

PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Telecommunications Division

RESOLUTION T-15978*
December 20, 1996

R E S O L U T I O N

RESOLUTION T-15978. Citizens Telecommunications Company of California, Inc. (U-1024-C). ORDER APPLYING THE ADOPTED PRICE CAP MECHANISM IN COMPLIANCE WITH DECISIONS 95-11-024, 94-09-065, 94-06-011, and 89-10-031 THROUGH ADJUSTMENTS TO SURCHARGES/SURCREDITS TO BE EFFECTIVE JANUARY 1, 1997.

BY ADVICE LETTER NO. 596, FILED September 30, 1996, AS SUPPLEMENTED BY ADVICE LETTER NO. 596A, FILED OCTOBER 18, 1996, AND BY ADVICE LETTER NO. 596B, FILED DECEMBER 2, 1996.

SUMMARY

This Resolution orders Citizens Telecommunications Company of California, Inc. (CTC-California) to increase its annual revenue by \$2.483 million effective January 1, 1997, to implement its 1997 annual price cap index filing in Advice Letter (AL) Number (No.) 596, as supplemented. The adopted revenue requirement adjustments and surcharge changes are shown in Appendices A and B attached to this Resolution. The revisions to CTC-California's price floors to reflect the change in the inflation factor are adopted as filed and are effective January 1, 1997.

The January 1, 1997 revenue increase reflects a net Z-factor adjustment increase of \$2.483 million. In a separate decision issued today, the Commission approved CTC-California's Petition for Modification of D.95-11-024, which suspends the indexing mechanism portion of the price cap formula.

Protests to CTC-California's AL Nos. 596, as supplemented, were filed by AT&T Communications of California (AT&T) and by the California Public Utilities Commission's (Commission's) Office of Ratepayer Advocates (ORA) [1].

1 The Commission's Office of Ratepayer Advocates was formerly known as the Division of Ratepayer Advocates.

CTC-California filed AL No. 596 on September 30, 1996, requesting an increase in its 1997 revenue of \$1.820 million. On October 18, 1996, CTC-California filed AL No. 596A to reflect that the proposed Z-factor adjustment for the Interstate High Cost Fund should be lowered from \$2.072 million to \$1.925 million. In addition, on December 2, 1996 CTC-California filed AL No. 596B to reflect a revision of its 1997 revenue request due to the use of eight and not seven months of annualized data in estimating the revenue requirement. Moreover, AL No. 596B contains a rounding correction in the Gross Domestic Product Price Index (GDP-PI) inflation index used in the price cap filing. AL No. 596B also attributes the proposed Z-factor adjustment for the Interstate High Cost Fund to CTC-California's local billing base only and the proposed Z-factor adjustment for Customer Notification and Education Plan (CNEP) to each of the local, toll and access billing bases. Given the changes to the price cap filing as included in AL Nos. 596A and 596B, CTC-California revised its request to increase its 1997 revenue by \$1.658 million to be effective January 1, 1997. CTC-California's revised request translates into a \$2.483 million request without the Price Cap Index.

The adopted revenue changes are summarized in the following table:

<u>1997 Price Cap Revenue Change (in \$000s)</u>	
Price Cap Impact (1.7%) without Z-Factors	\$ 0
Z-factors: ongoing revenue impact	
PBOPs Adjustment	371
Interstate High Cost Fund	1,925
Sub-Total	<u>2,296</u>
Z-factors: one-time revenue impact	
CNEP Costs to Implement CPN	187
Sub-Total	<u>187</u>
Net Z-factor adjustment	2,483
Total Price Cap Impact with Z-factors Effective January 1, 1997	\$2,483

BACKGROUND

In our Decision (D.) 95-11-024, we adopted an incentive-based regulatory framework for CTC-California similar to that which we adopted for GTEC California Incorporated (GTEC) and Pacific Bell (Pacific). In Ordering Paragraph (O.P.) 6 of that decision, we ordered that:

"The regulation of [CTC-California's] [2] operations shall follow the principles of the new regulatory framework (NRF) established in D.89-10-031 (33 CPUC2d), D.94-06-011, and D.94-09-065 subject to the following differences. Earnings between the benchmark and ceiling rates of return shall be shared equally between shareholders and ratepayers, with earnings above the ceiling rate of return returned to ratepayers. The "x" factor in the NRF formula for [CTC-California] shall be 4.00%."

In D.89-10-031, we adopted an incentive-based regulatory framework for Pacific and GTEC. In that decision, we stated:

This new regulatory framework is centered around a price cap indexing mechanism with sharing of excess earning above a benchmark rate of return level...

Following a startup revenue adjustment [D.89-12-048] . . . prices for the utilities' basic monopoly services and rate caps for flexibly priced services will be indexed annually according to the Gross National Product Price Index (GNP-PI) inflation index reduced by a productivity adjustment of 4.5%.

The indexing formula also allows for rate adjustments for a limited category of exogenous factors whose effects will not be reflected in the economy wide GNP-PI [since replaced by the GDP-PI]. While all such costs cannot be foreseen completely, we recognize that the following factors may be reflected in rates as exogenous factors (called Z-factors): changes in federal and state tax laws to the extent that they affect the local exchange carriers disproportionately, mandated jurisdictional separations changes, and changes to intralATA toll pooling arrangements or accounting procedures adopted by this Commission.

However, the we did not authorize Z-factor treatment for all unforeseen or exogenous factors. In D.89-10-031 the Commission also stated that:

normal costs of doing business (including costs of complying with existing regulatory requirements) or general economic conditions would be excluded as Z-factor items.

In D.93-09-038, we ordered GTEC to replace the GNP-PI with the Gross Domestic Product Price Index (GDP-PI) commencing with GTEC's 1994 price cap filing. In D.94-06-011, the Commission likewise ordered Pacific to replace the GNP-PI with the GDP-PI commencing with Pacific's 1995 price cap filing.

2 CTC-California was previously named Citizens Utilities Company of California and so referred to in D.95-11-024.

In D.94-09-065, we authorized Pacific and GTEC to implement the 1995 price cap rate adjustments through the billing surcharge/surcredit mechanism.

CTC-California's filing consists of proposed revenue adjustments (reductions in parentheses) for:

1. Price Cap Index, (\$.825) million - A 1997 Price Cap Index factor of -1.7%. This amount is calculated by using a GDP-PI amount of 2.3% with a productivity factor of 4.0%.
2. Customer Notification and Education Plan, \$.187 million - A Z-factor adjustment to reflect one-time costs associated with providing Customer Notification and Education on the passing of the Calling Party's Number.
3. Interstate High Cost Fund Adjustment, \$1.925 million - A Z-factor adjustment to reflect reduced recovery from Interstate High Cost Fund.
4. Post Retirement Benefits Other Than Pensions, \$.371 million - An on-going, Z-factor adjustment to reflect a reduction of payments in connection with Statement of Financial Accounting Standards No. 106 (SFAS 106), Employers Accounting for Post Retirement Benefits Other than Pensions (PBOPs).

The Price Cap Index factor is based on a change in GDP-PI of 2.3% for the second quarter of 1996 over the second quarter of 1995, which, together with the 4.0% productivity gain factor, results in a net Price Cap Index of -1.7%. Applied to a billing base of \$48.517 million this factor would have resulted in a revenue decrease of (\$.825) million. However, as approved in a separate Commission decision issued today, CTC-California's Petition to Modify D.95-11-024 (dated November 8, 1996) results in no revenue change for this factor since the price cap index is suspended.

PROTESTS

Protests were filed to CTC-California's 1997 Price Cap filing by AT&T on October 22, 1996 and by ORA on October 24, 1996.

CTC-California responded to both the AT&T and ORA protests on October 30, 1996.

No protests were received with respect to CTC-California's revenue adjustments for the Price Cap Index.

ORA protests CTC-California's adjustment for PBOPs. AT&T protests CTC-California's adjustments for CNEP Costs and for its application of the Interstate High Cost Fund Reduction. In addition, AT&T protests the GDP-PI inflation factor used by CTC-California in its filing. We will discuss both the AT&T and the

ORA protests in further detail below and adopt a final revenue adjustment for CTC-California.

DISCUSSION

I. Customer Notification and Education Program (CNEP)

CTC-California requests a one-time, Z-factor adjustment of \$.187 million to recover the costs of providing CNEP in relation to the passing of Calling Party Number (CPN).

In May 1995, the Federal Communications Commission (FCC) ordered local exchange carriers to transport the CPN to interconnecting carriers. The result of passing on the CPN is for possible disclosure on a calling party identification (Caller ID) display. In D.92-06-065 and D.92-11-062, we adopted certain conditions that applicant utilities³ needed to meet prior to making Custom Local Access Signaling Services (CLASS), including Caller ID, features available to customers. The development, approval and implementation of a CNEP was amongst these conditions. On April 10, 1996, we issued D.96-04-043 in which we authorized CTC-California to implement its CNEP, Caller ID and related blocking services.

While no party disputes the CNEP amount requested by CTC-California in its 1997 Price Cap filing, AT&T protests the application of the CNEP amount to both toll and local exchange customers. AT&T argues that CNEP is an expense that is directly attributable to local exchange customers and is scaled by the number of such customers. AT&T further states that since intraLATA toll customers are also basic exchange service customers, such application inappropriately burdens intraLATA toll customers with more than their fair share for these costs as compared to basic exchange customers. AT&T requests that the CNEP expenses be reallocated to local exchange revenues only.

CTC-California takes issue with AT&T's protest contending that it has not misapplied CNEP costs. CTC-California's response to AT&T's protest notes that Caller ID service is provided for all services and not just local exchange services. CTC-California states that it is consistent with both Commission and FCC rules to spread the cost of Caller ID across toll, access and exchange services. CTC-California cites D.92-06-065, in which the Commission defined Caller ID as a Category II discretionary service, as evidence that Caller ID and related CNEP are not considered basic service items and, thus, should not be attributed to local exchange revenues alone. Furthermore, CTC-California cites Resolution T-15820 (dated December 20, 1995) in which the Commission approved Pacific's 1996 Price Cap filing, including CNEP expenses, as applied to the total billing base

3 The applicant utilities addressed in D.92-06-065 and D.92-11-062 were Pacific Bell, Contel of California, Inc., and GTE California Incorporated.

for intraLATA exchange and private line services, intraLATA toll services, and intraLATA access services. On December 2, 1996, CTC-California submitted AL No. 596B in which it revised the application of the CNEP adjustment to all services, i.e. local exchange, toll and access.

We agree with CTC-California that Caller ID service and, therefore, related CNEP costs are attributable to all services and not just local exchange services. Therefore, similar to our order in Resolution T-15820, we conclude that the CNEP costs in CTC-California's 1997 Price Cap filing shall be applied to local exchange, toll and access services.

II. Interstate High Cost Fund

CTC-California included a \$2.072 million Z-factor adjustment in AL No. 596 to reflect reduced recovery from the Interstate High Cost Fund. In AL No. 596A, CTC-California revised the Z-factor amount requested to \$1.975 million. The Interstate High Cost Fund is administered by the National Exchange Carrier Association (NECA) and is geared at preserving universal service by offsetting the cost of the local loop in high cost areas.

While no party disputed the dollar amount of the Interstate High Cost Fund adjustment, AT&T protested CTC-California's application of the adjustment to both local exchange and toll services. AT&T contends that the Interstate High Cost Fund adjustment is specifically attributable to local exchange services and, thus, CTC-California should refile this Z-factor adjustment allocating its impact fully to local exchange services. In its October 30, 1996 response to AT&T's protest, CTC-California noted that it re-examined this issue and would file a supplemental advice letter applying the high cost fund adjustment to its local exchange services only. AL No. 596B contains the revision of that Z-factor adjustment.

We agree that the Interstate High Cost Fund adjustment should be applied to local exchange services only. Such application is consistent with our treatment of high cost fund adjustments in the previous years. For example, in Resolution T-15821 (dated December 20, 1995), we approved GTEC's Z-factor adjustment for an Interstate High Cost Fund reduction as applicable to its local exchange billing surcharge only.

III. Post Retirement Benefits Other than Pensions (PBOPs)

CTC-California submitted AL No. 596 with a \$.371 million Z-factor adjustment for PBOPs .

In its October 24, 1996 protest, ORA recommends that CTC-California's Z-factor adjustment for PBOPs be eliminated because of CTC-California's failure to comply with O.P. Nos. 1, 2, and footnote 30 of D.92-12-015. D.92-12-015, dated December 3, 1992, required utilities to utilize Statement of Financial Accounting for Standards No. 106 (SFAS 106), with certain modifications, to record and accrue their PBOPs liability. In

its protest, ORA asserts that CTC-California failed to do the following per D.92-12-015:

- a. establish independent PBOPs trusts for collectively bargained plans and for life insurance as required by O.P. No. 2.a;
- b. supply a complete copy of its actuarial valuation report. ORA alleges that this is technically in violation of footnote 30 and, as a result, interested parties to this filing cannot ascertain whether CTC-California is in compliance with O.P. No. 1 and 2.c.; and
- c. supply complete workpapers that indicate CTC-California is requesting \$24,290 in excess of its SFAS 106 costs, i.e. a violation of O.P. No. 1.

In response to ORA's protest, CTC-California argues that it has established independent PBOPs trusts that are maintained by sub-account and which comply with O.P. 2.a of D.92-12-015. CTC-California notes that it is providing ORA with a copy of the trust design and accounting procedures which elaborate on the nature of the sub-accounts and delineate the separate tracking of funding, payments, and income. A copy of the trust design and accounting procedures was provided to the Commission's Telecommunications Division.

To resolve the issue regarding the actuarial valuation report, CTC-California provided ORA with a supplemental schedule on October 29, 1996. CTC-California states that this schedule details SFAS 106 disclosure calculations and cost components at the employee group level. CTC-California contends that provision of this schedule makes all related PBOPs and SFAS 106 components explicitly determinable. A copy of the schedule was also provided to the Commission's Telecommunications Division.

In addition, CTC-California denies ORA's assertion that it is requesting amounts in excess of its SFAS 106 costs. CTC-California states that its proposed Z-factor adjustment does not include pay-as-you-go costs that are already in rates and that no compounding in the amount is being requested.

On December 2, 1996, CTC-California submitted AL No. 596B, which included the proposed text revision to CTC-California's PBOPs trust agreement, specifying the limitation on the use of PBOPs funds. This revision to the PBOPs trust agreement was suggested by ORA and is still awaiting finalization from CTC-California officials.

After reviewing AL Nos. 596, 596B and the other supporting documents provided by CTC-California, we conclude that the PBOPs adjustment included in CTC-California's 1997 Price Cap filing is in compliance with D.92-12-015. CTC-California's PBOPs adjustment shall be adopted, subject to submission of the final revised text of its PBOPs trust agreement in the supplemental compliance filing to AL No. 596 described in O.P. 2 of this Resolution.

IV. Inflation Factor

CTC-California submitted its 1997 Price Cap filing using a 2.32% GDP-PI inflation factor.

AT&T protests use of a 2.32% GDP-PI inflation factor because use of it does not comply D.89-12-048. In O.P. 7 of D.89-12-048, the Commission determined that the inflation component of the price cap indexing mechanism shall be the percentage change in the Gross National Product Price Index (GNP-PI) and rounded to one digit after the decimal. In D.94-06-011 and D.93-09-038, the Commission replaced the GNP-PI with the GDP-PI as the inflation factor in the price cap formula.

In its October 30, 1996 response to AT&T's protest, CTC-California agreed to round the GDP-PI inflation factor from 2.32% to 2.3% in accord with D.89-12-048 and include that adjustment in a supplemental advice letter filing and price floor calculations. AL No. 596B contains the rounding correction. We agree that a 2.3% GDP-PI inflation factor is appropriate for use in CTC-California's 1997 Price Cap filing.

V. Productivity Factor

CTC-California submitted its 1997 Price Cap filing using a 4.0% productivity factor. CTC-California cites O.P. 6 of D.95-11-024 which lists 4.0% as the productivity factor to be used by CTC-California for 1997.

On November 8, 1996, CTC-California filed a Petition for Modification of D.95-11-024 requesting that the Commission suspend the application of the GDP-PI minus the productivity factor formula (price cap index) used in price cap regulation in a similar manner as ordered for Pacific and GTEC in Second Triennial New Regulatory Framework (NRF) Review. In O.P. 4 of D.95-12-052, we suspended the application of the price cap index for Pacific and GTEC until further order of this Commission or until a final decision is issued in the next triennial review, anticipated to be undertaken in 1998. In its petition, CTC-California requests that we modify its price cap formula effective January 1, 1997.

No protests were filed regarding the productivity factor or the price cap index used by CTC-California in its 1997 Price Cap filing. ORA does not include a dollar amount for the price cap index in its protest to CTC-California's 1997 Price Cap filing. In a separate decision issued today, this Commission granted CTC-California's Petition for Modification of D.95-11-024 and, thus, suspended the application of the price cap index. Correspondingly, this Resolution adopts a \$0 amount for this factor.

VI. Price Floors

No protests or comments were received on CTC-California's revisions to its price floors. The revisions to the price

floors, as filed in AL 596, were reviewed and we find them to be reasonable.

FINDINGS

1. CTC-California's AL No. 596 filed September 30, 1996, and supplemented by AL No. 596A, filed October 18, 1996, and by AL No. 596B, filed December 2, 1996, proposes to increase its annual revenue by \$1.658 million effective January 1, 1997 to implement its 1997 annual price cap index filing.
2. CTC-California's proposed revenue adjustments reflect:
 - a. 1997 Price Cap Index of -1.7%, revenue decrease of (\$.825) million.
 - b. Z-factor revenue adjustments to reflect exogenous effects not reflected in the GDP-PI:
 - o PBOPs Adjustment, an on-going, revenue increase of \$.371 million
 - o Interstate High Cost Fund, an on-going, revenue increase of \$1.925 million
 - o CNEP Adjustment, an one-time, revenue increase of \$.187 million
3. A separate, Commission decision granting CTC-California's Petition to Modify D.95-11-024, dated November 8, 1996, to suspend the GDP-PI minus productivity factor portion of CTC-California's 1997 price cap index filing is issued today.
4. CTC-California's request for a PBOPs adjustment of \$.371 million attributable to local exchange, toll and access revenues is reasonable.
5. CTC-California's request for a revenue adjustment for the Interstate High Cost Fund attributed to local exchange revenues only is reasonable.
6. CTC-California's request for a revenue adjustment for CPN Customer Notification and Education Program costs attributable local exchange, toll, and access revenues is reasonable.
7. The use of a 2.3% GDP-PI Inflation factor in CTC-California's 1997 price cap filing is appropriate.
8. ORA's protest is denied except to the extent set forth herein.
9. AT&T's protest is denied except to the extent set forth herein.
10. A total price cap mechanism revenue increase of \$2.483 million effective January 1, 1997 is justified. The adopted

revenue adjustments are summarized in Appendix A to this Resolution.

11. CTC-California's requested price floor revisions are reasonable.

THEREFORE, IT IS ORDERED that:

1. Citizens Telecommunications Company of California Inc. shall increase its annual revenue by \$2.483 million effective January 1, 1997, as a result of its 1997 annual price cap index filing in Advice Letter (AL) Numbers 596, 596A, and 596B.

2. Citizens Telecommunications Company of California Inc. shall make a supplemental compliance filing to AL No. 596 on or before December 29, 1996 with the Commission's Telecommunications Division. The filing shall implement billing surcharges/surcredits reflecting the revenue increase in Ordering Paragraph 1, applied to a total billing base of \$48.517 million for intraLATA exchange and private line services, intraLATA toll services, and intraLATA access service as described in Findings of Fact 4, 5, and 6. This filing shall also contain the final text revision to the PBOPs trust agreement as included in AL No. 596B and specifying the limitation on the use of PBOPs funds. This filing will become effective on January 1, 1997, subject to review and approval by the Commission Telecommunications Division.

3. The supplemental compliance filing in Ordering Paragraph 2 of this Resolution shall take into consideration any change to the productivity factor ordered by a decision on CTC-California's Petition to Modify D.95-11-024, dated November 8, 1996

4. The revisions to the price floors filed by Citizens Telecommunications Company of California Inc. in AL No. 596, as supplemented, are adopted and shall be effective January 1, 1997.

This Resolution is effective today.

I hereby certify that this Resolution was adopted by the California Public Utilities Commission at its regular meeting on December 20, 1996. The following Commissioners approved it:


WESLEY M. FRANKLIN
Executive Director.....

P. GREGORY CONLON
President
DANIEL Wm. FESSLER
JESSIE J. KNIGHT, Jr.
HENRY M. DUQUE
JOSIAH L. NEEPER
Commissioners