ORIGINAL

Decision 82 02 031 FEB 17 1982

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of CONTINENTAL TELEPHONE COMPANY OF CALIFORNIA, a corporation, for an order authorizing it to issue and sell up to $30,000,000 of its First Mortgage Bonds, in one or more series and to execute one or more supplemental indentures.	Application 61139 (Filed December 18, 1981; amended December 23, 1981)

O P I N I O N

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

1. To issue and sell, through negotiated private placement or competitive biddings, its First Mortgage Bonds, in one more series (New Bonds), in an aggregate principal amount up to $30,000,000 and

2. To execute and deliver one or more indentures supplemental to its First Mortgage indentures.

Notice of the filing of the application and the amendment appeared on the Commission's Daily Calendars of December 22 and 29, 1981, respectively. No protests have been received.

This decision authorizes Continental to issue and sell its New Bonds for the purpose of refunding part or all of its short-term indebtedness and the residue, if any, to be applied against moneys spent from Continental's treasury for construction expenditures.

Continental, a California corporation (a subsidiary of Continental Telephone Corporation, a Delaware corporation), is primarily engaged in the business of furnishing local and toll telephone service in portions of Arizona, California, and Nevada.

For the 12 months ended September 30, 1981, Continental reported it generated total operating revenues of $159,193,800 and net income of $22,881,483 shown as part of Exhibit A attached to the application.

Continental's Balance Sheet as of September 30, 1981, also shown as part of Exhibit A is summarized as follows:

Assets		Amount
Net Telephone Plant		$352,198,128
Investment and Other Property		3,086,419
Current Assets		32,776,796
Deferred Charges		263,869
	Total	$388,325,212
Liability and Equity		
Common Equity		$155,385,803
Preferred Stock		14,310,100
Long-Term Debt		139,945,326
Current Liabilities		59,951,922
Deferred Credits		18,732,061
	Total	$388,325,212

Continental proposes to issue and sell up to $30,000,000 aggregate principal amount of its New Bonds under an existing indenture as previously amended and supplemented and to be further amended and supplemented by one or more supplemental indentures. The proposed supplemental indentures are to be substantially in the same form as the form of the Twentieth Supplemental Indenture filed in connection with Application (A.) 60262 (Decision (D.) 92878 dated April 7, 1981) and will include any changes as are required to reflect the terms of the New Bonds.

Continental, with the assistance of one or more investment bankers, intends to negotiate for the private placement of the New Bonds for issuance and delivery in 1982, at a time best coinciding with its financing needs. In addition, Continental requests alternative authorization to sell the New Bonds in one or more competitive offerings should its view of market conditions change prior to a commitment for a sale of the New Bonds. In the event of a private placement, the terms of the New Bonds will be fixed at the time of negotiation and will be embodied in a purchase agreement in a form substantially similar to that filed in connection with A.60262, which Continental expects to execute within a reasonable time after negotiations are complete, even if delivery of the New Bonds is delayed for several months.

Continental's capital ratios as of September 30, 1981 and adjusted to December 31, 1982 on a pro forma basis to give effect to:

1. The proposed issuance and sale of $30,000,000 of New Bonds,
2. The issuance and sale of $15,000,000 of Continental's 14-1/2%, First Mortgage Bonds, Series R, on November 20, 1981 (D.92878 dated April 7, 1981 in A.60262),
3. The retirement of $25,000,000 principal amount of 10% First Mortgage Bonds, Series K, due January 15, 1982,
4. The redemption of 27,775 shares of Preferred Stock, $20 par value, in the amount of $777,000,
5. Payments into sinking funds for the retirement of $3,172,000 of First Mortgage Bonds,
6. Contributions of $3,000,000 received from Continental Telephone Corporation to common equity, and
7. Estimated income of $4,670,000 for the period of September 30, 1981 to December 31, 1982

are as follows:

	September 30, 1981	Pro Forma
Long-Term Debt	49.7%	51.1%
Preferred Stock	4.2	3.7
Common Equity	46.1	45.2
Total	100.0%	100.0%

Excluded from the pro forma ratios above is the remaining $20,000,000 authority to issue and sell First Mortgage Bonds authorized by D.92878 dated April 7, 1981 in A.60262 because the timing of this proposed issue is uncertain. However, an extension of time to February 28, 1982 was granted in D.82-01-23 dated January 5, 1982.

The proceeds of the sale of the New Bonds will be applied to retire short-term indebtedness incurred to partially and temporarily finance Continental's construction program. Continental estimates that its indebtedness to holders of short-term obligations will exceed the proceeds of the New Bonds at the time the New Bonds are issued. All proceeds of the short-term obligations will have been spent by Continental for capital additions and improvements. If Continental sells New Bonds in a principal amount in excess of short-term indebtedness outstanding at the time of sale, the excess proceeds will be used to reimburse Continental for moneys actually expended from income or other moneys in its treasury, and not obtained from the issue of its securities for construction, completion, extension, or improvement of its utility properties.

Continental states in its application that it believes, in addition to authorization of a competitive offering, an exemption from the competitive bidding rule should be granted in order to permit a negotiated private placement of the New Bonds.

This would allow Continental reasonable flexibility in planning for the New Bond financing and the retirement of its short-term debt. Continental states that it believes it can sell the New Bonds at a cost as low, if not lower, than would prevail if the New Bonds were sold at competitive bidding and that this will result in the lowest cost to its ratepayers. Based on this belief, Continental states that it would be in the public interest to exempt the sale of New Bonds from the Commission's competitive bidding requirements.

Continental requests an exemption for the proposed sale of the New Bonds from the Commission's competitive bidding rule established by D.38614 dated January 16, 1946 as amended from time to time in Case 4761. Continental has set forth in A.59874, A.60262, and supplemental information furnished in connection with A.60262, the numerous reasons why it believes it can sell the New Bonds at a cost as low, if not lower, than would prevail if the New Bonds were sold at competitive bidding and that this will result in the lowest cost to its ratepayers. Continental believes these reasons are still pertinent.

Continental's reason for requesting an exemption for the proposed sale of its New Bonds are summarized below from a letter dated January 14, 1982 to the Commission:

1. A private placement is considerably less expensive than a public offering. Private placement avoids the costs of registration under the Securities Act of 1933, thus, reducing legal fees. Printing costs are lower. Also, fees paid to agents are lower than for public offerings.

2. Analysis of Continental's underwriting costs 1/ shows that competitive bidding costs are more than three times greater than for private placements. Privately placed issues were compared to those competitively placed. The comparison is based on the weighted average underwriting discounts 2/ of privately versus competitively placed issues.

3. The historic weighted average of underwriting discounts for privately placed issues is .4297% and for competitively placed issues is 1.2437%. For a $30,000,000 issue, at a market rate 3/ of 14.5%, the differential effective yield between a privately and competitively placed issue would be approximately 12 basis points ($244,200).

1/ Underwriting Costs - These are costs Continental must pay to agents for placing a bond before prospective lenders.

2/ Underwriting Discount - A percentage fee applied to the face value of the bond.

3/ Market Rate - The interest rate (nominal rate) the company anticipates it will have to pay on the open market in order to sell the issue.

4. Other costs in addition to underwriting of a competitive public offering are printing fees, accountant's fees, legal fees, and filing fees. These extra costs (from $260,000 to $400,000) would add an additional 6 to 12 basis points to the differential effective yield.

5. The total differential yield between privately placed debt and competitively placed debt would be 20 to 27 basis points (from $398,200 to $538,200).

Both Continental and the Commission's Revenue Requirements Division believe and conclude that a private placement of the proposed New Bonds is less costly because of reduced filing fees, printing costs, accountant's fees, attorney's fees, and underwriting fees.

In D.91984 dated July 2, 1980 for San Diego Gas & Electric Company's A.59633, we discussed the granting of exemptions from the competitive bidding rule, and we clarified the nature of the compelling showing that must be made to warrant an exemption from the rule. We served notice that assertions regarding the volatility of the market, the flexibility provided by a negotiated sale, and the importance of maximizing the effectiveness of the underwriting group will not serve as compelling reasons, individually or collectively, for granting an exemption from the competitive bidding rule.

Because Continental intends to sell the proposed New Bonds by private placement on terms which will be negotiated after the issuance of this decision and because of the Commission's Revenue Requirements Division's conclusion and belief that the New Bonds will be sold at a cost as low, if not lower, than would prevail if the New Bonds were to be sold at competitive bidding, we are of the opinion that applying the Commission's competitive bidding requirements and conditions set forth in D.91984 in this proceeding would not be in the best interest of Continental or its ratepayers. The rule would not operate to ensure that Continental's sale of the New Bonds would be at the most favorable cost of money. However, in order not to limit Continental's options, we will grant Continental the authority to issue the proposed New Bonds by means of a competitive offering or private placement according to Continental's estimation of where the most favorable opportunity lies.

If the New Bonds are sold by means of a negotiated private placement, Continental is put on notice that in its next general rate proceeding before the Commission, the reasonableness of the resulting interest rate and cost of money to the company 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 the most prudent. We will also require Continental to provide us with a showing of why it believes that the resulting interest rate and cost of money were the most advantageous to the company and its ratepayers. We will require this showing within a reasonable period of time after the issuance and sale of its New Bonds.

Continental's estimated net construction expenditures for calendar year 1982 will approximate $56,665,000. Continental has provided in detail its construction program estimated as follows:

Purpose	Amount
Construction and Plant Expenditure (Including Cost of Removal):	
Station Apparatus and Connections	$ 6,264,000
Other Operations (Key Systems, Special Systems, Furniture, and Work Equipment	786,000
Outside Plant	16,760,000
Central Office Equipment	20,818,000
Land and Buildings	3,527,000
Other	5,236,000
Overheads	7,420,000
Total Construction and Plant Expenditures	$60,811,000
Less Salvage Value	4,146,000
Net Construction and Plant Expenditures	$56,665,000

Continental reports that as of September 30, 1981, its unreimbursed construction expenditures amounted to $141,302,734 as shown in supplemental data provided to the Commission in connection with this application.

The Revenue Requirements Division and the Communications Division have reviewed the application and have concluded that the proposed financing is necessary to implement Continental's construction program. The Divisions reserve the right to reconsider the reasonableness of any specific construction expenditures in future rate proceedings.

The Commission's Revenue Requirements Division has analyzed the financial data provided by Continental. The Division determined that cash generated from internal operations will provide 45.3% of the capital requirements estimated for 1982 and 69.0% of those in 1983. The Division has concluded the proposed financing is necessary to help Continental meet its capital requirements.

Findings of Fact

1. Continental, a California corporation, operates under the jurisdiction of this Commission.

2. The proposed New Bonds would be for proper purposes.

3. Continental has need for external funds for the purposes set forth in the application.

4. Continental believes it will be able to obtain an effective interest rate on its New Bonds through a negotiated private placement for delayed delivery in 1982, as low as, or lower

than, it could obtain from a competitive bid public offering of the New Bonds and should be authorized to proceed in the manner described in the application.

5. Continental should be authorized to issue and sell up to $30,000,000 aggregate principal amount of the New Bonds, either through private placement or competitive bidding upon terms and at a time which Continental determines to be the most advantageous to it and its ratepayers.

6. The money, property, or labor to be procured or paid for by the proposed debt securities is reasonably required for the purposes specified in the application.

7. The sale of the New Bonds should not be required to be through competitive bidding.

8. The proposed supplemental indentures would not be adverse to the public interest.

9. There is no known opposition and 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 security issue is for lawful purposes and the money, property, or labor to be obtained by it is required for these purposes. Proceeds from the security issue may not be charged to operating expenses or income.

The action taken is for the purposes of this proceeding only and is not to be construed as indicative of the amounts to be included in proceedings for the determination of just and reasonable rates.

The following order should be effective on the date of signature to enable Continental to issue and sell its New Bonds expeditiously.

ORDER

IT IS ORDERED that:

1. Continental Telephone Company of California (Continental), on or after the effective date of this order and on or before December 31, 1982, may issue, sell, and deliver for cash, in one or more series, its First Mortgage Bonds, in an aggregate principal amount of up to $30,000,000 by private placement to be negotiated as described in the application or by competitive bidding. These sales are exempted from the Commission's competitive bidding rule.

2. Continental may execute and deliver one or more supplemental indentures in substantially the same form as that filed in connection with A.60262, filed February 13, 1981, with any changes that are required to reflect the terms of the First Mortgage Bonds. As soon as available, Continental shall file with the Commission the definitive form of any supplemental indenture.

3. Continental shall apply the proceeds from the sale of its First Mortgage Bonds to the purposes set forth in the application.

4. Promptly after Continental ascertains the price, interest rate, and other terms pertaining to the First Mortgage Bonds, the company shall notify the Commission in writing.

5. If the First Mortgage Bonds, in one or more series, or any series of them, are sold on a private placement basis, within 30 days after their issuance and sale, Continental shall file with the Commission a report setting forth the reasons why it believes the resulting interest rate and cost of money to the company were the most advantageous to the company and its ratepayers.

6. If the First Mortgage Bonds, in one or more series, or any series of them, are sold by competitive bidding, as soon as available, Continental shall file with the Commission three copies of its final prospectus relating to the issuance of New Bonds.

7. If the First Mortgage Bonds, in one or more series, or any series of them are sold on a private placement basis, as soon as available, Continental shall file with the Commission a conformed copy of the purchase agreement.

8. Continental shall file the reports required by General Order Series 24.

9. This order shall be effective upon payment of $21,000, the fee prescribed by PU Code Section 1904(b).

Dated FEB 17 1982, at San Francisco, California.

JOHN E. BRYSON
President
RICHARD D. GRAVELLE
LEONARD M. GRIMES, JR.
VICTOR CALVO
PRISCILLA C. GREW
Commissioners

PUBLIC UTILITIES COMMISSION
STATE OF CALIFORNIA
PAID
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FEB 19 1982
$21,000.00
By

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

Joseph E. Bodovitz, Executive Director