

FEB 4 1998

Decision 98-02-005 February 4, 1998

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 and/or Transfer Assets to
Administrative Affiliates.

Application 97-10-029
(Filed October 10, 1997)

O P I N I O N

ORIGINAL

1. Summary

Pacific Bell seeks Commission approval, pursuant to Public Utilities (PU) Code § 851, to lease or transfer office equipment and other assets to affiliate corporations which will perform administrative support functions for Pacific Bell. Pacific Bell states that the lease and transfer arrangements comply with affiliate transaction rules of this Commission and of the federal government. 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 to affiliates and other parties 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.

This application is related to Pacific Bell's A.97-09-027, filed on September 18, 1997. In that application, Pacific Bell requested authority to lease space currently used by certain internal administrative groups to affiliates which will be taking over the responsibility to perform those functions. The affiliates will perform the functions previously performed by and reside in the space occupied by Pacific Bell's Technologies Services Group, and the Real Estate, Collections, Fraud, Payment Processing, and Audit Service organizations, as well as portions of the Procurement, Human Resources, Marketing and Accounting organizations.

The Commission in D.97-12-087 approved A.97-09-027, authorizing Pacific Bell to lease space to the affiliate corporations that now are performing the administrative functions for Pacific Bell and for other affiliates of parent company SBC Communications Inc., such as Nevada Bell, Southwestern Bell Telephone Company, and others.

In this application, Pacific Bell proposes to lease computers, copiers, office furniture and other equipment now used by the administrative affiliates. Pacific Bell states that all of the leases and other arrangements will be under affiliate transaction agreements that comply with the Commission's decisions and federal requirements governing affiliate transactions, including accounting directives.

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 equipment lease and transfer arrangements here are similar to those previously approved by the Commission. Pacific Bell states that, as in those earlier arrangements, it seeks authority only to lease or transfer assets currently

used by the former internal organizations. The specific functions and the new administrative affiliates to which the assets will be transferred are summarized below:

Audit Services. This organization provides internal auditing functions. The entire 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.

Pacific Bell states that it seeks authority in this application only for the audit services, procurement, human resources and marketing affiliates. The company states that it will file a separate application for authority to lease and transfer assets of other organizations included in A.97-09-027, which include the Technologies Services, Group, Real Estate, Collections, Fraud, Payment Processing and Accounting organizations.

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 and transfer arrangements. Exhibit A is a matrix with details of the assets that would be leased or transferred, itemized by organizational group. Exhibit B contains a description of the billing process for assets leased to the affiliates. Exhibits C, D, E and F contain the company's transfer pricing manuals, affiliate transaction policies and reporting requirements, along with an example of the company's transfer pricing schedule for the lease of assets.

4. Affiliate Transaction Rules

Pacific Bell states that when it permits the administrative affiliates to use the equipment and assets, 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 the Commission's rules, each affiliate pays Pacific Bell the higher of fully distributed cost plus 10%, or market rate, whichever is greater.

5. Reasons for the Leases and Transfers

Pacific Bell states that the performance of 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 lease and transfer arrangements will not interfere with existing operations. In fact, Pacific Bell states, having these operations remain in California should mean better service for Pacific Bell and its customers. Pacific Bell states that, because the leases and transfers comply with affiliate transaction rules, the affiliates will not be subsidized by Pacific Bell and the arrangements will not create anticompetitive effects.

6. Comments to Application

The Commission's Office of Ratepayer Advocates (ORA) filed comments on this application on November 14, 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 transactions (Exhibit F) indicates that Pacific Bell will apply the same pricing method to the leased assets as has previously been approved by the Commission. (See D.96-11-019.) However, since copies of the actual lease and transfer documents are not included in the application, ORA urges that the Commission require Pacific Bell to verify that the executed 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 lease and transfer arrangements with affiliates.

Review of the information provided shows that Pacific Bell's lease and transfer of equipment and other assets to its affiliates will 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. At ORA's suggestion, we will require Pacific Bell to notify our Telecommunications Division in writing when the lease and transfer documents are executed, and to state at that time whether the documents conform to our affiliate transaction rules.

Findings of Fact

1. Pacific Bell seeks Commission approval, pursuant to PU Code § 851, of asset lease and transfer arrangements with administrative affiliates.
2. Notice of this application appeared on the Commission's Calendar on October 15, 1997.
3. No protests have been filed.
4. Pacific Bell has shown that the equipment and other assets to be leased or transferred to 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, whichever is greater, for the use of the leased or transferred assets.
6. Pacific Bell has supplied the information required by the Commission for review of the lease and transfer arrangements.
7. The ORA has reviewed the application and has raised no objection to its approval.

Conclusions of Law

1. Pacific Bell's proposed lease and transfer of assets to its administrative affiliates will not impair Pacific Bell's 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 arrangements.
4. The application should be approved.
5. Pacific Bell should be authorized to enter into the leases and transfer of the assets set forth in Exhibit A of the application.
6. Pacific Bell should be required to notify the Telecommunications Division when the leases and transfer documents have been executed and offer to make these documents available for inspection.

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

O R D E R

IT IS ORDERED that:

1. Pacific Bell is authorized, pursuant to Public Utilities Code § 851, to enter into the asset lease and transfer 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 and transfer 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 February 4, 1998, at San Francisco, California.

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