BEFORE

THE PUBLIC SERVICE COMMISSION OF

SOUTH CAROLINA

DOCKET NO. 94-024-C - ORDER NO. 95-868

APRIL 10, 1995

IN RE: Petition of Farmer's Telephone Cooperative, Inc. for an Increase in its Authorized Rate of Return.	)))	ORDER INCREASING AUTHORIZED RATE OF RETURN

On August 24, 1994, Farmers Telephone Cooperative, Inc. ("the Cooperative") filed a Petition with the Public Service Commission of South Carolina ("the Commission") requesting an increase in its authorized rate of return on rate base. The Cooperative's Petition was filed pursuant to R.103-830 et seq. of the Commission's Rules of Practice and Procedure and S.C. Code Ann. §58-9-10 et seq. (1976), as amended.

By letter dated September 6, 1994, the Commission's Executive Director instructed the Cooperative to publish, one time, a prepared Notice of Filing in newspapers of general circulation in the areas affected by the Cooperative's Petition. The purpose of the Notice of Filing was to inform interested parties of the nature of the Petition and of the manner and time in which to file the appropriate pleadings for participation in the proceeding. Thereafter, the Cooperative provided the Commission with proof of publication of the Notice of Filing. A Petition to Intervene was filed by Philip S. Porter, Acting Consumer Advocate for the State of South Carolina.

On March 21, 1995, at 11:00 a.m., a public hearing was

convened in the Commission's Hearing Room. The Honorable Rudolph Mitchell, Chairman, presided. M. John Bowen, Jr., Esquire, and Margaret M. Fox, Esquire, represented the Cooperative; Elliott F. Elam, Jr., Esquire, represented the Consumer Advocate; and Florence P. Belser, Staff Counsel, represented the Commission Staff.

The Cooperative presented Max R. Whitehurst, a Certified Public Accountant, and Dr. William E. Avera, of Financial Concepts and Applications, Inc., as witnesses. The purpose of Mr. Whitehurst's testimony was to sponsor certain accounting exhibits, explain certain adjustments to reflect known and measurable changes, and to explain the need for modification of the rate of return currently authorized for the Cooperative by the Commission. The purpose of Dr. Avera's testimony was to identify several factors properly considered in evaluating the rate of return for an independent telephone company such as the Cooperative and to demonstrate a reasonable rate of return for the Cooperative.

Witness Whitehurst testified that the Cooperative is requesting the Commission to authorize a return on rate base in the range of 11.5% to 12.5%. In his opinion, Mr. Whitehurst testified that a range of 11.5% to 12.5% would be a reasonable rate of return on investment for the Cooperative in view of all related circumstances.

According to Mr. Whitehurst, the Cooperative's present authorized rate of return on rate base is a range of 7.5% to 8.5%. This range was found to be a fair and reasonable rate of return for the Cooperative in Order No. 87-836 issued August 10, 1987, in Docket No. 86-607-C. In that proceeding the Commission did not

determine or authorize a rate of return on equity. Witness Whitehurst pointed out that in rate matters dealing with small independent telephone companies and cooperatives whose stock is not traded regularly or publicly, such as the Farmers Telephone Cooperative, the Commission has found it appropriate to determine a rate on rate base and not on equity.

Mr. Whitehurst stressed that the Cooperative was not seeking any changes in its basic local rates in this proceeding. Mr. Whitehurst testified that the Cooperative is requesting that the Commission adjust the authorized rate of return on rate base from the rate authorized in 1987 to a range of 11.5% to 12.5% which is within the range of what the Cooperative is actually earning. According to Mr. Whitehurst, the rates which the Cooperative is currently charging were approved by the Commission in 1982 and confirmed again in 1987.

Mr. Whitehurst presented a set of exhibits which sets forth the Cooperative financial position. See, Hearing Exhibit No. 1. The exhibits utilized a test year that ended April 30, 1994. Whitehurst Exhibit A of Hearing Exhibit 1 contains the realized numbers of the Cooperative and the accounting and pro forma adjustments made by Mr. Whitehurst. After adjustments, the Cooperative's resultant rate of return on rate base is 11.55%. Hearing Exhibit 1, Exhibit A.

Dr. Avera testified that he believes the requested rate of return on rate base is reasonable. Dr. Avera identified five factors which should be considered in evaluating the rate of return of the Cooperative. The five factors identified by Dr. Avera are:

(1) since the Cooperative's customers and shareholders are identical, traditional rate regulation is not necessary to prevent monopoly profits or the shifting of wealth from ratepayer to shareholder, so the Cooperative's rate of return may be evaluated more liberally than that for an investor owned utility; (2) the Cooperative's debt ratio, which is considerably greater than industry norms, implies a higher rate of return due to the greater financial risk associated with its debt ratio; (3) the rate of return shown on the Cooperative's books overstates the earnings actually retained within the Cooperative because a significant portion of the Cooperative's earnings are returned to customers through patronage capital rotation; (4) because the Cooperative's utility operations are largely exempt from income taxes, the Cooperative can be allowed a higher rate of return and its customers will still pay a lower total cost of capital than an investor-owned utility; and (5) because the Cooperative's service rates compare favorably with the rates charged by other telephone companies in South Carolina, the Cooperative's customers are not disadvantaged by the rate of return produced by current rates.

Based on the evidence presented at the hearing and the entire record, the Commission makes the following findings:

1. Farmers Telephone Cooperative, Inc. is a South Carolina corporation owning and operating equipment and facilities for the transmission of intelligence for hire in this state and is a telephone utility within the meaning of S.C. Code Ann. §58-9-10(6)(Law. Co-op. 1976) whose intrastate authorizations are subject to the jurisdiction of this Commission.

2. The Cooperative's present authorized rate of return on rate base of 7.5% to 8.5% was approved by the Commission in Order No. 87-836, issued August 10, 1987, in Docket No. 86-607-C.

3. The Cooperative filed a Petition on August 24, 1994, with the Commission seeking to increase its authorized rate of return on rate base.

4. The Cooperative alleges that a fair and reasonable rate of return which the Cooperative should have the opportunity to earn on its South Carolina rate base devoted to the discharge of its public duties is 11.5% to 12.5%.

5. The Cooperative is seeking an increase only in its authorized rate of return on rate base, and no adjustment in the rates and charges for basic local telephone service are being sought by the Cooperative.

6. The Cooperative presented accounting and pro forma adjustments so that the Cooperative's present earnings could be illustrated to the Commission, therefore, no determination need be made as to the appropriateness of the adjustments by the parties.

7. Because the Cooperative is a small independent telephone cooperative, the Commission will not make a determination as to the appropriate capital structure of the Cooperative nor authorize a rate of return on equity.

8. The Cooperative's present authorized rate of return of 7.5% to 8.5% does not provide the Cooperative an opportunity to earn a fair rate of return on its rate base.

9. The Commission will adopt in theory the proposal by Cooperative witness Whitehurst that a rate of return on rate base

within an authorized range is an appropriate measure of the Cooperative's earnings.

10. Based on the evidence of witnesses Whitehurst and Avera, a fair and reasonable range of return on rate base is 11.5% to 12.5%.

11. Based on the Commission's finding that a range of return on rate base of 11.5% to 12.5% is fair and reasonable, no rate modification is justified. Therefore, this increase in the Cooperative's authorized rate of return on rate base will not affect the Cooperative's present rates and charges for service.

12. A rate of return on rate base from 11.5% to 12.5% will allow the Cooperative to meet its statutory requirements to provide adequate, efficient, and reasonable service; to provide a return to the Cooperative's members commensurate with returns and investments and other enterprises with corresponding risks; and to assure confidence in the financial integrity of the cooperative.

IT IS THEREFORE ORDERED:

1. That Farmers Telephone Cooperative, Inc. is hereby granted the opportunity to earn an authorized rate of return within the range of 11.5% to 12.5% on its South Carolina rate base.

2. That this Order shall remain in full force and effect until further Order of the Commission.

BY ORDER OF THE COMMISSION:

Rudolph Mitchell
CHAIRMAN

ATTEST:

Charles W. Boltin
Executive Director

(SEAL)