

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Investigation into UNITED	)	DOCKET NO. 891239-TL
TELEPHONE COMPANY OF FLORIDA'S	)	
authorized return on equity and	)	ORDER NO. 22205
earnings.	)	
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The following Commissioners participated in the disposition of this matter:

- MICHAEL McK. WILSON, Chariman
- THOMAS M. BEARD
- BETTY EASLEY
- GERALD L. GUNTER
- JOHN T. HERNDON

FINAL ORDER INITIATING A LIMITED PROCEEDING TO  
 DETERMINE UNITED TELEPHONE COMPANY OF FLORIDA'S  
 APPROPRIATE RETURN ON EQUITY AND INITIATING AN  
 INVESTIGATION OF THE COMPANY'S EARNINGS

BY THE COMMISSION:

BACKGROUND

It has been over seven years since this Commission thoroughly investigated United Telephone Company of Florida's (United's or the Company's) earnings and set its authorized return on equity. Many changes have occurred in the last seven years in the communications industry. United's last rate case was processed in Docket No. 810211-TP, with a test year of the twelve months period ended June 30, 1981. At the time of United's last rate case, United consisted of four separate companies in Florida, excluding Quincy Telephone. The four companies were merged into one company after the last rate case. We have never set rates for the one combined Company.

By Order No. 19726, issued July 26, 1988, in Dockets Nos. 871206-PU, 880444-TL and 861616-TL, we authorized a rate of return on equity (ROE) for the Company for 1988 and 1989 of 13.5% + 1.0%. We also required United to record additional depreciation expense in an amount sufficient to reduce its earned return on equity by 100 basis points and also to cap its earnings at 14.5% ROE. Therefore, on January 1, 1990, United's authorized ROE will revert to 15.75% + 1.00%.

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United's latest surveillance report for the twelve months ended July 31, 1989, indicates an achieved return on equity of 13.54%. The Company recorded a large amount of non-recurring amortization expense during 1988. Much of that expense is reflected in the achieved ROE of 13.54%. It is, therefore, very possible that United's achieved ROE for the calendar year 1989 will exceed 14.0%.

During the last few years, numerous changes have occurred which have caused a negative impact on United's intrastate earnings. Some of these include a phase down of the interstate subscriber plant factor (SPF), implementation of bill and keep of intraLATA toll local exchange company (LEC), Uniform System of Accounts (USOA) rewrite and central office equipment category 3 (CAT 3) separations changes. In the future, at least through 1993, additional changes are expected yearly. In each of the years 1987, 1988 and 1989, significant negative impacts to United's earnings have occurred. Yet for each of the years 1987, 1988 and 1989, the Company's achieved ROE has been 14.59%, 14.28% and in excess of 14.0%, respectively. United's achieved earnings have not deteriorated significantly over the three year period. We believe this is due to various factors such as strong access line growth, increased toll volumes and even partly to company efficiency gains. It is impossible to determine today whether or not these factors which improve the Company's earnings will continue to grow each year and continue to offset the negative impacts which we know will occur. However, we must assume that these positive and negative factors will continue to offset one another as they have for the last three years. Therefore, it appears that United will continue to earn in excess of 14.0% ROE.

Our Quarterly Report on Equity Cost Rates estimates the Company's current cost of common equity to be 11.6%. In comparing this estimate of the current cost of equity to our estimate of United's achieved ROE in excess of 14.0%, it appears that the achieved ROE is at least 2.40% higher than our estimate of a midpoint ROE at which rates should be set. The 2.40% ROE represents \$14,525,000 in annual revenues. As in any other proceeding, factors can change significantly from the time the proceeding is initiated until the time it is concluded. The Company's earnings could increase or decrease. The cost of equity could increase or decrease. However, based on our current estimate of the cost of equity and United's authorized return on equity and its earnings, we find it appropriate to initiate an investigation into United's authorized return on equity and its earnings. We also find an

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investigation of United's current rate structure to be appropriate because of the changes in the Company's corporate structure.

LIMITED PROCEEDING SCHEDULED AND INVESTIGATION  
INTO COMPANY'S EARNINGS INITIATED

Based upon our general authority to regulate the telecommunications industry, as set forth in Section 364.14, Florida Statutes, we hereby schedule a limited proceeding to determine the appropriate return on equity for United and, if appropriate, to place revenues subject to refund. We hereby adopt the following schedule for this limited proceeding:

Prehearing statements shall be filed by November 24, 1989.

Prefiled direct testimony shall be filed by the Company by November 29, 1989.

The prehearing conference shall be held December 1, 1989.

Rebuttal testimony shall be filed by December 7, 1989.

On December 14, 1989, we shall hold the limited proceeding hearing and make our decisions regarding the appropriate return on equity for the Company and whether it is appropriate to place revenues subject to refund at a special agenda conference immediately following that hearing.

An order shall be issued on January 3, 1990, memorializing our decisions.

Subsequently, we will proceed with an investigation of United's earnings and rate structure. After the completion of the limited proceeding, we will require the Company to file MFRs by a date certain and on a test year to be determined at that time.

COMPANY'S PROPOSED ROE REJECTED

Based on our Quarterly Report on Equity Cost Rates, dated

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August 18, 1989, we estimate United's cost of common equity to fall within a range of 11.1% to 12.1%, with a midpoint of 11.6%. We believe 11.6% to be a reasonable estimate of United's cost of common equity given current economic conditions. This is supported by a review of the current yield on 30 year treasury bonds which is 7.96%. In addition, Aa rated utility bonds are yielding 9.32%. Furthermore, despite the approximately 190 point drop in the Dow Jones Industrial Average that occurred on October 13, 1989, we note that telecommunications stocks fell slightly less than the overall market and since that time have rebounded. Performing an analysis based on prices found in a recent edition of the Wall Street Journal (October 25, 1989), it appears that United's cost of equity has not changed from that shown in our Quarterly Report. Consequently, we reject the 13.2% cost of equity proposed for our acceptance by the Company.

Based on the foregoing, it is, therefore,

ORDERED by the Florida Public Service Commission that a limited proceeding to determine the appropriate return on equity for United Telephone Company of Florida shall be held on December 14, 1989, with the schedule for the proceeding as set forth in the body of this Order. In addition, there is hereby initiated an investigation into the rates and charges and earnings of United Telephone Company of Florida to proceed subsequent to the limited proceeding. It is further

ORDERED that United Telephone Company of Florida shall be ordered to file MFRs by a date certain and based on a test year to be determined after the limited proceeding. It is further

ORDERED that United Telephone Company of Florida's proposed return on equity of 13.2% is hereby rejected.

By Order of the Florida Public Service Commission,  
this 21st day of November, 1989.

  
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STIEVE TRIBBLE, Director  
Division of Records and Reporting

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NOTICE OF FURTHER PROCEEDINGS OR JUDICIAL REVIEW

The Florida Public Service Commission is required by Section 120.59(4), Florida Statutes, to notify parties of any administrative hearing or judicial review of Commission orders that is available under Sections 120.57 or 120.68, Florida Statutes, as well as the procedures and time limits that apply. This notice should not be construed to mean all requests for an administrative hearing or judicial review will be granted or result in the relief sought.

Any party adversely affected by the Commission's final action in this matter may request: 1) reconsideration of the decision by filing a motion for reconsideration with the Director, Division of Records and Reporting within fifteen (15) days of the issuance of this order in the form prescribed by Rule 25-22.060, Florida Administrative Code; or 2) judicial review by the Florida Supreme Court in the case of an electric, gas or telephone utility or the First District Court of Appeal in the case of a water or sewer utility by filing a notice of appeal with the Director, Division of Records and Reporting and filing a copy of the notice of appeal and the filing fee with the appropriate court. This filing must be completed within thirty (30) days after the issuance of this order, pursuant to Rule 9.110, Florida Rules of Appellate Procedure. The notice of appeal must be in the form specified in Rule 9.900(a), Florida Rules of Appellate Procedure.