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PUC BULLETIN

A Publication of the Public Utility Commission of Texas

Volume 14, No. 1 September 1988

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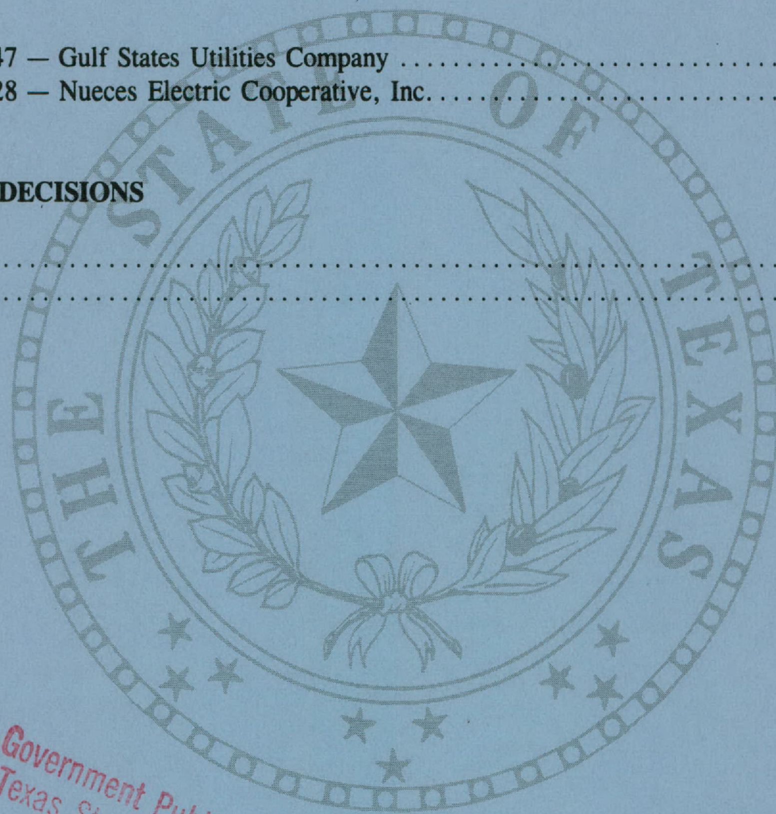

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APPLICATION OF SOUTHWESTERN BELL TELEPHONE COMPANY FOR A NEW TARIFF OFFERING DIAL 976 SERVICE	I I I	DOCKET NO. 6689

July 23, 1986

Southwestern Bell Telephone Company, Docket No. 6689, Examiner's Report adopted July 23, 1986. Application for authority to implement Dial 976 service in the Dallas, Fort Worth, Houston and San Antonio areas was granted.

[1] COMPLAINTS AND DISPUTES - TERMINATION OF SERVICE

Existing Commission rules prohibit disconnection of basic local exchange service for non-payment of billings for non-utility services provided by the utility.

[2] MISCELLANEOUS - TELEPHONE

The provision, by a telephone utility, of the medium (or facilities) for transporting Dial 976 messages is a utility service provided to the sponsor (Dial 976 service provider). However, the billing and collection services provided by the telephone utility for the sponsor are not utility services.

[3] MISCELLANEOUS - TELEPHONE

In making available Dial 976 service, a telephone utility is not providing a utility service to the local exchange customer. Therefore, in accordance with existing Commission rules, a customer's local exchange service should not be disconnected for non-payment of Dial 976 charges.

[4] RATEMAKING - COST OF SERVICE
RATEMAKING - RATE DESIGN - TELEPHONE

Where a utility is providing an optional, discretionary service, and the contributions or profits earned are to be utilized to offset the cost of local exchange rates, given the ultimate goal of universal service, the public interest is best served by maximizing the profitability of the service.

DOCKET NO. 6689

APPLICATION OF SOUTHWESTERN BELL TELEPHONE COMPANY FOR A NEW TARIFF OFFERING DIAL 976 SERVICE	§ § §	PUBLIC UTILITY COMMISSION OF TEXAS

EXAMINER'S REPORT

I. Procedural History

On January 6, 1986, Southwestern Bell Telephone Company (SWB or the telephone company) filed an application for a new tariff offering which introduces Information Delivery Service (Dial 976 service). This filing was initially assigned Tariff Filing No. T-9-6. On January 23, 1986, this filing was withdrawn as a tariff procedure and docketed. On January 24, 1986, the proposed effective date of February 10, 1986, was suspended for 150 days or until July 10, 1986, pursuant to Section 43(a) of the Public Utility Regulatory Act (PURA), Tex. Rev. Civ. Stat. Ann. art. 1446c (Vernon's Supp. 1986).

By order entered January 30, 1986, and pursuant to P.U.C. PROC. R. 21.25(a)(3), SWB was directed to publish notice of the proposed new tariff offering once a week for two consecutive weeks. Proof of publication of notice (printed in both English and Spanish) was filed on February 20, 1986. The January 30, 1986, order also established deadlines for discovery and prefiled testimony, and scheduled the hearing on the merits to commence on May 16, 1986.

On February 24, 1986, SWB filed a letter requesting a continuance of the hearing date until May 19, 1986. This request was granted by an order entered February 27, 1986.

On April 14, 1986, Phone Programs, Inc. (PPI) filed a motion to intervene in this docket.[1] PPI's unopposed motion was granted by an order entered April 28, 1986, however the ALJ informed the parties that the granting of this intervention did not affect the existing hearing and discovery schedule, nor the established deadlines for submitting prefiled testimony. No other motions to intervene were submitted in this docket. However, it is noted that two letters were filed by consumers and the American Coalition for Traditional Values (ACTV), expressing concern that approval of Dial 976 service might encourage the use of the telephone to provide pornographic or adult type messages.

The hearing on the merits was convened on May 19, 1986. Appearances were made by Ms. Barbara Hunt for SWB, Mr. Glenn Appleyard for PPI, and Mr. Jesus Sifuentes for the General Counsel's office representing the Commission staff and the public interest. Other than the parties of record, no

[1]Although PPI did not file its motion to intervene in this docket until April 14, 1986, it is noted that PPI, at its request, was placed on the service list herein on February 14, 1986, to allow PPI to monitor this case and determine whether or not to actively participate.

one appeared at the hearing for the purpose of making protest statements, expressing concerns regarding the application, or making statements in support of the application.

The hearing on the merits concluded on May 19, 1986. Posthearing briefs were due on June 5, 1986. Reply briefs were due on June 12, 1986. At the request of the General Counsel's office and by agreement of the parties the deadline for submitting reply briefs was extended until June 16, 1986. Thereafter, by a letter dated June 18, 1986, SWB voluntarily extended its effective date for 14 days to allow Commission consideration of this docket at the July 23, 1986, final order meeting.

II. Jurisdiction

The Commission has jurisdiction over the matter herein pursuant to Sections 16(a), 18(a) and (b), 37 and 38 of the Public Utility Regulatory Act (PURA or the Act), Tex. Rev. Civ. Stat. Ann. art. 1446c (Vernon Supp. 1986).

III. Opinion

A. Summary of Evidence

1. SWB

Information Delivery Service-Dial 976 (Dial 976 service) is described as "a service offering that utilizes the switched network to route and transport calls from the public entities that provide recorded announcements or interactive programs to the public for a charge. Such entities are Southwestern Bell's customers for the Dial 976 offering and are referred to as sponsors. Under this offering, a sponsor is assigned a telephone number of which the first three digits are "976." Individuals who call a sponsor's 976 number are considered clients of the sponsor and Southwestern Bell will bill, where possible, and collect on behalf of the sponsor, for each call from a client to the sponsor's 976 number." (SWB Ex. 1 at 3.) Initially, Dial 976 service will only be available in the Dallas, Fort Worth, Houston and San Antonio areas. The specific location of the central office(s) in each exchange which will be equipped to provide Dial 976 service will be determined by SWB. (Id., at 7.)

Dial 976 service calls will not be permitted from the following services: 4-party service; service with selective class of call screening; SWB's coin or coinless service; private coin service; or operator handled calls. (Id., at 8.)

Additionally, intraLATA[2] calls to Dial 976 numbers in SWB exchanges will, at this time, only be completed if such calls originate from SWB exchanges, as opposed to the exchanges of other independent telephone companies. (Id.)

Further, while long distance calls will be completed to the Dial 976 service, certain restrictions are posed by current technical limitations. For example, Mr. Springfield testified, on intraLATA calls to Dial 976 service SWB will bill the originating client the sponsor's charge for receipt of the message, plus the applicable intraLATA long distance charges. However, he testified, on interLATA calls to Dial 976 service, SWB cannot bill the sponsor's charge to the originating client's telephone account; and SWB will not bill the sponsor's charge to the interexchange carrier (IXC) absent the submission to SWB of a formal agreement between the sponsor and IXC regarding the handling of such charges. (Id., at 8-9.) SWB anticipates that potential sponsors will include: financial services and brokerage firms, book publishers, large and small newspapers, weather services, sports information services and other specialized information services. (Id., at 13.) SWB witness Springfield testified that as of February 26, 1986, the telephone company had been contacted by 199 potential sponsors regarding this service. (Id., at 12.)

Under SWB's proposal the Dial 976 sponsor will be responsible for: (1) furnishing the prerecorded announcement, recorder equipment, location for the recorder and the content of all program material; (2) all publicity or advertisements of Dial 976 service, which is to designate the 976 calling area and the per call rate; and (3) obtaining any licenses, written consent or permission, waivers or releases as required. (Id., at 12-13.) Additionally, before SWB provides Dial 976 service the sponsor must sign and return to the telephone company a Letter of Intent,[3] i.e., a detailed agreement setting forth the terms and conditions under which SWB will provide the Dial 976 service to the sponsor. (Id., at 13.)

The applicable client and sponsor charges associated with Dial 976 service were described as follows. The sponsor's clients (i.e., persons calling Dial 976 numbers) will be billed a flat rate per call for each Dial 976 call to the sponsors' announcements or interactive programs. Each sponsor will establish its own per call flat rate; thus the per call charge may vary from one sponsor to the next. The sponsors' clients will also be billed for any applicable tariff charges associated with the call such as intraLATA toll charges.

---

[2]LATA: Local Access and Transport Area. Used synonymously with "exchange" it describes the areas created as part of the AT&T divestiture. BOCs (Bell Operating Companies) may only provide certain services within LATAs or intraLATA. Telecommunication services between LATAs (or interLATA) is to be provided by the interexchange carriers (i.e., AT&T and its competitors).

[3]The Letter of Intent is sent to prospective sponsors as part of the Dial 976 service information package. A copy of the information package is set forth in SWB Ex. 1, (Springfield) Exhibit No. 3. The Letter of Intent is illustrated beginning at page 36 of this exhibit.

(Id., at 3.) However, under SWB's proposal the telephone company does not intend to disconnect a customer's service for non-payment of charges for calls placed to Dial 976 numbers. Explaining this Mr. Springfield testified that:

> Southwestern Bell believes that the provision for services by which calls may be placed to Dial 976 is a non-utility type service. Therefore, according to Section 23.46, paragraph (d), (2), of the Public Utility Commission of Texas' Substantive Rules, "Utility service may not be disconnected for failure to pay for merchandise or charges for non-utility service provided by the utility."

(Id., at 10.)

Each sponsor will be charged the following rate elements for Dial 976 service: (1) a nonrecurring service establishment charge of $1,000 for the activation of each Dial 976 announcement or interactive program; (2) a monthly charge of $32.00 per Dial 976 announcement line; (3) a per call charge for every client call to the sponsor's Dial 976 number; and (4) a one-time nonrecurring charge of $13.00 for each change in the length of the sponsor's message. (Id., at 4.) Additionally, if a sponsor's announcement equipment is located outside of the telephone company's selected service office area, then SWB's Private Line Tariff rates will be applied to connect the sponsor's announcement lines to the Dial 976 serving office. (Id., at 7.)

According to Mr. Springfield the recurring and non-recurring charge levels (other than the Private Line Tariff rates) were developed in part utilizing market data generally indicating market expectations regarding Dial 976 type services. (Id., at 5.) Testimony was also presented summarizing the results of cost studies which, the company indicates, were utilized in designing rates for Dial 976 service. (SWB Ex. 2.) Additionally, Mr. Springfield testified that discretionary services are priced to provide a contribution to help keep basic local exchange service low. (Tr. at 16.) A comparison of the costs, the proposed rates, and the resulting contribution for the proposed Dial 976 rate elements is set forth below:

	Monthly or Usage Cost	Proposed Monthly Rate or Rate Per Call	Contribution
1. Dial 976 Announcement Line	$22.52	$32.00	$9.48
2. Generic Rate-Per Call			
a. 60 seconds or less	.00247	.15	.148
b. Additional 30 seconds or fraction thereof	.00003	.03	.03
	Nonrecurring Costs	**Proposed Nonrecurring Charge**	
3. Service Establishment, per Announcement or Interactive Program	$2,446.37	$1,000.00	($1,446.37)
4. Sponsor Selected Price/ Variable Length Message	12.19	13.00	.81

(SWB Ex. 1, (Springfield) Exhibit No. 2.)

SWB witness Larry B. Carney testified regarding the results of the incremental cost study utilized in designing the Dial 976 service rates. According to Mr. Carney it is appropriate to utilize an incremental cost study in pricing decisions because: (1) incremental unit costs are based on direct cost responsibility. Only costs traceable to providing the service to those customers using the service are considered; and (2) incremental costs are forward-looking, allowing the costs to be projected over the period for which the rates will be set. (SWB Ex. 2 at 2.)

Mr. Carney testified that the incremental unit cost per Dial 976 announcement line includes the following four components: (1) drop wire--the means by which a sponsor is connected from his location to the local loop; (2) loop plant--cost of outside plant loops; (3) line termination--the equipment in the central office which is dedicated to each individual line; and (4) departmental expenses--the administrative expenses incurred by the telephone company. (Id., at 4-6.) Mr. Springfield further explained that the Dial 976 announcement line was set in order to generate a contribution of approximately 42 percent above the incremental unit cost. (SWB Ex. 1 at 6.)

The cost components included in the generic rate per call represent a combination of billing and measurement costs. Specifically, billing costs include costs associated with processing the billing information and producing the customer's bill, computer costs, and costs for additional forms and postage. The measurement costs include set-up costs--the processor (switch) and memory (call store) costs to establish the call--and cost per conversation minute--cost for the continuing use of the measurement equipment during the initial 60 seconds of the call. (SWB Ex. 2 at 7.) Additionally, Mr. Springfield testified that the generic rate per call represents the charge to the sponsor for each client call to the sponsor's recorded announcement or interactive program. The general rate per call varies, depending on the length of a sponsor's program, from a minimum 60 second (or less) charge of $.15 to a maximum $.27 charge for a three minute program. According to Mr. Springfield market data indicated that a sponsor would be willing to pay between $.15 to $.27 per call and the rates were set accordingly. The incremental additive for each additional 30 seconds (or fraction thereof) from the minimum program duration up to the maximum is priced at cost, $.03 per call. (SWB Ex. 1 at 4-7.)

With regard to the service establishment charge Mr. Carney identified the following components as being included therein: (1) billing--costs associated with upgrading SWB's computerized billing system to allow for the monthly billing of Dial 976 calls; (2) training methods--costs incurred in the development of training for service representatives; (3) training delivery--cost of the instructors presenting and the participants attending the training; (4) advertising--costs associated with introducing the service to the public; and (5) network allocation--fees charged by the certified public accounting firm that will administer the network allocation process. (SWB Ex. 2 at 6.)

As the above chart indicates, the service establishment charge was set at $1,000; $1,446.37 below the incremental cost of $2,446.37. According to Mr. Springfield this was done because market data indicated that a sponsor would not be willing to pay more than approximately $1,000 for initial start up costs for Dial 976 service. (SWB Ex. 1 at 5.) Mr. Springfield testified that the recovery of the difference between the incremental cost and the proposed charge will be accomplished through the contribution associated with the per call rate; noting that SWB estimates the full cost to be recovered within the first month that Dial 976 is provided to a sponsor. (Id.) Illustrating this Mr. Springfield testified that if a sponsor has a one line system, approximately 9,000 calls to the 976 number would be needed for SWB to break even on its investment in a one month period; or 4,500 calls over a two month period. If the sponsor has a two line system, 4,500 calls per line would be needed for recovery in one month; or 2,250 calls per line over a two month period, and so on. (Tr. at 34.)

The service order costs (sponsor selected price/variable length message rate) include the costs associated with changing a sponsor's message length and/or the per call client charge. These costs include service representatives and comptrollers costs. (SWB Ex. 2 at 7.) Mr. Springfield testified that the rate was set at $13.00 to reflect the actual cost rounded to the next highest dollar. (SWB Ex. 1 at 6.)

Network transport and switching costs and collection costs were not included in the cost study. Mr. Carney testified that because the network transport and switching costs are to be recovered under other existing tariffs it would be inappropriate to also include these costs in the Dial 976 service costs. (SWB Ex. 2 at 8.) Mr. Carney further testified that because any uncollected billings from Dial 976 service are to be deducted from the receipts prior to remitting the receipts to the sponsor, no collection costs are anticipated. (Id.)

SWB estimates that approximately $4.2 million will be generated during the first 12 months following the implementation of Dial 976 service. This revenue estimate is based on the assumption that during the first year after implementation 40 systems (sponsors) will be active and that each system will have 15 announcement lines, for a total of 600 announcement lines, which are expected to generate over 24 million calls. (Tr. at 31-32 and Staff Ex. 1 at 7.)

SWB does not intend to monitor sponsors' announcements or interactive programs for the purpose of determining if the content is obscene, and if so to discontinue service. However, Mr. Springfield testified, the Dial 976 tariff specifically provides that the service may not be utilized in any unlawful manner. (SWB Ex. 1 at 10.) Thus, if a court of law finds the content of a sponsor's program to be unlawful because of its obscene content, SWB will either

disconnect that sponsor's service or require compliance with requirements established by the Federal Communications Commission (FCC) and/or this Commission. (Id., at 10-11.)

To educate its customers regarding Dial 976 service, upon approval of the tariff SWB proposes to include educational information in the company's bill inserts. (Id., at 9.) Further, SWB proposes that each sponsor's advertisement or promotion include the following statement prominently displayed (no smaller than 12 point letter characters in publications) in printed advertisements and clearly communicated in any television or radio advertisements:

> A (the sponsor's selected price) charge will be billed for calling this (market location) telephone number in addition to applicable local or long distance charges.

(Id., and (Springfield) Exhibit No. 3, Attachment 4.)

Additional sponsor advertising guidelines proposed by SWB include the following:

> If a sponsor advertises the service, this advertising should commence by the date service begins or by the implementation date of a selected price change.
>
> The sponsor may not mention or refer to Southwestern Bell Telephone in any advertising.

(Id., (Springfield) Exhibit No. 3, Attachment 4.) The failure to comply with any of the proposed advertising guidelines could under SWB's proposal result in the termination of Dial 976 service to the sponsor. (Id.)

SWB has designated a Dial 976 service coordinator to handle any customer complaints or inquiries regarding the service, and whose duties also include: coordinating the service with the sponsors and managing the service allocation process. Initially all complaints or inquiries will be transferred to the Dial 976 service coordinator for resolution. If the coordinator's line is busy, the customer will be given a toll free number to call the coordinator directly. If the coordinator is otherwise unavailable, two additional management employees have been designated to handle the calls. Each complaint will be documented and kept on file in the coordinator's office. Customers complaining about the content of a sponsor's program will be referred to that sponsor and will upon request be given the sponsor's telephone number and address. (Id., at 11-12.) Disputes regarding 976 charges will not be referred to the sponsors, but will be investigated by SWB in accordance with its normal disputed billing processes. (Tr. at 37.) On a one time basis SWB will adjust a local exchange customer's bill to remove 976 charges if, for example, the customer contended that the calls were made by a child and unauthorized; or that he/she was unaware that charges were associated with the calls. The customer would then be reminded that charges will be made for all calls to 976 numbers, and that the customer is responsible for all communications originating from his/her premises. From then on, SWB would attempt to sustain all charges from that premises, but if uncollectible, the amounts would be subtracted from the remittance to the sponsor(s). (Tr. at 39, 42 and 107-108.)

Service representatives in the company's Residence Service Centers and Business Service Centers will eventually be trained so that they themselves will be able to handle most inquiries or complaints regarding Dial 976 service. (At the time of this tariff filing SWB anticipated the training to be completed by the end of March 1986 .) However, the Dial 976 coordinator will still be available to assist the service representatives should such be necessary. (Id., at 12.)

2. PPI

PPI did not submit testimony specifically analyzing SWB's proposal in this docket. Rather, Mr. Glenn Appleyard--President of PPI--adopted and submitted the prefiled testimony of Mr. Bruce Fogel--Chairman of the Board of PPI--which was presented in a proceeding before the Public Utility Commission of California. It is noted that the ALJ granted SWB's motion to strike those portions of PPI's testimony relating specifically to the California tariff. (The Commission General Counsel concurred with SWB's motion to strike.) Following is a summary of those portions of PPI's testimony relating to a generic discussion of Dial 976 services.

PPI began by discussing the history of Dial 976 service. (PPI Ex. 1 at 4-15.) Summarily, the history of Dial 976 service can be viewed in three phases:

1. Phase One--1928 to 1972. The telephone companies on their own provided certain programs such as time and weather information.

2. Phase Two--1972 to 1982. Several telephone companies hired private companies such as PPI to produce programs for them. The programming included sports, racing news, children's stories and business news.

3. Phase Three. This phase dates from the implementation of CI-II (computer inquiry) in 1983 to the present.

(Id., at 6-7.) PPI explained that upon divestiture private entrepeneurs became the owners of their own programming; they had to purchase and install their own equipment; they were responsible for advertising; and their revenues were dependent upon the success of the programs. The transport and billing services were and continue to be provided by the telephone companies. (Id., at 13.)

PPI pointed out that Dial 976 type service is a very expensive undertaking for the private companies because start up costs for equipment purchases and program development are enormous. Additionally, responsible advertising is a necessary, though very costly, method of entering and succeeding in a market, and the risk of not succeeding is high. (Id., at 18-20.) It was noted that for financial reasons there might be an incentive for sponsors to provide adult

type messages. However, PPI pointed out that regardless of any "financial rewards" associated with adult entertainment which might ensure the company's financial stability, PPI has no plans to ever enter the adult entertainment business. (Id., at 20-21.) In this regard PPI noted that adult entertainment type 976 services are expressly prohibited in some states. (Id., at 23-24.)

According to PPI the success of Dial 976 service will depend upon at least the following factors:

1. Diverse and popular programming;
2. Acceptance by the public of Dial 976 service;
3. A business environment which encourages the development of new and responsive programming;
4. Reasonable costs to be borne by the providers and reasonable prices charged to the public; and
5. Profit-making incentives for providers.

(Id., at 26.)

In PPI's opinion the government/Commission should not dictate the content of Dial 976 advertising; and that any truthful and accurate advertising should not be prohibited in any way by law. According to PPI the government/Commission should not go beyond a general proscription against false, misleading or deceptive language; which, PPI noted, is already unlawful. (Id., at 36-38.)

Regarding a one-time adjustment for callers' bills PPI suggested the following. On a first-time only basis (i.e., no prior 976 billings), callers who believe they deserve an adjustment should be required to complete a declaration (preprinted by the telephone company and available at its offices or by mail upon request), to allow the determination of: (1) whether an adjustment is warranted; and (2) if so, who then bears the cost. (Id. at 46-47.) According to PPI the declaration form--which could be in a multiple choice and multiple language format--should require the following information:

(1) Relevant phone bill attached;
(2) Telephone numbers called for which adjustment requested, and dates;
(3) Amount claimed;
(4) A statement that the person(s) on whose phone the calls were made was (were) not aware of the charges and has (have) not previously been billed for 976 calls;
(5) A statement of the caller's source in learning of the program;
(6) A statement of what information was lacking in the source; and
(7) A representation that no previous 976 adjustment request had been made.
(8) An authorization so that the declaration can be reviewed by the relevant IP's (information provider).

(Id., at 46-48.)

With regard to the possibility of blocking access to certain programs (e.g. adult entertainment and/or children's programs) PPI stated its concurrence with the following comments made by the NYNEX telephone companies in the FCC Dial-A-Porn proceeding:

> A. <u>Blocking at the Caller's Premises Is A Feasible and Attractive Option.</u>
>
> It now appears that a blocking circuit capable of being deployed at the calling party's premises would be technically and economically feasible. Network specialists at New York Telephone have initiated design of such a circuit, and have begun developing a working prototype. It appears that some equipment vendors may be offering similar devices. Use of such a blocking circuit to restrict minors' access to dial-a-porn numbers may be a practical solution to the dial-a-porn problem, as shown below.
>
> The blocking circuit could be installed where the access line enters the caller's premises, so that only one circuit would be required to control all extensions on the line. Alternatively, if desired, the circuit could be connected on an extension specific basis, so that a given telephone (for example, a phone in a child's room) could be blocked, while another served by the same line would not.
>
> The blocking circuit will be capable of being programmed to recognize up to 128 combinations of dialed digits. Immediately on recognition of any of the combinations, the circuit drops the connection to the central office. Consequently, the call is never connected through the switch and, therefore, is not billed. The number of digits screened is variable: the subscriber could block 976, 976-XXXX, (NPA) 976-XXXX, or any other combination. In any case, the circuit screens a specific string of digits, starting with the first digit dialed. The circuit could be reprogrammed by opening the box and installing another micro-chip. It is anticipated that the final design of the circuit will permit the individual subscriber to select the numbers to be blocked, and to modify the selection subsequently. It is anticipated that the programmable blocking circuit will sell for less than $50 per circuit.
>
> The blocking circuit described above would be more effective at its intended purpose--restricting minors' access to dial-a-porn--than screening and blocking in the central office. It will work equally well regardless of the type of serving central office. It would not depend on the availability of spare classes of service, code controls, or FAT frames. It can be programmed to lock non-976 dial-a-porn numbers, as well as those on the 976 exchange. And it can be adapted to block Feature Group A and B calls on a selective basis.
>
> At the same time, the blocking circuit would be less restrictive of the ability of adults and minors to make permissible calls. As noted, it could be attached, if the customer desired, to a single extension phone on a line, permitting an adult to call the blocked numbers from one extension while preventing a child from calling from the other. Moreover, it could be programmed to block on an individual line number basis, thus permitting children and adults to reach time, weather, sports, and other announcements while restricting access to dial-a-porn services.
>
> Finally, the blocking circuit would be more economical than central office blocking, in part because it could be more precisely targeted to the user. Under the central office blocking approach, the telephone company might have to invest the time and resources to convert an entire office in order to provide blocking capability to only a few customers. The

> blocking circuit approach would also save telephone company administrative costs which would otherwise be necessary to process a subscriber's blocking order, to effect a change in class of service, and so on.
>
> In short, the blocking circuit appears to be preferable in every way to the central office blocking option. For that reason, as well as the others given in Part III above, the NYNEX Telephone companies recommend that the Commission reject the central office screening and blocking approach, and allow customers who wish to restrict dial-a-porn calling from their home telephones to do so by means of a blocking circuit such as that described above.

(Id., at 50-53.) PPI stated that the blocking device should not be provided for free or for only a fraction of its cost because that would encourage callers to get one even if not needed. (Id., at 53-54.) However, PPI also stated that "the share of the cost of a blocking device should be entirely or mostly borne by the consumer who wants one." (Id., at 54.)

Addressing programming directed towards children PPI pointed out its awareness of potential problems in this area (Id., at 54-57); and noted that advertising should simply and truthfully explain a product to a child and state unequivocally that the child should seek parental permission before placing the call. (Id., at 58.)

At the hearing Mr. Appleyard testified that PPI is in favor of a tariff being approved allowing the provision of information services in Texas; and noted that any uncertainty PPI has regarding SWB's proposal herein relates to certain provisions which PPI might like to see written a different way. (Tr. at 78.)

3. Staff

Staff engineer David E. Featherston reviewed SWB's application and submitted testimony regarding the Dial 976 service proposed herein. Mr. Featherston pointed out that Dial 976 service takes advantage of existing technology and is a service which could be beneficial to the public in general; noting the more familiar Dial-A-Prayer, Dial-A-Joke, up-to-the-minute sports scores, stock market reports, news bulletins, vote-polling and other mass "call-in" programs. (Staff Ex. 1 at 2.)

Mr. Featherston noted that in reviewing this application the most important consideration is to determine whether or not the technological and revenue benefits outweigh the potential problems and marketing abuses. According to Mr. Featherston, given the controversial nature of Dial 976 service, in considering this application the Commission will need to make a policy decision as to whether or not this is the type of business venture in which SWB should be allowed to participate. (Id., at 10.)

Mr. Featherston also pointed out that in those areas where this service has been the source of controversy, such has generally centered around either: (1) advertising directed towards children; or (2) the transmission of pornographic messages (e.g., Dial-A-Porn). (Id.) Regarding the latter Mr. Featherston testified that the Commission has received letters from consumers expressing the concern that Dial 976 service would bring Dial-A-Porn to Texas. (Id., at 8.) He further testified that the FCC in its second Report and Order in Docket No. 83-989 ruled that providers of adult-type messages must place a device on their premises which would allow access to such messages only if an authorization personal identification code is entered. The purpose of this requirement was to restrict access of minors (persons under 18 years of age) to adult-type messages. However, Mr. Featherston testified, this FCC decision was overturned by the United States Court of Appeals for the Second Circuit and the FCC was ordered to examine other methods of restricting access. (Id., at 7-8.) (It was noted at the hearing that the court's ruling only exempts the State of New York from the FCC ruling. Tr. at 84.) Mr. Featherston further testified that an article in the April 28, 1986, issue of Telecommunications Reports indicates that there is a move in Congress to amend the Communications Act to prohibit "dial-a-porn" type service altogether. (Id., at 8.)

According to Mr. Featherston the only way to completely restrict or eliminate adult entertainment type messages from being provided through Dial 976 service is to deny approval of the service altogether. However, if adequate safeguards are in place such an extreme measure is unnecessary. Accordingly, Mr. Featherston recommended that adult entertainment message providers be required to conform to whatever restrictions the FCC finally adopts in Docket No. 83-989 or such restrictions as the Commission may adopt in future proceedings. (Id.)

No restrictions for advertising directed towards children was proposed by SWB. Mr. Featherston noted that such advertising could eventually pose problems to the extent that children are encouraged to repeatedly call a 976 number. According to Mr. Featherston Dial-A-Santa caused numerous problems on the West Coast, and the California Commission is considering guidelines which would require 976 advertisements directed towards children to state that parental consent is required before the placement of the 976 call. (Id., at 9.) Because Texas does not yet have actual 976 experience, the staff did not propose guidelines or restrictions pertaining to this issue at this time.

As previously noted SWB proposed certain advertising restrictions including a requirement that the sponsor state--no smaller than 12 point letter characters in print advertisements and verbally on radio and television--that a charge will be billed to the caller and that the charge will apply in addition to other applicable telephone charges. In Mr. Featherston's opinion this requirement is reasonable and should be required with the exception of the print size

requirement; which, he testified, would be difficult to enforce. Therefore, Mr. Featherston recommended that the print size requirement be eliminated. (Id., at 8-9).

With regard to the cost information provided by SWB for Dial 976 service Mr. Featherston testified that, with the exception of the service establishment charge, the rates are "priced above cost, and they appear to be reasonable for an optional, discretionary service based on 976 rates in other jurisdictions." (Id., at 6.) Regarding the service establishment rate--which is priced below cost--Mr. Featherston testified that:

> The $1,000 rate was based on what the company believes 976 customers are willing to pay (based on rates for 976 service in other states). The company expects call volumes to be such that the cost will be recovered from other rate elements within the first month of service. If a 976 provider went out of business before call volumes necessary to recover the costs are generated then SWB would have to absorb the loss which would take away from the benefits that would accrue to the general body of ratepayers. On the other hand, the $1,000 rate for service establishment is the same as proposed by General in Docket No. 6521 and is the same as the rate charged by the majority of companies around the country providing 976 service. In this circumstance, the benefit that is associated with the 976 providers establishing service for the $1,000 rate, in my opinion offsets the risks associated with pricing this service below cost. (Id.)

Mr. Featherston noted that SWB's proposed methodology for rendering payments to each sponsor (i.e., remitting a check each month to each sponsor based upon the difference between the charge for the billed calls and the company's generic rate, less charges for Dial 976 announcement lines, private lines service and uncollectible billings) is consistent with industry practices involving 976 sponsor compensation. (Id., at 6-7.) Mr. Featherston also concurred with SWB that Dial 976 service constitutes non-utility service provided by the utility and that telephone customers should not have their telephone utility service disconnected for failure to pay Dial 976 service charges. (Id., at 7.)

Regarding the procedure for handling customer complaints, Mr. Featherston recommended that SWB handle disputed Dial 976 bills in the same manner as any other disputed call billed by the telephone company. (Id., at 9.) Mr. Featherston also recommended that SWB include a tariff section addressing the Dial 976 callers' rights; specifically, information regarding adjustments for incomplete calls, adjustments for disputed or unauthorized calls, caller billing information, and callers' rights regarding disconnection. (Id., at 9-10.)

Mr. Featherston testified that under SWB's proposal the 976 sponsors will not be responsible for calls from unbillable locations (e.g., calls from 4-party service customers, public and private pay telephones, services with selective class of call screening, operator handled calls, and certain intraLATA and interLATA calls), which for the most part will be blocked. (Id., at 10.)

Summarizing the staff position Mr. Featherston testified that the Commission has the following options in this case:

I. Deny SWB's application for Dial 976 service. While this would eliminate any concerns about potential marketing abuses and associated problems, it would also deny the public access to a technologically feasible and possibly beneficial new service.

II. Approve SWB's application as filed. This would give callers the opportunity to utilize Dial 976 service but would not address any of the concerns raised by Mr. Featherston in his testimony.

III. Approve SWB's filing with the following modifications:

a. That the Dial 976 sponsor be required to conform to all present and future FCC or PUC requirements concerning adult-type messages.
b. That the requirement that the price for a Dial 976 call be printed in type no smaller than 12 point be eliminated. However, the price for the call should still appear in any advertisement.
c. That a callers' rights section that addresses the following be added to the proposed tariff: adjustments for incomplete calls, adjustments for disputed or unauthorized calls, caller billing information, and callers' rights regarding disconnection.

IV. Approve SWB's filing with the modifications set forth in Option III above on an experimental basis to be reexamined after 12 months.[4] This option would require SWB to automatically file an application for review of the tariff after 12 months to establish that Dial 976 service is still a worthwhile venture; and would give the staff an opportunity to examine actual revenue and cost information and evaluate potential problems.

(Id., at 11-12.) Mr. Featherston recommended the adoption of Option IV, testifying that in his opinion this option best balances the interests of the company, the Dial 976 sponsor, the caller, and the general body of ratepayers. Additionally, Mr. Featherston recommended that SWB be required to:

1. Track the results of Dial 976 service for 12 months after approval of the tariff and conduct a study based on the results; which study should include: the number of 976 customers, the number of calls

[4]Mr. Featherston originally testified that under Option IV the tariff should be approved on an experimental basis with an automatic expiration after 12 months. Thereafter, SWB would be required to file another application for permanent approval of the tariff. Mr. Featherston modified this option in the manner set forth above when he took the witness stand at the hearing.

placed to 976 numbers, the net revenue impact, the amount remitted to 976 customers, the amount of uncollectible or disputed revenue, and the number and nature of complaints concerning 976 service.

2. Provide the information utilized in the study referenced in Item 1 above to the Commission Engineering staff on a quarterly basis.

(Id., at 12-13.)

B. Review and Recommendation

1. Is approval of a tariff provision to allow the implementation of Dial 976 service in the public interest?

The ALJ is of the opinion that the answer to the foregoing question is: yes, the public interest will be served by allowing SWB the opportunity to provide, and ratepayers the opportunity to utilize, Dial 976 service. It is noted that while there may be some disagreement as to specific provisions in SWB's proposed tariff, which will be discussed below, no party to this proceeding opposed the implementation of Dial 976 service; in fact approval of such service was encouraged. It is further noted that it is a policy matter for the Commission as to whether or not the provision of Dial 976 service is the sort of venture that the telephone company should be encouraged to pursue. In a recently decided case, Docket No. 6521, Application of General Telephone Company of the Southwest for a New Tariff Offering 976 Service, ____ P.U.C. BULL. ____ (June 25, 1986), the Commission in modifying and approving General Telephone Company of the Southwest's (GTSW) application, determined that Dial 976 service appears to be a worthwhile venture, and that implementation of the service should be allowed.

Approval of Dial 976 service will allow the public access to a new, potentially beneficial and technologically feasible service; and will provide SWB an opportunity to increase its revenues and provide a contribution to help offset local rates, without the occurrence of an adverse impact on the general body of ratepayers. Additionally, ratepayers would be afforded an easily accessible and optional means of obtaining desired information. Accordingly, in the ALJ's opinion the public interest would be served by allowing SWB to implement Dial 976 service. This, however, does not mean that legitimate concerns do not exist regarding this service. The concerns identified to date[5] will be addressed below in the discussion of the specific tariff proposed for approval herein.

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[5]Because Dial 976 service is new to the State of Texas, problems or concerns may arise in the future which are not readily apparent at this time. Also, the extent to which the known concerns either dissipate or develop into major problems will only be realized once experience in the area has been gained.

2. Should the disconnection of basic local exchange service be allowed for non-payment of 976 billings?

[1] Under existing Commission rules the answer to this question turns on whether or not Dial 976 service is in fact a utility service. As previously noted, P.U.C. SUBST. R. 23.46(d)(2) prohibits disconnection of basic local exchange service for non-payment of billings for non-utility services provided by the utility. Also, as previously noted, SWB and the Commission staff hold the position that Dial 976 service is not a utility service. SWB's rationale was explained by Mr. Springfield, who testified that:

> We say our position is that the local exchange telecommunications service that the customer receives when he dials a 976 number ends when the number is answered. That the sponsor's message is not a utility service; that the message the sponsor or the message the customer is asked to pay for for receiving that message from the sponsor is not a utility service; that we have completed the local exchange communications to the number when the number is dialed.

(Tr. at 11-12.) Likewise Mr. Featherston testified that the staff considers Dial 976 service to be a non-utility service because it is not a direct utility service to the caller; and that from the telephone company's perspective it is merely a billing and transport service provided to the 976 sponsor. (Tr. at 83.)

PPI argued, however, that "the availability of the remedy of disconnection for non-payment of 976 charges is lawful, necessary and in furtherance of the public interest" (PPI Brief at 8) because:

1. By definition and usage 976 services are part of basic telephone services; the determining factor being whether the telephone company's utility (bottleneck) facilities constitute the necessary communications link between a caller and his/her message. PPI argued that the sponsor's message and the medium for transporting the message (the telephone company's facilities) are inextricably bound together. Thus Dial 976 service is a utility service which should be afforded equal treatment as other utility services. (Id., at 8-13.)

2. Information providers are entitled to the treatment given interexchange carriers (IXC) in situations where the local exchange company bills and collects on their (IXC's) behalf. Specifically noted was AT&T's Dial-It 900 service which SWB witness Springfield testified was conceptually no different than Dial 976 service (Tr. 13-15); and for which service the FCC allows disconnection as a lawful sanction for failure to pay the 900 charges billed by the local exchange carriers. (Id., at 13-15.)

3. Discontinuance of service is the only practical way for the telephone company to enforce collections for small amounts of unpaid 976 charges--there being no way for the information provider to do so; and would only occur in instances of clear abuse by the customer after a reasonable opportunity to dispute the charges. (Id., at 15-16.)

4. Discontinuance of service would resolve the problem of repetitive non-payers. (Id., at 16-17.)

Defining "service", Section 3(s) of PURA states that:

> "Service" is used in this Act in its broadest and most inclusive sense, and includes any and all acts done, rendered, or performed and any and all things furnished or supplied, and any and all facilities used, furnished, or supplied by public utilities in the performance of their duties under this Act to their patrons, employees, or public utilities, and the public, as well as the interchange of facilities between two or more of them. Service shall not include the printing, distribution, or sale of advertising in telephone directories.

[2] Thus, to determine whether or not Dial 976 service falls within the ambit of utility service, it is necessary to look at what is being provided by the utility, and to whom. Under the proposed Dial 976 tariff SWB will provide the sponsors facilities for transporting the sponsors' messages, in addition to billing and collection services. It is undisputed that the provision of the medium (or facilities) for transporting the 976 messages is telephone utility service provided to the sponsor. However, in the ALJ's opinion, the billing and collection services are not utility services. Merely because services are performed by a public utility does not make them utility services. For example, in the past SWB performed billing and collection services for yellow page directory advertising; however, these services were not deemed to be utility services. Thus, of the services SWB would provide to the sponsors under the 976 tariff, only the provision of the equipment and transport services actually constitutes utility services.

[3] Turning now to the question of the services SWB would be providing the local exchange customer (the sponsor's client) under the 976 tariff, the ALJ notes the following. Other than informing the local exchange customer of the existence of Dial 976 service, SWB provides no service to the local exchange customer under the 976 tariff. The ability of said customer to utilize his/her telephone to call a 976 number results from SWB's provision of local exchange service. The message that a caller to a 976 number receives and pays for is provided by the sponsor, not SWB; and SWB has nothing to do with the content of messages provided. Accordingly, under the Dial 976 tariff SWB is not providing a utility service to the local exchange customer.

PPI argues that the utility service provided the sponsors and the message provided the local exchange customers are integrally related and that "the product being sold is the combination of the message and the medium." (PPI Brief at 11.) The services may be integrally related, but does the fact that the viability of a particular service is dependent upon the telecommunications network automatically make that service a utility service? The ALJ is not convinced that such is necessarily the case. For example, if a bank offers, for a specific fee, the service of paying bills by telephone, would the fact that this service requires utilization of the telecommunications

network mean it is a utility service? Would the failure to pay the bank's fee for this service result in disconnection of the customers local exchange service? The ALJ would think not. Again, although the viability of the Dial 976 service is dependent upon the telecommunication network, it is not, in the ALJ's opinion, a utility service because the service a 976 caller receives and is billed for is not one provided by SWB in the performance of its duties, but rather one provided by the sponsors.

The ALJ concurs with SWB and the Commission staff that under existing Commission rules disconnection of basic local exchange service should not be allowed for non-payment of 976 billings. The ALJ is aware that experience with this service may indicate the need to implement measures to handle customers who continually make 976 calls and at the same time refuse to pay for them. In this regard the Commission may, after further investigation, determine that as a matter of policy it is appropriate to allow disconnection for failure to pay 976 charges. Accordingly, the ALJ recommends that the Commission adopt the following language in this case which is similar to that adopted by the Commission in Docket No. 6521:

> Until the policy and factual issues regarding disconnection of local exchange service for failure to pay 976 charges have been further investigated by the Commission, such disconnection shall not be allowed for failure to pay 976 charges.

The ALJ further notes that as an alternative to disconnection of basic local exchange service it is reasonable to explore the possibility of blocking calls to 976 numbers where made by persons who continually refuse to pay for them. Although SWB has not investigated this possibility in association with this case, Mr. Springfield testified that blocking an individual's access to Dial 976 service is technologically possible. (Tr. at 23.) One method of blocking would be through Central Office Screening utilizing central office equipment. Mr. Springfield testified that this method may prove to be fairly expensive, and possibly not cost effective if expensive equipment is put in the central office and calls from only three or four premises are blocked. (Tr. at 25-26.) Another blocking method is through the use of terminal equipment that could be purchased by the end user customer, installed at his premises, and would deny access to certain series of numbers. (Tr. at 24 and 36.)

The ALJ recommends that SWB be required to investigate the costs and feasibility of utilizing blocking of a particular premise's access to Dial 976 service as an alternative to the possible disconnection of service for non-payment of 976 charges.

3. Should the fact that SWB will not disconnect basic local exchange service for non-payment of 976 charges (and other customer rights) be set forth in the 976 tariff?

The staff proposed the inclusion of a callers' rights section in the Dial 976 service tariff which would include, among other things, a statement that basic local exchange service would not be disconnected for failure to pay 976 charges. PPI also questioned why SWB's uncollectible policy was not clearly defined in the tariff. SWB opposed the recommendation that the statement regarding disconnection be included in the Dial 976 service tariff, noting that no positive benefit would result from such; and that quite possibly it would have the effect of advertising to potential abusers that they may continually call 976 numbers, refuse to pay the associated charges, and still not have their local exchange service disconnected. If such statement is required to be included, it is SWB's position that it should be included in the general service tariff. SWB also pointed out that explanations of customers' rights and how to file complaints regarding telephone service and billings are set forth in the front of telephone directories. Therefore, it is unnecessary for such to be detailed in the Dial 976 tariff.

The ALJ concurs with SWB that it is not a good idea to publicize the fact that a caller may continually place calls to 976 numbers, never pay the associated charges and still retain his basic local exchange service; including the ability to continue placing 976 calls. The ALJ therefore recommends that SWB <u>not</u> be required to include in the Dial 976 service tariff the statement that basic local exchange service will not be disconnected for non payment of 976 charges. However, the fact that there will be no disconnection should be made clear to the sponsors in the 976 information packages provided.

However, given the nature of this service, it is reasonable to include in the Dial 976 service tariff information regarding adjustments for incomplete calls and the one time adjustment for unauthorized calls, as well as a statement that billing disputes or complaints will be handled in accordance with P.U.C. SUBST. R. 23.45(h).

4. Adult Entertainment Type Messages.

As previously noted, one of the generally cited problem areas associated with Dial 976 service is the area of adult entertainment or "dial-a-porn" type messages. Although PPI indicated that it has no plans to ever provide such messages, PPI represents only one of many potential sponsors. SWB did not propose specific tariff language dealing with adult-type messages, and the staff recommended that adult entertainment message providers be required to conform with whatever restrictions the FCC finally adopts in Docket No. 83-989; or such restrictions as the Commission may adopt in future proceedings. However, in the mean time, no restrictions or safeguards would be in effect.

The ALJ notes that in Docket No. 6521, supra, the Commission adopted the following language regarding the provision of adult entertainment messages, which language the ALJ recommends be adopted herein:

> 976 customers which offer sexually explicit messages shall restrict access to those messages by requiring callers which access the above described messages to:
>
> (a) input and authorized access or identification code before transmission of the subject message begins, where the 976 customer
>
> (1) has issued the code by mailing it to the caller after reasonably ascertaining through receipt of a written application that the caller is not under eighteen years of age; and
>
> (2) has established a procedure to cancel immediately the code of any person upon written, telephonic or other notice to the 976 customer's business office that such code has been lost, stolen, or used by a person or persons under the age of eighteen, or that such code is no longer desired.
>
> Upon complaint, the company shall investigate compliance with the required restrictions. If the company is satisfied that the 976 provider is not in compliance with the tariff, notice shall be issued to the customer of such noncompliance; the notice shall inform the customer that compliance with the tariff must be accomplished within twenty (20) days of receipt of the notice, or 976 service shall be discontinued.

5. Should the conditions for Dial 976 service include specific requirements regarding sponsor advertising?

SWB proposes that each sponsor's written advertisement identify the sponsor's selected charge and state in no smaller than 12 point letters that the sponsor's charge will be billed in addition to applicable local or long distance charges for each call made. This statement is to be clearly communicated in any radio or television advertisement. The staff concurs with this proposal except with regard to the size requirement for the letter characters in the written advertisements; which the staff found would be difficult to enforce. PPI argued that the advertisement requirements should be stricken because: (1) adequate public protection against misleading and/or deceptive advertising already exists under state law; and (2) the Commission's authority to devise regulations governing the advertisements information providers place in broadcast and print media is questionable. (PPI Brief at 25-27.)

The ALJ notes that while the Commission does not regulate information providers, the Commission may, in approving the Dial 976 service, establish terms and conditions under which the utility may provide the service to the sponsors or information providers. If the sponsor wants the service, it must comply with those terms and conditions. In the ALJ's opinion the Commission can and should as a condition of service require all sponsor advertising to clearly

and conspicuously communicate the sponsor's charge, and the fact that such will be billed in addition to applicable local or long distance charges for each call. This should be clearly announced in radio and television advertisements. The ALJ notes that while it may be difficult to enforce a particular size requirement for the letter characters as proposed by SWB, such a requirement eliminates any question as to what is meant by "clear and conspicuous". It further provides SWB and the Commission some guideline for determining if the communication of this information is adequate should complaints in this regard arise. The ALJ therefore recommends that SWB's proposed advertising requirement be adopted.

Additionally, the ALJ notes, concern was raised regarding advertising directed towards children and the problems which might result therefrom. Although specific language was not proposed dealing with this matter as problems have not yet arisen, in the ALJ's opinion it is reasonable to implement preventive measures in an attempt to avoid such a problem occurring. Accordingly, in concurrence with PPI the ALJ also recommends that any advertising directed towards children include the statement that parental consent should be obtained before a call is made to the 976 number.

6. Should SWB be responsible for advertising Dial 976 service beyond the proposed customer education efforts proposed?

As already noted, SWB plans to educate customers regarding the availability of Dial 976 service through billing inserts. Basically, the service and how it functions will be explained, as well as the fact that there are specific charges associated with each call made.

PPI argues that this is inadequate as it will not reach: (1) customers who ignore bill inserts; (2) customers who cannot read; and (3) Spanish-speaking customers. Accordingly, PPI argues that SWB should at a minimum be required to place a number of media spots on television and radio which would inform the public in a positive way, about the service, along with associated charges. (PPI Brief at 22-24.)

In the ALJ's opinion SWB should not be responsible for conducting a media blitz promoting Dial 976 service. The extent of SWB's participation in this regard should be as proposed: to inform customers that the service exists and if a call is placed charges are applicable. In the ALJ's opinion billing inserts, written in both English and Spanish, are sufficient. Promotional advertising by SWB would tend to give the impression that the telephone company is endorsing the messages of sponsors rather than merely providing the facilities over which the messages are to be transported. Additionally, any such advertising by SWB would not be sponsor specific and as such would not identify the specific per message charge which may vary from sponsor to sponsor. In the ALJ's opinion the promotional advertising should be the responsibility of the entities providing the service to the public--the information providers.

Therefore, the ALJ does not recommend that SWB be required to advertise (either in the newspaper or on radio or television) Dial 976 service.

7. Should SWB's proposed rate structure for Dial 976 service be modified?

SWB's proposed rate structure is set forth in Section III(A)(I) of this report. The record reflects that the rates recover the associated costs plus a contribution with the exception of the service establishment fee, which is priced $1,446.37 below the incremental cost of $2,446.37. It is expected, however, that the recovery of the difference between the incremental cost and the proposed charge will be accomplished through the contribution associated with the per call rate.

The staff found SWB's proposed rates to be reasonable for an optional, discretionary service and in line with 976 rates in other jurisdictions.

PPI argued in its brief that "the rates recommended by the telephone company are confiscatory, wholly unrelated to costs, and unfair to potential information providers, and that the Commission should adopt a rate structure which encourages the implementation and growth of a new information age industry." (PPI Brief at 18.) PPI proposed in its brief that the Commission set the service establishment charge at $2,500 (rather than the proposed $1,000) which would allow a $50.00 contribution; and that the per call rate for the initial 60 seconds (or less) be set at $.05 per call rather than the proposed $.15 per call rate. (Id., at 20.) No testimony was presented at the hearing regarding these rates; however, in PPI's opinion this rate level would have the following effect:

1. The lower per-call costs would have a tendency to reduce the charges to the consumer;

2. Lower per-call costs would encourage providers to offer more programs to specialized audiences with particular needs for information;

3. More reasonable charges by the telephone company (i.e., charges with a closer correlation to costs) would significantly diminish the existing barrier to entry in this new industry;

4. The $2,500 initial payment would ensure that the utility is charging for at least its costs in all aspects of the service from the first day of operation; and

5. PPI's proposed per-call rate allows for significant profits for the telephone company and funds to pay for media campaign.

(Id., at 20-21.)

[4] The ALJ does not agree with PPI that the rates proposed by SWB are unreasonable and confiscatory. Dial 976 is an optional and discretionary service; such services should be priced to cover their costs plus a contribution. The evidence reflects that with the exception of the service establishment charge, the proposed rates will from the outset cover the costs of the service and generate a contribution. Regarding the amount of the contribution, to the ALJ's knowledge there is no requirement that such be set at any particular level. However, where a utility is providing an optional, discretionary service, and the contributions or profits earned are to be utilized to offset the cost of local exchange rates, given the ultimate goal of universal service, the public interest would appear best served by maximizing the profitability of the service. It is further noted that Dial 976 service is not a monopoly but rather a competitive type service. It is reasonable to price such service on what the market will bear; especially given the fact that the information providers may set their rates at whatever level they choose, to recover costs and the desired profit. Although the market data relied on by SWB was not offered into evidence (nor is there any indication in the record that such was requested to be provided during the discovery process), no evidence was presented showing that information providers in the Texas market would be unwilling to pay the costs as proposed.

PPI argues that the service establishment fee be increased to $2,500 and that the per call rate be reduced to $.05. Although PPI appears willing to pay the significantly higher service establishment fee, it is not apparent that this is the consensus of information providers in the Texas market. In fact, in Docket No. 6521, the Commission approved a service establishment charge of $1,000 for General Telephone Company of the Southwest (GTSW). Further, the per call rate proposed by SWB is not out of line with that approved for GTSW. Specifically, SWB's proposed rate for 60 seconds or less is $.15 with each additional 30 seconds being priced at $.03 per call. The rates approved for GTSW are as follows:

Customer (Information Provider) Established Call Rate	Initial 60 Seconds	Rate Per Message Each Add'l 30 Seconds or Fraction Thereof
$0.20 to $0.55 (in $0.05 increments)	$.19	$.03
$0.60 to $1.20 (in $0.05 increments)	.30	.03
$1.25 and over (in $0.25 increments)	.50	.03

Further, the ALJ notes that reducing the per call charge from $.15 to $.05 would ultimately result in a lesser amount of revenues available as a contribution to local rates; with no simultaneous guarantee that the rates established by the sponsors would in fact be lower. As previously noted each sponsor establishes the rate to be charged for a particular message; these rates will not be subject to the Commission's regulatory authority. Thus it is possible that even if the per call charge to the sponsor is reduced, that the sponsor's per message charge to callers may not likewise be reduced.

Finally, it is unknown at this time whether this service will prove successful in Texas, what the actual costs will be, whether the proposed rates will continue to recover the costs and provide a contribution, how long it will take to actually recover an investment, etc. It is important that during this initial period the general body of ratepayers remain whole and not be required to bear the risk of losses associated with this venture. In the ALJ's opinion approving a $1,000 service establishment fee should achieve the goal of not discouraging potential sponsors; and at the same time the per call charges should in the aggregate not only provide a contribution, but also cover contingencies such as a sponsor going out of business before SWB has recovered the initial investment. Accordingly, the ALJ recommends approval of the rate structure proposed by SWB.

8. Should SWB's 976 service tariff be approved on an experimental or final basis?

The staff proposed that SWB's 976 tariff be approved on an experimental basis and that the company be required to file an application for final approval upon the expiration of the initial 12 month period of operation. The general counsel argued that approval on an experimental basis and re-examination after 12 months would provide an opportunity to examine actual revenue and cost data as well as potential problems, and assess the service in light of actual experience. (General Counsel Brief at 3.)

SWB and PPI strongly oppose approval of the tariff on an experimental basis primarily because:

1. There is no need to approve the tariff on a trial or experimental basis.
2. The "experimental" title would only serve to create uncertainty that could discourage information providers from expending the capital necessary to enter the 976 market, with little or no offsetting benefits to the Commission or SWB.
3. It is unnecessary to be locked into a hearing one year in advance when experience may prove that such would be more productive at the end of an 18 month or two year period, or prove unnecessary at all.
4. It is unnecessary to be locked into a hearing one year in advance when the availability of Commission resources at that time may be limited and no need may exist for such a hearing.
5. If SWB's tracking of costs, problems, and study of the financial performance of the 976 service are provided to the staff on a quarterly basis, then the staff could initiate an inquiry if and when problems develop and an inquiry appeared necessary.
6. If there is to be a re-examination of the service, the purpose should be to make improvements in areas where problems in fact arise.

(SWB Brief at 5-9 and PPI Brief at 6-7.)

In the ALJ's opinion it is unnecessary to approve SWB's Dial 976 service tariff on an experimental basis. According to staff witness Featherston, the only purpose of labeling the tariff "experimental" is to ensure that the service is reviewed after 12 months and to place the burden on the company of initiating this review. Mr. Featherston further testified that the purpose of this re-examination would be to review the cost data and the number of complaints, and to assess the problems, if any, associated with adult entertainment and advertising directed towards children. (Tr. at 91-93.) However, as pointed out by SWB and PPI, if problems--either service related or revenuewise--do not materialize, then a hearing to look into these matters may be unnecessary.

On the other hand, problems may arise such that a hearing or inquiry is warranted prior to the expiration of 12 months. In this regard the ALJ concurs with and joins in the staff recommendation that SWB be required to track the results of Dial 976 service for 12 months after the approval of the tariff, to conduct a study on the results, and provide such information to the engineering staff of the Commission on a quarterly basis. As pointed out by the staff, such study and information provided should consist of the following: the number of 976 customers, the number of calls placed to 976 numbers, the net revenue impact, the amount remitted to 976 customers, the amount of uncollectible or disputed revenue, and the number and nature of complaints concerning 976 service. Thus, if this recommendation is adopted, the staff will essentially be monitoring this service on a quarterly basis, and may, should circumstances so warrant, initiate an inquiry to modify the tariff as needed.

In the ALJ's opinion not much is gained by adding the uncertainty of an "experimental" label; especially when such might tend to discourage participation given the sizeable initial investment required to be made by the information providers. According to Mr. Appleyard, PPI would need to make an initial investment in excess of $100,000 to enter the Texas market. He noted that while the experimental label may not make the service prohibitive (as would a tariff which automatically expired at the end of one year), the tariff approved by the Commission would have to satisfy PPI's best business judgment before it would enter the market. (Tr. at 70-72 and 75.) Although any approved tariff may be subsequently reviewed and modified by the Commission, experimental approval appears to carry a stronger likelihood that the service may be discontinued, than would otherwise be the case.

Finally, the ALJ would note that given the fact that at least one other major telephone company will be offering this service within the State of Texas, problems that arise with the service may be common to more than one utility. In this regard the Commission may find more beneficial a generic inquiry to investigate the matter, or possibly a rulemaking proceeding.

For the foregoing reasons the ALJ recommends final approval of SWB's Dial 976 tariff.

IV. Findings of Fact and Conclusions of Law

The ALJ recommends the Commission adopt the following Findings of Fact and Conclusions of Law:

A. Findings of Fact

1. On January 6, 1986, Southwestern Bell Telephone Company (SWB) filed an application for a new tariff offering which introduces Information Delivery Service (Dial 976 service).

2. Dial 976 service consists of a serving arrangement for sponsor use to provide a recorded announcement or a recorded interactive program service. A "sponsor" is an information provider wishing SWB to transport calls and bill callers on their behalf for each call completed to the sponsor's recorded announcement or program. Sponsors are customers of SWB.

3. SWB's application was initially assigned Tariff Filing No. T-9-6. On January 23, 1986, this filing was withdrawn as a tariff procedure and docketed. On January 24, 1986, the proposed effective date of February 10, 1986, was suspended for 150 days or until July 10, 1986. Subsequently, by a letter dated June 18, 1986, SWB voluntarily extended its effective date for 14 days to allow Commission consideration of this docket at the July 23, 1986, final order meeting.

4. SWB published notice of the proposed new tariff offering once a week for two consecutive weeks. Proof of publication of notice (printed in both English and Spanish) was filed on February 20, 1986.

5. Only one request to intervene was filed and granted in this docket, that being on behalf of Phone Programs, Inc. (PPI). However, two letters were filed by consumers and the American Coalition for Traditional Values (ACTV) expressing concern that approval of Dial 976 service might encourage the use of the telephone to provide pornographic or adult type messages.

6. The hearing on the merits was convened and concluded on May 19, 1986.

7. Initially, Dial 976 service will only be available in the Dallas, Fort Worth, Houston and San Antonio areas. The specific location of the central office(s) in each exchange which will be equipped to provide Dial 976 service will be determined by SWB.

8. Individuals who call a sponsor's 976 number are considered clients of the sponsor and SWB will bill and collect on behalf of the sponsor for each call from a client to the sponsor's 976 number. The sponsors' clients will also be billed any applicable tariff charges associated with the call to a 976 number, such as intraLATA toll charges.

9. Regarding interLATA calls to Dial 976 service, SWB cannot bill the sponsor's charge to the originating client's telephone account; and SWB will not bill the sponsor's charge to the interexchange carrier (IXC) absent the submission to SWB of a formal agreement between the sponsor and IXC regarding the handling of such charges.

10. SWB will issue a remittance check each month to each sponsor based upon the difference between the total charge for the billed calls and SWB's monthly rate for 976 sponsors, less charges for announcement lines, private line service and uncollectible billings.

11. Calls will not be permitted from the following types of services:

a. 4-party service
b. Services with Selective Class of Call Screening
c. SWB Coin/Coinless and Private Coin Service
d. Operator handled calls

12. SWB has been contacted by 199 potential sponsors regarding this service. The potential sponsors include: financial services and brokerage firms, book publishers, large and small newspapers, weather services, sports information services and other specialized information services.

13. Dial 976 is a competitive type service. The fact that a sponsor provides a particular announcement or program will not preclude another sponsor from providing the same or similar announcement.

14. With one exception--the service establishment charge--SWB's proposed rates are set to recover the incremental cost of providing Dial 976 service plus a contribution. The service establishment fee was set below incremental cost; the recovery of the difference between the incremental cost and the proposed charge will be accomplished through the contribution associated with the per call rate.

15. A comparison of the costs, the proposed rates and the resulting contribution for the proposed Dial 976 rate elements is set forth below:

	Monthly or Usage Cost	Proposed Monthly Rate or Rate Per Call	Contribution
Dial 976 Announcement Line	$22.52	$32.00	$9.48
Generic Rate-Per Call			
a. 60 seconds or less	.00247	.15	.148
b. Additional 30 seconds or fraction thereof	.00003	.03	.03
	Nonrecurring Costs	**Proposed Nonrecurring Charge**	
Service Establishment, per Announcement or Interactive Program	$2,446.37	$1,000.00	($1,446.37)
Sponsor Selected Price/ Variable Length Message	12.19	13.00	.81

16. Where a utility is providing an optional and discretionary service, and the profits earned from the service will provide a contribution to help offset the cost of basic local exchange service, given the ultimate goal of universal service, the public interest would appear best served by maximizing the profitability of the service.

17. For the reasons set forth in Finding of Fact No. 16, it is reasonable to determine the level of the contribution generated by discretionary services based on what the market will bear.

18. No evidence was presented showing that sponsors/information providers in the Texas market would be unwilling to pay the costs proposed by SWB and set forth in Finding of Fact No. 15.

19. Each sponsor determines the per message rate to be charged its clients, and may set such rate to recover its costs and desired profit.

20. SWB does not propose the disconnection of basic local exchange service for non-payment of 976 charges.

21. No other mechanism is currently proposed for handling 976 callers who continually refuse to pay the charges for calls made.

22. The possibility of blocking an individual's access to 976 numbers as an alternative to disconnection for non-payment of 976 charges has not been fully explored. While blocking is technologically feasible, the magnitude of the costs involved is unknown.

23. For the reasons set forth in Findings of Fact Nos. 20, 21, and 22, it is reasonable to require SWB to investigate the costs and possibility of blocking as an alternative to disconnection of local exchange service.

24. It is reasonable that SWB not be required to include in the 976 tariff a statement that basic local exchange service will not be disconnected for non-payment of 976 charges, for reasons set forth in Section III(B)(3) of the Examiner's Report.

25. It is reasonable to require SWB to include in the Dial 976 service tariff information regarding adjustments for incomplete calls, the one time adjustment for unauthorized calls, and the statement that billing disputes or complaints will be handled in accordance with P.U.C. SUBST. R. 23.45(h).

26. It is reasonable to require SWB to include in the Dial 976 service tariff the following provision related to adult entertainment type messages:

> 976 customers which offer sexually explicit messages shall restrict access to those messages by requiring callers which access the above described messages to:
>
> (a) input and authorized access or identification code before transmission of the subject message begins, where the 976 customer
>
> (1) has issued the code by mailing it to the caller after reasonably ascertaining through receipt of a written application that the caller is not under eighteen years of age; and
>
> (2) has established a procedure to cancel immediately the code of any person written telephonic or other notice to the 976 customer's business office that such code has been lost, stolen, or used by a person or persons under the age of eighteen, or that such code is no longer desired.
>
> Upon complaint, the company shall investigate compliance with the required restrictions. If the company is satisfied that the 976 provider is not in compliance with the tariff, notice shall be issued to the customer of such noncompliance; the notice shall inform the customer that compliance with the tariff must be accomplished within twenty (20) days of receipt of the notice, or 976 service shall be discontinued.

27. SWB plans to educate customers regarding the availability of Dial 976 service through billing inserts. Basically, the service and how it functions will be explained, as well as the fact that there are specific charges associated with each call made.

28. SWB should not be required to conduct a media campaign to promote Dial 976 service.

29. As a condition of service it is reasonable to require that each sponsor's advertisement or promotion include the following statement prominently displayed (no smaller than 12 point letter characters in publications) in printed advertisements and clearly communicated in any television or radio advertisements:

> A (the sponsor's selected price) charge will be billed for calling this (market location) telephone number in addition to applicable local or long distance charges.

Additionally, advertising directed towards children should include, and prominently display, the statement that parental consent should be obtained before a call is made.

30. Approval of a Dial 976 service tariff will allow the public access to a new, potentially beneficial, and technologically feasible service; and will provide SWB an opportunity to increase its revenues and provide a contribution towards the cost of basic local exchange service, without the occurrence of an adverse impact on the general body of ratepayers.

31. It is reasonable to require SWB to track the following data and provide this information to the Commission's Engineering Division on a quarterly basis for the 12 month period immediately following the implementation of Dial 976 service:

number of 976 customers
number of calls placed to 976 customers
net company revenue impact
amount of revenue remitted to 976 customers
amount of uncollectible undisputed charges
amount of disputed charges
number and nature of complaints concerning 976 service

B. Conclusions of Law

1. Southwestern Bell Telephone Company (SWB) is a dominant carrier as defined by Section 3(c)(2)(B) of the Public Utility Regulatory Act (PURA or the Act), Tex. Rev. Civ. Stat. Ann. art. 1446c (Vernon Supp. 1986), and is thus a telecommunications utility subject to this Commission's jurisdiction.

2. The Commission has jurisdiction over the matters considered herein pursuant to Sections 16(a), 18(a) and (b), and 37 and 38 of the Act.

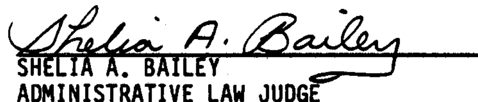
3. Notice of this application was properly published once each week for two consecutive weeks, pursuant to P.U.C. PROC. R. 21.25(a)(3).

4. The Dial 976 service rates proposed by SWB and set forth in Finding of Fact No. 15 are reasonable and not confiscatory for reasons set forth in Section III(B)(7) of the Examiner's Report and Findings of Fact Nos. 14, 16, 17, 18 and 19.

5. Until the policy and factual issues regarding disconnection of local exchange service for failure to pay 976 charges have been further investigated by the Commission, such disconnection shall not be allowed for failure to pay 976 charges.

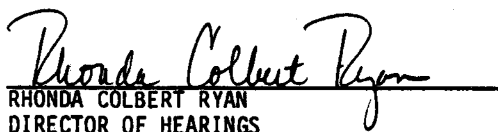
6. Approval of SWB's Dial 976 service tariff as modified in Findings of Fact Nos. 25, 26 and 29, is in the public interest for the reasons set forth in Finding of Fact No. 30.

Respectfully submitted,



SHELIA A. BAILEY
ADMINISTRATIVE LAW JUDGE

APPROVED on this the 11th day of July 1986.



RHONDA COLBERT RYAN
DIRECTOR OF HEARINGS

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DOCKET NO. 6689

APPLICATION OF SOUTHWESTERN BELL TELEPHONE COMPANY FOR A NEW TARIFF OFFERING DIAL 976 SERVICE	§	PUBLIC UTILITY COMMISSION OF TEXAS

ORDER

In public meeting at its offices in Austin, Texas, the Public Utility Commission of Texas finds that the above styled application was processed in accordance with applicable statutes by an administrative law judge who prepared and filed a report containing Findings of Fact and Conclusions of Law, which Examiner's Report is ADOPTED and made a part hereof. The Commission further issues the following Order:

1. Southwestern Bell Telephone Company's (SWB) application for authority to implement Dial 976 service is APPROVED as modified below.

2. SWB's Dial 976 tariff shall include information regarding adjustments for incomplete calls, the one time adjustment for unauthorized calls, and the statement that billing disputes will be handled in accordance with P.U.C. SUBST. R. 23.45(h).

3. As one of the conditions for service SWB's Dial 976 tariff shall include the requirement that all sponsor advertising directed towards children shall include, and prominently display (no smaller than 12 point letter characters in publications), the statement that parental consent should be obtained before a call is made.

4. As one of the conditions for service to providers of adult-type messages, SWB's Dial 976 tariff shall include the following language:

   976 customers which offer sexually explicit messages shall restrict access to those messages by requiring callers which access the above described messages to:

   (a) input and authorized access or identification code before transmission of the subject message begins, where the 976 customer

      (1) has issued the code by mailing it to the caller after reasonably ascertaining through receipt of a written application that the caller is not under eighteen years of age; and

      (2) has established a procedure to cancel immediately the code of any person written telephonic or other notice to the 976 customer's business office that such code has been lost, stolen, or used by a person or persons under the age of eighteen, or that such code is no longer desired.

Upon complaint, the company shall investigate compliance with the required restrictions. If the company is satisfied that the 976 provider is not in compliance with the tariff, notice shall be issued to the customer of such noncompliance; the notice shall inform the customer that compliance with the tariff must be accomplished within twenty (20) days of receipt of the notice, or 976 service shall be discontinued.

5. SWB shall track the following data and provide this information to the Commission's Engineering Division on a quarterly basis for the 12 month period immediately following the implementation of Dial 976 service:

   the number of 976 customers
   the number of calls placed to 976 customers
   the net company revenue impact
   the amount of revenue remitted to 976 customers
   the amount of uncollectible undisputed charges
   the amount disputed charges
   the number and nature of complaints concerning 976 service

6. For the reasons set forth in Findings of Fact Nos. 20, 21 and 22, and Conclusion of Law No. 5 of the Examiner's Report, SWB shall investigate the possibility of blocking an individual's access to Dial 976 service as an alternative to possible disconnection of local exchange service for non-payment of 976 charges.

7. Within 20 days after the date of this Order, SWB shall file with the Commission five copies of all pertinent tariff sheets revised to incorporate all the directives of this Order and shall serve one copy upon each party of record. No later than 10 days after the date of the tariff filing by SWB, parties shall file any objections to the tariff proposal and the general counsel shall file the staff's comments recommending approval or rejection of the individual sheets of the tariff proposal. No later than 15 days after the date of the tariff filing SWB, all parties and the general counsel shall file in writing any responses to the previously filed comments of other parties. The Hearings Division shall by letter approve or reject each tariff sheet, effective the date of the letter, based upon the materials submitted to the Commission under the procedure established herein. The tariff sheets shall be deemed approved and shall become effective upon expiration of 20 days after the date of filing, in the absence of written notification of approval or rejection by the Hearings Division. In the event that any sheets are rejected, SWB shall file proposed revisions of those sheets in accordance with the Hearings Division letter within 10 days after that letter, with the review procedures set out above again

to apply. Copies of all filing and of the Hearings Division letter(s) under this procedure shall be served on all parties of record and the general counsel.

SIGNED AT AUSTIN, TEXAS on this the 23rd day of July 1986.

PUBLIC UTILITY COMMISSION OF TEXAS

SIGNED:
PEGGY ROSSON

SIGNED:
DENNIS L. THOMAS

SIGNED:
JO CAMPBELL

ATTEST:

RHONDA COLBERT RYAN
SECRETARY OF THE COMMISSION

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COMPLAINT OF AMTEL CONSULTING COMPANY AGAINST SOUTHWESTERN BELL TELEPHONE COMPANY REGARDING BILLING FOR NEIMAN MARCUS OF DALLAS

DOCKET NO. 5580

October 31, 1984

Examiner's Report adopted. Request for refund of overcharges denied.

[1] COMPLAINTS AND DISPUTES - BILLING DISPUTES - CHARGING NON-TARIFFED RATES

P.U.C. SUBST. R. 23.45(f) does not prohibit an arm's length agreement to net out overbillings and underbillings on a complex business account, which is made in good faith and with the knowledge that the dollar difference is likely to be inconsequential in comparison with the volume of business transacted.

DOCKET NO. 5580

COMPLAINT OF AMTEL CONSULTING COMPANY AGAINST SOUTHWESTERN BELL TELEPHONE COMPANY REGARDING BILLING FOR NEIMAN MARCUS OF DALLAS	§	PUBLIC UTILITY COMMISSION OF TEXAS

EXAMINER'S REPORT

I. Procedural History

On January 17, 1984, Amtel Consulting Company (Amtel), agent for Neiman Marcus of Dallas, filed a complaint against Southwestern Bell Telephone Company (SWB) alleging that SWB made significant errors in past customer premises equipment billing for Neiman Marcus of Dallas and that SWB had failed to correct these deficiencies in violation of P.U.C. SUBST. R. 23.45(f). The Commission has jurisdiction over this complaint pursuant to Sections 16(a), 37, and 83 of the Public Utility Regulatory Act (the Act), Tex. Rev. Civ. Stat. Ann. art. 1446c (Supp. 1984).

A prehearing conference was conducted in this matter on February 23, 1984 by Hearings Examiner Thomas P. Groce, at which time appearances were made Mr. Albert Newman and Mr. Edward Mulcahy on behalf of Amtel, Ms. Barbara Hunt on behalf of SWB, and Ms. Debra Nikazy on behalf of the Commission staff and the public interest. No protestants or movants for intervention made appearance at the prehearing conference.

By Examiner's Order dated March 15, 1984, a schedule for discovery and the prefiling of testimony was adopted and the hearing on the merits was set for May 22, 1984.

The hearing on the merits was convened on May 22, 1984, with the undersigned examiner presiding. Appearances were made by Mr. Albert Newman and Mr. Edward Mulcahy on behalf of Amtel, Ms. Barbara Hunt on behalf of SWB, and Ms. Debra Nikazy on behalf of the Commission staff and the public interest. The direct testimony of staff witness Joan vom Eigen, the oral depositions of SWB witness Kathy Dvorak and SWB adverse witness John Davis and the direct testimony of SWB witness Peter Aube were admitted into evidence. Amtel presented no testimony in support of its complaint. All parties participated fully in cross-examination, after which the hearing was adjourned. The parties filed briefs in lieu of closing arguments.

II. Factual Summary

In order to fully grasp the issues in this proceeding it is first necessary to review the uncontested facts that form the basis of this dispute as revealed by the record. In late spring of 1981 Neiman Marcus of Dallas requested that SWB perform an inventory of the customer premises equipment and services provided by SWB to Neiman Marcus at its downtown Dallas retail store and its Dallas administrative facilities located at 2620 North Haskell. The physical inventory was completed on May 29 at the downtown location and on July 8 at the Haskell location. A preliminary review of the inventory results revealed that

overbilling errors and underbilling errors had occurred at both locations, but that the dollar amount of the underbilling errors exceeded the dollar amount of the overbilling errors on a monthly basis.

Prior to a final calculation of the net overbilling and net underbilling, Kathy Dvorak, marketing representative for SWB, advised John Davis, Telecommunications Manager for Neiman Marcus, of the respective monthly dollar amounts of overbilling and underbilling. Ms. Dvorak, in good faith, represented to Mr. Davis that, if the inventory analysis were completed, it might be found that Neiman Marcus owed SWB money or it might be found that SWB owed Neiman Marcus money. Ms. Dvorak further advised Mr. Davis that the best thing to do would be to correct the monthly billings at both locations and just move forward because the net difference between the underbillings and overbillings appeared to be very small.

Mr. Davis decided to settle the net difference by treating it as a "wash", correcting the billing records and going forward, based upon his understanding "that it (the net difference) was so small that it didn't really make a large difference to me one way or the other, and that I thought we ought to just correct the records and get on with it because I certainly wanted us to be billed for what we had." Therefore, based upon Mr. Davis' business decision and Kathy Dvorak's recommendation, Mr. Davis signed two letters addressed to SWB settling the net difference on both store locations. Both of those letters indicated that Neiman Marcus expected no adjustments nor backbilling. Based upon the letter from Mr. Davis stating that Neiman Marcus expected no adjustments or backbilling to be made, SWB did no further analysis of the Neiman Marcus inventory. A full analysis requires a determination of the date of installation, a determination of the historical rates on each piece of equipment, a determination of tax changes, and a determination of the actual amounts billed for each item for prior years, back to the date of installation.

In March of 1982, Amtel Consulting Company approached Neiman Marcus concerning Amtel's inventory services. Neiman Marcus employed Amtel to perform a second inventory at the downtown and Haskell locations. Amtel failed to present any evidence revealing a discrepancy between its inventory and SWB's inventory. In January of 1983, Amtel requested, on behalf of Neiman Marcus, that SWB determine the exact amount of the credit or debit resulting from SWB's 1981 inventory. In compliance with that request, Southwestern Bell made the necessary calculations and determined that the combined overbilling for both locations was $20,341.68, and that the combined underbilling at both locations was $16,856.40, resulting in a net credit to Neiman Marcus of $3,485.28. For purposes of calculating the total amount of underbilling, Southwestern Bell went back six months from November 22, 1981, being the date that Neiman Marcus' monthly billing was corrected as a result of the two letters received by Southwestern Bell from John Davis. The credit was a result of the operation of P.U.C. SUBST. R. 23.45(f) requiring correction of overbilling for the full

period of the overbilling, but permitting recovery of underbilling by the utility only for a six month period. Based upon the final inventory results, Southwestern Bell indicated to Amtel in September of 1983 that it was willing to credit $3,485.25 to the Neiman Marcus account. This offer was rejected by Amtel.

III. Opinion

It is Amtel's position that the total overbilled amount of $20,341.68 should be applied to the Neiman Marcus accounts, without offset for underbilling. As justification for this position, Amtel relies upon the language of P.U.C. SUBST. R. 052.02.04.046(a)(1)(c), which is an earlier version of the current P.U.C. SUBST. R. 23.45(f) which was in effect at the time this dispute initially arose. The text of that Substantive Rule is as follows:

> If billings for telephone utility services are found to differ from the utility's lawful rates for the services being purchased by the customer, a billing adjustment shall be calculated by the utility. If the customer is due a refund, an adjustment shall be made for the entire period of overcharge. If the customer was undercharged, the utility may backbill the customer for a period not to exceed six months from the date the utility initially notifies the customer of the amount of undercharge and the total additional amount that will be due. Said amount shall be added to the next regular billing. If the underbilling is $25 or more, the company shall offer to such customer a deferred payment plan option, for the same length of time as that of the underbilling.

Amtel contends that, as the final adjustments resulting from the 1981 inventory were not calculated and provided to Neiman Marcus until February 14, 1983 for the downtown store, and August 12, 1982, for the Haskell location, those are the respective dates which should be used in calculating backward in time the six month underbilling periods. As the billing for the Neiman Marcus accounts have been correct since November 22, 1981, Amtel concludes that no underbillings exist for the six month period prior to the dates the final calculations were made, with which to offset the total amount of overbilling. Amtel relies upon the language in the substantive rule which requires that the six month underbilling period be calculated "from the date the utility initially notifies the customer of the amount of undercharge".

It is SWB's position that if the overbillings and underbillings revealed by the inventory had been fully calculated at the time the monthly billings were corrected, Neiman Marcus would have been entitled to a credit in the amount of $3,485.28, but that in reliance upon the letter agreement that no credit was sought, SWB corrected the records and did not calculate or apply any credit. SWB contends that the letter agreements constituted a valid waiver of any credit owed but should the Commission determine that a credit is due, Amtel and Neiman

Marcus should not be permitted to stretch that credit to $20,341.68 by whipsawing Southwestern Bell with the time periods for calculating the underbilling offset.

In the examiner's opinion, this dispute can be boiled down to two straightforward issues. First, did the letters from Neiman Marcus to SWB, waiving retroactive billing adjustments and requesting prospective correction of Neiman Marcus' monthly billings, constitute a reasonable and proper settlement of billing errors? Second, if the letters constituted a proper settlement, could Neiman Marcus or its agent later repudiate the terms of the settlement?

In response to the first issue, the examiner is of the opinion that Neiman Marcus' request that billing adjustment be waived and that the monthly billings be corrected on a prospective basis, is reasonable, proper and is not prohibited by the Commission's substantive rule on overbilling and underbilling. The deposition of John Davis, Neiman Marcus' Telecommunications Manager, reveals that Neiman Marcus did not feel that the amount of money involved was sufficient to warrant the expenditure of time necessary to pursue the matter. This appears to be a legitimate cost/benefit determination. Ms. Dvorak, SWB's marketing representative, presented Mr. Davis with the dollar amounts of the overbilling and underbilling on a monthly basis. Mr. Davis stated that Ms. Dvorak acted in good faith. Further, Mr. Davis was aware that the final analysis of the inventory had not been completed and that the difference between the underbilling and overbilling could favor either party. Mr. Davis testified that he was eager to dispose of the matter and get on with other business. It appears to the examiner that Mr. Davis' decision was reasonable for both Neiman Marcus and SWB.

Amtel infers in its pleadings and brief that the Commission's substantive rule on overbilling and underbilling prohibits a settlement, based upon the following language: ". . . a billing adjustment shall be calculated by the utility". The examiner does not construe this language as prohibiting a settlement. The Neiman Marcus accounts are large. Telecommunication equipment at the two locations is removed, installed and rearranged with some frequency. The inventory revealed that many pieces of equipment found in use were not reflected in the billing records and that many pieces of equipment reflected on the billing records were not located. SWB witness Peter Aube, a SWB manager supervising billing and collections for SWB business customers, testified that SWB technicians on the premises often do work upon verbal request, without a written order, in order to facilitate the necessity of keeping Neiman Marcus' telephone system flexible enough to suit its changing needs, but that this arrangement makes it very difficult for SWB to keep its billing correct due to a large potential for human error. A technician may forget to write up an order already completed or may write up the order incorrectly. Over a period of time, a number of errors can accumulate.

In order to compute an adjustment, SWB must determine the date of installation, determine the historical rates on each item of equipment, determine tax changes, and determine the actual amounts billed for each item for prior periods, back to the date of installation. As a consequence, it takes a substantial amount of time to reconcile overbillings and underbillings revealed from a complex business account inventory. Both Neiman Marcus and SWB were aware that the net difference in overbillings and underbillings on a monthly basis was small. It appears to be imminently reasonable for Neiman Marcus and SWB to have entered into a settlement. A settlement, if it appears to be beneficial to both parties from a cost standpoint, should not be discouraged. In the examiner's opinion, the Commission substantive rule on overbilling and underbilling is not cast in stone. A sophisticated telephone customer should be permitted to make such a business decision and SWB should be permitted to agree to such a decision if it appears reasonable to do so.

Although the Commission staff is not in agreement with Amtel's position, staff witness Joan vom Eigen concurs with Amtel insofar as Amtel asserts that settlement of overbilling and underbilling should not be permitted. Under Ms. vom Eigen's rationale, no discretion on rate application is allowable under our rules, and consequently a utility should always charge tariffed rates for all equipment and systems to all customers. However, the examiner believes that acceptance of a settlement of overbillings and underbillings by SWB does not reflect an attempt to deviate from lawful tariffed rates, but rather constitutes a recognition of the fact that the time factor for billing the tariffed rates can, in many cases, never be pinned down with total certainty and the dollar amount of any adjustment must therefore be to some extent a disputed figure. This type of situation lends itself to a settlement.

[1] The examiner concludes that an arm's length agreement to net out overbillings and underbillings on a complex business account, which is made in good faith and with the knowledge that the dollar difference is likely to be inconsequential in comparison with the volume of business transacted, is not prohibited by the terms of P.U.C. SUBST. R. 23.45(f), and the examiner would urge the Commission to concur in this conclusion.

In response to the second issue, the examiner is of the opinion that the letters from Neiman Marcus to SWB, waiving retroactive billing adjustments and requesting prospective correction of monthly billings are binding and are not subject to later repudiation by either Neiman Marcus or its agent. This result flows directly from the examiner's conclusion that the settlement of the overbillings and underbillings was reasonable and proper and did not contravene the underlying intent of P.U.C. SUBST. R. 23.45(f). It appears to the examiner to be self evident that when a sophisticated business customer, such as Neiman Marcus, enters into a settlement of a billing dispute, it should be held to the terms of that settlement. Neiman Marcus' agreement to waive final calculation of a billing adjustment is not an adhesion contract. Neiman Marcus had a choice

of courses of action to take and chose the course it deemed appropriate based upon its business judgment. The evidence indicates that SWB did not engage in any misrepresentations and did not act in bad faith. Neiman Marcus certainly could not have interpreted its letters to SWB as saying anything other than what they clearly say on their face, to wit: ". . . I expect no adjustments nor backbilling and anticipate that a records order will be issued to correct the error in current billing. As we discussed, I anticipate the appropriate change will be reflected in the November bill." SWB acted in accordance with the letters. It seems clear that there was thus both an offer and acceptance, constituting a binding contract. There simply is no basis in the record for a finding that the agreement is subject to repudiation, absent a finding that the Commission's substantive rules prohibit the parties from entering into the agreement ab initio. Having concluded that Neiman Marcus cannot repudiate its letter agreement, it follows that Amtel as an agent for Neiman Marcus cannot, through the fact of its agency, place itself in a better position than that of Neiman Marcus. The law of agency is clear on this point.

In summary, the examiner finds that the letter agreements are reasonable and not inconsistent with P.U.C. SUBST. R. 23.45(f), that they are binding on both Neiman Marcus and Amtel, and that the complaint is without merit. Therefore the relief requested by Amtel should in every respect be denied. The examiner respectfully urges the Commission to join in these findings. However, the examiner will address two other issues that become relevant should the Commission decide that the examiner's conclusions are erroneous. First, whether or not SWB's methodology for calculating the amount of overbillings and underbillings is appropriate. Second, the appropriate time frame to be used for calculation of the amount of underbillings utilized to offset the overbillings.

Amtel has alleged in its brief that SWB arbitrarily took all underbilled items back six months with no documentation whatsoever for the purpose of calculating the allowable six months underbilling offset. However, Amtel never offered any evidence in support of its contention. SWB was the only party which presented testimony regarding the propriety of the methodology it used to calculate the amount of underbilling. The underbilling in this matter occurred as a result of telephone equipment revealed by the inventory to be in place and in use but not reflected in SWB's billing records. In these instances it is difficult if not impossible to determine when an unbilled piece of equipment was installed. The equipment may have been in place for a period of months or a period of years. Consequently, SWB has adopted quidelines for the determination of underbilled amounts. Mr. Peter Aube testified at the hearing that the SWB customer accompanies the SWB representative during the physical inventory. During the inventory, if an unbilled item is found, the SWB representative asks the customer whether he knows how long the particular item has been in use. If the customer indicates that the equipment has been in place less than six months, SWB uses the date indicated by the customer. If the customer does not know, SWB assumes that the piece of equipment has been in place for six months,

provided that the date of installation cannot be reasonably determined from back-up documentation. For instance, Mr. Aube testified that if a key system was installed on a specific date and the unbilled item in question is a key set, one can infer that the key set should go along with the key system and a date of installation can thereby be imputed. It appears to the examiner that one can never obtain a clear-cut resolution of date of installation for unbilled items and with that in mind, SWB's methodology for determining the amount of underbilling is reasonable.

Overbilling occurs in those instances where a piece of equipment is reflected on the customer bill, but is not found during the inventory process. In those instances, it cannot be determined whether the equipment was stolen or misplaced by employees or customers, or whether the equipment was never installed. SWB counts all missing equipment as being overbilled from the date of installation as revealed by SWB's records. Again, this appears to the examiner to be a reasonable method of determining the amount of overbilling. This also gives the customer the complete benefit of the doubt. As Amtel failed to present any evidence regarding SWB's methodology for determining amounts overbilled and underbilled, and as the methodology appears reasonable, the examiner concludes that the practices of SWB in this regard are appropriate and acceptable. Although a case could be made that SWB's premises equipment records are somewhat lacking in accuracy, it is foreseeable that errors can occur in the equipment records for large business accounts where equipment is removed, installed and rearranged frequently. As the General Counsel points out in her brief, the types of customer premises equipment involved in this dispute are difficult to track. The equipment is easily moved and substituted for other equipment, and individual pieces may not be serially numbered or otherwise distinguishable. Also, the examiner would note in passing that since SWB transferred its customer premises equipment to a subsidary of AT&T on January 1, 1984, complaints of this nature are unlikely to recur.

Having addressed the issue of whether the methodology used to calculate overbilled and underbilled amounts is appropriate, the question arises of what is the appropriate time frame to be used for calculation of the six months of underbillings utilized to offset overbillings. When asked by Amtel to complete the inventory analysis and determine the total amount of overbillings and underbillings, SWB utilized the six month period prior to November 22, 1981,(the date Neiman Marcus' billing was corrected), to calculate the total underbilled amount. SWB determined that Neiman Marcus was underbilled in the amount of $16,856.40 for the six month period. The total amount of overbilling, which is not limited to six months, was $20,341.68, leaving a net credit to Neiman Marcus of $3,485.28. Amtel has alleged that Neiman Marcus should be credited with the total overbilled amount without offset for underbilling, based upon Amtel's interpretation of the Commission's substantive rule on overbilling and underbilling. The version of P.U.C. SUBST. R. 23.45(f) then in effect (052.02.04.046(a)(1)(c)) provided that ". . . . if the customer was undercharged,

the utility may backbill the customer for a period not to exceed six (6) months from the date the utility initially notifies the customer of the amount of undercharge . . .". Amtel reasons that Neiman Marcus was not notified of the amounts of the undercharge until February 14, 1983, for the downtown location and August 12, 1982 for the Haskell location due to the fact that the inventory analyses had not been completed until a request had been made by Amtel. Amtel further reasons that, as Neiman Marcus' billings were corrected in November of 1981 and have been correct since then, SWB should use the six months prior to the February 14, 1983 and August 12, 1982 dates to calculate the underbilled amounts and that no underbilling occurred during those time frames. Therefore, Amtel concludes that Neiman Marcus is due a credit of $20,341.68, plus accrued interest.

In response, SWB asserts that even if the Commission finds that the letter agreements are not legally sufficient to prevent a later repudiation by Neiman Marcus, the doctrine of promissory estoppel bars Neiman Marcus or its agent (promisor) from seeking credit from SWB (promisee) for the total amount of overbilling without offset for underbilling. SWB cites the Supreme Court of Texas opinion in Wheeler v. White, 398 S.W.2d. 93 (Tex. 1965) wherein the court holds that," all that is required to achieve justice is to put the promisee in the position he would have been in had he not acted in reliance upon the promise."

SWB asserts that if the letter agreements are not binding, SWB should be put in the position it would have been in if it had not acted in reliance upon the representation of Neiman Marcus that no credit would be sought. When that is done, the only credit due Neiman Marcus is the $3,485.28 that would have been due at the time that Neiman Marcus agreed to forego the accounting analysis in order to correct the billing expeditiously. Further, SWB argues that promissory estoppel precludes the payment of any interest on the $3,485.28. The staff witness in this proceeding has taken the position that interest at the statutory rate of six percent should apply. The examiner believes that SWB's arguments concerning promissory estoppel are persuasive and correct, both as to the appropriate amount of the credit and the propriety of applying interest to the credit. Even without invocation of the doctrine of promissory estoppel, the examiner is of the opinion that Amtel's contention as to the applicable time frames for determining underbilling is unreasonable on its face, in light of the evidence developed in this proceeding.

Should the Commission disagree with the examiner's recommendation that all relief requested by Amtel be denied, the examiner would alternatively urge the Commission to find that SWB is obligated to credit Neiman Marcus with no more than the $3,485.38 credit which was initially waived by Neiman Marcus, and that the credit should be made without interest.

IV. Findings of Fact and Conclusions of Law

The examiner recommends that the Commission adopt the following Findings of Fact and Conclusions of Law.

A. Findings of Fact

1. On January 17, 1984, Amtel Consulting Company (Amtel), as agent for Neiman Marcus of Dallas, filed a complaint against Southwestern Bell Telephone Company, (SWB) alledging that SWB violated P.U.C. SUBST. R. 23.45(f) by failing to correct errors in past customer premises equipment billing.

2. A hearing on the merits was conducted in this matter on May 22, 1984.

3. Customer premises equipment inventories were performed by SWB at two Neiman Marcus locations in Dallas, in late spring and early summer of 1981, at Neiman Marcus' request.

4. Preliminary review of the inventory results revealed that overbilling and underbilling errors had occured at both locations and that the dollar amount of the underbilling errors exceeded the dollar amount of the overbilling errors on a monthly basis.

5. SWB representative Kathy Dvorak acted in good faith in advising Neiman Marcus Telecommunications Manager John Davis that if the inventory analysis were completed, it might be found that Neiman Marcus owed SWB money or that SWB owed Neiman Marcus money. Therefore, the best thing to do would be to forego the analysis and correct the monthly billings and move forward.

6. John Davis decided to settle the net difference between the overbillings and underbillings by treating it as a "wash", based upon Ms. Dvorak's recommendation and his business judgment.

7. Mr. Davis signed two letters addressed to SWB stating that Neiman Marcus expected no adjustment or backbilling to be made, and requesting correction of the monthly billings on a prospective basis.

8. The letters from John Davis to SWB constitute a binding settlement of a billing dispute.

9. SWB did not complete the analysis of the Neiman Marcus inventories, in reliance upon the letter agreements from John Davis, until Amtel requested a complete analysis in January of 1983.

10. Amtel conducted premise inventories of the two Neiman Marcus locations in 1982.

11. There is no evidence of record revealing any discrepancies between Amtel's inventory and SWB's inventory.

12. The final analysis of SWB's inventories revealed that the combined overbilling for both locations was $20,341.68 and the combined underbilling at both locations was $16,856.40, resulting in a net credit to Neiman Marcus of $3,485.28.

13. The credit resulted from the operation of P.U.C. SUBST. R. 23.45(f) requiring correction of overbilling for the full period of overbilling, but permitting recovery of underbilling by the utility only for a six month period.

14. Neiman Marcus cannot now, by repudiating the terms of the letter agreements, collect a credit which it waived in 1981.

15. The methodologies used by SWB to determine the date of equipment installation for purposes of calculating underbilling and overbilling are reasonable and appropriate.

16. It was reasonable and appropriate for SWB to calculate underbilling at the two Neiman Marcus locations based upon the six month period prior to November 22, 1981.

17. No credit is due Neiman Marcus from SWB.

B. Conclusions of Law

1. Southwestern Bell Telephone Company is a public utility as defined by Section 3(c)(2)(A) of the Public Utility Regulatory Act (the Act), Tex. Rev. Civ. Stat. Ann. art. 1446c (Supp. 1984).

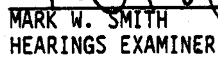
2. The Commission has jurisdiction over this complaint pursuant to Sections 16(a), 37 and 83 of the Act.

3. The letters from John Davis to SWB constitute a binding settlement of a billing dispute.

4. P.U.C. SUBST. R. 23.45(f) does not prohibit an arm's length agreement to net out overbillings and underbillings on a complex business account which is

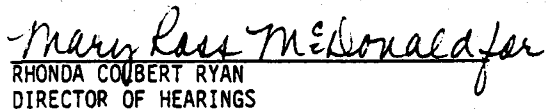
made in good faith and with the knowledge that the dollar difference is likely to be inconsequential in comparison with the volume of business transacted.

PUBLIC UTILITY COMMISSION OF TEXAS



MARK W. SMITH
HEARINGS EXAMINER

APPROVED on this the 17th day of October, 1984.



RHONDA COLBERT RYAN
DIRECTOR OF HEARINGS

nsh

DOCKET NO. 5580

COMPLAINT OF AMTEL CONSULTING COMPANY AGAINST SOUTHWESTERN BELL TELEPHONE COMPANY REGARDING BILLING FOR NEIMAN MARCUS OF DALLAS	PUBLIC UTILITY COMMISSION OF TEXAS

ORDER

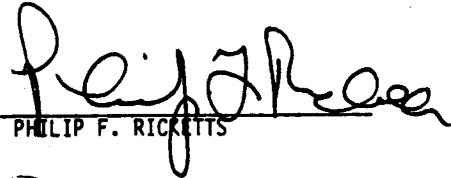
In a public meeting at its offices in Austin, Texas, the Public Utility Commission of Texas finds that the above styled and numbered case was processed in accordance with applicable statutes by an examiner who prepared and filed a report, containing Findings of Fact and Conclusions of Law, which Examiner's Report, Findings of Fact and Conclusions of Law are ADOPTED and made a part hereof. The Commission further issues the following Order:

1. The relief requested by Amtel Consulting Company is hereby DENIED in its entirety.

2. All other motions and requests for relief not granted herein are hereby DENIED for want of merit.

3. This Order is deemed to be effective upon the date of signing.

PUBLIC UTILITY COMMISSION OF TEXAS

SIGNED: 
PHILIP F. RICKETTS

SIGNED:
PEGGY ROSSON

SIGNED:
DENNIS THOMAS

ATTEST:

RHONDA COLBERT RYAN
SECRETARY OF THE COMMISSION

nsh 10/31/84

APPLICATION OF GULF STATES UTILITIES COMPANY FOR APPROVAL OF A JOINT VENTURE COGENERATION PROJECT AND TREATMENT OF REVENUES	I I I I	DOCKET NO. 7147

March 21, 1988

Gulf States Utilities Company (GSU) request for approval of a joint venture, as requested, was denied. Motion for Rehearing was denied by operation of law.

[1] RATEMAKING - COST OF SERVICE - ACCOUNTING ADJUSTMENTS

Eighty-three percent of the fixed asset payment to the joint venture should be treated as other electric utility income.

[2] PROCEDURE - JURISDICTION - COGENERATION

Because the joint venture is a qualifying facility as that term is defined under the Public Utility Regulatory Policies Act, the Commission has no jurisdiction to regulate its rates.

[3] PROCEDURE - JURISDICTION - COGENERATION

GSU is not required to obtain Commission approval of the transfer of Nelson Units 1 and 2 prior to its entering into a contract with the joint venture.

[4] COGENERATION - RATES FOR PURCHASES FROM QUALIFYING FACILITIES

It is not in the public interest for GSU's Texas ratepayers to pay in excess of GSU's avoided cost for purchased power from a qualifying cogeneration project.

DOCKET NO. 7147

APPLICATION OF GULF STATES UTILITIES COMPANY FOR APPROVAL OF A JOINT VENTURE COGENERATION PROJECT AND TREATMENT OF REVENUES	§	PUBLIC UTILITY COMMISSION OF TEXAS

EXAMINER'S REPORT

I. Procedural History

On October 17, 1986, Gulf States Utilities Company (GSU) filed its Application for Approval of a Joint Venture Cogeneration Project (Venture) and Treatment of Revenues. GSU requested Commission approval of its participation in the Venture, a prerequisite under the terms of the contract for the operation of the cogeneration plant by GSU and several of its Louisiana industrial customers.

Motions to Intervene of the following parties were granted: Office of Public Utility Counsel (OPC), Texas State Agencies (TSA), North Star Steel Texas, Inc. (North Star), and Texas Industrial Energy Consumers (TIEC). TSA subsequently withdrew its intervention on June 2, 1987. On January 26, 1987, Joseph C. Howell, Business Manager of the International Brotherhood of Electrical Workers, AFL-CIO-CLC, Local 2286 located in Beaumont, Texas, filed a letter in support of the Venture.

On January 23, 1987, OPC filed a motion to consolidate the instant case with Docket No. 7195, GSU's Application for Authority to Change Rates, GSU's current rate request. By joint order dated February 4, 1987, the examiners in Docket Nos. 7147 and 7195 denied OPC's request. On February 10, 1987, OPC filed its appeal of the examiners' joint order. The Commission declined to hear this appeal.

On February 3, 1987, the administrative law judge (ALJ) issued an order outlining the Commission's jurisdiction to hear the request, the scope of the proceedings, and the notice to be provided in this case. On February 5, 1987, OPC filed its appeal of the examiner's order. The Commission declined to hear OPC's appeal.

On March 26, 1987, a prehearing conference was convened to establish a procedural schedule in this case. Appearances were entered by GSU, TSA, OPC, and the Commission's general counsel. At the prehearing conference, Mr. Clements, attorney for GSU, informed the ALJ that public notice had been completed and that GSU would file publisher's affidavits as soon as they became available. Mr. Clements further advised the ALJ that the Federal Energy Regulatory Commission (FERC) had denied the application for qualifying facility (QF) status filed by the Venture. Mr. Clements indicated that the Joint Venture would file a Motion for Rehearing or seek alternatives to amend the filing at the FERC. He stated that the denial of the QF application is based upon the gas operation of the QF and that the coke operation poses no problem in certification. Pursuant to the ALJ's request, GSU agreed that it would determine within approximately two months from the date of the prehearing conference the course of action it intended to take regarding its application with the Commission.

On May 1, 1987, GSU filed a letter indicating that FERC would rule upon GSU's Motion for Rehearing on May 13, 1987. Under the ALJ's March 12, 1987 prehearing order which established the procedural schedule for this case, GSU was required to prefile its testimony on May 8, 1987. In order that GSU not be required to file testimony until after the FERC ruled on its Motion for Rehearing, GSU requested that the prefiling of its testimony be re-established to May 25th or 26th and that all corresponding dates be adjusted accordingly. No party filed any objections to GSU's motion. Pursuant to an order dated May 8, 1987, the examiner modified the procedural schedule established under her March 12, 1987 order.

On May 21, 1987, the FERC granted GSU's Motion for Rehearing and approved the QF's request for QF status contingent upon the Venture's completion of certain milestones in reaching the coke operation of the Venture. (Examiner's Attachment No. 1.)

On May 29, 1987, the ALJ issued an order ruling on a discovery dispute regarding the General Counsel's Fifth Request for Information. GSU stated that

the requested information contained confidential information. After conducting an *in camera* review, the examiner found that portions of the documents were not properly subject to non-disclosure and thus were ordered to be fully disclosed. The information subject to non-disclosure due to its confidential nature was made available to the parties under a protective order.

The hearing on the merits was convened on August 17, 1987, and subsequently adjourned on the same day after the taking of evidence. GSU, OPC, and the Commission's general counsel filed briefs on September 9, 1987, and reply briefs on September 16, 1987. Late-filed GSU Exhibit No. 9, by order dated December 1, 1987, was admitted into the record.

GSU published notice of its application once each week for two consecutive weeks in newspapers of general circulation in each county containing territory affected by its application.

Due to time constraints and in the interest of brevity, not every point raised by a participant in this case has been expressly discussed in the Examiner's Report. The ALJ has read the entire record and considered every issue raised. To the extent that arguments have not been addressed in this Report, they are rejected for lack of merit.

II. Jurisdiction

The Commission has jurisdiction over the matters presented in this case pursuant to Sections 16(a) and (g) and 63 of the Public Utility Regulatory Act (PURA or the Act), Tex. Rev. Civ. Stat. Ann. art. 1446c (Vernon Supp. 1987) and P.U.C. SUBST. Rs. 23.23 and 23.66.

III. Description of Request

GSU stated in its application that the generating units involved, Nelson Units 1 and 2, which are located in Louisiana and which will be converted into a

QF, are used in GSU's integrated two-state system. GSU and several Louisiana-based industrial companies--Conoco, Inc. (Conoco), Citgo Petroleum Corporation (Citgo), and Vista Chemical Company (Vista) and certain of their subsidiaries--desire to enter into the Nelson Industrial Steam Company Project (NISC or Venture). GSU would retain a one percent interest in the Venture. The remaining 99 percent would be held by the industrial participants. The execution of the proposed Venture contract, which was attached to GSU's application in this case, is contingent upon approval by this Commission and other regulatory bodies.

For a sum certain outlined under the terms of the proposed Venture contract, GSU will convey ownership of Nelson Units 1 and 2, together with necessary land and supporting facilities at Nelson Station in Lake Charles, Louisiana, to the Venture. The industrial participants would then construct two fluidized bed combustors to replace the existing natural gas-fired boilers which provide steam to Nelson Units 1 and 2. The converted units would consume petroleum coke furnished by the industrial participants to produce electric power which GSU will purchase, and steam which Vista and Conoco will purchase. However, in the first five years of operation during the design and construction of the coke facilities, the QF would use natural gas as a boiler fuel. Conoco, Citgo, and Vista and certain of their subsidiaries will continue to purchase electric power from GSU in accordance with contractual formulary rates reflected in the proposed Venture contract.

GSU requested the following specific relief from this Commission:

1. Approval of the transfer of Nelson Units 1 and 2;

2. Approval of GSU's proposed revenue treatment of the sale of Nelson Units 1 and 2;

3. Approval of proposed regulatory treatment of operations and maintenance expense;

4. Approval of the purchased power costs as reconcilable fuel;

5. Approval of the standby reservation fee; and

6. Approval of the terms of the contract.

GSU stated that in its current rate case, Docket No. 7195, it has made its filing in that case as if all of its requested relief in this case had been granted.

IV. Opinion

The case presented before the Commission is one of first impression. The professed reason for GSU's involvement in the Venture is to prevent loss of Louisiana industrial load from its system. GSU indicated that it has lost approximately 430 megawatts (MW) of industrial electric load to cogeneration. The industrial participants to the Venture have a total load of approximately 200 MW. It is this load which GSU wishes to retain on its system by its participation in the Venture.

GSU indicated that initially two of GSU's largest industrial customers approached GSU in 1984 regarding their plans to build a cogeneration facility. In response, GSU proposed an alternative which would consist of transferring Nelson Units 1 and 2 to the Venture for retrofit into a QF. Upon extensive studies, the parties negotiated a detailed agreement based upon GSU's proposal. (GSU Exhibit No. 1A.) The agreement sets forth the terms of the formation and operation of the Venture, NISC's payments for the assets of Nelson Units 1 and 2, the payments made by GSU to the Venture for purchased power, and the payments by the Venture for standby power supplied by GSU.

A. Approval of Transfer of Nelson Units 1 and 2

Pursuant to Section 63 of the (PURA) a public utility selling any plant as an operating unit or system in Texas for a total consideration in excess of

$100,000 must report such transaction to the Commission within a reasonable amount of time.

Although the property subject to sale in this case is located outside of the state of Texas, this Commission has determined in previous cases that the Commission has authority over out-of-state facilities. Docket No. 478, Application of El Paso Electric Company for a Certificate of Convenience and Necessity for Copper Station and Out-of-State Facilities (unpublished, August 29, 1977) and Docket No. 857, Application of Gulf States Utilities Company for a Certificate of Convenience and Necessity for Certain Out-of-State Facilities in Louisiana, 3 P.U.C. BULL. 1077 (March 21, 1978). Although these orders addressed certification of out-of-state facilities, the ALJ believes that, in like manner, the Commission can exert authority over out-of-state facilities which fall under Section 63 of the Act.

The Commission must determine whether the transfer of assets is consistent with the public interest. In this case, GSU not only requests approval of the transfer of assets but further requests approval of its treatment of the revenues and fuel expenses associated with the transfer of the property and the operation of the QF. The ALJ notes that no party has argued that the transfer of assets is not in the public interest. The controversy arises regarding GSU's treatment of the revenues it will receive from the sale of Nelson Units 1 and 2, and of the fuel expenses associated with the energy to be generated by the QF which GSU is required to purchase in toto under the terms of the Venture agreement.

The public interest determination, and thus approval or disapproval of the transfer of assets, rests upon whether the type of regulatory treatment GSU seeks regarding the revenues and expenses resulting from the transfer is in the public interest. For that reason, the ALJ will address the underlying issues prior to recommending approval or disapproval of the transfer under Section 63 of the Act. The ALJ further notes that GSU has not requested any amendment to its certificate of convenience and necessity as a result of the sale of its assets.

B. Approval of GSU's Proposed Revenue Treatment of the Sale of Nelson Units 1 and 2

[1] OPC witness Dr. Steven Andersen testified that GSU requested that the annual payment of $6.35 million per year, which GSU will receive from NISC for the Nelson units over a 20 year period, be booked below the line as non-utility income. Dr. Andersen discounted the payment at 10 percent to obtain the present value of the payments of approximately $51 million. As of May 31, 1987, the net original cost of Nelson Units 1 and 2 was approximately $6 million. The sale therefore will result, according to Dr. Andersen, in a capital gain to GSU of approximately $45 million. Both Dr. Andersen and staff accountant Paul Bellon testified that as of May 31, 1987, Nelson Units 1 and 2 were approximately 83 percent depreciated. Dr. Andersen testified that because 83 percent of the original cost of these units had been recovered from the ratepayers, no less than 83 percent of any gain realized from the sale of these units should accrue to the ratepayers by booking 83 percent of the annual capital charge, (i.e. the fixed asset payment) above rather than below the line. (Entries above the line impact the ratepayers, while entries below the line do not.) Similarly, Mr. Bellon testified that because the Company and the shareholders have recovered approximately 83 percent of the costs related to Nelson Units 1 and 2, the ratepayers should receive 83 percent of the fixed asset payment GSU receives from the sale of the units. In addition, Dr. Andersen recommended that the remaining 17 percent of gain be split equally between GSU's ratepayers and shareholders, with the ratepayers' portion being booked above the line.

Regarding the staff's and OPC's recommendation as to calculating the gain based on the plant's depreciable status, GSU argued that adoption of the staff's and OPC's proposal in this regard would constitute permitting the unamortized portion of the gain to be included in GSU's rate base. The ALJ is not persuaded by GSU's argument. First, although the ALJ was not provided a schedule by either OPC or the staff as to the accounting treatment for the gain, it appears from the testimony that 83 percent of the yearly fixed asset payment, or 83 percent of $6.35 million, would be booked above the line as a gain and as a

benefit to the ratepayers. The ALJ is not convinced that this would cause inclusion of unamortized amounts in GSU's rate base as alleged by GSU.

Second, in Docket No. 6890, Application of Central Power and Light Company and the Public Utilities Board of the City of Brownsville for Approval of the Sale and Purchase of an Interest in Oklaunion Unit No. 1, (unpublished, August 19, 1986) the gain resulting from the sale of Oklaunion plant was split between Central Power and Light Company's (CPL) shareholders and ratepayers, with the ratepayer's share being placed in CPL's CWIP account. Although GSU argued that this case is not dispositive because it was a stipulated rather than a litigated case, the ALJ remains persuaded that the Commission would not permit inclusion of gain pursuant to the stipulation if such result were improper.

The ALJ therefore finds that based upon the reasons provided by Messrs. Bellon and Andersen, 83 percent of the yearly fixed asset payment which GSU receives should be treated as other electric utility income. This recommendation should be reflected in GSU's current rate case, Docket No. 7195, and in subsequent rate cases.

Regarding the 17 percent remaining from the sale of the property, because the asset is no longer providing service to the ratepayers and the ratepayers will no longer have their rates based on inclusion of these units as plant in service, the ALJ finds that it is appropriate to treat the remaining 17 percent of the fixed asset fee as non-utility income as proposed by GSU.

C. Approval of Proposed Regulatory Treatment of Operations and Maintenance Expense

GSU requested that the reduction in operations and maintenance expenses associated with the removal of Nelson Units 1 and 2 from GSU's cost of service be treated as a third-party payment which is booked below the line. The items to be excluded from GSU's cost of service include operations and maintenance expense, depreciation expense, and related taxes. No party objected to GSU's proposed treatment. The ALJ concurs.

D. Approval of Cogeneration Payments as Reconcilable Fuel Expense

The most heated issue in GSU's proposal concerns the treatment of purchased power payments. GSU, under the terms of the contract, will purchase all of the energy output from the NISC. The cogeneration payments are for non-firm energy; no capacity payments will be made. (Tr. at 33.)

The contract includes proposed rates to be used in calculating these payments, which are collectively called "P1" rates. "P1" rates are very complex and primarily related to the IPS rate, which is a rate based upon the current Louisiana tariff for customers served on Schedule LIS (Large Industrial Service). The calculation of "P1" depends upon the magnitude of the Venture's energy sales to GSU relative to the Venture's energy purchases from GSU, and the operating status of the Venture, i.e., whether it is operating in the gas or coke phase. Dr. Andersen, Staff Rate Analyst Kelso King and Company witness David Beekman provided explanations as to the mechanics of the calculation of these formulary rates. (OPC Exhibit 3 at 3-4; Staff Exhibit No. 2 at 7-8, and Company Exhibit 4 at 5-9.) Thus, the formulary rate is not based on GSU's avoided cost but rather upon GSU's industrial rates and the Venture's cost of production. (Staff Exhibit No. 2 at 18.)

OPC witness Andersen objected to the use of the formulary rates to calculate GSU's purchased power expense from the Venture because it was unnecessarily complex and dependent upon the actions of the Louisiana Public Service Commission's rate schedules. If approval of the Venture were given, Dr. Andersen recommended that all costs in excess of GSU's avoided cost be assigned either to GSU's shareholders or to the Louisiana jurisdiction. Mr. King, on the other hand, recommended that the costs in excess of GSU's avoided costs be split equally between the shareholders and the ratepayers. Mr. King also testified that the manner in which GSU calculated its payments for purchased power bore little relationship to GSU's avoided costs.

The critical issue presented under GSU's proposal is not necessarily the methodology used to develop the formulary rate, but rather the fact that the calculated rate for GSU's purchased power costs may exceed its avoided cost. (The ALJ understands that the parties are referring to GSU's standard avoided cost in their testimony when they refer to GSU's avoided costs.) The ALJ will address the appropriateness of using the formulary rate to determine GSU's purchased power payments and will then address the gravaman of the dispute: that GSU's payments to the QF for purchased power will exceed GSU's standard avoided costs.

1. Methodology to Calculate GSU's Purchased Power Expense

Some difficulty arises regarding the manner in which GSU calculated the purchased power payments. Pursuant to P.U.C. SUBST. R. 23.66(d)(1)(F)(iii), the utility's avoided costs form the basis of the non-firm payments to QFs. P.U.C. SUBST. R. 23.66(g) provides the criteria to be used in calculating the utility's avoided cost for non-firm power. This subsection refers to the calculation of purchases for non-firm power by utilizing the utility's average avoided energy costs or, at the QF's option, the full cost at the time of delivery of decremental energy that would have been incurred by the utility had the QF not been in operation. There is no question that the calculation under the terms of the Venture agreement is not premised upon GSU's avoided cost but rather upon the tariffs in effect in Louisiana for the industrial participants and upon the Venture's production costs. There is no evidence, moreover, that these costs are in any way related to the cost of decremental energy. Although this issue was raised in OPC and staff testimony, counsel did not provide the ALJ any discussion of this issue in briefs. Thus, the ALJ must decide this issue without the benefit of the parties' legal arguments.

Regarding the apparent obstacle to permitting adoption of a rate which was not calculated upon GSU's avoided costs, Mr. King testified as follows:

> Q. Do you have any concerns that the arrangements proposed under the terms of the Joint Venture Agreement might be in conflict with regulations regarding arrangements between Qualifying Facilities and utilities?

A. Yes, I do.

Q. In what ways do you feel that the arrangements offered under the Joint Venture Agreement might be in conflict with the Substantive Rules of this Commission?

A. First, I understand that the stated objective of GSU in the Joint Venture is to provide for an arrangement that is in the public interest by allowing rates to be lower than they would otherwise be without the Joint Venture. However, it has not been conclusively demonstrated that the proposed arrangement optimizes the benefit to the ratepayers not involved in the Joint Venture project. Although optimal rates are difficult to achieve or quantify, their development should nevertheless be a rate design objective.

Second, guidelines for the rates for purchases from QF's under both state and federal regulations state the level of those rates in relation to the utility's avoided cost. This is done in an attempt to encourage rate making methodologies that will approximate the savings to the utility system by making such purchases from a QF. The rates for purchases from the QF that have been proposed in the Joint Venture Agreement have little relationship to the avoided costs of GSU. The Substantive Rules of the Commission do not require that the payments to a qualifying facility for firm power be identical to the payment streams for avoided energy and capacity costs of the utility. The Rules, however, do require that the value of the payments to the qualifying facility not exceed the expected value of the avoided costs of the utility during the same period.

Staff Exhibit No. 2 at 19-20.

The ALJ does not necessarily find, as Mr. King seems to infer, that the methodology used to calculate the non-firm rate is not important. The ALJ basis her understanding that rates must be tied to the utility's average avoided energy cost or decremental energy cost upon P.U.C. SUBST. R. 23.66(g) which states:

(g) Tariffs setting out the methodologies for purchasing nonfirm power from a qualifying facility. Tariffs setting out the methodologies for purchases of nonfirm power from a qualifying facility shall be filed with the Commission based on one of the following two approaches:

(1) Rates for purchases of nonfirm power may, by agreement of both the utility and the qualifying facility, be based on the utility's average avoided energy costs. A utility may use its fuel adjustment charge until it has developed an appropriate avoided energy cost rate but may not do so after June 30, 1982. Administrative, billing, and metering costs shall be recovered through a monthly customer charge to the qualifying facility.

(2) Rates for purchases of nonfirm power may, at the option of the qualifying facility, be based on the full cost at the time of delivery of decremental energy that would have been incurred by the utility had the qualifying facility not been in operation.

(A) The following factors should be considered in the calculation of the cost of decremental energy:

(1) fuel costs;
(ii) variable operating and maintenance costs;
(iii) line losses;
(iv) heat rates;
(v) cost of purchases from other sources;
(vi) other energy-related costs;
(vii) capacity costs, if, as a class, qualifying facilities providing nonfirm energy offer some predictable capacity; and
(viii) for short term energy purchases, the time and quantity of energy furnished.

(B) If practical, the avoided cost should be determined by calculating by time period, using the utility's economic dispatch model (or comparable methodology), the difference between the cost of the total energy furnished by both the qualifying facility and the utility, computed as though the energy furnished by the qualifying facility had been furnished by the utility, and the actual cost of energy furnished by the utility.

(c) The economic dispatch model should take into consideration the following factors:

(1) fuel costs;
(ii) variable operating and maintenance costs;
(iii) line losses;
(iv) heat rates;
(v) purchased power opportunity;
(vi) system stability; and
(viii) operating characteristics.

(D) Time periods should be hourly if the utility has an automated economic dispatch model available; otherwise the shortest reasonable time period for which costs can be determined should be used.

(E) Administrative, billing, and metering costs shall be recovered through a monthly customer charge to the qualifying facility.

Nevertheless, the ALJ agrees that the costs paid for purchased power cannot exceed the utility's avoided costs if they are to be found to be in the public interest under the Commission's rules. The methodology GSU used to calculate its purchased power expense should not stand as an obstacle to prevent Commission approval of the transfer.

2. Purchased Power Expense in Excess of Standard Avoided Costs

The issue as to payments in excess of avoided costs is more difficult to resolve. There is no dispute that under GSU's proposal, its payments for purchased power may exceed its avoided costs. Mr. Beekman testified as follows:

> Q. Does the "P1" formulary rate result in a price for the power purchased from the Joint Venture equal to avoided cost?
> A. Not necessarily. The formulary rate is not tied to avoided cost unless the output of the units exceeds the load of the Industrial Participants as adjusted for losses. The price at which Gulf States purchases the output from the Joint Venture as a result of the use of the formulary rate can either be higher than or lower than avoided cost.
>
> GSU Exhibit No. 4 at 5-6.

Additionally, Mr. King strongly agreed with GSU's statement that it is possible, from time to time, that the formulary rates will provide for purchases of power from the facility by GSU at higher than its then avoided cost. (Staff Exhibit No. 2 at 20.) Circumstances which could cause this result are when the incremental cost of gas is lower than the system average fuel cost, when the avoided cost excludes capacity payments to other qualifying facilities with similar levels of firmness, or when avoided costs are below the Venture's cost of production.

The ALJ finds that payments for power from a QF premised under the FERC and Commission cogeneration rules cannot be in excess of the utility's full avoided cost for two reasons. First, although the general counsel and GSU are correct that 18 C.F.R. 292.301(b)(1) and P.U.C. SUBST. R. 23.66(b)(2) provide that negotiated rates or terms may differ from those normally required, i.e., a rate at avoided cost, the Commission has further qualified the acceptable level of a rate achieved under negotiations. While a utility and a QF may negotiate a rate which differs from the avoided cost rate, that does not necessarily mean that the utility may recover that expense. P.U.C. SUBST. R. 23.66(d)(1)(F) provides:

(F) A utility shall purchase capacity from qualifying facilities on the basis of avoided cost adjusted for the quality of firmness of such capacity. If more capacity is offered by the qualifying facilities to any one utility than is required by the Commission-approved forecast and generation expansion plan for that utility, the utility is required to purchase capacity and energy from qualifying facilities according to the following order of priorities:

(i) qualifying facilities power produced from municipal solid waste, as defined in Texas Civil Statutes, Article 447-7, §2(6), or renewable fuel sources;
(ii) all others;
(iii) within each category listed in clauses (i) and (ii) of this subparagraph, nothing in these rules shall prohibit an electric utility from accepting through negotiation the most favorable capacity proposal available based on a balanced consideration of expected price, terms and conditions of purchase, and quality of firmness. The utility may consider, in addition, diversification of contracts with qualifying facilities which provide firm capacity with regard to ownership, type of industry, technology, and fuel type. Nothing in this priority system should be construed so as to permit capacity offered from qualifying facilities with a higher priority to displace or reduce the capacity currently being supplied, or to be provided, by qualifying facilities with lower priorities, with which contracts have been executed.

(Emphasis added.)

This rule, in providing standards to determine which contract, capacity or energy, to accept under negotiation, does not mention consideration of a utility's load requirements or a transaction ostensibly made to prevent loss of industrial load on its system.

More importantly, the Commission has determined the level of avoided cost rates which are deemed just and reasonable and in the public interest. P.U.C. SUBST. R. 23.66(e) states:

(e) Rates for purchases from a qualifying facility.
(1) Rates for purchases of energy and capacity from any qualifying facility shall be just and reasonable to the consumers of the electric utility and in the public interest, and shall not discriminate against qualifying cogeneration and small power production facilities.
(2) Rates for purchases of energy and capacity from any qualifying facility shall not exceed avoided cost; however, in the

case in which the rates for purchases are based upon estimates of avoided costs over the specific term of the contract or other legally enforceable obligation, the rates for such purchases do not violate this subsection if the rates for such purchases differ from avoided cost at the time of delivery.

(3) Rates for purchases satisfy the requirements of paragraph (1) of this subsection if they equal avoided cost.

(4) Rates for purchases from qualifying facilities shall be in accordance with paragraphs (1)-(3) of this subsection, regardless of whether the electric utility making such purchases is simultaneously making sales to the qualifying facility.

(5) Payments by a utility to any qualifying facility, if in accordance with paragraphs (1)-(3) of this subsection, shall be considered reasonable and necessary operating expenses of that utility.

(Emphasis added.)

The ALJ finds that the utility's avoided cost is the maximum rate allowed under the Commission's rules, which will be deemed just and reasonable and in the public interest. Any cost above that amount is not given such favored status. As will be discussed shortly, that is not to say that such costs may not be sought to be recovered by GSU in a reconciliation proceeding or in its next general rate case when reconciliation of such costs is achieved.[1] Although GSU should be commended for securing a transaction which will attempt to prevent the departure of industrial load from GSU's system, the ALJ cannot recommend in this docket full approval of GSU's proposed regulatory treatment as to purchased power expense.[2]

Second, GSU requested that the purchased power payments be included in its reconcilable fuel expense which is used to calculate its fixed fuel factors. Reconcilable fuel, by its very nature, requires re-evaluation of such costs at the time of GSU's reconciliation. The ALJ interprets GSU's instant request to

[1]Although the rule indicates costs equal to a utility's avoided cost are reasonable, the ALJ believes that any costs less than the utility's avoided costs are also just and reasonable and in the public interest, under this rule.

[2]The ALJ notes that no party argued the applicability of P.U.C. SUBST. R. 23.66(e)(2) regarding the fact that rates in excess of a utility's avoided cost at the time of delivery are appropriate if the estimates under the terms of the contract were arguably at or below avoided costs at the time the contract was entered.

be one of seeking permanent approval of its formulary rates, which can lead to an undetermined level of payments in excess of GSU's avoided costs, without further scrutiny by this Commission. This request would be inappropriate under the Commission's Fuel Rule, which requires the reconciliation of fuel costs in the utility's general rate case or fuel reconciliation hearing.[3] The only statutory provision which would ostensibly permit recovery of cogeneration payments without further scrutiny is found in Section 41A of the PURA. Yet, even this section of the Act states that contracts which are brought under this section for certification must be equal to or less than the utility's avoided cost established by the Commission and in effect at the time the agreement was signed. GSU's request, even if it could fall under this section of the Act, would not meet this test.[4]

The ALJ concludes that she need not resolve the actual recovery of GSU's purchased power payments because that issue is determined in a utility's reconciliation under the Fuel Rule for those reasons discussed above. The record evidence does not demonstrate how often, and to what extent, GSU's payments will exceed that amount equal to its standard avoided cost rate. The ALJ is reluctant to recommend approval of unknown amounts in excess of GSU's standard avoided cost rates which may result under the formulary rates to be recovered in GSU's reconcilable fuel expense. However, GSU's purchased power payments, although not calculated upon GSU's avoided costs, if they equal GSU's avoided cost rates, are just and reasonable and in the public interest pursuant to P.U.C. SUBST. R. 23.66(e). These costs may properly be included in GSU's reconcilable fuel expense.

[3]In reconciling the Fuel Rule, which requires that the utility prove that it incurred the lowest reasonable fuel cost, and P.U.C. SUBST. R. 23.66(e), which requires that cogeneration payments be at or equal to avoided cost, an argument exists that for the purposes of reconciliation, those payments at or equal to avoided costs will be deemed the lowest reasonable fuel cost in the reconciliation of these costs.

[4]This section is not applicable to GSU because neither GSU nor the QF has submitted an application under this section of the Act. This section of the Act is not applicable to those contracts which were entered before the effective date of this section, June 11, 1987.

The ALJ concludes that based upon inadequate data in this case, but moreover, based upon the Commission's fuel reconciliation rule, she cannot determine in this docket that costs in excess of avoided costs are just and reasonable and in the public interest.

The ALJ recommends, however, that GSU be permitted to include in its reconcilable fuel expense those costs associated with its payments to the Venture. GSU should maintain detailed records of its payments which are equal to its avoided costs and those payments which are in excess of its avoided costs. GSU should maintain these records until it reconciles these costs, either in a reconciliation proceeding or in its next general rate case. In such proceedings the Commission may determine whether GSU should refund any portion of its costs associated with such payments.[5] The ALJ believes that this mechanism will, to a certain extent, assure the industrial participants, and thereby GSU, that the Venture can proceed under the terms of the contract. The ALJ's proposal affects GSU's actual recovery of these costs and does not affect the contract into which GSU intends to enter with the industrial participants.

During the reconciliation of fuel costs, pursuant to P.U.C. SUBST. R. 23.23(b)(2)(H), GSU can argue that its avoided costs for cogeneration payments are just and reasonable and in the public interest pursuant to P.U.C. SUBST. R. 23.66(e) and that good cause exists for it to recover costs in excess of its avoided costs. GSU could argue that any costs in excess of its avoided costs are just and reasonable and in the public interest by demonstrating certain circumstances such as that the costs were necessary as a means to keep its industrial load on the system, that the ratepayers benefited by the retention of the industrial load on the system, that the costs in excess of avoided costs were at a minimum, and that given these circumstances, its fuel costs were at

[5] A similar treatment was arranged in Docket No. 6393, In Re the Reasonableness of the Spring Creek and Kerr-McGee Coal Contract Costs, where fuel expense which was included in Houston Lighting and Power Company's was earmarked for possible refunds.

their lowest reasonable level. (This list is by no means exhaustive but merely reflects this examiner's opinion as to the elements GSU might demonstrate to recoup costs in excess of its avoided costs.)

Regarding OPC's request that any excess costs be allocated to GSU's shareholders or to GSU's Louisiana customers, the ALJ finds that the issues of costs in excess of GSU's avoided costs be determined in GSU's reconciliation of such costs. As the ALJ understands GSU's requests, its fuel cost for NISC power is not solely allocated to Texas jurisdiction fuel, but is allocated to all jurisdictions; such fuel expense is then subsequently reallocated on a jurisdictional basis. If the ALJ is incorrect in her understanding and GSU is requesting that all fuel costs related to purchased power from the Venture be solely the responsibility of its Texas ratepayers, such treatment is improper because the loss or retention of these Louisiana industrial participants affects not only GSU's Texas ratepayers but also its Louisiana ratepayers. In that instance, the ALJ recommends that the purchased power costs be split by use of the jurisdictional allocators approved in GSU's pending rate case, Docket No. 7195.

3. Construction of GSU's Payments as an Incentive Rate

Mr. King testified that if the Commission construes GSU's payments as an incentive rate, the Commission would not necessarily need to reconcile the apparent conflict between GSU's request, which reflects that its payments may exceed its avoided costs, and P.U.C. SUBST. R. 23.66, which requires that cogeneration payments be less than or equal to a utility's avoided cost. Mr. King testified as follows:

> Q. Must the arrangements between GSU necessarily be regarded as a transaction between a utility and a qualifying facility?
>
> A. Yes and no. This arrangement must be regarded as a transaction between a utility and a QF because that is what it is and it is therefore governed by the rules concerning those arrangements. The qualifying facility aspect, however, is not necessarily the most critical aspect of this arrangement. The arrangement that has been proposed is primarily concerned with preventing the loss at this time of further industrial load on the GSU system. The

overriding characteristic could be deemed to be the nature of the proposed Joint Venture arrangement as an incentive rate including a purchased power contract at rates higher than the Company's avoided cost.

Staff Exhibit No. 2 at 27-28.

Although OPC argued that the loss of industrial load is not as precipitous as GSU and the industrial participants would have the Commission believe, based upon the testimony in this record and the amount of effort invested in this QF Venture by all the participants, the ALJ is persuaded that the industrial customers are looking to this Venture or self-generation as a means by which to meet their energy needs. Thus while not a certainty, the loss of further industrial load, in addition to the 430 MW already departed from GSU's system, is a real possibility in this instance.

The ALJ is nevertheless uncomfortable labeling GSU's payments as an incentive rate. Admittedly, GSU's participation in the Venture is prompted in large measure by the possibility of industrial load leaving the system. However, the rate to be paid by GSU is for energy generated by a QF. An incentive rate, such as GSU's SUS rate, is designed to provide customers having potential to cogenerate with prices for power which it purchases from a utility that are competitive with power costs that these customers could expect if they chose to construct a cogeneration facility. It is not based upon the utility's cost of service, but rather upon the economics of installing various arrangements of gas turbine based cogeneration systems. (Staff Exhibit No. 2 at 28-29.)

GSU's request cannot be deemed as one for a "rate" because it is GSU that would pay for services rendered by the QF. The ALJ is not persuaded that payments by a utility to a QF is a "rate" as that term is defined in Section 3(d) of the Act.

Moreover, the ALJ feels uncomfortable in recommending a finding that this payment is an incentive rate, based upon the limited testimony in this case on this issue. While GSU's desire to maximize the load on its system is

understandable, this docket should not be the basis for such far-reaching policy decision i.e., the construction of the payments by GSU as an incentive rate. The ALJ is apprehensive of the type of precedent this case would set if the Commission's decision were founded upon this "incentive rate" theory. The transaction presented in this case is a means by which GSU recoups fuel costs and it is not a rate paid by customers for a service GSU provides. That is not to say that the issue of benefit to GSU's ratepayers by the retention of the industrial customers' load on GSU's system is irrelevant in determining the appropriateness of the proposed transfer of assets under Section 63 of the Act.

4. Benefit to GSU's Ratepayers

GSU and the industrial participants testified that GSU's ratepayers would benefit by the retention of this industrial load on GSU's system. Moreover, the local economy will benefit by short-term construction employment and by the stabalization of employment for the industrial customers' approximately 3,000 employees. Mr. Beekman further testified that if the industrial customers leave GSU's system, GSU's remaining customers would need to pick up base rate expenses previously allocated to the departing industrial customers. GSU testified that its participation in the Venture will result in net savings to GSU's ratepayers, since the increase in fuel costs will be more than offset by a decrease in base rates. (GSU Exhibit No. 4, Exhibit DNB-2.)

Although Dr. Andersen was not convinced that these industrial customers would leave GSU's system if the Venture were not approved, Mr. King agreed with GSU that a strong probability exists that the industrial customers will leave the system if the Venture does not go forward. Dr. Andersen further pointed out that GSU did not provide the Commission an analysis reflecting the long-run effects of the industrial customers' departure from GSU's system, and the long-term corollary benefits to GSU's ratepayers by the continued presence of the industrial participant load on GSU's system.

In his discussion of GSU's proposed rates, Mr. King indicated that it is necessary that GSU provide an optimal rate, one that retains the greatest amount

of revenue from the industrial participants, while still providing sufficient benefit to the industrial participants to remain on the system. (Staff Exhibit No. 2 at 13.) Mr. King further recommended that to keep this industrial load on the system, GSU's other ratepayers should bear one-half of any costs in excess of GSU's avoided costs. Id. at 35. The ALJ infers from the staff's recommendation that the staff believes the retention of this load on GSU's system will benefit GSU's other remaining customers and thus the appropriateness of allocating to them one-half of GSU's payments in excess of GSU's avoided costs.

The ALJ agrees that a benefit inures to GSU's ratepayers because of GSU's participation in the Venture. Although not readily quantified in the record on a long-term basis, the departure of this industrial load from GSU's system, which is a real possibility, would result in GSU's other remaining ratepayers picking up those expenses currently recouped from these industrial customers. The ALJ, as discussed earlier, does not believe it appropriate to determine in this docket what level of costs in excess of GSU's avoided costs should be borne by GSU's ratepayers. The benefit to GSU's other ratepayers by the retention of this industrial load on GSU's system is relevant in determining that the transfer of assets is in the public interest.

5. Alternative Recommendation

It is important that the Venture project go forward. As referenced earlier, no party opposes the transfer of assets. In the alternative, should the Commission determine that it can decide the issue of fuel costs in this docket and that it need not be resolved in GSU's reconciliation of these costs, the ALJ recommends adoption of Mr. King's proposal to allow GSU to include all of its purchased power expense for NISC generated power which would equal those payments if calculated under GSU's avoided costs and to include one-half of any payments in excess of GSU's avoided costs as reconcilable fuel expense.

GSU did not enter the Venture agreement primarily to obtain energy from the QF, but rather to prevent the loss of industrial load from its system. While

the ALJ is less than comfortable in recommending a payment in excess of GSU's avoided costs, such is proper for good cause exists in those unique circumstances presented here: to prevent the loss of industrial load from GSU's system, which has already lost 430 MW of industrial load to cogeneration; to secure for GSU's other ratepayers by the retention of this industrial load the benefits associated with preventing an increase in rates based upon the reallocation of the rate base expenses of these industrial customers; and to encourage cogeneration in Texas.

It has not been demonstrated, however, that the payment schedule agreed to between GSU and the industrial participants fairly allocates the benefits of such Venture to GSU's other ratepayers. This is made clear by GSU Exhibit No. 9, which compares the cost of power to Conoco under the Venture to the industrial rate under the SUS schedule. (Examiner's Attachment No. 2.) Conoco could not realistically be expected to enter into an agreement under the SUS rate, an incentive rate, because that rate produces higher costs to Conoco than the payment schedule under the Venture contract and because that rate is of a short-term nature. (The SUS rate an experimental rider designed to be sufficiently attractive to prevent an industrial customer from turning to self generation.) It is reasonable to provide industrial participants payments for the cogenerated power which encourages retention of their load on the system while minimizing cross-subsidization to GSU's remaining customers. Under GSU's proposal, however, GSU's other ratepayers absorb all the excess costs associated with GSU's purchased power expense. Such allocation is improper.

The staff's recommendation is reasonable in that it recognizes the need for retention of industrial customers, but provides for a sharing of the cost resultant from their retention between GSU's ratepayers and shareholders. No party proposed that the industrial customers absorb all the costs of GSU's payments which exceed its avoided cost, perhaps because that result would require modification of the contract terms and could mean loss of industrial interest in the Venture. Under the staff's proposal, the contract would remain unchanged. The only modification is to the regulatory treatment of these expenses. (Tr. at 111-112.) While such treatment recognizes the benefit GSU's

other ratepayers derive from the retention of the industrial load on GSU's system, it does not require that these ratepayers absorb all costs in excess of GSU's avoided costs. GSU would absorb some of the costs in retaining its own industrial load on its system. The sharing of any excess costs is, moreover, in line with GSU's treatment of costs occasioned by the retention of industrial load under the SUS rate. Under this rate, GSU's shareholders absorb all the loss occasioned by an industrial customer's election of this incentive rate. It is only equitable in this instance, where retention of industrial load is the basis for the transaction, that a sharing of costs be effected.

Legal precedent exists for providing for payments that exceed a utility's avoided costs.

In Consolidated Edison Company of New York, Inc. v. Public Service Commission of New York, 472 N.E. 2d 981, 63 N.Y. 2d 424, 483 N.Y.S. 2d 153 (Ct. App. 1984), the N.Y. Appellate Court reversed the lower court's decision and held that PURPA does not preempt state regulation requiring electric utilities to purchase power from federal qualifying facilities at a rate in excess of the avoided cost purchased rate required under PURPA. Id. at 433, 156. In essence, utilities qoverned by state regulations were not bound by the FERC avoided cost rules.

While this case can form a certain basis for a cogeneration payment in excess of a utility's avoided costs, the ALJ notes two important considerations on this reliance. First, although the U.S. Supreme Court in a two page memorandum decision dismissed the appeal for want of a substantive federal question, 470 U.S. 1075, 105 S.Ct. 1831, 85 L.ed. 2d 132 (1985), Justices White and Blackman wrote a strenuous dissent regarding the Court's opinion.

Second, the reasonableness of granting such unique treatment in this case should be limited to the peculiar and extenuating facts presented in this case. In offering this alternative, the ALJ finds that qood cause exists pursuant to P.U.C. SUBST. R. 23.2 to permit the recovery of costs in excess of GSU's

avoided costs. The ALJ notes that if this alternative recommendation is adopted, new Findings of Fact and Conclusions of Law would be required.

E. Standby Reservation Fee

The Venture will purchase 10 MW of standby power from GSU to provide station service to Nelson Units 1 and 2 in the event that both units are out of service simultaneously. The revenue generated under this service is called the "Standby Reservation Fee." GSU has stated that this cogeneration revenue has been allocated to all of GSU's customer classes in its instant rate case, Docket No. 7195.

Dr. Andersen criticized GSU's calculation of this fee because GSU's calculation of $4,306,847 in revenues per year is based on the assumption that the Venture will be totally self-sufficient. If the installed capacity falls short of the Venture's total requirements <u>or</u> the equivalent availability of self-generating capacity is less then 93 percent, actual revenues would exceed GSU's estimates. Dr. Andersen further questioned whether the 93 percent equivalent availability factor (EAF) which GSU proposed could be sustained over the 20 year life of the Venture if the Nelson units are purchased or if alternative generating capacity is constructed by the industrial participants. (OPC Exhibit No. 3 at 10.)

In rebuttal, GSU witness Kenneth Richards testified that a 93 percent EAF is achievable over the life of the Venture project.

OPC's recommendation on this issue in unclear. No alternative calculation of revenues was provided and no specific recommendation was offered. The ALJ finds that in this docket, it is reasonable to determine the standby reservation fee based upon the company's methodology. The level of actual revenues generated under this rate, however, may be reviewed in subsequent rate cases before this Commission. As GSU realizes, it must prove the appropriate level of its revenues in each of its rate cases.

F. Miscellaneous Issues

1. Affiliate Transactions

OPC argued in brief that the Venture could be construed as an affiliate transaction under Sections 3(i)(6) or (7) of the PURA. Under the terms of the proposed Venture contract, the coke needed to operate the Venture will be supplied by Conoco and Citgo. OPC argued that no assurance exists that this coke will be priced at or below the market price.

Section 3 (i)(6) and (7) of the PURA define "affiliate or "affiliated interest" to inlcude the following:

> (6) any person or corporation that the commission, after notice and hearing, determines actually exercises any substantial influence or control over the policies and actions of a public utility, or over which a public utility exercises such control, or that is under common control with a public utility such control being the possession, directly or indirectly, of the power to direct or cause the direction of the management and policies of another, whether such power is established through ownership or voting of securities or by any other direct or indirect means; or
>
> (7) any person or corporation that the commission, after notice and hearing determines is actually exercising such substantial influence over the policies and action of the public utility in conjunction with one or more persons or corporations with which they are related by ownership or blood relationship, or by action in concert, that together they are affiliated with such public utility within the meaning of this section, even though no one of them alone is so affiliated.

Under the terms of the contract, GSU has a one percent ownership interest in the Venture. The management committee which will be established under the agreement, and will oversee the Venture's operations. The Venture has four participants and thus GSU would arguably exert a 25 percent influence in the management committee. However, unless otherwise stated under the terms of the contract, GSU's number of votes on the management committee is equal to its ownership interest. The ALJ does not find that GSU can exert a substantial influence over the operation of the Venture. It is not clear from the record

whether this is also the case with the industrial participants, which because of their ownership interests may arguably jointly exert substantial influence over GSU's policies and actions in this Venture.

The ALJ does not believe this issue need necessarily be resolved in the instant proceeding. The reconciliation of affiliate costs is properly the subject of GSU's rate cases where such costs are at issue. GSU should be prepared to demonstrate in future rate cases that the prices charged by Citgo and Conoco for coke are necessary and reasonable pursuant to Section 41(c)(1) of the Act. Once again, the actual true-up of GSU's expenses is best left for the reconciliation of these costs.

If on the other hand, the Commission adopts the alternative recommendation, it bears mentioning that this issue was developed on very limited cross-examination and the ALJ has not been persuaded that affiliate transactions is an issue in this case.

2. Other Contract Provisions

The contract between GSU and the industrial participants include provisions related to such items as liabilities and indemnities, withdrawal, dissolution, liquidation, bankruptcy or insolvency, insurance, and audits. Dr. Andersen and Mr. King both testified that they had no recommendation regarding such provisions and that they concentrated their efforts on the proposed regulatory treatment of the expenses under the contract. (Tr. 98-99, Tr. 112.)

These and other contract terms are outside the Commission's jurisdiction to adjudicate. The utility must engage in reasoned negotiation and contract procurement. The decision to enter into a contract and the terms of that contract are areas limited to the managerial discretion of the utility. While the Commission can approve the transfer of assets and allow a certain level of costs to be recouped and revenues recorded, the Commission cannot "approve" or "disapprove" a contract entered into between GSU and its industrial customers. However, in the alternative, the ALJ recommends that the Commission's order find

that GSU's participation in the Venture is noteworthy and appropriate. In that regard, reasons 2 and 3 found in the FERC order regarding certification of the QF, or similar language thereto, could be utilized to reflect the Commission's underlying support of the Venture in the Commission order. (See Examiner's Attachment No. 1 at 4.) The Commission could also include language regarding the retention of industrial load on GSU's system as another reason for approving the transfer of assets. (Alternative Proposed Order.)

The industrial participants require that the terms and conditions of the proposed contract remain unchanged. GSU states, on the other hand, that its proposed regulatory treatment must also remain unchanged. In its reply brief, GSU declares:

> The present terms and conditions of the Partnership Agreement, without modification, must be kept intact to keep the Industrial Participants on the Gulf States system and keep them from turning to self-generation. What OPC and Staff fail to see, or choose to ignore, is that acceptable regulatory treatment is a condition to the Company's participation in the Venture Project. Gulf States witness James R. Underhill offered the best evidence regarding the final agreement:
>
> The total contract has been negotiated, and there has been give and take on every part of this agreement. The price is merely one of the concessions there (Sic) were made both ways. There is (Sic) control issues; there are all sorts of issues that come up in the negotiations and each of those have a price tag, and we have negotiated those.
>
> Tr. 127(2-7). Gulf States has shown that the Industrial Participants will leave the Gulf States' system and turn to self-generation if the Joint Venture is not approved. Mr. Underhill testified that Conoco prefers self-generation because it puts Conoco in control of its own energy destiny. Tr. 123(22)-124(2). Apparently OPC believes that Mr. Underhill is bluffing - a mistake potentially fatal to the venture. GSU Exhibit No. 6 at 3(2-8) Underhill Rebuttal. A similar mistake is made in the presumative statements made by Staff in the conclusion of its brief. Gulf States has made it abundantly clear that it is requesting approval of the Venture Project, including regulatory treatment, as proposed. The Industrial Participants are not the only participants in the venture and their indifference to the regulatory treatment of revenue does not mean that the Commission can modify the

regulatory treatment sought without fear that such adjustments will nix the agreement."

GSU Reply Brief at 7-8. Emphasis added.

The ALJ interprets GSU's statements to mean that if the Commission modifies GSU's proposed regulatory treatment in any manner, GSU may withdraw its participation in the Venture.

Despite GSU's unflexible stance, the ALJ cannot recommend full approval of the contract and of the regulatory treatment as proposed for those reasons described in this Report. GSU is free to make whatever decision it feels appropriate. The Commission should be aware that in GSU's current rate case, it has made adjustments to its revenues and expenses as if the Commission had approved GSU's application in toto. GSU has also excluded capacity associated with Nelson Units 1 and 2 in its current rate case. (Tr. at 77-78.) If GSU does determine to withdraw its participation in the Venture, which the ALJ assumes would be done prior to the setting of GSU's rates in its current rate case, the rates set in Docket No. 7195 should reflect adjustments to GSU's revenues, expenses, capacity, and any other items which might be affected by GSU's decision to withdraw its participation in the Venture.

IV. Summary

The transfer of Nelson Units 1 and 2 is in the public interest pursuant to Section 63 of the Act as long as its is done in accordance with those regulatory recommendations made herein. Under the ALJ's primary recommendation, GSU will be able to include in its reconcilable fuel expense the costs of its payments to the Venture. In the reconciliation proceeding, GSU will then have the opportunity to prove that all of its payments, including those in excess of its standard avoided costs, were at the lowest reasonable level. Alternatively, the ALJ recommends that GSU be limited to recovering all of its payments which would equal payments at its avoided cost. GSU would also be able to recover one-half of any payments in excess of its avoided costs.

The ALJ finds that benefits do inure to GSU's other ratepayers by GSU's retention of the industrial participants' load to GSU's system, which is the result reached by the transfer of the assets. In that regard, the ALJ declines to recommend that the Commission approve the proposed contract, for certain of the contractual provisions contain issues over which this Commission has no jurisdiction. Moreover, the decision to enter into the Venture contract is within GSU's management discretion. The Commission, on the other hand, is concerned with the proper regulatory treatment of the effects of the Venture contract upon GSU's ratepayers.

VI. Findings of Fact and Conclusions of Law

The ALJ further recommends that the Commission adopt the following Findings of Fact and Conclusions of Law.

A. Findings of Fact

1. On October 17, 1986, GSU filed its application for approval of its participation in the NISC. In its application, GSU requested Commission approval of its proposed regulatory treatment of revenues and expenses associated with the Venture.

2. Conoco, Vista, and Citgo are Louisiana-based industrial customers of GSU who are participants in the Venture.

3. Interventions were granted to OPC, TSA, North Star and TIEC. TSA subsequently withdrew its participation in this case.

4. Joseph C. Howell, Business Manager of the International Brotherhood of Electrical Workers, AFL-CIO-CLC, Local 2286 located in Beaumont, Texas, filed a letter with the Commission supporting the Venture.

5. On May 21, 1987, FERC granted NISC's request for QF status contingent upon NISC's completion of certain milestones in reaching the coke operation of the Venture.

6. On August 17, 1987, the hearing on the merits in this docket was convened.

7. GSU provided notice of its application once each week for two consecutive weeks in newspapers of general circulation in each county containing territory affected by its application.

8. The Venture will construct two fluidized bed combustors to replace the existing natural gas fired boilers of GSU's Nelson Units 1 and 2, which units are located in Louisiana. During the design and construction of the QF facilities, the first five years of operation, the QF will use natural gas as a boiler fuel. The QF will consume petroleum coke after construction of the facilities is completed.

9. GSU has lost 430 MW of industrial electric load to cogeneration.

10. The industrial participants to the Venture have a total load of approximately 200 MW.

11. The Venture's industrial participants will likely turn to self-generation if the Venture does not go forward.

12. For those reasons set forth in Section IV.B. of this Report, it is reasonable that 83 percent of the yearly fixed asset payment of approximately $6.35 million which GSU receives be treated as other electric utility income.

13. For those reasons set forth in Section IV.B. of this Report, it is reasonable for GSU to treat the remaining 17 percent of the fixed asset payment as non-utility income.

14. For those reasons set forth in Section IV.C. of this Report, it is reasonable for GSU to treat saved operations and maintenance expense associated with Nelson Units 1 and 1 as third-party payments.

15. Under the terms of the proposed Venture contract, GSU is required to purchase all of the energy output generated by the QF.

16. The rate for payment by GSU for the purchased energy is not based upon GSU's avoided costs but rather upon the tariff in effect in Louisiana for the industrial participants and upon the Venture's production costs.

17. Under the terms of the contract, the rate of payment by GSU for the purchased power may exceed GSU's standard avoided costs.

18. For those reasons set forth in Section IV.D.1. of this Report, it is not improper for GSU's costs for purchased power to be based upon the methodology reflected in the proposed Venture contract.

19. For those reasons set forth in Section IV.D.2. of this Report, GSU may recover those cogeneration costs which are just and reasonable and in the public interest, as long as its payments do not exceed its avoided costs.

20. It is reasonable to permit GSU to recover all costs associated with its purchase of energy from the Venture as reconcilable fuel expense, as long as GSU maintains a record of its avoided cost payments and of its payments in excess of its avoided costs until such time these expenses are reconciled in an applicable reconciliation proceeding or rate case.

21. GSU must prove in a reconciliation proceeding or rate case that its avoided cost payments and any payments in excess of GSU's avoided costs were at the lowest reasonable level.

22. For those reasons set forth in Section IV.D.2. of this Report, GSU should maintain records regarding those payments in excess of its avoided cost for

possible refund in GSU's subsequent general rate cases or fuel reconciliation proceedings.

23. The retention of the industrial participants' load on GSU's system is relevant in determining whether GSU's sale of Nelson Units 1 and 2 is in the public interest.

24. For those reasons set forth in Section IV.D.3. of this Report, it is not reasonable to construe GSU's payments for the energy it purchases from the Venture as an incentive rate.

25. GSU's other ratepayers receive a benefit by retention of the industrial participants load on GSU's system, since any base rate revenues which have been allocated to these industrial customers would necessarily be absorbed by GSU's other ratepayers if these industrial customers left GSU's system.

26. For those reasons set forth in Section IV.E. of this Report, it is reasonable to establish the Standby Reservation fee as calculated by GSU.

27. For those reasons set forth in Section IV.F.1. of this Report, it is reasonable to address the issue of possible affiliate transactions related to the coke purchases in the applicable reconciliation of GSU's purchased power costs.

28. For those reasons set forth in Section IV.F.2. of this Report, it is not appropriate for the Commission to approve or disapprove the Venture contract.

29. For those reasons set forth in Section IV. of this Report, the transfer of Nelson Units 1 and 2 to the Venture is in the public interest as long as it is done in accordance with that regulatory treatment recommended herein.

B. Conclusions of Law

1. The Commission has jurisdiction over the matters presented in this case pursuant to Sections 16(a) and (g) and 63 of the Act and P.U.C. SUBST. Rs. 23.23 and 23.66.

2. In determining whether the transfer of assets is in the public interest pursuant to Section 63 of the Act, it is appropriate to review the regulatory treatment of the expenses and revenues associated with the transfer.

3. P.U.C. SUBST. R. 23.66(d)(1)(F)(iii) sets forth the methods necessary to calculate non-firm payments to QFs.

4. A utility's cogeneration payments are deemed just and reasonable and in the public interest if its payments are no more than its avoided costs, pursuant to P.U.C. SUBST. R. 23.66(e).

5. GSU's payments to the Venture cannot be construed as an incentive rate because such payments are not rates as defined under Section 3(d) of the Act.

6. 18 C.F.R. 292.301(b)(1) and P.U.C. SUBST. R. 23.66(b)(2) provide that negotiated rates or terms may differ from those normally required, i.e., a rate at avoided cost.

7. P.U.C. SUBST. R. 23.66(d)(1)(F) requires that a utility accept through negotiation the most favorable proposal.

8. P.U.C. SUBST. R. 23.66(e) sets forth that rates for purchases at the utility's avoided costs are just and reasonable and in the public interest.

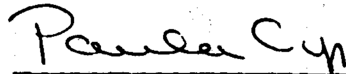
9. A utility's fuel expense is subject to review in its reconcilation to determine whether it was at the lowest reasonable level pursuant to P.U.C. SUBST. R. 23.23(b)(2)(H).

10. The Commission does not have jurisdiction pursuant to Section 16 of the Act to approve or disapprove the Joint Venture contract.

11. GSU's publication of notice is in compliance with P.U.C. PROC. R. 21.25.

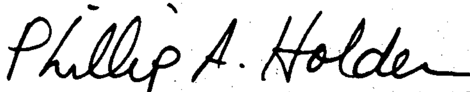
12. GSU's transfer of Nelson Units 1 and 2 is in the public interest pursuant to Section 63 of the Act.

Respectfully submitted,



PAULA CYR
ADMINISTRATIVE LAW JUDGE

APPROVED on this the 3d day of December 1987.



PHILLIP A. HOLDER
DIRECTOR OF HEARINGS

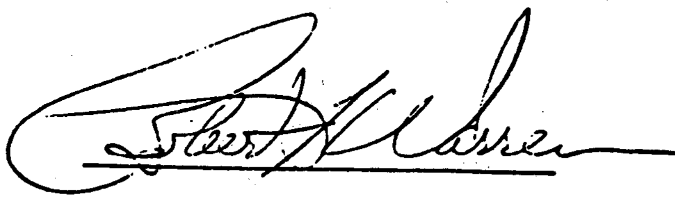
nsh

UNITED STATES OF AMERICA

FEDERAL ENERGY REGULATORY COMMISSION

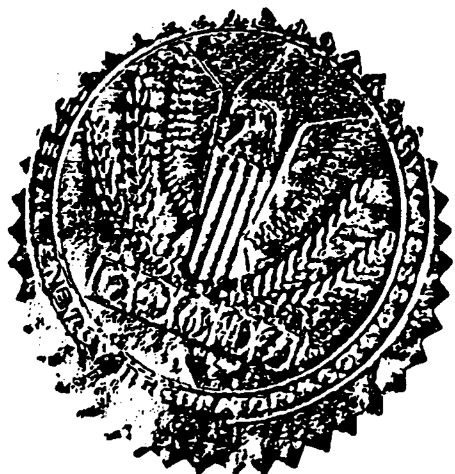
CERTIFICATION

I hereby certify that the attached 12 pages are true and correct copies of a document on file with the Commission.

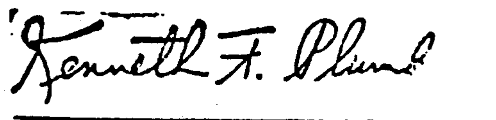


July 13, 1987
Date

Records Officer



I hereby certify that the Records Officer, whose signature appears above, is official custodian of the records of the Federal Energy Regulatory Commission which certification is made and was such official custodian at the time of executing the above certification.



SECRETARY

FERC-03-F-028

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

ELECTRIC RATES: Qualifying
Facilities; Cogeneration;
Waiver; Rehearing

Before Commissioners: Martha O. Hesse, Chairman;
Anthony G. Sousa, Charles G. Stalon,
Charles A. Trabandt and C. M. Naeve.

Nelson Industrial Steam Company) Docket No. QF86-512-001

ORDER ON REHEARING GRANTING APPLICATION FOR
CERTIFICATION AS A QUALIFYING COGENERATION FACILITY

(Issued May 21, 1987)

By order issued February 19, 1987, 1/ the Commission denied the application by Nelson Industrial Steam Company (Nelson) for certification of a facility (facility or project) as a qualifying cogeneration facility. The Commission found that the proposed facility was subject to the efficiency standard set out in section 292.205(a)(2)(i)(B) of the Commission's regulations 2/ based on the fact that construction necessary to convert the electric power station 3/ to a cogeneration facility commenced after March 13, 1980. The Commission also denied the requested waiver of the efficiency standard because it was unable to find, based on the information presented, that significant energy savings would be achieved by Nelson's project. 4/

1/ Nelson Industrial Steam Company, 38 FERC ¶ 61,162 (1987).

2/ 18 C.F.R. § 292.205(a)(2)(i)(B)(1986).

3/ Units 1 and 2 of the Roy Nelson electric power station, completed in 1959.

4/ The Commission's regulations provide for waiver upon a showing that the facility will produce significant energy savings. 18 C.F.R. § 292.205(d) (1986).

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Background

Nelson proposes to convert units 1 and 2 of the existing natural gas-fired Roy Nelson electric power station owned by Gulf States Utilities Company (Gulf States) to a topping-cycle cogeneration facility. Nelson plans to acquire and operate the existing facility in Phase I, using natural gas as its primary energy source. Nelson estimates that Phase I operations will continue for five years. The net electric power production capacity of the facility during Phase I will be 197.029 megawatts(MW).

In Phase II, Nelson proposes to install two new fluidized bed combustion boilers. The primary energy source during Phase II will be either petroleum coke or coal. The project, if certified, will have a net power production capacity of 201.990 MW. The steam output during both phases will be used by Vista Chemical Company (Vista) for both thermal and mechanical uses in its chemical production processes. 5/ The facility will be owned by Nelson, a joint venture partnership. The ownership interests are: Citgo Petroleum Company--49.5%; Conoco, Inc. -- 36.1%; Vista Chemical Company--13.4%, and Gulf States --1.0%. The facility thus satisfies the requirements of section 292.206 of the regulations, 18 C.F.R. § 292.206 (1986), because the utility's ownership does not exceed the fifty percent ownership threshold.

Request for Rehearing

In its request for rehearing filed March 20, 1987, Nelson argues that the reasoning employed and the result reached in the Commission's February 19th order are fundamentally inconsistent with the rationale and policy which underlie the Commission's implementation of section 201 of the Public Utility Regulatory Policies Act of 1978 (PURPA). 6/ Nelson argues that the "efficiency standards were meant to only apply to fuels the prices of which 'are subject to government control, and therefore. . . do not reflect replacement costs.' PURPA Proposed Regulations Preambles, 44 Fed. Reg. 38872, 38876 (July 3, 1979)." 7/ Nelson argues that the efficiency standard should only apply to facilities burning oil and gas, and the

5/ Nelson states that steam sold to Vista will supplement its industrial steam needs which would otherwise be supplied by Vista's natural gas-fired boilers.

6/ As codified, 16 U.S.C. § 796(18)(1982).

7/ Nelson request for rehearing at 2. (footnote omitted).

Commission, by including the Phase II energy inputs of petroleum coke in the calculation of energy savings for the purpose of applying the waiver provision, inappropriately subjected Phase II of the facility to the same efficiency standard which should be applied only to a gas or oil-fired project. Nelson contends this serves no policy objective. Nelson argues that the Commission's order ignores the facility's displacement of natural gas, a premium fuel, during Phase II, and thus ignores the thrust of PURPA: to conserve scarce premium resources, such as oil and gas.

In support of its position, Nelson relies on the Commission's decision in Mercy Hospital & Medical Center, 18 FERC ¶ 61,129 (1982). Nelson states that the Commission in its February 19th order wrongly relied on the decision in Mercy Hospital for the proposition that the central concern of PURPA is to "conserve energy in general." Nelson argues that Mercy Hospital stands for exactly the opposite proposition: that efficiency standards (and therefore energy conservation) were only intended to apply to those cogeneration facilities which use price-controlled fuels, i.e., oil and natural gas.

Alternatively, Nelson requests the Commission to exercise its general supervisory authority to waive the efficiency standard on the basis that the Commission has frequently waived specific rules where strict compliance would not have resulted in encouragement of cogeneration and small power production. American Electric Power Service Corp. v. FERC, 675 F.2d 1226, (D.C. Cir. 1982), rev'd on other grounds, 461 U.S. 402 (1983).

Discussion

Based on the facts raised in Nelson's request for rehearing, and pursuant to our general authority to waive Commission regulations where doing so would be in the public interest, 8/ we shall grant Nelson's request for rehearing and grant a temporary waiver of the efficiency standard contained in section 292.205 (a)(2)(i)(B), conditioned upon Nelson's furnishing us with satisfactory evidence that it has met the design, planning, construction and commissioning milestones, as discussed below. Nelson satisfies all requirements to be a qualifying cogeneration facility except for the applicable efficiency standard during a limited five-year period. We conclude that a strict application of the efficiency standard in this instance would frustrate PURPA's goal of encouraging cogeneration.

8/ 16 U.S.C. § 825h (1982).

Our decision to waive the efficiency standard during Phase I operation is based on the following specific facts unique to this case: (1) the major entities affected by this proceeding have urged our support of the project, and no party is opposed to it; 9/ (2) the Nelson project will increase employment through short-term construction activity and will help insure the long-term economic viability of three of the participants' industrial facilities, which are major employers in the economically depressed Lake Charles, Louisiana area; (3) Phase II of the facility will use fluidized bed combustion boilers, a technically advanced design which will use petroleum coke or coal as its primary fuel in an environmentally safe manner; (4) the waiver will fulfill PURPA's goal of encouraging cogeneration, and allow the facility to ultimately utilize petroleum coke or coal as its primary energy source; and (5) Nelson has provided assurances that the project will proceed on a timely basis and that additional waivers will not be needed.

In addition to the above factors, we note the temporary nature of the requested waiver. Because the waiver of the efficiency standard is being done on a temporary basis to encourage this particular project, there should be no concern that the Commission is hereby vitiating section 292.205 of the regulations.

We will require Nelson, however, to provide us with certain assurances that the project will proceed with due diligence. The Commission will therefore condition the grant of waiver upon Nelson's submission of evidence that it has met the project's milestones as set forth in this order. Within five months of the date of this order, Nelson must submit evidence to this Commission that it has established the venture project team, qualified and selected the engineering contractor, completed the preliminary engineering for detailed project scope, and initiated all environmental studies and applications.

Within 18 months of the date of this order, Nelson must submit evidence that it has prepared the basis for bids, performed commercial test burns on petroleum coke to determine the design of the fluidized bed combustion boiler, reviewed bids and selected the fluidized bed combustion boiler vendor, performed engineering for definitive cost estimates, and secured management

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9/ On April 8, 1987, Gulf States filed a letter with the Commission urging the Commission to grant Nelson's application for certification. According to Gulf States the project will result in savings to ratepayers in excess of ten million dollars annually.

approval for the final design, procurement and construction of the project.

Within 30 months, Nelson shall provide evidence that it has completed detailed engineering for construction and procurement, and begun construction. Also within 30 months, Nelson shall provide evidence that it has secured full financing for the project. Within 42 months Nelson shall give evidence of construction to completion.

Within 49 months, Nelson shall submit evidence that it has completed start-up/commissioning, necessary on-site revisions and debugging, and shall submit evidence of detailed performance testing and plant acceptance.

With the exception of the 30-month milestone for submission of evidence of securing of full financing, and the 30-month milestone for submission of evidence of the start of construction, this schedule is essentially identical to the one submitted by Nelson. The Commission also finds reasonable Nelson's inclusion in its schedule of an eleven-month contingency period for possible re-bidding on plant and equipment, environmental approvals, possible difficulty in securing commercial test burns on petroleum coke, and possible design corrections discovered during start-up. The report to the Commission of Nelson's satisfactory completion of each of these milestones is due within 60 days of the end of the particular milestone period. Nelson may apply the contingency period as it sees fit, as long as it notifies the Commission, and the contingency period does not exceed the aggregate eleven-month period. In any case, the total waiver period shall not exceed 60 months.

The Commission has concluded upon reconsideration that under the extremely narrow circumstances of this case, the public interest is best served by granting Nelson's application for certification as a qualifying cogeneration facility through waiver of section 292.205(a)(2)(i)(B) of the regulations. Because the waiver is being granted pursuant to our general equitable powers, we do not need to address Nelson's alternative grounds in support of a waiver. We emphasize that this decision should not be construed as an indication that the Commission will be inclined to grant efficiency standard waivers in other situations, and that absent extraordinary circumstances we will continue to apply the "significant energy savings" standard unless and until we decide to change the current regulation.

The Commission orders:

(A) Nelson's request for rehearing is hereby granted, as discussed in the body of this order.

(B) Nelson's request for waiver of the Commission's efficiency standard, 18 C.F.R. § 292.205(a)(2)(i)(B), during Phase I operations, or for a period of 60 months, whichever is shorter, is hereby granted, subject however to the conditions set forth above.

(C) The application for certification as a qualifying cogeneration facility filed on January 30, 1986, by Nelson Industrial Steam Company for a cogeneration facility pursuant to section 292.207(b) of the Commission's regulations and section 3(18)(B) of the Federal Power Act as amended by Title II of the Public Utility Regulatory Policies Act of 1978, is hereby granted. 10/

(D) Docket No. QF86-512-001 is hereby terminated.

By the Commission. Commissioner Sousa dissented with a separate statement attached.
Commissioner Stalon dissented with a separate statement to be issued later.

(S E A L)

Kenneth F. Plumb

Kenneth F. Plumb,
Secretary.

10/ Certification as a qualifying facility serves only to establish eligibility for benefits provided by the Public Utility Regulatory Policies Act of 1978, as implemented by the Commission's regulations, 18 C.F.R. Part 292. It does not relieve a facility of any other requirements of local state or Federal law, including those regarding siting, construction, operation, licensing and pollution abatement. Certification does not establish any property rights, resolve competing claims for a site, or authorize construction.

Nelson Industrial Steam Company) Docket No. QF86-512-001

(Issued May 21, 1987)

SOUSA, ANTHONY G., Commissioner, dissenting:

I must respectfully dissent from my colleagues' decision to grant the applicant a five-year waiver of the efficiency standard applicable to qualifying cogeneration facilities. I believe the majority's decision lacks any plausible factual or policy rationale.

The majority rests its decision to grant a waiver on the following "unique" facts:

> "(1) the major entities affected by this proceeding have urged our support of the project, and no party is opposed to it; (2) the Nelson project will increase employment through short-term construction activity and will help insure the long-term economic viability of three of the participants' industrial facilities, which are major employers in the economically depressed Lake Charles, Louisiana area; (3) Phase II of the facility will use fluidized bed combustion boilers, a technically advanced design which will use petroleum coke waste or coal as its primary fuel in an environmentally safe manner; (4) the waiver will fulfill PURPA's goal of encouraging cogeneration, and allow the facility to ultimately utilize a waste fuel or coal as its primary energy source; and (5) Nelson has provided assurances that the project will proceed on a timely basis and that additional waivers will not be needed."

These assertions, considered individually or collectively, do not show anything that can be reasonably characterized as a unique situation. I will consider these assertions in order.

First, the majority relies on the fact that the requested waiver is unopposed. I submit that this is irrelevant and that the majority fails to consider the wider consequences of its reasoning. Lack of opposition is irrelevant because the majority purports to apply a "public interest" standard. The public interest in certifying qualifying cogeneration facilities is conservation of energy. As the prior order in this proceeding noted, however, the Nelson Industrial Steam Company (Nelson)

oject will require more energy over the life of the project han would be required to produce the same amount of steam and electricity separately. 1/

Moreover, the lack of opposition stems from the fact that the purchasing utility (Gulf States Utilities, Inc.) is one of the project sponsors. Under the majority's reasoning, if a technically identical project without any ownership interest by the purchasing utility sought a waiver, that utility could prevent certification by opposing the waiver. Hence, the Commission here establishes a double standard: nonqualifying facilities in which the purchasing utility has invested may be eligible for waiver; non-qualifying utilities opposed by the purchasing utility will not be eligible for a waiver. This is arbitrary and discriminatory.

Second, the majority states that the Nelson project will increase employment through short-term construction activity and will help insure the long-term economic viability of three of the sponsors' industrial facilities, which are in a depressed area. Under this reasoning, to be consistent, the Commission should grant all requests for waivers of the efficiency standard (as well as other criteria for QF status) whenever the facility would be located in a depressed area. Thus, proposed facilities in farm states, the Pacific Northwest, oil and gas producing areas, northern New England, and "rust belt" states should all be granted waiver of whatever QF criteria will allegedly add cost to the project. 2/

Moreover, these claimed benefits are hardly unique. Construction of every QF project provides short-term employment benefits and every cogeneration project helps ensure the long-term viability of the commercial or industrial facility that uses the thermal output. If the thermal output had no economic benefit, no one would buy it.

1/ Nelson Industrial Steam Company, 38 FERC ¶ 61,162, mimeo at 5.

2/ I note in this regard that the sponsors here have not even claimed that the facility will not be built without the requested waiver. Rather, they contend that if required to meet the standard their internal rate of return will be reduced from 46 percent to 22 percent. Thus, compliance with the efficiency standard would hardly seem to prevent completion of the project. Rather, compliance would merely reduce the projected rate of return on equity to a level that is still quite comfortable.

Finally, there is nothing in PURPA or its legislative history to indicate that Congress intended for QF certification to hinge on the consideration that a facility may provide economic stimulation to depressed areas. Congress has ample authority to provide for such relief through a variety of means. It did not choose to do so in section 210 of PURPA. I would also note in this regard that it was the Commission's intent in promulgating the QF certification rules that they be as objective as possible, so as to be largely self-implementing. 3/ The majority now enters upon the slippery slope of deciding, case-by-case, on wholly subjective considerations, whether particular regions are sufficiently depressed and projects sufficiently capital intensive, to warrant waiver of the standards for certification.

Third, the majority points out that in Phase II of the project, the facility will use fluidized bed combustion (FBC) boilers, "a technically advanced design which will use petroleum coke waste or coal as its primary fuel in an environmentally safe manner." This is a laudatory objective. However, it is hardly unique. The Commission has already certified approximately 120 facilities using FBC boilers, totaling 4,000 MW of capacity. There is no basis to distinguish these other facilities from the Nelson plant, with the possible exception that since almost all of these other facilities will use culm waste or biomass fuels over the entire life of the project, they are more deserving of waivers. These other projects if not already constructed, cannot rationally be denied waivers of the efficiency or operating standards. 4/ Similarly, future culm-fired FBC projects should also be excused from the efficiency standards if they seek cogeneration certification and the fossil-fuel use restrictions if they are waste-fueled small power facilities. Also, by analogy, the Commission also could not, without acting arbitrarily and capriciously, deny waiver of the fossil fuel input restrictions on solar powered facilities.

The majority also asserts that the waiver "will fulfill PURPA's goal of encouraging cogeneration, and allow the facility to ultimately utilize a waste fuel or coal as its primary energy source." This assertion rests on a misstatement of the goals of

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3/ Power Developers, Inc., 34 FERC ¶ 61,136 at 61,235 (1986).

4/ Consider in this regard that many of these facilities are located in economically depressed Northeast Pennsylvania, will inevitably contribute to the economy of the region and will use a waste fuel or coal in an environmentally desirable manner. The only remaining criteria applied to the Nelson facility which they do not meet is lack of opposition, which has been shown above to be fundamentally unsound.

RPA and an unsupported assumption of fact. The goal of PURPA s not to encourage cogeneration for the sake of cogeneration. The underlying purpose of encouraging certain cogeneration facilities is that they use fuel more efficiently by sequentially producing electricity and thermal energy outputs. That is why the Commission has operating and efficiency standards. As noted above, the Nelson facility will not only save no energy, it will require more energy than would be required to produce the same amount of steam and electricity separately. Hence, it will serve no statutory purpose with regard to cogeneration.

Second, as noted above, there is no evidence that the waiver will enable a facility to be built that would not otherwise be built. The record shows only that the project sponsors may derive less profit from the facility if required to meet the standards to which other cogeneration facilities are held. 5/ Failure to grant the waiver thus has no bearing on the project's ability ultimately to use petroleum coke or coal as a fuel.

The majority also draws comfort from Nelson's assurances that the project will proceed on a timely basis and that further waivers will not be needed. This, too, is no evidence of unique circumstances and gives me no comfort. Any applicant for a waiver can provide such assurances. Moreover, if Phase II is delayed

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5/ The Commission recently spoke to this issue in an essentially identical context in Power Developers, supra, wherein it stated:

> Power Developers also implies that without the additional revenues from the combustion turbine's output, its facility may not be economically feasible and, thus, no biomass will be burned at all. However, it has submitted no data from which the Commission can conclude that that will be the case. In any event, the Commission believes it would be inappropriate and administratively unsound to hinge the permissibility of a proposed use of gas on whether or not that use would make any given facility economically feasible. The regulations regarding qualifying status are intended to be largely self-implementing, based on objective criteria. Whether a particular facility will be economically feasible is a subjective judgment which the Commission believes is best left to project developers, who are in a position to assess the financial considerations of particular projects (footnote omitted).

34 FERC at 61,235.

otwithstanding the assurances, the chances of QF status being revoked are negligible. The utility, as an investor, will have no incentive to seek a revocation. As there are no follow-up reporting requirements in the regulations, the Commission would have no way of knowing, five years from now, whether the facility has been brought into compliance with the regulations. The Commission would need to look into the matter sua sponte and would only revoke QF status after a hearing. 6/ Also, this Commission cannot assure that further extensions would not be granted. It is unlikely that any of us will be here in five years and this Commission cannot bind future Commissions.

In this regard, the majority attempts to distinguish this proceeding from others by establishing a detailed construction schedule with numerous reporting requirements for the Nelson project. This is a futile gesture and may also have dire precedential effects. It is futile because once the project sponsors have spent any significant amount of money to go forward, the pressure to continue the waiver indefinitely, if requested, will be enormous, if not irresistible. The notion that after three or four years of preliminary work and the expenditure of tens of millions of dollars, our successors will be in a position to turn down requests for extension of the 60-month deadline are wholly implausible.

A second, and more serious concern is the precedential impact of imposing such conditions on qualifying facility certificates. As noted above, the QF certification rules were intended to be objective and largely self-implementing. The majority now embraces for the first time the very form of micro-management by this Commission that QFs are supposed to be freed from. This is, to say the least, unusual behavior on the part of a Commission that depicts itself as wanting to reduce regulatory burdens. 7/

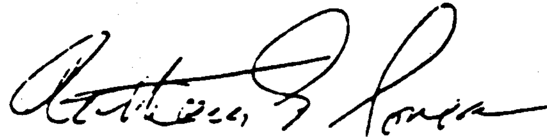
In sum, the majority's decision to get into the business of regulating QF construction activities has no redeeming virtue. It is inconsistent with the intent of our regulations and the Congressional intent to reduce regulatory burdens on QFs and it will be burdensome to the Commission and its staff. Moreover, our staff has little or no expertise in this area, which makes administration of these conditions a hollow exercise.

6/ See, Order No. 70, 45 Fed. Reg. 17,959 at 1,797, (March 13, 1980). Any such hearing would effectively extend the term of the waiver.

7/ This is all the more curious when one considers that the Commission has no direct authority to regulate construction of investor-owned electric utility power plants, let alone QFs.

Finally, the majority concludes with language to the effect that these are extremely narrow circumstances and that only in extraordinary cases will it waive the significant energy savings standard, as it does here. 8/ As shown above, there is nothing extraordinary about this case, and the supposedly narrow circumstances are in fact so broad as to apply to hundreds of facilities. Thus, the intimations that this case has no precedential impact are utterly hollow. If the majority proposes to treat this application as a special case, then it will only be able to exercise its discretion to deny many future waiver requests by arbitrary and discriminatory action.

For these reasons, I dissent.



Anthony G. Sousa
Commissioner

8/ It is also worth noting in this regard that the Commission's operating and efficiency standards are already low enough that the Commission has come under frequent criticism for promoting "PURPA machines," which are designed to maximize electrical output and save negligible amounts of energy. Here, the majority would dispense with even the minimal energy conservation requirements of the Commission's rules.

EVALUATION OF SUS RATES VS NISCO

YEAR	COST OF GEN. POWER IN NISCO ¢/KWH	COST OF PURCHASED POWER-GSU ON SUS ¢/KWH	CONOCO SAVINGS ¢/KWH	CONOCO POWER USAGE KWH $\times 10^6$/YR	POTENTIAL* SAVINGS $/YR
1 GAS OP.	3.02	3.48	0.46	450	2.07×10^6
2 GAS OP.	3.49	3.67	0.18	587	1.06 x10
3 GAS OP.	3.99	4.07	0.08	587	0.47×10^6
4 GAS OP.	4.14	4.53	0.39	587	2.29×10^6
5 COKE OP.	3.20	4.65	1.40	587	8.21×10^6
6 COKE OP.	3.08	4.65	1.57	587	9.22×10^6
7 COKE OP.	3.21	4.74	1.53	587	8.98×10^6
8 COKE OP.	3.34	4.96	1.62	587	9.51×10^6
9 COKE OP.	3.50	5.27	1.77	587	10.39×10^6
10 COKE OP.	3.67	5.51	1.84	587	10.80×10^6

* CONOCO ONLY SAVING IN NISCO VS PURCHASE FROM GSU ON SUS RATE. RATE SET BY GSU AND LA. PSC.

DOCKET NO. 7147

APPLICATION OF GULF STATES UTILITIES COMPANY FOR APPROVAL OF A JOINT VENTURE COGENERATION PROJECT AND TREATMENT OF REVENUES	§	PUBLIC UTILITY COMMISSION OF TEXAS

ORDER

In public meeting at its offices in Austin, Texas, the Public Utility Commission of Texas finds that, after statutory notice was provided to the public and interested persons, the application in this case was processed by an examiner in accordance with Commission rules and applicable statutes. An Examiner's Report containing Findings of Fact and Conclusions of Law was submitted, which report is hereby ADOPTED and made a part of this Order. The Commission further issues the following Order:

1. Findings of Fact Nos. 20, 21, 22 and 29 are hereby DELETED. New Findings of Fact Nos. 20, 21, 22, 29 and 29A are hereby ADOPTED and should read as follows:

[2] 20. Because the Venture is a qualifying facility as that term is defined under the Public Utility Regulatory Policies Act, the Commission has no jurisdiction to regulate its rates.

[3] 21. GSU is not required to obtain Commission approval of the transfer of Nelson Units 1 and 2 prior to its entering into a contract with the Venture.

[4] 22. It is not in the public interest for GSU's Texas ratepayers to pay in excess of GSU's avoided cost for purchased power from a qualifying cogeneration project.

29. In any future rate proceeding before this Commission, GSU is limited to recovering those purchased power payments to the Venture that do not exceed GSU's avoided costs.

29A. For those reasons set forth in Findings of Fact Nos. 1-29, the transfer of Nelson Units 1 and 2 to the Venture is in the public interest as long as it is done in accordance with the regulatory treatment recommended in the above findings.

2. Conclusion of Law No. 12 is amended to read as follows:

Pursuant to P.U.C. SUBST R. 23.66, GSU may recover its purchased power payments to the Venture as long as these payments do not exceed GSU's avoided cost.

3. Conclusion of Law No. 12A is ADOPTED and reads as follows:

GSU's transfer of Nelson Units 1 and 2 is in the public interest pursuant to Section 63 of the Act as long as the purchased power payments to the Venture do not exceed GSU's avoided costs.

The Commission further issues the following order:

1. The application of the Gulf States Utilities Company (GSU) for determination that the sale of Nelson Units 1 and 2 and the necessary and supporting facilities, is consistent with the public interest is GRANTED to the extent reflected in the Findings of Fact and Conclusions of Law made by the Commission.

2. GSU is hereby ORDERED to file with the Commission, within sixty days after the final Order in this case is rendered, the final journal entries which the GSU proposes to utilize to record the sale on its corporate books.

3. All motions, applications, proposed Findings of Fact and Conclusions of Law, and other requests or proposals for relief

not granted by the Commission, or ruled upon herein either expressly or by implication, are DENIED for want of merit.

4. This Order is effective on the date of signing.

SIGNED AT AUSTIN, TEXAS on this the 21st day of March 1988.

PUBLIC UTILITY COMMISSION OF TEXAS

SIGNED: Jo Campbell
JO CAMPBELL

SIGNED: Marta Greytok
MARTA GREYTOK

I dissent. I believe the joint venture proposal would have benefitted both ratepayers and shareholders, and was a good faith effort to deal with the changing economics of large industrial customer energy needs and the potential for industrial self-generation. GSU brought the proposal to the Commission for approval because of the unusual buyback provisions, triggered by fluctuating gas prices. GSU amended the proposal to share the profits from the sale of assets with ratepayers.

I believe the proposal should be viewed as a negotiated industrial, simultaneous sale and purchase agreement. The purchase agreement terms should not be limited by avoided cost because, unlike cogeneration under PURPA, the relationship is voluntary. With the offsetting requirement that the industrial customer buy additional power whenever the repurchase price goes above avoided cost, the larger body of ratepayers are protected.

The avoided cost standard was intended to ensure that ratepayers were indifferent to cogeneration purchases. In other words, they would pay no more than they would under utility generation. In the present case, strict adherence to the avoided cost standard is a misapplication because ratepayers will be

worse off if the joint venture does not go forward. I therefore respectfully dissent from the decision of the majority to limit purchases to avoided cost.

SIGNED: [signature]
DENNIS L. THOMAS

ATTEST:

[signature]
PHILLIP A. HOLDER
SECRETARY OF THE COMMISSION

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INQUIRY INTO THE LEGALITY OF THE SERVICES, PRACTICES AND RATES OF NUECES ELECTRIC COOPERATIVE, INC. RELATING TO SWITCHOVERS	§	DOCKET NO. 6928

July 30, 1987

Examiner's Report adopted. Cooperative ordered to cease and desist certain practices with respect to customer switchovers.

[1] COMPLAINTS AND DISPUTES - BILLING DISPUTES - SWITCHOVERS

The term "idle" as used in P.U.C. SUBST. R. 23.44(b)(i) relates to the usefulness of facilities to the disconnecting utility rather than to a third party.

[2] COMPLAINTS AND DISPUTES - BILLING DISPUTES - SWITCHOVERS

For purposes of calculating the disconnection fee authorized by P.U.C. SUBST. R. 23.44(b)(i), revenue obtained from the in-place sale of facilities, or the amount of the offer where the disconnecting utility declines to sell, constitutes salvage value.

[3] COMPLAINTS AND DISPUTES - BILLING DISPUTES - SWITCHOVERS

The practice of requiring payment by a non-member of a cooperative for the removal of distribution facilities from a location no longer served by the cooperative as a precondition to the release of the service location to another utility legitimately falls within the scope of regulated activity, and consequently, no charge can be assessed in that instance which is not specifically authorized by tariff.

[4] COMPLAINTS AND DISPUTES - BILLING DISPUTES - SWITCHOVERS

If the connecting utility in a switchover situation offers to purchase from the disconnecting utility any distribution facilities idled by the switchover and further offers to provide a liability indemnity guarantee as to those facilities, the disconnecting utility cannot charge the disconnecting customer for the cost of removal of those facilities should the disconnecting utility refuse to sell.

DOCKET NO. 6928

INQUIRY INTO THE LEGALITY OF THE SERVICE, PRACTICES AND RATES OF NUECES ELECTRIC COOPERATIVE, INC. RELATING TO SWITCHOVERS	§	PUBLIC UTILITY COMMISSION OF TEXAS

EXAMINER'S REPORT

I. Procedural History

On June 30, 1986, the Commission's general counsel filed an Original Petition of Inquiry into the legality of the service, practices and rates of Nueces Electric Cooperative, Inc. (NEC or the Cooperative) relating to customer switchovers of electric service from NEC to Central Power and Light Company (CP&L), alleging that the practices of NEC in this regard constitute a violation of NEC's tariff, the Commission's Substantive Rules and the Public Utility Regulatory Act (the Act), Tex. Rev. Civ. Stat. Ann. art. 1446c (Vernon Supp. 1987).

By order dated July 17, 1986, the examiner directed NEC to file a written answer to the allegations set forth in the petition of inquiry and scheduled a prehearing conference to address procedural matters.

NEC filed an Original Answer on August 1, 1986, specifically denying each of the allegations set forth in general counsel's petition.

A prehearing conference was convened on August 19, 1986, with the undersigned examiner presiding, at which time appearances were made by Mr. Earnest Casstevens and Mr. Sam Burris on behalf of the Cooperative, and Mr. Frank Davis on behalf of the Commission staff. During the conference, the parties agreed upon a schedule for discovery and the prefiling of testimony. The hearing on the merits was scheduled for December 10, 1986.

By examiner's order dated August 20, 1986, NEC was directed, pursuant to P.U.C. PROC. R. 21.25(a)(3), to provide notice of this proceeding to its current customers by bill insert in the Cooperative's September billings.

On August 22, 1986, general counsel filed a First Revised Petition of Inquiry, expanding the scope of the inquiry to include relief for non-members of the Cooperative who occupy premises previously occupied by a member of NEC and who want to take electric service from CP&L rather than NEC. The amended petition further requests that NEC be required to itemize switchover charges on all cost quotations and bills rendered to customers who desire to switch service from NEC to CP&L.

At the request of general counsel, NEC was directed by examiner's order dated September 8, 1986, to mail written notice of this proceeding, by no later than September 19, 1986, to all non-members who may have requested within the last two years that NEC's equipment be removed from their premises.

On September 8, 1986, NEC filed the affidavit of its general manager warranting that notice of this proceeding was mailed or hand delivered to each affected customer of the Cooperative and to certain other individuals. On September 19, 1986, the Cooperative filed a second affidavit reflecting the mailing of notice of this proceeding to the non-members who requested within the last two years, through September 16, 1986, that NEC's equipment be removed from their premises.

On September 24, 1986, NEC filed a motion for decision on the pleadings. The motion was denied by examiner's order dated October 21, 1986.

On September 25, 1986, general counsel filed a motion for leave to amend its petition to include a request that refunds be ordered of all charges assessed, demanded and collected illegally for the removal of idled NEC equipment from customer premises within the two years immediately preceding the original filing in this docket. By order dated September 26, 1986, the examiner granted general counsel's motion for leave to amend its petition.

On October 1, 1986, Mr. William J. Marek filed a motion to intervene. By examiner's order dated October 2, 1986, Mr. Marek was conditionally granted intervenor status, subject to the filing of timely objections to the request.

No objections to Mr. Marek's motion were filed, and his intervention became permanent on October 8, 1986.

On October 6, 1986, Mr. William Dunaway filed a motion to intervene, which motion was conditionally granted by examiner's order dated October 9, 1987. The intervention became permanent on October 14, 1986.

On November 18, 1986, general counsel filed a motion to compel NEC to produce certain information sought in requests for information served upon NEC, and by order dated November 24, 1986, the examiner scheduled a prehearing conference for December 4, 1986, to address the merits of the motion. However, NEC provided certain of the requested materials on December 2, 1986, as an attachment to NEC's response to the motion to compel. Although a prehearing conference was convened on December 4, 1986, to address general counsel's motion, neither general counsel nor NEC made appearance at the prehearing conference.

On November 20, 1986, general counsel filed a motion requesting the issuance of a commission to subpoena Mr. Duane Ricketson, an employee of CP&L. In response thereto, the examiner issued a Subpoena Duces Tecum and Praecipe Order for Issuance of Subpoena on November 24, 1986.

On December 9, 1986, general counsel filed a second motion to compel, which motion was subsequently denied by oral ruling of the examiner on December 10, 1986, at the commencement of the hearing on the merits.

The hearing on the merits was convened on December 10, 1986, with the undersigned examiner presiding. Appearances were made by Mr. Earnest Casstevens and Mr. Sam Burris on behalf of NEC, Mr. William Dunaway and Mr. William Marek on their own behalf as <u>pro</u> <u>se</u> intervenors, and Mr. Frank Davis on behalf of the Commission staff. After approximately 2½ days of hearing, the hearing on the merits was temporarily recessed and was subsequently reconvened on December 22, 1986. The hearing concluded on December 22, 1986.

By order dated January 20, 1987, the briefing schedule established at the close of the hearing was indefinitely suspended due to substantial delays in obtaining a written transcript of the hearing. By order dated February 3, 1987, a revised briefing schedule was established by the examiner. Pursuant to the revised briefing schedule, NEC and general counsel filed post hearing briefs on February 18, 1987, and reply briefs on February 27, 1987.

The Commission has jurisdiction over the matters raised in this proceeding pursuant to Sections 16, 17(e), 35, 37 and 38 of the Act.

II. Introduction

Nueces Electric Cooperative, Inc. provides retail electric utility service within a geographically and economically diverse service area encompassing parts of Nueces, Jim Wells, Kleberg, Kenedy, Duval, Live Oak, McMullen and Brooks Counties. A substantial portion of the geographical area certificated to NEC is also certificated to Central Power and Light Company (CP&L). Individuals and entities located within those dually certificated areas have the option of taking service form either NEC or CP&L. The transfer of service from one utility to another utility, in areas which are certificated to more than one utility, is commonly referred to as a "switchover." The primary motivations for switchovers appear to be differences in rates or quality of service between utilities. While the record does not establish that a difference in quality currently exists between service provided by NEC and service provided by CP&L, the record does reflect that NEC's current rates for residential service are higher than the rates for residential service currently charged by CP&L.

Recognizing that the ability to switch service from one utility to another utility within dually certificated areas is advantageous from the standpoint of the customer who desires to switch service, yet is disadvantageous from the perspective of the utility whose customers are migrating to the system of a competing utility, and further recognizing that this divergence of interests creates the potential for switchover disputes between customers and utilities, the Commission adopted a substantive rule on December 27, 1979, which attempts

to balance equitably the competing interests of the disconnecting customer and the disconnecting utility and to insure that switchovers are handled in a fair and consistent manner. The substantive rule requires each utility to incorporate its switchover policy in its tariff and establishes general parameters regarding permissible charges which can be assessed the disconnecting customer by the disconnecting utility. The Commission's policy regarding switchovers is embodied in P.U.C. SUBST. R. 23.44(b)(1) [formerly Rule 052.02.04.048(b)] which provides as follows:

> (1) Where service is being switched between electric companies, the electric utility disconnecting such customer shall be permitted to charge the customer a disconnection fee of an amount set forth in its tariff, and such fee shall be based upon the average direct labor and vehicle costs of disconnecting such customer and any distribution facilities rendered idle and not usable elsewhere on the system based upon the original cost of such facilities less depreciation and salvage. Prior to any disconnection under this section, the customer shall pay the disconnecting electric utility for service up through the date of disconnection and the charges for disconnection set forth in this section. Upon payment of such charges the utility shall give the customer a paid receipt. The connecting electric utility may not provide service to said customer until it has evidence from the disconnecting electric utility that the customer has paid for electric service through the date of disconnection and any charges for disconnection under this section.

This policy has not been changed by the Commission in any respect since its initial adoption in 1979.

In compliance with the requirement in the substantive rule that each utility's switchover practices be set forth in its tariff, NEC revised its tariff to include Section 204.8, pertaining to switchover fees, which section was approved by the Commission on December 1, 1981. Section 204.8 of the NEC tariff, which has been in effect without modification since 1981, provides as follows:

204.8 Switchover Fee.

> Where service to a Member is being switched between the Cooperative and another electric utility, the following charges shall apply when the Cooperative is the disconnecting utility:

A. A charge of $106.00. (This charge covers average labor and transportation costs incurred in making the disconnect.)

B. Any unpaid construction, line extension, or other contract charges.

C. A charge for removal of any property, plant or facilities of the Cooperative used to provide service to the Member if the customer requests removal or removal is required for legal or safety reasons, or by requirement of any authority:

	Single-phase	Multi-phase
First Span	$362.00	$555.00
Each Additional Span	$ 51.00	$ 78.00

D. A charge for distribution facilities rendered idle as a result of the disconnection and not usable on another part of the Cooperative's system based on the original cost of such facilities less depreciation, salvage and contributions in aid of construction, but including the cost of removing idled plant deemed by the Cooperative to be economically salvageable.

E. Prior to disconnection, the Member shall pay the Cooperative for all service up through the date of disconnection as well as the charges set forth in this tariff. Upon receipt of payment, the Cooperative shall give the Member a paid receipt.

In accordance with Public Utility Commission of Texas Substantive Rule 052.02.04.048(b), the Cooperative Member is hereby advised that the connecting electric utility may not provide service to said member until such connecting utility has evidence from the Cooperative that the Member has paid for electric service through the date of disconnection and any charges for disconnection under this tariff.

The petition of inquiry which forms the basis of this docket does not allege that NEC's tariff is inconsistent with the requirements of P.U.C. SUBST. R. 23.44(b) nor does it assert that NEC's tariff should be revised in any respect, although general counsel was afforded the opportunity to expand the inquiry to include a request that the tariff be modified. Rather, the petition of inquiry focuses solely upon general counsel's contention that NEC's practices with respect to customer switchovers are inconsistent with the terms of NEC's tariff, the Commission's substantive rules and PURA.

It is undisputed that when an NEC customer requests that service be switched from NEC to CP&L, NEC requires as a precondition to the switchover that all above-ground NEC facilities used to serve the customer be removed from the customer's premises and that the customer bear the cost of removal. Removal of the facilities is required by NEC even in instances where either the customer or CP&L desires to purchase all or part of the facilities for use in providing service to the customer by CP&L. NEC asserts that this practice is reasonable and necessary in order to minimize NEC's potential liability exposure, and is supportable under the terms of Section 204.8(c) of its tariff which authorizes assessment of a charge for removal of facilities used to provide service to the customer where removal is required for legal or safety reasons.

General counsel avers in its petition of inquiry that this practice is designed to thwart the wishes of NEC's customers to switch their electric supplier. The petition asserts that Section 204.8(c) of NEC's tariff is intended to cover instances where equipment is in such dangerous condition that further use would result in an immediate hazard, and that removal of NEC facilities as a matter of course at the customer's expense, based upon a "specious legal hazard of negligence liability," is not authorized by Section 204.8(c) of NEC's tariff. Additionally, general counsel asserts that P.U.C. SUBST. R. 23.44(b)(1) does not contemplate an automatic charge for removing the utility's equipment based upon potential negligence liability. Finally, general counsel argues that the practice of routinely removing all NEC facilities amounts to an artificial, unnecessary and unreasonable restraint upon the rights of a customer to be treated reasonably and justly, within the meaning of P.U.C. SUBST. R. 23.1, and the right of a dually certificated utility not to be interfered with when a customer requests that the utility provide electric service to it, within the meaning of P.U.C. SUBST. R. 23.44(a).

The portion of P.U.C. SUBST. R. 23.1 relied upon by general counsel provides as follows:

> This chapter is intended to establish a comprehensive regulatory system to assure rates, operations, and services which are just and reasonable to the consumer and the utilities and to establish the

> rights and responsibilities of both the utility and consumer. This chapter shall be given a fair and impartial construction to obtain these objectives...

The portion of P.U.C. SUBST. R. 23.44(a) relied upon by general counsel provides as follows:

> ...Each utility shall construct, install, operate, and maintain its plant, structures, equipment, and lines in accordance with these standards, and in such manner to best accommodate the public, and to prevent interference with service furnished by other public utilities insofar as practical.

Finally, the petition alleges that NEC has ignored the requirement imposed by P.U.C. SUBST. R. 23.46(j) that a dispute resolution procedure be articulated to the consumer. However, general counsel subsequently conceded NEC's compliance with the requirement at the hearing on the merits and this allegation is no longer at issue.

General counsel maintains in the petition of inquiry that the common practice in switchovers is for the new utility to purchase those facilities of the disconnecting utility which can be used to provide service to the customer. Accordingly, general counsel requests that NEC's practice of removing facilities as a matter of course at the customer's expense and its refusal to sell such facilities in place be found to be in violation of PURA, the Commission's substantive rules and NEC's tariff, that NEC be directed to cease and desist from those practices, and that in switchover situations NEC be ordered to negotiate in good faith with the connecting utility regarding the sale in place of idled NEC facilities which could be used by the connecting utility to provide service to the customer.

Subsequent to the filing of the petition of inquiry, general counsel filed an amended petition requesting that NEC be required to itemize, on cost quotations and bills rendered to disconnecting customers, all switchover charges which it assesses. The amended petition further requests that the switchover charges authorized by NEC's tariff be found inapplicable in instances where an individual who is not a member of NEC purchases property served by NEC and

wishes to switch service from NEC to CP&L, on the basis that the language used in NEC's tariff speaks only to charges which can be assessed to "members."

Finally, prior to the hearing on this matter, general counsel filed a second amended petition in which it requested that NEC be ordered to refund all charges illegally assessed, demanded and collected from its customers for removal of idled equipment within the past two years.

In addition to the issues outlined in general counsel's petition of inquiry, further issues have been raised by the two pro se intervenors in this proceeding, Mr. Marek and Mr. Dunaway. Mr. Marek asserts that the $106.00 charge authorized by Section 204.8(a) of NEC's tariff for average labor and transportation costs incurred in making a disconnect is excessive. General counsel opposes Mr. Marek on this issue and contends that the charge is reasonable and appropriate. Mr. Marek further alleges that the quotation of switchover costs provided him by NEC regarding the transfer of Mr. Marek's service from NEC to CP&L is excessive and is unreasonable when compared to the cost quotations provided to other similarly situated customers of NEC.

Mr. Dunaway, not a member of NEC, purchased a residence in a dually certificated area just outside of the city limits of the city of Kingsville and requested that NEC remove its electrical facilities from the premises. NEC charged Mr. Dunaway $768.48 to remove the facilities, which Mr. Dunaway paid under protest. Asserting that the assessment of a charge for removal of NEC facilities from property owned by a non-member is not authorized by NEC's tariff and is consequently illegal, Mr. Dunaway seeks the issuance of a Commission order directing NEC to refund the charges Mr. Dunaway paid, with interest, and directing NEC to reimburse Mr. Dunaway for the costs which he incurred in connection with this proceeding. Mr. Dunaway estimates his costs at $38.00 for a motel room, $91.00 for mileage for round trip travel from Kingsville to Austin, $35.00 for meals and $16.00 for long distance phone calls and postage.

III. Opinion

The hearing on the merits in this proceeding was unnecessarily long and divisive. Further, the record generated during the hearing is somewhat unfocused and confused. As a consequence, the factual issues raised by general counsel and the intervenors are difficult to resolve based upon the evidence of record. Nonetheless, a discussion and proposed resolution of each of the issues raised in this inquiry follows below.

A. Removal of Facilities

As discussed previously, it is undisputed that NEC follows a consistent practice of removing distribution facilities at the disconnecting customer's expense when a switchover renders the continued installed presence of the facilities no longer useful to the cooperative in serving its members. The legality of this practice is the fundamental issue raised by general counsel's inquiry. General counsel views this practice as what can best be termed a "scorched earth" policy designed to discourage customer switchovers, and in fact the practice increases the cost of a switchover to the customer and forces the connecting utility where necessary to engage in the uneconomic duplication of removed facilities. NEC counters that removal of distribution facilities rather than abandonment in place or sale of the facilities to the customer or the connecting utility is necessary to avoid continuing liability exposure in connection with such facilities, and that the practice is permitted under the express terms of NEC's tariff.

With respect to the liability issue, Mrs. Meridene Woodson, a member of NEC's board of directors, testified that injuries or death caused by electric shock, falling poles, or collision with an erect or fallen pole or conductor can give rise to large damage claims. Further, Mrs. Woodson testified that if idled facilities are left in place, the cooperative has a continuing obligation to maintain the facilities. Mr. Jerry Whitworth, NEC's general manager, testified to similar effect. Mrs. Woodson takes the position that prudent business practice and protection of NEC's members dictates that the cooperative minimize

its negligence liability exposure by removing facilities which are no longer necessary for the provision of service to its members.

In its original petition of inquiry, general counsel characterizes NEC's negligence liability concerns as "specious." The examiner does not agree with this characterization. Under Texas law, negligence on the part of an electric utility consists of a breach of duty to exercise reasonable care and diligence in preventing injuries to persons or property. An electric company's negligence may consist of either an act or omission and whether a given state of facts constitutes negligence depends upon what a reasonably prudent person would have done under existing circumstances. See Community Public Service Company v. Dugger, 430 S.W.2d 713 (Tex. Civ. App. - Texarkana 1968, no writ). This is not an unusually stringent standard. It is not at all inconceivable that a utility could be found negligent in failing to remove facilities which are no longer necessary for the provision of utility service, especially where the potential for harm is foreseeable and there is no benefit derived from retention of the facilities in place to offset the hazard occasioned by the presence of the facilities. While a utility is always subject to potential negligence liability in connection with transmission and distribution facilities, there is a valid distinction in the examiner's mind between involuntary liability exposure arising from the presence of facilities which are necessary to the provision of service to the public and voluntary exposure to liability arising from the continued presence of facilities which no longer serve a necessary function. Further, the fact that a utility carries liability insurance does not obviate the need for concern regarding exposure to risk. The examiner finds that prudent business practice dictates that a utility take such steps as may be necessary to minimize its liability exposure from idled distribution facilities which are no longer necessary in providing of service.

General counsel argues that NEC's liability exposure can be avoided by the sale in place of facilities idled by a switchover to the disconnecting customer or to the connecting utility. However, Mrs. Woodson testified that NEC will not sell its facilities in such situations based upon advice of NEC's legal counsel to the effect that the sale of facilities does not relieve the cooperative of

continuing negligence liability and may, under Texas products liability law, expose the cooperative to strict liability.

If the sale of idled facilities is subject to products liability law, the consequences which flow from that fact are substantial. As noted in NEC's brief, introduction into the stream of commerce of a product rendered dangerous to life or limb by reason of some defect imposes liability on the seller not only to the purchaser but to anyone else who might be injured by the product sold. Furthermore, a seller is subject to liability following sale of a nondefective product which the seller can anticipate may undergo change and become unreasonably dangerous. Darryl v. Ford Motor Company, 440 S.W.2d 630 (Tex. 1969), Hamilton v. Motor Carrier Industries, Inc., 569 S.W.2d 571 (Tex. Civ. App. -- Texarkana 1978, no writ). As noted by NEC, in a strict product liability action, the only defenses are assumption of risk and unforeseeable product misuse. Duncan v. Cessna Aircraft Co., 665 S.W.2d 414 (Tex. 1984).

It is far from certain, however, that the sale of idled facilities in the context of a customer switchover subjects a utility to strict liability. Strict liability actions in Texas are governed by the rule stated in Restatement (Second) of Torts, Sec. 402A(1966), McKisson v. Sales Affiliates, Inc., 416 S.W.2d 787, 788-90 (Tex. 1967), although Texas courts have expanded the risks which fall within its scope. Hamilton v. Motor Carrier Industries, Inc., 569 S.W.2d at 575. Section 402A provides as follows:

> **§ 402A. Special Liability of Seller of Product for Physical Harm to User or Consumer**
>
> (1) One who sells any product in a defective condition unreasonably dangerous to the user or consumer or to his property is subject to liability for physical harm thereby caused to the ultimate user or consumer, or to his property, if
>
> (a) the seller is engaged in the business of selling such a product, and
>
> (b) it is expected to and does reach the user or consumer without substantial change in the condition in which it is sold.
>
> (2) The rule stated in Subsection (1) applies although
>
> (a) the seller has exercised all possible care in the preparation and sale of his product, and

(b) the user or consumer has not bought the product from or entered into any contractual relation with the seller.

Under Section 402A, liability attaches only if the seller is engaged in the business of selling the product that causes harm. Therefore, the key question in evaluating NEC's strict liability argument is whether, in making sales of idled distribution facilities in the context of switchovers, NEC would be considered to be engaged in the business of selling distribution facilities. Comment f to Section 402A makes a distinction between an "occasional seller" and one who is "engaged in the business of selling a product" and provides that Section 402A is not intended to apply to the occasional seller who is not engaged in that activity as a part of his business. Although Texas courts have not yet addressed in any detail the distinction between "occasional sellers" and those "engaged in the business of selling" for purposes of determining in what instances strict liability should attach as a consequence of a sale, the Fifth Circuit has had occasion to construe Texas law on this issue in Galindo v. Precision American Corp., 754 F.2d 1212 (5th Cir. 1985). That case involved an appeal from the granting of a motion for summary judgment in a strict products liability action predicated on the theory that the defendant's sale of a used piece of equipment subjected the corporation to strict liability under Texas products liability law.

On the basis that comment f to Section 402A reflects that the occasional seller category applies where sales are so infrequent or sales efforts are so minimal that it cannot be said that the seller has voluntarily assumed a special responsibility for product safety, that the public has a right to expect that the seller will stand behind the product, or that the seller is best able to spread the loss caused by the products' defects, the Fifth Circuit held that the relevant inquiry in determining whether sales of depreciated owner-user equipment places the seller in the category of "one engaged in the business of selling" is whether the seller's conduct would justify a conclusion that (1) he has undertaken a special responsibility for product safety; (2) the public has a right to expect that he will stand behind the product; and (3) as between the consumer and the seller, it is equitable to impose upon the seller the loss caused by the product and the burden of spreading that loss as a cost of doing

business. The Fifth Circuit further indicated that, as it read Texas law, a determination of whether one is engaged in the business of selling depends on an analysis of the totality of the circumstances surrounding sales efforts, in the light of the rationale underlying imposition of strict liability.

The Fifth Circuit's guess as to what the Texas Supreme Court would hold with respect to this unsettled issue of Texas law is not of great precedential value. However, the court's analysis in Galindo v. Precision American Corp. appears to the examiner to be quite sound. Under the standard enunciated by the Fifth Circuit, the examiner believes it unlikely that NEC would be found to be engaged in the business of selling electrical distribution facilities as a consequence of the occasional sale of idled facilities in the context of customer switchovers. Nonetheless, it is not beyond the realm of possibility that Texas courts could construe the "occasional seller" category so narrowly that strict liability could attach as a consequence of such sales. The examiner would note that the record reflects that NEC is not alone in its concern over the possibility of application of products liability law to the sale or purchase of distribution facilities. On cross-examination by general counsel, Mr. Richard Byrne, a CP&L District Marketing Manager called to testify at the request of general counsel, indicated that because of product liability concerns by CP&L, the decision to purchase particular NEC facilities by CP&L would necessarily be made on a case by case basis at the executive level.

Although Texas product liability law constitutes a reasonable basis for concern that the sale in place of idled facilities may not exempt NEC from continuing liability exposure with respect to such facilities, general counsel notes in his brief that NEC could avoid such through execution of an indemnity agreement with the purchaser. NEC argues that as a consequence of the Texas Workers' Compensation Act, Tex. Rev. Civ. Stat. Ann. art. 8306 (Vernon Supp. 1987), only the seller is liable in a personal injury action brought by an employee of the purchaser and that the seller has no right of indemnity or contribution against the seller. NEC cites Varela v. American Petrofina, 658 S.W.2d 561 (Tex. 1983) in support of that proposition. However, that case pertains to a statutory tort action for contribution under Section 2(b) of Tex.

Rev. Civ. Stat. Ann. art. 2212a, in the instance where no written indemnity agreement exists. Section 3(d) of Article 8306 provides as follows:

> (d) If an action for damages on account of injury to or death of an employee of a subscriber is brought by such employee, or by the representatives or beneficiaries of such deceased employee, or by the association for the joint use and benefit of itself and such employee or such representatives or beneficiaries, against a person other than the subscriber, as provided in Section 6a, Article 8307, Revised Civil Statutes of Texas 1925, and if such action results in a judgment against such other person, or results in a settlement by such other person, the subscriber, his agent, servant or employee, shall have no liability to reimburse or hold such other person harmless on such judgment or settlement, nor shall the subscriber, his agent, servant or employee, have any tort or contract liability for damages to such other person because of such judgment or settlement, <u>in the absence of a written agreement expressly assuming such liability</u>, executed by the subscriber prior to such injury or death.

[Emphasis added]

Where a written indemnity agreement exists between the seller and the purchaser which expresses in clear and unequivocal terms that the purchaser will indemnify the seller against any and all injury or damages attributable to the manufacture, maintenance or sale of the facilities in question, including injury or damage arising as a consequence of the seller's own negligence, it is clear that that contractual right to indemnity is valid and enforceable. <u>See</u>, <u>Dorchester Gas Corp. v. American Petrofina</u>, 710 S.W.2d 541 (Tex. 1986). Thus, in instances where the purchasing utility agrees to a satisfactory indemnity agreement in connection with the purchase of facilities in place from NEC, the examiner is of the opinion that NEC has no legitimate basis for concern that it will be subject to continuing risk of financial liability with respect to such facilities. The examiner would emphasize, however, that this conclusion is limited to the purchase of facilities by the connecting utility. This is because an indemnity agreement is only useful where the purchaser has adequate financial resources to fulfill the agreement should the need arise. From a practical standpoint it is doubtful that an indemnity agreement would provide any substantial protection if the facilities are purchased by a residential customer.

In summary, the examiner finds that prudent business practice dictates that a utility take such steps as may be necessary to minimize its liability exposure from idled distribution facilities which are no longer necessary in providing service. The examiner further finds that NEC's liability exposure with respect to such facilities can be eliminated by removal of the facilities, or alternatively, by the sale in place of such facilities in instances where the connecting utility enters into a legally adequate indemnity agreement with NEC with respect to the transferred facilities.

The foregoing discussion of liability exposure with respect to idled facilities is essential to the formulation of a reasoned decision regarding the propriety of NEC's practice of routinely removing its facilities from the property of a disconnecting customer, at the customer's expense, in the context of a switchover. There is no question but that NEC has the right to remove its facilities in such instances. Section 305.8 of NEC's tariff makes it clear that NEC retains ownership of all facilities utilized to provide service to its customers regardless of whether the facilities were paid for by a customer or the cooperative, and Section 351.5 of NEC's tariff expressly states that NEC has the right upon discontinuance to dismantle and remove all lines, equipment, apparatus or other facilities which the cooperative may have installed to provide service to a member. Thus, the real question is not whether NEC has the right to remove idled facilities as a matter of course in a switchover, but rather, whether NEC has the right to charge the disconnecting customer for the cost of removal.

Section 204.8(c) of NEC's tariff provides that, in a customer switchover, NEC may charge the disconnecting customer for removal of any property, plant or facilities of the cooperative used to provide service to the customer if removal is requested by the customer or if removal is required for legal or safety reasons. NEC asserts that, due to the liability considerations discussed above, removal of the idled facilities is necessary for both legal and safety reasons

and that NEC is therefore entitled to charge the disconnecting customer for the costs of removal.

In the examiner's opinion, where removal of facilities idled by a switchover is the only reasonable means by which NEC can eliminate exposure to continued liability risk with respect to such facilities, removal is required for legal and safety reasons within the meaning of Section 204.8(c) of NEC's tariff and the cooperative is therefore entitled to charge the costs of removal to the customer. However, NEC's practice of routinely charging disconnecting customers for the costs of removal of facilities in every switchover situation is unsupportable under any reasonable construction of Section 204.8(c) of NEC's tariff.

As previously noted, removal of facilities is not the only means by which NEC can eliminate continued liability exposure. Such exposure can also be eliminated through sale of the facilities to the connecting utility where the connecting utility expressly agrees to indemnify NEC for any subsequent liability arising from those facilities. Consequently, where the connecting utility offers to purchase the facilities and agrees to enter into a satisfactory indemnity agreement with the disconnecting utility, the examiner finds that a removal of the facilities is not necessitated by legal or safety considerations.

In the above instance, the offer to purchase obviates the need to remove the facilities for legal or safety reasons. At that point, the need to remove the facilities can only arise as a consequence of the utility's refusal to sell. The decision to sell or not to sell rests purely on the discretion of the cooperative. The Commission lacks any authority to require consummation of the

sale[1]. However, where the cooperative refuses to sell to a qualifying buyer, the cooperative has in effect voluntarily brought upon itself the liability risk of which it complains. In such an instance, the costs of eliminating the risk which the cooperative voluntarily assumed by its own actions should appropriately fall upon NEC rather than the disconnecting customer. In the examiner's opinion, Section 204.8(c) of NEC's tariff cannot reasonably be construed as authorizing NEC to charge a disconnecting customer for the cost of removal of idled facilities, where no legal or safety reason for removal of the equipment exists, in the absence of deliberate and voluntary actions of the cooperative itself. To interpret Section 204.8(c) in any other fashion would be to permit the tariff provision to be used in a manner in which it was not intended, to wit: as an artificial economic impediment to the ability of a customer in a dually certificated area to switch electrical suppliers.

The examiner notes that under this construction of NEC's tariff, NEC would be permitted to charge for removal of idled facilities in the instance where not all of the facilities idled by switchover are purchased by the connecting utility. The examiner reaches this conclusion on the basis that, as the cooperative has not received an offer of purchase for those facilities in that instance, the cooperative has no option other than removal as a means of eliminating potential liability exposure associated with the unpurchased equipment.

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[1] It is well settled Texas law that an administrative agency has only such powers as are expressly conferred on it by statute, together with those necessarily implied from powers and duties expressly given or imposed. Stauffer v. City of San Antonio, 344 S.W.2d 158 (Tex. 1961) PURA does not provide express authority for the Commission to require the involuntary divestiture of utility assets, and such authority is not reasonably inferable. Indeed, with regard to the sale or purchase of facilities by a public utility, PURA does not authorize the Commission to prohibit the transaction, even where the Commission finds that the transaction is not in the public interest. Rather, the Commission's authority in that regard is limited under PURA Section 63 to disallowance of the effect of the transaction in the rate making

process where it is found that the transaction will unreasonably affect rates or service.

The examiner also notes that under the above construction of NEC's tariff, the disconnecting utility could not charge the disconnecting customer for the cost of removal of idled facilities which the connecting utility is willing to purchase, even though the purchase price offered may fall below the net book value of the facilities in question. This is not inequitable to the cooperative because, under the terms of Section 204.8(d) of NEC's tariff, NEC is authorized to charge the disconnecting customer for distribution facilities rendered idle as a result of the disconnection and not usable on another part of the cooperative's system, based upon the original cost of the facilities less depreciation, salvage and contributions in aid of construction. It seems clear to the examiner that the purchase price obtained from the sale in place of idled facilities constitutes salvage value. The disconnecting customer can be charged for any difference between net book value and the realized sales price pursuant to Section 204.8(d). Thus, neither NEC nor its remaining members would be required to suffer a loss on idled facilities sold to the connecting utility in the instance where the facilities are sold for less than net book value.

With respect to the issue of appropriate charges for removal of facilities, it appears that although NEC relies upon Section 204.8(c) of its tariff as its authority to charge for the removal of idled facilities as a matter of course, the record reflects that NEC does not in fact assess the removal charges specified in that subsection of the tariff. According to Mr. Hank Brown, system engineer for NEC, NEC customers requesting disconnection in switchovers are billed for the cost of labor to remove the facilities at rates specified in REA Form 792, which is a standard labor contract for installation and removal of distribution facilities which NEC awards each year on a competitive bid basis and forwards to the Rural Electrification Administration for review and approval. The removal work is performed by Industrial Electric Corporation, an NEC subcontractor, rather than by NEC personnel. The record does not reflect why NEC charges actual labor costs as opposed to the fixed charges specified in Section 204.8(c) of the tariff. Section 204.8(d) of the tariff permits NEC to charge a disconnecting customer for the cost of removing idled plant deemed by

the cooperative to be economically salvageable. Apparently, NEC is relying upon Section 204.8(c) for the authority to remove the facilities and upon Section 204.8(d) for authority to charge actual removal costs. Although NEC's current practice with respect to removal charges appears inconsistent with the terms of its tariff, the examiner recommends that NEC continue to charge actual labor costs in any instance where removal of facilities is accomplished for any reason specified in Section 204.8(c) of the tariff, and that it be required to amend its tariff to conform to its actual practice.

Although no party to this proceeding has requested modification of this portion of NEC's tariff, the examiner suggests that this modification is necessary for three reasons. First, the charges specified in Section 204.8(c) of the tariff bear no meaningful relationship to the actual labor costs associated with removal. Second, the use of a fixed charge to cover the variable costs associated with removal of idled facilities gives rise to potential inequity to both the customer and the cooperative. Depending upon the amount of work involved, the costs of removal may be substantially below or above the fixed charges specified in Section 204.8(c). Third, amendment of Section 204.8(c) as suggested would conform NEC's tariff to its current practice. Charging actual labor costs per REA Form 792 is a reasonable and equitable practice. Indeed, the purpose of a removal charge should be to recoup the cost of removal rather than to constitute a profit center or source of loss for the cooperative. The examiner submits that the assessment of actual removal costs is particularly appropriate where some but not all of the idled NEC facilities are useful to the connecting utility in providing service to the customer, and consequently only the useful facilities are purchased. In that instance, the fixed charges in Section 204.8 of the tariff, which are set in terms of "spans," will likely be very much out of line with the costs of removing the isolated remaining pieces of idled NEC equipment. In the examiner's opinion the concept of "spans" is not particularly applicable in the context of isolated pieces of idled equipment, or in reference to residential service in general. Further, the term is not defined in NEC's tariff although its meaning could be a subject ripe for dispute.

The examiner strongly urges that Section 204.8(c) of NEC's tariff be amended to conform to NEC's current practice of charging customers the actual labor costs incurred by NEC in removing facilities for any reason specified in that section of NEC's tariff.

B. Valuation of Idled Plant

Section 204.8(d) of NEC's tariff permits NEC to assess a variable charge for the value of distribution facilities rendered idle as a result of disconnection and not usable on another part of the cooperative's system based upon the original cost of such facilities less depreciation, salvage and contributions in aid of construction. Two fundamental issues have been raised with respect to this subsection of NEC's tariff: First, whether NEC distribution facilities used to serve a disconnecting customer can be considered "idle" if the connecting utility is willing to purchase the facilities; and second, whether NEC currently utilizes an acceptable methodology for calculating original cost of facilities less depreciation and salvage.

With respect to the first issue, general counsel asserts in its post hearing briefs and through the testimony of staff witness Harold Hughes that distribution plant may not reasonably be declared idled in a switchover where the connecting utility is willing to purchase the facilities. In the examiner's opinion, this assertion is incorrect. The purpose underlying this charge, which is expressly authorized by P.U.C. SUBST. R. 23.44(b)(1), is to insure that a utility and its ratepayers are not required to bear any loss with respect to facilities which are no longer useful to the utility as a consequence of a customer switchover. The term "idle" must necessarily relate to the usefulness of facilities to the disconnecting utility if the intent underlying the Commission's substantive rule is to be effectuated. In the examiner's opinion, the meaning of the term "idle" cannot reasonably be construed as being dependent upon whether all or part of the facilities in question may currently or in the future be useful to a third party.

Although the examiner disagrees with the general counsel on this issue, the disagreement is conceptual rather than substantive in nature. For instance, recognizing that the disconnecting utility should not suffer a loss on facilities which are no longer useful to it as a consequence of a switchover, staff witness Hughes testified that if there is a below net book value sale, "...the selling utility could accept what the buying utility offers and charge the difference to the customer." This cannot, however, be accomplished under NEC's tariff if the term "facilities rendered idle" in Section 204.8(d) of the tariff is defined as meaning facilities which cannot be of use to the connecting utility, since the customer cannot be charged for facilities which have not been idled.

[1,2] The examiner submits that a plain reading of P.U.C. SUBST. R. 23.44(b)(1) and Section 204.8(d) of NEC's tariff dictates the conclusion that the term "idle" is intended to mean those facilities which are no longer useful <u>to the disconnecting utility</u> as a consequence of a switchover. Revenue obtained from the in-place sale of the facilities, or the amount of the offer where the disconnecting utility declines to sell, clearly constitutes salvage value. Finally, to the extent that net book value of the facilities exceeds the salvage value, P.U.C. SUBST. R. 23.44(b)(1) and Section 204.8(d) of the tariff both unequivocally provide that the customer may be charged the difference.

The second issue concerning valuation of idled plant under Section 204.8(d) concerns the propriety of the methodology utilized by NEC to calculate net book value of facilities rendered idle by a switchover. This issue was never raised in general counsel's pleadings. However disposition of the issue is necessary to a fair resolution of this inquiry. As general counsel did not allege any impropriety regarding NEC's methodology for determining net book value in its petition of inquiry, the question of how NEC calculates net book value was not addressed in the prefiled testimony of any party to this proceeding. The issue arose for the first time in the middle of the hearing on the merits as a consequence of the examiner's clarifying examination of NEC witness Hank Brown, who is charged with responsibility for calculating the value of idled facilities:

Q: All right. With regard to Nueces Exhibit No. 4, the columns pertaining to material cost and extended material cost, how are those cost amounts determined? If you could explain that to me once again.

A: The cost on the labor?

Q: Is that the depreciated cost of the material?

A: Oh, this price?

Q: That's correct.

A. This is our latest current material prices. Then the 50 percent --

Q: You mean the new price?

A: Salvage.

Q: This 50 percent salvage, I assume is not depreciation?

A" That accounts for some depreciation, yes, sir.

Q: So you do not calculate your material costs, you calculate your material costs based on the new costs of the equipment rather than depreciated costs, taking into consideration the remaining life of the equipment in question?

A: Yes, sir. Then I account for it at the end.

Q: How did you determine this 50 percent salvage: Is that sort of just a ballpark kind of estimate? You can say, give a little depreciation here and eyeballing the equipment, we think about 50 percent of it will be reusable?

A: Yes, sir, more or less, that is correct.

(Tr. at 154-155)

Mr. Brown subsequently testified on clarifying cross that he uses the current replacement price for a piece of equipment as approximation of the depreciated original installed cost of facilities.

At the conclusion of NEC's direct case, general counsel requested to present rebuttal testimony on this issue, which request was denied in large part because expansion of the scope of the inquiry at that stage of the proceedings appeared unreasonable in light of the already lengthy and unfocused nature of

the hearing. The staff's rebuttal testimony on that issue was accepted as an offer of proof and the examiner advised the parties that the issue of whether NEC's methodology for calculating net book value is reasonable would be resolved by reference to NEC's tariff and the testimony solicited on cross-examination regarding that issue.

Based upon a preponderance of the record evidence, the examiner finds that NEC's practice of using current materials prices as a substitute for original cost less depreciation of idled facilities is unreasonable and unwarranted. Although NEC's tariff specifically requires use of net book value, as does the Commission's substantive rules, the individual charged with making that calculation testified that he was not even aware of whether or not NEC's plant in service accounts permit one to determine accumulated depreciation on specific items of equipment.

NEC argues in its brief that estimation of original cost less depreciation by some method is necessary because neither the cooperative nor any other utility keeps plant in service or depreciation records by installed service extension, by items of equipment or even by aggregates of numbers of items of the same piece of equipment. Accepting NEC's assertion as correct, that fact does not support the reasonableness of the method utilized by NEC. Neither Mr. Brown nor any other NEC witness testified that the method utilized by NEC to approximate net book value was reasonable nor did any NEC witness suggest that some credible basis exists which would support the use of current materials prices to approximate net book value. The examiner can ascertain no consistent or meaningful relationship between materials replacement prices and depreciated original cost.

Mr. Richard Byrne, a district marketing manager for CP&L, testified that for purposes of establishing value for facilities which CP&L is interested in purchasing from a utility, CP&L would look at the installed date of the materials and at CP&L's average installed cost for the corresponding date years and would then apply depreciation. This implies to the examiner that CP&L maintains continuing property records which contain data useful in determining

the installed cost of materials in prior years. There is no reason to believe that NEC does not also maintain records of a similar nature which would be useful in approximating original installed costs. NEC's general manager, Mr. Whitworth, testified on cross-examination that original cost could only be obtained from the original work order, and indicated that NEC maintains some but not all of its work orders on file in its office. It would seem that where the original work order is not available, original cost could be approximated from work orders of similar vintage. Mr. Whitworth indicated on cross-examination that NEC's poles bear a mark reflecting the date each pole was made. It would seem that that date might be useful in approximating vintage.

The methodology used by Mr. Brown to approximate net book value does not in any fashion take into consideration the age of the idled facilities. Mr. Brown testified on cross-examination by Mr. Marek that he does not perform any field work. Rather, he relies on the staking sheets furnished by NEC's field crew in preparing cost estimates. Mr. Brown is the only individual at NEC who determines the value of idled facilities. A review of NEC's staking sheets reflects that they bear no comments or notations regarding visual inspection by the field crew for age or condition of the facilities. The preponderance of the evidence reflects that Mr. Brown calculates a value for facilities idled by a switchover without any consideration for the age or condition of the facilities. The examiner believes that NEC has an obligation to estimate net book value (where actual values are not available) using a methodology which, at a minimum, attempts to determine the approximate age of the facilities, the approximate labor and materials costs for that vintage, and the approximate remaining service life of the facilities. Accordingly, the examiner concludes that NEC should be required to formulate and implement a new methodology for estimating net book value consistent with these criteria.

C. Removal Charges For Non-Members

General counsel's first amended petition of inquiry requests that the switchover charges authorized by NEC's tariff be found inapplicable in instances where an individual who is not a member of NEC purchases property served by NEC

and wishes to switch service from NEC to CP&L. The basis for this request lies with the previously described circumstances of Mr. Dunaway, a non-member of NEC who, upon purchasing a new residence in a dually certificated area, desired to obtain electrical service from CP&L rather than NEC, although NEC's facilities were connected to the residence. Mr. Dunaway testified that CP&L would not provide service to Mr. Dunaway's residence as long as NEC's facilities were in place. According to Mr. Dunaway, he orally informed NEC in July 1986, that he was purchasing the residence in question, that he had elected to take service from CP&L, and that he wanted NEC to remove their facilities. Mr. Dunaway subsequently made a written request on August 6, 1986, that NEC remove its facilities. The letter indicated that he would not pay to have any of the equipment removed and would assess NEC a daily rental charge for any NEC equipment remaining on this property after August 12, 1986. According to Mr. Dunaway, the letter was written after he became enraged in NEC's offices in Robstown.

Mr. Dunaway testified that after discussions with Mr. Underbrink with CP&L, and Mr. Irish and Mr. Davis with the Commission staff, he elected to pay NEC under protest for removal of the facilities and seek a Commission order directing NEC to make restitution for the charges. After payment of removal charges to NEC in the amount of $768.48, NEC issued a letter on August 12, 1986, to Mr. Underbrink informing CP&L that Mr. Dunaway had paid for removal of NEC facilities and that the letter constituted NEC's release of the service location to CP&L.

The arguments presented by the parties are straightforward. Mr. Dunaway asserts that Section 204.8 of NEC's tariff by its express terms specifies charges which may be assessed members of the cooperative, and that as he is not and has never been a member of the cooperative, the fees assessed by NEC are illegal. NEC responds that it did not assess switchover fees to Mr. Dunaway under authority of its tariff. Rather, NEC charged a non-member for removal of cooperative facilities at the request of the non-member, and the transaction is essentially a private matter outside of the legitimate purview of the Commission.

Mr. Brown testified that no switchover charges were assessed Mr. Dunaway and that NEC simply charged Mr. Dunaway for removal of NEC facilities from his property, as demanded. The cooperative's general manager, Mr. Whitworth, testified that NEC receives requests from the City of Corpus Christi as well as other entities, asking that NEC's facilities be removed or relocated, and NEC charges removal charges in those instances. Mr. Whitworth implies that Mr. Dunaway should not be treated in any different fashion.

It is worth noting that although Mr. Brown testified that NEC did not apply Section 204.8(d) of NEC's tariff to Mr. Dunaway, he indicated that he calculated the charges using the same methodology as used by NEC to compute the variable switchover costs under Section 204.8 of NEC's tariff. Indeed, a review of the cost summary sheet supporting the removal charges assessed Mr. Dunaway reflects that Mr. Dunaway was charged for labor costs for removal of facilities, labor costs for installation of a new dead end pole and associated equipment off of Mr. Dunaway's property, the cost of materials associated with the new construction and the net book value less salvage of the retired facilities. Clearly, NEC's assertion that Mr. Dunaway was charged solely for the cost of removal of the facilities is incorrect.

The heart of this dispute is whether requiring payment of removal charges as a condition to removal of facilities from a location no longer served by NEC and the release of the service location to CP&L is a practice which falls within the scope of legitimate Commission regulation. The line between those utility activities which are subject to regulation and those which are not is not always finely drawn. The application of reasoned judgment is essential to that determination.

The examiner finds that the above activity legitimately falls within the scope of regulated activity because it has a fundamental impact on a customer's ability to select his electric supplier of choice within a dually certificated area. NEC will not release the service location unless removal charges are paid. CP&L will not serve the location until it has been released by NEC. NEC's practice effectively denies a customer the right to be served by CP&L

unless the customer bears the cost of removal of NEC facilities. This situation is readily distinguishable from other instances where facilities are requested to be removed or relocated, since in those instances, NEC's practices will not substantially affect the rights of a customer to obtain electric service.

[3] The Commission has the authority to regulate this practice under the terms of PURA Section 17(e) which gives the Commission exclusive original jurisdiction over the rates, operations and services not within the incorporated limits of a municipality exercising exclusive original jurisdiction over those rates, operations and services. The practice of requiring the payment of removal charges by a non-member as a condition to removal of the facilities and release of the service location falls within the definitions of both "rate" under PURA Section 3(d) and "service" under PURA Section 3(s). Consequently, the charges which NEC may assess in this circumstance are appropriately determined by the Commission.

PURA Section 46 provides that a utility cannot "...directly or indirectly, by any devise whatsoever or in any manner, charge, demand, collect, or receive from any person a greater or less compensation for any service rendered or to be rendered by the utility than that prescribed in the schedule of rates of the public utility applicable thereto..." As NEC's practice falls within the legitimate scope of Commission regulation, NEC cannot assess a charge to Mr. Dunaway for removal of facilities unless that charge is specifically applicable under the terms of NEC's tariff. A review of NEC's tariff reveals that Section 204.8 is the only tariff provision authorizing a charge for removal of NEC facilities. Section 351.5 of NEC's tariff, which speaks to the dismantling of facilities, provides that NEC may dismantle facilities upon discontinuance of service to the member (in this case the prior owner of the Dunaway residence) and that the cooperative may at its option abandon in place its <u>underground</u> lines and equipment in lieu of removal of such facilities, but it does not authorize the imposition of a charge for removal.

The examiner finds that Section 204.8 of NEC's tariff does not authorize assessment of removal charges in the instance where the purchaser of a residence

previously served by one utility desires to obtain service from another utility. The express language of Section 204.8 of NEC's tariff speaks to charging members of the cooperative for the cost of removal of facilities. It does not authorize a charge assessable against non-members.

As a matter of equity one could argue that Section 204.8 should be construed as being applicable to non-members, on the basis that it is unfair to require members of a non-profit utility to bear the costs of removal of facilities as a consequence of the sale of a residence to an individual who elects not to obtain service from the utility even though the utility's facilities are already in place and available to serve the individual. However, one can also argue on equity grounds that it is unfair to charge an individual for the cost of removal of facilities which he never requested be installed and which he never utilized, especially in light of Section 351.5 of NEC's tariff, which appears to contemplate removal rather than abandonment in place of above ground facilities which are no longer useful in providing service at a discontinued service location.

Finding that it is appropriate to construe Section 204.8 of NEC's tariff narrowly, as not being applicable to non-members of the cooperative, and further finding that a narrow interpretation of Section 204.8 does not permit NEC to charge a non-member for the cost of removal of facilities in a subsequent owner situation, the examiner concludes that NEC was not authorized to charge Mr. Dunaway $768.48 for the removal of NEC facilities.

Mr. Dunaway has requested that the Commission issue an order requiring the refund of $768.48 in charges assessed by NEC for removal of facilities, plus accrued interest. Mr. Dunaway has further requested payment by NEC of $180.00 in expenses which he incurred as a consequence of his participation in this docket. As the examiner has found that the charges assessed by NEC against Mr. Dunaway were not authorized by NEC's tariff, the examiner recommends that NEC be ordered to refund $768.48 to Mr. Dunaway within ten days from the date of the final order in this docket, together with accrued interest from the date of payment of the charges by Mr. Dunaway, at the applicable interest rate for customer deposits specified by P.U.C. SUBST. R. 23.43(c)(3) for the period of time over which the monies were held by NEC.

With respect to Mr. Dunaway's request for recovery of expenses incurred in litigating this matter, the examiner has found no authority in support of the proposition that the Commission can assess litigation costs incurred by a private intervenor against a public utility. Therefore, the examiner urges that Mr. Dunaway's request for recovery of actual expenses from NEC be denied.

D. Marek Complaint

As discussed previously, Mr. Marek also intervened in this inquiry, alleging that the $106.00 charge authorized by Section 204.8(a) of NEC's tariff

for average labor and transportation costs incurred in making a disconnect is unreasonable, and further alleging that the quotation of switchover costs provided him by NEC regarding the transfer of service from NEC to CP&L is excessive and unreasonable as compared to the cost quotations provided to other similarly situated customers of NEC. Although Mr. Marek obtained a cost quotation from NEC regarding the costs of switching service to CP&L, Mr. Marek had not switched service to CP&L as of the date of the hearing in this matter.

With respect to the fixed $106.00 switchover fee, the examiner finds that the preponderance of the admittedly scant evidence on this issue supports a finding that the rate is reasonable. It should be noted that Mr. Marek presented no evidence in support of his assertion that the rate is excessive nor did he suggest an alternative rate level which he believed would be more appropriate than the currently tariffed charge. In the absence of any evidentiary support for Mr. Marek's allegation, the examiner must lend some weight to the fact that the rate has been addressed and approved by the Commission in prior NEC rate proceedings. Further, a review of the tariff provisions pertaining to switchovers contained in the tariffs of neighboring cooperatives of NEC reveals that the fixed charge contained in NEC's tariff falls well within the range of charges authorized by the tariffs of those cooperatives. In light of the foregoing, the examiner urges that the Commission make no attempt to modify, in this proceeding, the fixed charge currently authorized in Section 204.8(a) of NEC's tariff. Rather, the examiner would suggest that the NEC be ordered to fully document the cost support for the rate in next general rate proceeding.

With regard to Mr. Marek's assertion that the quotation of switchover costs provided by NEC is excessive and unreasonable as compared to the cost quotations provided to neighboring NEC customers, the examiner finds that the differences in facilities configuration between Mr. Marek's service drop and those of other NEC customers generally support the differences in cost quotations of which Mr. Marek complains.

Mr. Marek was provided a switchover cost summary by NEC on June 12, 1986, which, when corrected for errors in addition, reflects total costs of labor and materials less salvage of $623.70. Of that amount, $470.41 is attributable to labor and $153.29 to the cost of idled facilities not usable elsewhere on NEC's system.

The record reflects that the primary reason for the higher level of Mr. Marek's charges as compared to certain other customers is that Mr. Marek's service drop crosses a CP&L pole to which primary voltage CP&L lines are attached. Removal of Mr. Marek's facilities thus requires work on an energized NEC pole and an energized CP&L pole. This is referred to as "hot" work. The labor contract between NEC and Industrial Electric Corporation specifies that the labor prices in the contract apply solely to work with unenergized lines and that the labor prices will be increased by 50 percent for work on energized lines. As almost all of the equipment to be removed in Mr. Marek's instance is on energized poles, the labor charges are considerably higher than for customers whose circumstances require less hot work.

The current labor contract for facilities installation and removal became effective May 19, 1986. As prior contracts presumably provide for different labor charges and those contracts are not in the evidentiary record, the examiner reviewed cost summaries in the record for three individuals requesting switchovers after the effective date of the contact: Mr. Marek, Mr. Dunaway, and Mr. Garcia. The designation of "hot" work appeared correct in all three instances, after review of the staking sheet for each individual. Also, the application of contract labor prices appeared correct in Mr. Marek's instance, although Mr. Garcia's cost summary reflecting that labor was overstated for one item and understated for two other items.

If one assumes that CP&L does not wish to purchase the facilities serving Mr. Marek, and if one concurs in the examiner's finding that removal of facilities is necessary for legal and safety reasons where there exists no other way to avoid continuing liability exposure as to those facilities, the examiner finds that Mr. Marek's labor charges are correct.

However, as the service drop to Marek's residence actually attaches to a CP&L distribution pole, the examiner believes CP&L may well be willing to purchase some of the NEC facilities. If CP&L is willing to purchase some of the facilities and to provide NEC an adequate indemnity agreement with respect to those facilities, Mr. Marek's labor costs should decrease dramatically since a substantial amount of the equipment will not need to be removed. Should NEC refuse to sell to CP&L, Mr. Marek's labor costs will still be reduced dramatically, because in that instance, NEC can assess removal charges solely under authority of Section 204.8(d) of its tariff which provides that the cooperative can charge removal costs only in instances where idled plant not usable elsewhere on NEC's system is deemed by the cooperative to be "economically salvageable."

[4] The term "economically salvageable" can by any definition mean only that the value of the equipment exceeds the cost of removal. If the value of equipment not being utilized or sold in place is less than the labor costs associated with removal, the equipment has a negative salvage value. Clearly, an item must have a positive salvage value to be deemed "economically salvageable" under Section 204.8(d). A review of Mr. Marek's cost summary worksheet reveals not one instance in which the listed cost of any of the idled materials come even close to the cost of removal listed for that item. Thus, if CP&L offers to purchase with an indemnity guarantee, and NEC refuses to sell, NEC cannot charge Mr. Marek for the cost of removal of the facilities.

With respect to the cost of materials the examiner notes that, regardless of whether NEC has an offer to purchase the facilities or not, NEC can charge Mr. Marek for the depreciated cost less salvage of only those materials which are not usable elsewhere on NEC's system. The examiner has some concern that NEC may be charging Mr. Marek for materials which can be used elsewhere on NEC's system.

The cost summary provided to Mr. Marek reflects that NEC proposed to charge Mr. Marek $306.59 for the cost of materials, less 50 percent salvage, for a total materials cost of $153.29. When queried by Mr. Marek regarding the

salvage offset, NEC witness Brown testified that "...what I was trying to say there was that I was -- hopefully we could use 50 percent of all of these material items back somewhere else." The fair implication from this statement is that Mr. Brown thought that approximately 50 percent of the facilities which would be idled if Mr. Marek switched his service to CP&L would be reusable on other parts of NEC's system. If this is in fact the case, the assessment of a charge for the depreciated value of those facilities, less salvage, is in violation of Section 204.8(d) of NEC's tariff.

There is not sufficient information in the record for the examiner to determine what Mr. Marek's switchover costs should appropriately be. Therefore, the examiner makes the following recommendations. First, NEC should be required to inquire as to whether CP&L is willing to purchase any of the facilities used to serve Mr. Marek, subject to provision of a sufficient indemnity agreement. Second, NEC should be required to designate which of the items contained on Mr. Marek's cost summary are in fact reusable on other parts of NEC's system and to delete any materials costs associated with those items. Third, NEC should be required to provide to Mr. Marek (as well as all other individuals requesting a switchover cost quote) a specific salvage estimate for each component part of the service drop rather than providing a lump sum salvage estimate for the entire aggregation of materials. Finally, based upon the billing requirements and limitations discussed herein, a revised cost quotation should be provided to Mr. Marek within 30 days of the date of the final order in this docket.

E. Conclusions

Although the examiner disagrees with general counsel's reasoning in a number of respects, the examiner concurs with general counsel's assertion that NEC's practices with regard to customer switchovers have generally been inconsistent with the requirements of Section 204.8 of NEC's tariff and P.U.C. SUBST. R. 23.44(b)(1). Accordingly, the examiner concurs in general counsel's request that NEC be ordered to cease and desist from its present practices to the extent that they conflict with its tariff and the Commission's substantive rules as discussed herein. The examiner also concurs in general counsel's

requests that the switchover charges authorized by NEC's tariff be found inapplicable in subsequent owner situations and that NEC be required to itemize on cost quotations and bills rendered to disconnecting customers all switchover costs which are being assessed. The examiner cannot, however, concur in general counsel's request that NEC be ordered to refund all charges illegally assessed, demanded and collected from its customers for removal of idled equipment within the past two years. There is simply insufficient evidence of record to determine which customers may have been charged inappropriately for a switchover or what the appropriate charges should have been. Although a number of switchover cases were discussed in the record, Mr. Dunaway was the only customer of those whose situations were discussed who actually switched service to CP&L and the examiner has already recommended that a refund be required in that instance. Absent evidence concerning individuals who in fact paid switchover charges to NEC during the last two years, and absent the facts necessary to determine what the appropriate charges should have been, any order requiring that refunds be made would be too vague to enforce. Therefore, the examiner recommends that within 30 days of the date of the final order in this docket, NEC be required to furnish general counsel with a list of all such customers, together with the supporting documentation of the charges paid by those customers. General counsel may then review the specific cases and file an inquiry seeking the recovery of refunds for specific customers, in those instances, if any, where general counsel deems such action to be appropriate.

The examiner's specific recommendations are as follows:

1. NEC should be ordered to cease and desist its present practices with respect to customer switchovers to the extent that they may be inconsistent with the examiner's construction of the NEC tariff, as discussed herein.

2. Section 204.8(c) of NEC's tariff should be amended to require that, where removal of facilities is undertaken for any reason specified in that subsection, only the actual labor costs incurred in accomplishing removal may be assessed.

3. NEC should be directed to refund to Mr. Dunaway within 10 days from the date of the final order in this docket, $768.48, plus accrued interest from the date of payment of the charges to the date of refund at the applicable interest rates for customer deposits specified by P.U.C. SUBST. R. 23.43(c)(3) for the period in question.

4. NEC should be required to itemize on cost quotations and bills rendered to disconnecting customers all switchover costs which are being assessed to the customer.

5. NEC should be required to specify on its cost summary sheets those pieces of equipment which are reusable on other parts of the cooperative's system and should further specify the precise amount of salvage estimated for each component part of the service drop affected by the switchover.

6. NEC should be required within 30 days of the date of the final order in this docket to formulate and implement a new methodology for estimating net book value which, at a minimum, attempts to determine the approximate age of the facilities, the approximate labor and materials costs for that vintage, and the approximate remaining service life of the facilities.

7. Within 30 days from the date of the final order in this docket, NEC should be required to furnish general counsel with a list of all individuals who switched service from NEC to CP&L from the date of the final order in this docket to a period of two years prior to the date of initiation of this inquiry by general counsel, together with the supporting documentation of the charges paid by each of those individuals.

8. Within 30 days from the date of the final order in this docket, NEC should be required to provide a revised switchover cost quotation to Mr. Marek, calculated in accordance with the tariff construction

discussed in the examiner's report and itemizing the specific data addressed in recommendation number five, above.

9. NEC should be required to provide full evidentiary support for the fixed switchover changes contained in Section 204.8(a) of NEC's tariff in NEC's next general rate proceeding.

IV. Findings of Fact and Conclusions of Law

The examiner further recommends adoption of the following findings of fact and conclusions of law:

A. Findings of Fact

1. Nueces Electric Cooperative, Inc. (NEC) is an electric utility providing retail electric utility service within its certificated service area, under Certificate of Convenience and Necessity No. 30126.

2. On June 30, 1986, the Commission's general counsel filed a petition of inquiry into the legality of the service, practices and rates of NEC relating to customer switchovers of electric service from NEC to Central Power and Light Company (CP&L).

3. NEC provided notice of this proceeding to its current customers by bill insert in NEC's September, 1986, billings, and by individual mailing to the non-members of the cooperative who requested within the last two years preceding initiation of the inquiry through September 16, 1986, that NEC's equipment be removed from their premises.

4. Intervenor status was requested by Mr. William J. Marek and Mr. William Dunaway, both of whose requests were granted without opposition.

5. Prehearing conferences were convened in this docket on August 19, 1986, and on December 4, 1986.

6. The hearing on the merits was convened on December 10, 1986. Testimony was taken on December 10, 11, 12 and 22, 1986. The hearing was adjourned on December 22, 1986. Appearances were made at the hearing by Mr. Earnest Casstevens and Mr. Sam Burris on behalf of NEC, Mr. William Dunaway and Mr. William Marek as pro se intervenors, and Mr. Frank Davis on behalf of the Commission staff. Post-hearing briefs and reply briefs were timely filed by NEC and general counsel.

7. A substantial portion of the geographical service area certificated to NEC is also certificated to CP&L.

8. The transfer of service from one utility to another utility, in areas which are certificated to more than one utility, is commonly referred to as a "switchover."

9. The Commission adopted a substantive rule pertaining to switchovers on December 27, 1979, which rule has remained in effect without substantive change since that date.

10. Section 204.8 of NEC's tariff, approved on December 1, 1981, governs the charges which may be assessed by NEC in connection with a switchover.

11. General counsel's petition of inquiry does not request modification of Section 204.8 of NEC's tariff but rather seeks its proper enforcement.

12. When an NEC customer requests that service be switched from NEC to CP&L, NEC requires as a condition to the switchover that all above-ground NEC facilities used to serve the customer be removed from the customer's premises and that the customer bear the cost of removal.

13. NEC requires removal of facilities even where the customer or CP&L desires to purchase all or part of the facilities for use in providing service to the customer by CP&L.

14. NEC bases its requirement of removal of facilities and its refusal to sell facilities upon the need to minimize its potential liability exposure, and NEC charges the customer for the cost of removal in reliance upon Section 204.8(c) of jits tariff, which permits the customer to be charged for removal where removal is required for legal or safety reasons.

15. General counsel's petition requests that NEC's practice of refusing to sell facilities and charging the customer for the cost of removal in instances where CP&L desires to purchase the equipment be found to be improper, that NEC be ordered to cease and desist from engaging in such practices, that NEC be required to itemize switchover costs on all cost quotations and bills, that the assessment of switchover charges against a non-member of NEC be prohibited in subsequent owner situations, and that NEC be ordered to refund all charges illegally assessed, demanded and collected for removal of idled equipment over the two years prior to the date of initiation of this inquiry.

16. Mr. William Dunaway requests refund plus accrued interest of the amount charged him by NEC to remove its facilities from his property, and $180.00 in expenses incurred in participating in this docket.

17. Mr. Marek requests that NEC's fixed and variable switchover charges be found to be excessive and inconsistently applied among customers requesting switchover.

18. NEC's negligence liability concerns are not specious.

19. The negligence standard applicable to electric utilities is not an unusually stringent standard.

20. It is conceivable that a utility could be found negligent in failing to remove facilities which are no longer necessary for the provision of utility service by the disconnecting utility, especially where the potential for harm is foreseeable and where there is no benefit derived from retention of the

facilities in place to offset the hazard occasioned by the presence of the facilities.

21. Prudent business practice dictates that a utility take such steps as may be necessary to minimize its liability exposure from idled distribution facilities which are no longer necessary to the provision of service.

22. NEC will not sell its facilities, based upon advice of its legal counsel to the effect that the sale of facilities does not relieve the cooperative continuing liability and may in fact expose the cooperative to strict liability.

23. To the extent that the sale of idled facilities is subject to products liability law, the consequences which flow from that fact are substantial.

24. It is far from certain that the sale of idled facilities in the context of a customer switchover subjects a utility to strict liability.

25. The key question in evaluating NEC's strict liability argument is whether, in making sales of idled distribution facilities, NEC would be considered to be "engaged in the business" of selling distribution facilities.

26. It is unlikely that NEC would be found to be engaged in the business of selling electrical distribution facilities as a consequence of the occasional sale of idled facilities in the context of customer switchovers.

27. NEC is not alone in its concern over the possibility of application of products liability law to the sale or purchase of distribution facilities.

28. Because of CP&L's product liability concerns, the decision to purchase particular NEC facilities by CP&L would be made on a case by case basis at the executive level.

29. Liability exposure can be eliminated by removal of facilities, or alternatively, by the sale in place of such facilities where the connecting utility enters into a legally adequate indemnity agreement.

30. In instances where a purchasing utility agrees to a satisfactory indemnity agreement in connection with the purchase of facilities in place from NEC, NEC has no legitimate basis for concern that it will be subject to continuing risk of financial liability with respect to such facilities.

31. From a practical standpoint, it is doubtful that an indemnity agreement would provide any substantial protection if the facilities are purchased by a residential customer.

32. Where removal of facilities idled by a switchover is the only reasonable means by which NEC can eliminate its exposure to continued liability risk with respect to such facilities, removal is required for legal and safety reasons.

33. NEC's practice of routinely charging every disconnecting customer for the costs of removal of facilities in every switchover situation is unsupportable under any reasonable construction of Section 204.8(c) of its tariff.

34. An offer to purchase facilities and to enter into a sufficient indemnity agreement with respect to such facilities eliminates any need to remove idled facilities for legal or safety reasons.

35. Where NEC refuses to sell to a qualifying buyer, the cooperative has voluntarily wrought upon itself the liability risk of which it complains and in such instance, the cost of eliminating the risk should appropriately fall upon NEC rather than the disconnecting customer.

36. Section 204.8(c) of NEC's tariff cannot reasonably be construed as authorizing it to charge a disconnecting customer for the cost of removal of idled facilities where there is no legal or safety reason for removal of the equipment in the absence of deliberate and voluntary actions of the cooperative itself.

37. Under the examiner's construction of Section 204.8(c) of NEC's tariff, NEC could not charge the disconnecting customer for the cost of removal of idled

facilities which the connecting utility is willing to purchase, even though the purchase price may fall below the net book value of the facilities.

38. The purchase price obtained from the sale in place of idled facilities constitutes salvage value.

39. The disconnecting customer can be charged for any difference between net book value and the realized sales price of idled facilities pursuant to Section 204.8(d) of NEC's tariff.

40. Although NEC relies upon Section 204.8(c) of its tariff as its authority to charge for the removal of idled facilities as a matter of course, NEC does not in fact assess the removal charges specified in that subsection of the tariff.

41. NEC customers requesting disconnection in switchovers are billed for the cost of labor to remove the facilities at rates specified in REA Form 792.

42. Although NEC's current practice with respect to removal charges is inconsistent with the terms of its tariff, NEC should be required to continue to charge actual labor costs in any instance where removal of facilities is accomplished for any reason specified in Section 204.8(c) of NEC's tariff.

43. The recommendations in Finding of Fact No. 42 are based upon the fact that the charges specified in Section 204.8(c) of the tariff bear no meaningful relationship to the actual labor costs associated with removal, the use of a fixed charge to cover the variable costs associated with removal of idled facilities gives rise to potential inequity to both the customer and the cooperative, and amendment of Section 204.8(c) would conform NEC's tariff to its current practice.

44. The concept of "spans" is not particularly applicable in the context of isolated pieces of idled equipment, or in reference to residential service in general, and as the term is undefined in NEC's tariff, its meaning could be a subject ripe for dispute.

45. Section 204.8(d) of NEC's tariff permits it to assess a variable charge for the value of distribution facilities rendered idle as a result of disconnection and not usable on another part of NEC's system, based upon the original cost of such facilities less depreciation, salvage and contributions in aid of construction.

46. The term "idle" in Section 204.8(d) of NEC's tariff necessarily relates to the usefulness of facilities to the disconnecting utility and cannot reasonably be construed as relating to whether all or part of the facilities in question currently are or will in the future be useful to a third party.

47. NEC's practice of using current materials prices as a substitute for original cost less depreciation of idled facilities is unreasonable and unwarranted.

48. There is no consistent or meaningful relationship between materials replacement prices and depreciated original cost.

49. For purposes of establishing value for facilities which CP&L is interested in purchasing, CP&L would look at the installed date of the materials and at its average installed cost for the corresponding date years and then apply depreciation.

50. CP&L's methodology for approximating net book value is reasonable.

51. The methodology used by NEC to approximate net book value does not in any fashion take into consideration the age of the idled facilities.

52. NEC should be required to estimate net book value where actual values are not available using a methodology which, at a minimum, attempts to determine the approximate age of the facilities, the approximate labor and materials costs for that vintage, and the approximate remaining service life of the facilities.

53. Mr. Dunaway, although not a member of NEC, was charged $768.48 by NEC to remove NEC's facilities from Mr. Dunaway's property.

54. CP&L would not provide service to Mr. Dunaway until NEC removed its facilities from Mr. Dunaway's property.

55. NEC charged Mr. Dunaway for labor costs for removal of facilities, labor costs for installation of a new dead end pole and associated equipment off of Mr. Dunaway's property, the cost of materials associated with the new construction and the net book value, less salvage, of the retired facilities.

56. NEC's assertion that it charged Mr. Dunaway solely for the cost of removal of idled facilities is incorrect.

57. NEC's practice of not releasing a service location in a subsequent owner situation until removal charges have been paid legitimately falls within the scope of regulated activity because it has a fundamental impact on the subsequent owner's ability to select his electric supplier of choice within a dually certificated area.

58. NEC cannot assess a charge to Mr. Dunaway for removal of facilities unless that charge is specifically applicable under the terms of NEC's tariff.

59. Section 204.8 of NEC's tariff is the only tariff provision which authorizes a charge for removal of NEC facilities.

60. Section 204.8 of NEC's tariff does not authorize assessment of removal charges in the instance where the purchaser of a residence previously served by one utility desires to obtain service from another utility.

61. [Deleted.]

62. NEC should be required to refund to Mr. Dunaway $768.48 within ten days from the date of the final order in this docket, together with accrued interest from the date of payment of the charges by Mr. Dunaway, at the applicable interest rate for customer deposits specified by P.U.C. SUBST. R. 23.43(c)(3) for the period of time over which the monies were held by NEC.

63. NEC should not be required to reimburse Mr. Dunaway for his expenses incurred as a consequence of participation in this docket.

64. There is no substantial evidence in the record which can support a finding that the fixed $106.00 switchover fee authorized by Section 204.8(a) of NEC's tariff is unreasonable.

65. The fixed charge authorized by Section 204.8(a) is in line with those charges assessed by neighboring cooperatives.

66. NEC should be required to provide full evidentiary support for the fixed charge authorized by Section 204.8(a) in NEC's next general rate proceeding.

67. The primary reason for the higher level of Mr. Marek's costs of switching service as compared to certain other customers is that Mr. Marek's service drop configuration requires more labor on "hot" poles.

68. If one assumes that CP&L does not wish to purchase the facilities serving Mr. Marek, the examiner finds that the labor charges quoted to Mr. Marek by NEC appear to be correct.

69. NEC may be charging Mr. Marek for the cost of materials which are usable elsewhere on NEC's system, in violation of Section 204.8(d) of NEC's tariff.

70. There is not sufficient evidence of record for the examiner to determine what Mr. Marek's switchover costs should appropriately be.

71. NEC should be required to inquire as to whether CP&L is willing to purchase Mr. Marek's service drop and provide an indemnity agreement with respect to those facilities.

72. NEC should be required to designate which of the items contained on Mr. Marek's cost summary are in fact reusable on other parts of NEC's system.

73. NEC should be required to provide Mr. Marek as well as any future switchover applicants a specific salvage estimate for each component part of the service drop in question, rather than providing a lump sum salvage estimate for the entire aggregate of materials.

74. Based upon the billing requirements and limitations discussed herein, NEC should be required to provide Mr. Marek with a revised quotation of switchover costs within thirty days of the date of the final order in this docket.

75. NEC should be ordered to cease and desist from its present switchover practices to the extent that they conflict with its tariff and the Commission's substantive rules as discussed in Section III. A. through III. E. of the examiner's report.

76. NEC should be required to itemize all switchover costs which are to be assessed on cost quotations and bills rendered to disconnecting customers.

77. There is insufficient evidence of record to determine which customers may have been charged inappropriately for a switchover, or in such instances, what the appropriate charges would have been, except in the instance of Mr. Dunaway.

78. NEC should be required to furnish general counsel with a list of all customers who paid switchover charges to NEC from the two years preceding initiation of general counsel's inquiry to the present together with the supporting documentation for the charges paid by those customers, within thirty days of the date of the final order in this docket.

B. Conclusions of Law

1. Nueces Electric Cooperative, Inc. (NEC) is a public utility as defined in Section 3(c)(1) of the Public Utility Regulatory Act (PURA), Tex. Rev. Civ. Stat. Ann. art. 1446 (Vernon Supp. 1987).

2. The Commission has jurisdiction over the matters raised in this proceeding pursuant to PURA Sections 16, 17(e), 35, 37 and 38.

3. NEC provided notice of this proceeding in substantial compliance with the notice requirements established by the examiner under authority of P.U.C. PROC. R. 21.25(a)(3).

4. In instances where a connecting utility agrees to a satisfactory indemnity agreement in connection with the purchase of facilities in place from the disconnecting utility, the disconnecting utility has no legal basis for concern that it will be subject to continuing risk of financial liability with respect to such facilities.

5. Where removal of facilities idled by a switchover is the only reasonable means by which NEC can eliminate its exposure to continued liability risk with respect to such facilities, removal is required for legal and safety reasons within the meaning of Section 204.8(c) of NEC's tariff.

6. The Commission lacks any authority to require a utility to sell distribution facilities.

7. The practice of requiring the payment of removal charges by a non-member as a precondition to removal of the facilities and release of the service location falls within the definitions of both "rate" under PURA Section 3(d) and "service" under PURA Section 3(s). Consequently, the charges which NEC may assess in this circumstance are appropriately determined by the Commission.

8. Neither P.U.C. SUBST. R. 23.44(b)(1) nor Section 204.8 of NEC's tariff permits the assessment of removal costs in a subsequent owner situation.

9. NEC's assessment of switchover costs in the amount of $768.48 against Mr. Dunaway constitutes a violation of PURA Section 46.

10. NEC should refund $768.48 to Mr. Dunaway plus accrued interest from the date of payment of the charges to the date of refund.

11. NEC's practice of routinely removing facilities at the disconnecting customer's expense is violative of the express terms of NEC's tariff and is unjust and unreasonable within the intended meaning of PURA Section 38.

12. NEC should be ordered to cease and desist from engaging in its present practices with respect to customer switchovers to the extent that they are inconsistent with the examiner's construction of NEC's tariff, as outlined in Section III. A. through III. E. in the Examiner's Report.

Respectfully Submitted,

MARK W. SMITH
ADMINISTRATIVE LAW JUDGE

APPROVED on this the 22d day of June 1987.

PHILLIP A. HOLDER
DIRECTOR OF HEARINGS

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DOCKET NO. 6928
1987 JUL 31 AM 8 04

INQUIRY INTO THE LEGALITY OF THE SERVICE, PRACTICES AND RATES OF NUECES ELECTRIC COOPERATIVE, INC. RELATING TO SWITCHOVERS	§	PUBLIC UTILITY COMMISSION OF TEXAS

FILING CLERK

ORDER

In public meeting at its offices in Austin, Texas, the Public Utility Commission of Texas finds that the above styled inquiry was processed in accordance with applicable statutes by an administrative law judge who prepared and filed a report containing Findings of Fact and Conclusions of Law, which Examiner's Report is ADOPTED and made a part hereof. The Commission further issues the following Order:

1. Nueces Electric Cooperative, Inc. (NEC) is hereby ORDERED to cease and desist its present practices with respect to customer switchovers to the extent that such prctices are inconsistent with the terms of NEC's tariff as determined by the examiner in the attached Examiner's Report.

2. NEC SHALL, within thirty days of the date of this Order, provide the Commission's general counsel with a list of all customers who have switched service from NEC to Central Power & Light Company(CP&L) from two years prior to the date of filing of general counsel's petition of inquiry to the date of this Order, together with the supporting documentation of the charges paid by each of those customers.

3. NEC SHALL, within ten days from the date of the final Order in this docket, refund $768.48 plus accrued interest to Mr. Dunaway. Interest shall be calculated at the applicable interest rate for customer deposits specified in P.U.C. SUBST. R. 23.43(c)(3) for the period in question.

4. NEC SHALL, within thirty days of the date of this order, provide a revised switchover cost quotation to Mr. Marek, calculated in accordance with the tariff construction discussed in the Examiner's Report and the requirements specified in Findings of Fact Nos. 71-73 of the attached Examiner's Report.

5. NEC SHALL, within thirty days of the date of this Order, formulate and implement a new methodology for estimating net book value which, at a minimum, attempts to determine the approximate age of the facilities, the approximate labor and materials costs for that vintage, and the approximate remaining service life of the facilities.

6. NEC is hereby DIRECTED to itemize on all future cost quotations and bills rendered to disconnecting customers all switchover costs which are to be assessed to the customer.

7. NEC is hereby DIRECTED to specify on all cost summary sheets provided to disconnecting customers those pieces of equipment which are reusable on other parts of NEC's system, and further to specify the amount of salvage estimated by NEC for each component part of the disconnecting customer's service drop which is affected by a proposed switchover.

8. NEC is hereby DIRECTED to provide full evidentiary support for the fixed charge authorized by Section 204.8(a) of NEC's tariff in NEC's next general rate proceeding.

9. Within thirty days of the date of this Order, NEC SHALL file revised tariff sheets amending Section 204.8(c) of NEC's tariff to provide that only the actual labor costs incurred by NEC to remove idled facilities may be charged by NEC when removal of facilities is undertaken for any reason specified in Section 204.8(c) of NEC's tariff.

10. This Order is deemed effective upon the date of signing.

11. All motions, applications and requests for specific findings of fact and conclusions of law, if not expressly granted herein, are denied for want of merit.

APPROVED on this the 30th day of July 1987.

PUBLIC UTILITY COMMISSION OF TEXAS

SIGNED: Dennis L. Thomas
DENNIS L. THOMAS

SIGNED: Peggy Rosson
PEGGY ROSSON

SIGNED: Jo Campbell
JO CAMPBELL

ATTEST:

Phillip A. Holder
PHILLIP A. HOLDER
SECRETARY OF THE COMMISSION

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MEMORANDUM DECISIONS

TELEPHONE

General Telephone Company of the Southwest, Docket Nos. 6566 and 6716. Applications withdrawn by the applicant. Order of dismissal entered January 23, 1987.

Trinity Valley Telephone Company, Docket No. 7042. Examiner's Report adopted on February 25, 1987. Application for a depreciation rate change approved.

United Telephone Company, Docket No. 7211. Examiner's Report adopted on April 30, 1987. Application to detariff inside wire approved.

Southwestern Bell Telephone Company, Docket No. 7432. Application withdrawn by the applicant. Order of dismissal entered July 7, 1987.

Southwestern Bell Telephone Company, Docket No. 7536. Examiner's Report adopted on January 20, 1988. Stipulated case. Tariff amendment providing for the blocking of Dial 976 calls approved.

Southwestern Bell Telephone Company, Docket Nos. 6415, 6922 and 7169. Examiner's Report adopted January 20, 1988. These dockets were resolved by stipulation of the parties and consolidated for purposes of the Examiner's Report. As a result of the stipulations reached in these three dockets, revisions to certain rates and services under Southwestern Bell Telephone Company's Cellular Mobile Telephone Interconnection Service Tariff were approved.

La Ward Telephone Company, Docket No. 6028. Examiner's Report adopted with modifications on January 27, 1986. Complaint of Walter E. and Roberta Barrier against LaWard Telephone Company seeking to absolve the Barriers of responsibility for $5,766.77 in telephone bills was granted in part. Complainants absolved of responsibility of all but $993.34. LaWard's counter-claim against the Barriers to recover $14,800.72 in unpaid phone bills was denied except to the extent of the $933.34.

Southwestern Bell Telephone Company, Docket No. 8268. Withdrawn and dismissed July 29, 1988.

Southwestern Bell Telephone Company, Docket No. 5970. Complaint by Penelope Hatteras withdrawn, order of dismissal July 26, 1988.

Taylor Telephone Cooperative, Inc., Docket No. 7811. Examiner's Report adopted June 29, 1988. Applicant's request to establish new interexchange toll trunk facility within Taylor County granted.

Dell Telephone Cooperative, Docket No. 7962. Examiner's Report adopted June 29, 1988. Applicant's request to amend its certificate of convenience and necessity within Culberson and Jeff Davis Counties granted.

Contel of Texas, Inc., Docket No. 7963. Examiner's Report adopted June 29, 1988. Applicant's request for a service area revision within Castro County granted.

E.N.M.R. Telephone Cooperative, Inc., Docket No. 8004. Examiner's Report adopted June 29, 1988. Applicant's request to amend certificate of convenience and necessity within Parmer County granted.

E.N.M.R. Telephone Cooperative, Inc., Docket No. 8005. Examiner's Report adopted June 29, 1988; Order Nunc Pro Tunc issued August 3, 1988. Applicant's request to amend certificate of convenience and necessity within Oldham and Deaf Smith Counties granted.

Contel of Texas, Inc., Docket No. 8085. Examiner's Report adopted June 29, 1988. Applicant's request for a service area revision within Smith County granted.

GTE Southwest, Inc., Docket No. 8108. Examiner's Report adopted June 29, 1988. Applicant's request to amend its certificate of convenience and necessity within Fannin County granted.

Kerrville Telephone Company, Docket No. 7384. Examiner's Report adopted May 20, 1988. Stipulation resolving complaint regarding charges for DID numbers and mobile and paging service adopted.

Continental Telephone Company, Docket No. 6124. Examiner's Report adopted March 8, 1985. Complaint by El Paso Cellular Telephone Company dismissed for lack of jurisdiction.

ELECTRIC

Farmers Electric Cooperative of New Mexico, Inc., Docket No. 8011. Examiner's Report adopted August 3, 1988. Reciprocity rate increase approved.

Brazos Electric Power Cooperative, Inc., Docket No. 7726. Examiner's Report adopted August 3, 1988. Transmission line within Kent and Scurry Counties approved.

Deaf Smith Electric Cooperative, Docket No. 6131. Examiner's Report adopted January 28, 1987. Application for standard avoided cost approved.

Southwestern Electric Power Company, Docket No. 7036. Examiner's Report adopted on January 28, 1987. Application for a variance in tariff approved.

Southwestern Public Service Company, Docket No. 7144. Examiner's Report adopted on December 18, 1986. Application for approval of fuel refund and establishment of a new fixed fuel factor granted.

Brazos Electric Power Company, Docket No. 7809. Examiner's Report adopted May 18, 1988. Application for a temporary rate reduction approved.

West Texas Utilities Company, Docket No. 7933. Examiner's Report adopted July 14, 1988. Avoided cost filing approved pursuant to stipulation.

Lower Colorado River Authority, Docket No. 7512. Examiner's Report adopted October 22, 1987. Stipulated rate case adopted by Commission.

Texas Utilities Electric Company, Docket No. 7781. Examiner's Report adopted June 29, 1988. Applicant's request for transmission line and associated substation within Smith County granted.

Texas Utilities Electric Company, Docket No. 7927. Examiner's Report adopted June 29, 1988. Applicant's request for a transmission line within Andrews County granted.

Texas Utilities Electric Company, Docket No. 7964. Examiner's Report adopted June 29, 1988. Applicant's request for a transmission line within Stephens County granted.

Texas Utilities Electric Company, Docket No. 8039. Examiner's Report adopted June 29, 1988; Order Nunc Pro Tunc issued August 3, 1988. Applicant's request for a transmission line and associated substation within Lamar County granted.

El Paso Electric Company, Docket No. 6900. Dismissed by Examiner's Order dated August 16, 1988, based on withdrawal of petition of inquiry by general counsel because of mootness.

Texas Utilities Company, Docket No. 6190. Examiner's Report adopted September 12, 1985. Notice of intent application for a CCN for 960 MW of combustion turbine generating units approved.

Texas Apartment Association, Project No. 7129. Request for approval of a summary of the Commission's submetering rules granted by Order entered November 25, 1986.