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Decision 91-03-016 March 13, 1991

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BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of AT&T Communications)	
of California Inc. (U 5002 C) for)	
Authority to Increase the Rate for)	Application 90-02-060
Intrastate InterLATA Directory)	(Filed February 26, 1990)
Assistance Service.)	
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OPINION

I. Summary of Decision

AT&T Communications of California, Inc. (AT&T-C) seeks authority to increase the price of directory assistance (DA) calls that are made within the State of California between the state's 10 local access and transport areas (interLATA) from 40 cents to 50 cents per call. AT&T-C's request is opposed by Toward Utility Rate Normalization (TURN) and by the Commission's Division of Ratepayer Advocates (DRA). Additionally, the Commission has received approximately 600 letters from ratepayers, the great majority of them opposing an increase in directory assistance charges.

We deny the application. We find that AT&T-C has failed to meet the burden imposed by Public Utilities (PU) Code § 454(a) of presenting a reasonable showing before the Commission that the proposed new rate is justified.

II. Introduction

Directory assistance is a subject mired in confusion. Many believe that calls for directory assistance are free, as was essentially the case prior to divestiture. Others believe that the first two to five calls per month are without charge. In fact, there are different charges for three basic types of directory assistance calls:

A. Local Information

Directory assistance calls within a caller's local exchange area (reached by dialing 411) are handled by a local exchange carrier like Pacific Bell (PacBell) or GTE California Incorporated (GTEC). Residential consumers may make five such calls per month without charge, after which each directory assistance call is billed at 25 cents. In (D.) 84-06-111, we noted

that these local directory assistance calls constitute the great bulk of DA services.

B. Long Distance Information

Directory assistance calls through AT&T¹ for numbers outside the state (reached by dialing an area code and 555-1212) are billed by AT&T at 60 cents per call, with no free call allowance.

C. Intrastate InterLATA Information

Directory assistance calls within California but outside a caller's local exchange area (for example, a call from San Francisco for Los Angeles DA) are billed by AT&T-C at 40 cents per call. AT&T-C provides no monthly free call allowance, but it does not charge for directory assistance calls made from pay phones, hotels and motels, and hospitals.

This application and proceeding deal only with this third category of directory assistance service, that is, directory assistance offered within the state but between local telephone exchange areas (intrastate interLATA).

III. Procedural Background

AT&T-C filed this application on February 26, 1990. Originally, the company asked authority to increase intrastate interLATA directory assistance calls from 40 cents to 60 cents. Additionally, AT&T-C asked pricing flexibility around the proposed price of 5 cents upward and 10 cents downward. The 60-cent rate was expected to increase AT&T-C revenues by \$6.5 million a year.

In the same filing, AT&T-C requested authority to reduce its price for the "additional minute" category of daytime, direct-dialed long distance calls traveling more than 150 miles within

1 AT&T is the parent corporation of AT&T-C.

California. This rate reduction was expected to reduce AT&T-C's revenues by \$6.5 million a year.

Protests and comments to AT&T-C's application were filed by DRA, GTEC, MCI Communications Corporation (MCI), and US Sprint Telecommunications Company Limited Partnership (US Sprint). While not objecting substantively to the directory assistance increase, DRA argued that the increase was not a pass-through of costs and that AT&T-C therefore was required by Rule 24 of the Commission's Rules of Practice and Procedure to notify ratepayers of the application.

On May 29, 1990, following a prehearing conference, AT&T-C was ordered to notify customers of the proposed increase in directory assistance rates. The notice appeared in telephone bills in July 1990.² Approximately 600 persons wrote to the Commission, the great majority of them objecting to the DA increase. The letters, while not part of the evidence in this proceeding, raise objections similar to those stated by DRA and TURN, including:

- o A caller uses directory assistance in order to call the number sought. There is an appearance of unfairness in charging the caller both for the information and for the call.
- o Subscribers are provided with a local telephone directory, but there is no alternative to directory assistance for obtaining non-local phone numbers.
- o Few understand that different charges apply for directory assistance on a local, intrastate, and interstate basis.

Meanwhile, on June 15, 1990, AT&T-C filed Advice Letter 168 to reduce, on 40 days' notice, a number of direct-dialed long

² AT&T reports that the cost of providing this notice was \$1.5 million.

distance charges. AT&T-C explained that the filing was made in response to rates offered by competitors. Since the long distance reductions incorporated those proposed in its earlier DA application, AT&T-C on June 22, 1990, amended the DA application to delete the long distance price reduction proposal.

On August 9, 1990, AT&T-C filed a motion for immediate approval of its request to increase directory assistance rates. At a prehearing conference on September 4, 1990, parties were directed to assess the reasonableness of AT&T-C's proposed increase, and an evidentiary hearing was set for November 14 through 16, 1990, to take evidence on AT&T-C's motion for an immediate directory assistance increase.

The hearing was conducted on November 14 and 15, 1990. AT&T-C, TURN, and DRA presented witnesses, and GTEC and US Sprint participated on a limited basis. At the hearing, AT&T-C further amended its application to reduce its request for a directory assistance increase from 20 cents to 10 cents. AT&T-C's witness explained that the reduction was based in part on (a) reduced access charges made by PacBell to AT&T-C for directory assistance service, and (b) AT&T-C's concern with the large number of objections from customers about the proposed increase.

At the close of evidence and oral arguments, AT&T-C agreed to withdraw the rate flexibility portion of its application so that both its motion and the application for a directory assistance increase could be submitted promptly for decision. The parties on November 16, 1990 agreed to the joint submission of the motion and the application.

IV. Positions of the Parties

A. AT&T-C

AT&T-C seeks an increase in directory assistance price from 40 cents to 50 cents while not seeking any charge for such

calls from hospitals, public and semipublic phones, and hotels or motels. The increase is necessary, AT&T-C states, in order to raise the price of directory assistance above the long-run incremental cost of providing this service. Christopher Ensign, California State Manager for AT&T-C, testified:

"If DA does not recover its own costs in the competitive interexchange market, those costs must be covered by other services, most obviously AT&T's Long Distance Service. However, competition does not allow AT&T to burden its Long Distance prices with such subsidies. AT&T's view is that the cost of DA calls should be recovered from those who actually place the calls. This will permit the prices that all AT&T customers pay for Long Distance Service to be as low as possible." (Transcript (Tr.) p. 40, prepared testimony, p. 4.)

Ensign stated that, at 40 cents, the total long-run incremental cost (that is, the cost over a one-year period) of providing directory assistance service is \$13,405,380, versus revenue for the same period of \$13,239,820, representing a loss of \$165,560 annually. At 50 cents, total long-run incremental cost would be \$14,570,270 versus revenues of \$16,549,730, representing a gain of \$1,979,460 annually. AT&T-C notes that the documentation on its costs has been furnished to DRA and to TURN, and that neither challenges the cost computation.

Directory assistance calls from hospitals, hotels and coin phones -- which are provided by AT&T-C without charge -- constitute about 17 % of all such calls³. Ensign explained that, originally, AT&T-C lacked the technical capability to charge for these calls. As of January 1, 1991, however, the company would have the technical capability to charge for these calls if it

³ This represents free service in the amount of about \$2.7 million at the current rate of 40 cents per call.

chooses to do so. For now, however, AT&T-C as a marketing strategy will continue to offer this directory assistance service without charge. Witness Ensign explained:

"[I]n looking at...the market for directory services, AT&T sees [a] distinct away-from-home market. And AT&T's strategy recognizes that the away-from-home market is even less likely to have available directory material ...such as personal directories or home directories....

"[I]t is AT&T's marketing strategy in terms of packaging its services. We believe that we can distinguish ourselves from other interexchange carriers by attracting or recognizing the away-from-home market differently."
(Tr. p. 45.)

AT&T-C notes that the Commission has cautioned the company about offering services, like directory assistance, at less than cost, because of the anticompetitive implications of that practice. In granting AT&T-C flexibility to increase or decrease the price of services within defined bands of reasonableness, the Commission in D.88-12-091 stated:

"As AT&T-C has pointed out, certain rates are currently below costs, notably directory assistance, because of prior Commission action. We expect AT&T-C to use the flexibility we grant it today to improve that situation, not make it worse." (Re Regulatory Framework for InterLATA Telecommunications Market (1988) 30 CPUC 2d384, 408.)

AT&T-C exhausted the flexibility given to it for directory assistance when it increased the price per call to 40 cents on January 1, 1989.

On cross-examination, Ensign testified further about the composition of AT&T-C's directory assistance service. He stated that AT&T-C receives approximately 40 million directory assistance calls annually. These divide roughly into 50% residential and 50% business. Approximately one-third of AT&T-C's business customers use directory assistance regularly, and these businesses average 14

such calls per month. Similarly, about one-third of residential customers use directory assistance regularly, and these customers average about four calls per month. The overall residential subscriber average was four intrastate interLATA DA calls per year. The median for residential customers is two such calls per month. (Tr. pp. 70-71.)

Of the 40 million intrastate interLATA DA calls annually, approximately 6.8 million are unbilled because they are from hospitals, hotels, and coin phones. Dividing the 33.2 million billed calls by the annual shortfall of approximately \$200,000 means that AT&T-C's loss per call is approximately six-tenths of a cent. Witness Ensign acknowledged that AT&T-C could recoup its costs by charging for calls that now are not billed. He also acknowledged that a one cent increase in the rate, from 40 to 41 cents, would permit the service to be offered at cost. (Tr. pp. 51, 64.) Ensign added, however, that such a price would not contribute to overhead or to profit and would not assist AT&T-C in marketing its entire package of services against those of competitors. He stated:

"Now, when you ask me do I view AT&T competing specifically for directory service with other interexchange carriers, my answer is that AT&T is competing with other interexchange carriers to attract customers to its package of services, and to the extent that we can price our directory service so that it covers costs and contributes to the profitability of the business, we can do other -- take other pricing actions with other portions or other elements of our services to attract more customers and improve the efficiency of providing our entire package of services..." (Tr. p. 52.)

B. Division of Ratepayer Advocates

DRA takes the position that an increase in AT&T-C's directory assistance rate should await the outcome of other cases. Specifically, DRA notes that AT&T-C has pending before the Commission its application (A.90-07-015) seeking greater pricing

flexibility than that provided in D.88-12-091. If all or part of that application is granted, AT&T-C presumably would be able to further reduce the price of some services and increase the cost of others, including directory assistance. DRA also points to its own petition for modification of D.88-12-091, in which it seeks to reduce AT&T-C rates based on what it believes to be excess earnings. (Tr. p. 86, prepared testimony, p. 2.)

DRA also takes note of what it terms "an extraordinary number" of letters from the public protesting a directory assistance increase.

Witness Dick Van Aggelen, a certified public accountant and a financial examiner for the DRA, stated that the DRA's position is that rates for directory assistance should be limited to cost, without provision for contribution to overhead or profit. He testified:

"In the past it has been the policy of DRA to advocate limiting rates for directory assistance service to cost. The rationale for that position is that DA service is a monopoly service and should not support detariffed or unregulated services. That general philosophy has been incorporated in rates for DA services provided by local exchange carriers. The nature of DA services is similar in the case of IECs. Even though there are competitors for basic directory assistance services, few people know how to access alternative services and the added access difficulty makes it impractical [to do so] in all but exceptional cases." (Tr. p. 121, prepared testimony, p. 3.)

On cross-examination, Witness Van Aggelen acknowledged that the recommendation to price directory assistance at cost is DRA's policy position, rather than a statement of how the Commission has dealt with directory assistance in the past.

Van Aggelen testified that, in his judgment, the 40-cent current rate "is a rate that will recover their costs..." He added that the costs submitted by AT&T-C to justify an increase include

an element for rate of return. (Tr. p. 210.) Nevertheless, he said, DRA did not originally oppose the application because the cost data supplied by the utility "would support the conclusion that the service is being offered below cost." Van Aggelen said that the original data showed that AT&T-C was losing a net \$.046 per directory assistance call at 40 cents per billable call. Subsequent testing through a modified Transport Incremental Cost Model (TICM) indicated a loss of \$.005 (1/2 cent) at 40 cents per billable call.

C. TURN

TURN presented two recommendations with respect to AT&T-C's directory assistance request. Witness Karen L. Miller, an economist who is a telecommunications program manager and analyst for the ratepayer organization, described these recommendations.

First, TURN notes that local exchange carriers, such as PacBell and GTEC, provide residential customers with five free directory assistance calls a month, with a charge of 25 cents per call above that allowance. In addition, directory assistance calls made outside of the customer's area code, but within the local access and transport area, are provided without charge and are not counted toward the customer's five-call allowance.

By contrast, Miller stated, there is no consistency among interexchange carriers, such as AT&T-C, MCI, and US Sprint within the state. AT&T-C charges 40 cents per call, with no charge for directory assistance calls from pay phones, hospitals, and hotels. MCI charges 39 cents per call, with two free calls per month if the customer completes two long distance calls in the same month. US Sprint charges 50 cents per call, with two free calls per month.⁴

⁴ AT&T notes that US Sprint's Advice Letter 54 proposes, among other things, to increase directory assistance calls to 60 cents and reduce the price of its directory assistance calls from public phones to 40 cents.

Because customers find it difficult to comparison shop among these differing DA services, TURN urges the Commission to deny or defer AT&T-C's application in favor of establishing a consistent DA policy for interexchange carriers in California. TURN proposes that all interexchange carriers in California be required to provide two free DA calls each month and charge no more than 40 cents a call thereafter.

Second, TURN "opposes granting AT&T-C any rate increase for any service at this time, given AT&T-C's excessive earnings." Miller notes the pendency of DRA's motion to reduce AT&T-C intrastate rates, and she asserts that it would be "inappropriate" to grant an increase in directory assistance rates at this time. Moreover, she asserted TURN's position that AT&T-C's request should be examined as part of other proceedings that will consider costs and revenues of operator services provided by both local exchange carriers and interexchange carriers.⁵ (Tr. 114, prepared testimony pp. 6, 10-11.)

Based on her analyses, Miller also testified generally on the types and operation of various directory assistance services, and AT&T-C's Witness Ensign returned to the stand to provide further clarification. Their testimony is reflected in the introduction above.

Ensign explained that, in local intrastate and interstate directory assistance calls, the operator who handles the call is employed by a local exchange carrier. He stated:

"In fact, the operator's voice that you hear coming on is a mechanized reproduction of that person who is sitting in that operator position with his or her actual voice so that, that individual doesn't have to repeat 'what city

⁵ D.90-08-066 in Phase III of Order Instituting Investigation 87-11-033 states the Commission's intention to examine the costs and revenues associated with operator services provided by local exchange carriers and interexchange carriers.

are you calling' every time a customer calls in.

"So the mechanized operation takes place, and then the customer responds to that. Then the operator types in a few key numbers and phrases into the system. That then prompts a screen response that the operator then looks at and is able to locate the number for the calling party. [The operator] then presses a button, and the mechanized response gives the calling party the telephone number." (Tr. p. 118.)

While the local exchange operator handles the call, the operator at the conclusion of the call identifies the interexchange service that the caller has used, be it AT&T, MCI, US Sprint, or others. The local exchange carriers own and operate the facilities by which directory assistance service is provided. As relevant here, the local exchange carrier charges the interexchange carrier a service charge, or access charge, for each directory assistance call handled. PacBell charges AT&T-C 29 cents for each such call between LATAs in California. Thus, for billable calls, PacBell receives 29 cents, and AT&T-C receives 11 cents. For unbilled AT&T-C calls (hospitals, hotels, and pay phones), PacBell charges AT&T-C 29 cents, and AT&T-C receives nothing. (Tr. pp. 119-20.)

D. US Sprint and MCI

US Sprint and MCI appeared originally in this proceeding to respond to AT&T-C's requested reduction of certain long distance rates. When AT&T-C withdrew that part of its application (because it had filed for such reductions elsewhere), US Sprint and MCI appeared only to protest TURN's proposals to establish directory assistance rules for all interexchange telephone companies. Neither US Sprint nor MCI objects to AT&T-C's application to increase its directory assistance charge.

Accordingly, US Sprint and MCI confined themselves to cross-examination of TURN's witness. They established that TURN had conducted no cost analysis or comparisons of the interexchange

carriers' costs of providing directory assistance service (Tr. 102.) They also established that TURN's proposal for a uniform two free call allowance and 40-cent rate among interexchange carriers was based on a qualitative analysis, rather than upon an empirical analysis of cost or consumer use data. (Tr. p. 109.)

US Sprint, MCI, and AT&T-C objected to and moved to strike TURN's testimony as it addressed interexchange carriers other than AT&T-C on the basis that nonapplicant interested parties should not be bound or potentially prejudiced by TURN's testimony. The motion was denied and the objections were overruled to the extent they challenged the relevancy of TURN's testimony. The directory assistance prices and practices of other carriers are relevant to the consideration of AT&T-C's application for a directory assistance increase. The objection was sustained to the extent, if any, that TURN's testimony suggested that this application proceeding should be a generic hearing on directory assistance practices in general.

V. AT&T-C's Motion for Interim Relief

In addition to its application, AT&T-C has filed a motion for an interim increase in its directory assistance rates. As TURN notes, an interim rate increase generally requires the applicant to make a prima facie showing of financial emergency or other circumstance justifying extraordinary relief. (Pacific Tel. & Tel. Co. (1949) 48 CPUC 487, 488-89.) DRA argues that not only has such a showing not been made, but that evidence of a \$165,000 shortfall annually in a service that generates annual revenues of \$13 million "is just about a wash." (Tr. 157.) AT&T-C does not claim the existence of a financial emergency, but it argues that the length of time that its application has been pending (since February 1990) entitles it to interim relief. Since AT&T-C has agreed to submit

its application with its motion for resolution in this proceeding, any need for interim relief pending disposition of the application no longer exists. Accordingly, the motion for an interim increase in directory assistance rates is denied.

VI. Discussion

We turn now to consideration of AT&T-C's application for an increase in directory assistance rates from 40 cents to 50 cents per call with no charge for such calls from hotels and motels, hospitals, and pay phones.

A. Burden of Proof

AT&T-C, as the applicant, has the burden of proof in seeking an increase in its DA rates. PU Code § 454(a) provides, in part:

"(N)o public utility shall change any rate or so alter any classification, contract, practice, or rule as to result in any new rate, except upon a showing before the commission and a finding by the commission that the new rate is justified."

In reaching this finding that a rate increase is justified, the Commission is required to make separate findings of fact and conclusions of law on all material issues. Failure of the Commission to make such findings and conclusions may require annulment of the Commission's order. (Greyhound Lines, Inc. v. PUC (1967) 65 C.2d 811.) All such findings must be based on substantial evidence in the record. (Yucaipa Water Co. No. 1 v. PUC (1960) 54 C.2d 823.)

B. Cost Justification

AT&T-C states that an increase of 10 cents a call in directory assistance is justified because long-run incremental costs of this service exceed long-run incremental revenues. Yet, beyond that assertion, the record before us contains little cost

justification for the increase sought. Indeed, the evidence on cost that has been introduced appears adverse to the application.

DRA and TURN have established, and AT&T-C has acknowledged, that the cost data, at best, show a shortfall between costs and revenues of approximately half-a-cent per call, or an annual shortfall of \$165,000. AT&T-C admits that a one cent increase in its directory assistance price would cover any shortfall it has projected.

The evidence also shows that the major element of AT&T-C directory service cost is the access fee paid to local exchange carriers. AT&T-C provides DA service by connecting its customers to the directory assistance operator of the appropriate local exchange carrier, such as PacBell or GTEC. PacBell, effective August 12, 1990, reduced its per message directory assistance charge to AT&T-C from 33 cents to 29 cents.

Although there is little discussion on the record of these local exchange carrier access charges, we note that GTEC was authorized by this Commission in March 1989 to provide intrastate interLATA telephone directory service to AT&T-C and other interexchange carriers in competition with PacBell.

(D.89-03-051.) GTEC at that time proposed an access charge of 24.5 cents per DA call to interexchange carriers. AT&T-C surmised at hearing that PacBell's reduction in its access fee was a competitive response to GTEC's service. (Tr. 41.)

C. TICM Cost Methodology

AT&T-C elected not to produce a witness to testify about the company's computation of its directory assistance costs. This is understandable in that no party contested the cost computation. The strategy, however, leaves the record lacking in cost analysis and explanation. We know that AT&T-C used its Transport Incremental Cost Model (TICM) to calculate the cost of DA service. We also know that DRA in its analysis modified the TICM model on the basis of its belief that directory assistance is a monopoly or

near-monopoly service, thus deleting some cost-based items from consideration. Since DRA's analysis still showed an AT&T-C shortfall, AT&T-C apparently decided not to challenge DRA's analysis and assumptions in reviewing the TICM results.

The lack of examination or explanation of AT&T-C's cost methodology leaves a number of questions unanswered. We know, for example, that AT&T-C's costs include an element for rate of return. We do not know the effect on rate of return of a \$165,000 annual DA shortfall. We also know, from the record, that AT&T-C's long-run incremental shortfall was \$55,000 using a pre-TICM cost methodology, and that this shortfall was changed to \$165,000 at hearing because of the use of TICM. The record does not reflect, and AT&T-C has presented little evidence in explanation of why the calculation of a shortfall tripled with use of the TICM model (Tr. 48), particularly when PacBell access charges have declined.

Compounding this was the discovery by the parties, late in hearing, that D.90-11-029, issued on November 9, 1990, had not approved the use of TICM as a basis for setting rates and charges for directory assistance service. DRA's Van Aggelen testified that his analysis of AT&T-C's costs would have been the same both before and after D.90-11-029. Nevertheless, we are left with a record in which cost analysis, to the extent it is examined at all, is based on a methodology not yet approved for this purpose by the Commission.

Costing methodology is not dispositive of AT&T-C's application. However, as we have stated many times, the burden rests upon the applicant to prove that it is entitled to rate relief, and not upon the Commission or staff to prove the contrary. (Citizens Utilities Co. of California (1953) 52 CPUC 637.) In making its proof, AT&T-C was required to show that its cost data and methodology adequately supported its application.

D. Policy of Free Calls

Another significant element of AT&T-C's costs for DA service is the no-charge policy for calls from hotels and motels, hospitals, and pay phones. Until recently, AT&T-C had no real choice in this policy, since it lacked technical ability to charge for these calls. At hearing, however, AT&T-C stated that it would have the technology, by January 1, 1991, to charge for these calls if it decided to do so.

These "free" calls account for 17% of AT&T-C's DA calls, or approximately 6.8 million DA calls annually. The calls are doubly costly for AT&T-C. Not only does the company derive no revenue from them, it still must pay the 29-cent access charge to PacBell, or a similar access rate to another local exchange carrier, for each such call handled. Obviously, AT&T-C could recoup more than the annual \$165,000 shortfall in directory assistance costs if it imposed a charge on some of these calls.

AT&T-C offered no evidence of costs or revenue derived from offering no-cost directory assistance service to this away-from-home market. It justified the policy on competitive grounds, and on the basis that away-from-home callers are less likely than others to have personal phone directories with them. The Commission, in dicta, spoke to these arguments in 1984 in a general rate case decision (D.84-06-111), stating:

"We find it unreasonable to exempt calls from coin phones or handicapped callers from this 35-cent [directory assistance] charge. Very few callers, in any physical location or state of health, will have alternative sources of directory information available to them. An exemption for coin phone callers or the handicapped would be arbitrary discrimination."
(15 CPUC 2d 232, 404.)

In any event, the policy of not charging for these 17% of DA calls is premised on attracting customers to the company's total package of services. AT&T-C has provided no justification

for imposing the costs of this system marketing effort on only those DA users who are charged for their calls. If AT&T's concern is with the revenue adequacy of the DA service, a better alternative would be for AT&T to seek authority to impose a charge for these free calls consistent with D.84-06-011.

E. Flexible Ratemaking

Generally speaking, we have in the past set rates for particular telephone services based on one of three distinct models: (a) setting rates to recover the full costs of service, including an appropriate factor for return on invested capital; (b) setting rates to recover the full costs of service plus an additional contribution toward common costs or the costs of other services; and (c) setting rates residually to recover revenue requirements not achieved from other services.

The first model of fully cost based rates has been our general standard. For example, in D.89-03-051, this model was applied in authorizing GTEC's charge for directory service to interexchange carriers (proven costs plus 12.75% rate of return). The second ratemaking model has been applied 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 that the Commission historically has sought to protect from the impact of drastic rate increases, in the interest of promoting universally affordable telephone service. (See, generally, Re Pacific Telephone and Telegraph Company (1984) 15 CPUC 2d 232, 316.)

A rate increase for directory assistance sought under any of these models would, of course, require a more detailed presentation of costs than exists on this record.

Instead, relying on the limited rate flexibility that this Commission has granted it in D.88-12-091 and D.90-11-029, AT&T-C argues that it is or should be entitled to raise its price for a competitive service upon a showing that LRIC (or long-run incremental costs) exceeds long-run incremental revenues. It further argues that the amount of increase should essentially be a

matter of management discretion. Competition, presumably, will act as a curb on management to encourage it to keep the price increase low enough to be accepted by customers, yet high enough to contribute to the company's common costs.

By D.88-12-091, dated December 19, 1988, the Commission granted AT&T-C flexibility to increase or decrease its rates within established bands, for several existing services, by advice letter filings to become effective on five days' notice. The decision also granted AT&T-C the authority to introduce new services with flexible rate bands by advice letter on 40 days' notice using a standard costing methodology after that costing standard was formally approved by the Commission.

In D.90-11-029, the Commission approved AT&T-C's standard costing methodology or TICM, supra, to determine the cost "floor" for new competitive services, and it granted AT&T-C the flexibility, generally, to establish rate bands of plus 5% and minus 15% above and below reference rates established for specific services examined in that proceeding. Ordering Paragraph 8 of that decision instructed AT&T-C to use the formal application process to seek expansion or other modifications to the regulatory flexibility rate bands authorized in the decision. Conclusion of Law 19 of the decision stated, in part: "It is our goal to adopt reliable long-run incremental cost estimates as the standard for setting minimum rates and charges for all of AT&T-C's switched and private line services."

As discussed above, however, D.90-11-029 left consideration of directory assistance for another time and place, stating:

"The issue of using TICM and/or LRIC [Long-Run Incremental Cost] as a basis for setting rates and charges for directory service was not considered in the record evidence in this proceeding and AT&T-C's attempt to raise that as an issue in its eleventh-hour comments here is misplaced and inappropriate." (D.90-11-029, p. 48.)

AT&T-C does not in this proceeding seek an increase in the rate band applicable to its directory assistance service. Nor does it seek a rate increase based on evidence of costs and rate of return. Instead, it takes a hybrid approach, arguing that once it has established that costs for a service exceed revenues (using its TCM methodology), it then should be free to seek any increase that management deems appropriate. We find no support for this approach in D.88-12-091 or in D.90-11-019, and AT&T-C has provided little evidence that such an approach to ratemaking is appropriate for directory assistance service.

F. Competition

Competition underpins regulatory flexibility. The more competitive the service, the more market forces can be relied upon to restrain prices. The less competitive the service, the more the need for regulatory oversight. (See, generally, Re Regulatory Framework for InterLATA Telecommunications Market, 30 CPUC 2d 384, 388-89.)

We agree with DRA and with TURN that there is not now effective competition for directory assistance service among interexchange carriers. The record shows that, as a practical matter, a consumer can change directory assistance service only by changing the interexchange telephone provider. DA is part of the package of services one subscribes to in selecting a telephone carrier. In most cases, minimal use of directory assistance makes that a small and probably unremarkable cost of the service selected.

Significantly, AT&T-C argues that its directory assistance prices have little or no effect on the prices charged by competitors. It states that US Sprint has by advice letter proposed to increase its directory assistance rate to 60 cents per call (although retaining two free call allowances per month) and that this increase is made apparently without regard to the 39

cents per call now assessed by MCI and the 40 cents now assessed by AT&T-C.

AT&T-C advances this argument to make the point that the Commission's policy of regulating a dominant utility, with the expectation that this will restrain nondominant utilities, is not appropriate for directory assistance service. In other words, what AT&T-C charges for directory assistance will have little or no effect on the charges of US Sprint and MCI. We are not convinced that this assessment is accurate, particularly since DA rates for the interexchange carriers appear at this time to be similar (39 cents and two free calls for MCI; 50 cents, a use discount and two free calls for US Sprint; 40 cents and away-from-home free calls for AT&T-C).

Nevertheless, the fact that AT&T-C makes the argument at all tends to underscore the point that directory assistance is not a competitive service, and there is no effective restraint on directory assistance price except that imposed by regulation.

G. Conclusion

These matters go to the fundamental issue of whether AT&T-C has justified with substantial evidence its application for a 25% increase in the price of its directory assistance service. We find that AT&T-C has not met that burden. AT&T-C has not justified the use of its TICM cost methodology for directory assistance service, nor has it presented us with an alternative cost analysis that would permit us to conclude that an increase is justified by AT&T-C's costs. Moreover, AT&T-C has failed to rebut the contention of DRA that directory assistance is a monopoly or near-monopoly service, with its price restricted to cost recovery. It has failed to answer TURN's argument that local exchange carrier access fees (the price that AT&T-C pays for use of local directory assistance service) are going down, not up, because of competition. And AT&T-C has not answered the argument that it is unreasonable to charge only DA users for the 17% (\$2,720,000) of DA calls that are

offered free in order to attract new customers to the company's total package of services.

Finally, AT&T-C has not persuaded us on this record that principles of limited rate flexibility forged by the Commission support a theory that a utility may charge whatever the traffic will bear once its rate for a service falls, however slightly, below an established floor. Application of that theory to directory assistance seems particularly inappropriate, given the monopoly characteristics of that service.

H. TURN's Two Free Calls Proposal

Conversely, we are not prepared, in this application proceeding, to adopt TURN's proposal to establish a 40-cent rate and two free calls per month as a uniform standard for all interexchange carriers in California. The proposal was useful in assessing aspects of the reasonableness of AT&T-C's application. However, we agree with AT&T-C that this application proceeding is not the forum for so generic a proposal, and that much of TURN's argument amounted to a question of "your free call policy versus our free call policy." We note that the Commission has faced this proposal before. While it has sought to encourage consistent directory assistance services, it has not required consistency at the cost of further subsidizing this service. (22 CPUC 2d 329, 427.)

I. Comments: ALJ's Proposed Decision

In accordance with PU Code § 311 and Rule 77.1 of the Rules of Practice and Procedure, the draft decision prepared by the assigned administrative law judge was issued on February 1, 1991. Timely comments were filed by AT&T-C and TURN, and timely reply comments were filed by DRA, TURN, and US Sprint.

All of the comments and replies have been carefully considered by the Commission, and we have made minor changes in the text where warranted.

AT&T-C proposes other, more substantive changes. The changes are opposed by those filing reply comments. We decline to adopt these changes for the reasons discussed briefly below.

- o AT&T-C argues that the record reflects no admissible evidence to support a conclusion that directory assistance pricing is a subject of confusion. The record, including the testimony of TURN's witness, amply demonstrates this finding. (Tr. 74-75, 99; Exhibit 4, pp. 3, 5-8.)
- o AT&T-C argues that the testimony of DRA's witness supports the utility's position on directory assistance costs and pricing. DRA replies that the record does not reflect such agreement, and that, in fact, its witness testified that AT&T-C's cost and pricing data were inappropriate for directory service. (Tr. 207-09.) We agree with DRA.
- o AT&T-C states that the decision transforms the long-range incremental cost standard from a price floor to a price ceiling, and is in conflict with our decision in D.90-11-029. DRA, TURN, and US Sprint challenge these assertions. DRA correctly notes that D.90-11-029 authorized LRIC, as generated by TICM, for certain services, but specifically excluded the use of TICM in directory service filings. (See D.90-11-029, Ordering Paragraph 1.)

With the minor changes that we have made in the text, we are of the opinion that the proposed decision constitutes a fair, factual and thorough resolution of the remaining issues in this proceeding. Therefore, we will adopt the proposed decision without further changes to the results reached therein.

Findings of Fact

1. AT&T-C seeks an increase in intrastate interLATA directory assistance service rates from 40 cents to 50 cents per call, while continuing its policy of not charging for such calls from hospitals, public and semipublic phones, and hotels or motels.

2. At 40 cents per call, long-run incremental cost of providing directory assistance service is \$13,405,380, versus revenue for the same period of \$13,239,820, representing a shortfall of \$165,560 annually, using AT&T-C's TICM costing methodology.

3. At 50 cents per call, long-run incremental cost would be \$14,570,270 versus revenues of \$16,549,730, using TICM.

4. Directory assistance calls from hospitals, hotels and motels, and pay phones, which are provided by AT&T-C without charge, constitute 17% of AT&T-C's DA calls.

5. AT&T-C lacked technical ability to charge for DA calls from hospitals, hotels and motels, and pay phones, until recently, but such technology was to be in place by January 1, 1991.

6. AT&T-C exhausted the flexibility given to it for DA service in D.88-12-091 when it increased the price per call to 40 cents on January 1, 1989.

7. There are three basic types of DA calls: (a) Local exchange area directory assistance, which allows five calls monthly without charge, and 25 cents per call thereafter; (b) Interstate directory assistance, billed at 60 cents per call by AT&T, with no call allowance; and (c) Intrastate directory assistance, billed at 40 cents per call by AT&T-C, with no monthly allowance but with no-charge service for hospitals, hotels and motels, and pay phones.

8. Following AT&T-C's notification of its proposed DA increase, approximately 600 customers wrote to the Commission, the great majority of them objecting to a directory assistance increase.

Conclusions of Law

1. Under PU Code § 454(a), the applicant for a rate increase has the burden of proof to show that the new rate is justified. AT&T-C has failed to do so.

2. Commission findings must be based on substantial evidence in the record.

3. D.90-11-029 did not approve the use of AT&T-C's TICM as a basis for setting rates and charges for directory assistance service.

4. AT&T-C has not met its burden of rebutting or overcoming evidence presented in opposition to a rate increase request.

5. TURN's proposal to establish a uniform 40-cent rate and two free calls per month for all interexchange carriers in California is generic in nature and is not properly raised in this application proceeding, except as it is relevant to the issue of reasonableness of the application. Accordingly, TURN's proposal should not be adopted in this proceeding.

6. AT&T-C has not shown financial emergency or other circumstance justifying extraordinary relief, and its motion for an interim increase in directory assistance rates should be denied.

7. AT&T-C has failed on this record to show by substantial evidence that an increase in intrastate interLATA directory assistance rates is justified, and the application should be denied.

8. The public interest is served by making this order effective without further delay.

ORDER

IT IS ORDERED that:

1. The motion of AT&T-C Communications of California (AT&T-C) (U-5002-C) for immediate interim relief to increase the rate for directory assistance calls made within the California between local access and transport areas (interLATA) from 40 cents to 50 cents per call is denied.

2. Application 90-02-060 of AT&T-C to increase the rate for directory assistance calls made within California on an interLATA basis from 40 cents to 50 cents per call is denied.

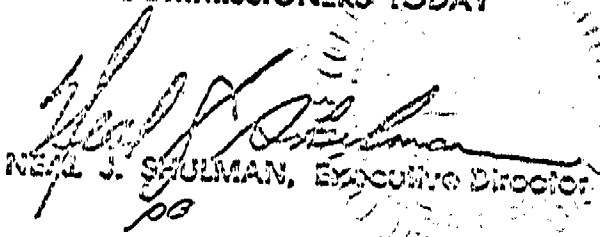
3. All remaining issues involved in Application 90-02-060 have been resolved, and this proceeding is closed.

This order is effective today.

Dated March 13, 1991, at San Francisco, California.

PATRICIA M. ECKERT
President
G. MITCHELL WILK
JOHN B. OHANIAN
DANIEL WM. FESSLER
NORMAN D. SHUMWAY
Commissioners

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


NEAL J. SHULMAN, Executive Director