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ORIGINAL

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking on the)
Commission's Own Motion into the)
Establishment of a Rate Case Plan)
for Small Local Exchange Carriers.)

F I L E D
PUBLIC UTILITIES COMMISSION
JUNE 25, 1997
SAN FRANCISCO OFFICE
R.97-06-038

O R D E R

Summary

By this order, we open a rulemaking proceeding to establish a rate case plan (RCP) applicable for the small local exchange carriers (LEC) under traditional cost-of-service regulation. All small LECs are required to comment and invited to provide reply comments on the proposed RCP set forth in Appendix B to this rulemaking proceeding. Interested parties are invited to comment and to provide reply comments on the proposed RCP.

Background

Prior to the issuance of Decision (D.) 89-10-031 (33 CPUC2d 43 (1989)), the basic regulatory framework for large, mid-size, and small LECs¹ in California had changed very little since this Commission began regulating telecommunications. This basic regulatory framework relied on traditional cost-of-service regulation, commonly known as rate base and rate-of-return regulation, to set rates for the LECs.

¹ The large LECs consist of GTE California Incorporated (GTEC) and Pacific Bell (Pacific). The mid-size LECs consist of Citizens Utilities Company of California (Citizens), Contel of California, Inc. (Contel), and Roseville Telephone Company (Roseville). The small LECs consist of all remaining certificated LECs, a total of 18, ranging in size from the Pinnacles Telephone Company with approximately 180 access lines to Sierra Telephone Company with approximately 18,000 access lines.

From the start of telecommunications regulation until the issuance of Resolution A-3792 on May 19, 1970, LECs sought general rate changes through the application process. This resolution enabled those LECs with less than \$50,000 in annual intrastate operating revenues to seek general rate changes through a simplified advice letter process, pursuant to Section VI of General Order (GO) 96-A. On September 24, 1974, we increased the annual operating revenue limit for general rate case advice letter filings from \$50,000 to \$150,000, pursuant to Resolution A-4313.

With regulatory lag i.e., the delay between seeking and obtaining relief from the Commission confronting our regulatory process, we adopted a Regulatory Lag Plan (RLP) for the large LECs, pursuant to Resolution A-4693 on July 6, 1977. The experience gained from processing general rate changes under the RLP enabled us to consider modifications that would make the RLP more workable and further minimize regulatory delay while providing an administrative forum with fairness to all. Hence, the RLP was modified to, among other matters, require the large LECs to file a general rate case proceeding every two years through the application process, pursuant to Resolution A-4706 on June 5, 1979. The RLP was renamed the Rate Case Processing Plan approximately three years later, pursuant to Resolution ALJ-149 on October 20, 1982.

Although the RLP was not designed to expedite rate relief for the small LECs, we acknowledged in Resolution M-4701 (August 8, 1978), that the small LECs could receive expedited rate relief through the advice letter procedure. Hence, to include more small LECs under the advice letter procedure, we again increased the annual operating revenue limit for general rate advice letter filings set forth in GO 96-A from \$150,000 to \$750,000. At the same time, we limited the number of general rate increase filings a small LEC may file to one every two years. The annual operating revenue limit for general rate advice letter filings was further

relaxed with the issuance of Resolution T-10408 on May 19, 1981. This resolution excluded toll revenues from the \$750,000 annual operating revenue limit for general rate advice letter filings. Both, the increase in the annual operating revenue limit and modification of the annual operating revenue definition qualified more small LECs to seek general rate changes through the simplified advice letter process.

However, in D.82-08-072 (9 CPUC2d 603 at 606 (1982)) we found that no LEC eligible under the annual revenue exemption had ever used the GO 96-A annual operating revenue authorization to submit a general rate case under the advice letter process. Accordingly, we exempted small LECs from the annual operating revenue limitation contained in Section VI of GO 96-A. This change enabled all small LECs to seek general rate changes through the advice letter process, irrespective of what their annual operating revenues were.

With the tremendous changes in the telecommunications industry and the California marketplace that occurred in the 1980's from technological innovations and regulatory developments, we found our traditional cost-of-service regulation becoming obsolete. Hence, we responded to these changing industry conditions in 1987 with the issuance of an investigation (I.87-11-033) to reconsider the regulatory framework within which LECs are regulated.

By D.89-10-031 we replaced the large LECs general rate case proceedings with a New Regulatory Framework (NRF). The traditional cost-of-service regulation for large LECs became extinct. The NRF started an incentive-based regulatory process centered on a price cap indexing mechanism that provides a sharing between ratepayers and shareholders, and as modified by subsequent Commission orders, of excess earnings above an initial benchmark rate of return, and a 100% assignment to ratepayers of excess earnings above a second, higher benchmark rate of return rate.

While adopting NRF for the large LECs, we foresaw a growing number of alternatives to LEC services. In response to such alternative services, we devised an incentive framework which separated services into three categories: monopoly services for which no competition is authorized, discretionary or partially competitive services for which competition is authorized with pricing flexibility between appropriate price ceilings and price floors, and fully competitive telecommunications services with full pricing flexibility and minimal tariff requirements. Price flexibility for Category II services was added to NRF pursuant to D.94-09-065.

The mid-size LECs, Citizens and Roseville, filed general rate cases and requested NRF regulation. Citizens' and Roseville's requests were approved by D.95-11-024 and D.96-12-074, respectively. The only remaining mid-size LEC, Contel, is in the process of completing a merger and integration of its rates with those of GTEC, already under NRF. Hence, all mid-size LECs are or soon will be under NRF regulation.

Up to this time, none of the mid-size or small LECs had concluded a recent general rate case or brought themselves under NRF. Most of the small LECs had not had a general rate review for seven to eleven years. To the extreme, three of the small LECs have not had a rate proceeding since the 1960's, approximately 30 years. We found that the returns actually earned by the mid-size and small LECs in the past years under the traditional cost-of-service regulation were substantially higher than their authorized returns. For example, one small LEC which was authorized a 13.0% return actually realized a 26.9% return in 1991. We, therefore, required the mid-size and small LECs to file general rate cases and, to the extent they wished, applications to adopt NRF, no later than December 31, 1995, pursuant to D.94-09-065.

Twelve of the small LECs submitted general rate case requests under the advice letter process while five others submitted general rate requests under the application process.

Telephone Utilities of Eastern Oregon, with a California exchange and not a party to I.88-11-033, did not file a general rate case request. All 17 of the small LECs requesting authorization to continue with traditional cost-of-service regulation were granted approval.

Discussion

We recognize that the small LECs do not routinely submit to general rate reviews. However, with their continued use of traditional cost-of-service regulation; dependency on toll, access, and intercompany settlements with Pacific; and the implementation of NRF regulation for the large and mid-size LECs, the small LECs revenue streams are subject to volatility that should be reviewed on a scheduled basis to assure a reasonable balance between the interest of small LECs and their respective ratepayers. Hence, this rulemaking procedure should be opened to establish an RCP for the small LECs which have opted to continue operating under traditional cost-of-service regulation. We will require the small LECs and invite other interested parties to comment on the proposed three-year RCP cycle set forth in Appendix B to this order.

IT IS ORDERED that:

1. A rulemaking proceeding is instituted to establish a rate case plan (RCP) for the small Local Exchange Carriers (LECs) which have opted to continue operating under traditional cost-of-service regulation, as listed in Appendix A to this order.

2. The small LECs listed in Appendix A to this order are named respondents to this rulemaking proceeding.

3. Named respondents are required and interested parties are invited to file comments on the small LECs RCP attached to this order as Appendix B. Comments shall be filed with the Docket Office on or before September 1, 1997. Comments need not be served on all parties receiving a copy of this rulemaking. However, copies shall be served on each respondent LEC to this rulemaking and shall be made available to any party requesting such copies.

In this regard, the Process Office shall maintain and make available to any party a list of parties who file comments and their addresses. It is the responsibility of the individual parties seeking copies of comments to request such copies from the parties who file comments.

4. Named respondents and interested parties are invited to file reply comments with the Docket Office on or before September 30, 1997. Copies of the reply comments shall be served on each party that filed comments.

5. The Executive Director shall have this order and appendices served by regular mail on the respondent LECs and on all parties to Investigation 87-11-033, the investigation into alternative regulatory frameworks for LECs.

This order is effective today.

Dated June 25, 1997, at San Francisco, California.

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

APPENDIX A

SMALL LOCAL EXCHANGE COMPANIES

Calaveras Telephone Company	U-1004-C
California-Oregon Telephone Company	U-1006-C
CTC of the Golden State	U-1025-C
CTC of Tuolumne	U-1023-C
Ducor Telephone Company	U-1007-C
Evans Telephone Company	U-1008-C
Foresthill Telephone Company	U-1009-C
GTE West Coast Incorporated	U-1020-C
Happy Valley Telephone Company	U-1010-C
Hornitos Telephone Company	U-1011-C
Kerman Telephone Company	U-1012-C
Pinnacles Telephone Company	U-1013-C
The Ponderosa Telephone Company	U-1014-C
Sierra Telephone Company, Inc.	U-1016-C
Telephone Utilities of Eastern Oregon, Inc.	U-1022-C
The Siskiyou Telephone Company	U-1017-C
The Volcano Telephone Company	U-1019-C
Winterhaven Telephone Company	U-1021-C

(END OF APPENDIX A)

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APPENDIX B

Appendix B
Small Local Exchange Company
General Rate Case Plan

1. Description
2. Advice Letter Filing
3. Application Filing
4. General Issues
5. Attachments (6)

Description

This plan presents a 3-year cycle in which 6 small LECs file a GRC each year such that all 18 small LEC GRCs are completed within the 3-year cycle. Each GRC involves a 420 day turnaround, consisting of a 60 day workpaper preview/approval by staff, and Commission approval by resolution or decision within 300 days. Compliance tariffs are filed and made effective before the 360th day.

The 18 small LECs are categorized into four classes based on size (see Attachment 1). One Class A GRC per year is allowed; affiliated companies are encouraged to file during the same year. Order of filing will be negotiated by the small LECs and staff, or will be determined by drawing if necessary.

The first 6 GRCs will be filed January 1999 (workpapers due October 1998) for Test Year 2000. Subsequent test years in the first cycle will be 2001 and 2002. Since all companies will have submitted Advice Letter workpapers or tendered a Notice of Intent to file a GRC application before 2001, California High Cost Fund eligibility at 100% will have been satisfied (the CHCF water fall drops to 80% in 2001, 50% in 2002, and 0% in 2003 for small LECs who have not filed a GRC).

Each small LEC may file a GRC by advice letter (GO-96A) or by application (Rules of Practice and Procedure).

Advice Letter Filing

Attachment 2 presents a timeline and milestones for those companies filing GRCs by advice letter. Attachment 3 illustrates the 3-year cycle in which all 18 small LEC GRC advice letter filings would be completed.

Application Filing

Attachment 4 presents a timeline and milestones for those companies filing GRCs by application. Attachment 5 illustrates the 3-year cycle in which all 18 small LEC GRC applications would be completed. Small LECs may file applications for GRC and New Regulatory Framework (NRF) authority. Once NRF authority and a start-up revenue requirement has been granted, the small LEC would be exempt from the GRC Rate Case Plan (annual Price Cap Advice Letters and triennial reviews are substituted).

General Issues

The actual filings by small LECs will be a mixture of advice letters and applications each year. Nevertheless, all six filings each year will be acted upon the Commission within 300 days of the filing, with compliance tariffs to be submitted and made effective by the 360th day. Commission staff working on GRC filings shall be segregated, so that a staff-

Appendix B - Small LEC General Rate Case Plan

Attachment 1 - Small LEC Class and Affiliations

Class A - 10,000 lines or more

***CTC of the Golden State
GTE West Coast, Inc.
Sierra Telephone Company**

Class B - more than 5,000 lines

**Evans Telephone Company
Kerman Telephone Company
The Ponderosa Telephone Company
*CTC of Tuolumne
The Volcano Telephone Company**

Class C - more than 1,000 lines

**Calaveras Telephone Company,
California-Oregon Telephone Company
Foresthill Telephone Company
#Happy Valley Telephone Company
The Siskiyou Telephone Company
#Winterhaven Telephone Company**

Class D - less than 1,000 lines

**Ducor Telephone Company
#Hornitos Telephone Company
Pinnacles Telephone Company
Telephone Utilities of Eastern Oregon, Inc.**

**Notes: * - affiliated companies of Citizens Telecommunications Company
- affiliated companies of TDS.**

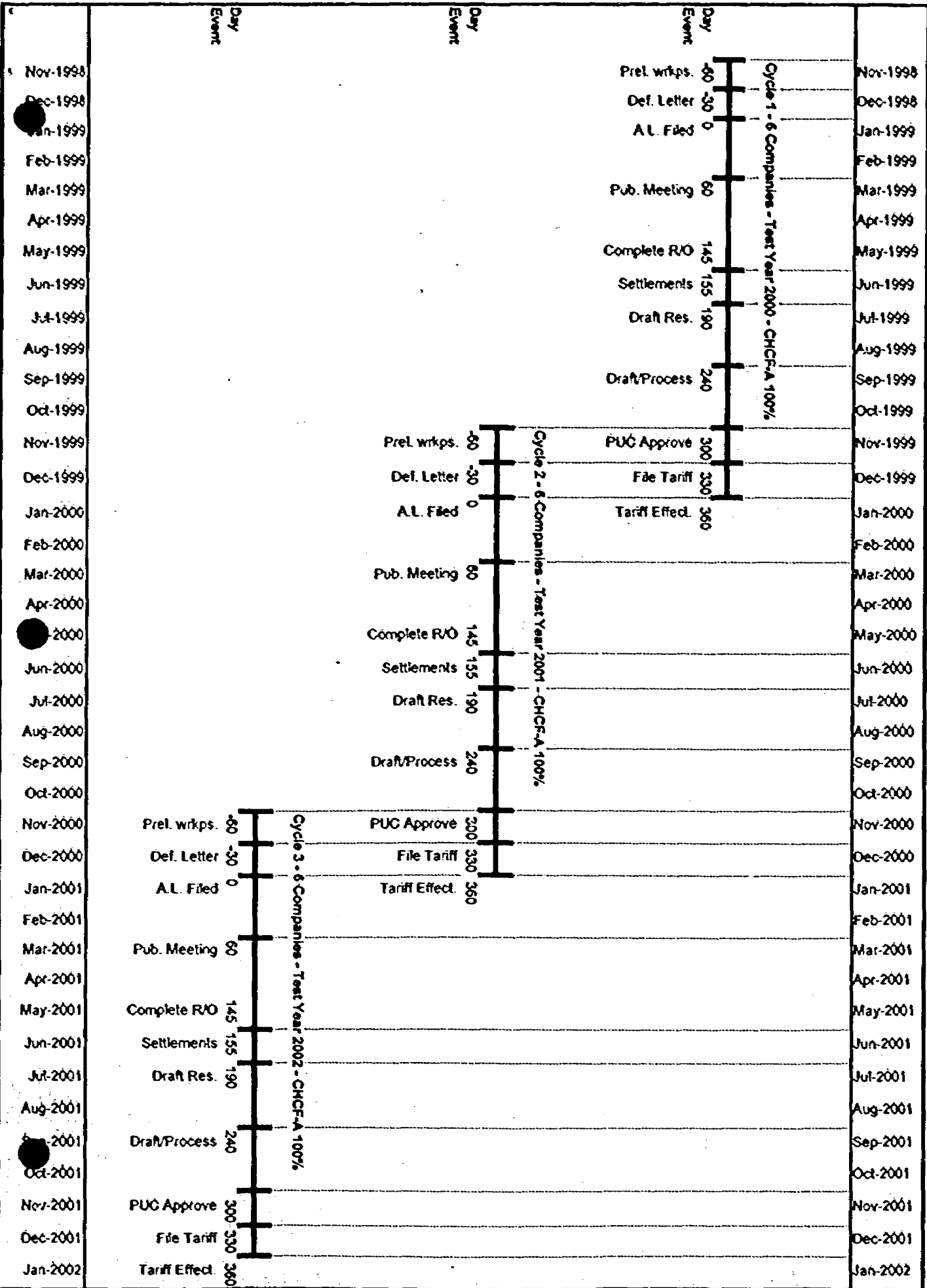
Appendix B - Small LEC General Rate Case Plan

Attachment 2 - Advice Letter Timeline and Milestones

**Calendar Day
Schedule**

-60	Tender preliminary workpapers.
-30	Staff issues deficiency letter.
1	File advice letter, set informal public meeting dates, mail customer notification.
45 to 60	Informal public meetings.
145	Completion of staff results of operation estimates and rate design.
155	Staff and company differences resolved.
190	Completion of draft resolution for management review.
240	Final draft resolution to Process Office.
300	Commission approval of resolution.
330	Company files compliance tariffs.
360	Compliance Tariffs reviewed and made effective.

Appendix B - Attachment 3 Timeline for Small LEC GRC Plan (Advice Letter Filing)

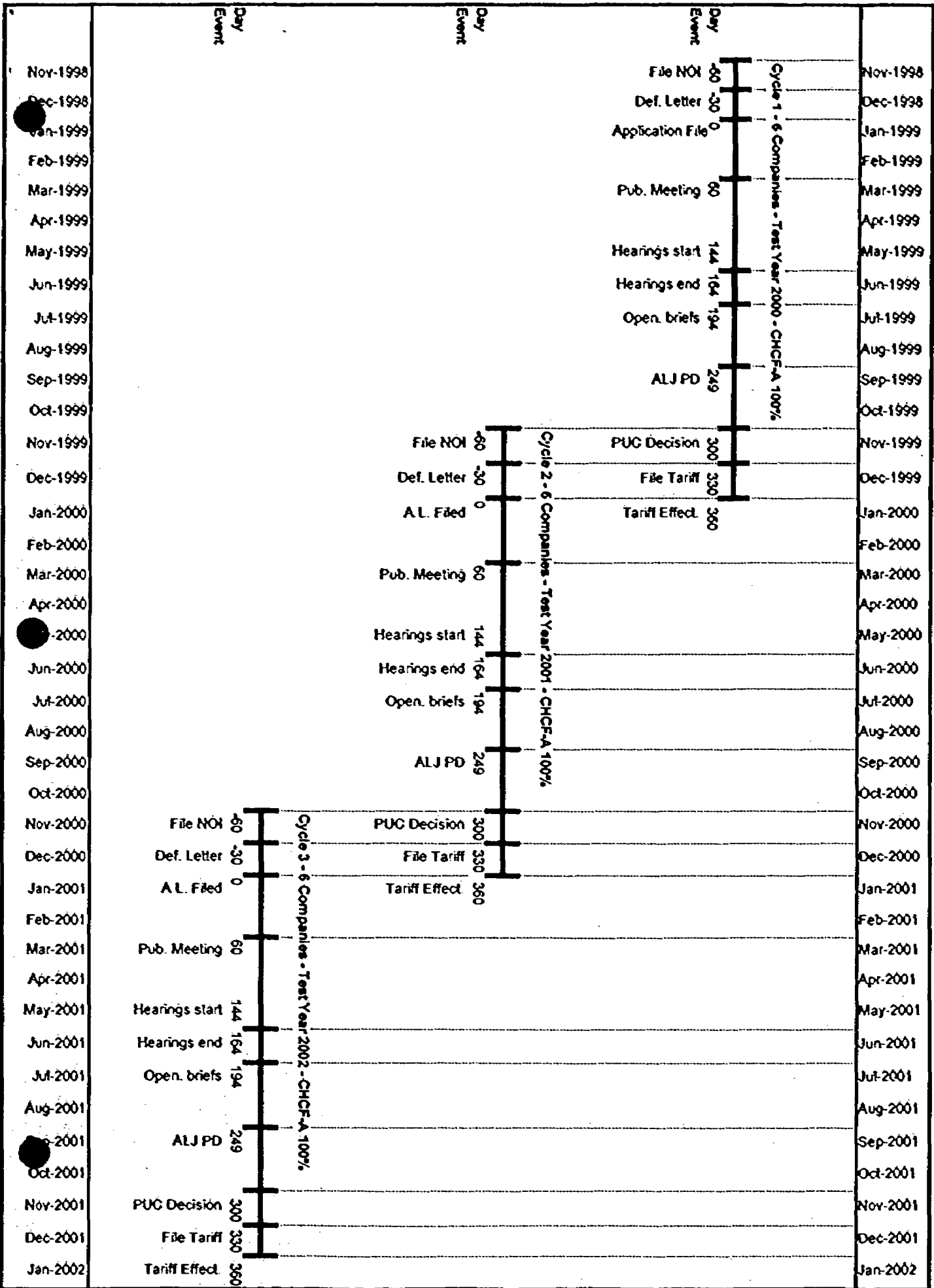


Appendix B - Small LEC General Rate Case Plan

Attachment 4 - Application Timeline and Milestones

<u>Calendar Day</u>	
<u>Schedule</u>	
-60	NOI Filed
-30	Staff Issues deficiency letter
-10	Commissioner and ALJ assigned
-5	Public Meeting dates set
1	Application filed
5 to 75	Hearing dates set
30	Final update of Utility showing
45 to 60	Public Meetings
124	Staff submits exhibits
144	Hearings start
164	Hearings end
194	Concurrent opening briefs
214	Concurrent reply briefs
249	ALJ's proposed decision
269	Comments on proposed decision
274	Replies to Comments
300	Commission Decision
330	Company files compliance tariffs
360	Compliance tariffs reviewed and made effective

Appendix B - Attachment 5 Timeline for Small LEC GRC Plan (Application Filing)



Appendix B - Small LEC General Rate Case Plan

Attachment 6 - Suggested Workpaper Content and Format

Test Year - a 2000 Test Year is assumed, with 1999 and 1998 Estimated Years.

Cost Support - Long Run Incremental Cost (LRIC), Direct Embedded Cost (DEC), and Fully Allocated Cost (FAC) studies should be submitted as appropriate to support cost based pricing of rate design emphasized in Decision No. 94-09-065. Pacific Bell or GTB California pricing may be submitted as surrogates.

Balance Sheet and Income Statements - a balance sheet as of the latest available date, together with an income statement covering period from close of last year for which an annual report has been filed with the Commission to the date of the balance sheet submitted.

Service -

GO 133-B: Monthly summary records of each service measurement for each reporting unit for the last two years in accordance with paragraph 4.4 of GO 133-B.

D.86593 (Nov 2, 1976): Copy of latest quarter's primary and regrade orders held for over 60 days with explanation of what steps are being taken to fill such orders.

General -

The advice letter should meet the requirements of Section VI of GO 96-A, Section 454 of the Public Utilities Code, and the Commission's Rules of Practice and Procedure.

Results of Operations should be provided for the Test Year (2000), 1999 and 1998 Estimated Years, and 1993 through 1997 recorded. Separated Results of Operations should be provided for 1993 through 2000, stated separately by year.

The calculation of the Net-to-Gross Multiplier should be presented.

The cost of capital and rate of return calculations and workpapers should be presented.

Five years recorded plus year-to-date number of access lines in service and inward movement for 1993 through 1997. In addition, please provide 1998, 1999, and 2000 estimated access lines in service and inward movement. Other station statistics may be requested.

A revenue effects table that documents, by tariff schedule, the revenue contributions for the Estimated and Test Years of all tariffed items in each schedule, i.e., the aggregate revenue contribution from exchange service, directory service, etc.

A rate table that documents your present and proposed rates by tariff schedule for all services you provide.

A draft of proposed tariff schedules which set forth your proposed rate design and tariff revisions.

A rate design and revenue effect for the Test Year of a restructuring of EAS routes and increments based on the revised Salinas Formula (D.93728), if applicable.

Operating Revenues -

Five years recorded uncollectible revenues separated for local service, interstate toll service, intrastate interLATA toll service, intrastate intraLATA toll service, miscellaneous revenues, etc.

All workpapers should be properly referenced to show or explain the basis or methodology used in the derivation of volumes and revenues for all services for 1998, 1999, and 2000 years, i.e., growth rates, stimulation factors, graphs, linear trend, known adjustments, subjective basis, correlation with account or statistics, etc.

All workpapers should be properly referenced to support the development of settlement revenues and separated results of operations, i.e., separation factors, settlement ratios for interstate toll and PL, intrastate interLATA toll and PL, intrastate intraLATA toll and PL, and EAS; explain how the separation factors and settlement ratios were derived, etc.

Estimated EAS Revenue Credit, if any, should be provided with supporting workpapers showing all calculations.

Expenses -

Breakdown of operating expenses by FCC account for the Test Year, Estimated Years, and for each of the preceding five years recorded.

Please provide current depreciation rates and provide depreciation study which is the basis of these rates, including workpapers properly referenced showing derivation of the depreciation expense and reserve for the Test Year and Estimated Years.

Please include statement of tax methods used for tax, book, and ratemaking purposes for the Test Year, including detailed workpapers properly referenced showing the calculation of all taxes.

Rate Base (Average) -

In the Summary of Separated Results of Operations Tables, compute Net Operating Income and Rate of Return, for each Recorded Year (1993-1997), the Estimated Years (1998, 1999), and the Test Year (2000).

Use Standard Practice U-16 (September 13, 1968) for completing Working Cash Allowance, Simplified Basis.

Show Rate Base components on Results of Operations tables.

Provide the Utility's Capital Expenditure Budgets for 1998 and next two years.

Provide complete and adequate workpapers to support all estimates, including the Estimated Years and the Test Year figures.

All Plant in Service, Depreciation, and Rate Base workpapers should be detailed and properly referenced.

Telecommunications Division staff will hold workshops to facilitate workpaper and spreadsheet (computer model) standardization.

(END OF APPENDIX B)