CACD/RHG

Decision 92-11-012 November 6, 1992

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

ORIGINAL

Application of ALPINE CA-3, L.P. (U-3040-C) to issue additional evidences of indebtedness in a principal amount of up to $500,000 and to further encumber its public utility property.	Application 92-07-023 (Filed July 14, 1992)

OPINION

Summary of Decision

This decision grants Alpine CA-3, L.P. (Alpine) the authority requested in Application (A.) 92-07-023.

Alpine requests authority, pursuant to §§ 816 to 830 and § 851 of the Public Utilities (PU) Code, for the following:

1. To issue one or more primissory notes in the cumulative principal amount of up to $500,000 to Ericsson Radio Systems, Inc. (Ericsson).

2. To encumber all of Alpine's existing and future property pursuant to a Borrower Security Agreement and Deed of Trust in favor of Ericsson.

Notice of the filing of the Application appeared on the Commission's Daily Calendar of July 16, 1992. No protests have been received.

Background

Alpine is a limited partnership, duly organized under the laws of California, and is primarily engaged in the provision of cellular radiotelephone service (nonwireline, frequency Block A) in the California 3 Rural Service Area (RSA). The California 3 RSA encompasses the counties of Alpine, Amador, Calaveras, Mariposa, and Tuolumne.

Alpine is the assignee of the authority granted to Constitution Cellular, a general partnership, by the Federal Communications Commission (FCC) to provide domestic public cellular radio telecommunications service in the Alpine RSA. The transfer of that authority to Alpine, with the approval of FCC occurred on February 19, 1991.

Decision (D.) 91-05-037 dated May 22, 1991, as modified by D.91-08-003 dated August 7, 1991, granted Alpine a certificate of public convenience and necessity (CPCN) and authorized Alpine to issue evidence of indebtedness of principal amount not exceeding $2,860,000, and to execute and deliver an encumbering document to Ericsson.

Pursuant to D.91-05-037, the loan agreement (Agreement) entered into on July 5, 1991 provides for two types of notes:

1. Equipment Note - Ericsson agreed to make advances (Equipment Loan Advances) from time to time to Alpine in an aggregate principal amount not to exceed at any time the Approved System Expenditures; provided, that notwithstanding the stated face amount of the Equipment Note and the Working Capital Note, in no event shall the aggregate amount of the Equipment Loan Advances and the Working Capital Loan Advances ever exceed the Maximum Loan Amount. The Maximum Loan Amount is $2,860,000.

2. Working Capital Note - Ericsson agreed to make advances (Working Capital Loan Advances) from time to time to Alpine in an aggregate principal amount not to exceed the Working Capital Loan Borrowing Base; provided, that notwithstanding the stated face amount of the Equipment Note and the Working Capital Note, in no event shall the aggregate amount of the Equipment Loan Advances and Working Capital Loan Advances ever exceed the Maximum Loan Amount.

Exhibit A to the Application indicates that, as of the date of the Application, Ericsson has extended funds to Alpine in a total amount of $2,968,991. Two notes evidencing the indebtedness have been issued by Alpine to Ericsson. One is an Equipment Note in the amount of $3,000,000, or such lesser amount actually extended by Ericsson, for equipment and construction pursuant to the Agreement. The other is a Working Capital Note in the amount of $1,500,000, or such lesser amount actually extended by Ericsson, for working capital purposes under the Agreement.

Alpine states it generated as of April 1992, total operating revenues of $71,316 and net loss of $73,892 shown as part of Exhibit B to the Application. Also shown as part of Exhibit B is Alpine's balance sheet as of April 1992, which is summarized below:

Assets	Amount
Net Property and Equipment	$ 1,797,123
Current Assets	400,051
Other Assets	53,912
Total	$ 2,251,086

Liabilities and Equity	Amount
Capital and Shareholder Deficit	($ 819,304)
Long Term Debt	2,968,991
Current and Accrued Liabilities	101,399
Total	$ 2,251,086

The contributed capital as of this date was $36,846; accumulated net losses $856,150; and the total shareholder deficit $819,304.

At the time Alpine applied for a CPCN, its Exhibit G of A.91-02-073 projected the following:

	1991	1992	1993	1994
Total Revenue	$ 895,542	$1,660,923	$2,488,476	$3,345,515
Net Income(Loss)	($ 681,193)	($ 218,192)	409,119	834,631

Exhibit G likewise indicates zero paid-in-capital. The projected owner's equity is composed solely of negative retained earnings for the years 1991 to 1993.

Because Alpine's initial operating losses have been greater than expected, the financial projections were revised by

Alpine as shown in Exhibit F to the Application:

	1992	1993	1994	1995
Total Revenue	$1,000,813	$1,983,929	$2,974,997	$3,817,360
Net Income(Loss)	($ 824,593)	($ 187,296)	659,545	980,956

Promissory Note

Alpine proposes to issue one or more promissory notes in the cumulative principal amount of up to $500,000. The proposed financing will be undertaken pursuant to amendment of Alpine's existing Agreement with Ericsson, or pursuant to a new loan agreement between Alpine and Ericsson in substantially the same terms and conditions as the existing Agreement.

In accordance with the existing Agreement, the interest will be based on the floating prime rate or an equivalent base reference rate, plus two percent, as determined by Morgan Guaranty Trust Company in New York or by the bank to which the loan agreement may be assigned from time to time.

The interest on the proposed loan amount will be payable monthly as it accrues. The repayment of principal will be made through forty-eight consecutive monthly installments beginning on July 1, 1994. Alpine's obligations under the proposed notes will be secured by full liens on all of Alpine's existing and future properties in substantially the same forms as the existing Borrower Security Agreement and Deed of Trust documents.

Capitalization Ratios

Alpine's capitalization ratios at April 30, 1992, recorded, and at April 30, 1992, pro forma after giving effect to the $500,000 issuance of Notes are as set forth below:

	Recorded		Pro Forma	
	Amount	Percentage	Amount	Percentage
Long-Term Debt	$2,968,991	131.9%	$3,468,991	126.1%
Short-Term Debt	101,399	4.5%	101,399	3.7%
Equity Capital	(819,304)	(36.4%)	(819,304)	(29.8%)
Totals	$2,251,086	100.0%	$2,751,086	100.0%

The above percentages point out that Alpine has an extreme debt position and negative equity, resulting in an incongruent debt to equity ratio.

Construction Budget

A summary of Alpine's construction budget for channel expansion as shown in Exhibit E to the Application is summarized as follows:

Item	Amount
Engineering	$ 5,000
Regulatory and Legal	5,000
Shelter, if required	10,000
Tower, if required	12,000
Cellular Equipment	90,000
Total per Location	$122,000

Alpine plans to construct two cell extenders immediately following approval of the Application. The antennas in both instances will be placed on existing structures. In one case, the radio equipment will be placed in an existing shelter. In the other a new shelter will be constructed. A third site will be undertaken later. The total estimated channel expansion cost is $335,000.

Cash Requirements Forecast

Alpine's cash flow statement for 1992 and 1993 which appears in Exhibit G to the Application is summarized as follows:

Components	1992	1993
Funds Needed for Construction Expenditures	$2,169,149	$ 334,333
License and Organizational Costs	30,000	0
Total	$2,199,149	$ 334,333
Less:		
Estimated Internal Cash Generation	(556,421)	(593)
Additional Funds Required from External Sources	$2,755,570	$ 334,926

Given the cash requirements forecast above, as presented by Alpine, internally generated funds would be deficient by $556,421 in 1992 and by $593 in 1993. The proposed loan under the Application would provide Alpine's cash requirements for expansion and working capital for the remainder of 1992 and for the year of 1993.

Use of Proceeds

Alpine plans to invest approximately $335,000 for channel expansion. The funds requested herein will be used for construction and improvement of facilities, to cover operating losses, and provide working capital.

The need to engage in channel expansion activities was projected to occur in 1992 at a cost of $307,307, as shown in Exhibit F to Alpine's A.91-02-073.

Alpine states in the Application that the proposed financing would be undertaken pursuant to amendment of Alpine's existing loan agreement with Ericsson, or pursuant to a new loan agreement between Alpine and Ericsson having substantially the same terms and conditions as the existing agreement. This constitutes a preconceived arrangement between the parties and confirms Ericsson's willingness to provide the financing prior to the Commission's receipt of the Application.

Alpine also states in the Application that it believes that further extension of funds by Ericsson presents the best financing alternative and that funding by Ericsson of expansion and operating costs is fully consistent with the Commission's prior decisions approving 100% debt financing for small rural cellular carriers.

D.91-05-037, as modified by D.91-08-003, recognized that a loan of operating capital by Ericsson is required in order to fund Alpine's initial operations.

It is appropriate to state that the Commission does not encourage 100% debt financing for small rural cellular carriers. While the supplemental opinion allowed the use of funds to meet initial operating requirements under D.91-05-037, it is not a pronouncement that 100% debt financing is prudent and reasonable for all small rural cellular carriers. What transpired in D.91-05-037, as modified by D.91-08-003 pertains only to a particular circumstance. It is the exception rather than the rule.

Section 817 of the PU Code provides that proceeds of indebtedness may be used only for the following purposes.

1. For the acquisition of property.

2. For the construction, completion, extension, or improvement of its facilities.

3. For the improvement or maintenance of its service.

4. For the discharge or lawful refunding of its obligations.

5. For the financing of the acquisition and installation of electrical and plumbing appliances and agricultural equipment which are sold by other than a public utility, for use within the service area of the public utility.

6. For the reorganization or readjustment of its indebtedness or capitalization upon a merger, consolidation, or other reorganization.

7. For the retirement of or in exchange for one or more oustanding stocks or stock certificates or other evidence of interest or ownership of such public utility, or bonds, notes, or other evidence of indebtedness of such public utility, with or without the payment of cash.

8. For the reimbursement of money actually expended from income or from any other money in the treasury of the public utility not secured by or obtained from the issue of indebtedness of the public utility.

For proper cause, Section 818 of the PU Code allows upon order of the Commission, the use of proceeds for purposes reasonably required in the operation of a utility, including operating capital.

In D.91-05-037, as modified by D.91-08-003, the Commission found that it is reasonable to allow Alpine to use lender-furnished funds as initial operating capital while the company is developing a stream of income from operations.

As a start-up company, Alpine has incurred operating losses greater than expected and anticipates achieving pre-tax profitability only in 1994. The proposed loan is required in part to fund the operations of the utility since Alpine has not yet developed sufficient income from operations. The construction and improvement of facilities are projected to generate revenues and place Alpine in a pre-tax profitability position.

In its Petition for Modification of D.91-05-037, Alpine sought an order modifying the Decision to clarify that it was authorized to use the financing proceeds for working capital during its start-up period. In the present Application, the proceeds would be used for both plant construction and improvement of facilities and to cover operating losses and working capital requirements during the initial years of operation. As we did in D.91-08-003, we will approve using the supplemental funds for those purposes.

From any creditor's point of view, a low ratio of debt to total assets is desirable. Trading on equity increases a company's financial risk, but it enhances residual earnings whenever the rate of return on assets exceeds the cost of debt capital. A company can achieve an excellent rate of return on common equity by using its debt leverage effectively. But just as a company's gains can be magnified, so also can its losses be magnified. Based on the authority requested, Ericsson bears the greatest risk for such an extension of funds. If Ericsson is willing to advance cash to cover Alpine's operating costs, it is their own judgement and prerogative. The Commission may caution Ericsson on this matter, but it has no hand or participation in Ericsson's credit decisions.

Alpine is placed on notice that our decision in this matter is simply permissive. In no way should it be construed to constitute an implied or expressed indemnification by ratepayers in the event Alpine is unable to meet its obligations under the proposed loan agreement.

Findings of Fact

1. Alpine, a California limited partnership, operates as a cellular radiotelephone provider subject to the jurisdiction of this Commission.

2. Alpine has an immediate need for external funds for the purposes set forth in the Application.

3. Ericsson is willing to provide additional funding to Alpine although it bears the greatest risk from such extension of funds.

4. If Alpine defaults in payment or in any provisions of the Agreement, the Commission does not guarantee payment or any indemnification of Ericsson.

5. The execution and issuance of Notes and a deed of trust and chattel mortgage to Ericsson would not be adverse to the public interest.

6. The proposed loan is for proper purposes.

7. The money, property, or labor to be procured or paid for by the proposed transaction are reasonably required for the purposes specified in the Application.

8. Although Alpine is not requesting any retroactive approval of unauthorized borrowings, the amount of funds extended by Ericsson to Alpine to date is over the approved amount of $2,860,000 authorized in D.91-05-037.

9. 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.

3. Alpine is a start-up company and it is reasonable to allow lender-furnished funds to be used as operating capital while the company is developing a stream of income from operations.

4. The proposed issuance of Notes is for lawful purposes, and the money, property, or labor to be obtained are required for these purposes.

5. The following order should be effective on the date of signature and payment of a fee of $1,000 as set forth by Section 1904(b) of the PU Code.

O R D E R

IT IS ORDERED that:

1. On or after the effective date of this order, Alpine CA-3, L.P. (Alpine) may execute and issue a promissory note or notes not exceeding $500,000 principal amount to Ericsson Radio Systems, Inc. (Ericsson), in substantially the same form as set forth in the Application.

2. Alpine may execute and deliver a deed of trust and chattel mortgage to Ericsson, in substantially the same form as set forth in the Application.

3. Alpine shall file with the Commission Advisory and Compliance Division (CACD) copies of the loan agreement, encumbering document, and the executed promissory note authorized by this Order, within 15 days of execution.

4. On or before the 25th day of each month, Alpine shall file the reports required by General Order Series 24.

5. CACD is directed to mail a certified copy of this decision to:

Ericsson Radio Systems Inc.
740 East Campbell Road
Richardson, Texas 75081
Attention: Rick Lorber
Vice President & Controller

6. The Application is granted as set forth above.

7. The authority granted by this order to issue the promissory note shall become effective when Alpine pays $1,000, the fee set forth by Public Utilities Code Section 1904(b). In all other respects this order is effective today.

Dated November 6, 1992, at San Francisco, California.

DANIEL Wm. FESSLER
President
JOHN B. OHANIAN
PATRICIA M ECKERT
NORMAN D. SHUMWAY
Commissioners

PUBLIC UTILITIES COMMISSION
STATE OF CALIFORNIA
PAID
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By E

R. 35885 . $1000.—

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

NEAL J. SHULMAN, Executive Director
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