(Decision No. C82-1905)

BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF COLORADO

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RE: INVESTIGATION AND SUSPENSION OF PROPOSED CHANGES IN TARIFF -- COLORADO PUC NO. 5 - TELEPHONE -- MOUNTAIN STATES TELEPHONE AND TELEGRAPH COMPANY, DENVER, COLORADO 80202.	INVESTIGATION AND SUSPENSION DOCKET NO. 1575 ORDER OF THE COMMISSION

December 7, 1982

P R E C I S

TARIFF SHEETS FILED BY MOUNTAIN STATES TELEPHONE AND TELEGRAPH COMPANY ON APRIL 12 AND 16, 1982, RESPECTIVELY, ARE PERMANENTLY SUSPENDED. RATE OF RETURN ON RATE BASE OF 11.93% AND RATE OF RETURN ON EQUITY OF 14.75% AUTHORIZED. ACROSS THE BOARD RATE INCREASES OF 5.27% AUTHORIZED TO MEET INCREASED REVENUE REQUIREMENT OF $30,068,000; CAPITALIZATION OF INTEREST ON $8,442,000 AUTHORIZED.

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Telephone Answering Bureau
Alert Telephone Answering Service, Inc.
The Main Answering Service, Inc.
Telephone Secretarial Bureau
Action Answering Service, Inc.
Telephone Answering Service
Pueblo Telephone Secretarial Service, Inc.
Able-1 Answering Service, WUI/TAS, Inc.
Aurora Telephone Answering Service
Colorado Springs Telephone Secretarial Service
AAA Answerphone, Inc.
Denver Answering Service
Skyline Telephone Answering Service, Inc.
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I N D E X

S T A T E M E N T

BY THE COMMISSION:

HISTORY OF PROCEEDINGS

Investigation and Suspension Docket No. 1575 (I&S 1575) involves the 1982 rate case of the Mountain States Telephone and Telegraph Company (hereinafter Mountain Bell, or Respondent, or Company). The background of I&S 1575, to date, is as follows:

On April 12, 1982, Mountain Bell filed three advice letters, namely: Advice Letter No. 1824 accompanied by 1,022 tariff sheets; Advice Letter No. 1825 accompanied by 46 tariff sheets; and Advice Letter No. 1826 accompanied by 22 tariff sheets, for a total of 1,090 tariff sheets. On April 16, 1982, Mountain Bell filed Advice Letter No. 1827 for the purpose of replacing Advice Letter No. 1826. Advice Letter No. 1827 was accompanied by 21 tariff sheets. Accordingly, the grand total of tariff sheets for Advice Letter Nos. 1824, 1825 and 1827 is 1,089. Mountain Bell states that the purpose of the foregoing filings is to put into effect rates and charges which will produce additional gross revenues of $127.4 million when applied to its intrastate service volumes experienced during the test year ended December 31, 1981.* These changes in rates and charges stem from the revenue deficiency based upon a rate of return on investment

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* By revised filing on August 18, 1982, Mountain Bell made an upward adjustment of $1,527,000 in its net operating earnings and decreased its net rate base by $160,000. A further revision by Mountain Bell on October 12, 1982 resulted in a net operating earnings increase of $9,085,000 and an increase in rate base of $4,103,000. Mountain Bell did not present figures which quantified the revision in its overall revenue requirement which resulted from its August 18, 1982 and October 12, 1982 revisions to net operating earnings and rate base, respectively.

of 13.7 percent. The annual revenue effect of the proposed changes in Advice Letter No. 1824 is $99.5 million. Advice Letter No. 1825, which deals with proposed restructuring and repricing of Mountain Bell's special channel services results in an annual revenue effect of $25.6 million. The annual revenue effect of Advice Letter No. 1827, which deals with the proposed restructuring and repricing of Wide Area Telecommunications Service (800 Service and Outward WATS) is $2.3 million. Mountain Bell requested that the proposed rates set forth in the tariffs accompanying Advice Letter Nos. 1824 and 1825 become effective on May 12, 1982 on statutory 30-day notice. Mountain Bell also requested that the tariffs accompanying Advice Letter No. 1827 become effective on May 16, 1982 on statutory 30-day notice.

Pursuant to the provisions of CRS 1973, 40-6-111(1), on May 11, 1982 by Decision No. C82-709, the Commission suspended the effective date of the tariffs filed with Advice Letter Nos. 1824, 1825 and 1827 and set the same for hearing. The effective date of the tariffs filed with Advice Letter Nos. 1824 and 1825 was suspended for 120 days or until September 9, 1982 and of that filed with Advice Letter No. 1827, for 120 days or until September 13, 1982. Also by Decision No. C82-709, the Commission provided that any person, firm or corporation desiring to intervene in Phase I as a party in I&S 1575 was to file a petition for leave to intervene on or before May 27, 1982.*

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* By Decision No. C82-1410, dated September 7, 1982, the Commission further suspended the effective date of the tariff sheets filed by Mountain Bell on April 12, 1982, pursuant to its Advice Letter Nos. 1824 and 1825 for an additional 90 days, or until December 8, 1982, or until further order of the Commission; and further suspended the effective date of the tariff sheets filed by Mountain Bell pursuant to Advice Letter No. 1827 for an additional 90 days or until December 12, 1982, or until further order of the Commission.

The following parties moved to intervene in Phase I and were granted intervenor status by Executive Rulings of the Commission's Executive Secretary:

4-30-82	Department of the Army	
5-4-82	City and County of Denver	
5-14-82	Mark Chandler, Jr.	
5-17-82	William E. Darden, III	
5-20-82	Division of Communications of Department of Administration	
5-20-82	Colorado Municipal League	(Georgetown Group)
5-25-82	Colorado Ski Country USA	(Georgetown Group)
5-25-82	Colorado-Wyoming Hotel and Motel Association	(Georgetown Group)
5-26-82	ROLM of Colorado	
5-26-82	Colorado Retail Council	
5-26-82	Answer Plus, Inc. Dawn Answering Service Telephone Answering Bureau Alert Telephone Answering The Main Answering Service, Inc. Telephone Secretarial Bureau Action Answering Service, Inc. Telephone Answering Service Pueblo Telephone Secretarial Service, Inc. Able-I Answering Service WUI/TAS, Inc. Aurora Telephone Answering Service Colorado Springs Telephone Secretarial Service AAA Answerphone, Inc. Denver Answering Service Skyline Telephone Answering Service, Inc. Summit Answering Service, Inc. Pat's A-1 Answering Service, Inc. Lakewood Telephone Answering Service Answer-All Secretarial Service, Inc. A Fast Phone	
5-26-82	Diane A. Thomson	
5-27-82	Denver Fire & Burglar Alarm Co.	
5-27-82	CF&I Steel Corp.	
5-27-82	Monfort of Colorado, Inc.	
5-28-82	Ann Speer	
6-1-82	Connie Orr	

6-1-82	Stephen A. Hodgson
6-3-82	Michael J. Raber
6-14-82	AMTEL Communications, Inc.
6-16-82	City of Colorado Springs
6-30-82	Board of Larimer County Commissioners
7-12-82	Affiliated Banks Service Co.
7-13-82	North American Telephone Assn.

Intervenor Monfort of Colorado, Inc. later requested withdrawal as an intervenor and said request was granted by Executive Ruling.

Decision No. C82-709 also provided that the Commission would hear I&S 1575 in two phases; Phase I to be concerned with the overall revenue requirements of Mountain Bell, and Phase II to be concerned with the manner in which the overall revenue requirement is to be raised, commonly known as the "spread of the rates." The Commission found that the test period in this Docket was to be 12 months ended December 31, 1981. It was provided in Decision No. C82-709 that Mountain Bell was to file its written direct testimony and exhibits in its direct case in Phase I on or before May 14, 1982.

On May 7, 1982, Mountain Bell filed the written direct testimony together with the accompanying exhibits of its witnesses, namely:

Thomas W. Lindblom
Irwin Friend
Bruce Wilson
Monte Shriver
Thomas L. Clark

On May 13, 1982, Mountain Bell filed the written direct testimony together with the accompanying exhibits of its witnesses:

Fred L. Stevenson
Joseph T. Dwyer.

Oral testimony on rebuttal was presented on behalf of Mountain Bell by Richard Walker, Monte Shriver, Thomas O. Phillips, Michael T. Metzger and Bruce Wilson.

Appendix A appended to Decision No. C82-709 set forth possible alternative dates to be established in this Docket. The initial hearing date was set for June 2, 1982 in the Commission hearing room, at which time a "prehearing" conference was held for the purpose of working out various procedures to be observed in this Docket. Following discussion by the parties, it was indicated by the Commission that it anticipated entering a "revenue requirements minute order" on or about December 1, 1982 and a Phase I order on December 7, 1982.

On June 4, 1982, the Commission entered Decision No. C82-884 in which it set forth the procedural dates for Phases I and II in this Docket. Said Decision also set forth procedural directives with respect to the filing of the written direct testimony and supporting exhibits by the Staff of the Commission and Intervenors.

The Commission in this rate proceeding has utilized certain procedural methods designed to reduce hearing time and afford parties testimony and exhibits in advance of cross-examination.

First of all, the Commission in this proceeding has required that all testimony filed in the direct case of the participating parties be in writing and pre-filed in advance of cross-examination. All hearing time, except for Respondent's rebuttal case in Phase I and receipt of testimony of public witnesses has been reserved solely for summaries of direct testimony and cross-examination of witnesses filing written testimony. Each of the pre filed written testimony was marked as an exhibit, offered and received into evidence instead of being orally read into the record. In addition, the Commission has separated this rate proceeding into two phases; i.e., Phase I to determine the Company's revenue requirement and Phase II to determine the spread of the rates.

In this proceeding, all pre filed written direct testimony was marked as an exhibit using letters of the alphabet. All exhibits filed with and in support of written direct testimony or which were offered

during cross-examination have been marked using Arabic numerals. A list of all pre-filed written direct testimony and exhibits in Phase I of this proceeding which have been marked and received into evidence is appended to the Decision herein as Appendix A.

Public testimony was heard by the Commission en banc on the following dates at the noted places:

July 12, 1982	Fort Morgan, Colorado
July 13, 1982	Colorado Springs, Colorado
July 14, 1982	Durango, Colorado
July 15, 1982	Grand Junction, Colorado
July 16, 1982	Glenwood Springs, Colorado
July 21, 1982	Denver, Colorado.

On July 30, 1982, notice of hearing for the taking of additional public testimony was sent to the parties. Public testimony was heard by Hearings Examiners on the following dates at the noted places:

August 12, 1982	Fort Morgan, Colorado
August 12, 1982	Colorado Springs, Colorado
August 13, 1982	Steamboat Springs, Colorado
August 16, 1982	Glenwood Springs, Colorado
August 17, 1982	Grand Junction, Colorado
August 18, 1982	Durango, Colorado
August 24, 1982	Denver, Colorado.

On August 27, 1982, Mountain Bell filed a "Motion for Interim Rates" wherein it requested that the Commission grant it immediate interim rates during the pendancy of the proceedings in the within Docket. Written responses to Mountain Bell's Motion for Interim Rates were filed by the Board of County Commissioners of Larimer County, The Colorado Municipal League, the Colorado State Agencies, and the Colorado Retail Council.

The Commission set Mountain Bell's Motion for Interim Rates for hearing on September 15, 1982. At that time, Mountain Bell presented as its witness in support of the motion, Monte Shriver. As pertinent to the hearing on Mountain Bell's Motion for Interim Rates, Exhibit 85 (Attachment 1 to Mountain Bell's Motion for Interim Rates) and Exhibit 86 (a letter dated October 7, 1981 from the Federal Communications Commission to Mountain Bell dealing with depreciation rates) were admitted.

At the conclusion of Mountain Bell's case in chief with respect to its Motion for Interim Rates, Colorado Ski Country USA and the Colorado-Wyoming Hotel and Motel Association orally moved that Mountain Bell's motion be dismissed on the basis of a failure to meet its burden of proof. Colorado Ski Country USA was supported by Colorado State Agencies, the Department of the Army, the Colorado Municipal League, CF&I Steel Corporation, and the Staff of the Commission. The Staff of the Commission urged the further ground for dismissing Mountain Bell's Motion for Interim Rates that procedurally it was defective for failure to give proper notice to Mountain Bell's customers.

By bench order, entered on September 15, 1982, the Commission substantively granted Colorado Ski Country USA's and the Colorado-Wyoming Hotel and Motel Association's motion to dismiss Mountain Bell's Motion for Interim Rates. The oral order of the Commission was later reduced to written Decision No. C82-1475, dated September 21, 1982, wherein Mountain Bell's Motion for Interim Rates was denied. The Commission's denial order was premised on the fact that even if Mountain Bell was not presently earning its authorized rate of return, that fact alone did not set forth a sufficient basis justifying relief on an interim basis, especially in view of the fact that the Commission indicated that it anticipated entering a Phase I revenue requirements order on December 7, 1982.

On August 27, 1982, CF&I Steel Corporation (CF&I) filed a "Motion for Order Limiting Rate Relief and Directing Inquiry into Effect of AT&T Divestiture Order." The Commission set the motion for oral argument on September 16, 1982 at which time CF&I argued that the relief in the instant docket should be limited to updated compliance with the Commission's decision in I&S Docket No. 1400, dated September 16, 1980, the last general rate case involving Mountain Bell. Subsequently the Commission allowed the parties to file opening and reply briefs with respect to eight "Briefing Issues with Respect to Divestiture and Computer II."

Opening briefs were filed by the following:

Colorado Municipal League, et al. (Georgetown Group)

Mountain Bell

CF&I Steel Corporation

Reply briefs were filed by:

Mountain Bell

CF&I Steel Corporation

Colorado Municipal League, et al. (Georgetown Group)

CF&I's Motion was taken under advisement, and is disposed of in accordance with the decision and order herein.

On or before September 28, 1982, the Staff of the Commission and certain intervening parties filed written direct testimony and supporting exhibits of witnesses as follows:

On behalf of the Department of the Army

Mark Langsam.

On behalf of the Staff of the Commission*

Eric L. Jorgensen

Garrett Y. Fleming

Anthony F. Karahalios

William A. Steele

Carl E. Hunt

Robert L. Ekland.*

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* Rebuttal written testimony of Robert L. Ekland was filed on November 1, 1982.

On behalf of the Colorado Municipal League, Colorado Ski Country USA and Colorado-Wyoming Hotel and Motel Association

Matityahu Marcus

Jamshed Madan

Michael D. Dirmeier

Richard W. LeLash

Richard J. Koda.

On behalf of ROLM of Colorado, Inc.

John W. Wilson.

On behalf of Colorado Retail Council and Colorado State Agencies

Paul Levy

Phase I was heard by the Commission on September 1, 2, 3, 8, and 9, 1982, October 18, 19, 20, 27, and 29, 1982, November 3, 4, and 5, 1982 and taken under advisement at the close of hearings on November 5, 1982.

On or before November 15, 1982 the following parties submitted post-hearing statements of position:

Mountain Bell

CF&I Steel Corporation

Colorado Municipal League

Staff of the Commission

ROLM of Colorado

Colorado State Agencies and Colorado Retail Council

Department of the Army.

On November 30, 1982, the Commission entered Decision No. C82-1862 which was denominated a "Revenue Requirements Minute Order of the Commission." The purpose of said order was to indicate to Mountain Bell and the parties, prior to the entry of the Commission's Phase I order on December 7, 1982, the magnitude of the overall additional revenue requirement which would be authorized by this Commission. In Decision No. C82-1862, the Commission indicated that the overall revenue requirement which will be authorized will result in overall

annual additional revenues of $38,510,000 (plus any capitalized interest as authorized in said decision).

Decision No. C82-1862 states in part:

> "Of the overall increase in Mountain Bell's revenue requirement $8,442,000 has been identified as being that portion of the overall revenue requirement increase associated with depreciation cost changes for which it is not possible, at this time, to apportion said amount between competitive and monopoly services. This coupled with the fact that Mountain Bell did not file proposed new tariffs for Tier A (fixed tier) customers and specifically requested that no interim rate be applied to Tier A customers, leaves the Commission no method to spread the $8,442,000 across the board at this time. Accordingly, in the order hereinafter to follow, we shall permit Mountain Bell to effect across-the-board increases in its rates which will produce an additional $30,068,000 ($38,510,000 minus $8,442,000) in increased revenues. We shall also permit Mountain Bell to capitalize interest on the $8,442,000 at the overall rate of return of 11.93% per annum in order that it will be kept whole with respect to its opportunity costs during the pendency of Phase II of the docket herein, in which the Commission will allow a portion of the overall revenue requirement increase as found appropriate in Phase I."

On December 1, 1982, Mountain Bell filed a "Motion to Supplement Record and to Modify Decision No. C82-1862," accompanied by an affidavit of Monte R. Shriver, wherein he states that he had isolated and segregated all remaining life depreciation charges associated with terminal equipment and the total as so derived was $2,531,000. Mr. Shriver's affidavit further states that the balance of remaining life depreciation expense related solely to other services addressed by the Commission is $5,911,000. Accordingly, Mountain Bell by its December 1, 1982 Motion seeks to amend Decision No. C82-1862 in order to permit Mountain Bell to spread on an across-the-board basis an additional $5,911,000, or a total of $35,978,000. In its Motion Mountain Bell also requested that the Commission shorten the period for a response to its Motion from ten days to five days, or to December 6, 1982.

On December 2, 1982, the Commission at a special open meeting entered an order shortening the response time from ten days to four days (or to December 6, 1982) with respect to Mountain Bell's Motion. Responses to Mountain Bell's December 1, 1982 Motion were filed on or before December 6, 1982 by the Colorado Municipal League and the Staff.

For reasons hereinafter stated, Mountain Bell's Motion of December 1, 1982 will be denied.

Phase I - Final Decision and Order

As indicated above, the Commission in its Decision No. C82-709, issued on May 11, 1982, stated its intention to hear Mountain Bell's rate request in two phases, a practice employed by the Commission in previous dockets involving other major utilities, such as Public Service Company of Colorado (Public Service). For example, in Investigation and Suspension Docket Nos. 1425 and 1525 involving Public Service, the Commission authorized Public Service to place into effect, in order to have opportunity to meet its revenue requirements as found in Phase I, final Phase I rates. In the instant docket, I&S 1575 involving Mountain Bell, we have decided to follow the same basic procedure that has been utilized in the two mentioned Public Service dockets. That is, hereinafter in this Phase I Decision we shall authorize Mountain Bell to place into effect a rate rider [excepting telephone service relating to the Tier A portion of two tier rates (fixed tier) and coin telephone rates] which will enable Mountain Bell to have the opportunity to meet its revenue requirements. The said rider shall be final for procedural provisions of CRS 1973, 40-6-114 and 40-6-115. Although the rate rider as authorized in this Decision is designated as final rate rider subject to the above-mentioned procedural provisions of the Public Utilities Law, it should be recognized that a portion of the revenue generated by the rate rider is subject to refund in accordance with the specific provisions relating thereto which are set forth later in this Decision.

Submission

The herein instant matter has been submitted to the Commission for decision. Pursuant to the provisions of the Colorado Sunshine Act 1972, CRS 1973, 24-6-401, et seq., and Rule 32 of the Commission's Rules of Practice and Procedure, the subject matter of this proceeding has been placed on the agenda for an open meeting of the Commission. At an open meeting the herein Decision was entered by the Commission.

II

DESCRIPTION OF THE COMPANY

Mountain Bell is a public utility engaged in the business of providing telephone utility service both intrastate and interstate in the State of Colorado and other states. Pursuant to the provisions of CRS 1973, 40-1-103, the Company's intrastate telephone business within the State of Colorado is subject to the jurisdiction of the Commission, and the Commission has jurisdiction over the subject matter herein.

Mountain Bell is a subsidiary of American Telephone and Telegraph Company (AT&T), which owns 100% of Mountain Bell's outstanding common stock. AT&T has a number of other operating subsidiaries similar in nature to Mountain Bell, and, in addition, has a manufacturing subsidiary, Western Electric Company (Western Electric), and a research subsidiary, Bell Telephone Laboratories (BTL), jointly owned by AT&T and Western Electric. The entire group of companies, including AT&T, Mountain Bell, Western Electric, BTL, and other operating companies, which are subsidiaries of AT&T, comprise what is known and generally referred to as the "Bell System."

On January 14, 1949, the United States filed an action in the Federal District Court for the District of New Jersey against Western Electric and AT&T wherein it was alleged that they had monopolized and conspired to restrain trade in the manufacture, distribution, sale, and installation of telephones, telephone apparatus, equipment, materials and supplies in violation of Sections 1, 2, and 3 of the Sherman Antitrust Act, 15 U.S.C., Sections 1, 2 and 3. The United States sought relief by way of divestiture of AT&T of its stock ownership in Western Electric, termination of exclusive relationships between AT&T and Western Electric, divestiture by Western Electric of its 50% interest in BTL, separation of telephone manufacturing from the provisions of telephone service, and the compulsory licensing of patents owned by AT&T on a non-discriminatory basis. Very little activity occurred in this case between the date of the filing of the complaint in 1949 and the entry of a consent decree in

1956. Without going into detail with respect to the negotiations between the United States and AT&T during the early 1950's, suffice it to say that the 1956 consent decree included neither the divestiture of Western Electric nor any of the other structural relief originally requested by the United States. Instead, an injunction was issued which precluded AT&T from engaging in any business other than the provision of common carrier communications services; precluded Western Electric from manufacturing equipment other than that used by the Bell System; and required the defendants to license their patents to all applicants upon the payment of appropriate royalties.

The United States filed a separate antitrust action on November 20, 1974 in the United States District Court for the District of Columbia against AT&T, Western Electric, and BTL. The complaint in the 1974 action alleged a monopolization by the defendants with respect to a broad variety of telecommunications services and equipment in violation of Section 2 of the Sherman Antitrust Act. In the 1974 action, the Federal government initially sought the divestiture from AT&T of the Bell operating companies (sometimes hereinafter referred to as operating companies or BOCs) as well as the divestiture and dissolution of Western Electric. While the 1974 action was pending, the Federal government changed its relief request several times asking, at various times or in various alternatives, for the divestiture from AT&T of Western Electric and portions of the BTL. In addition, the divestiture of all or at least some of the BOCs remained one of the Federal government's principle alternative relief requests.

It is not necessary to detail a procedural history of the 1974 antitrust suit against AT&T. It is interesting to note that on September 11, 1978, the District of Columbia Federal District Court issued an opinion which disposed of all then outstanding legal issues and set forth the future course of pretrial proceedings. The trial itself began on January 15, 1981. At the request of the parties, the trial was recessed immediately after the opening statements for a period of six weeks in

order to afford an opportunity for negotiated settlement. When the settlement discussions proved fruitless, the trial resumed on March 4, 1981. At the conclusion of the Government's case, the defendants moved to dismiss the action on a variety of grounds and its motion to do so was denied on September 11, 1981. The defendants commenced their case-in-chief on August 3, 1981, and during the next five months they presented approximately 250 witnesses and tens of thousands of pages of documents.

The defendants were scheduled to complete their presentation of evidence in the 1974 antitrust case on or about January 20, 1982 and it was expected that the Government's rebuttal evidence would be presented between that date and February 10, 1982. However, on January 8, 1982, the Court was advised that the parties had filed with the District Court for the District of New Jersey a stipulation consenting to the entry by the New Jersey court of a "modification of final judgment" filed therewith. The parties also filed a memorandum suggesting procedures for evaluating the settlement proposal and a motion to transfer the 1949 action to the District of Columbia Federal District Court. In addition, the parties filed a joint motion to dismiss appeals pending in the Court of Appeals for the Third Circuit from the New Jersey District Court's decision concerning the 1956 consent decree.

The Tunney Act, 15 U.S.C., Section 16(e), which was passed by Congress in the early 1970's, provides that a proposal for a consent judgment submitted by the United States in an action brought under the antitrust laws may not be entered by the court without prior compliance with certain procedures. These procedures include a sixty-day comment period, publication of a competitive impact statement by the Department of Justice, a sixty-day period for the receipt of public comments, and a determination by the court that "the entry of such judgment is in the public interest." In enacting the Tunney Act, Congress sought to insure that the Justice Department's use of consent decrees in antitrust cases would fully promote the goals of the antitrust laws and foster public confidence in their fair enforcement. Congress apparently had found that

the prior practice, which gave the Department of Justice almost total control over the consent decree process, with only minimal judicial oversight, had failed to accomplish these ends. Judge Greene, who was in charge of the 1974 antitrust litigation in the Federal District Court for the District of Columbia, did not hold that the Tunney Act applied of its own force in that litigation; however, he is following the requirements of the Tunney Act therein.

As a result of Judge Greene's utilization of the Tunney Act requirements, an initial comment period ran from February 19, 1982 to April 20, 1982. On May 25, 1982 Judge Greene invited a second round of comment to focus on certain key identified issues raised during the first period.

On August 11, 1982, Judge Greene issued a 178 page opinion asking for modifications in certain specified areas with respect to the proposed settlement agreement, but characterizing the same as generally in the public interest. Judge Greene gave the parties 15 days to accept the modifications, noting that if the parties accepted his changes, he would promptly approve the decree, and if not, the trial would be resumed. The Department of Justice proposed a modification to Judge Greene's modification, which was denied. Thereafter, on August 24, 1982, AT&T and the Department of Justice submitted a revised consent decree incorporating Judge Greene's modifications, which he promptly approved.

The AT&T settlement is probably the most important restructuring of a major industry since the 1911 divestiture of the Standard Oil Company of New Jersey. Certain of the more salient provisions of the modified consent decree are as follows:

A. AT&T is to present a reorganization plan which shall provide for the completion, on or before February 11, 1984, of the following steps:

1. The transfer from AT&T and its affiliates to the BOCs, or to a new entity subsequently to be

separated from AT&T and to be owned by the BOCs, sufficient facilities, personnel, system, and rights to technical information to permit the BOCs to perform, independently of AT&T, exchange telecommunications and exchange access functions.

2. The separation within the BOCs of all facilities, personnel and books of account between those relating to the exchange telecommunications or exchange access functions and those relating to other functions (including the provision of inter-exchange switching and transmission and the provision of customer premises equipment to the public); provided that there shall be no joint ownership of facilities but appropriate provision may be made for sharing, through leasing or otherwise, of multi-function facilities so long as the separated portion of each BOC has insured control over the exchange telecommunications and exchange access functions.

3. The termination of the license contracts between AT&T and the BOCs and other subsidiaries and

the standard supply contract between Western Electric and the BOCs and other subsidiaries.

4. The transfer of ownership of the separated portions of the BOCs providing local exchange and exchange access service from AT&T by means of a spin-off of stock of the separated BOCs to the shareholders of AT&T, or by other disposition. Nothing in the modification of final judgment requires or prohibits the consolidation of the ownership of the BOCs into any particular number of entities.*

B. Although there is a separation of ownership between AT&T and the BOCs, the BOCs may support and share the costs of a centralized organization for the provision of engineering, administrative and other services which can more efficiently be provided on a centralized basis. The BOCs shall provide, through a centralized organization, a single point of contact for coordination of BOCs to meet the requirements of national security and emergency preparedness.

C. Until September 1, 1987, AT&T, Western Electric and the Bell Telephone Laboratories shall, upon order of any BOC, provide on a priority basis all

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* AT&T has announced its intention of reconfiguring the twenty-two operating companies in seven regional groupings. Mountain Bell, Northwestern Bell, and Pacific Northwest Bell will be under an as yet unnamed holding company headquartered in Denver, Colorado.

research, development, manufacturing, and other support services to enable the BOCs to fulfill the requirements of the modification of final judgment.

D. After reorganization, AT&T shall not acquire the stock or assets of any BOC.

5. The BOCs are also subject to certain requirements which are:

a. Subject to certain phase-in provisions, each BOC shall provide interexchange carriers and information service providers, exchange access, information access, and exchange services for such access on an unbundled, tariffed basis, that is equal in type, quality and price to that provided to AT&T and its affiliates.

b. No BOC shall discriminate between AT&T and its affiliates and its products and services and other persons and its products and services in the: (1) procurement of products and services; (2) establishment and

dissemination of technical information procurement and interconnection standards; (3) interconnection and use of the BOC's telecommunications service and facilities or in the charges for each element of service; and (4) provision of new services and the planning for and implementation of the construction or modification of facilities, used to provide exchange access and information access.

c. Within six months after reorganization, each BOC shall submit to the Department of Justice procedures for insuring compliance with the requirements of paragraph B, above.

d. Upon completion of the reorganization, no BOC shall directly or through any affiliated enterprise: (1) provide inter-exchange telecommunications service or information services;

> (2) manufacture or provide telecommunications products or customer premises equipment (except for the provision of customer premises equipment for emergency service); or (3) provide any other product or service, except exchange telecommunications and exchange access service that is not naturally a monopoly service actually regulated by tariff.

The District of Columbia District Court made certain other modifications to the above provisions which provide, in essence, that BOCs shall be permitted to provide, but not manufacture, customer premises equipment (CPE); separated BOCs shall be permitted to provide yellow page directories; and upon a showing by a petitioning BOC that there is no substantial possibility that it could use its monopoly power to impede competition in the market which it seeks to enter, the restrictions relating to inter-exchange telecommunications and information services, and customer premises equipment shall be removed.

The District of Columbia District Court also made a further modification in prohibiting AT&T, for a period of seven years, from the date of the entry of the modified final judgment decree, from engaging in electronic publishing over its own transmission facilities. After the seven year period has expired, AT&T may petition for removal of the electronic publishing restriction which shall be granted unless the Court finds that competitive conditions clearly require extension of the restriction. AT&T is permitted, however, to continue to present traditional offerings such as time and weather.

The BOCs are to be spun-off with capital structures similar to AT&T, that is, debt ratio of 45%, except for Pacific Telephone and Telegraph Company, which shall have a debt ratio of approximately 50%. The quality of debt shall be representative of the average terms and conditions of the consolidated debt held by AT&T, its affiliates and the BOCs at that time.

Judge Greene also retained broad oversight over the proceedings and modified the decree to require Court approval of the reorganization plan. The Court retained jurisdiction to enforce the provisions and principles of the judgment on its own without regard to the request by any of the parties. The District Court also provided that the plan of reorganization shall not be implemented until approved by the Court as being consistent with the provisions and principles of the modified judgment consent decree.

The precise configuration of the AT&T reorganization are not known at this time because Judge Greene's order requires AT&T to file a reorganization plan in February of 1983 with final implementation to occur by February 1984.

Meanwhile, in a different forum, other significant changes in the telecommunications industry are in the making. The Second Computer Inquiry Decision (Computer II) of the Federal Communications Commission (FCC) has as its focus the creation of one or more fully separated subsidiaries (FSS) to provide CPE and enhanced telecommunications services. AT&T has formed American Bell, Inc. (American Bell) for this purpose. To insure against cross-subsidization from regulated entities, American Bell is subject to a host of arm's length requirements.

Computer II is scheduled for implementation on January 1, 1983, about a year earlier than the consent decree. Under Computer II, on January 1, 1983, all new CPE is to be detariffed and offered for sale through the FSS, that is, American Bell. Although the modified final judgment consent decree specifies no arm's length separation requirements among AT&T and its remaining affiliates, separation of American Bell from other AT&T entities will still apply under Computer II. If the BOCs

decide to offer CPE, pursuant to the modified consent decree, they may have to do so under a fully separated subsidiary to be consistent with Computer II.

Under Computer II, the BOCs will continue to offer embedded CPE, that is, equipment on the customer's premises or in the company's inventory, on a tariffed basis until the stock has been depleted or it is transferred to the FSS and detariffed. The modified final judgment consent decree, by way of contrast, calls for all CPE to be transferred to AT&T. This is to take place about one year after the Computer II decision is implemented. Thus, the modified final judgment consent decree will affect only embedded CPE. New CPE will have been offered by American Bell commencing in 1983 and will not be impacted by the implementation of the modified final judgment consent decree in 1984. After the transfer of embedded CPE to American Bell in 1984, the BOCs will also be permitted into the detariffed CPE field under the modified final judgment consent decree. They will enter as new entrants, however, with no embedded base.

In separate dockets, the FCC is considering changes in the separations formula by which inter-exchange revenues are allocated, and the formulation of access charges. Under the modified final judgment consent decree, access tariffs are required to be filed with both the FCC and the State Commissions to be in place at the time of divestiture. This will replace the current division of revenues. AT&T has indicated that the tariffs will be filed during the first quarter of 1983.

The FCC currently is also in a rulemaking proceeding to develop guidelines for setting interstate access charges. It is considering a number of alternative methodologies to recover the non-traffic sensitive costs allocated to interstate services, including a direct flat rate charge to exchange customers and usage-based charges. The various states also will have to address the problem of access charge methodology as well as the question of whether the access charge system will be applicable to independent telephone companies as well as to BOCs.

For purposes of the present proceeding, it should be noted that the separation between interstate and intrastate use of revenues, expenses, plant and investment of Mountain Bell located in the State of Colorado is determined by the Separations Manual adopted by the FCC and the National Association of Regulatory Utility Commissioners. The Separations Manual, presently in effect, for purposes of this proceeding, is approved by the Commission as the proper method in determining the proportionate share of intrastate revenue, expenses, plant, and investment. The actual accounting data presented in this proceeding directly reflect the application of said Separations Manual to determine the amounts applicable to intrastate telephone service.

The foregoing discussion points out the significant changes in the telecommunications industry with respect to the Bell System and will form the background of a motion presented by one of the intervenors, to be discussed later in this Decision.

III

GENERAL

The present Docket, Investigation and Suspension Docket No. 1575, is Mountain Bell's first major rate case before the Public Utilities Commission since 1980 in Investigation and Suspension Docket No. 1400. On September 16, 1980, by Decision No. C80-1784, the Commission entered an order permanently suspending the rates which had been filed by Mountain Bell on January 21, 1980, thereby continuing the then present rates in effect. Public awareness and interest in general rate cases has increased markedly within the past several years. In addition, the number of so-called spread-of-the-rates issues has increased, and there are more participants in rate hearings before the Commission as is evidenced by the large number of intervenors in this Docket.

The regulatory jurisdiction of the Public Utilities Commission over non-municipal utilities in the State of Colorado is grounded in Article XXV of the Constitution of the State of Colorado which was

adopted by the general electorate in 1954. The Public Utilities Law, which currently is contained in Article 40 of the Colorado Revised Statutes (1973, as amended), implements Article XXV of the Colorado Constitution. More specifically, CRS 1973, 40-3-102, vests in this Commission the power and authority to govern and regulate all rates, charges and tariffs of every public utility.

It first must be emphasized that ratemaking is a legislative function. The City and County vs. People ex rel Public Utilities Commission, 129 Colo. 41, 266 P.2d 1105 (1954); Public Utilities Commission vs. Northwest Water Corporation, 168 Colo. 154, 551 P.2d 266 (1963). It should also be emphasized that ratemaking is not an exact science, Northwest Water, supra, at 173. In the landmark case of Federal Power Commission vs. Hope Natural Gas Company, 320 U.S. 591, 602-603 (1944), Justice Douglas, speaking for the United States Supreme Court, stated that the "ratemaking process under the (Natural Gas) Act, i.e., the fixing of 'just and reasonable' rates, involves a balancing of the investor and consumer interests." The Hope case further sets forth the proposition that under "the statutory standard of 'just and reasonable,' it is the result reached, not the method employed, which is controlling."

In the case of Public Utilities Commission v. The District Court, 186 Colo. 278, 527 P.2d 233, the Colorado Supreme Court stated at pages 282 and 283:

> [4, 5] Under our statutory scheme, the PUC is charged with protecting the interest of the general public from excessive burdensome rates. The PUC must determine that every rate is "just and reasonable" and that services provided "promote the safety, health, comfort and convenience of its patrons, employees, and the public and shall in all respects be adequate, efficient, just and reasonable." C.R.S. 1963, 115-3-1. The PUC must also consider the reasonableness and fairness of rates so far as the public utility is concerned. It must have adequate revenues for operating expenses and to cover the capital costs of doing business. The revenues must be sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and to attract capital.

The process by which utility rates are established should be explained. Under current law, when a public utility desires to change

its rate or rates, it files its new rates with this Commission, and they are open for public inspection. Unless the Commission otherwise orders, no increase in any rate or rates may go into effect except after 30-day notice to the Commission and to the customers of the utility involved.

If the 30-day period after the filing goes by without the Commission having taken any action to set the proposed new rate or rates for hearing, the new rate or rates automatically become effective by operation of law.* However, the Commission has the power and authority to set the proposed new rate or rates for hearing, which, if done, automatically suspends the effective date of the proposed new rate or rates for a period of 120 days,** or until the Commission enters a decision on the filed rates within that time. The Commission has the further option, by separate order, of continuing the suspension of the proposed new rate or rates for an additional period of up to ninety (90) days for a total maximum of 210 days or approximately seven months. If the Commission has not, by order, permitted the proposed new rate or rates to become effective, or established new rates, after hearing, prior to the expiration of the maximum 210-day period, the proposed new rate or rates go into effect by operation of law and remain effective until such time thereafter as the Commission establishes the new rates in the docket.

In the simplest terms, the Commission must determine and establish just and reasonable rates. In order to make this determination, the Commission must answer two questions: first, what are the reasonable revenue requirements of the utility involved that will enable it to render its service; and, second, how are the reasonable revenues to be raised from its ratepayers. In other words, the Commission must deter-

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* Under CRS 1973, 40-3-104, most fixed utilities file rates on thirty (30) days notice; however, thirty (30) days is a minimum notice period, unless otherwise ordered by the Commission. A utility may select a longer notice period. In any event, if the Commission elects to set the proposed rate or rates for hearing, it must do so before the proposed effective date.

** CRS 1973, 40-6-111.

mine the "revenue requirement" and the "spread of the rates" to meet the revenue requirement. To accomplish its task, in these regards, it must exercise a considerable degree of judgment and, to the best of its ability, be as fair as possible to the different parties and positions that inevitably present themselves in any major rate case. The ratemaking function involves, in other words, the making of "pragmatic adjustments" (the Hope case, supra, at page 602). It is not an easy task, but, on the other hand, neither is it a task impossible of attainment.

Basically, the three major determinations to be made by the Commission in determining an overall revenue requirement for a public utility, such as Mountain Bell, are (1) to find the appropriate rate base of the utility which is dedicated to the service of the utility's customers, (2) to determine the appropriate test year income and expenses of the utility, and (3) to determine the appropriate return which the utility is entitled to earn on its investment. Having made these three determinations, the Commission can then calculate the revenue deficiency, if any.

When a revenue deficiency is found, it must be recovered by increasing the rates charged to the utility's customers. The Commission then has the additional task of determining the appropriate "spread of the rates." Some of the intervenors in this Docket have suggested that the Commission is not in a good position to determine Mountain Bell's expenses or proper rate of return or the appropriate spread of the rates in view of the large number of uncertainties that are attendant upon the AT&T reorganization. This matter will be discussed in the next section of this Decision.

IV

MOTION FOR ORDER LIMITING RATE RELIEF AND DIRECTING INQUIRY INTO EFFECT OF AT&T DIVESTITURE ORDER

On August 27, 1982, CF&I Steel Corporation (an intervenor herein) filed a "Motion for Order Limiting Rate Relief and Directing

Inquiry Into Effect of AT&T Divestiture Order." After an oral hearing on the Motion, the parties were allowed to submit statements to the Commission describing certain issues which they believed should be briefed as a result of CF&I's Motion. The issues generally related to the appropriate Commission remedies for dealing with impending changes to Mountain Bell's operations and structure as a result of the Computer II decision and the divestiture of AT&T as required by the modified final judgment consent decree in the United States District Court for the District of Columbia. Briefs were filed by Mountain Bell and various intervenors, and CF&I's Motion was taken under advisement.

In essence, intervenors such as CF&I, Colorado Municipal League, Colorado Ski Country USA, and Colorado-Wyoming Hotel and Motel Association, take the position that in view of the uncertainties arising from the impending implementation of the Computer II decision and the divestiture of AT&T, conditions during the period in which the rates will be in effect, namely in 1983, will not be comparable to the 1981 test year as proposed by Mountain Bell in this Docket. Accordingly, the suggestion has been made to the Commission that it find that Mountain Bell has failed in sustaining its burden of proof, and that the Commission dismiss the filing herein on that basis. Alternatively, the intervenors have suggested that the Commission authorize increased revenues, on a percentage surcharge basis, based upon the regulatory principles that existed in I&S Docket No. 1400. Another proposed remedy is that interim rates be authorized for a period certain or for a period which would expire upon the occurrence of a condition subsequent relating to the capital structure and operations of Mountain Bell.

CF&I argues that the surcharge vehicle is the most appropriate for collecting any additional revenues granted in this proceeding inasmuch as it is the most administratively workable solution for imposing any conditional rate. On occurrence of the appropriate condition subsequent in termination of a surcharge, Mountain Bell would merely be required to cancel the single surcharge tariff. The base rate tariffs would remain effective without any action being required and such rates

would then continue in effect until a new proceeding, considering the impact of divestiture, was completed.

By way of contrast, Mountain Bell, although conceding the uncertainties arising as a result of Computer II and the modification of final judgment consent decree, states that the statutory framework regarding the repricing of utility services is straightforwardly established therein. In other words, Mountain Bell argues that Colorado law empowers the Commission upon its own motion, or pursuant to complaint, to challenge the justness and reasonableness of any rates which are in effect at any time. See CRS 1973, 40-3-101. Thus, Mountain Bell states that when conditions change so to affect its structure and operation, the Commission already has the power on its own motion or pursuant to complaint to investigate the rates of Mountain Bell to insure that those rates are just and reasonable. Mountain Bell proposes that a reasonable solution exists to the problems perceived by the intervenors which will achieve the goals of assuring that in the year 1983 and beyond, Mountain Bell will not earn in excess of what is fair and reasonable as a result of the effects of Computer II and the AT&T divestiture. Mountain Bell proposes that if, at any point in the future, the Commission is concerned that Mountain Bell's then existing rates are producing earnings in excess of those which are fair and reasonable, the Commission, on its own motion, can order Mountain Bell to demonstrate the fairness and reasonableness of those then existing rates. In so doing, the Commission would be complying with the statutory mandate found in CRS 1973, 40-3-101. Mountain Bell has stated that in the event the Commission, on some future date, decides to initiate a show cause proceeding to inquire into the question of whether Mountain Bell is earning in excess of its then cost of capital as a result of the rates set in this Docket, Mountain Bell will waive its rights under CRS 1973, 40-3-101 and will accept the burden of the proceeding and the burden of proof as to the fairness and reasonableness of its overall rates. Mountain Bell has stated that its waiver is limited to an inquiry into the level of Mountain Bell's Colorado intrastate earnings, and does not extend to fairness of an individual rate or tariff.

Mountain Bell also has stated that it will provide to the Commission monthly financial reports, beginning with the first full month in which rates authorized in this Docket are in effect. In this way, Mountain Bell states, the Commission will be able to monitor the continued justness and reasonableness of the rates authorized in this Docket. Mountain Bell also submits that the Company's current financial condition and budgeting views mandate that a general rate case be filed in 1983, and Mountain Bell has stated its intention to file that case on or before May 1, 1983. Accordingly, Mountain Bell argues that during the 1983 proceeding, the effects of Computer Inquiry II will be known and a great deal more information concerning the effects of the AT&T divestiture will also be known and available.

The Commission has carefully considered the well-presented views of the intervenors and Mountain Bell with respect to the various issues arising as a result of Computer II and divestiture, and the range of possible remedies which the Commission could employ in view of the uncertainties arising therefrom. We believe that the parties generally are aware of the fact that the Commission does not take a truncated view of the powers which it has available to carry out its statutory responsibility to set just and reasonable rates and to insure the provisions of adequate service to consumers. To the extent the Commission has not been restricted by specific legislative enactment, and consistent with the due process rights of all the parties that appear before it, the Commission is willing to establish practices and procedures which will enable it to carry out its statutory responsibilities as above defined. On balance, however, we find that the various remedies proposed by the intervenors in this Docket need not, and should not, be implemented. The Commission well recognizes the fact that Computer II and the AT&T divestiture confront the Commission with a factual pattern which is unprecedented. We also must recognize that the future can never be an exact mirror image of the past and that the necessary uncertainty of the future has always faced regulatory bodies, such as this Commission. It is the magnitude of the uncertainty rather than its existence which makes the present situa-

tion unique. Basically, we agree with Mountain Bell that it is the obligation of this Commission to make its best judgment on the facts that are available to it now. Although we do not doubt our authority to utilize one or more of the remedies suggested to us by the intervenors, we do not believe their implementation would be appropriate. Accordingly, we shall hereinafter deny CF&I's "Motion for Order Limiting Rate Relief and Directing Inquiry Into Effect of AT&T Divestiture Order." This Docket shall proceed in the manner initially outlined by the Commission when it set Mountain Bell's filed rates for hearing and suspended the same.

V

TEST PERIOD

In each rate proceeding, it is necessary to select a test period. The operating results of the test period then are adjusted for known changes in revenue and expense levels so that the adjusted operating results of the test period will be representative of the future, and thereby afford a reasonable basis upon which to predicate rates which will be effective during a future period.

In this case, the Commission finds that the twelve-month period commencing January 1, 1981 and ending December 31, 1981 as filed by Mountain Bell is the appropriate twelve month period which constitutes a representative year and is the test period for purposes of determining the revenue requirement.

VI

RATE BASE

A. Rate Base Conversion Adjustment.

Rate base can be described as the property which is dedicated by the utility involved in providing utility service to its customers. The utility, of course, is entitled to a fair rate of return on its rate base investment. In this docket, Mountain Bell witness Shriver determined that the dollars of rate base was less than the dollars of invested

capital. Consequently, Mr. Shriver developed a capital-rate base conversion factor and determined that the Company's required return on its rate base was 13.70% (as compared with Mountain Bell's proposed weighted cost of capital submitted by the Company in its initial filing of 13.64%). Mr. Shriver testified that his observation of an imbalance between the total capital and rate base caused him to form the opinion that a conversion adjustment was necessary in order to produce earnings on rate base necessary to cover the cost of capital. It was Mr. Shriver's position that a utility is entitled to a return on rate base that produces earnings sufficient to meet the cost of the capital dedicated to the intrastate telecommunications services. In theory, the capital of a utility and its investment in rate base can be equal. In practice, however, rate base and capital are not always in balance. Rate base may be more or less than capital.

The Commission more precisely can examine rate base in order to determine what assets are dedicated to utility service. Accordingly, that is the basis upon which the Commission should set its rate of return. There is nothing in this Docket which proves that all of the capital employed by Mountain Bell with regard to its Colorado intrastate operations was dedicated to Colorado intrastate utility service subject to the jurisdiction of the Commission. Without a clear showing that all of the capital was dedicated to the rate base, to apply a rate of return on capital might result in the utility earning on capital which is not, in fact, dedicated to a used and useful rate base.

The test year booked rate base of Mountain Bell was $1,149,760,000. Mountain Bell proposed total adjustments of $15,077,000 resulting in its proposed rate base of $1,134,683,000. The Staff proposed adjustments of $75,342,000, resulting in a proposed rate base of $1,074,418,000, and the intervenors, Colorado Municipal League, Colorado Ski Country USA, and the Colorado-Wyoming Hotel and Motel Association (hereinafter sometimes collectively referred to as the "Georgetown Group") proposed adjustments of $69,832,000 resulting in a rate base of $1,079,928,000.

As hereinafter discussed, the Commission will disallow Mountain Bell's proposed adjustment relating to Bell Telephone Laboratories (BTL) in the amount of $2,199,000, and the Company's proposed adjustment related to equal life group (ELG) depreciation in the amount of ($175,000). We will accept the Staff's proposed adjustment of ($278,000) with respect to property held for future use, and will accept the construction work in progress pro forma adjustment proposed by Staff and the Georgetown Group in the amount of ($57,963,000). We also will accept Mountain Bell's and Staff's position on whole life depreciation, remaining life depreciation, certain miscellaneous accounting adjustments to depreciation, and retirement of central office equipment (COE) in the combined amount of ($4,890,000). In addition, the Commission will accept Mountain Bell's proposed uncontested adjustment in the amount of ($440,000) resulting from the Economic Recovery Tax Act (ERTA), and Mountain Bell's proposed adjustment for expensing station connections of ($11,771,000). We will accept the Georgetown Group adjustment of $1,290,000 relating to the 48% to 46% tax change, and will accept the $981,000 adjustment proposed by the Georgetown Group relating to vacation pay accruals. As a result of the aforegoing adjustments, the Commission finds that the test year booked rate base of $1,149,760,000 should be adjusted in the amount of ($73,071,000) resulting in a net rate base of $1,076,689,000 for Mountain Bell in the test period.

B. Unamortized Bell Laboratories Research and Development Adjustment.

In Decision No. C80-1784 in Investigation and Suspension Docket No. 1400, the Commission directed that $2,135,000 of BTL research and development (R & D) be capitalized as an intangible, amortized over ten years, but not included in rate base. Re: Mountain States Telephone and Telegraph Company, 39 P.U.R.4th 222, 246 (1980). In its direct case, Mountain Bell included $2,199,000 in rate base representing its calculation of the unamortized balance. Other than being larger than the amount the Commission directed Mountain Bell to amortize ($2,199,000 versus $2,135,000) and other than not taking into consideration three years and two months of amortization, Mountain Bell's inclusions of the unamortized

balance is directly contrary to the Commission's directives in Decision No. C80-1784. The propriety of the BTL R & D directive was appealed by Mountain Bell to the Denver District Court in Civil Action No. 80CV9255. Civil Action No. 80CV9255 was dismissed upon stipulation of the parties and thus is not subject to collateral attack in this or any other proceeding and is final. Mountain States Telephone and Telegraph Co. v. Public Utilities Commission, 186 Colo. 260, 269-271, 527 P.2d 524 (1974); 40-6-112(2), CRS 1973. Accordingly, the Commission does not accept the $2,199,000 BTL adjustment proposed by Mountain Bell.

C. Property Held for Future Use.

Three minor adjustments to rate base, as shown on Exhibit 120, page 2 of 2, lines 6, 7, and 8, were recommended by Staff through Witness William A. Steele to reflect the removal from the plant balance, plant amounts that were transferred to Account 103 (Miscellaneous Physical Property), a non-rate base account, and to reflect amounts booked in Account 100.3 (Property Held for Future Use) longer than two years. With respect to the latter, Mountain Bell neither transferred the original cost to Account 103, nor applied to the FCC for waiver of the two year limitation. Accordingly, the Commission accepts the Staff's ($278,000) adjustment with respect to property held for future use.

D. Construction Work in Progress.

Both the Staff and the Georgetown Group recommended that construction work in progress (CWIP) in the amount of $57,963,000 be removed from rate base. In the past, the Commission has permitted construction work in progress to be included in the rate base so long as Mountain Bell capitalized interest on CWIP at the same rate as the authorized rate of return on rate base. As the Commission pointed out in Decision No. 86103, dated December 20, 1974, if the amount of interest charged construction equals the return on the construction work in progress, the effect on revenue requirement is zero and it would not matter whether the construction work in progress was or was not included in rate base. In general rate increase proceedings, since I&S Docket No. 867 (the 1974 Mountain Bell case), the Staff has recommended, either or both, adjust-

ments to remove from rate base CWIP on which interest had not been capitalized to prevent current earnings on CWIP, or adjustments to rate base to reflect capitalization of interest on CWIP at the authorized rate of return. See, for example, Decision No. C80-1784, 339 P.U.R.4th at 233.

In this proceeding, the Staff is recommending that CWIP be removed from the calculation of rate base because Mountain Bell continues to ignore past Commission directives as to the proper rate at which interest should be capitalized on CWIP. During the test year, Mountain Bell capitalized interest at the AT&T quarterly rates of 10.9%, 11.1%, 11.4%, and 12.2%, respectively rather than at the 10.07% rate (or 10.08% rate, if the amount represented by ESOP is added to common equity, as proposed by Mountain Bell) authorized in Decision No. C80-1784. See 39 P.U.R.4th at 256-257.

By removing CWIP from rate base, the secondary problem of Mountain Bell not removing CWIP projects on which construction has been suspended is corrected. If a project on which work has been suspended is not removed from CWIP, and if the interest on such a project is not capitalized, Mountain Bell would earn a return currently.

Mountain Bell apparently takes the position that while no interest charged construction should accrue on projects for which work has been suspended, nevertheless a current return should be provided from the ratepayers. The logic of Mountain Bell's position is hard to understand. On those projects where the future of a project is in doubt, requiring that the project be suspended, and therefore bringing into question whether a capitalized return through the accrual of interest during construction is appropriate, Mountain Bell would have the current ratepayers support the carrying charge on the suspended project. We do not believe that this should be permitted to happen. Inasmuch as Mountain Bell has, in fact, been capitalizing interest at computed investment tax credit (ITC) rates, rather than at the authorized rate of return, and inasmuch as we believe that Mountain Bell is incorrect in wanting to obtain a return on suspended projects (even while no interest during

construction is accruing thereon), we agree with the Staff and the Georgetown Group that construction work in progress should be removed. Accordingly, the Staff's and the Georgetown Group's adjustment in the amount of ($57,963,000) will be adopted.

E. Accounts Payable.

The Georgetown Group has recommended that the Company's rate base be reduced by $4.7 million due to construction accounts payable owed during the test year to Western Electric and that rate base should be further reduced by an additional $4.1 million for accounts payable to Western Electric relating to materials and supplies. The Georgetown Group further recommends that the rate base should be reduced by accounts payable relating to construction because the Company's telephone plant under construction account accrues interest during construction on all the dollars included in that account even though the Company has not actually expended investor funds to the amount indicated in its balance for telephone plant under construction account. Georgetown Group further recommends that there be adjustments for accounts payable relating to materials and supplies which would be on the same basis as that for accounts payable relating to construction in that accounts payable also represent amounts on which the Company is earning a return for which the Company has not expended the funds of investors.

Mountain Bell Witness Shriver addressed the proposed reduction of rate base for accounts payable which was recommended by the Georgetown Group Witness Madan. Basically, Mr. Shriver contended that Mr. Madan was looking at only one side of the balance sheet and thereby reducing rate base by current liabilities without looking at the fact that dollars shown on the right hand side of the balance sheet are also supporting other current assets such as cash, accounts receivable, prepaid directory expense, and other prepayments such as prepaid rent and insurance. In other words, Mountain Bell submits that adjustments proposed by the Georgetown Group Witness Madan cannot appropriately be applied unless the entire financial picture of the Company is taken into account. Mountain Bell correctly states that it cannot run a business

without cash, accounts receivable and prepaid expenses. Accordingly, we will not adopt the proposed adjustments with respect to accounts payable proposed by the Georgetown Group Witness Madan in this Docket. The dispute between Mountain Bell and the Georgetown Group with respect to accounts payable vis-a-vis accounts receivable, etc., points out the necessity of Mountain Bell, in future proceedings, of providing a total comprehensive lead-lag cash working capital study and a general study of sources and uses of funds so that both sides of the balance sheet can be looked at as a whole to determine what cash working capital, if any, is necessary and appropriate as a part of rate base.

F. Federal Tax Rate Change From 48% to 46%.

The Georgetown Group proposed that the rate base of Mountain Bell be increased by $1,290,000 to reflect the fact that the Revenue Act of 1978 (Public Law 95/600) reduced the tax rate on corporate taxable income from 48% to 46%, effective January 1, 1979. The Staff, during the course of this proceeding, was persuaded of the appropriateness of this adjustment.

There is no question, of course, that a change in the tax rate from 48% to 46%, in effect, has created a "surplus" in Mountain Bell's deferred tax reserve account. In other words, prior to the tax rate change, the Company was booking its deferred taxes at a 48% rate which will be written off in the future at a lesser rate of 46%. There are two issues to be resolved by the Commission with regard to treatment of this surplus. First, over what period of time should the surplus be returned to ratepayers? Second, are there provisions in the Federal tax law which prohibit the elimination of that surplus in the deferred taxes reserved over a period of time other than as provided under the "average rate assumption" method?

As to the first issue, it is clear that the more rapid the return of the "surplus," the greater the likelihood that those who pay to build the tax reserve will receive the benefit of the surplus which is

being returned. Given the reorganization of the BOC's beginning in January 1983, the Commission believes that the return of this surplus should begin now. Otherwise, existing customers may never see the surplus amounts reducing their future rates when assets are transferred to the competitive arena.

With regard to the second issue as to requirements of Federal tax law pertaining to the time period for elimination of surplus, we are not aware of any provision which provides that a ratemaking treatment that reduces a public utility cost of service to reflect a surplus in the deferred tax reserve caused by a reduction in the corporate tax rate is inconsistent with the requirements of a normalization method of accounting. We agree with the New York Public Service Commission which stated in its Opinion 79-22 in Case No. 27469:

> We recognize the possibility that a future adverse IRS ruling could be applied retroactively to revoke the Company's tax benefit. For this to occur, however, the IRS would have to take the position that the existing statute, Section 167(3) of the Internal Revenue Code, required at all times whatever treatment is prescribed at any time by the IRS through its interpretive regulation. We believe that the risk of this occurring is so remote that it would be wrong to delay returning to consumers the excess accumulations solely on this basis.

With the passage of time, of course, that risk becomes even more remote. The Georgetown Group Witness Madan recommended the return of this surplus over the period of 1.5 years which has the effect of assuring payback to the monopoly customers. We agree. Accordingly, amortization of the surplus deferred income taxes over a 1.5 year period results in an increase in net operating earnings of $2,579,000 and a corresponding increase in average rate base of $1,290,000.

G. Vacation Pay Accrual.

The Georgetown Group has suggested that Mountain Bell's normalization for deferred income taxes relating to vacation pay accrual was self-created and should be reversed by this Commission. We agree. There is no requirement that these amounts have to be normalized under the tax code. By way of explanation of this adjustment, the Company is allowed

to deduct on its tax books every year an additional amount relating to vacation pay that employees have accrued as of the end of the year. This expense is permitted as a tax deduction and therefore reduces Mountain Bell's taxes.

The benefit of these lower taxes disappears when the Company "normalizes" for the tax-to-book timing differences relating to vacation pay accruals, thereby increasing booked tax expense to the amount that would be anticipated without the benefit of the vacation pay as a tax deduction. The effect of this treatment is to charge current customers more than is necessary, because it recognizes as an expense taxes that are not currently being paid. The requirement for current taxes of the Company's monopoly ratepayers should be the taxes actually paid to the government. The Company's attempt to arbitrarily assign these tax savings to some future period is rejected by this Commission.

There is also the issue of the impending divestiture to be considered. These tax benefits are benefits that have accrued to the monopoly customers. To the extent that the impending divestiture results in the transfer of some of these benefits to a nonregulated company, an inequitable result would be produced. There is simply no tax requirement that this Company do anything other than reflect the actual tax expenses with regard to this item on its books and that such tax expenses be used for regulatory purposes.

Reversals of the Company's adjustment to normalize the tax savings associated with vacation pay accruals would increase net operating earnings by $1,621,000 and increase the Company's average rate base by $981,000.

H. Deferred State Income Taxes.

The Georgetown Group has recommended that the Commission require the flow-through of Colorado State income taxes which are deferred which would have the result of increasing test year operating income by $3.13 million and raising rate base by $4.35 million. The Georgetown Group states that Mountain Bell unilaterally has made an accounting decision to normalize Colorado State deferred income taxes rather than flowing them

through. The Georgetown Group further states that there is no showing that normalization is required for the Company to be in an adequate cash flow and financial position. Inasmuch as the record indicates that Mountain Bell was in a very healthy position (59%) with regard to its internal generation of funds, the Georgetown Group contends that tax normalization for Colorado State income tax purposes is not required. The Georgetown Group contends that in the event the Colorado Legislature intended to preclude the flow through of state deferred income taxes, it could have so stated and that the limited incorporation of "federal taxable income" cannot be read so broadly as to restrict this Commission's statutory and constitutional power. The Georgetown Group further states that Federal regulations do not affect a state commission's ability to require the flow through of benefits to ratepayers for the year in which the benefits are generated.

Mountain Bell witness Shriver pointed out that Mountain Bell had been taking accelerated depreciation for state income tax purposes since 1970, which is a practice which has been recognized by this Commission continually for accounting and regulatory purposes. Accelerated depreciation is recognized under Section 167(1)(G) of the Internal Revenue Code which requires normalization in order to claim accelerated depreciation for Federal income tax purposes. Furthermore, the Uniform System of Accounts specifically provides accounts for reporting deferred state income taxes. Although the Georgetown Group believes that no provision of Colorado law requires similar normalization treatment, thereby enabling this Commission to flow through the benefits received from accelerated depreciation to the ratepayer public, we believe it is necessary to examine the relevant Colorado constitutional and statutory provisions.

Article X, Section 17 of the Colorado Constitution provides for the levy of income taxes by the General Assembly. Section 19 of Article X of the Colorado Constitution states as follows:

> The general assembly may by law define the income upon which income taxes may be levied under section 17 of this article by reference to provisions of the laws of the United States in effect from time to time, whether

> retrospective or prospective in their operation, and shall in any such law provide the dollar amount of personal exemptions to be allowed to the taxpayer as a deduction. The general assembly may in any such law provide for other exceptions or modifications to any of such provisions of the laws of the United States and for retrospective exceptions or modifications to those provisions which are retrospective. (Emphasis added.)

Colorado's Income Tax Act was promulgated pursuant to these constitutional provisions. A statement of the legislative intent is found at CRS 1973, 39-22-102, which reads as follows:

> The general assembly hereby finds and declares that it is implementing section 19 of article X of the State Constitution in order to:
>
> Simplify preparation of state income tax returns; aid interpretation of the state income tax law through increased use of federal judicial and administrative determinations and precedents; and improve enforcement of the state income tax laws through better use of information obtained from federal income tax audits.

The definitions section of the Colorado Income Tax Act of 1964 also makes clear that it was the intent of the General Assembly to adopt the actual provisions of the Internal Revenue Code. CRS 1973, 39-22-103 (13), reads:

> Any term used in this article shall have the same meaning as when used in a comparable context in the federal internal revenue code of 1954, as amended. Any reference in this article to the "internal revenue code" means the provisions of the internal revenue code of 1954, and amendments thereto, and other provisions of the laws of the United States relating to federal income taxes, as the same may be or become effective at any time or from time to time, for the taxable year.

This provision not only adopts and incorporates the provisions of the Internal Revenue Code but all other provisions of the laws of the United States relating to Federal income taxes.

Thus, when Colorado statute states that the ". . . net income of a corporation means the corporation's Federal taxable income, as defined in the internal revenue code, for the taxable year, with the modifications specified in this section," CRS 1973, 39-22-304, it is merely carrying out the clear intention of the framers of the Constitution and the General Assembly to adopt all provisions of the Federal Internal Revenue Code and associated laws, and to incorporate those provisions

through. The Georgetown Group further states that there is no showing that normalization is required for the Company to be in an adequate cash flow and financial position. Inasmuch as the record indicates that Mountain Bell was in a very healthy position (59%) with regard to its internal generation of funds, the Georgetown Group contends that tax normalization for Colorado State income tax purposes is not required. The Georgetown Group contends that in the event the Colorado Legislature intended to preclude the flow through of state deferred income taxes, it could have so stated and that the limited incorporation of "federal taxable income" cannot be read so broadly as to restrict this Commission's statutory and constitutional power. The Georgetown Group further states that Federal regulations do not affect a state commission's ability to require the flow through of benefits to ratepayers for the year in which the benefits are generated.

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into the determination of corporate taxable income for Colorado. Likewise, CRS 1973, 39-22-107(3) provides that the taxpayer's method of accounting under this article shall be the same as his method of accounting for Federal income tax purposes. Those provisions embrace all provisions of accelerated depreciation, including §167(1)(G) of the Code. CCH Colorado State Tax Reporter, paragraph 11-065.10, p. 1216. Further, when the General Assembly intended to modify Federal law in concert with Article X, Section 19 of the Colorado Constitution, it did so specifically. (See, e.g., CRS 1973, 39-22-110, 113, 39-22-501, et seq. [Special Rules].) No modifications have been made to the laws and regulations governing requirements for accelerated depreciation.

Since the provisions of the Federal Internal Revenue Code and associated regulations clearly require normalization of accelerated depreciation for ratemaking purposes, by adopting the provisions of these laws and regulations, Colorado would appear to require normalization in order for Mountain Bell to qualify for accelerated depreciation for Colorado state income tax purposes.

Accordingly, the Commission finds that it should not adopt the proposed adjustment made by the Georgetown Group deferral of state income taxes.

I. Depreciation.

In that portion of the decision entitled Income and Expenses, we shall discuss in more detail straight line remaining life depreciation (SLRL or remaining life) and straight line equal life group (SLELG or ELG), as well as certain other depreciation issues. For purposes of establishing the proper rate base figures, however, we shall state here that the Company proposed adjustment to rate base as a result of the remaining life depreciation in the amount of ($3,786,000) will be adopted but that the Company proposed adjustment for ELG depreciation in the amount of ($175,000) will be rejected.

J. Summary.

The following is a tabular summary of the adjustments which we are adopting in this proceeding with respect to Mountain Bell's rate base:

Depreciation	$ 55,000
ERTA	(440,000)
Expensing Station Connections	(11,771,000)
Whole Life Depreciation	(999,000)
Remaining Life Depreciation*	(796,000)
Remaining Life Terminal Equipment Represcription	(2,990,000)
Retirement of Central Office Exchange	(160,000)
Property Held for Future Use	(278,000)
CWIP	(57,963,000)
48% to 46% Tax Change	1,290,000
Vacation Pay Accrual	981,000
	($73,071,000)

As a result of the foregoing adjustments which we have adopted, we find that Mountain Bell's rate base is as follows:

Gross Rate Base	
Plant in Service	$1,478,803,000
Plant Under Construction	-0-
Property Held for Future Use	1,274,000
Materials and Supplies	12,069,000
TOTAL INVESTMENT	$1,492,146,000
Deductions From Gross Rate Base	
Depreciation Reserve	$ 244,693,000
Deferred Income Taxes	162,073,000

* The Commission's adoption of Mountain Bell's adjustment for SLRL carries with it the inclusion by Mountain Bell of $3,226,000 of SLRL in its booked depreciation reserves.

Unamortized Pre-1971	
Investment Tax Credits	1,566,000
Customer Deposits	4,774,000
Construction Charge Contracts	2,351,000
TOTAL DEDUCTIONS	$ 415,457,000
NET RATE BASE	$1,076,689,000

VII

INCOME AND EXPENSES

The booked test year net operating earnings (NOE) of Mountain Bell are $107,555,000 (Exhibit 182). Both Mountain Bell and the Staff made a number of positive and negative adjustments to the booked test year NOE. Mountain Bell's total adjustments were ($6,478,000), which brought the booked NOE down to $101,077,000. The Staff's net operating adjustments amounted to ($2,249,000), which brought the booked NOE down to $105,306,000. The Georgetown Group had positive and negative adjustments which resulted in an overall adjustment to net operating earnings of $13,782,000, which brings the net operating earnings of Mountain Bell, in its view, to $121,337,000. Basically, the Commission finds, that with certain exceptions noted below, the NOE and expenses as ultimately found by the Staff are correct. Accordingly, we shall set forth in Section A herein the net operating earnings as found by the Staff.

A. Net Operating Earnings (NOE).

As indicated above, Mountain Bell stated test year booked net operating earnings are set forth as $107,555,000. Either Mountain Bell, the Staff, or one or more of the intervenors proposed adjustments in approximately 46 areas relating to net operating earnings. However, for purposes of this Decision, the Commission will discuss only those adjustments upon which there was some disagreement which we believe merit discussion in this Decision. Generally speaking, the Commission is adopting the adjustments which have been made by the Staff, together with two adjustments proposed by the Georgetown Group. For ease of following

Unamortized Pre-1971	
Investment Tax Credits	1,566,000
Customer Deposits	4,774,000
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A. Net Operating Earnings (NOE).

As indicated above, Mountain Bell stated test year booked net operating earnings are set forth as $107,555,000. Either Mountain Bell, the Staff, or one or more of the intervenors proposed adjustments in approximately 46 areas relating to net operating earnings. However, for purposes of this Decision, the Commission will discuss only those adjustments upon which there was some disagreement which we believe merit discussion in this Decision. Generally speaking, the Commission is adopting the adjustments which have been made by the Staff, together with two adjustments proposed by the Georgetown Group. For ease of following

the discussion herein, Table No. 1 lists the adjustments which have been made by the Staff or proposed by the Company and accepted by the Staff, which increase or decrease Mountain Bell's pro forma net operating earnings in the following particulars:

Table No. 1
(000's)

	Test Year NOE Booked	$ 107,555
(1)	Advertising	1,336
(2)	Elimination of Contributions and Club Dues	232
(3)	Elimination of Legis. Advoc.	16
(4)	Normalization of Rate Case Exp.	15
(5)	Amortization of Bell Labs	(119)
(6)	Prior Period Adjustments	179
(7)	Operating Rents	252
(8)	Depreciation Expense	679
(9)	Economic Recovery Tax Act	(9)
(10)	Expensing Station Connections	1,200
(11)	ELG Depreciation	-0-
(12)	Whole Life Depreciation	(1,813)
(13)	Remaining Life Depreciation	(1,522)
(14)	Terminal Equip. Repres.	(1,771)
(15)	Retirement of COE	174
(16)	1981 Directory Advertising	1,679
(17)	1982 Directory Advertising	3,372
(18)	Local Exchange Reclassification	2
(19)	Terminal Equip. Repricing	1,044
(20)	Independent Company Settlement	(13)
(21)	1981 Wages and Benefits	(4,455)
(22)	1982 Wages and Benefits	(1,784)
(23)	Social Security Tax Increase	(14)
(24)	Postal Rate Increase	(178)
(25)	Annualization of 1981 Pensions	(26)
(26)	Annual Value of 1982 Pensions	18
(27)	Interest on Customer Deposits	(558)
(28)	Annualization of PUC Assessment	(33)
(29)	Cost of Debt	1,146
(30)	Semi-Public PBX	210
(31)	Semi-Public Coin Telephone	170
(32)	Interest Charged Construction	(5,823)
(33)	GS&L: FCC Memo & N.Y. Tax	187
(34)	GS&L: ERTA	26
(35)	GS&L	2,701
(36)	BIS	231
(37)	Cost Sharing	959
(38)	Conduit Billing	41
	Total Adjustments	$ (2,249)
	Staff Adjusted Net Operating Earnings	$ 105,306

Of the adjustments to NOE proposed by the Staff, or proposed by the Company and accepted by the Staff, listed above, Table No. 2 lists the adjustments that were uncontested between the Company and the Staff and are adopted by the Commission:

Table No. 2
(000's)

(1)	Elim. of Contrib. & Club Dues	$ 232
(2)	Elim. of Legis. Advoc.	16
(3)	Normalization of Rate Case Exp.	15
(4)	Amortization of Bell Labs	(119)
(5)	Prior Period Adjustments	179
(6)	Operating Rents	252
(7)	Depreciation Expense	679
(8)	Economic Recovery Tax Act	(9)
(9)	Expensing Station Connections	1,200
(10)	Whole Life Depreciation	(1,813)
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(23)	Annualization of PUC Assessment	(33)
(24)	Semi-Public PBX	210
(25)	Semi-Public Coin Telephone	170
(26)	GS&L: FCC Memo & N.Y. Tax	187
(27)	GS&L: ERTA	26
	Total Noncontested Adjustments	$ (1,060)

Of the adjustments to NOE proposed by the Staff or proposed by the Company and accepted by the Staff, listed above in Table No. 1, Table No. 3 lists adjustments which were contested between Mountain Bell and the Staff:

Table No. 3
(000's)

(1)	Advertising	$ 1,336
(2)	ELG Depreciation	-0-
(3)	1982 Wages and Benefits	(1,784)
(4)	Social Security Tax Increase	(14)
(5)	Annual Value of 1982 Pensions	18
(6)	Cost of Debt	1,146
(7)	Interest Charges Construction	(5,823)
(8)	GS&L	2,701
(9)	BIS	231
(10)	Cost Sharing	959
(11)	Conduit Billing	41
	Total Contested Adjustments	$ (1,189)

For reasons to be set forth later in this Decision, the Commission has adopted the Staff's recommended changes to NOE of the contested amounts from Table 3 as follows: (1) Advertising will become an adjust-

ment of $559,000 to NOE; (2) ELG Depreciation, $-0-; (3) 1982 Wages and Benefits, ($1,784,000); (4) Social Security Tax Increase, ($14,000); (5) Annual Value of 1982 Pensions, $18,000; (6) Cost of Debt, $1,146,000 (to be further modified to $1,191,000); (7) Interest Charges Construction, ($5,823,000); (8) GS&L, $2,701,000; (9) BIS, $231,000; (10) Cost Sharing, $959,000; and (11) Conduit Billing, $41,000.

In addition to the adjustments proposed by the Staff to NOE and accepted by the Commission, the Georgetown Group proposed the following additional adjustments as set forth in Table No. 4.

Table No. 4
(000's)

(1)	Amortization of Investment Tax Credits (ITC's) Relating to Expensing Station Connections (ESC)	$ 499
(2)	48% to 46% Tax Change	2,579
(3)	Vacation Pay Accrual	1,621
(4)	State Tax Flow-Through	3,130
(5)	Affiliated Interests	1,035
Total Additional Georgetown Group Adjustments		$ 8,864

For reasons to be delineated later in this Decision, the Commission will adopt the following Georgetown Group adjustments to NOE from Table 4: (2) 48% to 46% Tax Change, $2,579,000; and (3) Vacation Pay Accrual, $1,621,000.

B. Summary of Adjustments.

Table No. 5 is a tabular summary of the adjustments which we are adopting in this proceeding with respect to Mountain Bell's net operating earnings:

Table No. 5
(000's)

Test Year Booked NOE		$ 107,555
(1)	Advertising	559
(2)	Total Uncontested Adjustments (listed in Table 2)	(1,060)
(3)	Total Contested Adjustments (Table 3 excluding Advertising and Changing Cost of Debt to $1,191,000)	(2,480)
(4)	Georgetown Group Adjustments (Commission accepted Table 4 adjustments)	4,200

Commission Adopted Net Operating Earnings	$ 108,774

The Commission will discuss the foregoing adjustments.

C. Advertising.

Initially the Staff recommended that all advertising expenses be removed by virtue of the fact that Mountain Bell, in its direct case, had not put into evidence copies of the ads or their associated costs. On rebuttal, Mountain Bell did submit copies of its advertising together with the categorized costs of its various campaigns.* However, the specific costs of the individual ads were not furnished. On the record, counsel for Mountain Bell agreed that in the event the Commission determined that one or more ads within a particular campaign should not be included, that it would be necessary, and acceptable to Mountain Bell, that the entire cost of the particular campaign of which the disallowed ads were a part, would be removed from net operating expenses.

The Commission has also assigned the acceptable ads into competitive and non-competitive categories. With respect to the informative ads, all but one such ad have been approved by the Commission. Two of the informative ads have been allocated to the competitive sector. There were seven advertising campaigns in which Mountain Bell did not present ads for our review. Accordingly, the $56,714 cost of such ads will be removed from Mountain Bell's expenses. There were $71,285 of ads that were not properly assigned to a campaign and this amount will be disallowed. There were $323,334 of ads for long distance on-peak calling that Mountain Bell did not prove were cost beneficial and this amount

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* We basically agree with an objection raised by the Staff to Mountain Bell's presenting advertising evidence for the first time in rebuttal rather than in its direct case. However, for this proceeding only, we allowed this evidence to be submitted in rebuttal since we had not explicitly ruled on this procedure previously. Mountain Bell is now on notice that waiting to present significant and relevant testimony and exhibits of any nature until a rebuttal case, when the same normally can be presented in direct, will not be tolerated in future cases before this Commission.

will be disallowed. Finally, there were certain ads of a national nature costing $445,169 which were not identified with Mountain Bell's intrastate operations, which were billed to Mountain Bell by AT&T through conduit billing. Since Mountain Bell did not demonstrate that these "national" ads were of any particular benefit to Mountain Bell's ratepayers, the cost thereof shall be removed.

After removing total advertising costs in the amount of $896,502, and making the appropriate income tax adjustments with respect thereto, the net operating earnings of Mountain Bell are increased by $559,000.

D. Equal Life Group Depreciation (ELG).

Mountain Bell has requested approval of straight line equal life group (ELG) methodology based on its approval by the Federal Communications Commission in Docket No. 20188. ELG is a group based straight line method. Mountain Bell and the FCC are of the opinion that ELG will stimulate investment and maintain efficient communication services by insuring timely recovery of invested capital. In essence, Mountain Bell and the FCC appear to take the position that the seeming attraction of stretching out depreciation over a longer period of time to hold down the depreciation expenses may impose longer term costs on our society which far outweigh the short term advantages.

The ELG method of depreciation is, of course, a refinement of the straight line vintage group (SLVG) method. The difference between ELG and SLVG is in the definition of the basic group or vintage of equipment used for the determination of the depreciation rate. With SLVG depreciation, each account is subdivided into categories which are further divided into vintage groups. Under the ELG method, the vintage group is further subdivided into groups which have equal life characteristics. For example, all assets within a vintage which are expected to live one year make up one equal life group; those expected to live two years comprise a second equal life group, etc. SLVG and ELG utilize the same data and basic methodology; ELG is a refined SLVG.

The Staff has recommended that the Commission not authorize Mountain Bell to use ELG. First of all, as indicated, ELG attempts to segregate each vintage group into assets with equal projected lives. Two reasons can account for individual lives and the vintage not being equal--the asset groupings are not homogeneous or chance. We agree with the Staff that depreciation rates should not be designed to compensate for a chance occurrance.

Second, the Staff contends that implementation of ELG would cause a distortion in the depreciation expense until all plant originally depreciated under SLVG is retired. Historically, Mountain Bell has used SLVG for depreciating plant. With the SLVG, under-recovery on vintages of plant in the early stages of use is offset by over-recovery on vintages of plant nearing retirement. Overall, with a going business, SLVG tends to reflect overall consumption of plant. The initial increase in depreciation expense occurs when ELG is introduced, since the balancing of over- and under-recovery using the vintage group method is disrupted. The higher depreciation charges associated with ELG in the early years of vintages combined with the over-recovery of vintages in the later stages of asset lives under SLVG will produce a distortion in reasonable depreciation expense to the detriment of ratepayers until assets originally depreciated under SLVG are retired.

Third, the Staff contends, and we agree, that the impact of the increased depreciation charges associated with the introduction of ELG on new plant, combined with the increased depreciation charges associated with straight life remaining life (SLRL, which will be discussed below) on existing plant will cause inequity among generations of customers.

Fourth, ELG depreciation is complex, requires constant monitoring and extensive computer capabilities to oversee. These capabilities are not presently available to the Staff of the Commission.

Fifth, the lower salvage value of plant proposed by Mountain Bell is not consistent with its ELG rates, thus overstating depreciation expense.

Finally, over the short term ELG will result in substantial increases in rates to customers. The adjustment in this Docket contains only the impact of ELG on one plant category for one-half year. Although ELG is theoretically plausible, its practical implementation at this time would overburden current ratepayers as well as impose a burden upon Staff resources which cannot be undertaken at this time. Accordingly, we shall not grant Mountain Bell's request to adopt the ELG depreciation methodology at this time. The non-adoption by the Commission of ELG results in rejection of the $175,000 reduction of Mountain Bell's rate base and a reduction of $299,000 in net operating earnings for the Company.

E. Remaining Life Depreciation.

The Staff has recommended that the Commission recognize the depreciation represcription that took place at the three-way meeting between the Commission Staff, the FCC, and AT&T in August of 1982. This will render moot any necessary treatment of the 1981 depreciation represcription of terminal equipment. The Commission accepts the Staff's recommendation in this regard.

Mountain Bell has proposed, and the Staff agrees, that Mountain Bell be authorized to use straight line remaining life (SLRL) depreciation. SLRL adjusts for historic under- and over-accruals by amortizing the reserve deficiency or excess over the remaining life of the asset. In other words, SLRL provides a mechanism which would more nearly allocate capital recovery to the customer group receiving the benefit of the assets being depreciated. Since a utility has a right to recover capital prudently invested in providing utility service, a mechanism similar to remaining life is needed to achieve this objective. No party has contended that Mountain Bell should be precluded from recovering its invested capital because the capital was imprudently invested. Opposition to the use of SLRL has been to the effect that any decision on the use of SLRL should be postponed until after the AT&T divestiture. However, we agree with the Staff that this position has little merit for four reasons.

First, any delay in the implementation of SLRL or a similar mechanism will result in the allocation of the historic reserve deficiencies to customers less likely to receive any benefit from the assets during the period in which the under-recovery occurred. In other words, it is less likely that the customers who received the benefit of the lower depreciation rates will be the customers charged with recovering the deficient charges.

Second, any delay in the implementation of SLRL or a similar mechanism could significantly escalate the immediate customer impact at the time it is finally authorized. As was stated previously, in all probability estimated lives of assets will continue to decline. If the amortization of past deficiencies in accruals is postponed any existing reserve deficiencies will remain intact, and combined with probable future deficiencies will render the transition to SLRL significantly more burdensome to ratepayers at the time of transition.

Third, adoption of remaining life would not result in the over-recovery of the asset's costs prior to the divestiture. SLRL only compensates for the historic under-recovery of the asset's costs. The use of remaining life allocates asset's costs to the period in which they were dedicated to providing utility service, the same period in which those costs would have been allocated had regulators and Company personnel had perfect foresight when originally estimating asset lives.

Finally, at present the bond ratings of the BOCs are being held in suspension by both Moody's and Standard and Poor until more information on the effects of the divestiture is available. Both agencies have indicated that in the near future they will analyze the operations of each of the operating subsidiaries (to include the regulatory climate), in order to determine the bond ratings for each of the independent companies after divestiture. Therefore, any decision on the capital recovery issue before the Commission should include some consideration of the effect that such a decision will have on the ratings of Mountain Bell after divestiture.

Both Standard and Poor and Moody's are aware of the capital recovery problems currently confronting the Bell System. With respect to ratings, there are three possible consequences to inaction in addressing the depreciation issue.

(1) Inaction would preclude recovery of capital prudently invested in providing utility service;

(2) Inaction would delay recovery of currently invested capital resulting in declining internal funds generation ratios and a greater need to access capital markets; and

(3) Estimates of depreciable lives again will be extended and then stabilize rendering the vintage group method suitable for achieving Mountain Bell's capital recovery needs.

It is the Staff's position that the latter of these possibilities would be considered as extremely improbable by the rating agencies. In Standard and Poor's "Credit Comment" of September 20, 1982 (Exhibit 146) the capital recovery issue in this proceeding is addressed. In discussing the potential for lower ratios of internal cash generation to capital and the consequences of the divestiture generally it is stated: "Improvements in depreciation accruals relative to spending could, over time, fully offset and possibly more than offset, the negative cash flow internal funding impact of the transfer of customer premise equipment to AT&T."

In light of the recent published comments of the rating agencies any decision which fails to address the depreciation issue could be considered as detrimental by the agencies when determining bond ratings subsequent to the divestiture. Due to the fact that future bond ratings could affect Mountain Bell's ability to access capital markets and the cost of funds acquired through those markets, we do not believe it would be prudent, for the foregoing reasons, to give negative signals to the rating agencies with respect to SLRL. Accordingly, we shall approve SLRL

for Mountain Bell. The result of our approval of SLRL is to decrease Mountain Bell's rate base by $3,786,000 and to decrease its net operating earnings in the test year by $1,522,000.*

F. Remaining Life Terminal Equipment Represcription.

Concomitant with our adoption of SLRL, terminal equipment represcription results in a negative adjustment to Mountain Bell's NOE in the amount of $1,771,000.

G. 1981 Wages and Benefits.

As with all revenue and expense changes within the test period, Mountain Bell has annualized wage increases that became effective during the test period. Following past Commission practices, neither Mountain Bell nor the Staff of the Commission proposed a productivity offset to a test year wage increase. Georgetown Group Witness Madan again proposed an offset to the in-period wage increase annualization.

The evidence reflects that certain Mountain Bell employees received wage increases in April of 1981, and others received pay increases in August of 1981. Both the Company and the Staff of the Commission "annualized" these wage increases, i.e., revised wage expenses as if the rate of pay after the increases became effective was the rate of pay on the first day of the test period. The annualization method employed was identical to other expense changes, such as the two 1981 postage rate increases, and also identical in methodology to the 1981 directory advertising rate increases that caused test period revenues to be adjusted upwards.

Mr. Madan's adjustment focuses on the 12 months following the effective date of a wage increase. Under this adjustment, a productivity offset is applied to that portion of the 12-month period not booked by Mountain Bell during the 1981 test year. Mountain Bell submits, and we agree, that Mr. Madan has not provided any rationale supporting the need

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* The Commission's adoption of Mountain Bell's adjustment for SLRL carries with it the inclusion by Mountain Bell of $1,857,000 of SLRL in its booked depreciation expenses.

to focus on the first 12 months after a wage increase. The purpose of an annualization adjustment is to take a price level change during the test year and adjust the year as if that price were in effect on the first day of the test period. Test year volumes, therefore, remain unchanged. This annualization is necessary for both revenues and expenses. In this manner, the Commission is presented with a full 12 months of revenue-to-expense relationships more consistent with the revenue-to-expense relationships that will exist when rates authorized will be effective. Nothing in this process suggests that an annualization adjustment should somehow be modified by focusing on the first 6 months, 12 months, or 18 months that the revenue or expense level is booked by the utility.

Mountain Bell submits that all productivity increases realized by Mountain Bell in Colorado are reflected in 1981 operating results presented to the Commission as the test year in this proceeding. The Company and Staff wage annualization adjustment merely recasts the 1981 test year as if the wage levels increased during the year were effective from the first day of the year. No rationale has been presented to treat in-period wage annualizations in a manner different than other price level changes during the test year. Further, by focusing on the 12 months after a wage increase becomes effective (for whatever reason), and proposing to offset with a productivity adjustment that portion of the first 12 months not paid in the test year, Mr. Madan seeks to have productivity gains after the test period applied to wage increases annualized in the test year. This ignores the capital and other expenses attendant to productivity gains during the year 1982 and consequently we are of the opinion that Mr. Madan's adjustments would constitute a regulatory mismatch. Accordingly, we adopt the position of Mountain Bell and the Staff, consistent with our treatment in I&S Docket No. 1400, and reject the theory that an in-period wage annualization must be offset in part by a productivity factor. As a result of our acceptance of Mountain Bell's and the Staff's position with respect to 1981 wages and benefits, the booked net operating earnings of the Company are reduced by $4,455,000.

H. 1982 Wages and Benefits.

Mountain Bell has recommended an adjustment to test year wage related expenses due to known and measurable wage increases during 1982. The Colorado Supreme Court in Mountain States Telephone and Telegraph Company v. Public Utilities Commission, 182 Colo. 269, 513 P.2d 721 (1973) has stated as follows:

> The relationship between costs, investment, and revenue in the historic test year is generally a constant and reliable factor upon which a regulatory agency can make calculations which formulate the basis for fair and reasonable rates to be charged. These calculations obviously must take into consideration in-period adjustments which involve known changes occurring during the test period which affect the relationship factor. Out-of-period adjustments must also be utilized for the same purpose. An out-of-period adjustment involves a change which has occurred or will occur, or is expected to occur after the close of the test year. An increase in the public utility taxes effective after the test year is a good example of such an adjustment. Wages and salary increases which have been contracted for and which will take effect after the test year must also be analyzed in the process of calculations. Such wage and salary increases may not exceed to any large extent the usual consequent increase in the productivity of the employees. If they do, which is generally the case in periods of uncontrolled inflation, then such out-of-period adjustments must be reckoned within the rate fixing procedure. (513 P.2d at 724)

The Staff of the Commission has concurred with Mountain Bell that an adjustment should be made to test year wage expenses to reflect out-of-period wage increases. The Staff and Mountain Bell disagree as to the methodology that should be employed in computing a productivity offset to 1982 wage increases, but both agree that such an adjustment is appropriate and necessary. Georgetown Group Witness Madan, however, recommends that no adjustment be made for the 1982 wage increases. Mr. Madan's testimony reflects two reasons for rejecting this adjustment: (a) an "abnormal" increase in employees during the test year, causing the test year to contain "excess" employees; and (b) no erosion of the Company's operating income due to the 1982 wage increases. We do not agree that the factual evidence in this proceeding necessarily supports those reasons.

I. Alleged "Excess" Employees.

Mr. Jamshed K. Madan introduced evidence of an increase in the number of Colorado employees during the test year. The record establishes an increase (net of reorganization) of 1,142 employees. This amounts to an increase in Colorado employees of 8.97% (1,142 ÷ 12,720). Mr. Madan alleged that this increase was "abnormal" and suggested adjustments to the Company's recommendations based on "excess" employees.

Of course, the allegation of "excess" employees must be tested against the factual evidence in this record of the volume of work undertaken by the Company during the 1981 test year. Since we believe it has been established from the evidence in this record that customer demand for telecommunications services in Colorado rose in a manner consistent with the addition of employees to service that demand, the allegations of "excess" employees clearly has not been conclusively demonstrated.

J. Appropriate Productivity Offset.

Mountain Bell and the Staff of the Commission did not agree with respect to the development of an appropriate productivity offset regarding the 1982 test period wage increases. In its revenue requirement proposal filed in April of 1982, Mountain Bell proposed a 5% offset based on an increase in labor factor productivity. This offset was based on a five year average, the time period found acceptable by the Commission in previous cases.

Staff Witness Karahalios used a four year average, rather than a five year average, in computing the productivity factor on the basis of his opinion that the 1981 negative 2.6 productivity factor was "abnormal." The two reasons that Mr. Karahalios believes that 1981 productivity factor was abnormal were that the accounting change causing certain installation activity cost to be expensed rather than capitalized caused a great deal more labor input in 1981, thereby distorting the average, and also because of an increase in employee levels greater than that which occurred in prior years. Mr. Karahalios also expressed concern that Mountain Bell had changed its productivity methodology since I&S

Docket No. 1400 without justification on the record, thereby lowering its productivity factor by 1.55%.

Mountain Bell agrees that the first factor cited by Mr. Karahalios with respect to the increased costs of expensing, rather than capitalizing, certain installation activities has merit, but that the second factor, namely the increase in employee levels, does not have merit. Mountain Bell recomputed the labor productivity factor by removing the effect of the accounting change brought about by expensing certain installation activity costs. As a result of the removal of that accounting change, the 1981 labor factor productivity grows from a negative 2.6% to 0. As a result of this change for the year 1981, Mountain Bell's productivity factor #2, as presented in this Docket, rose from 5% to 5.68%.

The Staff used an 80.89% offset ratio which was derived by using a 7.1% labor productivity factor. As indicated above, Staff's 7.1% factor was arrived at by taking a four-year average (1977-1980). The Staff's four-year average of 7.1% is almost the same as the 7.2% offset used by Mountain Bell in its last rate proceeding in I&S Docket No. 1400. It also was demonstrated on redirect testimony of Staff Witness Karahalios that a reconstruction of the five-year average used by Mountain Bell, taking into account the effects of expensing station connection charges and the change of methodology from prior rate proceedings, produces a labor productivity factor of 7.23%. The Commission finds that a 7.1% labor productivity offset factor is appropriate in this Docket. However, we also believe that in future rate proceedings, Mountain Bell should explain and justify the methodology it uses to calculate its labor productivity factor and offset. Accordingly, the Commission will adopt the Staff's adjustment of ($1,784,000) to Mountain Bell's NOE.

K. Social Security Tax Increase.

The Staff made a $14,000 negative adjustment to Mountain Bell's NOE by removing the January 1, 1983 out-of-period adjustment made by Mountain Bell relating to increase in Social Security taxes. We agree

with the Staff's removal of the January 1, 1983 Social Security out-of-period increase inasmuch as that adjustment is one year and one day beyond the test period in this Docket.

L. Annualization of 1981 Pension.

As a result of the $4,455,000 negative out-of-period adjustment for 1981 wages and benefits, it is necessary to make an adjustment in the amount of ($26,000) for annualization of the 1981 pension.

M. Annual Value of 1982 Pension.

As a result of the negative adjustment of $1,784,000, with respect to the 1982 wages and benefits, it is necessary to make an $18,000 adjustment to the annual value of the 1982 pension.

N. Interest Adjustment for Cost of Debt.

Staff Witness Jorgensen proposed a methodology for determining an annualized interest expense for tax purposes. His methodology consisted of multiplying Staff's recommended average year, test year rate base (with CWIP added back in) of $1,134,652,000 (originally $1,132,381,000 before Commission adjustments) by the composite cost of debt of 4.02%. This produced an annualized interest expense of $45,613,000. Mountain Bell's 1981 per book interest (as adjusted by Mountain Bell) of $43,168,000 was then subtracted from Staff's annualized interest expense of $45,613,000 to derive an "interest annualization" which, in turn, was multiplied by the Federal income and state income tax rates to derive the Staff's recommended adjustments to income taxes. This resulted in an income tax adjustment of ($1,191,000), or a positive adjustment to net operating earnings of $1,191,000.

The Staff's 4.02% composite cost of debt had been calculated by Staff Witness Jorgensen by using a capital structure that did not include the job development investment credit (JDIC). It should be noted, however, that the Staff calculated revenue requirement through rate base (and not through capital as Mountain Bell had); Staff did not reduce Mountain Bell's rate base because of JDIC. Mountain Bell Witness Richard Walker was of the opinion that by not including JDIC in the capital

structure, the after tax return on JDIC was less than the after tax return granted to Mountain Bell through revenue requirement, thereby jeopardizing Mountain Bell's continued ability to take advantage of the JDIC. The only support offered by Mr. Walker for his opinion was Exhibit 174 (Internal Revenue Service Letter Ruling 8239122), which specifically provided that:

> This ruling is directed only to the taxpayer who requested it. Section 6110(j)(3) of the Code provides that it may not be used or cited as precedent.

IRS Ruling 8239122 is not only not a precedent by its own terms, but it appears also to be contrary to the opinion of the United States Court of Appeals for the District of Columbia, Public Service Company of New Mexico v. Federal Energy Regulatory Commission, 653 F.2d 681 (D.C. Circuit, 1981). In the Public Service Company of New Mexico case, the Federal Energy Regulatory Commission (FERC) had calculated an "overall rate of return" (composite cost of capital) without the inclusion of JDIC in the capital structure and applied this overall rate of return to the rate base, not capital. Like Mountain Bell, Public Service Company of New Mexico elected the second of three options provided under Section 46(f) of the Internal Revenue Code. Section 46(f)(2) of the Code prohibits either a cost of service reduction or a rate base reduction as a consequence of JDIC. The ability of a utility to continue to take JDIC would be lost if either of the prohibitions in Section 46(f)(2) is transgressed by a regulatory agency. In affirming the FERC, the District of Columbia Court of Appeals specifically found that not including JDIC in the capital structure of Public Service Company of New Mexico in calculating the "overall return," and the tax consequences thereof, did not result in either a cost of service reduction or a rate base reduction under Section 46(f)(2)(A) and (B). It should be noted that the Staff's treatment of Mountain Bell's JDIC (which is similar to the treatment by the FERC) produced a cost of service which was neither higher nor lower than would have been the case if JDIC did not exist. The FERC found that excluding accumulated deferred investment tax credit (ADITC) (i.e., JDIC)

from capitalization did not produce a reduction in cost of service beyond that permitted by Section 46(f)(2)(A). Id. at 691. The Court specifically affirmed this finding by the FERC.

In summary, although the funds to supply the JDIC are provided by ratepayers, the Staff, in accordance with the Congressional mandate, treated JDIC for cost of capital purposes in a manner equivalent to that had the funds been provided by investors and debt holders of the Company. In making its adjustment, the Staff neither lowered the Company's rate of return nor lowered its rate base. It merely gave the same treatment to JDIC, and in the same proportions, as it gave to the debt and equity components of Mountain Bell's capital structure. Doing that, of course, affects the overall expense level, and correspondingly, net operating earnings provided by the Company but it does not affect rate of return, rate base, or produce a cost of service that is higher or lower than the existing cost of service in the absence of the credit. Accordingly, the Commission accepts the Staff's $1,191,000 adjustment to Mountain Bell's net operating earnings with respect to the cost of debt.

O. Semi-Public PBX and Semi-Public Coin Telephone.

Mountain Bell did not contest the adjustment of $210,000 for semi-public PBX and the $170,000 adjustment for semi-public coin telephones made by the Staff, and accordingly, said adjustments are adopted by the Commission.

P. Interest Charged Construction.

As a result of the removal of CWIP from rate base, there is a corresponding adjustment of ($5,823,000) to Mountain Bell's NOE. Inasmuch as the Commission, as indicated above, has agreed with the Staff recommendation that CWIP be removed, this reciprocal adjustment is necessary.

Q. 48% to 46% Tax Change.

We have already discussed above, in connection with the proposed Georgetown Group adjustment to rate base, the effect of the Federal tax break change from 48% to 46%. Inasmuch as we have adopted the position

of the Georgetown Group with respect to this rate base adjustment, it is also necessary to make a net operating earnings adjustment in the amount of a positive $2,579,000.

R. Vacation Pay Accrual.

We have already discussed the vacation pay accrual issue in connection with rate base, and as indicated above, the reversal of Mountain Bell's adjustment to normalize the tax savings associated with vacation pay accruals would increase net operating earnings by $1,621,000.

S. State Tax Flow-Through.

Georgetown Group Witness Madan proposed a two-part adjustment for deferred state income taxes. He advocates flow-through to income during the test period of deferred Colorado income taxes realized during the year, accompanied by prospective termination of the accounting practice, and a five-year amortization of the amount in the State of Colorado deferred income tax reserve which resulted from utilizing accelerated depreciation for tax purposes under both State and Federal law. Mr. Madan's proposal would increase test year NOE by $3.13 million and rate base by $4.35 million. Mr. Madan did not recommend flowing through of deferred Federal income taxes.

The Commission does not agree with Mr. Madan's proposal. Mountain Bell has been taking accelerated depreciation for State income tax purposes since 1970, which is a practice which has been recognized by this Commission continually for accounting and regulatory purposes. Accelerated depreciation is recognized under Section 167(l)(G) of the Internal Revenue Code, which requires normalization as a predicate to claiming accelerated depreciation for Federal income tax purposes. The Georgetown Group apparently believes that although normalization of tax benefits received through accelerated depreciation (rather than flow-through) is required if Mountain Bell is to retain its entitlement to benefits of accelerated depreciation for Federal income tax purposes, that no corresponding provisions of the Colorado Income Tax Act of 1974,

39-22-101, et seq., CRS 1973, as amended, requires similar treatment. Our reading of the Colorado Income Tax Act leads us to the conclusion that Colorado intended to "track" Federal tax law through increased use of Federal judicial and administrative determinations and precedents.

The definitions section of the Colorado Income Tax Act of 1964 also make clear that it was the intent of the General Assembly to adopt the actual provisions of the Internal Revenue Code. CRS 1973, 39-22-103 (13) reads:

> Any term used in this article shall have the same meaning as when used in a comparable context in the Federal internal revenue code of 1954, as amended. Any reference in this article to the "internal revenue code" means the provisions of the internal revenue code of 1954, and amendments thereto, and other provisions of the laws of the United States relating to federal income taxes, as the same may be or become effective at any time or from time to time, for the taxable year.

This provision not only adopts and incorporates the provisions of the Internal Revenue Code but all other provisions of the laws of the United States relating to federal income taxes.

Thus, when Colorado statute states that the ". . . net income of a corporation means the corporation's federal taxable income, as defined in the internal revenue code, for the taxable year, with the modifications specified in this section," CRS 1973, 39-22-304, it is merely carrying out the clear intention of the framers of the Constitution and the General Assembly to adopt all provisions of the Federal Internal Revenue Code and associated laws, and to incorporate those provisions into the determination of corporate taxable income for Colorado. Likewise, CRS 1973, 39-22-107(3) provides that the taxpayer's method of accounting under this article shall be the same as his method of accounting for Federal income tax purposes. Those provisions embrace all provisions of accelerated depreciation, including §167(1)(G) of the Code. CCH Colorado State Tax Reporter, 11-065.10, p. 1216. Further, when the General Assembly intended to modify Federal law in accordance with Article X, Section 19, of the Colorado Constitution, it did so specifically. (See, e.g., CRS 1973, 39-22-110, 113, 39-22-501, et seq. [Special

Rules].) No modifications have been made to the laws and regulations governing requirements for accelerated depreciation.

Since the provisions of the Federal Internal Revenue Code and associated regulations clearly require normalization of accelerated depreciation for ratemaking purposes, by adopting the provisions of these laws and regulations, Colorado also would appear to require normalization in order for Mountain Bell to qualify for accelerated depreciation for Colorado State income tax purposes. Accordingly, no adjustment for flow-through of State deferred income taxes is made in this Docket.

Mountain Bell also raises the argument that accelerated depreciation provides for attendant reduction of capital costs by helping the internal generation of funds. It should be noted that by rejecting the Georgetown Group's proposal to flow-through State income taxes to flow-through the benefits received from accelerated depreciation, we are not thereby adopting Mountain Bell's position with respect to the internal generation of funds.

T. General Services and Licensing Agreement.

We agree with the recommendation of Staff Witness Hunt that the expense level of $6,729,871 be established for Mountain Bell's License Contract Agreement (LCA) expense. The LCA covers general services and license (GS&L) and certain BTL activities. We have adopted the Staff position because it excluded payments for services, research, and other activities that are not of direct benefit to the Colorado jurisdictional ratepayer and because the Staff followed the methodology which we outlined in I&S Docket No. 1400. Those services, research and activities that are not of direct benefit to the Colorado jurisdictional ratepayer are benefits accrued to competitive markets and products whose costs are assigned in whole or in part to the monopoly ratepayer; anti-trust cases and activities of AT&T which have no direct benefit to the Colorado jurisdictional ratepayer; activities which we have generally disallowed before, such as charitable contributions, memberships in social clubs, legislative contacts, etc.; and a proportion of the administrative and

support activities of the General Department of AT&T that reflect the administration of those activities which are not beneficial to the Colorado jurisdictional ratepayer.

Not only are these activities not beneficial to the Colorado jurisdictional ratepayer, but in addition, many of the services, research and activities performed under the LCA provide AT&T with the potential to underprice its competitive products and make up its lost revenue by shifting costs to the prices for monopoly services and products and consequently increasing monopoly services.

Also included in the Staff recommendation is a disallowance of the return on investment for the General Department and BTL. These Departments are funded by ratepayers who, rather than the stockholders, assume the risk. Inasmuch as the stockholders neither provided the funds for the General Department and BTL, nor assumed the risk with respect thereto, Mountain Bell should not be allowed to earn a return on that investment through the LCA. Furthermore, BTL is a non-profit organization and an expense entitling AT&T to earn a rate of return through the LCA fee would be a backdoor method of making BTL a profit-making organization, rather than a research organization. Accordingly, we shall adopt the Staff recommendation of expenses with respect to the LCA in the amount of $6,729,871. As a result of the acceptance of these expenses, the corresponding NOE of Mountain Bell is increased by $2,701,000.

U. Business Information Systems; Cost Sharing; and Conduit Billing.

We are adopting the Staff recommendation for expense levels for affiliated interest payments as follows:

Business Information Systems (BIS)	$1,373,780
Conduit Billing	776,800
Cost Sharing	435,100

It is clear that fees for each of the foregoing activities have risen rapidly with no indication of an equal increase in benefits to the Colorado jurisdictional ratepayer. Mountain Bell has not demonstrated that neither it nor AT&T has established an adequate method of cost control over these activities. On the contrary, testimony has demonstrated

that AT&T has the incentive to increase these expenses while Mountain Bell has no incentive not to take the services even if the costs far outweigh the benefits. Inasmuch as we believe that there has been an absence of an adequate method of cost control within AT&T, we agree with the Staff proposed methodology of allowing the cost and benefits of BIS expenditures to rise at the rate equal to the increase in the Consumer Price Index plus the rate of increase in the number of main telephones. The Staff recommended that two provisions be attached to this formulation. First, if the rate of increase in operating expenses per main telephone adjusted for inflation is greater than 3%, then no increase in BIS fees should be allowed. Second, if operating expenses adjusted for the Consumer Price Index decreases, then the allowable BIS expenditures should be increased by the rate of decrease in operating expenditures. We believe that the Staff proposed formula will help to check the seemingly uncontrolled increases in BIS expenditures. Allowing BIS fees to fluctuate with changes in the Consumer Price Index gives recognition to the fact that one must often increase one's pace to keep from falling behind. However, under this procedure, success in maintaining expenses will be recognized by the allowance of a greater expenditure for cost saving activities. In like manner, if expenditures on cost-saving activities rise rapidly, such an allowance would not occur. Thus, the Staff recommended formula provides incentives when the benefits are greater than costs. It also provides penalties when the costs outweigh the benefits, while recognizing the importance of efficiency producing programs and research. The Staff recommendation for a disallowance was also based on the fact that some BIS activities pertain primarily to competitive markets. As a matter of fact, it is admitted that 11.2% of the BIS system cost is related to competitive markets.

The cost sharing and conduit billing programs share many of the characteristics of the BIS methodology. Expenditures on conduit billing and cost sharing have also increased dramatically during the past few

years. The Colorado intrastate assessment for conduit billing has increased 235% between 1975 and 1981. Colorado intrastate assessment for cost sharing has increased 1331% since 1975. As with BIS, the Colorado ratepayers should receive the benefit of these expenditures. That benefit should be a reduction in operating expenses relative to expenditures on these items. Accordingly, we also adopt the Staff recommendation for the same treatment of conduit billing and cost sharing that has been recommended to be applied to BIS.

As a result of our adoption of the Staff recommendations with respect to the expense levels for BIS, conduit billing, and cost sharing, adjustments in Mountain Bell's NOE in the amount of $231,000 for BIS, $959,000 for cost sharing, and $41,000 for conduit billing, are adopted by the Commission in this Docket.

Summary

As a result of all contested and noncontested adjustments to Mountain Bell's stated test year booked net operating earnings of $107,555,000, we find that Mountain Bell's adjusted net operating earnings in the test year ending December 31, 1981 are $108,774,000.

VIII

RETURN ON INVESTMENT

A. Capital Structure.

1. AT&T Consolidated Capital Structure.

Inasmuch as Mountain Bell is a 100% owned subsidiary of AT&T, it is appropriate to use an adjusted AT&T consolidated capital structure as of December 31, 1981. As indicated by Staff Witness Jorgensen in his Exhibit 147 (page 1 of 2) the debt component of the AT&T consolidated capital structure as of December 31, 1981 was 45.27%, the preferred stock component was 2.33%, and the equity portion was 52.40%. Georgetown Group Witness LeLash, in his Exhibit 151, Schedule 1, Page 2, presented a basically similar, although not exactly identical, capital structure based upon amounts derived directly from AT&T source docu-

ments. Mr. LeLash's allocation (without adjustment for Western Electric) between preferred stock and common equity is not materially different from Mr. Jorgensen's. Accordingly, we will adopt the capital structure recommended by Staff Witness Jorgensen as set forth below.

Mountain Bell
Capital Structure

Bell System Capital Structure at 12-31-81	$ (Millions)	%	% Cost
Debt	47,895	45.27	8.87
Preferred Stock	2,469	2.33	7.83
Common Stock Equity	55,433	52.40	
TOTAL	105,797	100.00	

2. Employee Stock Ownership Plan (ESOP).

We agree with the Staff that it is not appropriate to include average employee stock ownership (ESOP) accruals as an explicit element of the capital structure as proposed by Mountain Bell. Throughout the year, Mountain Bell accrues its estimated contribution to ESOP. While this accrual is made monthly, the stock is purchased once per year when the Bell System files its consolidated income tax return. For the balance of the year, the monies that are accrued for this purpose are retained by the private trustee. ESOP funds that have been invested in AT&T common stock prior to and during the test year are already reflected in the test year and common equity ratios. Therefore, the addition of ESOP accruals to the capital structure need not be made. It is also true that ESOP accruals held by the trustee are not incurring the risk of an investment in AT&T common stock. If the uninvested ESOP accruals are not incurring the risk of an investment in AT&T common stock, the uninvested ESOP should not earn a corresponding equity rate of return.

3. Job Development and Investment Tax Credits (JDIC).

While it is true that JDIC is an item of capital to be earned on at the overall rate of return, we believe the Staff appropriately omitted JDIC from Mountain Bell's capital structure. If the approved rate of return is applied to rate base, rather than to the capital structure, then an item of capitalization that is deemed to be

earned upon at the overall rate of return need not be included in the capital structure. The computed cost of capital would be identical whether such an item of capitalization is included or excluded from the capital structure.

B. Rate of Return on Common Equity.

In this proceeding, the Commission heard testimony of five witnesses on the issue of fair rate of return on common equity. Mountain Bell sponsored two witnesses, Irwin Friend and Bruce B. Wilson. Intervenors Colorado Municipal League, Colorado Ski Country USA, and Colorado-Wyoming Hotel and Motel Association sponsored one witness, Matitayahu Marcus. Intervenor General Services Administration sponsored one witness, Mark Langsam. The Staff of the Commission sponsored one witness, Eric Jorgensen. In ascending order, the following ranges of fair rates of return on common equity were recommended to the Commission:

(a) Mark Langsam - 13.5% to 15%

(b) Eric Jorgensen - 13.75% to 14.75%

(c) Matitayahu Marcus - 15.1%

(d) Bruce B. Wilson (rebuttal case) - 17% to 18%

(e) Irwin Friend - 17.3%

(f) Bruce B. Wilson (direct case) - 17.5% to 19%

All five of the foregoing witnesses utilized the discounted cash flow (DCF) analysis. Mr. Langsam also employed a relative risk and earnings approach whereby he chose certain "reasonable alternatives to an investment in AT&T." Dr. Friend also employed a comparable earnings analysis in addition to his DCF analysis.

After analyzing methodologies used by the various witnesses, including the capital structures utilized to reach the recommended fair rates of return, the Commission finds that a fair rate of return on common equity for Mountain Bell, considering the economic and market conditions that exist today, is in the range of 13.75% to 14.75% as found by Staff Witness Jorgensen. We are inclined to pinpoint the appropriate rate of return at the upper end of that range or at 14.75%.

The DCF theory, accepted by this Commission, measures equity cost by combining current dividend yield and expected growth in imputed book value. This Commission has utilized the DCF methodology in a number of past proceedings, and we find that it is an acceptable and reliable method for deriving a fair rate of return on common equity. (See, e.g., decisions in I&S Docket No. 1330, I&S Docket No. 1400, I&S Docket No. 1425 and I&S Docket No. 1525.) The DCF methodology as used by this Commission is based upon the theory that the investor anticipates the cost of equity through the current market price of the stock by discounting the flow of future income attributable to both dividends and expected capital gains from the sale of the stock. The cost of equity is the discount rate which equates the present value of future income to the current market price of the stock.

Staff Witness Jorgensen determined that the current dividend yield was 9.75%, which was derived from his observations of daily yields of AT&T common stock for six- and twelve-month periods ending August 31, 1982, and updated through October 26, 1982. We agree that it is appropriate to use a historic yield based upon actual measured yields rather than forecasted dividend yields as proposed by Mountain Bell. Staff Witness Jorgensen testified that historic dividend yields best quantifies investor expectations with regard to yield. While some investors may expect an increase in dividends from year to year, AT&T did not increase its dividend per share from 1979 to 1980 and has not raised its dividend per share from 1981 to 1982. The annual dividend per share for AT&T common stock has been $5.40 since 1981. To compute a forecasted (or assumed) growth in dividend rate for the first year, based upon a composite of the predictions of selected investment analysts could overstate the current yield on the stock and could therefore overstate the cost of equity. Accordingly, we accept the historic 9.75% dividend yield as calculated by Staff Witness Jorgensen, and reject the projected dividend yield approach as proposed by Mountain Bell.

Staff Witness Jorgensen recommended that the Commission use growth rates of 4% to 5% in its DCF analysis to determine the cost of equity. Mr. Jorgensen measured historic growth rates in earnings, declared dividends, book value, and imputed book value per share of common stock for five- and ten-year holding periods ending December 31, 1981, using compound least squares, and logarithmic least squares methods. Compound growth rates were updated on data through August 31, 1982. Mr. Jorgensen checked the results of his historic growth rates with an implied growth rate test. We will accept the Staff recommendation set forth by Mr. Jorgensen to use historic growth rates of imputed book value per common share of 5%.

As Mr. Jorgensen testified, historic growth rates are a function of accounting data which in turn are a function of economic, financial, industrial, managerial and other conditions that existed during the period for which the accounting data are compiled. These growth rates, compiled over a period of time that encompasses a variety of conditions, represent trends which have remained relatively constant over time, and thus are a reasonable indication of the future. In I&S Docket No. 1400, we accepted the growth in book value per share as a proxy for growth. We continue to believe that growth in book value per share has the advantage of fluctuating less than growth rates produced by earnings per share or dividends per share and are less susceptible to distortion than are, for example, growth in dividends per share. In other words, growth in book value is a safer indication of growth to be produced by conditions in the long run.

Mr. Jorgensen testified that book value and imputed book value did not experience the sharp decline in growth, demonstrated by dividends and earnings in 1982. Indeed, growth in book value over time changes more slowly in both an upward and downward direction than do growth rates in dividends and earnings. Regardless of the volatility of long-term growth rates of dividends and earnings, growth in book value will change in the same direction but with less volatility.

We agree that the use of imputed book value obviates the need to separately calculate flotation costs or determine if market pressure exists because to the extent these factors have caused dilution (a decrease in net book value per share after a stock sale), they are included in the imputed book value. Imputed book value derives the change in book value from earnings per share less dividends per share, but does not include decreases in book value per share arising from dilution. That is to say imputed book value measures the changes in book value as though new shares had been issued at exactly 100% of existing book value.

The issue of whether to use projected growth rates in dividends rather than historic growth rates in book value in the DCF methodology, as proposed by Mountain Bell, is a question of first impression in this particular Docket as far as Mountain Bell is concerned. However, we note that in one recent case before this Commission, that is, I&S Docket No. 1564 involving the Southern Colorado Power Division of Centel Corporation, the Commission rejected Centel's proposal to use forecasted growth rates in the DCF analysis to determine a fair rate of return on equity. (See Decision No. C82-1662 and C82-1771.)

In summary the Commission accepts Staff Witness Jorgensen's measurement of dividend yield based upon his observations of daily yields of AT&T common stock for six- and twelve-month periods ending August 31, 1982 and updated through October 26, 1982, and we also accept his recommendation for the use of historic growth rates in imputed book value as being most representative of investor expectations of the future. A current divident yield of 9.75% plus expected growth in imputed book value of 5% provides a total rate of return on equity of 14.75% per year.

From the foregoing, the rate of return on Mountain Bell's average rate base, with the 14.75% return on equity, can be derived as follows:

Mountain Bell
Capital Structure and Rate of Return

Bell System Consolidated Capital Structure at 12-31-82	$ (Millions)	%	% Cost	Composite Cost %
Debt	47,895	45.27	8.87	4.02
Preferred Stock	2,469	2.33	7.83	0.18
Common Stock Equity	55,433	52.40	14.75	7.73
TOTAL	105,797	100.00		11.93

C. Overall Rate of Return and Pro Forma Earnings Requirement.

As previously indicated, the result of a 14.75% return to Mountain Bell equity translates to an overall rate of return to Mountain Bell of 11.93%. Applying the overall rate of return of 11.93% to Mountain Bell's rate base of $1,076,689,000 produces a required NOE of $128,449,000. As also indicated above, the Commission has found that Mountain Bell's test year pro forma earnings are $108,774,000, which means that on a test year pro forma basis, Mountain Bell's NOE failed to meet its required NOE by $19,675,000. To earn a dollar of NOE, the operating revenues must allow for income taxes. Thus, the $19,675,000 must be adjusted upward by revenue to income multiplier of 1.9573 which produces a revenue requirement deficiency of $38,510,000.

As indicated above, on November 30, 1982, the Commission entered Decision No. C82-1862, which was denominated as a "Revenue Requirements Minutes Order of the Commission." In Decision No. C82-1862, the Commission indicated that the overall revenue requirement which would be authorized was $38,510,000 (plus any capitalized interest as authorized therein). Earlier in this Decision, we quoted a portion of Decision No. C82-1862 which stated that $8,442,000 had been identified as being that portion of the overall revenue requirement increase associated with depreciation and cost changes for which it was not possible, at this time, to apportion between competitive and monopoly services. Thus, we stated that Mountain Bell would be permitted to effect across-the-board increases in its rates which will produce an additional $30,068,000 (i.e., $38,510,000 minus $8,442,000) in increased revenues and that Mountain Bell also would be permitted to capitalize interest on the

$8,442,000 at the overall rate of return of 11.93% per annum in order to be kept whole with respect to its opportunity cost during the pendency of Phase II of the Docket herein.

As indicated above, on December 1, 1982, Mountain Bell filed a "Motion to Supplement Record and to Modify Decision No. C82-1862," wherein it seeks to amend our December 1, 1982 decision in order to permit Mountain Bell to spread on an across-the-board basis an additional $5,911,000 (which Mountain Bell claims is the balance of remaining life depreciation expense related solely to services other than all remaining life depreciation charges associated with terminal equipment).

The Staff and the Colorado Municipal League filed responses to Mountain Bell's December 1, 1982 Motion, as previously indicated in this decision. Basically, the Staff and the Colorado Municipal League argue that Mountain Bell is attempting to supplement the record subsequent to the close of the hearing and that the information with respect to the segregation of remaining life depreciation charges between terminal equipment and other services could have, and should have, been submitted by Mountain Bell during the hearings in this Docket.

Mountain Bell refers, inter alia, to Rule 14 O. of our Rules of Practice and Procedure, which states that "Any time after any matter is taken under advisement before a decision of the Commission . . . the Commission, . . . may, on its own motion or for good cause shown, order that the record be reopened and the matter set for further hearing." It is our opinion that Mountain Bell's December 1, 1982 Motion, accompanied by the affidavit of Monte R. Shriver, is an attempt to reopen the record and to present new evidence, but without benefit of further hearing. Accordingly, Mountain Bell's reliance on Rule 14 O. is misplaced. December 7, 1982 is the final and 210th day of the statutory suspension period. Obviously, it is impossible at this late date to schedule a further hearing, thereby enabling the parties to test the evidence which Mountain Bell proposes to introduce by way of Mr. Shriver's affidavit. Accord-

ingly, Mountain Bell's "Motion to Supplement Record and Modify Decision No. C82-1862" will be denied.

IX

MOTIONS FOR REIMBURSEMENT

In recent years, parties filed motions in various dockets for reimbursement with respect to attorneys and expert witness fees. It is possible that one or more parties herein may file a motion relating to the reimbursement of attorneys and expert witness fees in this Docket. In the order hereafter, we shall set a date by which motions relating to reimbursement shall be filed. Thereafter, the Commission may set the same for hearing. However, in order to avoid any procedural confusion, the Commission states the decision and order issued today should be considered as a final decision subject to the provisions of CRS 1973, 40-6-114 and 40-6-115 notwithstanding retained jurisdiction in regard to motions for reimbursement. In other words, any further proceedings in this Docket with respect to various motions for reimbursement, if any, are to be considered ancilliary procedural matters which do not affect the substance of the decision herein, and, accordingly, do not affect the finality in terms of CRS 1973, 40-6-114 and 40-6-115.

X

CONCLUSIONS

This Docket has been a complex proceeding in which numerous issues have been raised by various parties. To the extent that specific issues have been raised by parties which are not addressed specifically in this Decision, the Commission states and finds that the particular treatment advanced with respect thereto by one or more of the parties does not merit adoption by this Commission in this Docket.

Based upon all of the evidence of record in this proceeding, we conclude that:

1. Existing rates and tariffs of Mountain Bell do not, and will not in the foreseeable future, produce a fair and reasonable rate of return to Mountain Bell.
2. Such rates and tariffs presently in effect are not, in the aggregate, just and reasonable or adequate, and, based upon the test period ending December 31, 1981, the overall revenue deficiency for Mountain Bell is $38,510,000.
3. Mountain Bell should be authorized to file new rates and tariffs that would, on the basis of test year conditions, produce additional revenues of $30,068,000 (i.e., $38,510,000 minus $8,442,000) spread among its ratepayers on an across-the-board basis, and Mountain Bell should be authorized to capitalize interest on $8,442,000 in the manner set forth in the Order to follow.
4. The rates and tariffs, as ordered herein, are just and reasonable.

Phase II of this Docket will be concerned with the appropriate spread-of-the-rates among the various services which Mountain Bell offers to its customers and it is likely that there will be some adjustments, upward and downward, from the across-the-board increases which we are permitting to be placed into effect at the conclusion of Phase I herein. As also indicated above, this Decision and Order with respect to Phase I (involving the revenue requirement of Mountain Bell) shall be considered as a final decision subject to the procedural provisions of CRS 1973, 40-6-114 and 40-6-115 notwithstanding retained jurisdiction with regard to motions for reimbursement in Phase I, and notwithstanding retained jurisdiction with respect to Phase II dealing with the spread-of-the-rates.

An appropriate Order will be entered.

O R D E R

THE COMMISSION ORDERS THAT:

1. The tariff sheets filed by The Mountain States Telephone and Telegraph Company on April 12, 1982, pursuant to its Advice Letter Nos. 1824 and 1825, be, and the same hereby are, permanently suspended.

2. The tariff sheets filed by The Mountain States Telephone and Telegraph Company on April 16, 1982, pursuant to its Advice Letter No. 1827, be, and the same hereby are, permanently suspended.

3. Of the $38,510,000 (plus any capitalized interest cost authorized herein) revenue requirement increase, Mountain States Telephone and Telegraph Company will be authorized to effect a portion thereof in the amount of $30,068,000 by increasing, on an across-the-board basis, its current rates by an appropriate rate interest rider of 5.27%. Said rider shall indicate therein that the same is subject to refund with interest, in whole or in part, as a result of any order or orders issued by this Commission subsequent to the effective date of said rider. Exempted from the requirement of Paragraph 3 herein will be the following services:

Tier A portion of two tier rates (fixed tier) and coin telephone rates.

4. On the $8,442,000 revenue requirement increase which will be deferred by this Commission until Phase II, Mountain States Telephone and Telegraph Company will be authorized to capitalize interest on $8,442,000 at the overall rate of return of 11.93% per annum in the following manner:

Dividing 11.93% by 12 results in .99417% per month. The sum of $8,442,000 times .99417% will produce the dollar amount to be used for each month implementation is delayed from December 8, 1982 until the effective date of the Commission's final Decision and Order in Phase II of this Docket. The $8,442,000 plus any capitalized interest thereon will be charged to the appropriate customers when it is established by the Commission pursuant to cost of service studies in

Phase II to whom these costs properly should be assigned.

5. The "Motion for Order Limiting Rate Relief and Directing Inquiry into Effect of AT&T Divestiture Order" filed by CF&I Steel Corporation on August 27, 1982, be, and the same hereby is, denied.

6. The "Motion to Supplement Record and to Modify Decision No. C82-1862" filed by The Mountain States Telephone and Telegraph Company on December 1, 1982, be, and the same hereby is, denied.

7. Any pending motions which are not otherwise disposed of by the Decision and Order herein be, and the same hereby are, denied.

8. The Mountain States Telephone and Telegraph Company shall comply with the following requirements:

a. It shall file with its next general rate case, as part of its case-in-chief, a detailed study of all advertising expenses. The study must include, but need not be limited to, (1) the costs and benefits of all ads by category as previously ordered by the Commission; (2) the expenses directly associated with each individual ad; and (3) an explanation of how each individual ad was a direct benefit to the Colorado jurisdictional ratepayers.

b. It shall file with its next general rate case, as part of its case-in-chief, a detailed productivity study. Said study shall include an individual input factor analysis and not merely a total factor analysis. The study shall include, but need not be limited to, the following: (1) the number of units of input by type, such as labor (management, non-management) and

capital (central offices, computers) on an average annual basis; (2) the gross output such as revenues, calls switched, main stations, access lines, and trunks; (3) total man hours worked; (4) average hourly compensation by labor type, such as management and non-management; and (5) total plant performance indicators.

The above data shall be submitted for the test year proposed and the prior six years in a consistent format and shall be disaggregated to Colorado jurisdictional rate base.

c. With respect to the existing two Bell System noncontributory pensions and death benefit plans for management or non-management employees, or any future additional or substitute plans, Mountain Bell shall address in its case-in-chief in its next general rate case, the appropriateness of its pension and death benefit expenses for the test year in question. A detailed explanation of all actuarial methods and assumptions as required for financial reporting, income taxes, Employee Retirement Income Security Act of 1974 (ERISA) standards, and regulatory requirements shall be included shall be submitted. In addition, it should provide an analysis that reconciles the investment assets structure, investment policy, risk, and expected rate of return on investments to the actuarially assumed rate of return used in determining

liabilities and test year expenses. The pension plan investment risk and expected return should be reconciled with its request for return on equity using a capital asset pricing model methodology.

e. As part of its next general rate case proceeding, it shall present as part of its case-in-chief, a detailed analysis of its net cash working capital requirements. In addition, a full analysis of all short run and long run sources and uses of funds required by its Colorado intrastate operations should be presented. For the net working capital analysis, a lead-lag study will represent a minimum compliance with this requirement.

f. The requirements set forth in 8.a.-8.e. are not to be construed as limitations upon the generality of evidence to be submitted as part of its direct case in its next general rate case.

g. Commencing with the month ending January 1, 1983, it shall submit to the Commission on a monthly basis within thirty (30) days following the end of the calendar month, a monthly financial report containing an intrastate per book income statement; an intrastate per book rate base; a consolidated Bell System capital structure including composite costs; and the resulting rate of return on rate base and common equity.

h. With respect to the 1982 Form M Annual Report and subsequent annual reports, submitted to the Commission, it shall supplement said reports by including therein full and complete Colorado interstate and intrastate balance sheets as of year end. Said reports also should provide the average of month-end balance sheets for the twelve months of each calendar year.

9. If at any time the Commission enters upon an investigation to review the justness and reasonableness of the rates as set herein, or as may hereafter be set in Phase II of this Docket, or to investigate the justness and reasonableness of the intrastate earnings or the rates of return on rate base or cost of capital, The Mountain States Telephone and Telegraph Company shall, pursuant to the representations made in this Docket, waive its rights under CRS 1973, 40-3-111 and will accept the burden of the proceeding, that is, the burden of going forward and the burden of proof as to the issues herein delineated.

10. The Mountain States Telephone and Telegraph Company, on or before January 5, 1983, shall inform in writing each of its Tier A customers that the Commission, in Phase II of this Docket, will apportion $8,442,000 between competitive and monopoly services as a result of the revenue requirement increase associated with depreciation cost changes. Said notice shall also inform each Tier A customer that said customer may move to intervene in Phase II of this Docket on or before January 20, 1983.

11. Any party herein who intends to file a motion for reimbursement of attorneys fees and/or expert witness fees with respect to this Docket shall do so on or before January 10, 1983. Any such motion filed should set forth in specific detail, by subject matter, the area or areas for which reimbursement is sought, the amount of time and expense associated therewith, and how reimbursement meets the established criteria of the Commission therefor.

12. For purposes of acting upon motions for reimbursement which may be filed pursuant to Ordering Paragraph 2 herein, the Commission shall retain jurisdiction and enter such further orders as may be necessary.

13. This Decision shall be considered a final Decision subject to the procedural provisions of CRS 1973, 40-6-114 and 40-6-115.

14. Unless subsequently modified by further order of the Commission, procedural dates for Phase II of this Docket shall be the same as had been set forth in Appendix A to Decision No. C82-884, dated June 4, 1982.

15. The twenty (20) day time period provided for pursuant to CRS 1973, 40-6-114(1) within which to file an application for rehearing, reargument, or reconsideration shall commence to run on the first day following the mailing or serving by the Commission of the Decision herein.

This Order shall be effective forthwith.

DONE IN OPEN MEETING the 7th day of December, 1982.

(S E A L)

ATTEST: A TRUE COPY

Harry A. Galligan, Jr.
Executive Secretary

THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF COLORADO

EDYTHE S. MILLER

DANIEL E. MUSE

CLARENCE RAYMOND CLARK, III

Commissioners

APPENDIX A
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PHASE I
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E X H I B I T S

Exhibit	Title and Description
A	Prepared Written Testimony of Thomas W. Lindblom
B	Prepared Written Testimony of Irwin Friend
C	Prepared Written Testimony of Bruce B. Wilson
D	Prepared Written Testimony of Monte Shriver
E	Prepared Written Testimony of Thomas L. Clark
F	Prepared Written Testimony of Fred L. Stevenson
G	Prepared Written Testimony of Joseph T. Dwyer
H	Prepared Written Testimony of Jamshed K. Madan
I	Prepared Written Testimony of Michael D. Dirmeier
J	Prepared Written Testimony of Richard J. Koda
K	Prepared Written Testimony of Garrett Y. Fleming
L	Prepared Written Testimony of William A. Steele
M	Prepared Written Testimony of Carl E. Hunt
N	Prepared Written Testimony of Anthony F. Karahalios
O	Prepared Written Testimony of Mark Langsam
P	Prepared Written Testimony of Eric L. Jorgensen
Q	Prepared Written Testimony of Paul F. Levy
R	Prepared Written Testimony of Richard W. LeLash
S	Prepared Written Testimony of Matitayahu Marcus
T	Prepared Written Testimony of Dr. John W. Wilson
U	Prepared Written Testimony of Robert L. Ekland

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EXHIBIT LIST

No.	Description
1	Exhibits of Thomas W. Lindblom
2	Exhibits of Irwin Friend
3	Exhibits of Bruce Wilson
4	Exhibits of Monte Shriver - Schedules and Financial Charts
4 1st Supp.	Additional Pages 59-75 - Exhibit 4, Supplement - App. H
5	Exhibits of Thomas L. Clark
6	Exhibits of Fred L. Stevenson
7	Exhibits of Joseph T. Dwyer
8	Employee Count by Department - 1981 - Colorado
9	Statistical Highlights-1981 from Mountain Bell Annual Report
10	"CPE Engineering Subsidiary"
11	American Bell, Inc. CPE Engineering, etc.
12	Adjusted Net Book Value
13	Response of Mountain Bell to Joint Data Request (Doc. 500)
14	Document No. 501 - Response to Joint Data Request
15	Intrastate Long Distance Messages
16	Colorado -- 1981-1982 Construction
17	Document No. 504 - Response to Joint Data Request
18	Document No. 582 - Budgeted Construction Expenditures
19	Document No. 891 - Response to Joint Data Request
20	Document No. 580 - NTRASTA

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EXHIBIT LIST

No.	Description
21	1981 Mountain Bell Annual Report to Shareholders
22	Document No. 607 "Summary Wage, Pension and SST, Inc."
23	Non-Management Salaries and Wages 12-31-81
24	Document No. 636 - "Productivity Study- Outline of Procedures"
25	Response to CSC Request in I&S 1400
26	Document 858 "Total Factor Productivity"
27	"Mountain Bell-Consolidated Statement of Source of Funds"
28	Document No. 604 - Consolidated Bell System Interest Adjustment
29	Document No. 583 - Response to Joint Data Request 99
30	Document No. 621 - Response to Joint Data Request 147
31	Document No. 622 - Response to Joint Data Request 148
32	Document No. 623 - Response to Joint Data Request 149
33	Document No. 888 - Response to Joint Data Request No. 141
34	Document No. 1134 - Response to Joint Data Request No. 141 (Revision)
35	Document No. 882 - Response to Joint Data Request No. 139
36	Mountain Bell Account 100.2 and Interest Charged Construction (ICC)
37	Document No. 623 - Response to Joint Data Request No. 140
38	Document No. 615 - Response to Joint Data Request No. 145
39	Document No. 613 - Response to Joint Data Request No. 143

EXHIBIT LIST

No.	Description
40	Document No. 869 - Response to Joint Data Request No. 128
41	Document No. 870 - Response to Joint Data Request No. 128 - Annual Directory Revenues
42	Document No. 871 - Directory Rate Increase
43	"Mountain States - Annual Directory Revenue"
44	Document No. 609 - Directory Rate Increase 1981
45	Document No. 639 - Response to Data Request No. 129
46	Document No. 640 - 2 Tier Pricing Tariff
47	Document No. 641 - PBX-Key Totals
48	Document No. 1141 - Response to Joint Data Request No. 115(e) (Additional)
49	Document No. 905 - Remaining Life - CPE
50	Document No. 906 - Summary of Changes in Depreciation Rates
51	Mountain Bell 234 Large PBX
52	Document No. 908 - Remaining Life - Depreciation
53	Document No. 142 - Preliminary Statement
54	Application No. 35033 - To Transfer Certain Assets to American Bell
55	Document No. 1144 - Memorandum - 6-1-81
56	Memorandum of 9-2-81
57	Memorandum of 9-24-81
58	BOCAP Analysis Plan
59	Document No. 1019 - Installation of BIS Systems 4-1-82
60	Document No. 946 - Narration 234 Large PBX
61	Document No. 1161 - Represcription Rate
62	"ELG" "RL"

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EXHIBIT LIST

No.	Description
63	P. 286 of "Public Utility Depreciation Practices"
64	Clark Cross-examination Diagram No. 2
65	Decision CC Docket 79-105
66	Mountain Bell Affiliated Interests
67	Document No. 893 - Response to Joint Data Request No. 172
68	Document No. 646 - License Agreement
69	Letter June 3, 1974 to R. K. Timothy
70	Document No. 893 - Letter April 24, 1979 to Jack A. MacAllister
71	Document No. 910 - Payments Colorado Intrastate
72	Document No. 1015 - Payments Colorado Total State
73	Document No. 670 - Response to Joint Data Request No. 180
74	Document No. 652 - Mtn. Bell Estimated Payments - 1981
75	Document No. 681 - Response to Joint Data Request No. 189
76	Document No. 682 - Response to Joint Data Request No. 190
77	Budget Decision Package
78	Document No. 664 - Response to Joint Data Request No. 169
79	Document No. 678 - Response to Joint Data Request No. 187
80	Document No. 680 - Affiliated Interest Disallowances
81	Document No. 643 - Response to Joint Data Request No. 156
82	Document No. 203 - Colorado 1981 Competitive Study Summary Report

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No.	Description
83	Memorandum to C. Connolly, etc. dated November 9, 1981
84	Stipulated Motion to Dismiss
85	Attachment 1 - Intrastate Operations Test Year 1981, Revenue Deficiency 11 pages.
86	Letter of 10-7-81 from FCC to Colorado PUC and Mountain Bell
87	Value Line
88	Status Report Paine Webber - February 1982
89	Status Report Paine Webber - June 1982
90	Mountain Bell - Utilities Raw Data
91	Earnings - 2 pages
92	Jan. 13, 1982 - Kidder Peabody
93	Value Line - Utility
94	Industrials
95	Industrials - Beta
96	Document No. 1201 - CF&I Data Request No. 6
97	Document No. 563 - Response to CML Request No. 63 - analysts' predictions 1982 dividends
98	Document No. 83 - audit document
99	Status Report Paine Webber - July 1982
100	Clarifying Telephone Calls
101	Response #303
102	Summary of Responses - AT&T
103	Response #055
104	Judge Greene's Opinion and Order
105	Exhibits of Jamshed K. Madan
106	Insert to Testimony of Jamshed K. Madan

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EXHIBIT LIST

No.	Description	
107	Document No. 1243 - Colorado Intrastate - Mountain Bell	
108	Document No. 1244 - Assessment of 8-5-82 - Computer II Planning View	
109	Schedules and Appendices of M. D. Dirmeier	
110	Remaining Life	
111	Divestiture - Rate Base Effects	
112	Exhibits of Richard J. Koda	
113	Case Authorization Packet	
114	Staff Exhibits of Garrett Y. Fleming	
115	Projection Life Table and Life Indications	
116	Letter dated 1-8-82 from AT&T to FCC Audits Division	
117	Diagram #1 (Survivors Curve)	
118	Diagram #2 (Depreciation Curve)	
119	Diagram #3 Equal Life Group	
120	Staff Exhibits of William A. Steele	
121	Deloitte, Haskins & Sells	
122	Staff Recommendation - Expense Levels	(Staff Witness Hunt)
123	License Contract Payments 1962-1981	(Staff Witness Hunt)
124	Bell System Operating Revenues and Main Telephones 1971-1981	(Staff Witness Hunt)
125	Mountain Bell Operating Revenues and Main Telephones 1971-1981	(Staff Witness Hunt)
126	Summary of License Contract Fees	(Staff Witness Hunt)
127	Mountain Bell List of Unauthorized Accounts	
128	Business Information Systems Payments 1971-1981	
129	Mountain Bell Real Operating Expenses	
130	Colorado Interstate BIS Payments Adjusted	

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No.	Description
131	Bell Telephone Labs BIS Recommended to be Disallowed
132	Colorado Intrastate Conduit Billing Adjusted
133	Colorado Intrastate Cost Sharing Adjusted
134	Case Authorizations
135	Mountain Bell - Colorado Intrastate Operations (Staff Witness Karahalios)
136	Mountain Bell - Determination of Productivity Offset (Staff Witness Karahalios)
137	Letter dated 8-25-82 to from AT&T to Robert K. Timothy (Staff Witness Karahalios)
138	Staff Exhibit Productivity Offset Ratio - 1982 (Staff Witness Karahalios)
139	Statement of Operating Earnings 12 Months ending 12-31-81 (Revised) (Staff Witness Karahalios)
140	Karahalios Diagram No. 1
141	Karahalios Diagram No. 2
142	20 Schedules of Mark Langsam, Witness for Dept. of the Army
143	First Data Requests to Dept. of Defense
144	Response of DOD to First Data Request
145	Wall Street Journal, 9-13-82
146	Credit Comment, 9-20-82
147	Staff Exhibit re Mountain Bell Capital Structure and Rate of Return (Staff Witness Jorgensen)
148	Staff Exhibit - AT&T Yields on Common Stock (Staff Witness Jorgensen)
149	Staff Exhibit - Revenue Requirement Increase (Staff Witness Jorgensen)
150	Exhibits of Witness Paul F. Levy

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EXHIBIT LIST

No.	Description
151	15 Schedules of Witness R. W. LeLash
152	Business Conditions Digest (2 pages)
153	Business Conditions Digest - October 1980 (18 pages)
154	LeLash Cross-examination Blackboard Example 10-29-82
155	Exhibit of M. Marcus - 22 schedules
156	Exhibits of Dr. J. W. Wilson (14 pages)
157	Bell Labs License Contract Expenses (J.W. - 2)
158	BIS Costs Billed to Mountain Bell (J.W. - 3)
159	Blackboard Diagram of J.W. Wilson
160	Revised Appendix I to Exhibit 4 (Substitute for Shriver's Original Appendix I)
161	J. Madan's Modified Exhibits as a result of Exhibit 160
162	Carl Hunt's Case Authorization Study Revision
163	Carl Hunt's Exhibit on Technical Areas Regarding % Allocated to Competitive Activity and % Allocated to Other
164	Exhibits of Staff Witness Ekland 3 Schedules
165	Professional Background of Richard Walker
166	Exhibit of Richard Walker (3 pages)
167-171	Exhibits of R. Walker
172	Letter of 3-27-79 from AT&T to IRS
173	Public Service Co. v. FERC 653 F 2d 681 (1981 Decision)
174	IRS Letter Ruling 8239122, June 30, 1982 [Code Sec. 46]

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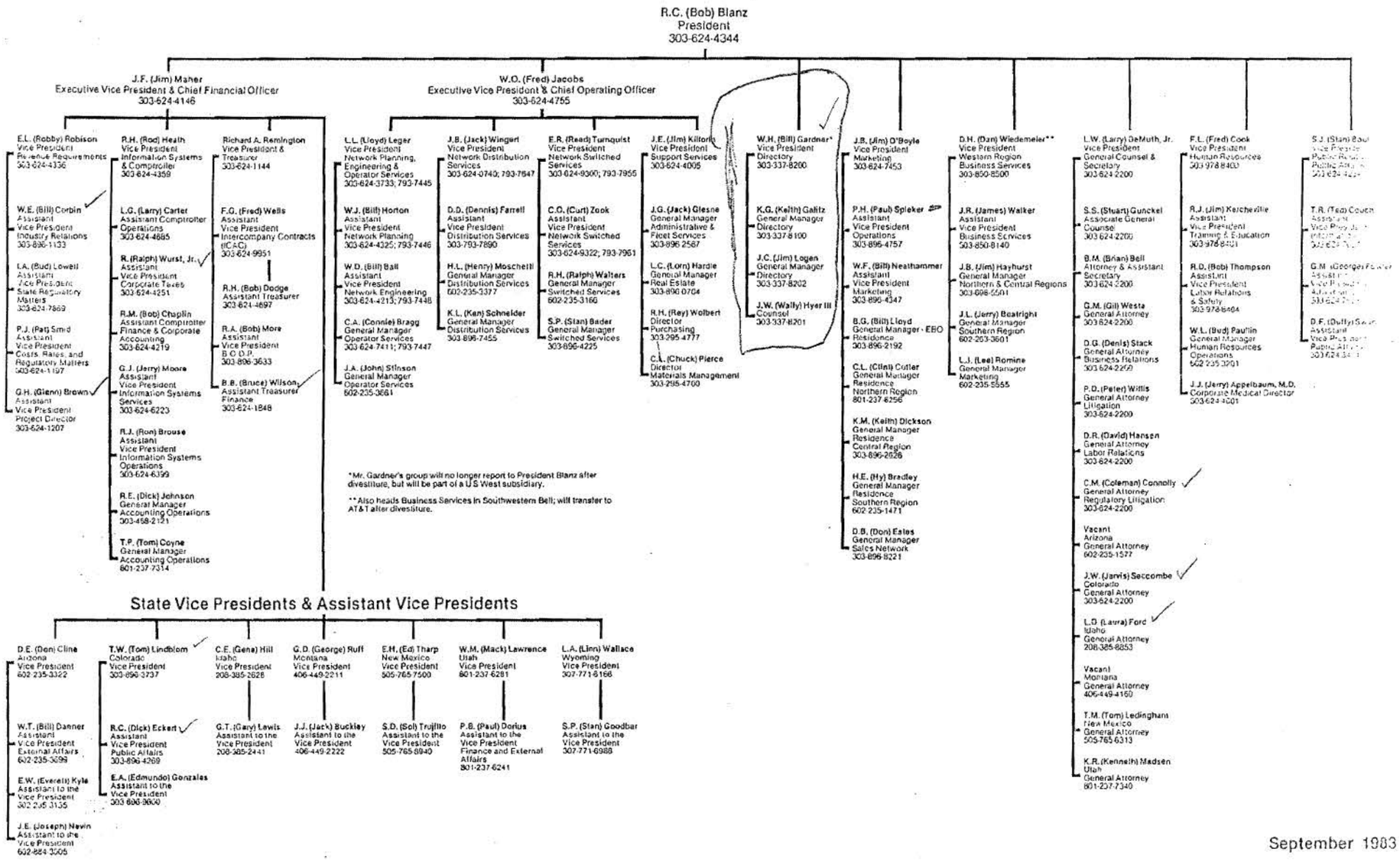
EXHIBIT LIST

No.	Description
175	1981 Allowable Advertising Expense Intrastate
176-179	Exhibits re Advertising Expense
180	Update to Analysts' Earnings and Dividends Forecasts
181	Mountain Bell- Colorado Intrastate Operations Statement of Net Operating Earnings 12 Months ended 12-31-81 (3 pages) (Staff Witness Karahalios)
182	Mountain Bell Colorado Intrastate Staff Net Operating Earnings Summary (5 pages) (Staff Witness Karahalios)

Mountain Bell Organization



*Mr. Gardner's group will no longer report to President Blanz after divestiture, but will be part of a U S West subsidiary.

**Also heads Business Services in Southwestern Bell; will transfer to AT&T after divestiture.

September 1983