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Decision No. 92359 OCT 22 1980

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the matter of the application
of Southern Pacific Communications
Company for authority to issue
notes and other evidences of
indebtedness in the aggregate
principal amount of \$31,806,854
and to exempt such notes from
competitive bidding.

ORIGINAL

Application No. 59922
(Filed September 4, 1980)

O P I N I O N

Southern Pacific Communications Company (SPCC) seeks an exemption from the Commission's competitive bidding rule, and the authority to issue notes and other evidences of indebtedness in the aggregate principal amount of \$31,806,854.

Authority is requested pursuant to Sections 816 through 830 of the Public Utilities Code. Notice of the filing of the application was published on the Commission's Daily Calendar of September 8, 1980. No protests have been received.

SPCC was incorporated on January 23, 1970, under the laws of the State of Delaware, and is a wholly-owned subsidiary of Southern Pacific Company. SPCC is a specialized common carrier of telecommunications currently operating between San Francisco, California, and Los Angeles, California, on the West Coast and such cities as Boston, New York, and Washington, D.C. on the East Coast. In addition to holding licenses and construction permits issued by the Federal Communications Commission, SPCC possesses the certificate of public convenience and necessity granted by our Decision No. 84167, dated March 4, 1975, (as affirmed by our Decision No. 89580, dated October 31, 1978) in Application No. 55284. The certificate authorizes SPCC, as a public utility, to establish intercity private line communication service for voice and data transmission between the cities of Bakersfield, Fresno, Los Angeles, Merced, San Francisco, and Stockton.

Attached to the application as part of Exhibit F is an Income Statement for the year ended December 31, 1979, showing that SPCC generated operating revenues of \$95,285,670 and a net loss of \$3,001,642. The company derived only 0.012% (approximately \$12,000) of its operating revenues from intrastate operations.

The company's Balance Sheet as of December 31, 1979, is summarized as follows from Exhibit F of the application:

<u>Assets</u>	<u>Amount (In Thousands)</u>
Current Assets	\$ 29,471
Property, Plant and Equipment, Less Accumulated Depreciation	202,232
Other Assets and Deferred Charges	<u>2,339</u>
Total	<u>\$234,042</u>
 <u>Liabilities and Common Equity</u>	
Current Liabilities	\$ 54,319
Notes Payable	120,800
Other Liabilities	77,436
Common Equity (Deficit)	<u>(18,513)</u>
Total	<u>\$234,042</u>

SPCC proposes to enter into financing transactions and issue notes and other evidences of indebtedness in an aggregate principal amount of \$31,806,504 to Nissho-Iwai American Corporation (Nissho) to finance the construction of a new microwave radio communications system between Cooksville, Maryland and Satsuma, Texas. Nissho will engineer, furnish, and install equipment and provide services to construct the new system. The proposed financing will consist of the following:

- a. The issuance of notes under a loan agreement to Nissho in the aggregate amount of \$20,953,133. The loan will be repaid in ten (10) equal semi-annual installments commencing August 15, 1981, with interest at one percent per annum above the London interbank offering rate (LIBOR) quoted by the London Branch of The Taiyo Kobe Bank, Ltd., for six-month deposits.

- b. The issuance of notes under a second loan agreement to Nissho in the aggregate amount of \$2,691,772.80. The loan will be repaid in ten (10) equal semi-annual installments commencing August 15, 1981, with interest at one percent per annum above the LIBOR quoted by the London Branch of The Taiyo Kobe Bank, Ltd., for six-month deposits. SPCC will open an irrevocable commercial letter of credit with the Bank of America in favor of Nissho in the amount of \$1,020,249.77 which is part of the \$2,691,772.80 proposed to be borrowed under this second loan agreement.
- c. Deferred installment payments of a total aggregate sum of \$8,161,998.20, pursuant to a purchase agreement with Nissho. There shall be ten (10) equal semi-annual installment payments commencing six (6) months from each shipment date of equipment purchased. Such deferred installment payments shall bear interest of 8-1/2 percent per annum net on the unpaid balance outstanding. SPCC will open an irrevocable letter of credit with the Bank of America in favor of Nissho to guarantee the deferred installment payments under the purchase agreement.

The notes and other evidences of indebtedness proposed to be issued will be general obligations of SPCC; will not be secured by a mortgage or other lien on any operating properties or other assets of SPCC; and, will be unconditionally guaranteed by Southern Pacific Company as to principal and interest. The application indicates that without such guaranty of Southern Pacific Company or without the letters of credit SPCC could not obtain the loans at the applicable rates of interest.

The estimated cost of construction of the new microwave radio system utilizing the proceeds from the proposed borrowings is as follows:

	Phase I (Cooksville, MD to Atlanta, GA)	Phase II (Atlanta, GA to Satsuma, TX)
Antennas and Waveguide	\$ 1,178,195	\$ 2,624,758
Radio Equipment	2,902,593	4,713,083
Towers	3,099,663	3,243,488
Buildings	2,033,940	2,739,165
Power	998,078	1,401,994
Site/Civil Work	2,058,581	-
Other	2,429,203	2,384,113
Total	\$14,700,253	\$17,106,601

As justification for seeking exemption from the competitive bidding requirements with respect to the notes, the application states the following:

"Applicant requests that the Commission find that the Notes may be issued, as aforesaid, without being offered for competitive bidding. It is not desirable or feasible for the notes to be sold at competitive bidding for the following reasons:

"Since the date of its incorporation in Delaware on January 23, 1970, the Applicant has been continuously occupied in obtaining its required licenses and permits from the FCC and other governmental agencies, in constructing its communications system, and in marketing its services. Applicant commenced interstate common carrier communications service on December 26, 1973. Since that time, it has experienced severe rate competition from American Telephone and Telegraph Company (and its operating subsidiaries) which has resulted in Applicant operating at a net loss in each year through 1979. Despite AT&T's rate competition (which Applicant believes has violated federal antitrust laws), Applicant expects to generate a positive cash flow and earn an operating profit for the year 1980. At the present time, Applicant does not have a history of earnings necessary to commend securities to the investing public and to meet rating standards acceptable to Applicant. However, due to confidence in the Applicant and its proposed operations, Nissho is prepared to loan necessary funds upon the terms stated in the application which are believed by the Applicant to be more advantageous than any loan financing which could be obtained by Applicant through competitive bidding.

"Greater flexibility is obtained by placing this financing privately with Nissho rather than making a public distribution of securities. Unexpected developments may occur in any new enterprise and it is of value to have its securities closely held to permit necessary changes to be negotiated in the event such developments become significant. Private placements of securities, including privately negotiated loans, have been widely adopted for the financing of new companies. Furthermore, Nissho has considerable knowledge of Applicant's proposed communications system and business operations by reason of its involvement in the construction of the Southeast segment.

"It is the considered judgment of Applicant that under present market conditions, loans on as favorable terms as the proposed financing cannot be obtained through the public offering of Applicant's securities, or by competitive bidding. \$8,161,998.20 of the proposed financing is at the favorable interest rate of 8-1/2 percent. The remainder to be financed is at 1 percent over the London Interbank Offering Rate which was 11-1/8 percent for six-month deposits on September 4, 1980. Applicant considers this financing to be extremely favorable."

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 debt securities will be placed privately on terms which will be executed after the issuance of this decision and because of the staff's conclusion and belief that the proposed debt would be issued at a cost as low, if not lower, than would prevail if the proposed financing were to be issued 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 SPCC or its ratepayers. We will, however, also grant SPCC the authority to issue the proposed debt securities by means of a competitive offering.

SPCC is put on notice that in the event of a 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.

SPCC requests the Commission find that the California Usury Law does not apply to the proposed issuance and sale of notes or to the proposed installment contract. The Commission in exercising its authority to regulate public utility debt securities is not restricted by the California Usury Law (Article XV, Section 1 of the California Constitution).

The Revenue Requirements Division and the Communications Division have reviewed the application, and have noted that the construction related to the proposed financing is for facilities located between Maryland and Texas only. None of these facilities is necessary to provide service in California pursuant to the certificate of public convenience and necessity granted to SPCC by Decision No. 84167, dated March 4, 1975. Should any portion of the funds from the proposed financing be expended in California, the Divisions reserve the right to reconsider the reasonableness of any construction expenditures in future rate proceedings.

Findings of Fact

1. Applicant is a Delaware corporation subject to the jurisdiction of this Commission.
2. The proposed notes, and the deferred installment payments would be for proper purposes.
3. Applicant has need for external funds for the purposes set forth in this proceeding.
4. The rates of interest applicable to the proposed notes and the deferred installment payments are favorable to applicant under current market conditions.
5. The proposed guaranty by Southern Pacific Company and the letters of credit are reasonable.
6. The issuance of the proposed notes and other evidences of indebtedness should not be required to be effective through competitive bidding.
7. Pursuant to plenary powers granted to the Legislature by Article XII, Section 5 of the California Constitution, the Legislature is authorized to confer additional consistent powers upon the Public Utilities Commission as it deems necessary and appropriate, unrestricted by any other provisions of the California Constitution.

8. The Legislature has conferred upon the Public Utilities Commission the authority to regulate the issuance of public utility securities, including evidence of indebtedness, and to prescribe restrictions and conditions as it deems reasonable and necessary (Sections 816 et seq. of the Public Utilities Code).

9. The money, property or labor to be procured or paid for by the notes and other evidences of indebtedness authorized herein are reasonably required for the purposes specified herein, which purposes are not, in whole or in part, reasonably chargeable to operating expenses or to income.

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.

O R D E R

IT IS ORDERED that:

1. The issuance of notes and other evidences of indebtedness by Southern Pacific Communications Company in the aggregate principal amount of \$31,806,854 are hereby exempted from the Commission's competitive bidding rule set forth in Decision No. 38614, dated January 15, 1946, as amended, in Case No. 4761.
2. Southern Pacific Communications Company may on or after the effective date hereof and on or before December 31, 1980, issue notes and other evidences of indebtedness in an aggregate principal amount not exceeding \$31,806,854 in accordance with the terms and conditions as described in the application, or may issue sell and deliver these securities by means of a competitive offering.

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3. Southern Pacific Communications Company shall use the proceeds from the borrowings herein authorized for the purposes stated in the application.

4. Southern Pacific Communications Company shall file with the Commission reports required by General Order No. 24-B, which order, insofar as applicable, is hereby made a part of this order.

5. This order shall become effective when Southern Pacific Communications Company has paid the fee described by Section 1904(b) of the Public Utilities Code, which fee is \$21,903.50.

Dated OCT 22 1980, at San Francisco, California.

John E. Byrne
President

Michael D. Hovalde

[Signature]
Commissioners

Commissioner Vernon L. Sturgeon, being necessarily absent, did not participate in the disposition of this proceeding.

Commissioner Claire T. Dedrick, being necessarily absent, did not participate in the disposition of this proceeding.

