BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

In the Matter of	)	
	)	
U S WEST COMMUNICATIONS, INC.'s	)	Docket No. UT-930074
	)	
Petitions Relating to the	)	Docket No. UT-930307
Effective Date for the	)	
Accounting Change to Implement	)	
SFAS 106, Post Retirement	)	
Medical Benefits and a	)	
Ratemaking Adjustment for the	)	
Pension Asset.	)	
--------------------------------	)	
	)	
In the Matter of the Petition of	)	
	)	
U S WEST COMMUNICATIONS, INC.	)	Docket No. UT-931378
	)	
Relating to the Implementation	)	Volume 2
of SFAS 112, Employers'	)	Pages 16 - 122
Accounting for Post Employment	)	
Benefits	)	
--------------------------------	)	

A hearing in the above matter was held on May 16, 1994 at 9:30 a.m., at 1300 South Evergreen Park Drive Southwest, Olympia, Washington, before Administrative Law Judge LISA ANDERL.

The parties were present as follows:

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION STAFF, by STEVEN W. SMITH, Assistant Attorney General, 1400 South Evergreen Park Drive Southwest, Olympia, Washington 98504.

U S WEST COMMUNICATIONS, INC., by EDWARD T. SHAW, Corporate Counsel, 1600 Bell Plaza, Room 3206, P.O. Box 21225, Seattle, Washington 98111.

Cheryl Macdonald, CSR, RPR
Court Reporter

TRACER, by ARTHUR A. BUTLER, Attorney at Law, 1201 Third Avenue, Suite 2850, Seattle, Washington 98101.

MCI COMMUNICATIONS, by BROOKS HARLOW, Attorney at Law, 4400 Two Union Square, 601 Union Street, Seattle, Washington 98101-2352.

I N D E X

P R O C E E D I N G S

(Marked Exhibits T-1 through T-6 and 7 through 24.)

JUDGE ANDERL: Let's be on the record then. This hearing will please come to order. The Washington Utilities and Transportation Commission has set for hearing at this time consolidated docket Nos. UT-930074, UT-930307 and UT-931378. Today's date is May 16, 1994 and we're convened in the Commission's hearing room in Olympia, Washington. My name is Lisa Anderl and I'm the administrative law judge who has been assigned to hear the case today.

We are convened for purposes of cross-examination of all of the witnesses. All of the testimony, both direct and rebuttal, and the staff's and intervenors' testimony has been prefiled. Let's begin by taking appearances at this time beginning with you Mr. Shaw.

MR. SHAW: Thank you. Ed Shaw for petitioner U S WEST Communications, Inc., Post Office Box 21225, Seattle, 98111.

MR. HARLOW: Good morning, Brooks Harlow representing MCI Telecommunications Corporation. My address is 4400 Two Union Square 601 Union Street Seattle, Washington 98101.

MR. BUTLER: Arthur A. Butler appearing on behalf of Tracer. My address is 1201 Third Avenue, Suite 2850, Seattle, Washington 98101.

MR. SMITH: Steven W. Smith, assistant attorney general, South 1400 Evergreen Park Drive Southwest, Olympia, Washington 98504 for the Commission staff.

JUDGE ANDERL: Thank you. Before we went on the record today, we marked for identification the prefiled testimony and exhibits of the company's three witnesses. I'm going to go over those now so that they're identified for the record. Exhibit WB-1 and WB-2, which are Wayne Borkowski's, are Exhibits T-1 and T-2. Exhibit GHW-1 and GHW-2, which are Mr. Wick's testimony, are Exhibits T-3 and T-4. Ms. Wright's MJW-1 is Exhibit T-5. Her rebuttal testimony, MJW-19 is Exhibit T-6. Her exhibits MJW-7 through MJW-18 are marked for identification as Exhibits 7 through 18. MJW 20 through 25 are marked sequentially as Exhibits 19 through 24 for the record.

(Discussion off the record.)

JUDGE ANDERL: Back on the record. Are there any preliminary matters we need to attend to before we begin with the company's first witness.

Hearing none then I will let you go ahead, Mr. Shaw.

MR. SHAW: Thank you.

DIRECT EXAMINATION

BY MR. SHAW:

Q. Mr. Borkowski, would you state your name, address and occupation for the record.

A. My name is Wayne Borkowski. Address 7548 Fair Oak Road, Olympia, Washington, 98503. I'm an adjunct professor at Pacific Lutheran University.

Q. Mr. Borkowski, do you have in front of you what has been marked for identification as Exhibit T-1 and T-2?

A. Yes.

Q. And did you prepare or have prepared under your direction those two exhibits?

A. Yes, I did.

Q. Do you have any changes, corrections that you need to make to those prefiled exhibits at this time?

A. No, I do not.

MR. SHAW: Your Honor, we would move the admission of Exhibits T-1 and T-2 and tender the witness for cross.

JUDGE ANDERL: Any objections to those two exhibits?

Hearing none, they will be admitted as identified. Mr. Smith, did you want to start?

(Admitted Exhibits T-1 and T-2.)

MR. SMITH: Yes, Your Honor.

CROSS-EXAMINATION

BY MR. SMITH:

Q. Good morning, Mr. Borkowski.

A. Morning.

Q. At page 1 of your rebuttal testimony, Exhibit T-2, you challenge staff witness Ms. Pitt's view that financial accounting is essentially investor-oriented. Would you agree, however, that there have been differences between financial accounting and regulatory accounting historically?

A. There are differences, yes.

Q. And FAS 106 does not mandate a particular rate making treatment for a utility's nonpension post-retirement benefits, does it?

A. It does not indicate that rate regulatory prices would do anything differently from other companies under the FASB jurisdiction.

Q. My question was it did not mandate a particular rate making treatment, did it?

A. No, it didn't.

Q. Under accrual accounting, is it generally true that an expense is recognized before it is actually paid?

A. Not necessarily. Some expenses are recognized after they are paid. In the example of acquisition of fixed assets you might have a cash outflow to acquire a building and that might be expensed over a 30- or 40-year period, so the expense comes after the actual cash outlay. In other cases the expense is concurrent with the cash outlay. If you pay salaries for employees, the cash outlay in the incurrence of the expense is exactly the same point in time. Other times expenses are recorded in advance of the cash payment. For example, several expenses which are incurred in a period to help generate current cash revenue might not be paid out in cash until a subsequent period, so we have three different possibilities.

Q. What is the one that is most common?

A. Most common is the incurrence of an expense and the cash outlay within the same period.

Q. Now, this Commission is not required to follow FASB pronouncements for rate making purposes, is it?

MR. SHAW: Objection. Calls for a legal conclusion. The witness has not testified on any legal conclusions.

JUDGE ANDERL: I will sustain that.

Q. Mr. Borkowski, do you know whether U S WEST has changed or modified its estimates of future post retirement benefits costs since 1992?

A. No, I do not.

Q. Turning to the transition benefit obligation amortization period. There's nothing in FAS 106 that would preclude the company from using a 20-year amortization period, is there?

A. Nothing that would preclude them from doing it, no.

Q. Do you know what amortization periods the company has requested in other states?

A. No, I do not.

Q. So you would not know whether that period has always been tied to the average remaining service period of employees, would you?

A. I would not know that. The standard indicated that the TBO should be spread over the average remaining service period of employees, and that would be -- that policy would be consistent with the provisions of the standards.

Q. But again you don't know what the company has requested in other states?

A. No, I do not.

Q. At the bottom of page 4 of T-2 which is your rebuttal testimony and going on to the top of 5, you disagree with Ms. Pitts' positions that ratepayers have previously paid more than they needed into the fund and you indicated that the actual returns on these funds have exceeded the estimates. Do you see that?

A. Yes.

Q. And there you're talking about pension asset petition?

A. Yes. Different issue from the FAS 106, yes.

Q. Right. If the company had known in advance what returns the funds were going to generate it would not have had to collect as much from the ratepayers at the outset. Is that fair to say?

A. It's a little bit hypothetical. I mean, how would anyone know what their investment returns would be over the next 20 or 40 or 60 years.

Q. You're always required to make an estimate?

A. Yes.

Q. But if they had estimated properly -- not properly -- if their estimates had been accurate with what actually happened, they would not have had to have collected so much from the ratepayers at the outset. Is that fair to say?

A. I'm not certain how you can tie this into collecting so much from the ratepayers at the early outset. The actuaries make actuarial evaluations based on historical records and information about the future, and they try to estimate current expenses based on those estimates.

Q. And they also try to estimate returns, do they not?

A. Yes.

Q. And that is one of the assumptions that goes into their projections; is that correct?

A. Yes.

Q. Now, turning to SFAS 112, page 5 of T-2, you indicate that the liabilities associated with those costs considered in FAS 112 are real rather than contingency liabilities. Would you agree that the liability is real but the exact amount of that liability is unknown?

A. The exact amount of that liability can be calculated by looking at the commitments company has made for things like workmen's comp and disability and subjecting that to present value calculations.

Q. All right. That requires estimates, does it not?

A. Some of those numbers are based on actual results. I'm not sure about the specific composition of it, but there is no hypothetical assumption about things that will happen in the future as far as new people becoming disabled, or it's primarily the individuals who are now on disability and there is a scheduled payment there and it's just a matter of determining the present value of those outlays.

Q. But the company cannot know in advance how long a particular disabled employee will be drawing workmen's compensation?

A. That's subject to actuarial estimate.

Q. Right. And there are also assumptions of medical costs, trend rates, are there not?

A. Are you talking about FAS 106 or are you talking about FAS 112?

Q. 112.

A. I don't know what was -- if there are any future medical costs -- assumptions in those calculations, I do not know that.

Q. And to the extent there are estimates involved, the cost involved in FAS 112 could be over estimated; is that fair to say?

A. I would not say that would be fair to say.

My understanding of the amount, I was more talking about the implementation date that it was based on current individuals who might be on disability, current workmen's comp claims which are subject to fairly precise estimation. But I did not review the specific calculations.

Q. Turning to page 6, lines 17 through 18.

MR. SHAW: Of which exhibit?

MR. SMITH: I'm sorry. Exhibit T-2. All these questions will be on rebuttal testimony.

Q. You state there that lower expenses and a higher net income do not benefit the shareholders. Do you see that?

A. Yes.

Q. Would it follow that since shareholders do not benefit from lower expenses that the company would have no incentive to be efficient?

A. Not at all. My point in that statement was to indicate that as far as shareholders their primary interest in being a shareholder is to generate cash flows, generate dividends, hopefully generate a return on their investment and that counting that income may not necessarily translate into cash flows.

Q. So shareholders benefit through dividends and the appreciation in the price of the stock?

A. That is a primary benefit a shareholder would get.

MR. SMITH: Those are all my questions.

JUDGE ANDERL: Thank you, Mr. Smith. Mr. Butler.

MR. BUTLER: No questions.

JUDGE ANDERL: Mr. Harlow.

MR. HARLOW: Thank you.

CROSS-EXAMINATION

BY MR. HARLOW:

Q. Mr. Borkowski, as I understand the theory of applying FAS 106 early the idea is that by paying more now the expenses will be lower later; is that correct?

A. That's correct. It's very similar to any long-term obligation. Say an individual's retirement, you're much better off funding for your retirement in the early years of your working career rather than in the later years and that's the same basic logic here. The sooner you prefund the greater the fund becomes and a larger fund balance translates according to standards into lower future expense.

Q. And I understand you pointed to other companies such as IBM that applied this FAS 106 principle early starting in 1992 because they believed

it would lead to lower expenses later; is that correct?
A. Actually, many companies implemented in 1991 including IBM, GE, Weyerhaeuser, yes.
Q. Was it -- is it your understanding that they did that because they expected that their shareholders would realize lower expenses in future years as a result of the increased expense in the initial year?
A. I think -- I can't speculate what the reasons were. Many companies recognize that this obligation was an obligation of the entity. The FASB encouraged early adoption of the standard and to get more proper financial reporting they decided to adopt earlier.
Q. Let me rephrase. You characterized those decisions as being financially astute, I believe. Do you recall that?
A. Certainly. I think the companies are financially astute.
Q. Why do you think it would be financially astute to implement FAS 106 earlier?
A. To begin the process of reflecting accurate numbers in the financial statements and to begin the process of prefunding the benefits.
Q. And it's your belief that this would result in lower expenses and therefore greater profits for the

shareholders in future years?

A. In the long run, yes.

Q. Do you believe that early implementation of FAS 106 would benefit U S WEST shareholders?

A. Well, I think it would benefit both the shareholders and the ratepayers.

Q. Just asking about the shareholders right now.

A. This is a revenue sharing state as I understand it, so both the ratepayers and shareholders should benefit.

Q. I take it from your assumption that the ratepayers benefit is that they will also under utility accounting result in lower expenses in future years and therefore higher earnings to be shared with the ratepayers.

A. Yes.

Q. Can you tell me when you would expect that those lower expenses would begin to be realized? How many years out?

A. I reviewed the present value calculations. I don't recall when that would happen. Most financial decisions are normally based on estimates of what is going to occur in the future and you normally discount that to the current date, so I don't recall when the turnaround period was off the top of my head.

Q. Do you know if it would be, say, more than five years or more than ten years?

A. I really don't recall. I reviewed those calculations several months ago.

Q. Would you expect it to happen in the first two or three years?

A. I really don't recall.

Q. Going back to your assumption then that the ratepayers benefit under sharing, would it be fair to say that if the company were not regulated under traditional rate base rate of return regulation where sharing dollars were based on traditional rate making accounting principles that there wouldn't necessarily be any benefit flowing to the ratepayers?

MR. SHAW: Object to the form of the question. I think it's vague. As I understood it, if the company were under some sort of regulation not traditional and not the current AFOR. I think that needs to be better defined for the witness to be able to answer the question.

MR. HARLOW: Withdraw the question.

Q. Mr. Borkowski, are you familiar with the proposals that are currently being considered by the Commission in AFOR notice of inquiry proceeding to have the company be regulated under price cap regulation?

A. I'm not familiar with that.

Q. Do you understand how price cap regulation works?

A. No.

Q. Would you be able to state whether there would be any potential benefit to the ratepayers over proving the company's FAS 106 petition under price cap regulation then?

A. Since I am not familiar with the regulation, I don't think I would be able to do that.

MR. HARLOW: That's all the questions I have.

JUDGE ANDERL: Thank you, Mr. Harlow.

Anything on redirect?

MR. SHAW: No.

JUDGE ANDERL: Thank you, Mr. Borkowski. You may step down.

MR. SHAW: Call Mr. Wicks.

Whereupon,

GENE WICKS,

having been first duly sworn, was called as a witness herein and was examined and testified as follows:

DIRECT EXAMINATION

BY MR. SHAW:

Q. Would you state your name, address and occupation for the record, please.

A. Yes. My name is Jean H. Wicks. My address is 121 7th Street, Suite 1200, Denver, Colorado 80202. I work as a consulting actuary for Towers Parrin.

Q. Directing your attention, Mr. Wicks, to what's been marked for identification as T-3 and T-4, your prefiled direct and rebuttal testimony in this case, did you prepare or cause to be prepared under your direction those two exhibits?

A. I did.

Q. Do you have any additions or corrections that you need to make in those exhibits at this time?

A. One correction to my direct testimony on page 1 line 3 it states I am employed to Towers Parrin and it should state I am employed by Towers Parrin.

MR. SHAW: Your Honor, we would move the admission of Exhibits T-3 and T-4 and tender the witness for cross.

JUDGE ANDERL: Thank you. Is there any objection to Exhibits T-3 or T-4?

Hearing none, those will be admitted as identified. Mr. Smith, do you want to go ahead with cross?

(Admitted Exhibits T-3 and T-4.)

MR. SMITH: Yes, thank you.

CROSS-EXAMINATION

BY MR. SMITH:

Q. Mr. Wicks, at page 3 and 4 of your rebuttal testimony, T-4, you state there that you oppose Ms. Pitts' suggestion that the TBO be amortized over 20 years rather than the 17.3 years. And you state that increasing the amortization period past 17.3 years means that future ratepayers who receive maybe no service from these employees will continue to pay for their benefits. Now my question is, is it also true that if the TBO is amortized over 17.3 years then there will be costs paid by ratepayers during that period which relate to services that were rendered to prior ratepayers or ratepayers that received services prior to the adoption of FAS 106?

A. In that regard it would be no different than the current situation with the pay as you go where the rate process is always put those costs on the current ratepayers.

Q. And a substantial portion of the TBO relates to employees that have already performed the service to prior ratepayers; is that correct?

A. That is correct, for whom promises have already been made.

Q. And the amortization of the TBO over 17.3 years would make the annual cost higher than the 20-year amortization period; is that correct?

A. The shorter the period the higher the cost, correct.

Q. In your testimony you indicate that some of the retirees have been retired over 40 years. I wonder just how many retirees the company has that have been retired for over 40 years?

A. There are quite a number. We have retirees who retired in the 1940's, so there are some who have been retired for 50 years. It's a very mature company and very mature retiree group.

Q. Can you tell us how many employees that would be?

A. Not off the top of my head, no, but there are a number who retired in the 40's, 50's, 60's.

Q. In your rebuttal testimony you indicate that Ms. Pitts recommended the disallowance of the charge for the adoption of FAS 112. Is it your understanding that she's recommending the disallowance or she's recommending that the conversion not be made regarding the catch-up entry?

A. My understanding is she recommended the disallowance of FAS 112. Again, I don't understand the difference between the disallowance of the catch-up, which is essentially FAS 112, and the adoption of FAS 112.

Q. If the 9 million is not charged to results of operations by a catch-up entry, the company will still recover these costs as they occur in future years?

A. Not under FAS 112, no, because FAS 112 requires the booking at the time the events occur, and there's a catch-up to take care of that so if you disallow it now you're not on FAS 112, which requires the accounting at the time that the disability occurs. And since disabilities have already occurred that's the one time catch up, so I don't understand how you can disallow the catch up piece which is for current disabilities and still say you're on FAS 112.

Q. But the expense level will continue to be the same in future as it is now?

A. Essentially they're calculated differently but the estimate is the expense level after the catch-up. The cost for the new disabled doesn't seem to be too different than what the current pay as you go is but more coincidental than anything. It's not because the methodology is the same.

Q. Page 6 of T-4, line 25, you state that the liabilities -- again talking about FAS 112 -- the liabilities calculated by the company are only for currently disabled employees and no future occurrence is required before the obligation to pay is established. Are you saying here that since an industrial injury has already occurred there is a current liability to pay medical benefits or time loss or disability to an injured worker?

A. If it's for worker's comp it's an industrial injury, yes. The FAS 112 accounting for the period, once they become injured when someone goes on worker's compensation, the obligation exists.

Q. However, the amount of the medical expenses, time loss and disability payments have to be estimated, do they not?

A. That is correct. They have to be estimated. And there is very set methodology to do that that has been in existence for many, many years. It's an industry that insurance companies readily insure. It's a very, very reasonably estimated liability.

Q. The company must make an estimate of each case and the costs that will potentially be associated with an industrial injury claim?

A. That is correct. And the company does do that.

Q. And if the worker rushed to work sooner than estimated, the amount of time loss paid would be lower than estimated; is that correct?

A. That is correct, and if the worker returns later it will be greater and the average is very close to what we've done for all the workers.

Q. In Exhibit T-3 -- I don't know if you need to refer to it, but it's page 2.

A. Is that my direct?

Q. Yes, direct testimony. You're asked the question, how does U S WEST calculate the appropriate accrual costs for retiring medical and dental benefits, and in your response you provided a description of the method which is used to determine costs associated with the implementation of FAS 106, and that method is based on an actuarial cost methodology. Am I correct about that?

A. That is correct.

Q. And are you familiar with the Actuarial Standards Board?

A. Yes, I am.

Q. Can you tell us what the function of that board is?

A. The function of the Actuarial Standards Board is to set standards for actuaries in implementing accounting and actuarial standards.

Q. And are you familiar with ASB's actuarial guideline No. 3 regarding FAS 106?

A. Yes, I am.

Q. And I have a copy of that form I would like to read to you. I have a copy if you need to refer to it. States in the background section, "The committee recognized that SFAS 106 implies more precision and accuracy than exist in this area of actuarial practice. To the extent that future experience differs from that assumed, actual results will differ from expected results. The combination of the relatively long-term nature of the obligations and the potential for significant, persistent differences between actual and expected results, coupled with the political and economic aspects of the benefits, increases the likelihood that significant variations can occur."

Have you read that statement before?

A. Yes, I have.

MR. SMITH: Those are all my questions.

JUDGE ANDERL: Mr. Butler, do you have any cross for this witness?

MR. BUTLER: No questions.

JUDGE ANDERL: How about you Mr. Harlow.

MR. HARLOW: No questions, Your Honor.

JUDGE ANDERL: I have one question. Mr. Wicks, either of these questions may be something that you need to defer to Ms. Wright.

THE WITNESS: I will happily do that.

JUDGE ANDERL: I think actually -- well, one is probably more particularly geared toward your being able to respond to it. On page 2 of your rebuttal testimony towards the bottom of that page you indicate that a 14 and a half percent return was already earned on the retiree medical trust fund. If FAS 106 is adopted effective January 1, 1992, do you know if the amounts contributed as a result of that would earn that same 14 and a half percent during 1993?

THE WITNESS: My understanding is that when the adoption occurs the company will fund at that point and it will earn those assets. The company has funded FAS 106 for many years and they will allocate those portions to the state of Washington, so this is one of the few opportunities we have of having hindsight as to we can invest once we know what the return is, and the funds did very well in the '93 and the '92 funding will get the credit of that earnings.

JUDGE ANDERL: What I would be interested in seeing if you have the information is your actuarial result of anticipating payment for FAS 112 by each year into the future.

THE WITNESS: I do not have that with me.

JUDGE ANDERL: Do you have it? Did you do that calculation?

THE WITNESS: I'm sure we have at some point, yes. Again, that's why we've estimated it would be very close to what the current situation is from year to year. That's something I think could be provided.

JUDGE ANDERL: Do you recall how far into the future your calculation goes?

THE WITNESS: No, I don't. My firm only does the calculations under 112 for the disability calculations. The worker's comp is performed by another actuarial firm so I only know the disability projections.

JUDGE ANDERL: Mr. Shaw, do you think that information could be provided as a bench request?

MR. SHAW: Certainly, Your Honor.

Do you understand?

THE WITNESS: Yes. Again, I can only do it on the one component, the disability component.

JUDGE ANDERL: I understand. We'll call

that bench request No. 1. Thank you. That's all that I have.

Mr. Shaw, anything on redirect?

MR. SHAW: Yes, Your Honor.

REDIRECT EXAMINATION

BY MR. SHAW:

Q. Mr. Wicks, do you recall Mr. Smith on behalf of the staff reading a somewhat lengthy quote from an actuarial standard of some sort?

A. Yes.

Q. What are the implications for this case of that statement that he read to you?

A. The Accounting Standards Board does make the statement that the FAS 106 needs to be taken very carefully and looked at and in adopting the standard the FASB recognized that calculations are done annually, the results are looked at very carefully each year, and there's a very specific methodology within FAS 106 to true up the difference each year as there's a variance from actual to expected. The standards board is stating that the calculations need to be looked at very carefully, reviewed from that standpoint, and they are. There's specific methodology to true up from year to year and to look at the results and valuation is performed each year and differences from expectations -- actual differences from expectation go through a very specific methodology to reflect that.

MR. SHAW: Thank you. Nothing further.

JUDGE ANDERL: Anything on recross.

MR. SMITH: Just one question.

RECROSS-EXAMINATION

BY MR. SMITH:

Q. Mr. Wicks, on the annual true-ups can you explain how those are performed?

A. Yes. Each year we come through and calculate the liability; for instance, in '93 we calculated what we expect it to be. In 1994 with a year's more experience and changes in the environment, we do a new calculation and if our calculation for 1994 varies from 1993, there is then a mechanism to bring the gains or losses, if they are higher or lower than expected, into account. Medical costs is one area much higher than -- and the stock market. As the returns are different we then bring in the differences into the calculations in preceding years -- succeeding years, not preceding.

Q. Are the true-ups flowed back to the next year or are they spread over the remaining service life of the employees?

A. Much like the transition obligation they are spread over the remaining service life. That's why again the transition obligation is amortized on the same basis. All amortization is set up on remaining future service life.

Q. So the benefits of the true-up aren't received the next year. They're trickled back over the estimated service life of the employees?

A. No. The amortization of a change is, but many of the components are also based on interest costs or expected return. A large portion of it flows back through immediately in the next year.

MR. SMITH: Thank you.

JUDGE ANDERL: Mr. Butler or Mr. Harlow, anything else?

Mr. Shaw, anything else?

Thank you, Mr. Wicks, for your testimony. You may step down.

JUDGE ANDERL: It's a little early but I think I am going to take our morning recess before you call your next witness. Be back in 15 minutes.

(Recess.)

JUDGE ANDERL: Lets be back on the record then.

MR. SHAW: Call Ms. Wright.

Whereupon,

MARGARET WRIGHT,

having been first duly sworn, was called as a witness herein and was examined and testified as follows:

DIRECT EXAMINATION

BY MR. SHAW:

Q. Would you state your name, address and occupation for the record, please.

A. Margaret J. Wright, 1600 7th Avenue, Room 3002, Seattle, Washington 98191, and I'm state finance director for U S WEST Communications.

Q. Ms. Wright, do you have what's been marked for identification as Exhibit T-5 and T-6 and Exhibits 7 through 24 in front of you?

A. Yes, I do.

Q. Did you prepare or cause to be prepared under your direction these exhibits?

A. Yes.

Q. Do you have any additions or corrections you need to make at this time other than the substitute page for Exhibit 22 which has already been done.

A. Yes. On Exhibit T-5 on page 12, line 23 the word VEBA should be changed to pension. And on Exhibit T-8 --

Q. Excuse me, just Exhibit 8?

A. Is it just 8? Okay. It was my MJW-8.

Q. Yes.

A. The word -- there's two line 2s. The word "amortization" should be "expense," so "net present value of reduced expenses for 17 years." In both lines 2s the word should be changed.

Q. Does that complete your corrections?

A. Yes, it does.

MR. SHAW: Your Honor, we would move the admission of Exhibits T-5, T-6 and 7 through 24.

JUDGE ANDERL: Any objection to those exhibits, Mr. Smith?

MR. SMITH: No objection.

JUDGE ANDERL: Any from Mr. Butler or Mr. Harlow?

Hearing none, then those exhibits will be admitted as identified.

(Admitted Exhibits T-5, T-6 and 7 through 24.)

MR. SHAW: Witness is ready for cross, Your Honor.

JUDGE ANDERL: Thank you. Was that just

expense substitute for amortization?

THE WITNESS: Yes. Go ahead.

CROSS-EXAMINATION

BY MR. SMITH:

Q. Ms. Wright, in your testimony you discuss the pension asset and associated deferred taxes. What is the Washington intrastate amount of deferred taxes associated with the closed pension assets for the latest available date?

A. As of 1993 the deferred taxes was 23 million.

Q. And at page 2 of your rebuttal testimony T-6 you indicate that ratepayers will benefit from a 1992 implementation date of FAS 106, and you state there that the ratepayers will give you $10.9 million in sharing but the company will fund the expenses of $25 million, and you go on to say that the ratepayers will benefit in increased sharing to the tune of 2.5 million in 1993 and you indicate this is a 23 percent return, which is better than ratepayers are likely to do elsewhere. This measurement is based on a comparison of what the ratepayers give up in 1992 versus what they gain in 1993; is that right?

A. Right.

Q. And that is based upon how the earlier implementation date will affect sharing; is that correct?

A. Yes. And actually how it will affect the expense level in 1993 that is included in our results of operations which our sharing is based on.

Q. Now, if the Commission approves the three petitions consolidated in this proceeding, there will be no amount available for sharing in 1993. Isn't that true?

A. Correct, but there is agreement between the interested party that if there is not enough sharing available in 1993 it would be applied against 1994 sharing and if there's no sharing available in 1994 it would be used in a rate proceeding following that.

Q. But if there's no amount available for sharing, then the ratepayers will not enjoy the 23 percent return in 1993 using the illustration of measuring their benefits in terms of sharing; is that correct?

A. I would say they benefit by just -- as a single item they're benefitting because their expenses are reduced by the 2.5 million.

Q. In your illustration does the 10.9 million represent the ratepayer's portion calculated on the basis of 1992 sharing bands or 1993 sharing bands?

A. 1992 sharing bands.

Q. And if the 106 petition is approved by the Commission, would the company recalculate the distribution of earnings on the basis of the 1992 sharing band?

A. Yes.

Q. Ms. Wright, in your view, do you anticipate the company will be subject to rate of return regulation in the year 2009?

MR. SHAW: Object, Your Honor. Calls for gross speculation. I don't think anybody has a crystal ball in this room.

JUDGE ANDERL: Response, Mr. Smith.

MR. SMITH: I will withdraw the question.

Q. Let me ask you this. In your direct testimony T-5 at page 7, line 6, you state that "ratepayer will benefit in any future rate proceeding because this change will reduce future revenue requirement." Now that statement is only accurate if the Commission continues under the current sharing or some form of sharing or returns to revenue requirement rate base regulation?

A. Currently the shareholder -- or the ratepayer will benefit in 1993 and 1994. However, if there is an earnings review the benefit of taking the expense in 1992 and funding it will be built into future rates so they will get the benefit at that point in time.

Q. Now, revenue requirement is not considered in price cap regulation, is it?

A. Again, I don't know exactly how price regulation would be determined, but I do believe that the recommendation is that the company's earnings would be reviewed before we got into a price cap or price regulation.

Q. Are you familiar with the Commission staff's recommendation regarding the successor AFOR for U S WEST?

A. Yes, I have read it.

Q. And in that document there is a recommendation that the company be subject to price cap regulation. Are you familiar with that?

A. Yes.

Q. Turning to FAS 112 for a moment. In your direct testimony on page 13 you state that the Commission should approve FAS 112 because it is proper accounting. Prior to the adoption of FAS 112, was pay as you go proper accounting for 112-type benefits?

A. That was what was practiced in the

accounting in most companies.

Q. And pay as you go was a FASB standard at that time?

A. Pay as you go -- I believe that all companies reviewed their -- the liabilities associated with FAS 12 under FAS 5 which is for contingent liability, and if a company determined that there was a significant liability that could be measured and that it was not -- it was probable to occur, they would accrue under the contingent liability FASB rather than the FAS 112.

Q. And pay as you go is used by U S WEST, was it not, prior to the implementation of 112?

A. Yes.

Q. Or the adoption of 112 I should say. Will there be any significant change in the company's ongoing expense levels related to 112-type expenses?

A. Except for the catch-up entry -- and it's not -- I think Mr. Wicks testified that it's not necessarily based on the same criteria but the ongoing expenses should be about the same level.

Q. And does the 9 million catch-up expense of applying 112 reflect any additional claims the company will be required to pay out to its employees in 1993?

A. The catch-up entry is based on the current actuarial assumptions for what our liability for worker's comp and disability plans were in 1993, and those are based on actuarial reports and those are the numbers that we're using for the catch-up entries.

Q. And that's present value of future payments for people who are presently drawing benefits; is that correct?

A. The worker's comp is based on present value; the disability plan is based on net present value.

Q. How does the company intend to reflect the catch up effect in its books and records?

A. We will reflect it as an expense on our books in 1993.

Q. Does the company intend to establish some internally controlled fund for this amount as in the case of the pension fund or post retirement benefits other than pension funds?

A. Worker's comp is usually -- the liability is usually short in duration. Normally you fund something that has a long-term duration such as pension plans and medical benefits. For that reason the company does not plan on funding the catch-up entry for FAS 112.

Q. However, if the company were to fund -- deposit ratepayers, money into the fund for these type of expenses, the earnings from that fund would offset future expenses; is that correct?

A. For the reason that workers comp is only for one to two years, it would be a very insignificant amount on those funds.

Q. And how about the disability programs?

A. The disability plans I'm not exactly sure what the effect would be on those plans.

Q. But you would agree if the money were put aside into a fund that the earnings from that fund would reduce future expenses just as in the case of FAS 106 funding?

A. Yes, if it was for a long term it would. In the short term it would have an insignificant impact.

Q. Now, turning to the pension asset. At page 3 of your rebuttal testimony, line 18, you state that "The company has shown how cash has been given back to ratepayers without a corresponding amount moved from the pension fund. Therefore, the money left in the pension fund belongs to the shareholder and is investor-supplied capital on which they should earn a return." When you say the cash has been given back to the ratepayer, are you referring to the ratepayer's share of the excess earnings under the current incentive regulation?

A. I'm actually talking about several areas.

First of all, there has been more sharing dollars thrown back to the ratepayers because of the pension credit. There has also been reduced rates in previous years because of the effect of the pension credit. And as demonstrated in my Exhibit No. 20, over the last 20 years there have been additional funds put into the pension fund by the company than what was recovered through rates, and I think if you look at my exhibit, I show about 39 million, and not only is that 39 million in excess funds that have been put into the pension fund but also that has had an earnings on the 39 million over time, and I would estimate if you took anywhere from an 8 percent return on that additional funds you would show well over 100 million that was shareholder funds that is sitting in the pension fund.

Q. At least since 1990 you're talking about the ratepayer's share of excess earnings; is that correct?

A. Right.

Q. So since 1990 at least are you saying that since the ratepayers shared in excess earnings they should have to pay a return on these funds?

A. No. I'm saying that because that credit did flow back to the ratepayers and the shareholder or the company was not allowed to take those funds from the pension fund that the company should be allowed to earn on that pension asset. Those funds are still sitting in the pension fund and earning a return that will reduce expenses in the future and it's only fair and equitable that both the shareholder and the ratepayer is treated fairly.

Q. Well, did the company add a corresponding amount to the pension fund equal to the amount of the shareholder's share of excess earnings?

A. No, but the company paid out through sharing funds back to the ratepayers. That is cash that the company no longer has and since the company cannot pull that cash out of the pension fund it sits in the pension fund and continues to earn and to the benefit of future ratepayers.

Q. Isn't what you're saying is that the pension assets are investor-supplied because the company has shared its excess earnings?

A. I'm saying the pension asset was created by the credits. The credits benefited the ratepayer, and if the ratepayer in the future should be allowed the return of those funds that have been left in the pension fund the ratepayer should be allowed -- or the shareholder should be allowed to earn on that pension asset.

Q. Associated with the $10.9 million ratepayer share of excess earnings, there is a shareholder share as well; is that correct?

A. You're referring to what now? OPEB or pension?

Q. FAS 106.

A. FAS 106. Would you repeat the question.

Q. Well, the 10.9 million that the ratepayers would lose in sharing if this is approved to 1-1-92, there is also an associated shareholder's share; is that correct?

A. In 1992 the reduction of $25 million of expense, yes, would both reduce the ratepayer and the shareholder amount of sharing.

Q. So the ratepayer and the shareholder reduction would be $25 million?

A. The $25 million reduces the results of operation in the year 1992 and therefore reduces the total sharing amount by $25 million that both affects the ratepayers and the shareholders.

Q. So all we're really saying here is that if we take the $10.9 million from the ratepayers' sharing and the appropriate amount from the shareholders' piece, we'll put that $25 million in the VEBA trust; is that correct?

A. That is correct.

Q. So actually, the company isn't funding the full $25 million. It's funding $25 million less the $10.9 million the shareholder puts up; is that correct?

A. That is correct.

Q. Now, page 5 of your rebuttal testimony, T-6, you indicate that Ms. Pitts' statement about use of constant work force levels for FAS 106 ignores true-ups and I asked the earlier witness about the true-ups. What is your understanding of the true-ups? Are they flowed back the next year or are they spread over the remaining estimated service lives of the employees?

A. According to Mr. Wicks, we --

Q. I'm interested in your understanding. If you don't know, that's fine.

A. My understanding is you base your accrual on various actuarial assumptions, but each year after the previous year you look at your actuals from the previous year and you true up for actuals, and my understanding is that true-up for your actual results is done immediately.

Q. Still on page 5, line 16, you discuss Ms. Pitts' concern about competition and the effect that might have on the benefits actually received by employees, and you note there that all companies will be required to adopt FAS 106 after December 15, 1992.

The magnitude of post-retirement benefits costs is not going to be the same for every company, though, is it?

A. It depends on the size of the company.

Q. So there will be differences among companies, in other words?

A. Well, just based on the size of the liability, and that's logical. If you have a small company, but in relationship to each individual employee it would be similar.

Q. And also if you had a company that just entered the market that company would not likely have the same magnitude of 106 -- or TBO liability as U S WEST; is that correct?

A. That's correct.

Q. And some companies may not pay any post retirement benefits at all; is that correct?

A. I don't know that to be true.

Q. Page 6, staying with your rebuttal testimony, line 27, you indicate that the staff's opposition to the implementation date of FAS 106 is improper because the settlement agreement would have been meaningless since the staff could choose a date far out in the future. Now, on the other hand U S WEST could have proposed an even earlier implementation date, for example, January 1990; isn't that correct?

A. Yeah, that is correct.

Q. And are you saying that in that case the staff would not have the ability to comment on that implementation date?

A. I was commenting on what has been laid out before me and that is, we were applying for implementation in 1992, and I was commenting in relationship to our request for a 1992 implementation date. I was not commenting in regard to previous years.

Q. When FASB recommended earlier implementation dates, they didn't limit it to 1992, did they?

A. No, but when the FASB was issued it was very difficult, I believe, for companies to go back many years because of when the decision was made.

Q. And FAS 106 has been adopted for rate making purposes in this jurisdiction already; isn't that correct?

A. Beginning with 1993, yes.

Q. Now, page 7 you indicate that it's improper for staff or inappropriate for staff to challenge those 106 promises just because the accounting for such benefits is changing. Is it your understanding that Ms. Pitts challenged -- questions these plans because of the accounting changes rather than the prudency of the expenses?

A. The expenses that we're proposing here have been the expenses in our results of operations for years and years and years. I am making the statement that those expenses have not been challenged in the past and they've been part of our sharing filing, and were not challenged in our 1992 sharing filing so I would assume that the staff did not have any objection to those expense levels.

Q. Can you tell me the last time U S WEST PNB had a rate case that was fully litigated and decided by the Commission rather than settled?

A. I believe it goes back to the early 1980's.

Q. Would you accept subject to check that it goes back prior to the divestiture of AT&T?

A. Yes.

Q. And that would have been the last opportunity staff would have had to challenge the welfare benefit plans, at least in a fully litigated hearing; is that correct?

A. I believe that the staff has always had the opportunity when they are reviewing our filing for sharing to challenge any of our expenses and they were allowed to bring that before the Commission in hearings.

Q. Page 8, beginning at line 14 still on the rebuttal testimony. You indicate that it's imprudent for staff to recommend a 20-year amortization period for the TBO over a 17.3 year period because it will cost the ratepayers $6 million extra, and this is based on the idea that the shorter the recovery period, the lower the amount of carrying charges. Am I correct on that?

A. The $6 million was taken from Ms. Pitts' exhibits. She laid out that $6 million amount as would be the additional amount if it was amortized over 20 years.

Q. But that's based on the idea that the carrying charge would be greater the longer the recovery period?

A. Yes.

Q. And would you agree that the Commission does not have to follow FAS 106 for rate making purposes?

MR. SHAW: Object to the extent it calls for a legal conclusion.

MR. SMITH: I will rephrase the question.

Q. Has the Commission always followed FASB SFAS for rate making purposes?

A. To the best of my knowledge I believe they have.

Q. Okay. If the Commission decided to amortize the TBO over, say, three years, that would produce greater savings to ratepayers than a 17.3 period, would it not?

A. That's correct.

Q. But the annual effect would be greater than a 17.3 year period; is that correct?

A. Yes, and as the FASB has stated, and as the FCC has stated, they said the average service life was a much more reasonable period to amortize the TBO. No one was suggesting a three-year amortization.

Q. Are you familiar with the company's FAS 106 petitions in other states?

A. Actually, I'm not real familiar. I know of the -- of our filing here in Washington. I know of our filing in Idaho, which I have responsibility for, and I am familiar with the FCC filing.

Q. Turning to page 9, line 26, and we're talking about FAS 106 still. You make the statement there that the company has already incorporated a correction for funding for the amount collected in 1988, and this has been reflected in the company's calculations in this proceeding. Would you explain what needed to be corrected and what U S WEST has done to incorporate a correction for funding for the amount collected in 1988?

A. First of all, when we were given approval to implement these expenses for the year 1988 and 1989, there was no provision put in any order or any letter from the Commission that said we had to fund this amount or make a rate base deduction. There's nothing on record that said that. The company did fund at the end of 1989 and we now have gone back to the end of 1988 and allocated funds to fund the Washington portion for both 1988 and 1989.

Q. So during 1988 the company did not contribute an amount equivalent to the amount accrued on the Washington intrastate basis for FAS 106 before 1988?

A. We fund at the end of the year. We are -- we have reflected the funding for the funds collected in 1988 at the end of 1988 and years since 1988.

Q. That originally didn't occur in 1988, if I understand your testimony?

A. There was no obligation to the company to fund it.

Q. Well, it did not occur in 1988?

A. It did not occur but we have sufficient funds to allocate the amount to the Washington ratepayers and we have agreed to fund it for the year

1988 and that's reflected in my numbers.

Q. On FAS 112 at page 11 you state there that the catch-up entry associated with the implementation of 112 is a contingent liability that the company is obligated to pay. And you go on to say that the company has actuarial reports that the company relied upon to determine the company's liability for this catch up amount. Now, the actuarial reports or analyses are necessary because the future costs of these obligations are unknown; is that correct?

A. No, they are known and measurable. The FASB would not have ordered companies to accrue under FAS 12 if these amounts were not known and measurable.

Q. They're known and measurable based on estimates, though; is that correct?

A. But the estimates are based on data that has been readily available for years and years to come up with these amounts.

Q. The company cannot say with precision how much time loss it will pay to each injured worker, can it?

A. No, but based on historical data I think you can come up with very reasonable estimates.

Q. And the company cannot know beforehand the total cost of medical expenses associated with any worker's injury, can it?

A. No, but I think it can use reasonable and accurate estimates.

Q. Page 12, line 22, you state, referring to 112 again, "The occurrences which established the obligation has already taken place; it is not some future event but a known and measurable liability." And what you mean, as I understand you, is that the injury has already occurred; is that correct?

A. That is correct.

Q. But the company cannot know precisely the cost that will be associated with that injury; is that correct?

A. Again, I would like to reiterate, the FASB would have not issued this statement for the companies to accrue for it unless they felt that this amount could be reasonably estimated and recorded.

Q. On the subject of pension assets at page 13 you state that "The average market return on assets for 60 years prior to 1986 was 8.2 percent and the assumptions made by the actuaries for the years 1987 through '92 ranged between 7 and 8.5 percent. Assumptions clearly align with average market return." Do you believe that an average market return for the years 1926 through 1986 is a reasonable basis for estimating potential returns for 1994?

A. I would say that returns have always been based on historical data. If you could forecast absolutely the future I guarantee you I wouldn't be in this business.

Q. Various places in your testimony you indicate that the pension asset has been investor-supplied. Can you point to any place in the record where the company has performed a working capital analysis that has been -- using methodology that has been approved by this Commission?

A. No. There's been no analysis done on that.

Q. Page 16 of your rebuttal testimony, line 20 through 23, you state that "The staff does not want to include the pension asset in the rate base and on the other hand they want to include the benefit of deducting for taxes that were created by this pension asset from the rate base."

Now, earlier I asked you about the intrastate amount of this, the deferred tax item associated with the expense and you told me it was $23 million. Was that as of December 1993?

A. Yes. That's end of period of December 1993.

Q. And that's the balance of that period?

A. Right.

Q. Can you tell me by what Commission order the company was authorized to normalize rather than flow through these deferred taxes?

A. The way that we record our results of operation is we record whatever is greater, flow through or normalization.

Q. You cannot cite me to any Commission order?

A. No.

Q. Is there a specific IRS regulation that you could provide us with that states that the company must normalize the tax timing differences associated with the pension asset?

A. It is -- I can't state the IRS ruling but there is a violation if you don't normalize for tax timing differences. It's a violation to -- I believe to IRS rules and regulation. The normalization versus flow-through is done as a regulatory adjustment. We normalize all taxes on our financial books.

Q. And a portion of the Commission's accounting rules for telecommunications companies -- that's WAC 480-120-031, subsection 3 states in part, "Unless specific exceptions are granted or required, all companies shall keep records for rate making and/or bookkeeping purposes which flow through tax benefits to the extent permitted by federal tax regulations." And

I take it you're familiar with that accounting rule?

A. Yes.

Q. And can you tell me what the balance of the deferred taxes was as of December 30, 1987 associated with the pension asset?

A. I believe we -- 1987?

Q. Yes.

A. I don't have that right at my access but it would be a very small amount because the pension asset just was developed in 1987.

Q. The December '93 balance though was $23 million?

A. Correct.

Q. Now, in the settlement agreement adopted by the Commission in docket U-89-3245 P.M. under item 18D, The certain traditional adjustments among those adjustments is a subitem small H which reads lower of normalization versus flow-through for tax timing differences where federal law does not mandate normalization. End of quotation. Can you tell me if the company has used a flow-through accounting treatment for the tax timing differences associated with the pension assets?

A. No. I believe we use normalization.

Q. Are you able to provide us with the next or the most current level of deferred taxes associated with the pension asset?

A. It was provided -- I believe deferred taxes was provided to the staff through 1992.

Q. I'm sorry, I'm talking about the balance. As of December it was $23 million. Do you have anything more current than that or can you provide us something more current than that?

A. Yeah. I'm sure we can.

Q. Okay.

A. What dates specific date would you like?

Q. The most current you have is what I'm interested in and hopefully we're going to be done tomorrow so if you could provide it by then that would be appreciated.

A. Okay.

Q. I just have a few more questions. In your revised Exhibit 16, which is part of your direct testimony, in the far right-hand corner, right-hand column you show additional sharing due to deferred taxes in the rate base. Does that additional sharing consider the reduction in NOI caused by the deferred tax charges included in operating taxes for the various measurement periods beginning in 1990?

A. The additional sharing to deferred tax is very specific, is just in the rate base itself.

Q. If you could turn to Exhibit 19 which was MJW-20. Do you have that?

A. Yes, I do.

Q. Could you explain that schedule, please.

A. One of the reasons this schedule was prepared was in regard to testimony of Steven Carver who was trying to go back and look at the amount funded by the company into the pension fund versus the rates that were given to us for pension expense. So what I have done here is I have listed the amount funded by the company from 1972 through 1992. I have listed cost of service which is what was given to us through rates in column B and the difference is in column C.

Q. Does the amount in column B differ from the amount of pension expense allocated to Washington intrastate for the same period?

A. It is the total cost of service which includes the expense and the capital piece.

Q. I'm not sure I got my answer. Is the amount in column B different from the intrastate Washington allocation for the same periods?

A. The cost of service in column B is the intrastate expense and capital associated with these expenses.

Q. Would you agree that an historical test period recognizes that there is a percentage relationship established between cost and revenues rather than an absolute dollar relationship?

A. I would say that under regulatory theory that is correct. This, again, was put together on -- to go back to prove what Steven Carver had put in his testimony in regard to comparing the amount funded by the company versus what was recovered through its rates.

Q. In your direct testimony, where you indicate the company will invest $25 million in cash into a voluntary employees' benefit association trust, what portion of that amount is attributable to benefits that were established pursuant to collective bargaining agreements?

A. I do know that about two-thirds of our employees are union employees, but again, I don't have that precise number.

Q. But is some percentage of that $25 million related to benefits that were not collectively bargained then?

A. The history of our company has been that the benefits that are given to our union members are also given to our management employees.

Q. I'm not squabbling about that, but is there some percentage there that does relate to nonunion employees in the 25 million?

A. Well, the 25 million applies to all of our employees and not all of our employees are unionized.

Q. And my understanding is that collectively bargained VEBA trusts have certain tax advantages over VEBAs that are not collectively bargained?

A. I believe that is correct but I'm not an expert on that subject.

Q. Does your Exhibit 8, which calculates the savings ratepayers will realize as a result of the adoption in 1992 instead of 1993, recognize that the earnings on the nonunion VEBAs are taxable?

A. There is limits on what is taxable and what is not. To date the company has been able to -- all amounts funded into the VEBA trust has been tax deductible.

Q. For both union and nonunion employees?

A. That is correct.

Q. Are the earnings on the noncollectively bargained VEBAs tax deductible?

A. The earnings are in the VEBA trust itself. The earnings just would be part of the total amount of the trust fund.

Q. Are they taxable or not? Do you know?

A. I do not believe they're taxable but I would have to -- that would be something I'm not certain of.

Q. On the sharing report by the staff, for the 1992 results, do you believe the staff made a full audit of the company's 1992 results of operation in making its April 1993 report?

A. It is my understanding that the staff had the opportunity to review our results of operation on a monthly basis because it is provided to them in detail on a monthly basis, and I would make the assumption that the results of operations would have been audited.

Q. And do you think the staff can effectively audit a company the size of U S WEST given the reported schedules set forth in the settlement agreement?

A. I believe that the company files -- well, I know the company files monthly reports of our intrastate operations to the Commission staff. They have a full year to review those results of operations. The final report is not filed until April 1, and I believe the staff has 30 days to make their reports but they have ample opportunity to audit the results of operations all year long.

Q. They have 30 days after the final report is in?

A. Final, but they would have received at least 11 months of data previous to that.

Q. And a typical suspended tariff takes 11-month period to fully litigate, does it not?

A. Typically.

Q. And there's substantial discovery and hearings involved in those kinds of cases; is that accurate?

A. Again, I'm not going to speculate on that. I just know that the results of operations are provided to the staff and the staff has the opportunity to file data requests during the whole year and with the company responding to those data requests.

MR. SMITH: That's all I have.

JUDGE ANDERL: Thank you, Mr. Smith. Mr. Butler, how does your estimate look?

MR. BUTLER: Still about an hour. At this point about the same.

JUDGE ANDERL: Let's go ahead.

CROSS-EXAMINATION

BY MR. BUTLER:

Q. Ms. Wright, there was an exchange between you and Mr. Smith earlier that I didn't quite understand. I would like to walk back through it and ask you to explain it for me. If I recall correctly he asked you whether there would be any earnings available for sharing in 1993 if the three petitions at issue in this case are approved and your response was no; is that correct?

A. That is correct.

Q. And then he asked you if there is no sharing in 1993, would there be a ratepayer benefit of approval of these petitions, particularly may have confined it to FAS 106, in 1993. And I believe you answered yes. Was that correct?

A. Yes, because --

Q. And your response was the benefit would be in the form of decreased expenses. Did I understand that correctly?

A. That's correct.

Q. If under the current AFOR there is no money available for sharing in 1993, could you explain to me how there would be a ratepayer benefit from decreased expenses in 1993?

A. Well, assuming if all of these adjustments are made then I would have to state that there wouldn't be sharing for the ratepayer if the whole amount of the sharing amount is reduced.

Q. So do I understand your answer to be that there would be no ratepayer benefit in 1993 if there's no money available for sharing?

A. I'm just trying to think this through because it overlaps into the agreement that these amounts would be applied against 1994 or in future rate proceedings if there was no sharing dollars. I believe that if there is no sharing in 1993, I guess the benefit to the ratepayer is that reduced expenses will be there forever by implementing in 1992 and having the amount put into the pension -- or into the VEBA trust the $25 million earning interest, it will benefit the ratepayer for future rates.

Q. But not in 1993; is that correct?

A. That's correct.

Q. So, in other words, would it be correct to say that for there to be a ratepayer benefit in any particular year there would either have to be money available for sharing so that the amount of the sharing would be affected or any decrease in expenses would have to be reflected in rates; is that correct?

A. That's correct.

Q. At line 10 of your rebuttal testimony, T-6, page 19, you're discussing Mr. Carver's testimony and you characterize some of his analysis as speculation, and I just wanted to explore that subject a little bit.

Would you agree that that is an appropriate characterization of your testimony regarding Mr. Carver's position?

MR. SHAW: Can we have a cite again, Counsel? I am not finding it.

MR. BUTLER: Yes. Page 19, line 10.

A. Page 19, line 10?

Q. Oh, I'm sorry. Line 28. This is not something that we need to dwell over. You characterized his testimony as speculation on this point, and I just wanted to refer you to that as a lead-in for the next series of questions. More specifically, I wanted to discuss your analysis about the financial benefit that you believe that ratepayers will realize if the Commission approves the 1992 implementation of FAS 106. And we've had some discussion about your Exhibit 8. And in that exhibit you present some analysis indicating a range of ratepayer benefits that extends from 12 million to 24 million; is that correct?

A. Yes.

Q. And it is your opinion, if I understand correctly, that the ratepayers will in fact benefit from the early adoption of FAS 106 somewhere in that range?

A. Correct.

Q. With respect to Exhibit 8, just to clarify something for me, you've got a section entitled Ratepayer Benefit Under AFOR Through 1994. There are dollar amounts that appear on line 3 and the range is from 12.3 million to 23.5. Am I correct that when we were discussing earlier the range of 12 to 24 that's simply a rounding up of the figures that are presented on that exhibit?

A. Yes.

Q. And when you refer to AFOR through 1994, does that mean that the company assumed that the existing AFOR plan would continue through 1994 and no longer?

A. Correct.

Q. And you assumed that the form of regulation that would be in place after 1994 was traditional rate base rate of return regulation; is that correct?

A. That's what I used in my analysis.

Q. And so you specifically did not assume that the existing AFOR would continue beyond that date or any form of regulation that involved sharing; is that correct?

A. I had no data to establish that.

Q. And it's your position that in order to

quantify the effect of any benefits under an assumption that AFOR or something like that would continue through 2010, you would need extensive information about anticipated rate base revenues operating expenses, et cetera; is that correct? Is that your position?
A. Under a sharing plan you have to look at what rate bands you're in and what you're sharing so you really have to know levels of expenses to understand that.
Q. At the time you prepared your testimony and you made this assumption that traditional rate of return regulation would be the form of regulation after 1994, did you make that assumption because you actually believed that that would be the form of regulation?
A. That was based on the best information I had to me at that point in time. I don't know what type of regulation we will have in the future.
Q. To your knowledge, was it a widely held opinion within U S WEST that there would be a return to traditional rate of return regulation in 1995?
A. Again, I don't have data to make a -- I don't have data to make an opinion on that.
Q. So you made that assumption just because you didn't know what else to assume. Is that a fair characterization?

A. I made that assumption because currently most of our -- well, in fact our rates are set on that, that we will recover expenses over time through our rates.

Q. To your knowledge, does U S WEST endorse a return toward traditional regulation in 1995?

A. Again, it's going to be the determination of this Commission that will determine what type of regulation we have in the future.

Q. I believe you testified in response to an earlier question that you are familiar with the may 2nd, 1994 letter from the Commission to Mr. Okamoto and the attached staff, the policy staff work proposal for successor AFOR plan for U S WEST?

A. Yes, I am.

MR. BUTLER: I ask that that document be officially noticed, please.

JUDGE ANDERL: Any objection?

MR. SHAW: No. I have no objection.

MR. SMITH: No objection.

JUDGE ANDERL: There being no objection I will for the record take official notice of that document and Mr. Butler is distributing copies now.

Q. If the form of price regulation that is recommended in that report and --

MR. HARLOW: Excuse me, did we want to have an exhibit number assigned to this or is this part of the record?

JUDGE ANDERL: Ordinarily when we take official notice of something we don't give it an exhibit number. Have to keep track of it separately.

Q. Again, if the form of price regulation that's recommended in the policy staff report which was appended to the Commission's letter is adopted, would you agree that there would no longer be, at least for the period of that plan, any direct connection between prices for products and services and cost of service as that concept is used in traditional rate of return regulation other than the way in which that might be reflected in setting of the initial rates?

A. Yes, but in setting the initial rates the savings from a 1992 implementation would be included and would therefore be in the rates over that five-year time period.

Q. And if after the setting of the initial rates there is no further earnings review or sharing between the company's shareholders and the ratepayers, that would be the extent of the supposed ratepayer benefit that would be reflected if your petitions were adopted; is that correct?

MR. SHAW: Objection to the form of the question if it assumes that the price regulation goes on forever. I believe the officially noticed the exhibit specifies a five year --

MR. BUTLER: That was the implicit assumption of the question.

A. Would you repeat the question.

Q. If after such a plan were adopted there were no further earnings review or sharing of earnings above bench marks between ratepayers and shareholders, then the extent of any ratepayer benefit of the adoption of your petitions here -- beyond that reflected in the initial setting of rates there would be no further benefit; is that correct?

A. Since the adoption of FAS 106 in 1992 would establish funds in a VEBA trust, the reduction in rates or expenses to the company would be carried forward into the future. As any company knows, you need to have revenues to cover your expenses and therefore since the company will have reduced expenses in the future, the prices that the company charges will capture those reduced expenses.

Q. Doesn't that response assume that in fact there would be a mechanism by which the company's prices will actually be changed and reflect level of expenses in the traditional rate base rate of return regulation sense?

A. Well, in the initial setting of rates that savings will already be captured.

Q. Beyond the initial setting of rates, however, and if there is no further earnings review, and there is no sharing, the extent of any ratepayer benefit would be limited to that that is reflected in the initial setting of rates; is that correct?

A. I would say that reduced expenses by the company would be reflected in their prices in the future and the customers will benefit from it.

Q. Under the form of regulation that's being proposed in the staff report, isn't it correct that that form of regulation assumes that prices would change according to a formula which would reflect some sort of general inflation index, whether it's a producer price index or consumer price index or some other form of inflation index, and would include a productivity offset factor, but beyond that would not be tied to specific levels of expenses or earnings of the company?

A. I think one of the statements that was made earlier that early -- one of the things why the FASB encouraged early implementation of these expenses is so that the companies could get these costs behind them and fund them and therefore reduce expenses in the future. I think the early implementation in 1992 is beneficial to the customers in the future because it establishes funds in a VEBA trust that will reduce expenses in the future, so there's not an absolute match but there is -- that's why it was encouraged early adoption so you get it behind you and your future expenses would be less.

Q. With respect to a form of regulation in which prices, however, were determined according to application of some formula to an initial price, the kind of adjustment you're talking about wouldn't necessarily take place; is that correct?

A. I would say that with the initial setting of rates that would incorporate this reduction in expense that the ratepayer will get that benefit at that point in time of those reduced rates.

Q. If the time of setting of initial rates predates the time at which you've reached those crossover points in the analysis of -- for lack of a better word -- detriment versus benefit, in fact the benefits would not be picked up, is that correct, if there is no later resetting of rates?

A. The break-even point, I believe in my analysis, using the highest net present value was in 1998. If we set rates in 1995 and these rates are -- incorporate those reductions and expenses over the five-year time period, we would reach the break-even analysis point.

Q. But if you don't then reset rates to reflect the lower level of expenses in the future, that benefit for the ratepayer doesn't materialize. Wouldn't you agree with that?

A. In what year?

Q. If you do not, subsequent to the setting of initial rates, reset rates thereafter to reflect the lower level of expenses, the benefit for the ratepayers would not materialize?

A. Those benefits will already be captured in the resetting of rates. You don't reset them for the benefit. The benefit will already have been established. Our expenses will be lower. Will be lower in 1993, '94, '95 because of the early implementation date.

Q. They will be lower than what they would have been, say, in some future year than if you had started that process in that year. Is that what you're saying?

A. I'm saying the initial setting of rates in 1995 will be lower with early implementation.

Q. I'm going to try to put this in other terms here. Is it correct that the absolute value of benefit by earlier adoption of this proposal will decline over time but that decline in the absolute value will not be reflected in rates under the scheme that we've been discussing as earnings continue to increase?

MR. SHAW: I will object unless this is put into a hypothetical. This is really getting --

MR. BUTLER: That's fine, hypothetical.

I've been advised I should just move on.

MR. SHAW: Good advice.

MR. BUTLER: I hear a consensus.

Q. If I could refer you to page 20 of Exhibit T-6, there you indicate that the company did not anticipate the pension credits to continue but did expect the pension asset to be reduced or eliminated through pension expenses. My question is does the company currently anticipate that the pension credits will continue thereby causing the pension asset to continue to grow for the indefinite future?

A. No, I do not believe the company anticipates that those credits will continue to exist over time.

Q. On page 21 of that rebuttal testimony, you indicate that if the company were to make -- according to this calculation it would most likely show that the pension costs recorded would be greater than the pension costs recovered from ratepayers because of regulatory lag. And from the 1940s through the 1980's pension expenses continued to grow on an annual basis and the company was always playing catch up. When you refer to this calculation in that passage, are you referring to a comparison of pension contributions with pension amounts included in the cost of service?

A. What I was referring to is if you look at the operating expenses on a Washington intrastate basis from 1945 through 1980s, you will see that the operating expenses continue to increase on an annual basis. We did not have rate cases every year so therefore we were always in a catch-up mode to recover the increase in expenses, and there was regulatory lag between when we got rates and when we actually incurred the expense.

Q. Did the company file for annual rate changes in Washington during that period of time?

A. I don't have all that data before me but I know they did not file on an annual basis.

Q. Would you agree that the decision whether or not to file for a rate increase generally lies with the company?

A. It does, but there is also a time period to process a rate case, and I believe that was stated as about 11 months, so you would always be in a catch-up mode.

Q. But it is generally within the discretion of the company whether or not to file. You would agree with that?

A. Yes.

Q. And would you agree, then, that the company's decision not to seek an annual rate increase to cover any increasing pension costs could contribute to any regulatory lag that you're talking about?

A. I would agree, but again, to process a rate case is a very time consuming process and would always put the company in the position that there would be some lag if their expenses were increasing on an annual basis.

Q. Would you agree that utility rates have historically been based on an overall cost of service not an increase in expenses in one particular category?

A. Yes, I agree to that.

Q. And would you also agree that a company's decision whether or not to file for a rate increase would be based at least in part upon an assessment of the overall adequacy of the rates that are being charged at that time?

A. Yes, I agree to that.

Q. And I take it you also agree that it's possible for one element or component of -- that comprises a rate making equation would increase while others could be decreasing?

A. That's correct, but if you look at the expenses in Washington state from the 1940's through the 1980's our total operating expenses were greatly increasing on an annual basis in total.

Q. But again you didn't file for annual rate cases?

A. Yes.

Q. Finally, would you agree that one reason you might not file for a rate increase is if in fact you're generating revenues that are in excess of your authorized rate of return?

A. That is correct.

MR. BUTLER: I think that's all the questions I have. Wait a minute. I'm sorry. I forgot. I lied. I have dual responsibilities.

JUDGE ANDERL: How much do you think you have then?

MR. BUTLER: Maybe 15 minutes or so.

JUDGE ANDERL: Mr. Harlow, what do you think?

MR. HARLOW: Five or less.

JUDGE ANDERL: Let's go ahead and finish up with this witness, then.

Q. I will try to get through this as quickly as I can. Again, referring you to page 21 of your rebuttal testimony. Starting at line 17 you state that the company has gone back to 1972 to perform the calculations similar to that offered by Mr. Carver which shows that the company has funded $39 million more than recovered from ratepayers; is that correct?

A. Yes, but that excludes the earnings on those funds over that 20-year time period and that number would increase from 39 million to over $100 million if you were going to calculate the return on that investment.

Q. And your calculation of that $39 million is what is set forth in Exhibit 19; is that correct?

A. Yes.

Q. And turning to that exhibit, you compare the amount funded in column A with the cost of service amounts in column B to quantify that column C difference and that's what totals the 39.4 million?

A. Right.

Q. Is the amount funded in column A comprised of both expense and capital amounts?

A. Yes, it is.

Q. And are the cost of service amounts in column B also comprised of both expense and capital amounts?

A. Yes.

Q. Are the column B amounts considered to represent the sum of both expense and capital because they represent income statement values which are prior to or gross of the expense credit transferring a portion to capital?

A. I don't understand that statement.

Q. We'll try this. Does the company first charge pension costs directly to expense and then later transfer a portion to the capital accounts by decreasing expense?

A. Yes. There is -- well, there's several things because you've got several years going here. Previous to the implementation of USOA, the whole amount of the expense --

JUDGE ANDERL: Previous to the implementation of --

THE WITNESS: It was the FCC uniform system of accounts.

A. -- we would book our total amount of our expense and then do a contra expense for the capitalized piece. I believe today that we book our pension expense and then it goes through an expense matrix and pieces of it are capitalized and expensed to the appropriate accounts.

Q. When was USOA adopted?

A. 1987.

Q. So is it correct to say that the vast majority of the years included in your study are prior to the adoption of the USOA?

A. Yes.

Q. Are the amounts that you picked up for column B before or after the transfer to capital?

A. That's a total amount of expense and capital.

Q. So it's before, correct?

A. Right, but in any kind of proceeding when we go in you apply both for the recovery of your expense and for the piece that's in your rate base.

Q. One piece is recovered through expense and the other through inclusion in rate base?

A. That is correct.

Q. Are the amounts in column B cost of service unadjusted test year amounts or annualized normalized levels?

A. The column B is the actual expenses recorded on our books. Let me just make sure this is correct. Yes, that's the actual cost of service.

Q. In your response to public counsel data request No. 28, paragraph F -- excuse me, 81. Excuse me, public counsel data request 81, paragraph F, you were asked with regard to each test year cost of service amount what was the basis for the cost of service valuation, e.g., unadjusted test year funding amount, annualized pension expense, updated actuarial study, et cetera, and your response was the basis was the unadjusted test year level; is that correct?

A. I would like to refer to that data request, please. I have that before me now. And which response are you referring to?

Q. Subparagraph F.

A. Okay.

Q. So is it correct, then, that the amounts in column B are unadjusted test year amounts not annualized normalized levels?

A. It would have been the amount that we used for our test period, yes.

Q. Unadjusted, correct?

A. Correct.

Q. Can you tell me why you used test year unadjusted amounts for the cost of service column B amounts?

A. My knowledge is that for that particular expense that for our -- we're normally allowed on a test period basis, not on an adjusted period basis.

Q. In your response to public counsel data request 81, the company provided cause numbers, citation and description for each of the amounts that are listed in column B; is that correct?

A. Right.

Q. And the response included copies of certain pages from each of the identified orders, correct?

A. Right.

Q. Were each of the amounts appearing in column B actually set forth within the text of the order pages that were copied and supplied or were there instances where company provided copies of documents entitled Results of Operations for the test years which support the amounts in column B?

A. I would have to go back and review all of these, but I believe that our rates were set on our results of operation plus any proformas that the company would have set forth and the Commission order would be based on that amount.

Q. The amounts appearing in column B were not always set forth within the text of the order pages that were supplied; is that correct?

A. It was set forth in regard to either accepting a staff recommendation on what the results of operations should be.

Q. Could you turn to the order pages section of your response and specifically to the order page associated with cause No. U-71-5.

A. Okay. What page?

Q. Page 17 of that, please.

A. Okay.

Q. Now, that cause was based on a 1970 test year; is that correct?

A. Yes.

Q. And item 3 on that page near the bottom identifies an uncontested net operating income adjustment in the amount of a negative 564,000; is that correct?

A. Yes, wage increases and fringe benefits, 564.

Q. If an expense adjustment has the effect of decreasing net operating income, would you agree that the adjustment increased expense?

A. If the adjustment -- would you repeat that again?

Q. If an expense adjustment has the effect of decreasing net operating income, would you agree that the adjustment increased expense?

A. Right.

Q. Did you review the actual work papers supporting the calculation of this adjustment which were prepared in the early 1970s?

A. No. I relied on the documents that we had at hand here that established our rates at that point in time.

Q. Do you know for a fact whether or not the reference to fringe benefits included pensions?

A. I've gone back and reviewed our expenses for pensions back to 1945 and our pension expense has increased every year since 1945 through the mid 80s. There was provided staff a documentation in response to a data request.

Q. But with respect to my specific question, do you know for a fact whether or not the reference to fringe benefits included pensions?

A. Based on the data that I have reviewed, our pension expense increased every year since 1945 through the 1980s. We would not be decreasing our pension expense if the pension expense itself was increasing.

Q. So you did review that adjustment, correct?

A. I went back and reviewed our operating expenses from 1945 through 19 -- the mid 1980s, and in our results of operations for the state of Washington on intrastate basis, our pension expense increased every year.

Q. But again, you have not reviewed the specific work papers supporting that adjustment that's indicated under item 3; is that correct?

A. No, but I believe it will be negligent on the part of the company not to put in the appropriate pension expense in a test period in establishing rates.

Q. Does the adjustment, the negative 564,000, increase or decrease expense?

MR. SHAW: Asked and answered, I believe. Object.

A. It says wage increases and fringe benefits 564.

Q. And at the top it says "Effect on net operating income," correct?

JUDGE ANDERL: Mr. Butler, there is an objection and it sounded to me as though you had gotten an answer to that earlier. Is there something that I am missing?

MR. BUTLER: Let me just clarify. What I'm hearing sounds like a contradiction, but maybe I need to clarify.

JUDGE ANDERL: Go ahead.

Q. Are you contending that the adjustment that's reflected in item 3, the negative 564, is increasing expense?

A. Yes.

Q. Okay. Would you turn to page 19 of this same cause and specifically with respect to item 22 that similarly identified as wages and fringe benefits with the net operating income effect of a negative 5,773,000; is that correct?

A. That is correct.

Q. Page 23. Referring to the last sentence of the first full paragraph on that page, would you agree that the Commission adopted almost the full amount of that adjustment?

A. Would you refer me to the --

Q. The first full paragraph on that page, the last sentence. Specifically if you look at the last three lines.

A. Without examining this whole document and reviewing all of the numbers, it's hard for me to determine precisely what this refers to.

Q. And this is your response to our data request asking for support, correct?

A. This is, but you're giving me -- asking me about adjustments that are adjustments for wage and fringe program and I believe that has nothing to do with pension expense.

JUDGE ANDERL: Mr. Butler, I am assuming these aren't your questions and so I am kind of cutting you a bit of slack. Is it possible to ask some of these things subject to check? Will that speed things up a little bit?

MR. BUTLER: Except I gather the purpose of this is to try to find out what she's done with her exhibit.

JUDGE ANDERL: I see. All right. That's fine.

MR. BUTLER: It's not clear to us. I'm sorry for the tortured way this is going but I'm doing the best I can.

JUDGE ANDERL: Go ahead. Perhaps if we break for lunch and come back.

I thought we were going to get through it but maybe it would be best that we take a lunch break and come back. Just for the record you're asking Mr. Manifold's questions just to make that clear. Let's take an hour and be back at 1:15 and we'll finish up.

(Luncheon recess taken at 12:00 noon.)

AFTERNOON SESSION

1:00 p.m.

JUDGE ANDERL: Let's be back on the record after our lunch recess. And we will continue with cross from Mr. Butler.

CROSS-EXAMINATION

BY MR. BUTLER:

Q. Again, we just have a couple of more of these. With respect to your response to public counsel request 81. If you could turn to the ordered pages associated with cause No. U-7540. Specifically at page 14, please.

A. I have that.

Q. At 14 there are a series of adjustments that are listed in terms of net operating income showing movement from actual to proforma, correct?

A. Right.

Q. And under the section titled Proforma Adjustments, there are two adjustments. One is entitled Pension and Benefit Increases and the amount associated with that is negative 1,056,000; is that correct?

A. Correct.

Q. And one right below that is entitled Pension

Increase to 16.9 percent -- accrual rate, and the amount is $203,000; is that correct?

A. Right.

Q. Then below that is a section entitled Late-filed Proforma Adjustments. And there is an adjustment under there entitled Pension Accrual Rate Increase Effective 1-1-76?

A. I see that.

Q. And the amount listed there is a negative $226,000, correct?

A. Uh-huh.

Q. The test year for Cause U-7540 was 1974, correct? If you look at the caption at the top?

A. Yes. It was 1974.

Q. Did you review the work papers underlying any of these pension adjustments?

A. The retention period on most of our work papers goes back about ten years so we did not have all of the work papers associated with these cases, so, no, I did not review all of the work papers.

Q. Did you include any of these pension adjustments in column B?

A. The amounts that I used for cost of service was based on our current results of operation in our test period. This Commission has been -- has used historical test periods and does not use future projected results of operations. Normally, pensions has been only -- normally pension expenses were not adjusted for. They were just what was in our test period. So, no, I did not use any adjustments.

Q. If you could now turn to the order pages for Cause U-7966, specifically page 17.

A. Page 17?

Q. 17, yes. Do you have that?

A. Yes.

Q. About a third of the way down the page, second line there reads, "31 uncontested adjustments." Do you have that?

A. Uh-huh.

Q. The total effect, the total NOI effect of those 31 adjustments is a negative 9,315,000, correct?

A. Correct.

Q. Did you review the work papers supporting each one of those adjustments?

A. No, I did not.

Q. And the test year for that cause was 1979; is that correct?

A. Yes.

MR. BUTLER: That's it. Thank you very much.

JUDGE ANDERL: Mr. Harlow, questions?
MR. HARLOW: Thank you.

CROSS-EXAMINATION

BY MR. HARLOW:
Q. Afternoon, Ms. Wright. I represent MCI Telecommunications Corporation. Are you familiar with the term "a balancing account"?
A. No. I'm not sure what you're referring to.
Q. On cross by Mr. Butler you stated that the breakeven point for ratepayers -- I believe this is just under FAS 106 -- is 1998 which you calculated based on the highest present value. Do you recall that testimony?
A. That was in my Exhibit 8, I believe.
Q. So looking at Exhibit 8, that would be based on a 5 percent discount factor; isn't that correct?
A. No. I was using the 10 percent net present value, I believe, and I was referring to Steven Carver's testimony, and he was using the breakeven analysis in 1998 using the 10 percent net present value.
Q. Does 10 percent refer to the net present value or does that refer to the discount factor?
A. The 10 percent is the discount factor.

Q. That's different from net present value, isn't it?

A. Well, you use a discount factor to get to your net present value and using a 10 percent discount brought us to a net present value because the analysis ratepayer benefit under AFOR through 1994 net present value of -- to ratepayer with a '92 implementation of 12.3 million.

Q. So what you're saying -- did I misunderstand your prior testimony or was your prior testimony mistaken when you said the highest present value? Did you mean the highest discount factor?

A. Yes, I did.

Q. Thank you for clarifying that. Would you agree that shareholders will definitely benefit with the earlier implementation of FAS 106, U S WEST shareholders?

A. Yes, it is my analysis that they will benefit from the earlier implementation because of the earlier funding of 25 million in 1992.

Q. Let me pose a hypothetical of a ratepayer who is currently in U S WEST territory but shortly before implementation of FAS 106 moves into GTE territory. Would you agree that that ratepayer would not benefit by the earlier implementation of FAS 106?

A. I would say to take that hypothetical example is very simplistic because we have ratepayers coming and going every day.

Q. I understand it's simplistic but if you can just answer the question based on the hypothetical, please. Would you agree that ratepayer wouldn't benefit?

A. Benefit specifically from the implementation at U S WEST C? They could benefit in GTE territory if GTE had early adoption.

Q. But assuming that all other things remained equal at GTE that ratepayer would not benefit from the earlier implementation of FAS 106; is that correct?

A. If you're purely looking at OPEB expenses, yes.

Q. Supposing we have a hypothetical customer who switches to Electric Lightwave or Digital Direct for their service before their breakeven point, would you agree that those hypothetical customers would not benefit from the early implementation of FAS 106?

A. Based on previous questions presented to me they may benefit because it was stated that these new up and coming companies have very little past TBO amortization, so therefore their expenses will be less and hopefully reflected in the prices, so hopefully the prices that these ratepayers will be paying will be less.

Q. That sounds like a lot of hopefullies. Would it be fair to say that there's no reason to believe that there's any direct connection between the rates charged by Electric Lightwave and DDS and other potential competitors of U S WEST and how soon U S WEST implements FAS 106?

A. I feel that U S WEST should be allowed to implement its accounting changes consistent with the outside financial community and potential competitors, so I think it's critical that we're allowed to implement FAS 106 effective in 1992.

Q. Did you understand my question?

A. Would you repeat it?

Q. All right. The question was, is it fair to say there's no direct connection between the rates that ELI, DDS and other potential competitors of U S WEST charges and how soon U S WEST implements FAS 106?

A. If you're referring to one customer, yes.

Q. I'm referring to the rates charged by the competitors.

A. In your hypothetical, you were talking about one ratepayer moving to another company.

Q. Right. I'm trying to do a follow-up because you indicated -- you gave a qualified answer that said hopefully this, hopefully that and hopefully they will benefit even if they move to ELI/DDS, but my specific question now is, is there any reason to assume that the rates of ELI/DDS and potential competitors of U S WEST had set their rates based on how soon U S WEST implements FAS 106?

A. No.

Q. So getting back to the initial question, then, do you have any reason other than speculation to believe that the hypothetical customers who switched to ELI or DDS before the breakeven date, be it 1988 or whatever, will benefit from the early implementation of FAS 106?

A. They may not benefit from the early adoption of implementation but they may benefit from lower prices in a competitive marketplace.

Q. You're saying that U S WEST may lower its prices in the future that therefore ELI and DDS may respond. Is that the basis of your answer?

A. Could be.

Q. That lowering of rates by U S WEST in your answer would be as a response to a competitive situation, would it not, rather than a result of accounting and rate base, rate of return regulation?

A. I believe companies set their prices both to recover their expenses and to compete in the marketplace and you won't be in business very long if you can't recover your costs.

Q. Let's talk about what would happen if U S WEST becomes a competitive company before the breakeven point, if you will. How will the rates for U S WEST's services be set at that point in time?

A. My analysis was based on what is currently known, and that is we will have sharing from 1992 and that the type of regulation that will be there in the future is not known and measurable.

Q. Well, then, based on that answer, would it be fair to say that if the assumptions underlying how U S WEST rates are regulated and set change that that would mean that your analysis does not take those into account?

A. My analysis assumes that it would be traditional rate of return regulation after the sharing plan ended in 1994.

Q. Would you acknowledge that there are substantial possibilities that those assumptions as to how U S WEST would be regulated may change before the breakeven point is reached?

A. I don't know that.

Q. Would you acknowledge that's a substantial possibility.

A. I'm not going to speculate on the future. I don't have the knowledge to speculate on the future.

Q. I'm not asking you to speculate. I'm just asking whether or not you would agree that that is a possibility?

A. Anything is a possibility, whether it's remote or probable is another question.

Q. Having in mind that possibility, having in mind my prior hypotheticals about the customer moving to GTE territory or switching to obtaining service from a competitor, would you agree that if those things occurred there would be the possibility that ratepayers might not benefit but nevertheless the shareholders would still benefit from this early implementation -- of FAS 106?

A. Based on my analysis we're showing that there would be increased expenses in 1992 which affected both the ratepayer and the shareholder and the company is willing to put 25 million and fund that whole expense even though the sharing amount is only 10.9 million, I think that's a great benefit to both the ratepayer and the shareholder.

Q. Well, I understand that. Let me try and rephrase the question. Perhaps you don't understand it. Basically what I'm asking is, isn't it true that it's possible that the shareholders can benefit and the ratepayers might not given certain uncertainties of the regulatory future?

A. Again, based on my analysis I show that there will be benefit to the ratepayers in the future and that's the best of my knowledge today.

Q. Well, let's -- since we can't seem to get an answer to my specific question, lets again go back to the very simple hypothetical of the customer that moves from the GTE -- excuse me -- moves from U S WEST territory to GTE territory before the break even point. Do you recall that one?

MR. SHAW: Your Honor, this has been asked and answered and counsel is not getting the answers he wants, but the witness has still answered the question. It's possible that the ratepayer may die and win the lotto and doesn't care. Anything is possible.

JUDGE ANDERL: I think he's getting answers but I don't actually think he's been getting answers to the questions he's been asking and I am going to let him try other avenues.

MR. HARLOW: Thank you. If we can get the answers we will be done.

Q. The question is, going back to the original hypothetical I posed, which is the customer moves to GTE territory and therefore doesn't get benefit, my question is simply, even though the ratepayer isn't getting the benefit in that hypothetical, the shareholders still get that benefit; isn't that right?

A. They get the benefit of the 10.9 million in reduced sharing in 1990.

Q. So the answer is yes?

A. For the one ratepayer. We're talking about over 2 million subscribers here. One ratepayer, the amount of that would be so insignificant in the calculation it wouldn't even be noticed.

Q. I understand. I'm trying to make a broader point and the broader point is that even though ratepayers may or may not benefit, the shareholder will always benefit; isn't that correct?

A. I think the shareholder doesn't completely benefit here because the shareholder is willing to fund $25 million and they're only allowed to reduce sharing by 10.9 million. That is, you know -- that's a large portion of that coming out of the shareholders' money versus the ratepayers' contribution, so I think in essence the shareholder is also giving for the implementation in 1992. So I think there's a balance there between the ratepayer and the shareholder.

Q. I understand the point you're trying to make which goes far beyond my question, but the question is, simply, are the benefits for the shareholder more certain than they are for the ratepayer because of the possible changes in the regulatory environment?

MR. SHAW: Your Honor, I will object to the form of the question. It's unfair and misleading. Counsel is comparing the benefit of all shareholders to the benefit of one hypothetical ratepayer who may or may not be around long enough. To be fair, the question would have to compare the benefit to one shareholder who may die or sell his stock before that shareholder gets the benefit, so the question is improper.

JUDGE ANDERL: Well, I think the question is phrased the way Mr. Harlow wants it to be phrased. I don't think it needs to be balanced the way you suggested in order to be a fair question, and I don't think that it's going to elicit a misleading answer given that we have the context of the specific question the way it's been asked, so I am going to allow it.

Q. Do you recall the question?

A. No, would you please repeat it, I'm not sure if I can.

MR. HARLOW: I'm not sure I can repeat it. Have the reporter read it back.

(Record read as requested.)

A. I would say that the benefits to the shareholder are no more certain than to the ratepayer. Depending on whether we can recover costs in the future, there is a large TBO amortization that goes out 17.3 years and whether we are -- the shareholder is ever going to recover those expenses is unknown. So there's all kinds of unknowns on both the shareholders and the ratepayers from the ratepayers's standpoint.

MR. HARLOW: Thank you.

JUDGE ANDERL: Is that it?

I have a couple of questions for you, Ms. Wright. Let me start by referring you back to the bench request that I made of Mr. Wicks. Were you in the room when I asked that?

THE WITNESS: Yes.

JUDGE ANDERL: Do you recall the information that he said he could provide?

THE WITNESS: I believe it was actuarial assumptions of the next so many years for the disability plans.

JUDGE ANDERL: Right. And he indicated that for the other elements of 112 somebody else did the calculation. Can you provide me with the calculation, the actuarial assumptions, for the other elements?

THE WITNESS: For the worker's compensation?

JUDGE ANDERL: Yes.

THE WITNESS: Yes. The study was provided to staff and we can provide you with the assumptions that were made in that study.

JUDGE ANDERL: That would also include the years and the dollar amounts into the future?

THE WITNESS: Yeah. I just want to make a clarification. Disability plans are for more than a few years. Most of the worker's compensation is within a one- or two-year time period and is based on just present value and so there will be very few assumptions, if any, made in the worker's compensation study.

JUDGE ANDERL: We're going to call that bench request No. 2, and then I have another one which we will call 3, and that is along the same lines. Could you provide a breakdown of the benefits included in the accrual for SFAS 112 including the amount for each and how the accrual for each was determined?

THE WITNESS: Yeah, I certainly can, but it was very specific in my testimony that it was for worker's compensation and disability plans and those are the only two components of FAS 112 catch-up entry, but I can provide the specific amounts.

JUDGE ANDERL: Thank you. That does it for bench requests. Now let me ask you one or two other things.

Do you recall the questions that Mr. Smith asked you about deferred taxes?

THE WITNESS: Yes.

JUDGE ANDERL: You seemed to indicate in your testimony that you normalized those taxes because you had to under an IRS regulation or ruling. Is that a correct summary of what your testimony was?

THE WITNESS: That for deferred taxes associated with the pension asset we used tax normalization rules.

JUDGE ANDERL: And that you were required to do so by the IRS?

THE WITNESS: That's my understanding.

JUDGE ANDERL: Can either you or counsel provide me with any sort of a citation?

MR. SHAW: We'll certainly look into that and submit it to you.

JUDGE ANDERL: I don't know if you can do it on the record tomorrow, but that will be fine. Otherwise we'll maybe have to make it another bench request.

MR. SHAW: I'm not sure I will be able to do it by tomorrow to get ahold of our tax experts who are back east but we'll try.

JUDGE ANDERL: Ms. Wright, I'm going to have handed to you a page from the Pacific Northwest Bell annual report for 1987 which was filed with the Commission. Page 14. Mr. Lott is going to give you a copy of that. Counsel, anyone want a copy?

Towards the bottom of that page under the note marked with the pound sign in the second paragraph indicates that U S WEST adopted SFAS 1987 effective 1987; isn't that correct?

THE WITNESS: Right.

JUDGE ANDERL: And the method used in SFAS 87 for calculating an accrued pension liability was different than the method to accrue for the funding; is that right?

THE WITNESS: Right.

JUDGE ANDERL: At the time that U S WEST adopted SFAS 87 was there an excess funding over the level required by SFAS 87?

THE WITNESS: Prior to 87?

JUDGE ANDERL: At the time that you adopted SFAS 87.

THE WITNESS: Well if you look at the statement right below that it says "The company's total annual pension expense for '87 was a negative 10.3. The decrease in pension costs for '87 was primarily due to favorable investment experience and increases in assumed actuarial rates of return." So basically that is stating that if we have a negative pension expense that means that we have more funds in the pension fund than was determined to be our liabilities associated with pension -- pension liabilities. Maybe to clarify that and in my testimony is we begin having a pension asset in 1987 and that pension asset has grown since then because of our pension credits.

JUDGE ANDERL: Maybe I should ask, prior to adopting SFAS 87, was there an excess funding?

THE WITNESS: Prior to 1987 that's not how you determined what your liability or your funding was in the pension fund. Not until the implementation in '87 did you make this determination.

JUDGE ANDERL: Also in the second paragraph of that note you state or the company states that "U S WEST and its subsidiaries continue to use the aggregate cost method for funding purposes." Is that also true today?

THE WITNESS: Yes. I believe that's

correct.

JUDGE ANDERL: Now, one other area that I want to cover with you is Exhibit 19, your MJW-20. You may have explained this in response to some questions from Mr. Smith but I'm not sure. The column entitled Ratepayer Benefits, D, is that calculated from any combination of the other three columns?

THE WITNESS: No. The ratepayer benefit is the benefit that flowed to the ratepayer because of our pension credits, and also if you see below it says includes the ratepayer benefit for both the impact due to pension credits and the impact on the rate base due to deferred taxes associated with the pension assets. So it's a combination of both.

JUDGE ANDERL: Yes, I did see that. I just wondered -- since column C is the difference between A and B I wondered if there was some relationship that D had to all of these where -- could I calculate D myself just looking at this exhibit?

THE WITNESS: No. You would have to go back to my previously filed exhibits which detail this.

JUDGE ANDERL: Thank you. Mr. Shaw, anything on redirect?

MR. SHAW: Just one question that might be helpful as to the bench's last question. Directing your attention to column D of Exhibit 19 and the three numbers there, 16.1, 12.2, and 11.3, shown for years respectively '90, '91 and '92, those are the three years of the current sharing plan?

THE WITNESS: That's correct.

MR. SHAW: And those numbers are derived from the sharing to ratepayers in the three years of the plan?

THE WITNESS: Yes.

MR. SHAW: One further question. I believe you stated early this morning that as to the USOA that was implemented in '87, do you need to correct that answer?

THE WITNESS: Yes. It was implemented 1-1-88.

MR. SHAW: No further questions.

JUDGE ANDERL: Anything on recross?

MR. SMITH: No.

JUDGE ANDERL: Mr. Butler?

MR. BUTLER: No.

JUDGE ANDERL: Mr. Harlow?

MR. HARLOW: No.

JUDGE ANDERL: Ms. Wright. Thank you for your testimony. You may step down.

MR. SHAW: That completes the company's

direct and rebuttal.

JUDGE ANDERL: It's been agreed amongst the parties that the remaining two witnesses will go tomorrow. Mr. Shaw, do you have any idea at this point how much cross you think you have?

MR. SHAW: Not precisely. I will have either no cross or limited cross, less than an hour, I would guess.

JUDGE ANDERL: Let's go ahead and reconvene tomorrow at 9:30 then. Apparently there's nothing further and we will reconvene at 9:30 tomorrow and be in recess until then.

(Hearing adjourned at 1:45 p.m.)