

Decision 12-04-016 April 19, 2012

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Petition of SureWest Telephone (U1015C)
to Adopt, Amend, or Repeal A Regulation
Pursuant to Public Utilities Code Section
1708.5 Governing the Requirement for
Commission Approval to Encumber
Assets to Secure Debt.

Petition 11-11-012
(Filed November 14, 2011)

**DECISION DENYING PETITION OF SUREWEST TELEPHONE FOR A
RULEMAKING REGARDING AMENDMENT OF
PUBLIC UTILITIES CODE SECTION 851 REGARDING
ENCUMBRANCE OF ASSETS TO SECURE DEBT**

1. Summary

This decision denies the petition of SureWest Telephone that asks the Commission to initiate a rulemaking to address exemption of incumbent local exchange carriers subject to the Uniform Regulatory Framework from the requirement that they obtain prior Commission approval pursuant to Public Utilities Code Section 851 to encumber public utility assets for the purpose of securing debt. Petition 11-11-012 is closed.

2. Background

SureWest Telephone (SureWest) filed Petition (P.) 11-11-012 (petition) on November 14, 2011. SureWest, a subsidiary of SureWest Communications, provides telecommunications services in portions of Sacramento and Placer Counties in California. SureWest operates as an incumbent local exchange

carrier (ILEC),¹ and is regulated in California under the uniform regulatory framework (URF).² Other URF ILECs include AT&T, Verizon, and Frontier Communications of California (Frontier).³ Comments in opposition to the petition were filed on December 14, 2011, by the Division of Ratepayer Advocates. SureWest filed a reply on December 27, 2011.

¹ An ILEC is a local telecommunications provider that operates in the United States that was in existence on the date the Telecommunications Act of 1996 was enacted. This includes independent telephone companies such as SureWest (formerly Roseville Telephone) and General Telephone (which has since been absorbed into Verizon), as well as the Regional Bell Operating Companies, which resulted from the breakup of the AT&T in existence at that time.

² During the late 1980's and early 1990's, in various proceedings, we addressed issues such as pricing flexibility and alternative ratemaking for basic telecommunications service rates which resulted in a New Regulatory Framework (NRF) applicable to telecommunications providers in California. NRF was authorized for Pacific Bell Telephone Company d/b/a AT&T California (AT&T) and Verizon California, Inc. (Verizon) in Decision (D.) 89-10-031, for Frontier in D.95-11-024, and for SureWest in D.96-12-074. Since the NRF decisions were issued, changes in the voice communications market have occurred, in particular, increased competition from the inclusion of multiple wireless carriers; competitive local exchange carriers (CLECs); and cable television companies. In 2005, we undertook a comprehensive review of the regulation of local exchange carriers in Rulemaking (R.) 05-04-005. By D.06-08-030, we further changed rate regulation for California's four largest ILECs, including SureWest, by adopting a URF. By that decision, we eliminated such requirement as price regulations, and price caps, relaxed the procedural requirements for the four ILECs when offering new services and filing tariffs, reduced or eliminated accounting rules that cause regulatory accounts to diverge from financial accounts, and eliminated all monitoring reports tied to NRF governing the ILECs, replacing them with standardized reporting requirements consistent with reports provided by all carriers to the Federal Communications Commission.

³ Throughout this decision we refer to SureWest, AT&T, Verizon, and Frontier collectively as URF ILECs.

3. Prior Consideration of URF ILEC Exemption from Public Utilities Code Section 851

We have considered exemptions of URF ILECs from Public Utilities (Pub. Util.) Code Section 851⁴ in two recent proceedings (Application (A.) 06-07-026 and R.09-05-006). In both proceedings, we granted partial exemptions, neither of which included an exemption from the requirement that an URF ILEC request authority to encumber all assets for securing indebtedness.

In A.06-07-026, AT&T requested authority for full exemption from § 851 for the disposition or encumbrance of utility assets. SureWest and Verizon supported this application and requested that the exemption requested by AT&T apply to all URF ILECs.⁵ Even though the responding ILECs favored full exemption, they were willing to accept CLEC/non-dominant interexchange carrier (NDIEC)—equivalent treatment as an interim measure.⁶ In D.07-11-048 in that proceeding, we denied the request by AT&T for full exemption from § 851's encumbrance requirement, but extended relief from the requirements of § 851 subject to certain limitations, to all of the URF ILECs.⁷ We also deferred consideration of full exemption by URF ILECs from § 851 to a future rulemaking.

In R.09-05-006, we considered, among other issues, the full exemption of both mid-size and large URF ILECs from § 851 with regard to the disposition or encumbrance of necessary and useful utility assets.⁸ In its opening comments

⁴ For the remainder of this decision Pub. Util. Code § 851 will be referred to as “§ 851.”

⁵ See D.07-11-048 at 2.

⁶ See D.85-11-044 for NDIEC authority and D.97-01-015 for CLEC authority.

⁷ See D.07-11-048 at Ordering Paragraph 2.

⁸ See R.09-05-006 at 1 and 7. Also considered exemption by CLECs and NDIECs from Pub. Util. Code § 851.

regarding the scope of R.09-05-006, SureWest supported exemption of URF ILECs from § 851. By D.10-05-019, we granted URF ILECs further exemptions from § 851 with respect to the disposition of certain non-controversial assets, but did not grant them full exemption from § 851 regarding encumbrance of assets.⁹

4. SureWest Request

In its petition, SureWest asks the Commission to initiate a rulemaking to consider authorizing an exemption of URF ILECs from the requirement that they obtain prior Commission approval pursuant to § 851, which requires them to request authority to encumber public utility assets for the purpose of securing debt. SureWest states that this requirement places SureWest at a disadvantage relative to its competitors and adversely affects its ability to raise capital in today's credit market. SureWest notes that its competitors, as "subsidiaries of large national holding companies with established credit rating for their debt offerings"¹⁰ are able to issue unsecured debt at a reasonable rate, therefore do not need to encumber their utility assets.

SureWest states that eliminating the requirement for prior Commission approval to encumber all utility assets to secure debt would promote the public interest because it would allow URF ILECs, such as SureWest, to raise capital at the best possible rates in the changing financing markets.

SureWest's finances are managed at the holding company level. Since the establishment of its parent (SureWest Communications) until recently, it had been able to issue debt on an unsecured basis, and therefore did not need to

⁹ See D.10-05-019 at 2.

¹⁰ P.11-11-012 at 6.

come to the Commission for authority to encumber assets. Now that lenders require its parent to issue secured debt, SureWest grants a security interest in all of its assets in connection with its parent's credit facilities and guarantees notes secured by these assets on behalf of its parent company. SureWest states that it would cost its parent, and ultimately itself and its ratepayers, between 300 and 500 basis points more to issue unsecured versus secured debt.¹¹

SureWest also notes that because it must request authority to encumber its assets, it is unable "to respond nimbly to changes in the credit market"¹² which adversely affects itself and its customers. In particular, SureWest references its most recent § 851 request (A.10-12-013) in which it took approximately two months for a decision to be issued by the Commission.¹³ SureWest also refers to past decisions in which we have granted URF ILECs partial relief,¹⁴ while granting its competitors more extensive relief.¹⁵ SureWest states that in these decisions, the Commission recognizes that the § 851 process does not suit the needs of the current telecommunications marketplace or its customers. SureWest concludes that the remaining applicable requirements of § 851 have a greater effect on it than on the other URF ILECs.

¹¹ P.11-11-012 at 5.

¹² P.11-11-012 at 8.

¹³ D.11-02-022.

¹⁴ See D.10-05-019.

¹⁵ See D.85-11-044 and D.97-01-015, in which the Commission exempted NDIECs and CLECs, respectively, from the § 851 requirement that it request authority to encumber utility assets to secure debt.

SureWest asserts that, in its most recent request to encumber assets to secure new indebtedness,¹⁶ it was unable to “nimble” adjust the amount of indebtedness it had requested in that § 851 application, when, subsequent to filing its application, the lender offered to increase the amount of the loan. Since it would have had to amend its application, including notice of the amendment as well as allowance for a protest period regarding the amendment, SureWest decided not to amend its application. SureWest states that if it had been exempted from § 851 as requested in the current application, it would have been able to accept the increased loan amount. SureWest posits that, inherent in being required to receive Commission approval, its ability to take advantage of low interest rates is jeopardized, and it is placed at a competitive disadvantage.

SureWest assures that, if it’s requested exemption is granted, the assets it encumbers to secure indebtedness could not be transferred without Commission approval.

5. Division of Ratepayer Advocates (DRA) Comments

DRA maintains that SureWest has failed to justify the need to open a rulemaking to address whether to exempt URF ILECs from the § 851 requirement to request authority to encumber assets to secure debt, stating that the Commission has recently considered granting full exemption from § 851 to URF ILECs, and rejected that request in D.10-05-019.

¹⁶ See A.10-12-013 and D.11-02-022. In that decision, the Commission granted SureWest Communications and SureWestUnit authority to encumber assets for the purpose of securing specific amounts and forms of debt.

In support of its opposition to SureWest's petition, DRA states that granting SureWest and other URF ILECs an exemption from § 851 to secure Commission approval to encumber assets to secure debt is not in the public interest. In particular, DRA states that the Commission should not relinquish its authority under § 851 to review such transactions, and the public should not relinquish the notice of such transactions and opportunity to comment on such requests as it currently does. DRA goes on to state that a request for encumbrance of assets could involve a significant dollar value, which, as surety for a secured loan, are forfeit (subject to seizure or sale) in the event of financial insolvency or bankruptcy.

In response to SureWest's claim that it is not able to react quickly to changes in the credit market, DRA references D.11-11-030,¹⁷ in which the Commission noted that SureWest could request authority to encumber assets prior to entering into negotiations with a lender for new indebtedness. DRA posits that prior authorization would enable SureWest to take advantage of any changes in the credit market or offers from a lender, while still complying with § 851.

DRA also asserts that SureWest fails to demonstrate that the application process is overly burdensome or results in an actual loss of the loan or a higher interest rate. Most recently, SureWest's A.10-12-013 took just 10 weeks to process. DRA goes on to state that the 30-day protest period is a reasonable time period that allows not only the Commission, but the general public the opportunity to voice any concern over a transaction that encumbers ratepayer

¹⁷ See D.11-11-030 at 7.

assets. If no protest is received within this 30-day protest period, the Commission can quickly issue a decision approving the application, as it did in A.10-12-013.

DRA also contends that SureWest admits in its Petition that the other URF ILECs are not currently affected by the requirement to encumber assets, since these companies are currently issuing unsecured debt, as their parent companies are large and have credit ratings.

6. Discussion

We deny SureWest's petition to open a rulemaking to determine if URF ILECs should receive an exemption from § 851 in order to secure debt. In D.11-10-030, we offered SureWest several "alternative solutions"¹⁸ for resolving its concern that it could not "nimble"¹⁹ react to changes in the market, including: a petition for modification of a decision in an applicable rulemaking; a petition for a rulemaking; or filing of an application to request authority to encumber assets prior to its being necessary, giving it the ability to react to changes in the market. We did not direct that SureWest act on any one of the options provided.

SureWest also raised many of the same issues in its petition as it did in A.11-04-022, that we addressed in D.11-10-030, such as a comparison of the cost of new secured versus unsecured debt available to SureWest,²⁰ its concern that

¹⁸ See D.11-10-030 at 1.

¹⁹ See D.11-10-030 at 6.

²⁰ See D.11-10-030 at 4-5.

the need to secure debt places it at a disadvantage,²¹ existing exemptions for NDIECs and CLECs,²² and our resolution of R.09-05-006.²³

As we stated in D.11-10-030, one option for SureWest to resolve its concerns was to petition for a rulemaking (which they did in the current petition). A rulemaking would require the time and effort of the Commission, the petitioner, and interested parties (such as all URF ILECs, DRA, Communications Division (CD), and Administrative Law Judge (ALJ) Division). Also, if, as a result of a rulemaking, the URF ILECs were authorized an exemption from § 851, the Commission would then not have the opportunity to properly review the effect of any proposed encumbrance of utility assets on ratepayers; in particular, what the effect would be if an URF ILEC eventually defaulted on the secured debt for which the assets were encumbered.

Another option we provided to SureWest in D.11-10-030 was to file an application for authority to encumber assets before it was needed. The filing of an application would not be an unduly cumbersome process, would involve fewer parties, and require much less time and effort than a rulemaking. SureWest's most recent § 851 request, which was processed in ten weeks, was processed quite expeditiously when compared to the 18 months provided for processing such a ratesetting application. The filing of an application would also retain a venue for the Commission to properly review the effect of any requested encumbrance.

²¹ See D.11-10-030 at 6.

²² See D.11-10-030 at 3.

²³ See D.11-10-030 at 4-5, and 7.

We therefore find that a much more efficient and straightforward solution to SureWest's concerns regarding § 851 is for URF ILECs to simply request authority via an application to encumber utility assets prior to its being necessary. As we stated in D.11-10-030, "By so doing, it will have the authority 'on the shelf' and ready to be used. SureWest and its parent would be able to take advantage of any changes in the credit market or offers from a lender, while continuing to comply with § 851."

We understand that this option still requires the URF ILECs to file an application requesting authority under § 851, but if such authority is requested prior to the URF ILEC approaching a lender to issue debt, it greatly mitigates any disadvantage of having to request such authority. In particular, by having such authority on hand prior to needing it, an URF ILEC would have the ability to quickly react to changes in the debt market, and approach potential lenders with the freedom to issue debt immediately or change the amount or rate if more favorable terms are offered.

Given the reasons detailed above, we find that the public interest is served by the best use of Commission and party resources, which in the current case is the URF ILEC's use of the existing application process to request encumbrance of utility assets to secure debt, prior to the existence of such need to issue debt exists.

7. Comments on Proposed Decision

The proposed decision of Commissioner Sandoval in this matter was mailed to the parties in accordance with Pub. Util. Code § 311 and comments were allowed pursuant to Rule 14.3 of the Commission's Rules of Practice and Procedure. Opening comments were filed by SureWest and no reply comments

were filed. Those comments have been considered and incorporated into this decision.

8. Assignment of Proceeding

Catherine J.K. Sandoval is the assigned Commissioner and Seaneen M. Wilson is the assigned ALJ in this proceeding.

Finding of Fact

1. On November 14, 2011, SureWest filed a petition for rulemaking pursuant to Pub. Util. Code § 1708.5, requesting that the Commission initiate a rulemaking to address exemption of URF ILECs from the requirement that they obtain prior Commission approval pursuant to § 851 to encumber all public utility assets for the purpose of securing debt.

2. The DRA protested this petition on December 27, 2011, to which SureWest replied on December 27, 2011.

3. In A.06-07-026, AT&T requested authority for full exemption from § 851 for the disposition or encumbrance of necessary and useful assets, which was supported by SureWest and Verizon. In D.07-11-048 in that proceeding, we denied the request by AT&T for full exemption from § 851, but extended relief from the requirements of § 851, subject to certain limitations, to all of the URF ILECs. We also deferred consideration of full exemption by URF ILECs from § 851 to a rulemaking.

4. In R.09-05-006, we considered, among other issues, the full exemption of both mid-size and large URF ILECs from § 851 with regard to the disposition or encumbrance of necessary and useful utility assets. By D.10-05-019 in that rulemaking, we granted URF ILECs further exemptions from § 851 with respect to the disposition of certain non-controversial assets, but did not grant them full exemption from § 851.

5. In D.11-10-013, we offered SureWest several alternatives for resolving its concern that it could not “nimble” react to changes in the market, including: petition for modification of a decision in an applicable rulemaking; petition for rulemaking; or file an application to request authority to encumber assets prior to its being necessary, giving it the ability to react to changes in the market.

Conclusions of Law

1. Opening a rulemaking to resolve SureWest’s concerns would require the time and effort of the Commission, the petitioner, and interested parties (such as all URF ILECs, DRA, CD, and ALJ Division).

2. If, as a result of a rulemaking, the URF ILECs were authorized an exemption from § 851, the Commission would then not have the opportunity to properly review the effect of any proposed encumbrance of utility assets on ratepayers; in particular, what the effect would be if an URF ILEC eventually defaulted on the secured debt for which the assets were encumbered.

3. The filing of an application for authority to encumber assets (another option provided to them in D.11-11-030), would: not be an unduly cumbersome process to the applicant, the utility, or the Commission; involve fewer parties; require much less time and effort to process; and would retain a venue for the Commission to properly review the effect of any requested encumbrance.

4. A much more efficient and straightforward, solution to SureWest’s concerns regarding § 851 is for URF ILECs to simply request authority via an application to encumber utility assets prior to its being necessary, as a shelf authority.

5. By requesting § 851 authority prior to the URF ILEC approaching a lender to issue debt, any disadvantages of having to request such authority (such as

timing and freedom to take advantage of changes in the credit market) are greatly mitigated.

6. Petition 11-11-012 is not in the public interest and should be denied.
7. Petition 11-11-012 should be closed.

O R D E R

IT IS ORDERED that:

1. Petition 11-11-012 is denied.
2. Petition 11-11-012 is closed.

This order is effective today.

Dated April 19, 2012, at San Francisco, California.

MICHAEL R. PEEVEY
President
TIMOTHY ALAN SIMON
MICHEL PETER FLORIO
CATHERINE J.K. SANDOVAL
MARK J. FERRON
Commissioners