RR/lq

Decision No. 92247 SEP 16 1980

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

ORIGINAL

Application of CONTINENTAL TELEPHONE COMPANY OF CALIFORNIA, a corporation, for an order authorizing it to issue and sell $30,000,000 of its First Mortgage Bonds, Series Q, through a negotiated private placement, and to execute a Nineteenth Supplemental Indenture.	Application No. 59874 (Filed August 12, 1980)

OPINION

Continental Telephone Company of California (Continental) requests authority, pursuant to Sections 816 through 818 and 851 of the Public Utilities Code, (a) to issue and sell through private placement its First Mortgage Bonds, Series Q, (New Bonds) in an aggregate principal amount not to exceed $30,000,000 and (b) to execute and deliver a Nineteenth Supplemental Indenture. Notice of the filing of the application appeared on the Commission's Daily Calendar of August 14, 1980.

Continental is a California corporation (a subsidiary of Continental Telephone Corporation, a Delaware corporation) primarily engaged in the business of furnishing local and toll telephone service in portions of Arizona, California and Nevada. For the Calendar year 1979, Continental reported total operating revenue of $131,702,732 and net income of $17,843,151. In the twelve months ended June 30, 1980, Continental reported total operating revenues of $136,883,666 and net income of $17,547,282.

Continental proposes to issue and sell $30,000,000 aggregate principal amount of its First Mortgage Bonds, Series Q, under an existing indenture as heretofore amended and supplemented and to be further supplemented and amended by a proposed Nineteenth Supplemental Indenture. The proposed supplemental indenture is to be substantially in the same form as the form of the Eighteenth Supplemental Indenture attached as Exhibit C to Application No. 59693 (filed May 27, 1980, and authorized by Decision No. 91983, dated July 2, 1980), with such changes as are required to reflect the terms negotiated for the New Bonds.

It is proposed that the New Bonds will be sold by private placement to institutional investors. Immediately after the issuance of this decision, Continental intends to negotiate the terms of the New Bonds, with issuance and delivery delayed to February 1981. The terms of the New Bonds will be fixed at the time of such negotiation and will be embodied in a purchase agreement substantially in the same form as Exhibit E to Application No. 59693, with such changes as are necessary to reflect the terms of the New Bonds. Continental expects to execute the purchase agreement before the end of September 1980.

The proceeds of the sale of the New Bonds will be applied to retire short-term debt (estimated to be $28,580,000 at December 31, 1980 and in excess of $30,000,000 at the time the New Bonds are issued). The proceeds of such short-term obligations have been spent by the utility for capital additions and improvements. The expenses of the issue will be paid from the company's general funds and not from the proceeds received from the sale of the New Bonds.

Continental's balance sheet as of June 30, 1980, attached to the application as Exhibit A, is summarized as follows:

Assets	Amount
Total Telephone Plant Less Accumulated Depreciation	$316,556,117
Investments	657,411
Current Assets	24,496,879
Deferred Charges	856,932
Total	$342,567,339
Liabilities and Other Credits	
Common Equity	$137,362,806
Preferred Stock	14,555,100
Long-Term Debt	147,832,146
Current Liabilities	27,810,428
Deferred Credits	15,006,859
Total	$342,567,339

Continental's estimated capital ratios at December 31, 1980, and adjusted on a pro forma basis to give effect to the sale of the New Bonds, are summarized from Exhibit B attached to the application as follows:

	December 31, 1980	Pro Forma
Long-Term Debt	48.9%	53.5%
Preferred Stock	4.8	4.4
Common Equity	46.3	42.1
Total	100.0%	100.0%

Continental's plant available for the issuance of additional securities at June 30, 1980 is summarized from Exhibit B to the application as follows:

	Detail	Amount
Telephone Plant, Net of Depreciation		$316,330,000
Less: Deferred Taxes	$3,916,000	
Unamortized Investment Credit	8,264,000	12,180,000
Telephone Plant Available for Issuance of Securities		$304,150,000
Less Securities Outstanding:		
Proceeds from Common Stock	$ 12,545,000	
Proceeds from Preferred Stock	15,111,000	
Principal Amount of Long-Term Debt	149,409,000	177,065,000
Total Telephone Plant Available for Issuance of Additional Securities		$127,085,000

Continental requests an exemption for the proposed sale of the New Bonds from the Commission's competitive bidding rule established by Decision No. 38614, dated January 15, 1946, as amended from time-to-time in Case No. 4761. Continental's reasons for requesting an exemption are set forth in its application as follows:

"(a) In the past five years, Continental has been successful in raising substantial long-term debt capital through private placement at effective interest costs at least as favorable as those which would have been available through a competitive bid public offering. This has resulted from both the timing flexibility of and the lower costs associated with a private placement. Applicant believes that the cost savings for the proposed New Bonds in the form of reduced filing fees, printing costs, accountant's fees, attorney's fees and underwriting discounts will amount to approximately 20-25 basis points on $30,000,000."

"(b) Based on applicant's analysis of current market conditions, applicant believes that a private placement negotiated and committed in September 1980 for delayed delivery in February 1981 will result in a lower nominal interest rate than the sale of New Bonds at competitive bid in February 1981. Applicant believes that private placement is the only practicable method to achieve the delayed delivery arrangements proposed. This can only be accomplished with an exemption from competitive bidding requirements."

"(c) As shown in Exhibit B, the substantial amounts of capital which applicant is required to raise in the long-term debt market to finance its construction program is depressing applicant's long-term interest coverage. In addition to the proposed New Bonds to be sold in February 1981, applicant must issue $25,000,000 of additional bonds in December 1981 to refund its outstanding Series K Bonds

> maturing on January 15, 1982. Applicant believes it must keep its interest coverage above 3.0x in order to maintain on "A" rating on its bonds. Applicant expects, however, that until it obtains rate relief in its pending NOI No. 27 an/or in Pacific Telephone and Telegraph Company's pending Application No. 59849, its interest coverage will stay slightly below 3.0x. Applicant believes that this circumstance will have less of an adverse impact on the interest rate for the New Bonds if they are sold at private placement rather than in a competitive bid public offering."

In Decision No. 91984, dated July 2, 1980 for the San Diego Gas & Electric Company, Application No. 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 the proposed New Bonds will be sold by private placement on terms which will be negotiated after the issuance of this decision and because of the staff'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, in this proceeding, the Commission's competitive bidding requirements and conditions set forth in Decision No. 91984, would not be in the best interests of Continental or its ratepayers. The rule would not operate in a manner so as to allow Continental's sale of the New Bonds at the most favorable cost of money. However, we will also grant Continental the authority to issue the proposed New Bonds by means of a competitive offering.

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 interest expense if it is determined that the cost of money incurred was not the most prudent.

Exhibit B to the application shows Continental's estimated net construction expenditures estimated for calendar years 1980 and 1981 will approximate $111,221,000. Exhibit B sets forth in detail the company's construction program estimated as follows:

	(In Thousands of Dollars) 1980	1981	Total
Construction and Plant Expenditures (Including Cost of Removal):			
Station Apparatus and Connections	$ 7,448	$ 3,889[1]	$ 11,337
Other Operations (Key Systems, Special Systems, Furniture and Work Equipment)	4,598	4,762	9,360
Outside Plant	15,959	16,279	32,238
Central Office Equipment	19,837	20,408	40,245
Land and Buildings	837	902	1,739
Other	2,538	2,169	4,707
Overheads	7,666	8,788	16,454
Total Construction and Plant Expenditures	$58,883	$57,197	$116,080
Salvage Value	(2,717)	(2,142)	(4,859)
Net Construction and Plant Expenditures	$56,166	$55,055	$111,221

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

1/ Assumes station connections will be expensed in 1981.

Findings of Fact

1. Continental is a California corporation operating under the jurisdiction of this Commission.

2. The proposed First Mortgage Bonds, Series Q, would be for proper purposes.

3. Applicant 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 First Mortgage Bonds through negotiated private placement for delayed delivery in February 1981, as low as or lower than it could obtain from a competitive bid public offering of such bonds in February 1981 and should be authorized to proceed in the manner described in the application.

5. The money, property or labor to be procured or paid for by the issuance and sale of the First Mortgage Bonds, herein authorized, is reasonably required for the purposes specified herein, which purposes are not, in whole or in part, reasonably chargeable to operating expenses or to income.

6. The sale of the proposed bonds should not be required to be through competitive bidding.

7. The proposed Supplemental Indenture would not be adverse to the public interest.

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

ORDER

IT IS ORDERED that:

1. Continental Telephone Company of California on or after the effective date hereof and on or before December 31, 1980, may issue, sell and deliver its First Mortgage Bonds, Series Q, in an aggregate principal amount not to exceed $30,000,000 hereby exempted from the Commission's competitive bidding rule and in accordance with the terms and conditions to be negotiated as described in the application, or may issue, sell and deliver these bonds by means of a competitive offering.

2. Continental Telephone Company of California may execute and deliver a Nineteenth Supplemental Indenture in substantially the same form as that attached to Application No. 59693, filed May 27, 1980, as Exhibit C with such changes therein as are required to reflect the terms negotiated for the First Mortgage Bonds, Series Q.

3. Continental Telephone Company of California shall apply the proceeds from the sale of its First Mortgage Bonds, Series Q, to the purposes set forth in the application.

4. Promptly after executing the contract for the sale of its First Mortgage Bonds, Series Q, Continental Telephone Company of California shall file a copy of the contract and a written report with the Commission, showing the interest rate and the cost of money to Continental based on such price and interest rate.

5. As soon as available, Continental Telephone Company of California shall file a conformed copy of the purchase agreement for the First Mortgage Bonds, Series Q, and the definite form of the Nineteenth Indenture.

6. Continental Telephone Company of California shall file with the Commission a report, or reports, as required by General Order No. 24-B, which order, insofar as applicable is hereby made a part of this order.

7. This order shall become effective when Continental Telephone Company of California has paid the fee prescribed by Section 1904(b) of the Public Utilities Code, which fee is $21,000.

Dated SEP 16 1980, at San Francisco, California.

John E. Bryson
President

Vernon L. Sturgeon

Richard D. Gravelle

Claire T. Dedrick

Leonard M. Grimes, Jr.
Commissioners