of January 1, 1988 the FCC implemented changes in the HCF formula. "Smaller" companies are now considered to be those with fewer than 200,000 working loops. Such smaller companies will be eligible to recover 90% of their local loop NTS costs within the range of 115% to 150% of the national average and 100% of their local loop NTS costs above 150% of the national average. Larger companies will receive somewhat less HCF support.

NTS costs to interstate CCLCs will be that the intrastate local loop costs of even the highest-cost ITCs will be less than 130% of the national average.

Because eligibility for the intrastate HCF proposal we adopted is based on a comparison of local exchange rates rather than costs, and thus unlike its interstate counterpart addresses all ITC operating costs rather than just the differences in local loop NTS costs, and because our adopted approach tends to concentrate the impact of all differences in operating costs on basic exchange rates, the "comparable rates" standard we adopted only permits an ITC to claim relief from the intrastate HCF after we have determined a revenue requirement for the ITC, and thus presumably weeded out any imprudently incurred costs. Further, we stated that our revenue requirement determination would remain in effect for a maximum of one year unless we extended it.

The same rates/costs distinction also convinced us to allow relief from the intrastate HCF only to the extent necessary to permit an ITC's basic exchange rates to be set at no more than 200% of the basic exchange rates charged by Pacific in comparable neighboring exchanges, rather than the 130% which the ITCs were then seeking.

Recognizing that many ITCs would not have current Commission-determined revenue requirements, and therefore would not be immediately eligible for the intrastate HCF at the time of the issuance of a decision terminating the pooled surcharge in the present proceeding, D.85-06-115 reiterated our authorization of ITC advice letter filings for a bill and keep surcharge, calculated to generate revenue equivalent to that generated from the present pooled surcharge, to become effective upon the issuance of this decision.

In preparation for that filing we required each ITC to file with the Telecommunications Branch of CACD and to serve on any persons requesting a copy, a report projecting the revenue requirements impact for that ITC of the reduction in the access services revenue pool which would result from eliminating surcharge revenues from the pool when this decision became effective. We ordered that the report propose a rate design to respond to the projected impact. This rate design was to be a proposal for either applying the new bill and keep surcharge to all the intraLATA services to which the present pooled surcharge applies or applying it to all those services plus all access services, and a proposal for the magnitude of the surcharge based on how it would be applied.

I.85-03-078, the OII consolidated with the present matter, finds that the interconnecting facilities of other telephone corporations in California will be affected by any general rate revisions granted to Pacific insofar as those revisions affect separations procedures and intercompany settlements and revenues as related to intrastate toll and private line rates concurred in by the ITCs, other rate changes in Pacific's tariffs, and any construction of interconnecting facilities. It was issued for the stated purpose of determining the reasonableness of the rates, tolls, rules, charges, operations, costs, separations, practices, contracts, and the adequacy of service facilities of Pacific and all the telephone corporations operating within the state of California interconnecting their facilities with those of Pacific.

To that end the OII ordered Pacific to file compliance reports setting forth the estimated settlements effects of the proposed rates of Pacific and the proposed rates of DRA upon each respondent ITC. It further ordered that each respondent ITC file a report of total California results of operations and of separated California intrastate results of operations for calendar year 1986 estimated at present rates and charges and the year 1986 first adjusted to include the effects of Pacific's requested rates and charges in A.85-01-034 and second adjusted for DRA's proposed rates and charges. These reports and the projected revenue requirements impact and rate design reports were timely filed.

B. Initial Positions of Parties

1. The ITCs

At the hearings on this issue the ITCs presented evidence of the revenue effects and projected bill and keep surcharge requirements they expected to result from elimination of the present billing surcharge from the access services revenue pool.

Additionally, the ITCs requested that the direct assignment of interLATA WATS and the proposed intraLATA SPF to SLU transition, if adopted, be pooled or treated as a loss of pooled revenue. To this end some presented evidence of the reduction of available pooled settlements revenue they expected to result from access charge reductions accompanying the direct assignment of intrastate interLATA WATS becoming effective on January 1, 1987, and the reduction of available pooled settlements revenue they expected to result if the intraLATA SPF to SLU transition proposed by DRA and endorsed by Pacific in this proceeding were adopted. Further, where relevant, the ITCs who addressed the matter assumed that the surcharge revenues should not be treated as exchange revenues for purposes of EAS settlements. They point out that the bill and keep surcharge would need to be larger otherwise. Many ITCs also recommend that all other settlements effects be offset against each other and combined with the losses from the access services revenue pool, the direct assignment of WATS and the intraLATA transition from SPF to SLU to produce a single surcharge.

Some of the ITCs also proposed new local exchange rate designs as an alternative to the bill and keep surcharge, or they proposed that this Commission permit them to transfer their surcharge revenue requirement to their local exchange rate schedule by a uniform percentage increase in each rate category. Once this is done they propose that this Commission authorize those companies whose local exchange rates qualify for the intrastate HCF to collect such funds immediately.

In rebuttal testimony Pacific and most of the smaller ITCs agreed to the basic concepts of a Local Rate Stabilization (LRS) plan and fund which was presented by Pacific's witness, Ondeck in Exhibit 386. Unlike the authorized HCF, the LRS plan retains the local exchange rate funding source of the present surcharge rather than receiving funding from intrastate CCLCs. It accomplishes this by replacing the surcharge with an adjustment to local exchange rates. DRA also offered a rate design proposal which differed somewhat from that set out in D.85-06-115. Most of the ITCs opposed DRA's proposal.

2. DRA

Pointing out that these matters had already been authorized by D.85-06-115, DRA's witness Marks testified that staff agreed that the effect of the elimination of the present intraLATA surcharge should be recovered by the ITCs by an advice letter filing coincident with the final rate order in this proceeding and that the effects on the ITCs of the direct assignment of WATS should be adjusted by a revised surcharge effective January 1, 1987 (as it was). Marks stated, however, that staff did not agree that reduced settlements resulting from the adoption of rate design changes proposed in the present proceeding should be likewise offset. She stated that such rate increases should only be granted after Commission rate review during a general rate application or a GO 96-A rate application. On cross-examination Marks agreed that a regulatory log jam would be created if all the ITCs filed for rate relief simultaneously.

DRA's Shantz' testimony recommended that specific rates be adopted for the ITCs in lieu of the bill and keep surcharges authorized in D.85-06-115. His recommended ITC rate revisions only addressed the changes in revenue requirement associated with the elimination of the pooled billing surcharge. Specifically, he recommended increasing service connection charges up to a level 100% and then increasing the rates for basic exchange services up to the amount necessary to recover the pooled surcharge revenue loss, using a uniform percentage increase with rate maximums not to exceed 100% of Pacific's comparable rates. His testimony was based on Pacific rates then in place but recommended that final rates be adjusted to reflect the actual rates authorized by this decision. Under Shantz' scheme revenue requirement (after being established in a Commission rate review) could be recovered from the intrastate HCF to the extent it could not be met by these increased rates or other revenue sources.

3. General

General does not concur in Pacific's access services tariffs and thus is not a participant in the pooled surcharge that we ordered in D.85-06-115 or in the access services revenue pool. However, General's witness, Jensik, testified that several of Pacific's rate design proposals will have unspecified negative settlements effects on General, which General wishes to eliminate by alternative proposals. Jensik also testified that General wishes to increase its basic local service rates to recover any settlements revenue deficiency which results from any rate design changes we adopt for Pacific. Though it is not clear from his testimony, it appears that Jensik was asking that we authorize such recovery in this decision.

C. The Motion for Leave to Late-File Brief

About three months after the briefs were filed in the present matter a motion was filed with the Commission on behalf of DRA, Pacific, General, and twenty other ITCs. The motion requests leave to late-file a joint supplemental brief on HCF issues and asserts that good cause exists for granting such leave because the joint brief presents a compromise consensus position and recommendation submitted by all parties who actively participated in the high-cost fund phase of the hearings and briefing, with the sole exception of General. It goes on to explain that General joins in the motion that the filing be permitted, but does not join as a party to the proposal solely because General and the DRA were unable to reach agreement on the question whether General should be included within the settlement effects mechanism set forth in the brief for the rural and small metro[politan] independent companies.

The ALJ issued a ruling dated June 4, 1987 granting the motion for good cause shown and instructing the parties that they had 15 days to respond to the joint supplemental brief. Two parties responded within the 15 days, General and AT&T. A third party, MCI, filed an opposition to the motion. This opposition does not address any procedural reason why the motion should not have been granted, but instead addresses the substance of the joint proposal. Therefore, we uphold the ALJ's granting of the joint motion. We note that MCI's pleading was not filed within the required 15 days of the ALJ's Ruling. It was filed 26 days after that ruling, but 30 days after the joint motion was filed. Since 30 days is the common time for filing a protest, and since MCI's filing is in the nature of a protest, we will treat it as timely filed and consider its contents as a timely response to the joint supplemental brief.

D. The Joint Proposal

As a predicate to their proposal the parties note that their support for the recommendation is expressly conditioned on the "package" aspect of the proposal adding that their support for the whole proposal should not be construed as support for any partial aspect of the proposal and reaffirming the positions stated in their previously-filed briefs if this Commission chooses not to accept their joint proposal as-is.

The central premise of the joint recommendation is that this Commission needs to adopt modifications to the HCF mechanism adopted in D.85-06-115 in order to maintain a fair and equitable local rate structure for the predominately rural ratepayers served by the rural and small metropolitan independent telephone companies of the state.

1. Determination of the HCF Funding Requirement

a. Calculation of Settlement Effects

The parties agree that the first step in determining the HCF funding requirement is to calculate the impact of settlement effects shifts upon the local exchange portion of each ITC's revenue requirement. They point out that there was concensus in the evidentiary record on the methodology for calculation, but disagreement about whether certain items of rate adjustment and offset should be included in the calculation or not. Their compromise recommendation is that we continue the policies adopted in Pacific's last general rate decision, D.84-06-111, the decision after reconsideration in that rate proceeding, D.85-08-091, and the 1985 access decision, D.85-06-115, of flowing-through to affected companies both positive and negative settlement effects adjustments for regulatory changes which impact settlement revenues.

While D.85-06-115 adopted an HCF for which eligibility is based on comparable local rates, and, thus included consideration of the revenue effects of operating costs beyond local loop NTS costs, this proposal goes beyond the effects on rates of the termination of the uniform pooled surcharge on settlements revenues to include the effects on settlements revenue of all of the following:

(1) Termination of the uniform pooled surcharge (which is presently being added to the access services revenue pool to make up for various reductions that were made to access rates in D.85-06-115);

(2) Extended area service (EAS) rate changes;

(3) IntraLATA toll rate revisions or separations revisions adopted in this rate decision;

(4) The net of the combination of the receipt of interstate HCF funds with the effect on intrastate costs resulting from the shift from interstate SPF to the interstate NTS gross allocator; and

(5) Any other aspects of this Pacific rate decision with industry-wide settlement revenue impacts.

The parties to the joint proposal anticipate that based on evidence in this record we will make the necessary calculations and specify the settlement effects impact on each ITC.

b. Basis for New Rate Design and HCF Funding Level

One of the principal modifications to the existing HCF recommended by the joint proposal is a change in the eligibility threshold from 200% of the rates for similar services in comparable neighboring exchanges to 150% of the rates for comparable services in the urban areas of the state. This threshold would be used as a guideline by the Commission in approving rate designs for individual companies. It would not be used to reduce any presently authorized rates which are already above that amount except where the Commission authorizes an exception to the rule.

Thus, after determining the settlements effects the next step proposed is for this Commission to measure the impact of each company's net settlements effects upon its present level of local exchange revenues and then to define the 150% target level for each ITC. Then, each company electing to do so would implement a local exchange rate design by advice letter filing immediately following issuance of this Pacific rate decision which would allow it to attain this 150% target level. These advice letters are to include supporting workpapers calculating the level of additional local exchange revenues generated by the local exchange rate designs incorporating the 150% threshold and calculating the residual revenue requirement to be met by HCF funding.

The parties claim that this change from 200% to 150% is consistent with both evidence in this proceeding and with existing and proposed legislation aimed at promoting the goals of universal telephone service and urban/rural ratepayer equity. The Smaller Independents[9] laud our adoption in D.85-06-115 of the application of a "comparable rates" standard under which we agreed that it is reasonable to make intrastate HCF relief available. However, they opine that application of this equitable principle of comparable rates can be made substantially more fair if the Commission will see fit to adopt a reduced threshold of 150%. They also ask that the prior rate review requirement of that decision be modified. Smaller Independents cite Section 1(d) of Chapter 1047, Statutes of 1986 which is a legislative declaration that this Commission shall ensure that local telephone subscribers are not unduly burdened by reductions in the rates and charges LECs adopt for IEC access. Smaller Independents argue that this statute shows a legislative concern for impact on the great majority of ratepayers served by the largest companies and point out that the impact on these cost shifts upon the customers of Smaller Independents, constituting six-tenths of 1% of telephone ratepayers

9 The term "Smaller Independents" refers to a large group of independent exchange companies which have filed joint pleadings in this matter. They are: Calaveras Telephone Company, Capay Valley Telephone System, Inc., California-Oregon Telephone Co., Citizens Utilities Company of California, Ducor Telephone Company, Evans Telephone Company, Foresthill Telephone Co., Happy Valley Telephone Company, Hornitos Telephone Co., Pinnacles Telephone Company, The Ponderosa Telephone Co., Sierra Telephone Company, Inc., The Siskiyou Telephone Company, and The Volcano Telephone Company.

statewide, is several times greater than it is on the statewide averaged ratepayers of Pacific.

2. The Funding Source

As we pointed out above, prior to filing this joint proposal the ITCs generally supported the basic concept of the LRS plan drawn up by an industry task force and presented by Pacific (Exhibit 386). Like the joint proposal, that plan provides for a fund, not a pool. The LRS plan provides that the funding company may recover net prospective funding requirements by advice letter filing. This provision would presumably permit the funding company to propose a surcharge on its rates, or some segment of its rates to accomplish this recovery. Testimony of various witnesses seems to assume that this recovery would be limited to local exchange rates.

Noting that the ITCs initially supported the LRS plan for funding the HCF while DRA supported and continues to support use of the access charge funding source, the joint brief takes what it describes as a "compromise position" which advocates maintaining the presently-authorized HCF funding source, the CCLC of all local exchange carriers statewide, and determining an annual revenue requirement for the HCF rate element of that CCLC charge. Once the annual HCF revenue requirement is established the amount of the uniform funding increment may be adjusted as often as quarterly to compensate for any under- or overcollection of that current revenue requirement. The joint brief adds that the parties reserve the right to propose modifications in the future, if experience proves it appropriate, which would shift the funding source from the carrier common line element to other aspects of local exchange company rate designs.

3. Other Provisions

The joint brief also includes a proposal for annual adjustments for future net settlements effects; a provision which would allow 100% of HCF funds for 1987, 1988, and 1989 followed by an annual reduction to 80%, then 50% and then 0% for companies which have not initiated a general rate proceeding by year's end for the next consecutive years; and a proposal that a decision in an ITC rate proceeding should have the effect of a fresh start under the HCF plan. Costs to Pacific for administration are to be recovered as additional expenses of access pool administration.

E. Responses to the Joint Brief

1. General

General has only one objection to the joint proposal. General points out that the proposed advice letter filing process for implementing the flow-through of changes resulting from this decision and for implementing the annual flow-through of changes thereafter is made available only to the rural and small metropolitan independent companies and not to General. Although General does not concur in Pacific's access services tariffs as those other independent companies do, it seeks to be included in the joint proposal's provision for an annual flow-through adjustment for net settlements revenue impact brought about by this decision and future regulatory changes of this Commission and the FCC.

General states that it will suffer reduced settlements revenues as a result of the adoption of proposals in this proceeding to reduce intraLATA toll rates because General concurs in some of them and has division of revenue contracts with Pacific for some of them. It states that it will also be affected by adoption of proposals to reduce Pacific's exchange rates because it has EAS contracts with Pacific which make certain revenues dependent on Pacific's rate of return. And, it states that application of the proposed SPF to SLU allocations to intraLATA toll will affect it because of the different relative impacts of the cost allocation change for General as compared to Pacific.

If not included in the flow-through process General is left to deal with such changes in its rate case and attrition filings under the Rate Case Plan. Thus, while acknowledging that it should not be a recipient of HCF funds, General contends that when Pacific receives a decision changing toll and/or other separations revenue, General might have to wait a year or more to adjust its revenue requirements to compensate for these changes--a unique and unfair position relative to all other exchange carriers.

General's opening brief on this issue concludes that if the Commission doesn't allow it to make a showing of its revenue losses or provide the mechanism to automatically offset these losses, there is a taking by the State without any attempt to provide the right of due process of law.

The joint motion indicates that DRA disagrees with General's position, but DRA has not provided us with its argument on this issue, except to the extent that, prior to the introduction of the joint proposal, its witness Marks testified that any pursuit of increased ITC rates to offset the impact of reduced settlements resulting from newly adopted Pacific rate design should not occur without a full showing of the justness and reasonableness of the proposed new rates by the ITC, such as in a general rate application.

2. MCI

MCI regards the joint proposal as an attempt by parties to modify, without notice, a previous California Public Utilities Commission access charge decision, namely D.85-06-115. MCI states that this Commission has always judiciously avoided addressing access charge rate design issues in LEC general charge rate case proceedings and regards this joint proposal as an improperly noticed attempt to change this policy. MCI concludes that the HCF plan adopted in D.85-06-115 must remain in place and such changes in funding levels and revenue recovery as proposed in the joint brief should only be addressed on a company by company basis after a general rate case review.

3. <u>AT&T</u>

AT&T does not express opposition to the recovery sought by the joint proposal, just the source of that recovery. As with the HCF we authorized in D.85-06-115, the joint proposal confines funding for the HCF to a surcharge on the access CCLC. AT&T points out that this means that funding will be derived only from interLATA toll customers, and argues that this is a blatantly discriminatory tax on one class of customer. AT&T asserts that because the joint brief does not propose a limited high cost fund to offset the interLATA access SPF to SLU phase down and the elimination of the pooled billing surcharge--but rather an entirely new high cost fund whose purpose is primarily to offset a host of <u>intraLATA</u> revenue shifts. AT&T prefers the LRS plan with its more broadly based funding. AT&T adds that if this Commission prefers that the HCF be supported by toll customers, it should at least spread that burden over both inter- and intraLATA toll customers.

AT&T maintains that concomitant with the approval of new ITC rate designs this Commission should order the elimination of the bill and keep surcharge on intraLATA services which was authorized as an alternative to participation in the HCF by D.85-06-115 since we have an opportunity to put into place a legitimate comprehensive rate design, avoid possible duplicative collection of revenue requirement, avoid de-averaging of toll rates which would defeat the effects of the SPF to SLU transition, and avoid repression of toll service and loss of associated revenue.

AT&T also contends that we should eliminate any current surcharges on access services or interLATA toll rates, including that portion of the 24% bill and keep surcharge on intrastate toll rates which Citizens Utilities Company of California (Citizens) is presently assessing for interLATA toll, that portion of the 5% surcharge on intrastate toll rates which Sierra Telephone Company is assessing for interLATA toll, and that portion of the "percentage of charges" intrastate toll surcharge being levied by

California-Oregon Telephone Company (Cal-Oregon) on AT&T for interLATA toll. Cal-Oregon itself is also seeking elimination of the latter surcharge.

F. <u>The Ferndale Position</u>

On September 8, 1986 two similar documents were filed with this Commission. One is a motion filed in this rate proceeding by Carlos E. Benemann. The motion explains that Benemann is a customer of Citizens and asks that the portion of hearings in the Pacific rate proceeding set to address the rate design proposals of the ITCs which concur in Pacific's tariffs be held in abeyance pending timely and proper public notice to the customers of the ITCs.

The other document was a complaint docketed as C.86-09-007. The complaint, signed by 26 Citizens customers, including Benemann, was dismissed by this Commission in D.87-07-013 upon a finding that the subject matter of the complaint was the same as that in Benemann's motion and that the issues raised were more appropriately and efficiently addressed by the motion in the existing proceeding.

As did the complaint, the motion claims that Citizens' proposal is tantamount to an application for a rate increase application and that notice must therefore be in compliance with Public Utilities Code (PU) Section 454, the relevant part of which states:

> ". . . Whenever any electrical, gas, heat, telephone, water, or sewer system corporation files an application to increase any rate or charge, other than an increase reflecting and passing through to customers only increased costs to the corporation, for the services or commodities furnished by it, the corporation shall furnish to its customers affected by the proposed increase notice of its application to the commission for approval of the increase. The corporation may include the notice with the regular bill for charges transmitted to the customers within 45 days if the corporation operates on a 30-day billing cycle, or within

> 75 days if the corporation operates on a 60-day billing cycle. The notice shall state the amount of the proposed increase expressed in both dollar and percentage terms, a brief statement of the reasons the increase is required or sought, and the mailing address of the commission to which any customer inquiries relative to the proposed increase, including a request by the customer to receive notice of the date, time and place of any hearing on the application, may be directed."

Although the ITCs had already notified their customers about Pacific's public hearings in this proceeding, on September 15, 1986, at the first day of hearings scheduled to address the settlement effects of Pacific's rate design proposals on the ITCs, the ALJ, without ruling on the merits of the motion, and declining to require the postponement of the settlement effects hearings, ruled that the ITCs which have been joined as parties by the OII issued in this proceeding should provide another notice to their customers, in a form designed in conjunction with the Commission's Public Advisor's office, stating what the effects of the settlement change proposals of Pacific and DRA would be, and informing their customers that there would be a public participation hearing specifically addressing this issue to be held at the Commission's hearing room in San Francisco on December 15, 1986. Later that date was changed to Tuesday, December 16, 1986 and, due to the amount of public interest in Benemann's community, Ferndale, in Humboldt County a second public participation hearing was scheduled there on Wednesday, December 17, 1986.

After the hearings Benemann and David Kilmer, on behalf of themselves and other residents of Ferndale who are customers of Citizens, filed a brief as intervenors on this settlement effects issue. The briefs again contend that our policy of issuing an OII making all ITCs which interconnect with Pacific respondents, and consolidating that OII with Pacific's rate proceeding is a denial of due process because it violates the notice requirements of PU

§ 454. They also claim that this Commission has ordered the ITCs to be party to a rate application case without requiring separate applications - without jurisdiction. They take the position that we may not order any rate increases or redesigns except in a properly noticed rate proceeding for each ITC, that since there has been no showing that the rate changes the ITCs will propose at the conclusion of this proceeding will be minor in nature the GO 96-A advice letter procedure is not available, and that the ITCs' rate proceedings cannot begin until this Commission has issued the present decision so that the settlements effects can be known.

G. Discussion

1. Jurisdiction

Because nearly all of the ITCs, including Citizens, concur in Pacific Bell's access charge rates they are, at present, collecting an 8.57%[10] surcharge on local and intraLATA toll charges. As we explained in detail above, we ordered implementation of this surcharge in D.85-06-115 as an interim measure to alleviate the revenue loss from the access services revenue pool which would have otherwise resulted when we lowered Pacific's access rates. Under the interim scheme this surcharge revenue is pooled with access services revenue and then divided among the pool members by a settlement procedure. It was initially our plan to eliminate the pooled surcharge in this decision by incorporating the 6.76% portion of the ITC's surcharge which is based on test year volumes into rates. The remaining 1.81% which is based on later volumes would have been collected by a bill and keep surcharge.

10 At the time of hearing this figure was 5.11%. It became 6.76% on January 1, 1987 when direct assignment of WATS was implemented, and 8.57% on January 1, 1988 to offset the interLATA SPF to SLU phase down. The corresponding portion of Pacific's surcharge is presently 8.81%.

CORRECTION

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Our decision to postpone spreading all billing surcharges also postpones the date of our elimination of the pooled surcharge. Further, it will allow us to be able to spread the surcharges accrued subsequent to 1986 along with the earlier ones. As for the present, we will authorize the ITCs to make Advice letter filings under the terms of GO 96-A to implement revisions in their pooled billing surcharges consistent with this decision. Further, although we will not eliminate the pooled surcharge now, we still address below the mechanism by which the parties will accomplish that end at a later date.

In D.85-06-115 we ordered that the ITCs could make an advice letter filing under the terms of GO 96-A to implement, following this rate design decision, a revised billing surcharge on a bill and keep basis to replace the pooled billing surcharge. Because Benemann was a party to the proceeding leading to D.85-06-115 and expressed interest in this issue the decision specified that his telephone company, Citizens, would be required to serve him with its compliance and advice filings.

Although there was criticism of the procedure from Benemann, we agree with the ALJ that it was inappropriate to postpone the settlement effects hearings scheduled to begin on September 15, 1986. Customers of the ITCs were adequately informed of these Pacific rate proceedings in 1985. The further notice and public participation hearings that were provided pursuant to the ALJ's ruling which was issued on the first day of those hearings provided these ratepayers with a further opportunity to participate in the settlement effects portion of this proceeding and to apprise this Commission of their concerns regarding the rate implications for ITCs of Pacific's and DRA's rate design proposals in the present proceeding. The ruling, with which the ITCs complied, required the ITCs to send notices which described what the ITC and what DRA contended the effect would be on ITC rates from Pacific's proposed elimination of the 5.11% surcharge then being applied to regular monthly billings for local and intraLATA toll calls placed by customers of Pacific and the ITCs. All the notices announced the public participation hearing in San Francisco. The notices going to Citizens customers in the Ferndale area also announced the Ferndale hearing. Both hearings were in December 1986.

While we understand the concern of Benemann and other ITC customers for the fact that ITCs' rates could be significantly altered as a result of this decision, the ITCs' proposals for changes in their own rates in the settlement effects portion of this proceeding are compliance filings required by both the OII and by D.85-06-115. They are not rate case applications as Benemann asserts. For that reason the notice requirements of PU § 454 do not apply to them.

It has been our long-standing practice to issue an OII in Pacific's general rate case in order to deal with the settlement implications of Pacific's new rate design on the ITCs. The problem, as Benemann has pointed out in his testimony, his pleadings and the briefs he filed with Kilmer in the settlements effects phase, is that no notice provided to ITC customers in this proceeding can give them a very accurate picture of what the effect of Pacific's rate design will be on the ITCs' rates until Pacific's rate design is finally adopted. In the past change has been slight, and there has usually been an advantage to the ITC customers. Therefore, the procedure engendered little interest among ITC ratepayers.

The realities of divestiture have changed the way revisions in Pacific's rates impact the concurring ITCs. Divestiture has not, however, changed the fact that in order to have a complete picture of Pacific's rate design and revenues it is still necessary for this Commission to consider the implications of Pacific's rate revisions on intercompany settlements and revenues as related to intrastate toll and private line rates concurred in by these ITCs. Furthermore, it is both appropriate and necessary to address that portion of the ITCs' rates which are funded for the most part by contributions from Pacific, in the context of a Pacific proceeding.

For these reasons we will deny Benemann's motion that we find notice to the ITCs inadequate for failure to comply with the requirements of PU section 454. That section is not relevant to the ITC filings discussed above. We agree with DRA, however, that once a final rate decision is issued in this matter directing these ITCs to make advice letter filings requesting new rates consistent with this decision that §454 does require that the ITCs provide notice to their customers of the new rates prior to implementation. We believe a minimum of 30 days' notice prior to implementation is adequate.

2. The Present HCF and the Proposed Differences

We have consistently expressed our belief that there is a fundamental public interest in maintaining stable and reasonable basic exchange rates. That is why we authorized the HCF in D.85-06-115 which permits the continuation of a policy of statewide uniform toll rates while protecting ITC customers from the effects of shifting a greater burden for NTS and other costs onto their local rates through the application of the principle of rate comparability to rates that would otherwise be increased due to the annual intrastate interLATA SPF to SLU transition to the extent that change is not offset by interstate HCF revenue.

The joint proposal broadens the scope of HCF recovery by applying the principle of rate comparability not only to the rate changes enumerated in D.85-06-115, but also to any other rate change in this rate decision which will affect ITC settlements revenues, and any PUC or FCC-ordered changes occurring during the year which have an industry-wide effect, either positive or negative, on settlement revenues or cost assignment including shifts in interstate NTS and the loss or gain in revenue occasioned by the interstate SPF to SLU shift offset by interstate HCF revenue, the loss or gain of revenue due to changes in Pacific's non-access rates with which the ITCs concur, and losses or gains resulting from any other aspects of this Pacific rate decision or other Commission or FCC actions which have settlement revenue impact on the ITCs.

As we pointed out in D.85-06-115, since the HCF we adopted was based on rates rather than costs, it allows recovery from the HCF fund not only for the reduction in access services revenues occasioned by the intrastate interLATA SPF to SLU transition and other adjustments to access services revenue objectives, but also, because the basic exchange rates are set residually, it allows for the recovery of high operating costs in general. Some of these recoverable operating costs are clearly intraLATA costs, which under this HCF plan are recoverable from the interLATA CCLC. That being the case, the joint proposal's expansion of the rate comparability principle to certain intraLATA rate changes is not such a drastic departure. Nonetheless, AT&T finds it to be objectionable.

a. The Funding Source and Scope of Revenue Protection

It is our fundamental concern that a source of supplemental revenue be maintained for the ITCs in order to protect the availability of universal service for all California's citizens once we have eliminated the pooled surcharge these ITCs presently depend on. We meant to achieve that end by adopting the presently authorized HCF plan to fill the gap between a reasonable revenue requirement and "existing sources of revenue including interstate HCF assistance and basic exchange rates set at the highest level consistent with a 'comparable rates' standard." (D.85-06-115, mimeo. p. 205.)

Although the scope of rate protection is extended under the joint proposal, the proposed additions address the same fundamental issue, toll- and access-related changes and their effect on the ITCs' settlements revenue, and hence their continued viability. Thus, we cannot agree with AT&T that adjustments for the effects of intraLATA rate changes such as EAS rates and intraLATA toll rates are necessarily unfair and inappropriate. In fact, the presently authorized HCF already permits CCLC adjustments to recover some intraLATA costs, namely high intraLATA operating costs. Furthermore, the impact of these adjustments can be minimized by our permitting regulated IECs to flow through the effects of such changes on the CCLC access charge.

The wide support for the joint proposal persuades us that it is reasonable to permit the proposed extensions to the list of recoverable revenue changes. We are also persuaded to authorize the use of CCLCs as the HCF funding source, at least until there is some data indicating that a different distribution of the burden is warranted. Until such information is available to us, we are reluctant to add further to the burden on local rates. We fail to see any legal or equitable impediment to the adoption of this aspect of the joint proposal as AT&T suggests. We would point out that, contrary to AT&T's apparent understanding, our purpose in establishing the SPF to SLU transition in D.85-06-115 was not to decrease a specific rate. Rather, it was our purpose to decrease the assignment of NTS to interLATA access.

For these reasons we will adopt the proposed expansion of recoverable revenue changes and the use of the CCLC as a funding source for the HCF.

b. Revenue Requirement Review

The joint proposal would also have us deviate from our present policy that HCF relief should be awarded only in the rate design phase of a particular ITC's rate case. We are concerned that the ITCs not be in a position to collect HCF revenue for an unreasonably high revenue requirement. On the other hand, we are sympathetic to the fact that this Commission could not process the rate filings of all the ITCs at once, and that the ratepayers of some ITCs would likely experience dramatic local service rate increases if the ITCs simply implemented a bill and keep surcharge while awaiting our action on their rate cases. Therefore, we conclude that it is reasonable to adopt the proposal allowing the ITCs up to three years to make rate filings before their HCF funding is affected. It appears that this leeway along with the annual reductions in available funding levels will permit an orderly progression of rate case processing while adequately protecting against rate shock in the short run.

AT&T is also concerned that the joint proposal invites abuse of the HCF since the funders are not the companies administering the fund. We believe these same funding level safeguards will adequately prevent such abuse by encouraging filing for timely rate review by each ITC. If our assessment of this situation proves to be inaccurate or appears to be causing some inequity we will reassess our position.

c. The 150% Eligibility Threshold

There is very little information in this record about the propriety of moving from a 200% eligibility threshold to a 150% threshold. During the hearings the various witnesses for the Smaller Independents supported either a dollar cap or a lower percentage threshold, never more than 150%. The joint brief states that the parties to the proposal who had not previously supported the 150% concept (i.e., Pacific and DRA) now support it in conjunction with their support of the whole of this comprehensive proposal. This is explained with the statement that the whole proposal contains appropriate mechanisms for review of high-cost funding levels and associated annual changes.

Many of the witnesses who testified in opposition to the 200% level noted that each time Pacific's local rates increase, the dollar amount to which the percentage is to be applied increases. They argued that while the dollar differentials may be affordable when Pacific's local rates are relatively low, the 200% threshold will become more and more unfair as Pacific's rates rise. They also argue that the 150% level would be fairer and more in keeping with the legislature's intent. Those parties who oppose the joint proposal do not base specific objections on what the funding level should be.

As we have said we are sympathetic to the plight of the ratepayers of these small, primarily rural ITCs who may be exposed to very large rate shifts due to the impact of the reallocation of costs that we will be engaged in for the next few years. The mandate of Public Utilities Code §728 that in setting rates we consider, among other things, the rates for comparable service of adjacent local exchange carriers, directs us to assure that the exchange rates of the ITCs are reasonable when compared to those of the dominant local exchange carriers, most often Pacific. Further, we continue to believe that this end can be accomplished for now with respect to those ITCs which concur in Pacific's access rates by keeping the ITC's local rates within a reasonable percentage of rates for comparable urban service (usually Pacific's) and then recovering any still unmet costs from the intrastate HCF.

As we stated above, we have some reservations about the possibility of short-run overstatements of revenue requirement by the ITCs with these changes in eligibility criteria. However, we are impressed with the diligence with which these parties have worked on a resolution to this intricate problem. Keeping in mind the dearth of data to support either the presently effective 200% threshold, or the proposed one of 150% and the strong support evidenced by this joint proposal, we conclude that it is reasonable to adopt this aspect of the recommendation.

d. **Retention of Bill and Keep Surcharges**

At present Pacific's annual interLATA SPF to SLU phase-down of access charges is accounted for by a decrease in access rates and a corresponding surcharge to intraLATA service billings. Pacific and the ITCs pool and share these surcharges in the access service pool. In this decision, however, we have accounted for the intraLATA SPF to SLU phase-downs by reducing Pacific's intraLATA toll rates and correspondingly increasing non-toll, non-access rates, including basic local rates. Thus, although the intraLATA pool and the access services pool still exist, they have shrunk. Because we agree with DRA's Shantz that it is inequitable for the ITCs to increase basic rates by more than 100%, this pool shrinkage could result in a settlements revenue shortfall for some ITCs. It is not our intent to decrease the settlement recovery for any ITC, including General, as a result of this decrease in pooled revenue. Therefore, keeping in mind our concern about increases in basic rates, we will authorize the ITCs to recover any such revenue shortfall by a uniform increase in basic exchange access line service rates, not to exceed 100% of present rates, followed by a bill and keep surcharge on intraLATA services where necessary. We agree with AT&T, however, that the bill and keep surcharge should not be retained as an alternative to the intrastate HCF for these ITCs. Since General is not eligible for the intrastate HCF, however, we will authorize it to recover any shortfall by a bill and keep billing surcharge on intraLATA services.

AT&T also argues for the removal of the previously authorized Citizens 24% bill and keep surcharge on intrastate toll rates and the smaller surcharge on intrastate toll rates previously authorized for Sierra Telephone Company (Sierra). AT&T adds that Cal-Oregon, itself, seeks to eliminate its annual $35,000 intrastate toll surcharge in the context of the revisions it proposes to its rate design in this proceeding.

The surcharges that AT&T is concerned about are surcharges on intrastate toll service which we authorized prior to divestiture. Specifically AT&T is concerned with the portion of those surcharges which is levied on interLATA toll service. That issue is the subject of a pending complaint proceeding, C.85-07-062, initiated by AT&T, which is addressing the question of whether these surcharges should be eliminated. Therefore, we will leave the authorized toll surcharges as they are until we have determined the merits of AT&T's complaint.

AT&T is asking us to address the details of ITC rate design. Although the ITCs which interconnect with Pacific are parties to this proceeding this is not a rate proceeding for each of those ITCs. Therefore, it is inappropriate to adopt a new rate design for those companies in this proceeding. Nonetheless, we have determined that once the pooled surcharge is eliminated these ITCs should continue to recover the revenue which that surcharge now provides, and should remain whole despite the settlement effects of Pacific's rate decision. We believe that a rate design modeled after that proposed by DRA's Shantz accomplishes that end well while avoiding a further surcharge by spreading revenue changes as a capped uniform percentage increase across an ITC's existing rate design with the residual recoverable from the intrastate HCF. Therefore, we will authorize adoption of that model, revised to take account of the elements of the joint proposal--principally the 150% eligibility threshold, based on Pacific's rates in effect at the time this proposal is implemented. However, we will not adopt Shantz' proposal to increase ITC service connection charges up to 100% of Pacific's rates for comparable service before applying the flat percentage rate. This provision is less fair to ratepayers than permitting the entire surcharge to be spread over a much broader base, and also constitutes the type of substantive rate design change described below which must be avoided in this proceeding.

The equitable spreading of surcharges and their incorporation into the existing rate design framework is qualitatively different from the substantive rate design changes proposed by some of the ITCs, namely that Happy Valley Telephone Company, Cal-Oregon, and Hornitos Telephone Company be permitted to remove their mileage charges, that Kerman Telephone Company be permitted to raise its coin rates from $.10 to $.20, that Cal-Oregon be permitted to place all four of its exchanges on the same rate schedule, and that Siskiyou be authorized to change or eliminate various rates. Such structural changes should only occur in the context of a properly noticed rate filing. The only surcharge that is affected by adoption of the proposed HCF plan is the pooled access services surcharge which we will eliminate in the decision we will issue following supplementary rate design hearings after our Phase I rate flexibility hearings in I.87-11-033. Other ITC surcharges will stay in place until they are specifically addressed in a rate review or some other proceeding.

e. **Time Frame for the 100% Funding Level**

The joint proposal allows HCF recipients to receive funding at 100% of their determined funding requirement for the years 1987 through 1989. Since 1987 has already passed, and in order to avoid a glut of rate case filings, we find it appropriate to modify the proposal to allow the 100% funding for 1988 through 1990.

3. **Notice of Broadened HCF**

Contrary to MCI's contention, all the parties to this proceeding did receive "notice" of the attempt to move from a narrow to a broader HCF, since the LRS plan presented by Pacific's witness, Ondeck, at the hearing also went beyond offsetting the intrastate interLATA access SPF to SLU phase down and the elimination of the pooled billing surcharge. We do not view such a proposal as inappropriate to this proceeding.

4. **Participation of General in the HCF Plan**

We turn now to the concern of General that it be permitted an annual adjustment, outside a rate case or attrition filing, to flow through to its rates the effects of Commission and FCC actions in the same manner permitted to the ITCs under the joint proposal.

The primary purpose of the joint proposal is to deal with the settlement effects of changes in access rates in Pacific's rate decision on the smaller ITCs. Our endorsement of a plan which recognizes the settlement effects of certain other actions of this Commission and the FCC is an extraordinary one which is based on what appears to be extreme and temporary rate pressure being placed upon these small ITCs during this transitional period of SPF to SLU phase-down and the phased implementation of the interstate HCF. Our primary concern in granting this proposal is to preserve the public interest in maintaining stable and reasonable basic exchange rates.

General's request to be included in the flow-through provisions of the proposed HCF plan, while at the same time acknowledging that it should not be a recipient of high cost funds, misconstrues the plan. This flow-through provision is only an element of the calculation which is made to determine whether an ITC is eligible to receive HCF funding. The reasonableness of this particular provision does not arise from the notion that these ITCs deserve guaranteed rates, but rather from our policy to protect universal service in situations where we have already found that the rate impacts on the smaller ITCs are likely to be so disproportionately large that basic service rates would become inequitably high. The proposal does not single out General for different treatment. It simply makes eligibility for the flow-through provision ultimately contingent on eligibility to receive HCF funds. If an ITC is not eligible to receive HCF funds after making this flow-through calculation it is assumed that the ITC's rates do not warrant the extraordinary protection of the provisions of the joint proposal. Therefore, we will deny General's request.

5. Procedural Request of the ITCs

In response to a March 11, 1988 petition for modification of Ordering Paragraph 15a of D.87-12-067, filed by the smaller ITCs we issued D.88-03-064. In that decision we determined that it was preferable to postpone addressing one of the issues raised by the petition until we addressed rate design. The Petition, at page 5, requests that we adopt the following language:

> "Further, those rural and small metro local exchange companies electing to do so may combine the net settlement effect of future annual intraLATA separations changes by combining them in a single advice letter filing with other Commission-ordered settlement and separations changes under existing advice letter procedures, as the same may be modified in the rate design decision to be issued in this Pacific Bell rate case."

The ITCs' request to combine various Commission ordered separations and settlements changes in one annual advice letter filing is unopposed and appears to be advantageous to both the ITCs and their customers since it would alleviate the possibility of a number of separate rate changes in a year and reduce implementation costs for the ITCs. Therefore we will authorize the ITCs to follow such a procedure if they choose to do so.

6. Relationship Between Settlements and the High Cost Fund for ITCs

At the time the parties presented the HCF proposal it was assumed that all surcharges would be spread over rates in this proceeding. In fact, D.88-03-064 was a direct result of the concern that the large surcredits for local exchange services, which some ITCs would be required to implement as a result of our Phase II revenue requirement decision's (D.87-12-067 as modified) treatment of the intraLATA SPF to SLU transition at Ordering Paragraph 15A, would be largely offset by the revenue shifts from reductions to intraLATA toll rates expected to be adopted in the present decision. Because we shared that concern D.88-03-064 gave the ITCs the choice of either implementing a new bill and keep surcharge (or surcredit) on intraLATA services excluding intraLATA toll, or simply accruing the net settlements impacts of the SPF to SLU phase-down from January 1, 1988 in an interest bearing memorandum account, the balance of which could then be combined with the settlement impacts of this decision so as to alleviate great rate fluctuations. Sixteen ITCs chose to establish memorandum accounts. Appendix C of this decision shows the net settlements effects resulting from the rate design authorized herein and the intraLATA SPF to SLU phase down authorized by Ordering Paragraph 15A of D.87-12-067 as amended, for the ITCs which chose to implement memorandum accounts.

Since we have not eliminated the surcharges which would have been a primary cause of the large rate changes these parties were planning for, the effects on the ITCs will not be so great as anticipated. Therefore, it is not necessary or reasonable, with one exception, Hornitos Telephone Company, to continue the memorandum accounts pending our supplementary rate design consideration in a further phase of this proceeding.

In the meantime, for those ITCs whose net settlements effect is a revenue shortfall, (shown on Appendix C as an amount in parentheses), we will authorize a uniform percentage increase in basic exchange service rates in the manner described in our HCF eligibility discussion. With the exception of Hornitos, we will direct ITCs whose net settlements effect is a positive amount, to refund that amount by a bill and keep billing surcredit on the intraLATA billing base.

Among the ITC's for which a reduction in basic exchange rates is indicated, Hornitos Telephone presents the greatest problem. Due to its small billing base, the flow through of reductions may cause cash flow problems for the company. Rather than imposing such a reduction on the company, when the impact of it will probably be alleviated once we have adopted a supplementary rate design in the next rate design phase of this proceeding, we will authorize Hornitos to accrue the net settlement effect in an interest bearing memorandum account.

Further, in order to avoid accruing exorbitant amounts or unnecessary interest, those ITCs, except Hornitos, which now have memorandum accounts should eliminate the funds in those accounts by incorporating the amount into a bill and keep surcharge or surcredit spread over a one year period. We realize that at some point it will likely be necessary for Hornitos to refund the amounts it is now accruing and will continue to accrue too. Therefore, we invite Hornitos and any other party interested in doing so to propose, in the supplementary rate design proceeding, a solution for dealing with this problem.

Although this unanticipated situation will be alleviated somewhat with the spreading of surcharge revenue into rates, it appears that our adoption of the SPF to SLU mechanism for intraLATA toll revenues (identified in column (g) of Appendix C) will, for some ITCs, continue in the future to result in an increase of revenues from intraLATA toll which is so substantial that it will more than offset the decrease in revenues expected to result from the shifting of NTS costs out of intraLATA MTS rates.

The presumed decrease in toll revenues resulting from the intraLATA SPF to SLU transition was to be made up by a change in basic exchange rates. In certain cases, however, the revenues received by some ITCs from the settlements pool are to be offset by a reduction to their basic exchange rates. This result is the opposite of what the Commission expected to occur. The Commission anticipated that the SPF to SLU transition would require an increase in basic exchange rates, and that this increase would be tempered by revenues from the HCF. Unfortunately, since revenues from the settlements pool are pre-determined, to avoid overcollecting their revenue requirement, certain ITCs would have to reduce their basic exchange rates to such a level that they would bear little relation to the rates for comparable service charged by telephone corporations in adjacent territory. (Pub. Util. Code Section 728).

The problem appears to lie in the fact that the settlements process does not impute any contribution to the companies' revenues from basic rates. This results from our historic practice of setting basic rates residually. Thus, the ITCs' eligibility for settlements revenues is not based on their total costs of service, but only on their proportional amount of statewide plant used to provide intraLATA service.

The settlements process should be revisited at the earliest time practical to ensure that contributors to the settlements pool are not forced to subsidize some participants without regard to their total revenue requirement and reasonable contributions from basic exchange service. We will invite the parties to present recommendations in the supplemental rate design proceeding or a later phase of I.87-11-033 for ensuring that these pooling mechanisms operate equitably for both contributors and recipients. A specific request for testimony will be made by ALJ or assigned Commissioner ruling.

IX. Issues Related to Rate Design and/or Revenue Requirement

A. Shift of $11 Million from Special Access Rates to Non-Access Rates Per D.87-08-048

Our decision in Phase III of Pacific's access proceeding concluded that the revenue requirement for Pacific's special access services should be reduced by $11 million and that this reduction should be offset by an increase in Pacific's nonaccess services. We determined that it would be best to implement this rate design change concurrently with the effective date of the present rate design decision, since there would only be a few months difference in effective dates and doing so would avoid the adverse effects on ratepayers of short-term billing changes. Therefore, in this decision we are ordering Pacific to decrease its special access rates by $11 million.

This rate shift will have the added effect of lowering expenses for AT&T. In D.85-06-113, we modified D.85-03-056, to require that within 14 days of local exchange utilities making their advice letter filings to reduce local access charges AT&T pass on to its customers through a corresponding incremental reduction in the billing surcharge any reduction in its expense stemming from reductions in local exchange utilities' access charges. However, in D.87-12-067 as amended by D.88-02-046 we took note of AT&T's recently filed application for rate flexibility and several other pending rate matters which would affect AT&T's access charge expenses. We therefore determined that for the present AT&T should accumulate the revenue reduction we were ordering in a memorandum account, with interest, commencing on the effective date of the tariff revision. Since that time we have issued D.88-06-036 in which we ordered AT&T to shift the accrual in its memorandum account into its surcharge commencing in July, 1988. We wish AT&T to avoid future large accumulations in a memorandum account, but we realize that another rate change soon after the July change may be disruptive and confusing to customers and costly to the company. Therefore, we will direct AT&T to accumulate this latest revenue reduction in a memorandum account until January, 1989 when it is mandated by previous order of this Commission to adjust its surcharge to account for the effect on access rates of Pacific's annual SPF to SLU phase down.

Ordering Paragraph 38 of our Phase III access decision, D.87-08-048, invited interested parties to propose a rate design or otherwise comment on the disposition of the $11 million in revenue requirement which has been transferred from access services to nonaccess services. That decision was served on all the parties to the proceeding.

DRA responded by recommending that the increase in revenue requirement for nonaccess services be recovered through an adjustment in the billing surcharge mechanism set forth in schedule Cal. P.U.C. No. A2 Rule No. 33 of Pacific's nonaccess tariffs. DRA calculates that based on Pacific's retaining 96.5% of the billings from access services, Pacific's share of this rate reduction is $10.615 million and that recovering this from nonaccess rates will require an incremental increase in the customer billing surcharge applicable to nonaccess services of .219%, thus raising Pacific's present surcharge from 1.288% to 1.507%. DRA adds that each of the ITCs which concur in Pacific's access services tariff should also be permitted to increase their respective customer billing surcharges by the same .219% increment. It does not indicate what the dollar effect of this increment would be on each concurring ITC.

Despite our finding in D.87-08-048 that the proposed market pricing for Digital Data Services (DDS) and High Capacity Services (HiCap) is reasonable, DRA's response goes on to suggest that we order Pacific to reflect this $11 million decrease in access services revenue requirement in the rates associated with these two services. It is unclear whether DRA is recommending that this decrease be accomplished solely from these two special access rates or simply that the decreased revenue requirement be spread over all special access services, including these two.

Both Pacific and AT&T responded to DRA's recommendations. AT&T does not address the rate spreading issue, but Pacific contends that this treatment should be an interim measure pending this final rate design decision which should eliminate billing surcharges by spreading the associated revenue requirement to appropriate service rates, specifically suggesting that the rates for business services currently priced below cost and not targeted by the Commission for subsidization should be increased.

AT&T objects to DRA's suggestion about reflecting the $11 million decrease in revenue requirement for access services in rates associated with DDS and HiCap. AT&T claims that DRA's proposal would result in non-cost based rates for special access services other than DDS and HiCap contrary to the intent of D.87-08-048. Pacific asks us to reject DRA's recommendation for the reasons set forth in the Proposed Rate Design of Pacific Bell for Special Access Service, filed by Pacific on September 15, 1987 and to adopt that proposed rate design. So far as we can observe that document offers no reasons. It simply submits a new rate design for special access services which seeks to establish structural parity with the analogous FCC tariff and purports to reduce revenue by $11 million by reducing certain proposed special access rates, including DDS and HiCap.

We agree with AT&T that DRA's recommendation should be rejected. D.87-08-048 specifically found that the market based rates proposed by Pacific for DDS and HiCap were reasonable. Therefore, it is inappropriate to now require, based on no new evidence, a revenue requirement spread which would ignore that finding. Furthermore, adoption of DRA's proposal would require that rates for the other special access services might result in a contribution beyond what we determined to be reasonable in that decision. Therefore, we will order that the $11 million reduction be spread across all access services rates, except DDS and HiCap, on a uniform percentage basis.

As for the disposition of the revenue requirement to be transferred to nonaccess service rates, we will increase Pacific's annual nonaccess revenue requirement by $10.615 million, which represents Pacific's settled share of the total rate reduction for access services.

Since D.85-06-115 authorized concurring ITCs to adopt the same percentage surcharge as Pacific in order to adjust nonaccess rates to make up for the reduction in revenue objective for access charges, it is also appropriate here to authorize an increase in nonaccess revenue requirement to offset the settlements effects for each ITC which will reflect this $11 million shift. The settlements effects for each ITC are set forth in Table 2, below.

TABLE 2

Revenue Requirement Increase Attributable to
$11 Million Shift from Special Access Charges

ITC	Amount
Calaveras Telephone Company	$ 5,400
Capay Valley Telephone System, Inc.	1,180
California-Oregon Telephone Co.	8,338
Citizens Utilities Company of Calif.	162,786
Continental Telephone Company of Cal.	336,350
C. P. National	21,372
Ducor Telephone Company	2,530
Evans Telephone Company	11,866
Foresthill Telephone Co.	2,269
Happy Valley Telephone Company	10,607
Hornitos Telephone Company	2,836
Kerman Telephone Co.	5,196
Pinnacles Telephone Company	397
The Ponderosa Telephone Co.	19,330
Roseville Telephone Company	60,225
Sierra Telephone Company, Inc.	27,430
The Siskiyou Telephone Company	10,970
Tuolumne Telephone Company	20,068
The Volcano Telephone Company	19,773

B. Quality of Service to Private Line Alarm Customers

1. Standards

The Commission's General Order (GO) 152 establishes standards for the installation, maintenance and operation of private line alarm service provided by telephone utilities to their customers. It sets two service criteria for each of five areas of service measurement. The first criterion is called the standard service level, which is considered adequate performance. The second is called the reporting service level, which is significantly below the standard service level and is considered inadequate service. Performance at or below this level is to be addressed in quarterly reports from the utility to the Commission. In between these levels is a category called service below standard. Performance in this range is only considered inadequate if it is frequent and substantially below the standard range.

The five service measurements to which these criteria are applied are (1) installation alarm held orders; (2) installation commitments; (3) installation trouble reports; (4) non-installation service trouble reports; and (5) non-installation repair response. One of the issues addressed in this proceeding was whether Pacific is meeting the standard service level criteria for each of these areas.

Pacific presented testimony of R.N. Dills who is its Division Staff Manager responsible for the guidelines for the provisioning and maintenance of the bulk of the services offered by Pacific Bell. At the time of the hearing he was also the chairman of the GO 152 committee, a group comprised of representatives from the Commission staff, the telephone utilities, and the alarm industry which meets to consider whether revisions in the scope of GO 152 are needed. Dills testified that Pacific has generally exceeded the minimum requirements for the standard service level for each of the five service measurements. He documented this claim with exhibit 83 which was received in June, 1985, and with exhibit 235 which was received in the later hearing on November 4, 1985.

The exhibits, as required by GO 152 list nine, rather than five service measurements. This is because alarm held orders are divided into three categories to show orders held from 31 to 60 days, from 61 to 90 days, and over 90 days; and because repair response times are also divided into three categories. The first is designed to show the average duration for responding to private alarm service measured by Pacific's SSTAR measurement system; the second shows that measured by its TREAT measurement system; and the third lists the total trouble reports which took over 48 hours to clear.

Each of these nine service measurements is shown on a monthly basis from January 1983 through June 1985 for each of Pacific's reporting units. Pacific has five such reporting units, the San Francisco Bay region, the Los Angeles region, the San Diego region, the remainder of northern California, and the remainder of southern California. The exhibits show a steadily improving record of meeting the measurement standards over that time period, with only one service measurement during one month at one reporting unit in 1985 being at or below the reporting service level.

2. <u>Opposition Witnesses</u>

The Western Burglar and Fire Alarm Association (WBFAA), an industry organization, offered three witnesses for the proposition that the quality of Pacific's private line alarm service is inadequate. They were Jerry O'Brien, the Director of Telecommunications for API Alarm Systems which does business primarily in southern California; Roger L. Westphal, the President of Bay Alarm Company, Inc., which does business in the San Francisco Bay area; and Warren V. Glass, III, the President and founder of Warren Security Systems, Inc., which does business in the northern San Francisco Bay area.

a. O'Brien

O'Brien expressed concern about Pacific's repair response time. He testified that as a result of significant differences between the repair response times recorded by API on its computerized system and those reported by Pacific that the two entities conducted a special supervised testing comparison which was completed in October, 1985, which he claimed revealed 134 discrepancies. However, as of the November 4, 1985 hearing date, API and Pacific had not reviewed those discrepancies because Pacific cancelled a scheduled meeting.

Schedule B to O'Brien's testimony, Exhibit 236, shows that API recorded more outages for 3002-type circuit service than Pacific did, and that the average duration time for repair to these lines was recorded by API as being nearly an hour longer than what Pacific recorded. Likewise, for 1009-type metallic circuits, API recorded more outages than Pacific, with API recording 14 and Pacific recording 7. API found the average duration for completion of service in this case to be quite a bit shorter than Pacific recorded.

O'Brien gave several examples of discrepancies. One demonstrated Pacific not including certain waiting time in its duration time which API did include. Another was a disagreement about whose problem the outage was. Two of the examples were of situations where there were acknowledged Pacific faults, but the problems came clear while testing, and were therefore reported by Pacific as no trouble found. O'Brien contends that Pacific did not record these as trouble reports although there is no basis in GO 152 for not doing so. He stated that this is the primary reason that Pacific's number of reported outages is lower than API's. Another example was one where Pacific claimed the problem was API's because Pacific's records showed locations which Pacific claimed were under API's control, while API contends that API had previously cancelled them. O'Brien also testified that a common trouble with a 3002 circuit is described as no answer back, and that on several occasions API placed trouble reports with Pacific for this reason only to get a report back from Pacific that the problem was no answer back.

O'Brien states that these examples illustrate the need for better training of Pacific's service and test-board personnel. He claims that if they were reporting properly Pacific's performance for 3002 circuits used by API would be below the mandated reporting levels as is Pacific's performance for the 1009 circuits used by API as measured by Pacific's TREAT system.

During cross-examination by Pacific's counsel O'Brien acknowledged that: "[O]ne of the problems that we had in comparing information from your company to our company is your information is presented by area code 213, 818 in GO 152 and our information is presented by our central station that--our circuits may cross a number of area codes."

In addition to more training O'Brien recommends that we consider adopting a modification to GO 152 which might continue to permit the present duration times to clear for individual loops but sets shorter duration times for the mid-links or back-bones of the circuit because when they go out every customer is affected and the present durations times for these outages is too long.

b. Westphal

Westphal also testified about Pacific's repair response time, stating that it has improved but not as much as reflected in Dills' testimony. Westphal noted that his company, Bay Alarm, is one of the largest alarm company users of private lines in area code (415). He explained that Bay Alarm and Pacific conducted a controlled joint comparison of trouble report records in January, 1985 because Pacific was consistently reporting lower repair response times for the San Francisco Bay area than Bay Alarm was experiencing. Based on that comparison Westphal concluded that Pacific was closing out its trouble tickets before a circuit was ultimately repaired or clearing the ticket for a single trouble on a circuit and then opening a new trouble ticket for another trouble on that same circuit, resulting in more tickets, but shorter average times. This conclusion led Westphal to recommend that this Commission continue to actively participate in the quarterly GO 152 meetings and continue to monitor the accuracy of Pacific's reporting, and its compliance with the GO 152 standards.

c. Glass

Glass' concern was with another aspect of the GO 152 requirements, the provision of new service. He testified that his company, Warren Security Systems, Inc., which has about 1000 accounts that use private line services in the northern Bay area, has experienced significant difficulties in the provisioning of new services, particularly on Morse Multiplex Polling circuits (type 3002 circuits). He testified that almost every time a new loop is added to an existing circuit, the new loop fails to work, and may impact the whole circuit. He went on to state that these loops often fluctuate between normal status and outage status, taking as much as three to six months to finally work consistently. He also stated that the addition of new legs to existing loops also often causes trouble on one or more of the existing loops. He also testified that these troublesome type 3002 loops are being used because Pacific asked the industry to use this more modern technology rather than the 1009 signal grade metallic circuits because, among other things, Pacific's employees were more familiar with 3002 circuits and were better equipped to install and maintain them, resulting in less installation troubles.

In addressing why Pacific reports virtually no installation troubles, Glass explained that GO 152 requires that along with making a trouble report for Pacific's reporting system by dialing 611, installation troubles must also be reported to a special telephone number within seven days of installation. He expressed his belief that this additional reporting was not being done in compliance with these requirements despite attempts by WBFAA and other associations to educate their members to do so. He further testified that there is a second reason for this discrepancy, which is that his company often does not arrive at a location to make a final hook-up of the alarm system within seven days from Pacific installing the circuit. In each of these cases the trouble would show on Pacific's records as a service trouble report, not as an installation trouble report.

Glass made two recommendations based on these problems. First, he recommended that Pacific, the Commission and the alarm industry should conduct further meetings to attempt to improve this reporting methodology; and second, he recommended that Pacific emphasize its training of its installation personnel for the installation of these special 3002 circuits.

3. Pacific's Rebuttal

In response to Glass' examples, Pacific's Dills testified that when Pacific receives a trouble report, conducts a test and concludes that the trouble is not with Pacific equipment, a Pacific employee will call the alarm company and tell that to the alarm company technician or tester. If the alarm company's technician so requests, Pacific will keep its ticket open on the report for up to four hours to give the alarm company a chance to discern whether the problem is in its equipment. He stated that if Pacific does not hear back from the alarm company within four hours it closes the ticket. Otherwise, the policy is to come to agreement as to the disposition. Therefore, he concluded that the example of multiple tickets for problems proximate in time on one circuit were the result of separate problems on separate segments of a circuit. He stated that after Pacific conducted a test for the first problem and determined it had been resolved, the alarm company agreed and both Pacific and the alarm company closed their tickets on the matter. Then the company filed a separate trouble report shortly thereafter on the second problem. He added that Pacific would not have closed its ticket if the company's technician had stated that he still showed the circuit being down.

Turning to the other problems with installation that Glass testified about, O'Brien noted that once the issue was brought to Pacific's attention, it was remedied, so that as shown by the table attached to Glass' testimony, all the problems save one were repaired in August and September of 1985. He added that it has become apparent from Glass' input at GO 152 meetings that when Pacific adds a segment onto an existing circuit it is necessary for Pacific to test the circuit overall or at least test the circuit from the bridge to which that segment is being added. He stated that Pacific was now doing such testing with all installations for Warren Security. Further, O'Brien testified that Pacific's records showed that some of the dates Warren Security listed as dates when the circuit was finally okay were incorrect and that the dates were actually earlier.

Dills also testified that he believed the differences between the response times reported by Pacific and those reported by API and Bay Alarm resulted from the fact that the companies' studies represented one part, not the total, of a Pacific reporting region, and from the fact that API's data for type 1009 circuits was very sparse and, therefore, unrepresentative as was Bay Alarm's data for type 3002 circuits. Dills did not press his original claim (Exhibit 234, p. 9) that any differences between repair response times tracked and reported by Pacific and by alarm companies have been generally due to differences in tracking methodologies, and, in fact, he disagreed with claims of O'Brien that problems that cleared while testing were not being counted by Pacific as trouble reports though they were counted by API.

He further testified that Pacific had just completed a review of the 134 discrepancies between its report and API's and he concluded that the largest number of them, were cases where Pacific had determined that API's equipment was the cause of the problem, while API determined that Pacific was responsible. He claimed that the number of these differences was large enough, and the response times were generally so short, that adding them to Pacific's figures would lower its overall average repair response time. He testified that adding the "test okay" and "cleared while testing" which O'Brien had apparently omitted, would have the same effect. Dills added that the employees in Pacific's Alhambra Special Service Center whom API deals with have all worked there at least two years and have had 13 weeks of classroom training on testing of these types of specialized services followed by supervised on-the-job training, and that Pacific is also giving these employees two days of training on the technology of the bridges that Pacific gets from Tel Labs Corporation, and which API happens to use a lot.

In explaining his understanding of the discrepancies between the reports of Pacific and Bay Alarm, Dills admitted that Pacific's data base is sometimes incomplete or inaccurate so that when Pacific receives a trouble report it sometimes happens that the report refers to circuit nomenclature or a segment number which is not in Pacific's data base. He stated that it is Pacific's policy to accept the trouble report and then fix its data base afterwards. He testified that he thought Pacific's data base was much more accurate than Bay Alarm's list of 17 unmatched problems indicated, but he had no explanation for it.

4. <u>Discussion</u>

Pacific briefly addressed this GO 152 service quality issue in its concurrently filed opening brief on rate design and settlement effects. WBFAA did not. Nor did any other party. Both Pacific and WBFAA addressed the issue in their reply briefs. On March 3, 1987 WBFAA filed a motion to strike the portion of Pacific's reply brief addressing the issue on the ground that it was not replying to anything since no other party had argued about the issue in opening briefs. Ten days later Pacific filed an opposition to the motion to strike arguing that WBFAA's motion was unsupported by legal citation, that Pacific's reply brief raised no new issues, "but simply elaborated briefly...on the previous discussion," and that it would be unfair to grant the motion because doing so would deny Pacific "the opportunity to address the issues WBFAA raised for the first time in its reply brief." This last argument seems to contradict the first one.

We appreciate WBFAA's apparent concern with reducing the amount of verbiage presented to this Commission for consideration. (Although the motion and opposition to it were about as long as Pacific's discussion on the subject in its reply brief.) We also agree that a reply brief ought to reply to something and do nothing more. However, Rule 75, our procedural rule on briefs does not even mention reply briefs let alone delineate their content, and the ALJ did not make any such proscription. Therefore, although we are not impressed with Pacific's argument in opposition, especially its last argument, we find no basis for granting the motion.

Turning to the presentation of the parties on this issue, it seems clear to us that the process created by GO 152 is working and has improved the quality of Pacific's installation and maintenance of private line alarm service. We are satisfied that Pacific is in substantial compliance with the requirements of GO 152 and that many of the discrepancies between the response times reported by WBFAA members and by Pacific have to do with industry misunderstandings of reporting requirements and, perhaps, insufficiently precise definitions in GO 152. Many other problems described by the WBFAA testimony either have been or can be remedied by informal discussions between the parties or GO 152 committee discussion and possible recommendations for GO modification. We find that the errors for which Pacific is responsible are neither so great nor so egregious that we ought to intervene by now adopting modifications to GO 152. The witnesses have offered no evidence that the GO 152 committee process is ineffective. In fact their testimony indicates that it is working quite well. Therefore, we conclude that it is not necessary or appropriate to adopt GO 152 modifications at this time.

We believe there are still many areas where service improvement can be achieved and that regular meetings of the committee is the best means of addressing such issues. For this reason we agree with Westphal that there should continue to be Commission representation at the quarterly GO 152 meetings, and we would therefore not approve a modification which removed the requirement from the General Order.

On the whole we find Pacific's service quality for the installation and maintenance of private line alarm service to be satisfactory.

C. Notice

In order to assure that their customers are aware of the changes authorized by this decision, we will require Pacific and the ITCs which are parties to this proceeding to notify their customers of changes in rates and services at least 15 days before these changes take effect.

X. Supplementary Rate Design

As indicated previously this decision leaves in place all the components of the surcharges on intraLATA billings. I.87-11-033, which is addressing regulatory flexibility for local exchange companies, holds open this present general rate proceeding for a supplementary rate design. Among other things, the revenue requirement changes due to the 1987 federal tax law changes, the USOA rewrite, inside wire, and 1988 attrition decisions will be reflected in rates based on the record developed in the supplementary rate design. We have also herein specified that we will address the rate design for Touchtone service in that phase. There will no doubt be still further issues needing to be addressed in that proceeding, including issues raised in the proposed stipulation in I.87-11-033. Such issues may be specified in one or more ALJ rulings, assigned Commissioner rulings, or Commission orders, to be issued as appropriate in conjunction with our review of Phase I rate flexibility issues. We do wish, however, to remind the parties that we intend to abandon the 1986 test year billing base with the close of this decision and to rely on more up to date billing base data in the supplementary rate design. For that reason we have ordered the parties to file 1988 and 1989 projected billing base data in the supplementary rate design phase.

On July 1, 1985 an Administrative Law Judge Ruling established an ex parte rule in this proceeding on the motion of William Knecht made on behalf of the Ad Hoc Group of Private Line Users, Parts Locator, Inc., Telephone Users Foundation, and California Association of Utility Shareholders. These parties were not active in Phase 2 of this proceeding and we conclude that their interest in having an ex parte rule in A.85-01-034 has lapsed. Our supplementary rate design will be developed in conjunction with our decisions in I.87-11-033, which does not have a similar ex parte rule in place. To place both proceedings on a consistent footing, therefore, we will extinguish the requirements of the July 1, 1985 ruling effective on the same date as the order in this proceeding.

Findings of Fact

1. In order to spread Pacific's billing surcharges equitably and avoid unnecessary rate fluctuations, surcharges should be spread in the supplemental rate design based upon updated billing base data.

2. Pacific's 130 Call Allowance Plan proposal caps the monthly rate at the same price as its flat rate Unlimited Calling Plan proposal.

3. Although flat rate service is less costly to administer than measured service, the structure of Pacific's 130 Call Allowance Plan would make the flat rate service option uneconomical and would essentially eliminate it.

4. Pacific proposes separate access and usage rate elements for local residence services, though the rate design does not track access and usage costs.

5. Pacific proposes eliminating the present 2-tier pricing structure and reducing the charge for calls in excess of the 60-call allowance under the present Lifeline Measured Call Plan.

6. It is this Commission's intent to authorize a rate design, including the authorization of measured basic rates, which promotes economic efficiency.

7. Pacific's Universal Lifeline Telephone Service (ULTS or Lifeline) proposal expands service options for the low income customers who qualify for ULTS consistent with AB 3288.

8. Pacific proposes to increase the charge for installation or service on the first business line by over 42%.

9. CBCHA/TCA and FEA argue that it is necessary to move away from residual pricing and toward market-based or cost-based pricing for residence service except Lifeline.

10. Pacific proposes to increase measured line business rates, and has proposed an original and an alternative rate increase for the initial minute of local business usage.

11. Pacific proposes rate design changes in its PBX trunk rates which will bring revenue closer to costs.

12. The services available to a customer through a PBX trunk accompanied with Direct Inward Dialing (DID) are similar to the services available through Centrex.

13. In response to the argument that the determination of when a PBX trunk rather than an ordinary business line is necessary, Pacific has proposed an alternative to its initial proposal which increases rates for PBX trunk access by less than the initial proposal.

14. Pacific needs adequate written criteria describing the design parameters for PBX service so that its customers know when they need a PBX trunk rather than an ordinary business line.

15. Pacific's proposed Centrex rate design adds rates for its new digital services.

16. Pacific has not demonstrated the reasonableness of its proposed large decrease in the tie line rate, or the large overall revenue requirement decrease in its Centrex proposal.

17. Implementation of a separate trunk sensitive rate provides an equitable balance of charges for both PBX and TAS users of DID services.

18. Though Pacific's DID cost study is not as thorough as it could have been, it clearly shows that there is no cost basis for differentiating charges for successive blocks of DID station numbers.

19. Pacific's cost study is not complete enough to warrant the rates it proposes for DID station number block charges.

20. TASC proposes reducing the rate for DID station number blocks from the proposed 1.25 to a 1.0 revenue to cost ratio.

21. TASC's request for cancellation of Pacific's Basic Termination Charge for termination of DID service raises an issue which cannot be resolved in this proceeding because Pacific has had no opportunity to respond.

22. TURN asks that Pacific's public coin telephone rates be reduced from $.20 to $.10, or at least to $.15.

23. Pacific requests a 55% increase in its access rates for semi-public coin service. Its evidence shows that costs exceed revenue by 45%.

24. Pacific requests an increase in service charge rates for semi-public coin service which approximately reflects the amount by which costs exceed revenue.

25. Pacific proposes to add a deposit requirement of about $400 to $500 for semi-public coin service at locations it deems to be "not secure."

26. Pacific has produced no new COPT cost evidence since that presented to this Commission when its present COPT rates were authorized.

27. Pacific's presently authorized recurring COPT rates are the same as its ZUM Zone 1 rates.

28. At the time present COPT rates were set residence and business usage rates were the same for ZUM Zone 1.

29. COPT costs have characteristics similar to those for measured business lines.

30. The record in this proceeding presents no cost data which supports adopting nonrecurring COPT rates for installation, repair, and conversion different from the percentage increase this decision adopts for business and residence services.

31. Pacific proposes increasing the rate for its nonpublished service and adding a new service, Directory Assistance Listing (DAL) at the present rate for nonpublished service.

32. Pacific proposes increasing the rate for its Verification Interrupt service.

33. The impact of Pacific's proposal to reduce certain Remote Call Forwarding (RCF) rates depends upon authorization of its concomitant proposal to grandfather foreign exchange service.

34. Pacific and DRA both propose consolidation of certain MTS mileage bands and new rates for these mileage bands. DRA's consolidation proposal addresses only the longer-haul bands, while Pacific's consolidates shorter-haul as well.

35. The consolidation and rate proposals of DRA, Pacific, and CBCHA/TCA all provide a contribution over cost.

36. CBCHA/TCA's MTS rate proposal is part of an overall rate design proposal which is premised on moving usage rates for those with bypass alternatives toward economic costs, without consideration of the benefits of economic pricing to captive consumers.

37. DRA's MTS rate proposal provides a very minimal impact on the rates of MTS users.

38. It is the Commission's policy to give greater weight to economic pricing, including its application to MTS rates.

39. Pacific proposes to eliminate its Optional Calling Measured Service (OCMS), changing the way the monthly allowance is deducted for the Community Calling Plan, extending Circle Calling to 50 miles to conform to its proposed rate band consolidation, and reducing the choices under its Call Bonus Wide Area Plan from six to three.

40. General supports Pacific's proposed changes in optional toll discount plans and further proposes that Community Calling also be eliminated.

41. DRA objects to any changes in optional toll discount plans.

42. This Commission ordered Pacific and General to prepare and submit studies of subscriber usage of OCMS and ORTS in order to determine the degree of diverted usage and the degree of additionally generated usage under these plans.

43. Pacific states that the sample size of its OCMS subscriber usage study "cannot represent a valid sample."

44. Pacific proposes rate changes for 800 Service which will reduce revenue by over $11 million.

45. Pacific proposes rate changes for Outward WATS service which would increase revenue by $1.516 million.

46. The criteria Pacific applied in determining its proposed ZUM expansion are appropriate.

47. Pacific's claim of $1.13 million in implementation costs for ZUM expansion appears to be valid.

48. Pacific proposes consolidating ZUM Zones 2 and 3.

49. CBCHA/TCA propose an additional ZUM zone to cover distances between 17 and 30 miles which are presently billed at toll rates.

50. CBCHA/TCA propose elimination of detailed ZUM billing.

51. TURN proposes elimination of ZUM and adoption of an optional metropolitan flat rate service in metropolitan extended areas.

52. General, Pacific, and DRA have asked this Commission to designate a forum to hear the ZUM issues affecting customers of General, Pacific, and Continental, which General has raised in this proceeding.

53. The weight of the favorable data on metropolitan flat rate service is not strong enough to overcome the considerable likelihood that implementation of such service could jeopardize the subsidy to basic rates provided by the present discounted toll options.

54. Pacific proposes withdrawing FEX service except as to existing customers at existing locations without providing a bottoms-up cost study for FEX service.

55. Pacific has studied less costly alternatives to present FEX provisioning which are presently technically feasible.

56. Pacific's FEX cost studies are sufficient for determining rates, but do not provide a sufficient basis for the authorization of grandfathering FEX service.

57. Pacific's proposal to unbundle FEX rates is unopposed.

58. General's proposal to set FEX rates based on a private line model does not reflect the type of service FEX customers receive. Pacific's local service model does.

59. Present FEX mileage rates are close enough to cost that it is unnecessary to adopt rates different from the present mileage rates for local service which this decision retains.

60. It is reasonable for Pacific to adopt rates for FEX access to the local network which are the same as local service access rates.

61. Pacific's nonrecurring FEX rates are set far below cost.

62. Raising Pacific's nonrecurring FEX rates by more than 100% would produce unnecessary rate shock.

63. Pacific has proposed adopting the proportion of its present FEX rate which is attributable to the FEX increment as its FEX increment rate.

64. General's meet-point billing proposal does not detail how such billing will assure that customers will not be double-billed for any portion of their FEX service, how tariffs would be restructured, or how customers would be notified of the change.

65. Pacific's use of Functional Accounting in its tops-down category analysis improved Pacific's ability to produce reliable tops-down cost allocations.

66. Pacific's use of Functional Accounting made it more difficult for the parties to review and verify Pacific's reconciliations between tops-down and bottoms-up studies.

67. Pacific's cost studies comply with the requirements of D.83-04-012, the Commission's Cost Manual decision.

68. Pacific's loop study is acceptable although the overall study results do not comport with this Commission's intent in D.85-02-030.

69. The methodology of Pacific's Ready to Serve cost study is acceptable, as is the distribution of total RTS plant to private line service.

70. Pacific's private line service volume estimates showed some errors and variations between different witnesses.

71. DRA's review of Pacific's private line service volumes concluded that the volumes based on Pacific's PLHF reports are more accurate than earlier volume projections.

72. Pacific's allocation of SARTS testing costs to private line service offerings is reasonable.

73. Although Pacific's estimates for nonrecurring labor activities for private line are somewhat overstated, the intervenors' claims of overstatement are exaggerated.

74. DRA proposes a moderate downward adjustment to Pacific's private line nonrecurring labor costs.

75. The cost conclusions in the "Robin & Dackerman Report" and in Pacific's "SSA Report" have no bearing on the cost studies presented by Pacific in this proceeding.

76. Pacific proposes deaveraged private line local loop rates.

77. Pacific proposes to implement a separate alarm transport tariff in order to offer alarm transport customers lower rates.

78. TASC proposes disaggregation of secretarial line installation charges between designed and nondesigned lines.

79. A customer's decision about whether to order designed or nondesigned secretarial lines is often based on Pacific's engineering needs rather than the customer's usage.

79a. Separate cost-based installation charges for designed and nondesigned secretarial lines will promote more cost-effective use of secretarial lines by answering services and thereby reduce the revenue needed to subsidize designed secretarial line installation.

79b. Answering services operate in a competitive voice messaging market which will produce more overall benefits for consumers if nondesigned secretarial lines are priced at their cost.

79c. Based on Pacific's study of the cost to install non-designed secretarial lines, we find that the reasonable cost of installing nondesigned secretarial lines is $125.

80. TASC asks this Commission to adopt a new "move" charge for secretarial lines.

81. TASC requests that Pacific be required to submit a bulk move tariff for secretarial lines.

82. Pacific has requested that certain telegraph private line services be limited to those customers currently receiving the service.

83. Pacific's private line costs far exceed its private line revenues.

84. Pacific proposes increasing private line recurring rates in three annual increments.

85. DRA proposes a single private line recurring rate increase, which is larger than Pacific's first year increase, but much smaller overall.

86. Pacific proposes increasing most nonrecurring private line rates by 25%.

87. DRA proposes increasing most nonrecurring private line rates by 100%.

88. Changes in Pacific's private line rates affect the settlements revenue of the independent telephone companies (ITCs).

89. The pooled billing surcharge imposed by Pacific and the ITCs which concur in its access services tariffs was established in D.85-06-115 as an interim measure pending the adoption of a rate design for Pacific in this proceeding.

90. The ITCs have filed with this Commission reports of their total and separated California results of operations for 1986 at present rates and charges and adjusted to include the effects of Pacific's requested rates and charges and DRA's proposed rates and charges, as required by Order Instituting Investigation and Consolidating Proceeding (OII) I.85-03-078.

91. Some ITCs which concur in Pacific's access services tariffs have filed with this Commission advice filings with proposals to replace the expiring pooled surcharge with a bill and

keep surcharge calculated to generate equivalent revenue to be effective after the issuance of this rate design decision pursuant to authority granted in D.85-06-115.

92. Customers of ITCs were notified of the Pacific rate proceedings in 1985, and each ITC again notified its customers of the hearing dates and the ITC revenue effects and tariff changes precipitated by the expiration of the pooled access surcharge projected by the ITC and DRA prior to settlements effects hearings in 1986.

93. A late-filed supplemental brief on HCF issues and a motion for leave to file it were presented to the Commission after the submission date for briefs on this issue.

94. The ALJ granted the motion to late-file the supplemental brief.

95. The presently authorized HCF and the HCF proposed by the joint brief, both of which are funded from the interLATA Carrier Common Line Charge (CCLC), allow for recovery of some intraLATA operating costs. AT&T claims that the latter unlawfully discriminates against the IECs because they alone pay the CCLC.

96. The scope of rate protection under the joint HCF proposal is expanded from that of the previously adopted HCF to include other toll- and access-related changes and their effect on the ITC's settlements revenue.

97. The joint HCF proposal eliminates the prior revenue requirement review which this Commission found to be necessary in D.85-06-115.

98. The joint proposal for an HCF reduces the eligibility threshold previously established from 200% to 150% of rates charged for similar services in comparable neighboring exchanges. There is little data to support either figure.

99. Prior to divestiture this Commission authorized intrastate toll surcharges for Citizens, Sierra, and Cal-Ore. The question of whether these surcharges should continue is pending before this Commission in C.85-07-062. AT&T claims that the interLATA portion of these surcharges should be removed in the present proceeding.

100. AT&T objects to the continuation of the bill and keep access surcharge as an alternative to participation in the intrastate HCF for concurring ITCs as authorized by D.85-06-115.

101. General requests to be included in the flow-through provisions of the joint proposal's HCF.

102. Eligibility for the flow-through provision of the intraLATA HCF is contingent on eligibility to receive high cost funds.

103. The ITCs' request to combine various Commission ordered separations and settlements changes in one annual advice letter filing is advantageous to both the ITCs and their customers.

104. Ordering Paragraph 25 of D.87-08-048 directs that the $11 million access services rate reduction authorized by that decision is to be implemented by this final rate design order.

105. The $11 million excess revenue should be generated from all special access services except DDS and HiCap.

106. Pacific's settled share of the $11 million shift in revenue requirement out of access services authorized by D.87-08-048 will be $10.615 million.

107. Unless an adjustment is authorized ITCs which concur in Pacific's access rates will experience a reduction in settlements revenues as a consequence of the $11 million shift this Commission authorized for Pacific in D.87-08-048.

108. When Pacific's $11 million shift takes effect, AT&T's access expenses will be reduced.

109. D.87-12-067 as modified by D.88-03-064 authorizes small metropolitan local exchange companies the option of accruing the settlements effects resulting from the intraLATA SPF to SLU phase-down authorized beginning on January 1, 1988 in an interest bearing memorandum account or implementing a surcharge or surcredit. Sixteen ITCs elected to accrue the amounts in an interest bearing memorandum account.

110. The settlements effect in the memorandum account, when combined with the settlements effect resulting from the rate design authorized herein, produces a revenue shortfall for some ITCs and a revenue overcollection for others.

111. Pacific is meeting the overall installation and maintenance requirements for the provision of private line alarm service set out in GO 152.

112. Installation and maintenance of private line alarm service still requires the regular monitoring of a committee of utility, industry, and Commission representatives.

113. A.85-01-034 has an ex parte rule put into place by an ALJ Ruling dated July 1, 1985 while I.87-11-033 does not.

Conclusions of Law

1. There is no basis in the record for eliminating the flat rate service option; therefore, Pacific's 130 Call Allowance Plan should not be adopted.

2. Since local residence rates are set residually the proposed new access and usage rate elements serve no purpose and may create confusion. Their implementation should be denied.

3. Incremental cost data is necessary to a more accurate determination of whether measured rates for basic exchange service promote or hinder economic efficiency.

4. Lifeline-eligible customers will be better served if they receive the same plan options available to other ratepayers, but at a discounted rate. The Lifeline rates Pacific proposes comply with statutory requirements. Therefore, Pacific's proposal to add a flat rate Lifeline option and to reduce the charge for measured rate calls beyond the 60-call allowance should be granted.

5. The purpose of the Universal Telephone Service Fund is to make telephone companies whole for the provision of discounted service to low-income individuals or families.

6. Pacific's proposal to give residence customers a 90-day period to choose a different basic service without being subject to a change fee is reasonable and should be granted.

7. The evidence on this record does not warrant moving to strictly cost-based or market-based pricing of local residence service at this time. However, there should be some adjustment to local residence service to reflect diminishing subsidy sources.

8. The revenue requirement increase for local residence and business service should be set residually.

9. The revenue requirement increase for local residence service should be spread across all recurring local rates, including service connection rates but excluding rates for minutes of use or message units, on a uniform basis, rounded for ease of administration.

10. Pacific's proposed increases in measured business line rates should not be adopted. Rates other than trunk rates should be increased by the same percentage as authorized for residence rates.

11. Pacific's alternative rate for the initial minute of local business usage is not justified and should not be adopted.

12. It is reasonable to raise PBX trunk rates to make them more competitive with Centrex rates.

13. Because of the ambiguity inherent in determining when a PBX trunk, rather than an ordinary business line, is needed, it is not reasonable to raise PBX trunk rates by over 94% as Pacific initially proposed. Pacific's reduced alternative proposal is a reasonable compromise if Pacific first develops a set of criteria describing to potential PBX customers when a designed circuit is required.

14. Pacific's Centrex revenue requirement should not be decreased by the large amount proposed by Pacific.

15. Pacific's Centrex rate design should be changed to incorporate rates for Pacific's new Centrex services.

16. A slight decrease in Pacific's Centrex revenue requirement will allow Centrex to be reasonably competitive with PBX service in conjunction with DID.

17. Keeping the Centrex tie line rate at its present level rather than reducing it as Pacific proposes is a reasonable means of avoiding a large overall revenue decrease from Centrex services.

18. It is reasonable for Pacific to adopt a disaggregated rate design for DID which has a separate trunk sensitive rate element.

19. Pacific's DID station number block charge should be the same for each block of 100 numbers.

20. TASC's proposal for DID station number block rates would result in a charge of $45 for each 100 DID station numbers.

21. Pacific's proposed rate level for DID station number blocks should be denied and TASC's should be adopted.

22. Pacific should address the reasonableness of retaining its DID Basic Termination Charge in its next general rate proceeding.

23. The evidence upon which TURN relies for its public coin rate proposal was considered when this Commission adopted the present coin rate in D.84-06-111. There is no basis for reexamining that evidence now.

24. Semi-public coin service rates should cover costs, but setting them above costs may discourage subscription to the detriment of users for whom this service provides their only ready access to the local network and a primary means of contacting those users.

25. Pacific's proposal for a semi-public coin service deposit requirement is too broad and open-ended. It should be denied.

26. Pacific's access and usage rates for COPT service should continue to reflect Pacific's measured business rates.

27. Pacific's nonrecurring rates for COPT installation, repair, and conversion service should be increased by the same

percentage adopted in this decision for similar business and residence services.

28. Pacific's proposed DAL service should be adopted, but the rates it proposes for DAL and for nonpublished service are not appropriate.

29. The evidence does not support an increase in Verification Interrupt rate.

30. The disposition of foreign exchange service rates in this opinion causes Pacific's projected revenue increase for RCF to be unrealistic.

31. Pacific's MTS rate band consolidation plan, which also applies to ZUM zones, obscures the transitional rate zone between local service rates and toll rates.

32. Pacific's MTS mileage zone consolidation and rate plan increases short-haul toll disproportionately to long-haul toll without justification. It should not be adopted.

33. CBCHA/TCA's MTS rate design which bestows benefit on those customers with bypass alternatives while ignoring the captive residence ratepayers should not be adopted.

34. DRA's MTS consolidation plan does not disadvantage short-haul customers, residential customers, or potential future competing intraLATA long distance carriers, and will promote increased usage.

35. DRA's MTS mileage band rate proposal should be adopted, except that the present rates for the initial minute of use for the 0 to 8, the 9 to 12, and the 13 to 16 mile-rate bands should be retained and the rates for additional minutes of use for these three-rate bands should be reduced by one cent.

36. Pacific has not informed this Commission about usage diversion and newly generated usage attributable to OCMS in its usage study or elsewhere.

37. Pacific has not studied the impact of its Community Plan proposal on subscribers who now exhaust their call allowance each month.

38. It is inappropriate, when designing rates to reflect a decrease, to change the Community Plan so that it provides less to the subscriber.

39. Pacific's proposal to reduce the choices for its Call Bonus Wide Area Plan from six to three, to reduce rates, and to reduce the monthly allowance is not sufficiently supported by the evidence.

40. Pacific's proposal to extend its Circle Calling Plan from 40 to 50 miles is mooted by the MTS mileage band configuration adopted in this decision.

41. Pacific's proposal for the Call Bonus Wide Area Plan is not adequately supported by the evidence.

42. Pacific's evidence is inadequate to support the rate changes it proposes for 800 Service and Outward WATS.

43. The ZUM expansion Pacific proposes into the San Francisco-East Bay Extended Area should be granted.

44. Pacific's ZUM expansion implementation costs should be recognized in its rates.

45. Consolidation of ZUM Zones 2 and 3 would tend to obscure the Commission policy to position ZUM rates between local service rates and toll rates to reflect costs which are lower than those for comparable MTS calls and to serve the needs of local communities of interest.

46. Expansion of ZUM to 30 miles would require unreasonable rate increases to other service offerings.

47. ZUM rates should continue to be set to reflect Commission policy, including consideration of economic pricing.

48. Moderate reductions in ZUM rates for additional minutes of use will provide the ZUM rate reduction which both CBCHA/TCA and

Pacific favor without disadvantaging the small consumer or obscuring the distinction between ZUM and MTS service.

49. ZUM customers should continue to receive detailed ZUM bills.

50. The benefits of TURN's metropolitan flat rate proposal are insufficient to support its adoption.

51. The record does not support Pacific's proposal to grandfather FEX service.

52. That part of Pacific's unbundled FEX rate design which sets a separate FEX increment should be granted; however, access and usage rates should remain as one rate.

53. Pacific's nonrecurring FEX rates should be increased by 100%.

54. Pacific's proposal to set rates for the FEX increment to reflect that portion of the present rate which is attributable to the FEX increment should be adopted.

55. General's meet-point billing proposal cannot be adopted unless further implementation detail is provided.

56. DRA's difficulty in assessing Pacific's use of Functional Accounting in its future tops-down category analyses is alleviated by the conversion mechanism agreed to in I.87-02-023.

57. The overall reliability of Pacific's loop study is reduced by its failure to allow a meaningful tops-down to bottoms-up comparison.

58. The inconsistency in Pacific's service volume projections does not seriously affect its recurring cost study conclusions.

59. The service volumes relied upon by DRA were superior to those relied upon by Pacific in its private line cost studies.

60. DRA's proposed adjustment to Pacific's private line nonrecurring costs is reasonable.

61. The evidence does not support deaveraged private line local loop rates.

62. The evidence does not support the reasonableness of implementing a separate alarm transport tariff.

63. It is reasonable to adopt TASC's proposal to the extent of disaggregating the secretarial line installation charge into one rate for designed lines and another for nondesigned lines.

64. TASC's proposal for a "move" charge for secretarial line service is inconsistent with Pacific's cost studies.

65. There in not sufficient evidence in this record to warrant ordering Pacific to submit a bulk move secretarial line tariff.

66. Pacific's proposal to limit certain telegraph private line services is reasonable.

67. Pacific's private line revenues should be increased.

68. Pacific's proposal for three annual incremental recurring private line rate increases is excessive in light of the possibilities for error in its cost studies.

69. DRA's proposed recurring private line rate increases are reasonable.

70. Pacific's proposed nonrecurring private line rate increases are not sufficient in light of the gap between costs and revenues.

71. DRA's proposed nonrecurring private line rate increases are reasonable.

72. The ITCs should be authorized to offset settlements revenue losses due to the changes adopted in this Decision.

73. Reports filed by ITCs pursuant to I.85-03-078 and advice filings made by ITCs pursuant to the authority granted in D.85-06-115 regarding revenue changes precipitated by the expiration of the pooled access surcharge do not constitute applications to increase a rate or charge as that phrase is used in Public Utilities Code § 454.

74. The notices given by ITCs to their customers regarding possible tariff changes resulting from the expiration of the pooled access surcharge were timely, adequate, and proper.

75. The accompanying motion stated good cause for filing the late-filed supplemental brief on HCF issues.

76. The ALJ's ruling granting the motion to late-file the supplemental brief was proper.

77. Allowing regulated IECs to flow through the effects of changes in the HCF increment on the CCLC access charge eliminates any unfair disadvantage to the IECs.

78. The scope of rate protection in the joint proposal's HCF is an appropriate means of protecting ITC settlements revenues, and ultimately protecting the continued availability of basic telephone service to ITC customers.

79. The provisions of the joint proposal for an HCF which allow the ITCs until December 31, 1989 to file for rate review without loss of HCF funding, and then provide for annual funding reductions, will allow an orderly progression of rate case processing while preventing against rate shock and protecting HCF funders and ratepayers generally from abuse.

80. The strong support expressed for the move to a 150% eligibility criterion balanced against the scanty data to support either that criterion or the previously adopted 200% criterion makes it reasonable to adopt the 150% figure at this time.

81. The provisions of the jointly proposed HCF are reasonable and should be adopted.

82. This is not the proper forum to determine the merits of continuing the previously authorized intrastate toll surcharges of Citizens, Sierra, and Cal-Ore.

83. The option of a bill and keep access surcharge as an alternative to participation in the intrastate HCF for ITCs concurring in Pacific's access services tariffs should be eliminated.

84. General is ineligible for HCF funds.

85. The flow-through provisions of the new HCF are only reasonably applicable where an ITC is found to be eligible for HCF

funds. Since General will not be eligible for these funds, it should not be eligible for the flow-through of rate changes set out in the new HCF scheme.

86. The special access revenue requirement reduction of $11 million should be spread on a uniform percentage basis among all special access services excluding DDS and HiCap.

87. Pursuant to policy set forth in D.85-06-115, each ITC concurring in Pacific's access services tariffs is entitled to increase its rates for nonaccess services by a dollar amount equivalent to the settlement impact on it from the $11 million access rate shift which this Commission authorized for Pacific in D.87-08-048. The amount of the settlement impact on each concurring ITC is set forth in Table 2 to this decision.

88. Pursuant to policy set forth in D.85-03-056, as modified by D.85-06-113, AT&T must pass on to its customers the expense reduction accruing to it from reductions in Pacific's access charges.

89. To recognize the effect of this Commission keeping surcharges in place in this proceeding, the ITCs which implemented memorandum accounts pursuant to Ordering Paragraph 15A of D.87-12-067 as modified, should refund the settlement gains in those accounts.

90. Pacific is in compliance with the service quality criteria of GO 152 for the installation and maintenance of private line alarm service.

91. The GO 152 requirements for regular monitoring by a committee of utility, industry, and Commission representatives should not be modified at the present time.

92. Pacific's discussion of the GO 152 issue in its reply brief is not improper.

93. The Supplementary rate design phase of A.85-01-034 should be procedurally consistent with I.87-11-033 and for this reason the

requirements of the ALJ Ruling dated July 1, 1985 should be extinguished.

O R D E R

IT IS ORDERED that:

1. Pinnacles Telephone Company's late-filed comments to the ALJ's Proposed Decision are accepted.

2. In the supplementary rate design proceeding, showings of the parties, including the ITCs, shall be based on 1988 and 1989 projected billing base information including the number of access lines by service type, customer volume by service type, and billing volume by operation service category--e.g., interLATA access, intraLATA toll, toll private line, ZUM, and local exchange.

3. Pacific Bell's (Pacific) proposal for a 130 Call Allowance Plan is denied.

4. Pacific shall provide evidence of its incremental costs for basic exchange service and for calls within its ZUM areas in the supplementary rate design proceeding.

5. Pacific's proposal to create separate rate elements for access and usage for local residence services is denied.

6. Pacific shall continue to offer flat rate Lifeline service as an option for customers eligible for this program. Rates shall be one-half the regular rates less a credit of $.75 for telephone set rental, and less $.25 for inside wire maintenance.

7. Pacific's proposal to charge $.08 per call for all measured rate Lifeline calls after the 60-call allowance is granted.

8. Pacific may continue to seek reimbursement for all Lifeline discounts from the Universal Telephone Service Fund.

9. Pacific's specific proposals for test year 1986 rate increases for recurring local residence rates, and for service connection and installation and service, are denied. However,

Pacific is authorized to increase the tariff rates for these services as described in the foregoing opinion.

10. Pacific's proposed increases in measured business line rates are denied. However, Pacific is authorized to increase the tariff rates for all recurring local business rates, including installation and service, but not including trunk rates or minutes of use or message unit charges as described in the foregoing opinion.

11. Pacific's proposed alternative rate for the initial minute of local business usage of $.047 and its assignment of 4.7 message units for the initial minute of local measured service are denied.

12. Pacific shall make an advice letter filing with this Commission pursuant to General Order (GO) 96-A to amend the appropriate tariff schedules to describe design parameters which require the use of a designed circuit from the central office serving a PBX service.

13. Pacific's proposed rates of $12.25 for measured business trunk access and $34.25 for flat rate business trunk access as well as $4 per month increase in the rates for measured PBX trunk applicable to FEX with dial tone from an exchange other than an exchange of Pacific are granted upon adoption by this Commission of Pacific's PBX design parameter tariff.

14. Upon adoption by this Commission by Resolution of Pacific's PBX design parameter tariff, and implementation of the new PBX tariffs authorized in this order, Pacific shall provide each customer seeking PBX service, a copy of the design parameter tariff.

15. Pacific's proposed Centrex rate design is granted except that the tie line monthly rate element shall remain at its present level and the Exchange Access Trunking charge shall be set at one-tenth of the adopted measured and flat business trunk rate, rounded to the nearest $.05.

16. Pacific's proposal for a separate DID trunk sensitive rate element is granted as proposed.

17. Pacific's DID station number block charge proposal is denied. The alternative proposal of TASC, which sets the rate at $45 for each 100 DID station numbers is adopted.

18. Pacific shall address the reasonableness of continuing its DID Basic Termination Charge, including submission of a cost study of the costs this charge is designed to cover, in its next general rate proceeding.

19. TURN's proposal to reduce coin telephone rates is denied.

20. Pacific is authorized to increase its access rates for semi-public coin service by 45%.

21. Pacific is authorized to adopt its requested increase in service charge for semi-public coin service.

22. Pacific's proposal to require, at its discretion, a deposit for certain semi-public coin service installations is denied.

23. Pacific is authorized to set its COPT access line rates to reflect the uniform percentage increase authorized for business access rates in this decision.

24. Pacific is authorized to increase its rates for COPT installation, repair, and conversion by the same percentage authorized in this decision for business and residence installation and repair services.

25. Pacific is authorized to implement its proposed new Directory Assistance Listing service at the monthly rate of $.15.

26. Pacific's proposal to increase its rate for nonpublished service is denied.

27. Pacific shall provide this Commission with cost and revenue information for Touchtone service for consideration in the supplementary rate design proceedings.

28. Pacific's proposal to increase its Verification Interrupt rate is denied.

29. Pacific's proposal to reduce certain Remote Call Forwarding rates is denied.

30. Pacific's proposal for MTS rate band consolidation and pricing is denied.

31. CBCHA/TCA's proposal for MTS rate band pricing is denied.

32. DRA's proposal for MTS mileage zone consolidation is granted.

33. DRA's proposal for MTS rate band rates, as modified by this decision, is granted.

34. Pacific's proposal to eliminate OCMS is denied.

35. Pacific's proposal to change the means of deducting the monthly allowance under the Community Plan is denied.

36. General's proposal to eliminate the Community Plan is denied.

37. Pacific's proposal to reduce the choices for its Call Bonus Wide Area Plan from six to three, to reduce rates, and to reduce the monthly allowance is denied.

38. Pacific's proposal to amend its rates for 800 Service is denied.

39. Pacific's proposal to amend its rates for Outward WATS service is denied.

40. Pacific's ZUM expansion proposal in Exhibit 285 to add 12 exchanges to the San Francisco-East Bay Extended Area is granted. Within 90 days of the effective date of this order Pacific shall make an advice letter filing under the terms of GO 96-A to amend the appropriate tariffs for implementation of the ZUM expansion described in this decision.

41. Within 180 days of the effective date of this order Pacific, General, and Continental shall submit in I.87-02-025, in a phase separate from the current rate proceeding with which I.87-02-025 is consolidated, testimony and exhibits which address

the feasibility of implementing ZUM service over the additional routes set forth in Exhibit 384, the revenue requirement in terms of added plant and additional expenses associated with the expansion of ZUM over these additional routes, and the customer billing effects and settlements effects associated with implementing ZUM over these additional routes. These parties may also submit alternative proposals to that offered by General. Such alternative proposals shall also include testimony and exhibits addressing feasibility, revenue requirement, customer billing effects, and settlements effects. Further, prior to the submission of the testimony and exhibits Pacific, General, and Continental shall provide written notice to each of their customers who would be affected by the implementation of ZUM over the additional routes.

42. Pacific's proposal to consolidate ZUM Zones 2 and 3 is denied.

43. Pacific's proposal to differentiate between business and residence ZUM rates is denied.

44. CBCHA/TCA's proposal to adopt Pacific's consolidated ZUM rate zones and to add a new Zone 3 for distances from 17 to 20 miles is denied.

45. Pacific's specific proposal to decrease ZUM rates is denied, however, for ZUM Zones 2 and 3 "additional minutes of use" shall be reduced by one "calling unit" (presently $.01).

46. TURN's request that Pacific be ordered to implement optional flat rate metropolitan service is denied.

47. Pacific's proposal to grandfather FEX service is denied.

48. Within 60 days of the effective date of this order Pacific shall file an advice letter, with service upon all parties to this proceeding, which revises the appropriate tariffs to implement the mirroring of the Centrex exchange access trunking charges when providing FEX service to Centrex customers as described in the foregoing opinion. The advice letter shall also

contain the estimated 1986 annual billing and revenue effects associated with the implementation of such tariff revisions, and revisions to the customer billing surcharge to reflect the annual revenue effect of implementing such tariff revisions for Centrex service. The advice letter filing shall be subject to Commission authorization by resolution in order to take effect.

49. Pacific's proposal to unbundle recurring FEX rates is granted in a modified form. Pacific is authorized to set a rate for FEX access and usage and a separate rate for the FEX increment consistent with the foregoing opinion.

50. Pacific, General, and all other LECs which provide intercompany FEX service shall jointly consider a method for offering meet-point billing on a bill and keep basis for FEX service. LECs wishing to provide such service shall, within 120 days of the issuance of this order, file separate or joint studies with the CACD for review and approval setting forth the results of their study and their proposed tariff changes which provide for bill and keep billing of FEX service and which assure that FEX subscribers are not double-billed for any portion of their FEX service. The joint study shall address the type and methods of customer notice to be used as well as the conversion of each LEC's FEX tariff rate structure to a structure which will facilitate the implementation of the meet-point billing concept for FEX services. The LECs may thereafter file the approved plan with this Commission as an advice letter filing pursuant to GO 96-A. Such advice letter filings shall be served on all parties to this proceeding and shall be subject to authorization by Commission resolution before becoming effective. In those instances where the implementation of the meet-point billing concept for FEX services will result in a change in the annual revenues for a utility, the advice letter filing shall also include a revision to the utility's customer billing surcharge applicable to intraLATA services to reflect such a change in annual revenues.

51. Pacific's proposal for deaveraged private line local loop rates is denied.

52. Pacific's proposal for a separate alarm transport tariff is denied.

53. TASC's proposal to disaggregate the secretarial line installation charge is denied, except to the extent provided for in this order.

53a. Pacific shall make an advice letter filing with this Commission pursuant to GO 96-A to establish separate tariff language for designed and nondesigned secretarial lines. This distinction shall be based on the multi versus single central office distinction developed by TASC on the record. Upon adoption by this Commission by resolution of Pacific's tariff language, new installation rates of $125 for a nondesigned line and $277 for a designed line shall be authorized.

54. TASC's proposal for a "move" charge for secretarial line service is denied.

55. TASC's request that this Commission order Pacific to submit a proposal for a bulk move tariff is denied.

56. TASC's request that this Commission order Pacific to permit outside parties to place concentrators in Pacific's central offices is denied.

57. Pacific's proposal to limit certain telegraph private line services to current customers is granted. Pacific's tariffs for these services shall be consistent with the foregoing opinion as set forth in Appendix A.

58. Pacific's private line recurring rate proposal is denied.

59. DRA's private line recurring rate proposal is granted to the extent described in the foregoing opinion and set forth in the attached Appendix A.

60. Pacific's private line nonrecurring charge proposal is denied.

61. DRA's private line nonrecurring charge proposal is granted as described in the foregoing opinion and set forth in the attached Appendix A.

62. The motion of Carlos E. Benemann that we find untimely and improper the notice to the customers of independent telephone companies (ITCs) regarding the portion of these proceedings which addressed changes in ITC rate design necessitated by the impact of Pacific's eliminating its pooled access surcharge is denied.

63. The ALJ's ruling granting the motion to late-file a supplemental brief on intrastate High Cost Fund (HCF) issues is upheld.

64. The proposed modifications to the intrastate HCF mechanism adopted in D.85-06-115, as described in the foregoing opinion, are hereby adopted and shall be implemented in the manner described in Appendix B of this decision.

65. Until such time as an ITC's rates have been reviewed in a GO 96-A rate review or a general rate application proceeding, changes in rates as authorized by the intrastate HCF mechanism set forth in Appendix B shall be made by a uniform percentage increase or decrease applied to all nonaccess rates, except as specifically limited elsewhere in these orders.

66. Pacific Bell and ITCs implementing rate and offering changes pursuant to this order shall notify their customers of such changes at least 15 days prior to the effective date of such changes.

67. The request of General to be eligible for the flow-through provisions of the intrastate HCF as described in Appendix B is denied.

68. ITCs which are eligible to participate in the intrastate HCF may not, after the effective date of this order, choose to adopt a bill and keep access surcharge as an alternative to participation in the intrastate HCF.

69. Any interexchange carrier which is subject to rate base regulation by this Commission may make appropriate advice letter filings under GO 96-A to flow through to its rates the effect of changes in the HCF fund increment on the CCLC access charge, except in cases where a change is of minimal effect. The annual HCF

changes on January 1 shall be netted against contemporaneous access charge reductions reflecting SPF to SLU separations changes.

70. The ITCs which participate in the intrastate HCF may combine in a single annual advice letter filing the net settlements effect of changes in the HCF fund increment described in the above ordering paragraph with other Commission ordered settlements and separations changes.

71. Within 30 days after the effective date of this order each of the following ITCs: Calaveras, Cal-Oregon, Ducor, Foresthill, Happy Valley, Pinnacles, Siskiyou, and Tuolumne, shall make an advice letter filing to adjust its tariff schedules to implement a bill and keep surcredit on intraLATA services to reflect the settlements gains of today's rate design decision as shown in Appendix C. In establishing the bill and keep surcredit each ITC shall use the 1986 intraLATA billing base set forth in Appendix E. The advice letter filing with revised tariff schedules shall conform with the provisions of GO 96-A. The revised tariff schedules shall become effective 60 days after the effective date of this order and shall apply to services rendered on and after their effective date.

72. Hornitos Telephone Company shall accrue its settlements gains as reflected in Appendix C, in a memorandum account from the effective date of this decision with interest accrued at a rate equal to 1/12th the interest rate on 3-month commercial paper for the previous month, as published in the Federal Reserve Statistical Release, G.13, or its successor, until further order of this Commission.

73. Within 30 days of the effective date of this order each ITC except Hornitos Telephone Company shall eliminate its interest bearing memorandum account by implementing a bill and keep surcharge or surcredit, spread over one year, on intraLATA services by advice letter filing in conformance with GO 96-A. In establishing the bill and keep surcharge or surcredit the ITC shall use the 1986 intraLATA billing base reflected in Appendix E. The revised tariff schedules shall become effective 60 days after the

effective date of this order and shall apply to services rendered on or after the effective date of the tariff revisions.

74. Within 30 days of the effective date of this order Pacific shall make an advice letter filing under the terms of GO 96-A to amend its Access Services Tariff, Schedule Cal. P.U.C. 175-T, to reduce its billings from special access services on a uniform percentage basis, excluding DDS and HiCap, by $11 million in a manner consistent with the foregoing opinion. The effective date of the revised tariff sheets shall be 60 days after the effective date of this order. The revised tariff schedules shall apply to services rendered on and after the effective date of the revised schedules.

75. Within 14 days after Pacific makes its advice letter filing to reduce its special access rates in the manner described in this decision AT&T shall file an advice letter with this Commission under the terms of GO 96-A which proposes accumulating the reduced access charge expense resulting from this decision in a memorandum account, with interest, commencing on the effective date of the Pacific tariff revision and running through December 31, 1988 at which time AT&T shall roll this accumulated reduced expense into its computation of the effects on access rates of the SPF to SLU phase down of the local exchange carriers which will be reflected in AT&T's rates.

76. Western Burglar and Fire Alarm Association's motion to strike the discussion in Pacific's reply brief of GO 152 regarding the installation and maintenance of private line alarm service is denied.

77. Within 30 days after the effective date of this order Pacific shall make an advice letter filing under the terms of GO 96-A to amend its tariffs to reflect the rates, charges, and conditions as set forth in Appendix A. The effective date of the revised tariff sheets shall be 60 days after the effective date of this order. The revised tariff schedules shall apply to service rendered on and after the effective date of the revised schedules.

78. Within 30 days after the effective date of this order each Independent Telephone Company, except for General Telephone Company of California, is authorized to make an advice letter filing to adjust its basic exchange service rates and establish a bill and keep billing surcharge on intraLATA services to reflect the settlement effects of today's rate design decision as set forth in Appendix C of this decision. Each ITC which has already incorporated a billing surcharge for the settlements effect of SPF to SLU may, at its option, add the amount reflected in its surcharge to the total settlements figure shown on Appendix C and adjust its advice letter filing accordingly. Each ITC shall use the 1986 customer volumes which are shown in Exhibit 352 and are reflected in Appendix D of this decision. Further, in establishing the bill and keep intraLATA billing surcharge each ITC shall adjust its 1986 intraLATA billing base set forth in Appendix E of this decision to reflect the newly revised basic exchange service rates. The process which each ITC shall use to recover its settlement effects is as follows:

1. Increase basic exchange service rates exclusive of EAS and SRA increments by a uniform percentage up to 100% of the present rates, rounded to the nearest $.05 but not to exceed the 150% threshold level of comparable urban rates.

2. Implement a bill and keep surcharge on intraLATA services to recover the remaining settlements effects if the revised basic rates do not fully recover the settlements effects and the 1-party residence flat rate has not exceeded the threshold level of 150% of comparable California urban rates.

3. Recover the remaining settlements effects from the intrastate High Cost Fund if the revised basic local rates do not fully recover the settlements effects but the 1-party residence flat rate has reached the 150% threshold level.

The advice letter filing with revised tariff schedules shall conform with the provisions of GO 96-A. The revised tariff schedules shall become effective 60 days after the effective date of this order, and shall apply to services rendered on or after the effective date of the tariff revisions.

79. Within 30 days of the effective date of this order General Telephone Company of California is authorized to make an advice letter filing under the terms of GO 96-A to incrementally revise its bill and keep intraLATA billing surcharge to reflect its settlements effect as set forth in Appendix C. In calculating the incremental billing surcharge General shall use the adopted 1986 customer billing base in D.85-12-081. The revised tariff schedule shall become effective 60 days after the effective date of this order, and shall apply to services rendered on or after the effective date of the tariff revision.

80. The requirements of the ALJ Ruling dated July 1, 1985 are extinguished on and after the effective date of this order.

This order is effective today.

Dated July 8, 1988, at San Francisco, California.

STANLEY W. HULETT
President
DONALD VIAL
G. MITCHELL WILK
JOHN B. OHANIAN
Commissioners

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

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

Victor Weisser

Victor Weisser, Executive Director

APPENDIX A
SHEET 1 OF 20
PACIFIC BELL
RATES AND CHARGES

Schedule Cal. P.U.C. No. A2.
Billing Surcharges

The following revisions are ordered:

2.1 RULES
2.1.33 RULE NO. 33 - BILLING SURCHARGES

1.A	Rates	Monthly Percentage
	Adjustment Factor	(2.916%) *

The monthly percentage applies to all recurring and nonrecurring rates and charges for service or equipment provided under all of the utility's tariff schedules except the following:

The list of excepted services shall remain unchanged.

1.B	Rates	Monthly Percentage
	Adjustment Factor	(2.616%) **

The monthly pecentage applies to intraLATA toll provided under all of the Utility's tariff schedules except those items excluded in 1.A preceeding, other than Message Telecommunications Service A6., exclusive of Federal and Local excise taxes, and Federal income taxes.

1.C	Rates	Monthly Percentage
	Adjustment Factor	(11.552%) ***

The monthly pecentage applies to all recurring and nonrecurring rates and charges for service or equipment provided under Schedule Cal. P.U.C. No. 175-T.

* Monthly Percentage shall be 1.446% effective January 1, 1989.
** Monthly Percentage shall be 2.176% effective January 1, 1989.
*** Monthly Percentage shall be (6.882%) effective January 1, 1989.
( ) Denotes negative surcharge.

APPENDIX A
SHEET 2 OF 20
PACIFIC BELL
RATES AND CHARGES

Schedule Cal. P.U.C. No. A3.
Dual Element Charges

The following charges are authorized:

3.1. CHARGES FOR ACCESS LINES, LABOR AND SERVICE ENHANCEMENTS

3.1.2 ACCESS LINES (PRIMARY AND EXTENDED SERVICES)

A. INDIVIDUAL, PARTY LINE, SUBURBAN, TELEPHONE ANSWERING AND FARMER LINE SERVICE

New and additional local and extended area service charges, each line

	Service Charge
- Answering line	$ 70.75
- Individual line residence or business Service, complex	70.75
- Individual, party line, suburban or Farmer line business service, simple	70.75
- Individual, party line, suburban or Farmer line flat rate residence service, simple	34.75
- Individual, party line or measured rate residence service, simple	34.75
- Individual line, AIS (Airport Intercommunicating Service)	70.75
- Individual line measured rate business service - data, all services	176.75
- Individual Resale Line	70.75
- Toll terminal line	70.75

B. TRUNK LINE SERVICE

New and additional local and extended area service charges, each trunk

- Trunk line service, residence, business or TAS (Telephone Answering Service)	70.75
- Trunk resale line	70.75
- Toll terminal trunk	70.75

D. Charges set forth in the adopted revisions for schedule Cal. P.U.C. No. A9. apply.

APPENDIX A
SHEET 3 OF 20
PACIFIC BELL
RATES AND CHARGES

Dual Element Charges - continued

	Service Charge
3.1.	
3.1.2	
E. CENTREX DORMITORY SERVICE	
- Each primary line	$ 34.75
G. FOREIGN EXCHANGE SERVICES - BUSINESS AND RESIDENCE SERVICES	
1. Foreign Exchange (FXS) or Foreign District Area Service (FDA of the same exchange only)	
a. Contiguous, each line or trunk	
Business	
- Individual access line	380.00
- Answering line	380.00
- Trunk line service	380.00
- Trunk line service, TAS	380.00
- Centrex primary access line (see Note 1)	340.00
- Toll terminal	380.00
- Tie line (FDA of same exchange only)	380.00
Residence	
- Individual and party line service	260.00
- Trunk line service	380.00
b. Noncontiguous, each line or trunk	
Business	
- Individual access line	580.00
- Answering line	580.00
- Trunk line service, residence or business	580.00
- Trunk line service, TAS	580.00
- Tie line (FDA of same exchange only)	580.00
- Centrex primary access line (see Note 1)	540.00
Residence	
- Individual and party line service	460.00
- Trunk line service	580.00
2. Foreign Prefix Service (FPS), of the same exchange	
a. Contiguous	
- Each residence or business line or trunk	380.00
b. Noncontiguous	
- Each residence or business line or trunk	580.00

NOTE: 1: Plus Installation Charge for primary line as set forth in Schedule Cal.P.U.C. No. A.9.1.

APPENDIX A
SHEET 4 OF 20
PACIFIC BELL
RATES AND CHARGES

Dual Element Charges - continued

3.1.
3.1.2.

J. SEMIPUBLIC SERVICE

	Service Charge
- Each access line, with Utility provided set and premises wiring	$ 240.00
- Each COPT access line, with customer provided set	111.25

3.1.6 MOVE, CHANGE, REARRANGEMENT OR MODIFICATION OF ACCESS LINE AND OTHER MISCELLANEOUS CHANGES, ALL SERVICES, EACH LINE OR TRUNK

	Service or Labor Charges
n. Change from utility provided Semipublic Coin, Public Coin, Business, or Residence service to COPT service - Each access line	$ 75.75

APPENDIX A
SHEET 5 OF 20
PACIFIC BELL
RATES AND CHARGES

Schedule Cal. P.U.C. No. A5.
Basic Exchange Access Line Services

The following rates are authorized:

5.2 LOCAL EXCHANGE SERVICE

5.2.1 MEASURED RATE SERVICE

A. LOCAL EXCHANGE MEASURED RATE SERVICE

4. Rates and Charges

Service	Monthly Rate*
Individual Line Measured Rate Service - Data	$ 22.50
Individual Line Measured Rate Business Service	8.35
Individual Resale Line Measured Rate Business Service	19.20

5.2.4 FLAT RATE SERVICE

A. LOCAL EXCHANGE FLAT RATE SERVICE

4. Rates and Charges

Service	Monthly Rate*
Individual Line Flat Rate Business Service	$ 17.55
Individual Line Flat Rate Residence Service	8.35
Two-Party Line Flat Rate Business Service	11.90
Two-Party Line Flat Rate Residence Service	4.70

*Plus Extended Area Service Increments where applicable. Monthly rates apply in exchanges where the service is offered.

APPENDIX A
SHEET 6 OF 20
PACIFIC BELL
RATES AND CHARGES

Basic Exchange Access Line Services - continued

5.2
5.2.5 LOCAL SERVICE OPTIONS
B. FARMER LINE SERVICE

4. Rates and charges

Service	Monthly Rate*
Business Farmer Line Service	$ 4.95
Residence Farmer Line Service	2.65

C. SUBURBAN SERVICE

4. Rates and Charges

Service	
Four-Party Line Suburban Flat Rate Business Service	12.15
Four-Party Line Suburban Flat Rate Residence Service	4.90

5.3 PRIVATE BRANCH EXCHANGE TRUNK LINE SERVICE

5.3.1 MEASURED RATE TRUNKS

B. RATES AND CHARGES

Service	Monthly Rates*
Resale Trunks	$ 19.20

5.3.3 FLAT RATE TRUNKS

A. RATES AND CHARGES

Service	
Residence Trunks	12.55

*Plus Extended Area Service increments where applicable. Monthly rates apply in exchanges where the service is offered.

APPENDIX A
SHEET 7 OF 20
PACIFIC BELL
RATES AND CHARGES

Schedule Cal. P.U.C. No. A5.
Universal Lifeline Telephone Service

The following revisions are ordered:

5.2 LOCAL EXCHANGE SERVICE
5.2.5 LOCAL SERVICE OPTIONS
E. UNIVERSAL LIFELINE TELEPHONE SERVICE
4. Rates and Charges

g. ULTS - all day/hours

1PQ service is provided with an allowance of 60 untimed local calls. Local messages over this designated allowance are provided at the rates following:

	Rate per Message
61 and over	$ 0.08

Schedule Cal. P.U.C. No. A5.
Semipublic Telephone Service

The following revisions are authorized:

5.5 PUBLIC COMMUNICATION SERVICE - COIN AND COINLESS

5.5.2 SEMIPUBLIC TELEPHONE SERVICE

D. RATES AND CHARGES

Service	Monthly Rates*
Individual Line Semipublic Service	$ 29.00
Four-party Line Semipublic Service	29.00

*Plus Extended Area Service Increments where applicable. Monthly rates apply in exchanges where the service is offered.

PACIFIC BELL
RATES AND CHARGES

Schedule Cal. P.U.C. No. A5.
Customer-Owned Pay Telephone (COPT) Service

The following increases in rates are authorized:

5.5.3 CUSTOMER-OWNED PAY TELEPHONE (COPT) SERVICE

D. RATES AND CHARGES

Service	Monthly Rate Increase
COPT Measured Rate Business Service	$ 0.20
COPT Flat Rate Business Service	0.50

Schedule Cal. P.U.C. No. A5.
Zone Usage Measurement Service

The following revisions are ordered:

5.2 LOCAL EXCHANGE SERVICE
5.2.1. MEASURED - RATE SERVICE
B. ZONE USAGE MEASUREMENT SERVICE

4. Rates and Charges

c. Zone Calling

(1) Zone Calling Units are applicable to calls between the Zone as such Zones are identified in 3. preceding.

Zone Calling Units

Zone	Each Addl. Minute or Portion Thereof
2 (9-12 miles)	2 Units
3 (13-16 miles)	4 Units

APPENDIX A
SHEET 9 OF 20
PACIFIC BELL
RATES AND CHARGES

Schedule Cal. P.U.C. No. A5.
Foreign Exchange Service

The revisions set forth on pages 117 through 123 of Exhibit No. 286 except as modified below are authorized.

5.1 EXCHANGE AREAS
5.1.4 FOREIGN EXCHANGE SERVICE
D. ROUTES BETWEEN PACIFIC BELL EXCHANGES

2. Rates and Charges

a. Business Service

Within an exchange or district area contiguous or noncontiguous to the foreign exchange or district area. Rate per month for each business individual line measured rate primary station, business measured rate PBX trunk and joint user service.

(1) Foreign Exchange Station Service

	Monthly Rate
- Foreign exchange service increment	$ 11.25
- Basic access line rate	See Note 1
- Local Usage	See Note 2
- Mileage Rates	See Note 3
Los Angeles Exception Rate Treatment	
- DA's 1 thru 14	11.25
Exception:	
Contiguous Service in:	
- Rate Area A	12.85
- Rate Area B	14.45
- Rate Area C	16.05
- Noncontiguous Service	16.05

NOTE 1: Basic access line rate as set forth in Schedules Cal. P.U.C. Nos. A5.2. and A5.3.1. including EAS/SRA increments, if applicable.

NOTE 2: Local usage as set forth in Schedule Cal. P.U.C. No. A5.1.4.

NOTE 3: Mileage rates as shown in General Rates and Charges in C.1. and 2., preceding.

APPENDIX A
SHEET 10 OF 20
PACIFIC BELL
RATES AND CHARGES

Foreign Exchange Service - continued

5.1
5.1.4
D. ROUTES BETWEEN PACIFIC BELL EXCHANGES (cont'd.)
2. Rates and Charges (cont'd.)

b. Residence Service, Individual and Suburban

(1) Foreign exchange Station Service

	Monthly Rate
Foreign exchange Service Increment	
- 1FR/FW	$ 6.75
- 1MR/1SY	4.05
- 4ZR	2.70
- Basic access line rate	See Note 1
- Local Usage	See Note 2
- Mileage Rates	See Note 3

c. Residence Service Party Line

Within the listed local exchanges continguous to the listed foreign exchange. Rate per month for each residence two party line primary station, furnished only to the same customer on the same premises as of November 11, 1973.

USOC	Service
2FR++	FXS Two-Party Line flat Residence Service

	Monthly Rate
- Foreign exchange service increment	$ 2.90
- Basic access line rate	See Note 1
- Local Usage	See Note 2
- Mileage Rates	See Note 3

NOTE 1: Basic access line rate as set forth in Schedule Cal. P.U.C. No. A5.2. including EAS/SRA increments, if applicable.

NOTE 2: Local usage as set forth in Schedule Cal. P.U.C. No. A5.1.4.

NOTE 3: Mileage rates as shown in General Rates and Charges in C.1. and 2., preceding.

APPENDIX A
SHEET 11 OF 20
PACIFIC BELL
RATES AND CHARGES

Foreign Exchange Service - continued

5.1
5.1.4
D. ROUTES BETWEEN PACIFIC BELL EXCHANGES (cont'd.)
2. Rates and Charges (cont'd.)

d. Residence Service, Trunk Lines

USOC	Service
TFR++	FXS Flat Rate Residence Service First Trunk
RHR++	FXS Flat Rate Residence Service Additional Trunk

Within the listed local exchange to the listed foreign exchange. Rate per month for each residence trunk line service.

	Monthly Rate
- Foreign exchange service increment	$ 2.60
- Basic access line rate	See Note 1
- Local Usage	See Note 2
- Mileage rates	See Note 3

Foreign Exchange	Monthly Rate TFR/RHR
Los Angeles	
Contiguous Service in Exception Rate Areas (see Note 1)	
- Rate Area A	$ 4.20
- Rate Area B	5.80
- Rate Area C	7.40
- Noncontiguous Service (see Note 1)	7.40

NOTE 1: Basic access line rates apply as set forth in Schedule Cal. P.U.C. No. A5.3.3.A, including EAS/SRA increments, if applicable.

NOTE 2: Local usage as set forth in Schedule Cal. P.U.C. No. A5.1.4.

NOTE 3: Mileage rates as shown in General Rates and Charges in C.1. and 2., preceding.

APPENDIX A
SHEET 12 OF 20
PACIFIC BELL
RATES AND CHARGES

Foreign Exchange Service - continued

5.1

5.1.4.

E. ROUTES INVOLVING CONNECTING COMPANY EXCHANGES - SOUTHERN CALIFORNIA

F. ROUTES BETWEEN CONTIGUOUS EXCHANGES-CONNECTING COMPANY EXCHANGES-NORTHERN CALIFORNIA

G. ROUTES BETWEEN NONCONTIGUOUS EXCHANGES-CONNECTING COMPANY EXCHANGES-NORTHERN CALIFORNIA

Rates and Charges

Within an exchange contiguous or noncontiguous to the to the foreign exchange.

Rate per month for each Individual Line Primary Station, Business PBX Trunk and Joint User Service from the exchanges listed below:

Business and Residence Service

USOC	Service
1FR++	FXS Individual Line Flat Rate Residence Service
1FW++	FXS Individual Line Flat Rate Residence Service
4ZR++	FXS Four-Party Line Suburban Flat Rate Residence
1MB++	FXS Individual Line Measured Rate Business Service
1ML++	FXS Individual Line Measured Rate Business Line
1MS++	FXS Individual Line Measured Rate Business Line - Single Line Customer
7FB++	FXS Business Answering Line terminating on 6 Line Concentrator
7FL++	FXS Business Answering Line Terminating on a TAS
TMB++	FXS Measured Rate Business Service First Trunk
TM2++	FXS Measured Rate Business Service Additional Trunk
TM3++	FXS Measured Rate Business Service Additional Trunk-Outward Only
TM4++	FXS Measured Rate Business Service Trunk Inward Only

The following increases in monthly rates for foreign exchange services are authorized:

Services	Monthly Rate Increase
1FR, 1FW, 4ZR	$ 0.10
1MB, 1ML, 1MS, 7FB, 7FL	0.10

APPENDIX A
SHEET 13 OF 20
PACIFIC BELL
RATES AND CHARGES

Schedule Cal. P.U.C. No. A5.
Direct-In-Dialing To PBX Systems

The following rates are ordered:

5.3 PRIVATE BRANCH EXCHANGE TRUNK LINE SERVICE

5.3.4 DIRECT-IN-DIALING TO PBX SYSTEMS

C. RATES AND CHARGES

Trunk line services as shown elsewhere in this schedule, furnished at the appropriate rates and charges, are required in sufficient quantitites to meet the traffic demand in addition to the rates and charges for DID service:

1. Provided within the same exchange or district area:

	Monthly Rate
First 200 Direct Inward Dialing station numbers - Each 100 DID station numbers	$ 45.00
Over 200 Direct Inward Dialing station numbers - Each additional 100 DID station numbers	45.00
Circuit Termination - Each trunk	8.00

2. Provided within a different exchange or district area:

First 200 direct inward station numbers - Each 100 DID station numbers	45.00
Over 200 direct inward station numbers - Each 100 DID station numbers	45.00
Circuit Termination - Each trunk	8.00

APPENDIX A
SHEET 14 OF 20
PACIFIC BELL
RATES AND CHARGES

Direct-Inward-Dialing To PBX Systems - continued

5.3
5.3.4
C. RATES AND CHARGES

3. Provided from a foreign exchange, between district areas of an exchange or from a district area of an exchange to a contiguous or noncontiguous exchange:

	Monthly Rate
First 200 direct inward station numbers - Each 100 DID station numbers	$ 45.00
Over 200 direct inward station numbers - Each additional 100 DID station numbers	45.00
Circuit termination - Each trunk	8.00

Schedule Cal. P.U.C. No. A5.
Directory Listing Service

The revisions set forth in Appendix C of Exhibit 351 are ordered.

Schedules Cal. P.U.C. Nos. A5. and A9.
Centrex Service

The revisions set forth on pages 904 through 956 of Exhibit No. 286 except as modified below are authorized.

APPENDIX A
SHEET 15 OF 20
PACIFIC BELL
RATES AND CHARGES

Centrex Service - continued
9.1 DIAL SWITCHING SYSTEMS
9.1.1 CENTREX
D. RATES AND CHARGES

Exchange Access Trunking Charge Each Primary Line

1. A minimum requirement for each Centrex service is 20 or 100 working and/or non-working primary lines. Designate USOCs as follows:

Working primary lines - NRX
Non-working lines to make up minimum - NRXMN

a. Measured Rate Service	Monthly Rate Primary Lines ESS;DSS 1st 20 or less	#5XB 1st 100 or less	ESS;DSS;#5XB each Addl.
- Charge for working primary line	$ 25.00	$ 125.00	$ 1.25
- Charge to meet minimum requirement of primary lines	25.00	125.00	1.25
b. Flat Rate Service			
(1) Flat Rate Service			
- Charge for working primary line	69.00	345.00	3.45
- Charge to meet minimum requirement of primary lines	69.00	345.00	3.45

2. Private Network Access	Monthly Rate
a. Arrangement of a tie line or interexchange channel - interwire center private line telephone line to select and be selected by lines of the Centrex system.	
(1) Rate for First two way 4-wire termination, Per CO Per Service Order	
- Centrex to Centrex, each	$ 92.75
- Centrex to CPE PBX, each	92.75
- Centrex to IEC, each	92.75
Additional two way 4-wire termination, Per CO Per Service Order	
- Each	92.75

APPENDIX A
SHEET 16 OF 20
PACIFIC BELL
RATES AND CHARGES

Centrex Service - continued
9.1
9.1.1
D. RATES AND CHARGES (cont'd)
5. Station-Controlled Features

	Installation Charge	Monthly Rate
1. Speed Calling		
Customer changeable, primary line equipped for individual		
- Each 6-10 numbers	$ 5.00	$ 1.50
Customer changeable, primary line equipped for groups		
- Each 30 numbers	5.00	1.70
- Each 50 numbers	5.00	1.85
- Each 70 numbers	5.00	2.00
v. Call Park		
- Each	5.00	.75

APPENDIX A
SHEET 17 OF 20
PACIFIC BELL
RATES AND CHARGES

Schedule Cal. P.U.C. No. A6.
Message Telecommunications Service

The following revisions are ordered:

6.2 STANDARD SERVICE OFFERINGS
6.2.1 TWO-POINT MESSAGE TELECOMMUNICATION SERVICE
A. GENERAL
4. RATES AND CHARGES
a. Method of Applying Rates

(12) Mileages and Corresponding Rates of Different Classes of Service

BASIC SCHEDULE	DAY RATE		
	Initial Period Station (Sent Paid)		
RATE MILEAGE	DIAL 1-MINUTE	COIN 3-MINUTES	EACH ADDITIONAL MINUTE ALL CLASSES OF SERVICE
0 - 8	$ 0.17	$ 0.30	$ 0.07
9 - 12	0.17	0.30	0.07
13 - 16	0.20	0.40	0.10
17 - 20	0.22	0.45	0.13
21 - 25	0.25	0.55	0.16
26 - 30	0.28	0.70	0.19
31 - 40	0.31	0.75	0.22
41 - 50	0.34	0.85	0.25
51 - 70	0.37	0.90	0.28
71+	0.40	1.00	0.31

APPENDIX A
SHEET 18 OF 20
PACIFIC BELL
RATES AND CHARGES

Message Telecommunications Service - continued

6.3 OPTIONAL CALLING PLANS
6.3.1 CALL BONUS-COMMUNITY PLANS
F. RATES AND CHARGES

Option 1 - Community Plan

Service Area Rate Group	Service Offerings Rate Mileage	MESSAGE RATE First Minute Day	MESSAGE RATE Add'l Minute Day
1	9 - 12	$ 0.119 *	$ 0.049 **
2	13 - 16	0.140 ***	0.070 ****
3	17 - 20	0.154	0.091
4	21 - 25	0.175	0.112
5	26 - 30	0.196	0.133
6	31 - 40	0.217	0.154

Option 2 - Community Circle Plan

Service Area Rate Group	MESSAGE RATE First Minute Day	MESSAGE RATE Add'l Minute Day
1	$ 0.119 *	$ 0.049 **
2	0.140 ***	0.070 ****
3	0.154	0.091
4	0.175	0.112
5	0.196	0.133
6	0.217	0.154

* $0.08 on ZUM routes
** $0.02 on ZUM routes
*** $0.10 on ZUM routes
**** $0.04 on ZUM routes

APPENDIX A
SHEET 19 OF 20
PACIFIC BELL
RATES AND CHARGES

Message Telecommunications Service - continued

6.3
6.3.2 OPTIONAL CALLING MEASURED SERVICE

E. RATES

Rate Group	Overtime Rate Per Minute Over Allowance
1	$ 0.07
2	0.10
3	0.13
4	0.16
5	0.19
6	0.22

APPENDIX A
SHEET 20 OF 20
PACIFIC BELL
RATES AND CHARGES

Schedules Cal. P.U.C. Nos. A3., A9., A10. and B3.
Private Line and Private Line-Like Services

The revisions set forth on Sheets 22 through 72 of 72 of Exhibit No. 330 are authorized except for Sheet 24 of 72 and as modified by the following:

Schedule Cal. P.U.C. No. B3.

3.2 CLASSIFICATION AND RATES
3.2.1 SERIES 1000 CHANNELS
B. REGULATIONS

1. Applicable to Types 1001, 1002, 1005 and 1006 channels for remote metering, supervisory control and miscellaneous signaling purposes.

   Types 1002, 1005 and 1006 channels

   Rates and charges apply only to those services in service as of the effective date of tariffs filed under the authority granted in this decision, and which continue to be furnished to the same customer at the same location.

2. Applicable to Types 1002, 1005 and 1006 channels for private line teletypewriter and morse services.

   Channels for teletypewriter and morse services apply only to those services in service as of the effective date of tariffs filed under the authority granted in this decision, and which continue to be furnished to the same customer at the same location

3. Applicable to Types 1001, 1002, 1005 and 1006 channels for Data Transmission.

   Types 1002, 1005 and 1006 channels for data transmission apply only to those services in service as the effective date of tariffs filed under the authority granted in this decision, and which continue to be furnished to the same customer at the same location.

Sheet 53 of 72 of Exhibit 330, Section 3.2.1C.16.b(2) should read "Intraexchange, Intradistrict Area".

Sheet 57 of 72 of Exhibit 330, Section 3.2.2C.9 delete the word "Centrex".

APPENDIX B
Page 1

Implementation of the California Intrastate High Cost Fund

A. 1988 Settlements Effects and HCF Filings

Each rural and small metropolitan exchange telephone company shall file an advice letter implementing the tariffs necessary to collect on a "flow-through" basis the settlement effects revenue impact specified for such company in the foregoing opinion. Such advice letter tariff filings shall become effective concurrently with implementation of the revised Pacific Bell rate design set forth in this decision.

Such advice letters shall calculate the impact of each company's net settlements effects upon its present level of local exchange revenues and shall additionally describe the rate design necessary to adjust present local exchange revenue levels to reflect the specified settlements effects impact. The company's average local exchange rates contained in any rate design proposed by such advice letter filings shall not exceed the target level of 150% of comparable California urban rates, a standard to be measured generally by a target R-1 flat rate of $8.35 monthly. Presently authorized rates shall not, however, be reduced to this target level by operation of this mechanism. Any proposals for an exception to this rule shall be addressed separately to the Commission. The 150% level of comparable California urban rates shall constitute a benchmark against which specific company rate designs are measured rather than a rigid requirement that each rate design element be set at 150% of the underlying urban rate.

Those companies with a revised local exchange revenue requirement (the sum of the present level of local exchange revenues and the net positive and negative settlements effects for such company herein specified) which cannot be met from the local exchange rate designs incorporating the 150% threshold shall be eligible to receive the balance of their revised local exchange revenue requirement from the HCF, and each such company's advice letter shall set forth calculations of its HCF funding requirements for the year 1988, adjusted for the partial year. Companies with revised local exchange revenue requirements which can be met from rate design adjustments contained in their advice letters shall not receive HCF funding during 1988.

B. Annual Settlements Effects and HCF Adjustments

In each succeeding year, each rural and small metropolitan company shall file with the Commission an advice letter incorporating the net settlements effects upon such company of regulatory changes ordered by the Commission and the Federal Communications Commission (FCC). These advice letter filings will include the previously authorized annual filings for interLATA SPF to SLU shifts set forth in D.85-06-115 as well as all other regulatory changes of industry-wide effect such as changes in levels of interstate high cost funding, interstate NTS assignment, other FCC-ordered changes in separations and accounting methodology and Commission-ordered changes such as rate changes affecting access charges, intraLATA toll or EAS settlements revenues, interLATA separations shifts and the effects of other Commissions decisions which increase or decrease settlements revenues or cost assignments.

Each company shall file an advice letter by October 1 of each year (commencing October 1, 1988) setting forth the net increase or decrease from these factors upon that portion of its revenue requirement which must be met from its local exchange rate design. The advice letter and supporting workpapers shall also set forth proposed revisions to the company's local exchange rate design to compensate for the net positive or negative settlements effects while maintaining the overall rate design within the 150% guidelines as most recently defined by Commission decision and further calculating any resultant increases or decreases in the company's HCF funding requirements. The advice letter shall be reviewed by the Commission Advisory and Compliance Division (CACD) and incorporated, as approved, in Commission resolutions to take effect by January 1 of the year following filing. The CACD staff shall coordinate the advice letter filing process each year with all local exchange companies through appropriate procedures.

C. HCF Funding and Administration

The HCF funding process shall be administered by Pacific Bell (Pacific), and the HCF shall function as a separate fund rather than as a pool. HCF funding shall be provided by a uniform incremental amount on the carrier common line charge (CCLC) of all local exchange company interLATA access tariffs. Concurrently with this decision and in each succeeding year, Pacific shall determine the total statewide HCF funding requirement based on the funding requirements identified in the advice letters described in (1) paragraph A for 1988 and (2) paragraph B for succeeding years, and shall coordinate the filing of appropriate advice letter modifications to all California exchange carrier access charge tariffs to generate the calculated level of HCF revenue requirement.

The HCF funding increment shall be adjusted each January 1 to implement the annual revisions to HCF funding requirements. The HCF access charge increment may also be adjusted not more often than quarterly during any year where revision is required to compensate for any overcollection or undercollection of the then-current Commission authorized fund revenue requirement, including adjustments caused by variation in actual and projected usage used in developing the HCF CCL increment and adjustments caused by any mid-year changes in the funding revenue requirement due to decisions in pending rate proceedings or any other decisions of the Commission affecting the HCF funding level. Any end-of-year HCF fund residual amount (positive or negative) shall be netted with the succeeding year's HCF prospective funding requirement.

HCF funding adjustments shall be coordinated by Pacific Bell in conjunction with other local exchange companies and the CACD staff. Each exchange carrier shall remit monthly to Pacific for the HCF that portion of the CCLCs collected from the HCF access charge increment, and Pacific shall make disbursements monthly from the fund to each recipient local exchange carrier. Pacific shall not separately account for any incremental administrative costs incurred by it in administering the HCF fund, but rather it shall treat such costs as additional expenses of administering the access charge pool.

D. Rate Proceedings and Funding Levels

HCF funding shall continue at 100% of the Commission authorized funding requirement for the years 1988 and 1989. The HCF support level for those local exchange companies which have not initiated a general rate proceeding, either under General Order 96-A or by a general rate case application, by December 31, 1990, shall be reduced during the year 1991, so that such a company shall receive only 80% of the amount of funds that would otherwise be paid to it from the HCF during 1991. The HCF funding level for those companies not initiating rate proceedings by December 31, 1991, shall be further reduced to 50% of the funding requirement during the year 1992, and HCF funding for those companies which have not initiated rate proceedings by December 31, 1992, shall

APPENDIX B
Page 5

terminate entirely in 1993. A company's initiation of a general rate proceeding prior to the end of 1990 shall freeze its funding level at 100% during the pendency of its rate proceeding. A company's initiation of a general rate proceeding during 1991 shall freeze its 80% funding level during the pendency of its rate proceeding, and a company's initiation of a rate proceeding during 1992 shall similarly freeze its funding at the 50% level pending its rate decision.

The issuance of a Commission decision or resolution in a general rate proceeding of an independent company will have the effect of a "fresh start" for that company under the HCF plan. The company's rate case decision will specify its new local exchange rate design and state whether the company is to receive HCF support as part of its newly adopted revenue requirement and rate design. In years following the decision in the general rate proceeding, the company will continue to file annual advice letters reflecting net incremental changes of the type described in paragraph B and corresponding adjustments in its local exchange rate design and HCF funding amounts.

(END OF APPENDIX B)

APPENDIX - C
SHEET 1 OF 1

PACIFIC BELL

SETTLEMENT REVENUE EFFECTS ON INDEPENDENT TELEPHONE COMPANIES (ICOs) **

($000)

INDEPENDENT COMPANIES	INTERLATA ACCESS	----INTRALATA---- MTS	TOLL PL	EAS	IX ZUM	SUBTOTAL	INTRALATA SPF to SLU	TOTAL
	(a)	(b)	(c)	(d)	(e)	(f)	(g)	(h)
1 CALAVERAS	($5)	($30)	$0	$3	$0	($31)	$63	$32
2 CAPAY	(1)	(7)	0	0	0	(8)	*	(8)
3 CAL-OREGON (with DORIS)	(8)	(21)	1	0	0	(27)	38	11
4 CAL PAC NATIONAL	(20)	(150)	3	1	0	(167)	139	(28)
5 CITIZENS	(150)	(680)	56	128	0	(646)	(99)	(745)
6 CONTINENTAL	(310)	(3,959)	158	43	0	(4,068)	(595)	(4,663)
7 DUCOR	(2)	(15)	0	0	0	(17)	22	5
8 EVANS (with LIVINGSTON)	(11)	(98)	5	5	0	(99)	*	(99)
9 FORESTHILL	(2)	(21)	0	0	0	(23)	25	2
10 GENERAL OF CAL	0	(33,777)	2,221	(2,659)	(6,839)	(41,054)	*	(41,054)
11 HAPPY VALLEY	(10)	(20)	0	25	0	(4)	37	33
12 HORNITOS	(3)	(25)	0	0	0	(28)	107	79
13 KERMAN	(5)	(21)	0	11	0	(14)	9	(5)
14 PINNACLES	(0)	(1)	0	0	0	(2)	5	3
15 PONDEROSA	(18)	(159)	6	0	0	(171)	83	(88)
16 ROSEVILLE	(56)	(378)	10	(118)	0	(542)	(352)	(894)
17 SIERRA (with MARIPOSA)	(25)	(110)	5	0	0	(130)	(17)	(147)
18 SISKIYOU	(10)	(60)	8	0	0	(62)	136	74
19 TUOLUMNE	(18)	(141)	0	3	0	(156)	210	54
20 VOLCANO	(18)	(56)	0	5	0	(69)	*	(69)
21 WEST COAST	0	(86)	1	0	0	(85)	*	(85)
22 TOTAL OF COLUMNS	($672)	($39,814)	$2,476	($2,553)	($6,839)	($47,401)	($189)	($47,590)

NOTES:

( ) - DENOTES A DECREASE IN ICO REVENUES (i.e. AN INCREASE IN RATES).

* - THESE UTILITIES HAVE ALREADY INCORPORATED BILLING SURCHARGES FOR THE SETTLEMENT EFFECTS OF INTRALATA SPF TO SLU.

** - INCLUDES EXPENSE SAVINGS.

APPENDIX D
SHEET 1 OF 6
SERVICE VOLUMES
FOR BASIC EXCHANGE SERVICES

	CALAVERAS	CAL-ORE:D&M	CAL-ORE:N&T	CAPAY VALLEY	CITIZENS	CONTEL	CP NATL.	DUCOR
LOCAL								
RESIDENCE								
1-PARTY--flat	775	382	710	338	28,627	149,064	7,257	455
--measured	---	---	---	---	3,381	23,039	243	---
2-PARTY--flat	304	see below	190	0	1,498	1,916	56	---
--measured	---	286	---	---	---	---	---	---
4-PARTY--flat	---	---	---	---	54	3,687	79	---
SUBURBAN--flat	0	---	---	---	2,456	---	479	---
FARMER LINE--flat	---	---	---	---	5	66	1	---
KEY--flat	---	---	---	---	11	48	45	---
--measured	---	---	---	---	---	26	---	---
MULTILINE--flat	---	---	---	---	---	87	---	---
--measured	---	---	---	---	---	30	---	---
BUSINESS								
1-PARTY--flat	102	96	167	43	3,772	15,690	964	72
--measured	---	---	---	---	1,562	4,100	340	---
2-PARTY--flat	7	see below	8	0	---	91	31	---
--measured	---	17	---	---	---	---	---	---
4-PARTY--flat	---	---	---	---	---	106	---	---
SEMI-PUBLIC COIN	1	4	0	4	94	604	27	3
SUBURBAN--flat	0	---	---	---	138	---	66	---
FARMER LINE--flat	---	---	---	---	8	22	0	---
KEY--flat	---	27	61	0	1,380	10,039	651	0
--measured	---	---	---	---	895	2,939	228	---
PBX--flat	7	0	0	2	385	2,475	44	0
--measured	---	---	---	---	241	623	68	---
MULTILINE--flat	---	---	---	---	---	666	---	---
--measured	---	---	---	---	---	180	---	---
FEX								
RESIDENCE								
1-PARTY--flat	---	---	---	---	105	433	8	---
--measured	---	---	---	---	889/64/39	407	---	---
2-PARTY--flat	---	---	---	---	---	1	---	---
4-PARTY--flat	---	---	---	---	---	85	---	---
SUBURBAN--flat	0	---	---	---	5	0	---	---
FARMER LINE--flat	---	---	---	---	---	12	---	---
BUSINESS								
1-PARTY--flat	---	---	---	---	47	371	8	1
--measured	---	---	---	---	145/33/35/66	51	---	---
--message	---	---	---	---	13	---	---	---
2-PARTY--flat	---	---	---	---	---	0	---	---
4-PARTY--flat	---	---	---	---	---	0	---	---
FARMER LINE--flat	---	---	---	---	---	0	---	---
KEY--flat	---	---	---	---	15	---	---	---
--measured	---	---	---	---	117/100/55	459	---	---
--message	---	---	---	---	11	---	---	---
PBX--flat	---	---	---	---	0	159	---	---
--measured	---	---	---	---	50/20/6	---	---	---
--message	---	---	---	---	3	---	---	---

APPENDIX D
SHEET 2 OF 6
SERVICE VOLUMES
FOR BASIC EXCHANGE SERVICES

	EVANS--LPW	EVANS--SA	FORESTHILL	GENERAL	HAPPY VALLEY	HORNITOS	KERMAN	PINNACLES
LOCAL								
RESIDENCE								
1-PARTY--flat	4,112	125	1,112	2,032,624	1,678	245	2,764	38
--measured	---	---	---	63,847	---	---	---	---
2-PARTY--flat	325	---	122	80	40	13	422	---
--measured	---	---	---	---	---	---	---	---
4-PARTY--flat	---	---	0	---	228	24	---	6
SUBURBAN--flat	---	---	---	925	65	39	---	54
FARMER LINE--flat	---	---	---	4	---	0	---	---
KEY--flat	---	---	---	---	---	---	---	---
--measured	---	---	---	---	---	---	---	---
MULTILINE--flat	---	---	---	---	---	---	---	---
--measured	---	---	---	---	---	---	---	---
BUSINESS								
1-PARTY--flat	559	30	212	542,054	234	64	502	39
--measured	---	---	---	362,498	---	---	---	---
2-PARTY--flat	23	---	0	---	3	---	17	---
--measured	---	---	---	---	---	---	---	---
4-PARTY--flat	---	---	---	---	1	---	---	---
SEMI-PUBLIC COIN	30	0	1	11,730	5	0	2	---
SUBURBAN--flat	---	---	---	50	0	2	---	9
FARMER LINE--flat	---	---	---	0	---	0	---	---
KEY--flat	---	---	0	---	---	---	---	0
--measured	---	---	---	---	---	---	---	---
PBX--flat	470	0	6	73,309	---	---	78	0
--measured	---	---	---	52,732	---	---	---	---
MULTILINE--flat	---	---	---	---	---	---	---	---
--measured	---	---	---	---	---	---	---	---
FEX								
RESIDENCE								
1-PARTY--flat	84	---	11	3,646	---	---	61	---
--measured	---	---	---	116	---	---	43	---
2-PARTY--flat	---	---	---	---	---	---	---	---
4-PARTY--flat	---	---	---	---	---	---	---	---
SUBURBAN--flat	---	---	---	0	---	---	0	---
FARMER LINE--flat	---	---	---	0	---	---	---	---
BUSINESS								
1-PARTY--flat	77	---	---	5,098	---	---	---	---
--measured	---	---	5	3,508	---	---	35	---
--message	---	---	---	---	---	---	---	---
2-PARTY--flat	---	---	---	---	---	---	---	---
4-PARTY--flat	---	---	---	---	---	---	---	---
FARMER LINE--flat	---	---	---	0	---	---	---	---
KEY--flat	---	---	---	---	---	---	---	---
--measured	---	---	---	---	---	---	---	---
--message	---	---	---	---	---	---	---	---
PBX--flat	---	---	---	8,601	---	---	---	---
--measured	---	---	---	6,205	---	---	---	---
--message	---	---	---	---	---	---	---	---

APPENDIX D
SHEET 3 OF 6
SERVICE VOLUMES
FOR BASIC EXCHANGE SERVICES

	PONDEROSA	ROSEVILLE	SIERRA	SISKIYOU	TUOLUMNE	VOLCANO	WEST COAST
LOCAL							
RESIDENCE							
1-PARTY--flat	2,065	38,965	4,767	1,800	2,062	5,514	6,112
--measured	---	3,090	---	---	1,009	---	---
2-PARTY--flat	2,163	153	2,051	---	---	---	60
--measured	---	---	---	---	---	---	---
4-PARTY--flat	---	85	1,637	705	---	---	193
SUBURBAN--flat	---	---	---	---	285	---	370
FARMER LINE--flat	---	---	---	---	---	---	---
KEY--flat	---	---	---	---	0	---	---
--measured	---	---	---	---	---	---	---
MULTILINE--flat	---	---	---	---	---	---	---
--measured	---	---	---	---	---	---	---
BUSINESS							
1-PARTY--flat	543	---	1,887	590	83	1,050	860
--measured	---	8,246	---	---	225	---	---
2-PARTY--flat	86	---	76	---	---	---	6
--measured	---	---	---	---	---	---	---
4-PARTY--flat	---	---	62	40	---	---	9
SEMI-PUBLIC COIN	10	138	1	12	8	10	32
SUBURBAN--flat	---	---	---	---	---	---	0
FARMER LINE--flat	---	---	---	---	---	---	---
KEY--flat	94	---	0	50	22	19	---
--measured	---	---	---	---	32	---	---
PBX--flat	56	---	46	42	0	---	129
--measured	---	659	---	---	0	---	496
MULTILINE--flat	---	---	---	---	---	---	---
--measured	---	---	---	---	---	---	---
FEX:							
RESIDENCE							
1-PARTY--flat	---	---	---	---	76	0	0
--measured	---	1,440	---	---	---	---	---
2-PARTY--flat	---	---	---	---	---	---	---
4-PARTY--flat	---	---	---	---	---	---	---
SUBURBAN--flat	72	---	---	---	---	1	---
FARMER LINE--flat	---	---	---	---	---	---	---
BUSINESS							
1-PARTY--flat	---	---	---	---	---	0	---
--measured	21	1,168	0	2	0	---	---
--message	---	---	---	---	---	---	0
2-PARTY--flat	---	---	---	---	---	---	---
4-PARTY--flat	---	---	---	---	---	---	---
FARMER LINE--flat	---	---	---	---	---	---	---
KEY--flat	---	---	---	---	---	---	---
--measured	---	---	---	---	---	---	---
--message	---	---	---	---	---	---	---
PBX--flat	---	---	---	---	---	---	---
--measured	---	144	---	0	---	---	---
--message	---	---	---	---	---	---	---

APPENDIX D
SHEET 4 OF 6
PRESENT RATES
FOR BASIC EXCHANGE SERVICES

	CALAVERAS	CAL-ORE:D&M	CAL-ORE:N&T	CAPAY VALLEY	CITIZENS	CONTEL	CP NATL.
LOCAL							
RESIDENCE							
1-PARTY--flat	$5.00	$12.95	$5.50	$10.00	$12.75	$13.50	$10.80
--measured	---	---	---	---	7.00	8.50	7.80
2-PARTY--flat	4.00	11.95	4.10	9.75	10.85	11.40	9.15
--measured	---	11.95	---	---	---	---	---
4-PARTY--flat	---	---	---	---	8.95	11.40	8.55
SUBURBAN--flat	4.00	---	---	---	11.75	---	9.70
FARMER LINE--flat	---	---	---	---	5.00	1.40	2.75
KEY--flat	---	---	---	---	12.75	23.15	10.80
--measured	---	---	---	---	---	8.50	---
MULTILINE--flat	---	---	---	---	---	23.15	---
--measured	---	---	---	---	---	8.50	---
BUSINESS							
1-PARTY--flat	$6.00	$19.75	$10.25	$21.50	$24.90	$36.10	$22.25
--measured	---	---	---	---	22.10	31.65	18.25
2-PARTY--flat	5.00	17.25	7.60	21.25	---	29.00	17.90
--measured	---	17.25	---	---	---	---	---
4-PARTY--flat	---	---	---	---	---	29.00	---
SEMI-PUBLIC COIN	1.50	19.75	10.25	23.55	29.60	36.10	27.80
SUBURBAN--flat	5.00	---	---	---	22.70	---	19.00
FARMER LINE--flat	---	---	---	---	7.50	1.85	4.50
KEY--flat	---	19.75	15.20	21.50	37.25	52.90	22.25
--measured	---	---	---	---	22.10	31.65	18.25
PBX--flat	9.00	29.65	15.20	32.25	37.25	52.90	33.45
--measured	---	---	---	---	22.10	31.65	18.25
MULTILINE--flat	---	---	---	---	---	52.90	---
--measured	---	---	---	---	---	31.65	---
PBX							
RESIDENCE							
1-PARTY--flat	---	---	---	---	10.00	4.05	8.30
--measured	---	---	---	---	5.00/14.00/34.00	4.05	---
2-PARTY--flat	---	---	---	---	---	4.05	---
4-PARTY--flat	---	---	---	---	---	3.50	---
SUBURBAN--flat	5.75	---	---	---	7.00	3.50	---
FARMER LINE--flat	---	---	---	---	---	9.75	---
BUSINESS							
1-PARTY--flat	---	---	---	---	22.00	45.75	16.70
--measured	---	---	---	---	6.00/17.00/41.00/4.00	45.75	---
--message	---	---	---	---	4.00	---	---
FARMER LINE--flat	---	---	---	---	---	17.00	---
KEY--flat	---	---	---	---	22.00	---	---
--measured	---	---	---	---	6.00/17.00/41.00	45.75	---
--message	---	---	---	---	4.00	---	---
PBX--flat	---	---	---	---	23.75	45.75	---
--measured	---	---	---	---	7.75/18.75/42.75	---	---
--message	---	---	---	---	5.75	---	---

NOTE: RATES SHOWN DO NOT REFLECT EAS INCREMENTS, SRA INCREMENTS AND BILLING SURCHARGES

APPENDIX D
SHEET 5 OF 6
PRESENT RATES
FOR BASIC EXCHANGE SERVICES

	DUCOR	EVANS--LPW	EVANS--SA	FORESTHILL	GENERAL	HAPPY VALLEY	HORNITOS	KERMAN
LOCAL								
RESIDENCE								
1-PARTY--flat	$13.50	$11.60	$19.60	$7.65	$9.75	$5.50	$7.00	$14.80
--measured	---	---	---	---	5.25	---	---	---
2-PARTY--flat	---	11.35	---	5.25	8.70	11.45	6.40	14.75
--measured	---	---	---	---	---	---	---	---
4-PARTY--flat	---	---	---	7.75	---	3.90	5.50	---
SUBURBAN--flat	---	---	---	---	8.70	4.65	6.00	---
FARMER LINE--flat	---	---	---	---	3.65	---	2.25	---
KEY--flat	---	---	---	---	---	---	---	---
--measured	---	---	---	---	---	---	---	---
MULTILINE--flat	---	---	---	---	---	---	---	---
--measured	---	---	---	---	---	---	---	---
BUSINESS								
1-PARTY--flat	$20.75	$22.30	$33.30	$12.55	$21.70	$8.75	$10.00	$26.50
--measured	---	---	---	---	9.10	---	---	---
2-PARTY--flat	---	21.80	---	23.60	---	7.00	---	25.35
--measured	---	---	---	---	---	---	---	---
4-PARTY--flat	---	---	---	---	---	29.15	---	---
SEMI-PUBLIC COIN	28.50	25.00	25.00	12.55	26.45	1.25	5.00	26.50
SUBURBAN--flat	---	---	---	---	18.45	6.50	7.50	---
FARMER LINE--flat	---	---	---	---	7.25	---	2.25	---
KEY--flat	20.75	---	---	12.55	---	---	---	---
--measured	---	---	---	---	---	---	---	---
PBX--flat	31.15	30.00	30.00	18.85	32.70	---	---	26.50
--measured	---	---	---	---	9.10	---	---	---
MULTILINE--flat	---	---	---	---	---	---	---	---
--measured	---	---	---	---	---	---	---	---
FEX								
RESIDENCE								
1-PARTY--flat	---	11.00	---	8.00	5.00	---	---	14.00
--measured	---	---	---	---	5.00	---	---	14.00
2-PARTY--flat	---	---	---	---	---	---	---	---
4-PARTY--flat	---	---	---	---	---	---	---	---
SUBURBAN--flat	---	---	---	---	4.00	---	---	10.00
FARMER LINE--flat	---	---	---	---	4.00	---	---	---
BUSINESS								
1-PARTY--flat	20.00	16.35	---	10.00	31.55	---	---	---
--measured	---	---	---	---	31.55	---	---	18.50
--message	---	---	---	---	---	---	---	---
FARMER LINE--flat	---	---	---	---	7.50	---	---	---
KEY--flat	---	---	---	---	---	---	---	---
--measured	---	---	---	---	---	---	---	---
--message	---	---	---	---	---	---	---	---
PBX--flat	---	---	---	---	31.55	---	---	---
--measured	---	---	---	---	31.55	---	---	---
--message	---	---	---	---	---	---	---	---

NOTE: RATES SHOWN DO NOT REFLECT EAS INCREMENTS, SRA INCREMENTS AND BILLING SURCHARGES

APPENDIX D
SHEET 6 OF 6
PRESENT RATES
FOR BASIC EXCHANGE SERVICES

	PINNACLES	PONDEROSA	ROSEVILLE	SIERRA	SISKIYOU	TUOLUMNE	VOLCANO	WEST COAST
LOCAL								
RESIDENCE								
1-PARTY--flat	$10.70	$17.85	$11.20	$9.75	$7.60	$13.20	$7.55	$8.55
--measured	---	---	7.20	---	---	8.95	---	---
2-PARTY--flat	---	13.75	8.85	8.25	---	---	---	6.85
--measured	---	---	---	---	---	---	---	---
4-PARTY--flat	10.70	---	7.45	7.25	7.20	---	---	5.50
SUBURBAN--flat	10.70	---	---	---	---	13.10	---	6.30
FARMER LINE--flat	---	---	---	---	---	---	---	---
KEY--flat	---	---	---	---	---	13.20	---	---
--measured	---	---	---	---	---	---	---	---
MULTILINE--flat	---	---	---	---	---	---	---	---
--measured	---	---	---	---	---	---	---	---
BUSINESS								
1-PARTY--flat	$20.00	$33.90	---	$16.50	$9.75	$26.10	$12.85	$17.05
--measured	---	---	15.00	---	---	22.10	---	---
2-PARTY--flat	---	27.25	---	15.75	---	---	---	13.70
--measured	---	---	---	---	---	---	---	---
4-PARTY--flat	---	---	---	10.75	9.25	---	---	11.95
SEMI-PUBLIC COIN	---	33.00	21.90	23.50	17.90	31.75	13.00	17.10
SUBURBAN--flat	20.00	---	---	---	---	---	---	11.95
FARMER LINE--flat	---	---	---	---	---	---	---	---
KEY--flat	20.00	33.90	---	16.50	10.15	26.10	12.85	---
--measured	---	---	---	---	---	22.10	---	---
PBX--flat	30.00	45.30	---	16.50	14.95	41.35	---	34.20/25.55
--measured	---	---	15.00	---	---	22.10	---	---
MULTILINE--flat	---	---	---	---	---	---	---	---
--measured	---	---	---	---	---	---	---	---
FEX								
RESIDENCE								
1-PARTY--flat	---	---	---	---	---	9.30	2.50	7.30
--measured	---	---	14.40	---	---	---	---	---
2-PARTY--flat	---	---	---	---	---	---	---	---
4-PARTY--flat	---	---	---	---	---	---	---	---
SUBURBAN--flat	---	16.11	---	---	---	---	2.00	---
FARMER LINE--flat	---	---	---	---	---	---	---	---
BUSINESS								
1-PARTY--flat	---	---	---	---	---	---	5.00	---
--measured	---	30.95	30.00	10.45	9.75	18.60	---	---
--message	---	---	---	---	---	---	---	22.15
FARMER LINE--flat	---	---	---	---	---	---	---	---
KEY--flat	---	---	---	---	---	---	---	---
--measured	---	---	---	---	---	---	---	---
--message	---	---	---	---	---	---	---	---
PBX--flat	---	---	---	---	---	---	---	---
--measured	---	---	30.00	---	14.95	---	---	---
--message	---	---	---	---	---	---	---	---

NOTE: RATES SHOWN DO NOT REFLECT EAS INCREMENTS, SRA INCREMENTS AND BILLING SURCHARGES

APPENDIX E
SHEET 1 of 1
PACIFIC BELL
BILLING BASES AND ADJUSTMENTS TO BILLING
BASES FOR INDEPENDENT TELEPHONE COMPANIES

---------------------------- I N T R A L A T A ----------------------------

COMPANIES	1986 BILLING BASE	NTS EFFECTS	TOLL PRIVATE LINE EFFECTS	ZUM EFFECTS	ADJUSTED 1986 BILLING BASE (excl. EXCHANGE)
	(a)	(b)	(c)	(d)	(e) = (a+b+c+d)
1. CALAVERAS	357,195	(10,789)	0	0	346,406
2. CAL-OREGON	514,680	(9,670)	0	0	505,010
3. CP NATIONAL	3,554,286	(93,070)	0	0	3,461,216
4. CAPAY VALLEY	143,000	(4,690)	0	0	138,310
5. CITIZENS	21,291,697	(243,126)	536	(45,751)	21,003,356
6. CONTINENTAL	124,115,952	(2,186,627)	44,257	0	121,973,582
7. DUCOR	195,435	(4,210)	0	0	191,225
8. EVANS	2,484,551	(47,737)	0	0	2,436,814
9. FORESTHILL	645,615	(18,892)	0	0	626,723
10. GENERAL	1,596,898,000	(25,978,735)	1,158,613	(12,157,064)	1,559,920,814
11. HAPPY VALLEY	496,882	(10,155)	0	0	486,727
12. HORNITOS	90,685	(2,907)	0	0	87,778
13. KERMAN	1,600,859	(19,461)	0	0	1,581,398
14. PINNACLES	69,471	(1,356)	0	0	68,115
15. PONDEROSA	2,328,767	(51,842)	0	0	2,276,925
16. ROSEVILLE	21,251,926	(226,987)	0	(347,562)	20,677,377
17. SIERRA	3,430,100	(75,369)	0	0	3,354,731
18. SISKIYOU	976,800	(25,703)	413	0	951,510
19. TUOLUMNE	1,451,820	(38,111)	0	0	1,413,709
20. VOLCANO	1,500,225	(27,450)	0	0	1,472,775
21. WEST COAST	2,790,071	(57,112)	479	0	2,733,438
22. Total	1,786,188,017	(29,133,999)	1,204,298	(12,550,378)	1,745,707,938

APPENDIX F
Sheet 1 of 2
PACIFIC BELL
DEVELOPMENT OF CUSTOMER BILLING SURCHARGES
DUE TO CHANGES TO CUSTOMER BILLING BASE
($000)

LINE	DESCRIPTION	INTERLATA ACCESS	INTRALATA TOLL	INTRALATA EXCHANGE	TOTAL INTRALATA	TOTAL INTRASTATE
1	1986 Billing Base Adopted in D.86-03-049	$1,160,324	$2,089,830	$2,746,416	$4,836,246	$5,996,570
2	1986 Billing Base Adopted in D.86-03-049 & Adjusted by Advice Letter (AL) 15190	1,080,724	2,089,830	2,746,416	4,836,246	5,916,970
3	Change in 1986 Billing Base due to Rate Design	(11,000)	(73,721)	71,743	(1,978)	(12,978)
4	Adjusted 1986 Billing Base (L2+L3)	1,069,724	2,016,109	2,818,159	4,834,268	5,903,992
	Applicable Rev. Req./Surcharge Yields:					
5	D.86-03-049 (Phase I)	(27,235)	51,913	68,224	120,137	$92,902
6	AL 15190 (InterLATA Direct Assign. of WATS)	--	34,397	45,203	79,600	79,600
7	D.87-12-067 (Phase II R.O. excl. IntraLATA SPF-SLU and Direct Assignment of WATS)	(30,478)	(58,954)	(77,482)	(136,436)	(166,914)
8	Subtotal (L5+L6+L7)	(57,713)	27,356	35,945	63,301	5,588
9	Present Surcharge (L8/L2)	-5.340%	1.309%	1.309%		
10	Adopted Surcharge (L8/L4)	-5.395%	1.357%	1.275%		
11	1987 Billing Base Adopted in 1987 Attrition	1,304,501	2,293,718	3,123,066	5,416,784	6,721,285
12	1987 Billing Base Adopted in 1987 Attrition and Adjusted by AL 15325	1,207,766	2,293,718	3,123,066	5,416,784	6,624,550
13	Adjusted 1987 Billing Base ((L12/L2)*L4)	1,195,473	2,212,805	3,204,648	5,417,453	6,612,926
	Applicable Rev. Req./Surcharge Yields:					
14	AL 15215B (1987 Attrition)	(37,078)	(65,195)	(88,768)	(153,963)	(191,041)
15	AL 15253	--	(25)	(34)	(59)	(59)
16	AL 15325 (1988 InterLATA SPF-SLU)	--	41,455	56,445	97,900	97,900
17	AL 15356 (86&88 IntraLATA SPF-SLU & DA of WATS)	--	--	(14,635)*	(14,635)	(14,635)
17a	AL 15377C (1986 Tax Reform Act or TRA)	(18,969)	(36,025)	(49,051)	(85,076)	(104,045)
18	Subtotal (L14+L15+L16+L17+17a)	(56,047)	(59,790)	(96,043)	(155,833)	(211,880)
19	Present Surcharge (L18/L12) **	-6.068%	-3.833%	-4.301%		
20	Adopted Surcharge (L18/L13) **	-6.157%	-3.973%	-4.192%		
21	TOTAL PRESENT SURCHARGE (L9+L19) ***	-11.407%	-2.520%	-2.989%		
22	TOTAL ADOPTED SURCHARGE (L10+L20)	-11.552%	-2.616%	-2.916%		

* Full year settlements effect is adjusted for the period from 1/1/88 to 4/10/88.
** Present surcharge reflects full year 1986 TRA effect applied to the period from 6/10/88 to 12/31/88.
Adopted surcharge reflects full year 1986 TRA effect reduced by the amount refunded from 6/10/88 to 9/6/88.
Surcharge for access reflects adjustments due to reduction in access billings resulted from AL 15325.
*** Discrepancies are due to rounding.

APPENDIX F

Sheet 2 of 2

PACIFIC BELL

DEVELOPMENT OF CUSTOMER BILLING SURCHARGES

DUE TO CHANGES TO CUSTOMER BILLING BASE

($000)

LINE	DESCRIPTION	INTERLATA ACCESS	INTRALATA TOLL	INTRALATA EXCHANGE	TOTAL INTRALATA	TOTAL INTRASTATE
1	1986 Billing Base Adopted in D.86-03-049	$1,160,324	$2,089,830	$2,746,416	$4,836,246	$5,996,570
2	1986 Billing Base Adopted in D.86-03-049 & Adjusted by Advice Letter (AL) 15190	1,080,724	2,089,830	2,746,416	4,836,246	5,916,970
3	Change in 1986 Billing Base due to Rate Design	(11,000)	(73,721)	71,743	(1,978)	(12,978)
4	Adjusted 1986 Billing Base (L2+L3)	1,069,724	2,016,109	2,818,159	4,834,268	5,903,992
	Applicable Rev. Req./Surcharge Yields:					
5	D.86-03-049 (Phase I)	(27,235)	51,913	68,224	120,137	$92,902
6	AL 15190 (InterLATA Direct Assign. of WATS)	--	34,397	45,203	79,600	79,600
7	D.87-12-067 (Phase II R.O. excl. IntraLATA SPF-SLU and Direct Assign. of WATS and One-time Rev. Req. Reduction of $108.1M)	(10,751)	(20,796)	(27,331)	(48,127)	(58,878)
8	Subtotal (L5+L6+L7)	(37,986)	65,514	86,096	151,610	113,624
9	Present Surcharge (L8/L2)	-3.515%	3.135%	3.135%		
10	Adopted Surcharge (L8/L4)	-3.551%	3.250%	3.055%		
11	1987 Billing Base Adopted in 1987 Attrition	1,304,501	2,293,718	3,123,066	5,416,784	6,721,285
12	1987 Billing Base Adopted in 1987 Attrition and Adjusted by AL 15325	1,207,766	2,293,718	3,123,066	5,416,784	6,624,550
13	Adjusted 1987 Billing Base ((L12/L2)*L4)	1,195,473	2,212,805	3,204,648	5,417,453	6,612,926
	Applicable Rev. Req./Surcharge Yields:					
14	AL 15215B (1987 Attrition)	(37,078)	(65,195)	(88,768)	(153,963)	(191,041)
15	AL 15253	--	(25)	(34)	(59)	(59)
16	AL 15325 (1988 InterLATA SPF-SLU)	--	41,455	56,445	97,900	97,900
17	AL 15336 (86&88 IntraLATA SPF-SLU & DA of WATS)	--	--	(19,198)*	(19,198)	(19,198)
18	Subtotal (L14+L15+L16+L17)	(37,078)	(23,765)	(51,555)	(75,320)	(112,398)
19	Present Surcharge (L18/L12) **	-3.272%	-1.036%	-1.651%		
20	Adopted Surcharge (L18/L13) **	-3.331%	-1.074%	-1.609%		
21	TOTAL PRESENT SURCHARGE (L9+L19) ***	-6.785%	2.102%	1.487%		
22	TOTAL ADOPTED SURCHARGE (L10+L20)	-6.882%	2.176%	1.446%		

* Full year settlements effects.

** Surcharge for access reflects adjustments due to reduction in access billings resulted from AL 15325.

*** Discrepancies are due to rounding.

ALJ/AC/jt

Decision ____________

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 intrastate 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)
And Related Matters.	I.85-03-078 (Filed March 20, 1985) OII 84 (Filed December 2, 1980) C.86-11-028 (Filed November 17, 1986)

(See Decisions 85-08-047, 86-01-026, and 87-12-067 for appearances.)

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OPINION ADOPTING A RATE DESIGN FOR PACIFIC BELL

I. Summary of Decision

In this rate design portion of Phase II of Pacific Bell's (Pacific) general rate case it was our initial intent to reflect the revenue requirement decrease of $86.435 million which we adopted in Decision (D.) 87-12-067 as modified by D.88-02-046, and D.88-03-064 by eliminating most positive or negative surcharges and adjusting rates to incorporate those amounts. Instead, this decision finds that because this proceeding is limited to 1986 projected volumes and cannot distribute that portion of Pacific's surcharges which became effective after 1986, following such a plan would likely result in rate increases now which would be followed by rate decreases in a short while when we conduct the supplementary rate design hearings in the present docket following the Phase I hearings in Order Instituting Investigation (I.) 87-11-033. Therefore, this decision retains the presently effective surcharges, with some modification, and only redistributes revenues presently collected in rates, including a shift out of toll rates and toll related services of about $71 million which was authorized in the Assigned Commissioner's Ruling in this proceeding dated April 1, 1986, and an industry shift of $11 million from Special Access revenues to nonaccess revenues which we authorized in D.87-08-048, with implementation put over to the present proceeding.

This rate redesign recognizes the impact of recent changes in the telephone marketplace, chief among which is the need for substantial reductions in rates for toll service, in order to position Pacific to better deal with potential direct intraLATA toll competition as well as indirect competition. Thus, for example, we adopt the proposal of the Division of Ratepayer Advocates (DRA) for a shift from the present subscriber plant

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factor (SPF) means of allocating nontraffic sensitive costs of the local network to toll to the subscriber line usage (SLU) allocation factor.

Based on detailed and voluminous service cost studies we conclude that private line rates fall far below costs. We therefore increase Pacific's private line service recurring rates by up to 50%, and its nonrecurring private line charges by up to 100% of present levels, resulting in an overall private line revenue increase of $67.020 million. This increase is only for the test year. We do not grant the three-year incremental rate increases Pacific proposes, nor do we adopt any proposal for deaveraged local loop rate schedules or for separate alarm transport tariffs. We also decline to adopt the disaggregated installation charges and other changes for secretarial lines proposed by Telephone Answering Services of California, Inc. (TASC).

While we continue to set basic residence and business rates residually for now--partly in recognition of the fact that Pacific's cost data, even if it is accurate, does not necessarily reflect the <u>most efficient</u> costs of service,--we do adopt increases which have the purpose of moving these rates, except for Lifeline rates, gradually toward costs. Thus, we increase recurring basic residence and business rates by approximately 1%, and service connection charges by the same percentage. We make no change in the usage rates for local service. We reject Pacific's 130 Call Allowance Plan and retain the present service offerings, but we expand the Lifeline options as Pacific proposes. The overall effect of these basic exchange changes is a revenue increase of $10.476 million which includes the effects of increasing FEX access rates by the same amounts as basic residence and business service rates.

Recognizing that a PBX line equipped with Direct Inward Dialing (DID) competes with Centrex, which is designed to provide a

factor (SPF) means of allocating nontraffic sensitive costs of the local network to toll to the subscriber line usage (SLU) allocation factor.

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contribution over cost, this decision adopts an increase of 48.48% for measured rate trunk access and 33.53% for flat rate trunk access, contingent on Pacific developing a set of unambiguous design parameters describing when a designed circuit (PBX line equipped with DID) rather than a regular business line is required from the serving central office. These changes increase PBX revenues by $20.554 million which includes the effects of increasing FEX trunk rates by the same amount as PBX trunk rates.

We also authorize a number of changes in Centrex service including the unbundling of the primary station line charge, an increase in the Centrex trunking charge from $.85 to $1.25, the addition of new optional service features, and a simplification of charges for optional services. Together the adopted changes in Centrex service result in a revenue decrease of $0.912 million. At the same time, we authorize a separate trunk sensitive circuit termination rate element for DID which treats all blocks of 100 station numbers the same, rather than charging more for the first 200, and results in lower cost to the customer than present rates until the customer reaches about 600 station numbers. This design benefits telephone answering service (TAS) users, while slightly increasing the DID rate component for very large users. This change results in an overall revenue decrease of $1.870 million.

The decision does not change coin telephone rates, but does increase access rates and service connection charges for semi-public coin service to approach costs, and does increase the access and installation rates for coin operated public telephone (COPT) service by the same percentages as basic service. These new rates will increase revenues for semi-public service by $9.005 million, and revenues for COPT by $.019 million.

We leave the rate for nonpublished service at $.30 per month and adopt Pacific's proposal for a new service, Directory Assistance Listing, which permits the customer to be unlisted in the telephone directory, but makes the customer's name, address, and telephone number available in the directory assistance data base. The adopted rate for this service is $.15 per month. Rates for Touchtone service remain unchanged for lack of any evidence to justify other action, but Pacific is directed to provide cost and revenue data about this service in the supplementary rate design proceedings. The charge for Verification Interrupt remains unchanged as do the rates for Remote Call Forwarding.

The rates for Message Toll Service (MTS) and related optional calling plans are modified by this decision to produce a revenue decrease of $68.166 million. The modifications include a reduction in the number of MTS rate bands and a slight reduction in usage rates for MTS "additional minutes of use." The optional calling plans are all retained in their present forms, but their revenues are affected by the changes in MTS usage rates. WATS and 800 Service will remain unchanged, but changes in other rates will produce a slight reduction, $0.427 million, in revenues from WATS.

Turning to ZUM, we adopt Pacific's proposal to expand ZUM on the periphery of the San Francisco-East Bay Extended Area, resulting in a revenue reduction of $6.252 million. We do not adopt the proposals to change the ZUM Zones 2 and 3 boundary definitions, but we adopt rate reductions for usage rates which are analogous to the usage rates we adopt for MTS. The result is a revenue reduction of $30.531 million. The proposal of TURN for a flat rate metropolitan plan and the elimination of ZUM and optional toll calling plans is rejected, as is General Telephone's request for ZUM expansion. However, we do authorize the parties to study the feasibility of General's ZUM expansion proposal.

This decision denies Pacific's request to restrict Foreign Exchange (FEX) service to present customers, adopts an FEX rate design disaggregated into an access component which mirrors recurring basic exchange rates and a separate FEX increment component set at the rate presently attributable to this increment. Nonrecurring charges for FEX are increased by 100%. We also authorize the parties to study meet-point bill and keep billing of FEX services and to present this Commission, after staff review and approval, with a proposal for its implementation. The revenue impact of these authorized nonrecurring FEX changes is an increase of $12.751 million.

We authorize the Independent Telephone Companies (ITCs) which concur with Pacific's access services tariff, 175-T, to recover any revenue shortfall caused by the adopted rates and charges by a uniform increase capped at 100% in their basic exchange rates and FEX services, followed by a bill and keep surcharge on intraLATA services where necessary. Since General and West Coast Telephone Companies do not concur in Pacific's access rates, we authorize these companies to recover any revenue shortfall by a bill and keep billing surcharge on intraLATA services. The net settlement effects for each ITC of the adopted rate design and the intraLATA SPF to SLU phase-down in compliance with ordering paragraph 15A of D.87-12-067, (which have been placed into a memorandum account as required by D.88-03-064), are shown in Appendix C. Appendix D sets forth the adopted 1986 customer and FEX service volumes for each ITC. Appendix E shows each ITC's adopted 1986 customer billing base and the effects on its billing base of the adopted toll and toll private line rates and the adopted ZUM rates. We deny the motion of customers of Citizens Utility Company that we find that notice of changes in rates of the ITCs occasioned by this Pacific rate design did not meet statutory requirements. We adopt the intraLATA High Cost Fund proposed by DRA and the ITCs.

Additionally, this decision revises Pacific's present billing surcharges to reflect the change in customer billing base due to the adopted rate design. The present billing surcharge is revised from 0.276% to 0.283% for intraLATA toll and toll-related services; from -0.193% to -0.191% for local exchange service; and from -8.611% to -8.722% for access service. Should we not order any additional revenue requirement changes before January 1, 1989, the surcharges applicable from that day forward shall be 2.176% for intraLATA toll and toll-related services, 1.446% for local exchange service, and -6.879% for access service. These authorized billing surcharges are set forth in Appendix A. The development of these revised billing surcharges is contained in Appendix F.

The following Table 1 is a summary of the changes in 1986 customer billings and revenues generated by the adopted rate design. The changes in revenues reflect the settlements factors resulting from the Phase 2 Results of Operations decision, D.87-12-067 as modified.

Table 1

Summary of Changes in 1986 Customer Billings And Revenues at Adopted Rates and Charges
($000)

	Item	PACIFIC BELL Change in Billings	PACIFIC BELL Change in Revenues
1.	PBX (Incl. FEX recurring)	$21,415	$20,554
2.	Remote Call Forwarding	0	0
3.	Centrex	(950)	(912)
4.	Direct Inward Dialing	(1,948)	(1,870)
5.	Directory access listing	(118)	(113)
6.	Foreign area serv. - nonrecurring	13,285	12,751
7.	Local usage - Lifeline	(376)	(361)
8.	MTS	(61,031)	(56,478)
9.	Call Bonus	(1,735)	(1,150)
10.	Operatory - Busy verify	0	0
11.	Optional calling plans	(11,314)	(10,538)
12.	Private Line (incl. exp. savings)	73,647	67,020
13.	Semi-public (incl exp. savings)	9,671	9,005
14.	WATS	(660)	(527)
15.	800	0	0
16.	ZUM	(32,474)	(30,531)
17.	ZUM Expansion - LCAR	(12,671)	(6,252)
18.	Implementation	(1,130)	(800)
19.	Decrease in Access Charges	(10,615)	(10,293)
20.	Subtotal, Lines 1 - 19	(17,004)	(10,495)
21.	COPT	20	19
22.	Service Connection	1,194	1,146
23.	Basic Exchange Svc. (incl recur. FEX)	9,721	9,330
24.	Subtotal (lines 21 - 23)	10,935	10,495
25.	TOTAL	(6,069)	0

(Negative Amount)

Finally, we address the quality of Pacific's private line service and find it to be in compliance with the requirements of General Order (GO) 152.

II. Introduction

A. Procedural and Policy Considerations

1. Procedural History of this Matter

It is our purpose in the present decision to adopt a new rate design for Pacific Bell, but the scope of the revenues that should be included in this rate design is somewhat problematic.

On June 25, 1986 Pacific filed its final rate design testimony in the present matter. It purports to make no change in total annual revenues, except to redesign rates in a way which will allow the elimination of the 2.48% billing surcharge in effect at the time by incorporating the net revenues derived from that surcharge into rates. The rate design proposed by DRA proposes to spread the same surcharge, but also suggests alternatives should we wish to consider later surcharges. Additionally, both these rate designs attempt to comply with the Assigned Commissioner's Ruling issued on April 1, 1986 which is discussed below.

From our issuance of D.85-03-042 in March of 1985 to our issuance of D.87-12-067 as modified by D.88-02-046 in February, 1988 and D.88-03-064 in March, 1988 we have imposed a number of positive and negative surcharges on Pacific's rates to adjust for reductions we ordered in access revenues and for attrition or rate case adjustments. Since the time of Pacific's filing this intraLATA portion of Pacific's billing surcharge was increased to 4.13% effective January 1, 1987 (see Resolution T-11091 (December 22, 1986)), and was then decreased to 1.287% effective May 1, 1987 (see Resolution No. T-12007 (March 25, 1987)). It was slightly decreased again by D.87-04-024, effective June 7, 1987 and was again decreased to -0.193% effective January 1, 1988 as a result of D.87-12-067. Finally, by Advice Letter 15356 filed in compliance with Ordering Paragraph 15A of D.87-12-067 as modified by D.88-02-046 and D.88-03-064, different surcharges were established for intraLATA toll and for intraLATA exchange services effective April 10, 1988. The latter remains at -0.193%, while the former is 0.276%.

Now that we have the rate design proposals and comments of the various parties before us for this general rate case, two problems have become clear. The first is that we are necessarily confined to the 1986 estimated billing base, which means that any increases will be spread under the assumption of a lower volume than likely exists today, thereby magnifying the impact of rate increases on ratepayers. The second is that if various components of the surcharge are spread in rates today, a rate increase followed quickly by a rate decrease would likely result. The surcharge in place through 1986 plus the direct assignment of WATS closed end costs as of January 1, 1987, and the 1988 interLATA SPF to SLU phase-down which had been authorized prior to 1986 all require a rate increase. They are currently being offset by the revenue requirement reductions which were adopted subsequent to 1986. But since those reductions result from proceedings which assume a post-1986 billing base, the reductions could not be used to offset the revenue increases if those increases are spread in rates.

In Order Instituting Investigation (OII) In the Matter of Alternative Regulatory Frameworks for Local Exchange Carriers, issued November 25, 1987 we stated that Pacific should accumulate revenue requirement changes occurring subsequent to its general rate case Phase 2 decision (D.87-12-067, as modified) in a memorandum account. Further, we noted that "[t]he net effect of several upcoming revenue requirement changes...will probably be a reduction in total revenue requirement" adding that "following our Phase I flexibility hearings, we will hold limited supplementary rate design hearings to determine how to reflect these revenue requirement changes in rates." We further added, "[w]e see these supplementary rate design hearings as providing an opportunity to move rates downward for services currently priced above cost without necessarily having to adjust rates upward for basic services that are priced below cost."

Because of the unnecessary rate fluctuation which we now recognize as the likely outcome of spreading some, but not all, of the billing surcharges which have already been adopted, we believe it is preferable to address the appropriate spreading of all billing surcharges ordered for services other than access since D.85-03-042, along with the surcharges and other rate changes which will be addressed following the Phase I flexibility hearings. To assure the most accurate rate design possible in disposing of these surcharges, we will direct Pacific and the other parties, including the ITCs, to file testimony using 1988 and 1989 projected billing base data for use in the supplementary rate design phase of the present proceeding. Until then we will keep in place the existing billing surcharge/surcredit.

The result of our adopting this position is that rather than considering how to spread about $118 million which includes the surcharge revenues plus revenue requirements which we have ordered to be adjusted or shifted among Pacific's service offerings, this decision will address only the spreading of revenue from the latter source, which comes to about $82 million.

2. The Regulatory Context of the Rate Design

It is our intent that this decision continue an evolution in rate design reflected in various Commission decisions since the AT&T divestiture which we cite above. More significantly, with this rate design we establish a baseline for moving ahead with any further changes which may be made in conjunction with our investigation into alternate regulatory frameworks in I.87-11-033. Before proceeding with the discussion of specific issues therefore, we briefly review some fundamental principles which are and will continue to be important considerations for this Commission.

For a variety of economic efficiency reasons, we are guided by the same desire voiced by most of the parties to this revenue requirement reductions which were adopted subsequent to 1986. But since those reductions result from proceedings which assume a post-1986 billing base, the reductions could not be used to offset the revenue increases if those increases are spread in rates.

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proceeding, to move rates over time toward economic costs. Among other benefits, moving toward economic pricing promises to improve efficiency in both the provision and consumption of telecommunications services. Economic pricing can help promote uses for which value exceeds the "true" cost of providing service. It can also discourage the allocation of utility resources toward uneconomic uses and prevent a misallocation of society's resources in facilities which unnecessarily duplicate those of the utility.

The long-run sustainability of large contribution flows from usage rates to support low basic exchange access rates is also a central concern--not only in this proceeding but in the regulatory framework OII as well. As we have previously noted, short-run competitive threats do not appear to be nearly as catastrophic as sometimes has been suggested. We have the time to plan an organized, deliberate course to implement "rationalized" rates based much more closely on economic costs. In this instance, the inertia and the caution of business users in making substantial investments in private networks weighs in the Commission's favor.

As a specific target of our continuing rate design policy we hope to minimize the potential for uneconomic bypass of the public telecommunications network. In D.85-06-115 we established an initial series of steps aimed particularly to achieve this end by ordering the interLATA SPF to SLU transition. In doing this we effectively cut in half the burden of non-traffic sensitive costs borne by interexchange carriers which pay access charges, shifting it to intraLATA services. In our recent decision on Pacific's revenue requirement, D.87-12-067, we indicated that the SPF to SLU methodology for allocating non-traffic sensitive costs would be applied to intraLATA toll service, thus reducing the costs of intraLATA usage as well. We intend to continue the clear signaling of our long-run direction, as manifested by our SPF to SLU decisions, D.85-06-115 and D.87-12-067, to forestall uneconomic bypass decisions.

Continuing market, technological and federal regulatory changes may very well accelerate the bypass threat in the future. This Commission must be prepared with a consistent and continuing long-term strategy for rate design so that it can phase in significant changes gradually and so that the process can be implemented in the most effective and least disruptive way possible should an accelerated threat materialize.

In large part, these adjustments to rates will lower the price of using the public network, while raising the price of obtaining access to the network to levels which more closely reflect the costs of service.

Our course toward economic pricing has been a moderate one and it is the intent of this decision to continue to balance efficiency benefits with the equally important goal of maintaining affordable basic service for all Californians. We must proceed cautiously because the evidence of marginal costs, which would greatly assist us in basing rates on economic costs, is incomplete. Given our commitment to economic usage pricing, we must guard against overreacting to the need for pricing adjustments by shifting too high a percentage of fixed costs to basic service rates. Such a tendency might result from the fact that basic residential and business service charges and rates are priced residually after other services have been priced to recover as much of the utility's fixed costs as feasible.

As the utility responds to more concrete evidence of the bypass options of large users and to competitive forces, we should resist the abuse of residual pricing to pursue economic efficiency objectives that are still in the formative stages of development. At this point the shifting of fixed costs from usage to basic exchange services is still fraught with many value judgments. The technological imperative is that we give greater weight to economic pricing. This acknowledgement of alternatives to the utility system does not require us to ignore other noneconomic policy objectives. In fact, we have no intention of abandoning those consumers who are most subject to monopoly power and who are most in need of the Commission's protection, nor do we believe that we must choose between efficiency and affordable service. The decision below reflects these principles.

B. The Source of Remaining Revenue Requirement Changes

1. Centrex Service Feature Changes

On May 13, 1987, we issued Resolution T-12023, effective that same date, which authorized Pacific to offer 25 new Centrex service features from certain central offices, pursuant to Pacific's Advice Letter 15243. Seven of these features were included in the rate design Pacific submitted in the present proceeding. Five of these seven, however, are set at higher rates than those proposed in this rate proceeding. The resolution found that the newly approved rates for these five services would produce an additional $58,932 over the annual revenues proposed by Pacific in its filing in this present proceeding. Therefore, the resolution directs that this rate effect be taken into account in the present decision. Our accounting for this revenue effect can only be prospective from the effective date of this decision.

2. Private Line Revenue Requirement Reduction

In D.87-08-048 issued August 26, 1987, we found Pacific's special access (private line and private line-like services) revenue requirement should be reduced, this time by $11 million. And again, we necessarily found that that reduction should be offset by an increase in nonaccess service rates, chief among which are basic local exchange services. Because D.87-08-048 was issued shortly before the expected date of this decision, we directed that comments on the appropriate rate design for these changes should be filed for consideration and disposition in the present proceeding and that implementation of these revenue requirement shifts should occur in the context of this proceeding in order to avoid the adverse effects of short-term billing changes. Therefore, in this decision we are ordering Pacific to shift $11 million in revenue from its special access rates on a prospective basis. The appropriate special access rate design after removing this $11 million and the impact of this shift on other telephone companies are discussed below.

3. <u>The Assigned Commissioner's Ruling</u>

The final action governing the extent of rate changes is the Assigned Commissioner's Ruling issued in this proceeding on April 1, 1986. The Ruling states at Ordering Paragraph 2:

> "Pacific's rate design proposal shall be heard by the Commission except that the rate shift presented shall not be greater than that recommended by PSD [Public Staff Division, now called Division of Ratepayer Advocates or DRA] in the compromise proposal filed in its motion of February 7, 1986, adjusted solely to account for changes caused by D.86-03-049, unless a hearing on a greater revenue shift is permitted by order or ruling after the Commission has more information as to long-range rate projections."

At the time this Ruling was issued Pacific had a proposal before this Commission which included a shift of over $400 million in revenue from intraLATA toll service to local exchange rates. The DRA proposal mentioned reduced rates for message toll service (MTS) and MTS-related service by $71 million to reflect its proposed <u>intra</u>LATA SPF to SLU transition. The subsequent proposal filed by Pacific increases residence basic service revenue by $71.3 million. We consider that some or all of the $11 million shift which we ordered in D.87-08-048 as well as this $71 million SPF to SLU change could be shifted to local basic exchange rates. Therefore, we are bound to keep any prospective increase in the total revenue requirements for local exchange rates within a maximum of about $82 million prospectively, and about $71 million for the test year.

C. Rate Design Objectives of Pacific and DRA

At the same time that Pacific has been experiencing an overall reduction in its revenue requirements, there have been pressures tending to push the revenue requirement for some end user services, notably basic exchange services, upward. This is due in part to the entry of competitors into the interstate long distance market following the divestiture of AT&T's monopoly of those services, and the impact of that competitive force on the rates Pacific is authorized to charge those competitors for such things as access to the local network. Thus, for example, in D.85-06-115 we authorized changes in the methods used to calculate Pacific's revenue objective for access services which resulted in reducing Pacific's access charges by about $140 million. We offset that reduction with a complementary billing surcharge on most of Pacific's end user services--many of which are basic exchange services. Another pressure comes from the possibility of competition in the intraLATA MTS market which we will address in Phase III of I.87-11-033.

Based on an overall rate design meant to eliminate the 2.48% surcharge on nonaccess services in effect after our Phase I interim decision in this proceeding, D.86-03-049, which ordered a revenue decrease of $120.649 million, and to redesign some rates so as to redistribute revenue while remaining revenue neutral overall, and taking note of the rate pressures referred to above, Pacific proposes to deal with them by decreasing MTS rates and certain other service rates and offsetting these decreased revenues by increasing basic residence service rates, private line rates, and business rates. Pacific's rate design testimony emphasizes its belief in the necessity of our authorizing rate-setting principles which target basic residence service at subsidized rates and which assure that other rates are set to move toward costs. Pacific asks us to move away from a focus on average historical costs and toward a focus on economic costs, giving consideration to such issues as geographical cost differences, cost differences due to usage variations among types of customers, perceived value or demand balanced against the availability and prices of substitute services, and efficient network utilization.

DRA has proposed two rate designs, one based only on spreading the 2.48% surcharge in effect in 1986 as a result of the $120.649 million reduction in revenue requirement adopted in D.86-01-026, and another which assumes a total 1986 test year revenue requirement reduction of about $300 million based on DRA's recommendations in the Results of Operations phase of this proceeding.

In the first design DRA witness Shantz proposes reducing MTS revenue by $47.428 million, increasing business and residence basic exchange service rates by a uniform percentage amount to recover an additional $101.825 million, increasing rates for private line and private line-like services by about $67.5 million, and increasing service connection charges by about $7 million. (See p. 1 to attachment to Exhibit 351.)

His second rate design, filed subsequent to Pacific's June 25, 1986 rate design and based on a reduction in revenue requirement of about $300 million, proposes reducing MTS and MTS-related services by about $125 million, <u>reducing</u> basic exchange rates by nearly $88 million and retaining most of the other proposed rate revisions. (See Exhibit 352, p. DMS-3.)

DRA presents yet a third rate design in its opening brief. This design proposal addresses spreading about the same $300 million revenue reduction; however, it includes spreading an additional amount which recognizes the increase in the billing surcharge which became effective on January 1, 1987 to account for a reduction in the revenue requirement for interLATA access services. This third rate design proposes decreasing MTS rates by about $26.7 million, very slightly changing the previously proposed increase for private line and private line-like services (from $67.54 million to $68.165 million), leaving the increase in service connection charges the same, and continuing to decrease basic local service rates but by the much smaller amount of about $19 million. DRA advocates spreading this basic exchange rate decrease uniformly across all basic service rates.

D. Rate Design Objectives of Other Parties

In the principal decision in Pacific's previous general rate case we described our rate-setting process as follows:

> "Generally speaking, we set rates for a particular service based on one of three distinct models: (1) setting rates to recover the full costs of service, including an appropriate factor for return on invested capital; (2) setting rates to recover the full costs of service plus an additional contribution toward common costs or the costs of other services; and (3) setting rates residually to recover revenue requirement not achieved from other services. The first model of fully cost-based rates is our general standard. We apply the second model to optional, discretionary services where considerations of demand elasticity, value of service, and historical rate relationships justify setting rates above cost. The third model, residual pricing, is reserved for basic exchange services and related essential services which the Commission historically has sought to protect from the impact of drastic rate increases, in the interest of promoting the goal of universally affordable telephone service." (Pacific Tel. & Tel. Co. (1984), D.84-06-111, mimeo. at 142-143.)

The parties to this present rate design proceeding differ in their views of how costs should be measured, how we should determine which of the above models to apply to a particular rate, and how we should determine the appropriate amount of contribution to assign to rates for those optional or discretionary services which are set according to the second model.

Further, three parties, the California Bankers Clearing House Association and the Tele-Communications Association, herein jointly referred to as CBCHA/TCA, and sometimes called the Users Group, a group comprised of the United States Department of Defense, the General Services Administration, and all other Federal Executive Agencies, herein jointly referred to as FEA, and the Western Burglar and Fire Alarm Association (WBFAA) prefer that there be no rate design at all, and that we simply reflect the changes in Pacific's revenue requirements by adopting a uniform surcredit or surcharge to be applied to all services.

CBCHA/TCA argue that the Commission should wait to adopt a rate design "until the revenue requirement is more certain and the cost study support more accurate." However, they ask that in the event we do adopt a new rate design, that we reject Pacific's and adopt the one which they offer. The key feature of CBCHA/TCA's proposal is its elimination of most residual rate-setting and covering a far greater portion of costs through access rates, thereby reducing usage rates.

It is FEA's position that rates should be set for each particular service at least as high as the incremental cost for providing that service, and then any augmentation in the price/cost margin should be set on the basis of market conditions, with lower price/cost margins for services with a relatively elastic demand curve and higher price/cost margins for services with a relatively inelastic demand curve--with certain narrow exceptions where subsidies are maintained for "those customers who are truly in need." However, FEA maintains that Pacific could not set prices in this way because it has not produced incremental cost studies for each specific service category. FEA concludes that this constitutes a failure to comply with this Commission's prior decisions and the recommendations of Pacific's own pricing policy witness, Dr. Harris, and therefore requires that Pacific's rate proposals be rejected.

WBFAA finds Pacific's cost studies to be "uncertain," its revenue projections to be "unclear," and its view of the future to be "murky," and asserts that the result might be "unanticipated and undeserved revenues [for Pacific], and irreparable harm to the ratepayers." WBFAA therefore urges that the present surcharge remain in place or that all rates be adjusted by the amount of the surcharge. Though WBFAA does not address other revenue shifts, we assume that it prefers that any rate shift be spread across all services on the same percentage basis.

Further, Telephone Answering Services of California, Inc. (TASC) also argues that Pacific's cost studies are unreliable and supports this Commission's rejection of the Pacific cost studies and adoption of the motion filed in February, 1986 by DRA and the subject of the Assigned Commissioner's Ruling mentioned above, which proposed setting the then-current billing surcharge to zero, reducing MTS rates by $71 million to reflect DRA's proposed intraLATA SPF to SLU transition, realigning certain ZUM rates in the San Francisco Bay area, and applying the remaining revenue requirement (about $201 million) as a uniform increase across all service categories except Coin, Lifeline, and Centrex.

We agree with CBCHA/TCA, FEA, WBFAA, and TASC that problems with cost studies as well as other issues these parties raise have made our rate design efforts more difficult; however, Pacific and its ratepayers have a right to the rate design they seek rather than continued across-the-board additions and subtractions to rates which may deserve different treatment or may deserve to be supplanted with new or different rate elements. The issues these parties have raised are not insurmountable. There is always some imprecision in this process. We do not believe it is so great in this record that we must forego a review of Pacific's rate design proposals altogether.

III. Basic Residential and Business Service

A. Residential and Business Rates

1. Pacific's Basic Residence Access and Usage Proposal

Pacific proposes a new billing disaggregation for basic residence exchange service which distinguishes between that portion of exchange service which is common to all customers and not usage sensitive, which it designates as access, and that portion of exchange service which is usage sensitive. Pacific proposes setting the residence access line rate at $4.45 per month for all its residence offerings. Its cost witness, Mr. Scholl, claims the average historical cost for access is $25 per month.

Pacific then proposes three usage offerings, also targeted at rates requiring subsidy. The plans include a continuation of the present "Unlimited Calling Plan" within the local (ZUM Zone 1) area, and the "Measured Call Plan" designed for those whose local usage needs are minimal, and the establishment of a new "Call Allowance Plan."

The Unlimited Calling Plan would be set at a flat rate of $5.55, so that with the addition of the access charge the total cost for unlimited usage would become $10 rather than the $8.25 presently authorized.

The Call Allowance Plan would be set at $3.80 per month in addition to the access charge and would permit 130 untimed local messages per month with each local message thereafter being charged at $.08 per message, up to a maximum of $1.75. Thus, this plan would also be capped at $10 per month, but those customers accumulating no more than 130 local messages would pay only $8.25 per month, the same as the presently authorized unlimited calling rate. Pacific states that about 65% of today's residence customers make fewer than 130 local calls per month and that this plan would, therefore, meet their needs. Pacific's rate design witness

Sullivan testified that this plan would keep most customers' rates at their present level and would cost Pacific $8- to $10 million to implement. Further, according to Exhibit 345 Pacific proposes to notify its customers that their service will automatically be converted to the 130 Call Allowance Plan unless they request a different service.

The Measured Call Plan would not change except for the names of the rate elements. It is set at the access rate plus $.04 for the first minute of usage and $.01 for each additional minute. Additionally, customers of this service would receive a $3.00 monthly allowance against their local and ZUM Zone 2 usage. That comes to 37 1/2 5-minute local calls per month. Sullivan asserts that about 20% of Pacific's present residential customers could subscribe to this plan, continue their present calling patterns, and pay no more than the $4.45 access charge each month.

As for Universal Lifeline Telephone Service (ULTS or Lifeline) Pacific proposes to leave the rate for measured service at $1.48, which is computed as 50% of the measured access rate less $.75 Customer Premises Equipment (CPE) rental credit. Lifeline measured rate service continues to provide a call allowance of 60 local calls (as contrasted with $3.00 worth of measured local usage for non-Lifeline measured service) and proposes reducing the additional charge to $.08 for all calls rather than the present rates of $.10 for 61 to 70 calls and $.15 for all calls after the 70th.

Sullivan testified that Pacific wishes to make Lifeline service more valuable to those who qualify for it by also offering a discounted 130 Call Allowance Plan and the Unlimited Calling Plan so that economically disadvantaged customers can have the same options as other customers. Initially Pacific proposed a $2.00 monthly discount for the 130 call plan and the unlimited call plan for Lifeline customers; however, with the intervening passage of AB 3288 on September 23, 1986 amending Public Utilities Codes

§ 739.2, Pacific asks that these services be offered to Lifeline customers on the same 50% tariff rate basis as basic measured service. Pacific requests that it be permitted to recover the discounted Lifeline amounts for these optional services from the Universal Telephone Service Fund.

Pacific also proposes that the charge for installation or service on individual residence lines be raised from $70 to $100 for the first line, but stay at $70 for each additional line. Further, it proposes to give customers 90 days from implementation of these new rates to choose a new service (or, presumably, to choose <u>not</u> to be transferred to the 130 Call Allowance Plan) without being subject to a charge for the change.

2. **Criticism and Alternatives to <u>Pacific's Residence Proposal</u>**

a. <u>CBCHA/TCA</u>

The CBCHA/TCA proposal agrees with the concept of separate charges for residential access and usage; however, as their witness Dr. Selwyn testified, they believe that Pacific's proposal detrimentally perpetuates an unnecessarily high annual subsidy to basic exchange access lines of about $2 billion (the amount by which costs Pacific assigns to local access exceed revenues), and consequently, excessive rates for other services such as intraLATA usage, intrastate interLATA access, and interstate access. Selwyn testified that this policy results in suppressing demand and giving customers incentive to bypass. He argues that the goal of universal service can be met at a far lower cost through a targeted subsidy program for Lifeline customers while moving access line rates for all other residential exchange access toward cost.

Citing a study performed by the staff of the Florida Public Service Commission, Selwyn claims that residential demand for local service is highly price inelastic, and concludes that the Lifeline mechanism already provided for in California is all we need to assure the universal availability of basic telephone service. He therefore proposes to reduce, and eventually eliminate the subsidy to non-Lifeline residential ratepayers.

As a first step CBCHA/TCA proposes a plan with three basic options for residential customers. All customers would pay $5.00 monthly for access. Under the first service option the customer would pay an additional $2.10 which would include a $3.00 usage allowance. Additional calls would be $.04 for the first minute and $.01 for each additional minute. Thus, this option would cost $7.10 for up to $3.00 of usage. The second option, untimed measured service would be priced at the access rate plus $4.25 per month for up to 130 untimed calls. Additional calls would be priced at a flat $.07, with no usage cap. Thus this option would cost $9.25 for up to 130 untimed calls per month. The third option is for flat rate service at $9.00 per month plus the $5.00 access charge, or a total of $14.00 per month. Each service would be discounted by 50% plus the $.75 equipment credit for Lifeline customers. Selwyn's minimal reliance on local measured calls arises from his concern that, at an average cost increment of $.08 more than a local flat rate call, measured calls are of dubious value.

Selwyn asserts that the combination of his exchange rate proposal and his ZUM proposal discussed below will stimulate calling and create a better balance between rates and costs for both access and usage.

Pacific responds to the proposal of CBCHA/TCA by noting that the existing subsidy requirement "can and should be substantially reduced by eliminating, over a reasonable period of time, the subsidies which many business services currently enjoy." Pacific claims that its proposals will more effectively accomplish that goal and will also appropriately reflect the variances in the magnitude of revenue-to-cost shortfalls among services.

DRA urges this Commission to reject Selwyn's proposal as an unjustified departure from our traditional policy of setting residential rates on a residual basis. It also claims that Selwyn's proposal would only spread the benefit of reduced revenue requirement to business customers when both business and residential customers should share the benefit.

b. FEA

The FEA assert that traditional rate structure must be changed by reducing price/cost margins for those services which are sensitive to price and subject to competition. FEA claim that this should be accomplished by assuring that any subsidy to local exchange customers goes only to those who are truly in need. Thus, FEA propose moving pricing for services with relatively inelastic demands, presumably including basic residential service to those who are not truly needy, to incremental cost, plus whatever further amount basic demand considerations will permit. Recognizing that customers with relatively inelastic demands for particular services will resent an immediate doubling or tripling of prices, FEA suggest that the change be made by degree and not all at once.

FEA argue that this measure is necessary to circumvent bypass by large users, including FEA which will occur because alternative suppliers and new technologies [are] driving down cost. FEA claim that loss of business from these large users would result in stranded investment and increase the revenue requirement on basic exchange service even further. FEA add that offering volume discounts will also encourage these high volume business and government customers not to bypass.

Further, FEA assert that incremental or marginal cost information is crucial to determining appropriate rates, and point out that we ordered Pacific to submit such information in this proceeding. FEA claim that Pacific should have provided incremental cost data by service category, and that the data provided is insufficient since it only relates to three broad categories of plant: local loop, interoffice facilities and switching equipment. FEA add that since both their witness, Dr. Baughcum, and Pacific's expert witness on pricing policy, Dr. Harris, testified that incremental cost is the proper cost methodology this Commission should require Pacific to submit incremental cost data by service category in its next rate case.

As for the present, FEA argue that we should reject Pacific's rate design proposals because they are based on estimates of embedded costs which FEA's Baughcum describes as having little to do with economic or market value. He cites with approval the testimony of Harris that in a competitive environment, setting prices on the basis of historic costs will cause substantial allocative and technical inefficiencies. (Ex. 316, pp. 30-31.)

c. TURN

TURN's witness, Sylvia M. Siegel, argues that Pacific's residential customers are entitled to a share of the revenue requirement reduction by way of reduced rates for basic service. She proposes a "Residential Rate Simplification Plan" under which local measured service (LMS) would be eliminated altogether in favor of universal flat rate service and flat rate lifeline service. Siegel proposes offering this flat rate service at $6.00 per month, with lifeline set at $2.25 (one half the normal rate less $.75 to offset telephone equipment costs). Further, she testified that based on Pacific's workpaper volumes she estimates that a revenue neutral universal flat rate would be $7.73 per month and that her proposal would reduce annual revenues by roughly $128 million.

TURN urges this Commission to reject Pacific's 130 Call Allowance Plan for being priced specifically to make flat rate service uneconomical for each and every residence customer, despite any considerations of costs and revenues. TURN points out that Pacific's costs of serving customers who switch from flat rate to this measured service would rise by the cost of measuring the calls. TURN states that if 58%, or 3.7 million, of Pacific's residential customers switch to the new 130-call plan, as Pacific's workpapers suggest, and if Scholl's estimate of $.004 per message for measuring is accurate, and if it is assumed that each customer averages 100 calls per month (a figure which appears low to TURN), then the additional annual cost for measurement would be $17.76 million. TURN concludes that the 130-call plan is a loss-leader for Pacific under which every customer will pay less than the flat rate, while every customer will actually create higher costs of service than do flat rate customers.

TURN also opposes Pacific's efforts to separate basic service into access and usage components, reminding this Commission that we rejected a similar proposal in our last Pacific rate design decision, D.84-06-111, which, among other things, found that the proposed distinction was more didactic than practical. TURN asserts that the proposal is purely a marketing tool that attempts to redefine existing services in ways that would slant Commission and public attitudes toward the Utility's repricing schemes. TURN alleges that nothing has changed since we made the observation in D.84-06-111, that "PacBell does not actually propose unbundled rates but merely uses the access/usage dichotomy to explain the relationship between its proposed rates and its calculated costs." (D.84-06-111 at 275). Further, TURN alleges that the policy is illegally discriminatory in that a residential flat rate customer would pay $4.45 for access alone, while an LMS customer would receive access plus $3 worth of free usage for the same amount.

CBCHA/TCA expresses agreement with TURN that Pacific's measurement of local calls improperly inflates the cost of providing residential exchange service, but does not agree with TURN's rate proposal, since it contends that even Pacific's proposal prices local access too far below cost.

Pacific is also critical of TURN's proposals, claiming that it is necessary to narrow subsidy targets to residence access and a reasonable amount of usage and service connection, in this period of diminishing sources of subsidy. Pacific argues that TURN's proposal would decrease rates for customers who generate the greatest costs, the residence flat rate customers, while increasing rates for the measured service customers who generate the least costs, and adds that the 130 Call Allowance Plan together with its other proposed local offerings more appropriately provide the Commission with the means to direct subsidy flows to achieve its policy objectives in the most efficient manner.

d. Brylawski

Dr. Robert E. Brylawski testified on his own behalf about Pacific's residential basic exchange service proposal. His testimony agrees with that of Siegel that Pacific has not provided cost support to justify increasing flat rate service rates as proposed while leaving measured service rates unchanged. He further asserts that Pacific's cost studies suggest that current relative prices of the two services are reasonably in balance from a revenue/cost standpoint.

Brylawski bases his testimony on a comparison of Scholl's testimony and related workpapers, Exhibit 293, a customer usage study done by Pacific, and portions of Sullivan's testimony and workpapers which, he states, together lead him to conclude that there are several errors in Scholl's data input which distort the revenue and cost figures Pacific adopts for residential basic exchange service.

As shown in Table 2 to Exhibit 379, Brylawski's calculations conclude that the revenue shortfall is fairly similar for either flat or measured service based on either Scholl's data or Exhibit 293, but that the revenue to cost ratio revealed that in both instances flat rate service contributes proportionally more to meet its costs than measured service. Based on this finding and his contention that revenue shortfall is a more reasonable basis for comparing alternative services in the same service class, he recommends preserving the present balance by spreading the new revenue requirement for residential basic exchange service between flat and measured services by raising or lowering the rates for both services by essentially equal dollar amounts.

Brylawski is opposed to the 130 Call Allowance Plan, claiming that support data for both costs and revenues are woefully inadequate and cautioning that the data available suggest that it is designed primarily to draw customers away from flat rate service and raise a distinct possibility that this plan may actually produce incremental costs in excess of incremental revenue. He also objects to the plan on policy grounds, claiming that it will further complicate the customer's choice of basic service and require them to be dependent on Pacific's representatives for advice. Brylawski points out that flat rate service would become superfluous under Pacific's proposal and expresses the suspicion that it is designed to drive flat rate service out of existence.

Brylawski asserts that there is no discussion of the incremental costs of this plan when compared to the status quo, but claims that there will at least be a cost for service regrades for the 4.2 million customers who will switch to the service. Suggesting the "modest" assumption of $30 per regrade, he calculates this nonrecurring cost to be $125 million. Brylawski also claims there will be a new cost of measuring and billing for local calls that are currently unmeasured under flat rate. He estimates this as ranging between $2.5 and $7.5 million annually, depending on the call volume estimate used and the measuring cost per call used, and points out that adding this additional cost to the incremental revenue of $4.5 million which Pacific projects will result in something between a $2 million increment and a $3 million loss.

e. DRA

DRA's Exhibit 329 critiques Pacific's various cost studies. It agrees that Pacific's methodology for establishing the cost of service connection for residence and business services is sound and produces acceptable results, but expresses skepticism of the accuracy of Pacific's bottoms-up studies of subscriber access lines and local usage.

DRA agrees with Pacific's conclusion that costs of subscriber access are likely to exceed revenue from present rates, but does not accept Pacific's estimates because they are not based on a true bottoms-up cost study. Specifically, DRA criticizes the major component of the access cost study, the local access line loop study, for not using a larger sample size. DRA argues that Pacific's precision level of plus or minus 13% for residence loop length and plus or minus 16% for business loop length at a confidence probability of 95% is inadequate and that the precision level should be plus or minus 5%. DRA also criticizes as unscientific some of the assumptions Pacific made about various quantities of outside plant not included in the loop study which result in more than doubling the total loop length. DRA also objects to Pacific's use of booked investments for outside plant to distribute investment dollars to the loop footage, arguing that this is inappropriate to a true bottoms-up study.

DRA addresses the reasonableness of the methodology of Pacific's bottoms-up local usage study, finding the methodology Pacific uses to determine costs of two of the three equipment categories to be appropriate, but the third to be inconsistent. The first two give embedded cost output. The third provides incremental costs, to which Pacific has added an "embedding factor." DRA points out that this inconsistency "casts doubt on the likelihood that the switching cost component represents an average embedded bottoms-up cost." (Exhibit 329, 10-4.) Further, DRA points out that since the usage costs are not current, but embedded, they are of very limited use in evaluating bypass potential or other competitive pressures or in analyzing pricing proposals in the present environment.

With these reservations in mind, DRA has relied little on Pacific's cost studies and has instead emphasized the importance of making rate design changes which address its policy goals by making rate changes which protect basic service rates. DRA states that its primary goals are to eliminate the billing surcharge and decrease MTS rates. DRA witness Shantz suggests that a first priority for accomplishing that is an increase in rates and charges for private line and private line-like services and possibly a slight increase in basic local residence and business services rates.

DRA proposes increasing the rates for service connection charges, but slightly decreasing basic exchange service rates. In his pre-filed testimony of July 10, 1986, (Exhibit 351), Shantz explains DRA's rationale for increasing service connection charges. He states that the present service connection charges were established in mid-1984 and that "DRA does not believe that the charges for these labor intensive activities should remain unchanged for as long as five years." Nonetheless, DRA does not agree with the imposition of a large increase in this rate. Rather, this initial testimony of Shantz proposes a uniform percentage increase of about 5% for each service which can be characterized as a form of access lines. This, he asserts, will reflect the labor intensive nature of these services while excluding increases for services which were the subject of our investigation into Pacific's marketing practices such as Touchtone and optional calling plans.

DRA opposes Pacific's unbundling of residence rates into access and usage components, stating that it will lead to customer confusion and makes no sense when discussing a flat rate service. DRA also opposes the 130 Call Allowance Plan and the automatic conversion to this plan which Pacific proposes, arguing that the similarity between this and the proposed flat rate service will lead to customer confusion and could mislead customers into believing that the 130-call plan is the same as flat rate service. DRA therefore advocates leaving the residential service choices as-is. Further, DRA points out that this Commission has traditionally set residential rates on a residual basis, and concludes that there is no justification for abandoning that policy as some of the parties have suggested.

Although DRA initially opposed Pacific's proposed flat rate lifeline offering, it now contends that the proposal is supported by the January, 1987 amendment to Public Utilities Code § 739.2.

CBCHA/TCA criticize DRA's residual pricing argument as simply a characterization of past Commission practice which has no place in a post-divestiture environment where competitive and potentially competitive services ought to be priced to reflect economic costs of providing them except in those limited areas where subsidy is required to ensure universal service. CBCHA/TCA adds that absent some valid public policy rationale the subsidy to residential basic exchange service which DRA advocates is unreasonable and discriminatory in violation of Public Utilities Code §§ 451 and 453.

FEA criticize DRA's proposal because of the significant risk of stranded investment and ultimately higher basic exchange rates which arise from not following marginal cost-based or market-based pricing policies.

Pacific also criticizes DRA's proposal for disregarding the competitive threats to the services which help subsidize basic exchange service in order to achieve a minimal reduction in basic exchange rates (e.g. DRA's proposed reduction of $.15 in the monthly rate for Individual Line Measured Rate Residence Service with a $3.00 usage allowance and its $.05

proposed reduction for Individual Line Measured Rate Business Service). Furthermore, Pacific defends against DRA's criticism of its local usage cost study and its access line loop study precision factor pointing to DRA witness statements which it claims support Pacific's conclusions.

3. Discussion of Residence Rate Proposals

The importance of taking account of economic costs of service and setting rates that promote efficient use of the network will be growing as our economy becomes increasingly dependent on communications networks for transaction and information services. Large applications in particular may be greatly affected by uneconomic usage rate design, and such rate design will probably aggravate other tendencies toward private networks. At the same time that we recognize this future scenario we also recognize the need to provide rate subsidies for those who truly need them through the Lifeline program. Outside this focus, however, it is our intent that basic exchange rates should gradually but continually move toward a closer relationship with efficient economic costs of service.

This is different from the abandonment of residual pricing of basic residence services as proposed by CBCHA/TCA or FEA with only a targeted subsidy for Lifeline customers. Both base their argument for this policy change, as they have in the last several Pacific proceedings, on the bypass threat. We recognize that bypass is a problem facing Pacific; however, we believe that the presently authorized interLATA SPF to SLU phase-down, along with the intraLATA SPF to SLU phase-down which we authorized in D.87-12-067 will provide a sufficient signal of our continued intent to limit incentives for uneconomic bypass without the need for the sort of dramatic shifts in basic rates they advocate.

As we have pointed out before in proceedings addressing this question of how to deal with the costs of the local network, the great bulk of the nontraffic sensitive (NTS) costs at issue here are capital-related costs such as earnings on capital investment, income taxes on those earnings, depreciation charges, and property taxes. The magnitude of these capital costs is attributable to the method of accounting for subscriber plant costs over the years which was designed to keep the costs of becoming a subscriber to telephone service low in keeping with the national (and Bell system) telecommunications policy goal of universal telephone service. The costs of these local facilities were not charged to the local subscribers whom they were built to serve. Often the facilities were built to meet anticipated future need so there were no subscribers to charge. The ubiquitous nature of the resulting telephone network benefits all users. The logic of these accounting practices and the shared benefits that resulted from them seem to this Commission to mandate that the costs of that network should be shared and not now thrust solely upon the shoulders of the local users. At the same time, however, in response to the emergence of technological alternatives to the local network, we give greater recognition to the economic pricing of usage. We believe that the transition from SPF to SLU cost allocation accomplishes these goals.

Further, we expect basic exchange rates in the long-run to approach the <u>most efficient</u> costs of service. We explicitly make no endorsement that, even assuming their accuracy, the costs currently reflected by Pacific as the cost of basic access lines, for example, <u>are</u> those most efficient costs. Observers should not mistake the willingness and even the desire to accommodate increases in basic exchange access <u>rates</u> as any relief from this Commission's will to apply continuing regulatory pressure on corresponding <u>costs</u>.

Indeed, one of the Commission's challenges as it considers changes in regulatory mechanisms in I.87-11-033 will be to find more effective ways to keep pressure on exchange carriers to minimize the cost of basic exchange access lines. Basic exchange access is perhaps the service least subject to competitive pressures for cost reduction and most susceptible to the "goldplating" and lack of managerial attention popularly and frequently cited as one of the primary rationales for reexamining the effectiveness of rate of return regulation.

Considering the questionable reliability of the available cost information the fairest means of instituting a rate increase for local exchange services is to adopt a uniform percentage increase spread across all recurring local service rates as DRA suggests. For this reason we find no merit in TURN's proposal to simply reduce flat rate service rates to $6.00 per month. There is no reason to exempt any service, including the measured call plan, from this spread. We will not adjust rates for message units in this process. As Pacific's rate design indicates, these rates should remain at their present levels.

Pacific proposes increasing its service connection charge for installation of an initial residence line from $70 to $100. We agree with DRA that service connection charges should be moderately increased to take increasing labor costs into account. However, there is no more basis in the record for authorizing an inconsistently large increase in a charge which impacts the residential customer's ability to establish basic service, than there is for authorizing a large increase which impacts that customer's ability to maintain basic service. Therefore, we will adopt the same uniform percentage increase for this service that we adopt for other residence rates.

Turning to the specific service categories of Pacific's residence rate design proposal, we find the pricing structure of Pacific's proposed 130 Call Allowance Plan troubling. As DRA, TURN, and Brylawski point out, the Plan would make the proposed flat rate service uneconomical and therefore essentially eliminate the flat rate service option. The 130 Call Allowance Plan proposal would simply confuse ratepayers and obscure the distinct difference between flat rate plans and measured call plans which exists today. Flat rate service is less costly to administer than measured rate service. The record demonstrates no basis for eliminating it. Flat rate service should continue to be an option. Therefore, we reject Pacific's 130 Call Allowance Plan. Obviously, Pacific's claimed implementation expense of $9.394 million for this plan is also rejected.

We are likewise not persuaded by TURN's argument that the present measured call plan should be eliminated. Pacific shall continue to offer its two present basic services to residential customers--individual line measured rate service with a usage allowance presently set at $3.00, and individual line flat rate service.

As for Pacific's proposal to create two separate rate elements for residence service, access and usage, we find such a step adds terminology which implies rate policies which are inconsistent with the use of residual pricing of residential basic rates which we follow in this decision, and which are also inconsistent with flat rate pricing. Therefore, we will not adopt the proposed separate rate elements for residence service at this time.

In our efforts to promote efficient use of the local telephone system, we have authorized tariffs which charge separately for access and usage and are known as "measured rates." However, as noted above, Pacific's proposal to charge each subscriber an access fee plus an additional usage fee, regardless of whether the usage rate is flat or measured, is not acceptable.

The concept of measured rates intrigues industry pundits, since such pricing might give a more accurate signal of the cost of service to the telephone customer. Ideally, calls should be priced at no more than marginal cost so that incremental usage will not be overpriced to the extent that uneconomic bypass occurs. Given rates that reflect the cost of service, the consumer presumably will tailor his or her demand in such a way that increases in the capacity of the phone system will be required only when consumer demand justifies additional investment by the phone company.

After the evidentiary portion of this proceeding was concluded, the Rand Corporation published a study entitled, "Optimal Peak-Load Pricing for Local Telephone Calls" (Rolla E. Park, Bridger M. Mitchell; March 1987, The Rand Corporation). The authors conclude that:

> "(C)ontrary to conventional wisdom, measured-rate pricing of local telephone calls is likely to be somewhat less efficient than traditional flat-rate pricing. If local measured service is desirable public policy, it must be justified on grounds other than economic efficiency." (Park & Mitchell, p. v.)

> "We find that...measured rates will at best produce very modest efficiency gains; more likely, they will result in small efficiency <u>losses</u>." (Ibid, p. 3, emphasis in original.)

This conclusion rests largely on the fact that because pricing periods could not feasibly be tailored to give consumers the appropriate signals, variation in customer demand limits the efficiency gains that price rationing can achieve.

Although the study surveyed the calling patterns of a limited number of residences and businesses in Clinton Illinois for one year, the results invite comparison with Pacific Bell's pricing scheme. This study indicates that the concept propounded by TURN in its proposal for a metropolitan flat rate, if priced properly, may have merit. On the other hand, it is possible that customers in Pacific's serving area exhibit a pattern of demand that can be mirrored by appropriate pricing periods, and that the cost of call measurement by Pacific differs from that assumed in the Rand study.

Since our rate design is intended to promote economic efficiency, we must be fairly certain that this goal will be realized, and not frustrated. We conclude that we should examine

Pacific's customer and cost data to test the Rand study's conclusions and determine whether measured rates for basic exchange service actually promote or hinder economic efficiency in Pacific's service territory. Therefore, we will direct Pacific to introduce evidence of the incremental costs of basic exchange service in the supplemental rate design proceeding. We wish also to explore the implications of the Rand study for other services wherein pricing signals are used to optimize the balance between utility cost and consumer usage, such as ZUM rates. To that end we will also direct Pacific to present evidence of incremental costs of calls within its ZUM areas for our consideration in the supplemental rate design phase of this proceeding. The evidence may persuade us to amend the terms and conditions of services priced at measured rates in our supplemental rate design proceeding.

Turning to Lifeline, we see that the program must be "filled out" to provide completely for the protection of ratepayers with limited means. We agree with Pacific's conclusion that Lifeline would better serve the varying needs of those who qualify by offering the same plan options that are offered to other customers. In fact, with the implementation of AB 3288, the flat rate Lifeline option with unlimited local calls has begun. We will continue to authorize it at one-half the adopted flat rate less $.75 for telephone set rental and less $.25 for inside wire maintenance. We will also authorize a continued Lifeline measured access rate at 50% of the regular measured rate less the inside wire and rental amounts, and we will adopt Pacific's unopposed proposal to reduce the charge for additional calls after the 60-call allowance to $.08. We will also continue to authorize Pacific to recover the amount of discount it provides to Lifeline customers for these services from the Universal Telephone Service Fund. Today's economic climate suggests that further expansion or refinement of the scope of this program may be required as Lifeline takes on an even more important role than it bears today.

4. Pacific's Business Rate Proposal

Pacific proposes increasing the charge for the initial minute of business usage from $.04 to $.043, and measured line business access rates from the present $8.25 to $10.75. This access rate increase is just over 30%. It proposes increasing the rest of its business line access rates by over 48%. Citing the additional cost of providing trunks (also called Private Branch Exchange or PBX trunks), and Pacific's belief that customers will use the network more efficiently and avoid ordering designed circuits when they are not necessary if there is a price differential between regular business lines and trunks, Sullivan initially also proposed a new separate measured trunk rate at $16.00, a 93.93% increase, and an increase for the flat trunk rate from $25.65 to $38.00. The measured trunk rate is not presently differentiated from the business line rate of $8.25. Further, as with residence service, Pacific's proposed tariffs would raise the charge for installation or service on the first business line from $70 to $100, and leave the charge for each additional line at $70. It proposes charging even more for the installation of trunks, raising the charge from $70 to $175.

5. Other Parties' Positions On Business Rates

CBCHA/TCA do not comment on Pacific's proposal to increase measured line business rates, except insofar as they propose extending ZUM calling to distances up to 30 miles as the first step toward establishment of metropolitan-wide "community-of-interest-wide flat rate local calling." The proposal encompasses consolidation of ZUM Zones 2 and 3 and creation of a new Zone 3 to cover distances between 17 and 30 miles. It also includes day rates set at $.13 for the first minute and $.07 for each additional minute for this new Zone 3 rather than Pacific's proposed toll rates for that distance of $.25 and $.16. As we explain in our discussion of ZUM, below, we reject this ZUM rate consolidation plan.

As we have stated above, CBCHA/TCA also generally support cost based local calling rates, and Selwyn expresses a preference for flat rate local service, asserting that measured service unnecessarily increases local costs.

CBCHA/TCA do not approve of Pacific's proposals for increases in rates for trunk lines. They argue that the fact that PBX trunks have to be "designed" should not determine the pricing policy since many users of trunks select them not because of their design features, but because of customer distance from the servicing central office, the gauge of the wire Pacific chooses to use for the access lines, the number of splices or connection points, or the routing of the cable to the central office. They claim that each of these things can affect the quality of a normal business line in such a way that the customer must use trunk lines instead. CBCHA/TCA also argue that trunks are less costly and more profitable than business lines in that costs of billing and collections may be lower on a per-line basis since they are normally utilized by customers who require many lines. They also claim that the rate of call completion is higher for PBX trunks than for regular business lines. Based on this analysis CBCHA/TCA recommend that Pacific raise its PBX trunk rate from $8.25 per month to $10.75 per month, the same amount proposed for the regular business lines.

DRA recommends rejecting both Pacific's measured PBX trunk rate and its flat PBX trunk rate. DRA argues that the measured rate discriminates against customers and appears to be set to "better position the price of Centrex service to the price of PBX trunk service." Like Selwyn, DRA also argues that there are no unambiguous criteria which a customer can use to determine whether it needs designed PBX trunks rather than nondesigned business lines. Citing D.93367 at 6 CPUC 2d 441, DRA claims that this fact led the Commission to establish identical rates for measured business service and measured trunk service in the first place.

Both DRA and CBCHA/TCA point out that this ambiguity leaves Pacific with too much discretion and could result in abusive marketing practices. DRA again argues that the objective of this rate design proceeding "should be to eliminate Pacific's surcharge, and not to reflect an increase in the revenue requirement." With this in mind, DRA suggests that a 50% increase for any BEAL (Basic Exchange Access Line) service should be the maximum, but it recommends a uniform percentage decrease for all business BEAL service based on the adopted revenue requirement decrease.

As with residential service, DRA agrees that service connection charges should be increased, but objects to Pacific's proposal and instead asks us to adopt the same percentage increase it advocates for residential service connection charges.

6. **Pacific's Rebuttal and <u>Alternative PBX Proposal</u>**

Pacific's Sullivan responds to criticism of its PBX trunk pricing proposal by asserting that Pacific's primary reason for proposing higher rates for trunks than for business lines is that trunks cost more to provide and they are more valuable to the customer because they support greater usage. Pacific also asserts that PBX trunk line service is not an economical alternative to Centrex service, but that in California Centrex rates are set high enough so that PBX trunk line service is used to bypass Centrex. This, contends Pacific, is an example of the sort of uneconomic bypass this Commission has repeatedly stated it wishes to prevent.

Further, in his rebuttal testimony Sullivan makes an alternative proposal for Pacific's PBX trunk pricing based on the opposition of so many parties to its initial proposal. The alternative is to increase the PBX measured trunk line rate by $4.00 per month to $12.25 rather than increasing them to $16.00. Sullivan states that this will accomplish the same 12% increase in cost coverage which Pacific's proposed individual business line rate increase will accomplish. He goes on to claim that this rate would result in a $19 million net revenue shortfall which could be recovered through increasing the business local usage rate from $.04 to $.047 rather than to the originally proposed $.043. Further, he claims that while Centrex customers pay rates that recover its costs, PBX customers presently pay Pacific less than half of the cost of their trunks. Pacific argues that if this anomaly in pricing is not corrected, residential ratepayers will bear the burden of the lost Centrex revenues while underpriced PBX trunk service will continue to absorb large quantities of scarce subsidy.

7. <u>Discussion of Business Rate Issues</u>

We have already stated that the evidence in this record does not warrant total abandonment of our present policy and an immediate shift to cost-based rates for all local services except for a narrowly defined subsidy as FEA and CBCHA/TCA advocate. This holds true for basic business service as well as residence service. In order to continue the present policy it is appropriate to apply the same residual pricing model to basic business service that we apply to basic residence service. Likewise, we are unconvinced of the wisdom of Selwyn's related recommendation of significant reductions in minutes of use rates, offset by higher access rates for all local service. Therefore, we will follow the general recommendation of DRA and adopt the same percentage increase for business services that we have adopted for the residence services. Furthermore, Pacific's rationale for increasing the initial minute rate for business usage goes unexplained. We will authorize no increase in local usage rates.

Contrary to DRA's claim, our decision to keep trunk rates and individual business line rates the same in D.93367 was the result of monitoring difficulties which Pacific would have had at a time prior to the deregulation of customer premises equipment. The rationale does not apply today. Furthermore, there is nothing inappropriate in Pacific attempting to reconcile PBX trunk and

Centrex pricing, so long as both remain at justifiable levels. We agree with Pacific that it is reasonable for PBX trunk rates to be raised to a level closer to costs. Unlike basic residence and business services, a PBX line equipped with Direct Inward Dialing (DID) is in competition with another service, Centrex, and Centrex is designed to provide a contribution over costs as defined by Pacific in Exhibit 260, p. 4.2. Obviously, if we require this combination of services, PBX and DID, to be priced below cost, the contribution from Centrex will be diminished and efficient use of the network will be reduced to the disadvantage of Pacific and consumers of basic services.

On the other hand, the ambiguities in determining when a PBX trunk is needed rather than an ordinary business line lead us to conclude that it is inappropriate to approve rates which are totally competitive with Centrex at this time. Thus, we agree with the critics that the 94% increase in trunk access rates initially proposed by Pacific is not reasonable. The compromise proposed by Sullivan, which increases the measured trunk access rate by 48.48% and the flat rate trunk access rate by 33.53%, is more appropriate under the circumstances. We will authorize its adoption contingent on Pacific developing, as a part of its tariffs a set of written criteria setting forth design parameters for PBX, and explaining when a designed circuit is required from the central office serving that customer. After its submission by an advice letter and approval by the Commission by Resolution, Pacific shall provide a copy of this tariff to each customer seeking to establish PBX service.

Finally, seeing no justification to depart from our policy with regard to service connection charges, we will authorize the same percentage increase here that we have authorized for residence service connection charges.

8. The Revenue Increase to be Spread Over Basic Residence and Business Services

Based on the considerations described above we will authorize adoption of a rate design which spreads the test year residual revenue requirement using a uniform percentage increase for all recurring local business and residence service rates and service connection charges, except that business trunk rates shall be increased by the amounts set forth above. Basic rates will be rounded to the nearest $.05 and service connection charges will be rounded to the nearest $.25. Rates thus derived are set out in Appendix A to this decision.

B. Centrex Service

1. Pacific's Proposal

Centrex is a service provided from a Pacific central office which allows intercom calling at the customer's premises, access from these telephone sets to Pacific's network, the ability to transfer calls among telephones at the customer's premises, and various additional optional features such as call forwarding, speed calling, and call waiting. Pacific proposes to restructure Centrex rate elements and to change the way these rate elements are offered to the customer as well as the prices for certain of the the offerings.

The most significant changes proposed are the unbundling of the present Centrex primary station line charge into two elements, Centrex switching and Centrex access; charging two different rates for the new access element to offset the difference in the two End User Common Line (EUCL) charge rates the Federal Communications Commission (FCC) has mandated for service commenced pre-July, 1983 and post-July, 1983; reducing the rates for tie line termination (private network access); including single digit dialing as an element of basic Centrex service; increasing the Centrex Exchange Access Trunking charge to $1.60 to "reflect"

Pacific's proposed $16 PBX business measured trunk rate;[1] adding new optional service features; and simplifying charges for optional services by charging one or the other of two rates depending on whether the service has been classified as "high demand, low cost" or "low demand, more complex."

According to Sullivan this proposal will result in an overall revenue decrease of $3.176 million for the 1986 test year. However, as we mentioned above, since the time Pacific's proposal was filed this Commission has issued Resolution T-12023 authorizing 25 additional optional Centrex service features and authorizing rate increases for some of these services which would produce $58,932 more than the annual revenues which would be produced by Pacific's proposal as filed.

Further, since the time Pacific's proposal was filed the FCC has raised the pre-1983 EUCL by $1 per month, from $2 to $3 in its apparent plan to phase out the differential between the two EUCLs. The result is that Pacific's proposed pre-July, 1983 and post-July, 1983 rate parity would be lost or else it would be necessary to adjust rates to take cognizance of this change. Sullivan cites the language of Pacific's proposed tariff Schedule CPUC No. A 9.1.1.A. 1.i. which, in anticipation of such an FCC change, states:

> i. Any change (increase or decrease) in the End User Common Line Access Charge (EUCL) stated in Tariff F.C.C. No. 128, will be offset by a change in the Centrex Line rate in the same amount. The revenue requirement associated with the change will be recovered within the Centrex category as determined by the Utility with at least 30 days notice to the CPUC.

1 This is considered a "reflection" because it is generally assumed that one PBX trunk is the equivalent of ten Centrex lines.

Since the EUCL change was effective on June 1, 1986, Pacific could not offer any evidence in this proceeding on its revenue requirement impact. Therefore, at least until such time as the recovery contemplated by the above tariff language became effective Pacific's pre-1983 customers would actually be paying $1 more for basic Centrex service than its post-1983 customers, rather than $2.54 less as is now the case.

In discussing reasons for setting prices to offset the different EUCL rates, Pacific argues that the present rate difference is not cost-based and establishes an artificial cost barrier which keeps customers from adding new Centrex lines or commencing Centrex service, either of which would benefit Pacific's general body of ratepayers by providing a contribution of revenues over costs. Sullivan adds that Centrex customers make a relatively greater contribution of revenues over costs than do PBX type customers because Centrex customers buy more features and usage, apparently implying that more customers would choose Centrex instead of PBX or move from PBX to Centrex and would spend more money for features and services if this barrier were removed.

2. <u>Positions of the Other Parties</u>

CBCHA/TCA oppose Pacific's Centrex proposal as simply another element of PacBell's marketing efforts to enhance the competitive position of Centrex versus PBX. CBCHA/TCA cite with approval the opinion testimony of DRA's Shantz that this price positioning by Pacific, where it proposes <u>reducing</u> new Centrex service from $18.68 to $16.00 while <u>increasing</u> PBX trunk rates from $8.25 to $16.00, "is akin to the unethical and abusive marketing practices for which Pacific has already been partially reprimanded by the Commission." (Ex. 351, p. 4.) CBCHA/TCA also argue that the effect of Pacific's proposal is to circumvent the actions of the FCC by causing customers to pay more for their pre-July, 1983 Centrex lines than for their post-July, 1983 lines. CBCHA/TCA conclude that this Commission should reject the proposal and leave the present Centrex rates in effect.

Besides the above-cited statement by Shantz, he also expressed concern about Pacific's motivation in moving from its May, 1986 rate design proposal which would have produced a $2.5 million Centrex revenue increase, and its June, 1986 final proposal which would produce a $3.176 million decrease. He proposes instead that Pacific be authorized to adopt a provisional Centrex offering, applicable to new service only, while retaining the present rate design for service already in effect and changes to such service. He also proposes that while the provisional offering is in effect, each customer subscribing to it sign a statement which puts that customer on notice that the offering is provisional and subject to change. DRA's proposed provisional offering is the same as Pacific's proposal except it does not include Pacific's proposed reduction from $92.75 ($88 plus a 5.4% surcharge) per month to $55 for tie line terminations because Shantz regards this rate change as intended to improve the price position of Centrex service at the expense of non-Centrex services. Shantz testified that the DRA provisional offering proposal should remain in effect until this Commission addresses the appropriate rates and charges for Centrex services and PBX BEAL services in a separate proceeding after which this Commission would establish permanent rates for all Centrex customers and eliminate the interim provisional offering. Meanwhile, since the provisional offering only applies to new systems, DRA believes that there will be no change in annual test year revenues.

The basis for Shantz' recommendation seems to be a letter which he quotes in his testimony (Exhibit 351). It was sent by the Commission's Advisory and Compliance Division (CACD) to Pacific in December, 1985 refusing to process any more contracts for Centrex services and recommending that Pacific file an application, apparently offering tariffs to cover the services then being offered by contract. The letter criticized Pacific for failing to adhere to Commission procedures in handling these contracts. Shantz seems to take the position that the tariff revisions filed by Pacific in this proceeding, and its failure to file an application as directed by CACD are inappropriate in that they make it impossible for this Commission to give the careful consideration necessary to this question of the wisdom of altering the rate relationship between Centrex service and PBX trunks equipped with DID service.

3. Discussion

We view Centrex as a service which can provide a contribution to Pacific's basic rates. Thus, it is appropriate for Pacific to set rates to maximize this contribution so long as they remain reasonable. PBX rates and DID rates must also be set at reasonable levels. We set those rates above based on their independent merit, but with consideration given to the fact that they compete with Centrex.

Much of DRA's concern about Pacific's Centrex proposal relates to our investigation of Pacific's abusive marketing practices and DRA's concern that such practices have extended into Pacific's business services and may be in operation here. DRA, concerned with the need to further investigate the appropriate relationship between Centrex and PBX services, but wanting Pacific to be able to offer the new digital services in its proposal, contends that we should adopt Pacific's new proposed rates with one exception on a provisional basis for new Centrex service only, applying the existing tariffs to systems in service and growth additions or supersedures to them. We do not believe that the record before us requires the further investigation DRA requests; however, we agree with DRA that Pacific's customers should have the benefit of a rate design which includes its new digital offerings.

Some aspects of appropriate Centrex rate design are clear. For example, hearing no argument to the contrary, we will continue to assume that ten Centrex lines are the equivalent of one PBX trunk. Since we have adopted a PBX trunking rate of $12.25, a consistent Centrex trunking charge would be $1.25 (we round to the nearest $.05), rather than the $1.60 which Pacific proposes based on its $16 PBX trunking rate proposal. This change alone would reduce Centrex revenue by about $3 million.

On the other hand, this record provides no information on which to determine the reasonableness of the one very large rate change that Pacific proposes - the reduction in tie line charges from $92.75 per month to $55. In fact, its initial proposal did not make such a shift. Furthermore, we have very little information on the relative costs for meeting any particular user's needs via PBX trunks versus Centrex service should these proposed changes be implemented. Thus, while there is no evidence of marketing abuse with respect to the marketing of Centrex vis-a-vis PBX trunk lines equipped with DID service, the evidence available is inadequate to warrant a rate design which would amplify the revenue effects of the reduced trunking charge by incorporating this further rate reduction.

According to Pacific the revenue difference between its earlier Centrex proposal and the June 25, 1986 final proposal is about $5.676 million. Leaving the single tie line monthly rate element at its present $92.75 level, rather than the proposed $55, adopting the $1.25 trunking rate, and adopting the rest of Pacific's final proposal, excluding the five features adopted by Resolution T-12023, results in a $0.968 million revenue decrease. When we include the additional revenue from Resolution 12023 the total Centrex revenue effect is a negative $0.912 million, which still provides a contribution over cost.

These changes leave a rate design which incorporates the new digital offerings and also achieves a reasonably small revenue change in a relatively straightforward manner. Therefore, Pacific is authorized to adopt its final proposed rate design for Centrex except that the tie line termination charge shall remain at its present $92.75 and the Centrex Exchange Access Trunking Charge shall be set at $1.25. These new rates shall apply to all Centrex customers.

C. Direct Inward Dialing (DID) Service

1. Background

DID is a service which allows a caller to call directly to a telephone number which is on a PBX or telephone answering service (TAS) or similar service without having to be answered by an attendant. This is done by an arrangement in the central office serving the PBX or TAS customer which sends the call from the local network to the PBX or TAS dial switching or number identifying equipment, which then relays it to the appropriate telephone set. The DID capability is also a part of Centrex service, however in that case the individual telephone line terminates at a "port" on Pacific's central office switching machine rather than on equipment at a user location.

During hearings in Pacific's last general rate proceeding Telephone Answering Services of California (TASC) objected to Pacific's present DID rate structure which bases charges on the volume of telephone numbers without a separate trunk charge. TASC argued that because call holding times for TAS are shorter than they are for PBX systems where full length conversations transpire, TAS customers require fewer trunks for a given quantity of telephone numbers than PBX customers do, and so impose less trunking costs on the utility. In effect, they argued, they are being charged for trunks they do not use. TASC therefore urged disaggregation of charges for DID numbers and trunks. In D.84-06-111 we found that TASC had not sustained its burden of proving the unreasonableness of Pacific's DID rates but at Ordering Paragraph 16.c. we ordered Pacific to conduct and file in the present general rate proceeding, a study of DID costs and, if appropriate, a rate proposal addressing these issues.

2. Pacific's Study and Proposal

Pacific conducted the study (Exhibit 264) and determined that its DID rate design should be changed. It proposes three changes; the first two essentially do away with the present declining block pricing by decreasing the charge for the first two blocks of 100 DID station numbers from $200 to $60, and increasing the charge for additional blocks of 100 DID station numbers from $35 to $60, making each block the same. The third change is to add a trunk-sensitive monthly circuit termination rate element of $8 per trunk. The effect of such a change, of course, is to reduce the rates for users of fewer than 200 station numbers but to increase rates for the largest customers of DID service such as large PBX users. Pacific claims that its new rate structure strikes a more equitable balance between the PBX and telephone answering service markets than the existing rate structure. The annual revenue effect for the 1986 test year is an additional $38,000.

3. Positions of Other Parties

DRA reviewed Pacific's study and concluded that the cost study is inadequate in several respects. The review finds that rates for trunks and numbers should be separated, but DRA's Shantz cautions that without an adequate cost study it is not appropriate to reduce the aggregate customer billing from DID service because of its similarity, when used in conjunction with a PBX, to Centrex service. Nonetheless, Shantz testified that DRA supports Pacific's proposed rate revisions and recommends their adoption because they address the need for restructured rates and result in a small change in aggregate customer billing.

TASC generally supports the Pacific rate proposal. However, pointing out that Pacific's work papers show a revenue to cost (R/C) ratio of 1.25 for the proposed DID station number charge, while Centrex is proposed to be priced at 1.0, TASC argues that since these services compete, they should both be priced at the same 1.0 R/C ratio. Further, TASC asserts that since the trunk charge proposal will have differing effects on customers depending on how long their calls tend to be, the fairest way to price it is to adopt the same R/C ratio for it as for the station number charge.

In addition TASC requests that we do away with Pacific's Basic Termination Charge (BTC) which is assessed for terminating service prior to the 3-year minimum period provided for in the DID tariff. It is set at $6,500 per 100 numbers for the first 200 DID numbers and $1100 per 100 numbers thereafter. TASC points out that if Pacific's new rate proposal is adopted and a hypothetical TAS customer with 400 DID numbers, paying a recurring charge of $240 per month, discontinues service after one year that subscriber will be obligated to pay Pacific 2/3 of $15,200 for the 400 numbers, or $10,133. However, if the customer simply continues paying the monthly payments for the next 24 months and leaves the service idle, its payments will total only $5,760. TASC claims that the nonrecurring charge at the time of installation is supposed to cover both installation and removal charges, and questions what cost is left that requires this payment. Further, TASC asserts that there is no similar charge for Pacific's Centrex service.

FEA claim they generally support the unbundling of rate elements, but oppose Pacific's proposed $8 per month trunk termination charge, claiming that it would cause rate shock when considered in conjunction with the increased PBX trunk rate Pacific has proposed. This concern is based on the assumption that we will adopt Pacific's proposed $16 measured trunk rate.

CBCHA/TCA, oppose adoption of Pacific's DID rate design. They assert that while small PBX customers would receive a rate reduction under the proposal large customers would be unfairly burdened with increases of up to 100%. They argue that these rates will have an anticompetitive impact on PBX service, that Pacific's own cost study shows that the rates exceed costs by 156% to 176%, but that this cost study is flawed and unreliable. Selwyn expressed several concerns about the cost study including lack of detail as to assumptions Pacific employed in undertaking the study including what type of central office equipment it examined, what level of utilization of the central processor it assumed and why, how consistent these costs are with those parallel costs developed for Centrex - e.g., allocation of fixed central office processor capacity costs, and the lack of consideration given to economies of scale. Selwyn concludes that Pacific's cost study probably overstates costs, but that it would be fair to set rates at precisely the level of cost that the cost study shows. He finds this to be $25 per 100 DID station numbers for all 100 number blocks and $8 per DID trunk.

Pacific cites the rebuttal testimony of Scholl (Exhibit 402) as well as other exhibits to defend against almost every item of criticism leveled at its cost study by DRA and Selwyn.

4. Discussion

None of the criticism of Pacific's DID pricing proposal disputes the need for disaggregating rates to provide a separate trunk sensitive circuit termination rate element. Only FEA object to the amount Pacific proposes to charge, on the ground that this rate in conjunction with the $16 measured trunk rate Pacific proposes for PBX service would produce rate shock.

In fact, this decision adopts a lower measured trunk rate of $12.25. When added to the termination charge the new rate per trunk would be $20.25. The present rate, which has no termination charge, is $8.25. However, this comparison does not consider the monthly reduction proposed for the first 200 DID station numbers. If we accept Pacific's estimate that on average one trunk will support 18 PBX numbers (and 30 TAS numbers), then a PBX customer would pay about $342.75 for the first 200 DID station numbers under the new proposal with the newly adopted PBX trunk rate, as compared with $490.75 under the present rate design. On the other hand, the second 200 numbers would cost the same $342.75 under the proposed plan, but only $160.75 under the present rate design. Thus, the average PBX customer will begin to see a slight ($34.00) rate disadvantage under the new proposal at the 400 station number level, and that disadvantage will average about $182 or 107% for each additional 200 DID station numbers.

Comparing just the DID rates rather than combined with the PBX trunk rate, shows that charges under the new rates do not exceed charges under the present rates until a customer reaches the station number level of about 500, at which point DID charges under the proposed rates are about $17 higher per month than under the present rates. From that point on the disparity continues to grow as the old rates increase by $35 per month per 100 numbers while the new rates increase by about $104 per 100 numbers, with rates under the new proposal becoming double that under the present design at about 1,900 lines.

These calculations indicate to us that the rate increases to large PBX users under this proposal do not outweigh the more equitable treatment of TAS users provided by a separate trunk sensitive rate element for DID service. TASC, DRA, and CBCHA/TCA agree that it is appropriate to adopt this element, and we agree.

Although there are some questions about the accuracy of data Pacific relied upon in arriving at its costs, we are confused by DRA's criticism of the major features of Pacific's DID cost study. For example, DRA's witness Singh criticizes Pacific because its estimates of investments and expenses come from Pacific's Results of Operation report which is based on tops-down, not bottoms-up study methodology. He also faults Pacific for allocating these investments and expenses to DID services using Functional Accounting methodology. Singh does not criticize the results of Pacific's tops-down studies. We do not know if DRA finds that they are, in fact, inadequate or not. Likewise, even assuming Pacific did use Functional Accounting, Singh's only comment is that it "has not been recognized by this Commission as a proper method of accounting for rate making purposes." We do not know whether he views it as a reasonable method or not. In any case, Pacific argues that a bottoms-up study was not required for DID, and Scholl adds that Pacific did not derive unit investment costs from its books of account, but relied on current prices charged by the manufacturer to determine costs (apparently costs for switching equipment). Further, Pacific is correct about cost studies. Ordering Paragraph 16 d. of D.84-06-111 only ordered bottoms-up studies for service categories where Pacific "proposes rate increases substantially greater in percentage terms than the proposed increase in total revenues."

We do agree with DRA's uncontroverted claim that the variables used in the SCIS model which was used to assign costs between touchtone and dial pulse were not demonstrated to be valid. We are further concerned about the issue raised by Selwyn regarding the comparability of cost assignment between Centrex and DID, since DID is a component of a service used in competition with Centrex. Scholl asserts in his rebuttal testimony (Exhibit 402) that costs were assigned to both in the same way, but cites no documentation which demonstrates this.

Since we find it reasonable to adopt a disaggregated rate element for the trunk component, we must now arrive at a reasonable rate for station numbers. Pacific's cost study shows that there is no basis for differentiating between the first two blocks of 100 numbers and subsequent blocks. Therefore, we will adopt a rate which treats each block the same. We are not confident enough in the accuracy of Pacific's cost study, however, to adopt the $60 rate it suggests. We are not certain how Pacific has allocated similar costs to DID and to Centrex. A lower rate would more certainly protect PBX customers from rates set too high when considered in relationship to competitive Centrex service rates.

It appears to us that TASC's recommendation of setting this rate at a R/C ratio of 1.0, based on Pacific's cost study is a reasonable means of achieving these goals. The appropriate rate thus defined is $45 per each 100 DID station numbers rather than the $60 Pacific has proposed. Charges reach the same amount under this rate design and under the present rates at about 600 lines. Rates do not double in comparison to present rates until a customer reaches nearly 2,900 lines. This change along with the adopted trunk sensitive termination rate element will reduce Pacific's proposed DID revenues by $1.870 million.

We are sympathetic with TASC's request that the termination of service charge for DID be removed. TASC's assertions make the validity of the charge seem quite dubious. There has been no opportunity in this proceeding, however, for Pacific to provide its rationale for continuing the charge. Therefore, we will take no action on the TASC request, but we will order Pacific to address the reasonableness of continuing this charge, including a showing of costs which it is designed to cover, in its next general rate proceeding.

D. Coin Services

1. Coin Telephone Rates

Pacific proposes no change in its local coin telephone rates; however, TURN's witness Siegel proposes that the rates be reduced from $.20 to $.10, based on the results of the cost study presented by a TURN witness in Pacific's last general rate proceeding. We considered that study and adopted the present rate in D.84-06-111. No new evidence convinces us that we should now revert to the coin rate level which we adopted in 1952. We also find no basis in the record for adopting TURN's alternative recommendation that the coin rate be reduced to $.15. We will deny TURN's request.

2. Semi-Public Coin Service

a. The Service and Pacific's Proposal

As Sullivan explained on cross examination, semi-public coin service is a service provided to a business customer which allows the features of a regular business service, including directory listing, but gives the customer a coin telephone for the use of employees, the transient public or the like which assures that the caller pays for his or her own call. Such service is common in dormitories and sorority and fraternity houses as well as business locations. Exhibit 287 shows that Pacific projected 77,553 semi-public in-service access lines in 1986.

Pacific proposes increasing its access rate for semi-public coin service by 55% from $20 to $31. It also proposes changing extended area service (EAS) and Special Rate Area (SRA) rate increments for semi-public rates and increasing the service connection charge by 37.14% from $175 to $240. Sullivan testified that Pacific wishes to relate its price more closely to the cost of providing the service, and also stated Pacific's position that this service should cover its own costs. In addition to these rate increases Pacific proposes that it be entitled to require a deposit equal to the replacement cost of the instrument and associated equipment when service is requested in locations Pacific deems to be not secure. The proposed tariff gives examples such as construction sites and temporary structures. Sullivan testified that the purpose of this provision is to assure that general ratepayers are not burdened with the cost of lost equipment. He stated that he believed the charge would be in the range of $400 to $500 and that Pacific did not expect it to diminish the ordering of semi-public service. There appears to be no offset for this expense savings in any cost calculation.

Cost witness Scholl's original testimony (Exhibit 260) shows a revenue to cost ratio for monthly service at present rates, based on average historical cost, of .5 and for service connection of .4. Scholl's later testimony, Exhibit 261, shows that in order to reflect the results of operations this Commission actually adopted in D.86-01-026 the costs of these services should be reduced by the appropriate scaling factor. In the case of the recurring charge, the factor is 90%. It is 93% for the nonrecurring charge. Thus Pacific acknowledges that its revenue to cost ratios overstate the amount by which average historical costs exceed revenues by 10% and 7% respectively.

b. Positions of Other Parties

DRA advocates applying the same percentage adjustment for the access rate for this service that is adopted for recurring business and residence services. On behalf of DRA Shantz testified that DRA opposes any change in EAS rates on the grounds that Pacific has not provided any basis for increasing EAS, that these increments are generally intended to represent the loss in message toll revenue that results when message toll routes are converted to local (EAS) routes and that little attention has been given to sustaining the relationship between the EAS increments and the message toll rates in recent years. While DRA does not specifically address the extension of EAS or SRA rate increments to services to which they have not previously been applied, we take this statement to indicate that DRA contends that such extension should be denied except upon a specific showing of the relationship between the increments and message toll losses.

c. Discussion

If it is the case that we need to reset EAS rates so that they better reflect the difference between message tolls previously collected and local rates, then we will do so when we are presented with evidence of the problem. However, since we are not adopting the toll zone consolidation Pacific proposes it does not appear that any change in EAS or SRA rates is necessary at this time. Therefore, we will not grant Pacific's proposal to change EAS and SRA rate increments for semi-public rates.

Pacific's cost evidence indicates that access costs would match revenue if a 45% increase were granted, yet it asks for a 55% increase. This service is not one which we consider to be primarily a basic service, although it may be a substitute for basic service for many users. Because it is not a basic service it is reasonable that revenues cover costs. On the other hand, the service is not the sort from which the subscriber gains any direct benefit. We are therefore reluctant to permit rates which might discourage subscribers from continuing to provide this service to its employees or residents who rely upon it. This is not a service which ought to subsidize basic service rates. Therefore, we will permit a rate increase of 45%, which raises access rates from $20 to $29. Based on the same rationale, we find Pacific's proposal to increase the service charge to $240 to be appropriate, and will adopt it.

We are sympathetic to Pacific's desire to prevent burdening general ratepayers with costs for equipment loss. Requiring a deposit from certain types of customers may be a reasonable way of accomplishing this end. However, the language of Pacific's proposed tariff is too broad. It could be used discriminatorily. It could have been drafted in more specific terms. Had Pacific chosen to do so, we may have found it acceptable, but in the form presented it must be rejected. Furthermore, while the cost saving is likely to be small, if Pacific chooses to propose such a provision in a future proceeding, it should at least address that cost savings.

The rate changes we adopt for Semi-public Coin Telephones, including expense savings, provide a test year revenue increase of $9.005 million.

3. Customer-Owned Pay Telephone (COPT)

a. Pacific's Proposal

A COPT telephone is similar to a semi-public telephone except that the COPT customer owns and operates the telephone instrument, the proceeds of the coin box belong to the COPT customer and the service is not confined to business premises. Exhibit 287 shows a Pacific projection of about 4,500 COPT access lines in service for 1986. Pacific proposes increasing measured access line rates for COPT by 29.4% from $17 to $22, and flat access line rates from present rates between $27 and $43 to new rates between $32 and $48, and increasing the allocation of message units for the initial minute of measured service by 5% from $.06 to $.063. Sullivan changed this message unit figure in his rebuttal testimony to an 11.7% increase from $.06 to $.067. Subsequent minutes remain at $.01. Additionally Pacific proposes increasing the installation charge from $110 to $175 and the charge for converted service from $75 to $115.

Sullivan described these proposed rates as an attempt to achieve movement toward coverage of costs and also testified that the proposed access rate increases are meant to mirror the percentage changes Pacific is proposing for business line access rates. Sullivan testified that this is consistent with Ordering Paragraph 11 of D.85-11-057 which states that rates and charges for COPT service should be "subject to adjustment in the rate design phase of Application (A.) 85-01-034 only for the purpose of maintaining consistency with rates for comparable services." He further testified that his originally proposed rate for an increase in the initial message unit is meant to reflect corresponding proposed changes in MTS rates and thus to maintain the present relationship between toll rates from coin phones and toll rates from dial stations. The change to this rate that he proposed on rebuttal is to account for the increase in message unit charges for business services which adjusts for Pacific's proposed alternative rate for Centrex service. He also testified about Exhibit 301 which projects that the new rates would cause a repression rate of 15% in station growth due to nonrecurring rate increases and 5% due to recurring rate increases, producing an overall revenue increase of about $226,000 or about 13%, over the baseline total at current rates of about $1,719,000.

Scholl testified that his service cost studies did not address COPT service because COPT was not yet a Pacific offering at the time his cost exhibits were being prepared.

b. Positions of Other Parties

DRA again advocates applying the same percentage adjustment to recurring rates for this service that is adopted for business services, and the same lower rate increase for the installation charge that is advocates for all service connection charges. Shantz testified that DRA does not propose a change for the $75 charge for conversion of service.

California Payphone Association (CPA), whose 35 members conduct private payphone businesses in California, presented the testimony of its President, John Cunningham, who is also an officer of a company which owns, installs, and operates private payphones in Pacific's service area. He testified that at present rates the COPT operator must generate revenues of $349 per month on an annual basis in order to stay in business, assuming that the COPT operator charges the maximum allowable $.25 per local call, that capital costs per COPT are $2,500 with a 5-year depreciation life for installation, that 20% of the operating profit will be paid as a commission to the location owner or manager, that operating and maintenance expenses plus administrative and general expenses for the operator are about $55 per month per station, and that a 14% annual return on investment is the minimum reasonable return.

He claims that fewer than 15% of the public telephones in Pacific's service area can generate that much revenue and that COPT operators must concentrate their services in these high usage market locations. At Pacific's proposed rates (without Sullivan's last increase in the initial minute rate) Cunningham estimates that the return from a COPT generating $349 per month would be reduced to 11.8% and that the COPT would have to generate $365 per month to produce a 14% return, thereby reducing even further the selection of COPT locations. To this he adds other inherent competitive disadvantages in COPT operations which he says lead him to conclude that the proposed rate increase could lead to an end to the long-term viability of the private pay telephone market in California. These unquantified disadvantages include the COPT's "need" to charge the allowable maximum of $.25 rather than Pacific's $.20 rate, the "need" of COPTs to limit calls to 15 minutes, the COPT's inability to derive much revenue from nonlocal calls, and its inability to receive any share of "nonsent paid toll revenues" or access service revenues for interLATA calls made from COPT stations. We put the word "need" in quotation marks because these practices are not tariff requirements, but business decisions.

CPA asserts that the increased revenue Pacific expects to generate from its proposed COPT rate changes is miniscule by PacBell's standards, but very ominous to the small businesses which comprise CPA's membership. Although there are no cost studies specifically addressing COPT in this record, CPA states that the information about coin services in the cost studies Pacific sponsored show revenues approximately equal to cost for coin access lines, local usage and sent-paid toll. CPA goes on to claim that there is insufficient detail to identify not-sent-paid (i.e., credit card or operator assisted) toll revenues and access charge revenues related to coin service. Citing the analogous 2.8 revenue to cost ratio for intraLATA MTS set out in Scholl's testimony, Exhibit 260, CPA claims that these two revenue categories are among the most profitable to PacBell, and concludes that Pacific's coin services as a general class produce revenues well in excess of costs. Based on this conclusion CPA argues that there is no basis in the record for presuming that subscribers to

COPT do not, likewise, pay rates which fully cover the costs of those services which PacBell provides to them.

CPA adds that D.85-11-057 does not mandate a rate adjustment for COPT in this proceeding, it merely "place[s] a ceiling on the degree to which COPT service rates might be adjusted in this proceeding" (emphasis in original). Further, CPA points out that the present monthly rate for measured COPT service was developed based on Pacific's own cost estimates and the cost study which provided the firmest basis for the COPT line rate we adopted is the cost study for a measured business line which was prepared by Pacific and sponsored by Scholl in this current rate proceeding. (See D.85-11-057, mimeo. at 45-50, Finding 24, at 114; D.86-01-059, mimeo. at 4.) CPA concludes that our prior decision does not absolve Pacific of its obligation to provide adequate evidentiary support for these rate change proposals.

CPA argues that we should deny the COPT increases Pacific seeks because the competitive inroads private operators have made into the public telephone services market are small and their profit margins are already narrow. It adds that adoption will imperil the vitality and the future of the private payphone industry as well as the services which that industry could offer to the general public.

c. Discussion

We stated our priorities for the setting of COPT rates quite clearly in D.85-11-057. We said:

> "We need not evaluate the business prospects of COPT operators in detail, because we conclude that the viability of the business potential for COPT operators is at most a consideration of secondary importance in our setting rates for COPT service. Our primary concerns are to assure that COPT rates are set at levels which do not seriously impair Pacific's net revenues and are reasonable in relation to Pacific's service costs and its rates for comparable services. We agree with TURN that if,

> having analyzed and weighed these relevant factors, we adopt rates which offer only a narrow window of business opportunity in especially high volume locales, that may disappoint prospective entrepreneurs but will nonetheless serve the interests of the general body of ratepayers. If the adopted rates are low enough to foster widespread COPT operations in California, that will be so much the better. Thus, in setting rates for COPT service, we shall direct our attention to the interests of the general body of ratepayers rather than to those of the potential COPT operator. On the other hand, we recognize that Pacific will be a competitor with COPT operators as well as a provider of services to them. We therefore intend to assure that the rate structure and rate levels adopted for COPT service do not unduly or unnecessarily discriminate against the COPT operator in relation to Pacific's own pay telephone services." (D.85-11-057, mimeo. at 34-35.)

Keeping this in mind we evaluated the various proposals before us. Pacific's proposal for the access line rate was based on its costs of providing measured business (1MB) lines, which have cost characteristics similar to COPT lines. The accuracy of this proposal was corroborated during the hearing in that proceeding, with one slight adjustment, by Scholl based on cost study data which had been prepared for, but not yet presented in, the present proceeding. We further adjusted Pacific's figure to account for the appropriate rate of return, the proper attribution of the interstate Customer Access Line Charge (CALC), the adopted revenue requirement, the value of the 411 directory assistance allowance included in the COPT service, and continuing administrative costs. We found that the cost of an average call was very close to the then-effective ZUM Zone 1 rates, and concluded that simplicity of rate design, ease of future adjustment, and consistency with Pacific's service costs as well as alleviation of any incentive for customers to connect COPTs improperly to ordinary business lines by setting this rate at the same level as those business lines, made it reasonable to set the rates for local COPT calls at the ZUM Zone 1 rates as DRA recommended.

Since no new cost evidence has been presented and the amount of time since we authorized Pacific's present COPT rates is relatively short, we assume that the cost of an average COPT call is still very close to the ZUM Zone 1 rate. The advantages we cited in D.85-11-057 for using this same rate for COPT service still hold true. At the time we adopted the present COPT rates residence and business usage rates were the same for ZUM Zone 1. That fact is not changed by this decision. Since COPT costs have characteristics similar to measured business lines it is appropriate for Pacific's COPT rates to continue to reflect those rates. Therefore, Pacific's COPT access rates should be increased by the same percentage as business access rates and COPT usage rates should remain at present levels.

We see no reason in this record to deviate from the across-the-board percentage increase for installation and repair that we have adopted for business and residence services. Pacific should adopt the same increase. Furthermore, since conversion of service is just as "labor intensive," as DRA put it, as installation or repair, that cost should reasonably be expected to increase by the same percentage. Therefore, we will permit Pacific to adopt the same increase factor for conversion as for new installation.

Clearly these rate changes will have less impact on the COPT operators than the changes Pacific proposes. The impact that the changes do cause are reasonably related to costs and protect the general ratepayer from subsidizing this service. While this decision may reduce their rate of return to something less than 14%, and perhaps cause them to reconsider contemplated new services, it is certain that these changes will not deprive CPA members of their ability to operate.

The COPT rates and charges we adopt in this decision will produce a $0.019 million revenue increase for the test year.

IV. Incidental Services

A. Nonpublished Service

Pacific presently provides nonpublished service to its customers for $.30 per month. This service allows a customer to be unlisted in both the telephone directory and with directory assistance. Sullivan testified that Pacific's market studies show that this service is grossly underpriced in relationship to the value many customers place on it. Based on this he recommends increasing the monthly rate by 83.33% to $.55.

Additionally, Sullivan described a new service which Pacific proposes to call Directory Assistance Listing (DAL). This service permits the customer to be unlisted in the telephone directory, but includes that customer's name, address, and telephone number in the Directory Assistance Service data base, so that a caller who knows the name and location of the customer can get his or her number from Directory Assistance, but the customer can avoid random solicitations and nuisance calls. Pacific proposes pricing this service at $.30 per month. Taken together Pacific projects that these services as proposed will generate an additional $7.443 million in the test year.

DRA supports both these proposals but argues that the rates for nonpublished service should remain at their present $.30 level and that rates for DAL should be set at half that price, $.15 per month. DRA's rationale for its rate proposals is Shantz' testimony that it is inappropriate to increase rates for this service on a value of service basis in a period of declining overall costs for Pacific. DRA calculates that its rate proposal results in a revenue <u>decrease</u> of about $113,000 to Pacific.

TURN also objects to any increase for nonpublished service, arguing that ratepayers have a right to protect their privacy and should not have the cost of this privacy nearly doubled.

We believe that Pacific's new offering is a useful addition to its nonpublished service offering, and will adopt it. Some customers object to paying anything over cost for unpublished service. We recognize that many people believe it is important to keep their numbers private, but we think this is the sort of nonessential service which ought to continue to provide some subsidy to basic service. On the other hand, we agree with DRA that it is inappropriate to increase the rates for existing nonpublished service when the rates are already set well above costs.

It seems intuitively likely that DAL service would have higher per-unit costs than nonpublished service, and its costs ought to be set to reflect that fact. However, we can find nothing in the record to verify this, and both Pacific and DRA endorse setting DAL rates at half the nonpublished service rates. We will defer to their positions. Since we have kept the $.30 rate level for nonpublished service, we will also adopt DRA's proposed $.15 level for DAL service. The small revenue reduction which results from DRA's proposal is too small to have a noticeable effect on the overall revenue contribution of these services.

B. <u>Touchtone Service</u>

Pacific's initial proposal suggests no change in its Touchtone service rates. In his rebuttal testimony, however, Sullivan proposed reducing rates for three services if the revenue requirement we adopt in this proceeding is lower than what Pacific proposed. Making Touchtone a standard rather than an optional offering was the third of these proposed rate changes. Sullivan points out that since the Touchtone function is necessary to many new telephone products and services, such treatment would guarantee the broadest possible availability of new offerings to Pacific Bell customers. Pacific's closing brief adds that Touchtone service generates approximately $80 million in annual revenues, but fails to cite any reference in the record which yields such information.

DRA does not comment on this proposal; however, TURN does. TURN recites the arguments it made in Pacific's previous general rate proceeding for the elimination of additional charges for Touchtone service. It states that Touchtone service automatically becomes available, without any extra cost to Pacific, in areas where Pacific installs electronic switches; that calls made with Touchtone should cost less than rotary-dialed calls due to shorter set-up times; and that the overwhelming majority of residential customers now have Touchtone phones, so that this former luxury is now a near-universal element of basic service. TURN urges that such a rate change is an equitable alternative for spreading part of the rate reductions which it contends are due residential customers.

In the past it has been our position that Touchtone service was an appropriate demarcation line between basic service and access to the optional features and information services which ought to cover their own costs and, where possible, provide a contribution to basic service. The Touchtone rates have remained at their current levels, $1.20 for residence lines and $1.70 for business lines, since they were first authorized in 1967. Of course, they have become increasingly more useful since that time as the number of services available through them has continued to increase.

It is reasonable to argue that Touchtone should be offered at no premium since its broad availability does not result in extra direct costs to Pacific, but might encourage more customers to buy additional optional services which are priced to subsidize basic service. We are not averse to considering the elimination of extra charges for Touchtone service. However, we cannot do so in this proceeding since Pacific's cost and revenue witness did not address this particular service and we have no evidence of the revenue impact of such a change. The statement in Pacific's closing brief is not evidence. Even if this statement could be regarded as evidence we note that Pacific projected Touchtone revenues of about $107 million in 1984, in contrast to the $80 million figure which Pacific now claims, apparently as a 1986 figure. (See D.84-06-111, mimeo. at p. 201.) This large discrepancy alone makes reliance on Pacific's unsubstantiated claim unreasonable. For these reasons we will leave Pacific's Touchtone rates as-is for the present, but we will direct Pacific to provide cost and revenue data for Touchtone service in the supplementary rate design proceedings.

C. Verification Interrupt

This is a service by which toll operators may verify that a line is actually busy at the request of a calling party. Sullivan testified that Pacific wishes to increase the charge from $.50 to $.75 in order to bring the rates more in line with the cost of handling this type of service. DRA opposes the increase.

Scholl's testimony, Exhibit 260, does not specifically indicate the cost of providing Verification Interrupt service. It divides operator services between two categories, directory assistance (DA) and "other." In this "other" subcategory, to which Verification Interrupt service would belong, Scholl shows an overall revenue to cost ratio of 0.7. Applying the 82% adjustment factor to the costs for this subcategory brings that ratio to about 0.9. In Exhibit 351 Shantz points out that Pacific has projected an annual revenue increase of $247,000 for this service in the test year based on calculations using a unit cost of $.27, and assuming adoption of the proposed rate increase. Shantz argues that this unit cost figure is well below the present rate already and does not seem to justify a further increase. We agree. There is no clear basis in this record for raising the Verification Interrupt rate. We will leave it as-is.

D. Remote Call Forwarding

Remote Call Forwarding (RCF) is an optional service allowing customers a local telephone number identity in a remote location without actually maintaining an office there. Incoming calls to this remote number are automatically forwarded to the telephone number where the customer is actually located. The calling party is billed for the call to this remote telephone number, while the subscribing customer is billed for the remaining portion.

The present monthly rate for this service is $18 per access path. Pacific proposes to retain the same rate for initial access paths, but to reduce the charge for the second and third access paths to $10 and to reduce the charge for the fourth and further access paths to $5. Sullivan testified that such pricing would produce usage stimulation thereby producing optimum revenue. He added that this service is a partial substitute for FEX. Despite the rate reduction, Pacific projects a revenue gain of $1.143 million with this rate change due to the growth it estimates will take place in RCF access paths.

DRA opposes any change in RCF rates, pointing out that the revenue gain Pacific projects is the result of its proposed limitation on Foreign Exchange Service to existing customers, which DRA also opposes. DRA also opposes the proposal on the ground that RCF is a type of basic exchange service and that it would be improper to permit a decrease in this rate if we are adopting increases in other basic exchange service rates. Finally, DRA also objects to this proposal because RCF was one of the services which was the subject of our marketing abuse findings. DRA argues that we should not permit changes in rate structures for any such service "until the effects of the unethical and abusive marketing activities have been corrected and eliminated."

We agree with DRA that RCF rates should not be reduced in this decision. The basis for Pacific's projection of a revenue gain is the grandfathering of its FEX service. Elsewhere in this decision we explain why that grandfathering proposal is not reasonable. This being so, the revenue effect of Pacific's proposed changes in RCF rates is not likely to be the increase which it has projected. We will authorize no change in RCF rates.

V. Message Toll Service (MTS) and MTS-Related Services

A. Introduction

Pacific proposes various rate changes for Message Toll Service (MTS) and related services. The related services are Call Bonus Wide Area, Community Calling Plans, Circle Calling, Optional Calling Measured Service (OCMS), Wide Area Telephone Service (WATS), and 800 Service. Pacific says that the MTS and MTS-related services rate design which it proposes will produce a test year revenue decrease of $51.718 million for these services. With parentheses denoting negative revenue effects, this breaks down as follows:

MTS:	($36.719 million)
Call Bonus Wide Area:	(5.521 million)
Community Calling:	0.661 million
Circle Calling:	(1.327 million)
OCMS:	0.739 million
WATS:	1.516 million
800 Service:	(11.067 million)

DRA's revenue neutral proposal for the same time frame would decrease revenues from this source by a slightly larger amount, $54.010 million. It breaks down as follows:

MTS:	($46.860 million)
Call Bonus Wide Area:	(0.568 million)
Community Calling:	(2.719 million)
Circle Calling:	(2.925 million)
OCMS:	(0.460 million)
WATS:	(0.478 million)
800 Service:	0.0 million

In DRA's alternative rate design to reflect its later revenue requirement proposal, the portion for MTS and MTS-related services comes to a negative $166.212 million, and in the rate design proposal in its Concurrent Opening Brief, which is based on the total revenue reduction of $181.557 million, (which includes DRA's calculations for a revenue neutral outcome plus an additional revenue requirement decrease of $79.6 million to reflect the direct assignment of closed end WATS costs on January 1, 1987 as shown in DRA's latest proposal in the Results of Operations Phase) DRA proposes reducing MTS and MTS-related services by only $33.295 million. The details of Pacific's proposal as well as DRA's alternatives and the suggestions and comments of other parties are addressed below.

B. Message Toll Service (MTS)

1. Pacific's Rate Band Proposal

Pacific proposes re-pricing and simplifying its MTS service. Under the plan intraLATA message toll rate bands would be reduced from seventeen to four. Pacific would consolidate the first two of these bands into one larger zone encompassing the area from beyond the 8-mile local calling area up to 16 miles. (Pacific proposes the same change in major metropolitan areas where these two zones are known as ZUM Zones 2 and 3 and their rates are set below toll rates to recognize the differences in costs and calling needs in highly urbanized areas. Pacific's plan for the ZUM zone consolidation is discussed along with other ZUM proposals below.)

The remaining 15 message toll rate bands, which account for calls in mileage increments from 16+ miles up to 245 miles, with the last band being for calls of over 245 miles, would be consolidated into three bands: 16+ to 30 miles, 30+ to 50 miles, and over 50 miles. Pacific then proposes setting rates for its consolidated first rate band at $.59 for a five-minute call. This contrasts with the present rate of $.49 for a five-minute call in the 9-12 mile mileage band, a 20% increase, and $.64 for a five-minute call in the 13-16 mile mileage band, an 8% decrease. Additionally, Pacific proposes rate decreases in the consolidated longer mileage bands, with the most expensive five-minute call decreasing from $2.42 to $1.50. However, these rates would still result in a rate increase for one more of the present rate bands, the 16+ to 20 mile band, by about 12%. Pacific projects the overall test year revenue effect of these changes to be a reduction of $36.719 million.

Pacific's Scholl points out that the proposed MTS rate restructuring still results in revenues which exceed costs of service for every mileage band although the revenue to cost ratio will be greater for short-haul mileage bands and less for the longer-haul bands. He adds that the new rate design would bring these ratios into a much tighter range. (Exhibit 402, p. 137.) In other words, the profit margins would become more similar among the bands. Pacific's Sullivan cites the following objectives for proposing these changes: to stimulate usage on the most profitable longer-haul routes, to protect against bypass, and to continue the revenue contribution to provide a sustainable means of sustaining the support of Residence Exchange Telephone Service. (Exhibit 283, pp. 10-11.)

Pacific adds that in the face of ever-increasing competitive pressures underpriced business services rates should be increased thereby facilitating toll-related rate decreases as a first line of defense of the basic residence service subsidy.

Further, Pacific argues that longer-haul calls tend to have the highest revenue-to-cost ratios and therefore are most vulnerable to bypass. It makes sense, adds Pacific, to focus rate reductions on such calls, partly because the per-mile costs of such calls are less than for shorter-haul calls.

Finally, Pacific suggests that if further revenue requirement reductions are required, MTS services should be given first priority for such reductions, and those (longer-haul) mileage bands with the highest revenue to cost ratios should be reduced first.

2. DRA's Rate Band Proposal

DRA's witness, Karen L. Miller, testified about DRA's revenue neutral rate design proposal, which she designed based on the instruction of Project and Program Supervisor, Shantz, that the level of revenue decrease for these services should be about $50 million for the test year.

Miller testified that DRA proposes reducing the number of MTS rate bands from 17 to 9 by combining all the rate bands from 71 miles and greater into one band, consolidating the message toll coin rate bands to be consistent with this regular MTS rate band proposal, and reducing the rates for the initial minute of service for each of these remaining bands. Miller testified that DRA's proposal would reduce rates in each rate band by $.01 out to 71+ miles where, because the rest of the bands are consolidated, the rate reduction effectively increases with distance. She claims that consolidation of these longest-haul rate bands makes sense because, as a result of divestiture traffic over these routes has become small compared to the shorter-haul rate bands.

Shantz testified that it is DRA's position that these intraLATA message toll-type services should reflect the shift in revenue requirement brought about by implementation of DRA's proposed intraLATA SPF to SLU transition and the direct assignment of costs for closed end intraLATA WATS which we adopted in

D.87-12-067. Shantz also cautioned Commission against "dipping into the toll pot...in lieu of raising basic rates." He added, "[W]e must be very careful that the subsidy be made smaller so that if there is intraLATA competition authorized and the golden egg completely disappears you do not suddenly see very large increases in basic rates."

3. US Sprint's Position

US Sprint Communications Company (US Sprint) supports DRA's MTS rate design because it reduces rates in all mileage bands, and allows end users to share approximately equally in the benefits for reduced intraLATA toll rates, and because the DRA proposed rate design more closely reflects cost causation.

US Sprint asks us to reject Pacific's proposed revisions to MTS rates. It claims that the proposal has no basis in cost causation and is anticompetitive in that it is an attempt to position Pacific for potential intraLATA toll competition and to disadvantage potential competitors by attempting to set relatively low prices for the longer haul intraLATA toll routes which are most vulnerable to potential competition while increasing rates on short-haul intraLATA toll routes which are in Pacific's view least vulnerable to competition. US Sprint also claims that Pacific's proposal requires the users of short-haul and long-haul toll to pay disproportionate amounts in relation to the cost of service and adds that interexchange carriers (IECs) pay more to use the same facilities.

4. CBCHA/TCA's Position

In the event this Commission chooses to go forward with a rate design, CBCHA/TCA's witness Selwyn offers a proposal for ZUM[2] expansion which increases the scope of applicability of ZUM

2 Zone Usage Measurement, or ZUM is a discounted metropolitan toll plan discussed in detail in Section VI, below.

rates, and thus decreases the scope of applicability of MTS rates and the revenue from toll-related services. Selwyn proposes that we adopt Pacific's proposal to consolidate ZUM Zones 2 and 3 but that we create a new ZUM Zone 3 for the 17-30 mile distance band. He adds that he does not object to Pacific's toll rate restructuring and toll rate reductions <u>if</u> his additional ZUM zone is adopted <u>and</u> the same rate differential which exists between Pacific's proposed consolidated 9-16 mile ZUM zone and the corresponding MTS rates is maintained between the additional 17-30 mile ZUM zone and corresponding MTS rates. Selwyn states that his proposal will more appropriately reflect the lower costs associated with metropolitan area calling and the traditionally lower levels of contribution expected from these fundamentally <u>local</u> messages, and will allow Pacific to more directly target its policies at reducing the potential for uneconomic bypass of the Company's message services. He states that the potential competitive threat to long-haul and nonurban intraLATA toll routes, (which US Sprint addresses), is minimal when compared with the potential for customer-specific alternatives within the more concentrated metropolitan areas. He adds that this conversion from MTS to the 30-mile extended ZUM zone would result in a net revenue reduction, before settlements, of $250 million. He claims that this figure should be lowered to $206 million to account for net revenues derived from the additional calling which this plan would foster.

5. <u>Discussion</u>

We agree with both Pacific and DRA that a reduction in the number of MTS rate bands is appropriate. Consolidation of the longer-haul mileage bands produces the simplification which Pacific describes, and the flattening of rates for those bands should also produce usage stimulation. Scholl's Exhibit 260, Part 2, p. 7-10 shows projected MTS usage revenues exceeding costs by $740 million. It is clear that the proposals of DRA and Pacific will continue to provide a substantial contribution over cost, and it appears that the proposal of CBCHA/TCA's Selwyn would too.

Not being convinced of the equity of increasing short-haul toll so disproportionately to long-haul toll, we are not willing, however, to adopt the rate band consolidation which Pacific advocates and which CBCHA/TCA's proposal is premised upon. As we explain in our discussion of ZUM service, below, we wish to retain a distinct transitional rate zone between local service rates and toll rates. Pacific's proposal averages rates. While this is appropriate for some lower volume long-haul rate bands, it will make it more difficult to maintain ZUM rates distinct from local and toll rates, and it will not provide the users of the higher volume short-haul routes with the same level of control over their toll bills that they presently have. Such control includes choosing an optional calling plan best tailored to the customer's calling patterns as well as adjusting calling patterns. For these reasons we find Pacific's mileage zone consolidation unacceptable.

Nor are we convinced that it would be appropriate to shift revenue requirement from usage to access rates and from toll to local service in the manner proposed by CBCHA/TCA. Although much of our focus to date has been on the need to reduce toll rates to mitigate the potential for bypass, we wish to make it clear that our objective is not merely to craft a defensive strategy, but to achieve the broad range of benefits accruing from economic efficiency. Further, although the SPF-to-SLU reallocations reduce the revenue requirements attributed to toll services in particular, our concern is more generally focused on bringing all usage rates more into line with economic costs.

One sometimes forgets that even small consumers can benefit from reductions in usage rates which in large measure may offset increases in residence access line rates. In order for this to happen, however, the movement of rates toward economic costs must not be limited to those with bypass alternatives as is the

CBCHA/TCA proposal, for a preoccupation with meeting competitive threats will leave out small users. Captive consumers are also entitled to the benefits of economic pricing.

As applied specifically to this proceeding, economic efficiency favors bringing rates more in line with economic costs for all usage rates, not merely long-haul toll usage rates. Particularly high contribution margins on long-haul toll routes may open such traffic to indirect bypass pressure even in the face of our intraLATA ban and may indicate a strategic need to adjust those rates. Aside from bypass threats, however, efficiency losses--that is, foregone benefits of calling in excess of the "true" costs of that calling--as a result of call suppression due to over-priced usage rates are of equally fundamental concern.

As we have acknowledged by our adoption of an intraLATA SPF to SLU transition plan, it is important to track intraLATA toll costs and one important reason is that such information will assist in setting rates which will allow Pacific to be in a position to compete should intraLATA toll competition be permitted in the future. At the same time, as US Sprint reminds us, it is important in any future competitive environment that Pacific not have an unreasonable advantage over its competitors. DRA's proposal, both for rate band consolidation and for rates, is fair in that respect. The principal appeal of this proposal so far as it goes, however, is not the fairness of its effect on potential future competition, but the fact that this proposal cuts the number of rate zones by nearly half, retains most of the present revenue to cost ratios, and still provides a zone configuration which will promote increased usage without disadvantaging today's short-haul customers.

While CBCHA/TCA's Selwyn advocates a policy based on economic pricing of MTS service, his proposal fails to consider the broader application of economic pricing which we believe is essential. In his recommendations for ZUM service Selwyn proposes moving toward more economic pricing by reducing the usage rates for ZUM service. As we discuss in Part VI below, we find some merit in this concept. Moreover, we believe that policy should also be applied to the analogous shortest MTS rate bands, those for 9 to 12 miles and 13 to 16 miles, in recognition of the policy concerns we have described above. With the knowledge that usage within these rate bands provides a substantial contribution, but absent more precise cost data, we conclude that it is reasonable to achieve these policy goals by adopting a modification of DRA's pricing proposal.

DRA had proposed only $.01 reduction to the initial minute of MTS usage. This is but a token reduction in rates, as a 5-minute call in band 9-12 at current rates costs $.49, but would only be reduced to $.48 under DRA's proposed rates. A much more significant savings would be achieved by leaving the initial minute rate for toll bands 9-12 and 13-16 as-is and reducing the rates for additional minutes per call by $.01. Under this rate design the band 9-12 call would cost $.45.

We calculate that the application of this modest reduction in the rates for additional minutes of use will increase Pacific's revenue reduction for MTS from the $46.860 million initially projected by DRA to about $56.478 million if we adopt DRA's proposed rates for the remaining rate bands. Such a rate design provides an equitable way for Pacific to recognize the economies inherent in MTS service in the shortest, most heavily used rate bands, while benefiting all MTS users.

For all the reasons set forth we will adopt DRA's mileage zone consolidation proposal and we will adopt the rates set forth in its MTS rate band rate proposal shown in Appendix A, sheet 1 of 1 of Exhibit 348 (as amended to remedy a transcriptional error by Wilson by a letter to all parties dated February 18, 1987) except that we will retain the present rates for the initial minute of use for the 0 to 8, the 9 to 12, and the 13 to 16 mile rate bands and reduce the rates for additional minutes of use for these three rate bands by one cent.

C. Optional Toll Discount Plans

1. Pacific's Proposals

Pacific presently offers four optional calling plans which provide discounts for short-haul intraLATA usage services, both ZUM and MTS, for residence one-party customers. The first three, referred to as the Call Bonus Plans, are the Community Plan and the Circle Calling Plan which are limited to areas within 40 rate miles of the customer's home exchange and which were previously referred to as ORTS, and the group of Wide Area Plans which apply to toll calls throughout the customer's LATA. The fourth usage discount plan is called OCMS. It is also limited to a 40-mile radius of the customer's home exchange. Pacific proposes various changes to these services which it claims will result, on a test year basis, in a revenue decrease of $5.521 million for the Wide Area Plans and an overall revenue increase of $73,000 for the rest of the plans.

a. The Community Plan

For a monthly charge ranging from $3.60 to $8.55, depending on the rate mileage (9 to 40 miles), the Community Plan allows the subscriber to choose up to four communities in toll or ZUM areas within 40 miles of his or her premises (actually the home exchange or district area) to which discounted measured intraLATA toll rates plus a dollar amount allowance between $7.20 and $17.10, again varying with the rate mileage, will be applied. The customer may subscribe for double or triple allowances at comparable charges.

The mileage "Rate Steps" for both the Community Plan and the Circle Calling Plan correspond to the first six present MTS mileage bands (and the ZUM zones). The measured rate discount is 30% of the regular MTS rates.

The allowance for the Community Plan is double the flat monthly charge for the service. It is deducted from the discounted charges accumulated for calls to that exchange (or community) during the billing cycle. Thus, for example, a customer subscribing to a Community Plan for a community 18 miles from his or her exchange will be billed an additional $5.50 per month, for the 17 to 20 mile Rate Step, and will receive a 30% rate discount on calls to that community and an $11 allowance applied to those discounted charges.

Sullivan testified that Pacific proposes to keep the basic allowance at double the monthly rate and the discount at 30%, but to consolidate the Rate Steps into three steps, the last of which ranges from 31 to 50 miles, to be consistent with Pacific's proposed MTS mileage bands. Since this plan is restricted to communities listed in the tariffs and none of Pacific's routes is beyond 40 miles, this does not extend available service. Pacific also proposes deducting the allowance from the accumulated charges before the discount is applied, as is the case with Wide Area Plans. With these revisions Pacific projects a test year revenue increase of $661,000.

b. <u>The Circle Calling Plan</u>

For $4.75 per month the Circle Calling option provides the same 30% discounted measured intraLATA toll rates as the Community Plan, but without a usage allowance. However, the discount is applied to all toll/ZUM calls within the 40 miles (with certain exceptions such as where reciprocal availability is required). Sullivan testified that Pacific proposes reducing the rate for this service to $4.25 and also increasing the available radius from 40 to 50 miles to be consistent with the proposed rate band consolidation. Pacific projects a revenue decrease of $1.327 million due to these changes.

c. Optional Calling Measured Service

OCMS is a service which combines the time of day restrictions of the Wide Area Plan, below, the specific community restriction of the Community Plan, with unlimited free calling to the selected exchanges or district areas (communities) between those off-peak hours (8 p.m. and 8 a.m. on weekdays and all day Saturday and Sunday), and an allowance of one, two, or three hours of calling to that community at other times for a flat monthly rate (based on the Rate Step and time allowance selected and ranging from $4.50 to $27.00 per month). Peak hour calls to the selected communities beyond the subscribed-for allowance are charged at an overtime charge which is the same as the regular MTS rates for additional minutes. Other toll calls are charged under the regular MTS tariff. Only one OCMS service may be subscribed to for any particular service area, but the customer may subscribe to the service for several service areas. Customers in service areas where OCMS is available may also subscribe to a regular Call Bonus-Community Plan, but may not subscribe to the Circle Calling Plan.

Sullivan testified that OCMS is a form of Community Plan and stated that Pacific proposes withdrawing this service option and providing the present subscribers with Community Plan service instead. Pacific claims that withdrawal of this plan will result in a test year revenue increase of $739,000, which Sullivan seems to attribute to expense savings.

d. The Call Bonus Wide Area Plan

There are six permutations to the Call Bonus Wide Area Plan. Each is designed to provide a discount and two also provide a monetary allowance for all toll (and ZUM Zones 2 and 3) calls within the LATA so long as the calls are placed within the designated time frames. The allowance is applied to charges for calls placed within the designated time frames at undiscounted rates. There are two possible time frames, the first is for off-peak calls only. That is, calls placed between 11 p.m. and 8 a.m.

weekdays (and all day Saturday and Sunday). This is called a basic hour plan. The second is for these off-peak times plus calls placed between 12 noon and 2 p.m. and between 9 p.m. and 11 p.m. on weekdays. This is called an extended hour plan. Thus there are three possible basic hour plans and three possible extended hour plans.

Sullivan testified that less than 7% of Wide Area Plan customers subscribe to the three basic hour plans, and he therefore proposes withdrawing those three plans and converting the customers to the comparable extended hour plans. He also proposes reducing the recurring charge for these three plans to the level of the basic hour plans (to $2.00, $4.00, and $6.00, from $2.75, $4.75, and $6.75) and changing the allowance for the $6.00 plan (the only plan which includes an allowance) from $8.50 to $8.00. The percentage discounts would stay the same. Based on its rate band consolidation and rate proposals Pacific projects the revenue impact of these changes for the test year to be a $5.521 million decrease.

2. DRA's Proposals for Optional Toll Discount Plans

Miller testified that DRA opposes all of the revisions to discounted ZUM/toll rates proposed by Pacific. Her testimony expresses a general opposition based on the fact that these services were the subject of our investigation of Pacific's marketing abuses. In addition to this general opposition Miller also expresses a specific objection to changes proposed for one of the optional toll discount plans, Circle Calling. Specifically she objects to the expansion of Circle Calling to 50 miles because the service is not available to all residence customers and is not available to any business customers. Miller contends that increased benefits should, wherever possible, be directed to all ratepayers rather than a selected few.

Miller argues that Pacific's proposal to withdraw its OCMS plan must be denied because this Commission specified, at Ordering Paragraph 14.b. in D.84-06-111, in Pacific's last rate proceeding, that future decisions concerning this service would be based upon the results of Pacific's study of subscriber usage of ORTS and OCMS and the degree to which these services merely divert usage from MTS rather than generating additional usage which otherwise would not occur. She asserts that the study Pacific submitted does not fulfill the requirements of D.84-06-111 necessary to the withdrawal of OCMS.

Although DRA's revenue-neutral scenario proposes no changes in Pacific's discounted ZUM/toll services, Miller testified that the changes it proposes in Pacific's MTS rate schedule would reduce annual revenue from the Wide Area Plan by $568,000 and would reduce revenue for the rest of these services by about $6.104 million based on DRA's assumption that the measured rate discount for the Community Plan and the Circle Calling Plan would be set at 30% of the effective MTS rate schedule, as is now the case. Miller's revenue figures are also based on our adoption of the DRA proposed MTS rates which we did adopt with one modification, above.

3. <u>General Telephone's Position</u>

As a general proposition the independent telephone companies (ITCs) do not have independent rates for intraLATA toll and toll-related services. Instead, they concur with Pacific's tariffs. For that reason these tariffs are of some interest to the ITCs. General Telephone Company of California presented John Jensik to address Pacific's rate design proposals, including optional toll discount plans.

Jensik states that Pacific's proposal for call bonus plans is an improvement over the existing plans. He endorses Pacific's proposal to eliminate OCMS and says that Pacific's proposal to reduce the amount of discount for the Community Calling

Plan moves in the right direction, but he adds that General recommends withdrawing both OCMS and Community Calling, leaving Circle Calling as the only optional discounted toll plan. He bases this position on General's response to Ordering Paragraph 14.b. of D.84-06-111, which, he claims, shows that Community Calling Plans have been excessively discounted. He points out that under Pacific's present proposal Community Calling is still discounted more than Circle Calling. General argues that DRA's proposal promotes customer confusion caused by too many similar choices and retains excessive discounts for Community Plan subscribers at the expense of other customers.

4. <u>TURN's Position</u>

TURN contends that all Pacific's optional toll discount plans should be eliminated along with ZUM service and replaced with an optional flat rate metropolitan service. As explained elsewhere in this decision, we do not adopt the flat rate metropolitan plan at this time. Therefore, TURN's proposal for these other services is not addressed below.

5. <u>Discussion</u>

Pacific proposed the essential elimination of OCMS in its last rate proceeding and suggests it again here. In our decision in that last case we expressed our concern about the dwindling sources available for contribution toward the maintenance of low basic rates and our concern about the adverse impact on toll separations arising from our recognition of higher depreciation costs for Pacific, and concluded that it was necessary to diminish the preference in rate levels which has been allowed to ORTS and OCMS subscribers. We did so through the adopted rate design. However, we determined that it was inappropriate to discontinue the OCMS offering at that time. Instead, we ordered Pacific and General to study subscriber usage of both OCMS and ORTS "toward the goal of determining to what degree each of these services merely diverts usage which otherwise would be priced at higher MTS rates and to what degree each service generates additional usage which otherwise would not occur, and also to determine the effects of each service on intercompany settlements and separation of revenues." (D.84-06-111, mimeo. at p. 224.)

Pacific admits that the sample size of its study, as to Circle Calling and OCMS at least, cannot represent a valid sample. Nonetheless, Pacific asks us to authorize the discontinuance of OCMS. In his rebuttal testimony Sullivan asks that we rely on a different study which shows that 81.85% of Pacific's OCMS subscribers would benefit from being reassigned to Community Calling Plans. He also asserts that the number of OCMS plans in service has decreased from 85,000 to 35,000 in less than three years. What he does not testify about, and what we still do not know, is what part of this OCMS usage is usage diverted from MTS and what part would not exist but for the existence of OCMS. Nor do we know what effect reassignment would have on these usage patterns. That is the information we asked Pacific to provide. Since it was not provided we will not grant its request to eliminate OCMS at this time. However, we invite Pacific to provide the information we requested in D.84-06-111 in our next review of its rate design, if it wishes further consideration of this proposal.

Pacific asks that the Community Plan monthly allowance be deducted from an undiscounted sum of charges to the selected community, rather than a discounted sum as is now the case. Pacific argues that this change will not result in a rate increase as DRA claims, but only a more rapid exhaustion of the allowance. That is true, it would be worth 30% less. That would mean that subscribers who now exhaust their allowance each month would either curtail their calling or continue their same calling behavior and pay more. Pacific has not studied the impact of such possibilities. The only basis for such a move that Pacific gives is consistency with the treatment of the allowance for the Wide

Area Plan. We concur with DRA that the proposed change is inappropriate in the context of attempting to decrease MTS rates, and we are further concerned that its adoption might produce additional revenue which Pacific has not included in its revenue calculations. Therefore, we decline to adopt it. Obviously, we find even less merit in General's proposal to do away with the Community Plans altogether. General produced no evidence in this proceeding to support its proposal. The Community Plan rate design will remain unchanged.

Turning to Circle Calling, the question of whether to extend it to 50 miles is mooted by our decision not to adopt Pacific's rate band changes. There is no explanation of Pacific's proposal to decrease the monthly rate for this plan. Therefore, we will authorize no change in rate design for Circle Calling.

As with its OCMS proposal, there is some missing data in Pacific's Call Bonus Wide Area Plan proposal. It appears that reducing the choices from six to three in conjunction with the proposed rate reduction might reduce administrative costs and possibly benefit consumers. What we have not been provided, however, is information about the percentage and total number of customers who would be affected by having their allowance reduced from $8.50 to $8.00. Although it might be that the rate reduction of $.75 would compensate for that loss, the fact that this service was the subject of our marketing abuse investigation taken together with the paucity of data to support the Pacific proposal leads us to conclude that the Call Bonus Wide Area Plan rate design should remain in its present format. We will authorize no change in rate design.

Since we have adopted no changes in the Community Plan, Circle Calling, OCMS, or Call Bonus Wide Area Plan but have adopted the DRA proposal for rate bands and a modified form of its proposed usage rates, as well as decreases in ZUM rates, the revenue effect for these services will be a $11.688 million revenue reduction in the test year.

D. WATS and 800 Service

800 Service provides a reverse billing capability, so that calls of business customers to the subscribing business are charged to the business and not the customer. There are three plans. Full State and Half State plans are offered in conjunction with an IEC. The Metro plan is offered by Pacific and other local exchange carriers. Pacific's Sullivan testified that 800 service is priced above cost, but that the access and nonrecurring rate elements are priced below cost and supported by the hourly usage rate. Therefore, he recommends increasing the monthly access rate by 50% from $20 to $30 and also increasing the nonrecurring charge by 50% from $70 to $105. He further recommends reducing the Rate Group 1 (peak hour) hourly usage rates for Half State by 1.32%, from $15.20 to $15.00; for Full State by 30.23% from $21.50 to $15.00; and for Metro service by 20% from $12.50 to $10.00. Pacific would reduce the Rate Group 2 rates (off-peak hours: 9 p.m. to 9 a.m.) by the same percentages. The amounts corresponding to those above would be $6.08 to $6.00, $8.60 to $6.00, and $5.00 to $4.00. Pacific estimates that these rate changes will result in a revenue reduction of $11.067 million for the 1986 test year.

Pacific proposes rate changes in Outward WATS rates too. The proposals are for an increase from $25 to $30 in the access rate and a decrease in the first two steps of the four-step average hourly usage schedule. Thus Rate Group 1, for 0 - 5 average hours of use would be reduced by 9.09% from $11 to $10, and Rate Group 2, for 5.1 - 15 average hours of use would be reduced by 2.56% from $9.75 to $9.50. Group 3 for average hours between 15.1 and 30 would remain at $9.00 and Group 4 for average hours over 30 would remain at $8.25. Pacific would also increase nonrecurring costs by the same amount as for 800 Service. Pacific projects that these changes would result in a $1.516 million revenue increase for the test year.

On behalf of DRA, Miller expressed opposition to any change in WATS rates or 800 Service rates, on the grounds that a rate increase in MTS and related services is inappropriate in the atmosphere of an overall revenue decrease. She also states that repression due to DRA's proposed changes in MTS rates under its revenue neutral proposal would decrease annual WATS revenue by $.478 million in the test year, but would have no effect on 800 Service revenues.

In his testimony General's Jensik states that General agrees with the direction chosen by Pacific regarding MTS and ZUM rate structure, noting that the proposed rate structure is easier to understand.

Pacific's Exhibit 260 lumps 800 Service and WATS together in its illustration of recurring access cost and revenue data and nonrecurring cost and revenue data projected for the test year, showing total recurring revenues of $39 million and recurring costs of $37 million, for a $2 million contribution; and nonrecurring revenues of only $2 million as opposed to costs of $15 million, for a net contribution of ($13 million).

Usage figures are separated for each service. They show 800 Service usage revenue at $110 million with costs of $34 million for a contribution of $76 million, and WATS usage revenue of $63 million with costs of $41 million for a $22 million contribution.

We agree with the principle of setting rates for both these services so that the access and nonrecurring charges cover their costs, assuming we know what those costs are. It appears that access is covering its costs, and that nonrecurring rates probably are not. However, we do not know how these recurring access costs and revenues and these nonrecurring costs and revenues are divided between the two services. Nor have we been informed of the rationale for the rate change proposals and how they will alter the revenue to cost ratios for these cost components.

Assuming that the 800 Service usage contribution of $76 million is in the ballpark, a revenue reduction of $11.067 million seems reasonable when reducing revenues is a goal. However, we are concerned that the focus of Pacific's rate reductions be to benefit the general body of ratepayers to the greatest extent possible. 800 Service rates do not directly benefit most consumers of toll-related services. Therefore, without a showing that such a revenue reduction is necessary to the viability and reasonable growth of this service, the present contribution level should remain. The record offers no suggestion why that contribution should be reduced. Further, there is no explanation for the rate design which essentially eliminates the category of Half State. For these reasons we agree with DRA's position that 800 rates should not be changed at the present. We will deny Pacific's 800 Service rate proposal. The adopted 800 Service rate design will result in no revenue effect.

Pacific's witnesses also offer no explanation for its proposal to change its WATS rates. As we have pointed out, so far as we can ascertain from the joint data, recurring rates already produce revenue to cover costs. We are not inclined to authorize this WATS proposal without some justification on the record. The WATS proposal is denied. The effect of the adopted MTS rate design, however, will be a $0.527 million WATS revenue reduction.

VI. Other Toll-Related Services

A. Pacific's Proposed ZUM Expansion and Other Changes

ZUM is a measured rate plan which is provided to all customers in designated metropolitan areas. It provides rates for two mileage bands beyond the local calling area which are set at about half the rates for message toll service (MTS) calls to analogous rate bands, i.e. the 9-12 and the 13-16 mile zones. In ZUM parlance these zones are respectively designated ZUM Zone 2 and ZUM Zone 3. ZUM service is designed to recognize the economies of volume which exist in these high density areas. It further recognizes that the very urbanization which is exemplified by these economies of volume is also exemplified by communities which spread from their centers and merge with adjacent communities thereby increasing the likelihood that the customer will utilize basic services within a wider area than the local calling area. In other words the customer's community of interest is no longer restricted to the area that forms her or his local exchange. Thus, the goal of ZUM service is to allow customers in urban areas to communicate with others in their more extensive community of interest at an affordable rate.

1. ZUM Expansion

Pacific proposes to expand its ZUM rate plan on the periphery of the San Francisco-East Bay Extended Area to add 12 exchanges. In addition Pacific proposes structural changes in the 39 exchange or district areas affected by this expansion. These changes include one consolidation, two divisions, relocation of six rate centers, and the elimination of two district area designations. The result of these changes will be that eight local routes will become nonlocal and seven nonlocal routes will become local. DRA supports Pacific's ZUM expansion proposal. No other party takes a position on this issue. We agree that the criteria Pacific used to determine the applicability of ZUM to these new areas was appropriate and the characteristics of the areas warrant ZUM expansion. We will authorize the adoption of Pacific's proposed ZUM expansion.

Based on its proposed rates and charges Pacific claims that this ZUM expansion would result in a revenue reduction of $4.521 million in the test year. Considering the rates which we have actually adopted in this decision, the test year revenue effect of this ZUM expansion is a negative $6.252.

In addition to the ongoing revenue effects of this ZUM expansion, Pacific has asked this Commission authorize a one-time implementation cost of $1.13 million for the test year. DRA's Shantz opposes the request, explaining that the costs of [implementation] activities such as bill inserts and order processing are embedded in the historical data upon which the adopted results of operations is based. He adds that these activities normally occur as a part of the implementation of the rates and charges adopted by the Commission in a major rate proceeding. We find no support for this proposition. We will authorize adoption of Pacific's $1.13 million ZUM expansion implementation costs (which equates to $.8 million in revenue).

2. <u>ZUM Zone Boundary and Rate Change Proposal</u>

According to Pacific's rate design witness, G. J. Sullivan, Pacific proposes doing away with separate ZUM Zones 2 and 3 and replacing them with a single designation and a single rate. This is parallel to the MTS rate band consolidation proposal which we discuss in Part V, above. Presently in the areas where ZUM service is provided ZUM Zone 2 rates are charged for calls between 9 and 12 miles and ZUM Zone 3 rates are charged for calls between 13 and 16 miles. (The Zone 3 tariff is applied to calls between 12 and 13 miles.) Pacific proposes consolidating these zones and charging a new tariff for all ZUM calls between 9 and 16 miles. Presently a 5-minute Zone 2 call costs $.20 and a 5-minute Zone 3 call costs $.30. Under Pacific's proposal either call would cost $.21. In addition, Pacific proposes distinguishing between business and residence rates for local calls (ZUM Zone 1) in areas where ZUM rates are in effect. The result is that a local call which is now measured at 4 units for the first minute and one unit for each additional minute would continue to be measured the same way for residential service, but would be counted as 4/3 units for the first minute and one unit for each additional minute for business service. No such distinction is proposed for calls between 9 and 16 miles, i.e. the new consolidated Zone 2.

DRA's Shantz describes Pacific's proposal as an attempt to subject the short-haul user to unreasonable increases in short-haul usage charges consistent with Pacific's past proposals to change the ZUM concept of providing a rate transition from local usage to message toll usage. DRA is concerned that this ZUM zone change is the first step in an attempt to do away with the concept of ZUM as a transitional phase with rates set at levels between local and toll rates. This is part of a plan, as DRA sees it, for Pacific to increase short-haul toll rates in order to decrease long-haul rates to be more competitive in the event this Commission permits intraLATA toll competition in the future.

As described in our discussion of MTS rates, above, CBCHA/TCA's Selwyn supports the consolidation of ZUM Zones 2 and 3 but urges that a new Zone 3 be established to cover distances between 17 and 30 miles. CBCHA/TCA argue that California does not recognize the fundamental distinction between calling within a metropolitan area, with its economies of volume, that it ought to recognize. As a consequence, they argue, much "local" calling in metropolitan areas, most of which is usage, is priced at toll rates. Since toll rates have historically been a source of subsidy to basic exchange service, local <u>usage</u> is, in their view, inappropriately subsidizing the cost of local <u>access</u>. According to CBCHA/TCA's witness, Nancy J. Wheatley, their proposal would result in a net reduction in MTS revenue of about $206 million. CBCHA/TCA argue that implementation of this proposal "would provide a healthy stimulus to the use of the network by local subscribers." Much of this shortfall would be recovered from the increases CBCHA/TCA propose for basic exchange rates which are discussed above.

Selwyn used various Pacific workpapers to produce calculations which he claims indicate that the total annual cost for measurement and the provision of detailed billing of measured local and ZUM Zone 1 calling is $77.5 million. He goes on to state that the total annual cost for these measured services, based on Pacific's workpapers, is $447.1 million, but that it would be only $369.6 million if Pacific did away with measurement and simply provided flat rate service. Using rather speculative data Selwyn also calculated that the costs of detailed billing and measurement of ZUM Zones 2 and 3 calling is $37.9 million out of a total cost of $157.8 million. He concludes that the cost Pacific incurs to measure local calls and to provide detailed billing for local and ZUM calls may be impeding greater use of the network, and he therefore additionally urges this Commission to scrutinize this question of the propriety and value of local measured service.

Pacific opposes Selwyn's proposed ZUM mileage band expansion, stating that it seems out of harmony with the Commission's policy objectives and claiming that its own proposal is the most balanced and represents the greatest benefit to the general body of ratepayers. Based primarily on its study of savings which would result through offering detailed billing of ZUM messages only as an optional service in response to Ordering Paragraph 15.c. of D.84-06-111, Pacific also opposes Selwyn's proposal to eliminate detailed ZUM billing, stating that his cost figures are highly exaggerated as a result of his assumption that difference between the cost of a flat rate day period call and a similar measured call is due entirely to the measurement costs of a measured call. Scholl testified that this difference is largely due to time of day distribution, rather than measurement costs. Further, Scholl pointed out that his workpapers show measurement costs to be less than half that estimated by Selwyn. Finally, Pacific argues that detailed ZUM billing assists customers in understanding and controlling their telephone charges and allows customers with low usage to receive service at less than the flat rate.

DRA states that adoption of Selwyn's proposal would be unfair to rural, nonmetropolitan customers and would unjustly provide exchanges in the San Francisco-East Bay Extended Area and certain exchanges in the Los Angeles Extended Area with rates which are inequitable when compared to the exchanges in the Orange County Extended Area and the San Diego Extended Area.

3. Discussion

While the pricing structure Pacific proposes for its simplified ZUM configuration has some appeal, we must agree with DRA that this scheme moves in the direction of obscuring the transitional quality of ZUM. We agree with DRA and CBCHA/TCA that it is important to retain a clear pricing distinction between local and toll calls of similar distances. As we said in our last Pacific Bell rate decision:

> "[T]here are significant differences between ZUM service provided in a metropolitan area and short-haul toll service provided elsewhere in PacBell's service area. The differences are matters of averages: The typical ZUM route is denser and provides service more efficiently than the typical MTS route." (D.84-06-111, mimeo. at p. 246.)

We do not agree with CBCHA/TCA, however, that it is reasonable to consolidate the present ZUM zones and add a new one thereby decreasing revenues by over $200 million in order to redefine the community of interest of callers in high density urban areas. In actuality a community of interest clearly differs from customer to customer. The scope of the ZUM discount does not coincide precisely with the calling patterns of all callers in these highly urbanized areas, nor should it. Our ZUM policy attempts to strike a balance in setting rates which will provide the ratepayer with a reasonably defined calling area for meeting his or her basic local calling needs at relatively low rates. That is what we mean by "community of interest." There are clearly many ratepayers in urban areas who regularly make calls well beyond 16 miles. It cannot be stated without qualification that none of these calls should be regarded as the type which ought to constitute basic local service. Selwyn's proposal, however, would adversely impact on other important policies, such as keeping basic service prices at reasonable levels, by unduly burdening rates for the basic area of local service in order to increase the benefit to ratepayers making calls to farther points. Therefore, we conclude that the present ZUM boundaries ought to be retained. We decline to adopt Selwyn's proposal to extend ZUM boundaries or Pacific's proposal to consolidate ZUM Zones 2 and 3. We will direct Pacific to maintain its present ZUM zone definitions.

Turning to the issue of economic pricing raised by Selwyn, we agree that the underlying costs of providing local and metropolitan service can be kept lower than the costs for comparable nonmetropolitan service, due to increased traffic-handling efficiencies. The reduction in the cost of ZUM rates is an equitable step which should be taken now both to recognize this cost advantage and to recognize the decrease in the value of basic exchange service due to urbanization. However, as we said above in our discussion of MTS rates all consumers should benefit from reductions in usage rates. Selwyn's proposal provides a disproportionate benefit to large users, and a disproportionate basic rate increase to small consumers.

It is appropriate to recognize both the lower relative costs and the community of interest for the majority of metropolitan callers but neither Pacific's nor CBCHA/TCA's proposals equitably distribute cost savings in the context of a reasonable reduction of usage rates. Adoption of the same moderate usage rate reduction for additional minutes of use for ZUM Zones 2 and 3 that we have adopted for the analogous toll rate zones would accomplish this policy goal and continue to allow Pacific's ZUM service to provide a contribution. In fact, a reduction in these usage based rates also have the potential for greater revenues, as lower rates may cause a relaxation of usage suppression. Under such a rate design a ZUM Zone 2 call would cost $.26 rather than $.35 for a 10-minute call. Therefore, we will direct Pacific to retain its present ZUM pricing schedule, except that the rate for additional minutes of use will be treated analogously with that we have adopted for the first two MTS rates bands. We calculate that this change will decrease ZUM revenues by $30.531 million in the test year. We are not convinced of the need for different ZUM rate treatment for business and residence service as Pacific requests, and will therefore not adopt it. The rates we adopt here will apply to both business and residence ZUM.

We are satisfied with Pacific's Ordering Paragraph 15.c. study results and conclude that the costs of ZUM measurement are not so great as to outweigh the benefit to customers. Therefore, we will not adopt Selwyn's proposal to eliminate ZUM measurement.

B. General's ZUM Expansion Proposal

General's witness Jensik testified that General disagrees with Pacific's proposed ZUM expansion to the extent that Pacific has failed to propose expansions to many areas in LATA 5 and LATA 1, specifically as it affects General's customers in the San Bernardino, Redlands, Thousand Oaks, and Oxnard regions. Therefore, Jensik asks that the Commission order Pacific and General to file a plan to expand ZUM to include certain Pacific and General exchanges shown in Attachment 1 to Exhibit 384. He makes this proposal because General cannot file for ZUM expansion unilaterally in most locations since the ZUM tariff is a Pacific tariff in which General concurs and since Pacific must be involved to assure customer benefits and acceptance by keeping calls priced equally in both directions over common routes.

DRA responds to General's request by noting that at least three of the exchanges included in General's proposal are

Continental Telephone Company of California (Continental) exchanges which therefore require Continental's participation, and by raising the issue of providing notice and an opportunity to be heard to affected ratepayers. DRA concludes that the issue should be heard in Pacific's next general rate proceeding. Pacific suggests that the appropriate forum should not be its next rate proceeding, but a separate application by any of the affected telephone utilities. Pointing out that General's recommendation encompasses several nonmetropolitan areas, which have not previously been deemed appropriate for ZUM expansion and also encompasses an alteration in ZUM availability criteria, Pacific adds that a proper analysis of the relevant issues will take 8 to 12 months. Pacific also claims that the parties should not be limited to evaluating General's proposals, but should be free to propose alternatives. General argues that Pacific's time estimate is greatly exaggerated, that the investigation and analysis, including that for the small number of Continental's affected exchanges, could be completed in 90 to 120 days, that the proposals of these other parties will unnecessarily delay needed beneficial changes, and suggests that the matter be taken up in General's ongoing general rate proceeding, A.87-01-002. In the alternative General supports the Commission's filing in the near future an OII with regard to ZUM expansion.

Since these arguments were presented General has unsuccessfully attempted to add this issue to A.87-01-002, its pending general rate proceeding. The denial of that further issue was appropriate. We believe that the issue is best raised in an OII. It need not be a new one, however. Since I.87-02-025, which has been consolidated with A.87-01-002, is already open and all the relevant parties are respondents to it, a later phase of that proceeding will provide an appropriate forum to address this issue. Before that phase commences, however, the parties must have an opportunity to study General's proposal, notify potentially affected customers, and prepare alternative proposals. Therefore, we will order that this issue be heard in a later phase of I.87-02-025. The burden of proof of the feasibility of this proposal will not be altered by the forum in which it is to be heard. It will lie with the plan's proponent. The timing of this proceeding should be worked out by the parties in a prehearing conference.

C. TURN's Metropolitan Flat Rate Proposal

1. The Costs and Benefits Study

TURN proposes the addition of an optional metropolitan flat rate service and the elimination of ZUM (and other metropolitan rate options discussed in Part V of this decision). In making this proposal, TURN refers to Exhibits 294 through 296 which describe the results of the cost and benefit study regarding the establishment of residence flat rate metropolitan calling plans offering unlimited residential calling without charge in all or portions of the San Francisco-East Bay Extended Area or the Los Angeles Extended Area, which we required Pacific to conduct by Ordering Paragraph 16(b) of D.84-06-111.

Pacific's study involved offering one of three plans to different customers in selected prefixes in each of the extended areas between May 1 and December 31, 1985. Plans 1 and 2 each offered a choice of Metropolitan ZUM, which allowed residence customers unlimited usage on their ZUM Zones 2 and 3 routes for a fixed monthly rate, or Metropolitan Extended Area (EA), which offered unlimited usage throughout a wider extended area. Plan 3 only offered the ZUM choice. Pacific defines an extended area as an aggregation of exchanges within a geographical area that has ZUM. (Exhibit 295, part 2, p. 1.) The plans and price options were as follows:

Flat Rate Plans

	ZUM Option	EA Option
Plan 1		
8:00 am - 5:00 pm	$10.00	$35.00
5:00 pm - 8:00 am	5.00	25.00
24 hours	15.00	60.00
Plan 2		
8:00 am - 5:00 pm	$15.00	$45.00
5:00 pm - 8:00 am	10.00	35.00
24 hours	25.00	80.00
Plan 3		
8:00 am - 5:00 pm	$15.00	N/A
5:00 pm - 8:00 am	10.00	N/A
24 hours	25.00	N/A

2. Pacific's Findings

Pursuant to D.84-06-111 Pacific's study contains findings on the issues set out below.

a. Extent of Subscriber Interest

Exhibit 295 states that the flat rate trial plan was offered to over 91,500 residence customers and that over the eight months of the plans' existence 302 customers purchased one of the ZUM plans and 274 purchased one of the extended area (EA) plans. This breaks down to a net subscription rate of .88% or about 9 subscribers per 1,000 customers offered the plans. The subscription rate for EA was somewhat higher, at .50%, than the subscription rate for ZUM plans at .38%. Further, the study shows that price level significantly influenced both the EA and the ZUM plan subscription levels. The ZUM subscription rate for the higher priced plans was approximately 20% of that for the lower priced plans, and the EA subscription rate for the higher priced plan was approximately 75% of that for the lower subscription rate plan. Still, the subscription rates disaggregated by price are only 1.22%

for lower priced offerings and .57% for the higher priced offerings.

Pacific's Sullivan argues that the rate of subscription to the trial plan was so low as to suggest that there is no significant unmet consumer need, and adds that the Circle Plan already offered by Pacific has similar geographic boundaries to the metro plan. He also argues against the implementation of such a plan based on the findings of the the post-trial survey of about 300 of the trial plan's purchasers, the results of which are set out in Attachment 4 to Exhibit 400, which shows that they are different from Pacific's typical customers in that they are older, have a higher level of education and income, are more often self-employed, are more likely to have more than one telephone number in their homes, are more likely to own personal computers with modems, and are more likely to conduct business-related or paid work from their homes.

b. Effects on Pacific's Revenues and Costs of Service

The study found that customers subscribing to EA plans increased their usage by 317.5% with 24-hour EA subscribers increasing their usage most at 468.8%, while ZUM subscribers increased their overall average usage by 31.5%, with a high of 36.8% for the daytime plan. Pacific's final report on this study states that during March 1985 trial participants used 100% more minutes, initiated 80% more messages, and generated 47% more revenue for Pacific Bell than did typical customers. (Exhibit 400, Attachment No. 4 at p. 23.)

The study compared the cost of subscribers' pretrial usage to Pacific's revenue breakeven point for ZUM and EA services and found that 79.9% of EA subscribers were, pretrial, below the breakeven point and that 58.6% of ZUM plan subscribers were below. The study then compared usage during November of the period and found that only 31.6% of EA subscribers were below the breakeven point, but the percentage of ZUM subscribers rose to 68.2%.

With such levels of subscription, Pacific projects an overall change in revenue requirement for 1987 ranging from a decrease of $19.12 million for the ZUM Plan 1 option to an increase of $9.28 million for the EA Plan 2 option.

Although its study shows that implementation would generally increase revenue and encourage increased metropolitan usage, in assessing long-term risk Pacific claims that the profitability of flat rate plans depends on a balance of subsidy flow among subscribers below and above breakeven points, and that the study indicates that low-end users who provide the subsidy increase their calling the most, thereby generating both incremental revenue and the majority of costs so that the subsidy from these subscribers decreases.

Pacific reports that the trial showed a trend for customers below the breakeven point to drop their plans (17.4% of total subscribers), and also claims that flat rate plans are riskier than Call Bonus plans based on allowances and discounts because costs under flat rate plans increase substantially since calling increases, but revenues do not increase proportionately. Thus, Exhibit 295 shows lower revenue to cost ratios for both Plans 1 and 2 than would exist without the plans.

In his rebuttal testimony, Exhibit 400, Sullivan asserts that the flat rate structure of this plan is inherently unfair, because it divides subscribers into two distinct groups - one which subsidizes the other. He states that the resulting profitability thus becomes dependent upon customers who do not benefit subsidizing those who do.

c. **Appropriate Rate Levels to Avoid <u>Diminution in Net Revenues</u>**

We issued a Supplemental Opinion, D.85-02-030, after the issuance of our last Pacific Bell general rate decision, in order to review Pacific's plans for conducting certain cost studies which we had ordered, including the optional metropolitan flat rate study. We explained that it was not our intention to approve the precise terms of the various study plans, but to address criticisms which went to the heart of the study plans, raising questions whether the studies as proposed to be conducted would provide at all the sorts of information which the Commission sought by Ordering Paragraph 16 [of D.84-06-111]. In that cost study review proceeding TURN urged us to require Pacific to set the total price for 24-hour metropolitan calling plans to begin at no more than $25. We found that such a price ceiling apparently is inconsistent with the avoidance of net revenue loss, and is therefore inappropriate. The lowest price offered for 24-hour EA service in this study is $60 per month.

Pacific's Exhibit 295 does not explain how it arrived at the prices it selected for this study. It merely states what prices it chose to test. According to Table A2.1, the total amount of revenue generated by implementation of the plans was $5,072 per month. This revenue results from gains of $5.01 or 67.9% per month from the average ZUM subscriber and $22.62 or 127.8% from the average EA subscriber, and these figures average the much higher subscription rate of Pacific's lower priced Plan 1 offerings with the lower subscription rates of its higher priced Plan 2 and Plan 3 offerings.

d. **Effects on Separations and Settlements Arrangements**

Pacific's study includes the projected results of the effects of the plans for 1987, 1988, and 1989, including effects of the plans for the intrastate revenue requirement after settlements with the independent companies. It indicates that the intrastate revenue requirement would range in 1987 from a decrease of $12.49 million for ZUM Plan 1 to an increase of $5.88 million for EA Plan 2.

e. Cross-elasticities of Demand With Other Optional Discounted Services

The final report found that trial participants were much more likely to have an optional calling plan before the trial than were typical customers. For example, 46% of trial participants had some optional calling plan while only 28% of typical customers had one, and 15% of trial participants had circle calling while only 2% of typical customers had it. By far the greatest predictor of participation in this trial was heavy pretrial usage.

3. TURN's Position

TURN points out that Pacific's exhibits show that virtually every version of the flat rate metropolitan service made money for the utility, while encouraging customers to increase their metropolitan calls and that Pacific found that the 5:00 p.m. to 8:00 a.m. extended area plan was the most popular among customers. TURN concludes that flat rate metro plans can be a profitable way to increase calls during the relative slack evening hours. TURN's witness Siegel recommends that an EA-wide service plan available from 12:00 noon to 8:00 a.m. weekdays and all Saturday and Sunday at $15 per month should be implemented.

TURN argues that service enhancements such as the flat rate metropolitan plan increase absolute usage and thus Pacific's revenues, and sees arguments about which customers pay what portion of the revenue increase as irrelevant since according to the data correlating existing optional calling plans with income such service enhancements are targeted to well-heeled customers as a way to attract more of their disposable income to profitable telephone services. TURN disputes Pacific's interpretation of the significance of the subscriber interest statistics Sullivan cites and concludes that the response to the metropolitan plan does show an unmet need.

4. Discussion

TURN's proposal for a trial metropolitan flat rate is apparently intended to safeguard residential ratepayers from our increased loading of marginal costs onto the monthly rate. However, its flaws cannot be overlooked. Pacific's cost study clearly demonstrates that revenue to cost ratios for the plans are much lower than the revenue to cost ratios for present discounted toll options, thus exposing Pacific to more risk of revenue shortfall from these plans, especially if those subscribers below the breakeven point continue to drop their plans.

Further, while we are not particularly concerned to learn that this service is more appealing to people who are better educated and make more money than the average subscriber, we are concerned with the fact that the cross-elasticity of demand between flat rate metropolitan service and present optional calling plans, particularly circle calling, is very high. If significant numbers of customers were to simply switch from another optional calling plan to this one the overall revenue increase would be eroded considerably.

We are also concerned with the possibility, as indicated at page 14 of Pacific's final report, that 36% of the trial customers, but only 14% of typical customers do paid work or business at home frequently or occasionally; and the further indication that 52% of this subgroup of trial customers use the telephone frequently while working at home. These statistics seem to support Pacific's concern that this plan might be used in place of basic business service and thus negatively impact Pacific's revenue from business services.

While it is true that Pacific's study indicates that a flat rate metropolitan plan could increase Pacific's overall revenue, at least in the short run, the limited appeal of the offering coupled with the strong likelihood that the plan will lead to a reduced subsidy source, the fact that the overall subscriber interest is lower than that for the present discounted toll options, and the fact that the particular flat rate metropolitan plans with the highest subscriber interest show projected overall revenue requirement increases, lead us to conclude that the risks of adopting a flat rate metropolitan plan at this time exceed the benefits to ratepayers and are not a reasonable way to recognize the economies of scale stemming from heavy users of the shorter range intraLATA long distance services while assuring that the program for recognizing those economies continues to provide a contribution over costs. Our adoption in this decision of usage rate decreases for MTS and ZUM services already accomplishes this goal with less risk. We will deny TURN's proposal.

D. Foreign Exchange Service (FEX)

FEX Service is telephone service which has dial tone and access to the network provided from an exchange or district area other than the one in which the customer's premises are located. It consists of a basic exchange access line plus network facilities connecting the customer's home central office to the remote central office of the customer's choice. There are three different ways that Pacific can provide this service. It provides each subscriber with service using whichever method it deems to be least costly.

The most common is called the Line Haul method. It uses a private line channel to connect the subscriber's serving central office to a central office in the desired distant exchange. The second method is the Dedicated Prefix method in which an office in one exchange is made to appear as though it were in another exchange through a billing arrangement (often referred to as a Dedicated NNX) and no private line channel is required. Dedicated prefixes exist only in central offices where Pacific has experienced a large enough demand for FEX service to another specific exchange to justify the dedication of a substantial portion of a central office switch and a large block of telephone numbers to that service. The third method is called the Cross

Boundary arrangement. It connects a customer's premises directly to a central office in a contiguous exchange. This is a very infrequently used method which requires that the customer location be close to the exchange boundary. Additionally, there is one permutation with characteristics of both the Line Haul method and the Dedicated Prefix method, called the Hybrid Line Haul. In this configuration the customer's serving central office is not a Dedicated NNX office, but there is one close by, then a private line channel is installed from the serving central office to the Dedicated NNX office.

1. <u>Pacific's FEX Proposal</u>

At present FEX subscribers pay a specified rate for FEX service which varies based on whether they are residence or business subscribers, whether their business service is measured line or trunk, whether their residence service is flat, measured or party-line, whether the service is to a noncontiguous location, and, in some instances, whether service is in exception rate areas. Pacific proposes retaining these distinctions, but unbundling rates so that each rate has the same access component and usage component as basic local residence or business service plus a new FEX increment component.

Sullivan proposes setting the residence flat FEX increment at $6.75 per month, the measured residence increment at $4.05, and the business increment at $11.25. He also proposes continuing the present policy for determining the mileage used in setting certain rate levels. He explains that the proposed FEX rate elements are not increases, but simply the difference between the current FEX rate and the current rates for flat and measured service. When they are added to the access and usage rate increases Pacific has proposed for basic local residence and business service, the overall effect is an increase in rates for FEX subscribers.

In its last general rate case Pacific proposed limiting or "grandfathering" the offering of FEX service to existing subscribers. In addition to the described unbundling of rates in the present proceeding, Pacific again proposes grandfathering this service, for both residence and business FEX customers by limiting it to existing subscribers at their existing premises and existing class of usage service. In explanation of this aspect of its proposal, Pacific contends that the ratio of revenues to historical costs of FEX access, service connection, and mileage will show huge shortfalls in the test year. Sullivan cites examples ranging from 10% to 40% at current rates.

Pacific asserts that the extent of FEX demand is attributable to the inordinate discount it provides over toll services; and goes on to claim that stimulation of that demand in light of the poor financial performance of FEX is not sound ratemaking policy. Sullivan explains that it is Pacific's objective to ultimately replace this service with software-based services priced at compensatory levels. He contends that the proposed grandfathering is reasonable because there are enough optional calling plans and other substitutes for FEX available to new subscribers so that the growth of FEX can be eliminated. By way of example he points to ZUM expansion in the San Francisco-East Bay area which will eliminate some FEX needs, and to possible boundary realignments. Pacific also mentions Call Bonus plans and Remote Call Forwarding (RCF) as possible solutions for residence customers, and 800 Service and WATS for business customers. Pacific claims that RCF is a complete substitute for incoming FEX calling, but acknowledges that while there are means of achieving substantial toll discounts, there is not yet a direct substitute for all the outgoing calling components of FEX. It contends, however, that utilization of the available alternatives are preferable to FEX service at the extremely large price increases which Pacific's cost evidence demonstrates would be necessary to make them fully compensatory.

2. Positions of Other Parties

No other party which addressed the FEX issue disagrees with Pacific's proposal to unbundle FEX rates, but every other party which addressed the issue disagrees with its grandfathering proposal.

a. General

General's Jensik testified that General and other local exchange companies in California concur in Pacific's tariffs for FEX service. He objects both to Pacific's grandfathering FEX service and to its freezing rates at present levels. Instead, General proposes continuing the FEX offering, but moving prices toward cost. Jensik does not address residence FEX service, only business FEX service.

Claiming that all FEX service requires connecting a private line from a location in one exchange to a dial tone in another, he recommends that FEX rates should be consistent with the rates for private lines, plus dial tone [access] rates for business. Based on this model he goes on to recommend that a local channel termination rate be charged at the local loop end and usage be charged at the dial tone end. He states that where measured service is not available at the dial tone (open) end that the difference between the individual business line flat rate and the individual business line measured rate be charged.

Jensik added that his proposal arises in part from the incompatibility of Pacific's private line tariff structure with the one General has proposed in its pending general rate proceeding, and in part from General's view that the emerging competitive telecommunications marketplace makes it more necessary for these companies to be independent of one another in their pricing and selling of local exchange services. Intercompany settlements procedure for private line, including FEX, would be replaced by a "bill and keep" approach. Further, he proposes that for intercompany FEX service the companies use meet point billing to bill for the interoffice private line, i.e. the portion in General's territory would be billed at General's rates and the portion in Pacific's territory would be billed at Pacific's rates.

b. CBCHA/TCA

Selwyn opines that in addition to there being no direct substitute for FEX outward calling, as Pacific acknowledges, neither 800 Service nor Remote Call Forwarding provides an adequate substitute for inward business FEX service, i.e., service which provides a means for a caller from the distant exchange to place a local call to the FEX business subscriber. He explains that 800 service does not allow a business to create a "presence" in a distant market area in that it implies to the customer that wherever it was that they were calling was located at some distance from their own community.

Selwyn's only objection to Remote Call Forwarding as a substitute is that the MTS charges associated with the use of the service would be much higher than the access line and mileage charges for FEX service, assuming that there is some reasonable level of traffic to the remote location.

Selwyn asserts that the need for the magnitude of the loop costs which Pacific assigns to FEX service is questionable at best. He states that about $35 of the monthly loop expense for business FEX circuits which Scholl's workpapers set at $85 is associated with design and testing costs. He states that these design costs are associated with the claimed need to provide additional circuit equipment in order to achieve adequate transmission characteristics on the circuit and argues that there is little need for such "design" of FEX lines since the nature of FEX line usage is more likely to be limited to the immediate area around the exchange where dial tone is provided, with little if any use of toll or other long-haul connections where transmission losses in the line would be expected to have the greatest adverse effect. He also argues that FEX subscriber loops are not longer than average subscriber loops, but that since the need for design of a loop is associated with loop length, the costs Pacific attributes to these loops are too high. Selwyn also claims that Pacific's FEX testing costs are entirely unreasonable.

Finally, stating that Exhibit 287, Pacific's revenue impact workpapers, show no offsetting revenue increase for other services resulting from stimulation due to the grandfathering of FEX, Selwyn asserts that Pacific has either materially understated the revenue effect of its FEX proposal or else it is the case that there are no present alternatives to FEX service and the functions now provided through FEX will no longer be available to new customers. He concludes that Pacific's grandfathering proposal must be denied or at least this Commission must impute offsetting stimulated revenues equaling the $47 million revenue loss Pacific claims will be due to FEX grandfathering.

In his rebuttal testimony Pacific's Scholl testified that Selwyn's assertion that FEX loop length indicates that the need for "designed" access lines (i.e., lines with additional transmission equipment) is overstated is premised on a false assumption, and that while the PBX loops to which Selwyn compares this cost element are only designed when loop resistance is great, FEX service requires designing whenever an interoffice facility is required to provide the service (e.g., whenever the 'line haul' serving arrangement is required). He adds that this is the case for 67% of FEX lines. Scholl specifies that the elements of this design process are the assignment of the interoffice facility and the associated central office service area transmission equipment. Thus, Scholl asserts that the recurring costs for designed circuits which Pacific assigns to FEX are not overstated.

c. Centex

Centex describes itself as a communications manager for small and medium sized businesses which assists its clients in forming joint user groups, which enables them to qualify for service options not otherwise available to business customers of their size. Centex explains that its interest in FEX service is based on its clients' use of the service for outward calling.

Centex presented the testimony of Stephen E. Siwek, a telecommunications consultant, with degrees in economics and business administration. Siwek asserts that Pacific's grandfathering proposal should be rejected because its arbitrary customer disaggregation will stimulate inefficient consumption patterns and fails to let the mechanism of market selection function, leaving customers and the company less well off. (See generally Exhibit 370.)

Centex concurs with Shantz and Selwyn that there are no adequate alternatives for business FEX service, particularly outward calling. Centex cites Exhibit 403, the final report of Pacific's Special Services Administration Task Force (SSA Task Force), which was received into evidence very late in this proceeding. The document describes possible alternative FEX provisioning to reduce costly line haul. These include creating additional dedicated prefixes, where cost justified, creating shared dedicated prefixes, and the use of 2-Number FX.

Centex points to Scholl's testimony that shared dedicated prefixes have the advantage of permitting the assignment of just 1,000 calling numbers to a particular central office, rather than the dedication of a block of 10,000 numbers which the present dedicated prefix requires. Scholl also testified that Pacific was having difficulty in interfacing such a plan with interexchange carriers. The report explains that 2-Number FX would use a combination of Remote Call Forwarding and a redesign of Pacific's present billing system, called Front End Guide, which would allow the provision of both FEX service and conventional local service on a single line.

Centex asserts that the possibilities for Pacific provisioning FEX service more efficiently and in a less costly manner in the future as described in the SSA Report underscore the unreasonableness of permitting this service to be grandfathered and, like Selwyn, urges that we concentrate instead on appropriate pricing.

In its concurrent opening brief Centex moves for the admission, as a late-filed exhibit, of a Response to Transcript Request which it received after these hearings had concluded. Centex asserts that the document describes the 2-Number FX service and Front End Guide concepts more fully than Exhibit 403. Centex apparently offers this document to show that Pacific has studied technologically feasible ways of provisioning FEX service which do not require line haul configurations. The alleged contents of the document would merely be cumulative in supporting such a proposition. The description of these services in Exhibit 403 is adequate. We will therefore deny the motion.

Siwek supports the concept of unbundled FEX rate elements, but differs with Pacific on what the rates should be. In his analysis of Pacific's FEX cost studies, he cites Scholl's testimony that FEX access costs for Centrex customers would probably be less expensive to provide than a simple line haul service because, although there would be some additional switching-type costs, access line costs would be eliminated. (See Tr. 10051-10052.) Siwek argues that since Pacific has not quantified the savings associated with FEX service to Centrex customers, as an interim measure pending new company cost studies, this Commission ought to recognize the difference by applying Pacific's proposed increases in FEX access rates only to customers requiring access lines, maintaining access rates at current levels for customers who avoid the use of FEX access lines. On redirect examination Siwek was asked whether he would agree with Shantz' suggestion for setting an appropriate recurring monthly charge for customers who use FEX service in conjunction with Centrex service, which the questioner characterized as being the sum of an FEX rate increment applicable to all business FEX service plus the Centrex exchange trunking charge. Siwek stated that he did agree with such an approach in concept.

Siwek states that Pacific's decision not to increase FEX mileage rates seems consistent with its cost studies, which show these rates to be reasonably in line with 1986 costs, but adds his opinion that as Pacific's use of fiber optic plant increases incremental cost will decrease, thereby producing future revenue excesses which can be used in the future to offset any shortfalls from nonrecurring FEX charges.

Turning to nonrecurring costs, Siwek contends that the cost study portrayed in Pacific's data response Exhibit 276 which shows the nonrecurring cost per FEX business connection at $1,378 is so much higher than the total unit cost expense saving it shows for grandfathering FEX service in its transcript request Exhibit 303 ($541), and the estimated service connection costs it estimated in its 1984 rate proceeding ($333 for the 83% of service that is to contiguous areas and $573 for the 17% to noncontiguous areas--the weighted average is $374) that the accuracy of these studies is questionable.

Siwek adds the connect and disconnect savings figures from Exhibit 303 plus two times Pacific's claimed record costs to represent two service orders, plus Pacific's calculation for investment-related nonrecurring FEX costs to arrive at his $895 proposed connection rate for new business customers. He cautions that this figure is probably high because the disconnect figure is somewhat overstated and because no cost adjustment factor has been applied to it to reflect Pacific's 1986 authorized revenue requirement. Later, based on Scholl's rebuttal testimony, Centex concluded that the two "record" service order inclusions in Siwek's calculation are inappropriate, so that the total should be reduced to $833. In any case Siwek goes on to state that we should not authorize even his proposed increase all at once, but should limit any connection rate increase to 100% above current rates in keeping with what he understands to be Commission policy regarding nonrecurring rate increases. Current rates are $190 for business connections for service between contiguous exchanges and $290 for service between noncontiguous exchanges. The weighted average would be $188.

Citing Selwyn's criticism of Pacific's allocation of design and testing costs to recurring FEX service rates, Centex' opening brief claims that comparable allocations were made to the nonrecurring cost categories on which Scholl's $1,378 estimate was based, and suggests that Pacific's failure to produce a bottoms-up cost analysis of nonrecurring FEX services is justification for authorizing no increase at all in these charges, or alternatively, for limiting them to the across-the-board 5% increase which Shantz proposed in his original testimony for all service connection charges.

Furthermore, Centex contends that the ratio of service connections to disconnections shown in Appendix B to Scholl's rebuttal testimony (Exhibit 402), which is based on the assumption that the grandfathering proposal is not adopted and that there are no rate changes in the test year, is unrealistically low when compared to the 1984 volumes. Centex asserts that if these figures were brought more in line with recorded figures for 1985 the allocation of nonrecurring costs to business FEX service would have produced a much smaller indicated cost per service connection.

Centex also suggests that there are two possibilities for unbundling FEX rates. One is to calculate rates which are revenue neutral with respect to the combined FEX rates for any particular customer, the other, which Centex recommends, is to establish a uniform FEX increment and allow the total rates paid by particular customers to vary, depending on the choice of access line.

Replying to Siwek's claim that the difference between Pacific's $1,378 total FEX nonrecurring cost figure and its $541 calculation of test year expense savings raises the question of the reliability of Pacific's projections, Scholl explained that the former figure is an average of all business FEX nonrecurring inward movement costs, including connects, disconnects, change orders, and record orders, while the latter is only the average connection cost of a business FEX access line. Scholl also explained that this $541 projected test year business FEX connection cost and the costs estimated in its 1984 rate case ($573 and $333) are not exactly comparable since the 1984 costs represent a composite average cost of service connection for both residential and business FEX while the cost projections presented in the pending matter are separated for business and residential. In response to Centex' skepticism about the number of inward orders (installations) Pacific projected for the test year, Scholl testified that he went back to the project management people who developed these numbers, and learned from them that business FEX would decline because of the growth of some cross-elastic services. He further learned that the tracking results through November, 1986 (the month before his testimony) had indicated that FEX did, in fact, decline throughout 1986. (TR at 19083-19084.)

d. <u>DRA</u>

DRA takes the position that Pacific's grandfathering proposal should be rejected because there are no adequate substitutes for this service, and adoption of it would thus be repressive. Shantz also contends that it would be inappropriate to drive more customers toward Remote Call Forwarding, as Pacific's plan would presumably do, when RCF has been the subject of this Commission's investigation of Pacific's marketing practices. DRA recommends that we require Pacific to file a tops-down and bottoms-up study of FEX service before considering granting any service discontinuance.

. As an alternative to Pacific's grandfathering proposal, DRA's concurrent closing brief proposes decreases for FEX services in direct relationship to the decreases DRA proposed for residence and business BEAL services. When Shantz testified he was proposing service rate increases, the decreases are set forth in DRA's final rate design which was incorporated into the concurrent closing brief. The revenue effects of this change are factored into DRA's revenue effects for basic services and service connection changes.

DRA does support Pacific's proposed tariff structure, but stated that DRA did not have time to develop tariff revisions, and recommended that we authorize Pacific to file an advice letter setting forth an incremental FEX tariff structure, subject to review by CACD and final approval by Commission resolution. Shantz does not agree with Siwek's proposal to charge FEX subscribers who have Centrex service (and therefore do not need a line haul access line) only the FEX increment but no FEX access rate element. Shantz asserted that there are access costs which such a subscriber should cover and agreed with his cross-examiner, Mr. Mattes, that it would be equitable to set this rate element at the one to ten ratio that is used for Centrex exchange access trunking charges as compared to PBX trunking charges. Shantz further states that the FEX increment should be set at a level designed to generate zero revenue effect in relation to the prior unbundled service.

3. <u>Discussion</u>

a. <u>The Grandfathering Proposal</u>

Selwyn's assertion that Pacific's failure to show offsetting revenue increases for other services as a result of its grandfathering proposal indicates either understated revenue effect or a situation where no alternatives exist is well taken. While it appears that there are adequate substitutes for most residence FEX service requirements and that there has been a steady decline in residence FEX service subscription since Pacific's last rate decision was issued, Pacific acknowledges that there is no complete substitute for business FEX service and that subscription is increasing. This fact dictates that Pacific's grandfathering proposal only be authorized where the inequities of any other possible solution are beyond doubt.

Though Pacific's costing methodology seems appropriate and it has reasonably explained the points of it that have been criticized by various parties, we must agree with DRA that the marketing practices Pacific followed with respect to such options as Remote Call Forwarding may well have influenced the growth rate of this service in the recent past in a way which may not be characteristic of future growth. Further, although Pacific is correct that Ordering Paragraph 16d of D.84-06-111 only requires bottoms-up and tops-down cost studies for service categories where Pacific is proposing greater than average rate increases, the import of our order was that any plan to significantly alter an element of rate design should be based on cost data which allows a comparison of methodologies, and allows more precise cost allocation than tops-down studies alone can provide.

It may or may not be possible to bring FEX revenues to the level of costs. Nonetheless, it would be unreasonable to deny FEX service to future businesses seeking it based only on the record before us. This conclusion is reinforced by the suggestion of Pacific's SSA Task Force Report and the testimony of Sullivan that there are less costly alternatives to present FEX provisioning which are already technically possible. Perhaps our denial of this grandfathering proposal will spur Pacific to develop a means of implementing FEX innovations. In any case, we agree with General, Centex, Selwyn, and Shantz that a pricing solution is the most appropriate means of addressing FEX revenue shortfall at the present. We will not grant the grandfathering proposal. If Pacific wishes to offer the proposal again in a subsequent rate proceeding, it shall present both bottoms-up and tops-down cost studies to justify it.

b. Unbundled Rates

The concept of unbundled rates is one which we generally endorse. Although most FEX connections are presently made using a private line channel between central offices, the customer does not receive private line or private line-like service. Therefore, we see no merit in General's proposal to set FEX rates to be consistent with private line rates. Nor is Pacific's model for unbundling FEX rates entirely appropriate since we have already denied its proposal to unbundle basic rates into an access and a usage component. We will instead adopt a modification of Pacific's proposal which is disaggregated into a single rate encompassing both access and usage and a new FEX increment component for FEX services with dial tone from a Pacific central office. As we explain below we will authorize Pacific to set the access component at the same level as local service, and add a new FEX increment component. We adopt Pacific's proposal for the FEX increment component for FEX services with dial tone from a Pacific central office.

(1) Recurring Rates - Mileage and Access

We do not find convincing Selwyn's assertions about the impropriety of the assignment of design and testing costs for loops, the only recurring cost criticized. Scholl's explanation of the need for designing circuits whenever line haul is used seems reasonable. On the other hand, it is clear that such assignment could be lowered significantly if Pacific were able to implement any of the alternative FEX delivery systems described in Exhibit 403.

We agree with Siwek, who apparently does not dispute its accuracy, that the .9 revenue to cost ratio shown at

p. 7-127 of Exhibit 260 (to which no scaling factors have been applied) indicates that present FEX business mileage rates are reasonably close to 1986 costs. The ratio for residence measured service though, at .7, is somewhat low, even if cost is reduced by a factor in the range of 82% to 90% which is the range of all but one of the adjustment factors in Pacific's Exhibit 261. Nonetheless, it appears that mileage rates are close enough to cost that it is unnecessary to adopt an FEX mileage rate which differs from the present rates which we have retained. Furthermore, adoption of such rates may prod Pacific to act with more dispatch in attempting to institute alternative methods for providing FEX service.

There is no doubt that overall FEX service revenue is less than cost. Setting rates for access to the exchange to mirror those for basic service will not affect this picture, and it will provide a rate scheme which is easier for the customer to understand and easier for the utility to administer. No FEX customer should be exempt from exchange access charges; however, we agree with Siwek and Shantz that it is equitable to mirror Centrex exchange access trunking charges when providing FEX service to Centrex subscribers.

No party, however has presented us with a specific proposal for implementation of this concept. We will therefore order the filing of an advice letter which implements this concept. The advice letter should contain the tariff revisions necessary to implement the mirroring of the Centrex exchange access trunking charges when providing FEX service to Centrex subscribers; the estimated 1986 annual billing and revenue effects associated with the implementation of such tariff revisions; and revisions to the customer billing surcharge to reflect the annual revenue effect of implementing such tariff revisions for Centrex service. The advice letter shall be subject to Commission authorization by resolution before becoming effective.

(2) Nonrecurring Charges

Even with its doubts about tops-down cost study reliability and Pacific's $1,378 figure, Centex is willing to assert that FEX business connection costs could be $833 per connection if we assume, as we do, that allocation of design and testing costs to recurring service rates is appropriate and that the ratio of service connections to disconnections which Pacific used is appropriate. Charges are presently $170 for contiguous service to a Centrex line, $190 for all other contiguous service, $270 for noncontiguous service to a Centrex line, and $290 for all other noncontiguous service. Clearly, these charges would still be priced below cost even at 100% increase which Centex would prefer as a maximum. Looked at in this light, DRA's proposal would require Pacific to continue to heavily subsidize this rate element from other sources. FEX is not a basic service and ought not to be the recipient of large subsidies. On the other hand, it has been our policy to ameliorate the effects of rate shock by limiting individual nonrecurring charge increases to 100%. It is clear that such an increase, for both business and residence nonrecurring FEX charges, is reasonable now. We will authorize adoption of such charges.

(3) FEX Increment

As we understand it, General advocates setting the FEX increment at the channel termination rate for private line service. While 67% of FEX service is provided over lines that are similar to private lines, the remainder is not. The proposal ignores the treatment of residence service. Further, since we do not adopt General's private line costing model, it makes little sense to set the FEX increment to be consistent with the model.

Pacific does not propose a change in the portion of its FEX rate which is attributable to the FEX increment. There is no reason for this Commission to adopt a different result. We will authorize Pacific to set its FEX rate increments at the rates Sullivan has proposed for FEX services with dial tone from a Pacific central office. The increase realized from this adopted rate design will be far below any estimate of the difference between revenues and costs.

(4) Revenue Effect

The overall test year revenue effect for changes in FEX nonrecurring charges will be an increase of $12.751 million. The revenue effect for FEX recurring access rates is reflected in our discussion of basic exchange service revenues.

c. Bill and Keep Billing

It makes sense to move the billing structure for FEX services to a structure in which a customer receives a bill for the services which are provided from the particular utility which provides the service. In order to implement the meet-point billing proposal which General advocates, however, it is necessary to develop and adopt billing policies in the form of tariff provisions applicable to each carrier which provides intercompany FEX services, which assure that customers are not double-billed for any portion of their service. We must also ensure that each carrier which provides intercompany FEX services notifies its customers of the change in order to mitigate the confusion which might otherwise result upon the customer's receipt of separate bills from two local exchange carriers.

Detailed specific tariff provisions and customer notice provisions were not addressed in this proceeding. It is not possible to implement the meet-point billing concept for FEX services until such specific tariff provisions and customer notice provisions have been provided. Therefore, we will require Pacific and the other local exchange companies (LECs) to jointly study this proposal and then file with CACD for review and approval, either jointly or separately, the study results, detailing the means of achieving meet-point billing for intercompany FEX service pursuant to a bill and keep plan.

The joint study should address the type and methods of customer notice to be used as well as the conversion of each local exchange company's FEX tariff rate structure to a structure which will facilitate the implementation of the meet-point billing concept for FEX service. Further, in those instances where the implementation of the meet-point billing concept for FEX service will result in an increase in a utility's annual revenues, the advice letter filing should include a revision to the utility's customer billing surcharge applicable to intraLATA services to counterbalance that increase.

Once CACD approval has been received the LECs may make an advice letter filing for Commission authorization of the approved plan.

VII. Private Line and Private Line-like Services

A. Introduction

Scholl describes private line services as connections between two or more customer locations which do not utilize the public switched network, but are fixed or dedicated in nature. Pacific claims that with no rate changes its test year private line revenue will fall short of costs by about $400 million, the shortfall for its recurring costs being about 50% of the test year average historical costs or $300 million and the shortfall for its nonrecurring costs being about 70% or $95 million.

To reduce this shortfall Pacific's revenue neutral rate design proposal of June 25, 1985 proposes increasing test year revenue from private line services by $29.127 million which becomes $26.569 million after settlements, a 22.4% overall increase. Additionally, Pacific calculates that its proposed rate design will result in an expense savings from repression of $4.237 million. No proposed recurring rate is set more than 100% above present rates. Proposed nonrecurring rates are set at one quarter of the difference between present rates and cost coverage. In order to come closer to cost coverage while continuing to moderate the impact, Pacific also proposes phasing in some further private line increases over the two years following the test year, targeting these increases to cover revenue shortfalls created by reductions in carrier access charges and shifts in intraLATA NTS costs. These automatic step increases would result in additional revenue increases of $41.180 million for the second year and $36.293 million for the third year. Since these revenue increases are cumulative, total revenue increase in the third year would be $106.6 million, and the total revenue increase for the three years, excluding expense savings, would amount to $206.034 million.

Besides rate revisions for local loops, Associated Channel Equipment, intraLATA interoffice mileage and channel terminations, Pacific's proposed rates include some restructuring. For one thing, Pacific proposes deaveraging local loop rates by establishing two tariff schedules which recognize the different cost characteristics of serving wire centers with respect to loop length, age of plant, type of facility and structures, and density of development and to base rates on the ratio of average wire center loop investment compared with the statewide average loop investment. About 76% of all local loops would be charged under the lower priced Schedule I rates, and the remainder under the Schedule II rates. Another rate restructure Pacific proposes is making Alarm Transport a separate private line subcategory with smaller rate increases than the rest of private line services in order to recognize "differing market characteristics and different service alternatives that are emerging." This entails establishing a new tariff schedule for Alarm Transport. Further, Pacific proposes raising secretarial line rates somewhat less than other rates to avoid an excessive increase in one year. Finally, it proposes that certain telegraph private line services be limited to those customers currently receiving the services, on the ground that terminal equipment for the services is no longer being manufactured and new demand is therefore virtually non-existent.

B. Pacific's Cost Studies

1. Overview of Pacific's Methodology

Pacific conducted various cost studies to support its private line rate proposals. Separate studies were conducted for recurring and for nonrecurring private line costs. Ordering Paragraph 16.d. of D.84-06-111 required Pacific to conduct and file, as a part of this rate application, detailed bottoms-up as well as tops-down cost studies for any major service category for which PacBell proposes rate increases substantially greater in percentage terms than the proposed increase in total revenues. Thus, both tops-down and bottoms-up methodologies were used.

Pacific's basic cost study is the category analysis, which uses a tops-down methodology to disaggregate projected 1986 average historical (embedded) costs into 16 broad categories of service, one of which is private line. Pacific's category analysis studies were conducted in 1984 and early 1985 and the projected 1986 dollar amounts in each revenue, expense, and investment subaccount which these studies allocated to the various categories are the ones used in Pacific's Results of Operations (R/O) presentation.[3]

Pacific has changed its category analysis since its last rate proceeding by translating and regrouping its investment dollars from the Uniform System of Accounts (USOA), which identifies plant investment by type, to a Functional Accounting system which identifies plant investment by function. Pacific claims that this reorganization and the consequent further disaggregation of cost information allows investment-related costs to be assigned to service categories much more precisely. Thus, Scholl explained that where the accounting system provided sufficient detail, Pacific's investment-related costs and expenses were directly assigned to one of the service subcategories or to one of the cost components. Where this was not possible, Pacific used cost causative attribution methods to assign the costs.

Pacific's allocation rules are described by Kenneth G. Docter, a Price Waterhouse Certified Public Accountant, and Pacific witness, as being more detailed and complex than commonly used by major firms. Docter testified that he concluded that Pacific's information regarding the relative costs of categories of service was reliable after examin[ing] the major inputs to the embedded

3 Subsequently, in response to D.85-09-018, Scholl also provided cost adjustment factors for each of the studied categories in order to reconcile costs with the reduced R/O adopted in D.86-01-026 as modified by D.86-03-049. The adjustment factor for private line recurring costs is 89%.

analysis, review[ing] allocation rules and verif[ying] calculations for the major inputs. He explained that this process included tests of the processes Pacific used for accumulating costs and investments and allocating to the service categories, as well as tests of reconciliation to the projected 1986 books of account at the account level, the total Company level and the category level. He added: "We tested the computerized model to ensure that it functioned as described and followed the allocation logic which we had reviewed. In addition, we reviewed development of input ratios and the control processes in place in [Pacific's] Service Costs [department] to ensure input and processing integrity." See Exhibit 275, pp. 5-6.

Pacific's category analysis for private line shows total projected test year costs of $720 million and revenues of $320 million producing a negative $390 million contribution, an overall 0.4 revenue to cost ratio, a revenue to cost ratio for recurring rate services of 0.5, and a revenue to cost ratio for nonrecurring rate services of 0.3. See Exhibit 260, pp. 7-17.

Pacific conducted two studies of private line costs which, according to Pacific, incorporate the bottoms-up methodology as we required in D.84-06-111. One of these studies was for recurring costs and the other was for nonrecurring costs. In its brief Pacific asserts that its bottoms-up studies offer a valid and worthwhile comparison between "identifiable bottoms-up costs" and tops-down accounting costs adding that it is not reasonable to anticipate that a bottoms-up study process would capture each and every cost of a given service. Rather, the extent of any difference is a measure of the reasonableness of the tops-down results. Pacific concludes that the accuracy of its projected unit costs for both recurring and nonrecurring private line costs is demonstrated through its tops-down/bottoms-up reconciliation. The reconciliation shows a difference for total loop investment of $300 million, or less than 5% of total. By way of comparison, the difference in these two loop investment figures in Pacific's last general rate proceeding was $2.6 billion. See D.84-06-111, mimeo., at 167.

2. Specific Cost Studies

a. The Recurring Cost Study

Scholl describes the recurring cost study for private line as being an average historical cost analysis with additional information complying with D.83-04-012. The recurring study begins by identifying the station designs and central office equipment associated with each private line service offering. Eight private line cost elements were thus identified. They are:

* loop (sometimes called channel),
* central office service area transmission equipment (CO SAT),
* station service area transmission equipment (station SAT)[4],
* channel terminations, and
* interoffice trunk equipment (line haul and outside plant components),
* bridging,
* signaling, and
* conditioning.

The cost study identifies end channel termination investment per termination. Interoffice equipment investments are identified on a per mile basis within mileage bands. Investments in the remaining items are identified per local loop.

Pacific relied on its Facilities System data base for information about station designs and central office equipment.

4 Together, station SAT and CO SAT are sometimes referred to as Associated Channel Equipment or ACE.

Then it developed a current unit investment for equipment associated with each station design and an average historic unit investment for each piece of central office equipment. Its Continuing Property Record data base provided the information Pacific used to develop these bottoms-up unit investment figures. These unit investments were multiplied by their occurrences (volumes) at each type of service offering to determine total investment by service offering. Then these total investments per service offering were divided by the number of local channels in that service offering (also identified from the Facilities System data base) to develop a weighted average unit investment per local channel (loop) per service offering for CO SAT and station SAT.

In a separate bottoms-up study the Facilities System data base provided identification of channel terminations and circuit mileage, tracking the transmission medium; i.e. cable, analog carrier, digital carrier, or broadband; thereby allowing a determination of the number of end channel terminations, intermediate channel terminations, route miles, and equivalent air miles for specified mileage bands per service offering, per transmission type. These volumes were multiplied by the average embedded unit investment for channel terminations, and by the average embedded investment per mile for each transmission type (determined in yet another bottoms-up study giving average line haul, interoffice outside plant, and channel termination investments for each type of transmission technology). The results show channel termination investment, line haul investment, and interoffice outside plant investment per mileage band for each service offering.

Scholl testified that these total bottoms-up investments in each mileage band for each service offering were then divided by the total number of end channel terminations and by the total mileage to yield a weighted average investment per mile in each mileage band for line haul and interoffice outside plant and a weighted average investment per channel termination in each mileage band.

Pacific also derived a weighted average investment per loop. The separate loop cost study is described below.

Pacific's next step was to multiply these weighted unit investments by loading (or investment allocation) factors, computed individually for each cost element, to load for "secondary gross investments,"[5] producing a loaded unit investment for each of these cost elements.

To close the bottoms-up investments to the tops-down total gross investments, the loaded unit investments for line haul, outside plant, and channel terminations were then multiplied by facility system miles and channel terminations projected for the test year, and the loaded unit investments for station SAT and CO SAT were multiplied by billing record service quantities. The total of all service offerings thus derived yielded what Scholl describes as total bottoms-up loaded investment figures for these cost elements. A similar process was applied to loaded loop unit investment to obtain a total loaded investment figure.

Finally, the gross investment identified by the category analysis for each cost element was divided by the corresponding bottoms-up loaded total investment for that cost element. This produced the scaling factor for each cost element by which each corresponding bottoms-up loaded unit investment was multiplied to yield an Average Original Investment (AOI) for each cost element.

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5 Scholl explained that these loading factors were derived by dividing the gross investment determined by the category analysis model by the principle investment without any loadings, also determined through the category analysis process. Ex. 260, p. 5-46. The secondary gross investment would load for costs incidental to providing the particular service, such as office space, which would not be included in the annual cost factors described below.

Annual cost factors determined separately for each subcategory of service offerings and for each cost element within the subcategory were then applied to the AOI to determine the annual recurring cost of private line services. These cost factors were for return and taxes, maintenance, commercial and marketing, depreciation, general expense, and other taxes and charges.

Pacific's cost exhibit shows the ratio of total tops-down to total bottoms-up investment costs for all of private line, including loop, to be 1.03. (Exhibit 260, pp. 7-111.)

b. <u>The Local Loop Component of Recurring Costs</u>

Local loop makes up a significant portion of the recurring private line costs. Thus, one of the building blocks used to obtain the private line recurring costs above was input on local loop costs. According to Scholl, this input was derived from the separate service-specific bottoms-up loop study which depicts the average subscriber loop plant investments associated with each of the eight service classes studied. Five of these eight studies relate to private line. They are: telephone answering service (TAS), alarm central station, alarm patron, Voicegrade Data, and exchange-related private line. Scholl testified that the sampling approach Pacific used resulted in all private lines having an opportunity to be selected. Thus, these five functional service classes are designed to include all of the services provided in each of Pacific's private line service subcategories.

Using what Scholl describes as a bottoms-up technique the loop studies derived universe listings for each of the subcategories of private line service from certain existing mechanized data bases which contain all statewide working lines which Pacific bills.

A random sample of lines was selected for each of these service groupings, the cable and pair associated with each line was identified, and field engineers identified specific loop characteristics (cable gauge, plant account (aerial, buried or underground), and length) for each of these samples. This data was entered into a computer program called "Loop Category Analysis" which calculates the length of each loop by plant account (buried, aerial or underground) then totals all loops sampled for each service offering and gives a statewide average loop length for working plant for each service offering by plant account. The statistician refined these figures to produce final results of average length by account.

These average lengths for working plant for each plant account per service group together with overall total working plant length by account were used to create an allocation factor for each service offering. The allocation factors were then applied to total investment in booked outside plant and to drop and pair feet to determine total working plant investment per service offering.

Next, Pacific conducted what Scholl describes as a tops-down to bottoms-up reconciliation by assigning the results of Pacific's Ready-to-Serve (RTS) analysis in proportion to the average relative lengths of in-service loop for each service offering. See Exhibit 260, p. 5-25. The RTS is a separate tops-down private line loop study. Its purpose was to identify Pacific's entire investment in subscriber outside plant (i.e., loop) by putting a dollar value on the investment in that portion of plant which is not currently working, but is ready to serve, and is, according to Pacific, a reasonable and economic reserve. Assignment of the RTS results to the working plant investment produced what Scholl calls the embedded unit investment for the service offering.

To the embedded loop unit investment figure thus derived, Pacific then added annual loop plant category charge factors (for depreciation, return, taxes, maintenance, etc.)

developed from the tops-down category analysis, thus identifying annual cost for the loop portion of each service offering.

c. <u>The Nonrecurring Cost Study</u>

Pacific's bottoms-up nonrecurring private line study identifies the following types of private line investment:

* service order costs
* channel connect costs

Service order costs are defined by Scholl as those costs associated with the receipt, negotiation, processing and completion of a customer's request for private line service. Channel connect costs are those costs associated with the physical wiring and testing of a requested private line circuit or circuitry. The study produced unit costs by service offering and total cost by service offering. These service order and connection costs were derived by identifying the work components associated with these two activities and relying on panels of estimators with expertise in the areas to identify tasks required for various private line services and to provide average low, usual, and high work times for those tasks. These time estimates were used to compute average work times which were then multiplied by loaded labor rates to derive bottoms-up unit costs. Pacific provided data for 1984 actuals and projections for the test year using this methodology. Because we criticized the lack of explanation for the large discrepancy between Pacific's tops-down and bottoms-up results for nonrecurring costs in D.84-06-111, Pacific's filing this time includes a reconciliation for 1984 actuals which shows a closure factor of 1.2 and a 1986 projected closure factor, using the same methodology of 1.09. Scholl testified that a 94% adjustment factor should be applied to Pacific's nonrecurring cost projections for the test year to conform to the R/O adopted in D.85-01-034.

d. Incremental Cost Study

In D.84-06-111 (mimeo. at 294) we stated that we wished Pacific and other parties to address whether marginal cost analysis might be used as a basis for rate design decisions. To that end, Ordering Paragraph 16g ordered Pacific to file in the present proceeding an analysis of the relationship between incremental capital costs in the local network and incremental service demand for various services on a recent historical and prospective basis.

When we reviewed Pacific's incremental cost study plan in D.85-02-030 we clarified what we expected Pacific to produce in compliance with Paragraph 16g and we further found that the Paragraph 16g study was not likely to generate the sort of data on the incremental costs of providing particular services that we had hoped for. Therefore we required Pacific to submit a further incremental cost filing in this proceeding which would include: (1) an appropriate method for defining Pacific's incremental service costs for major service categories; (2) numerical estimates, to the extent available, of incremental costs defined by service category, calling characteristics (e.g., time of day), and subscriber density; and (3) for competitive or potentially competitive services, estimates of the relationship between Pacific's incremental service costs and the costs of competitive entry, with assessment of the relevance of these factors to rate design.

Pacific submitted its 16g study as ordered. The further study was filed as a part of Scholl's testimony in Exhibits 260 and 261. Exhibit 260 explained the three incremental cost methodologies used to look at the incremental capital costs associated with these major investment components of telephone plant: (1) customer loop plant, (2) interoffice facilities and equipment, and (3) switching equipment. Scholl testified that he used the engineering construct method for loop plant costs, the project or budget analysis technique for identifying the incremental capital costs of interoffice facilities and equipment (to be used as a building block for determining private line and usage services), and the statistical or regression technique for investigating the incremental capital costs of switching plant. Scholl explained that he chose to study only the loop plant portion of residential access service because that represents the greatest concentration of capital costs associated with residential access service. He does not state whether the same rationale was responsible for his decision to study the loop plant portion of business access service. However, it appears that private line loop is treated as a component of the business loop study.

The costs associated with loop plant were broken down both by residence and business categories, and by six density zones within each category. Exhibit 260 however, addressed only total plant level costs within each cost category, with some information about residence costs, but no specific business cost data.

Exhibit 261 provides supplemental incremental cost data for the loop portion of the Exhibit 260 study, at both the plant element level and the more disaggregated customer type level (business or residence) and the six subscriber density zones per customer type. The plant level estimate used a sample of about 5000 working loops to determine loop characteristics, including type of construction used and loop length. These characteristics were used to calculate the average statewide investment required to construct new loops. Then average customer loop incremental investments were calculated for each of the six density zones and a statewide weighted average incremental loop investment was calculated from the investments within each zone. Additional incremental capital costs for return, income tax and depreciation factors were applied to these investments to determine the capital costs associated with them. The results of this study varied somewhat from the results of the Exhibit 260 study, but still showed that subscriber loop incremental costs are considerably higher than embedded costs.

The same 5000 loop sample which was used in the studies above was disaggregated into residence and business components and each of these was further stratified into the six density zones in order to produce residence- and business-specific loop characteristics for each density zone. From these characteristics incremental customer specific loop investments were calculated, and this figure was used, as described above, to calculate a customer group specific statewide weighted average incremental investment for each density zone.

Scholl testified that the incremental capital costs were calculated using the same methodology as that described for the loop investments described above.

Based on this methodology Scholl's Exhibit 261 at p. 4.3 shows an average incremental loop investment per working business loop of $600 (residence is more) and an average incremental monthly capital cost per working business loop of $9 (residence is more). His statewide average figure for capital costs in Exhibit 260 was different (over twice as high) from the figure in Exhibit 261 ($10), but he testified that the latter study figures are more precise. Exhibit 261 does not show much cost variation for business service incremental capital cost based on density zone. The bar graph at p. 4-4 shows a range of between about $7.50 and $11, while the residence range is between $5 and $25. No figures are presented for the range of incremental investment for business service by density zone.

Private line was not a service which Pacific treated as competitive or potentially competitive. Thus it made no estimate of the relationship between its private line incremental service costs and the costs of competitive entry. Further, Pacific did not use its incremental cost studies as the basis for any of its pricing proposals.

C. DRA's Critique and Its Own Private Line Rate Design Proposal

1. Recurring Costs

In Chapter 11 of DRA's cost of service report, Exhibit 329, Shankey, DRA's private line witness, stated that DRA did not have the resources to review Pacific's tops-down recurring cost studies, and was only commenting on Pacific's methodology for determining these investment-related recurring costs. He testified that DRA supports the methodology Pacific used to derive its tops-down unit investments, but objects to Pacific's use of the Functional Accounting system rather than the USOA for determining costs.

Shankey explained the accounting format objection on two grounds. First, he stated that this Commission does not recognize the Functional Accounting format. Second, he seems to say that DRA would not object if the bottoms-up cost studies were truly stand alone studies, but asserts that because the investment-related costs allocated to private line services were allocated based on ratios with tops-down studies, which DRA did not have the resources to review, DRA cannot be sure of their accuracy. Further, Shankey added that this use of the Functional Accounting format is inconsistent with all Pacific's other filings, and for that additional reason prevents comparison and tracking for accuracy.

Shankey went on to note that in lieu of a conversion of Pacific's cost study results into a USOA format DRA had met with Pacific and agreed to consider two sets of adjustment factors provided by Pacific to adjust Pacific's cost studies. One was to reflect Pacific's R/O as set forth in the joint R/O comparison exhibit, and the other was to reflect DRA's R/O from the comparison exhibit. In later testimony, however, Shankey testified that DRA found the methodology Pacific used to develop the adjustment factors to be unacceptable because it used Functional Accounting translations which could not be reviewed and tested. Shankey added that it would be inappropriate to apply Pacific's cost adjustment factors across the board in the individual service cost studies because the quality of Pacific's cost analysis was not consistent. Instead, DRA applied an across-the-board adjustment factor of 85% to Pacific's figures. Shankey explained that factor represents the approximate difference between the aggregate costs which Pacific estimated for test year 1986 and the level of aggregate costs found reasonable by the Commission in D.86-01-026 (as modified by D.86-03-049). (Exhibit 330, pp. 8-9.)

Shankey also criticized Pacific's recurring service volume information for relying on information from only two points in time, June 1982 and June 1983. He claims that DRA's volume calculations based on five quarterly reports from Pacific's Private Line History File 9PLHF) are more representative of in-service volumes which can be expected for the test year.

In his rebuttal testimony, Exhibit 412, Shankey offers his opinion that Pacific's cost studies are in compliance with the Cost Manual guidelines. He explains that this Commission found tops-down allocation of some expenses to be proper in a bottoms-up cost development, and states that it is therefore up to Pacific to show that it has used those allocations properly. It is up to the Commission to decide to accept or reject Pacific's explanation. (Exhibit 412 at p. 2.)

DRA's opening brief advances this same position, adding that DRA agrees with Scholl's rebuttal testimony that Pacific did conduct a bottoms-up investigation of private line investment and that Pacific's tops-down cost study is validated by its reconciliation with this recurring bottoms-up cost study. In fact, DRA states that Pacific's bottoms-up study was an extensive and thorough study and adds that Pacific has made great strides in improving its private line cost study. The focus of DRA's concern with Pacific's cost studies is Pacific's use of the Functional Accounting format, and DRA's inability to analyze expense allocations derived from this format. DRA suggests that it had hoped Pacific's adjustment factors would be developed in a way that would allow their application to individual service accounts reported in the Functional Accounting format. When that proved not to be true DRA decided, as Shankey testified, that it would be more reasonable to rely on Pacific's overall adjustment factor than the one it developed specifically for private line.

2. Nonrecurring Costs

DRA developed its own nonrecurring private line cost projections. They are set out in Chapter 11 of Exhibit 329, DRA's cost of service report. Chapter 11 was prepared by Shankey. In that report DRA supports Pacific's nonrecurring cost study methodology, but finds the costs to be overstated. DRA's analysis of nonrecurring costs focuses on the activity times which Pacific used in its nonrecurring cost calculations. Shankey made field inspections at Pacific's facilities and observed the activities of Pacific personnel involved in the provisioning of private line services. He decided to conduct time and motion studies of work times for major tasks from a representative service offering in order to assess the reasonableness of Pacific's activity times, since his casual observations of the work groups' activities lead him to believe that significant reductions in personnel were possible. The 3002 4-wire voice grade (3002 4WVG) circuit was selected as the representative circuit. The time and motion studies were conducted on employees in each of the ten major work groups involved in provisioning 3002 4WVG service.

The studies eliminated nonproductive time and then added a standard allowance of 15% to account for personal, fatigue and delay time. The times DRA computed were then compared to the times recorded by Pacific to derive a ratio. The ratio was applied to Pacific's total activity time. The activity times thus adjusted were then multiplied by the fully assigned labor rates which Shankey adjusted by the ratio of the staff wage escalation factor as presented in DRA's R/O showing, to Pacific's wage escalation factor, to produce adjusted unit costs for the representative channel connect activity and the representative service order activity. The ratio between these DRA-adjusted unit cost and Pacific's unit costs were used as overall private line adjustment factors to be applied to Pacific's projected nonrecurring costs. The adjustment factor derived for channel connect activity was 0.798, that for service order activity was 0.486.

DRA contends that Pacific's proposed 25% increase in nonrecurring charges is much too low in light of its very low revenue to cost ratio (0.3 according to Pacific's cost studies). Therefore, DRA proposes increasing nonrecurring rates by 100% or to DRA estimated cost, whichever is less. No increases are proposed for new services such as DDS and HiCap transport service because they are, according to Shankey, new and therefore do not have as low a revenue to cost relationship.

In Exhibit 329, Shankey reported that DRA was unable to clarify the source of Pacific's forecasted 1986 nonrecurring volumes. DRA used different volumes, as described below. The overall effect of DRA's proposal, even with application of the cost adjustment factor, and different volume projections is a revenue increase for nonrecurring services of about $20 million for the test year.

3. <u>DRA's Position</u>

Even with its change in the adjustment factor, its reduction of the activity cost estimates in Pacific's recurring cost study, which resulted in a reduction of about $24 million from Pacific' recurring cost estimates, and its adjustments to Pacific's nonrecurring cost study, DRA argues that it is reasonable to authorize a large private line rate increase. In fact, as shown in Appendix A to Exhibit 330, DRA proposes a larger total test year rate increase than Pacific, at $67.540 million. However, since it does not propose incremental increases for the following two years, the result at the end of three years is that DRA's proposal would continue to produce revenues $67.540 million higher than present revenues while Pacific's rates would produce revenues $106.600 million higher than present. In its post-hearing brief, DRA sets the projected private line revenue increase from its proposed rate design a little higher, at about $68.1 million.

DRA's proposed rates were devised by establishing a revenue to cost ratio, after adjusting Pacific's rates as described above, for each private line cost element and service offering. Where the overall ratio was found to be greater than 1.0, no rate change was proposed. Further, DRA's proposed rates rely on in-service volumes for 1986 based on third quarter 1985 actual data from the PLHF report grown to mid-year 1986, and the inward movement volumes are based on recorded activity for the first nine months of 1985 grown for 1986.

DRA opposes Pacific's proposal to deaverage local loop rates into two subcategories based on geographical cost differences. For one thing, DRA asserts that it is unlikely that the cutoff point of 76% of loops being placed in the low cost Schedule I category will remain constant, and adds that the ratio has little validity on a per-service-offering basis. For another, DRA notes that loop costs are driven primarily by loop length, and Pacific's proposal would inequitably charge customers served from a high cost wire center at the premium rate no matter what their distance from the wire center might be. Shankey also claims that Pacific's private line volume data have been too inaccurate in the past to allow for reasonable reliance on such a classification of wire centers. And, DRA claims that such a scheme violates Section 453(c) of the Public Utilities Code by discriminating unreasonably among users. Instead, DRA proposes increasing local loop recurring rates by 50% or to DRA's estimated cost, whichever is less. The outcome is that DRA's rate design raises most local loop rates by 50%.

Noting that services utilized to provide telephone answering service were exempted when this Commission ordered the restructuring of private line and private line-like services mileage sensitive rate elements from rate center to rate center pricing to wire center to wire center pricing, Shankey testified that if the exemption were removed now DRA's proposal would increase recurring rates by more than 50%. Therefore, DRA's rate design leaves the present pricing structure, raises recurring rates by 50% for secretarial lines and concentrator-identifier lines, and recommends that Pacific be ordered to submit a study of the revenue impacts of restructuring the mileage sensitive rate elements applicable to TAS services to a wire center to wire center rate structure. DRA adds that it still supports a single averaged rate for the service charges for designed and nondesigned secretarial lines, but if the Commission permits the establishment of two separate rates, the 100% increase limitation should be disregarded and both rates should be set at cost. However, Shantz stated that the tariff should leave the final decision about the most economical manner for providing the service with Pacific.

DRA opposes adding a new tariff schedule for Alarm Transport services, arguing that it offers preferential treatment to alarm services which unreasonably burdens the general body of ratepayers. Shankey also argues that adding a new rate schedule further complicates Pacific's ability to properly and accurately render bills and to track in-service and inward movement data. He states that leaving Alarm Transport services in their present schedules will assist Pacific in developing better volume data for forecasting and analysis purposes and more accurate billing.

As a final note, DRA reminds us that several ITCs in California concur in Pacific's private line and private line-like tariffs. Thus, we must consider the impact on customer billing for those utilities as well.

D. The Critique and Proposal of CBCHA/TCA

CBCHA/TCA oppose both Pacific's and DRA's private line proposals on the ground that there is no adequate cost support to show that private line is underpriced at present. In explanation, CBCHA/TCA point to the fact that Pacific's cost studies were conducted using the revenue requirement which it projected before our R/O decision, D.86-01-026, which reduced that test year revenue requirement proposal by about 12%. CBCHA/TCA argue that the adjustment factors we ordered Pacific to develop are insufficient to assure accurate rates because developments in Phase II of the R/O proceeding, and other Pacific cases, including the 1987 attrition decision, D.86-12-099, have or will change the revenue requirement again. Further, CBCHA/TCA's Selwyn contends that Scholl's claim that the adjustment factors are only accurate at the service category level is preposterous, and CBCHA/TCA add that if we do adopt Pacific's 89% adjustment factor for private line, we should, at a minimum, do it by reducing each of the cost elements by 11% as Selwyn illustrated in Table 10 to his testimony, Exhibit 361.

CBCHA/TCA also assert that Pacific's application of average unit investment figures based on its books of account to, for example, the bottoms-up derived average number of feet by plant type in its private line loop study make that study a tops-down study, not a bottoms-up study as this Commission ordered. Further, they argue that Pacific's AOI fails to reflect the age of the facilities, and therefore may reflect incremental or replacement cost rather than embedded historical cost. Also, CBCHA/TCA's post-hearing brief faults Pacific's study for simply adding an amount to reflect nonworking facilities, without determining the actual spare capacity required to provide the particular service in question. They add that this step also converts the cost study into a tops-down study. Finally, CBCHA/TCA argue that Pacific's reconciliation of its cost study calculations to its tops-down assigned expenses makes its use of factors to calculate recurring costs flawed, and makes the factoring process inherently a tops-down study. Because of each of these perceived flaws CBCHA/TCA state that any increase in Pacific's private line rates must be very moderate.

Turning to specific costs, CBCHA/TCA dispute Pacific's assignment of its Switched Access Remote Testing System (SARTS) investment and related costs exclusively to private line. Claiming that labor expense savings which result from not needing the frame technician and field repairman when SARTS is used are not likewise being assigned solely to private line, Selwyn argues that if this cannot be done then that savings is being unfairly spread across all services and the only fair solution is to likewise spread the cost of SARTS across all services. He calculates that this reduces annual cost for CO SAT, after applying the .89 rate case scaling factor, from \$250 to \$134. (Before applying the scaling factor, the figure is about \$150.)

While asserting that they do not know precisely what private line service costs are, CBCHA/TCA concede that the revenue to cost ratio is probably less than 1.0 presently. They therefore acknowledge that a moderate rate increase may be in order. However, they further argue that any such increase must take into account the differences in cost between private line services in dense metropolitan areas and in spread-out suburban and rural areas as well as the differences created by the size or amount of service at a given location and by the length of the commitment of the customer to the service as discussed by Selwyn. CBCHA/TCA add that average rates expose Pacific to the risk of uneconomic bypass in that the customer may obtain service at a rate below Pacific's averaged rate, but in excess of its actual cost. CBCHA/TCA do not find Pacific's dual rate plan for loop rates is a good way to accomplish this. Instead Selwyn suggests concentrating on the six Pacific wire centers which contain 10% of all private line loops and have costs less than 50% of the statewide average, and making them one group for rate purposes. He proposes a second group of wire centers representing another 27% of loops, which exhibit loop costs between 50% and 75% of the statewide average. Selwyn's proposed rate design applies the cost factors for each of these three schedules, and the .89 rate case scaling factor, as well as his assumption that 4-wire loop is not twice the cost of 2-wire loop to arrive at the loop rate proposal set out in Table 13 to Exhibit 361. CBCHA/TCA recommend adopting the other private line rate elements proposed by Pacific for the first year, but they oppose any further increases in years 2 and 3 on the grounds that the cost studies are too defective and the revenue requirement is too unsettled.

Finally, citing DRA's failure or refusal to evaluate critically the PacBell cost studies, and citing what it describes as an inconsistency between DRA's criticism in Exhibit 329 (distributed in December 1985) of Pacific's use of ratios based on tops-down studies in its bottoms-up study, Pacific's use of the Functional Accounting format, and Pacific's use of forecasted service volumes in its cost study, with DRA's July 1986 rate design testimony, Exhibit 351, advocating large private line increases, CBCHA/TCA submits that DRA's position must be rejected.

E. The Critique of API

API Alarm Systems, Inc. (API) criticizes Pacific's recurring and nonrecurring cost studies as they affect the provision of alarm circuits as well as DRA's private line rate recommendations. It concludes that all services, including alarms services should benefit from revenue requirement reductions which have occurred and will occur as a result of this proceeding.

1. Pacific's Recurring Cost Study and Incremental Cost Analysis

Like CBCHA/TCA, but focusing on 3002 private line alarm transport services, API argues that Pacific's recurring cost studies overstate costs by directly assigning investment and expenses for SARTS testing technology to certain private line services while spreading the related savings to all service categories. API's witness, W. Kenneth Edwards, testified that he believed that Pacific's rate and cost personnel have improperly allocated SARTS investment. He points, for example, to Exhibit 273 which contains work papers showing the assignment of testboard investment for SARTS and SMAS (Switched Maintenance Access System) used to determine loaded unit investment for CO SAT. That exhibit shows no assignment to 3002C-type circuits for SARTS/SMAS, but does show it for other circuits, including 3002A/B. Edwards testified that it was widely known that SARTS/SMAS is used to test 3002C service, and he went on to note that Pacific did assume wiring of a SARTS/SMAS access points to 3002 service in developing its nonrecurring costs. API acknowledges that Scholl testified in rebuttal that there should have been a SARTS investment assigned to 3002C service and that doing so would produce an annual unit CO SAT cost of $260 per 3002C circuit rather than the $180 identified in his cost exhibit, Exhibit 260.

Edwards states that Pacific's failure to show a reduction in the maintenance carrying charge for the offerings to which the SARTS/SMAS technology is assigned also causes an overstatement of costs. API's closing brief suggests that Scholl should have assigned savings to the 3002C service when he calculated the SARTS investment.

API also endorses Selwyn's claim that Pacific's labor savings have not been appropriately assigned to private line and his proposal for reducing total testboard investment for all private line services. API further asserts that there is no evidence that the Pacific private line customers who are paying for SARTS have received any other consequential benefits from their expenditures. API concludes that this Commission should either adjust the allocation of SARTS investment and savings as Selwyn recommends or disallow some or all of the costs of the SARTS program and remove those costs from all rate elements to which they have been assigned as Edwards recommends.

According to Edwards' calculations, Pacific's annual testing labor expense savings due to SARTS use is $96.6 million. He added that one could effectively and reliably double this amount of savings to reflect other savings that would emanate from implementing SARTS testing. He opined that Pacific has thus saved a minimum of $193 million on a service category-wide basis. Edwards apparently proposes spreading this expense over Pacific's service categories as an alternative to Selwyn's proposal. API goes on to note that Scholl identified hypothetical savings for 1986 which had resulted from implementation of the SSIMS project, of which SARTS is a component, at about $33 million.

API asserts that Ordering Paragraph 17 of D.86-01-026 which ordered Pacific to continue preparing its Report on the Results of Operations in the same general format employed in the R/O phase of this proceeding (i.e., using USOA accounting), and Shankey's testimony that Pacific's use of Functional Accounting created problems in tying Functional Accounting investments and allocations back to the R/O expenses, are reasons to reject the accuracy of Pacific's allocation of SARTS savings to the private line category through its use of Functional Accounting. API also cites what it claims to be contradictory statements by Scholl about whether SARTS is really only used for private line testing, and adds that these recurring cost studies are also affected by wide discrepancies in volumes.

For all these reasons, API urges this Commission to reject Pacific's private line recurring cost studies.

Turning to Pacific's incremental cost information, API takes the position that Pacific's incremental cost conclusions should be rejected because they fail to consider cost-reducing effects of derived channel service, i.e., Pacific's Poll Star alarm service technology, which Pacific used for the first time during the test year, and because Pacific's subscriber loop incremental cost study erroneously assumes no utilization of existing plant to satisfy additional demand, and uses inconsistent fill factor assumptions to account for spare capacity requirements.

2. Pacific's Nonrecurring Cost Study

API also urges that none of Pacific's nonrecurring rate increases be granted on the ground that discrepancies in Pacific's loading of labor rates, its time estimates for nonrecurring tasks, its recognition of efficiencies as identified in Exhibit 403, and its volume projections make the cost study unreliable.

With regard to labor rates, API points to three specific items which it believes to be unreasonable. First is the loaded labor rate element. In Pacific's example in Exhibit 334, it provides for $3.56 for paid absence and productive wages and salaries of $11.22 for a given employee. Edwards asserts that the paid absence amounts to 31% of wages, which he claims translates to an unreasonable 16 weeks of vacation or nonproductive time.

Within the same exhibit is reference to average work time hours/day of 4.55. Edwards testified that the methodologies used to calculate these labor rates would mean that rates per hour range from $37.52 to $61.54 and that Pacific was therefore spending from $78,000 to $120,000 on these employees, making the loads on actual wages three to four times the wage in many cases. API states that this is also unreasonable since, if it were correct, Pacific would have been operating with a negative cashflow.

Based on the personal observations of Edwards and the observations and experience of API's witness, Diane Martinez, API asserts that Pacific's panel of estimators overstated the frequency of occurrence of certain tasks. Martinez argued that Pacific's cost study overstates the costs of provisioning 3002C 2-wire bridged alarm private line service by at least 50%. Martinez based this opinion on her work at Pacific where she worked as an alarm service representative and, for a time, trained others to do that job. She apparently left Pacific something over one year before her testimony was prepared.

In support of her opinion she claims in Exhibit 354 that Pacific's Exhibit 271 overstates both the amount of time necessary to do certain tasks and the need for certain work groups to be involved in the task at all. She states that activity times designated for service representatives in Exhibit 271 do not reflect the streamlining mechanization or automation of the operation that has taken place in recent years. For example, she claims that order writers as a result of mechanization or automation no longer perform any tasks with respect to any private line alarm service order. Further, she states that the MA or "marketing administrator" virtually is never involved with respect to the provisioning of 2-wire private line alarm services. She concludes that the combined times of up to 74.4 minutes shown for the service representative, order writer, and marketing MA for processing a 3002C order ought to be 5 to 10 minutes. She also asserts that the activity time of 12.9 minutes for the NTEC to review order is unreasonably high.

As another example, Martinez suggests that task code 204, "update force mgmt sys," should not have an occurrence factor of 100% since it is apparently only done when there is a cancellation or due date change to the information already in the force management system.

API makes reference to Exhibit 403, Pacific's Special Services Administration Task Force Report (SSA Report), which, because it was prepared between one and two years after Pacific's nonrecurring costs were developed by its panel of estimators, identifies many instances where both recurring and non-recurring private line ("Special Services") provisioning has been streamlined resulting in concrete savings of many millions of dollars in the test year. API suggests that this report dooms the accuracy of the study results Scholl presented.

API also points out that the testimony of J. M. Swenson, filed in the utilization phase of this proceeding, stated that Pacific would process over three million inward service orders for residence and single line business customers in the test year, and that the annual capital cost for its 25 million idle assigned pairs would produce a savings of $84 million in expense by eliminating the need for installation visits and additional assignment costs. Exhibit 577, p. 19. Edwards states that Swenson's figures produce a cost of $28 for the assignment and installation of residence and single line business customers, while the nonrecurring cost study shows just the assignment cost for 3002C 2-wire loops to be $49 and the installation cost to be another $200. Based on these differences API argues that Swenson's testimony tends to discredit Scholl's cost of service claims relatively more than Scholl's studies discredit Swenson's claims, because of Swenson's greater familiarity with the plant itself. Swenson is Pacific's division staff manager in charge of engineering.

Turning to volume projections API asserts that Pacific's cost studies show inconsistencies. Edwards noted, as an example, that Exhibit 273 identifies 745 type 3002C channels, and that Pacific work papers assume approximately three local channels per circuit, but that another work paper showed 745 channels and 19,608 circuits, a phenomenon, which API describes as a physical impossibility. Further, Edwards testified that Sullivan's Exhibit 267 shows 14,000 type 3002C loops as opposed to the 745 shown in Exhibit 273 and the 14,041 shown in Exhibit 332. API states that the use of "internally consistent" incorrect volumes does not result in a wash as the Company brief apparently contends. Instead, asserts API, the result will be an "internally consistent" incorrect rate and incorrect earnings level--and not a correct development of rates.

3. DRA's Private Line Rate Recommendations

API urges this Commission to reject DRA's private line proposal as not being the result of independent analysis, and being the result of impaired objectivity brought on by either Shankey's excessive reliance upon, or erroneous interpretation of, prior Commission orders. API claims that Shankey's testimony demonstrated uncritical acceptance of Pacific's recurring costs which merely adjusted these costs to reflect the R/O decision. Edwards claims that such factoring adjustments will replicate the Pacific cost study discrepancies about which he testified.

API finds DRA's review of Pacific's nonrecurring costs to be better, but Edwards testified that Shankey improperly adjusted labor times by a factor that resulted in a double count. API also finds it inappropriate that Shankey's projected volumes were primarily the result of using Pacific's PLHF data, together with an adjustment factor jointly developed by Shankey and the Company.

Likewise API asserts that Shankey should not have accepted Pacific's loaded labor rates, and then only applied the R/O factor and his own factor to account for nonproductive time.

API states that Shankey's approach to Pacific's cost studies was result-oriented and therefore not as objective as it should have been in that he began with the notion that private line services were priced below costs. Further, API notes that Shankey was unaware of the results of the "Robin & Dackerman Report," Exhibit 401, or the SSA Report, Exhibit 403, and that this later information is another factor which reduces the value of DRA's recommendations for alarm services increases.

4. Import of the Robin & Dackerman Report and the SSA Report

These two reports, Exhibits 401 and 403, were received during the rebuttal phase of this proceeding. API contends that the former provides important evidence that both Pacific Bell personnel and its outside consultants viewed its private line cost studies as suspect and biased. Further, it submits that the SSA Report shows that approximately $160 million in savings have been and will be achieved in future years. API concludes that together these reports confirm the contradictions of Pacific's private line cost study.

F. The Critique of WBFAA

1. Introduction and Background

Like CBCHA/TCA the preference of Western Burglar and Fire Alarm Association (WBFAA) is that rate design be foregone until Pacific's next general rate case and, in the meantime, the surcharge now in place be continued, so that all ratepayers can benefit equally from Pacific's revenue requirement reduction. WBFAA opposes rate design changes because Pacific's uncertain cost studies, unclear revenue projections, and murky view of the future might, in its opinion, result in Pacific realizing unanticipated and undeserved revenues, and irreparable harm to the ratepayers. Should we choose to adopt a new rate design, WBFAA urges this Commission to adopt Pacific's proposal to separately tariff alarm transport services, its proposal to create two private line local loop rate schedules, and its test year recurring rate design for alarm transport services, but to reject Pacific's nonrecurring rate design for alarm transport services and its proposal for further alarm transport services in the second and third years, as well as DRA's proposals for recurring and nonrecurring rates for alarm transport services. WBFAA also asks that we refuse to consider any further private line rate increases until Pacific demonstrates that it can and will comply with the costing methodologies prescribed in the Cost Manual.

WBFAA is an association representing over 500, mostly small, burglar and fire alarm companies and equipment manufacturers in California. Rod Uffindell, current president of WBFAA and the owner and president of an alarm company, testified that the private line services utilized by the alarm industry include 1009, 3002C, 3007, 3009, DSAS, and Poll Star. He added: DSAS and Poll Star are already separately tariffed services. It makes sense to use the same treatment for those private lines services that are unique to alarm services. (Exhibit 367, p. 16.) He explained that Poll Star is a derived channel or quasi private line service which is piggy-backed onto the customer's regular telephone service. He went on to note that 1009 services, including 1009A direct wire service and 1009B/C McCulloh service, are used exclusively by the alarm industry. He pointed out that, in addition to these alarm circuits, alarm companies also transmit alarm signals using either ordinary business lines or 800 service, and to a very limited extent, cable TV facilities and long range radio.

He explained that most alarm service subscribers use 1009 service but that many companies have installed multiplex receiving equipment which utilizes the voice grade 3002C bridged alarm service. He further stated that he was reluctant to make the investment necessary to use Poll Star because some Pacific employees have told him that Poll Star will be replaced with other technology and he fears he may end up with stranded investment.

2. <u>Pacific's Recurring Cost Study</u>

Central to WBFAA's criticism of Pacific's recurring cost study is its assertion that Pacific's volume information is not reliable. Choosing one of the private line services which it utilizes, 3002C, WBFAA asserts that the volumes used in Pacific's recurring cost studies and presented by Scholl in Exhibit 260, shows both a lack of understanding of how the service is used, and Pacific's failure to verify the information it presented. WBFAA points out the inaccuracy in the volume used for 3002C patron loops which Scholl acknowledged in his rebuttal testimony, Exhibit 402. WBFAA argues that the revisions Scholl submitted in Exhibit 402 also have volume errors since they show 11,382 full duplex (FDX) patron loops, and only 2,216 half duplex (HDX) patron loops though

Scholl acknowledged that the predominance of patron loops are HDX, which is less costly than FDX.

WBFAA also points out that Scholl's count of local loop volumes was 14% higher than the loop counts used by Sullivan. According to the testimony of WBFAA's economic consultant, Charles W. King, since Scholl allocated 80% of private line recurring cost and 95% of alarm private line recurring cost based on his overstated local loop count, an extra $72.3 million in investment costs was assigned to private line service that would not have been assigned using Sullivan's counts.

In response to Scholl's testimony that volume differences do not matter because both revenues and costs would change correspondingly and financial performance is a function of the relationship between unit costs and rates rather than the value of the category totals, WBFAA asserts that since aggregate investment was determined by multiplying unit costs by overstated unit volumes, Pacific's bottoms-up investment was overstated. Further, WBFAA contends that because tops-down investment is based on the proportion of private line local loops relative to total working loops for all service categories and since private line loop count was overstated by 14%, the allocation of most central office and all subscriber outside plant to private line would be correspondingly overstated, thus overstating tops-down investment too. Likewise, WBFAA claims that Pacific's revenue to cost ratios, which were developed by comparing these tops-down costs allocated among services based on overstated unit counts with actual revenues, are understated.

3. Tops-Down and Bottoms-Up Reconciliation

It is WBFAA's position that Pacific's bottoms-up studies are not true bottoms-up studies and therefore, there can be no real tops-down and bottoms-up reconciliation as our Cost Manual requires. Noting that Pacific's 1983 bottoms-up loop study for developing unit cost, identified the primary cost-causing characteristics of cable size, gauge, year of placement, and fill factor for each section of the cable, including the bridge tap, and that a computer program then applied unit capital cost dollars per pair foot by cable type, cable size and gauge for each of the loops, King asserts that the later loop study Pacific conducted for this proceeding has abandoned the procedure of synthesizing investment cost from actual, identified loop plant facilities which Pacific used in the 1983 loop study, for a plan which uses bottoms-up data from the sampled loops for the purpose of developing allocators to distribute the tops-down totals of subscriber access outside plant by primary plant account. He goes on to state: The synthesis of actual facilities costs is limited to central office equipment and interoffice outside plant. Loop plant is allocated from investment totals. (Exhibit 365, p. 9.) King argues that this is not a true bottoms-up cost study, and fails to meet the bottoms-up study criteria we set forth in D.85-02-030. WBFAA concludes that these facts justify our rejection of Pacific's rate design proposals.

4. Unexplained Loop Investment

WBFAA also argues that just as it did in the last rate case, Pacific has a great deal of unexplained subscriber loop investment. Via different sorts of calculations King suggests that this amount might be $3 billion, $2 billion, or $1.82 billion. The first figure is calculated by first comparing what he describes as Scholl's tops-down average loop cost of $515 to the 1984 tops-down amount of $441, and then applying the percentage difference to the 1984 bottoms-up unit cost and multiplying the difference between these two figures by 13.1 million, the number of working loops in Pacific's system.

WBFAA dismisses Scholl's explanation that the 1984 study did not properly account for ready-to-serve plant, by asserting that the 1984 study did include an allowance for RTS, and that the only use made of the RTS study in the present case is to inflate the kilofeet assigned to each service. WBFAA adds that even if it assumes Scholl is correct and adjusts its trended bottoms-up cost by 10% to reflect the failure of the earlier study's fill factor to include Pacific's estimate of "restricted" cable, there is still $2 billion unaccounted for.

Citing, as did API, the testimony of J. M. Swenson in the utilization phase of this proceeding (Exhibit 578), WBFAA adds the amount his testimony shows for investment per additional loop added from 1982 to 1985 related to feeder cable, and the amount of additional distribution cable, and dividing that sum by the number of available pairs added during those years arrives at an incremental investment per cable pair. Using that figure, WBFAA derives an average embedded cost per cable pair to which it then applies an outside plant utilization factor of 66.3% from Exhibit 412. The shortfall thus derived is then multiplied by the number of Pacific's loops to obtain the unexplained investment figure of $1.82 billion.

WBFAA also claims that Pacific's idle distribution loop plant quantities result in private line costs with unproven and probably unreasonable overheads. WBFAA suggests that it might be appropriate to allocate the cost of particular idle distribution to particular service, and states that since private lines are most often placed in high density locations it is likely that their requirement for redundant distribution cable pairs is significantly less than business and residence exchange lines.

5. Pacific's Nonrecurring Cost Study

Again WBFAA points to the discrepancies between the volumes in Scholl's studies and in Sullivan's work papers for 3002C service for the purpose of discrediting the service order volume projections proffered by Pacific. WBFAA pointed out that there are 26 patron loops for every sponsor loop. Uffindell testified that it was thus not credible for Pacific to attribute the same factors for patron and sponsor loop provision. Further, WBFAA asserts that Pacific's attribution of loop provisioning should trend downward because as the network expands and bridges are installed it is more likely that the simplest design loops will be provisioned.

Based on various calculations made by King, WBFAA states its belief that Pacific's nonrecurring costs were overstated by 28% or at least $30 million. It specifies that the cost study's 57M circuit central office equipment moves and changes costs and PADS (Pacific Administration Design Services) costs were overstated by 34% each due to Scholl's count of channel connections being 34% higher than Sullivan's, and that the other major item, inside wire costs were overstated by 60%, or $17.1 million, as a result of the FCC's detariffing of inside wire which became effective on January 1, 1987. (The FCC decision was issued after Pacific's studies were done). Altogether, WBFAA's claims of overstated costs would reduce Pacific's tops-down nonrecurring costs from $110.3 million to $79.9 million.

WBFAA also asserts that the company's work times were exaggerated and inaccurate, e.g. simple designs for a service had higher work times than more complex designs for the same service, work activity time for taking a patron loop order was erroneously assigned to an employee who was not involved in the process, travel times for going to the same account premises were different for different tasks. Further, WBFAA claims that Pacific's labor costs are excessive in that they have risen disproportionately since Pacific's last rate proceeding, and they show unreasonably low ratios of productive to nonproductive time.

6. <u>DRA's Cost Review</u>

WBFAA argues that Shankey's review of Pacific's nonrecurring costs should not be adopted because it only looked at one service and then applied the same findings to the remaining 62 services. WBFAA states that such an approach frustrates the very concept of disaggregation. WBFAA also claims that because rates for private line have increased much faster than inflation, and faster than exchange rates since 1979, DRA's goal of focusing on private line rates is unjustified.

7. Rate Design Proposals

WBFAA maintains that it makes sense for Pacific to separately tariff alarm transport services because Poll Star and DSAS are separately tariffed and telephone answering services are separately tariffed, and because it is consistent with the manner in which cost studies are performed, and will assist in the implementation of General Order 152 regarding service standards for the alarm industry. WBFAA claims that it makes sense to adopt dual loop schedules because it is logical to disaggregate rates just as costs for loops have been disaggregated.

Turning to nonrecurring rates, WBFAA claims that 1009 service demand is already on the decline due in part to prior increases in the nonrecurring charge for this service. Therefore, it urges caution in granting any further increases for 1009 service. It asserts, however, that the increase proposed for 3002C service from $179 to $275 plus the $14 bridging charge is more significant. WBFAA points out that this service cost $40 in 1979, and argues that nonrecurring costs are dropping, and that cost studies do not validate these rates.

WBFAA states that Sullivan's rate proposal for 3002C service would cause rate shock for alarm companies and require them to raise their customer's rates by large percentages. Uffindell testified that he would have to raise his rates to 3002 customers from $45 per month to $60.75 per month to recover the DRA-proposed recurring rate increases and maintain the same gross profit margin. WBFAA argues that granting these requested increases will result in a stranding of the alarm companies' investment in their 3002C receiving equipment and in Pacific's existing bridged alarm network. WBFAA also argues that DRA's proposal would increase rates beyond what AT&T charges for the same service on an interLATA basis.

As for Pacific's proposal for second and third year private line increases, WBFAA urges that they be denied due to the probability that Pacific's revenue requirement will decrease in the future, and Pacific's inability to reasonably approximate its costs and revenues for the future.

G. FEA's Position

FEA claims that Pacific's data on the price elasticity of demand for private line services, as shown in the addendum to Baughcum's testimony, Exhibit 360, show that rate increases of the magnitude proposed by Pacific and DRA will adversely impact private line users, cause a reduction in volumes of up to 11.38%, and result in self-supply or bypass by many private line customers. FEA points to Pacific data showing that private line service is nearly ten times as price elastic as residential access, which, it asserts, means that private line service must be priced in light of competitive alternatives. FEA also argues that Scholl's studies are based on embedded historical costs, not incremental costs, and thus rates may already be set at or above the appropriate economic costs.

FEA adds that Pacific's failure to provide incremental cost data by service category ignores "earlier Commission edict," specifically the Commission's statement in D.84-06-111 that the parties should address whether incremental or marginal cost analysis should be used as a basis for rate design decisions. For this failure, FEA recommends that Pacific's and DRA's rate proposals should be rejected.

H. General's Position on Private Line

General and other local exchange companies concur in Pacific's private line rates. Existing settlements agreements describe how the revenue from these rates is distributed among the concurring companies. General's witness, Jensik testified that the rates are based only on Pacific's costs. He asserts that all parties would benefit if the present scheme were eliminated in favor of access charging arrangements between exchange carriers. Jensik favors replacing private line settlements with bill and keep charges for jointly provided private lines. General would bill its customers its own rates for the portions of jointly provided services that it provides and would charge its customers Pacific's rates for the portions provided by Pacific. Jensik refers to this as "meet point billing."

Jensik also testified that adoption of Pacific's proposed deaveraged local loop rates would negate the administrative advantage and customer satisfaction General has experienced as a result of discontinuing charging suburban mileage on local loops pursuant to our order in D.84-07-108.

I. TASC's Position on Secretarial Line Charges

Secretarial line is one of the services which this Commission designates as "private line-like." Technically the service is not provided under Pacific's private line tariffs, but under its Network and Exchange Services tariffs. Nonetheless, the service has the characteristics of private line service and is appropriately addressed in conjunction with private line services. Pacific's opening brief explains that there are three types of secretarial line service. Type 6A service extends from the termination of the subscriber's loop in the central office serving the subscriber to the telephone answering service (TAS) premises; type 6B service extends from the end of the subscribers loop in the central office serving that subscriber to a concentrator located in the same central office; and type 27B service extends from the end of the subscriber's loop in the central office serving that subscriber to a concentrator not located in the central office.

Pacific also explains that each of these types of secretarial line service may be provided using one of five distinct circuit designs depending upon the number of of central offices and the type of facilities used to provide the circuit. Ninety percent of the service, however, is provided using two of these circuit designs and another nine percent is attributable to a third design.

Telephone Answering Services of California, Inc. (TASC) represents the interests of TAS operators. TASC continues to prefer the rate design propounded in DRA's motion of February 7, 1986, which removed the then-current surcharge, reduced message toll rates by $71 million and expanded certain ZUM zones in the San Francisco Bay area. TASC offers an alternative in the event this Commission chooses not to adopt the described DRA proposal.

1. <u>The TASC Proposal and its Rationale</u>

TASC's alternative proposes the following: (1) Adoption of two installation charges, one for secretarial line connections in which the TAS and its subscriber are served from the same central office (CO) and one where they are served out of different COs. TASC calls these single-CO and multi-CO lines and proposes that the charges be set at Pacific's cost of installation and removal (i.e., the in and out costs) except that no charge should exceed 100% of the existing $92 charge; (2) Adoption of an expanded definition of the charge for a "move" which would not be limited to moves occurring at the same premises, and which would be set at 50% of the new connection charge; (3) A study of the feasibility of a new tariff for bulk moves. TASC proposes that this tariff should reflect the economies of scale inherent when a TAS moves a large number of secretarial lines at once, and proposes that the tariff include an alternative payment arrangement based solely on the labor costs for the specific project so that there will be no dispute over whether the charges paid by the TAS did or did not cover Pacific's costs. TASC also proposes that Pacific be required to submit a proposal for such a tariff to CACD and to TASC for review.

In addition, claiming that the use of concentrators can obviate the need for more expensive multi-CO service instead of single-CO 6B or 27B service, TASC proposes that this Commission order Pacific to permit customer-owned concentrators to be placed in Pacific's central offices, or to order Pacific to participate in a joint endeavor with TASC to develop a program to accomplish such a goal.

In explaining why this Commission should not treat secretarial line service as a discretionary service which is undeserving of protection from rate increases, TASC asserts that there is no reliable substitute for secretarial line service, explaining that, for example, the possible alternatives of call forwarding or delayed call forwarding (DCF) to a DID number require programming of the telephone each time the service is enabled or disabled and/or are not universally available because the TAS subscriber CO must have call forwarding or DCF capability and the TAS CO must have DID capability.

Based on that premise, TASC goes on to explain that the point of its two-tier installation charge proposal is to provide an incentive for TAS subscribers to employ single-CO facilities while not prohibitively pricing the multi-CO lines for those who, for one reason or another, elect to employ them notwithstanding the higher rate. TAS points out that nearly all (over 99%) single-CO lines are non-designed, and that the cost of installing a single-CO line is several times the cost of installing a non-designed secretarial line. Table 2.1 of Pacific's Exhibit 402 shows the single-CO line cost to be $125 for 6A, $63 for 6B, and $126 for 27B, while TASC's witness Krause set the costs at $48, $44 and $49, respectively. See Exhibit 405, p. 19, Table 2.1. TASC points out that this single line service represents over 60% of all secretarial lines. Pacific's same table 2.1 shows multi-CO line installation costs to be $805 for 6A, $744 for 6B, and $811 for 27B, while Krause's Table 2.2 shows these three multi-CO services to have an average installation cost of $275. Thus, the effect of TASC's proposal with its 100% cap would be charges of a maximum of $126 for single-CO service and $184 for multi-CO service. Using Krause's figures, the charges would be $46 and $184. Pacific proposes an aggregate charge of $160, while DRA proposes an aggregate charge of $184.

One of the reasons TASC offers for limiting multi-CO service charge increases to 100%, aside from the fact that that has been a Commission policy, is that the alternative to multi-CO 6A service, single-CO concentrator service (6B/27B), is not always available. Another reason is that application of this cap will render moot, at least for purposes of this proceeding, the considerable controversy that exists with respect to the actual cost of installing multi-CO secretarial line connections.

2. TASC's View of Cost Estimates

Should we choose to consider Pacific's secretarial line nonrecurring cost estimates, TASC argues that Pacific's service order and channel connect costs are overstated. While maintaining its preference for our adoption of the charges recommended by Krause, described above, TASC urges that we at least apply the following considerations in designing secretarial line nonrecurring charges: (1) setting the same charge for all three types of single-CO lines for ease of administration; (2) reducing the existing aggregate charge as to single-CO service; (3) applying a 100% charge cap on multi-CO charges; (4) requiring Pacific to develop service order change costs based on TASC's broader definition of a change order; (5) requiring Pacific to file interim tariffs that establish the move charge for secretarial lines at 50% of the "new" installation charge until this Commission has adopted charges based on Pacific's newly developed costs; (6) requiring Pacific to submit a proposal for a bulk move tariff to CACD and TASC for review.

J. Discussion

1. The Tops-down Category Analysis

DRA's Shankey criticizes Pacific's use of Functional Accounting rather than the Uniform System of Accounts (USOA) in its category analysis for the disaggregation of its projected 1986 average historical costs. We are troubled by DRA's inability to verify the reconciliations Pacific claimed between its tops-down and its bottoms-up studies due to this change in investment definitions. However, it appears that the Functional Accounting system allows much more precision than the USOA in assigning costs to specific service categories, or even to subcategories. That being the case, we are unwilling to reject Pacific's use of Functional Accounting in this category analysis. What was lacking in the present instance was a ready means for the other parties to verify the "translation" from USOA to Functional Accounting. Such information was apparently available to Docter, but as he testified, he and his associates spent a great deal of time checking the logic and integrity of Pacific's Functional Accounting system. In the present instance the parties did have an opportunity to review Docter's report and cross-examine him. However, we are sympathetic with the difficulty of that endeavor leading to a careful evaluation and full understanding of the process in light of the enormous number of issues which this proceeding has presented.

The USOA which we refer to here is the system of accounting adopted by the Federal Communications Commission (FCC) in 1935. In 1987 the FCC issued Part 32, Uniform System of Accounts for Telephone Companies, which became effective January 1, 1988. Part 32 uses functional accounting. We issued an order instituting investigation, I.87-02-023, to determine if the Part 32 system should be adopted for companies subject to this Commission's jurisdiction. We concluded in D.87-12-063 that it should. During those hearings DRA recommended that the major telephone companies implement a data continuity mechanism for converting new data into the old USOA format. These companies all agreed to do so. This fact alleviates the major concern raised by DRA, at least as to future reliance on functional accounting. As for the present, while the use of Functional Accounting has added one more variable to this record, we are satisfied that Docter's assessment of its reliability is reasonably accurate, and that Pacific's use of Functional Accounting to distribute test year revenue, expense and investment has improved the reliability of Pacific's tops-down cost allocations to private line.

2. <u>Pacific's Recurring Cost Studies</u>

a. <u>Cost Manual Costing Procedures</u>

Attachment A to D.83-04-012 sets forth procedures to be used in the development of general customer premises equipment service costs and Attachment B sets forth procedures to be used in the development of private line service costs. These attachments are generally referred to as our "Cost Manuals." The cost element detail which Pacific's cost studies provide is basically in accord with Cost Manual requirements.

Scholl's Exhibit 260 provides Cost Manual unit cost values at pages 7-49 through 7-79. However, Pacific does not use the values derived using Cost Manual methodology as a basis for the cost projections on which it bases its revenue and rate proposals. Instead, its projections are based on average historical costs. At page 4-32 of his prepared testimony, Exhibit 260, Scholl states:

> "The average historical costs differ from the cost manual values in that the net plant factors are different from the depreciated investment factors, the return and income tax factors (R.I.T.) are different, and the depreciation rates are different. The effects of these differences vary by cost element. In general, cost manual numbers are lower than the average historical costs--largely due to a representation of depreciation expense

which is lower than that identified in the results of operations."

In D.83-04-012, we recognized that adoption of the Cost Manual procedures would result in costs that understate Pacific's net booked investment for particular product lines and services. We explained that this result is due to a rather substantial amount of stranded investment (which Pacific calls reserve deficiency) in Pacific's books of account. We were concerned that unless something was done to change depreciation practices this undepreciated investment would simply continue to grow. We concluded that our adoption of the Cost Manual procedures as recommended by the ALJ would bring that stranded investment into focus and allow some estimate of its size to become available. We noted that our adoption of these costing methods did not stop Pacific from proposing "anything it wants in the way of rates which would bring the revenues derived from such rates to the overall revenue requirement found reasonable by the Commission." (D.83-04-012, mimeo. at p. 8.)

Pacific has complied with this Cost Manual requirement. We can compare its Cost Manual results with its annual historical costs. For example, Exhibit 260 shows 3002C total test year 1986 annual Cost Manual costs to be $4.8 million (p. 7-59), while it shows average historical costs for the same service to total $5.0 million (p. 7-18); and, it shows Cost Manual costs for 1009C service to be $400,000 (p. 7-54), while average historical costs for that service are shown to be $410,000 (p. 7-23).

b. Recurring Cost Study Methodology

In our review of Pacific's various cost study proposals in D.85-02-030, we stated:

> "We wish to make clear that we envision proper bottoms-up cost studies as filling at least two important functions: (1) to facilitate the further disaggregation of tops-down accounting costs on a service-specific basis and (2) to reveal the extent of inconsistency between tops-down accounting costs and identifiable bottoms-up costs of plant and operations, thus compelling the sort of reconciliation of differences which the Cost Manual prescribes. . . .
>
> "We do not accept Pacific's assertion that 'true' bottoms-up cost studies are impossible. Of necessity, recourse must be had to Pacific's accounting books to establish investment values for items of plant employed to provide service, and so there may have to be a 'tops-down' element to any bottoms-up study of recurring costs. However, it appears that Pacific intends to substitute such tops-down allocations for any meaningful bottoms-up assembly of service costs." (D.85-02-030, mimeo. p. 13.)

CBCHA/TCA and WBFAA both take the position that Pacific has not complied with the intent of the above-cited statements. These parties take exception to the bottoms-up study's application of investment allocation factors, especially in the loop study. Loop investment is a significant portion of private line investment. A computation of the figures presented on p. 7-111 of Exhibit 260 shows it to be about 29% of Pacific's recurring private line investment.

Obviously our statement quoted above contemplated the need for <u>some</u> tops-down input into bottoms-up costs. The question is whether the use Pacific has made of allocation factors is reasonable.

For recurring costs other than loop costs, Pacific has used the allocation factors only to distribute certain tops-down derived secondary gross investments onto the indisputably bottoms-up derived weighted unit investment figures. The methodology Pacific has used to determine bottoms-up recurring costs for line haul, interoffice outside plant, CO-SAT, and Station SAT equipment is thorough and reliable. It certainly comports with this Commission's desire for the development of bottoms-up cost data.

c. Loop Study Methodology

Pacific's 1983 bottoms-up loop study, which WBFAA and CBCHA/TCA seem to regard as superior to the present effort, identified cost-causing characteristics (cable size, gauge, year of placement, and fill factor) for each portion of cable and calculated a unit capital cost per pair foot by cable type, size and gauge for each loop. Pole and conduit costs were separately determined and assigned. In the present loop study, Pacific skipped the step of building bottoms-up unit costs based on calculated costs of the various cost-causing loop characteristics. Instead, it simply calculated a statewide average loop length for in-service plant for each of its service offerings by plant account, and then allocated tops-down derived costs to the service offerings using the average relative loop lengths as allocation factors. CBCHA/TCA and WBFAA assert that this procedure prevents the loop study from being a bottoms-up study and therefore prevents the reconciliation between it and the tops-down category analysis from being credible.

Scholl disagrees with the critics, claiming that the loop study is a statistical analysis of bottoms-up determined loop characteristic information, and that the comparison between Pacific's tops-down total loop plant determined from the Company's records with the private line loop plant determined in the service specific loop study was a true bottoms-up/tops-down reconciliation as required by this Commission.

The application of allocation factors developed through bottoms-up studies is a proper means of further disaggregating tops-down costs. However, in order to judge the reasonableness of these allocation factors, we must have a sense of the reasonableness of the bottoms-up costs which underly them. The problem with Pacific's loop study is that so far as can be discerned from the evidence the only statistical analysis that Pacific makes of its bottoms-up determined loop characteristic information is to count the number of feet by plant account for each service offering. There is no indication that information about cable gauge was used in the analysis nor, as Selwyn pointed out, is there any indication that Pacific considered year of placement. The absence of consideration of these factors casts some doubt on whether the costs thus derived are truly historical costs. As a consequence it might be expected that the resultant allocation factors would be less precise and less reliable than those derived in the last general rate proceeding.

On the other hand, the 1983 study did not separately analyze costs for in-service and RTS plant--a fact which Scholl cites as a major reason for the large discrepancy between tops-down and bottoms-up costs in that proceeding. Pacific's decision to evaluate RTS plant on a separate basis from in-service plant seems to be reasonable. However, even if it is true, as Scholl asserts, that there is no truly bottoms-up unit cost value which could be appropriately applied to both working and RTS plant using this scheme of evaluation, we do not understand Scholl's position that Pacific could not use actual bottoms-up costs, at least for in-service plant, as input into its bottoms-up study, but had to rely on the tops-down analysis for this portion of the input.

We find no fault with the methodology Pacific used in gathering the bottoms-up data it did gather for this loop study. Length is clearly the most significant factor in determining loop cost and the source of Pacific's loop length data seems quite reliable. However, while it appears that Pacific's loop cost study reasonably portrays loop cost distribution among Pacific's service offerings, its reliability is reduced by its failure to allow a determination of the extent of inconsistency between tops-down and bottoms-up cost data as intended by D.85-02-030.

d. <u>RTS Cost Development</u>

The most significant impact of the RTS study is due to Pacific's decision to treat the cost of spare capacity as an incremental cost. This treatment, according to Pacific, lowers the cost attributable to RTS from the $2.6 billion figure referenced in its last rate proceeding to $1.038 billion. No party takes issue with the cost methodology used to arrive at this RTS cost.

Selwyn maintains that Pacific neither attempts to associate the nonworking capacity with private line service nor to justify the aggregate level of nonworking plant. He is correct that the cost study assumes that the distribution of spare capacity should be proportional to the distribution of working plant. Scholl's justification of its RTS plant levels is that the determination of how much subscriber loop plant to place is based on demand forecasts. He concludes that the RTS cost study "showed that building excess capacity to provide for the uncertainty of service demand locations, is the most economic long term design." (Ex. 260, p. 5-26.) In D.87-12-067 as modified we considered the possibility that Pacific is maintaining excess levels of plant for which ratepayers are receiving no benefit, and concluded that we would take no further action on the question until Pacific's modernization audits were completed. Obviously the reliability of Pacific's cost allocations would have been enhanced if Pacific had provided some showing that its present level of spare capacity is necessary. This issue presents one more item of imprecision which must be considered in evaluating overall rate changes.

As for appropriate distribution of total RTS plant among the various service offerings, Pacific's cost study distributed RTS in two ways, the first, which Pacific opted to use, was by in-service proportions. The second was by inward movement proportions. The two distributions are set forth in parallel columns at p. 46 of Exhibit 402. The variation is not great, nor has this record been apprised of any reason why one should be preferred to the other. In fact, the number of variables which must be calculated and then weighted in order to come up with a total inward movement proportion makes distribution by in-service proportion preferable absent some showing of prejudice, since the in-service proportion is less problematic.

e. Service Volumes

Turning to service volumes, we note that Pacific's cost studies were prepared based on projections from 1982 and 1983 data. Scholl testified that introducing later volume data does not invalidate Pacific's cost projections or proposed rates because total service costs and revenues would also change if quantities were to change, so that the revenue to cost ratio and the unit costs of providing the service would remain constant. This position assumes, of course, that volumes are relatively accurate in relationship to one another. As Edwards pointed out there is the possibility of volumes fluctuating while the revenues remain constant. He suggests that that is what the differences in the volume claims for 3002C alarm service between Scholl and Sullivan seem to do, and suggests that an internally consistent revenue and rate are not supported by such volumes.

In his rebuttal testimony, Scholl acknowledged that the volume figures Sullivan used employed a more accurate view of 3002C volumes. (Exhibit 402, p. 21.) He went on to assert that using Sullivan's volume figures rather than the ones he employed in Exhibit 260 results in absolutely no change in the identified unit cost of any of the local channel cost elements (loop, central office SAT, station SAT, bridging, signaling and conditioning), changes unit channel termination costs in only two mileage bands (by 2% and 6% respectively), and only makes a noticeable change in interoffice trunk costs--all of which are less than 9%. Further, on cross-examination Scholl explained that the study analysis performed to illustrate this fact (Exhibit 402 pp. 22-24), applied two-wire and four-wire proportions uniformly to 3002C service because the data base did not provide information from which it could be determined which were actually patron loops and which were sponsor loops. This accounts for the discrepancy between the proportions of sponsor and patron loops for full- and half-duplex 3002C service which WBFAA pointed out.

Sullivan's rebuttal (Exhibit 400) adequately explained the different volume figures Edwards cited, stating that the 14,041 figure referred to by Edwards is a total quantity for 1985 while 13,991 is a 1986 volume for half duplex only. He also testified that volume changes in his revenue impact calculations reflect the clean-up of Pacific records which Shankey referred to in his testimony. (Exhibit 330, p. 10.) Shankey testified that DRA's development of revenue effects used in-service and inward movement volumes based on Pacific's PLHF report. In cross-examination, Shankey expressed confidence that Pacific's PLHF volumes allowed DRA to be at the point where we feel that the volumes are accurate enough that we can now go forward and develop some kind of a trend. (90 Tr., 10822.)

We are well aware that Pacific has had difficulty in establishing accurate private line volumes in the past and the criticism of intervenors point up a continuing difficulty. However, we are satisfied by the testimony of Shankey as well as the explanations of Scholl and Sullivan that overall, Pacific's volume estimates were consistent enough so that cost attributions among the various private line services, while far from perfect, may be regarded as providing a generally accurate portrayal of relative volumes. Further, it appears that Pacific's PLHF program may well end the difficulty Pacific has experienced in the past in providing accurate volumes.

f. Assignment of SARTS to <u>Recurring Costs</u>

The appropriate allocation of SARTS costs was a major issue in this proceeding. Pacific describes SARTS as a system which permits the remote testing of voice grade special services, interoffice trunks and facilities more efficiently than certain other testing methods, thereby reducing maintenance testing expense. Selwyn and others claim that Pacific has assigned the costs of SARTS to specific private line services but has not determined the expense savings due to the SARTS investment. They assert that these expense savings are not being likewise assigned only to the services which are assigned the SARTS costs, and that this is the case because the labor expense for central office and field craftspersons are assigned to the various service categories and rate elements without a distinction as to the use or nonuse of SARTS. Scholl argues that this is not the case, and that the Functional Accounting system has separate function code accounts for specific labor expenses charged to various services, including interoffice trunks associated with in-service intraLATA voice special services, and that this results in the labor expense and savings resulting from the SARTS testing program to be assigned specifically just to those services which use it.

Of course to the extent the reasonableness of the Functional Accounting system is in question, so too is the reasonableness of these allocations in question. Assuming, as we have, that Pacific's use of Functional Accounting is reasonably reliable, its description of the manner in which testing costs and labor expenses for testing of interoffice trunks were specifically assigned to particular private line services under the Functional Accounting system make it clear that the methodology was appropriate, and that the concerns of Edwards and Selwyn that Pacific failed to appropriately account for cost savings arising from the use of the SARTS technology are not well founded.

The level of confidence which can be placed on the accuracy of these allocations is somewhat reduced by Pacific's failure to assign SARTS to 3002C service and later acknowledgment that this service did use SARTS testing.

3. Pacific's Nonrecurring Cost Study

Pacific incorporated a number of changes into its nonrecurring cost study in response to D.84-06-111, which improved the methodology substantially. Nonetheless, while no one has suggested a better means of producing bottoms-up nonrecurring costs, reliance upon panels of estimators naturally results in a degree of subjectivity which opens the study to criticism.

One of the major areas of criticism was that time estimates for labor activities were overstated. We agree that Pacific's nonrecurring labor cost projections are overstated. Scholl has acknowledged some of the errors pointed out by intervenors, such as the inappropriate inclusion of task assignments to market administrators and order writers cited in the testimony of Uffindell and Martinez, but Scholl's explanation of the duties inherent in such functions as the NTEC task of reviewing an order, the basis for identifying 57M and PADS expenses associated with nonrecurring costs, and his provision of such information as the fact that only 13% of Pacific's Loop Assignment Centers have been mechanized, lead us to disagree with the estimates of the magnitude of the overstatement of nonrecurring charges proposed by King, Uffindell, Martinez, O'Brien, or Edwards. We also reject WBFAA's contention that Pacific has overstated the costs of inside wiring. Scholl explained on cross-examination that the term was used to describe costs of the installation of wiring on the network side of the standard network interface. (Exhibit 402 at 50.) That being the case, the FCC's detariffing of inside wiring has no impact on Pacific's cost projection.

API supports the nonrecurring study conducted by DRA, but API's Edwards asserts that DRA should not have made a 15% adjustment for nonproductive labor time because such an adjustment was already included in Pacific's loaded labor rates, and therefore the nonproductive time was double counted. Shankey and Scholl both responded that API had misunderstood Pacific's loaded labor rate calculations, which, he stated, do not include allowances for personal, fatigue and delay factors. Shankey therefore stands by his adjustment.

Scholl states that Shankey's observed labor times were lower than those of the panel of estimators because he "stopped the watch" whenever there was a difficulty rather than considering a weighted average of work times and because Pacific's estimates include a weighting for those instances where a second work location is involved.

We recognize that Pacific's nonrecurring cost studies used rather old volume estimates and overstated work times. We do not agree with the critics that these studies are replete with drastic errors or omissions and are so grossly overstated as to be useless. Nor are we persuaded by the evidence about overstated task frequency of occurrence figures. Nonetheless, we agree that a moderate downward adjustment to Pacific's estimates is in order. The across-the-board adjustment proposed by DRA presents the sort of reasonable and moderate adjustment which is appropriate under these circumstances.

4. <u>Impact of Pacific's Other Reports</u>

WBFAA claims that the statement of the Robin & Dackerman report that it should cost Pacific Bell less to provide 3002 private line services for alarm circuits than to provide 3002 data circuits. Accordingly, this service should be distinguished from 3002 data lines and offered at a lower price (Exhibit 401, p. 9.) supports the proposal for a separate tariff for alarm transport services. API claims that the Robin & Dackerman report is important evidence that both Pacific Bell personnel and its outside consultants viewed its private line cost studies as suspect and biased. We view the Robin & Dackerman report as an unsubstantiated opinion which has no probative value in the present matter. We accord no weight to its conclusions.

As for Pacific's SSA Report, Exhibit 403, API asserts that it shows that Pacific's private line cost study and rate design is significantly overstated, adding that the amount of achieved savings described in the report comes to $23.8 million and the amount of future savings comes to $134.8 million. Of this latter amount, about $23 million is clearly projected as annual savings. WBFAA does not claim that Exhibit 403 invalidates Pacific's cost study, but asserts that the issues addressed by the report show that Pacific is improving its provisioning of private line services, and that the realization of those improvements will reduce the future costs of private line provision, thereby making the granting of rate increases unwarranted.

We agree with Pacific's position that its SSA Report does not have any bearing whatsoever on Pacific's cost data. The document was not completed until November 1986--well after Pacific's cost studies were completed. Pacific's decision to look for improvements in the provisioning of its special services, of which private line is one, are to be commended. This report, however, does not provide this Commission with reason to adjust or ignore the projections of Pacific's cost studies.

5. <u>Deaveraged Local Loop Rates</u>

The division point for the Schedule I and Schedule II local loop rates which Pacific proposes is set so that about 76% of all private line loops will be included in the definition of the lower priced Schedule I serving wire centers. Pacific does not specify what the cutoff point is in terms of ratio of average cost for Schedule I wire centers to statewide average cost, but it is certainly greater than 75%. Selwyn would provide lower rates in two tiers, but only include about 37% of the local loops altogether, with the first tier being for the six urban wire centers with average costs less than 50% of the statewide average and containing about 10% of all local loops and the second tier being for an additional 27% of customers served by wire centers with costs between 50% and 75% of the statewide average.

We are not inclined to authorize any deaveraging plan for private line local loop rates. The tradeoff, as we see it, is between lowering the rates for the largest urban users, while increasing the rates (at least proportionately) for smaller, more rural users. The fact that these users are businesses rather than residential users does not detract from our underlying concern that telephone service be universally available. To the extent that we permit deaveraged rates which disadvantage the small consumer, we are working against that principle. Furthermore, we agree with DRA that since loop costs are driven primarily by loop length, this proposal would inequitably charge customers in the high cost wire centers who happen to have short loops. We believe such a plan is only justifiable where there is strong evidence that alternative rates will disadvantage ratepayers generally in the long run. That is the argument that the parties make here, but it is not supported by the evidence. We remind the parties that our concern is with <u>uneconomic</u> bypass. So far as we can ascertain from the record before us, there is no imminent threat of uneconomic bypass should Pacific retain a single local loop rate. We will not authorize deaveraged local loop rates.

6. <u>Separate Alarm Transport Tariff</u>

Pacific's proposal for a separate alarm transport tariff would increase nonrecurring charges for alarm transport customers by only 20% rather than the 25% Pacific proposes for other private line customers, smaller loop rate increases, and, where bridging is used, a small decrease in the rates for associated channel equipment and bridging. Sullivan's explanation of this proposal is baffling. He states: "We believe that the combination of increased prices and the availability of service alternatives will result in a reduction and ultimately the elimination of any perceived subsidy in this market." (Exhibit 283, p. 21.) Perhaps the meaning of Sullivan's cryptic statement will become clear in the future, but for now we perceive a subsidy, and one which would be larger for alarm transport services than for other private line services. We do not perceive a continued need to shield alarm transport customers from bearing their fair share of the costs of providing service to them. We will not grant Pacific's proposal for separate alarm transport tariffs.

7. Secretarial Line Rates

TASC's assertions about secretarial lines seems to assume that this Commission's rate design policy does not recognize the importance of secretarial lines, and attempts to convince us that secretarial line service is, indeed, important. We do not doubt that fact. However, it does not give rise, as TASC would apparently like us to find it does, to the conclusion that we must treat secretarial line rates in the same way in which we treat rates for basic residence service. Our conviction about the need to preserve universal telephone service does not encompass the notion that secretarial line service must be set at rates which will assure universal availability. To the extent possible and reasonable secretarial line rates should be set to at least recover costs.

Since it is not our intent to adopt the across-the-board rate changes which TASC prefers, we therefore address below the secretarial line proposals presented.

a. Disaggregated Installation Charges

TASC proposes two separate secretarial line installation charges instead of one in order to recognize the difference in costs between installation of designed lines and nondesigned lines. Shankey testified that DRA's opposition to such a rate design is based on same reason as its opposition to Pacific's proposal for two local loop rates. There is no dispute that a designed line displays significant differences from a nondesigned line, or that the very, very low incidence of designed single-CO line service makes it reasonable to accomplish charge disaggregation by setting one charge for single-CO line service and another for multi-CO line service, each charge being based on its disaggregated average costs. That being the case, it appears that DRA's main criticism of the loop rate proposal--its arbitrary cut-off point, and the small difference in average costs between the two groups--are inapplicable to TASC's proposal.

It is clear that TASC's proposal would result in a much lower overall revenue recovery than would a single charge based on aggregate costs. Pacific proposes increasing this aggregated service charge element from its present $92 to $160. DRA proposes an aggregate increase to $184, but TASC would increase charges to $184 for only about 38% of subscribers while setting it for the other 62% of subscribers at somewhere between $126 (if we were to adopt Pacific's cost figures), and $46 (if we were to adopt Krause's cost figures).

The size of the difference between costs for designed and nondesigned secretarial lines seems to argue in favor of disaggregated charges. On the other hand, differential costs alone are not sufficient reason for us to authorize the disaggregation of a particular charge. TASC assumes that TASs choose designed lines even though they don't need them, and that adoption of this proposal would encourage them to choose single-CO configurations which are less costly for Pacific to provide. The significance of these differing line configurations, is not so clear as TASC would suggest, however. It appears that the decision about which line configuration to use, as TASC itself notes, is often, --perhaps more often than not--, based on the availability of concentrators within or near Pacific's CO, or other Pacific engineering needs rather than the customer's usage. That being the case a charge bifurcation such as TASC proposes simply has the effect of penalizing those customers who are more distantly located from the central office or who happen to be served by a central office that has not been modernized. The idea that customers can save money by choosing different technology certainly does not apply in such instances. Such factors argue strongly for retention of the single averaged charge which is now in place. We are not convinced by this record that the decision to use designed service is so closely linked to the customers' advantage that differential charges are reasonable. We will deny the proposal. A single installation charge for secretarial lines will be retained.

In attempting to determine an appropriate charge for secretarial line installation, we note that Krause's calculations suggest that a charge of $133 would achieve cost coverage for the aggregated installation charge, while Pacific and DRA assume the costs are far more than 100% of present charges. DRA chooses to cap the charge at a 100% increase while Pacific chooses to increase this charge by about 75%. Sullivan testified that Pacific's private line rate design treats secretarial lines separately to avoid an excessive increase in one year. On this same theme of the impact of increases, TASC argues that secretarial line subscribers should be protected from large increases because the service is not discretionary, in that some TAS subscribers cannot make use of secretarial line alternatives such as call forwarding and DCF because their CO doesn't have that capability and/or the TAS CO doesn't have DID capability.

The first question we must answer is whether the cost studies support charges as high as Pacific and DRA propose. Then we must determine what constitutes a reasonable charge for this service.

TASC claims there are several errors in Pacific's nonrecurring charge studies, as they apply to the installation of secretarial lines. It claims an error in the time a service representative needs to process a service order, and based on the testimony of Gladstone, and Martinez reduces Pacific's estimate from 19 minutes to 3 minutes. This change (along with TASC's elimination of any allocations for marketing) is the primary basis for TASC's reduction of Pacific's estimated overall cost of $29.37 to $8.14, though TASC's conclusion that Pacific's claim of marketing costs attributable to these services is implausible and TASC's deletion of any allocation for it is also a factor.

TASC also criticized other aspects of Pacific's cost projections. First, it points out that Pacific misplaced a decimal point and showed an occurrence factor for certain "IMF and I&M" work activities which Pacific later acknowledged was ten times higher than it should have been, and also acknowledged that it had miscalculated an input for the 6X2 line which resulted in a reduction of that input from $442 to $276. It also cites several instances of incredible ranges of time estimates from the panel of estimators. It goes on to suggest that Pacific's reassessment of the multi-CO secretarial line costs and its adjustments that reflect new subjective determinations by one member of the panel of estimators had the effect of partially offsetting the "premise occurrence" and "calculation error" adjustment which TASC had criticized, and is unreliable.

TASC further finds fault with Pacific's choice of weighting the high, usual and low time estimates on a 1:4:1 basis, asserting that such weighting presumes that everything goes right too infrequently, and claims that the confusion in the record about Krause's use of Shankey's observed work times, and Scholl's criticism of that use is another example of why this Commission cannot confidently set a NRC for multi-CO lines. Finally, TASC were to adopt Pacific's cost figures), and $46 (if we were to adopt Krause's cost figures).

While the size of the difference between costs for designed and nondesigned secretarial lines seems to argue in favor of disaggregated charges, differential costs alone are not sufficient reason for us to authorize the disaggregation of a particular charge. TASC assumes that TASs choose designed lines even though they don't need them, and that adoption of this proposal would encourage them to choose single-CO configurations which are less costly for Pacific to provide. The significance of these differing line configurations, is not so clear as TASC would suggest, however. It appears that the decision about which line configuration to use, as TASC itself notes, is often, --perhaps more often than not--, based on the availability of concentrators within or near Pacific's CO, or other Pacific engineering needs rather than the customer's usage. That being the case a charge bifurcation such as TASC proposes simply has the effect of penalizing those customers who are more distantly located from the central office or who happen to be served by a central office that has not been modernized. The idea that customers can save money by choosing different technology certainly does not apply in such instances. Such factors argue strongly for retention of the single averaged charge which is now in place. We are not convinced by this record that the decision to use designed service is so closely linked to the customers' advantage that differential charges are reasonable. We will deny the proposal. A single installation charge for secretarial lines will be retained.

In attempting to determine an appropriate charge for secretarial line installation, we note that Krause's calculations suggest that a charge of $133 would achieve cost coverage for the aggregated installation charge, while Pacific and DRA assume the costs are far more than 100% of present charges. DRA chooses to cap the charge at a 100% increase while Pacific chooses to increase claims that Pacific could achieve cost reductions if it would employ the SLC-96 as an alternative to a standard concentrator.

There is no doubt that Pacific's cost studies are imperfect. Cost studies encompassing so much material could hardly be otherwise. Aside from simple mathematical errors, there are hundreds of points where choices must be made, and there are generally arguments which can support choices different from the one selected. We do not find Pacific's methodology to be so sloppy or ill-conceived that its cost studies deserve to be ignored. Still, we are convinced by the anecdotal testimony as well as Shankey's survey that the nonrecurring cost figures derived from the panel of estimators are most likely overstated in many instances. We do not find Krause's worktime estimates for secretarial orders to be appropriate either. They minimize or delete costs to an unreasonable degree. While it may not be possible to derive an exact amount, we do not doubt that overall secretarial line installation charges are presently less than half the costs for that service.

It has been our policy in recent times to restrict nonrecurring charge increases to no more than 100%, where costs would justify more, in order to ameliorate rate shock. Pacific would have us adopt a lesser increase for secretarial line installation. The tradeoff for reduced increases, of course, it that someone else must pay. We are not convinced of the necessity of following Pacific's proposal in this matter. We will adopt a 100% increase in secretarial line installation charges as proposed by DRA.

b. <u>Move and Bulk Move Charges</u>

TASC claims that there is no justification for Pacific charging for a new installation any time a TAS subscriber moves from one premises to another in the same or a different building. It takes the position that the language of the present tariff is overbroad, and asserts that the present charge for the this charge by about 75%. Sullivan testified that Pacific's private line rate design treats secretarial lines separately to avoid an excessive increase in one year. On this same theme of the impact of increases, TASC argues that secretarial line subscribers should be protected from large increases because the service is not discretionary, in that some TAS subscribers cannot make use of secretarial line alternatives such as call forwarding and DCF because their CO doesn't have that capability and/or the TAS CO doesn't have DID capability.

The first question we must answer is whether the cost studies support charges as high as Pacific and DRA propose. Then we must determine what constitutes a reasonable charge for this service.

TASC claims there are several errors in Pacific's nonrecurring charge studies, as they apply to the installation of secretarial lines. It claims an error in the time a service representative needs to process a service order, and based on the testimony of Gladstone, and Martinez reduces Pacific's estimate from 19 minutes to 3 minutes. This change (along with TASC's elimination of any allocations for marketing) is the primary basis for TASC's reduction of Pacific's estimated overall cost of $29.37 to $8.14, though TASC's conclusion that Pacific's claim of marketing costs attributable to these services is implausible and TASC's deletion of any allocation for it is also a factor.

TASC also criticized other aspects of Pacific's cost projections. First, it points out that Pacific misplaced a decimal point and showed an occurrence factor for certain "IMF and I&M" work activities which Pacific later acknowledged was ten times higher than it should have been, and also acknowledged that it had miscalculated an input for the 6A2 line which resulted in a reduction of that input from $442 to $276. It also cites several instances of incredible ranges of time estimates from the panel of estimators. It goes on to suggest that Pacific's reassessment of relocation of the end of a channel at the existing customer premises should be expanded to include any relocation which does not alter the design, operation or function of the secretarial line service so long as both premises are served by the same central office. TASC contends that the cost study's failure to differentiate between work activity costs which occur only upon the initial installation of a new secretarial line connection, and those that are required for both a move and a new installation result in an overstatement of "channel connect establish" and "channel connect out" costs for moves in the category it has described. TASC urges that we adopt a new "move" charge for secretarial lines at 50% of the new installation charge until we have better cost information. We are not persuaded by TASC's arguments. We agree with Pacific that the definition of a move charge which TASC proposes is inconsistent with Pacific's cost studies as well as the tariffs. We will deny TASC's proposal. Similarly, there in not sufficient evidence in this record to warrant our requiring Pacific to submit a proposal for a bulk move tariff as TASC requests.

We will also deny TASC's request that we order Pacific to permit outside parties to place concentrators in Pacific's central offices. In light of the considerable questions of liability, safety, protection of property, etc., there was not a sufficient evidentiary showing of reasonableness.

8. Miscellaneous Private Line Issues

Pacific has requested that certain telegraph private line services be limited to those customers currently receiving the service. We will grant that request. It appears that there is no longer a demand for these services.

FEA requests that we reject Pacific's cost proposals for failure to provide sufficient incremental cost data. We decline to the multi-CO secretarial line costs and its adjustments that reflect new subjective determinations by one member of the panel of estimators had the effect of partially offsetting the "premise occurrence" and "calculation error" adjustment which TASC had criticized, and is unreliable.

TASC further finds fault with Pacific's choice of weighting the high, usual and low time estimates on a 1:4:1 basis, asserting that such weighting presumes that everything goes right too infrequently, and claims that the confusion in the record about Krause's use of Shankey's observed work times, and Scholl's criticism of that use is another example of why this Commission cannot confidently set a NRC for multi-CO lines. Finally, TASC claims that Pacific could achieve cost reductions if it would employ the SLC-96 as an alternative to a standard concentrator.

There is no doubt that Pacific's cost studies are imperfect. Cost studies encompassing so much material could hardly be otherwise. Aside from simple mathematical errors, there are hundreds of points where choices must be made, and there are generally arguments which can support choices different from the one selected. We do not find Pacific's methodology to be so sloppy or ill-conceived that its cost studies deserve to be ignored. Still, we are convinced by the anecdotal testimony as well as Shankey's survey that the nonrecurring cost figures derived from the panel of estimators are most likely overstated in many instances. We do not find Krause's worktime estimates for secretarial orders to be appropriate either. They minimize or delete costs to an unreasonable degree. While it may not be possible to derive an exact amount, we do not doubt that overall secretarial line installation charges are presently less than half the costs for that service.

It has been our policy in recent times to restrict nonrecurring charge increases to no more than 100%, where costs would justify more, in order to ameliorate rate shock. Pacific do so. Pacific's incremental cost study complies with the requirements of D.84-06-111.

9. **Appropriate Private Line Rates**

Applying allocation factors to the tops-down data (booked outside plant investment) assures that this element of the cost study will achieve closure with the tops-down study. Such a practice gives the appearance of a much improved reconciliation between total tops-down and bottoms-up data. However, we have no way of judging how reliable this information might be. We are certainly not confident of the accuracy of the 5% discrepancy Pacific suggests. We are confident, however, that the refinements to the category analysis and to the non-loop components of the recurring cost study have improved the reliability of those two studies, and that fact suggests the likelihood that Pacific's bottoms-up studies do, in fact, account for many of the costs which went unidentified in the last rate proceeding.

One of the benefits of a bottoms-up cost study is that it provides a way of further disaggregating tops-down costs. Docter's testimony makes it clear that the category analysis process by which Pacific assigned costs to the private line service offering in this proceeding was much more refined and much more reliable than previous tops-down analyses. Further, the category analysis itself provided some disaggregation of private line costs.

As we said in D.84-06-111, the purpose of the bottoms-up studies is not to validate the category analysis but to carry it one step further through cost-based apportionment of the category costs to specific service offerings.

Therefore, Pacific's flawed tops-down to bottoms-up cost study reconciliation does not discredit the category analysis results. It simply compels caution in setting rates based on those results. The cost studies do not permit this Commission to set rates for private line services upon a precise cost basis, but would have us adopt a lesser increase for secretarial line installation. The tradeoff for reduced increases, of course, it that someone else must pay. We are not convinced of the necessity of following Pacific's proposal in this matter. We will adopt a 100% increase in secretarial line installation charges as proposed by DRA.

b. <u>Move and Bulk Move Charges</u>

TASC claims that there is no justification for Pacific charging for a new installation any time a TAS subscriber moves from one premises to another in the same or a different building. It takes the position that the language of the present tariff is overbroad, and asserts that the present charge for the relocation of the end of a channel at the existing customer premises should be expanded to include any relocation which does not alter the design, operation or function of the secretarial line service so long as both premises are served by the same central office. TASC contends that the cost study's failure to differentiate between work activity costs which occur only upon the initial installation of a new secretarial line connection, and those that are required for both a move and a new installation result in an overstatement of "channel connect establish" and "channel connect out" costs for moves in the category it has described. TASC urges that we adopt a new "move" charge for secretarial lines at 50% of the new installation charge until we have better cost information. We are not persuaded by TASC's arguments. We agree with Pacific that the definition of a move charge which TASC proposes is inconsistent with Pacific's cost studies as well as the tariffs. We will deny TASC's proposal. Similarly, there in not sufficient evidence in this record to warrant our requiring Pacific to submit a proposal for a bulk move tariff as TASC requests.

We will also deny TASC's request that we order Pacific to permit outside parties to place concentrators in these cost studies, for the most part, have once again shown progress in moving toward a more accurate and finely disaggregated tops-down analysis on the one hand, and the development of bottoms-up studies which will facilitate differential pricing of specific private line services on the other.

As with the studies for recurring costs, Pacific's nonrecurring cost study displays many imperfections. Nonetheless, the study is an admirable effort to provide better information about the costs of provisioning activities for private line service offerings. Application of the reasonable but moderate downward adjustment to these costs which DRA proposes, and even application of Scholl's private line nonrecurring cost scaling factor of .94 still reveals an unacceptably low revenue to cost ratio.

Together, Pacific's cost studies show a clear need for substantial rate increases. When weighed against the possibilities for error, especially in the recurring rate bottoms-up studies, we find it reasonable to provide private line rate increases for one year rather than incremental increases over three years as Pacific proposes.

Considering that the shortfall for nonrecurring private line charges will have to be collected from other customers, we see no reason to adopt Pacific's proposal for nonrecurring rate increases of only 25%. The shortfall is too large and the evidence of customer hardship insufficient to justify such a departure from our usual rate policies with respect to services for which rates are being moved toward costs. We will adopt the nonrecurring rates proposed by DRA.

Nor do we intend to set recurring rate increases at the rates Pacific proposes for the first year of its 3-year proposal, ignoring the effect of the proposed increases for the second and third years. The cost studies justify a much greater increase than that. Thus we will adopt the DRA proposal, which provides a substantially lower cumulative revenue increase (about half), but a larger increase for the test year than Pacific proposes.

Adoption of these rate proposals will result in a test year revenue increase for private line services of $67.020 million.

VIII. Settlements Effects

In March, 1985 we issued I.85-03-078, making all California independent telephone companies (ITCs) which interconnect their facilities with those of Pacific respondents for the purpose of investigating the effect of rate revisions to be granted to Pacific in the present general rate proceeding on separations procedures and intercompany settlements and revenues as related to intrastate toll and private line rates concurred in by these ITCs and related matters. We held five days of hearings on these issues in September and December 1986. The parties which participated in this phase all briefed the settlements effects issue in concurrently filed opening and closing briefs.

A. Background

As a result of decisions by the federal courts and the Federal Communications Commission (FCC) which restructured the Bell System and allowed entry of competition into the interstate and intrastate, interLATA long distance marketplace at the beginning of 1984, the traditional system of cost allocation, division of revenues, and ratemaking for long-distance telecommunications (toll) services was replaced with a system of exchange access charges and interexchange transmission charges to compensate local exchange carriers for the origination and termination of interstate traffic. This Commission opened a proceeding to determine access rates and related matters.

The ITCs were joined as parties to the access proceeding by an Order Instituting Investigation (OII). Under the jurisdiction established by that OII we approved the concurrence of

ITCs in Pacific's access services tariffs along with their agreement with Pacific to pool all costs and revenues associated with access charges. At the same time we recognized that although there were serious time constraints imposed by the federal court as well as limitations on our staff's ability to review additional rate proposals, any ITC opting for a "bill and keep" approach to access charges and establishing its own access tariffs reflecting its own costs of offering access services had the right to do so, so long as it did not disadvantage the general body of ratepayers or impose inordinate administrative burdens on our staff. (D.83-12-024 at 137.) General and its affiliate West Coast Telephone Company chose to establish their own "bill and keep" access tariffs. The others adopted concurring tariffs.

A major purpose of this new system of separate access charges was to reduce the allocation of costs to toll services by relieving them of some of the burden of overallocated local network costs which they then bore. We did so as we have explained above by adopting a policy of gradual and moderate reductions in tariffs for intrastate, interLATA access services. This policy came to be known as "SPF to SLU," referring to a gradual shift in cost allocation factors from the use of a subscriber plant factor to the use of a subscriber line usage factor.

As a result of adopting the SPF to SLU policy as well as other rate changes D.85-06-115, our next major decision in the access proceeding, significantly reduced Pacific's intrastate access charges. To make the effect of the change revenue neutral to Pacific it was necessary to authorize an increase in the existing billing surcharge applied to most of Pacific's nonaccess rates.

Since smaller ITC rates have normally been set on a residual basis after taking account of the contribution of toll settlements (now including settlements from the intrastate access revenue pool), and since access revenues are a relatively high proportion of total revenues for most ITCs, the adopted reduction in Pacific's access revenue objective would have reduced the pool on which the ITCs could draw thereby potentially causing the ITCs to institute relatively high (as compared with Pacific) percentage increases on their basic local rates to meet their revenue requirements. Therefore, a number of the small ITCs which concurred in Pacific's access rates asked that we protect them from such disproportionate impacts.

Recognizing that while PU Code § 728 does not mandate the same or similar rates it does require that comparability of rates between similar neighboring service areas be considered in setting rates for exchange carriers, and also recognizing that we had authorized a similar equitable principle, that of rate averaging, to allow the rates of Pacific's rural ratepayers to be similar to those of its urban ratepayers, we determined that it was reasonable to apply a comparability test to the relationship between Pacific's basic exchange rates and basic exchange rates of interconnected ITCs concurring in Pacific's access rates. We concluded that the disproportionate impact of the Pacific access charge changes warranted, as an interim measure, the provision of a means of compensating for the total diminution in ITC access services revenues. We accomplished that end by ordering an interim surcharge for Pacific and all the ITCs and ordering that the revenue from this surcharge increase would be included in the access services revenue pool. The order stated that Pacific and the ITCs were to make advice letter filings pursuant to General Order (GO) 96-A to amend their tariffs to implement this additional billing surcharge.

Since we intended this surcharge to exist only until a new rate design was authorized for Pacific in the present rate proceeding, and since the new interstate High Cost Fund (HCF) would, when fully implemented in 1991, protect the ITC's customers against unreasonably burdensome local exchange rates, D.85-06-115 also authorized as a longer term interim solution an intrastate HCF which would draw upon the residually set intrastate carrier common line charge (CCLC) revenues from Pacific and those ITCs which concur in its access services tariff and in the associated revenue pool to assure that ITC exchange rates remain within a reasonable range of comparison with Pacific's exchange rates in comparable neighboring exchanges.

The interstate HCF, when and if fully implemented will allow exchange carriers to recover, from a fund financed by interstate CCLCs, 100% of that portion of their local loop NTS costs exceeding 150% of the national average local loop costs, and 75% of such NTS costs within the range of 115 to 150% of the national average. As we pointed out in D.85-06-115 the effect of this assignment of high NTS costs to interstate CCLCs will be that the intrastate local loop costs of even the highest-cost ITCs will be less than 130% of the national average.

Because eligibility for the intrastate HCF proposal we adopted is based on a comparison of local exchange rates rather than costs, and thus unlike its interstate counterpart addresses all ITC operating costs rather than just the differences in local loop NTS costs, and because our adopted approach tends to concentrate the impact of all differences in operating costs on basic exchange rates, the "comparable rates" standard we adopted only permits an ITC to claim relief from the intrastate HCF after we have determined a revenue requirement for the ITC, and thus presumably weeded out any imprudently incurred costs. Further, we stated that our revenue requirement determination would remain in effect for a maximum of one year unless we extended it.

The same rates/costs distinction also convinced us to allow relief from the intrastate HCF only to the extent necessary to permit an ITC's basic exchange rates to be set at no more than 200% of the basic exchange rates charged by Pacific in comparable neighboring exchanges, rather than the 130% which the ITCs were then seeking.

Recognizing that many ITCs would not have current Commission-determined revenue requirements, and therefore would not be immediately eligible for the intrastate HCF at the time of the issuance of a decision terminating the pooled surcharge in the present proceeding, D.85-06-115 reiterated our authorization of ITC advice letter filings for a bill and keep surcharge, calculated to generate revenue equivalent to that generated from the present pooled surcharge, to become effective upon the issuance of this decision.

In preparation for that filing we required each ITC to file with the Telecommunications Branch of CACD and to serve on any persons requesting a copy, a report projecting the revenue requirements impact for that ITC of the reduction in the access services revenue pool which would result from eliminating surcharge revenues from the pool when this decision became effective. We ordered that the report propose a rate design to respond to the projected impact. This rate design was to be a proposal for either applying the new bill and keep surcharge to all the intraLATA services to which the present pooled surcharge applies or applying it to all those services plus all access services, and a proposal for the magnitude of the surcharge based on how it would be applied.

I.85-03-078, the OII consolidated with the present matter, finds that the interconnecting facilities of other telephone corporations in California will be affected by any general rate revisions granted to Pacific insofar as those revisions affect separations procedures and intercompany settlements and revenues as related to intrastate toll and private line rates concurred in by the ITCs, other rate changes in Pacific's tariffs, and any construction of interconnecting facilities. It was issued for the stated purpose of determining the reasonableness of the rates, tolls, rules, charges, operations, costs, separations, practices, contracts, and the adequacy of service facilities of Pacific and all the telephone corporations operating within the state of California interconnecting their facilities with those of Pacific.

To that end the OII ordered Pacific to file compliance reports setting forth the estimated settlements effects of the proposed rates of Pacific and the proposed rates of DRA upon each respondent ITC. It further ordered that each respondent ITC file a report of total California results of operations and of separated California intrastate results of operations for calendar year 1986 estimated at present rates and charges and the year 1986 first adjusted to include the effects of Pacific's requested rates and charges in A.85-01-034 and second adjusted for DRA's proposed rates and charges. These reports and the projected revenue requirements impact and rate design reports were timely filed.

B. Initial Positions of Parties

1. The ITCs

At the hearings on this issue the ITCs presented evidence of the revenue effects and projected bill and keep surcharge requirements they expected to result from elimination of the present billing surcharge from the access services revenue pool.

Additionally, the ITCs requested that the direct assignment of interLATA WATS and the proposed intraLATA SPF to SLU transition, if adopted, be pooled or treated as a loss of pooled revenue. To this end some presented evidence of the reduction of available pooled settlements revenue they expected to result from access charge reductions accompanying the direct assignment of intrastate interLATA WATS becoming effective on January 1, 1987, and the reduction of available pooled settlements revenue they expected to result if the intraLATA SPF to SLU transition proposed by DRA and endorsed by Pacific in this proceeding were adopted. Further, where relevant, the ITCs who addressed the matter assumed that the surcharge revenues should not be treated as exchange revenues for purposes of EAS settlements. They point out that the bill and keep surcharge would need to be larger otherwise. Many ITCs also recommend that all other settlements effects be offset against each other and combined with the losses from the access services revenue pool, the direct assignment of WATS and the intraLATA transition from SPF to SLU to produce a single surcharge.

Some of the ITCs also proposed new local exchange rate designs as an alternative to the bill and keep surcharge, or they proposed that this Commission permit them to transfer their surcharge revenue requirement to their local exchange rate schedule by a uniform percentage increase in each rate category. Once this is done they propose that this Commission authorize those companies whose local exchange rates qualify for the intrastate HCF to collect such funds immediately.

In rebuttal testimony Pacific and most of the smaller ITCs agreed to the basic concepts of a Local Rate Stabilization (LRS) plan and fund which was presented by Pacific's witness, Ondeck in Exhibit 386. Unlike the authorized HCF, the LRS plan retains the local exchange rate funding source of the present surcharge rather than receiving funding from intrastate CCLCs. It accomplishes this by replacing the surcharge with an adjustment to local exchange rates. DRA also offered a rate design proposal which differed somewhat from that set out in D.85-06-115. Most of the ITCs opposed DRA's proposal.

2. DRA

Pointing out that these matters had already been authorized by D.85-06-115, DRA's witness Marks testified that staff agreed that the effect of the elimination of the present intraLATA surcharge should be recovered by the ITCs by an advice letter filing coincident with the final rate order in this proceeding and that the effects on the ITCs of the direct assignment of WATS should be adjusted by a revised surcharge effective January 1, 1987 (as it was). Marks stated, however, that staff did not agree that reduced settlements resulting from the adoption of rate design changes proposed in the present proceeding should be likewise offset. She stated that such rate increases should only be granted after Commission rate review during a general rate application or a GO 96-A rate application. On cross-examination Marks agreed that a regulatory log jam would be created if all the ITCs filed for rate relief simultaneously.

DRA's Shantz' testimony recommended that specific rates be adopted for the ITCs in lieu of the bill and keep surcharges authorized in D.85-06-115. His recommended ITC rate revisions only addressed the changes in revenue requirement associated with the elimination of the pooled billing surcharge. Specifically, he recommended increasing service connection charges up to a level 100% and then increasing the rates for basic exchange services up to the amount necessary to recover the pooled surcharge revenue loss, using a uniform percentage increase with rate maximums not to exceed 100% of Pacific's comparable rates. His testimony was based on Pacific rates then in place but recommended that final rates be adjusted to reflect the actual rates authorized by this decision. Under Shantz' scheme revenue requirement (after being established in a Commission rate review) could be recovered from the intrastate HCF to the extent it could not be met by these increased rates or other revenue sources.

3. General

General does not concur in Pacific's access services tariffs and thus is not a participant in the pooled surcharge that we ordered in D.85-06-115 or in the access services revenue pool. However, General's witness, Jensik, testified that several of Pacific's rate design proposals will have unspecified negative settlements effects on General, which General wishes to eliminate by alternative proposals. Jensik also testified that General wishes to increase its basic local service rates to recover any settlements revenue deficiency which results from any rate design changes we adopt for Pacific. Though it is not clear from his testimony, it appears that Jensik was asking that we authorize such recovery in this decision.

C. The Motion for Leave to Late-File Brief

About three months after the briefs were filed in the present matter a motion was filed with the Commission on behalf of DRA, Pacific, General, and twenty other ITCs. The motion requests leave to late-file a joint supplemental brief on HCF issues and asserts that good cause exists for granting such leave because the joint brief presents a compromise consensus position and recommendation submitted by all parties who actively participated in the high-cost fund phase of the hearings and briefing, with the sole exception of General. It goes on to explain that General joins in the motion that the filing be permitted, but does not join as a party to the proposal solely because General and the DRA were unable to reach agreement on the question whether General should be included within the settlement effects mechanism set forth in the brief for the rural and small metro[politan] independent companies.

The ALJ issued a ruling dated June 4, 1987 granting the motion for good cause shown and instructing the parties that they had 15 days to respond to the joint supplemental brief. Two parties responded within the 15 days, General and AT&T. A third party, MCI, filed an opposition to the motion. This opposition does not address any procedural reason why the motion should not have been granted, but instead addresses the substance of the joint proposal. Therefore, we uphold the ALJ's granting of the joint motion. We note that MCI's pleading was not filed within the required 15 days of the ALJ's Ruling. It was filed 26 days after that ruling, but 30 days after the joint motion was filed. Since 30 days is the common time for filing a protest, and since MCI's filing is in the nature of a protest, we will treat it as timely filed and consider its contents as a timely response to the joint supplemental brief.

D. The Joint Proposal

As a predicate to their proposal the parties note that their support for the recommendation is expressly conditioned on the "package" aspect of the proposal adding that their support for the whole proposal should not be construed as support for any partial aspect of the proposal and reaffirming the positions stated in their previously-filed briefs if this Commission chooses not to accept their joint proposal as-is.

The central premise of the joint recommendation is that this Commission needs to adopt modifications to the HCF mechanism adopted in D.85-06-115 in order to maintain a fair and equitable local rate structure for the predominately rural ratepayers served by the rural and small metropolitan independent telephone companies of the state.

1. Determination of the HCF Funding Requirement

a. Calculation of Settlement Effects

The parties agree that the first step in determining the HCF funding requirement is to calculate the impact of settlement effects shifts upon the local exchange portion of each ITC's revenue requirement. They point out that there was concensus in the evidentiary record on the methodology for calculation, but disagreement about whether certain items of rate adjustment and offset should be included in the calculation or not. Their compromise recommendation is that we continue the policies adopted in Pacific's last general rate decision, D.84-06-111, the decision after reconsideration in that rate proceeding, D.85-08-091, and the 1985 access decision, D.85-06-115, of flowing-through to affected companies both positive and negative settlement effects adjustments for regulatory changes which impact settlement revenues.

While D.85-06-115 adopted an HCF for which eligibility is based on comparable local rates, and, thus included consideration of the revenue effects of operating costs beyond local loop NTS costs, this proposal goes beyond the effects on rates of the termination of the uniform pooled surcharge on settlements revenues to include the effects on settlements revenue of all of the following:

(1) Termination of the uniform pooled surcharge (which is presently being added to the access services revenue pool to make up for various reductions that were made to access rates in D.85-06-115);

(2) Extended area service (EAS) rate changes;

(3) IntraLATA toll rate revisions or separations revisions adopted in this rate decision;

(4) The net of the combination of the receipt of interstate HCF funds with the effect on intrastate costs resulting from the shift from interstate SPF to the interstate NTS gross allocator; and

(5) Any other aspects of this Pacific rate decision with industry-wide settlement revenue impacts.

The parties to the joint proposal anticipate that based on evidence in this record we will make the necessary calculations and specify the settlement effects impact on each ITC.

b. Basis for New Rate Design and HCF Funding Level

One of the principal modifications to the existing HCF recommended by the joint proposal is a change in the eligibility threshold from 200% of the rates for similar services in comparable neighboring exchanges to 150% of the rates for comparable services in the urban areas of the state. This threshold would be used as a guideline by the Commission in approving rate designs for individual companies. It would not be used to reduce any presently authorized rates which are already above that amount except where the Commission authorizes an exception to the rule.

Thus, after determining the settlements effects the next step proposed is for this Commission to measure the impact of each company's net settlements effects upon its present level of local exchange revenues and then to define the 150% target level for each ITC. Then, each company electing to do so would implement a local exchange rate design by advice letter filing immediately following issuance of this Pacific rate decision which would allow it to attain this 150% target level. These advice letters are to include supporting workpapers calculating the level of additional local exchange revenues generated by the local exchange rate designs incorporating the 150% threshold and calculating the residual revenue requirement to be met by HCF funding.

The parties claim that this change from 200% to 150% is consistent with both evidence in this proceeding and with existing and proposed legislation aimed at promoting the goals of universal telephone service and urban/rural ratepayer equity. The Smaller Independents[6] laud our adoption in D.85-06-115 of the application of a "comparable rates" standard under which we agreed that it is reasonable to make intrastate HCF relief available.

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6 The term "Smaller Independents" refers to a large group of independent exchange companies which have filed joint pleadings in this matter. They are: Calaveras Telephone Company, Capay Valley Telephone System, Inc., California-Oregon Telephone Co., Citizens Utilities Company of California, Ducor Telephone Company, Evans Telephone Company, Foresthill Telephone Co., Happy Valley Telephone Company, Hornitos Telephone Co., Pinnacles Telephone Company, The Ponderosa Telephone Co., Sierra Telephone Company, Inc., The Siskiyou Telephone Company, and The Volcano Telephone Company.

However, they opine that application of this equitable principle of comparable rates can be made substantially more fair if the Commission will see fit to adopt a reduced threshold of 150%. They also ask that the prior rate review requirement of that decision be modified. Smaller Independents cite Section 1(d) of Chapter 1047, Statutes of 1986 which is a legislative declaration that this Commission shall ensure that local telephone subscribers are not unduly burdened by reductions in the rates and charges LECs adopt for IEC access. Smaller Independents argue that this statute shows a legislative concern for impact on the great majority of ratepayers served by the largest companies and point out that the impact on these cost shifts upon the customers of Smaller Independents, constituting six-tenths of 1% of telephone ratepayers statewide, is several times greater than it is on the statewide averaged ratepayers of Pacific.

2. The Funding Source

As we pointed out above, prior to filing this joint proposal the ITCs generally supported the basic concept of the LRS plan drawn up by an industry task force and presented by Pacific (Exhibit 386). Like the joint proposal, that plan provides for a fund, not a pool. The LRS plan provides that the funding company may recover net prospective funding requirements by advice letter filing. This provision would presumably permit the funding company to propose a surcharge on its rates, or some segment of its rates to accomplish this recovery. Testimony of various witnesses seems to assume that this recovery would be limited to local exchange rates.

Noting that the ITCs initially supported the LRS plan for funding the HCF while DRA supported and continues to support use of the access charge funding source, the joint brief takes what it describes as a "compromise position" which advocates maintaining the presently-authorized HCF funding source, the CCLC of all local exchange carriers statewide, and determining an annual revenue requirement for the HCF rate element of that CCLC charge. Once the annual HCF revenue requirement is established the amount of the uniform funding increment may be adjusted as often as quarterly to compensate for any under- or overcollection of that current revenue requirement. The joint brief adds that the parties reserve the right to propose modifications in the future, if experience proves it appropriate, which would shift the funding source from the carrier common line element to other aspects of local exchange company rate designs.

3. Other Provisions

The joint brief also includes a proposal for annual adjustments for future net settlements effects; a provision which would allow 100% of HCF funds for 1987, 1988, and 1989 followed by an annual reduction to 80%, then 50% and then 0% for companies which have not initiated a general rate proceeding by year's end for the next consecutive years; and a proposal that a decision in an ITC rate proceeding should have the effect of a fresh start under the HCF plan. Costs to Pacific for administration are to be recovered as additional expenses of access pool administration.

E. Responses to the Joint Brief

1. General

General has only one objection to the joint proposal. General points out that the proposed advice letter filing process for implementing the flow-through of changes resulting from this decision and for implementing the annual flow-through of changes thereafter is made available only to the rural and small metropolitan independent companies and not to General. Although General does not concur in Pacific's access services tariffs as those other independent companies do, it seeks to be included in the joint proposal's provision for an annual flow-through adjustment for net settlements revenue impact brought about by this decision and future regulatory changes of this Commission and the FCC.

General states that it will suffer reduced settlements revenues as a result of the adoption of proposals in this proceeding to reduce intraLATA toll rates because General concurs in some of them and has division of revenue contracts with Pacific for some of them. It states that it will also be affected by adoption of proposals to reduce Pacific's exchange rates because it has EAS contracts with Pacific which make certain revenues dependent on Pacific's rate of return. And, it states that application of the proposed SPF to SLU allocations to intraLATA toll will affect it because of the different relative impacts of the cost allocation change for General as compared to Pacific.

If not included in the flow-through process General is left to deal with such changes in its rate case and attrition filings under the Rate Case Plan. Thus, while acknowledging that it should not be a recipient of HCF funds, General contends that when Pacific receives a decision changing toll and/or other separations revenue, General might have to wait a year or more to adjust its revenue requirements to compensate for these changes--a unique and unfair position relative to all other exchange carriers.

General's opening brief on this issue concludes that if the Commission doesn't allow it to make a showing of its revenue losses or provide the mechanism to automatically offset these losses, there is a taking by the State without any attempt to provide the right of due process of law.

The joint motion indicates that DRA disagrees with General's position, but DRA has not provided us with its argument on this issue, except to the extent that, prior to the introduction of the joint proposal, its witness Marks testified that any pursuit of increased ITC rates to offset the impact of reduced settlements resulting from newly adopted Pacific rate design should not occur without a full showing of the justness and reasonableness of the proposed new rates by the ITC, such as in a general rate application.

2. MCI

MCI regards the joint proposal as an attempt by parties to modify, without notice, a previous California Public Utilities Commission access charge decision, namely D.85-06-115. MCI states that this Commission has always judiciously avoided addressing access charge rate design issues in LEC general charge rate case proceedings and regards this joint proposal as an improperly noticed attempt to change this policy. MCI concludes that the HCF plan adopted in D.85-06-115 must remain in place and such changes in funding levels and revenue recovery as proposed in the joint brief should only be addressed on a company by company basis after a general rate case review.

3. AT&T

AT&T does not express opposition to the recovery sought by the joint proposal, just the source of that recovery. As with the HCF we authorized in D.85-06-115, the joint proposal confines funding for the HCF to a surcharge on the access CCLC. AT&T points out that this means that funding will be derived only from interLATA toll customers, and argues that this is a blatantly discriminatory tax on one class of customer. AT&T asserts that because the joint brief does not propose a limited high cost fund to offset the interLATA access SPF to SLU phase down and the elimination of the pooled billing surcharge--but rather an entirely new high cost fund whose purpose is primarily to offset a host of intraLATA revenue shifts. AT&T prefers the LRS plan with its more broadly based funding. AT&T adds that if this Commission prefers that the HCF be supported by toll customers, it should at least spread that burden over both inter- and intraLATA toll customers.

AT&T maintains that concomitant with the approval of new ITC rate designs this Commission should order the elimination of the bill and keep surcharge on intraLATA services which was authorized as an alternative to participation in the HCF by D.85-06-115 since we have an opportunity to put into place a legitimate comprehensive rate design, avoid possible duplicative collection of revenue requirement, avoid de-averaging of toll rates which would defeat the effects of the SPF to SLU transition, and avoid repression of toll service and loss of associated revenue.

AT&T also contends that we should eliminate any current surcharges on access services or interLATA toll rates, including that portion of the 24% bill and keep surcharge on intrastate toll rates which Citizens Utilities Company of California (Citizens) is presently assessing for interLATA toll, that portion of the 5% surcharge on intrastate toll rates which Sierra Telephone Company is assessing for interLATA toll, and that portion of the "percentage of charges" intrastate toll surcharge being levied by California-Oregon Telephone Company (Cal-Oregon) on AT&T for interLATA toll. Cal-Oregon itself is also seeking elimination of the latter surcharge.

F. The Ferndale Position

On September 8, 1986 two similar documents were filed with this Commission. One is a motion filed in this rate proceeding by Carlos E. Benemann. The motion explains that Benemann is a customer of Citizens and asks that the portion of hearings in the Pacific rate proceeding set to address the rate design proposals of the ITCs which concur in Pacific's tariffs be held in abeyance pending timely and proper public notice to the customers of the ITCs.

The other document was a complaint docketed as C.86-09-007. The complaint, signed by 26 Citizens customers, including Benemann, was dismissed by this Commission in D.87-07-013 upon a finding that the subject matter of the complaint was the same as that in Benemann's motion and that the issues raised were more appropriately and efficiently addressed by the motion in the existing proceeding.

As did the complaint, the motion claims that Citizens' proposal is tantamount to an application for a rate increase application and that notice must therefore be in compliance with Public Utilities Code (PU) Section 454, the relevant part of which states:

> ". . . Whenever any electrical, gas, heat, telephone, water, or sewer system corporation files an application to increase any rate or charge, other than an increase reflecting and passing through to customers only increased costs to the corporation, for the services or commodities furnished by it, the corporation shall furnish to its customers affected by the proposed increase notice of its application to the commission for approval of the increase. The corporation may include the notice with the regular bill for charges transmitted to the customers within 45 days if the corporation operates on a 30-day billing cycle, or within 75 days if the corporation operates on a 60-day billing cycle. The notice shall state the amount of the proposed increase expressed in both dollar and percentage terms, a brief statement of the reasons the increase is required or sought, and the mailing address of the commission to which any customer inquiries relative to the proposed increase, including a request by the customer to receive notice of the date, time and place of any hearing on the application, may be directed."

Although the ITCs had already notified their customers about Pacific's public hearings in this proceeding, on September 15, 1986, at the first day of hearings scheduled to address the settlement effects of Pacific's rate design proposals on the ITCs, the ALJ, without ruling on the merits of the motion, and declining to require the postponement of the settlement effects hearings, ruled that the ITCs which have been joined as parties by the OII issued in this proceeding should provide another notice to their customers, in a form designed in conjunction with the Commission's Public Advisor's office, stating what the effects of the settlement change proposals of Pacific and DRA would be, and informing their customers that there would be a public participation hearing specifically addressing this issue to be held at the Commission's hearing room in San Francisco on December 15, 1986. Later that date was changed to Tuesday, December 16, 1986 and, due to the amount of public interest in Benemann's community, Ferndale, in Humboldt County a second public participation hearing was scheduled there on Wednesday, December 17, 1986.

After the hearings Benemann and David Kilmer, on behalf of themselves and other residents of Ferndale who are customers of Citizens, filed a brief as intervenors on this settlement effects issue. The briefs again contend that our policy of issuing an OII making all ITCs which interconnect with Pacific respondents, and consolidating that OII with Pacific's rate proceeding is a denial of due process because it violates the notice requirements of PU § 454. They also claim that this Commission has ordered the ITCs to be party to a rate application case without requiring separate applications - without jurisdiction. They take the position that we may not order any rate increases or redesigns except in a properly noticed rate proceeding for each ITC, that since there has been no showing that the rate changes the ITCs will propose at the conclusion of this proceeding will be minor in nature the GO 96-A advice letter procedure is not available, and that the ITCs' rate proceedings cannot begin until this Commission has issued the present decision so that the settlements effects can be known.

G. Discussion

1. Jurisdiction

Because nearly all of the ITCs, including Citizens, concur in Pacific Bell's access charge rates they are, at present, collecting an 8.57%[7] surcharge on local and intraLATA toll charges. As we explained in detail above, we ordered

7 At the time of hearing this figure was 5.11%. It became 6.76% on January 1, 1987 when direct assignment of WATS was implemented, and 8.57% on January 1, 1988 to offset the interLATA SPF to SLU phase down. The corresponding portion of Pacific's surcharge is presently 8.81%.

implementation of this surcharge in D.85-06-115 as an interim measure to alleviate the revenue loss from the access services revenue pool which would have otherwise resulted when we lowered Pacific's access rates. Under the interim scheme this surcharge revenue is pooled with access services revenue and then divided among the pool members by a settlement procedure. It was initially our plan to eliminate the pooled surcharge in this decision by incorporating the 6.76% portion of the ITC's surcharge which is based on test year volumes into rates. The remaining 1.81% which is based on later volumes would have been collected by a bill and keep surcharge.

Our decision to postpone spreading all billing surcharges until a decision following the Phase I rate flexibility hearings in I.87-11-033 postpones the date of our elimination of the pooled surcharge. Further, it will allow us to be able to spread the surcharges accrued subsequent to 1986 along with the earlier ones. As for the present, we will authorize the ITCs to make Advice letter filings under the terms of GO 96-A to implement revisions in their pooled billing surcharges consistent with this decision. Further, although we will not eliminate the pooled surcharge now, we still address below the mechanism by which the parties will accomplish that end at a later date.

In D.85-06-115 we ordered that the ITCs could make an advice letter filing under the terms of GO 96-A to implement, following this rate design decision, a revised billing surcharge on a bill and keep basis to replace the pooled billing surcharge. Because Benemann was a party to the proceeding leading to D.85-06-115 and expressed interest in this issue the decision specified that his telephone company, Citizens, would be required to serve him with its compliance and advice filings.

Although there was criticism of the procedure from Benemann, we agree with the ALJ that it was inappropriate to postpone the settlement effects hearings scheduled to begin on

September 15, 1986. Customers of the ITCs were adequately informed of these Pacific rate proceedings in 1985. The further notice and public participation hearings that were provided pursuant to the ALJ's ruling which was issued on the first day of those hearings provided these ratepayers with a further opportunity to participate in the settlement effects portion of this proceeding and to apprise this Commission of their concerns regarding the rate implications for ITCs of Pacific's and DRA's rate design proposals in the present proceeding. The ruling, with which the ITCs complied, required the ITCs to send notices which described what the ITC and what DRA contended the effect would be on ITC rates from Pacific's proposed elimination of the 5.11% surcharge then being applied to regular monthly billings for local and intraLATA toll calls placed by customers of Pacific and the ITCs. All the notices announced the public participation hearing in San Francisco. The notices going to Citizens customers in the Ferndale area also announced the Ferndale hearing. Both hearings were in December 1986.

While we understand the concern of Benemann and other ITC customers for the fact that ITCs' rates could be significantly altered as a result of this decision, the ITCs' proposals for changes in their own rates in the settlement effects portion of this proceeding are compliance filings required by both the OII and by D.85-06-115. They are not rate case applications as Benemann asserts. For that reason the notice requirements of PU § 454 do not apply to them.

It has been our long-standing practice to issue an OII in Pacific's general rate case in order to deal with the settlement implications of Pacific's new rate design on the ITCs. The problem, as Benemann has pointed out in his testimony, his pleadings and the briefs he filed with Kilmer in the settlements effects phase, is that no notice provided to ITC customers in this proceeding can give them a very accurate picture of what the effect of Pacific's rate design will be on the ITCs' rates until Pacific's rate design is finally adopted. In the past change has been slight, and there has usually been an advantage to the ITC customers. Therefore, the procedure engendered little interest among ITC ratepayers.

The realities of divestiture have changed the way revisions in Pacific's rates impact the concurring ITCs. Divestiture has not, however, changed the fact that in order to have a complete picture of Pacific's rate design and revenues it is still necessary for this Commission to consider the implications of Pacific's rate revisions on intercompany settlements and revenues as related to intrastate toll and private line rates concurred in by these ITCs. Furthermore, it is both appropriate and necessary to address that portion of the ITCs' rates which are funded for the most part by contributions from Pacific, in the context of a Pacific proceeding.

For these reasons we will deny Benemann's motion that we find notice to the ITCs inadequate for failure to comply with the requirements of PU section 454. That section is not relevant to the ITC filings discussed above. We agree with DRA, however, that once a final rate decision is issued in this matter directing these ITCs to make advice letter filings requesting new rates consistent with this decision that §454 does require that the ITCs provide notice to their customers of the new rates prior to implementation. We believe a minimum of 30 days' notice prior to implementation is adequate.

2. The Present HCF and the Proposed Differences

We have consistently expressed our belief that there is a fundamental public interest in maintaining stable and reasonable basic exchange rates. That is why we authorized the HCF in D.85-06-115 which permits the continuation of a policy of statewide uniform toll rates while protecting ITC customers from the effects of shifting a greater burden for NTS and other costs onto their

Our decision to postpone spreading all billing surcharges until a decision following the Phase I rate flexibility hearings in I.87-11-033 postpones the date of our elimination of the pooled surcharge. Further, it will allow us to be able to spread the surcharges accrued subsequent to 1986 along with the earlier ones. As for the present, we will authorize the ITCs to make Advice letter filings under the terms of GO 96-A to implement revisions in their pooled billing surcharges consistent with this decision. Further, although we will not eliminate the pooled surcharge now, we still address below the mechanism by which the parties will accomplish that end at a later date.

In D.85-06-115 we ordered that the ITCs could make an advice letter filing under the terms of GO 96-A to implement, following this rate design decision, a revised billing surcharge on a bill and keep basis to replace the pooled billing surcharge. Because Benemann was a party to the proceeding leading to D.85-06-115 and expressed interest in this issue the decision specified that his telephone company, Citizens, would be required to serve him with its compliance and advice filings.

Although there was criticism of the procedure from Benemann, we agree with the ALJ that it was inappropriate to postpone the settlement effects hearings scheduled to begin on September 15, 1986. Customers of the ITCs were adequately informed of these Pacific rate proceedings in 1985. The further notice and public participation hearings that were provided pursuant to the ALJ's ruling which was issued on the first day of those hearings provided these ratepayers with a further opportunity to participate in the settlement effects portion of this proceeding and to apprise this Commission of their concerns regarding the rate implications for ITCs of Pacific's and DRA's rate design proposals in the present proceeding. The ruling, with which the ITCs complied, required the ITCs to send notices which described what the ITC and what DRA contended the effect would be on ITC rates from Pacific's local rates through the application of the principle of rate comparability to rates that would otherwise be increased due to the annual intrastate interLATA SPF to SLU transition to the extent that change is not offset by interstate HCF revenue.

The joint proposal broadens the scope of HCF recovery by applying the principle of rate comparability not only to the rate changes enumerated in D.85-06-115, but also to any other rate change in this rate decision which will affect ITC settlements revenues, and any PUC or FCC-ordered changes occurring during the year which have an industry-wide effect, either positive or negative, on settlement revenues or cost assignment including shifts in interstate NTS and the loss or gain in revenue occasioned by the interstate SPF to SLU shift offset by interstate HCF. revenue, the loss or gain of revenue due to changes in Pacific's non-access rates with which the ITCs concur, and losses or gains resulting from any other aspects of this Pacific rate decision or other Commission or FCC actions which have settlement revenue impact on the ITCs.

As we pointed out in D.85-06-115, since the HCF we adopted was based on rates rather than costs, it allows recovery from the HCF fund not only for the reduction in access services revenues occasioned by the intrastate interLATA SPF to SLU transition and other adjustments to access services revenue objectives, but also, because the basic exchange rates are set residually, it allows for the recovery of high operating costs in general. Some of these recoverable operating costs are clearly intraLATA costs, which under this HCF plan are recoverable from the interLATA CCLC. That being the case, the joint proposal's expansion of the rate comparability principle to certain intraLATA rate changes is not such a drastic departure. Nonetheless, AT&T finds it to be objectionable.

a. The Funding Source and Scope of Revenue Protection

It is our fundamental concern that a source of supplemental revenue be maintained for the ITCs in order to protect the availability of universal service for all California's citizens once we have eliminated the pooled surcharge these ITCs presently depend on. We meant to achieve that end by adopting the presently authorized HCF plan to fill the gap between a reasonable revenue requirement and "existing sources of revenue including interstate HCF assistance and basic exchange rates set at the highest level consistent with a 'comparable rates' standard." (D.85-06-115, mimeo. p. 205.)

Although the scope of rate protection is extended under the joint proposal, the proposed additions address the same fundamental issue, toll- and access-related changes and their effect on the ITCs' settlements revenue, and hence their continued viability. Thus, we cannot agree with AT&T that adjustments for the effects of intraLATA rate changes such as EAS rates and intraLATA toll rates are necessarily unfair and inappropriate. In fact, the presently authorized HCF already permits CCLC adjustments to recover some intraLATA costs, namely high intraLATA operating costs. Furthermore, the impact of these adjustments can be minimized by our permitting regulated IECs to flow through the effects of such changes on the CCLC access charge.

The wide support for the joint proposal persuades us that it is reasonable to permit the proposed extensions to the list of recoverable revenue changes. We are also persuaded to authorize the use of CCLCs as the HCF funding source, at least until there is some data indicating that a different distribution of the burden is warranted. Until such information is available to us, we are reluctant to add further to the burden on local rates. We fail to see any legal or equitable impediment to the adoption of this aspect of the joint proposal as AT&T suggests. We would point out that, contrary to AT&T's apparent understanding, our purpose in establishing the SPF to SLU transition in D.85-06-115 was not to decrease a specific rate. Rather, it was our purpose to decrease the assignment of NTS to interLATA access.

For these reasons we will adopt the proposed expansion of recoverable revenue changes and the use of the CCLC as a funding source for the HCF.

b. Revenue Requirement Review

The joint proposal would also have us deviate from our present policy that HCF relief should be awarded only in the rate design phase of a particular ITC's rate case. We are concerned that the ITCs not be in a position to collect HCF revenue for an unreasonably high revenue requirement. On the other hand, we are sympathetic to the fact that this Commission could not process the rate filings of all the ITCs at once, and that the ratepayers of some ITCs would likely experience dramatic local service rate increases if the ITCs simply implemented a bill and keep surcharge while awaiting our action on their rate cases. Therefore, we conclude that it is reasonable to adopt the proposal allowing the ITCs up to three years to make rate filings before their HCF funding is affected. It appears that this leeway along with the annual reductions in available funding levels will permit an orderly progression of rate case processing while adequately protecting against rate shock in the short run.

AT&T is also concerned that the joint proposal invites abuse of the HCF since the funders are not the companies administering the fund. We believe these same funding level safeguards will adequately prevent such abuse by encouraging filing for timely rate review by each ITC. If our assessment of this situation proves to be inaccurate or appears to be causing some inequity we will reassess our position.

c. The 150% Eligibility Threshold

There is very little information in this record about the propriety of moving from a 200% eligibility threshold to a 150% threshold. During the hearings the various witnesses for the Smaller Independents supported either a dollar cap or a lower percentage threshold, never more than 150%. The joint brief states that the parties to the proposal who had not previously supported the 150% concept (i.e., Pacific and DRA) now support it in conjunction with their support of the whole of this comprehensive proposal. This is explained with the statement that the whole proposal contains appropriate mechanisms for review of high-cost funding levels and associated annual changes.

Many of the witnesses who testified in opposition to the 200% level noted that each time Pacific's local rates increase, the dollar amount to which the percentage is to be applied increases. They argued that while the dollar differentials may be affordable when Pacific's local rates are relatively low, the 200% threshold will become more and more unfair as Pacific's rates rise. They also argue that the 150% level would be fairer and more in keeping with the legislature's intent. Those parties who oppose the joint proposal do not base specific objections on what the funding level should be.

As we have said we are sympathetic to the plight of the ratepayers of these small, primarily rural ITCs who may be exposed to very large rate shifts due to the impact of the reallocation of costs that we will be engaged in for the next few years. The mandate of Public Utilities Code §728 that in setting rates we consider, among other things, the rates for comparable service of adjacent local exchange carriers, directs us to assure that the exchange rates of the ITCs are reasonable when compared to those of the dominant local exchange carriers, most often Pacific. Further, we continue to believe that this end can be accomplished for now with respect to those ITCs which concur in Pacific's access rates by keeping the ITC's local rates within a reasonable percentage of rates for comparable urban service (usually Pacific's) and then recovering any still unmet costs from the intrastate HCF.

As we stated above, we have some reservations about the possibility of short-run overstatements of revenue requirement by the ITCs with these changes in eligibility criteria. However, we are impressed with the diligence with which these parties have worked on a resolution to this intricate problem. Keeping in mind the dearth of data to support either the presently effective 200% threshold, or the proposed one of 150% and the strong support evidenced by this joint proposal, we conclude that it is reasonable to adopt this aspect of the recommendation.

d. Retention of Bill and Keep Surcharges

At present Pacific's annual intraLATA SPF to SLU phase-down of access charges is accounted for by a decrease in access rates and a corresponding surcharge to intraLATA service billings. Pacific and the ITCs pool and share these surcharges in the access service pool. In this decision, however, we have accounted for the intraLATA SPF to SLU phase-downs by reducing Pacific's intraLATA toll rates and correspondingly increasing non-toll, non-access rates, including basic local rates. Thus, although the intraLATA pool and the access services pool still exist, they have shrunk. Because we agree with DRA's Shantz that it is inequitable for the ITCs to increase basic rates by more than 100%, this pool shrinkage could result in a settlements revenue shortfall for some ITCs. It is not our intent to decrease the settlement recovery for any ITC, including General and West Coast, as a result of this decrease in pooled revenue. Therefore, keeping in mind our concern about increases in basic rates, we will authorize the concurring ITCs to recover any such revenue shortfall by a uniform increase in basic exchange access line services, not to exceed 100% of present rates, followed by a bill and keep surcharge on intraLATA services where necessary. We agree with AT&T, however, that the bill and keep surcharge should not be retained as an alternative to the intrastate HCF for the concurring ITCs. Since General and West Coast do not concur in Pacific's access rates, however, we will authorize them to recover any shortfall by a bill and keep billing surcharge on intraLATA services.

AT&T also argues for the removal of the previously authorized Citizens 24% bill and keep surcharge on intrastate toll rates and the smaller surcharge on intrastate toll rates previously authorized for Sierra Telephone Company (Sierra). AT&T adds that Cal-Oregon, itself, seeks to eliminate its annual $35,000 intrastate toll surcharge in the context of the revisions it proposes to its rate design in this proceeding.

The surcharges that AT&T is concerned about are surcharges on intrastate toll service which we authorized prior to divestiture. Specifically AT&T is concerned with the portion of those surcharges which is levied on interLATA toll service. That issue is the subject of a pending complaint proceeding, C.85-07-062, initiated by AT&T, which is addressing the question of whether these surcharges should be eliminated. Therefore, we will leave the authorized toll surcharges as they are until we have determined the merits of AT&T's complaint.

AT&T is asking us to address the details of ITC rate design. Although the ITCs which interconnect with Pacific are parties to this proceeding this is not a rate proceeding for each of those ITCs. Therefore, it is inappropriate to adopt a new rate design for those companies in this proceeding. Nonetheless, we have determined that once the pooled surcharge is eliminated these ITCs should continue to recover the revenue which that surcharge now provides, and should remain whole despite the settlement effects of Pacific's rate decision. We believe that a rate design modeled after that proposed by DRA's Shantz accomplishes that end well while avoiding a further surcharge by spreading revenue changes as a capped uniform percentage increase across an ITC's existing rate design with the residual recoverable from the intrastate HCF. Therefore, we will authorize adoption of that model, revised to take account of the elements of the joint proposal--principally the 150% eligibility threshold, based on Pacific's rates in effect at the time this proposal is implemented. However, we will not adopt Shantz' proposal to increase ITC service connection charges up to 100% of Pacific's rates for comparable service before applying the flat percentage rate. This provision is less fair to ratepayers than permitting the entire surcharge to be spread over a much broader base, and also constitutes the type of substantive rate design change described below which must be avoided in this proceeding.

The equitable spreading of surcharges and their incorporation into the existing rate design framework is qualitatively different from the substantive rate design changes proposed by some of the ITCs, namely that Happy Valley Telephone Company, Cal-Oregon, and Hornitos Telephone Company be permitted to remove their mileage charges, that Kerman Telephone Company be permitted to raise its coin rates from $.10 to $.20, that Cal-Oregon be permitted to place all four of its exchanges on the same rate schedule, and that Siskiyou be authorized to change or eliminate various rates. Such structural changes should only occur in the context of a properly noticed rate filing. The only surcharge that is affected by adoption of the proposed HCF plan is the pooled access services surcharge which we will eliminate in the decision we will issue following supplementary rate design hearings after our Phase I rate flexibility hearings in I.87-11-033. Other ITC surcharges will stay in place until they are specifically addressed in a rate review or some other proceeding.

e. **Time Frame for the 100% Funding Level**

The joint proposal allows HCF recipients to receive funding at 100% of their determined funding requirement for the years 1987 through 1989. Since 1987 has already passed, and in order to avoid a glut of rate case filings, we find it appropriate to modify the proposal to allow the 100% funding for 1988 through 1990.

3. Notice of Broadened HCF

Contrary to MCI's contention, all the parties to this proceeding did receive "notice" of the attempt to move from a narrow to a broader HCF, since the LRS plan presented by Pacific's witness, Ondeck, at the hearing also went beyond offsetting the intrastate interLATA access SPF to SLU phase down and the elimination of the pooled billing surcharge. We do not view such a proposal as inappropriate to this proceeding.

4. Participation of General and West Coast in the HCF Plan

We turn now to the concern of General that it be permitted an annual adjustment, outside a rate case or attrition filing, to flow through to its rates the effects of Commission and FCC actions in the same manner permitted to the ITCs under the joint proposal.

The primary purpose of the joint proposal is to deal with the settlement effects of changes in access rates in Pacific's rate decision on those ITCs which concur in its access tariffs. Our endorsement of a plan which recognizes the settlement effects of certain other actions of this Commission and the FCC is an extraordinary one which is based on what appears to be extreme and temporary rate pressure being placed upon the concurring ITCs during this transitional period of SPF to SLU phase-down and the phased implementation of the interstate HCF. Our primary concern in granting this proposal is to preserve the public interest in maintaining stable and reasonable basic exchange rates.

General's request to be included in the flow-through provisions of the proposed HCF plan, while at the same time acknowledging that it should not be a recipient of high cost funds, misconstrues the plan. The HCF is an option only to ITCs which concur in Pacific's Access Services Tariff Schedule 175-T. Further, this flow-through provision is only an element of the calculation which is made to determine whether an ITC is eligible to receive HCF funding. The reasonableness of this particular provision does not arise from the notion that these ITCs deserve guaranteed rates, but rather from our policy to protect universal service in situations where we have already found that the rate impacts on the smaller ITCs are likely to be so disproportionately large that basic service rates would become inequitably high. The proposal does not single out General for different treatment. It simply makes eligibility for the flow-through provision ultimately contingent on eligibility to receive HCF funds. If an ITC is not eligible to receive HCF funds after making this flow-through calculation it is assumed that the ITC's rates do not warrant the extraordinary protection of the provisions of the joint proposal. Therefore, we will deny General's request.

Since General's affiliate, West Coast, also does not concur in Pacific's Access Services Tariff 175-T, it is likewise ineligible to participate in the HCF plan.

5. <u>Procedural Request of the ITCs</u>

In response to a March 11, 1988 petition for modification of Ordering Paragraph 15a of D.87-12-067, filed by the smaller ITCs we issued D.88-03-064. In that decision we determined that it was preferable to postpone addressing one of the issues raised by the petition until we addressed rate design. The Petition, at page 5, requests that we adopt the following language:

> "Further, those rural and small metro local exchange companies electing to do so may

> combine the net settlement effect of future annual intraLATA separations changes by combining them in a single advice letter filing with other Commission-ordered settlement and separations changes under existing advice letter procedures, as the same may be modified in the rate design decision to be issued in this Pacific Bell rate case."

The ITCs' request to combine various Commission ordered separations and settlements changes in one annual advice letter filing is unopposed and appears to be advantageous to both the ITCs and their customers since it would alleviate the possibility of a number of separate rate changes in a year and reduce implementation costs for the ITCs. Therefore we will authorize the ITCs to follow such a procedure if they choose to do so.

6. Relationship Between Settlements and the High Cost Fund for ITCs

At the time the parties presented the HCF proposal it was assumed that all surcharges would be spread over rates in this proceeding. In fact, D.88-03-064 was a direct result of the concern that the large surcredits for local exchange services, which some ITCs would be required to implement as a result of our Phase II revenue requirement decision's (D.87-12-067 as modified) treatment of the intraLATA SPF to SLU transition at Ordering Paragraph 15A, would be largely offset by the revenue shifts from reductions to intraLATA toll rates expected to be adopted in the present decision. Because we shared that concern D.88-03-064 gave the ITCs the choice of either implementing a new bill and keep surcharge (or surcredit) on intraLATA services excluding intraLATA toll, or simply accruing the net settlements impacts of the SPF to SLU phase-down from January 1, 1988 in an interest bearing memorandum account, the balance of which could then be combined with the settlement impacts of this decision so as to alleviate great rate fluctuations. Sixteen ITCs chose to establish memorandum accounts. Appendix C of this decision shows the net settlements effects resulting from the rate design authorized herein and the intraLATA SPF to SLU phase down authorized by Ordering Paragraph 15A of D.87-12-067 as amended, for the ITCs which chose to implement memorandum accounts.

Since we have not eliminated the surcharges which would have been a primary cause of the large rate changes these parties were planning for, the effects on the ITCs will not be so great as anticipated. Therefore, it is not necessary or reasonable, with one exception, Hornitos Telephone Company, to continue the memorandum accounts pending our supplementary rate design consideration in a further phase of this proceeding.

In the meantime, for those ITCs whose net settlements effect is a revenue shortfall, (shown on Appendix C as an amount in parentheses), we will authorize a uniform percentage increase in basic exchange service rates in the manner described in our HCF eligibility discussion. With the exception of Hornitos, we will direct ITCs whose net settlements effect is a positive amount, to refund that amount by a bill and keep billing surcredit on the intraLATA billing base.

Among the ITC's for which a reduction in basic exchange rates is indicated, Hornitos Telephone presents the greatest problem. Due to its small billing base, the flow through of reductions may cause cash flow problems for the company. Rather than imposing such a reduction on the company, when the impact of it will probably be alleviated once we have adopted a supplementary rate design in the next rate design phase of this proceeding, we will authorize Hornitos to accrue the net settlement effect in an interest bearing memorandum account.

Further, in order to avoid accruing exorbitant amounts or unnecessary interest, those ITCs, except Hornitos, which now have memorandum accounts should eliminate the funds in those accounts by incorporating the amount into a bill and keep surcharge or surcredit spread over a one year period. We realize that at some point it will likely be necessary for Hornitos to refund the amounts it is now accruing and will continue to accrue too. Therefore, we invite Hornitos and any other party interested in doing so to propose, in the supplementary rate design proceeding, a solution for dealing with this problem.

Although this unanticipated situation will be alleviated somewhat with the spreading of surcharge revenue into rates, it appears that our adoption of the SPF to SLU mechanism for intraLATA toll revenues (identified in column (g) of Appendix C) will, for some ITCs, continue in the future to result in an increase of revenues from intraLATA toll which is so substantial that it will more than offset the decrease in revenues expected to result from the shifting of NTS costs out of intraLATA MTS rates. This may be the result of the calling patterns experienced by these particular ITCs. Since SPF to SLU was adopted for intraLATA toll, more of the NTS costs associated with providing intraLATA toll service are attributed to toll revenues with each year of the phase down. Apparently toll usage is a much greater proportion of total usage for the rural ITCs than it is for Pacific. Because of this disproportionally high toll usage, the costs of NTS equipment attributable to the provision of MTS service has increased for these ITCs though the opposite is true for Pacific as the SPF to SLU phase down takes effect. Under the settlements process, each of these ITCs is thus entitled to more money from the settlements pool as compensation for the cost of providing MTS services.

Since the effect of the intraLATA SPF to SLU transition is designed to be borne by basic exchange rates, the revenues received by these ITCs from the settlements pool is to be offset by a reduction to their basic exchange rates. This result is the opposite of what the Commission expected to occur. The Commission anticipated that the SPF to SLU transition would require an increase in basic exchange rates, and that this increase would be tempered by revenues from the HCF. Unfortunately, since revenues from the settlements pool are pre-determined, to avoid overcollecting their revenue requirement, certain ITCs would have to reduce their basic exchange rates to such a level that they would bear little relation to the rates for comparable service charged by telephone corporations in adjacent territory. (Pub. Util. Code Section 728).

The problem appears to lie in the fact that the settlements process does not impute any contribution to the companies' revenues from basic rates. This results from our historic practice of setting basic rates residually. Thus, the ITCs' eligibility for settlements revenues is not based on their total costs of service, but only on their proportional amount of statewide plant used to provide intraLATA service. After contributions from the settlement pool are factored into the ITC's revenues, the ITC's eligibility for contributions from the HCF is based on the relation of its rates, rather than costs, to the prevailing carrier's rates. The ITC's receipts from the HCF may therefore be greater than actually needed to carry out the purpose of the fund.

It is clear from the outcomes we are seeing that the relationship between the HCF and the settlements process should be revisited at the earliest time practical, with an eye to possible modification of the settlements process to ensure its compatibility with the HCF and to ensure that contributors to the settlements pool are not forced to subsidize some participants without regard to their total revenue requirement and reasonable contributions from basic exchange service. We invite the parties to present recommendations in the supplemental rate design proceeding for ensuring that these pooling mechanisms operate equitably for both contributors and recipients. A more specific request for testimony will be made by ALJ or assigned Commissioner ruling.

IX. Issues Related to Rate Design and/or Revenue Requirement

A. Shift of $11 Million from Special Access Revenues to Non-Access Rates Per D.87-08-048

Our decision in Phase III of Pacific's access proceeding concluded that the revenue requirement for Pacific's special access services should be reduced by $11 million and that this reduction should be offset by an increase in Pacific's nonaccess services. We determined that it would be best to implement this rate design change concurrently with the effective date of the present rate design decision, since there would only be a few months difference in effective dates and doing so would avoid the adverse effects on ratepayers of short-term billing changes. Therefore, in this decision we are ordering Pacific to decrease its special access rates by $11 million.

This rate shift will have the added effect of lowering expenses for AT&T. In D.85-06-113, we modified D.85-03-056, to require that within 14 days of local exchange utilities making their advice letter filings to reduce local access charges AT&T pass on to its customers through a corresponding incremental reduction in the billing surcharge any reduction in its expense stemming from reductions in local exchange utilities' access charges. However, in D.87-12-067 as amended by D.88-02-046 we took note of AT&T's recently filed application for rate flexibility and several other pending rate matters which would affect AT&T's access charge expenses. We therefore determined that for the present AT&T should accumulate the revenue reduction we were ordering in a memorandum account, with interest, commencing on the effective date of the tariff revision. We will order the same treatment here.

Ordering Paragraph 38 of our Phase III access decision, D.87-08-048, invited interested parties to propose a rate design or otherwise comment on the disposition of the $11 million in revenue requirement which has been transferred from access services to nonaccess services. That decision was served on all the parties to the proceeding.

DRA responded by recommending that the increase in revenue requirement for nonaccess services be recovered through an adjustment in the billing surcharge mechanism set forth in schedule Cal. P.U.C. No. A2 Rule No. 33 of Pacific's nonaccess tariffs. DRA calculates that based on Pacific's retaining 96.5% of the billings from access services, Pacific's share of this rate reduction is $10.615 million and that recovering this from nonaccess rates will require an incremental increase in the customer billing surcharge applicable to nonaccess services of .219%, thus raising Pacific's present surcharge from 1.288% to 1.507%. DRA adds that each of the ITCs which concur in Pacific's access services tariff should also be permitted to increase their respective customer billing surcharges by the same .219% increment. It does not indicate what the dollar effect of this increment would be on each concurring ITC.

Despite our finding in D.87-08-048 that the proposed market pricing for Digital Data Services (DDS) and High Capacity Services (HiCap) is reasonable, DRA's response goes on to suggest that we order Pacific to reflect this $11 million decrease in access services revenue requirement in the rates associated with these two services. It is unclear whether DRA is recommending that this decrease be accomplished solely from these two special access rates or simply that the decreased revenue requirement be spread over all special access services, including these two.

Both Pacific and AT&T responded to DRA's recommendations. AT&T does not address the rate spreading issue, but Pacific contends that this treatment should be an interim measure pending this final rate design decision which should eliminate billing surcharges by spreading the associated revenue requirement to appropriate service rates, specifically suggesting that the rates for business services currently priced below cost and not targeted by the Commission for subsidization should be increased.

Both respondents object to DRA's suggestion about reflecting the $11 million decrease in revenue requirement for access services in rates associated with DDS and HiCap. AT&T claims that DRA's proposal would result in non-cost based rates for special access services other than DDS and HiCap contrary to the intent of D.87-08-048. Pacific asks us to reject DRA's recommendation for the reasons set forth in the Proposed Rate Design of Pacific Bell for Special Access Service, filed by Pacific on September 15, 1987. So far as we can observe that document offers no reasons. It simply submits a new rate design for special access services which purports to reduce revenue by $11 million by reducing certain proposed special access rates, not including DDS and HiCap rates.

Nonetheless, we agree that DRA's recommendation should be rejected. D.87-06-048 specifically found that the market based rates proposed by Pacific for DDS and HiCap were reasonable. Therefore, it is inappropriate to now require, based on no new evidence, a revenue requirement spread which would ignore that finding. Furthermore, adoption of DRA's proposal would require that rates for the other special access services might result in a contribution beyond what we determined to be reasonable in that decision. Therefore, we will order that the $11 million reduction be spread across all access services rates, except DDS and HiCap, on a uniform percentage basis.

As for the disposition of the revenue requirement to be transferred to nonaccess service rates, we will increase Pacific's annual nonaccess revenue requirement by $10.293 million, which represents Pacific's settled share of the total rate reduction for access services.

Since D.85-06-115 authorized concurring ITCs to adopt the same percentage surcharge as Pacific in order to adjust nonaccess rates to make up for the reduction in revenue objective for access charges, it is also appropriate here to authorize an increase in nonaccess revenue requirement to offset the settlements effects for each ITC which will reflect this $11 million shift. The settlements effects for each ITC are set forth in Table 2, below.

TABLE 2

Revenue Requirement Increase Attributable to
$11 Million Shift from Special Access Charges

ITC	Amount
Calaveras Telephone Company	$ 5,236
Capay Valley Telephone System, Inc.	1,144
California-Oregon Telephone Co.	8,085
Citizens Utilities Company of Calif.	157,850
Continental Telephone Company of Cal.	326,150
C. P. National	20,724
Ducor Telephone Company	2,453
Evans Telephone Company	11,506
Foresthill Telephone Co.	2,200
Happy Valley Telephone Company	10,285
Hornitos Telephone Company	2,750
Kerman Telephone Co.	5,038
Pinnacles Telephone Company	385
The Ponderosa Telephone Co.	18,744
Roseville Telephone Company	58,399
Sierra Telephone Company, Inc.	26,598
The Siskiyou Telephone Company	10,637
Tuolumne Telephone Company	19,459
The Volcano Telephone Company	19,173

B. Quality of Service to Private Line Alarm Customers

1. Standards

The Commission's General Order (GO) 152 establishes standards for the installation, maintenance and operation of private line alarm service provided by telephone utilities to their customers. It sets two service criteria for each of five areas of service measurement. The first criterion is called the standard service level, which is considered adequate performance. The second is called the reporting service level, which is significantly below the standard service level and is considered inadequate service. Performance at or below this level is to be addressed in quarterly reports from the utility to the Commission. In between these levels is a category called service below standard. Performance in this range is only considered inadequate if it is frequent and substantially below the standard range.

The five service measurements to which these criteria are applied are (1) installation alarm held orders; (2) installation commitments; (3) installation trouble reports; (4) non-installation service trouble reports; and (5) non-installation repair response. One of the issues addressed in this proceeding was whether Pacific is meeting the standard service level criteria for each of these areas.

Pacific presented testimony of R.N. Dills who is its Division Staff Manager responsible for the guidelines for the provisioning and maintenance of the bulk of the services offered by Pacific Bell. At the time of the hearing he was also the chairman of the GO 152 committee, a group comprised of representatives from the Commission staff, the telephone utilities, and the alarm industry which meets to consider whether revisions in the scope of GO 152 are needed. Dills testified that Pacific has generally exceeded the minimum requirements for the standard service level for each of the five service measurements. He documented this claim with exhibit 83 which was received in June, 1985, and with exhibit 235 which was received in the later hearing on November 4, 1985.

The exhibits, as required by GO 152 list nine, rather than five service measurements. This is because alarm held orders are divided into three categories to show orders held from 31 to 60 days, from 61 to 90 days, and over 90 days; and because repair response times are also divided into three categories. The first is designed to show the average duration for responding to private alarm service measured by Pacific's SSTAR measurement system; the second shows that measured by its TREAT measurement system; and the third lists the total trouble reports which took over 48 hours to clear.

Each of these nine service measurements is shown on a monthly basis from January 1983 through June 1985 for each of Pacific's reporting units. Pacific has five such reporting units, the San Francisco Bay region, the Los Angeles region, the San Diego region, the remainder of northern California, and the remainder of southern California. The exhibits show a steadily improving record of meeting the measurement standards over that time period, with only one service measurement during one month at one reporting unit in 1985 being at or below the reporting service level.

2. <u>Opposition Witnesses</u>

The Western Burglar and Fire Alarm Association (WBFAA), an industry organization, offered three witnesses for the proposition that the quality of Pacific's private line alarm service is inadequate. They were Jerry O'Brien, the Director of Telecommunications for API Alarm Systems which does business primarily in southern California; Roger L. Westphal, the President of Bay Alarm Company, Inc., which does business in the San Francisco Bay area; and Warren V. Glass, III, the President and founder of Warren Security Systems, Inc., which does business in the northern San Francisco Bay area.

a. O'Brien

O'Brien expressed concern about Pacific's repair response time. He testified that as a result of significant differences between the repair response times recorded by API on its computerized system and those reported by Pacific that the two entities conducted a special supervised testing comparison which was completed in October, 1985, which he claimed revealed 134 discrepancies. However, as of the November 4, 1985 hearing date, API and Pacific had not reviewed those discrepancies because Pacific cancelled a scheduled meeting.

Schedule B to O'Brien's testimony, Exhibit 236, shows that API recorded more outages for 3002-type circuit service than Pacific did, and that the average duration time for repair to these lines was recorded by API as being nearly an hour longer than what Pacific recorded. Likewise, for 1009-type metallic circuits, API recorded more outages than Pacific, with API recording 14 and Pacific recording 7. API found the average duration for completion of service in this case to be quite a bit shorter than Pacific recorded.

O'Brien gave several examples of discrepancies. One demonstrated Pacific not including certain waiting time in its duration time which API did include. Another was a disagreement about whose problem the outage was. Two of the examples were of situations where there were acknowledged Pacific faults, but the problems came clear while testing, and were therefore reported by Pacific as no trouble found. O'Brien contends that Pacific did not record these as trouble reports although there is no basis in GO 152 for not doing so. He stated that this is the primary reason that Pacific's number of reported outages is lower than API's. Another example was one where Pacific claimed the problem was API's because Pacific's records showed locations which Pacific claimed were under API's control, while API contends that API had previously cancelled them. O'Brien also testified that a common trouble with a 3002 circuit is described as no answer back, and that on several occasions API placed trouble reports with Pacific for this reason only to get a report back from Pacific that the problem was no answer back.

O'Brien states that these examples illustrate the need for better training of Pacific's service and test-board personnel. He claims that if they were reporting properly Pacific's performance for 3002 circuits used by API would be below the mandated reporting levels as is Pacific's performance for the 1009 circuits used by API as measured by Pacific's TREAT system.

During cross-examination by Pacific's counsel O'Brien acknowledged that: "[O]ne of the problems that we had in comparing information from your company to our company is your information is presented by area code 213, 818 in GO 152 and our information is presented by our central station that--our circuits may cross a number of area codes."

In addition to more training O'Brien recommends that we consider adopting a modification to GO 152 which might continue to permit the present duration times to clear for individual loops but sets shorter duration times for the mid-links or back-bones of the circuit because when they go out every customer is affected and the present durations times for these outages is too long.

b. Westphal

Westphal also testified about Pacific's repair response time, stating that it has improved but not as much as reflected in Dills' testimony. Westphal noted that his company, Bay Alarm, is one of the largest alarm company users of private lines in area code (415). He explained that Bay Alarm and Pacific conducted a controlled joint comparison of trouble report records in January, 1985 because Pacific was consistently reporting lower repair response times for the San Francisco Bay area than Bay Alarm was experiencing. Based on that comparison Westphal concluded that Pacific was closing out its trouble tickets before a circuit was ultimately repaired or clearing the ticket for a single trouble on a circuit and then opening a new trouble ticket for another trouble on that same circuit, resulting in more tickets, but shorter average times. This conclusion led Westphal to recommend that this Commission continue to actively participate in the quarterly GO 152 meetings and continue to monitor the accuracy of Pacific's reporting, and its compliance with the GO 152 standards.

c. Glass

Glass' concern was with another aspect of the GO 152 requirements, the provision of new service. He testified that his company, Warren Security Systems, Inc., which has about 1000 accounts that use private line services in the northern Bay area, has experienced significant difficulties in the provisioning of new services, particularly on Morse Multiplex Polling circuits (type 3002 circuits). He testified that almost every time a new loop is added to an existing circuit, the new loop fails to work, and may impact the whole circuit. He went on to state that these loops often fluctuate between normal status and outage status, taking as much as three to six months to finally work consistently. He also stated that the addition of new legs to existing loops also often causes trouble on one or more of the existing loops. He also testified that these troublesome type 3002 loops are being used because Pacific asked the industry to use this more modern technology rather than the 1009 signal grade metallic circuits because, among other things, Pacific's employees were more familiar with 3002 circuits and were better equipped to install and maintain them, resulting in less installation troubles.

In addressing why Pacific reports virtually no installation troubles, Glass explained that GO 152 requires that along with making a trouble report for Pacific's reporting system by dialing 611, installation troubles must also be reported to a special telephone number within seven days of installation. He expressed his belief that this additional reporting was not being done in compliance with these requirements despite attempts by WBFAA and other associations to educate their members to do so. He further testified that there is a second reason for this discrepancy, which is that his company often does not arrive at a location to make a final hook-up of the alarm system within seven days from Pacific installing the circuit. In each of these cases the trouble would show on Pacific's records as a service trouble report, not as an installation trouble report.

Glass made two recommendations based on these problems. First, he recommended that Pacific, the Commission and the alarm industry should conduct further meetings to attempt to improve this reporting methodology; and second, he recommended that Pacific emphasize its training of its installation personnel for the installation of these special 3002 circuits.

3. Pacific's Rebuttal

In response to Glass' examples, Pacific's Dills testified that when Pacific receives a trouble report, conducts a test and concludes that the trouble is not with Pacific equipment, a Pacific employee will call the alarm company and tell that to the alarm company technician or tester. If the alarm company's technician so requests, Pacific will keep its ticket open on the report for up to four hours to give the alarm company a chance to discern whether the problem is in its equipment. He stated that if Pacific does not hear back from the alarm company within four hours it closes the ticket. Otherwise, the policy is to come to agreement as to the disposition. Therefore, he concluded that the example of multiple tickets for problems proximate in time on one circuit were the result of separate problems on separate segments of a circuit. He stated that after Pacific conducted a test for the first problem and determined it had been resolved, the alarm company agreed and both Pacific and the alarm company closed their tickets on the matter. Then the company filed a separate trouble report shortly thereafter on the second problem. He added that Pacific would not have closed its ticket if the company's technician had stated that he still showed the circuit being down.

Turning to the other problems with installation that Glass testified about, O'Brien noted that once the issue was brought to Pacific's attention, it was remedied, so that as shown by the table attached to Glass' testimony, all the problems save one were repaired in August and September of 1985. He added that it has become apparent from Glass' input at GO 152 meetings that when Pacific adds a segment onto an existing circuit it is necessary for Pacific to test the circuit overall or at least test the circuit from the bridge to which that segment is being added. He stated that Pacific was now doing such testing with all installations for Warren Security. Further, O'Brien testified that Pacific's records showed that some of the dates Warren Security listed as dates when the circuit was finally okay were incorrect and that the dates were actually earlier.

Dills also testified that he believed the differences between the response times reported by Pacific and those reported by API and Bay Alarm resulted from the fact that the companies' studies represented one part, not the total, of a Pacific reporting region, and from the fact that API's data for type 1009 circuits was very sparse and, therefore, unrepresentative as was Bay Alarm's data for type 3002 circuits. Dills did not press his original claim (Exhibit 234, p. 9) that any differences between repair response times tracked and reported by Pacific and by alarm companies have been generally due to differences in tracking methodologies, and, in fact, he disagreed with claims of O'Brien that problems that cleared while testing were not being counted by Pacific as trouble reports though they were counted by API.

He further testified that Pacific had just completed a review of the 134 discrepancies between its report and API's and he concluded that the largest number of them, were cases where Pacific had determined that API's equipment was the cause of the problem, while API determined that Pacific was responsible. He claimed that the number of these differences was large enough, and the response times were generally so short, that adding them to Pacific's figures would lower its overall average repair response time. He testified that adding the "test okay" and "cleared while testing" which O'Brien had apparently omitted, would have the same effect. Dills added that the employees in Pacific's Alhambra Special Service Center whom API deals with have all worked there at least two years and have had 13 weeks of classroom training on testing of these types of specialized services followed by supervised on-the-job training, and that Pacific is also giving these employees two days of training on the technology of the bridges that Pacific gets from Tel Labs Corporation, and which API happens to use a lot.

In explaining his understanding of the discrepancies between the reports of Pacific and Bay Alarm, Dills admitted that Pacific's data base is sometimes incomplete or inaccurate so that when Pacific receives a trouble report it sometimes happens that the report refers to circuit nomenclature or a segment number which is not in Pacific's data base. He stated that it is Pacific's policy to accept the trouble report and then fix its data base afterwards. He testified that he thought Pacific's data base was much more accurate than Bay Alarm's list of 17 unmatched problems indicated, but he had no explanation for it.

4. Discussion

Pacific briefly addressed this GO 152 service quality issue in its concurrently filed opening brief on rate design and settlement effects. WBFAA did not. Nor did any other party. Both Pacific and WBFAA addressed the issue in their reply briefs. On March 3, 1987 WBFAA filed a motion to strike the portion of Pacific's reply brief addressing the issue on the ground that it was not replying to anything since no other party had argued about the issue in opening briefs. Ten days later Pacific filed an opposition to the motion to strike arguing that WBFAA's motion was unsupported by legal citation, that Pacific's reply brief raised no new issues, "but simply elaborated briefly...on the previous discussion," and that it would be unfair to grant the motion because doing so would deny Pacific "the opportunity to address the issues WBFAA raised for the first time in its reply brief." This last argument seems to contradict the first one.

We appreciate WBFAA's apparent concern with reducing the amount of verbiage presented to this Commission for consideration. (Although the motion and opposition to it were about as long as Pacific's discussion on the subject in its reply brief.) We also agree that a reply brief ought to reply to something and do nothing more. However, Rule 75, our procedural rule on briefs does not even mention reply briefs let alone delineate their content, and the ALJ did not make any such proscription. Therefore, although we are not impressed with Pacific's argument in opposition, especially its last argument, we find no basis for granting the motion.

Turning to the presentation of the parties on this issue, it seems clear to us that the process created by GO 152 is working and has improved the quality of Pacific's installation and maintenance of private line alarm service. We are satisfied that Pacific is in substantial compliance with the requirements of GO 152 and that many of the discrepancies between the response times reported by WBFAA members and by Pacific have to do with industry misunderstandings of reporting requirements and, perhaps, insufficiently precise definitions in GO 152. Many other problems described by the WBFAA testimony either have been or can be remedied by informal discussions between the parties or GO 152 committee discussion and possible recommendations for GO modification. We find that the errors for which Pacific is responsible are neither so great nor so egregious that we ought to intervene by now adopting modifications to GO 152. The witnesses have offered no evidence that the GO 152 committee process is ineffective. In fact their testimony indicates that it is working quite well. Therefore, we conclude that it is not necessary or appropriate to adopt GO 152 modifications at this time.

We believe there are still many areas where service improvement can be achieved and that regular meetings of the committee is the best means of addressing such issues. For this reason we agree with Westphal that there should continue to be Commission representation at the quarterly GO 152 meetings, and we would therefore not approve a modification which removed the requirement from the General Order.

On the whole we find Pacific's service quality for the installation and maintenance of private line alarm service to be satisfactory.

X. Supplementary Rate Design

As indicated previously this decision leaves in place all the components of the surcharges on intraLATA billings. I.87-11-033, which is addressing regulatory flexibility for local exchange companies, holds open this present general rate proceeding for a supplementary rate design. Among other things, the revenue requirement changes due to the 1987 federal tax law changes, the USOA rewrite, inside wire, and 1988 attrition decisions will be reflected in rates based on the record developed in the supplementary rate design. We have also herein specified that we will address the rate design for Touchtone service in that phase. There will no doubt be still further issues needing to be addressed in that proceeding, including issues raised in the proposed stipulation in I.87-11-033. Such issues may be specified in one or more ALJ rulings, assigned Commissioner rulings, or Commission orders, to be issued as appropriate in conjunction with our review of Phase I rate flexibility issues. We do wish, however, to remind the parties that we intend to abandon the 1986 test year billing base with the close of this decision and to rely on more up to date billing base data in the supplementary rate design. For that reason we have ordered the parties to file 1988 and 1989 projected billing base data in the supplementary rate design phase.

On July 1, 1985 an Administrative Law Judge Ruling established an ex parte rule in this proceeding on the motion of William Knecht made on behalf of the Ad Hoc Group of Private Line Users, Parts Locator, Inc., Telephone Users Foundation, and California Association of Utility Shareholders. These parties were not active in Phase 2 of this proceeding ad we conclude that their interest in having an ex parte rule in A.85-01-034 has lapsed. Our supplementary rate design will be developed in conjunction with our decisions in I.87-11-033, which does not have a similar ex parte rule in place. To place both proceedings on a consistent footing, therefore, we will extinguish the requirements of the July 1, 1985 ruling effective on the same date as the order in this proceeding.

__Findings of Fact__

1. In order to spread Pacific's billing surcharges equitably and avoid unnecessary rate fluctuations, surcharges should be spread in the supplemental rate design to follow Phase I hearings in I.87-11-033 based upon updated billing base data.

2. Pacific's 130 Call Allowance Plan proposal caps the monthly rate at the same price as its flat rate Unlimited Calling Plan proposal.

3. Pacific proposes reducing the present 2-tier charge for calls in excess of the 60-call allowance under the present Measured Call Plan, but proposes no other changes.

4. Although flat rate service is less costly to administer than measured service, the structure of Pacific's 130 Call Allowance Plan would make the flat rate service option uneconomical and would essentially eliminate it.

5. Pacific proposes separate access and usage rate elements for local residence services, though the rate design does not track access and usage costs.

6. It is this Commission's intent to authorize a rate design, including the authorization of measured basic rates, which promotes economic efficiency.

7. Pacific's Universal Lifeline Telephone Service (ULTS or Lifeline) proposal expands service options for the low income customers who qualify for ULTS consistent with AB 3288.

8. DRA opposes Pacific's request for authority to recover the difference between regular and Lifeline rates from the Universal Telephone Service Fund.

9. Pacific proposes to increase the charge for installation or service on the first residential line by over 42%.

10. Pacific proposes giving customers a 90-day grace period from the implementation of its new rate design to choose a new residential service without being subject to a change fee.

11. CBCHA/TCA and FEA argue that it is necessary to move away from residual pricing and toward market-based or cost-based pricing for residence service except Lifeline.

12. Pacific proposes to increase measured line business rates, and has proposed an original and an alternative rate increase for the initial minute of local business usage.

13. Pacific proposes rate design changes in its PBX trunk rates which will bring revenue closer to costs.

14. The services available to a customer through a PBX trunk accompanied with Direct Inward Dialing (DID) are similar to the services available through Centrex.

15. In response to the argument that the determination of when a PBX trunk rather than an ordinary business line is necessary, Pacific has proposed an alternative to its initial proposal which increases rates for PBX trunk access by less than the initial proposal.

16. Pacific has no written criteria describing the design parameters for PBX service.

17. Pacific's proposed Centrex rate design adds rates for its new digital services.

18. Pacific has not demonstrated the reasonableness of its proposed large decrease in the tie line rate, or the large overall revenue requirement decrease in its Centrex proposal.

19. Implementation of a separate trunk sensitive rate provides an equitable balance of charges for both PBX and TAS users of DID services.

20. Though Pacific's DID cost study is not as thorough as it could have been, it clearly shows that there is no cost basis for differentiating charges for successive blocks of DID station numbers.

21. Pacific's cost study is not complete enough to warrant the rates it proposes for DID station number block charges, since

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5. Pacific proposes eliminating the present 2-tier pricing structure and reducing the charge for calls in excess of the 60-call allowance under the present Lifeline Measured Call Plan.

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cost allocations for DID cannot be compared with cost allocations for Centrex.

22. TASC proposes reducing the rate for DID station number blocks from the proposed 1.25 to a 1.0 revenue to cost ratio.

23. TASC's request for cancellation of Pacific's Basic Termination Charge for termination of DID service raises an issue which cannot be resolved in this proceeding because Pacific has had no opportunity to respond.

24. TURN asks that Pacific's public coin telephone rates be reduced from $.20 to $.10, or at least to $.15.

25. Pacific requests a 55% increase in its access rates for semi-public coin service. Its evidence shows that costs exceed revenue by 45%.

26. Pacific requests an increase in service charge rates for semi-public coin service which approximately reflects the amount by which costs exceed revenue.

27. Pacific proposes to add a deposit requirement of about $400 to $500 for semi-public coin service at locations it deems to be "not secure."

28. Pacific has produced no new COPT cost evidence since that presented to this Commission when its present COPT rates were authorized.

29. Pacific's presently authorized recurring COPT rates are the same as its ZUM Zone 1 rates.

30. At the time present COPT rates were set residence and business usage rates were the same for ZUM Zone 1.

31. COPT costs have characteristics similar to those for measured business lines.

32. The record in this proceeding presents no cost data which supports adopting nonrecurring COPT rates for installation, repair, and conversion different from the percentage increase this decision adopts for business and residence services.

33. Pacific proposes increasing the rate for its nonpublished service and adding a new service, Directory Assistance Listing (DAL) at the present rate for nonpublished service.

34. Pacific proposes increasing the rate for its Verification Interrupt service.

35. The impact of Pacific's proposal to reduce certain Remote Call Forwarding (RCF) rates depends upon authorization of its concomitant proposal to grandfather foreign exchange service.

36. Pacific and DRA both propose consolidation of certain MTS mileage bands and new rates for these mileage bands. DRA's consolidation proposal addresses only the longer-haul bands, while Pacific's consolidates shorter-haul as well.

37. The consolidation and rate proposals of DRA, Pacific, and CBCHA/TCA all provide a contribution over cost.

38. CBCHA/TCA's MTS rate proposal is part of an overall rate design proposal which is premised on moving usage rates for those with bypass alternatives toward economic costs, without consideration of the benefits of economic pricing to captive consumers.

39. DRA's MTS rate proposal provides a very minimal impact on the rates of MTS users.

40. It is the Commission's policy to give greater weight to economic pricing, including its application to MTS rates.

41. Pacific proposes to eliminate its Optional Calling Measured Service (OCMS), changing the way the monthly allowance is deducted fer the Community Calling Plan, extending Circle Calling to 50 miles to conform to its proposed rate band consolidation, and reducing the choices under its Call Bonus Wide Area Plan from six to three.

42. General supports Pacific's proposed changes in optional toll discount plans and further proposes that Community Calling also be eliminated.

43. DRA objects to any changes in optional toll discount plans.

44. This Commission ordered Pacific and General to prepare and submit studies of subscriber usage of OCMS and ORTS in order to determine the degree of diverted usage and the degree of additionally generated usage under these plans.

45. Pacific states that the sample size of its OCMS subscriber usage study "cannot represent a valid sample."

46. Pacific proposes rate changes for 800 Service which will reduce revenue by over $11 million.

47. Pacific proposes rate changes for Outward WATS service which would increase revenue by $1.516 million.

48. The criteria Pacific applied in determining its proposed ZUM expansion are appropriate.

49. Pacific's claim of $2.13 million in implementation costs for ZUM expansion appears to be valid.

50. Pacific proposes consolidating ZUM Zones 2 and 3.

51. CBCHA/TCA propose an additional ZUM zone to cover distances between 17 and 30 miles which are presently billed at toll rates.

52. CBCHA/TCA propose elimination of detailed ZUM billing.

53. TURN proposes elimination of ZUM and adoption of an optional metropolitan flat rate service in metropolitan extended areas.

54. General, Pacific, and DRA have asked this Commission to designate a forum to hear the ZUM issues affecting customers of General, Pacific, and Continental, which General has raised in this proceeding.

55. The weight of the favorable data on metropolitan flat rate service is not strong enough to overcome the considerable likelihood that implementation of such service could jeopardize the subsidy to basic rates provided by the present discounted toll options.

34. Pacific and DRA both propose consolidation of certain MTS mileage bands and new rates for these mileage bands. DRA's consolidation proposal addresses only the longer-haul bands, while Pacific's consolidates shorter-haul as well.

35. The consolidation and rate proposals of DRA, Pacific, and CBCHA/TCA all provide a contribution over cost.

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43. Pacific states that the sample size of its OCMS subscriber usage study "cannot represent a valid sample."

56. Pacific proposes withdrawing FEX service except as to existing customers at existing locations without providing a bottoms-up cost study for FEX service.

57. Pacific has studied less costly alternatives to present FEX provisioning which are presently technically feasible.

58. Pacific's FEX cost studies are sufficient for determining rates, but do not provide a sufficient basis for the authorization of grandfathering FEX service.

59. Pacific's proposal to unbundle FEX rates is unopposed.

60. General's proposal to set FEX rates based on a private line model does not reflect the type of service FEX customers receive. Pacific's local service model does.

61. Present FEX mileage rates are close enough to cost that it is unnecessary to adopt rates different from the present mileage rates for local service which this decision retains.

62. It is reasonable for Pacific to adopt rates for FEX access to the local network which are the same as local service access rates.

63. Pacific's nonrecurring FEX rates are set far below cost.

64. Raising Pacific's nonrecurring FEX rates by more than 100% would produce unnecessary rate shock.

65. Pacific has proposed adopting the proportion of its present FEX rate which is attributable to the FEX increment as its FEX increment rate.

66. General's meet-point billing proposal does not detail how such billing will assure that customers will not be double-billed for any portion of their FEX service, how tariffs would be restructured, or how customers would be notified of the change.

67. Pacific's use of Functional Accounting in its tops-down category analysis improved Pacific's ability to produce reliable tops-down cost allocations.

68. Pacific's use of Functional Accounting made it more difficult for the parties to review and verify Pacific's reconciliations between tops-down and bottoms-up studies.

69. Pacific's cost studies comply with the requirements of D.83-04-012, the Commission's Cost Manual decision.

70. Pacific's loop study is acceptable although the overall study results do not comport with this Commission's intent in D.85-02-030.

71. The methodology of Pacific's Ready to Serve cost study is acceptable, as is the distribution of total RTS plant to private line service.

72. Pacific's private line service volume estimates showed some errors and variations between different witnesses.

73. DRA's review of Pacific's private line service volumes concluded that the volumes based on Pacific's PLHF reports are more accurate than earlier volume projections.

74. Pacific's allocation of SARTS testing costs to private line service offerings is reasonable.

75. Although Pacific's estimates for nonrecurring labor activities for private line are somewhat overstated, the intervenors' claims of overstatement are exaggerated.

76. DRA proposes a moderate downward adjustment to Pacific's private line nonrecurring labor costs.

77. The cost conclusions in the "Robin & Dackerman Report" and in Pacific's "SSX Report" have no bearing on the cost studies presented by Pacific in this proceeding.

78. Pacific proposes deaveraged private line local loop rates.

79. Pacific proposes to implement a separate alarm transport tariff in order to offer alarm transport customers lower rates.

80. TASC proposes disaggregation of secretarial line installation charges between designed and nondesigned lines.

81. A customer's decision about whether to order designed or nondesigned secretarial lines is often based on Pacific's engineering needs rather than the customer's usage.

82. TASC asks this Commission to adopt a new "move" charge for secretarial lines.

83. TASC requests that Pacific be required to submit a bulk move tariff for secretarial lines.

84. Pacific has requested that certain telegraph private line services be limited to those customers currently receiving the service.

85. Pacific's private line costs far exceed its private line revenues.

86. Pacific proposes increasing private line recurring rates in three annual increments.

87. DRA proposes a single private line recurring rate increase, which is larger than Pacific's first year increase, but much smaller overall.

88. Pacific proposes increasing most nonrecurring private line rates by 25%.

89. DRA proposes increasing most nonrecurring private line rates by 100%.

90. Changes in Pacific's private line rates affect the settlements revenue of the independent telephone companies (ITCs).

91. The pooled billing surcharge imposed by Pacific and the ITCs which concur in its access services tariffs was established in D.85-06-115 as an interim measure pending the adoption of a rate design for Pacific in this proceeding.

92. The ITCs have filed with this Commission reports of their total and separated California results of operations for 1986 at present rates and charges and adjusted to include the effects of Pacific's requested rates and charges and DRA's proposed rates and charges, as required by Order Instituting Investigation and Consolidating Proceeding (OII) I.85-03-078.

69. The methodology of Pacific's Ready to Serve cost study is acceptable, as is the distribution of total RTS plant to private line service.

70. Pacific's private line service volume estimates showed some errors and variations between different witnesses.

71. DRA's review of Pacific's private line service volumes concluded that the volumes based on Pacific's PLMF reports are more accurate than earlier volume projections.

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80. TASC asks this Commission to adopt a new "move" charge for secretarial lines.

81. TASC requests that Pacific be required to submit a bulk move tariff for secretarial lines.

93. Some ITCs which concur in Pacific's access services tariffs have filed with this Commission advice filings with proposals to replace the expiring pooled surcharge with a bill and keep surcharge calculated to generate equivalent revenue to be effective after the issuance of this rate design decision pursuant to authority granted in D.85-06-115.

94. Customers of ITCs were notified of the Pacific rate proceedings in 1985, and each ITC again notified its customers of the hearing dates and the ITC revenue effects and tariff changes precipitated by the expiration of the pooled access surcharge projected by the ITC and DRA prior to settlements effects hearings in 1986.

95. A late-filed supplemental brief on HCF issues and a motion for leave to file it were presented to the Commission after the submission date for briefs on this issue.

96. The ALJ granted the motion to late-file the supplemental brief.

97. The presently authorized HCF and the HCF proposed by the joint brief, both of which are funded from the interLATA Carrier Common Line Charge (CCLC), allow for recovery of some intraLATA operating costs. AT&T claims that the latter unlawfully discriminates against the IECs because they alone pay the CCLC.

98. The scope of rate protection under the joint HCF proposal is expanded from that of the previously adopted HCF to include other toll- and access-related changes and their effect on the ITC's settlements revenue.

99. The joint HCF proposal eliminates the prior revenue requirement review which this Commission found to be necessary in D.85-06-115.

100. The joint proposal for an HCF reduces the eligibility threshold previously established from 200% to 150% of rates charged for similar services in comparable neighboring exchanges. There is little data to support either figure.

82. Pacific has requested that certain telegraph private line services be limited to those customers currently receiving the service.

83. Pacific's private line costs far exceed its private line revenues.

84. Pacific proposes increasing private line recurring rates in three annual increments.

85. DRA proposes a single private line recurring rate increase, which is larger than Pacific's first year increase, but much smaller overall.

86. Pacific proposes increasing most nonrecurring private line rates by 25%.

87. DRA proposes increasing most nonrecurring private line rates by 100%.

88. Changes in Pacific's private line rates affect the settlements revenue of the independent telephone companies (ITCs).

89. The pooled billing surcharge imposed by Pacific and the ITCs which concur in its access services tariffs was established in D.85-06-115 as an interim measure pending the adoption of a rate design for Pacific in this proceeding.

90. The ITCs have filed with this Commission reports of their total and separated California results of operations for 1986 at present rates and charges and adjusted to include the effects of Pacific's requested rates and charges and DRA's proposed rates and charges, as required by Order Instituting Investigation and Consolidating Proceeding (OII) I.85-03-078.

91. Some ITCs which concur in Pacific's access services tariffs have filed with this Commission advice filings with proposals to replace the expiring pooled surcharge with a bill and keep surcharge calculated to generate equivalent revenue to be effective after the issuance of this rate design decision pursuant to authority granted in D.85-06-115.

101. Prior to divestiture this Commission authorized intrastate toll surcharges for Citizens, Sierra, and Cal-Ore. The question of whether these surcharges should continue is pending before this Commission in C.85-07-062. AT&T claims that the interLATA portion of these surcharges should be removed in the present proceeding.

102. AT&T objects to the continuation of the bill and keep access surcharge as an alternative to participation in the intrastate HCF for concurring ITCs as authorized by D.85-06-115.

103. General requests to be included in the flow-through provisions of the joint proposal's HCF.

104. General and West Coast do not concur in Pacific's Access Services Tariff Schedule 175-T.

105. Eligibility to participate in the HCF is contingent on concurrence in Pacific's Access Services Tariff Schedule 175-T.

106. The ITCs' request to combine various Commission ordered separations and settlements changes in one annual advice letter filing is advantageous to both the ITCs and their customers.

107. Ordering Paragraph 25 of D.87-08-048 directs that the $11 million access services rate reduction authorized by that decision is to be implemented by this final rate design order.

108. D.87-08-048 states that the $11 million excess revenue is generated from all special access services except DDS and HiCap.

109. The settlements effect on Pacific of the $11 million shift in revenue requirement out of access services authorized by D.87-08-048 will be $10,293,000.

110. Unless an adjustment is authorized ITCs which concur in Pacific's access rates will experience a reduction in settlements revenues as a consequence of the $11 million shift in revenue this Commission authorized for Pacific in D.87-08-048.

111. When Pacific's $11 million revenue shift takes effect, AT&T's access expenses will be reduced.

92. Customers of ITCs were notified of the Pacific rate proceedings in 1985, and each ITC again notified its customers of the hearing dates and the ITC revenue effects and tariff changes precipitated by the expiration of the pooled access surcharge projected by the ITC and DRA prior to settlements effects hearings in 1986.

93. A late-filed supplemental brief on HCF issues and a motion for leave to file it were presented to the Commission after the submission date for briefs on this issue.

94. The ALJ granted the motion to late-file the supplemental brief.

95. The presently authorized HCF and the HCF proposed by the joint brief, both of which are funded from the interLATA Carrier Common Line Charge (CCLC), allow for recovery of some intraLATA operating costs. AT&T claims that the latter unlawfully discriminates against the IECs because they alone pay the CCLC.

96. The scope of rate protection under the joint HCF proposal is expanded from that of the previously adopted HCF to include other toll- and access-related changes and their effect on the ITC's settlements revenue.

97. The joint HCF proposal eliminates the prior revenue requirement review which this Commission found to be necessary in D.85-06-115.

98. The joint proposal for an HCF reduces the eligibility threshold previously established from 200% to 150% of rates charged for similar services in comparable neighboring exchanges. There is little data to support either figure.

99. Prior to divestiture this Commission authorized intrastate toll surcharges for Citizens, Sierra, and Cal-Ore. The question of whether these surcharges should continue is pending before this Commission in C.85-07-062. AT&T claims that the interLATA portion of these surcharges should be removed in the present proceeding.

112. D.87-12-067 as modified by D.88-03-064 authorizes small metropolitan local exchange companies the option of accruing the settlements effects resulting from the intraLATA SPF to SLU phase-down authorized beginning on January 1, 1988 in an interest bearing memorandum account or implementing a surcharge or surcredit. Sixteen ITCs elected to accrue the amounts in an interest bearing memorandum account.

113. The settlements effect in the memorandum account, when combined with the settlements effect resulting from the rate design authorized herein, produces a revenue shortfall for some ITCs and a revenue overcollection for others.

114. Pacific is meeting the overall installation and maintenance requirements for the provision of private line alarm service set out in GO 152.

115. Installation and maintenance of private line alarm service still requires the regular monitoring of a committee of utility, industry, and Commission representatives.

116. A.85-01-034 has an ex parte rule put into place by an ALJ Ruling dated July 1, 1985 while I.87-11-033 does not.

Conclusions of Law

1. There is no basis in the record for eliminating the flat rate service option; therefore, Pacific's 130 Call Allowance Plan should not be adopted.

2. Since local residence rates are set residually the proposed new access and usage rate elements serve no purpose and may create confusion. Their implementation should be denied.

3. Incremental cost data is necessary to a more accurate determination of whether measured rates for basic exchange service promote or hinder economic efficiency.

4. Lifeline-eligible customers will be better served if they receive the same plan options available to other ratepayers, but at a discounted rate. The Lifeline rates Pacific proposes comply with statutory requirements. Therefore, Pacific's proposal to add a

flat rate Lifeline option and to reduce the charge for measured rate calls beyond the 60-call allowance should be granted.

5. The purpose of the Universal Telephone Service Fund is to make telephone companies whole for the provision of discounted service to low-income individuals or families.

6. Pacific's proposal to give residence customers a 90-day period to choose a different basic service without being subject to a change fee is reasonable and should be granted.

7. The evidence on this record does not warrant moving to strictly cost-based or market-based pricing of local residence service at this time. However, there should be some adjustment to local residence service to reflect diminishing subsidy sources.

8. The revenue requirement increase for local residence and business service should be set residually.

9. The revenue requirement increase for local residence service should be spread across all recurring local rates, including service connection rates but excluding rates for minutes of use or message units, on a uniform basis, rounded for ease of administration.

10. Pacific's proposed increases in measured business line rates should not be adopted. Rates other than trunk rates should be increased by the same percentage as authorized for residence rates.

11. Pacific's alternative rate for the initial minute of local business usage is not justified and should not be adopted.

12. It is reasonable to raise PBX trunk rates to make them more competitive with Centrex rates.

13. Because of the ambiguity inherent in determining when a PBX trunk, rather than an ordinary business line, is needed, it is not reasonable to raise PBX trunk rates by over 94% as Pacific initially proposed. Pacific's reduced alternative proposal is a reasonable compromise if Pacific first develops a set of criteria

describing to potential PBX customers when a designed circuit is required.

14. Pacific's Centrex revenue requirement should not be decreased by the large amount proposed by Pacific.

15. Pacific's Centrex rate design should be changed to incorporate rates for Pacific's new Centrex services.

16. A slight decrease in Pacific's Centrex revenue requirement will allow Centrex to be reasonably competitive with PBX service in conjunction with DID.

17. Keeping the Centrex tie line rate at its present level rather than reducing it as Pacific proposes is a reasonable means of avoiding a large overall revenue decrease from Centrex services.

18. It is reasonable for Pacific to adopt a disaggregated rate design for DID which has a separate trunk sensitive rate element.

19. Pacific's DID station number block charge should be the same for each block of 100 numbers.

20. TASC's proposal for DID station number block rates would result in a charge of $45 for each 100 DID station numbers.

21. Pacific's proposed rate level for DID station number blocks should be denied and TASC's should be adopted.

22. Pacific should address the reasonableness of retaining its DID Basic Termination Charge in its next general rate proceeding.

23. The evidence upon which TURN relies for its public coin rate proposal was considered when this Commission adopted the present coin rate in D.84-06-111. There is no basis for reexamining that evidence now.

24. Semi-public coin service rates should cover costs, but setting them above costs may discourage subscription to the detriment of users for whom this service provides their only ready access to the local network and a primary means of contacting those users.

25. Pacific's proposal for a semi-public coin service deposit requirement is too broad and open-ended. It should be denied.

26. Pacific's access and usage rates for COPT service should continue to reflect Pacific's measured business rates.

27. Pacific's nonrecurring rates for COPT installation, repair, and conversion service should be increased by the same percentage adopted in this decision for similar business and residence services.

28. Pacific's proposed DAL service should be adopted, but the rates it proposes for DAL and for nonpublished service are not appropriate.

29. The evidence does not support an increase in Verification Interrupt rate.

30. The disposition of foreign exchange service rates in this opinion causes Pacific's projected revenue increase for RCF to be unrealistic.

31. Pacific's MTS rate band consolidation plan, which also applies to ZUM zones, obscures the transitional rate zone between local service rates and toll rates.

32. Pacific's MTS mileage zone consolidation and rate plan increases short-haul toll disproportionately to long-haul toll without justification. It should not be adopted.

33. CBCHA/TCA's MTS rate design which bestows benefit on those customers with bypass alternatives while ignoring the captive residence ratepayers should not be adopted.

34. DRA's MTS consolidation plan does not disadvantage short-haul customers, residential customers, or potential future competing intraLATA long distance carriers, and will promote increased usage.

35. DRA's MTS mileage band rate proposal should be adopted, except that the rates for additional minutes of use should be reduced by one cent for the two shortest MTS rate bands.

36. Pacific has not informed this Commission about usage diversion and newly generated usage attributable to OCMS in its usage study or elsewhere.

37. Pacific has not studied the impact of its Community Plan proposal on subscribers who now exhaust their call allowance each month.

38. It is inappropriate, when designing rates to reflect a decrease, to change the Community Plan so that it provides less to the subscriber.

39. Pacific's proposal to reduce the choices for its Call Bonus Wide Area Plan from six to three, to reduce rates, and to reduce the monthly allowance is not sufficiently supported by the evidence.

40. Pacific's proposal to extend its Circle Calling Plan from 40 to 50 miles is mooted by the MTS mileage band configuration adopted in this decision.

41. Pacific's proposal for the Call Bonus Wide Area Plan is not adequately supported by the evidence.

42. Pacific's evidence is inadequate to support the rate changes it proposes for 800 Service and Outward WATS.

43. The ZUM expansion Pacific proposes into the San Francisco-East Bay Extended Area should be granted.

44. Pacific's ZUM expansion implementation costs should be recognized in its rates.

45. Consolidation of ZUM Zones 2 and 3 would tend to obscure the Commission policy to position ZUM rates between local service rates and toll rates to reflect costs which are lower than those for comparable MTS calls and to serve the needs of local communities of interest.

46. Expansion of ZUM to 30 miles would require unreasonable rate increases to other service offerings.

47. ZUM rates should continue to be set to reflect Commission policy, including consideration of economic pricing.

48. Moderate reductions in ZUM rates for additional minutes of use will provide the ZUM rate reduction which both CBCHA/TCA and Pacific favor without disadvantaging the small consumer or obscuring the distinction between ZUM and MTS service.

49. ZUM customers should continue to receive detailed ZUM bills.

50. The benefits of TURN's metropolitan flat rate proposal are insufficient to support its adoption.

51. The record does not support Pacific's proposal to grandfather FEX service.

52. That part of Pacific's unbundled FEX rate design which sets a separate FEX increment should be granted; however, access and usage rates should remain as one rate.

53. Pacific's nonrecurring FEX rates should be increased by 100%.

54. Pacific's proposal to set rates for the FEX increment to reflect that portion of the present rate which is attributable to the FEX increment should be adopted.

55. General's meet-point billing proposal cannot be adopted unless further implementation detail is provided.

56. DRA's difficulty in assessing Pacific's use of Functional Accounting in its future tops-down category analyses is alleviated by the conversion mechanism agreed to in I.87-02-023.

57. The overall reliability of Pacific's loop study is reduced by its failure to allow a meaningful tops-down to bottoms-up comparison.

58. The inconsistency in Pacific's service volume projections does not seriously affect its recurring cost study conclusions.

59. The service volumes relied upon by DRA were superior to those relied upon by Pacific in its private line cost studies.

60. DRA's proposed adjustment to Pacific's private line nonrecurring costs is reasonable.

61. The evidence does not support deaveraged private line local loop rates.

62. The evidence does not support the reasonableness of implementing a separate alarm transport tariff.

63. It is not reasonable to disaggregate the secretarial line installation charge.

64. TASC's proposal for a "move" charge for secretarial line service is inconsistent with Pacific's cost studies.

65. There in not sufficient evidence in this record to warrant ordering Pacific to submit a bulk move secretarial line tariff.

66. Pacific's proposal to limit certain telegraph private line services is reasonable.

67. Pacific's private line revenues should be increased.

68. Pacific's proposal for three annual incremental recurring private line rate increases is excessive in light of the possibilities for error in its cost studies.

69. DRA's proposed recurring private line rate increases are reasonable.

70. Pacific's proposed nonrecurring private line rate increases are not sufficient in light of the gap between costs and revenues.

71. DRA's proposed nonrecurring private line rate increases are reasonable.

72. The ITCs should be authorized to offset settlements revenue losses due to the changes adopted in this Decision.

73. Reports filed by ITCs pursuant to I.85-03-078 and advice filings made by ITCs pursuant to the authority granted in D.85-06-115 regarding revenue changes precipitated by the expiration of the pooled access surcharge do not constitute applications to increase a rate or charge as that phrase is used in Public Utilities Code § 454.

74. The notices given by ITCs to their customers regarding possible tariff changes resulting from the expiration of the pooled access surcharge were timely, adequate, and proper.

75. The accompanying motion stated good cause for filing the late-filed supplemental brief on HCF issues.

76. The ALJ's ruling granting the motion to late-file the supplemental brief was proper.

77. Allowing regulated IECs to flow through the effects of changes in the HCF increment on the CCLC access charge eliminates any unfair disadvantage to the IECs.

78. The scope of rate protection in the joint proposal's HCF is an appropriate means of protecting ITC settlements revenues, and ultimately protecting the continued availability of basic telephone service to ITC customers.

79. The provisions of the joint proposal for an HCF which allow the ITCs until December 31, 1989 to file for rate review without loss of HCF funding, and then provide for annual funding reductions, will allow an orderly progression of rate case processing while preventing against rate shock and protecting HCF funders and ratepayers generally from abuse.

80. The strong support expressed for the move to a 150% eligibility criterion balanced against the scanty data to support either that criterion or the previously adopted 200% criterion makes it reasonable to adopt the 150% figure at this time.

81. The provisions of the jointly proposed HCF are reasonable and should be adopted.

82. This is not the proper forum to determine the merits of continuing the previously authorized intrastate toll surcharges of Citizens, Sierra, and Cal-Ore.

83. The option of a bill and keep access surcharge as an alternative to participation in the intrastate HCF for ITCs concurring in Pacific's access services tariffs should be eliminated.

62. The evidence does not support the reasonableness of implementing a separate alarm transport tariff.

63. It is not reasonable to disaggregate the secretarial line installation charge.

64. TASC's proposal for a "move" charge for secretarial line service is inconsistent with Pacific's cost studies.

65. There in not sufficient evidence in this record to warrant ordering Pacific to submit a bulk move secretarial line tariff.

66. Pacific's proposal to limit certain telegraph private line services is reasonable.

67. Pacific's private line revenues should be increased.

68. Pacific's proposal for three annual incremental recurring private line rate increases is excessive in light of the possibilities for error in its cost studies.

69. DRA's proposed recurring private line rate increases are reasonable.

70. Pacific's proposed nonrecurring private line rate increases are not sufficient in light of the gap between costs and revenues.

71. DRA's proposed nonrecurring private line rate increases are reasonable.

72. The ITCs should be authorized to offset settlements revenue losses due to the changes adopted in this Decision.

73. Reports filed by ITCs pursuant to I.85-03-078 and advice filings made by ITCs pursuant to the authority granted in D.85-06-115 regarding revenue changes precipitated by the expiration of the pooled access surcharge do not constitute applications to increase a rate or charge as that phrase is used in Public Utilities Code § 454.

74. The notices given by ITCs to their customers regarding possible tariff changes resulting from the expiration of the pooled access surcharge were timely, adequate, and proper.

84. General and West Coast are ineligible for HCF funds.

85. The flow-through provisions of the new HCF are only reasonably applicable where an ITC is found to be eligible for HCF funds. Since General will not be eligible for these funds, it should not be eligible for the flow-through of rate changes set out in the new HCF scheme.

86. The special access revenue requirement reduction of $11 million should be spread on a uniform percentage basis among all special access services excluding DDS and HiCap.

87. Pursuant to policy set forth in D.85-06-115, each ITC concurring in Pacific's access services tariffs is entitled to increase its rates for nonaccess services by a dollar amount equivalent to the settlement impact on it from the $11 million access revenue shift which this Commission authorized for Pacific in D.87-08-048. The amount of the settlement impact on each concurring ITC is set forth in Table 2 to this decision.

88. Pursuant to policy set forth in D.85-03-056, as modified by D.85-06-113, AT&T must pass on to its customers the expense reduction accruing to it from reductions in Pacific's access charges.

89. To recognize the effect of this Commission keeping surcharges in place in this proceeding, the ITCs which implemented memorandum accounts pursuant to Ordering Paragraph 15A of D.87-12-067 as modified, should refund the settlement gains in those accounts.

90. Pacific is in compliance with the service quality criteria of GO 152 for the installation and maintenance of private line alarm service.

91. The GO 152 requirements for regular monitoring by a committee of utility, industry, and Commission representatives should not be modified at the present time.

92. Pacific's discussion of the GO 152 issue in its reply brief is not improper.

93. The Supplementary rate design phase of A.85-01-034 should be procedurally consistent with I.87-11-033 and for this reason the requirements of the ALJ Ruling dated July 1, 1985 should be extinguished.

O R D E R

IT IS ORDERED that:

1. In the supplementary rate design proceeding which will follow Phase II hearings in I.87-11-033, showings of the parties, including the ITCs, shall be based on 1988 and 1989 projected billing base information including the number of access lines by service type, customer volume by service type, and billing volume by operation service category--e.g., interLATA access, intraLATA toll, toll private line, ZUM, and local exchange.

2. Pacific Bell's (Pacific) proposal for a 130 Call Allowance Plan is denied.

3. Pacific shall provide evidence of its incremental costs for basic exchange service and for calls within its ZUM areas in the supplementary rate design proceeding which will follow Phase II hearings in I.87-11-033.

4. Pacific's proposal to create separate rate elements for access and usage for local residence services is denied.

5. Pacific shall continue to offer flat rate Lifeline service as an option for customers eligible for this program. Rates shall be one-half the regular rates less a credit of $.75 for telephone set rental, and less $.25 for inside wire maintenance.

6. Pacific's proposal to charge $.08 per call for all measured rate Lifeline calls after the 60-call allowance is granted.

7. Pacific may continue to seek reimbursement for all Lifeline discounts from the Universal Telephone Service Fund.

8. Pacific's specific proposals for test year 1986 rate increases for recurring local residence rates, and for service connection and installation and service, are denied. However, Pacific is authorized to increase the tariff rates for these services as described in the foregoing opinion.

9. Pacific shall notify its residential customers that they may have up to 90 days from the implementation date of Pacific's new rates to choose a different service without incurring any fee for the change.

10. Pacific's proposed increases in measured business line rates are denied. However, Pacific is authorized to increase the tariff rates for all recurring local business rates, including installation and service, but not including trunk rates or minutes of use or message unit charges as described in the foregoing opinion.

11. Pacific's proposed alternative rate for the initial minute of local business usage of $.047 and its assignment of 4.7 message units for the initial minute of local measured service are denied.

12. Pacific shall make an advice letter filing with this Commission pursuant to General Order (GO) 96-A to amend the appropriate tariff schedules to describe design parameters which require the use of a designed circuit from the central office serving a PBX service.

13. Pacific's proposed rates of $12.25 for measured business trunk access and $34.25 for flat rate business trunk access are granted upon adoption by this Commission of Pacific's PBX design parameter tariff.

14. Upon adoption by this Commission by Resolution of Pacific's PBX design parameter tariff, and implementation of the new PBX tariffs authorized in this order, Pacific shall provide each customer seeking PBX service, a copy of the design parameter tariff.

requirements of the ALJ Ruling dated July 1, 1985 should be extinguished.

ORDER

IT IS ORDERED that:

1. Pinnacles Telephone Company's late-filed comments to the ALJ's Proposed Decision are accepted.

2. In the supplementary rate design proceeding which will follow Phase I hearings in I.87-11-033, showings of the parties, including the ITCs, shall be based on 1988 and 1989 projected billing base information including the number of access lines by service type, customer volume by service type, and billing volume by operation service category--e.g., interLATA access, intraLATA toll, toll private line, ZUM, and local exchange.

3. Pacific Bell's (Pacific) proposal for a 130 Call Allowance Plan is denied.

4. Pacific shall provide evidence of its incremental costs for basic exchange service and for calls within its ZUM areas in the supplementary rate design proceeding which will follow Phase I hearings in I.87-11-033.

5. Pacific's proposal to create separate rate elements for access and usage for local residence services is denied.

6. Pacific shall continue to offer flat rate Lifeline service as an option for customers eligible for this program. Rates shall be one-half the regular rates less a credit of $.75 for telephone set rental, and less $.25 for inside wire maintenance.

7. Pacific's proposal to charge $.08 per call for all measured rate Lifeline calls after the 60-call allowance is granted.

8. Pacific may continue to seek reimbursement for all Lifeline discounts from the Universal Telephone Service Fund.

15. Pacific's proposed Centrex rate design is granted except that the tie line monthly rate element shall remain at its present level and the Exchange Access Trunking charge shall be set at one-tenth of the adopted measured and flat business trunk rate, rounded to the nearest $.05.

16. Pacific's proposal for a separate DID trunk sensitive rate element is granted as proposed.

17. Pacific's DID station number block charge proposal is denied. The alternative proposal of TASC, which sets the rate at $45 for each 100 DID station numbers is adopted.

18. Pacific shall address the reasonableness of continuing its DID Basic Termination Charge, including submission of a cost study of the costs this charge is designed to cover, in its next general rate proceeding.

19. TURN's proposal to reduce coin telephone rates is denied.

20. Pacific is authorized to increase its access rates for semi-public coin service by 45%.

21. Pacific is authorized to adopt its requested increase in service charge for semi-public coin service.

22. Pacific's proposal to require, at its discretion, a deposit for certain semi-public coin service installations is denied.

23. Pacific is authorized to set its COPT access line rates to reflect the uniform percentage increase authorized for business access rates in this decision.

24. Pacific is authorized to increase its rates for COPT installation, repair, and conversion by the same percentage authorized in this decision for business and residence installation and repair services.

25. Pacific is authorized to implement its proposed new Directory Assistance Listing service at the monthly rate of $.15.

26. Pacific's proposal to increase its rate for nonpublished service is denied.

9. Pacific's specific proposals for test year 1986 rate increases for recurring local residence rates, and for service connection and installation and service, are denied. However, Pacific is authorized to increase the tariff rates for these services as described in the foregoing opinion.

10. Pacific's proposed increases in measured business line rates are denied. However, Pacific is authorized to increase the tariff rates for all recurring local business rates, including installation and service, but not including trunk rates or minutes of use or message unit charges as described in the foregoing opinion.

11. Pacific's proposed alternative rate for the initial minute of local business usage of $.047 and its assignment of 4.7 message units for the initial minute of local measured service are denied.

12. Pacific shall make an advice letter filing with this Commission pursuant to General Order (GO) 96-A to amend the appropriate tariff schedules to describe design parameters which require the use of a designed circuit from the central office serving a PBX service.

13. Pacific's proposed rates of $12.25 for measured business trunk access and $34.25 for flat rate business trunk access are granted upon adoption by this Commission of Pacific's PBX design parameter tariff.

14. Upon adoption by this Commission by Resolution of Pacific's PBX design parameter tariff, and implementation of the new PBX tariffs authorized in this order, Pacific shall provide each customer seeking PBX service, a copy of the design parameter tariff.

15. Pacific's proposed Centrex rate design is granted except that the tie line monthly rate element shall remain at its present level and the Exchange Access Trunking charge shall be set at one-

27. Pacific shall provide this Commission with cost and revenue information for Touchtone service for consideration in the supplementary rate design proceedings.

28. Pacific's proposal to increase its Verification Interrupt rate is denied.

29. Pacific's proposal to reduce certain Remote Call Forwarding rates is denied.

30. Pacific's proposal for MTS rate band consolidation and pricing is denied.

31. CBCHA/TCA's proposal for MTS rate band pricing is denied.

32. DRA's proposal for MTS mileage zone consolidation is granted.

33. DRA's proposal for MTS rate band rates, as modified by this decision, is granted.

34. Pacific's proposal to eliminate OCMS is denied.

35. Pacific's proposal to change the means of deducting the monthly allowance under the Community Plan is denied.

36. General's proposal to eliminate the Community Plan is denied.

37. Pacific's proposal to reduce the choices for its Call Bonus Wide Area Plan from six to three, to reduce rates, and to reduce the monthly allowance is denied.

38. Pacific's proposal to amend its rates for 800 Service is denied.

39. Pacific's proposal to amend its rates for Outward WATS service is denied.

40. Pacific's ZUM expansion proposal in Exhibit 285 to add 12 exchanges to the San Francisco-East Bay Extended Area is granted. Within 90 days of the effective date of this order Pacific shall make an advice letter filing under the terms of GO 96-A to amend the appropriate tariffs for implementation of the ZUM expansion described in this decision.

tenth of the adopted measured and flat business trunk rate, rounded to the nearest $.05.

16. Pacific's proposal for a separate DID trunk sensitive rate element is granted as proposed.

17. Pacific's DID station number block charge proposal is denied. The alternative proposal of TASC, which sets the rate at $45 for each 100 DID station numbers is adopted.

18. Pacific shall address the reasonableness of continuing its DID Basic Termination Charge, including submission of a cost study of the costs this charge is designed to cover, in its next general rate proceeding.

19. TURN's proposal to reduce coin telephone rates is denied.

20. Pacific is authorized to increase its access rates for semi-public coin service by 45%.

21. Pacific is authorized to adopt its requested increase in service charge for semi-public coin service.

22. Pacific's proposal to require, at its discretion, a deposit for certain semi-public coin service installations is denied.

23. Pacific is authorized to set its COPT access line rates to reflect the uniform percentage increase authorized for business access rates in this decision.

24. Pacific is authorized to increase its rates for COPT installation, repair, and conversion by the same percentage authorized in this decision for business and residence installation and repair services.

25. Pacific is authorized to implement its proposed new Directory Assistance Listing service at the monthly rate of $.15.

26. Pacific's proposal to increase its rate for nonpublished service is denied.

27. Pacific shall provide this Commission with cost and revenue information for Touchtone service for consideration in the supplementary rate design proceedings.

41. Within 180 days of the effective date of this order Pacific, General, and Continental shall submit in I.87-02-025, in a phase separate from the current rate proceeding with which I.87-02-025 is consolidated, testimony and exhibits which address the feasibility of implementing ZUM service over the additional routes set forth in Exhibit 384, the revenue requirement in terms of added plant and additional expenses associated with the expansion of ZUM over these additional routes, and the customer billing effects and settlements effects associated with implementing ZUM over these additional routes. These parties may also submit alternative proposals to that offered by General. Such alternative proposals shall also include testimony and exhibits addressing feasibility, revenue requirement, customer billing effects, and settlements effects. Further, prior to the submission of the testimony and exhibits Pacific, General, and Continental shall provide written notice to each of their customers who would be affected by the implementation of ZUM over the additional routes.

42. Pacific's proposal to consolidate ZUM Zones 2 and 3 is denied.

43. Pacific's proposal to differentiate between business and residence ZUM rates is denied.

44. CBCHA/TCA's proposal to adopt Pacific's consolidated ZUM rate zones and to add a new Zone 3 for distances from 17 to 20 miles is denied.

45. Pacific's specific proposal to decrease ZUM rates is denied, however, rates for ZUM Zones 2 and 3 "additional minutes of use" shall be reduced by $.01.

46. TURN's request that Pacific be ordered to implement optional flat rate metropolitan service is denied.

47. Pacific's proposal to grandfather FEX service is denied.

48. Within 60 days of the effective date of this order Pacific shall file an advice letter, with service upon all parties

to this proceeding, which revises the appropriate tariffs to implement the mirroring of the Centrex exchange access trunking charges when providing FEX service to Centrex customers as described in the foregoing opinion. The advice letter shall also contain the estimated 1986 annual billing and revenue effects associated with the implementation of such tariff revisions, and revisions to the customer billing surcharge to reflect the annual revenue effect of implementing such tariff revisions for Centrex service. The advice letter filing shall be subject to Commission authorization by resolution in order to take effect.

49. Pacific's proposal to unbundle recurring FEX rates is granted in a modified form. Pacific is authorized to set a rate for FEX access and usage and a separate rate for the FEX increment consistent with the foregoing opinion.

50. Pacific, General, and all other LECs which provide intercompany FEX service shall jointly consider a method for offering meet-point billing on a bill and keep basis for FEX service. LECs wishing to provide such service shall, within 120 days of the issuance of this order, file separate or joint studies with the CACD for review and approval setting forth the results of their study and their proposed tariff changes which provide for bill and keep billing of FEX service and which assure that FEX subscribers are not double-billed for any portion of their FEX service. The joint study shall address the type and methods of customer notice to be used as well as the conversion of each LEC's FEX tariff rate structure to a structure which will facilitate the implementation of the meet-point billing concept for FEX services. The LECs may thereafter file the approved plan with this Commission as an advice letter filing pursuant to GO 96-A. Such advice letter filings shall be served on all parties to this proceeding and shall be subject to authorization by Commission resolution before becoming effective. In those instances where the implementation of the meet-point billing concept for FEX services will result in a

change in the annual revenues for a utility, the advice letter filing shall also include a revision to the utility's customer billing surcharge applicable to intraLATA services to reflect such a change in annual revenues.

51. Pacific's proposal for deaveraged private line local loop rates is denied.

52. Pacific's proposal for a separate alarm transport tariff is denied.

53. TASC's proposal to disaggregate the secretarial line installation charge is denied.

54. TASC's proposal for a "move" charge for secretarial line service is denied.

55. TASC's request that this Commission order Pacific to submit a proposal for a bulk move tariff is denied.

56. TASC's request that this Commission order Pacific to permit outside parties to place concentrators in Pacific's central offices is denied.

57. Pacific's proposal to limit certain telegraph private line services to current customers is granted. Pacific's tariffs for these services shall be consistent with the foregoing opinion as set forth in Appendix A.

58. Pacific's private line recurring rate proposal is denied.

59. DRA's private line recurring rate proposal is granted to the extent described in the foregoing opinion and set forth in the attached Appendix A.

60. Pacific's private line nonrecurring charge proposal is denied.

61. DRA's private line nonrecurring charge proposal is granted as described in the foregoing opinion and set forth in the attached Appendix A.

62. The motion of Carlos E. Benemann that we find untimely and improper the notice to the customers of independent telephone companies (ITCs) regarding the portion of these proceedings which

addressed changes in ITC rate design necessitated by the impact of Pacific's eliminating its pooled access surcharge is denied.

63. The ALJ's ruling granting the motion to late-file a supplemental brief on intrastate High Cost Fund (HCF) issues is upheld.

64. The proposed modifications to the intrastate HCF mechanism adopted in D.85-06-115, as described in the foregoing opinion, are hereby adopted and shall be implemented in the manner described in Appendix B of this decision.

65. Until such time as an ITC's rates have been reviewed in a GO 96-A rate review or a general rate application proceeding, changes in rates as authorized by the intrastate HCF mechanism set forth in Appendix B shall be made by a uniform percentage increase or decrease applied to all nonaccess rates, except as specifically limited by Paragraph 74, below.

66. Pacific Bell and ITCs implementing rate changes pursuant to this order shall notify their customers of such changes at least 30 days prior to the effective date of such changes.

67. The request of General to be eligible for the flow-through provisions of the intrastate HCF as described in Appendix B is denied.

68. ITCs which concur in Pacific's access services tariffs may not, after the effective date of this order, choose to adopt a bill and keep access surcharge as an alternative to participation in the intrastate HCF.

69. Any interexchange carrier which is subject to rate base regulation by this Commission may make appropriate advice letter filings under GO 96-A to flow through to its rates the effect of changes in the HCF fund increment on the CCLC access charge, except in cases where a change is of minimal effect. The annual HCF changes on January 1 shall be netted against contemporaneous access charge reductions reflecting SPF to SLU separations changes.

51. Pacific's proposal for deaveraged private line local loop rates is denied.

52. Pacific's proposal for a separate alarm transport tariff is denied.

53. TASC's proposal to disaggregate the secretarial line installation charge is denied.

54. TASC's proposal for a "move" charge for secretarial line service is denied.

55. TASC's request that this Commission order Pacific to submit a proposal for a bulk move tariff is denied.

56. TASC's request that this Commission order Pacific to permit outside parties to place concentrators in Pacific's central offices is denied.

57. Pacific's proposal to limit certain telegraph private line services to current customers is granted. Pacific's tariffs for these services shall be consistent with the foregoing opinion as set forth in Appendix A.

58. Pacific's private line recurring rate proposal is denied.

59. DRA's private line recurring rate proposal is granted to the extent described in the foregoing opinion and set forth in the attached Appendix A.

60. Pacific's private line nonrecurring charge proposal is denied.

61. DRA's private line nonrecurring charge proposal is granted as described in the foregoing opinion and set forth in the attached Appendix A.

62. The motion of Carlos E. Benemann that we find untimely and improper the notice to the customers of independent telephone companies (ITCs) regarding the portion of these proceedings which addressed changes in ITC rate design necessitated by the impact of Pacific's eliminating its pooled access surcharge is denied.

70. The ITCs which concur in Pacific's access rates may combine in a single annual advice letter filing the net settlements effect of changes in the HCF fund increment described in the above ordering paragraph with other Commission ordered settlements and separations changes.

71. Within 30 days of the effective date of this order each of the following ITCs: Calaveras, Cal-Oregon, Ducor, Foresthill, Happy Valley, Pinnacles, Siskiyou, and Toulumne, shall make an advice letter filing to adjust its tariff schedules to implement a bill and keep surcredit on intraLATA services to reflect the settlements gains of today's rate design decision as shown in Appendix C. In establishing the bill and keep surcredit each ITC shall use the 1986 intraLATA billing base set forth in Appendix E. The advice letter filing with revised tariff schedules shall conform with the provisions of GO 96-A. The revised tariff schedules shall become effective 15 days after the advice letter filing and shall apply to services rendered on and after their effective date.

72. Hornitos Telephone Company shall accrue its settlements gains as reflected in Appendix C, in a memorandum account from the effective date of this decision with interest accrued at a rate equal to 1/12th the interest rate on 3-month commercial paper for the previous month, as published in the Federal Reserve Statistical Release, G.13, or its successor, until further order of this Commission.

73. Within 30 days of the effective date of this order each ITC except Hornitos Telephone Company shall eliminate its interest bearing memorandum account by implementing a bill and keep surcharge or surcredit, spread over one year, on intraLATA services by advice letter filing in conformance with GO 96-A. In establishing the bill and keep surcharge or surcredit the ITC shall use the 1986 intraLATA billing base reflected in Appendix E. The revised tariff schedules shall become effective 15 days after the

63. The ALJ's ruling granting the motion to late-file a supplemental brief on intrastate High Cost Fund (HCF) issues is upheld.

64. The proposed modifications to the intrastate HCF mechanism adopted in D.85-06-115, as described in the foregoing opinion, are hereby adopted and shall be implemented in the manner described in Appendix B of this decision.

65. Until such time as an ITC's rates have been reviewed in a GO 96-A rate review or a general rate application proceeding, changes in rates as authorized by the intrastate HCF mechanism set forth in Appendix B shall be made by a uniform percentage increase or decrease applied to all nonaccess rates, except as specifically limited elsewhere in these orders.

66. Pacific Bell and ITCs implementing rate and offering changes pursuant to this order shall notify their customers of such changes at least 15 days prior to the effective date of such changes.

67. The request of General to be eligible for the flow-through provisions of the intrastate HCF as described in Appendix B is denied.

68. ITCs which are eligible to participate in the intrastate HCF may not, after the effective date of this order, choose to adopt a bill and keep access surcharge as an alternative to participation in the intrastate HCF.

69. Any interexchange carrier which is subject to rate base regulation by this Commission may make appropriate advice letter filings under GO 96-A to flow through to its rates the effect of changes in the HCF fund increment on the CCLC access charge, except in cases where a change is of minimal effect. The annual HCF changes on January 1 shall be netted against contemporaneous access charge reductions reflecting SPF to SLU separations changes.

70. The ITCs which participate in the intrastate HCF may combine in a single annual advice letter filing the net settlements

advice letter filing and shall apply to services rendered on or after the effective date of the tariff revisions.

74. Within 30 days of the effective date of this order Pacific shall make an advice letter filing under the terms of GO 96-A to amend its Access Services Tariff, Schedule Cal. P.U.C. 175-T, to reduce its billings from special access services on a uniform percentage basis, excluding DDS and HiCap, by $10.615 million in a manner consistent with the foregoing opinion. The effective date of the revised tariff sheets shall be 15 days from the date of filing. The revised tariff schedules shall apply to services rendered on and after the effective date of the revised schedules.

75. Within 14 days after Pacific makes its advice letter filing to reduce its special access rates in the manner described in this decision AT&T shall file an advice letter with this Commission under the terms of GO 96-A which proposes accumulating the reduced access charge expense resulting from this decision in a memorandum account, with interest, commencing on the effective date of the Pacific tariff revision.

76. Western Burglar and Fire Alarm Association's motion to strike the discussion in Pacific's reply brief of GO 152 regarding the installation and maintenance of private line alarm service is denied.

77. Within 30 days after the effective date of this order Pacific shall make an advice letter filing under the terms of GO 96-A to amend its tariffs to reflect the rates, charges, and conditions as set forth in Appendix A. The effective date of the revised tariff sheets shall be 15 days after the date of filing. The revised tariff schedules shall apply to service rendered on and after the effective date of the revised schedules.

78. Within 30 days of the effective date of this order each Independent Telephone Company, except for General Telephone Company of California and West Coast Telephone Company, is authorized to

effect of changes in the HCF fund increment described in the above ordering paragraph with other Commission ordered settlements and separations changes.

71. Within 30 days after the effective date of this order each of the following ITCs: Calaveras, Cal-Oregon, Ducor, Foresthill, Happy Valley, Pinnacles, Siskiyou, and Toulumne, shall make an advice letter filing to adjust its tariff schedules to implement a bill and keep surcredit on intraLATA services to reflect the settlements gains of today's rate design decision as shown in Appendix C. In establishing the bill and keep surcredit each ITC shall use the 1986 intraLATA billing base set forth in Appendix E. The advice letter filing with revised tariff schedules shall conform with the provisions of GO 96-A. The revised tariff schedules shall become effective 60 days after the effective date of this order and shall apply to services rendered on and after their effective date.

72. Hornitos Telephone Company shall accrue its settlements gains as reflected in Appendix C, in a memorandum account from the effective date of this decision with interest accrued at a rate equal to 1/12th the interest rate on 3-month commercial paper for the previous month, as published in the Federal Reserve Statistical Release, G.13, or its successor, until further order of this Commission.

73. Within 30 days of the effective date of this order each ITC except Hornitos Telephone Company shall eliminate its interest bearing memorandum account by implementing a bill and keep surcharge or surcredit, spread over one year, on intraLATA services by advice letter filing in conformance with GO 96-A. In establishing the bill and keep surcharge or surcredit the ITC shall use the 1986 intraLATA billing base reflected in Appendix E. The revised tariff schedules shall become effective 60 days after the effective date of this order and shall apply to services rendered on or after the effective date of the tariff revisions.

make an advice letter filing to adjust its basic exchange service rates and establish a bill and keep billing surcharge on intraLATA services to reflect the settlement effects of today's rate design decision as set forth in Appendix C of this decision. Each ITC shall use the 1986 customer volumes which are shown in Exhibit 352 and are reflected in Appendix D of this decision. Further, in establishing the bill and keep intraLATA billing surcharge each ITC shall adjust its 1986 intraLATA billing base set forth in Appendix E of this decision to reflect the newly revised basic exchange service rates. The process which each ITC shall use to recover its settlement effects is as follows:

1. Increase basic exchange service rates exclusive of EAS and SRA increments by a uniform percentage up to 100% of the present rates, rounded to the nearest $.05 but not to exceed the 150% threshold level of comparable urban rates.

2. Implement a bill and keep surcharge on intraLATA services to recover the remaining settlements effects if the revised basic rates do not fully recover the settlements effects and the 1-party residence flat rate has not exceeded the threshold level of 150% of comparable California urban rates.

3. Recover the remaining settlements effects from the intrastate High Cost Fund if the revised basic local rates do not fully recover the settlements effects but the 1-party residence flat rate has reached the 150% threshold level.

The advice letter filing with revised tariff schedules shall conform with the provisions of GO 96-A. The revised tariff schedules shall become effective no sooner than 30 days after customers have been notified of the revisions and 15 days after the advice letter filing and shall apply to services rendered on or after the effective date of the tariff revisions.

74. Within 30 days of the effective date of this order Pacific shall make an advice letter filing under the terms of GO 96-A to amend its Access Services Tariff, Schedule Cal. P.U.C. 175-T, to reduce its billings from special access services on a uniform percentage basis, excluding DDS and HiCap, by $11 million in a manner consistent with the foregoing opinion. The effective date of the revised tariff sheets shall be 60 days after the effective date of this order. The revised tariff schedules shall apply to services rendered on and after the effective date of the revised schedules.

75. Within 14 days after Pacific makes its advice letter filing to reduce its special access rates in the manner described in this decision AT&T shall file an advice letter with this Commission under the terms of GO 96-A which proposes accumulating the reduced access charge expense resulting from this decision in a memorandum account, with interest, commencing on the effective date of the Pacific tariff revision and running through December 31, 1988 at which time AT&T shall roll this accumulated reduced expense into its computation of the effects on access rates of the SPF to SLU phase down of the local exchange carriers which will be reflected in AT&T's rates.

76. Western Burglar and Fire Alarm Association's motion to strike the discussion in Pacific's reply brief of GO 152 regarding the installation and maintenance of private line alarm service is denied.

77. Within 30 days after the effective date of this order Pacific shall make an advice letter filing under the terms of GO 96-A to amend its tariffs to reflect the rates, charges, and conditions as set forth in Appendix A. The effective date of the revised tariff sheets shall be 60 days after the effective date of this order. The revised tariff schedules shall apply to service rendered on and after the effective date of the revised schedules.

79. Within 30 days of the effective date of this order General Telephone Company of California is authorized to make an advice letter filing under the terms of GO 96-A to incrementally revise its bill and keep intraLATA billing surcharge to reflect its settlements effect as set forth in Appendix C. In calculating the incremental billing surcharge General shall use the adopted 1986 customer billing base in D.85-12-081. The revised tariff schedule shall become effective no sooner than 30 days after customers have been notified of the revision and 15 days after the advice letter filing, and shall apply to services rendered on or after the effective date of the tariff revision.

80. Within 30 days of the effective date of this order West Coast Telephone Company is authorized to make an advice letter filing under the terms of GO 96-A to incrementally revise its bill and keep intraLATA billing surcharge to reflect its settlements effect as set forth in Appendix C. In calculating the incremental billing surcharge West Coast shall use the 1986 customer billing base reflected in Appendix D. The revised tariff schedule shall become effective no sooner than 30 days after customers have been notified of the revision and 15 days after the advice letter filing, and shall apply to services rendered on or after the effective date of the tariff revision.

81. The requirements of the ALJ Ruling dated July 1, 1985 are extinguished on and after the effective date of this order.

This order is effective today.

Dated _______________, at San Francisco, California.

APPENDIX A
SHEET 1 OF 20
PACIFIC BELL
RATES AND CHARGES

Schedule Cal. P.U.C. No. A2.
Billing Surcharges

The following revisions are ordered:

2.1 RULES
2.1.33 RULE NO. 33 - BILLING SURCHARGES

	Rates	Monthly Percentage
1.A	Adjustment Factor	(0.191%) *

The monthly percentage applies to all recurring and nonrecurring rates and charges for service or equipment provided under all of the utility's tariff schedules except the following:

The list of excepted services shall remain unchanged.

	Rates	Monthly Percentage
1.B	Adjustment Factor	0.283% **

The monthly pecentage applies to intraLATA toll provided under all of the Utility's tariff schedules except those items excluded in 1.A preceeding, other than Message Telecommunications Service A6., exclusive of Federal and Local excise taxes, and Federal income taxes.

	Rates	Monthly Percentage
1.C	Adjustment Factor	(8.722%) ***

The monthly pecentage applies to all recurring and nonrecurring rates and charges for service or equipment provided under Schedule Cal. P.U.C. No. 175-T.

* Monthly Percentage shall be 1.446% effective January 1, 1989.
** Monthly Percentage shall be 2.176% effective January 1, 1989.
*** Monthly Percentage shall be (6.879%) effective January 1, 1989.
( ) Denotes negative surcharge.

APPENDIX A
SHEET 20 OF 20
PACIFIC BELL
RATES AND CHARGES

Schedules Cal. P.U.C. Nos. A3., A9., A10. and B3.
Private Line and Private Line-Like Services

The revisions set forth on Sheets 22 through 72 of 72 of Exhibit No. 330 are authorized except as modified by the following:

Schedule Cal. P.U.C. No. B3.

3.2 CLASSIFICATION AND RATES
3.2.1 SERIES 1000 CHANNELS
B. REGULATIONS
1. Applicable to Types 1001, 1002, 1005 and 1006 channels for remote metering, supervisory control and miscellaneous signaling purposes.

Types 1002, 1005 and 1006 channels

Rates and charges apply only to those services in service as of the effective date of tariffs filed under the authority granted in this decision, and which continue to be furnished to the same customer at the same location.

2. Applicable to Types 1002, 1005 and 1006 channels for private line teletypewriter and morse services.

Channels for teletypewriter and morse services apply only to those services in service as of the effective date of tariffs filed under the authority granted in this decision, and which continue to be furnished to the same customer at the same location

3. Applicable to Types 1001, 1002, 1005 and 1006 channels for Data Transmission.

Types 1002, 1005 and 1006 channels for data transmission apply only to those services in service as the effective date of tariffs filed under the authority granted in this decision, and which continue to be furnished to the same customer at the same location.

Sheet 53 of 72 of Exhibit 330, Section 3.2.1C.16.b(2) should read "Intraexchange, Intradistrict Area".

eet 57 of 72 of Exhibit 330, Section 3.2.2C.9 delete the word entrex".

APPENDIX A
SHEET 2 OF 20
PACIFIC BELL
RATES AND CHARGES

Schedule Cal. P.U.C. No. A3.
Dual Element Charges

The following charges are authorized:

3.1. CHARGES FOR ACCESS LINES, LABOR AND SERVICE ENHANCEMENTS

3.1.2 ACCESS LINES (PRIMARY AND EXTENDED SERVICES)

A. INDIVIDUAL, PARTY LINE, SUBURBAN, TELEPHONE ANSWERING AND FARMER LINE SERVICE

New and additional local and extended area service charges, each line

	Service Charge
- Answering line	$ 70.75
- Individual line residence or business Service, complex	70.75
- Individual, party line, suburban or Farmer line business service, simple	70.75
- Individual, party line, suburban or Farmer line flat rate residence service, simple	34.75
- Individual, party line or measured rate residence service, simple	34.75
- Individual line, AIS (Airport Intercommunicating Service)	70.75
- Individual line measured rate business service - data, all services	176.75
- Individual Resale Line	70.75
- Toll terminal line	70.75

B. TRUNK LINE SERVICE

New and additional local and extended area service charges, each trunk

- Trunk line service, residence, business or TAS (Telephone Answering Service)	70.75
- Trunk resale line	70.75
- Toll terminal trunk	70.75

D. Charges set forth in the adopted revisions for schedule Cal. P.U.C. No. A9. apply.

APPENDIX A
SHEET 3 OF 20
PACIFIC BELL
RATES AND CHARGES

Dual Element Charges - continued

	Service Charge
3.1.	
3.1.2	
E. CENTREX DORMITORY SERVICE	
- Each primary line	$ 34.75
G. FOREIGN EXCHANGE SERVICES - BUSINESS AND RESIDENCE SERVICES	
1. Foreign Exchange (FXS) or Foreign District Area Service (FDA of the same exchange only)	
a. Contiguous, each line or trunk	
Business	
- Individual access line	380.00
- Answering line	380.00
- Trunk line service	380.00
- Trunk line service, TAS	380.00
- Centrex primary access line (see Note 1)	340.00
- Toll terminal	380.00
- Tie line (FDA of same exchange only)	380.00
Residence	
- Individual and party line service	260.00
- Trunk line service	380.00
b. Noncontiguous, each line or trunk	
Business	
- Individual access line	580.00
- Answering line	580.00
- Trunk line service, residence or business	580.00
- Trunk line service, TAS	580.00
- Tie line (FDA of same exchange only)	580.00
- Centrex primary access line (see Note 1)	540.00
Residence	
- Individual and party line service	460.00
- Trunk line service	580.00
2. Foreign Prefix Service (FPS), of the same exchange	
a. Contiguous	
- Each residence or business line or trunk	380.00
b. Noncontiguous	
- Each residence or business line or trunk	580.00

NOTE: 1: Plus Installation Charge for primary line as set forth in Schedule Cal.P.U.C. No. A.9.1.

APPENDIX A
SHEET 4 OF 20
PACIFIC BELL
RATES AND CHARGES

Dual Element Charges - continued

3.1.
3.1.2.

J. SEMIPUBLIC SERVICE

	Service Charge
- Each access line, with Utility provided set and premises wiring	$ 240.00
- Each COPT access line, with customer provided set	111.25

3.1.6 MOVE, CHANGE, REARRANGEMENT OR MODIFICATION OF ACCESS LINE AND OTHER MISCELLANEOUS CHANGES, ALL SERVICES, EACH LINE OR TRUNK

	Service or Labor Charges
a. Change from utility provided Semipublic Coin, Public Coin, Business, or Residence service to COPT service - Each access line	$ 75.75

APPENDIX A
SHEET 5 OF 20
PACIFIC BELL
RATES AND CHARGES

Schedule Cal. P.U.C. No. A5.
Basic Exchange Access Line Services

The following rates are authorized:

5.2 LOCAL EXCHANGE SERVICE

5.2.1 MEASURED RATE SERVICE

A. LOCAL EXCHANGE MEASURED RATE SERVICE

4. Rates and Charges

Service	Monthly Rate*
Individual Line Measured Rate Service - Data	$ 22.55
Individual Line Measured Rate Business Service	8.35
Individual Resale Line Measured Rate Business Service	19.15

5.2.4 FLAT RATE SERVICE

A. LOCAL EXCHANGE FLAT RATE SERVICE

4. Rates and Charges

Service	Monthly Rate*
Individual Line Flat Rate Business Service	$ 17.25
Individual Line Flat Rate Residence Service	8.35
Two-Party Line Flat Rate Business Service	11.90

*Plus Extended Area Service Increments where applicable. Monthly rates apply in exchanges where the service is offered.

PACIFIC BELL
RATES AND CHARGES

Basic Exchange Access Line Services - continued

5.2
5.2.5 LOCAL SERVICE OPTIONS
B. FARMER LINE SERVICE

4. Rates and charges

Service	Monthly Rate*
Business Farmer Line Service	$ 4.95
Residence Farmer Line Service	2.70

C. SUBURBAN SERVICE

4. Rates and Charges

Service	
Four-Party Line Suburban Flat Rate Business Service	12.20

5.3 PRIVATE BRANCH EXCHANGE TRUNK LINE SERVICE

5.3.1 MEASURED RATE TRUNKS

B. RATES AND CHARGES

Service	Monthly Rates*
Resale Trunks	$ 19.15

5.3.3 FLAT RATE TRUNKS

A. RATES AND CHARGES

Service	
Residence Trunks	12.55

*Plus Extended Area Service increments where applicable. Monthly rates apply in exchanges where the service is offered.

APPENDIX A
SHEET 7 OF 20
PACIFIC BELL
RATES AND CHARGES

Schedule Cal. P.U.C. No. A5.
Universal Lifeline Telephone Service

The following revisions are ordered:

5.2 LOCAL EXCHANGE SERVICE
5.2.5 LOCAL SERVICE OPTIONS
E. UNIVERSAL LIFELINE TELEPHONE SERVICE
4. Rates and Charges

g. ULTS - all day/hours

1PQ service is provided with an allowance of 60 untimed local calls. Local messages over this designated allowance are provided at the rates following:

	Rate per Message
61 and over	$ 0.08

Schedule Cal. P.U.C. No. A5.
Semipublic Telephone Service

The following revisions are authorized:

5.5 PUBLIC COMMUNICATION SERVICE - COIN AND COINLESS

5.5.2 SEMIPUBLIC TELEPHONE SERVICE

D. RATES AND CHARGES

Service	Monthly Rates*
Individual Line Semipublic Service	$ 29.00
Four-party Line Semipublic Service	29.00

*Plus Extended Area Service Increments where applicable. Monthly rates apply in exchanges where the service is offered.

APPENDIX A
SHEET 8 OF 20
PACIFIC BELL
RATES AND CHARGES

Schedule Cal. P.U.C. No. A5.
Customer-Owned Pay Telephone (COPT) Service

The following increases in rates are authorized:

5.5.3 CUSTOMER-OWNED PAY TELEPHONE (COPT) SERVICE

D. RATES AND CHARGES

Service	Monthly Rate Increase
COPT Measured Rate Business Service	$ 0.20
COPT Flat Rate Business Service	0.50

Schedule Cal. P.U.C. No. A5.
Zone Usage Measurement Service

The following revisions are ordered:

5.2 LOCAL EXCHANGE SERVICE
5.2.1. MEASURED - RATE SERVICE
B. ZONE USAGE MEASUREMENT SERVICE

4. Rates and Charges

c. Zone Calling

(1) Zone Calling Units are applicable to calls between the Zone as such Zones are identified in 3. preceding.

Zone Calling Units

Zone	Each Addl. Minute or Portion Thereof
2 (9-12 miles)	2 Units
3 (13-16 miles)	4 Units

APPENDIX A
SHEET 9 OF 20
PACIFIC BELL
RATES AND CHARGES

Schedule Cal. P.U.C. No. A5.
Foreign Exchange Service

The revisions set forth on pages 117 through 123 of Exhibit No. 286 except as modified below are authorized.

5.1 EXCHANGE AREAS
5.1.4 FOREIGN EXCHANGE SERVICE
D. ROUTES BETWEEN PACIFIC BELL EXCHANGES

2. Rates and Charges

a. Business Service

Within an exchange or district area contiguous or noncontiguous to the foreign exchange or district area. Rate per month for each business individual line measured rate primary station, business measured rate PBX trunk and joint user service.

(1) Foreign Exchange Station Service

	Monthly Rate
- Foreign exchange service increment	$ 11.25
- Basic access line rate	See Note 1
- Local Usage	See Note 2
- Mileage Rates	See Note 3
Los Angeles Exception Rate Treatment	
- DA's 1 thru 14	11.25
Exception: Contiguous Service in:	
- Rate Area A	12.85
- Rate Area B	14.45
- Rate Area C	16.05
- Noncontiguous Service	16.05

NOTE 1: Basic access line rate as set forth in Schedules Cal. P.U.C. Nos. A5.2. and A5.3.1. including EAS/SRA increments, if applicable.

NOTE 2: Local usage as set forth in Schedule Cal. P.U.C. No. A5.1.4.

NOTE 3: Mileage rates as shown in General Rates and Charges in C.1. and 2., preceding.

APPENDIX A
SHEET 10 OF 20
PACIFIC BELL
RATES AND CHARGES

Foreign Exchange Service - continued

5.1
5.1.4
D. ROUTES BETWEEN PACIFIC BELL EXCHANGES (cont'd.)
2. Rates and Charges (cont'd.)

b. Residence Service, Individual and Suburban

(1) Foreign exchange Station Service

	Monthly Rate
Foreign exchange Service Increment	
- 1FR/FW	$ 6.75
- 1MR/1SY	4.05
- 4ZR	2.70
- Basic access line rate	See Note 1
- Local Usage	See Note 2
- Mileage Rates	See Note 3

c. Residence Service Party Line

Within the listed local exchanges continguous to the listed foreign exchange. Rate per month for each residence two party line primary station, furnished only to the same customer on the same premises as of November 11, 1973.

USOC	Service
2FR++	FXS Two-Party Line flat Residence Service

	Monthly Rate
- Foreign exchange service increment	$ 2.90
- Basic access line rate	See Note 1
- Local Usage	See Note 2
- Mileage Rates	See Note 3

NOTE 1: Basic access line rate as set forth in Schedule Cal. P.U.C. No. A5.2. including EAS/SRA increments, if applicable.

NOTE 2: Local usage as set forth in Schedule Cal. P.U.C. No. A5.1.4.

NOTE 3: Mileage rates as shown in General Rates and Charges in C.1. and 2., preceding.

APPENDIX A
SHEET 11 OF 20
PACIFIC BELL
RATES AND CHARGES

Foreign Exchange Service - continued

5.1
5.1.4
D. ROUTES BETWEEN PACIFIC BELL EXCHANGES (cont'd.)
2. Rates and Charges (cont'd.)

d. Residence Service, Trunk Lines

USOC	Service
TFR++	FXS Flat Rate Residence Service First Trunk
RHR++	FXS Flat Rate Residence Service Additional Trunk

Within the listed local exchange to the listed foreign exchange. Rate per month for each residence trunk line service.

	Monthly Rate
- Foreign exchange service increment	$ 2.60
- Basic access line rate	See Note 1
- Local Usage	See Note 2
- Mileage rates	See Note 3

Foreign Exchange	Monthly Rate TFR/RHR
Los Angeles	
Contiguous Service in Exception Rate Areas (see Note 1)	
- Rate Area A	$ 4.20
- Rate Area B	5.80
- Rate Area C	7.40
- Noncontiguous Service (see Note 1)	7.40

NOTE 1: Basic access line rates apply as set forth in Schedule Cal. P.U.C. No. A5.3.3.A, including EAS/SRA increments, if applicable.

NOTE 2: Local usage as set forth in Schedule Cal. P.U.C. No. A5.1.4.

NOTE 3: Mileage rates as shown in General Rates and Charges in C.1. and 2., preceding.

APPENDIX A
SHEET 12 OF 20
PACIFIC BELL
RATES AND CHARGES

Foreign Exchange Service - continued

5.1
5.1.4.

E. ROUTES INVOLVING CONNECTING COMPANY EXCHANGES - SOUTHERN CALIFORNIA
F. ROUTES BETWEEN CONTIGUOUS EXCHANGES-CONNECTING COMPANY EXCHANGES-NORTHERN CALIFORNIA
G. ROUTES BETWEEN NONCONTIGUOUS EXCHANGES-CONNECTING COMPANY EXCHANGES-NORTHERN CALIFORNIA

Rates and Charges

Within an exchange contiguous or noncontiguous to the to the foreign exchange.

Rate per month for each Individual Line Primary Station, Business PBX Trunk and Joint User Service from the exchanges listed below:

Business and Residence Service

USOC	Service
1FR++	FXS Individual Line Flat Rate Residence Service
1FW++	FXS Individual Line Flat Rate Residence Service
4ZR++	FXS Four-Party Line Suburban Flat Rate Residence
1MB++	FXS Individual Line Measured Rate Business Service
1ML++	FXS Individual Line Measured Rate Business Line
1MS++	FXS Individual Line Measured Rate Business Line - Single Line Customer
7FB++	FXS Business Answering Line terminating on 6 Line Concentrator
7FL++	FXS Business Answering Line Terminating on a TAS
TMB++	FXS Measured Rate Business Service First Trunk
TM2++	FXS Measured Rate Business Service Additional Trunk
TM3++	FXS Measured Rate Business Service Additional Trunk-Outward Only
TM4++	FXS Measured Rate Business Service Trunk Inward Only

The following increases in monthly rates for foreign exchange services are authorized:

Services	Monthly Rate Increase
1FR, 1FW	$ 0.10
1MB, 1ML, 1MS, 7FB, 7FL	0.10
TMB, TM2, TM3, TM4	4.00

APPENDIX A
SHEET 13 OF 20
PACIFIC BELL
RATES AND CHARGES

Schedule Cal. P.U.C. No. A5.
Direct-In-Dialing To PBX Systems

The following rates are ordered:

5.3 PRIVATE BRANCH EXCHANGE TRUNK LINE SERVICE

5.3.4 DIRECT-IN-DIALING TO PBX SYSTEMS

C. RATES AND CHARGES

Trunk line services as shown elsewhere in this schedule, furnished at the appropriate rates and charges, are required in sufficient quantitites to meet the traffic demand in addition to the rates and charges for DID service:

1. Provided within the same exchange or district area:

	Monthly Rate
First 200 Direct Inward Dialing station numbers - Each 100 DID station numbers	$ 45.00
Over 200 Direct Inward Dialing station numbers - Each additional 100 DID station numbers	45.00
Circuit Termination - Each trunk	8.00

2. Provided within a different exchange or district area:

First 200 direct inward station numbers - Each 100 DID station numbers	45.00
Over 200 direct inward station numbers - Each 100 DID station numbers	45.00
Circuit Termination - Each trunk	8.00

APPENDIX A
SHEET 14 OF 20
PACIFIC BELL
RATES AND CHARGES

Direct-Inward-Dialing To PBX Systems - continued

5.3
5.3.4
C. RATES AND CHARGES

3. Provided from a foreign exchange, between district areas of an exchange or from a district area of an exchange to a contiguous or noncontiguous exchange:

	Monthly Rate
First 200 direct inward station numbers - Each 100 DID station numbers	$ 45.00
Over 200 direct inward station numbers - Each additional 100 DID station numbers	45.00
Circuit termination - Each trunk	8.00

Schedule Cal. P.U.C. No. A5.
Directory Listing Service

The revisions set forth in Appendix C of Exhibit 351 are ordered.

Schedules Cal. P.U.C. Nos. A5. and A9.
Centrex Service

The revisions set forth on pages 904 through 956 of Exhibit No. 286 except as modified below are authorized.

APPENDIX A
SHEET 15 OF 20
PACIFIC BELL
RATES AND CHARGES

Centrex Service - continued
9.1 DIAL SWITCHING SYSTEMS
9.1.1 CENTREX
D. RATES AND CHARGES

Exchange Access Trunking Charge Each Primary Line

1. A minimum requirement for each Centrex service is 20 or 100 working and/or non-working primary lines. Designate USOCs as follows:

   Working primary lines - NRX
   Non-working lines to make up minimum - NRXMN

a. Measured Rate Service

	Monthly Rate Primary Lines		
	ESS;DSS 1st 20 or less	#5XB 1st 100 or less	ESS;DSS;#5XB each Addl.
- Charge for working primary line	$ 25.00	$ 125.00	$ 1.25
- Charge to meet minimum requirement of primary lines	25.00	125.00	1.25

b. Flat Rate Service

(1) Flat Rate Service			
- Charge for working primary line	69.00	345.00	3.45
- Charge to meet minimum requirement of primary lines	69.00	345.00	3.45

2. Private Network Access

	Monthly Rate
a. Arrangement of a tie line or interexchange channel - interwire center private line telephone line to select and be selected by lines of the Centrex system.	
(1) Rate for First two way 4-wire termination, Per CO Per Service Order	
- Centrex to Centrex, each	$ 92.75
- Centrex to CPE PBX, each	92.75
- Centrex to IEC, each	92.75
Additional two way 4-wire termination, Per CO Per Service Order	
- Each	92.75

APPENDIX A
SHEET 16 OF 20
PACIFIC BELL
RATES AND CHARGES

Centrex Service - continued
9.1
9.1.1
D. RATES AND CHARGES (cont'd)
5. Station-Controlled Features

	Installation Charge	Monthly Rate
l. Speed Calling		
Customer changeable, primary line equipped for individual		
- Each 6-10 numbers	$ 5.00	$ 1.50
Customer changeable, primary line equipped for groups		
- Each 30 numbers	5.00	1.70
- Each 50 numbers	5.00	1.85
- Each 70 numbers	5.00	2.00
v. Call Park		
- Each	5.00	.75

APPENDIX A
SHEET 17 OF 20
PACIFIC BELL
RATES AND CHARGES

Schedule Cal. P.U.C. No. A6.
Message Telecommunications Service

The following revisions are ordered:

6.2 STANDARD SERVICE OFFERINGS
6.2.1 TWO-POINT MESSAGE TELECOMMUNICATION SERVICE
A. GENERAL
4. RATES AND CHARGES
a. Method of Applying Rates

(12) Mileages and Corresponding Rates of Different Classes of Service

BASIC SCHEDULE

	DAY RATE		
	Initial Period Station (Sent Paid)		
RATE MILEAGE	DIAL 1-MINUTE	COIN 3-MINUTES	EACH ADDITIONAL MINUTE ALL CLASSES OF SERVICE
0 - 8	$ 0.17	$ 0.30	$ 0.07
9 - 12	0.17	0.30	0.07
13 - 16	0.20	0.40	0.10
17 - 20	0.22	0.45	0.13
21 - 25	0.25	0.55	0.16
26 - 30	0.28	0.70	0.19
31 - 40	0.31	0.75	0.22
41 - 50	0.34	0.85	0.25
51 - 70	0.37	0.90	0.28
71+	0.40	1.00	0.31

APPENDIX A
SHEET 18 OF 20
PACIFIC BELL
RATES AND CHARGES

Message Telecommunications Service - continued

6.3 OPTIONAL CALLING PLANS
6.3.1 CALL BONUS-COMMUNITY PLANS
F. RATES AND CHARGES

Option 1 - Community Plan

Service Area Rate Group	Service Offerings Rate Mileage	MESSAGE RATE First Minute Day	MESSAGE RATE Add'l Minute Day
1	9 - 12	$ 0.119 *	$ 0.049 **
2	13 - 16	0.140 ***	0.070 ****
3	17 - 20	0.154	0.091
4	21 - 25	0.175	0.112
5	26 - 30	0.196	0.133
6	31 - 40	0.217	0.154

Option 2 - Community Circle Plan

Service Area Rate Group	MESSAGE RATE First Minute Day	MESSAGE RATE Add'l Minute Day
1	$ 0.119 *	$ 0.049 **
2	0.140 ***	0.070 ****
3	0.154	0.091
4	0.175	0.112
5	0.196	0.133
6	0.217	0.154

* $0.08 on ZUM routes
** $0.02 on ZUM routes
*** $0.10 on ZUM routes
**** $0.04 on ZUM routes

APPENDIX A
SHEET 19 OF 20
PACIFIC BELL
RATES AND CHARGES

Message Telecommunications Service - continued

6.3
6.3.2 OPTIONAL CALLING MEASURED SERVICE

E. RATES

Rate Group	Overtime Rate Per Minute Over Allowance
1	$ 0.07
2	0.10
3	0.13
4	0.16
5	0.19
6	0.22

APPENDIX A
SHEET 20 OF 20
PACIFIC BELL
RATES AND CHARGES

Schedules Cal. P.U.C. Nos. A3., A9., A10. and B3.
Private Line and Private Line-Like Services

The revisions set forth on Sheets 22 through 72 of 72 of Exhibit No. 330 are authorized except as modified by the following:

Schedule Cal. P.U.C. No. B3.

3.2 CLASSIFICATION AND RATES
3.2.1 SERIES 1000 CHANNELS
B. REGULATIONS

1. Applicable to Types 1001, 1002, 1005 and 1006 channels for remote metering, supervisory control and miscellaneous signaling purposes.

   Types 1002, 1005 and 1006 channels

   Rates and charges apply only to those services in service as of the effective date of tariffs filed under the authority granted in this decision, and which continue to be furnished to the same customer at the same location.

2. Applicable to Types 1002, 1005 and 1006 channels for private line teletypewriter and morse services.

   Channels for teletypewriter and morse services apply only to those services in service as of the effective date of tariffs filed under the authority granted in this decision, and which continue to be furnished to the same customer at the same location

3. Applicable to Types 1001, 1002, 1005 and 1006 channels for Data Transmission.

   Types 1002, 1005 and 1006 channels for data transmission apply only to those services in service as the effective date of tariffs filed under the authority granted in this decision, and which continue to be furnished to the same customer at the same location.

APPENDIX B
Page 1

Implementation of the California Intrastate High Cost Fund

A. 1988 Settlements Effects and HCF Filings

Each rural and small metropolitan exchange telephone company shall file an advice letter implementing the tariffs necessary to collect on a "flow-through" basis the settlement effects revenue impact specified for such company in the foregoing opinion. Such advice letter tariff filings shall become effective concurrently with implementation of the revised Pacific Bell rate design set forth in this decision.

Such advice letters shall calculate the impact of each company's net settlements effects upon its present level of local exchange revenues and shall additionally describe the rate design necessary to adjust present local exchange revenue levels to reflect the specified settlements effects impact. The company's average local exchange rates contained in any rate design proposed by such advice letter filings shall not exceed the target level of 150% of comparable California urban rates, a standard to be measured generally by a target R-1 flat rate of $8.35 monthly. Presently authorized rates shall not, however, be reduced to this target level by operation of this mechanism. Any proposals for an exception to this rule shall be addressed separately to the Commission. The 150% level of comparable California urban rates shall constitute a benchmark against which specific company rate designs are measured rather than a rigid requirement that each rate design element be set at 150% of the underlying urban rate.

Those companies with a revised local exchange revenue requirement (the sum of the present level of local exchange revenues and the net positive and negative settlements effects for such company herein specified) which cannot be met from the local exchange rate designs incorporating the 150% threshold shall be eligible to receive the balance of their revised local exchange revenue requirement from the HCF, and each such company's advice letter shall set forth calculations of its HCF funding requirements for the year 1988, adjusted for the partial year. Companies with revised local exchange revenue requirements which can be met from rate design adjustments contained in their advice letters shall not receive HCF funding during 1988.

B. Annual Settlements Effects and HCF Adjustments

In each succeeding year, each rural and small metropolitan company shall file with the Commission an advice letter incorporating the net settlements effects upon such company of regulatory changes ordered by the Commission and the Federal Communications Commission (FCC). These advice letter filings will include the previously authorized annual filings for interLATA SPF to SLU shifts set forth in D.85-06-115 as well as all other regulatory changes of industry-wide effect such as changes in levels of interstate high cost funding, interstate NTS assignment, other FCC-ordered changes in separations and accounting methodology and Commission-ordered changes such as rate changes affecting access charges, intraLATA toll or EAS settlements revenues, interLATA separations shifts and the effects of other Commissions decisions which increase or decrease settlements revenues or cost assignments.

Each company shall file an advice letter by October 1 of each year (commencing October 1, 1988) setting forth the net increase or decrease from these factors upon that portion of its revenue requirement which must be met from its local exchange rate design. The advice letter and supporting workpapers shall also set forth proposed revisions to the company's local exchange rate design to compensate for the net positive or negative settlements effects while maintaining the overall rate design within the 150% guidelines as most recently defined by Commission decision and further calculating any resultant increases or decreases in the company's HCF funding requirements. The advice letter shall be reviewed by the Commission Advisory and Compliance Division (CACD) and incorporated, as approved, in Commission resolutions to take effect by January 1 of the year following filing. The CACD staff shall coordinate the advice letter filing process each year with all local exchange companies through appropriate procedures.

C. HCF Funding and Administration

The HCF funding process shall be administered by Pacific Bell (Pacific), and the HCF shall function as a separate fund rather than as a pool. HCF funding shall be provided by a uniform incremental amount on the carrier common line charge (CCLC) of all local exchange company interLATA access tariffs. Concurrently with this decision and in each succeeding year, Pacific shall determine the total statewide HCF funding requirement based on the funding requirements identified in the advice letters described in (1) paragraph A for 1988 and (2) paragraph B for succeeding years, and shall coordinate the filing of appropriate advice letter modifications to all California exchange carrier access charge tariffs to generate the calculated level of HCF revenue requirement.

The HCF funding increment shall be adjusted each January 1 to implement the annual revisions to HCF funding requirements. The HCF access charge increment may also be adjusted not more often than quarterly during any year where revision is required to compensate for any overcollection or undercollection of the then-current Commission authorized fund revenue requirement, including adjustments caused by variation in actual and projected usage used in developing the HCF CCL increment and adjustments caused by any mid-year changes in the funding revenue requirement due to decisions in pending rate proceedings or any other decisions of the Commission affecting the HCF funding level. Any end-of-year HCF fund residual amount (positive or negative) shall be netted with the succeeding year's HCF prospective funding requirement.

HCF funding adjustments shall be coordinated by Pacific Bell in conjunction with other local exchange companies and the CACD staff. Each exchange carrier shall remit monthly to Pacific for the HCF that portion of the CCLCs collected from the HCF access charge increment, and Pacific shall make disbursements monthly from the fund to each recipient local exchange carrier. Pacific shall not separately account for any incremental administrative costs incurred by it in administering the HCF fund, but rather it shall treat such costs as additional expenses of administering the access charge pool.

D. Rate Proceedings and Funding Levels

HCF funding shall continue at 100% of the Commission authorized funding requirement for the years 1988 and 1989. The HCF support level for those local exchange companies which have not initiated a general rate proceeding, either under General Order 96-A or by a general rate case application, by December 31, 1990, shall be reduced during the year 1991, so that such a company shall receive only 80% of the amount of funds that would otherwise be paid to it from the HCF during 1991. The HCF funding level for those companies not initiating rate proceedings by December 31, 1991, shall be further reduced to 50% of the funding requirement during the year 1992, and HCF funding for those companies which have not initiated rate proceedings by December 31, 1992, shall

APPENDIX B
Page 5

terminate entirely in 1993. A company's initiation of a general rate proceeding prior to the end of 1990 shall freeze its funding level at 100% during the pendency of its rate proceeding. A company's initiation of a general rate proceeding during 1991 shall freeze its 80% funding level during the pendency of its rate proceeding, and a company's initiation of a rate proceeding during 1992 shall similarly freeze its funding at the 50% level pending its rate decision.

The issuance of a Commission decision or resolution in a general rate proceeding of an independent company will have the effect of a "fresh start" for that company under the HCF plan. The company's rate case decision will specify its new local exchange rate design and state whether the company is to receive HCF support as part of its newly adopted revenue requirement and rate design. In years following the decision in the general rate proceeding, the company will continue to file annual advice letters reflecting net incremental changes of the type described in paragraph B and corresponding adjustments in its local exchange rate design and HCF funding amounts.

(END OF APPENDIX B)

APPENDIX - C
SHEET 1 OF 1

PACIFIC BELL

SETTLEMENT REVENUE EFFECTS ON INDEPENDENT TELEPHONE COMPANIES (ICOs)

($000)

		INTERLATA	----INTRALATA----					INTRALATA	
	INDEPENDENT COMPANIES	ACCESS	MTS	TOLL PL	EAS	IX ZUM	SUBTOTAL	SPF to SLU	TOTAL
		(a)	(b)	(c)	(d)	(e)	(f)	(g)	(h)
1	CALAVERAS	($5)	($30)	$0	$3	$0	($31)	$63	$32
2	CAPAY	(1)	(7)	0	0	0	(8)	*	(8)
3	CAL-OREGON (with DORIS)	(7)	(21)	1	0	0	(27)	38	11
4	CAL PAC NATIONAL	(19)	(150)	3	1	0	(166)	139	(27)
5	CITIZENS	(145)	(680)	56	173	0	(596)	(99)	(695)
6	CONTINENTAL	(300)	(3,959)	158	42	0	(4,058)	(595)	(4,653)
7	DUCOR	(2)	(15)	0	0	0	(17)	22	5
8	EVANS (with LIVINGSTON)	(11)	(98)	5	5	0	(99)	*	(99)
9	FORESTHILL	(2)	(21)	0	0	0	(23)	25	2
10	GENERAL OF CAL	0	(33,777)	2,221	2,648	(6,839)	(35,747)	*	(35,747)
11	HAPPY VALLEY	(9)	(20)	0	25	0	(3)	37	34
12	HORNITOS	(3)	(25)	0	0	0	(28)	107	79
13	KERMAN	(5)	(21)	0	11	0	(14)	9	(5)
14	PINNACLES	(0)	(1)	0	0	0	(2)	5	3
15	PONDEROSA	(17)	(159)	6	0	0	(171)	83	(88)
16	ROSEVILLE	(54)	(378)	10	229	0	(193)	(352)	(545)
17	SIERRA (with MARIPOSA)	(24)	(110)	5	0	0	(129)	(17)	(146)
18	SISKIYOU	(10)	(60)	8	0	0	(62)	136	74
19	TUOLUMNE	(18)	(141)	0	3	0	(156)	210	54
20	VOLCANO	(18)	(56)	0	5	0	(69)	*	(69)
21	WEST COAST	0	(86)	1	0	0	(85)	*	(85)
22	TOTAL OF COLUMNS	($650)	($39,814)	$2,476	$3,145	($6,839)	($41,682)	($189)	($41,871)

NOTES:

( ) - DENOTES A DECREASE IN ICO REVENUES (i.e. AN INCREASE IN RATES).

* - THESE UTILITIES HAVE ALREADY INCORPORATED BILLING SURCHARGES FOR THE SETTLEMENT EFFECTS OF INTRALATA SPF TO SLU.

APPENDIX D
SHEET 1 OF 6
SERVICE VOLUMES
FOR BASIC EXCHANGE SERVICES

	CALAVERAS	CAL-ORE:D&M	CAL-ORE:N&T	CAPAY VALLEY	CITIZENS	CONTEL	CP NATL.	DUCOR
LOCAL								
RESIDENCE								
1-PARTY--flat	775	382	710	338	28,627	149,064	7,257	455
--measured	---	---	---	---	3,381	23,039	243	---
2-PARTY--flat	304	see below	190	0	1,498	1,916	56	---
--measured	---	286	---	---	---	---	---	---
4-PARTY--flat	---	---	---	---	54	3,687	79	---
SUBURBAN--flat	0	---	---	---	2,456	---	479	---
FARMER LINE--flat	---	---	---	---	5	66	1	---
KEY--flat	---	---	---	---	11	48	45	---
--measured	---	---	---	---	---	26	---	---
MULTILINE--flat	---	---	---	---	---	87	---	---
--measured	---	---	---	---	---	30	---	---
BUSINESS								
1-PARTY--flat	102	96	167	43	3,772	15,690	964	72
--measured	---	---	---	---	1,562	4,100	340	---
2-PARTY--flat	7	see below	8	0	---	91	31	---
--measured	---	17	---	---	---	---	---	---
4-PARTY--flat	---	---	---	---	---	106	---	---
SEMI-PUBLIC COIN	1	4	0	4	94	604	27	3
SUBURBAN--flat	0	---	---	---	138	---	66	---
FARMER LINE--flat	---	---	---	---	8	22	0	---
KEY--flat	---	27	61	0	1,380	10,039	651	0
--measured	---	---	---	---	895	2,939	228	---
PBX--flat	7	0	0	2	385	2,475	44	0
--measured	---	---	---	---	241	623	68	---
MULTILINE--flat	---	---	---	---	---	666	---	---
--measured	---	---	---	---	---	180	---	---
FEX								
RESIDENCE								
1-PARTY--flat	---	---	---	---	105	433	8	---
--measured	---	---	---	---	889/64/39	407	---	---
2-PARTY--flat	---	---	---	---	---	1	---	---
4-PARTY--flat	---	---	---	---	---	85	---	---
SUBURBAN--flat	0	---	---	---	5	0	---	---
FARMER LINE--flat	---	---	---	---	---	12	---	---
BUSINESS								
1-PARTY--flat	---	---	---	---	47	371	8	1
--measured	---	---	---	---	145/33/35/66	51	---	---
--message	---	---	---	---	13	---	---	---
2-PARTY--flat	---	---	---	---	---	0	---	---
4-PARTY--flat	---	---	---	---	---	0	---	---
FARMER LINE--flat	---	---	---	---	---	0	---	---
KEY--flat	---	---	---	---	15	---	---	---
--measured	---	---	---	---	117/100/55	459	---	---
--message	---	---	---	---	11	---	---	---
PBX--flat	---	---	---	---	0	159	---	---
--measured	---	---	---	---	50/20/6	---	---	---
--message	---	---	---	---	3	---	---	---

APPENDIX D
SHEET 2 OF 6
SERVICE VOLUMES
FOR BASIC EXCHANGE SERVICES

	EVANS--LPW	EVANS--SA	FORESTHILL	GENERAL	HAPPY VALLEY	HORNITOS	KERMAN	PINNACLES
LOCAL								
RESIDENCE								
1-PARTY--flat	4,112	125	1,112	2,032,624	1,678	245	2,764	38
--measured	---	---	---	63,847	---	---	---	---
2-PARTY--flat	325	---	122	80	40	13	422	---
--measured	---	---	---	---	---	---	---	---
4-PARTY--flat	---	---	0	---	228	24	---	6
SUBURBAN--flat	---	---	---	925	65	39	---	54
FARMER LINE--flat	---	---	---	4	---	0	---	---
KEY--flat	---	---	---	---	---	---	---	---
--measured	---	---	---	---	---	---	---	---
MULTILINE--flat	---	---	---	---	---	---	---	---
--measured	---	---	---	---	---	---	---	---
BUSINESS								
1-PARTY--flat	559	30	212	542,054	234	64	502	39
--measured	---	---	---	362,498	---	---	---	---
2-PARTY--flat	23	---	0	---	3	---	17	---
--measured	---	---	---	---	---	---	---	---
4-PARTY--flat	---	---	---	---	1	---	---	---
SEMI-PUBLIC COIN	30	0	1	11,730	5	0	2	---
SUBURBAN--flat	---	---	---	50	0	2	---	9
FARMER LINE--flat	---	---	---	0	---	0	---	---
KEY--flat	---	---	0	---	---	---	---	0
--measured	---	---	---	---	---	---	---	---
PBX--flat	470	0	6	73,309	---	---	78	0
--measured	---	---	---	52,732	---	---	---	---
MULTILINE--flat	---	---	---	---	---	---	---	---
--measured	---	---	---	---	---	---	---	---
FEX								
RESIDENCE								
1-PARTY--flat	84	---	11	3,646	---	---	61	---
--measured	---	---	---	116	---	---	43	---
2-PARTY--flat	---	---	---	---	---	---	---	---
4-PARTY--flat	---	---	---	---	---	---	---	---
SUBURBAN--flat	---	---	---	0	---	---	0	---
FARMER LINE--flat	---	---	---	0	---	---	---	---
BUSINESS								
1-PARTY--flat	77	---	---	5,098	---	---	---	---
--measured	---	---	5	3,508	---	---	35	---
--message	---	---	---	---	---	---	---	---
2-PARTY--flat	---	---	---	---	---	---	---	---
4-PARTY--flat	---	---	---	---	---	---	---	---
FARMER LINE--flat	---	---	---	0	---	---	---	---
KEY--flat	---	---	---	---	---	---	---	---
--measured	---	---	---	---	---	---	---	---
--message	---	---	---	---	---	---	---	---
PBX--flat	---	---	---	8,601	---	---	---	---
--measured	---	---	---	6,205	---	---	---	---
--message	---	---	---	---	---	---	---	---

APPENDIX D
SHEET 3 OF 6
SERVICE VOLUMES
FOR BASIC EXCHANGE SERVICES

	PONDEROSA	ROSEVILLE	SIERRA	SISKIYOU	TUOLUMNE	VOLCANO	WEST COAST
LOCAL							
RESIDENCE							
1-PARTY--flat	2,065	38,965	4,767	1,800	2,062	5,514	6,112
--measured	---	3,090	---	---	1,009	---	---
2-PARTY--flat	2,163	153	2,051	---	---	---	60
--measured	---	---	---	---	---	---	---
4-PARTY--flat	---	85	1,637	705	---	---	193
SUBURBAN--flat	---	---	---	---	285	---	370
FARMER LINE--flat	---	---	---	---	---	---	---
KEY--flat	---	---	---	---	0	---	---
--measured	---	---	---	---	---	---	---
MULTILINE--flat	---	---	---	---	---	---	---
--measured	---	---	---	---	---	---	---
BUSINESS							
1-PARTY--flat	543	---	1,887	590	83	1,050	860
--measured	---	8,246	---	---	225	---	---
2-PARTY--flat	86	---	76	---	---	---	6
--measured	---	---	---	---	---	---	---
4-PARTY--flat	---	---	62	40	---	---	9
SEMI-PUBLIC COIN	10	138	1	12	8	10	32
SUBURBAN--flat	---	---	---	---	---	---	0
FARMER LINE--flat	---	---	---	---	---	---	---
KEY--flat	94	---	0	50	22	19	---
--measured	---	---	---	---	32	---	---
PBX--flat	56	---	46	42	0	---	129
--measured	---	659	---	---	0	---	496
MULTILINE--flat	---	---	---	---	---	---	---
--measured	---	---	---	---	---	---	---
FEX							
RESIDENCE							
1-PARTY--flat	---	---	---	---	76	0	0
--measured	---	1,440	---	---	---	---	---
2-PARTY--flat	---	---	---	---	---	---	---
4-PARTY--flat	---	---	---	---	---	---	---
SUBURBAN--flat	72	---	---	---	---	1	---
FARMER LINE--flat	---	---	---	---	---	---	---
BUSINESS							
1-PARTY--flat	---	---	---	---	---	0	---
--measured	21	1,168	0	2	0	---	---
--message	---	---	---	---	---	---	0
2-PARTY--flat	---	---	---	---	---	---	---
4-PARTY--flat	---	---	---	---	---	---	---
FARMER LINE--flat	---	---	---	---	---	---	---
KEY--flat	---	---	---	---	---	---	---
--measured	---	---	---	---	---	---	---
--message	---	---	---	---	---	---	---
PBX--flat	---	---	---	---	---	---	---
--measured	---	142	---	0	---	---	---
--message	---	---	---	---	---	---	---

APPENDIX D
SHEET 4 OF 6
PRESENT RATES
FOR BASIC EXCHANGE SERVICES

	CALAVERAS	CAL-ORE:D&M	CAL-ORE:N&T	CAPAY VALLEY	CITIZENS	CONTEL	CP/NATL.
LOCAL							
RESIDENCE							
1-PARTY--flat	$5.00	$12.95	$5.50	$10.00	$12.75	$13.50	$10.80
--measured	---	---	---	---	7.00	8.50	7.80
2-PARTY--flat	4.00	11.95	4.10	9.75	10.85	11.40	9.15
--measured	---	11.95	---	---	---	---	---
4-PARTY--flat	---	---	---	---	8.95	11.40	8.55
SUBURBAN--flat	4.00	---	---	---	11.75	---	9.70
FARMER LINE--flat	---	---	---	---	5.00	1.40	2.75
KEY--flat	---	---	---	---	12.75	23.15	10.80
--measured	---	---	---	---	---	8.50	---
MULTILINE--flat	---	---	---	---	---	23.15	---
--measured	---	---	---	---	---	8.50	---
BUSINESS							
1-PARTY--flat	$6.00	$19.75	$10.25	$21.50	$24.90	$36.10	$22.25
--measured	---	---	---	---	22.10	31.65	18.25
2-PARTY--flat	5.00	17.25	7.60	21.25	---	29.00	17.90
--measured	---	17.25	---	---	---	---	---
4-PARTY--flat	---	---	---	---	---	29.00	---
SEMI-PUBLIC COIN	1.50	19.75	10.25	23.55	29.60	36.10	27.80
SUBURBAN--flat	5.00	---	---	---	22.70	---	19.00
FARMER LINE--flat	---	---	---	---	7.50	1.85	4.50
KEY--flat	---	19.75	15.20	21.50	37.25	52.90	22.25
--measured	---	---	---	---	22.10	31.65	18.25
PBX--flat	9.00	29.65	15.20	32.25	37.25	52.90	33.45
--measured	---	---	---	---	22.10	31.65	18.25
MULTILINE--flat	---	---	---	---	---	52.90	---
--measured	---	---	---	---	---	31.65	---
FEX							
RESIDENCE							
1-PARTY--flat	---	---	---	---	10.00	4.05	8.30
--measured	---	---	---	---	5.00/14.00/34.00	4.05	---
2-PARTY--flat	---	---	---	---	---	4.05	---
4-PARTY--flat	---	---	---	---	---	3.50	---
SUBURBAN--flat	5.75	---	---	---	7.00	3.50	---
FARMER LINE--flat	---	---	---	---	---	9.75	---
BUSINESS							
1-PARTY--flat	---	---	---	---	22.00	45.75	16.70
--measured	---	---	---	---	6.00/17.00/41.00/4.00	45.75	---
--message	---	---	---	---	4.00	---	---
FARMER LINE--flat	---	---	---	---	---	17.00	---
KEY--flat	---	---	---	---	22.00	---	---
--measured	---	---	---	---	6.00/17.00/41.00	45.75	---
--message	---	---	---	---	4.00	---	---
PBX--flat	---	---	---	---	23.75	45.75	---
--measured	---	---	---	---	7.75/18.75/42.75	---	---
--message	---	---	---	---	5.75	---	---

NOTE: RATES SHOWN DO NOT REFLECT EAS INCREMENTS, SRA INCREMENTS AND BILLING SURCHARGES

APPENDIX D
SHEET 5 OF 6
PRESENT RATES
FOR BASIC EXCHANGE SERVICES

	DUCOR	EVANS--LPW	EVANS--SA	FORESTHILL	GENERAL	HAPPY VALLEY	HORNITOS	KERMAN
LOCAL								
RESIDENCE								
1-PARTY--flat	$13.50	$10.90	$18.90	$7.65	$9.75	$5.50	$7.00	$14.80
--measured	---	---	---	---	5.25	---	---	---
2-PARTY--flat	---	10.65	---	5.25	8.70	11.45	6.40	14.75
--measured	---	---	---	---	---	---	---	---
4-PARTY--flat	---	---	---	7.75	---	3.90	5.50	---
SUBURBAN--flat	---	---	---	---	8.70	4.65	6.00	---
FARMER LINE--flat	---	---	---	---	3.65	---	2.25	---
KEY--flat	---	---	---	---	---	---	---	---
--measured	---	---	---	---	---	---	---	---
MULTILINE--flat	---	---	---	---	---	---	---	---
--measured	---	---	---	---	---	---	---	---
BUSINESS								
1-PARTY--flat	$20.75	$21.60	$32.60	$12.55	$21.70	$8.75	$10.00	$26.50
--measured	---	---	---	---	9.10	---	---	---
2-PARTY--flat	---	21.10	---	23.60	---	7.00	---	25.35
--measured	---	---	---	---	---	---	---	---
4-PARTY--flat	---	---	---	---	---	29.15	---	---
SEMI-PUBLIC COIN	28.50	24.30	24.30	12.55	26.45	1.25	5.00	26.50
SUBURBAN--flat	---	---	---	---	18.45	6.50	7.50	---
FARMER LINE--flat	---	---	---	---	7.25	---	2.25	---
KEY--flat	20.75	---	---	12.55	---	---	---	---
--measured	---	---	---	---	---	---	---	---
PBX--flat	31.15	29.30	29.30	18.85	32.70	---	---	26.50
--measured	---	---	---	---	9.10	---	---	---
MULTILINE--flat	---	---	---	---	---	---	---	---
--measured	---	---	---	---	---	---	---	---
FEX								
RESIDENCE								
1-PARTY--flat	---	11.00	---	8.00	5.00	---	---	14.00
--measured	---	---	---	---	5.00	---	---	14.00
2-PARTY--flat	---	---	---	---	---	---	---	---
4-PARTY--flat	---	---	---	---	---	---	---	---
SUBURBAN--flat	---	---	---	---	4.00	---	---	10.00
FARMER LINE--flat	---	---	---	---	4.00	---	---	---
BUSINESS								
1-PARTY--flat	20.00	16.35	---	10.00	31.55	---	---	---
--measured	---	---	---	---	31.55	---	---	18.50
--message	---	---	---	---	---	---	---	---
FARMER LINE--flat	---	---	---	---	7.50	---	---	---
KEY--flat	---	---	---	---	---	---	---	---
--measured	---	---	---	---	---	---	---	---
--message	---	---	---	---	---	---	---	---
PBX--flat	---	---	---	---	31.55	---	---	---
--measured	---	---	---	---	31.55	---	---	---
--message	---	---	---	---	---	---	---	---

NOTE: RATES SHOWN DO NOT REFLECT EAS INCREMENTS, SRA INCREMENTS AND BILLING SURCHARGES

APPENDIX D
SHEET 6 OF 6
PRESENT RATES
FOR BASIC EXCHANGE SERVICES

	PINNACLES	PONDEROSA	ROSEVILLE	SIERRA	SISKIYOU	TUOLUMNE	VOLCANO	WEST COAST
LOCAL								
RESIDENCE								
1-PARTY--flat	$10.70	$17.85	$11.20	$9.75	$7.60	$13.20	$7.55	$8.55
--measured	---	---	7.20	---	---	8.95	---	---
2-PARTY--flat	---	13.75	8.85	8.25	---	---	---	6.85
--measured	---	---	---	---	---	---	---	---
4-PARTY--flat	10.70	---	7.45	7.25	7.20	---	---	5.50
SUBURBAN--flat	10.70	---	---	---	---	13.10	---	6.30
FARMER LINE--flat	---	---	---	---	---	---	---	---
KEY--flat	---	---	---	---	---	13.20	---	---
--measured	---	---	---	---	---	---	---	---
MULTILINE--flat	---	---	---	---	---	---	---	---
--measured	---	---	---	---	---	---	---	---
BUSINESS								
1-PARTY--flat	$20.00	$33.90	---	$16.50	$9.75	$26.10	$12.85	$17.05
--measured	---	---	15.00	---	---	22.10	---	---
2-PARTY--flat	---	27.25	---	15.75	---	---	---	13.70
--measured	---	---	---	---	---	---	---	---
4-PARTY--flat	---	---	---	10.75	9.25	---	---	11.95
SEMI-PUBLIC COIN	---	33.00	21.90	23.50	17.90	31.75	13.00	17.10
SUBURBAN--flat	20.00	---	---	---	---	---	---	11.95
FARMER LINE--flat	---	---	---	---	---	---	---	---
KEY--flat	20.00	33.90	---	16.50	10.15	26.10	12.85	---
--measured	---	---	---	---	---	22.10	---	---
PBX--flat	30.00	45.30	---	16.50	14.95	41.35	---	34.20/25.55
--measured	---	---	15.00	---	---	22.10	---	---
MULTILINE--flat	---	---	---	---	---	---	---	---
--measured	---	---	---	---	---	---	---	---
FEX								
RESIDENCE								
1-PARTY--flat	---	---	---	---	---	9.30	2.50	7.30
--measured	---	---	14.40	---	---	---	---	---
2-PARTY--flat	---	---	---	---	---	---	---	---
4-PARTY--flat	---	---	---	---	---	---	---	---
SUBURBAN--flat	---	16.11	---	---	---	---	2.00	---
FARMER LINE--flat	---	---	---	---	---	---	---	---
BUSINESS								
1-PARTY--flat	---	---	---	---	---	---	5.00	---
--measured	---	30.95	30.00	10.45	9.75	18.60	---	---
--message	---	---	---	---	---	---	---	22.15
FARMER LINE--flat	---	---	---	---	---	---	---	---
KEY--flat	---	---	---	---	---	---	---	---
--measured	---	---	---	---	---	---	---	---
--message	---	---	---	---	---	---	---	---
PBX--flat	---	---	---	---	---	---	---	---
--measured	---	---	30.00	---	14.95	---	---	---
--message	---	---	---	---	---	---	---	---

NOTE: RATES SHOWN DO NOT REFLECT EAS INCREMENTS, SRA INCREMENTS AND BILLING SURCHARGES

APPENDIX E
SHEET 1 of 7
PACIFIC BELL
BILLING BASES AND ADJUSTMENTS TO BILLING
BASES FOR INDEPENDENT TELEPHONE COMPANIES

	INTRALATA				
COMPANIES	1986 BILLING BASE	MTS EFFECTS	TOLL PRIVATE LINE EFFECTS	ZUM EFFECTS	ADJUSTED 1986 BILLING BASE (excl. EXCHANGE)
	(a)	(b)	(c)	(d)	(e) = (a+b+c+d)
1. CALAVERAS	357,195	(10,789)	0	0	346,406
2. CAL-OREGON	514,680	(9,670)	0	0	505,010
3. CP NATIONAL	3,554,286	(93,070)	0	0	3,461,216
4. CAPAY VALLEY	143,000	(4,690)	0	0	138,310
5. CITIZENS	21,291,697	(243,126)	536	(45,751)	21,003,356
6. CONTINENTAL	124,115,952	(2,186,627)	44,257	0	121,973,582
7. DUCOR	195,435	(4,210)	0	0	191,225
8. EVANS	2,484,551	(47,737)	0	0	2,436,814
9. FORESTHILL	645,615	(18,892)	0	0	626,723
10. GENERAL	1,596,898,000	(25,978,735)	1,158,613	(12,157,064)	1,559,920,814
11. HAPPY VALLEY	496,882	(10,155)	0	0	486,727
12. HORNITOS	90,685	(2,907)	0	0	87,778
13. KERMAN	1,600,859	(19,461)	0	0	1,581,398
14. PINNACLES	32,290	(1,356)	0	0	30,934
15. PONDEROSA	2,328,767	(51,842)	0	0	2,276,925
16. ROSEVILLE	21,251,926	(226,987)	0	(347,562)	20,677,377
17. SIERRA	3,430,100	(75,369)	0	0	3,354,731
18. SISKIYOU	976,800	(25,703)	413	0	951,510
19. TUOLUMNE	1,451,820	(38,111)	0	0	1,413,709
20. VOLCANO	1,500,225	(27,450)	0	0	1,472,775
21. WEST COAST	2,790,071	(57,112)	479	0	2,733,438
22. Total	1,786,150,836	(29,133,999)	1,204,298	(12,550,378)	1,745,670,757

APPENDIX F
Sheet 1 of 2
PACIFIC BELL
DEVELOPMENT OF CUSTOMER BILLING SURCHARGES
DUE TO CHANGES TO CUSTOMER BILLING BASE

($000)

LINE	DESCRIPTION	INTERLATA ACCESS	INTRALATA TOLL	INTRALATA EXCHANGE	TOTAL INTRALATA	TOTAL INTRASTATE
1	1986 Billing Base Adopted in D.86-03-049	$1,160,324	$2,089,830	$2,746,416	$4,836,246	$5,996,570
2	1986 Billing Base Adopted in D.86-03-049 & Adjusted by Advice Letter (AL) 15190	1,080,724	2,089,830	2,746,416	4,836,246	5,916,970
3	Change in 1986 Billing Base due to Rate Design	(10,615)	(73,721)	71,408	(2,313)	(12,928)
4	Adjusted 1986 Billing Base (L2+L3)	1,070,109	2,016,109	2,817,824	4,833,933	5,904,042
	Applicable Rev. Req./Surcharge Yields:					
5	D.86-03-049 (Phase I)	(27,235)	51,913	68,224	120,137	$92,902
6	AL 15190 (InterLATA Direct Assign. of WATS)	--	34,397	45,203	79,600	79,600
7	D.87-12-067 (Phase II R.O. excl. IntraLATA SPF-SLU and Direct Assign. of WATS)	(30,478)	(58,954)	(77,482)	(136,436)	(166,914)
8	Subtotal (L5+L6+L7)	(57,713)	27,356	35,945	63,301	5,588
9	Present Surcharge (L8/L2)	-5.340%	1.309%	1.309%		
10	Adopted Surcharge (L8/L4)	-5.393%	1.357%	1.276%		
11	1987 Billing Base Adopted in 1987 Attrition-Resolution T-12007 (AL 15215B)	1,304,501	2,293,718	3,123,066	5,416,784	6,721,285
12	1987 Billing Base Adopted in 1987 Attrition and Adjusted by AL 15325	1,207,766	2,293,718	3,123,066	5,416,784	6,624,550
13	Adjusted 1987 Billing Base ((L12/L2)*L4)	1,195,903	2,212,805	3,204,267	5,417,072	6,612,975
	Applicable Rev. Req./Surcharge Yields:					
14	AL 15215B (1987 Attrition)	(37,078)	(65,195)	(88,768)	(153,963)	(191,041)
15	AL 15253	--	(25)	(34)	(59)	(59)
16	AL 15325 (1988 InterLATA/SPF-SLU)	--	41,455	56,445	97,900	97,900
17	AL 15356 (1986 & 1988 IntraLATA SPF-SLU & Direct Assign. of WATS)	--	--	(14,635)*	(14,635)	(14,635)
18	Subtotal (L14+L15+L16+L17)	(37,078)	(23,765)	(46,992)	(70,757)	(107,835)
19	Present Surcharge (L18/L12) **	-3.272%	-1.036%	-1.505%		
20	Adopted Surcharge (L18/L13) **	-3.329%	-1.074%	-1.467%		
21	TOTAL PRESENT SURCHARGE (L9+L19) ***	-8.611%	0.276%	-0.193%		
22	TOTAL ADOPTED SURCHARGE (L10+L20)	-8.722%	0.283%	-0.191%		

* Full year settlements effects adjusted for the period from 1/1/88 to 4/10/88.
** Surcharge for access reflects adjustments due to reduction in access billings resulted from AL 15325.
*** Discrepancies are due to rounding.

APPENDIX F
Sheet 2 of 2
PACIFIC BELL
DEVELOPMENT OF CUSTOMER BILLING SURCHARGES
DUE TO CHANGES TO CUSTOMER BILLING BASE

($000)

LINE	DESCRIPTION	INTERLATA ACCESS	INTRALATA TOLL	INTRALATA EXCHANGE	TOTAL INTRALATA	TOTAL INTRASTATE
1	1986 Billing Base Adopted in D.86-03-049	$1,160,324	$2,089,830	$2,746,416	$4,836,246	$5,996,570
2	1986 Billing Base Adopted in D.86-03-049 & Adjusted by Advice Letter (AL) 15190	1,080,724	2,089,830	2,746,416	4,836,246	5,916,970
3	Change in 1986 Billing Base due to Rate Design	(10,615)	(73,721)	71,408	(2,313)	(12,928)
4	Adjusted 1986 Billing Base (L2+L3)	1,070,109	2,016,109	2,817,824	4,833,933	5,904,042
	Applicable Rev. Req./Surcharge Yields:					
5	D.86-03-049 (Phase I)	(27,235)	51,913	68,224	120,137	92,902
6	AL 15190 (InterLATA Direct Assign. of WATS)	--	34,397	45,203	79,600	79,600
7	D.87-12-067 (Phase II R.O. excl. IntraLATA SPF-SLU and Direct Assign. of WATS and One-time Rev. Req. Reduction of $108.1M)	(10,751)	(20,796)	(27,331)	(48,127)	(58,878)
8	Subtotal (L5+L6+L7)	(37,986)	65,514	86,096	151,610	113,624
9	Present Surcharge (L8/L2)	-3.515%	3.135%	3.135%		
10	Adopted Surcharge (L8/L4)	-3.550%	3.250%	3.055%		
11	1987 Billing Base Adopted in 1987 Attrition-Resolution T-12007 (AL 15215B)	1,304,501	2,293,718	3,123,066	5,416,784	6,721,285
12	1987 Billing Base Adopted in 1987 Attrition and Adjusted by AL 15325	1,207,766	2,293,718	3,123,066	5,416,784	6,624,550
13	Adjusted 1987 Billing Base ((L12/L2)*L4)	1,195,903	2,212,805	3,204,267	5,417,072	6,612,975
	Applicable Rev. Req./Surcharge Yields:					
14	AL 15215B (1987 Attrition)	(37,078)	(65,195)	(88,768)	(153,963)	(191,041)
15	AL 15253	--	(25)	(34)	(59)	(59)
16	AL 15325 (1988 InterLATA SPF-SLU)	--	41,455	56,445	97,900	97,900
17	AL 15356 (1986 & 1988 IntraLATA SPF-SLU & Direct Assign. of WATS)	--	--	(19,198)*	(19,198)	(19,198)
18	Subtotal (L14+L15+L16+L17)	(37,078)	(23,765)	(51,555)	(75,320)	(112,398)
19	Present Surcharge (L18/L12) **	-3.272%	-1.036%	-1.651%		
20	Adopted Surcharge (L18/L13) **	-3.329%	-1.074%	-1.609%		
21	TOTAL PRESENT SURCHARGE (L9+L19) ***	-6.785%	2.102%	1.487%		
22	TOTAL ADOPTED SURCHARGE (L10+L20)	-6.879%	2.176%	1.446%		

* Full year settlements effects.

** Surcharge for access reflects adjustments due to reduction in access billings resulted from AL 15325.

*** Discrepancies are due to rounding.