

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

SEPARATION OF COSTS OF REGULATED)	ADMINISTRATIVE
TELEPHONE SERVICE FROM COSTS OF)	CASE NO. 362
NONREGULATED ACTIVITIES)	

O R D E R

On October 3, 1997, the Commission issued its final Order in this case establishing revised cost allocation procedures for the Independent Telephone Group¹ ("ITG"). On October 16, 1997, the ITG filed a motion for rehearing pursuant to KRS 278.400. The ITG requested that the Commission reconsider its decision to require allocation of Account 7510 - Interest on Funded Debt on a net plant basis. Prior to the October 3, 1997 revision of the ITG's cost allocation manual ("CAM"), interest on funded debt had been directly assigned in its entirety to regulated operations. On November 4, 1997, the Commission granted the motion for rehearing and scheduled an informal conference for November 20, 1997.

The Commission's Order stated that construction loans produce a benefit to both regulated and nonregulated activities and cited examples of telecommunications plant which could be used in providing nonregulated activities.² The ITG argued that the

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

² Order dated October 3, 1997, at 3-4.

examples cited by the Commission had not, in all cases, been financed or if they had, the financing had been retired.³

On November 20, 1997, an informal conference was held to discuss the issue.⁴ During the informal conference the ITG further explained why interest expense on its construction loans should not be allocated. The ITG referred to the Code of Federal Regulations, Section 1735.17, which states the restrictions the Rural Utility Service ("RUS") (formerly the Rural Electrification Agency) places upon borrowers regarding the use of loan proceeds. The ITG also stated that the financing of units of plant not specifically allowed through RUS loans was accomplished through the use of equity. Finally, the ITG summarized the procedures for applying for, receiving, and disbursing loan proceeds. This summary was intended to show that loan funds have not been commingled with company funds at any time. The ITG's presentation supported its position that RUS loans were not used to finance units of plant previously regulated but now deregulated. However, it is clear that some regulated plant constructed with RUS loans benefits nonregulated services, such as voice mail and Internet access, provided by the ITG companies. Nonetheless, the ITG stressed that these services compensate the regulated network via basic local service rates.

The Federal Communications Commission ("FCC") recognized the need to allocate a portion of telecommunications plant to nonregulated activities in its order in CC Docket

³ ITG's Motion at 2.

⁴ Informal Conference Memo dated November 24, 1997.

86-111.⁵ In that docket, the FCC required that telephone plant investment be allocated based on forward looking relative use measures. This allocation is codified in Part 64, paragraph 64.901(4) of the FCC's rules.

The Commission has endeavored to establish cost allocation procedures for small companies which do not place an unreasonable burden on their accounting systems and personnel. Requiring allocation of ITG plant based upon relative usage represents such a burden. Nonregulated usage of regulated plant at this time is de minimis, and collection of such data would not be productive.

Net plant value has no relationship to existing debt, and nonregulated activities have been financed with equity rather than construction loans. Consequently, using an allocator for funded debt based upon existing net plant values of regulated and nonregulated plant would not provide an accurate allocation methodology.

Therefore, the Commission will grant the ITG's motion and amend the ITG CAM to allocate Interest on Funded Debt-Account 7510 to regulated activities in its entirety. However, this decision should not be interpreted as a lessening of the Commission's concern about cross-subsidization nor of its vigilance in ensuring that captive ratepayers do not finance telephone companies' nonregulated ventures. At some future time it may be appropriate to require the ITG companies to incorporate some allocation methodology to recognize nonregulated use of regulated plant.

⁵ CC Docket 86-111, Separations of Costs of Regulated Service From Costs of Nonregulated Activities. Amendment of Part 31, The Uniform System of Accounts for Class A and Class B Telephone Companies to Provide for Nonregulated Activities and to Provide for Transactions Between Telephone Companies and Their Affiliates.

The Commission, having been otherwise sufficiently advised, HEREBY ORDERS that the ITG CAM issued by Order on October 3, 1997 shall be amended to reflect the allocation of Interest on Funded Debt-Account 7510 to regulated activities in total. Attached to this Order is a copy of the amended page.

Done at Frankfort, Kentucky, this 22nd day of January, 1998.

By the Commission

ATTEST:


Executive Director

COST ALLOCATION PROCEDURES - INDEPENDENT TELEPHONE GROUP
PSC CASE NO. 362

<u>ACCOUNT NUMBER</u>	<u>DESCRIPTION</u>	<u>REGULATED/NONREGULATED APPORTIONMENT BASIS</u>	<u>COMMENTS</u>
7370.000	SPECIAL CHARGES CONTRIBUTIONS	GENERAL ALLOCATOR	GENERAL ALLOCATION BASED ON DIRECTLY ASSIGNABLE EXPENSES
7510.000	INTEREST ON FUNDED DEBT	DIRECTLY ASSIGNABLE TO REGULATED	REA INTEREST ON FUNDED DEBT FOR REGULATED ACTIVITIES
7540.000	OTHER INTEREST DEDUCTIONS	DIRECTLY ASSIGNABLE TO REGULATED	INTEREST ON SECURITY DEPOSIT FOR REGULATED SERVICES
7620.000	EXTRAORDINARY INCOME CHARGES	DIRECTLY ASSIGNABLE TO REGULATED OR NONREGULATED	NATURE OF EXTRAORDINARY CHARGE WILL DETERMINE HOW IT IS ASSIGNED
7990.240- 7990.550	NONREGULATED EXPENSE ACCOUNTS	DIRECTLY ASSIGNABLE TO NONREGULATED	EXPENSES ASSOCIATED WITH NONREGULATED ACTIVITIES
9010.000	PLANT CLEARING-NONPRODUCTIVE	DIRECT (PLANT) LABOR HOURS	DIRECT RELATIONSHIP TO PERCENTAGE OF DIRECT LABOR HOURS INCURRED FOR MONTH
9020.000	CLEARING - PAYROLL BENEFITS	TOTAL LABOR DOLLARS	ALLOCATED BASED ON RELATIONSHIP TO PAYROLL DOLLARS DIRECTLY ASSIGNED TO REGULATED AND NONREGULATED