COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

THE ADOPTION OF A STANDARD METHODOLOGY FOR ESTABLISHING RATES FOR CONDUIT USAGE	)))	ADMINISTRATIVE CASE NO. 304

O R D E R

PROCEDURAL BACKGROUND

On January 30, 1984, the Kentucky Cable Television Association ("KCTA") filed a complaint with the Commission concerning South Central Bell Telephone Company's ("SCB's") pole and anchor attachment, and conduit occupancy rates.[1] In an Order dated July 26, 1985, the Commission ordered that the portion of KCTA's complaint dealing with conduit usage be addressed in Case No. 9272.[2] On December 4, 1985, an Order was issued by the Commission in Case No. 9272 denying SCB's request for an increase in its conduit usage rate. On December 26, 1985, KCTA filed a petition requesting that the Commission reconsider and modify its Order of December 4, 1985. However, that request was denied by Commission Order dated January 15, 1986.

1 Case No. 8973, Kentucky Cable Television Association, Inc., Complainant vs. South Central Bell Telephone Company, Inc., Defendant.

2 The Tariff Application of South Central Bell Telephone Company to Reflect Changes in Rates and Text for Conduit Occupancy Accommodations For InterLATA Carriers and CATV Firms.

Subsequently, as a result of a continuing review of complaints concerning conduit rates and the various alternatives presented by the participants in Case No. 9272, the Commission, on its own motion, issued an Order dated June 3, 1986, opening this administrative proceeding to consider whether a new methodology for conduit rates should be developed. In that Order, the Commission also requested that all utilities providing conduit, and all other parties desiring to be included, file conduit rate methodology and/or testimony no later than June 23, 1986.

On June 12, 1986, the Attorney General of the Commonwealth of Kentucky ("AG") filed a motion for full intervention. In an Order dated June 16, 1986, the AG was granted full intervention. On June 19, 1986, SCB filed a motion for an extension of time to file a response to the June 3, 1986, Order. On June 20, 1986, Storer Communications of Jefferson County, Inc., Storer Communications of Northern Kentucky, Inc., and Storer Communications of Bowling Green - Warren County, Inc., (collectively "Storer") filed a motion for full intervention and for an extension of time to submit comments on its conduit rate methodology, and General Telephone Company of the South ("GTS") filed testimony. On June 23, 1986, KCTA filed motions for full intervention and to incorporate by reference into the record in this proceeding the record in Case No. 9272. Louisville Gas and Electric Company ("LG&E") filed a motion for limited participation, and Cincinnati Bell Telephone Company ("CBT") requested an extension of time in filing its response to the Commission's Order. On this same date, Meade County Rural Electric Cooperative Corporation ("Meade

County"), Henderson Union Rural Electric Cooperative Corporation ("Henderson-Union") and Kentucky Utilities Company ("KU") filed requests to be deleted from the service list because they did not wish to participate. In an Order dated July 10, 1986, the Commission granted an extension of time to all parties of record in filing testimony to September 1, 1986, granted Storer and KCTA full intervention, denied KCTA's request to have the record in Case No. 9272 incorporated by reference into this proceeding, sustained LG&E's request for limited intervention, and sustained the requests of Meade County, Henderson-Union and KU to be deleted from the service list.

On July 30, 1986, the following distribution electric cooperatives: Big Sandy RECC, Blue Grass RECC, Clark RECC, Cumberland Valley RECC, Farmers RECC, Fleming-Mason RECC, Fox Creek RECC, Grayson RECC, Green River EC, Harrison RECC, Inter-County RECC, Jackson County RECC, Jackson Purchase RECC, Licking Valley RECC, Nolin RECC, Owen County RECC, Salt River RECC, Shelby RECC and Taylor County RECC, by counsel, filed a motion requesting they not be required to participate in this proceeding and that they be removed from the service list. On August 6, 1986, the Commission, by Order, sustained the cooperatives' motion to be deleted from the service list.

On September 2, 1986, in compliance with the Commission's Order dated July 10, 1986, CBT, SCB and Storer filed comments and/or testimony.

On September 17, 1986, the Commission issued an Order establishing procedural dates. In that Order the Commission allowed a discovery period for information requested and responses to be filed by the parties of record.

On October 20, 1986, KCTA notified the Commission by letter that it would withdraw as an active participant in this proceeding, but requested that it be allowed to remain on the official service list.

A hearing was held on December 9, 1986, in the offices of the Public Service Commission in Frankfort, Kentucky. At the hearing, certain requests for additional information were made. This information has been filed. Also, between January 28 through 30, 1987, briefs were filed by CBT, GTS, SCB and Storer as requested by the Commission in an Amended Order dated December 15, 1986.

On January 30, 1987, Storer Communications of Bowling Green - Warren County, Inc., and Storer Communications of Northern Kentucky, Inc., by counsel, filed with the Commission a motion for leave to withdraw as parties in this proceeding. In an Order dated February 11, 1987, the Commission sustained that motion.

DISCUSSION

In response to the Commission's Order dated June 3, 1986, CBT, GTS, SCB, Storer, and KCTA all filed proposed conduit rate methodologies. These methods ranged from a market based pricing approach to the current method adopted pursuant to Administrative Case No. 251 ("Adm. 251").[3]

3 The Adoption Of A Standard Methodology For Establishing Rates For CATV Pole Attachments.

CBT proposed to continue using the methodology set out in Adm. 251. Simply stated, CBT's recommended methodology is the current cost of adding a duct foot of conduit multiplied by an annual carrying charge factor and divided by a conduit occupancy ratio.

In his prefiled testimony, Robert C. Steele was asked why current costs were used in CBT's methodology. His response was that current costs were more relevant costs for setting rates, mainly because there is a limited number of ducts available in CBT's conduit system. As a result of this limited capacity, any use of duct space by any party advances the time for replacement of the conduit system. When the conduit system is exhausted, new ducts will be placed at the prevailing cost and current costs are a good estimate of that cost.[4]

During the hearing, Mr. Steele was asked why the use of a fill factor (defined in a later section of the Order) was appropriate in CBT's methodology. He responded by saying that the fill factor is appropriate whenever there is spare capacity, which is a benefit to all customers.[5]

GTS' current conduit rate was determined by using the methodology set out in Adm. 251, and includes concessions made in a settlement with KCTA. In response to the Commission's information Order dated October 14, 1986, GTS proposed a conduit

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4 Direct Testimony of Robert C. Steele on Behalf of Cincinnati Bell Telephone Company, dated September 2, 1986, page 3.

5 Transcript of Evidence ("T.E."), December 9, 1986, page 140, Question No. 1.

rate methodology that would apply a carrying charge factor to embedded investment in conduit. This methodology, similar to the Commission's methodology for determining pole attachment rates, would require the CATV firm to pay the annual embedded cost GTS incurs for maintaining the duct space occupied. During the hearing, Al Banzer indicated that GTS' willingness to use this method was based on his evaluation of the Adm. 251 Order dated September 17, 1982, and GTS' posture concerning treatment of CATV customers, along with its objectives to provide services to customers at fair, equitable, and competitive rates.[6]

SCB's present conduit rate is determined by the methodology set out in Adm. 251. The methodology it proposes in this proceeding is similar to that methodology in that it utilizes current replacement cost, a fill factor, and contribution toward common cost. The difference lies in the fact that SCB proposes that the Commission allow it to consider changing market conditions in determining conduit rates. In his testimony, John F. Dorsch defines a market price as the price that both a buyer and a seller are willing to accept, considering the availability of alternatives or opportunities to them to place their resources elsewhere.[7] If the Commission cannot agree with this proposal and

6 Ibid., page 122, Question 6.

7 Direct Testimony of John F. Dorsch on Behalf of South Central Bell Telephone Company, dated September 2, 1986, page 2.

wants a more formal approach such as the present methodology, then SCB proposes as an alternative that it be given the authority to adjust the contribution factor to vary depending upon changes in market conditions.[8]

Storer proposes a conduit rate methodology based on the net investment per duct foot multiplied by an annual carrying charge rate. Similar to the methodology proposed by GTS, Storer argues that basing conduit rate on embedded investment would generally be consistent with the Commission's rate-making principles, and thus would allow Storer to be treated like other customers of utility service. Storer further argues that a methodology based on embedded cost will allow a utility to recover its embedded investment, common cost, and a reasonable return. Moreover, information necessary for Storer's approach is publicly available data from the utilities' annual reports, and can be adjusted periodically to account for changes in investments and expenses.[9]

Investment In Conduit

In Adm. 251 the Commission ordered that current cost was the appropriate cost for conduit investment on the basis that once a section of conduit has reached maximum fill, it is not as easily "changed out" to a larger size as are poles. Furthermore, conduit is generally installed under city streets and sidewalks, and

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8 Brief of South Central Bell Telephone Company, dated January 30, 1987, page 17.

9 Brief of Storer Communications Of Jefferson County, Inc., dated January 30, 1987, pages 7-8.

replacements or additions thereto are quite troublesome and expensive.[10]

Like CBT, SCB contends that current replacement costs are the appropriate costs to use in pricing conduit. When questioned on the relevancy of current costs, Mr. Dorsch stated that conduit, like other outside plant facilities, is capacity limited and that replacement of this plant placed to provide facility capacity will be put in at labor and material costs that are in effect at the time of placement.[11] In contrast, Storer and GTS advocate an investment in conduit based on embedded cost.

The Commission has evaluated the various proposals and herein concurs with GTS and Storer that embedded costs are more appropriate than current costs in determining rates for conduit usage. The mere fact that a customer occupies a given facility does not justify that customer paying a rate based on the current replacement cost of that facility, especially when it is placed for the benefit of the utility and not the customer. Moreover, it appears that while SCB continues to increase the amount of conduit it has available, usage by conduit users is continually decreasing.[12] To charge CATV or other users a rate that reflects the additional plant placed at current cost for future or long run service needs of the utility is unreasonable.

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10 Adm. 251, Appendix, dated September 17, 1982, page 8.

11 T.E., page 158.

12 Ibid., pages 206-207.

In determining the embedded investment per duct foot, the Commission has chosen the gross book methodology instead of the net book method as proposed by Storer. Although both methodologies produce the same result, the gross book method is easier to calculate.

Fill Factor

In Adm. 251 the Commission allowed the use of a fill factor to compute conduit rates; however, the Order did not define fill factor. A fill factor is simply a measure of the amount of conduit occupied by all users of a utility's facilities. In this proceeding, CBT and SCB have recommended that we continue to allow an occupancy ratio while GTS and Storer recommend that we not.

SCB like CBT believes that a fill factor is appropriate because all occupants of conduit benefit from access facility capacity and therefore should contribute to the cost of maintaining those facilities.[13] In contrast, Storer contends that there is no justification for the use of a fill factor because utility conduit is not built for CATV use, nor can these customers occupy conduit space when the utility has forecasted the use of the space in the next 10 years. Moreover, CATV and other users are required to pay rearrangement costs in connection with the use of conduit.[14]

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13 Ibid., page 240.

14 Brief of Storer, pages 14-15.

The Commission concurs with GTS and Storer that occupancy ratios are not appropriate in determining conduit usage rates and, therefore, should not be included in conduit rate calculations.

Annual Carrying Charge

In Adm. 251 the Commission allowed an annual carrying charge designed to recover the utility's cost of providing service. Items included in this calculation are depreciation, maintenance, tax, administrative and overhead expenses, and a rate of return factor. In this proceeding, the only party who disagreed with the carrying cost was SCB.

SCB disagreed with the maintenance and depreciation components of the carrying charge presently in effect since a maintenance factor developed using embedded cost applied to an investment based on current cost appeared inappropriate.[15] The Commission concurs with SCB; however, the Commission as discussed previously did not agree with current cost investment. Therefore, the annual carrying charge components should continue to be developed based on embedded cost, but should be applied to embedded investment. Furthermore, the annual carrying charge should be based on readily available information, should be Kentucky specific where possible, should be adjusted in accordance with normal rate-making procedures, and should be calculated in an easily understood manner as set out in Attachment II.

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[15] T. E., pages 248-249.

Non-recurring Charges

SCB proposed that all non-recurring cost items such as make-ready work, rearrangement of facilities, and inspection and removal of facilities, be recovered through non-recurring rates equivalent to the direct cost associated with the function, plus a contribution factor to provide contribution toward common cost.[16] The Commission concurs with SCB that all utilities providing conduit accommodations to CATV and other users are entitled to recover these costs. The contribution factor charged by the utility should be equal to the rate of return on net rate base authorized by this Commission in the most recent general rate case.

FINDINGS AND ORDERS

The Commission, after consideration of the application and evidence of record and being advised, is of the opinion and FINDS that:

1. The methodology for determining conduit usage rates should be the Gross Investment per duct foot multiplied by an annual Carrying Charge Rate, or as set out in Attachment I.

2. The investment portion of the methodology should be based on gross embedded investment in conduit instead of net embedded investment and should be calculated in accordance with the formula set out in Attachment I.

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16 Testimony of John F. Dorsch, pages 7-8.

3. Fill factors or occupancy ratios are not appropriate in determining conduit usage rates and should not be included in conduit rate calculations.

4. The annual carrying charge should be based on Kentucky specific information, adjusted for normal rate-making procedures, and calculated as set out in Attachment II.

5. All non-recurring cost should be based on the direct cost associated with the function, plus contribution toward common cost equal to the utility's authorized return on investment authorized by the Commission in its most recent general rate case.

6. Each utility providing conduit accommodations should file revised tariffs for conduit charges conforming with the findings set forth in this Order and should be effective on or before July 1, 1987.

IT IS THEREFORE ORDERED that:

1. All utilities providing conduit accommodations shall comply with all matters set out in findings 1 through 6 as if the same were individually so Ordered.

Done at Frankfort, Kentucky, this 4th day of May, 1987.

PUBLIC SERVICE COMMISSION

Richard D. Heman, Jr.
Chairman

Vice Chairman

Commissioner

ATTEST:

Executive Director

ATTACHMENT I

Conduit Methodology

The rates for third party conduit usage shall be determined as follows:

$$\frac{\text{Gross Investment}}{\text{Per Duct Foot}} \quad \times \quad \frac{\text{Annual Carrying}}{\text{Charge Rate}}$$

Investment In Conduit

The Gross Investment in Conduit shall be determined as follows:

$$\text{Investment Cost Per Duct Foot} = \frac{\text{End of Period Gross Book In Conduit}}{\text{End of Period Duct Feet}}$$

ATTACHMENT II

Conduit Annual Carrying Charge

1. Depreciation

The authorized depreciation rate for conduit as set out in Kentucky Form M.

2. Taxes

The formula for calculating taxes is:

$$\frac{\text{Total Taxes}}{\text{Average Total Gross Plant}}$$

3. Administrative and Overhead

The formula for calculating administrative and overhead is:

$$\frac{\text{Total Commercial, General Office, and Other Operating Expenses*}}{\text{Average Total Gross Plant}}$$

4. Maintenance

The formula for calculating maintenance is:

$$\frac{\text{Total Conduit Repair Expense}}{\text{Average Total Conduit Gross Plant}}$$

5. Rate of Return

The formula for calculating the rate of return (adjusted to gross book) is:

$$\frac{\text{Average Net Book}}{\text{Average Gross Book}} \quad x \quad \begin{array}{l}\text{Authorized Rate of}\\ \text{Return on Investment**}\end{array}$$

* Excludes all expenses attributable to lobbying or charitable contributions.

** The rate of return should be the most recent rate of return authorized by the Commission.