

ORIGINAL

Decision No. 88465 FEB 7 1978

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of THE PACIFIC TELEPHONE  
AND TELEGRAPH COMPANY, a corporation  
for a tariff for 770A Package II Dial  
Private Branch Exchange Service.

Application No. 55276  
(Filed October 29, 1974)

Application of THE PACIFIC TELEPHONE  
AND TELEGRAPH COMPANY, a corporation,  
for authority to carry out the terms  
and conditions of agreements with  
certain customers covering the offering  
of 770A Dial Private Branch Exchange  
Service.

Application No. 54881  
(Filed May 16, 1974)

CONSUMERS LOBBY AGAINST MONOPOLIES,  
DAVID L. WILNER, In Pro Per,

Complainant,

vs.

THE PACIFIC TELEPHONE & TELEGRAPH  
COMPANY, a corporation,

Defendant.

Case No. 9794  
(Filed September 23, 1974)

Investigation on the Commission's own  
motion into the rates, rules, charges,  
operations, practices, contracts,  
services, and facilities of THE  
PACIFIC TELEPHONE AND TELEGRAPH  
COMPANY, a California corporation, as  
such relate to the 770A Dial PBX  
System.

Case No. 9838  
(Filed December 10, 1974)

Roger P. Downes, Attorney at Law, for The Pacific Telephone and Telegraph Company, applicant in A.55276 and A.54881, defendant in C.9794, and respondent in C.9838.

David Wilner, for National Semiconductor, Langley-Porter Institute, Independent Journal Newspaper, Envirotech Corporation, Consumers Lobby Against Monopolies, and Rayne Communications, protestants in A.55276 and A.54881, complainant in C.9794, and interested parties in C.9838.

Joel Effron, for Scott-Buttner Communications, Inc., intervenor.

Richard B. Fuller, for Moore Business Forms, Inc., Pacific Division; Roger L. Mosher, for Rolenz Corporation; Otha P. Rice, Jr., for O'Brien, Rice, Quam & Associates; and Allen B. Wagner, Attorney at Law, for Regents of the University of California; interested parties.

Ira R. Alderson, Jr., Attorney at Law, Ermet Macario, and Steven Peopler, for the Commission staff.

# O P I N I O N

## The Cases

Application No. 54881 concerns certain contracts for Package II 770A<sup>1/</sup> service. A prehearing conference was held in that matter on July 13, 1974. On July 16, 1974, by Interim Decision and Order No. 83158, The Pacific Telephone and Telegraph Company (Pacific) was authorized to carry out the terms and conditions of such contracts and to give certain notification to its customers, the protestant, and the Commission staff.

Application No. 55276 is Pacific's application for an initial tariff for Package II 770A service. As originally filed, the proposed rates would have produced approximately \$800,000 per

<sup>1/</sup> The 770A is a type of electro-mechanical Private Branch Exchange (PBX) equipment manufactured by the Western Electric Company and supplied to California customers by applicant, The Pacific Telephone and Telegraph Company.

year of revenue in addition to that generated by existing contract prices. On November 21, 1974, by Interim Decision No. 83761, we authorized Pacific's requested rates, subject to refund and further hearings.

On February 13, 1976, Pacific filed an amended application seeking a further increase based upon more recent cost studies reflecting past and foreseeable inflationary factors. The amendment sought an additional \$788,600 in annual revenues. Package I customers would pay an average 17.4 percent more than the interim rates. Package II customers would find their rates increased by about 11.8 percent.

The complaint in Case No. 9794 asserted that there were several major defects in a previous advice letter concerning this service (A.L. No. 11372 filed August 13, 1974). The principal issue concerns the alleged failure to disclose a proposed increase in rates.

On December 10, 1974, we opened an investigation (Case No. 9838) into all matters concerning the 770A. On the same day we ordered the consolidation of these related proceedings for hearing. Hearings commenced before Administrative Law Judge John C. Gilman on May 1, 1975 and continued from time to time for 17 days of hearing through October 14, 1976. Oral argument was heard on October 29, 1976 in San Francisco.

#### The Parties

The applicant is a telephone corporation providing exchange, private line, mobile, and other communication services within the State of California. Pacific is one of the operating telephone companies which comprise the Bell System. The American Telephone and Telegraph Company (American Telephone) owns approximately 89 percent of the common stock of Pacific and completely owns the Western Electric Company, manufacturer of the 770A. Pacific's rates, terms, and conditions of service to the public (including the 770A) are subject to the jurisdiction of the Commission.

Complainant/protestant David L. Wilner is the sole proprietor of Rayne Communications, a communications consulting firm. In an additional capacity, Mr. Wilner also appeared in these matters representing Consumers Lobby Against Monopolies (Consumers Lobby).

Scott-Buttner Communications, Inc. (Scott-Buttner) is an unregulated supplier of PBX equipment. It is one of several such companies which provide PBX equipment in competition with Pacific's 770A in the California market.

#### History

Pacific has been providing PBX service in California since well before World War II. Such service in those days was normally provided by bulky, slow, and mechanical step-by-step switching equipment. PBX services in this period were exclusively offered by regulated telephone companies under rates, terms, and conditions of service prescribed by the companies' tariffs, subject to regulation by the Commission. During the 50's and 60's, as switching technology advanced, Pacific began offering cross-bar and electronic PBXs to its California market.

In 1968, the Federal Communications Commission (FCC) announced its decision in Carterfone, 13 F.C.C. 2d 420. While the facts and circumstances of that case are not material here, the result of the decision was a substantial growth in the number of customer-owned devices connected to the switched network of the nation's telephone companies. What was formerly a nearly exclusive market for regulated utility PBXs became in the years immediately following Carterfone, an increasingly competitive market in which

unregulated suppliers offer pricing, service, and ownership alternatives to the regulated telephone company's PBX services.<sup>2/</sup> There has also been an acceleration of technical change.

Just prior to the introduction of the 770A PBX, the California Supreme Court issued an opinion which mandated fundamental changes in this Commission's response to issues involving competition and public utilities. (Northern California Power Agency v Public Utilities Commission (1971) 5 Cal 3d 370.)

That appeal was from a Commission decision granting Pacific Gas and Electric Company (PG&E) a certificate to construct a geothermal generating plant in the Geysers area. The plaintiff was a joint powers agency composed of 11 cities which owned and operated municipal public electrical systems. NCPA had attempted to compete with PG&E in acquiring steam rights in order to generate its own geothermal power. After failing to do so, it appeared before the Commission in the certificate proceeding, arguing that the contracts PG&E had used to acquire the steam rights violated federal and state antitrust law. The Commission granted the certificate.

<sup>2/</sup> As we noted in Decision No. 85791, the market share of Pacific has declined significantly.

<u>Year</u> <u>End</u>	<u>Customer</u> <u>PBXs</u>	<u>Interconnect</u> <u>Market</u> <u>Share (%)</u>	<u>Pacific</u> <u>PBXs</u>	<u>Pacific</u> <u>Market</u> <u>Share (%)</u>
1970	52	0.7	8,010	99.3
1971	316	3.7	8,297	96.3
1972	537	5.9	8,643	94.1

By 1976 Pacific's share had declined to approximately 86 percent.

finding that there was no need to consider NCPA's arguments. The Court, however, reversed; it held even though the Commission was not specifically bound by the dictates of the antitrust statutes, that the basic economic concepts underlying that body of law were important components of the public interest. Consequently, the Court held that the Commission was obliged to make findings, draw conclusions, and weigh competitive considerations against other elements of the public interest.

The Commission argued that it had not been provided with the necessary expertise to perform the functions sought by NCPA. The Court brusquely rejected this contention; the opinion indicated that the Court would expect the Commission to be at least as competent in this area as its federal counterparts and remarked that if it lacked the necessary expertise that the Commission was under an unqualified duty to obtain it.

The Commission claimed that NCPA's standing was clouded by the lack of a definite plan to build a geothermal plant. The Court also rejected that theory; it held that the Commission, even in the absence of any protests was required to consider competitive problems on its own motion.

Consequently, the most significant events in this proceeding occurred during a period in which unparalleled technological change, change in the structure of the marketplace, and in the law of regulation all coincided.

For both this utility and the regulators, the transition was neither instantaneous nor uniformly appropriate. Each responded to novel problems with actions which were acceptable or even commendable under previous standards but which were nevertheless not fully responsive to the new problems.

For example, the Commission staff entered this era confident that its primary responsibility was to keep utility rates low. It found itself having to invent ad hoc new procedures to prevent a utility from offering services at assertedly insufficient prices. Likewise, the utility entered the era with a service-type tariff structure for PBXs (the so-called "series" rates). Under this system, each customer receiving similar services would pay the same rate regardless of the type of switching equipment used to provide the service. While individuals within the utility quickly recognized that such a rate pattern would be difficult to defend in litigation with a competitor, it took some time before the company actually made the transition to a type of rate in which individual prices of PBX equipment were separately priced. This type of rate structure is referred to as a hardware rate.

Faced with a competitive change in marked circumstances, Pacific introduced the 770A Package I in the year 1972. This new cross-bar PBX was developed and produced by the Western Electric Company in response to the needs of the operating telephone companies of the Bell System. Competitors claim that it is basically a copy of products offered by them. The modular and cabinetized 770A was an improvement over much of Pacific's then existing product line and as such was a significant factor in the developing competitive market. Pacific sought to introduce Package II (equivalent to 300 series features) later in 1972.

#### Discussion

##### I. Rates

Pacific seeks its first permanent tariff for the Package II 770A system in this proceeding. The positions of the parties on the permanent price level for the service have varied

widely. The nonregulated participant urges a higher rate than sought by the utility. The consumer advocate/communications consultant and the staff have avoided taking a position, while certain customers have opposed the permanent rate levels and suggested reductions. Pacific has produced a cost study on GE-100 forms which we have often relied upon in the past.

There is no disagreement with the basic principle that the rates for the 770A should be at least high enough so that 770A customers are not subsidized by any of the revenues from services which are monopolized by Pacific as a public utility. None of the parties have challenged the view that this is best accomplished by applying conventional costing procedures to develop a full-cost rate for each item of hardware in the 770A system.

One of Scott-Buttner's arguments would have required Pacific to base its PBX rates on the cost of the last item of any particular type of hardware rather than on the average cost of all the items in the inventory. Since such a rule would produce a fair rate of return on the highest priced acquisitions, it would tend to produce excessive rates of return on items acquired at substantially lower cost. Application of this costing principle would tend to make competition less effective. It would tend to promote either profiteering or inefficiency in Pacific's competitors at the expense of Pacific's PBX customers. When Pacific has low-cost items in its inventory, it should be able to pass the savings on to its PBX customers. We will adopt rates based on average procurement costs, and reject Scott-Buttner's proposal.

The principal issue concerning the reasonableness of the proposed rates involves the location and service lives of the 770A PBX. Based on its experience with other PBXs, Pacific proposed a location life of 10 years and a service life of 13 years.



Scott-Buttner asserted that these lives are too long. It claimed that the 770A is already obsolescent, and that this factor in conjunction with accelerating technological change would reduce the location life to 7 years and the service life to 10 years. If Scott-Buttner's prediction should prove correct, there will be a shortfall in the total revenues received by applicant. Scott-Buttner claims that adopting Pacific's proposed rates will thus produce a substantial subsidy of one of applicant's competitive ventures by the general body of ratepayers.

A similar problem was presented in Application No. 55527, which dealt with the SG-1 PBX; we said in Decision No. 85790 in that proceeding:

"All of our concerns would be satisfied, the parties would be fairly treated, and competition between the parties would be price-fair if we could with certainty prescribe rates and charges which will recover actual future costs of service. This we cannot do. If we should inadvertently set Pacific's prices above cost, Pacific's competitors will have an undue competitive advantage. Likewise, prices below cost will give Pacific an undue competitive advantage and result in discrimination between Pacific's customers. . . . Therefore, we shall authorize the rates and charges proposed by Pacific. However, we shall require Pacific to keep separate accounts of the revenues, expenses and plant involved in SG-1 service, and we shall not permit Pacific in future rate proceedings to recoup from its non-SG-1 revenues. Thus Pacific will be authorized to file the rates and charges for SG-1 service it proposes herein to recover costs and to meet the competition." (Mimeo. pp. 7-8.)

Scott-Buttner is now attempting to convince the Commission to reverse the precedent set forth above and instead adopt its own proposed service lives.

If we were to adopt the Scott-Buttner estimated lives, the rates proposed by Pacific would have to be increased about 9 percent in order to maintain the projected rate of return. If we adopt Pacific's estimated lives and if Scott-Buttner's predictions were to prove precisely correct, the error would reduce Pacific's rate of return over the total life of equipment to somewhere between 8.4 and 8.6 percent instead of the intended 10.5 percent. This figure can be contrasted to Pacific's present authorized overall rate of return, 8.85 percent.

Even if Pacific's proposed rates earn only 8.4 to 8.6 percent, Pacific's general ratepayers will have been fully protected by the ratemaking techniques and the special accounting procedures described in Decision No. 85790, supra; Pacific will have met all of its costs including cost of debt and will earn some return for its shareholders.

Thus, adopting Pacific's rates is a safe course of action; all public interests are protected even if its estimates are wrong. On the other hand, if Scott-Buttner's projections are too pessimistic, its proposal would leave PBX customers worse off than if they had dealt either in a free market or with a conventionally regulated monopoly. Therefore, we will not increase the rates above those proposed and will readopt the safeguards devised in the SG-1 proceeding.

No one has claimed that the proposed rates are too high in relationship to Pacific's costs. The difference between Pacific's authorized overall rate of return and the overall 10.5 percent rate of return authorized here is justified alternatively as compensation for the added risk of a competitive venture or as a margin for error in estimating.

## II. Service

The evidence presented by the staff in May of 1975, consisting primarily of a customer survey, tended to show that the 770A was plagued with service difficulties. Pacific asserted that Western Electric had made modifications on the 770As located on customer premises, thus correcting such service deficiencies. The staff submitted the results of a subsequent survey of 770A subscribers in October 1976 which determined that although the 770A tended to have more service difficulties than another Pacific-offered PBX (the NA4-09) "...it appears that the defects in the 770A have been corrected to an adequate degree.". The staff then withdrew its previous recommendation that Pacific be ordered to discontinue offering the 770A because of chronic service difficulties.

There is no question but that the 770A was initially plagued with service problems. In a letter from Pacific to the director of American Telephone's Engineering Department, dated

October 13, 1972, Pacific indicated that one-third of the 770A PBX vehicles installed as of that date "are considered to have serious problems," and set out the various manufacturing and design shortcomings as viewed by Pacific.

It appears that Pacific undertook to market the 770A before all the developmental problems were identified and remedied. In the future, we will expect Pacific not to make a general offering of a PBX until it has reasonable grounds to believe that developmental problems are no longer present. There is, however, no necessary bar to field testing of an unproven new PBX provided that the customers involved have consented to be used as experimental subjects.

The field testing of new telephone devices might well be an appropriate occasion for the use of special contracts under General Order No. 96-A. Any proposal for field testing will have to be scrutinized carefully to determine whether the conditions are fair to customers. Specific areas of concern would include limitation of liability and termination charges. Where field testing is involved, each of these topics may need rules differing from those applied to general offerings.

### III. Marketing Practices

There was significant controversy concerning certain practices of Pacific in marketing the 770A. The issues were:

Is the use of Commission-approved contracts an unfair practice during the period prior to an effective tariff for a competitive service?

Is the use of a factor for "future rate increases" in a computerized communication comparison an unfair marketing practice?

#### (A) Contracts

Pacific had more than 400 contracts for 770A Package II service on file with the Commission at the time the interim tariff for the service was approved. Both Consumers Lobby and Scott-Buttner

have asserted that the use of contracts instead of tariffs to offer the 770A was a device to evade regulatory scrutiny.

If a tariff stating initial rates had been proposed, it would almost certainly have been protested by Consumers Lobby or by a competitor. Under the Commission's nearly invariable practice at that time, the Commission would have responded to a protest by suspending the tariff, without considering the market impact of its action. The suspension would have continued until final decision on the rate issues, causing a long delay in the introduction of the 770A. Pacific thus had a legitimate business reason to avoid delays which could have rendered the 770A obsolete before it was offered to the public. The Commission and its staff have an obligation to ensure that the Commission's procedures do not unnecessarily delay a utility's entry into the marketplace. A regulatory procedure or practice which arbitrarily gives one competitor an artificial advantage in the marketplace is a breach of the Commission's obligations under Northern Calif. Pwr. Agency, supra. (cf. Cal. Motor Transport v Trucking Unlimited (1972) 30 L ed 2d 642.) The practice of using individual contracts was defensible as a means of ensuring that the 770A was marketed without delays caused by disputes over rate levels between competitors.

In any case, Pacific made an early and continuous effort to have the 770A tariffed. The problems that delayed tariffing were largely outside of its control. There is no evidence of footdragging on Pacific's part. Nor is there evidence to support a finding that either contract or interim rates were knowingly set at an unreasonably low level.

One of the principal reasons for requiring a utility to publish all its rates and conditions of service in a tariff is to

prevent or at least deter discrimination. Pacific managed to avoid unlawful discrimination by ensuring that each of the contract prices was based on a common formula. But by so doing Pacific violated another statutory requirement. The common formula became, for all practical purposes, Pacific's rate for the 770A, a rate which under Section 489 of the Public Utilities Code, should have been published in tariffs. ~~Nothing should be done to prevent the use of such contracts.~~

Purportedly these contracts were issued under the authority of paragraph X of General Order No. 96-A. That paragraph is an exercise of the Commission's power to grant deviations (Sections 489 and 532 of the Public Utilities Code). Deviation contracts are intended for use in situations unique or exceptional enough that they cannot practically be dealt with by tariffs. A paragraph X deviation contract should not be used to establish interim rates for a generally offered new service. Under General Order No. 96-A, paragraph IX, any contract for a service which is available to the general public must be included in the utility's tariff. Therefore, we must conclude that the practice of using individually approved contracts in lieu of a tariff was unlawful. However, according to the record the use of de facto contract rates did not, in fact, produce discrimination or an unauthorized rate increase. In balance, it appears that this practice, even though technically illegal, tended to promote competition without violating any overriding public interest.

Staff and protestants urge the Commission to prohibit the future use of untariffed contracts in similar situations. As noted above, that prohibition is implicit in General Order No. 96-A. Therefore, no special prohibition is required. As the Utilities Division proposed, the first general offering of a competitive device must be by tariff, whether interim or permanent.

Since the use of contracts is prohibited, it is imperative to find an alternative means whereby Pacific can offer new PBXs as soon as they are available and properly tested even if it has not completed the costing process. It is also imperative to permit competitors to have at least some interim relief from an allegedly unfair utility rate without keeping the new device off the market altogether. Therefore, we will no longer reject advice letters proposing initial rates for competitive devices because of protests asserting that the rates are too low. Rather, we will use a new form of interim relief, allowing the device to be offered immediately, but at a surcharged rate. The level of the surcharge will be designed to offset any anticompetitive effect or cross-subsidy, and it will be refundable when and if found not to be cost justified.

We will expect any protestant to identify the price of the closest competitive offering available in the market. This will enable us to set the surcharge at a level so that the rates are approximately the equivalent of the market price for the competitive device. If there is no information to establish a market price, we will use whatever cost information that is available to fix the amount of the surcharge. We recognize that even a refundable surcharge will tend to put the utility at a competitive disadvantage. Therefore, expedited hearings will be scheduled on any competitive rate protests. Surcharge relief may be denied or terminated if there is reason to believe that the protests are unsubstantial or not made in good faith.

(B) Future Rate Factor - Unregulated competitors can sell or lease their PBXs at a fixed price or rate. Pacific, however, must always inform its potential customers that its rates are subject to revision and to increase by this Commission. This uncertainty imposes a severe competitive handicap on Pacific. To counter this difficulty Pacific in marketing the 770A provided a complete long-range presentation worth comparison of 770A rates with competitors' prices. One necessary element in this comparison was a projection of future PBX rate increases.

In some instances, Pacific supplied figures as low as 1.1 percent or 3 percent for annual rate increases. Both protestants claim that these representations were fraudulent. These figures were purportedly based on past experience. There has been no showing that these figures were not an accurate description of past experience. Nor was there any showing that any responsible official perceived or understood the changes in the law and regulatory practice which make past experience an unreliable guide for the future.



In all probability Pacific's PBX costs in the next decade will increase by more than 1.1 or 3 percent; it is unlikely that Pacific, even if it wished to do so, could allow its rates to lag significantly behind costs. Therefore the comparisons used by Pacific were unreliable. We cannot find, however, that they were fraudulent.

Protestants contend that we should prescribe, within limits, the representations which Pacific's salesmen can make concerning future rates. We will reject this suggestion. We cannot ourselves predict what PBX rates will be 6 or 10 years hence.

We think the proper response to this problem is not to add another regulation to Pacific's competitive handicaps. Rather we should adopt rate patterns which may make future rate increases an item of minor concern. We have already approved in principle, a two-tier rate structure which is almost the economic equivalent of a sale and maintenance contract which might be offered by an unregulated competitor (Decision No. 83958; Applications Nos. 55242). One of the features of that type of rate is that only the maintenance segment of the customer's total bill will normally be adjusted to reflect inflationary changes. Use of this type of rate will reduce the temptation by any competitor, regulated or unregulated, to emphasize future rates in its sales pitch.

#### IV. Regulatory Procedures

Consumers Lobby asserts that the utility violated the Commission's Rules when it filed Advice Letter No. 11372 in 1974. That advice letter proposed to substitute tariff rates for the contracts then in effect for the 770As. The tariff rates would have increased the amounts paid by existing contract customers. Pacific, nevertheless, used the advice letter procedure appropriate for an initial rate.<sup>3/</sup> The advice letter included the traditionally required statement indicating that the proposal would not "increase any rate or charge."

<sup>3/</sup> Compare Section 454(a) of the Public Utilities Code with Section 4.

Consumers Lobby argues that this statement was fraudulent on the basis that the contracts collectively constituted a rate. Our staff, after protest by Consumers Lobby, adopted the argument that this was an increase in a de facto rate and requested detailed information on the revenue change. The advice letter was ultimately withdrawn and Application No. 55276 was substituted.

The challenged statement, even though incorrect as a matter of law, cannot be found fraudulent unless the responsible utility officials knew or should have known that the statement was incorrect.

The responsible official testified that he questioned the statement and was informed by other utility officials with experience in California regulation that the contracts did not constitute a rate and that the proposed tariff was therefore an initial, rather than an increased, rate.

That advice was a correct description of the traditional staff view at that time. The staff's adoption of the de facto rate theory marked a change in position.

Since the statement was made in reliance on a staff practice, we can hardly find that this reliance was misplaced. In any case, the staff's timely change in position prevented the statement from having any adverse impact either on the Commission or on customers.

#### V. Policy Statement

This is not a case such as NCPA, supra, where the Commission is called upon to determine whether and to what extent competition is required by the public interest. In the PBX market, full competition by unregulated companies is an established fact.

Our obligation is, therefore, to tailor our regulatory activities to ensure that the public receives the maximum possible benefit from the competition that does exist.

Statutes provide some limitations on our freedom of action to adjust to competitive situations. We could not, for example, find that competition excuses us from the duty to make formal findings whenever Pacific seeks to increase a competitive rate (Section 454 of the Public Utilities Code). It might, however, permit us to find that a rate was not unreasonably high based simply on a showing that it is controlled by effective competition.

Thus, the existence of competition may permit the relaxation of some of the requirements which were necessary to protect consumers when the utilities had a monopoly on PBX service. It creates new responsibilities, however, to ensure that our residual regulatory efforts do not give the regulated entities unintended competitive advantages or disadvantages. We must also be sure that the utilities do not abuse their natural and legal monopoly over most other forms of telephone service by using it as a source of excessive revenues with which to subsidize competitive ventures.

Our objective in regulating the future competitive ventures of communication utilities is to allow competition to have the maximum impact on the market behavior of both regulated and unregulated competitors. In order to accomplish this objective, we will develop procedures which allow utilities to act as much like unregulated competitors as possible.

There are, of course, limits to the amount of freedom we can allow. Statutory requirements must be observed and we must also be vigilant to ensure that revenues from the general ratepayer are not used to subsidize the competitive activity. Also, we will feel free to impose special disclosure rules on utilities if necessary to ensure that consumers can intelligently exercise their freedom of choice. We will continue to expect that all utility equipment meets high standards of safety and reliability regardless of whether it is offered in a competitive environment. Finally, of course, our complaint procedure is available to all utility customers regardless of whether a competitive product or service is involved.

In the findings which follow, we have not attempted a factual analysis of the market impact of Pacific's new rates.

Competitors, who produce comparable equipment at equal or lower cost, presumably need no protection from a competitor who cannot beat their prices. Competitors with higher costs likewise cannot claim any protection from us. If they are affected by Pacific's competition, they have the option of abandoning the market, finding a method of cutting costs or surviving at reduced profit levels.

We have not instituted sua sponte investigations of Pacific's early marketing practices or rates, since our primary concern is with strengthening future competition, not with past conduct, especially when apparently not in violation of any specific statute or order.

Findings

1. The 770A is an electro-mechanical private branch exchange manufactured by the Western Electric Company.
2. Pacific has been attempting to establish a permanent tariff for Package II 770A since 1972.
3. In the period prior to the establishment of an interim tariff for Package II 770A, Pacific satisfied customer demands for such service by filing contracts with the Commission under the provisions of General Order No. 96-A.
4. The record does not show that the revenues received by Pacific under contract or under interim rates were less than the total costs of providing service to those customers at the time such rates were instituted.
5. The 770A was offered generally to the public under individual contracts.
6. Each of Pacific's contracts for the 770A set prices based on a uniform formula.

7. Advice Letter No. 11372 was filed by Pacific with the statement, "This filing will not increase any rate or charge." The rates set forth in that advice letter were an increase over contract rates.

8. Pacific reasonably believed that a group of contract services did not constitute a rate.

9. Pacific had no sufficient reason to believe that statement incorrect as a matter of law.

10. Pacific filed amended Application No. 55276 on February 13, 1976.

11. The 770A PBX rates sought by Pacific in the amended application seek to recover the costs of service as reflected in the GE-100 cost studies attached as Exhibit "D" to the amended application.

12. The rates and charges proposed by Pacific will not recover revenues in excess of reasonable costs of service plus fair return.

13. The rates proposed for the 770A PBX system as found in Exhibit "C" to the amended application fully recover the appropriate costs as identified in Pacific's GE-100 cost studies including a fair return.

14. Pacific should adopt the special accounting rules and procedures set forth in Ordering Paragraphs 2 and 3. Used in pending and future rate cases, these will prevent subsidization of Pacific's competitive ventures, even if PBX rates yield revenues which are insufficient to cover costs.

15. If Pacific earns significantly more than 10.5 percent for the 770A PBX, its return will be excessive. It would earn significantly more than a 10.5 percent rate of return if Pacific's proposed rates were increased to the levels proposed by Scott-Buttner and if the longer lives projected by Pacific actually occur.

16. The rate of return to be produced by the rates proposed in Exhibit "C" to the amended application is 10.5 percent.

17. There is no objective reason to select either Pacific's or Scott-Buttner's estimate of lives. The rates adopted herein will produce returns of 8.4 to 8.6 percent if location life is 7 years and service life is 10 years.

18. The authorized overall rate of return for the applicant is 8.85 percent.

19. Based upon the record herein, the increases in 770A rates and charges authorized herein are justified; the rates and charges authorized herein do not exceed reasonable levels and are not unreasonable; and the present 770A rates and charges insofar as they differ from those prescribed herein, are for the future unjust and unreasonable.

20. Interim Decision No. 83158 granted Pacific the full authority requested in Application No. 54881.

21. Pacific sales personnel use a computerized communications analysis called the COMPAR.

22. The COMPAR is used to analyze and compare non-Bell system leases, lease-purchases, and purchases of equipment with Bell's (applicant's) rental of equipment.

23. One element of the COMPAR is an estimate of an anticipated amount for future Bell rate increases.

24. Applicant's sales personnel have in several instances projected future PBX rate increases averaging 1.1 - 3 percent per year, while selling the 770A.

25. No showing has been made that the figures used by Pacific's sales personnel were not accurate representations of past experience.

26. There is no evidence to show that Pacific's sales personnel who used the rate increase figures had knowledge or understanding of circumstances which might require more rapid increases in the future.

27. The current policies and procedures of the Commission are inadequate with regard to the handling of protests, complaints, advice letters, applications, and contracts for competitive services of a utility.

28. Expedited handling of a regulated competitor's rate requests is required. Uncertainty over rates can place a regulated competitor at a disadvantage.

29. A utility's rate application, or advice letter for a competitive service, should contain an adequate showing of lawfulness of rates. Introduction of a new offering should, however, not be delayed if the showing has minor defects.

30. An immediate interim tariff, at rate levels high enough so as to make refunds at a later date probable, is preferable to a lengthy regulatory delay of a competitive offering of a regulated public utility.

31. The Commission has a basic responsibility to devise procedures which neither handicap nor unduly benefit a regulated competitor.

32. No practice, policy, or procedure of the Commission should enable a competitor to unduly delay introduction of a utility offering in a competitive market. Our staff, however, has established informal practices to clear tariffs before formal filing; this decision is not intended to modify that practice.

33. Requiring a formal application for initial pricing of a competitive device would impose unnecessary delay and formality. The Commission staff can require supplementary cost information and notice to interested parties when an advice letter is filed.



34. The use of contracts avoided delay in introducing the 770A. The use of contracts did not result in discrimination or unauthorized rate increases.

35. The contract and interim rates were not intended to deceive customers or disturb competition.

36. The 770A PBX is now rendering generally adequate service to the public.

37. Pacific should not in the future provide untested equipment to the public. Experimental offerings may be authorized, provided there is full disclosure to the customers and full staff review of the terms and conditions, including termination charges and limitation of liability.

38. It would be premature to modify General Order No. 96-A at this time.

#### Conclusions

1. Pacific's amended Application No. 55276 for 770A PBX rate increases should be granted.

2. Pacific should be required to set up and maintain separate accounts for revenues, expenses, and plant, attributable to rendering 770A PBX service.

3. As a part of its showing in support of any future requests for authorization to generally increase rates, Pacific should be required to report the annual amounts by which the costs of rendering 770A service exceed the revenues derived from rendering the service.

4. Pacific should be required to set up and maintain separate accounts and supporting data for depreciation expense and reserve accruals for the 770A system.

5. The relief requested in Case No. 9794 should be denied.

- IT IS ORDERED that:

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date of the revised schedule shall be the date of filing. The revised schedule shall apply only to service rendered on and after the effective date.

2. On or before April 30, 1978, Pacific shall install, and thereafter maintain until further order of this Commission, separate accounts in which shall be recorded revenues, expenses, and plant attributable to rendering 770A PBX service subsequent to the effective date of this order. Memorandum accounts shall be developed and maintained for 770A revenues, expenses, and plant prior to the effective date of this order.

3. In addition to the data required by Rule 23 of the Commission's Rules of Practice and Procedure for a rate increase application, Pacific shall include as an exhibit annexed to future general rate increase applications the annual amounts by which the costs of rendering 770A PBX service exceed its revenues.

4. On or before April 30, 1978, Pacific shall install, and thereafter maintain, separate accounts and supporting data for depreciation expense and reserve accruals for the 770A system. Pacific shall be prepared at all times to report until further order the annual actual depreciation accruals for the 770A PBX plant and the amounts which would result from applying the lives estimated in the GE-100 cost studies attached as Exhibit "D" to the amended application in this proceeding.

5. Application No. 54881 is dismissed.
6. The relief requested in Case No. 9794 is denied.
7. The investigation in Case No. 9838 is terminated.

The effective date of this order shall be thirty days  
after the date hereof. ✓

Dated at San Francisco, California, this 7th  
day of FEBRUARY, 1978.

Robert Batimael  
President  
William J. Lyons Jr.  
William L. Lichten  
Charles D. Howell  
David L. D. D.  
Commissioners

EXCHANGE TELEPHONE SERVICE  
 PRIVATE BRANCH EXCHANGE SERVICE

XI. MODULAR DIAL PBX SERVICE - CLASS A

APPLICABILITY

Applicable to Modular Dial PBX Service - Class A

TERRITORY

Within the exchange area of exchanges as said areas are defined on maps filed as part of the tariff schedules.

CHARGES AND RATES

(1) Type I System (T70A)

- Capacity 400 station lines:

- (a) Initial common equipment for 40 station lines and 3 simultaneous talk paths, including batteryless power plant and capacity for 3 consoles and 9 trunk units for terminations of trunk lines, tie lines, interexchange private line telephone service lines and supplemental services.

	USOC	BTC*	IC	MR
Feature Package 1 (T)	TAP	\$2,200.00	\$2,200.00	\$ 255.25(I)
Feature Package 2 (T)	TAPF2	2,400.00	2,400.00	297.80(I)

- (b) Additional common equipment for 40 station lines and for more simultaneous talk paths, including capacity for 3 trunk units for terminations of trunk lines, tie lines, interexchange private line telephone service lines and supplemental services.

Feature Package 1 (T)	TAR	600.00	600.00	81.15(I)
Feature Package 2 (T)	TARF2	750.00	750.00	109.75(I)

See Special Conditions: \*6

Continued

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EXCHANGE TELEPHONE SERVICE  
PRIVATE BRANCH EXCHANGE SERVICE

XI. MODULAR DIAL PBX SERVICE - CLASS A - Continued

CHARGES AND RATES - Continued

(1) Type I System (770A) - Continued

- Capacity 400 station lines: - Continued

Note: The maximum number of simultaneous talk paths which may be included in a Type I system at the above Charges and Rates are:

System Capacity  
(Station Lines)

Simultaneous  
Talk Paths

Up to 80  
81 to 160  
161 to 240  
241 to 320  
321 to 400

3  
4  
5  
6  
7

Continued

APPENDIX A  
Page 3 of 14

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## EXCHANGE TELEPHONE SERVICE

## PRIVATE BRANCH EXCHANGE SERVICE

## XI. MODULAR DIAL PBX SERVICE - CLASS A - Continued

## CHARGES AND RATES - Continued

## USOC

## BTC\* - ICDAR CEA CEMRANO

## (2) Type II System (770A)

- Capacity 400 station lines: *See Appendix A - ICDAR CEA CEMRANO*

- (a) Initial common equipment for 40 station lines and 4 simultaneous talk paths, including batteryless power plant and capacity for 3 consoles and 20 trunk units for terminations of trunk lines, tie lines, interexchange private line telephone service lines and supplemental services.

Feature Package 1	(T)	HH2	\$2,400.00	\$2,400.00	\$ 301.35(I)
Feature Package 2	(T)	HH2P2	2,700.00	2,700.00	354.15(I)

- (b) Additional common equipment for 40 station lines and for more simultaneous talk paths, including capacity for 10 trunk units for terminations of trunk lines, tie lines, interexchange private line telephone service lines and supplemental services.

Feature Package 1	(T)	HH5	650.00	650.00	91.25(I)
Feature Package 2	(T)	HH5P2	1,000.00	1,000.00	155.90(I)

See Special Conditions: \*6

Continued

## EXCHANGE TELEPHONE SERVICE

## PRIVATE BRANCH EXCHANGE SERVICE

## XI. MODULAR DIAL PBX SERVICE - CLASS A - Continued

## CHARGES AND RATES - Continued

(2) Type II System (770A) - Continued  
- Capacity 400 station lines: - Continued

Note: The maximum number of simultaneous talk paths which may be included in a Type II system at the above Charges and Rates are:

System Capacity  
(Station Lines)Simultaneous  
Talk Paths

40  
80  
120  
160  
200  
240  
280  
320  
360  
400

4  
5  
7  
8  
10  
11  
12  
14  
15  
16

Continued



APPENDIX A  
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## EXCHANGE TELEPHONE SERVICE

## PRIVATE BRANCH EXCHANGE SERVICE

## XI. MODULAR DIAL PBX SERVICE - CLASS A - Continued

## CHARGES AND RATES - Continued

BASIC RATES - BASIC RATES

				USOC	BTC*	IC	MR
(3) Consoles for direct termination of trunk lines - Types I and II Systems:							
(a) Capacity for 12 trunk lines and 100 station lines, including console common equipment (23 Type):	(T)						
Feature Package 1 or 2	(T)						
1. First console	72A				\$ 550.00(R)	\$ 550.00(R)	\$ 64.45 (I)
2. Second console	PCL				600.00(R)	600.00(R)	74.95 (I)
(b) Capacity for 30 trunk lines and 200 station lines, including console common equipment (53 Type):	(T)						
Feature Package 1 or 2	(T)						
1. First console	7TD				650.00(R)	650.00(R)	69.65 (I)
2. Second console	7TA				650.00(R)	650.00(R)	83.45 (I)
(c) Capacity for 30 trunk lines, without busy lamp or direct station selection field, including console common equipment (43 Type):							
Feature Package 1 or 2	7AF				550.00	550.00	57.00 (T) (D)
- Maximum of one console in a system which is equipped with up to 3 switched loop console							

\* - BASIC RATES

APPENDIX A  
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## EXCHANGE TELEPHONE SERVICE

## PRIVATE BRANCH EXCHANGE SERVICE

## XI. MODULAR DIAL PBX SERVICE - CLASS A--Continued

## CHARGES AND RATES - Continued

			USOC	BTC*	IC	MR
(4) Consoles for switched loop operation - Types I and II Systems:						
(a) Capacity 100 station lines and 20 trunk lines, including console common equipment (23 Type):	(T)					
Feature Package 1 or 2	(T)					
1. First console		72D	\$ 700.00(R)	\$ 700.00(R)	\$ 94.00(I)	
2. Second console		72E	550.00(R)	550.00(R)	52.75(I)	
(b) Capacity 200 station lines and 20 trunk lines, including console common equipment (53 Type):	(T)					
Feature Package 1 or 2	(T)					
1. First console		7SD	700.00(R)	700.00(R)	98.75(I)	
2. Second console		7SA	550.00(R)	550.00(R)	57.80(I)	
(c) Additional 20 trunk line capacity for consoles		7AV		110.00	24.15(I)	

See Special Conditions: \*6

Contin

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## EXCHANGE TELEPHONE SERVICE

## PRIVATE BRANCH EXCHANGE SERVICE

## XI. MODULAR DIAL PBX SERVICE - CLASS A - Continued - EXCLUDED FROM CLASSIFICATION

## CHARGES AND RATES - Continued

Excluded - CHARGE FOR CHARGE

	USOC	IC	MR
(5) Module to increase capacity of console from 200 to 400 station lines in the busy lamp or direct station selection field	7CB	\$ 290.00	\$ 20.80(R)
(6) Trunk unit, capacity one trunk line			
Feature Package 1 or 2 (T)			
Outgoing only	7B4	25.00	3.20(I)
Incoming and outgoing, or incoming only	7B8	41.00	6.90(I)
(7) Attendant-Controlled Dial Conference Arrangement, Capacity 5 lines			
Feature Package 1, Only (T)	7BX	80.00	15.60(R)
(8) Supplemental attendant trunk from common equipment to console	(T) P25AA		1.25
(9) Battery Power Plant			
			Charges and Rates (C) applicable to Type A Battery Plants, Section XIV, A. General of this Schedule (C)

Continued

APPENDIX A  
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## EXCHANGE TELEPHONE SERVICE

## PRIVATE BRANCH EXCHANGE SERVICE

## XI. MODULAR DIAL PBX SERVICE - CLASS A - Continued

## CHARGES AND RATES - Continued

	USOC	IC	MR
(10) Trunk unit for access to:			
(a) Dial code calling or dial dictation* (C) 7D3	\$55.00(I)	\$6.25(R)	
- Capacity of 1 dial code calling circuit or 2 dial dictation circuits			
(b) Loudspeaker paging	7R9	39.00(I)	5.70(R)
- Capacity of 1 circuit (C)			
(11) Trunk unit for termination of a tie line or private line telephone channel in common equipment	7AM	240.00(I)	23.30(I)
(D)			
(D)			
(12) Each intercepting trunk unit for unassigned station lines of a system	44H	30.00	4.90
(13) Executive Override circuit, each*	TEO	47.00	6.00
(14) Executive Ringback circuit, each*	TEP	49.00	6.25
(15) Simultaneous talk paths in addition to those included with common equipment			
Each four simultaneous talk paths	7WN	130.00	19.70(I)
(16) Call transfer of Outgoing Calls by Stations**			
Each trunk line arranged	7T3	26.00	1.95(I)
(17) Stutter Dial Tone			
Each dial transfer trunk arranged	7E6AA	6.00(R)	.90(I)

(D)

See Special Conditions: \*7  
\*\*9

Continued

APPENDIX A  
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## EXCHANGE TELEPHONE SERVICE

## PRIVATE BRANCH EXCHANGE SERVICE

## XI. MODULAR DIAL PBX SERVICE - CLASS A - Continued

## CHARGES AND RATES - Continued

	<u>USOC</u>	<u>IC</u>	<u>MR</u>	
(18) Automatic Call Queuing Feature for Consoles in Switched Loop Systems	7QS	\$ 25.00	\$8.50	(T)
- One feature required for each system				(D)
(19) Timed Reminder Feature for Switched Loop Systems*	TRMCE	16.00	3.80	(T)
- One feature required for each attendant trunk circuit				(D)
(20) Subsequent-equipment additions	SCO			(N)
				(N)

See Special Conditions: \*10.

Continued

## EXCHANGE TELEPHONE SERVICE

## PRIVATE BRANCH EXCHANGE SERVICE

## XI. MODULAR DIAL PBX SERVICE - CLASS A - Continued

## SPECIAL CONDITIONS

## 1. General

## a. Terms

In the application of the tariff schedules, the terms "console" and "common equipment", as used in connection with Modular Dial PBX Service - Class A, are construed as the equivalents of the terms "cordless service attendant position" and "dial switching equipment", respectively, as used in connection with Commercial, Hotel, and Residence Manual and Dial PBX Service.

## b. Trunk Line Service, Messages or Local Units and Stations

Trunk lines, messages or local units and stations will be furnished with Modular Dial PBX Service - Class A at the charges and rates and special conditions specified for Commercial, Hotel, and Residence Manual and Dial PBX Service.

## c. Minimum Requirements

The minimum number of consoles, trunk lines, and station lines comprising a Modular Dial PBX - Class A system is the same as for Commercial, Hotel, and Residence Manual and Dial PBX systems.

## d. Auxiliary and Subsidiary PBX Systems

The special conditions applicable to auxiliary and subsidiary PBX systems furnished under this schedule are the same as the special conditions applicable to auxiliary and subsidiary PBX systems furnished in connection with Commercial, Hotel, and Residence Manual and Dial PBX Service.

## e. Availability and Stop Hunting Control Arrangement, Tie Line Service, Exchange and Toll Message Diverting Equipment

Charges and rates and special conditions of Schedule Cal.P.U.C. Nos. 12-T, VI. "Tie Line Service", VII. "Exchange and Toll Message Diverting Equipment" and 32-T, "Availability and Stop Hunting Control Arrangements", apply to such services when furnished with Modular Dial PBX Service - Class A.

Continued

## APPENDIX A

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## EXCHANGE TELEPHONE SERVICE

PRIVATE BRANCH EXCHANGE SERVICE

## XI. MODULAR DIAL PBX SERVICE - CLASS A - Continued

## SPECIAL CONDITIONS - Continued

## 2. Features

## a. Feature Package 1 (T)

## CONSOLE

Busy Lamp Field

Call Transfer by Attendant

Night Connection by Attendant

Trunk to Station Connection

## STATIONS

Station-to-Station Dialing

Direct Outward Dialing

Station Hunting

Restriction of Outgoing Calls

## b. Feature Package 2 (T)

In addition to the equivalent features of Feature Package 1, the following features will be provided:

## CONSOLE

Direct Station Selection

Camp-on

Attendant-Controlled Dial Conference

## STATIONS

Indication of Camp-on

Call transfer by stations

Consultation Hold

Add-on Conference

Trunk Answer Any Station

## c. System

Batteryless Power Plant

Continued

## EXCHANGE TELEPHONE SERVICE

## PRIVATE BRANCH EXCHANGE SERVICE

## XI. MODULAR DIAL PBX SERVICE - CLASS A - Continued

## SPECIAL CONDITIONS - Continued

## 3. Capacities

## a. Common Equipment

The maximum capacity of the common equipment is 400 station lines. The capacity of the common equipment may be reduced by the number of station lines required for use with additional features furnished in connection with the service.

## b. Console

A maximum of two consoles for direct termination of trunk lines or three consoles for switched loop operation may be provided per system.

A console for direct termination of trunk lines and without a busy lamp or direct station selection field may be added to an installation of from one to three consoles for switched loop operation.

Each console is provided with an attendant's handset or a headset telephone set with single head receiver at the customer's option.

When the station line capacity of the common equipment exceeds 200 station lines, only up to 200 of the station lines may appear in the busy lamp field of the console.

The 200 station line capacity of the busy lamp or direct station selection field of the console may be exceeded by furnishing the "Module", Charges and Rates (5), above.

## 4. Cable

The charges and rates for consoles include 100 feet of cable between the associated common equipment and the console on the same or different premises on the customer's continuous property.

Where facilities and operating conditions permit, cable in excess of 100 feet may be furnished on the same or different premises on the customer's continuous property, at a charge equal to the estimated cost of labor and nonrecoverable material used.

## 5. Attendant-Controlled Dial Conference Arrangement

The attendant-controlled dial conference arrangement allows the connection of up to five station lines in addition to the attendant. One tie line or one trunk line may be substituted for one station line. An interexchange private line telephone service line may be furnished instead of a tie line, where facilities and operating conditions permit.

Continued



## EXCHANGE TELEPHONE SERVICE

## PRIVATE BRANCH EXCHANGE SERVICE

## XI. MODULAR DIAL PBX SERVICE - CLASS A - Continued

## SPECIAL CONDITIONS - Continued

## 6. Basic Termination Charges

If at any time during the five-year period following the installation of the common equipment or consoles, such equipment is disconnected, as a result of a request of the customer or disconnection of customer's telephone service in accordance with Utility's applicable tariffs, the customer shall pay to the Utility, upon demand, the basic termination charge specified in Charges and Rates, above, less a credit of one-sixtieth ( $1/60$ ) of said charge for each month between the date on which it was so disconnected. For the purpose of computing basic termination charges, the last equipment installed shall be considered to be the first equipment removed. (T)

## 7. A system may be arranged with either Executive Override circuits or Executive Ringback circuits but not with both in the same system.

The number of Executive Override circuits or Executive Ringback circuits which may be provided in a system is subject to the limitations of the common equipment for that system.

These circuits are furnished only with those systems for which they are adapted. Other systems will require rearrangements to make them adaptable for these circuits. Charges for these rearrangements are applicable in accordance with Schedule Cal.P.U.C. No. 28-T, III, MOVE AND CHANGE CHARGES, Other Equipment and Wiring.

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EXCHANGE TELEPHONE SERVICE

PRIVATE BRANCH EXCHANGE SERVICE

XI. MODULAR DIAL PBX SERVICE - CLASS A - Continued  
SPECIAL CONDITIONS - Continued

8. Changes in types of systems, Packages 1 and 2, and consoles may be made at charges listed below:

From Type I to Type II Difference between BTC, IC and MR  
From Package 1 to Package 2 Apply remaining portion of difference in BTC  
From Type II to Type I Apply remaining portion of difference in BTC  
From Package 2 to Package 1 New BTC and IC applicable to console installed  
Change to console of larger or smaller capacity or change in type of console.

9. Call Transfer of Outgoing Calls by Stations  
This feature may be provided only on trunk lines arranged for "Call transfer by stations". The trunk lines must have the capability of handling incoming and outgoing calls (two-way operation).

The number of trunk lines arranged with this feature in a system is subject to the limitations of the common equipment for that system.

This feature may be furnished only with those systems for which it is adapted. Other systems will require rearrangements to make them adaptable for this feature. Charges for these rearrangements are applicable in accordance with Schedule Cal.P.U.C. No. 28-T, II., Move and Change Charges, Other Equipment and Wiring.

10. The Timed Reminder Feature operates when an attendant-connected call has not been answered within a predetermined interval. The length of the interval must be selected by the customer, within the limitations of the system, prior to the installation of the feature in the system. Charges for changes in the length of the predetermined interval subsequent to the installation of the feature are applicable in accordance with Schedule Cal.P.U.C. No. 28-T, II., Move and Change Charges, Other Equipment and Wiring.