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Decision 90-10-039 October 12, 1990

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of Alternative
Regulatory Frameworks for Local
Exchange Carriers.

I.87-11-033
(Filed November 25, 1987)

In the Matter of the Application
of Pacific Bell (U 1001 C), a
corporation, for authority to
increase 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)

Application of General Telephone
Company of California (U 1002 C), a
California corporation, for authority
to increase and/or restructure
certain intrastate rates and charges
for telephone services.

Application 87-01-002
(Filed January 5, 1987)

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)

I.87-02-025
(Filed February 11, 1987)

C.87-07-024
(Filed July 16, 1987)

A.88-07-020
(Filed July 15, 1988)

(See Appendix A in Decision 88-08-024,
Attachment D in Decision 89-10-031, and Appendix A in
Decision 90-04-023 for appearances.)

INTERIM OPINION ON PETITIONS FOR MODIFICATION OF D.89-12-048

In Decision (D.) 89-12-048 in Investigation (I.) 87-11-033, the Commission adopted revenue adjustments effective January 1, 1990 for Pacific Bell (Pacific) and GTE California Incorporated (GTEC) in order to implement the new incentive-based regulatory framework adopted in D.89-10-031 for these two local exchange carriers. Under the new framework, rates for Pacific's and GTEC's basic monopoly services and rate caps for flexibly priced services will be indexed annually according to the Gross National Product Price Index (GNP-PI) inflation index reduced by a productivity adjustment of 4.5%. Rate floors for flexibly priced services will be indexed annually according to the GNP-PI, with no productivity adjustment. The indexing formula also allows for rate adjustments for a limited category of exogenous factors (Z factors) whose effects are not reflected in the economywide GNP-PI.

Today's decision addresses petitions for modification of D.89-12-048 filed on April 9, 1990 by GTEC and on August 31, 1990 by the Commission's Division of Ratepayer Advocates (DRA). An application for rehearing of D.89-12-048 filed by Pacific was addressed in D.90-02-053 and D.90-04-031.

DRA Petition

DRA requests that D.89-12-048 be modified to order Pacific to include tax benefits resulting from early bond retirements as an exogenous or Z factor adjustment in its annual price cap advice letter filing due October 1, 1990.

DRA submits that flowing these tax benefits through to ratepayers would be consistent with D.89-10-031, in which the Commission stated:

"As a starting point, we accept the following [Z] factors: changes in federal and state tax laws to the extent they affect the local exchange carriers disproportionately, mandated jurisdictional separations, changes to intraLATA toll pooling arrangements or .

accounting procedures adopted by this Commission, changes in regulatory amortizations such as expensing of station connections, and reflection of tax benefits resulting from premature retirements of high coupon bonds pursuant to D.88-12-024. (D.89-10-031, mimeo. p. 182, emphasis added.)

DRA proposed last year in filings and workshops leading to D.89-12-048 that an adjustment for these tax benefits be made as part of the January 1, 1990 startup revenue adjustment, and Pacific did not oppose DRA on this issue. However, in D.89-12-048 we declined to reflect the tax benefits as part of the startup revenue adjustment because Commission review of the proposed adjustments was still pending in other proceedings.

DRA submits that requiring Pacific to flow through these tax savings would be consistent with the treatment given other utilities. Pacific and GTEC participated in workshops which developed the ratemaking treatment of bond redemption benefits for energy utilities and agreed to a consensus methodology for flowing through tax benefits to ratepayers which was adopted in D.89-11-068 for the energy utilities.

Subsequent to D.89-12-048, the Commission directed GTEC in D.90-05-083 in Application (A.) 87-01-002 to flow through its tax benefits using the workshop methodology adopted in D.89-11-068. As DRA notes, Pacific's comparable tax benefits are not being passed on to ratepayers because there has not yet been a Commission order requiring Pacific to do so. DRA reports that Pacific's tax benefits annualized amount to \$8.9 million for 28 years, and concludes that Pacific should be ordered to flow through these tax benefits to ratepayers.

In a response to DRA's petition, Pacific states that it does not oppose DRA's petition, provided that the Commission recognize that the adjustment fully resolves all issues involving the ratemaking treatment of these embedded tax benefits.

Because there is no reason to treat Pacific differently from the other utilities for which the Commission has adopted the workshop method for flowing through these tax benefits and because no party disputes Pacific's annualized tax benefit reported by DRA, DRA's petition should be granted to the extent provided in this order.

GTEC Petition

GTEC requests that the requirement for annual Z factor adjustments to reflect the continuing impact of the uniform system of accounts rewrite (USOAR) be deleted, asserting that this requirement is based on a misinterpretation of D.87-12-063' and D.88-09-030. According to GTEC, the impact of the USOAR was fully incorporated into GTEC's startup revenue requirement calculation as a result of D.89-12-048. Further, GTEC contends that it is unfair and discriminatory to single out this one past event for treatment as an exogenous event on a prospective basis when other events which have ongoing impacts on the company's revenue requirement (e.g., depreciation) are not given similar treatment.

As DRA and AT&T Communications of California, Inc. point out in their oppositions filed in response to GTEC's petition, we denied a similar request by Pacific in D.90-04-031. Just as we found regarding Pacific's request, GTEC has raised no new arguments which warrant the modification it seeks. As a result, GTEC's petition should be denied.

While we deny GTEC's petition, additional comments regarding future USOAR adjustments are appropriate. We would be willing to entertain proposals to assess the remaining USOAR impacts and reflect such impacts in rates, e.g., through a one-year present-value rate adjustment or an annuity-like rate adjustment similar to the adjustment for tax benefits resulting from early bond retirements. We note that DRA made similar recommendations in both the USOA proceeding and in its startup revenue adjustment filings.

Findings of Fact

1. In D.89-11-068 the Commission ordered energy utilities to flow through to ratepayers tax benefits realized due to early bond retirements in accordance with a consensus methodology agreed to in workshops.

2. Pacific and GTEC participated in the energy utility workshops and agreed with the workshop methodology.

3. In D.89-10-031 the Commission found that tax benefits resulting from premature retirements of high coupon bonds should be reflected as exogenous factors in the adopted price cap indexing mechanism.

4. In D.89-12-048 the Commission declined to reflect the tax benefits resulting from premature retirements of high coupon bonds as part of the January 1, 1990 startup revenue adjustment because Commission review of the proposed adjustments was pending in other proceedings.

5. In D.90-05-083 the Commission directed GTEC to flow through its tax benefits due to premature retirements of high coupon bonds using the methodology adopted in D.89-11-068.

6. Pacific does not dispute that its annualized tax benefit due to premature retirement of high coupon bonds is \$8.9 million for 28 years, as reported by DRA.

7. There is no reason to treat Pacific differently from the other utilities for which the Commission has adopted the workshop methodology for calculating and passing through to ratepayers the tax benefits of bond refinancing.

8. In its petition for modification of D.89-12-048, GTEC raises no new arguments which warrant the modification it seeks.

Conclusions of Law

1. Because there is no reason to treat Pacific differently from the other utilities for which the Commission has adopted the workshop method for flowing through the tax benefits realized from early bond retirements, D.89-12-048 should be modified to direct Pacific to flow through to its ratepayers these tax benefits in accordance with the annuity developed for it in the workshops leading to D.89-11-068.

2. Because no party disputes Pacific's annualized tax benefit reported by DRA, the \$8.9 million tax benefit for a 28-year period beginning January 1, 1991 should be included as a Z factor adjustment in Pacific's price cap revenue adjustment effective January 1, 1991.

3. GTEC's petition to modify D.89-12-048 should be denied because GTEC raises no new arguments which warrant the modification it seeks.

4. In order to provide timely implementation of revenue changes adopted in this decision, this order should be effective today.

INTERIM ORDER

IT IS ORDERED that:

1. The petition for modification of Decision (D.) 89-12-048 filed by GTE California Incorporated is denied.

2. Findings of Fact 66a, 66b, and 66c are added to D.89-12-048 as follows:

66a. In D.90-05-083 the Commission directed GTEC to flow through the tax benefits of bond refinancing using the methodology adopted in D.89-11-068.

66b. Pacific does not dispute that its annualized tax benefit due to bond refinancing is \$8.9 million for 28 years, as reported by DRA.

- 66c. There is no reason to treat Pacific differently from the other utilities for which the Commission has adopted the workshop methodology for calculating and passing through to ratepayers the tax benefits of bond refinancing.

3. Conclusion of Law 29 in D.89-12-048 is modified to read as follows:

29. Benefits resulting from premature retirement of high coupon bonds should be excluded from startup revenue adjustments since the Commission did not review this issue prior to January 1, 1990. These tax benefits should be reflected in rates following Commission review.

4. Conclusions of Law 29a and 29b are added to D.89-12-048 as follows:

- 29a. Because there is no reason to treat Pacific differently from the other utilities for which the Commission has adopted the workshop method for flowing through the tax benefits realized from early bond retirements, Pacific should flow through to its ratepayers these tax benefits in accordance with the annuity developed for it in the workshops leading to D.89-11-068.

- 29b. Because no party disputes Pacific's annualized tax benefit reported by the Division of Ratepayer Advocates, the \$8.9 million tax benefit for a 28-year period beginning January 1, 1991 should be included as a Z factor adjustment in Pacific's price cap revenue adjustment effective January 1, 1991.

5. Ordering Paragraph 15 is added to D.89-12-048 as follows:

15. The \$8.9 million tax benefit for a 28-year period beginning January 1, 1991 shall be included as a Z factor adjustment in Pacific's price cap revenue adjustment effective January 1, 1991.

I.87-11-033 et al. ALJ/CLF/vdl

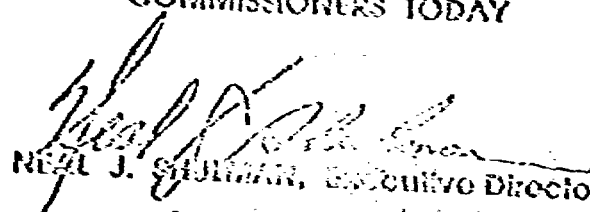
6. To the extent not otherwise granted by this order, the Division of Ratepayer Advocates' petition for modification of D.89-12-048 is denied.

This order is effective today.

Dated October 12, 1990, at San Francisco, California.

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

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


NEAL J. SULLIVAN, Executive Director