BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

In the matter of Southwestern Bell Telephone Company's tariffs to revise local and intraLATA operator assistance surcharge.	)))	CASE NO. TR-91-278

APPEARANCES: Joseph F. Jedlica, III and Darryl W. Howard, Attorneys at Law, 100 North Tucker Boulevard, Room 630, St. Louis, Missouri 63101, for Southwestern Bell Telephone Company.

William M. Barvick, Attorney at Law, 231 Madison Street, Suite 301, Jefferson City, Missouri 65101, for Midwest Independent Coin Payphone Association

Randy Bakewell, Assistant Public Counsel, P. O. Box 7800, Jefferson City, Missouri 65102, for the Office of the Public Counsel and the Public.

Penny G. Baker, Deputy General Counsel, P. O. Box 360, Jefferson City, Missouri 65102, for the Staff of the Missouri Public Service Commission. 12-91

Hearing Examiner: Mark Grothoff

REPORT AND ORDER

On January 22, 1991, Southwestern Bell Telephone Company (SWBT) filed with the Commission a proposed tariff to revise Missouri Local Exchange Tariff, P.S.C. Mo. No. 24 and Missouri Long Distance Merger Telecommunications Tariff, P.S.C. Mo. No. 26 to accommodate a change in rates for the Local Operator Assistance Tariff and the IntraLATA Toll Tariff Operator surcharges. Additionally, on January 22, 1991, SWBT filed a proposed revision of those same tariffs which would increase rates associated with Busy Line Interrupt and Line Status Verification Services.

On February 13, 1991, Midwest Independent Coin Payphone Association (MICPA) filed a Motion To Suspend Tariff requesting a hearing on the reasonableness of the proposed changes to the Local Operator Assistance Tariff and to the IntraLATA Toll Tariff Operator surcharges. On February 26, 1991, the Office of the Public Counsel (OPC) also filed a Motion to Suspend the same tariffs. This matter was docketed as Case No. TR-91-278.

On March 4, 1991, the OPC filed a Motion To Suspend Tariff requesting a hearing on the reasonableness of the proposed changes to the Busy Line Interrupt and Line Status Verification Services tariff. This matter was docketed as Case No. TR-91-287.

On March 14, 1991, the Commission issued separate Suspension Orders in Case Nos. TR-91-278 and TR-91-287, each suspending the tariffs to July 13, 1991. On March 25, 1991, SWBT filed a motion to consolidate Case Nos. TR-91-278 and TR-91-287. By Notice dated April 4, 1991, the dockets were consolidated for further proceedings. On April 11, 1991, the Commission further suspended the tariffs an additional six months to January 13, 1992.

On July 31, 1991, SWBT withdrew its proposed tariff containing rate increases for Busy Line Interrupt and Line Status Verification services. Also on July 31, 1991, as a result of SWBT's withdrawal, the Commission dismissed Case No. TR-91-287.

On August 1, 1991, a hearing was held as scheduled in Case No. TR-91-278. Briefs were subsequently filed by all parties.

Findings of Fact

The Missouri Public Service Commission, having considered all of the competent and substantial evidence upon the whole record, makes the following findings of fact:

On May 1, 1991, SWBT placed into service an automated operator system. The system allows callers to choose the amount of operator assistance they wish to use. Currently, SWBT operator service rates are based on three call classifications:

station-to-station calls, person-to-person calls, and calling card calls. Within each classification, the rate charged remains the same regardless of the amount of automation used, except for operator handled calling card calls. SWBT's current operator services rates are as follows:

	Operator Handled	Semi-Automated	Fully-Automated
Person-to-Person	2.40	2.40	N/A
Station-to-Station	1.05	1.05	1.05
Calling Card	1.05	.30	.30

SWBT has proposed to change its rate structure to a three-tiered price schedule within each call classification to augment its automated operator system. The rate charged within each classification would decrease as the amount of automation chosen by the caller increased.

SWBT initially proposed rates that would have resulted in a revenue increase of approximately $650,000. In response to the objections of the other parties, SWBT revised its proposal and is currently proposing the following rates:

	Operator Handled	Semi-Automated	Fully-Automated
Person-to-Person	2.40	2.00	N/A
Station-to-Station	1.10	.90	.70
Calling Card	1.10	.65	.35

The rates proposed by SWBT would result in a net revenue increase of approximately $25,000, while the level of contribution would increase by approximately $399,000. Contribution is the amount of revenue in excess of the incremental cost of providing a service, which is allocated towards recovery of shared and common costs.

The rate changes have been proposed in response to an apparent reduction in SWBT's share of the operator services market. SWBT claims to have lost market share because of increased levels of competition. SWBT is attempting to reverse such market share loss by complementing its automated operator system with the proposed three-tiered rate structure.

SWBT proposed the new rate structure with the intention of enticing customers to use its operator services, and to provide an incentive to use the automated options. The rate structure was also designed to provide benefits to the consumer. The incremental cost of the services decrease as the amount of automation increases, due to the lower level of operator involvement and lower labor cost. The new rates will follow the incremental costs of providing the services, thereby passing the cost savings on to the consumer.

In developing the proposed rates, SWBT considered competitor's rates and the customers' willingness to pay. SWBT also wanted a large enough price differential between the service options to entice customers to use the automated options. While SWBT has proposed increasing the rates for certain service options, it has also proposed rate reductions in other areas. The combination of increases for some services and decreases for other services is designed to achieve SWBT's stated goal of not only attracting customers to SWBT but also enticing them to use the lower cost automated options.

The Commission Staff (Staff) objects to certain of the rates proposed by SWBT. Staff argues that it is inappropriate to increase rates to increase market share; that given the increased competition, raising prices is illogical. Staff proposes maintaining the existing rate of $1.05 for operator handled station-to-station and calling card calls, and the existing rate of $.30 for fully-automated calling card calls. In addition, Staff proposes an increase in the rate for semi-automated calling card calls from $.30 to $.60 in order to recover costs (as opposed to SWBT's proposed increase to $.65).

Staff's rate proposal would cause a decrease in SWBT's revenues of approximately $722,000. Staff claims, though, that SWBT's percentage of contribution would increase. Staff argues that because of the lower cost due to savings realized from the automated operator system, the percentage of contribution would increase even though the amount of revenue would decrease.

MICPA disputes that SWBT is losing market share or faces growing competition in the operator services market. MICPA claims that SWBT's market share calculations are unreliable and unsupportive of the claim of market share loss. MICPA further argues that SWBT is attempting to avoid the requirements of Section 392.361, RSMo, and have its operator services classified as competitive or transitionally competitive.

In addition, MICPA objects to SWBT's use of an incremental cost study to determine cost levels, and questions the results of that study. MICPA points out that under Case No. 18,309, SWBT's operator services are Category 1 services and, thus, are expected to cover all of its own costs plus make a contribution to basic services. MICPA claims that rates set according to the results of the incremental cost study would not cover SWBT's costs.

The Commission finds that SWBT's proposed rates have been reasonably designed to increase SWBT's market share while passing cost savings on to consumers. Staff has argued that it is inappropriate and illogical to increase rates in an attempt to increase market share. However, price alone does not determine market share. Several factors affect the market, including competitors' prices and customers' willingness to pay. Even with the increases, SWBT's rates remain competitive.

For operator-handled station-to-station and calling card calls, the competitors' average price is $1.47. At the proposed rate of $1.10, SWBT's rates are 25 percent below the average price. Also, for fully-automated calling card calls, SWBT's proposed rate of $.35 would be the lowest rate in the market. Likewise, the proposed rate of $.65 for semi-automated calling card calls is within 4 percent of the median rate charged in the market. Thus, even with the increases, SWBT's rates appear to remain well within the market price range and the market's willingness to pay.

Further, while the above rates are increased, SWBT has proposed rate reductions in other areas. The rate for a semi-automated person-to-person call would drop from $2.40 to $2.00. The semi-automated station-to-station rate would fall from $1.05 to $.90, and the rate for a fully automated station-to-station call would decrease from $1.05 to $.70.

Nonetheless, market share is not the only consideration. Revenue and contribution generated by these services must also be addressed. Staff claims that although SWBT's revenues would decrease approximately $722,000 under the Staff's proposal, SWBT's percentage of contribution would increase because of cost savings from the automated operator system. Staff based its calculations on a comparison of revenues prior to implementation of the automated operator system with anticipated revenues under Staff's proposed rate structure.

However, the automated operator system has been in operation since May 1, 1991, with SWBT already enjoying the cost savings associated with it. Consequently, under Staff's proposal, even though theoretically the percentage of contribution may increase, SWBT would experience a real decrease in the amount of contribution of approximately $460,000.

Furthermore, Staff's proposal is contrary to the pricing guidelines set forth by the Commission in Case No. 18,309. *Re: Southwestern Bell Telephone Company,* 21 P.S.C. (N.S.) 397 (1977). SWBT's operator services are Category 1 services as defined in Case No. 18,309, and as such, should be priced "to generate the largest practical level of contribution." Ibid., p. 399. SWBT's proposal would generate an additional $399,000 in contribution, while Staff's proposal would produce a decrease in contribution of $460,000 - a difference of $859,000. SWBT's proposal is more consistent with the pricing philosophy of Case No. 18,309.

MICPA has depicted SWBT's proposal as an attempt to have its operator services classified as competitive or transitionally competitive while avoiding the requirements of Section 392.361, RSMo. However, such a characterization does not appear to be accurate. No petition was filed pursuant to Section 392.361, RSMo, and SWBT has not proposed rate bands or ranges under Section 392.510, RSMo for its services. SWBT has sought only to replace the current rates with another set of specified rates. SWBT is not seeking reclassification of its services but is merely proposing a new rate structure.

MICPA cites the Commission's rejection of incremental cost studies as an accounting procedure in reviewing transitionally competitive and competitive (TC and C) services in Case No. TO-89-56, Report and Order, issued 8-28-91, as a basis for rejecting the incremental cost study in this case. However, SWBT's operator services are classified as noncompetitive, and, as stated previously, SWBT is not seeking to have them reclassified.

In Case No. TO-89-56, the Commission determined that the pricing methods of Case No. 18,309 are not appropriate for use as an accounting procedure for TC and C services. The Commission did not reject or prohibit the use of incremental cost studies in setting rates for services classified as noncompetitive. Since SWBT has not sought reclassification, these services are still priced pursuant to the procedures in Case No. 18,309.

MICPA also contends that SWBT's cost study is inaccurate and unreliable in that the study does not include amounts paid as commissions on operator service transactions; validation, billing, and collection costs; or joint and common costs. The Commission, though, has defined incremental costs as being "forward-looking and are based upon the addition to a firm's total cost when producing more of something as compared to not producing the additional items." Case No. TO-89-56, Ibid., p. 15. In addition, incremental costs "only include variable costs of production. This means that expenditures which are fixed or shared are not regarded as incremental costs." Id. "[I]ndirect costs or shared costs of a company" are also not included as incremental costs. Id. at p. 24. Thus, under the Commission's definition, SWBT correctly excluded joint and common costs from its incremental cost study. Likewise, amounts paid as commissions and validation, billing, and collection costs are not "variable costs of production" and are correctly excluded from the study.

MICPA further disputes that SWBT is losing market share or faces growing competition. However, the reason SWBT is proposing new rates is irrelevant to the question of whether the proposed rates are just and reasonable. Nonetheless, Gary Pace, MICPA's own witness, in contradiction of MICPA's position, testified as to the competitive nature of the operator services market.

The OPC and SWBT are in apparent agreement as to the reasonableness of SWBT's proposed rates. Yet, through the course of this case, a disagreement has surfaced between OPC and SWBT over the interpretation of the Incentive Regulation Plan (Plan) entered into by SWBT, OPC, Staff, and other parties in Case No. TO-90-1. The disagreement was initiated over SWBT's original proposal that would have resulted in a revenue increase of $650,000. OPC claims the original proposal would violate the Plan because the Plan requires "aggregate revenue neutrality". SWBT claims that the Plan only prohibits rate increases for certain specified services. SWBT has requested that the Commission resolve this issue.

Staff has characterized the request as one for a declaratory judgment because there is not an issue in controversy. Staff has taken the position that the Commission does not have the authority to issue declaratory judgments. Staff also points out that Case No. TO-90-1 remains an open docket and that any issue concerning the Plan should properly be considered within that docket.

This issue is not relevant to the outcome of the present case, and it is the Commission's opinion that the interpretation of the Plan would be more properly considered within the docket of Case No. TO-90-1, or within a new, separate docket. This action should in no way be interpreted as a finding by the Commission that it does not have the authority to issue a judgment on this question. The Commission makes no such finding, but, rather, defers its judgment in favor of a more appropriate docket.

The Commission has determined that SWBT's proposed rates, as modified, are virtually revenue neutral, increase the level of contribution by approximately $399,000, and pass on to the consumer the cost savings realized by SWBT through its automated operator system. SWBT's proposal will also enable SWBT to better compete in the marketplace. The Commission finds that SWBT's proposed rates are just and reasonable.

Conclusions of Law

The Missouri Public Service Commission has arrived at the following conclusions of law:

SWBT is a public utility subject to the jurisdiction of the Commission pursuant to Chapters 386 and 392, RSMo (Cum. Supp. 1990). The tariffs filed by SWBT which are the subject matter of this proceeding were suspended pursuant to Section 392.230, RSMo (Cum. Supp. 1990). The Commission, after notice and hearing, may order a change in any rate or charge pursuant to Section 392.230, RSMo (Cum. Supp. 1990).

The standard for Commission approval of the proposed rates is whether they are just and reasonable. The burden of proof to demonstrate that the proposed rates are just and reasonable is upon SWBT.

The Commission has found that SWBT's proposed rates are just and reasonable. The Commission, therefore, concludes that the tariffs filed by SWBT should be approved.

IT IS THEREFORE ORDERED:

1. That the tariffs filed by Southwestern Bell Telephone Company in this case be approved for service on and after January 13, 1992.

2. That this Report and Order shall become effective on January 9, 1992.

BY THE COMMISSION

Brent Stewart

Brent Stewart
Executive Secretary

(S E A L)

Steinmeier, Chm., Mueller, Rauch,
McClure and Perkins, CC., Concur.

Dated at Jefferson City, Missouri,
on this 20th day of December, 1991.