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Decision 97-08-054 August 1, 1997

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

ORIGINAL

In the Matter of the Application of Marin Door to Door, Inc., a California passenger stage corporation, to transfer control from Gregory McCord and Gary S. Gross to Michael Bey and Beysim O. Yakuboff.	Application 96-06-040 (Filed June 26, 1996)

OPINION

This application seeks Commission authority to transfer control of Marin Door to Door, Inc. (Marin) (PSC 10110) from Gregory McCord and Gary Gross, who hold all existing shares, to Michael Bey and Beysim Yakuboff. Marin is authorized to perform an on-call passenger stage service to and from points in Marin County to San Francisco International Airport (SFO). A timely protest was filed by Paul Bobrow.

Allegations

Protestant Bobrow is the previous owner of the corporation with its PSC certificate, and the registered owner of its buses. He was authorized to transfer to McCord and Gross by Decision 95-12-045. He now alleges that McCord and Gross have failed to pay him the purchase price as agreed. He also alleges that McCord and Gross plan to transfer the vans to Bey and Yakuboff in defiance of his rights as registered owner. (The pink slips are held by Ford Motor Company with $65,000 still owing.) He argues that the Commission should intervene on his behalf, disapproving the presently proposed transfer until and unless the debt is paid.

None of the applicant parties have responded to the protest. Because there has been no response, we will presume that its allegations are true. For that reason, no public hearing is necessary.

None of the parties are represented by an attorney. If it were not for the protest, this application would be unconditionally recommended for approval without hearing.

The Law

The pertinent authority governing such a protest is still Hanlon v. Eshelman (1915) 169 C. 200. In Hanlon, an individual who had contracted to purchase a tract of water utility property, requested that the Commission entertain his application for authority to purchase, even though the utility owner had entered into a subsequent contract to sell to the City of Los Angeles. Citing the fact that the owner no longer wished to sell to the complainant, the Commission refused to consider the earlier contract, but approved the sale to the City.

The Supreme Court upheld the Commission. It agreed that the predecessor to Public Utilities Code § 851 gave the Commission only limited jurisdiction over a sale of utility property. The court held that the Commission had no power to determine for example whether there was a valid contract between parties or whether either had a claim against the other. In short, "All that the Commission is concerned with, therefore, is whether a proposed transfer will be injurious to the rights of the public." (169 C. at 203.) The right of an intending purchaser or a former seller are questions for the courts, and not for the Commission.

As applied here, Hanlon's holding would require that the protest be denied and the transfer considered without hearing on the protest.

Protestant's remedy would lie in a conventional action in court.

On March 10, 1997, Bobrow asked the Commission to take official notice of an affidavit, filed in a court proceeding, in which the complaining party asserted that McCord operated multiple vehicles for a period of several months without insurance. In a ruling dated May 7, 1997, the Administrative Law Judge ruled that

this new information was untimely, but agreed to take notice of the existence of the affidavit. In addition, he allowed McCord the opportunity to rebut the assertion that he was uninsured. On May 14, 1997, McCord filed his rebuttal, which provides us with evidence that he was carrying insurance on 28 taxis and 11 vans as of February 25, 1996. We do not know if the vans used for Marin are among those insured. On June 17, 1997, protestant Bobrow tendered a reply of the McCord response. While such a pleading is not authorized, we have accepted it for filing as of that date to ensure completeness of the record. Bobrow raises two contentions. The first takes issue with a statement in the McCord response regarding whether a decision had been issued in Application 96-09-027. Our records show no decision issued in that proceeding. The second contention concerns allegations about a traffic accident and whether there was insurance on the vehicles involved. However, questions about McCord's past diligence in maintaining adequate insurance are not relevant to this application. We are more concerned with the diligence that the new owners will show in maintaining the insurance required by law. Nothing brought before us here places that issue into question.

Findings of Fact

1. Buyers have the ability, equipment, and financial resources to continue the existing passenger stage service between Marin County and SFO.

2. The proposed transfer will not adversely affect the public interest.

3. A public hearing is not necessary.

4. Nothing in this record indicates that the new owners will not show due diligence in meeting all regulatory requirements, including maintaining proper insurance coverage.

5. It can be seen with certainty that there is no possibility that the activity in question may have a significant effect on the environment.

Conclusions of Law

1. The application should be granted, and the protest denied.

2. The authority sought by buyers and sellers is permissive only. The Commission should not deny or condition that authority to help protestant collect his debts.

Only the amount paid to the State for operative rights may be used in rate fixing. The State may grant any number of rights and may cancel or modify the monopoly feature of these rights at any time.

O R D E R

IT IS ORDERED that:

1. Pursuant to Public Utilities Code § 854(a), Michael Bey and Beysim Yakuboff are authorized to acquire and control Marin Door to Door, Inc., through the purchase of all the outstanding shares of stock in the corporation from Gregory McCord and Gary Gross.

2. Within fifteen (15) days of the date of the transaction closes, Michael Bey and Beysim Yakuboff shall notify the Rail Safety and Carriers Division in writing thereof.

3. The authority granted by this order shall lapse unless it is exercised within 90 days of the effective date of this order.

4. The application is granted as set forth above, and the protest denied.

5. This proceeding is closed.

This order is effective today.

Dated August 1, 1997, at San Francisco, California.

P. GREGORY CONLON
President
JESSIE J. KNIGHT, JR.
HENRY M. DUQUE
JOSIAH L. NEEPER
RICHARD A. BILAS
Commissioners

A. 96-12-009
D. 97-08-056

COMMISSIONER JESSIE J. KNIGHT, JR. CONCURRING:

I support this decision, but feel compelled to memorialize thoughts that may aid future commission deliberation in dealing with new unbundling issues that will surely arise over time. The decision here provides a fair allocation of costs among the classic functional areas of transmission, generation and distribution, as well as an economically efficient means of calculating the competition transition charge (CTC). Yet, I must express concerns that the premise driving this stage of unbundling has a basic flaw. The exercise to divide the electric industry into three distinct functional components is an idea that no longer fits the reality of the evolving competitive market for electricity. Traditionally, the electricity industry has been segmented into three primary functions -- transmission, distribution and generation.

This decision reflects our own institutional biases that were cultivated during the several stages of our own initial procedural and issue development in the electrical restructuring proceeding, as well as the strictures evident in AB 1890 that serve as the intellectual and legislative anchors justifying the attempt to put costs into these three baskets. The study and debate over the course of this decision has highlighted the unequivocal fact that there are many costs that did not fit easily into one basket or the other.

Generally, these costs should be characterized as "retailing costs". These retailing costs can be categorized as reflecting the cost of selling electricity to an end-user. They are not costs associated with the generation of electricity. Fundamentally, the production of power, the actual generation of electricity, is a wholesale function rather than a retail function. These retailing costs are not a true component of the cost of distribution, because the business function of selling a product to a customer is inherently not a distribution cost. By definition, transmission costs are not associated with providing retail service.

The procedural necessity in place currently, that insists that all costs must be allocated to generation, transmission, or distribution, has obscured the issues in this proceeding. There are identifiable costs associated with the provision of retail electric service, costs that should be unbundled from wholesale costs, recovered through the provision of retail service and therefore solely collected from retail customers of the utility.

As a result of this decision, some of these retailing costs have been allocated to generation and some assigned to distribution. Of paramount concern is the fear that recovery of retailing costs in distribution rates will require competitive retail providers to inadvertently pay the retailing costs of the utilities. Realization of this envisioned circumstance would create a subsidization of the utility's retailing function, thus promoting injury to the development of a competitive retail electric marketplace.

As the Commission proceeds to fashion a robust and competitive retail market, it must actively seek to further unbundle these "retailing costs" from distribution and generation rates. Only this proactive effort can ensure a level playing field between the utilities and competitive energy service providers.

The Commission's experience in overseeing the natural gas and the telecommunications industries prepares us for the inevitable fact that the unbundling that is occurring here will be the first of many such proceedings, as our thinking and analysis mature. It is a historic fact that the telecommunications industry has undergone many rounds of unbundling. First, customer-premise-equipment was unbundled from telephony. Later, long distance was unbundled from the local service market, as a result of the disaggregation of AT&T that resulted from the Modified Final Judgement in 1984. Since then, central office space has been unbundled, as was the many underlying basic service elements in the 1980's and early 1990's, as part of the federal open network architecture policy. Currently, local telephone service is being further unbundled with links being unbundled from ports. In fact, the entire network is being unbundled into basic network functions, with each getting unbundled from each other. Furthermore, in the wholesale provision of bundled service, the Commission has seen fit to ensure that wholesale rates are discounted to unbundle retailing costs.

In the natural gas industry, the merchant function, gas gathering, and interstate transport are all unbundled. In a Commission decision that is a mere few weeks old, gas storage was unbundled. Moreover, this Commission is actively engaged in bringing about even greater unbundling in the intrastate gas arena as a result of D.97-08-055. Furthermore, it is the intention of the Commission to ensure that its forthcoming long term gas strategy also addresses this issue of unbundling retailing costs from the provision of wholesale services.

In the electricity industry, as we explored the various aspects of the industry, it became apparent that generation is made up of many severable components. Electricity has an energy component, reliability components, and retailing components. Distribution has revenue cycle components with distinct retailing elements. Even the overall revenue cycle of the utility can be further unbundled into meter reading, billing, and other severable parts. It is not beyond the pale for the Commission to potentially find that many

more underlying functions may eventually be unbundled one from another as a result of federal policies that will certainly emerge and evolve over time.

The process of unbundling can be likened to the peeling of an onion. Under each layer, there is another layer that can be peeled away, or further unbundled, if you will. The Commission should fully expect and more importantly, **seek** the further unbundling of distribution functions to assure that retailing costs are truly unbundled from distribution. Only this strategy will yield a competitive market such that future retailers will be able to compete on a level playing field with the utility distribution companies. In short, the development of a competitive retail market **requires** the unbundling of retail costs from wholesale services and the sole recovery of these costs from utility retail customers.

Dated August 1, 1997 in San Francisco, California.

Jessie J. Knight, Jr.
Commissioner

D.97-08-058
A.96-11-037

H-16

Commissioner Josiah L. Neeper Dissenting

I dissent from the majority opinion on Item H-16, which would disapprove PG&E's application for derivatives, without prejudice. I would have preferred item H-16a, which was an alternate I sponsored that would have approved PG&E's application, with various appropriate conditions. My alternate would have allowed PG&E to enter into derivative contracts, with PG&E shareholders taking all the risks and gaining all potential rewards. Some of the conditions included a limit on the amount of derivatives, a requirement that derivatives be traded on exchanges overseen by the Commodity Futures Trading Commission, and a requirement that any physical sale or delivery of energy through derivatives transactions be accomplished through the Power Exchange. Further, safeguards to protect ratepayers include a prohibition on any costs related to derivatives being passed on through a rate case, a cost-of-capital proceeding, or in Section 376 costs. The alternate also requires a case-by-case application for any contracts-for-differences with customers, consistent with the 1995 restructuring Policy Decision.

The fundamental issue here is whether a utility should have the opportunity to control its costs and risks. PG&E is constrained by a rate freeze and cannot increase its rates. PG&E has significant risks, not only from our regulatory schemes, but also due to the limits imposed by AB 1890, including a time limit on transition cost recovery. I am aware of no

law or regulation that prevents PG&E or any other utility from attempting to decrease its costs or risks, and would strongly oppose any such limitations.

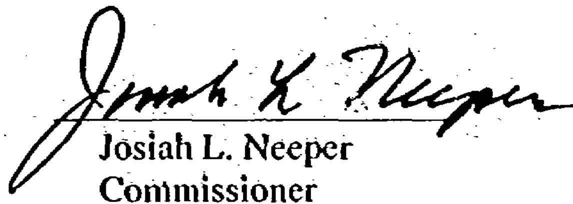
If PG&E enters into derivatives transactions for its own purposes, I agree with the majority that such activities should not put ratepayers at risk. My alternate shielded ratepayers from such risks. But in return for taking all the risks, shareholders must be given the opportunity to gain the benefits of the company's efforts.

The major concern about this application, aside from risk issues, is that derivatives purportedly may have a deleterious impact on the marketplace, due to the potential of PG&E to exercise market power. Let's take it as a given that the exercise of market power is a bad thing. In that case, what we should be doing is working to prevent the exercise of market power, or perhaps even preventing the achievement of market power in the first place. We should focus on the cause of the problem, not the symptoms.

My understanding is that we are actively participating in a proceeding at FERC, at which market power is an important topic. My understanding is that we expect FERC to take actions to limit or prevent the exercise of market power. My understanding is that this may involve design issues regarding the Power Exchange and the ISO, divestiture issues, and perhaps many other conditions for approval. I am told that FERC is unlikely to approve the utilities' applications without mitigation of market power. We are also undertaking efforts on our own initiative to deal directly with market power issues. The majority opinion agrees that derivatives do not become a problem unless the utility is able to exercise market power.

I am confident we will do our job, and we should let FERC do its job, regarding market power. Given that, I see no reason not to allow PG&E to use financial tools such as derivatives (with proper safeguards to protect ratepayers) to do what any other company can already do to control its costs and risks.

For all the above reasons, I dissent.



Josiah L. Neeper
Commissioner

San Francisco, California
August 1, 1997

A. 94-05-042
D. 97-08-060

COMMISSIONER JESSIE J. KNIGHT JR. DISSENTING IN PART:

This decision is another step in the long process to reduce the Commission's regulation governing the long-distance market and AT&T in particular. The decision here is a major leap forward and I support the decision, but I strongly disagree with the majority with respect to the requirement that AT&T continue to provide annual reports of its intrastate return on ratebase. What some have characterized as a small requirement, I am of the view, is a weighty and pernicious impediment.

The evidence is clear, AT&T has lost significant market share over the last ten years. Despite increasing regulatory flexibility over time, AT&T's market share, by any measure continues to decline. AT&T's market share is 49% of revenues, 55% of minutes of use (down from 70% in 1989) and 66% of presubscribed lines.

AT&T's share of capacity has declined from nearly 100% in 1984 to just 21.5% today. While AT&T has the largest share of activated capacity, several of its competitors have comparable levels of capacity as well. LDDS-Worldcom has 18.5%, MCI has 13.9%, and Sprint has 9.6 percent. With the remaining 18 facilities-based carriers holding 36.7% of the capacity.

There does not appear to be <u>any</u> significant barrier to entry in the interexchange market. In 1994 California had 14 long-distance carriers. Today, there are over 500 non-dominant interexchange carriers (NDIEC) operating in the state, with 22 of these entities doing business as facilities-based carriers.

When this Commission adopted the dominant/non-dominant regulatory framework for the long distance market, it said "after equal access allows competitors to provide equivalent service, we will entertain AT&T's application for more flexible regulation". Today, 99.98% of the 20 million-plus access lines have the ability to choose their long-distance company. Each year a smaller and smaller proportion of customers are choosing AT&T to be their long distance provider.

I fully support the reclassification of AT&T as a non-dominat carrier and firmly believe that AT&T should be regulated the same as its competitors in the long-distance market. I fully support the conclusion that AT&T is no longer dominant in the marketplace and no longer wields significant market power. However, this decision does

not eliminate all of the AT&T reporting requirements but retains the antiquated requirement that AT&T report its earnings. It is this regulatory hold on the past that does not receive my support.

I would prefer a decision that would sweep away the last vestiges of traditional regulation of AT&T. Not only is the evidence compelling that the long-distance market is competitive and that AT&T lacks significant market power, but also <u>no</u> other carrier in the California long distance telecommunication market is required to report its earnings. The only possible usage of these reports is for the Commission to use them in the future as a means of regulating the profit of AT&T. If the Commission is truly moving away from traditional rate-or-return regulation, there is no need for this information nor should the Commission tempt its inappropriate use. Like the Administrative Law Judge in this case, I believe that earnings reports are of very little use for government to analyze the marketplace and their probative value is indeed minimal.

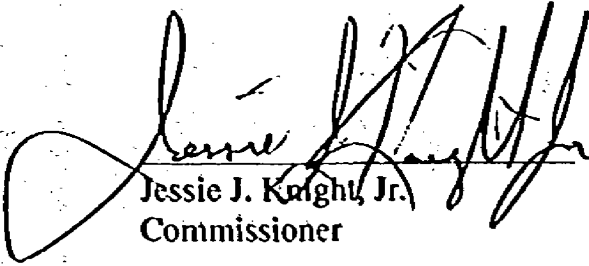
The calculation of return on intrastate ratebase has lost its currency and relevance, as today's advanced network completes intrastate calls using assets that are not even located in California. The structure of today's telecommunication networks are increasingly non-hierarchical and calls are routed on a dynamic basis without regard to the jurisdictional nature of the call. The result is that traditional jurisdictional separations of costs no longer match well with revenues, thus the intrastate return on ratebase calculation is rendered meaningless. Furthermore, return on capital, itself a measure tied to traditional cost-of service regulation, has less and less unique relevance in the telecommunications industry; an industry that is becoming less capital intensive. It is indisputable that the major cost drivers in the business are not capital costs but rather operating expenses. Finally, we have consistently ruled that return should <u>only</u> be used in conjunction with other measurements of market conditions. However, it is ironic to note that in this decision, now this return information will no longer have other market information to be reviewed alongside the lone earnings report.

I regret that California chooses not to join the Federal Communications Commission and 47 other states that have ended the rate of return reporting requirements on AT&T. For this reason I dissent in part with respect to the requirement that AT&T provide annual earnings reports to this Commission. I do, however, fully support the majority's choice to commit a venial sin rather than a mortal sin in electing to sunset this requirement when an affiliate of Pacific Bell enters the long distance market.

The remainder of the decision has my full support. It is well founded on the evidence presented by AT&T's witnesses and the testimony elicited by cross examination by Office of Ratepayer Advocates (ORA) and The Utility Reform Network (TURN). The decision considered and responded thoughtfully to the comments of the parties and does an excellent job of assessing the marketplace.

In summary, the California long-distance market has been open for serious competition since 1984. Over time, it has become increasingly competitive and today it is undeniably competitive. Because of this fact, AT&T does not retain significant market power, and our regulation should be the same for all carriers in the marketplace.

Dated August 1, 1997 in San Francisco, California.



Jessie J. Knight, Jr.
Commissioner

A. 94-05-042
D. 97-08-060

COMMISSIONER RICHARD A. BILAS, CONCURRING:

I support this decision which grants AT&T non-dominant status. It is certain that much has changed since we established AT&T in its own category in 1984. By measures such as market share, available capacity and the number of competitors, AT&T participates in a competitive industry. However, one measure seems to indicate a less-than-competitive market: AT&T's intrastate rate of return.

Critics have suggested that such a high rate of return is proof that AT&T either operates in a non-competitive industry and/or holds market power. I suggest other possible factors. The denominator used to calculate AT&T's intrastate rate of return results from regulatory allocations which may no longer make sense. Additionally, that denominator is small which will tend to exaggerate any errors caused by improper allocations. Indeed, even though the rate of return figure may provide some indication of the market and/or AT&T's market power, it is apparent that this number is used in more of a qualitative manner than in a quantitative manner. In other words, if we really believed in the accuracy of the rate of return calculation we would have been concerned whenever it rose over the 20% level or any other specific level. In contrast, we did not have enough discomfort to open an investigation when AT&T earned 43% rate if return in 1994. We know the intrastate rate of return calculation has flaws. Hence, AT&T's rate of return is used qualitatively. My belief is that quantitative numbers should provide more than a mere qualitative understanding of the market.

With those comments as background, I still support this decision because there needs to be some data flow in the short term even if the number is flawed. AT&T's rate of return may provide an indirect measure of what I believe is the critical question to determine competitive pricing— is the firm pricing at or near marginal cost?

Only in a very indirect manner will AT&T's rate of return figure assist in making the determination of whether AT&T is pricing at or near marginal cost. A high rate of return does not preclude the possibility that it is pricing at or near marginal cost. There can be many other factors, including my previously stated questions about cost allocation. Conversely, a low rate of return may not be a result of AT&T pricing at or near marginal cost. A poorly received service or an extraordinary expense could lower the rate of return.

A. 94-05-012
D. 97-08-060

My preference to solve this seeming dilemma would have been to require a ratio which more closely captures the concept of pricing at or near marginal cost. In fact, the record shows that such a ratio was discussed. A calculation of Average Switched Revenue per Conversation Minute (ARPM) is on the record.

In addition to giving useful information about the market, ARPM would have also addressed one of TURN's concerns in this proceeding. TURN is concerned that AT&T did not pass-through all of its access cost reductions. If the ARPM were calculated net of access charges, it would be quite obvious if access cost reductions were not being passed along to the end user.

Additionally, if the ARPM were calculated separately for different market segments, this would provide more refined data to evaluate the relative competitiveness of the different markets as opposed to AT&T's overall rate of return which is based upon all of its services.

With the shortcomings that are inherent with the usefulness of AT&T's rate of return figure that I note above, I hope that AT&T will also keep track of its ARPM by market segment to answer likely questions about its rate of return. It is also my hope that AT&T file both its rate of return and its ARPM by market segment in order to show the superiority of ARPM. If ARPM proves its usefulness, as I believe it will, I would then encourage AT&T to file a petition to modify this decision substituting ARPM for rate of return.

San Francisco, California
August 1, 1997

Richard A. Bilas, Commissioner