

Decision No. 92545 **DEC 17 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 \$50,000,000 aggregate principal amount of its 12-3/8% Notes due 1995 and to exempt such Notes from competitive bidding.

ORIGINAL

Application No. 60002
(Filed October 14, 1980)

O P I N I O N

Southern Pacific Communications Company (SPCC) seeks (a) authority to issue \$50,000,000 aggregate principal amount of its 12-3/8% Notes due 1995, (b) an exemption from the Commission's competitive bidding rule, and (c) to enter into a cash deficiency agreement with lenders and the Southern Pacific Company.

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 October 17, 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, 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 possess a certificate of public convenience and necessity granted by Commission 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 cities of Bakersfield, Fresno, Los Angeles, Merced, San Francisco, and Stockton.

SPCC, by letter dated November 17, 1980, provided the Commission's staff with the most current financial statements for 1980. The Income Statement for the nine months ended September 30, 1980 indicates that SPCC generated operating revenues of \$107,419,235, and a net loss for the period of \$14,237,235. In 1979 the company derived \$11,436 (approximately .012%) of its operating revenues from intrastate operations. The company's Balance Sheet as of September 30, 1980, is summarized as follows:

<u>Assets</u>	<u>Amount</u>
Current Assets	\$ 40,559,884
Property, Plant and Equipment Less Accumulated Depreciation	202,831,001
Other Assets and Deferred Charges	<u>2,037,460</u>
Total	<u>\$245,428,345</u>
<u>Liabilities and Common Equity</u>	
Current Liabilities	47,866,833
Notes Payable	120,800,000
Other Liabilities	109,436,691
Common Equity (Deficit)	<u>(32,675,179)</u>
Total	<u>\$245,428,345</u>

SPCC proposes to borrow \$50,000,000 and issue its notes in an aggregate principal amount not to exceed that sum. The proposed notes 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 subject to a cash deficiency agreement between Southern Pacific Company, SPCC, and the lenders. The cash deficiency agreement provides that Southern Pacific Company shall be liable for any cash deficiency of SPCC, if the utility is unable to discharge its obligations under the proposed notes. A form of the proposed cash deficiency agreement was provided to the Commission's staff with a letter of transmittal dated November 5,

1980. The application indicates that without the cash deficiency agreement, SPCC could not obtain the loans at the applicable rates of interest.

The notes will be issued in an aggregate principal amount not exceeding \$50,000,000 and for terms not exceeding fifteen years; will be payable at their maturity in 1995; and, will bear an interest rate of 12-3/8% per annum, payable quarterly. SPCC will be obligated to make payments of \$5,000,000 annually, commencing in 1986 and in each year thereafter until 1994. The balance of \$5,000,000 will be paid at maturity. The notes will be issued to the following entities and in the amounts as shown:

<u>Name of Entity</u>	<u>Amount</u>
Teachers Insurance and Annuity Association of America	\$15,000,000
Aetna Life Insurance Company	15,000,000
The Prudential Insurance Company of America	10,000,000
J.P. Morgan Interfunding Corporation	5,000,000
Great-West Life Assurance Company	<u>5,000,000</u>
Total	<u>\$50,000,000</u>

SPCC proposes to utilize the proceeds from issuance of the notes to expand its existing microwave radio communications system and to add switching, transmission and multiplex equipment. In 1981, SPCC plans to overbuild its existing facilities between San Francisco-Olathe (Kansas City area), San Francisco-Los Angeles, Dallas-Chicago, St. Louis-Olathe (Kansas City area) and Woodworth (Illinois) - New York.

SPCC requests an exemption from the Commission's competitive bidding requirements with respect to the proposed issuance of notes. The application sets forth the following reasons as justification for an exemption:

"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 the 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, 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, the Lenders are prepared to loan necessary funds upon the terms stated in Exhibit B of 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 Note financing privately with the Lenders 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, the Lenders have considerable knowledge of Applicant's proposed communications system and business operations by reason of prior negotiations for said Note financing, and other prior note financing transactions.

"Applicant's investment banking representative, Goldman, Sachs and Co., believes and it is the considered judgement of Applicant, that under present market conditions, loans on as favorable terms as the proposed Note financing cannot be obtained through the public offering of Applicant's securities, or by competitive bidding."

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 to known parties, on terms which are reasonable under the circumstances, we are of the opinion that applying, in this proceeding, the Commission's competitive bidding requirements and conditions set forth in Decision No. 91984, is not necessary. 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. We will also require SPCC to provide the Commission

with a showing that the interest rate on the proposed notes and the resulting cost of money were the most advantageous to the company and its ratepayers. We will require this showing within a reasonable period after the issuance and sale of the proposed securities.

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 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.

Findings of Fact

1. SPCC is a Delaware corporation subject to the jurisdiction of this Commission in that it is authorized and qualified to do business in the State of California.
2. The proposed notes would be for proper purposes.
3. SPCC has need for external funds for the purposes set forth in this proceeding.
4. The rates of interest applicable to the proposed notes are favorable to SPCC under current market conditions.
5. The proposed cash deficiency agreement between Southern Pacific Company, SPCC and the lenders is reasonable.
6. The proposed notes should not be required to be issued through competitive bidding.
7. 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.
8. Because the issuance of these debt securities will occur on December 18, 1980, this matter qualifies as an unforeseen emergency situation pursuant to Section 306(b) of the Public Utilities Code.

Conclusions of Law

1. 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.

2. 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).

3. Pursuant to the plenary powers granted to the Legislature in Article XII, Section 5 of the California Constitution, it conferred on the Public Utilities Commission the comprehensive and exclusive power over the issuance of public utility securities, including evidences of indebtedness, and the California Usury Law cannot be applied as a restriction on the Public Utilities Commission's regulation of such issuances of public utility securities, including its authorization of a reasonable rate of interest.

4. If the usury limitation contained in Article XV of the California Constitution and the Usury Law Initiative Act is exceeded, but the transaction is authorized by this Commission and the terms thereof are the best SPCC can obtain because of market conditions, SPCC, its assignees or successors in interest, will have no occasion to and cannot assert any claim or defense under the California Usury Law; further, and necessarily, because of lawful issuance by SPCC of notes in compliance with authorization by the Public Utilities Commission, persons collecting interest on such authorized notes are not subject to the Usury Law sanctions.

5. A public hearing is not necessary.

6. The application should be granted to the extent set forth in the order which follows.

A.60002 RR/lq

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 by Southern Pacific Communications Company of its \$50,000,000 aggregate principal amount 12-3/8% Notes due 1995 is 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 issue 12-3/8% Notes due 1995 in an aggregate principal amount not to exceed \$50,000,000, 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.
3. Southern Pacific Communications Company is authorized to pay on such notes an interest rate in excess of the maximum annual interest rate otherwise permitted under the California Usury Law, as contained in Article IV of the California Constitution and the Usury Law Initiative Act, if market conditions so require.
4. Neither Southern Pacific Communications Company nor any person purporting to act on its behalf shall at any time assert in any manner, or attempt to raise as a claim or defense in any proceeding, that the interest on said notes exceeds the maximum permitted to be charged under the California Usury Law or any similar law establishing the maximum rate of interest that can be charged to or received from a borrower.
5. Southern Pacific Communications Company shall use the proceeds from the borrowings herein authorized for the purposes stated in the application.

6. 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.

7. Within thirty days after the issuance and sale of the proposed debt securities herein authorized, Southern Pacific Communications Company shall file with the Commission a report showing that the interest rate and cost of money to the company were the most advantageous to the company and its ratepayers.

8. This order shall become effective when Southern Pacific Communications Company has paid the fee prescribed by Section No. 1904(b) of the Public Utilities Code, which fee is \$31,000.

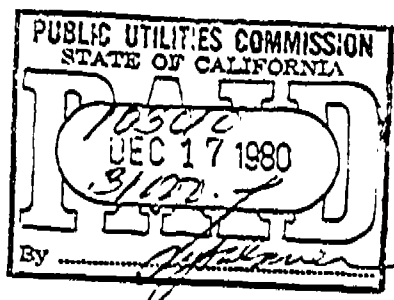
Dated DEC 17 1980 at San Francisco, California.

John E. Byrne
President

Richard D. Howell

Clair J. Derrick

Commissioners



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

Commissioner Leonard M. Grimes, Jr., being necessarily absent, did not participate.