CACD/BVC

Decision 90-09-079 September 25, 1990

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Contel of California, Inc. (U 1003 C), a corporation for an order authorizing it to issue and sell up to $30,000,000 of long-term indebtedness and for exemption from competitive bidding.	Application 90-07-047 (Filed July 20, 1990)

OPINION

Summary of Decision

This decision grants Contel of California, Inc. (Contel) the authority requested in the application.

Contel requests authority under Sections 816 through 830 and 851 of the California Public Utilities Code (PU Code), for the following:

1. To issue and sell a new series of Contel's First Mortgage Bonds in the aggregate principal amount of $30,000,000;
2. To execute and deliver a supplemental indenture to its First Mortgage Indenture, dated as of February 1, 1954;
3. To sell the proposed issue by negotiated private placement;
4. Exemption from the Commission's Competitive Bidding Rule for the proposed issue; and
5. To use the net proceeds for the purposes set forth in the application.

Notice of the filing of the application appeared on the Commission's Daily Calendar of July 25, 1990. No protests have been received.

Contel, a California corporation, and the wholly owned subsidiary of Contel Corporation, a Delaware corporation, owns and operates telephone systems in various portions of California, Nevada and Arizona, providing exchange telephono service for its local customers and exchange access service to interexchange carriers. Contel is a public utility subject to the jurisdiction of this Commission.

For the calendar year 1989, Contel's Schedule V to its supplementary data filed with the application shows total operating revenue of $356,524,000, of which $328,699,000 was derived from California operations, and total operating income of $73,150,000.

Exhibit A, attached to the application, presents Contel's Condensed Balance Sheet as of December 31, 1989, summarized as follows:

Assets	Amount
Net Utility Plant	$483,159,000
Current Assets	98,887,000
Deferred Debits	11,444,000
Total	$593,490,000

Liabilities and Equity	Amount
Common Equity	$236,583,000
Preferred Stock	2,105,000
Long-Term Debt	138,785,000
Current Liabilities	149,698,000
Deferred Credits	66,319,000
Total	$593,490,000

Proposed Financing

Contel proposes to issue $30,000,000 aggregate principal amount of a new series of its First Mortgage Bonds (Bonds), to provide funds to finance in part its planned construction program for 1990 and/or to be applied to the reimbursement of its treasury for construction expenditures not previously funded through external financing. Contel's 1990 gross construction program totals approximately $73,575,000, and at March 31, 1990, Contel had $263,283,000 of unreimbursed treasury.

Contel states that it believes that by increasing its percentage of long-term debt it will benefit its customers by lowering its overall cost of capital. Contel further believes that the interest rate on the proposed Bonds is reasonable, given current long-term debt market conditions.

Subject to the entry of the final order requested in the application, Contel, with the assistance of its investment bankers, First Chicago National Bank, has negotiated for the sale of the Bonds by private placement with a single major institutional purchaser, Allstate Insurance Company. The proposed Bonds will be designated "First Mortgage Bonds, Series X, (9.44%) due 2015," will bear interest at 9.44% perannum, and mature on October 15, 2015. The Bonds will be non-callable for 10 years and callable thereafter at gradually reducing premiums. The purchase price will be 100% of the aggregate principal amount thereof, plus accrued interest, if any, to the date of closing. For its assistance in the transaction, Contel has agreed to pay its investment bankers a fee of .375% of the principal amount of the Bonds (or $112,500).

The Bonds will be issued in accordance with, secured by, and have terms and conditions as set forth in the Indenture dated February 1, 1954, executed and delivered by Contel to Bank of America National Trust and Savings Association and successor individual trustee, as Trustees, as amended to date by twenty-five supplemental indentures, and the proposed supplemental indenture. The proposed supplemental indenture will be substantially similar to the form of the Twenty-Fifth Supplemental Indenture filed with the Commission in connection with Application 89-07-039 (filed July 9, 1989), except for those changes necessary to reflect the designation and series, aggregate principal amount, interest rate, maturity, sinking fund requirements, and other terms negotiated for the proposed Bonds.

The purchase agreement to be used in connection with the sale of the Bonds will be substantially similar to the form of purchase agreement used in connection with Contel's Series W Bonds, except for changes similar to those required in the supplemental indenture providing for the Bonds.

Exemption from the Commission's Competitive Bidding Rule

Contel states that the Bonds are entitled to an exemption from the Competitive Bidding Rule under Paragraph (3) of the Order contained in Resolution No. F-616 (dated October 1, 1986). A sale of the entire issue of the Bonds to one major institutional investor can not be accomplished through a competitive bidding process. The Staff Report attached to Resolution No. F-616 recognized this fact (see page 5, lines 16-17). The application states that, by dealing with a single purchaser, Contel is able to negotiate terms which are tailored to the needs of the purchaser, while at the same time producing terms (both as to interest rate and maturity) which are more favorable to Contel than those available through a public offering and sale; based on Contel's extensive review of current market conditions, it is convinced that the interest rate on the Bonds is 10 basis points lower, and avoiding the printing, legal, accounting, and SEC registration fee expenses, and other miscellaneous costs, and the delay of a public sale (a savings of approximately $250,000). In addition, the private placement fee is 37.5 basis points less than the spread which might be expected with a public sale.

Contel states that the sale of the Bonds in the manner proposed will produce the lowest effective interest cost, for the benefit of both Contel and its ratepayers, and that the exemption from competitive bidding is in the public interest.

The Commission Advisory and Compliance Division (CACD) has reviewed Contel's request and reasons for an exemption from the Competitive Bidding Rule. The CACD has determined that Contel has made a compelling showing that the exemption as requested is warranted and recommends that Contel's request be granted.

CACD notes and we concur that this decision does not find these costs or the proposed costs of this debt issue to be reasonable for ratemaking purposes. We place Contel on notice that in its next general rate proceeding before the Commission, the reasonableness of the interest rate and cost of money resulting from the issuance of the Bonds will be closely scrutinized and may result in a disallowance of the interest expense, if it is determined that the cost of money incurred was not prudent. We will also require Contel to provide us with a showing of why Contel believes that the resulting interest rate and cost of money were advantageous to Contel and its ratepayers. We will require this showing within a reasonable period of time after issuance of its Bonds.

Use of Proceeds

Contel proposes to use the proceeds of the Bonds, other than accrued interest and after payment of expenses of issuance, for one or more of the following purposes:

(a) For the acquisition of property;

(b) For the construction, completion, extension or improvement of its facilities;

(c) For the improvement or maintenance of its services;

(d) For the lawful refunding of its obligations; and

(e) For the reimbursement of its treasury for money actually expended for the foregoing purposes from income or from other money in its treasury not secured by or obtained from the issue of stocks, stock certificates or other evidences of interest or ownership, or bonds, notes or other evidences of indebtedness. In addition, a portion of such proceeds may be used to repay short-term indebtedness incurred for the foregoing purposes.

Capital Ratios

Contel's capital ratios as of June 30, 1990 are shown below, as recorded and as adjusted to give *pro forma* effect to the proposed financing and planned long-term debt and preferred stock retirements in 1990:

	Recorded		Pro Forma	
	Amount	Percentage	Amount	Percentage
Common Equity	$238,344,000	61.0%	$238,344,000	61.0%
Pref. Stock	2,330,000	.6	2,105,000	.5
Long-Term Debt	149,772,000	38.4	150,193,000	38.5
Totals	$390,446,000	100.0%	$390,642,000	100.0%

Contel is placed on notice, by this decision, that the Commission does not find that its capital ratios are necessary or reasonable for ratemaking purposes. These are issues which are normally tested in general rate cases or cost of capital proceedings.

Construction Budget

Contel's gross construction budgets for calendar years 1990 and 1991 amount to approximately $141,419,000, summarized as follows:

Item	1990	1991
Land	$ 483,000	$ 216,000
Vehicle/Aircraft	1,731,000	2,101,000
Building	3,223,000	1,133,000
COE-Digital	22,023,000	12,411,000
COE-All Other	6,917,000	7,464,000
Outside Plant	26,702,000	30,394,000
All Other Plant	12,496,000	14,125,000
Total	$73,575,000	$67,844,000

The CACD has reviewed the application and Contel's construction program. The CACD concludes that the proposed financing is necessary to fund the proposed retirement of Contel's long-term indebtedness, payment of the preferred stock sinking fund requirements in 1990 and construction program; however, Contel is placed on notice, by this decision, that the Commission does not find that Contel's construction program is necessary or reasonable for rate making purposes. These are issues normally tested in general rate or rate base offset proceedings.

Cash Requirements Forecast

Contel's cash requirements, for the years 1990 and 1991 estimated as of March 31, 1990 and shown as part of the supplemental data furnished to the CACD, are shown as follows:

	1990	1991
Funds used and/or Required for Construction Expenditures	$73,575,000	$ 67,844,000
L-T Debt & Pref. Stk. Redempt.	29,804,000	12,298,000
Short-Term Debt as of Beginning of Year	-0-	-0-
Less:		
Cash from Internal Sources	81,167,000	118,822,000
Additional Funds Required From Outside Sources	$22,212,000	$(38,680,000)

The CACD notes that for Contel's cash requirements forecasts for 1990 and 1991 internally generated funds will provide approximately $81,167,000 or 78.51% of capital requirements in 1990 and approximately $118,822,000 or 148.26% in 1991. CACD concludes that Contel's proposed issuance and sale of the Bonds is necessary to help meet forecasted cash requirements.

Findings of Fact

1. Contel, a California corporation, operates as a public utility under the jurisdiction of this Commission.

2. Contel has need for external funds for the purposes set forth in the application.

3. The proposed issuance and sale of the Bonds are for proper purposes and not adverse to the public interest.

4. The money, property, or labor to be procured, or paid for, by the proposed Bonds is reasonably required for the purposes specified in the application, and such purposes are not, in whole or in part, reasonably chargeable to operating expenses or to income.

5. There is no known opposition and there is no reason to delay granting the authority requested.

Conclusions of Law

1. A public hearing is not necessary.

2. The application should be granted to the extent set forth in the order which follows.

The proposed Bonds are for lawful purposes and the money, property, or labor to be obtained by them is required for these purposes. Proceeds from the Bonds are not reasonably chargeable to operating expenses or to income.

The following order shall be effective on the date of signature and payment of a fee set by §1904(b) of the PU Code to enable Contel to proceed with its financing expeditiously.

O R D E R

IT IS ORDERED that:

1. Contel of California, Inc. (Contel), on or before December 31, 1991, is authorized to issue, sell and deliver not exceeding $30,000,000 aggregate principal amount of a new series of Contel's First Mortgage Bonds (Bonds), by negotiated private placement, on terms and conditions substantially consistent with those described in or contemplated by the application and such additional terms and conditions to be negotiated by Contel customary for an issue such as the Bonds.

2. Contel is authorized to execute and deliver a supplemental indenture in substantially the same form as its Twenty-Fifth Supplemental Indenture filed in connection with Application 89-07-039, with such changes as are required to reflect the terms and conditions negotiated for the Bonds.

3. Contel shall use the net proceeds from the sale of the Bonds for the purposes set forth in the application.

4. Contel shall file with CACD copies of the purchase agreement and any related agreements, within 15 days after the documents have been executed.

5. Contel shall file with CACD a report showing why the resulting interest rate and cost of money were the most advantageous to Contel and its ratepayers within 15 days after the issuance and sale of its Bonds by means of a negotiated private placement.

6. Contel shall file with CACD copies of the supplemental indenture within 15 days after the sale of the Bonds.

7. Contel shall file the reports required by General Order Series 24.

8. The application is granted as set forth above.

The authority granted by this order shall become effective when Contel pays $392, the fee set forth by Public Utilities Code §1904(b). In all other respects this order is effective today.

Dated September 25, 1990, at San Francisco, California.

G. MITCHELL WILK
President
FREDERICK R. DUDA
STANLEY W. HULETT
PATRICIA M. ECKERT
Commissioners

Commissioner John B. Ohanian, being necessarily absent, did not participate.

PUBLIC UTILITIES COMMISSION
STATE OF CALIFORNIA
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I CERTIFY THAT THIS DECISION WAS APPROVED BY THE ABOVE COMMISSIONERS TODAY

NEAL J. SHULMAN, Executive Director
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