PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

EVALUATION & COMPLIANCE DIVISION
Telecommunications Branch

RESOLUTION NO. T-12007
March 25, 1987

RESOLUTION

PACIFIC BELL: ORDER REQUIRING ATTRITION YEAR 1987 REVENUE REQUIREMENT REDUCTION OF $191,041,000.

SUMMARY

In compliance with D.86-12-099 Pacific Bell (Pacific) filed Advice Letter No. 15215 on January 21, 1987 and Supplemental Advice Letter No.15215A on February 24, 1987, requesting 1987 attrition year revenue requirement reduction of $75,748,000. To implement this, Pacific proposed an adjustment to its current billing surcharge to be applicable to amounts shown on bills rendered on and after the effective date of the tariff.

Ordering Paragraph No. 1 of D.86-12-099 required Pacific to file a 1987 attrition year advice letter addressing both operational and financial attrition. Operational attrition requests were to be developed using formulas and inputs listed in Appendices A, B and C of the Decision. The financial attrition filing was to include Pacific's year-end 1986 capital structure and embedded debt costs. Ordering Paragraph No. 4 of D.86-12-099 provided that Pacific's intrastate rates and charges be collected subject to refund after January 1, 1987 to account for any adjustments associated with the 1987 attrition review.

Based on our review, Pacific's 1987 attrition revenue requirement is a reduction of $191,041,000, as shown in Appendix A of this resolution. The issues which result in the $115,293,000 difference are:

Financial Attrition	<$64,387,000>
Depreciation Technical Update	< 35,892,000>
Excess management salary increase	< 3,560,000>
Attrition effect on interest	< 12,715,000>
Other	1,261,000
TOTAL	<$115,293,000>

These categories and their dollar amounts are offered as summaries. Each interacts to some extent with the other.

PROTESTS

Public Staff Division (PSD) filed a protest to Pacific's Advice Letter No. 15215 on February 6, 1987. PSD objected to the financial attrition, citing that the use of year-end 1986 capital structure resulted in (1) the equity component of 56.02% exceeded the cap of 55% set in D. 86-01-026 by 102 basis points and by 452 basis points over the 51.5 % component authorized in that Decision and (2) it does not include the imputed $82,000,000 of 6% preferred stock which the Commission indicated it would continue to impute (D.86-01-026, mimeo,p.16). Both of the conditions adversely affect the ratepayers. PSD recommends the original capital structure determined reasonable in D. 86-01-026, which includes the 6% preferred stock adjustment and formed the basis for the currently authorized 15% return on common equity, be utilized in determining financial attrition.

Pacific responded to PSD's protest on February 17,1987. Pacific states its advice letter filing is in compliance with D.86-12-099 and PSD's protest should be denied. Pacific further states, "The PSD apparently claims that Pacific should have purposely chosen not to comply with the express Order of Decision No. 86-12-099....The PSD's argument ignores Pacific's statutory obligation to comply with Commission's Orders (see, Public Utilities Code Section 702)." Pacific also notes the "Commission's expressed desire to review year-end data 'because [such data] is available and easily verifiable' (D.86-12-099, mimeo p. 7)."

On February 17, 1987 PSD filed a supplement to its February 6, 1987, protest objecting to the depreciation technical update. PSD states the increase in intrastate depreciation expense of $53,442,000 is based on Pacific's mismatched use of composite accrual rates. The mismatch arises by Pacific's use of the technically updated composite rate of 6.51% (authorized by Resolution No.T-11098, dated January 28,1987) derived from 1987 projected plant and the adopted test year 1986 composite accrual rate of 6.12% derived from 1986 adopted plant. PSD recommended the 1986 composite depreciation rate be recomputed to reflect 1985/86 adopted parameters and rates applied to the 1987 plant mix. The recomputed composite 1986 rate would be 6.43%

Pacific responded to PSD's supplemental protest on February 27, 1987, stating, "Pacific has correctly calculated the 1987 growth in the composite depreciation rate from 6.12 to 6.51 percent by analyzing the following three factors: (1) changes in plant mix, (2) second year ELG and (3) rate changes on individual accounts." Pacific further stated, "If the PSD's contention is valid that Pacific's 1986 adopted accrual rate should be transformed to 6.43 percent, then, simply put, Pacific has been under-recovering a legitimate revenue requirement throughout 1986."

Turn Utility Rate Normalization (TURN) filed its protest to Pacific's Advice Letter No. 15215 on February 4, 1987 and a supplement on February 27, 1987. Turn concurs with PSD's protests and raises additional objections to (1) Pacific using a 1985 estimate of 1987 Telephone Plant Index and (2) inclusion of "discretionary and exhorbitant (sic) increases in certain labor expenses..." It also requests a review in more detail of Pacific's refinancing of earlier high-cost debt issues.

On March 9, 1987, Pacific responded to TURN's protests. Pacific referred to its responses to PSD's protests regarding depreciation technical update and financial attrition. It also referred to an article in the Wall Street Journal of January 19, 1987, in support of its management salary increase. Concerning the Telephone PLant Index, Pacific stated it used the most recent data available at the time of the filing. With reqard to refinancing debt, Pacific stated, "TURN does not detail its concerns...TURN's protest is without merit."

PSD's protest of February 6, 1987 and supplement of February 17, 1987, and Pacific's responses are attached as Appendices B and C. Appendices D and E contain TURN's protests of February 4, 1986 and February 27, 1987 and Pacific's March 9, 1987 response.

Our review of financial attrition and technical update incorporate the concerns covered in PSD's protests. Matters raised by TURN are dealt with in our handling of the labor growth factor and financial attrition and need no further action.

DISCUSSION

OPERATIONAL ATTRITION

Appendices A, B,and C of D.86-12-099 provide the formulas, definitions and selected adopted 1986 results for calculating operational attrition. Our review found two formulas and two factors used by Pacific were not consistent with the above Decision. The Attrition Year 1987 Telephone Plant in Service (TPIS) formula should include an intrastate separation factor. The adjustment made to Federal Income Tax (FIT) and California Corporate Franchise Tax (CCFT) should include the FIT/CCFT effects on change in taxable income.

1. Nonlabor escalation factor

In Decisions 86-12-099 and 85-03-042 the Commission dealt extensively with methods to develop an appropriate nonlabor escalation factor. Since no superior method has been demonstrated, in D.86-12-099 we retained the methodology developed by PSD in D.85-03-042. The factor is developed on a detailed analysis of the composition of Pacific's nonlabor expenses, using appropriate indices for unfinished goods for measuring the expected change in price for major components of nonlabor expenses. Using the methodology adopted in D.85-03-042 results in a nonlabor escalation factor of 3.04%, 6 basis points lower than Pacific's 3.10%.

Pacific's nonlabor escalation factor of 3.10% was developed using new relative weightings of purchasing categories other than those adopted in D.85-03-042. We caution Pacific that in future attrition filings it should comply with the adopted methodology. If Pacific would like the Commission to consider a new nonlabor escalation factor using new relative weightings and categories, Pacific should introduce them in its next general rate case.

Application of the 3.04% nonlabor escalation factor yields an intrastate materials, rents and services expense of $1,258,009,000, which is $732,000 lower than Pacific's filing of $1,258,741,000.

2. Growth in composite salaries and wages

Inflation factors received extensive discussion in Decisions 86-01-026 and 86-12-099. Several pages were devoted to determine wage and salary growth rates and nonlabor inflation factors. Growth rates in composite salaries and wages is not a simple or straight forward factor as the lengthy discussion indicates. Page 2 of Appendix B in Decision 86-12-099 states, "Growth in composite salaries and wages is based on labor contracts, and shall be adjusted to reflect test year actual wage agreements, if different than adopted test year forecasts."

Pacific calculated its 5.00% factor for growth in composite salaries and wages by weighting the relative growth of: (1) salaries and wages, (2) team incentive plan, (3) benefit plans, and (4) payroll taxes. Pacific claims that since the labor and labor overheads expense include these four items, it is only consistent that the growth rate includes these same items. Pacific further states that in its 1985 attrition filing, the factor included total compensation which includes benefits and social security taxes.

The team incentive plan and benefit plans are items not specially provided for in our attrition review. The team incentive plan provides compensation to employees based upon Pacific's previous year's (1986) financial and service goals.

The discussion on Page 2 of Appendix B of D.86-12-099 specifically lists wages/salaries, relief and pensions, and Social Security taxes as "labor and labor overheads", while it mentions "Growth in composite salaries and wages is based on labor contracts, and shall be adjusted to reflect test year actual wage agreements, if different than adopted test year forecasts." Although the attrition formula set forth on Page 2 of Appendix B of D.86-12-099 does not specifically mention team incentive plan or benefits plan we will include these items since they are part of the labor contract. However the inclusion of team incentive plan and benefits plan in attrition should be reviewed in a future appropriate proceeding in which the attrition mechanism will be re-examined.

Social Security tax increases are recognized to be statutory changes beyond Pacific's control, and therefore we will accept the inclusion of Social Security in the growth rate in this filing.

With regard to the payroll portion of the growth factor, our estimate is 2.39% compared to Pacific's estimate of 2.53%. Consistent with Appendix B, Page 2 of D.86-12-099, "Growth in composite salaries and wages is based on labor contracts...", the payroll portion of the growth rate is based on union wage agreement increases for non-management personnel. The same increase is applied to management for attrition purposes and to maintain the salary/wage alignment.

The revised composite salaries and wages growth rate, which includes team incentive plan, benefit plan, and Social Security is 4.86%. Application of this factor yields an intrastate labor and labor overhead expense of $2,427,165,000 which is $3,241,000 lower than Pacific's estimate of $2,430,406,000.

FINANCIAL ATTRITION

In D.86-12-099 Pacific was ordered to file its financial attrition using its actual year-end 1986 capital structure and embedded cost of debt for our consideration in determining Pacific's attrition adjustment. In response to that order, Pacific filed its financial attrition based on a capital structure consisting of 56.02% common equity and 43.71% debt and 0.27% preferred stock. In D.86-01-026 we expressed our concern regarding Pacific's level of common equity. We stated (mimeo, page 14), "We do not want to see the component rise above 55%. We are placing Pacific on notice that if it rises above 55%, we will not hesitate to impute a different capital structure which is more in line with the interests of ratepayers than those of Pacific and/or Telesis." It was because of our concern over Pacific's common equity ratio that we ordered the company to file its actual year-end 1986 capital structure and embedded cost of debt.

Pacific's financial attrition filing, based on a capital structure consisting of 56.02% common equity is 102 basis points higher than the 55% maximum level which we indicated would not be acceptable, and 452 basis points higher than 51.5% which we authorized in D.86-01-026. In addition, Pacific also failed to take into consideration $82,000,000 of 6% preferred stock the Commission imputed in D.86-01-026.

In D.86-01-026, we authorized a 15% return on common equity which was based on a 51.5% common equity ratio and a long-term debt ratio of 45.10% at an embedded cost of 10.03%. In the determination of a reasonable rate of return, we look at an equity ratio as a major element in our evaluation of financial risk. Generally speaking, the lower the equity ratio, the higher the risk; and the higher the ratio, the lower the risk. The 452 basis point increase in Pacific's equity ratio over that which was adopted when we authorized the 15% return on common equity plus the decrease in embedded cost of debt from the 10.03% adopted in D.86-01-026 to 9.25% at year-end 1986, significantly lowers Pacific's financial risk. If we were to consider a return on equity for Pacific utilizing its actual year-end 1986 equity ratio of 56.02% or the 55% which we indicated in D.86-12-099 plus the reduction in embedded cost of debt, we would likely re-evaluate the reasonableness of the 15% return on equity that was originally authorized in D.86-01-026.

In D.86-12-099 we determined that the 15% return on common equity was to be maintained in this filing. Whereas, as discussed earlier, we asked for the 1986 year-end capital structure so that we could monitor the capital structure in light of our previously expressed concerns. We do not modify our January 1986 Decision (D.86-01-026) where we found the 51.5% common equity component to be reasonable and adopted it. Therefore it would be unreasonable to use a common equity ratio above the 51.5% which we found reasonable in that Decision. We shall, therefore, compute Pacific's financial attrition by using the capital structure adopted in D.86-01-026 including the imputation of the 6% preferred stock adjusted for year-end 1986 actual embedded debt cost rate as filed by Pacific. The resulting overall rate of return will decrease by 36 basis points from the 12.52% adopted in D.86-01-026 to 12.16%, and the corresponding times-interest coverage will increase from 2.77X to 2.91X. Applying the reduction in rate of return to intrastate rate base will result in a $74,772,000 reduction in gross revenue requirements. However, because Pacific's composite rate in the embedded cost of debt has decreased, there will be a lesser amount of interest expense available as a tax deduction. This will result in an increase in revenue requirements of $37,459,000 over that using the composite debt rate adopted in D.86-12-099. The resulting overall net reduction in revenue requirements due to the change in rate of return and embedded cost of debt is negative $37,313,000.

We note that Pacific's proposed financial attrition is a $10,385,000 reduction in revenue requirement due to the decrease in overall rate of return. However, the change in income tax expense due to the decrease in Pacific's debt ratio and embedded cost of debt increases revenue requirements by $51,379.000. Therefore, the overall change in revenue requirements under Pacific's financial attrition proposal is an increase of $40,944,000.

OTHER ADJUSTMENTS

Decision 86-12-099 indicated other adjustments are appropriate for attrition filing. Revenues should be adjusted to reflect timing of rate awards and technical update of book depreciation rates.

1. Advice letters for new services.

Pacific has included $5,900,000 incremental revenue requirement effect due to Advice Letters for new services effective from January 1986 through June 1986. We note that this $5,900,000 is currently under consideration in Phase II of A.85-01-034, and therefore, will be excluded from this attrition filing. The amount that we will include is the revenue requirement effect of $3,900,000 for Advice Letters for the period from July through December 1986, which is not currently considered in Phase II of A.85-01-034.

2. Technical Update for Depreciation Expense

On January 28, 1987 we issued Resolution T-11098. This resolution provided technical update of straight-line remaining life depreciation rates for all telephone plant, except Circuit and Electronic categories of Central Office equipment, which use equal life groups, based on 1987 average plant. Table A of that resolution shows the 1987 estimated average plant; the 1987 depreciation expense at 1986 depreciation rates; the 1987 depreciation expense at 1987 depreciation rates; and the difference in depreciation expense between 1986 and 1987 depreciation rates. Resolution T-11098 is the basis of our technical update and is attached as Appendix F.

Pacific proposed an intrastate depreciation expense increase of $53,443,000 for technical update. Pacific used, for its 1987 attrition calculation a composite depreciation rate of 6.51% based on 1987 plant mix and a 1986 composite depreciation rate of 6.12% based on the adopted 1986 plant mix rather than the 1987 plant mix as shown in Resolution T-11098.

However, technical update reflects the change in depreciation expense due to the change in depreciation rates applied to the same year plant mix. Our 1986 composite depreciation rate, consistent with Resolution T-11098, based on 1987 plant mix is 6.43% as compared with Pacific's 1986 composite depreciation rate of 6.12%.

Using the revised 1986 composite depreciation rate of 6.43% yields an intrastate depreciation expense of $10,963,000, or $42,480,000 lower than Pacific's estimate of $53,433,000. The revised revenue requirement, taking into effect depreciation reserve, deferred taxes and income taxes is $9,391,000, which is $35,892,000 less than Pacific's estimate of $45,283,000.

BILLING SURCHARGE/SURCREDIT

Pacific proposes to adjust its current intrastate intraLATA billing surcharge and access service billing surcredit to flow through the 1987 attrition revenue requirement reduction applicable to bills rendered on and after the effective date of the tariff on a Bill-and-Keep basis. Pacific proposes a one-time one-month IntraLATA billing surcharge of 0.74% (reduced by 3.39 from the existing 4.13%) and an access billing surcredit of -5.91% (reduced by 3.39 from existing -2.52%) to reflect the reduction in attrition revenue requirement accrued from January 1,1987 through the first month after the effective date of the tariff. Thereafter a monthly intraLATA billing surcharge of 3.00% and an access surcredit of -3.65% (both reduced by 113 basis points from 4.13% and -2.52% respectively) would be applied. We agree with Pacific's surcharge/surcredit concept, but recognize that the surcharge/surcredit needs to be revised due to attrition revenue requirements adopted herein and the timing of the effective date of this resolution. The Bill-and-Keep surcharge/surcredit is consistent with D.85-03-042.

APPLICATIONS FOR REHEARING

Pacific filed an application for rehearing of D.86-12-099 on January 21, 1987. TURN filed its application to rehear the Decision on January 26, 1987. Pacific alleges (1) the adopted attrition methodology is imbalanced and retrogressive; (2) the decision contemplates an involuntary reduction to rates absent evidence that its current rates are unjust and unreasonable; and (3) the decision contemplates retroactive ratemaking. TURN requests, among other things, the Commission review the reasonableness of Pacific's authorized 15.0% return on equity in 1987. We have not yet acted upon these applications for rehearing of D.86-12-099.

FINDINGS OF FACT

1. It is appropriate to include the intrastate separation factor to the formula for attrition year average TPIS.

2. It is appropriate to include the FIT/CCFT effects on change in taxable income due to attrition year revenues and expenses.

3. Pacific's method of calculating the nonlabor escalation factor is not in compliance with D.85-01-042. Pacific is required to calculate the nonlabor escalation factor based on adopted methodology set forth in D.85-01-042.

4. The growth rate in salaries and wages should be limited to consideration of salaries and wages, consistent with Appendix B, page 2 of D.86-12-099, which states in part, "Growth of composite salaries and wages is based on labor contracts...." The inclusion of Social Security taxes in the growth factor is reasonable in this filing.

5. The team incentive plan and benefits plan, while not specifically mentioned in the attrition formula for Labor and Labor Overhead set forth on Page 2 of Appendix B of D.86-12-099, should be included in this filing because they are part of the labor contract.

6. The inclusion of team incentive plan and benefits plan in attrition should be reviewed in a future proceeding in which the attrition mechanism will be re-examined.

7. For attrition filings, the management salary alignment should reflect the same proportionate increase as union agreements for non-management, consistent with Appendix B, page 2, of D,86-12-099, which states, "Growth in composite salaries and wages is based on labor contracts...".

8. Pacific used year-end 1986 capital structure to calculate financial attrition as required by D.86-12-099.

9. The equity ratio of 56.02%, as filed by Pacific exceeds the 55% cap set in D.86-01-026 by 102 basis points and by 452 basis points over the 51.5%. authorized in D.86-01-026.

10. The use of recorded year-end 1986 capital structure eliminates the previously ordered imputed $82,000,000 of 6% preferred stock, adopted by D.86-01-026.

11. The 1987 attrition year rate of return on rate base of 12.16% is reasonable and is adopted herein. Using the 1987 attrition year rate of return yields a 1987 financial attrition revenue requirement reduction of $74,772,000. The capital structure adopted in D.86-01-026 where we found the 51.5% common equity component to be reasonable, is adopted herein.

12. The $5,900,000 revenue requirement effect of advice letters for new services from January 1986 through June 1986 is currently being considered in Phase II of A.85-01-034 and should not be included in this attrition filing.

13. The $3,900,000 revenue requirement effect of advice letters for new services for the period from July 1986 to December 1986 should be reflected in this attrition filing, since this amount is not being considered in Phase II of A.85-01-034.

14. Technical update of depreciation reflects the change in depreciation expense due to the change in depreciation rates applied to the same composition of plant categories as set forth in Resolution T-11098.

15. Pacific's calculation of the depreciation technical update adjustment should be revised according to PSD's recommendation. This results in a lesser revenue requirement increase of $9,931,000 than Pacific's $45,283,000.

16. Pacific's request to apply the billing surcharge/surcredit on bills rendered on and after the effective date of the filed tariffs is reasonable. The Bill-and-Keep provision is consistent with D.85-03-042. Pacific's concept of adjusting its current billing surcharge/surcredit is reasonable.

17. The 1987 attrition revenue requirement set forth in Appendix A of this resolution is reasonable and therefore adopted.

18. The Commission has not yet acted on Pacific's or TURN's application for rehearing of D.86-12-099.

19. Our treatment of financial attrition, technical update, and labor growth incorporates the concerns of PSD's protest and TURN'S protest. No further action is needed.

20. Our ordered rate reduction will affect all of Pacific's customers, including AT&T Communications. AT&T-C's revenue requirement will decrease because its access charges paid to Pacific will now be less.

21. In Decision No. 85-06-113, dated June 12, 1985, we ordered that ordering paragraph 3 of Decision No. 85-03-056 is modified to read in full as follows:

> "3. Any reduction in AT&T-C's expense stemming from reductions in local exchange utilities' access charges shall be concurrently passed on to AT&T-C's customers through a corresponding incremental reduction in the billing surcharge. The tariff filings by AT&T-C to comply with this order shall be filed so that they are effective within 14 days after local exchange utililties have made the advice letter filings required to reduce their local access charges."

IT IS ORDERED THAT:

(1) Within five days of the effective date of this resolution Pacific shall file a 1987 attrition year supplemental advice letter with revised tariff sheets incorporating the changes adopted in this resolution. The billing surcharge/surcredit shall be on a Bill-and-Keep basis and shall reflect interest accrued at the current three month commercial paper rate from January 1, 1987 to the effective date of the tariff.

(2) The billing surcharge/surcredit shall become effective May 1, 1987.

(3) AT&T Communications is ordered to file an advice letter within 30 days to flow through its share of Pacific's rate reduction to its customers pursuant to D.85-06-113. AT&T Communicatons may include in the advice letter filing any reservations it may have as to the disposition of its share of today's ordered rate reduction.

(4) This Resolution is effective today.

I certify that this Resolution was adopted by the Public Utilities Commission at its regular meeting on March 25, 1987. The following Commissioners approved it:

Victor Weisser

Executive Director

I will file a concurring opinion.

G. Mitchell Wilk, Commissioner

STANLEY W. HULETT
President
DONALD VIAL
FREDERICK R. DUDA
G. MITCHELL WILK
Commissioners

Commissioner John B. Ohanian, present but not participating.

1987 ATTRITION YEAR
GROSS REVENUE REQUIREMENT
($000)

	Pacific Bell 1987 Attrition *	Adopted 1987 Attrition
1. INTRASTATE REVENUES	$7,136,949	$7,136,949
2. LABOR AND LABOR OVERHEADS	2,430,426	2,427,165
3. MATERIALS RENTS & SERVICES	1,258,741	1,258,005
4. DEPRECIATION EXPENSE	1,112,241	1,112,241
5. FEDERAL AND STATE INCOME TAXES	844,591	840,349
6. AD VALOREM TAXES	151,116	151,116
7. OTHER TAXES	7,400	7,400
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8. BALANCE NET REVENUE	1,332,455	1,340,669
RATE BASE COMPONENTS		
9. TELEPHONE PLANT IN SERVICE	15,901,511	15,901,511
10. PROPERTY HELD FOR FUTURE USE	11,480	11,480
11. WORKING CASH	242,404	242,404
12. MATERIALS AND SUPPLIES	73,035	73,035
13. less: DEPRECIATION RESERVE	3,855,890	3,855,890
14. less: TAX RESERVE	2,344,729	2,344,729
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15. NET RATE BASE	10,027,810	10,027,810
REVENUE REQUIREMENT CALCULATION		
16. NET RATE BASE	10,027,810	10,027,810
17. times: RATE OF RETURN	0.1252	0.1252
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18. RETURN ON RATE BASE	1,255,482	1,255,482
19. less: BALANCE NET REVENUE	1,332,455	1,340,669
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20. NET REVENUE REQUIREMENT	(76,973)	(85,187)
21. times: NET TO GROSS MULTIPLIER	2.07125	2.07125
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22. GROSS REVENUE REQUIREMENT	(159,430)	(176,444)
ADJUSTMENTS		
23. Base Year Adjustment	24,984	24,984
24. Technical Update	45,283	9,391
25. CPE Phaseout	29,700	29,700
26. Advice Letters	(5,900)	(3,900)
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27. Adjustments Total	94,066	60,175
FINANCIAL ATTRITION		
28. Financial Attrition	(10,385)	(74,772)
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29. ADJUSTED GROSS REVENUE REQUIREMENT	($75,748)	($191,041)
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(Red Figure)

* As filed by Pacific Bell

Appendix B

GEORGE DEUKMEJIAN, Governor

STATE OF CALIFORNIA

PUBLIC UTILITIES COMMISSION
505 VAN NESS AVENUE
SAN FRANCISCO, CA 94102

February 6, 1987

The Honorable Victor Weisser
Executive Director
California Public Utilities Commission
505 Van Ness Ave.
San Francisco, CA 94102

Dear Mr. Weisser:

Re: Protest of the Public Staff Division to Pacific Bell Advice Letter No. 15215

Pursuant to General Order 96A (III H), the Commission's Public Staff Division hereby protests Pacific Bell (PacBell) Advice Letter No. 15215 filed on January 21, 1987. As explained more fully below, while the Advice Letter filing appears to be technically in compliance with Decision No. 86-12-099, the results appear to run counter to the Commission's stated intent to set rates that are just and reasonable consistent with improved economic conditions.

BACKGROUND

By Decision No. 86-01-026 issued January 10, 1986, in PacBell Application 85-01-034, the Commission approved a 15% return on common equity for Test Year 1986 and the succeeding two years (D. 86-01-026 mimeo page 22, Finding of Fact 3 page 205). This was based upon an adopted capital structure with a common equity component of 52.10% and a cap of 55% (mimeo page 14, Finding of Fact 2 page 205). The Commission continued to impute $82 million of 6% voting preferred stock to the adopted capital structure which had the effect of lowering the common equity component from 52.10% to 51.50% (mimeo page 15, Findings of Fact 1 and 2 page 205). The Commission also stated its intention to issue a separate decision on the policy issue surrounding attrition methodology and the inputs resulting from the 1986 adopted results of operations following the filing of a joint exhibit as a necessary predicate to the final determination of attrition methodology (D. 86-01-026 page 5).

On December 22, 1986, the Commission issued Decision 86-12-099 resolving certain outstanding questions regarding the attrition methodology adopted for PacBell and General Telephone Company of California (General). PacBell was ordered to make an Advice Letter filing so this Commission could review operational and financial attrition for 1987. Rates were ordered to be collected subject to refund after January 1, 1987 to account for any adjustments associated with the 1987 attrition year review.

The Commission also rejected the request of Toward Utility Rate Normalization (TURN) to review the adopted 15% return on common equity (D. 86-12-099, page 6). The Commission however, indicated it would review PacBell's capital structure in line with the 55% cap on common equity in order to avoid driving up the overall cost of service. The Commission also indicated its intention to review PacBell's debt costs in light of the expectation that a prudent utility would refinance older, high-cost debt during the current more favorable economic environment and lower interest rates. (D. 86-12-099, p. 6.) The Commission indicated that because of developments in the financial markets since the latter part of 1985 when evidence was taken on which PacBell's 1986 rate of return was adopted, financial attrition would be reviewed in order to assure that rates in attrition year 1987 are set at levels which are just and reasonable. (D. 86-12-099, p. 39 Finding of Fact 4.) The Commission further indicated that in times of the declining inflation experienced over the last year, it would be necessary to require the utility to file an attrition application in order to make appropriate adjustments to reflect current economic conditions and ensure that rates are just and reasonable. (D. 86-12-099, p. 39, Finding of Fact 6.) PacBell was directed to file its attrition advice letter using year-end 1986 capital structure and embedded debt costs because the data is available and easily verifiable. (Decision 86-12-099, page 7.)

On January 21, 1987, PacBell filed Advice Letter No. 15215 in compliance with Ordering Paragraph 1 of Decision No. 86-12-099. The utility also filed a Petition for Rehearing of that Decision on the same day.

ADVICE LETTER NO. 15215 SHOULD BE REJECTED

A preliminary review by the staff reveals that while technically the Advice Letter may conform to D.86-12-099 the results would not conform to the expressed intention of the Commission for the following reasons:

1. The year end 1986 equity component of the capital structure is 56.02% representing an increase of 452 basis points from the 51.5% component authorized by the Commission in Decision 86-01-026. It also exceeds by 1.02 basis points the 55% cap set by the Commission in Decision No. 86-01-026.

2. The Advice Letter filing does not include the imputed $82 million of preferred stock the Commission indicated it would continue to impute to the company. (D. 86-01-026, page 16.)

3. The significantly increased equity component of the capital structure serves to increase ratepayer costs in the face of a substantial decline in inflation and thus does not allow the ratepayer to benefit from improved economic conditions.

4. PacBell's workpapers supporting its advice letter indicated that the increase in equity ratio using year-end 1986 capital structure in conjunction with the decrease in recorded embedded debt and preferred costs results in a decrease in financial attrition of $10.385 million. Staff's review indicates that the actual impact of PacBell's financial attrition filing is an increase in revenue requirements in 1987 when the income tax effects of the higher equity ratio are considered. Thus, PacBell's compliance with D. 86-12-099 results in an increased revenue requirement when the Commission stated its concern about driving up the overall cost of capital.

The staff respectfully submits that Advice Letter No. 15215 should be rejected because it is inconsistent with the capital structure and the ratemaking philosophy upon which the 15% return on equity was adopted in Decision 86-01-026. The 15% equity return was predicated on the capital structure comprised of 51.5%

common equity and included an adjustment for $82 million of 6% preferred stock.

PacBell's 1987 financial attrition should reflect the reduced embedded debt and preferred stock costs as ordered in D. 86-12-099. The capital structure to be utilized however, should be the original capital structure determined reasonable in D. 86-01-026 which includes the 6% preferred stock adjustment and formed the basis for the currently authorized 15% return on common equity.

Respectfully Submitted,

Rufus G. Thayer

RUFUS G. THAYER
Staff Counsel

cc: All Respondent Telephone Utilities - I. 85-03-078
All Parties - A. 85-01-034
W. M. McCraney

Appendix C

GEORGE DEUKMEJIAN, Governor

STATE OF CALIFORNIA

PUBLIC UTILITIES COMMISSION

505 VAN NESS AVENUE
SAN FRANCISCO, CA 94102

February 17, 1987

The Honorable Victor Weisser
Executive Director
California Public Utilities
Commission
505 Van Ness Avenue
San Francisco, CA 94102

Dear Mr. Weisser:

Re: Protest of the Public Staff Division
to Pacific Bell Advice Letter No. 15215

Further to the Public Staff Division (Staff) letter of protest dated February 6, 1987, the Staff has discovered another deficiency in the Pacific Bell (PacBell) Advice Letter as explained below.

Further review by the Staff has uncovered an error in the derivation of the depreciation expense revenue requirement impact predicted on the technical update of depreciation rates. It appears that PacBell has developed a net depreciation revenue requirement impact of $53,443,000 based on mismatched use of composite accrual rates. The mismatch arises by PacBell's use of the technically updated composit rate of 6.51% (Res. #T-11098) derived from 1987 projected plant and the adopted test year 1986 composite accrual rate of 6.12% derived from 1986 plant. The 1986-87 accrual difference was represented by PacBell as the net depreciation effect of $53,443,000.

To understand the Staff perspective it is necessary to reaffirm that the basic Commission adopted depreciation parameters are the remaining life and salvage for a particular category of plant. From this is developed the depreciation rate for that category of plant which remains fixed until revised by the Commission. Composite depreciation rates on the other hand reflect the mix in the various plant categories at any point in time and obviously varies continuously. To properly compute the composite rate, for attrition purposes, it is necessary to recompute the 1986 composite depreciation rate, reflecting the 1985/86 Commission adopted parameters and rates, but applied to the 1987 plant mix.

Correctly recomputed the composite 1986 rate would be 6.43%. PacBell instead chose to utilize the 1986 test year adopted composite depreciation rate of 6.12%. The Commission adopted technically updated depreciation composite rate of 6.51% was developed on the proper 1987 plant mix basis. The Staff estimates the depreciation effect utilizing the proper methodology would be $10,963,000, reducing the attrition revenue requirements by an additional $42,480,000.

The foregoing explanation is further grounds for rejecting PacBell Advice Letter No. 15215.

Very truly yours,

Rufus G. Thayer

Rufus G. Thayer
Staff Counsel

RGT:lz

cc: All Respondent Telephone Utilities - I.85-03-078
All Parties - A.85-01-034
J. M. McCraney

[illegible]

[illegible] New Montgomery Street
San Francisco, California [illegible]
[illegible]

PACIFIC BELL.
A Pacific Telesis Company

Appendices B & C Responses

February 17, 1987

Victor Weisser
Executive Director
California Public Utilities Commission
505 Van Ness Ave.
San Francisco, CA 94102

Re: Response of Pacific Bell (U 1001 C) to Protest of the Public Staff Division to Pacific Bell Advice Letter No. 15215

Dear Mr. Weisser:

Pacific Bell ("Pacific") hereby responds, pursuant to General Order 96A (III H), to the Public Staff Division's ("PSD's") Protest to Pacific's Advice Letter No. 15215. As shown below, Pacific has fulfilled its statutory obligation to comply with Ordering Paragraph No. 1 of Decision No. 86-12-099.

<u>The PSD's Protest Should be Denied since Advice Letter No. 15215 Admittedly Complies with Decision No. 86-12-099.</u>

The only valid basis for a PSD protest to the substance of a utility's compliance Advice Letter Filing is that it does not comply with the Commission's Ordering Paragraph directives. However, the PSD admits in several places in its Protest that Pacific's Advice Letter filing in fact <u>complies</u> with Ordering Paragraph No. 1 of Decision No. 86-12-099. On page 1 of its protest, the PSD states: "the Advice Letter filing appears to be technically in compliance with Decision No. 86-12-099." Additionally, on page 3 of its protest the PSD states: "technically the Advice Letter may conform to D.86-12-099." The PSD is correct; Pacific's Advice Letter complies with Decision No. 86-12-099. As a result, the Commission should <u>deny</u> the PSD's Protest on the ground that it fails to state a valid objection to Pacific's compliance filing.

The PSD's Protest makes the inappropriate argument that Pacific's Advice Letter filing should be rejected because it complies with the Commission's directive. The PSD apparently claims that Pacific should have purposely chosen not to comply with the express Order of Decision No. 86-12-099. For example, the PSD claims that Pacific should have utilized the original capital structure determined in Decision No. 86-01-026 (PSD Protest, p. 4), even though the PSD admits that Pacific was ordered to utilize its "year-end 1986 capital structure" (Id. at 2 (emphasis added)). The PSD's argument ignores Pacific's statutory obligation to comply with Commission Orders (see, Public Utilities Code Section 702). The PSD's argument also ignores the Commission's expressed desire to review year-end data "because (such data) is available and easily verifiable" (Decision No. 86-12-099, mimeo p. 7). The Commission's decision to use year-end 1986 data was a purposeful result of its efforts to ensure that the attrition procedure is "straightforward and heavily dependent on recorded verifiable data" (Id.).

The PSD's Protest also should be denied because it contains fallacious assumptions. Foremost among these is the PSD's speculative and unsupported claim that the Commission "expressly" intended and required Pacific's financial attrition to result in a negative revenue requirement adjustment (PSD Protest, p. 3). The PSD fails to cite to any language in Decision No. 86-12-099 which "expressly" states such a Commission directive. Indeed, Decision No. 86-12-099 makes no such finding or assumption.

An equally compelling reason to deny the PSD's Protest is that it contains factual mistakes. Paramount among these is the PSD's misstatement that Pacific's "15% equity return was predicated on the capital structure comprised of 51.5% common equity" (Id. at 3-4 (emphasis added)). In actuality, Pacific's authorized return on equity is not predicated on a capital structure; rather, it is influenced by many factors, including current and future economic conditions and investor perceptions of Pacific's unique business and financial risks (see, Decision No. 86-01-026, pp. 16-22).

The PSD is improperly attempting to rewrite Decision No. 86-12-099; accordingly, its Protest should be denied. Such a result is especially appropriate in light of the fact that the PSD admits that Pacific's Advice Letter complies with that Decision.

Respectfully Submitted,

Daniel J. McCarthy

DANIEL J. McCARTHY
Attorney for Pacific

cc: All Parties, Application 85-01-034

[illegible]

PACIFIC BELL.

A Pacific Telesis Company

Appendices B & C Responses

February 27, 1987

Victor Weisser
Executive Director
California Public Utilities Commission
505 Van Ness Ave.
San Francisco, CA 94102

Re: Response of Pacific Bell (U 1001 C) to February 17, 1987 Protest of the Public Staff Division to <u>Pacific Bell Advice Letter No. 15215</u>

Dear Mr. Weisser:

Pacific Bell ("Pacific") hereby responds, pursuant to General Orde 96A (III H), to the Public Staff Division's ("PSD's") February 17, 1987 Protest to Pacific's Advice Letter No. 15215. Pacific previously filed a response to the PSD's earlier protest.

<u>The PSD's Supplemental Protest To Pacific's 1987 Attrition Adjustment Advice Letter Is Unjustified And Should Be Denied.</u>

The PSD correctly notes that Pacific's appropriate 1987 attrition year composite depreciation rate is 6.51 percent. However, the PS incorrectly contends that the adopted 1986 composite depreciation rate (6.12 percent) should be recomputed to 6.43 percent, thereby driving a 1987 incremental difference of only .08 percent.

The Commission previously adopted a 1986 plant balance of $19.7 billion (including land and motor vehicles) (D. 86-03-049, mimeo p 196). The Commission also adopted Pacific's test year depreciatio expense as $1.3 billion (<u>Id.</u>). When amortizations for step, crossbar and inside wire (and land and motor vehicles, in the case of plant) are excluded, the values yield a composite rate of 6.12 percent, as correctly noted in the PSD's protest. If the PSD's contention is valid that Pacific's 1986 adopted accrual rate shoul somehow be transformed to 6.43 percent, then, simply put, Pacific Bell has been under-recovering a legitimate revenue requirement throughout 1986.

The PSD's logic infers that the growth of the composite rate is simply a function of anticipated changes in plant mix, including that for which the Commission authorized equal life group ("ELG") treatment, and that such events are outside of the bounds of a technical update. In such a case, however, they must be included as elements of operational attrition. It is untenable for the PSD to claim that Pacific's adopted composite depreciation rate has increased from 6.12 to 6.43 percent without allowing Pacific the attendant recovery.

Pacific has correctly calculated the 1987 growth in the composite depreciation rate from 6.12 to 6.51 percent by analyzing the following three factors: (1) changes in plant mix, (2) second year ELG and (3) rate changes on individual accounts. Each of these components are discussed below.

Plant Mix Changes: The Commission has consistently recognized a need to adjust rates between general rate cases to account for the impact of changes in plant mix on the overall composite (or weighted average) rates. As stated on page 48 of Decision No. 84-06-111: "The technical update is an essential part of the remaining life process in that it provides for automatic adjustment of depreciation rates to account for changes in the composition of utility plant and relative growth or decline in depreciation reserve" (emphasis added). Thus, this element of Pacific's calculation is clearly appropriate.

Second Year ELG: The Commission previously ordered ELG methodology for the Circuit-Other and COE-Electronic accounts because it "can result in a more precise matching of depreciation accruals and consumption of assets" (D. 85-08-047, mimeo p. 88). The initial year (1986) had a relatively small impact on the 1986 test year composite rate, because it included only a half year of 1986 additions. In 1987, all of the 1986 additions plus half of 1987 additions are depreciated using ELG rates. Second year ELG is the difference between the ELG rates and the vintage group rates that otherwise would have been applicable if not for Decision No. 85-08-047. In 1987, second year ELG results in $21.2 million of separated accruals that would not be recovered if the PSD's suggested composite rate change from 6.51 to 6.43 percent is adopted. Second year ELG was ordered as a legitimate expense and thus must be recognized for purposes of computing revenue.

Rate Changes on Individual Accounts: As affirmed in Resolution No. T-11098 (adopted January 28, 1987), Pacific Bell technically updated its depreciation rates. These rates have been booked since January 1, 1987. The PSD does not dispute these valid and proper changes.

A further point should be made; the PSD has incorrectly quantified the revenue requirement impact of its erroneous proposal. The PSD has considered only the effects of the depreciation expense differences from Pacific's proposal. The PSD has failed to include the impacts of the various other elements of the 1987 attrition year results of operations. For example, the PSD has not considered the depreciation reserve, deferred tax reserve or income tax impacts of its proposed change. As a result, the PSD's quantitatively and conceptually flawed proposal should not be adopted.

This response has shown the PSD's second protest to Pacific's Advice Letter No. 15215 to be meritless. Pacific has properly developed the impacts of technical update as reflected in Advice Letter No. 15215. The PSD's treatment of this matter is wrong. Whether the change in attrition year depreciation expense is characterized as a technical update or as operational attrition, the Commission undoubtedly intends the attrition process to capture the elements which the PSD has recognized in recomputing the 1986 composite depreciation rate to 6.43 percent. However, the Commission did not intend for the same process to refuse to recognize those same elements for revenue conveyances, as the PSD erroneously and unfairly contends.

Sincerely,

Daniel J. McCarthy
Attorney for Pacific

cc: All Parties, Application 85-01-034.

THE NEXT 5

DOCUMENTS

ARE POOR

ORIGINALS

MICROFILMING SERVICES
WILL NOT ASSUME
RESPONSIBILITY FOR THE
IMAGE QUALITY

TURN
Toward Utility Rate Normalization
693 Mission Street
San Francisco, CA 94105
(415) 543-1576
849 S. Broadway
Los Angeles, CA 90014
(213) 622-8876

Sylvia M. Siegel
Executive Director

Appendix D

February 4, 1987

Victor Weisser, Executive Director
California Public Utilities Commission
505 Van Ness Avenue
San Francisco, CA 94102

Re: Pacific Bell: Advice Letter No. 15215 (1987 Attrition)

Dear Mr. Weisser:

This letter constitutes TURN's formal protest to Pacific Bell Advice Letter No. 15215, which presents Pacific's 1987 Attrition proposal in compliance with D.86-12-099 in A.85-01-034. TURN is of course delighted with the existence of the filing, but has unresolved questions regarding its content.

After reviewing the workpapers supporting A.L. 15215, TURN finds certain elements of support to be insufficiently detailed or documented. Accordingly, TURN presented a detailed data request to the utility on January 27, 1987, asking for information to be supplied by February 6, 1987.

By this protest, TURN asks that no final action be taken on A.L. 15215 until after TURN has received adequate data. TURN will inform this record promptly when the data has been reviewed, either to withdraw this protest or to request action by this Commission to resolve any disputed points.

Copies of this protest are being served on all parties to A.85-01-034, including Pacific Bell.

Sincerely,

Jon Frederick Elliott

Jon F. Elliott
Staff Counsel

cc: A.L.J. Carew
Service list, A.85-01-034

JFE:gs

TURN
Toward Utility Rate Normalization
693 Mission Street
San Francisco, CA 94105
(415) 543-1576
849 S. Broadway
Los Angeles, CA 90014
(213) 622-8878

Sylvia M. Siegel
Executive Director

Appendix E

February 27, 1987

Victor Weisser, Executive Director
California Public Utilities Commission
505 Van Ness Avenue
San Francisco, CA 94102

Re: PacBell A.L. No. 15215 (1987 Attrition)

Dear Mr. Weisser:

TURN hereby updates and affirms its protest to Pacific Bell's Advice Letter No. 15215, which presents Pacific's 1987 Attrition proposal in compliance with Commission D.86-12-099 (in A.85-01-034, et al). I initially wrote you on February 4, 1987 to present TURN's protest to A.L. 15215; at that time TURN's protest was more procedural than substantive, asking that no formal action be taken on the Advice Letter until TURN had the opportunity to acquire and review documentation underlying Pacific's submission.

Since February 4, TURN has requested and received from Pacific the documentation underlying the Advice Letter. TURN has also received from the Commission's Public Staff Division ("PSD") a protest letter (dated February 6) and supplemental protest (dated February 17), as well as Pacific's response thereto.

In view of this information TURN now affirms its protest of A.L. 15215, and asks that the Commission either set hearing on the matter, or direct Pacific to confer with PSD and TURN to attempt to reach a stipulation as to appropriate 1987 attrition adjustments.

First, TURN concurs with PSD's identifications of problems with Pacific's filing, expressed in PSD's two letters of protest. However, while PSD politely professes these problems with the statement that "technically the Advice Letter may conform to D.86-12-099," TURN takes a stronger view. The utility appears to have adopted strained (eg., the common equity component) or deliberately noncomplying (eg., the erasure of the $82 million imputed stock element) interpretations of orders in A.85-01-034 so as to minimize the potential attrition adjustment. In this regard, TURN finds Pacific's sanctimonious reply to PSD's protest to be particularly objectionable.

Additionally, TURN has additional concerns regarding the Advice Letter. For example, Pacific uses an estimate of 1987 inflation in the "TPI" index that was formulated in 1985; an updated estimate is now becoming available, which should be substituted (see D.86-04-021, in A.83-07-02, updating General's TPI calculation). Second, TURN also has questions regarding what appear to be discretionary and exhorbitant increases in certain labor expenses for management employees, which should be explored further before Pacific's proposed adjustments are conceded to be appropriate. Third, Pacific's refinancing of earlier high-cost debt issues, which does not at first glance appear to be unreasonable, should be reviewed in more detail.

Accordingly, TURN asks that this Commission not order the $75.75 million adjustment at this time (see Item C-3, Commission agenda of March 6, 1987) but instead either direct further ex parte negotiations among the three parties, or order hearings.

Sincerely,

Jon F. Elliott

Jon F. Elliott
Staff Counsel

cc: Commissioners
Appearances, A.85-01-034

[illegible]
Senior Counsel
Legal Department

[illegible] New Montgomery Street
San Francisco, California [illegible]
[illegible]

PACIFIC BELL.
A Pacific Telesis Company

Appendices D & E Response

March 9, 1987

Victor Weisser
Executive Director
California Public Utilities Commission
505 Van Ness Ave.
San Francisco, CA 94102

Re: Response of Pacific Bell (U 1001 C) to Toward Utility Rate Normalization's February 27, 1987 Affirmation of <u>Its Protest to Pacific Bell's Advice Letter No. 15215</u>

Dear Mr. Weisser:

Pacific Bell ("Pacific") hereby responds, pursuant to General Order 96A (III H), to Toward Utility Rate Normalization's ("TURN's") "updated" protest to Pacific Bell's ("Pacific's") Advice Letter No. 15215. As shown below, TURN's affirmance of its earlier procedural protest is unwarranted, and should be dismissed.

TURN states that it "concurs" with the two PSD protests already filed. Pacific's responses to those two earlier PSD protests equally apply to TURN's concurrence.

TURN has concerns regarding Pacific's use of the only available, and most current Telephone Plant Index ("TPI") data. However, Pacific had no other choice at the time it was ordered to file the advice letter but to rely on the most recent and available TPI data. TURN's concerns should be dismissed.

TURN has questions about the management employee wage escalation factor. It claims Pacific's projected 1987 management salary increase of 3.7% <u>over Commission-adopted 1986 salary levels</u> "appear[s] to be discretionary and exhorbitant [sic]". In its data response to TURN, Pacific included two articles from leading business newspapers stating that an independent research firm (Conference Board) had estimated that, nationwide, wage increases for management employees would increase by only 5.5% in 1987, down from 6.0% in 1986. The 5.5% figure represented "the smallest raises in 13 years" (<u>Wall Street Journal</u>, January 19, 1987, p. 12). TURN's labelling as exorbitant Pacific's significantly lower than average 1987 management wage increase is clearly not accurate.

TURN also raises the issue of Pacific's refinancing of its debt. However, TURN does not detail its concerns. Indeed, its response that Pacific's refinancing "does not at first glance appear to be unreasonable" is all but an admission that Pacific's refinancing efforts were prudent. This basis of TURN's protest is without merit.

Pacific remains willing to meet with the PSD and TURN to facilitate an understanding of the basis for Pacific's attrition filing.

Sincerely,

David J. McCarthy

D. J. McCarthy
Attorney for Pacific

cc: All parties, Pacific Bell Application 85-01-034

PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

RESOLUTION NO. T-11098

EVALUATION AND COMPLIANCE DIVISION

DATE: JANUARY 28, 1987

Copy for:
Orig. and Copy
________to Executive Director

RESOLUTION

________Director
________Numerical File
________Alphabetical File
________Accounting Officer

SUBJECT: Pacific Bell. Order Authorizing Technical Update in the 1987 Depreciation Rates for all Telephone Plant. Resolution No. T-11098.

WHEREAS: PACIFIC BELL, by letter dated October 16, 1986, requests authority under Section 795 of the Public Utilities Code to make a technical update of depreciation rates of estimated 1987 telephone plant.

Pacific Bell filed a similar request on July 3, 1986, with the Federal Communications Commission and has obtained FCC staff approval.

Public Staff Division has reviewed Pacific's proposed depreciation rates and recommends approval of proposed rates as shown in Table A.

The proposed technical update of straight-line remaining life depreciation rates for all telephone plant, and Circuit and Electronic categories of Central Office Equipment, which uses equal life group, results in an annual increase in depreciation accrual of approximately $14 million based on 1987 average plant of $21,048,157,000. Table A sets forth the proposed depreciation accruals.

The proposed depreciation rates reflect changes in the composition of the utility plant and relative growth or decline in depreciation reserves.

The revenue requirement impact of the proposed depreciation rates shown in Table A will be included in Pacific's 1987 attrition filing.

Pacific Bell's depreciation rates were last represcribed by D.85-08-047. The 1985 represcription included depreciation rate review of changes in service life, future net salvage and retirement pattern due to technological changes and growth of telephone plant.

TABLE -A-

CPUC TECHNICAL UPDATE 1986

COMPANY: PACIFIC BELL
STATE : CALIFORNIA

STATEMENT B

CHANGE IN ANNUAL DEPRECIATION ACCRUALS
RESULTING FROM CHANGES IN DEPRECIATION RATES
(000)

ANNUAL DEPRECIATION ACCRUALS FOR INVESTMENT AND SALVAGE RECOVERY

ACCOUNT NUMBER	CLASS OR SUBCLASS OF PLANT	** 1987 AVERAGE INVESTMENT	RATES IN EFFECT 1986	RATES EFFECTIVE 1987	CHANGE IN ANNUAL DEPRECIATION EXPENSE
		I	J=I*D	K=I*H	L=K-J
212	BUILDINGS	1738783	33037	36514	3477
221	CENTRAL OFC EQPT				
	*STEP BY STEP	153708	33000	33000	0
	*CROSSBAR	662865	175000	175000	0
	CIRCUIT-OTHER (VG)	2455782	235755	235755	0
	(ELG)	483996	84292	86151	1859
	DDS CIRCUIT	126741	12040	12421	381
	RADIO	86660	5980	6240	260
	ELECTRONIC (VG)	2819257	169155	166336	-2819
	(ELG)	640826	52526	51907	-619
231	STATION APPARATUS				
	TELETYPEWRITER	1275	147	437	290
	TELEPHONE & MISC.	6456	0	0	0
232	STATION CONNECTIONS *INSIDE WIRE	1565494	148422	148422	0
234	LARGE PBX				
	PBX-OTHER	180358	25611	38416	12805
	PBX-DDS	9752	926	1024	98
235	PUBLIC TEL EQPT.	146802	14731	13987	-744
241	POLE LINES	410887	22188	21777	-411
242.1	AERIAL CABLE				
	EXCHANGE	2114691	103620	105735	211[illegible]
	TOLL	15502	2186	2310	12[illegible]

TABLE -A-

CPUC TECHNICAL UPDATE 1986

COMPANY: PACIFIC BELL
STATE : CALIFORNIA

STATEMENT B

CHANGE IN ANNUAL DEPRECIATION ACCRUALS
RESULTING FROM CHANGES IN DEPRECIATION RATES
(000)

ANNUAL DEPRECIATION ACCRUALS FOR INVESTMENT AND SALVAGE RECOVERY

ACCOUNT NUMBER	CLASS OR SUBCLASS OF PLANT	** 1987 AVERAGE INVESTMENT	RATES IN EFFECT 1986	RATES EFFECTIVE 1987	CHANGE IN ANNUAL DEPRECIATION EXPENSE
		I	J=I*D	K=I*H	L=K-J
242.2	*UNDERGROUND CABLE				
	EXCHANGE	2296505*	89564	89564	0
	TOLL	120284	4571	4691	120
242.3	BURIED CABLE				
	EXCHANGE	1222096	54994	54994	0
	TOLL	103630	4871	4974	103
242.4	SUBMARINE CABLE	11673	782	794	12
243	AERIAL WIRE				
	EXCHANGE	24214	1453	1429	-24
	TOLL	1902	645	719	74
244	U.G. CONDUIT	1707137	37557	37557	0
261	FURN. & OFC. EQPT.				
	FURNITURE	262050	11792	12578	786
	COMPUTER & AMA	1000043	173007	167007	-6000
262	OTHER COMM EQPT.	329901	36949	39918	2969
264	VEH & OTH. WK. EQPT.	346887	24629	23935	-694
	TOTAL	21048157	1559430	1573592	14162

*AMORTIZATION
**ESTIMATED ACTUAL 1987 AVERAGE PLANT
ACCOUNT 261 REFLECTED MIDNIGHT DIRECTORY TRANSFER
@NOT PRESENTLY BOOKING ACCRUALS; RESERVE GREATER THAN 100%-FNS%

	1986	1987
TOTAL COMPOSITE RATE:	7.41	7.48
COMPOSITE RATE, 608 ONLY:	7.41	7.49

In accordance with the procedures for depreciation reviews adopted by the Commission on September 13, 1977, Public Staff Division gave notice of the proposed depreciation rates to all interested parties by letter dated December 3, 1986. By January 2, 1987, the end of the 30-day response period, staff had received no protests.

The Commission finds that the depreciation rates, set forth in this Resolution are appropriate. This finding is not a finding of reasonableness for ratemaking purposes. Therefore, good cause appearing,

IT IS ORDERED that authority is granted to make the depreciation revisions reflected in Table A of this Resolution, effective for calendar year 1987 and subsequent years until the Utility files a new depreciation study with the Commission.

The effective date of this Resolution is today.

I hereby certify that the foregoing Resolution was duly introduced, passed and adopted at a regular meeting of the Public Utilities Commission of the State of California, held on January 28, 1987, the following Commissioners voting favorably thereon:

Executive Director

Resolution T-12007

G. MITCHELL WILK, Commissioner, Concurring Opinion:

I will support the majority decision today, however, I will do so somewhat reluctantly.

On the one hand, ratepayers deserve the benefits of lowered inflation and debt costs, yet I am concerned that the attrition process as applied to the telecommunications industry may need careful reexamination in light of the transitional pressures confronting this industry.

I am unconvinced that some of the formulas contained in our 1985 "Cookbook" decision are dynamic enough to properly reflect the changes occurring in telecommunications, and equally, there is a need for regulators to establish consistent, dependable, and longer range operating parameters upon which the utilities, ratepayers, and investors can rely with certainty.

We need to take another look at the "recipes" in our "cookbook", and the sooner the better. I ask the staff to expeditiously set up a workshop to revisit attrition in the telecommunications industry, and to advise us on options and additional proceedings to consider and implement any needed changes.

/s/ G. Mitchell Wilk
G. MITCHELL WILK, Commissioner

March 25, 1987
San Francisco, California