COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

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In the Matter of:

APPLICATION OF GENERAL TELEPHONE)
COMPANY OF KENTUCKY FOR AN ORDER)
IMPLEMENTING A DIRECT SALES) CASE NO. 8258
PROGRAM RELATING TO ITS SINGLE)
LINE TELEPHONE INSTRUMENTS)

O R D E R

On June 12, 1981, General Telephone Company of Kentucky ("General") filed its application for authority to implement a direct sales program of its single line telephone instruments. On March 1, 1982, the Commission issued an Interim Order accepting General's proposal to sell single line terminal equipment. General was given a period of 4 months from the date of the Interim Order to develop specific procedures for proper allocations between the regulated and nonregulated portions of its operations, subject to final review and modification by the Commission. On July 1, 1982, General filed cost allocation procedures using the guidelines specified in the Commission's Interim Order.

Following a review of General's proposed cost allocation procedures, the Commission, on September 30, 1982, sent a letter to General accepting the procedures with certain modifications. On November 24, 1982, General filed its response to the Commission's letter of September 30, 1982, submitted certain clarifications to the cost allocation procedures and further changed the method of calculating the capital carrying cost rate in accordance with its system-wide method.

The Commission concurs with General's responses and accepts the revisions made with the exception of the capital carrying cost rate on jointly used assets and the cash working capital carrying cost rate.

In its letter of September 30, 1982, the Commission stated that it was of the opinion that the capital carrying cost rate on jointly used assets should be determined using General's embedded cost of debt and the requested cost of equity proposed in General's most recent rate case. General, in its response, stated that under a shared asset concept, there was no need to establish a separate cost of capital for the nonregulated business, that the purpose of the capital carrying cost rate on jointly used assets is to fully compensate but not overcompensate the regulated business and further that it may not earn the requested return on equity from its regulated business.

The Commission agrees with General that the nonregulated portion of its business should fully compensate the regulated portion. However, the Commission disagrees that the use of the capital carrying cost rate on jointly used assets specified in the Commission's letter to General would overcompensate the regulated business. The nonregulated portion of General's business is not a ratepayer as General's formula assumes. Had the nonregulated business entered the marketplace on its own, it would have been subject to arms-length bargaining resulting in the rental or purchase of all necessary assets at whatever prices the market would demand. Since this scenerio did not occur, these prices are unknown. It is however highly unlikely that prices would be established that would result in the relatively low cost of capital which a utility incurs.

Moreover, the formula proposed by General creates an inverse relationship between the regulated and nonregulated businesses. When the regulated business is earning well, the nonregulated earnings will suffer and vice versa. The Commission is of the opinion that a formula susceptible to these fluctuations is unsound. Therefore, the Commission finds that the proper carrying cost rate of jointly used assets should be based on General's embedded cost of debt and the return on equity requested in General's most recent rate case.

Further the Commission is of the opinion that the cash working capital carrying cost rate should be set at the rate originally stated in the Commission's letter of September 30, 1982, or General's current annual weighted cost of short-term debt plus 2 percent.

IT IS THEREFORE ORDERED that the amended cost allocation procedures submitted November 24, 1982, be and they hereby are approved with the exception of the capital carrying cost rate on jointly used assets and the cash working capital carrying cost rate.

IT IS FURTHER ORDERED that the capital carrying cost rate on jointly used assets and the cash working capital carrying cost rate specified in the Commission's letter of September 30, 1982, be and they hereby are approved.

IT IS FURTHER ORDERED that portions of the Commission's Interim Order entered March 1, 1982, not specifically modified herein shall remain in full force and effect.

Done at Frankfort, Kentucky, this 17th day of January, 1983.

PUBLIC SERVICE COMMISSION

Chairman

Vice Chairman

Commissioner

ATTEST:

Secretary