COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

A REVIEW OF THE RATES AND CHARGES AND INCENTIVE REGULATION PLAN OF SOUTH CENTRAL BELL TELEPHONE COMPANY)	CASE NO. 90-256 PHASE I

O R D E R

On April 3, 1991, the Commission entered a final Order continuing incentive regulation in Phase I of this proceeding. The Independent Telephone Group ("ITG")[1] has requested the Commission clarify its Order with respect to the intraLATA settlement pool. The Attorney General ("AG"), by and through his Utility and Rate Intervention Division, has requested the Commission modify its Order to permit ratepayers of South Central Bell Telephone Company, Inc. ("SCB") to receive 100 percent of the reduction in the return on capital from the previously authorized return in Case No. 10105.[2] SCB responded to the AG's petition.

Following are the Commission's decisions on these matters:

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1 Ballard Rural Telephone Cooperative, Inc.; Brandenburg Telephone Company; Duo County Telephone Cooperative, Inc.; Foothills Rural Telephone Cooperative; Harold Telephone Company; Highland Telephone Cooperative, Inc.; Logan Telephone Cooperative, Inc.; Mountain Rural Telephone Cooperative; North Central Telephone Cooperative, Inc.; Peoples Rural Telephone Cooperative; South Central Rural Telephone Cooperative; Thacker-Grigsby Telephone Company; West Kentucky Rural Telephone Cooperative.

2 Case No. 10105, Investigation of the Kentucky Intrastate Rates of South Central Bell Telephone Company, Inc.

PETITION OF THE INDEPENDENT TELEPHONE GROUP

On April 17, 1991, the ITG filed a request for clarification of the Commission's Order of April 5, 1991, moving the Commission "to restrict comments and testimony on the intraLATA pooling process to address how rate changes for SCB could be accommodated in the current intraLATA pooling structure without negative effects on the other local exchange carriers." The ITG believes it is premature to consider structural changes to the intraLATA pooling process. The ITG requests that all LECs participating in the intraLATA pool be made parties to this proceeding, if the Commission plans to change the pool or the relationships of the LECs.

The Commission does not contemplate abandonment or overhaul of the current intraLATA pooling process in this investigation. However, the intraLATA pool operations may be affected. Specifically, the Commission will consider in this investigation whether intraLATA pool participants, other than SCB, should be insulated from or "made whole" relative to any toll rate reductions, or whether they should share in the revenue effect of any toll rate reductions.

PETITION OF THE AG

On April 23, 1991, the AG specifically requested rehearing to flow through, in full, the reduction in the cost of capital from that authorized in SCB's experimental incentive plan in Case No. 10105. The AG argued that this modification was necessary to avoid SCB being permitted to retain half of the reduction in capital costs over which SCB had no control.

SCB filed a response to the AG's petition on April 30, 1991. SCB argued that the new return would be incorporated in all future points of test. SCB further argued that the AG, by his petition, was requesting a return to traditional regulation without giving consideration to the fact that SCB's earnings had been reduced during the past 2 years under incentive regulation. SCB moved the Commission deny the AG's petition.

The Commission is not persuaded by the AG's argument. SCB agreed to extend incentive regulation; however, until the April 3, 1991 Order was issued, SCB's return was still that set in Case No. 10105.[3] Cost of capital is an allowable cost determined at a specific point in time and thus, only changes beyond April 3, 1991 should be made. Had the Commission chosen to make the full return adjustment proposed by the AG, it could only be applied to approximately 2 months, April and May, of the 12-month test period ended May 1991.

The AG's annualized figure is incorrect for two reasons. Should the Commission make a capital market test for the 12 months ended May, 1991, 50 percent of the AG's estimated $7.8 million would have already been reflected as reduction in the normal incentive process. Secondly, a capital market test, as specified in the Commission's Order, requires that SCB's earnings be modified to leave SCB in the same relative position as before. These two adjustments, combined with the actual capital cost

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3 Transcript of Evidence, Vol. I, February 12, 1991, Dixon, page 131.

changes, reduce the AG's annual estimate to approximately $1.7 million. With only 2 months of this annual figure at stake, the nonrecurring adjustment would have been only $280,000. Moreover, were this reduction made, it would simply reduce earnings in the next points of test, and the ratepayers would see no gain. For these reasons, the AG's petition for rehearing should be denied.

ORDERS

The Commission, having reviewed the evidence of record and being otherwise sufficiently advised, HEREBY ORDERS that:

1. ITG's request is granted to the extent of the clarification stated herein.

2. All LECs participating in the intraLATA toll settlement pool are hereby made parties to Phase II (rate design) of this proceeding and shall be added to the service list.

3. The AG's April 23, 1991 petition for rehearing be and it hereby is denied.

Done at Frankfort, Kentucky, this 13th day of May, 1991.

PUBLIC SERVICE COMMISSION

Chairman

Vice Chairman

Commissioner

ATTEST:

Executive Director