

ORIGINAL

Decision No. 86541

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of
The Pacific Telephone and Telegraph
Company, a corporation, for telephone
service rate increases to offset
increased wage, salary and associated
expenses.

Application No. 55214

Investigation on the Commission's
own motion into the rates, tolls,
rules, charges, operations, costs,
separations, inter-company settle-
ments, contracts, service, and
facilities of The Pacific Telephone
and Telegraph Company, a California
corporation; and of all the telephone
corporations listed in Appendix A,
attached hereto.

Case No. 9832

Milton J. Morris, Attorney at Law, for The Pacific
Telephone and Telegraph Company, applicant and
respondent.

William Shaffran, Attorney at Law, for the City of
San Diego; Leonard Snaider, Attorney at Law, and
Manual Kroman, for the City of Los Angeles;
Sylvia Siegel for Toward Utility Rate Normalization;
David L. Wilner, for Consumers Lobby Against
Monopolies; and William L. Knecht, Attorney at Law,
for California Farm Bureau Federation; interested
parties.

Ira R. Alderson, Attorney at Law, and James G. Shields,
for the Commission staff.

OPINION ON REHEARING

In this application, The Pacific Telephone and Telegraph Company (Pacific) sought rate relief totaling \$97.9 million. Decision No. 85287 herein, dated December 30, 1975, awarded a rate increase of \$65.2 million based upon a twelve-month test period ending June 30, 1975.

In adopting an estimate of revenues for the test year, we stated (mimeo. p.6):

"Effects of increased directory advertising rates, effective January 1, 1975, and the timing of local calls, which will start in selected areas in the second quarter of 1976, are insignificant for this test period. These items will be analyzed in future proceedings."

The city of San Diego (San Diego) petitioned for a rehearing regarding this determination, arguing that the increased rates should have been considered, thereby reducing the revenue requirement. We granted a limited rehearing to consider the problem (Decision No. 85557 dated March 9, 1976). San Diego is supported in its position by the staff and the city of Los Angeles (Los Angeles). A hearing was held on this subject before Examiner Meaney in San Francisco on April 19, 1976 and the matter was submitted at that time subject to the filing of briefs.

The question involved is whether the estimates of revenue and expenses attributable to the institution of single message rate timing of local calls in five-minute units (SMRT) and increased classified telephone directory advertising rates should be treated in the same manner as they were in Decision No. 83162 (Application No. 53587, et al., dated July 23, 1974). In that decision (see table on mimeo. p. 97) the sources of increased revenue included a net figure of \$7.3 million for timing of local message units and \$7.7 million for increased directory advertising revenue.

That decision does not contain (and the exhibits and testimony in that proceeding do not contain) any discussion to the effect that such revenues would not actually be received during the test year, and the most reasonable inference is that such revenues were included upon the assumption that at least a substantial amount of them would actually be received during the test year.

This did not occur. Pacific's original plans called for the installation of very simple SMRT equipment, but the Commission stated, in Decision No. 83162 (mimeo. p. 81):

"We are aware of the virtue of off-peak pricing to reduce Pacific's peak loads. It is probable that eventually evening usage of message units will be provided at a lower price than day usage, just as now evening usage of toll is provided at a lower price. Because of this we expect that Pacific, when installing its timing equipment, will provide equipment that either has the capability of off-peak pricing, or can be adapted to provide off-peak pricing."

This requirement sent Pacific back to the drawing board. As Pacific's witness Hamish Bennett testified at the rehearing in this present application (Application No. 55214, Tr. 2771):

"When we read that decision, we recognized that if we were to comply in the future with the provisions of that decision, it would be necessary to go into development work on equipment that would in fact provide that capability, the capability that was not originally intended in our proposal."

The delay in designing, procuring, and installing SMRT equipment (manufactured by an independent company and not by Western Electric) proved to be substantial. As staff witness Carlson, who made the staff's revenue estimates in this proceeding testified in the case-in-chief (Exhibit 30, answer 16):

"In Decision No. 83162, signed July 23, 1974, the Commission authorized Pacific Telephone to institute timing of local calls. No time limit was set for accomplishing this. The utility has been studying various methods and equipment designed to time local calls. Present indications are that the utility will start this project during the last half of 1975 and that they will complete the project within two years. The utility estimates that, if timing of local messages had been in effect during the test year, it would have produced a gross revenue for Pacific Telephone of \$16,000,000. The \$7,900,000 shown above is the staff estimate of revenues to Pacific from this source after deducting charges in the same ratio as was indicated in D-83162, page 97. The utility did not include a revenue effect from this source in their revenue estimate."

The last half of 1975, mentioned above, is after the conclusion of the test period in this application; thus by the staff's (uncontroverted) testimony, there was no estimated revenue effect for this application's test year as a result of our previous authorization to begin SMRT.

Mr. Carlson then explained his position on directory sales and advertising revenues as follows (Exhibit 30, answer 17):

"D-83162 authorized increases in Classified Directory Advertising which, if effective during the test period, would produce an increase in revenues of an estimated \$8,400,000. The full effect of the authorized increases will not be realized until 1976 when all California directories will have been revised. It is estimated that \$868,000 in added revenues from this source will be realized during the first six months of 1975. The utility did not include additional revenues from this source during the test period. The staff estimate reflects the full annualized effect during the test period."

The argument against the result we reached on these items in this application in Decision No. 85287 is that it is inconsistent with Decision No. 83162 (Application No. 53587) and that it will, in the future, cause an excess rate of return because certain revenues will be discounted in violation of principles set forth in City of Los Angeles v Public Utilities Commission (1972) 7 Cal 3d 331, 102 Cal Rptr 313.

In other words, the question is: did we adopt an unrepresentative test-year revenue-expense estimate regarding these items because post-test-year conditions are not properly reflected?

After consideration of the record, we believe the answer to this question is "no".

Single Message Rate Timing

Because the problems are similar but not identical, we must consider SMRT and yellow-page advertising rates separately.

San Diego and its supporters do not argue that during the test year for Application No. 55214, there will be a significant effect as a result of SMRT. The point made by the staff and the cities is that we are setting rates for future years, and that, therefore, regardless of the negligible impact during the Application No. 55214 test year, the pronounced effect thereafter should be considered in order to correctly apply "test year" theories.

This argument is sound from a theoretical standpoint, but is incorrectly applied to the situation with which we are presented here. Concededly, a test year, under more normal (i.e., more non-inflationary) circumstances, reflects not only itself but, for ratemaking purposes, conditions in at least the immediate period beyond the test period. This is true for the simple reason that under less inflationary circumstances, a general rate increase application

occurs only once in a few years, and short-term revenue problems in between such cases are usually handled by way of offset relief.^{1/}

But what is the context in which our statement concerning test year revenues (quoted above, see page 1) should be measured? Decision No. 85287 was dated December 30, 1975. Application No. 55492, which we are now actively considering was filed on February 13, 1975, and a substantial amendment to that application was filed on April 17, 1975. Thus any relief awarded in Application No. 55214 must be considered as reflecting our cognizance of the pendency of Application No. 55492, and a reasonable estimate on our part of how long the Application No. 55214 relief will be in effect before it would be superseded by whatever order we might make in Application No. 55492.^{2/}

We have already expressed our disapproval of overlapping applications,^{3/} but, leaving that aside, it is obvious that a forward-looking view of SMRT revenues is more appropriately considered in Application No. 55492, rather than in this application, considering the short time period during which we may expect rates found reasonable in this application to be in effect.

1/ As we have already noted, notwithstanding the language in the caption of this application, it is not "offset" in character because a new test year is involved. See discussion in our Order Denying Motion to Set Public Hearings in Application No. 55492 (Decision No. 84938 dated September 30, 1975). The new test year for Application No. 55214 was, as stated above, a twelve-month period ending June 30, 1975, while the Application No. 53587 test year was 1973. San Diego's assertion ("prepared statement", p. 2) that Decision No. 85287 in this application made use of the 1973 test year for the previous Application No. 53587 is erroneous.

2/ Hearings in Application No. 55492 are at present in progress, and are currently scheduled through various dates in October of this year.

3/ Decision No. 84938 (Application No. 55492) dated September 30, 1975.

We emphasize that our discussion of the problem of future SMRT revenues in this decision applies to the facts presented, and should, most emphatically, not be construed to mean that we consider estimates for a test year in a vacuum, without regard to revenue and expense factors which immediately follow the exact period selected as the test year (which, after all, is normally selected by the applicant and not by the Commission). Rather, our view of the allegations of the cities and the staff affirms our determination to deal fairly with all parties regarding a forward-looking view of rate relief.

Based upon the above factors, we hold that our determination in Decision No. 85287 of the effects of increased net revenues, if any, for SMRT for the test period is correct, and that any long-range forward-looking view of such revenue-expense consideration is more appropriately, and more accurately, resolved in presently pending Application No. 55492.

Classified Directory (Yellow Page) Revenue

The same arguments discussed above apply to classified advertising but for one important difference: as Mr. Carlson's testimony (page 4, above) explains, it was estimated that \$868,000 in added net revenue from such advertising would be realized during the first six months of 1975 (the last six months of the test year in this application).

The question for us to consider here is, therefore, whether we should allow any adjustment in rates or any refund based upon the fact that Decision No. 85287 made no allowance for such revenue, or whether we are entitled to rely upon our determination in that decision, as quoted above on page 4, that any such revenue effect is "insignificant" and may be analyzed in "future proceedings".

We believe our conclusion to the effect that the \$868,000 of estimated revenue requires no rate adjustment may stand.

First, we reiterate our position concerning the application of test-year principles. We are not here setting rates for several future years; Application No. 55492 presently pending and its test year is the twelve-month period ending June 30, 1976; we expect a decision on this application toward the end of this calendar year; therefore, the problem of how increased yellow-page advertising affects post-Application No. 55214 results is better considered in Application No. 55492.

This statement does not, however, account for the problem of what to do with \$868,000 of anticipated net revenue for the test year in Application No. 55214 itself. We believe a common-sense solution, in view of the pendency of Application No. 55492, is to inspect recorded results for the test period in Application No. 55214, especially since San Diego and its supporters have emphasized their fears that if the Commission makes no adjustment to existing rates, Pacific would exceed its assigned rate of return.^{4/} Recorded results for this test period show that Pacific has earned below its assigned rate of return during the entire Application No. 55214 test period and for the first few months of 1976, and that therefore no refund or adjustment of rates is warranted. Reports filed in compliance with Decision No. 83162 show the following results (for information available so far for 1976, based upon rate relief awarded in this application):

^{4/} Problems relating to alleged excessive rate of return resulting from depreciation methods and federal tax considerations will be dealt with in other decisions.

PACIFIC TELEPHONE AND TELEGRAPH COMPANY

12 Months Ended Actual Rate of Return for 1976

<u>12 Months Ended (1976)</u>	<u>D.83162 and D.85287 Basis</u>	<u>Excluding Annualization of Wages</u>
Jan.	7.90%	8.32%
Feb.	7.86	8.22
Mar.	7.97	8.27
Apr.	8.08	8.32
May	8.13	8.31

Based upon such results, and assuming test-year normalization (see Footnote 4), it is reasonable to assume that Pacific will not earn an amount in excess of its assigned rate of return (8.85%) in the immediate future and that, therefore, no adjustment in rates or refund is necessary or warranted. No principle enunciated in City of Los Angeles v Public Utilities Commission, supra, or any other case, requires us to consider test-year results in a vacuum while paying no attention to recent recorded information.^{5/}

Findings

1. In Decision No. 85287, we stated, and we hereby adopt as a finding, the following:

"Effects of increased directory advertising rates, effective January 1, 1975, and the timing of local calls, which will start in selected areas in the second quarter of 1976, are insignificant for this test period. These items will be analyzed in future proceedings."

2. No evidence presented upon rehearing in this proceeding leads us to modify the determination in Finding 1, above, for the following reasons:

- a. Decision No. 83162, assumed that a substantial amount of the increased revenues for SMRT and increased yellow-page advertising would be received in the Application No. 53587 test year, while this proved not to be the case;

^{5/} Cf. the discussion of the use of certain post-test period results in City of LA v PUC at page 674.

b. Increased classified advertising revenues, notwithstanding their authorization, were not received during the test year in this application, except for \$868,000, and the receipt of this amount has not resulted in excessive earnings.

3. Because of the pendency of Application No. 55492, we are not setting rates for several years into the future in Application No. 55214, and adjustments to any anticipated net revenues resulting for SMRT and/or increase classified (yellow page) advertising rates, including the \$868,000 mentioned in Finding 2(b) are more appropriately considered in Application No. 55492.

Conclusion

Relief requested by San Diego and other parties supporting San Diego should be denied.

ORDER ON REHEARING

IT IS ORDERED that the relief requested on rehearing is denied.

The effective date of this order is the date hereof.

Dated at San Francisco, California, this 26th day of OCTOBER, 1976.

I dissent
Leonard Ross
Commissioner

I dissent
Robert Bateman
Commissioner

[Signature]
President
William J. Quinn, Jr.
[Signature]
Commissioners