

BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF COLORADO

* * *

RE: APPLICATION FOR APPROVAL OF)
THE CONTINUATION AND COMPLETION)
OF THE RURAL FACILITIES IMPROVE-)
MENT PROGRAM.)

DOCKET NO. 92A-109T

COMMISSION ORDER

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Mailed Date: January 22, 1993

Adopted Date: January 13, 1993
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BY THE COMMISSION:

INTRODUCTION

On February 7, 1992, U S WEST Communications, Inc. ("USW" or "Company") filed its Application for Approval of the Continuation and Completion of the Rural Facilities Improvement Program. As discussed, *infra*, the application seeks Commission approval of the second phase of the Rural Facilities Improvement Program ("RFIP II" or "Program"). The application was set for hearing, and a number of parties intervened, including the Colorado Office of Consumer Counsel ("OCC"), Mr. Wayne Turnbow, The Coalition of Rural Telephone Users, AT&T Communications of the Mountain States ("AT&T"), MCI Telecommunications Corporation ("MCI"), and Commission Staff ("Staff"). Hearings were held beginning October 1, 1992 and continuing October 2, 5, 8, and 9, 1992.

After hearings were concluded, the parties filed closing Statements of Position. The Commission met in open meeting on October 26 and November 30, 1992 to consider its decision in this matter. Having carefully considered all the evidence and arguments

of the parties, we now enter our decision approving the Company's application with the modifications specified herein.

As noted, *supra*, this application concerns the second phase of the Rural Facilities Improvement Program. The first phase of the Company's rural facilities programs ("RFIP I") was approved by the Commission in 1987. RFIP I was also initiated by an application filed by USW. In that application proceeding (Application No. 37788), the Company proposed, in part, to make certain expenditures to regrade eight-party customers to at least four-party service, with the option of one-party service, and to upgrade four-party service customers to one-party service based upon customer demand within each exchange. After evidentiary hearings, the Commission issued Decision No. C87-905 in which we approved Company expenditures of up to \$110 million over a five-year period. That approval allowed the Company to recover the revenue requirement associated with that investment on an expedited basis (*i.e.*, instead of waiting until its next general rate case to begin recovery in rates, the Company was allowed to implement an annual rate rider based upon the RFIP investment made during that year).

RFIP I lasted from 1987 to 1991. As a result of the program, approximately 30,000 party-line customers were provided improved and upgraded service. Notably, RFIP I was not intended to provide

upgraded service for all USW multi-party customers.¹ In addition, the program did not envision single-party service for all affected customers (e.g., RFIP facilities were engineered for single-party service for all existing and potential USW subscribers but not for additional growth, and customers were not required to subscribe to one-party service even where facilities were available).

The present application was filed to complete the initiatives begun in RFIP I.² In the present application, the Company proposed to invest up to \$188.9 million in specified rural exchanges over a five-year period ending in 1996.³ In return for an accelerated recovery mechanism to be described, *infra*, the Company committed to a number of undertakings:

1. The Company would establish the Program with a capital budget of \$188.9 million;

¹ At the time the RFIP I application was filed, the Company served approximately 60,560 four- and eight-party customers. The investment approved by the Commission in Application No. 37788 contemplated improved and upgraded service for approximately 50 percent of those telephone subscribers.

² In addition to RFIP, the Commission has approved a number of other programs designed to improve rural telephone service. These include expansion of local calling areas in I&S Docket No. 1766 and Docket No. 89M-083T, the accelerated replacement of electromechanical switches under the SAFE Program in Docket No. 89A-474T, elimination of the four-party option in the Company's last rate case, and modification of line extension charges.

³ The evidence at hearing pointed out that the Company will have expended approximately \$38 million in RFIP II exchanges in 1992 in anticipation of the Commission's approval of the Program. The \$188.9 million investment contemplated in the application includes these expenditures, inasmuch as the Company requests expedited recovery of the 1992 investment as well investments through 1996.

2. The Company would establish a five-year construction schedule for the Program;
3. The Company would install the necessary facilities to provide all customers in all RFIP II exchanges single-party service by the end of 1996;
4. The installed facilities would be engineered according to new Company guidelines.⁴

All parties in this proceeding support some type of program designed to improve rural telephone service. Points of disagreement concern specific aspects of such a program. In this decision, we approve RFIP II with the elements specified herein.

NEED FOR THE PROGRAM

As noted, all parties who participated at hearing supported a plan intended to improve rural telephone service. According to the Company, RFIP II facilities, in conjunction with other construction, will enable USW to provide universal single-party service in

⁴ Mr. Overturf testified that the new engineering guidelines call for distribution facilities to be sized to provide 1.5 to 3.0 pairs per living unit; known areas of development are to be considered in the sizing of feeder and distribution; no analog carrier is to be reused or placed; all subscriber carrier is to be digital, and fiber optic cable is to be used in feeder facilities to the extent it is economically feasible; and a minimum of five years of growth is to be planned. As noted above, the second phase of RFIP differs from RFIP I since the initial phase of the program was not, in retrospect, sufficiently designed to accommodate growth. The Company is now making additional investment in RFIP I exchanges to account for growth.

the state.⁵ We now rule that, as a matter of state policy, universal single-party service is in the public interest. Consequently the RFIP II proposal, as modified here, is also in the public interest.

During the 19 public hearings held by the Commission across the State, many people commented regarding the desirability of one-party service, and the number of USW multi-party customers who have requested upgrades convince us that the public now views single-party lines as part of basic telephone service.⁶ In addition to simply increasing the availability of the access line for present multi-party customers, single-party service will allow rural telephone users to benefit from a number of existing telecommunications products. These include facsimile, answering machines, custom calling, and equal access.

⁵ The above discussion noted that RFIP I facilities were not intentionally designed to accommodate growth of one-party service in those exchanges. However, Company witnesses testified that USW proposes to add necessary plant in RFIP I exchanges to provide universal single-party service. This investment is related to growth and is to be incorporated within the Company's normal construction program, and is not included in the RFIP II recovery mechanism approved in this decision.

⁶ On December 30, 1992, in a separate proceeding, Docket No. 92R-282T, the Commission revised its telephone service rules to require universal single-party service by December 30, 1994. The Commission acknowledged changing public expectations regarding "adequate" basic telephone service. This rule was not designed to place USW in a position of non-compliance prior to completion of RFIP II, but rather to phase out existing multi-party service. This decision approves a different time schedule from that in the adopted rules.

Furthermore, in this case as well as others, the Commission has been informed of quality-of-service problems in USW rural areas. Staff witness Armstrong, for example, presented testimony indicating that in several exchanges excessive trouble report rates exist. As noted in the testimony of USW witness Overturf, the experience from RFIP I indicates that the new construction substantially reduced incidents of reported trouble. We therefore conclude that RFIP investment is likely to improve the quality of rural service.

Without a special initiative such as RFIP II, including its recovery mechanism, necessary improvements to the USW rural telephone network would be funded through the Company's normal capital budgeting process. The evidence at hearing indicates that the lines to be upgraded in RFIP II provide service to customers at the highest cost per customer. Additionally, the Company believes that the incremental revenues which would be generated by the investment would not cover costs. In light of these arguments, the Company represents that, without the Program, RFIP II exchanges would likely not be upgraded until well past the 1996 date contemplated in the application. In fact, the Company's testimony indicates that this type of rural investment would not be undertaken voluntarily. Consequently, absent an agreed upon program such as RFIP, the Commission, in order to improve rural service, would be required to attempt to secure compliance with its rules through compulsion. This alternative, with its attendant delay and

uncertainty is not desirable. We believe that a cooperative endeavor such as RFIP II is preferable. The plan approved in this decision advances the goals of universal single-party service and improved telecommunications in rural areas at a reasonable cost to ratepayers.

As a result of RFIP II investment, the Company will be capable of providing ubiquitous single-party service, and we have now determined that such service is in the public interest. The record indicates that once the RFIP investment is in place, there are no cost savings in continuing to provide a multi-party offering. Therefore, consistent with the suggestion of various parties, we now decide that single-party service will be mandatory once facilities to provide this service are in place. The Company shall modify its tariff to include only single-party offerings once the required facilities are installed. Existing four-party and two-party customers will be allowed to remain on those services only until the Company has placed facilities necessary to provide single-party service. In exchanges certified by the Company as being one-party capable under RFIP I, all multi-party customers shall be regraded under the requirements of Docket No. 92R-282T ("the Basic Service Rule"). For exchanges nominated by the Company to be included within RFIP II, regrades of all multi-party customers accomplished under the time schedule outlined in this decision shall be sufficient for compliance with the requirements in Docket No. 92R-282T.

FUNDING FOR RFIP II

The Parties' Proposals

In return for the above-referenced investment and construction commitments, the Company requests accelerated recovery in rates of a certain portion of the RFIP II revenue requirement. Essentially, USW proposes to reduce regulatory lag for recovery of RFIP II investment to one year from four to five years, which is the Company's estimate of the time between the actual placement of investment and recovery of the costs of the investment in rates. The expedited recovery mechanism presented in the application would operate as described here.

First, the Company proposed to place a cap of \$188.9 million on total investment. For this amount, USW commits to upgrade all listed RFIP II exchanges by the end of 1996.⁷ The Company proposes to implement an annual surcharge on January 1 of each year (for five years) to recover the calculated revenue requirement resulting from the average level of investment in the Program for the prior year (using nine months actual data and three months forecasted data). The revenue requirement that is eligible for accelerated recovery under the RFIP II mechanism would be reduced

⁷ The upgraded facilities would be engineered as stated in footnote 4, *supra*, and would provide single-party service for all customers in all RFIP II exchanges. Exhibit C to the application lists all RFIP exchanges, and provides estimated RFIP II costs by exchange. While the Company believes the overall cost estimate is reliable, it makes no such claim for the exchange estimates. Nevertheless, USW is willing to agree to the stated cap for total investment, as stated in the testimony of witness Hatzenbuehler.

by 25 percent (i.e., the Company would seek expedited recovery of only 75 percent of the RFIP revenue requirement). Acknowledging the criticism leveled at the program that the Program should not be a substitute for construction required for normal growth or maintenance, USW offered to exclude this 25 percent from its original proposal in order to account for growth and maintenance investment. The RFIP II revenue requirement would be split between Part 2 (fully regulated) and Part 3 (emerging competitive) services in proportion to their total revenues. That is, since Part 2 services account for 70 percent of the Company's Colorado jurisdictional revenues, 70 percent of the RFIP II revenue requirement would be recovered in a surcharge upon those service. Part 3 service would be assigned 30 percent of the revenue requirement.

After hearing, the Company filed its Investment Incentive Proposal which would modify the application's suggested funding mechanism. The incentive plan essentially reduces the cap that is eligible for accelerated recovery from \$141.7 million (75 percent of \$188.9 million) to \$125.9 million (66.67 percent of \$188.9 million). USW proposes that it be allowed to recover, on an expedited basis, all of its investment up to the new cap. The original mechanism allowed for recovery of 75 percent of all amounts up to \$188.9 million. According to the Company, this modification would provide incentives to finish the program at the least cost.

Staff and the OCC disputed various aspects of the Company's proposal. The OCC primarily disagrees with the suggestion to recover 75 percent of the Program's revenue requirement in an accelerated fashion. The OCC contends that in addition to excluding 25 percent to account for normal growth and maintenance, the Commission should exclude another 25 percent since a portion of investment in RFIP II exchanges should be regarded as "baseline investment" (i.e., investment which the Company would make even in the absence of a special recovery mechanism). Arguing that all "normal" investment should be excluded from the Program, the OCC suggests that only 50 percent of RFIP-related revenue requirement be eligible for accelerated recovery. The OCC also takes issue with the Company's proposed rate spread. See discussion, *infra*.⁸

In its closing statement of position, the OCC suggested one modification to its position to provide USW an incentive to complete the Program at the least cost. The proposal would fix the accelerated cost recovery at 62.5 percent of estimated costs on an exchange basis, capped at 100 percent of actual expenditures. (The OCC modification uses the exchange estimates contained on Exhibit C to the application.) The RFIP II rider filings would be based upon estimated costs to upgrade specific exchanges. To the extent the

⁸ The Commission understands that the OCC and Staff agree, for the most part, with USW's method of calculating the revenue requirement as set forth in Mr. Fleming's testimony. One major exception is Staff's suggestion that a 12.5 percent return on equity, instead of the Company's currently authorized return of 13.5 percent, be used in the calculation.

Company completes the upgrade at less than estimated costs, its percentage recovery of actual cost would increase.

Staff agrees that an expedited recovery mechanism is appropriate. However, Staff advocates recovery of a fixed dollar amount for each line actually converted to single-party status. Staff originally recommended that the Commission allow accelerated recovery of \$1500 for each access line actually upgraded. This amount was based upon costs per access line of the State's independent telephone companies ("Independents"), and Staff believes that these costs are representative of reasonable access line costs for RFIP II since the Independents primarily serve the types of rural areas that USW will be upgrading as a result of RFIP II. That is, Staff would base the annual rider upon the number of RFIP II lines actually upgraded to single-party service multiplied by \$1500.

In his direct testimony, Staff witness Armstrong suggested adoption of an incentive or penalty scheme to encourage the Company to complete multi-party upgrades more quickly than the contemplated five-year schedule. Consistent with that suggestion, Staff, in its Statement of Position, offered an incentive plan which would explicitly reward the Company for faster completion of upgrades. Staff's plan operates in the following manner:

1. The cumulative number of lines converted under RFIP II from multi-party to single-party service is calculated at the end of each year.
2. The average cumulative percentage conversion rate is calculated by dividing the number of converted lines by the total lines at the beginning of the program and then dividing that result by the number of years of the program which have been completed.
3. The allowed expedited recovery is determined using the average percentage conversion rate, based on higher recovery per line with higher average cumulative conversion rates, capped at some maximum dollar level per line converted.

For example, during the first year of the Program, Staff would allow accelerated recovery of costs based upon assumed investment of \$3,000 per converted line if the Company completes 20 percent of the Program (i.e., converts 20 percent of the approximately 28,000 multi-party lines to single-party service). A conversion rate of 30 percent would result in rate recovery based upon an assumed investment of \$4,500 per line. Conversion of only 10 percent of RFIP II service lines would result in recovery of costs at \$1,500 per line.

APPROVED FUNDING MECHANISM

With respect to accelerated recovery of RFIP II costs, the Commission finds meritorious the conceptual approach suggested by Staff. Specifically, we agree that the annual rate rider should be based upon some allowance for each access line (customer) actually converted to single-party service. The advantages of this method, as Staff witnesses pointed out, include ease of tracking and administration. In addition, a fixed allowance per converted line provides the Company an incentive to implement the upgrades at the least cost (consistent with the engineering guidelines cited in footnote 4 on page 4, *supra*). However, the current requirements for reporting of investment and calculation of the revenue requirement, as described in the testimony of USW witness Fleming, shall be maintained in order to properly calculate such important ratios as the revenue requirement and intrastate separations factors.

We also agree with Staff's suggested manner of encouraging the Company to complete the Program as quickly as possible. That is, we find it appropriate to allow a higher per line allowance based upon faster completion of the Program. Our discussion in the previous section emphasized the desirability of single-party service. Given that determination, it is in the public interest to upgrade multi-party service as quickly as possible. We note that the incentive schemes offered by the Company and the OCC do not encourage faster completion of the Program, but are designed to

encourage cost efficiency only. (As noted, the fixed allowance per converted line also contains incentives for such efficiency.)

However, while we accept Staff's conceptual approach, we do not accept the specific costs per access line suggested. The evidence in this proceeding raised substantial questions regarding the applicability of the Independents' average access line costs to RFIP II costs. For example, lines to be upgraded in RFIP II provide service to customers at the highest cost. Insufficient evidence was presented to convince us that the Independents' average line costs are representative of the average costs of per line conversion for RFIP II customers.

We will fix the average recoverable cost per converted four-party line at \$4,060 for the 28,123 four-party customers in existence in RFIP II nominated exchanges at the end of September 1991 as shown in Exhibit C to the application. This average cost per line would result in a \$114,179,380 investment base allowable for expedited funding treatment. To this amount we will add \$10,996,350 as a lump sum, which amount is 75 percent of the investment made by the Company during 1991 in exchanges included in RFIP II. This equates to a total allowable investment base of \$125,175,730 for conversion of all four-party lines in the State. This investment amount is very close to the investment cap contained in the efficient investment incentive proposal of the Company. However, our order differs from the proposal of the

Company in that all customers will be regraded for this amount, and sales or transfers of customers will result in a lessening of this amount based on the number of customers that the Company relinquishes.

This difference from the proposal of the Company is reasonable based upon consideration of the trouble report data contained within the exhibits of Staff. It appears that the high trouble report rates in some exchanges reflect less than satisfactory investment in those exchanges by the Company in the past. As noted in the testimony of Mr. Overturf, investment, such as that contemplated under RFIP II, can significantly reduce high trouble report rates.

However, we will provide the Company with an opportunity to increase the amount of allowable investment subject to expedited recovery up to the amount originally requested by the Company in its application \$141.7 million (75 percent of \$188.9 million). We also will provide the Company with an "opportunity" to recover on an investment base less than the previously discussed \$125.2 million if the actual number of four-party conversions lags behind the schedule proposed by the Company in Exhibit C to the application. Since we have adopted Staff's incentive formula, we will modify it to provide an allowable recovery amount of \$114.2 million under the regrade conversion schedule in Exhibit C. In order to do this, Attachment A to the incentive proposal of the Staff is

modified so that the 10 percent breakpoint on the curve begins at \$1,940 per line, passes through the 20 percent figure at approximately \$3,500 per line in a straight progression until it reaches \$4,940 at the 30 cumulative percent of the program completed. The Appendix to this decision depicts our adopted formula. To determine the revenue requirement for the program, the investment calculated by this method will be less than or equal to the total amount of actual investment in all exchanges certified by the Company as being single-party capable. (The Company may choose to certify exchanges on a feeder route basis.) In order to reinforce our desire for quick and efficient implementation of this program, all multi-party customers in non-RFIP II exchanges must be regraded pursuant to the requirements of Docket No. 92R-282T, and all RFIP II exchanges must be certified by December 31, 1996 for the RFIP tariff riders to continue in force after those dates. If these objectives are not met, the tariff riders for RFIP shall cease until these objectives are achieved. The Commission will not allow recovery of these foregone revenues for the time period in which these tariff riders are suspended due to a failure to meet these objectives.

If the Company sells or transfers customers to other providers, the customer base of 28,123 four-party customers will be adjusted in the year such transfer is legally completed unless granted an exception by the Commission because of extenuating circumstances, such as lengthy delays caused by federal procedures.

With the tariff filing for this program, the Company will furnish the number of four-party customers who were regraded during the year, with any necessary projections made on a monthly pro rata estimate from the months of available actual data.

The Company will receive increased revenues as multi-party subscribers are upgraded. For example, the monthly rate for single-party service is greater than that for multi-party service. Additionally, Outside Base Rate Area ("OBRA") charges are higher for single-party service as compared to multi- or two-party offerings. These effects should be easily calculable based upon the number of upgraded lines. Therefore, the annual amount eligible for recovery in the RFIP II rider will be offset by these revenue gains.⁹

The actual annual revenue requirement to be recovered in the RFIP II rider will be calculated as suggested by USW witness Fleming, unless otherwise ordered in this decision (e.g., we have directed that new revenues due to customers' upgrades shall be offset against the revenue requirement). We specifically reject the Staff suggestion to employ a 12.5 percent return on equity in the calculation. The Company's authorized return was set at

⁹ We do not accept the proposal to offset the RFIP II revenue requirement by additional amounts to account for increased revenues from custom calling, toll, and other services presently unavailable to multi- or two-party customers. The record indicates that some of these revenues are used as an offset to the revenue requirement in the SAFE program. Furthermore, revenue gains due to RFIP from other services such as toll would likely be unknown.

13.5 percent in its last rate case, and it is not the purpose of the present docket to re-examine that determination. Therefore, the revenue requirement shall be calculated using a 13.5 percent return on equity until the Commission specifically examines and orders a new base authorized ROE.

Staff witness Jorgensen noted that previous surcharges to the Company's rates, such as the RFIP I and SAFE riders, have precluded overearnings (i.e., if the full rider would cause USW to earn over its authorized return, the rider was reduced accordingly). However, as Staff witness Jorgensen points out, the Commission has issued an initial decision in Docket No. 90A-665T, the Alternative Form of Regulation ("AFOR") case, which would require certain adjustments to USW rates in the event of Company overearnings. The directives in AFOR are potentially inconsistent with an overearnings test specifically applicable to the RFIP rider.

Since the decision in AFOR is not yet final, we now order an overearnings adjustment to the RFIP II annual surcharge, consistent with past practice in RFIP I and SAFE. That is, in the event the Company would overearn as a result of the RFIP II rider, an appropriate adjustment in the rider will be made. In the event a final AFOR decision is implemented which generally examines Company earnings and requires an adjustment to rates in the event of overearnings, no overearnings adjustment will be made to the RFIP II surcharge.

RATE SPREAD

The Company proposed to recover 70 percent of the Program's revenue requirement by a uniform surcharge to all Part 2 services normally subject to across-the-board riders (e.g., nonrecurring charges and coin service would be exempt from the surcharge). This allocation to Part 2 products was not disputed by any party. Since Part 2 services account for 70 percent of the Company's intrastate jurisdictional revenues, the Company's proposal is reasonable and hereby is approved.

USW also proposed to recover the remaining 30 percent of the RFIP II revenue requirement by a "discrete" rate spread to Part 3 services. The Company suggests that some services such as switched access would be excluded from the surcharge, since, according to the Company, these services are already overpriced and are subject to competitive entry from alternative providers.

Not surprisingly, the Company's recommendation to exclude access is supported by the interexchange carriers (AT&T and MCI). These parties likewise argue that carrier access is greatly overpriced in relation to cost and that access is already subsidizing Part 2 services.¹⁰ The OCC contends that all Part 3 services

¹⁰ By "cost," the interexchange carriers and USW apparently refer to the incremental costs advocated by the Company in the last rate case. Since those costs and cost studies were rejected by the Commission in that case, we do not now imply, in this decision, that we find the "subsidy" argument to be credible to the extent it relies on costs and cost studies previously found to be unacceptable. Furthermore, the carriers' apparent claim that access rates are improperly subsidizing the Company's loop costs (e.g., the references to payments made pursuant to the Carrier Common Line Charge) are also rejected. The carriers apparently object to having to contribute to the Company's common and shared costs.

should be subject to the surcharge. In part, the OCC argues that these products, including switched access, will benefit from the RFIP upgrades (e.g., increased line availability and better quality of service will stimulate toll). Moreover, the OCC contends that the present case is not intended to restructure rates approved by the Commission in the last rate case.

We now rule that access should be excluded from the rider. Without relying upon USW's cost studies, we conclude that switched access has traditionally been one of the services earning well in excess of costs. Furthermore, the arguments that access is increasingly subject to competitive entry, especially if rates are raised, are credible. Since access is becoming more competitive, and since access rates have been decreasing in recent years, it would be counterproductive to increase those rates as a result of the Program.

Therefore, we now hold that, at the time it files to implement the annual rider (e.g., through the advice letter process), the Company will propose for Commission approval, a rate spread to recover 30 percent of the revenue requirement from Part 3 service. Switched access shall be excluded from the surcharge unless otherwise ordered by the Commission.

HIGH COST CUSTOMERS

USW's original position in this proceeding was that all of the approximately 28,000 multi-party customers in RFIP II exchanges would be upgraded to single-party status by the end of the Program.¹¹ In its direct testimony, the OCC expressed concern with the Company's proposal to upgrade all lines regardless of cost. The OCC noted that, according to exchange estimates on Exhibit C to the application, the Company was planning to spend many thousands of dollars per customer in some of the exchanges in order to upgrade multi-party service. OCC witness Binz stated that it may not be in the public interest to upgrade service for extremely high-cost customers at the expense of all USW ratepayers. In its rebuttal testimony, the Company essentially agreed with the OCC's concern. These two parties posit that, as a matter of public policy, the costs for upgrading some customers may be so great as to outweigh any benefits of single-party service. Consequently, OCC and USWC suggested that the Commission should rule that upgraded service for customers in extremely high cost areas should not be required under the Program.

In order to address the issue of whether the Commission should require upgraded service for extremely high-cost customers, the OCC

¹¹ At times, some of the parties have used the term "two-party customers" in addition to the term "multi-party customers," apparently drawing a distinction between the terms. In light of the Company's representation that statewide single-party service will be available after RFIP II, the Commission interprets USW's commitment to upgrade all multi-party customers as also applying to two-party subscribers in RFIP II exchanges, to the extent they exist.

and USW separately make certain suggestions which are similar in several respects. First, the OCC and USW propose that the Commission set a threshold amount (expressed as dollars per customer). Customers below the threshold amount would be qualified for upgrades without further action by the Commission.¹² The Company suggests a threshold amount between \$10,000 and \$20,000 per customer. Such a threshold amount would limit further examination to approximately 1000 customers, to be discussed, *infra*. Including more than this limited number, the Company asserts, would make the process unwieldy and possibly would lead to delay in RFIP construction. The OCC recommends a threshold amount of up to \$7,500 per customer. At this level, over 70 percent of multi-party lines would qualify for upgrade, assuming the correctness of the specific exchange estimates. This threshold amount was chosen by the OCC in order to limit the costs of the Program.

After the threshold amount is set, the OCC and the Company suggest an examination of high-cost lines by a committee composed of Staff, the OCC, and the Company. This committee would investigate whether single-party service could be provided using alternative technologies (*i.e.*, instead of wireline-based upgrades), or

¹² USW advocated that the threshold amount apply on a customer or route basis. That is, subscribers below the threshold amount regardless of the exchange would automatically qualify for upgraded service (most likely using wireline based technology). The OCC suggested that the threshold amount first be applied on an exchange basis--all exchanges with an average customer cost below the threshold amount would be qualified for upgrade. However, the OCC proposal allows, after further information and study, for high-cost lines or routes (*i.e.*, those above the predetermined threshold amount) in qualified exchanges to be moved below the threshold amount. Similarly, the OCC would allow low-cost lines or routes in high-cost exchanges to be moved above the threshold amount.

alternative institutional serving arrangements (i.e., sale or transfer of USW exchanges to an Independent Telephone Company). The parties suggest that it may be possible to provide single-party service at lower costs using some alternative technology (e.g., mobile radio, VSAT (Very Small Aperture Terminal) satellite service, BETRS (Basic Exchange Telecommunications Radio Service) radio). At the very least, the parties claim, it is worthwhile to examine these technologies before upgrading service to high-cost customers.

Similarly, the parties, especially the OCC through witness Lehr, suggest that some USW customers may be better served at lower costs by the Independents. Lehr testified that the Independents have access to federal funds (e.g., the Universal Service Fund, REA financing), while USW does not. In addition, Lehr argued that management of the Independents is more likely to be attentive and responsive to rural customers than the Company. For these reasons, the OCC proposes that the committee study whether high-cost customers could be more efficiently served by the Independents. If so, these high-cost customers or routes should be sold or transferred from USW to an Independent. The Company, in fact, agreed to investigate such potential sales or transfers by early 1993.

After investigation of alternative technologies and institutional serving arrangements for high-cost customers, the OCC and

USW contemplate Commission review of the committee's recommendations. The Commission could then approve an upgrade, perhaps with a non-wireline technology, or a sale or transfer to an Independent. Notably, both the OCC and the Company suggest that at the end of the process some customers simply may not receive upgraded service because of exorbitant costs and lack of feasible alternatives.

Generally, we accept the suggestions of the OCC and the Company with respect to high-cost customers. We believe that a high-cost threshold amount of \$15,000 per customer on a feeder route is acceptable. This standard will allow for further examination of potentially costly upgrades without making the process unwieldy by requiring examination of too many customers. Customer regrades that cost less than the \$15,000 threshold amount are hereby approved without further order of the Commission. As suggested by the parties, a committee comprised of Staff, the OCC, and the Company is directed to examine high-cost routes (i.e., upgrades costing \$15,000 or more per customer). Other parties may become a member of the committee only upon motion stating good cause. The committee shall consider whether single-party service can be provided to USW high-cost customers at less cost using alternative technologies or alternative institutional serving arrangements. From this review may come a decision by the Company to seek other institutional serving arrangements for certain exchanges or feeder routes within an exchange. The committee

should begin immediately to review high-cost routes for exchanges that the Company nominates for the 1993 construction season. By March 1, 1993, an interim report should be filed in this docket outlining the high-cost routes, if any, included in the 1993 construction schedule and the proposed disposition of the construction for these feeder routes. At this same time, the committee should file a proposed procedural schedule for completing its examination of all high-cost routes in RFIP II exchanges.

Although we are not mandating a certain time schedule for the committee, it would be desirable for the committee to have completed its examination of any high-cost routes in the 1993 construction schedule by May 1, 1993. By March 1, 1993, it would appear desirable for the Company to nominate any high-cost routes in the construction schedule for the following year and for the review of these routes to be completed and a report filed by the committee in this docket by the end of October of the year preceding construction. This schedule appears compatible with the recommendations of Staff witness Jones and USW witness Overturf as outlined on lines 1-10 of page 18 of his rebuttal testimony. The Commission fully expects that committee recommendations concerning use of technologies, whether the current USW standard or an alternative, will be supported by standard engineering economic analysis which would include the costs and advantages of the alternatives.

Based on the committee recommendations, the Commission will authorize or provide additional direction for the implementation of regrades on the nominated high-costs routes by the first of the year. The Commission intends that the implementation of the Program shall not be delayed as a result of the committee's investigation. At this time, the Commission declines to approve an overall annual schedule for the program as suggested by USW witness Overturf, except to require filing with the Commission by March 1, 1993, of the exchanges or exchange routes which the Company intends to include in the construction schedule for the following year. As noted in our conclusion to this decision, we fully expect the Company to include trouble spots within its scheduling criteria, particularly those areas which have been brought before the Commission regarding complaints of inadequate service.

In its rebuttal testimony, the Company offers to prepare a list of potential exchanges or routes for sale or transfer by February 15, 1993. As previously noted, the committee will not be directly charged with the responsibility of selecting exchanges or routes for possible sale or transfer, as this is the responsibility of the Company within the oversight and final approval of the Commission. However, the Commission directs the Company to file its initial list of potential sales or transfers in this docket by the date proposed by the Company, in order to facilitate the work of the committee and to more fully inform the Commission, the

industry, and the public of the potential magnitude of this transfer of service responsibility.

The evidence in this docket supports a conclusion that USW neglected to maintain and upgrade, in the normal course of business, the telephone network in many rural areas it is authorized to serve. The Commission RFIP decisions should not be viewed as approval of the Company's past neglect. Nor should the Company assume from the Commission's decision to review the Company's and committee's proposals for transfer and sale of certain areas that the Commission necessarily will approve the transfers or sales. It is not an acceptable remedy to merely cast off previously un-served or under-served areas so that the problems are transferred to another provider. Proposed sales and transfers will be reviewed carefully to determine whether such sales or transfers are in the public interest.

Although we believe it worthwhile to further explore alternatives for providing service to high-cost customers, we now state our intention that all RFIP II customers shall obtain upgraded service at the end of RFIP II. The high per customer costs for some subscribers must be balanced against the relatively minor effects of the entire Program on USW rates and the importance we place on single-party service. In light of these considerations, we now hold that, in the absence of sales or transfers to Independents, all USW multi-party customers in RFIP II exchanges shall be upgraded as part of this approved Program.

TRACKING AND REPORTING

Staff, through the testimony of witness Jones, expressed concern with the manner in which the Company accounted for RFIP I expenditures on its books and records. According to Jones, the Company's present records do not identify investment amounts specifically related to programs such as RFIP or SAFE which have been accorded unique regulatory treatment (e.g., expedited revenue recovery). Staff is concerned that, given the Company's present records, it is unable to audit these programs and track investment back to the continuing property records for each program and verify that the plant included in the recovery mechanism is indeed used and useful. Jones concluded that USW's current continuing property records do not meet the Federal Communications Commission's and its own internal requirements regarding auditability. Based upon these concerns, Staff recommended that the Commission order the Company to modify its general ledger and continuing property records to establish subaccounts for the classification and recording of plant investment arising from programs or initiatives such as RFIP II.

USW witness Fleming generally disputed Staff witness Jones' recommendations. Fleming stated that revision of the general ledger and continuing property records as suggested by Staff would be very costly. Moreover, USW contends, the revisions would not provide the information desired by Staff, inasmuch as the ledger and continuing property records are cumulative accounts (i.e., these records reflect additions to and replacements of plant, in

addition to the original investment). Since only initial investment is eligible for accelerated revenue recovery, Fleming represents that the costly revisions to the accounting system would not accomplish Staff's stated purpose. Declaring that the Company is willing to give Staff necessary information to adequately track and monitor the Program, Fleming proposes that Staff and the Company meet and agree on tracking and reporting requirements. In its closing Statement of Position, Staff agrees with the Company's suggestion.

We agree with Staff that Commission ability to track and monitor RFIP II expenditures is critical. Our decision according the Company accelerated recovery of RFIP II costs is unique regulatory treatment. As such, the Commission (including Staff) must be able to ensure itself that investment included in the accelerated recovery mechanism is used and useful at the time of its inclusion in the Program. The Company, on the other hand, which is the recipient of a publicly protected monopoly, should assume that it is accountable to that public for its expenditures. Failure to maintain easily decipherable and readily accessible records is simply inexcusable. For the time being, we accept the Company's proposal to jointly develop with Staff an accounting and tracking system which satisfies the concerns expressed here. The Company and Staff are hereby directed to meet and agree on methods and information which would allow adequate tracking of RFIP II expenditures. The Company and Staff shall submit their agreement

to the Commission for approval within 90 days after entry of this decision. If no agreement is reached within 90 days, the proposals of Staff witness Jones (i.e., modification of general ledger and continuing property records) shall be implemented immediately by the Company for all investment accorded unique regulatory treatment under RFIP II. The Company shall not be allowed accelerated recovery unless it implements a tracking mechanism permitting Staff audit of RFIP II expenditures.

Staff witness Jones also recommended that the Company file various reports or documents which would enable the Commission to monitor USW's ongoing activities under the Program. These include:

1. By October 1 of each year, the Company would file the detailed planning and scheduling documents referenced in the application.
2. By January 1 of each year, the Company would make available for Staff review the detailed work prints and associated engineering estimates for construction to be performed during that year.
3. Beginning with the filing of the first RFIP II rider and each quarter thereafter, the Company would file a report stating:

- a. actual versus estimated amount of calendar year construction performed by wire center;
- b. wire center certification dates and date of first regrade subsequent to certification; and
- c. wire center number/type of multi-party customers:
 - (1) converted to single-party lines,
 - (2) on held regrade status, and
 - (3) on a waiting list for service.

These suggestions are reasonable and hereby are approved. Again, failure by the Company to fully account for its expenditures and progress shall be deemed a failure to meet the preconditions for expedited recovery.

MODIFICATIONS TO USW TARIFF

Various parties asserted that the Company may not be meeting its obligation to serve in light of the number of existing "held orders" (i.e., persons desiring some kind of service, whether single- or multi-party, but who are unable to obtain it). In response to this criticism, the Company suggested, in part, that it modify its tariff to allow for "farmer lines" and a reduction of the construction credit allowance for new service.

Farmer lines allow for held order customers to construct their own lines, at their own cost, in accordance with USW specifications. The current tariff does not allow for such construction. No party opposed this suggestion, and we agree with the intent of such tariff. USW is directed to develop and submit a tariff which allows for farmer lines within 90 days of the effective date of this order. In its tariff filing, USW shall address the extent and applicability of farmer lines to issues such as, for example, the feasibility of privately owned lines in public rights-of-way and whether or when USW will assume ownership of such lines and the amount of compensation or recurring rate discount appropriate for such service or facilities. The Commission's willingness to consider such a tariff should not be construed as detracting from the Company's ordinary responsibility to adequately serve these areas.

As to the proposal to lower the construction credit from its current \$5,000 to \$1,500, we reject the Company's position. The rationale for the suggestion is, in essence, to discourage requests for new service. The record contains little, if any, support to abandon the existing credit amount, and no support to order the new suggested limit. If the Company wishes to pursue this course of action, it should do so in a separate proceeding. Alternatively, this may be an issue for the telephone planning process discussed, *infra*.

Telephone Least Cost Planning

The OCC proposed that the Commission, as part of the RFIP II ruling, establish a Telephone Resources Integrated Planning ("TRIP") docket. The TRIP proposal is conceptually identical to the integrated resource planning initiatives which a number of regulatory commissions have undertaken with respect to electric utilities. Pursuant to the OCC proposal, USW would be required to enter into a public planning process. The general purpose of the process would be to examine the future investment plans of the Company. The OCC suggests that TRIP investigate issues such as the unavailability of single-party service for many customers, the unavailability of any service for some persons residing within the Company's service territory, the kinds of new services desired by both business and residential customers, etc. In addition to focusing on long-range planning, the OCC suggests that the new docket examine some of the issues raised in the present case (e.g., identification of high-cost customers, and whether they could be better served by alternative technologies or institutional serving arrangements). Under its proposal, the OCC would require the Company to participate in telephone resource planning as a condition for obtaining accelerated recovery of RFIP II investment.

The OCC even suggests specific procedures and methods for conducting the TRIP proceeding. For example, key "stakeholders" would be identified, the Company would be required to conduct certain analysis of existing telephone resources, and the Company

would be required to address existing problems in service as part of its planning process. Just as with integrated resource planning for electric utilities, USW would be required to develop a least-cost plan for meeting the telephone needs of its customers. The OCC proposes certain procedures for accommodating public and Commission participation in the planning process.

The Commission is very interested in long-range and comprehensive telephone planning. However, we decline to adopt the OCC's detailed proposals. First, in light of our decision here, no need exists for RFIP II issues to be examined in a TRIP proceeding. Our order establishes a procedure for examining high-cost lines, and it appears that the OCC's contemplated process would likely delay implementation of RFIP II.

As for the proposals regarding long-range planning, it would be improper for us to adopt the specific detailed methods and procedure suggested by the OCC without further investigation. Integrated resource planning for telephone utilities is a new concept for our State. Even in this case, no party other than the OCC addressed issues regarding such a process. We note that in the electric Integrated Resource Planning Docket, the Commission has only recently, after a long and extensive inquiry in which numerous parties participated, determined processes and methods to be incorporated in IRP rules. In the proceeding to adopt electric IRP regulations, we conducted over two weeks of hearings. Several

thousand pages of testimony and comments were filed before and after the hearings. In short, we conducted an intensive inquiry before deciding to adopt specific resource planning rules on the electric side. Moreover, there are sensitive issues of competition in the telephone planning arena that are not present in electric IRP. Our experience dictates that because such an inquiry regarding telephone resource planning has not yet been conducted, it is premature to adopt the OCC's proposal.

We believe a new docket should be established to investigate the concept of telephone least cost planning. That docket should investigate methods, procedures, goals, issues, etc., which would be appropriate for telephone resource planning. In light of this conclusion, we do not now approve the OCC's TRIP proposal. Instead, we will open a docket to further investigate the issue.

CONCLUSION

We believe that the Company's application should be approved with the modifications discussed in this decision. The evidence in this case indicates a need for the upgrades which the Company intends to undertake as part of the Program. Although we have not mandated a particular schedule for exchange upgrades under RFIP II, we strongly urge the Company to pay particular attention to existing trouble spots. That is, as part of its scheduling criteria, the Company should consider exchanges with the highest

trouble report rates, high numbers of held orders, high levels of customer complaints, and E-911 service requests.

THEREFORE THE COMMISSION ORDERS THAT:

1. U S WEST Communications, Inc.'s application for continuation and completion of the rural facilities improvement program is approved consistent with the above discussion.

2. In the absence of sales or transfers of USW exchanges as approved by the Commission, all multi-party customers in all RFIP II exchanges listed on Exhibit C to the USW application shall be upgraded to single-party service. Upgrades shall be accomplished by the end of 1996, in accordance with the engineering design criteria discussed in this decision.

3. Once necessary facilities are in place, single-party service shall be the only service option available to USW customers.

4. U S WEST Communications, Inc., shall be allowed expedited recovery in rates of RFIP II investment in accordance with the funding mechanism approved in the above discussion. The revenue requirement for the annual RFIP II rider shall be calculated in accordance with the above determinations.

5. In order to allow for recovery of RFIP II investment consistent with this decision, 70 percent of the calculated revenue

requirement shall be "spread" to Part 2 services. The remainder shall be recovered from Part 3 rates. The Company shall propose a rate design for recovery from Part 3 services, and the Commission shall review those proposals in accordance with established procedures.

6. In order to explore alternative technologies or alternative institutional serving arrangements for high-cost lines as defined in this decision, a committee comprised of U S WEST Communications, Inc., the Office of Consumer Counsel, and Staff of the Public Utilities Commission is hereby established. This committee shall meet and file its first report and a proposed schedule for completing its review of all RFIP II high-cost lines by March 1, 1993.

7. U S WEST Communications, Inc., shall modify its tariff to provide "farmer lines" within 90 days of the effective date of this Decision.

8. Staff of the Public Utilities Commission and U S WEST Communications, Inc., shall meet, and agree if possible, on the manner in which U S WEST Communications, Inc., shall maintain its books and records to allow for necessary tracking of RFIP II investment. That agreement shall be filed for Commission approval within 90 days of the effective date of this Order. In the absence of agreement, the parties shall file a status report with the

Commission within 90 days of the effective date of this Decision. The recording methodologies suggested by Staff witness Jones shall be implemented.

9. U S WEST Communications, Inc., shall file reports as directed in the above discussion.

This Decision is effective on its Mailed Date.

ADOPTED IN OPEN MEETING January 13, 1993

(S E A L)



ATTEST: A TRUE COPY

Bruce N. Smith
Bruce N. Smith
Executive Secretary

THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF COLORADO

ROBERT E. TEMMER

CHRISTINE E. M. ALVAREZ

Commissioners

RFIP-II Accelerated Recovery Incentive Under Commission Order C93-36



