

Decision 97-12-087 December 16, 1997

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of
Pacific Bell (U 1001 C) for Authority
Pursuant to Public Utilities Code
Section 851 to Lease Space to
Administrative Affiliates.

ORIGINAL
Application 97-09-027
(Filed September 18, 1997)

OPINION

1. Summary

Pacific Bell seeks Commission approval, pursuant to Public Utilities Code (PU Code) § 851, to lease space to affiliate corporations which will perform administrative support functions for Pacific Bell. Pacific Bell states that the lease arrangements comply with affiliate transaction rules of this Commission and of the federal government. Commission staff members examined the application and do not object to Pacific Bell's request. The application is granted.

2. Background

In Application (A.) 95-10-019, filed on October 4, 1995, Pacific Bell asked the Commission to grant Section 851 authority for a number of space use arrangements with both non-affiliated parties and affiliated parties.

In Decision (D.) 96-04-045, an interim decision, the Commission approved several of the agreements that the utility has with non-affiliated parties but, at the urging of staff investigators, the Commission required additional information on the agreements with affiliates. Among other things, Pacific Bell was required to make a further showing that its charges for use of utility space were proper and that the arrangements met affiliate transaction rules intended to prevent anticompetitive dealings.

Pacific Bell filed the additional information requested and, in D.96-09-069, the Commission reviewed and approved several space use arrangements between Pacific Bell and its affiliates. The arrangements included space provided to Pacific Telesis

Group, Pacific Bell Mobile Services, Pacific Bell Video Services, Pacific Bell Internet, and Pacific Bell Network Integration, among others.

In this application, Pacific Bell proposes to lease space for certain administrative functions that now will be done by "administrative affiliates." These administrative affiliates will provide support services to Pacific Bell and to other affiliates of parent company SBC Communications Inc., such as Nevada Bell and Southwestern Bell Telephone Company, as well as nonregulated affiliates. The affiliates will perform the functions previously performed by and reside in the space previously occupied by Pacific Bell's Technologies Services Group, and the Real Estate, Collections, Fraud, Payment Processing, and Audit Service organizations, and portions of the Procurement, Human Resources, Marketing, and Accounting organizations.¹

3. Nature of Application

The Commission previously has granted Pacific Bell authority to lease space and transfer or lease assets to administrative affiliates. In A.95-12-054, the company sought Section 851 authority to lease space and transfer or lease assets to the Pacific Telesis Group and the Pacific Telesis Legal Group. In Interim Decision 96-11-019 and in D.97-04-022, the Commission approved these arrangements.

Pacific Bell states that the lease arrangements here are similar to those sought earlier. The leased space is currently being used for these internal administrative organizations. Pacific Bell seeks authority only to lease the space currently used by these organizations, and it does not seek authority to use any additional unused space in Pacific Bell properties.

The specific affiliate functions and the new administrative affiliates they will be transferred to are summarized below:

¹ Pacific Bell states that the administrative affiliates will lease or otherwise obtain the equipment and assets now used by the existing organizations. Pacific Bell states that it intends to submit a follow-up Section 851 application that will request approval to lease and transfer equipment to the affiliates.

Technology Services Group. This organization provides computer support services, including software development, maintenance and systems integrity. This entire function will be performed by affiliate SBC Services, Inc.

Real Estate. This organization provides facility management, design and construction, real estate transactions, planning, and real estate systems, property upkeep and finance. This function also will be performed by affiliate SBC Services, Inc.

Auditing. This organization provides internal auditing. The function will be performed by Pacific Telesis Group.

Procurement. The contracting support function of this organization will be performed by Southwestern Bell Communications Inc.

Human Resources. Portions of this organization, namely Staffing and Employment, Human Resources Services Centers, and Human Resources Finance, will be performed by Pacific Telesis Group. In addition, the functions of the Human Resources Center for Learning, which includes personnel training, will be performed by the SBC Center for Learning.

Marketing. Product marketing support for business and consumer sales functions will be performed by Southwestern Bell Communications Inc.

Collections, Fraud, and Payment Processing. These functions will be performed by SBC Services, Inc.

Accounting. Accounting functions such as payroll processing, accounts payable and asset services will be performed by SBC Services, Inc.

In accordance with the Commission's direction in D.96-04-045, Pacific Bell has attached exhibits to its application with further details of the proposed lease arrangements. Exhibit A is a matrix of lease property locations. Exhibit B is a chart showing property management billing. Exhibits C, D, and E contain the company's transfer pricing manuals, affiliate transaction policies, and reporting requirements. Exhibit F shows the terms and conditions under which Pacific Bell will lease space to the administrative affiliates.

4. Affiliate Transaction Rules

Pacific Bell states that when it permits the administrative affiliates to use the same space in Pacific Bell buildings and other properties, it will do so under affiliate transaction agreements that comply with Commission and Federal Communications Commission affiliate transaction rules. (See, e.g., D.86-01-026, 20 CPUC2d 237 (1986); D.87-12-067, 27 CPUC2d 1 (1987); 47 CFR §§ 64.209, 32.27.) Under this Commission's affiliate transaction rules, the affiliate pays Pacific Bell the higher of fully distributed cost plus 10%, or market rate. To determine the higher amount, Pacific Bell performs market price studies to determine current market rate for particular properties. The space use arrangements for which approval is sought in this application are all subject to such affiliate transaction agreements.² The exhibits attached to the application show space use payments ranging from \$1.66 to \$4.84 per square foot, depending on location. Pacific Bell states that no space will be priced less than statewide average fully distributed cost plus 10%.

5. Reasons for the Leases

Pacific Bell states that the performance of the functions by administrative affiliates will enable the company to achieve efficiencies by sharing the cost of these operations with other organizations and by avoiding duplicate services. The cost of providing the services will be allocated between Pacific Bell and other users pursuant to cost allocation guidelines. According to Pacific Bell, this will lower costs to it, thus benefiting its customers.

Pacific Bell states that the space use arrangements will not interfere with existing operations. In fact, the company states, having these operations remain in California should mean better service for Pacific Bell and its customers. Pacific Bell states that,

² In A.95-10-019, Pacific Bell provided the Commission staff with information about the billing process for these transactions, along with other information intended to show that Pacific Bell is properly billing affiliates for their space use under the affiliate transaction agreements.

because the leases comply with affiliate transaction rules, the affiliates will not be subsidized by Pacific Bell and the lease of space will not create anticompetitive effects.

6. Comments to Application

The Commission's Office of Ratepayer Advocates (ORA) filed comments on this application on October 23, 1997. ORA confirms that the application comports with requirements established by the Commission and applied in similar applications in the past. ORA states that the content of the generic lease agreement for these leases (Exhibit F) indicates that Pacific Bell will apply the same pricing method to the lease space as has previously been approved by the Commission. (See D.96-11-019.) However, since copies of the actual leases are not included in the application, ORA urges that the Commission require Pacific Bell to verify that the executed lease agreements conform to the Commission's affiliate transaction rules.

7. Discussion

PU Code § 851 requires Commission authorization before a utility may "sell, lease, assign, mortgage, or otherwise dispose of or encumber" utility property. The purpose of the section is to enable the Commission, before any transfer of public utility property is consummated, to review the situation and to take such action, as a condition of the transfer, as the public interest may require. (San Jose Water Co. (1916) 10 CRRC 56.)

Another purpose of the Commission's review is to ensure that any revenue from the transaction is accounted for properly, and that the utility's rate base, depreciation, and other accounts correctly reflect the transaction. Under the New Regulatory Framework (NRF), these items do not have the same significance as they did under traditional regulation, but they continue to be an integral part of the calculation of rate of return, which serves as a check on the results of NRF. For this reason, the Commission reviews the accounting of the transaction for conformance with its requirements.

When, as here, the transactions are with a corporate affiliate, the Commission's review also includes consideration of whether the transaction may have anticompetitive

effects or result in cross-subsidization of nonregulated entities. (See Re Pacific Bell (1992) 45 CPUC2d 109, 125.)

There have been no protests to Pacific Bell's application. ORA has reviewed the application and its exhibits, and it advises that Pacific Bell has complied with Commission requirements in seeking Section 851 approval of these space use arrangements with affiliates.

Review of the information provided shows that Pacific Bell's space use arrangements with its affiliates do not impair its ability to serve the public. Pacific Bell's accounting for the revenue from the leases and other arrangements appears to be in order. No evidence has been submitted which reveals any anticompetitive effects or cross-subsidization of nonregulated entities from these use agreements. Accordingly, Pacific Bell has met the requirements for authorization under PU Code § 851, of the existing and proposed arrangements.

At ORA's suggestion, we will require Pacific Bell to notify our Telecommunications Division in writing when the leases are executed, and to state at that time whether the leases conform to our affiliate transaction rules.

Findings of Fact

1. Pacific Bell seeks Commission approval, pursuant to PU Code § 851, of space use arrangements with administrative affiliates.
2. Notice of this application appeared on the Commission's Calendar on September 23, 1997.
3. No protests have been filed.
4. Pacific Bell has shown that the space to be leased or otherwise occupied by its administrative affiliates is no more than that now used for these support functions.
5. Affiliates will pay Pacific Bell the higher of fully distributed costs plus 10%, or market rate, for the use of office and other space.
6. Pacific Bell has supplied the information required by the Commission for review of the space use arrangements.

7. The ORA has reviewed the application and has raised no objection to its approval.

Conclusions of Law

1. Pacific Bell's space use arrangements with its administrative affiliates do not impair its ability to serve the public.

2. Pacific Bell's accounting for the revenue from the leases and other arrangements appears to be in order.

3. There is no evidence of anticompetitive effects or cross-subsidization of non-regulated entities from these use agreements.

4. The application should be approved.

5. Pacific Bell should be authorized to enter into the leases and other space use arrangements as set forth in Exhibit A of the application.

6. Pacific Bell should be required to notify the Telecommunications Division when the leases have been executed and offer to make the leases available for inspection.

7. This order should be made effective immediately in order that the arrangements can be implemented promptly.

ORDER

IT IS ORDERED that:

1. Pacific Bell is authorized, pursuant to Public Utilities Code § 851, to enter into the space use leases and other arrangements with administrative affiliates as set forth in Exhibit A of this application, on the terms and conditions set forth in the application.

2. Pacific Bell shall notify the Director, Telecommunications Division, in writing, when the lease agreements authorized herein have been executed, and shall state at that time whether the agreements conform to the Commission's affiliate transaction rules.

3. This proceeding is closed.

This order is effective today.

Dated December 16, 1997, at San Francisco, California.

P. GREGORY CONLON

President

JESSIE J. KNIGHT, JR.

HENRY M. DUQUE

JOSIAH L. NEEPER

RICHARD A. BILAS

Commissioners