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BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION,

Complainant,

vs.

PACIFIC NORTHWEST BELL
TELEPHONE COMPANY, d/b/a
U S WEST COMMUNICATIONS,

Respondent.

.....)

In the Matter of the
Petition of:

PACIFIC NORTHWEST BELL TELEPHONE
COMPANY, d/b/a U S WEST
COMMUNICATIONS FOR AN
ALTERNATIVE FORM OF REGULATION

.....)

DOCKET NO. U-89-2698-F

DOCKET NO. U-89-3245-P

FOURTH SUPPLEMENTAL
ORDER ACCEPTING SETTLEMENT
WITH MODIFICATIONS,
RESOLVING COMPLAINT AND
AUTHORIZING AN ALTERNATIVE
FORM OF REGULATION

PROCEEDINGS: A complaint in Docket No. U-89-2698-F was initiated by the Commission on its own motion for the purpose of investigating the propriety of rates and charges applicable to services provided by Pacific Northwest Bell Telephone Company, d/b/a U S WEST Communications (hereafter referred to as "respondent", "company" or "USWC"). On September 26, 1989, a proposed settlement (agreement) of all disputed issues of the complaint and stipulation to an alternative form of regulation was filed with the concurrence of the respondent, the Office of the Attorney General on behalf of the Commission Staff, and the Public Counsel Section of the Office of the Attorney General.

As provided in the agreement, USWC, on October 4, 1989, filed a petition pursuant to section 1, chapter 101, Laws of 1989, seeking approval of an alternative form of regulation, Docket No. U-89-3245-P. Following the commencement of hearings, the matters were consolidated.

HEARINGS: Hearings were held before Chairman Sharon L. Nelson, Commissioner Richard D. Casad, Commissioner A. J. Pardini, and Administrative Law Judge Elmer E. Canfield

of the Office of Administrative Hearings, pursuant to due and proper notice to all interested parties. The hearings were held on October 23 and 24, in Olympia, November 27 and 28, in Seattle, November 29 in Olympia, and November 30, 1989 in Yakima and Spokane. Four of these sessions were held for the purpose of taking testimony from members of the public.

APPEARANCES: The respondent was represented by Edward T. Shaw and Mark Roellig, Attorneys at Law, Seattle. The staff of the Washington Utilities and Transportation Commission was represented by Donald T. Trotter and Stephen W. Smith, Assistant Attorneys General, Olympia. The public of the State of Washington was represented by Charles F. Adams, Assistant Attorney General, Seattle. Intervenor MCI Telecommunications Corporation (MCI) was represented by Clyde H. MacIver, Attorney at Law, Seattle, and Mark Jason, Attorney at Law, Denver, Colorado. Intervenor Telecommunications Ratepayers Association for Cost-Based and Equitable Rates (TRACER) was represented by Arthur A. Butler, Attorney at Law, Seattle. Intervenor AT&T Communications (AT&T) was represented by Daniel M. Waggoner and Craig A. Gannett, Attorneys at Law, Seattle. Intervenor Department of Defense and other federal executive agencies (DOD) were represented by Cecil O. Simpson, Jr., Attorney at Law, Falls Church, Virginia. Intervenor State of Washington Department of Information Services (DIS) was represented by Robert V. Jensen, Sally G. Brown and Roselyn Marcus, Assistant Attorneys General, Olympia. Intervenor U.S. Sprint Communications Company (U.S. Sprint) was represented by Frederic A. Morris, Attorney at Law, Seattle. Intervenors Washington Independent Telephone Association (WITA) and Contel of the Northwest, Inc. (Contel) were represented by Richard A. Finnigan, Attorney at Law, Tacoma. Telephone Utilities of Washington, Inc., Inter Island Telephone Company and Peninsula Telecommunications, Inc. (PTI Companies) were represented by Calvin K. Simshaw, Attorney at Law, Vancouver. Intervenors consisting of three Seattle residential ratepayers were represented by Deborah Senn, Attorney at Law, Seattle. Intervenor GTE Northwest Incorporated (GTE-NW) was represented by Richard E. Potter and A. Timothy Williamson, Attorneys at Law, Everett. Intervenor United Telephone Company of the Northwest (United) was represented by Tim J. Bonansinga, Attorney at Law, Hood River, Oregon. Intervenor Whidbey Telephone Company (Whidbey) was represented by Robert S. Snyder, Attorney at Law, Seattle.

SUMMARY: This case involves a proposed settlement of an earnings complaint and a petition for an alternative form of regulation presented by the Commission staff, U S WEST Communications, and the Public Counsel Section of the Office of the Attorney General. Because of the importance of the issues presented, the Commission perceived the need to develop

a full public record for Commission review. After receiving the proposal, the Commission allowed all interested parties to intervene and present evidence on the settlement. The Commission also held hearings throughout the state to take public testimony on the proposal. Based upon the extensive record developed in this proceeding, the Commission is issuing this order.

The Commission accepts the settlement of the earnings complaint, with a correction. The settlement will provide an estimated cumulative five-year revenue decrease of \$337.75 million. The 1990 decrease is \$65 million. Over the term of the settlement the decreases in revenue will be distributed by reducing exchange rates and decreasing the number of rate groups; capping the maximum monthly charge for Enhanced 911 service, eliminating suburban mileage charges and making one-party service available throughout USWC service territory; reducing traffic sensitive access charges and carrier common line rates; eliminating remaining Touch-Tone charges; changing the definition of complex business lines; and changing toll call timing methods.

The Commission also accepts the petition for an alternative form of regulation with modifications. The modifications include lowering the earnings level at which sharing of earnings begins from 11.25% to 11.00%; ensuring that "traditional miscellaneous filings" will not be used to defeat the incentives in the plan; and stating a preference that rate restructures be used to return excess earnings. With these modifications, the Commission finds the alternative form of regulation is in the public interest.

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I. PROCEDURAL HISTORY

On February 21, 1989, in Docket No. U-89-2698-F, the Commission, on its own motion, issued a complaint, later amended, against USWC for the purpose of investigating the propriety of rates and charges applicable to the services it provides. The respondent answered the amended complaint. The matter was scheduled for hearing. On September 26, 1989, a proposed settlement of all disputed issues of the complaint and stipulation to an alternative form of regulation was filed with the concurrence of the respondent, the Office of the Attorney General on behalf of the Commission Staff, and the Public Counsel Division of the Office of the Attorney General. Hearings were continued and interested persons were given additional time to review the proposed settlement. After interventions were granted, the parties agreed to the exchange of information by dates certain and cooperatively worked together in this regard; ample and reasonable discovery was provided to all parties of record.

On October 4, 1989, USWC filed a petition pursuant to section 1, chapter 101, Laws of 1989, seeking approval of an alternative form of regulation, Docket No. U-89-3245-P. This proposed alternative form of regulation is related to the proposed settlement in Docket No. U-89-2698-F. Following the commencement of hearings, Docket Nos. U-89-2698-F and U-89-3245-P were consolidated by Commission order dated October 27, 1989. After discovery, all parties were given full opportunity to present testimony and evidence on the proposed settlement of the complaint and the proposed alternative form of regulation.

Pursuant to prior notices, hearings on the proposed settlement as it related to the complaint in Docket No. U-89-2698-F were commenced on October 23, 1989 and hearings on the petition for an alternative form of regulation in Docket No. U-89-3245-P were commenced on October 24, 1989. Hearings in the consolidated matters were conducted as indicated above on November 27, 28, 29, and 30, 1989 in Seattle, Olympia, Yakima and Spokane. Testimony was received from the respondent, the Commission staff and various intervenors. Hearings for the purpose of taking testimony from members of the public were conducted in Seattle on November 27, in Olympia on November 29, and in Yakima and Spokane on November 30, 1989.

Following the hearings, Staff filed a motion to correct the transcript in order to accurately set forth the respective witnesses' testimony at hearing. All parties of record were provided with a copy of the corrections and there were no objections to the motion. The corrections will be accepted.

II. SETTLEMENT AGREEMENT

A. Complaint

On September 26, 1989, a proposed settlement agreement of all disputed issues of the complaint in Docket No. U-89-2698-F and stipulation to an alternative form of regulation, later filed in Docket No. U-89-3245-P, was filed with the concurrence of the respondent, Commission staff and public counsel. The Settlement Agreement is attached to this order as Appendix A and is incorporated herein by this reference. A summary of the settlement agreement was provided in the record and will essentially be set forth below. The settlement of the Commission's complaint provides for a series of rate decreases which the Company estimates will total \$337.75 million over the next five years. The 1990 decrease effect is \$65 million.

B. Alternate Form of Regulation

Applicable Law

During the 1989 session, the Legislature declared that changes in technology and the structure of the telecommunications industry may produce conditions under which traditional rate of return, rate base regulation of telecommunications companies may not in all cases provide the most efficient and effective means of achieving the public policy goals of this state; the Legislature thereupon adopted a new section to Chapter 80.36 RCW to provide for incentive regulation in the telecommunications industry, 1989 Wash. Laws, Ch. 101, Sec. 1. The Commission is to determine the manner and extent of any alternative form of regulation as may in the public interest be appropriate. In evaluating such plans, the Commission is to consider the public policy goals of RCW 80.36.300, which are to:

- (1) Preserve affordable universal telecommunications service;
- (2) Maintain and advance the efficiency and availability of telecommunications service;
- (3) Ensure that customers pay only reasonable charges for telecommunications service;
- (4) Ensure that rates for noncompetitive telecommunications services do not

subsidize the competitive ventures of regulated telecommunications companies;

- (5) Promote diversity in the supply of telecommunications services and products in telecommunications markets throughout the state; and
- (6) Permit flexible regulation of competitive telecommunications companies and services.

Subsection 2 goes on to provide that, in determining the appropriateness of any alternative form of regulation, the Commission is to consider whether it will:

- (a) Reduce regulatory delay and costs;
- (b) Encourage innovation in services;
- (c) Promote efficiency;
- (d) Facilitate the broad dissemination of technological improvements to all classes of ratepayers;
- (e) Enhance the ability of telecommunications companies to respond to competition;
- (f) Ensure that telecommunications companies do not have the opportunity to exercise substantial market power absent effective competition or effective regulatory constraints; and
- (g) Provide fair, just, and reasonable rates for all ratepayers.

The Commission shall review plans for alternative forms of regulation proposed by companies and can approve, modify or reject such plans. Subsection 3 provides that the Commission may approve the plan or modified plan and authorize its implementation, if it finds, after notice and hearing, that the plan or modified plan:

- (a) Is in the public interest;
- (b) Is necessary to respond to such changes in technology and the structure of the intrastate telecommunications industry as are in fact occurring;
- (c) Is better suited to achieving the policy goals set forth in RCW 80.36.300 and this section than the traditional rate of return, rate base regulation;
- (d) Ensures that ratepayers will benefit from any efficiency gains and cost savings arising out of the regulatory change and will afford ratepayers the opportunity to benefit from improvements in productivity due to technological change;
- (e) Will not result in a degradation of the quality or availability of efficient telecommunications services;
- (f) Will produce fair, just, and reasonable rates for telecommunications services; and
- (g) Will not unduly or unreasonably prejudice or disadvantage any particular customer class.

Provision was also made in Subsection 5 for the Commission to waive regulatory requirements under Title 80 RCW. Subsection 6 provides that the Commission may rescind its approval of an alternative form of regulation if it finds that the conditions set forth in Subsection 3 can no longer be satisfied. Provision is also made for the filing of complaints concerning rates charged under an alternative form of regulation.

The USWC Proposal

The proposed alternative form of regulation is a five-year incentive regulation plan that provides for a sharing of excess revenues if the Company earns above an authorized rate of return range, and for a cap on basic exchange rates and the carrier common line charge (CCLC). The five-year period of the agreement runs through December 31, 1994. There is a two-month window starting July 1, 1992 in which the Commission can terminate the agreement. The agreement, as proposed, sets

an authorized rate of return on investment range at 9.25% to 11.25%. Earnings above the range for a calendar year are to be shared as follows: (1) If earnings are due to pass-through items of tax, separations or accounting changes, the excess earnings flow 100% to the ratepayer; (2) Other excess earnings between 11.25% and 11.875% rate of return flow 60% to the ratepayer; (3) Other excess earnings between 11.875% and 12.50% rate of return flow 50% to the ratepayer; and (4) Other excess earnings above 12.50% rate of return flow 40% to the ratepayer. Earnings flowed to the ratepayer would, at the Commission's direction be used for service improvements or rate restructures, or be credited to the depreciation reserve, in which case the company also contributes its share of excess earnings to the reserve, or be returned to the ratepayers in the form of a negative surcharge applied to rates for exchange access lines and the carrier common line charge. As proposed, if the company's earnings fall below 9.25%, the company can file on an expedited basis for recovery of tax, separations, and accounting changes, and other items to bring earnings up to a 9.25% rate of return. The achieved rate of return is to be measured on a booked basis recognizing traditional Commission disallowances. A U S WEST Direct revenue imputation at 12.50% rate of return on investment is to be used for the period of the agreement. The pending U S WEST Direct court case will go forward, but any final outcome would not be implemented before the end of the five-year period. Service reports are required by the Commission during the agreement period.

Rate Cap

Under the agreement, rates for exchange residence, business, and complex lines, and the carrier common line rate are capped as of September 25, 1989. Rates may decrease from the September 25, 1989 level and may be subsequently increased, but not above the cap. Revenue neutral, new service and other miscellaneous tariff filings are permitted.

Exchange Rate Restructure

Under the proposal, Extended Area Service (EAS) increments are eliminated. The number of rate groups is reduced from six to three and the rates are reduced. The 1990 reduction is estimated to be \$24.0 million.

One Party Universal Service

The suburban mileage charge of \$.28 per quarter mile is to be immediately eliminated in all exchanges. One party service will be made available in all locations before the end of the settlement period. The 1990 equivalent revenue effect is a decrease of \$5.5 million.

Enhanced 911 Service in Small Communities

Enhanced 911 service is to be provided under the agreement with a maximum charge of \$.25 per access line. The equivalent revenue reduction 1990 impact is \$360,000.

Carrier Switched Access Charges

Under the agreement, the company will file an immediate \$8.2 million reduction. On March 1, 1990, the company will file an update based on 1989 costs and volumes.

Complex Business Line Definition

The proposal changes the definition of complex line such that systems with less than five lines that include trunk hunting or call forward-busy features are reclassified to flat business lines. The 1990 impact is a revenue reduction of \$12.8 million.

Touch Tone Charges on Business Lines

The Touch Tone charges of \$.50 per month for business and \$1.05 for Complex lines are eliminated. The 1990 revenue reduction is \$2.6 million. There are no Touch Tone charges on residence lines because such charges have previously been eliminated.

Toll Call Timing

The current method of timing minutes after the initial setup minute is to round up to the next higher minute. Under the agreement, the method will be changed to round up to the next higher one-tenth minute. The 1990 impact is a revenue reduction of \$11.2 million.

III. POSITIONS OF THE PARTIES

A. COMMISSION STAFF

The Commission Staff presented testimony and exhibits from Tony M. Cook, Utilities Division Director, and Robert L. C. Damron, Revenue Requirement Specialist 5.

Mr. Cook supported the rate spread and rate design embodied in the proposed settlement agreement. Recognizing that the Commission encourages settlements, Mr. Cook emphasized that the staff does not agree to a settlement just for the sake of agreement, but does so only when the terms and conditions are clearly in the public interest. He testified that

the proposed agreement is in the public interest and recommended that the Commission approve it. He summarized the rate spread issues of the agreement.

Mr. Cook emphasized the two major changes in rate design accomplished by the proposal, i.e., (1) the tariff is simplified by reducing the number of rate groups from six to three and by eliminating the extended area service increments, and (2) the ratio of residence to business rates is reduced. He explained that the changes in rate groups and rate increments establishes a more rational tariff design for basic exchange rates and better balances cost-of-service and value-of-service principles than the current design.

Mr. Damron, the staff revenue requirement witness, presented the results of staff's accounting investigation. He explained the underlying assumptions and adjustments made by the staff in determining that the proposed settlement of the complaint is reasonable from a revenue requirements perspective. Staff used the 12 twelve months ending December 31, 1988 as the historical test period and applied traditional ratemaking concepts accepted by the Commission in prior proceedings. Mr. Damron explained that an assumed authorized return of 10.53%, applied to staff's pro forma analysis in this case, yields excess revenues of \$65 million. A return of 10.53% is the approximate upper end of USWC's present authorized return range.

On cross-examination, Mr. Damron was also questioned regarding the proposed alternative form of regulation. He expressed some reservations about ratepayer benefits under paragraph 14 of the agreement, which provides for the disposition of excess revenues. His primary concern was with the provision for a negative surcharge, which would not be accompanied by a permanent rate reduction. Mr. Damron noted a "circularity" issue i.e., if the company is in a continuing excess earnings posture, the company would, in effect, collect excess revenues from ratepayers, and then return a portion by way of a negative surcharge, only to recollect excess revenues in the next year.

Mr. Cook testified in support of the alternative form of regulation and recommended that the Commission approve the petition. According to Mr. Cook, alternative forms of regulation should be used only if they are better than traditional rate of return regulation. He referred to the Commission's "Open Letter on Incentive Regulation", which listed the advantages of rate of return regulation as "preventing monopoly abuse, ensuring that customers benefit from industry cost reductions, and meeting important social goals such as universal service" and the disadvantages as, "slow, deters

innovation, and promotes over-investment." He went on to explain that traditional regulation is often reactive. As a result, excess earnings may occur and persist for an extended period of time. Therefore, customers may not receive the full benefit of industry cost reductions and the regulated firm has a limited incentive to achieve overall cost reductions. Because regulation usually cannot react quickly, excess earnings end up flowing disproportionately to the shareholders.

Mr. Cook summarized the proposed alternative regulation plan and testified that the proposed plan meets the statutory criteria. In addition, Mr. Cook described a variety of unique ratepayer protections in the plan that meet the objectives of providing fair rates and controlling monopoly power. These ratepayer protections include: restrictions of rate activity during the agreement term; a provision that no mandatory measured service will be proposed; a provision that residence and business exchange rates cannot be raised above today's levels; and a provision that the carrier common line charge could not be increased. Other tariffed rates can be changed, but only in a revenue neutral or miscellaneous filing, subject to the suspension and hearing process. The company could file a request for a non-revenue neutral rate increase if its earnings fall below the bottom of the authorized return range of 9.25%, but it could not seek a return in excess of 9.25%. The re-evaluation period in 1992 was also cited as significant ratepayer protection.

Mr. Cook testified that the proposed incentive plan also meets the guidelines set forth in the Commission's open letter. Concerning "rates for monopoly services", the proposal caps monopoly rates at their existing level, and then incorporates substantial reductions. Although there still may be some controversial items, the plan provides that undisputed amounts of excess revenues can be dealt with expeditiously. No rate banding or detariffing is included in the proposal.

Mr. Cook went on to explain the "rate of return" range and ratepayer sharing bands contained in the proposal noting that the purpose of earnings sharing is to provide the company with productivity incentives and to guarantee ratepayers a fair share of those earnings. Pointing to the delays involved in the traditional regulatory approach, Mr. Cook explained that under the plan, ratepayers are assured of a timely participation in cost reductions. He also explained the provision for 100% ratepayer receipt of excess earnings due to tax, accounting or separations changes. According to Mr. Cook, the range rate of return serves as an additional incentive/protection balancing mechanism, with the incentive being that up to the top of the range the company is permitted to retain the earnings with no ratepayer sharing. An additional

protection is that a failure to achieve productivity cannot be cured by rate increases unless earnings fall below 9.25%. Concerning "service quality", Mr. Cook pointed out that the proposal provides for monthly service indicator reports that will show the Commission if any degradation in service quality occurs. In the "plant modernization" area, Mr. Cook pointed to the elimination of suburban mileage and touch calling charges immediately and that universal one-party availability is to be achieved by the end of the agreement term. Filings for "new services" are permitted subject to all existing procedural requirements.

B. U S WEST

USWC presented testimony and exhibits from Mike Moran, its director of regulatory affairs for the State of Washington. Mr. Moran presented USWC's petition for an alternative form of regulation and recommended Commission approval. He pointed out that for the last several years it has been recognized in the industry that traditional rate base regulation does not work well in today's dynamic telecommunications environment. He explained that it made sense to deal with the subject of an alternative form of regulation during the course of the negotiations with Commission Staff and Public Counsel on the related matter of settling the earnings complaint. Mr. Moran stated that the agreement was very delicately balanced and that all parties agreed not to be bound if the Commission were to disapprove or modify the agreement; he did not see how the agreement could be modified in any significant way without destroying the balance. He described the agreement as a conservative proposal because it does not introduce any new pricing flexibility. He added that no rate banding is sought and that the agreement does not deregulate or contain any formulas that automatically increase rates. To the contrary, it provides for rate caps with no potential adjustments, even for inflation. He also pointed out that the agreement expands formal service quality reporting by USWC and that it retains rate base, rate of return regulatory oversight. He added that USWC is not requesting the Commission to waive any regulatory requirements under Title 80 RCW.

Mr. Moran described various features of the agreement beginning with the cap on basic exchange rates and the carrier common line rate. He added that as part of the settlement of the earnings complaint, the agreement includes reductions to these rates as well as a restructure of the basic exchange rates. He further explained that the agreement allows the Commission to approve a basic rate increase above the cap for customers who subsequently receive the benefits of corresponding Extended Area Service (EAS). No such action is required of

the Commission, but the agreement gives the Commission flexibility to expand EAS and increase rates to the benefited consumer, if it chooses to do so. Concerning permitted filings, Mr. Moran pointed out that tariff filings under the agreement are submitted for Commission approval in the traditional manner. He also explained that adjustments made to the cost derived carrier common line rate will be made to preserve the effect of increases and decreases and the rate cap. Nothing in the agreement changes any Commission requirements regarding USWC's imputation of access charges to its own message toll rates. Mr. Moran also noted that the company cannot file for tariff changes except as provided in paragraph 10 of the agreement. He went on to explain how the proposed sharing formula works.

Mr. Moran testified that the proposed plan reduces regulatory delay and costs so that traditional, time consuming rate cases are avoided over the next few years. He estimated that to fully litigate the earnings complaint would cost the company, the Commission and intervenors (and ultimately ratepayers) several hundreds of thousands of dollars. More importantly, regulatory delays are eliminated, i.e., approval of the agreement eliminates any further delay of the proposed \$65 million rate reduction. Additional revenues earned by the company above a range rate of return are promptly shared with the ratepayers without further extensive proceedings.

Mr. Moran stated that the proposal promotes efficiency in a number of ways. The bottom of the range encourages the company to do everything possible to not go to the bottom of the range. He pointed out that the more positive part of the motivation for efficiency comes from the formula for sharing the benefits of the company's efficiency and marketing innovation in that real incentive for efficiency comes from the company being able to keep a portion of the fruits of its work to cut costs, invest wisely, and manage and market better. The slightly larger share of revenue at higher levels of earnings will cause USWC to work hard for efficiencies no matter how high the earnings produced. An earnings cap at some point over which 100% is to go to ratepayers was viewed as a disincentive by Mr. Moran.

Mr. Moran explained that the proposed plan facilitates the broad dissemination of technological improvements to all classes of ratepayers. In smaller communities, the proposal facilitates the deployment of Enhanced 911, a service they might otherwise not be able to afford under current funding levels. Also noted was the proposal's recognition that the benefits of Touch Tone service and hunting on multiple business lines should be available to all without artificial price barriers. He further explained that the incentives in the plan will induce the company to make cost cutting, service

improving, technological investments available as soon as reasonably possible. The agreement also provides that the Commission can direct the use of any ratepayer share of excess revenues to special service improvement projects.

Mr. Moran testified that the proposal provides for fair, just, and reasonable rates. In this regard, he pointed to the rate spread rate design and rate reductions, the rate cap on all exchange access and carrier common line rates, and the negative surcharge provision. As to the matter of USWC having an opportunity to exercise market power, Mr. Moran explained that nothing in the agreement gives the company any more market power than it currently has and that no Commission oversight or statutory requirements are waived in this area. He added that nothing in the proposal gives the company any pricing flexibility that it does not already have and, further, that nothing in the agreement waives any of the non-discrimination requirements found in existing statutes and Commission rules.

C. PUBLIC COUNSEL

Public Counsel, in its brief, argued that the agreement was in the public interest and urged the Commission's acceptance. Public Counsel did not offer testimony, but did cross-examine witnesses at the hearings.

Public Counsel supported the \$65 million rate reduction and the proposed rate design as being reasonable and appropriate. The reduction in local exchange rates, the reduction of rate groups from six to three, the reduction in the business/residence ratio, and the elimination of existing EAS additives were all cited as being in the public interest. The elimination of current mileage charges was noted to be a benefit to both business and residential customers. The change in complex business line definition was characterized as being not only appropriate, but long overdue. Universal support was also cited for the elimination of the remaining Touch Tone charges.

Public Counsel described the incentive regulation portion of the settlement as a conservative step which is still based upon rate base rate of return regulation. Although not all regulatory proceedings will end, there will be a reduced need for major general rate cases for five years. While highlighting the provision for reopening by the parties after three years, Public Counsel noted that the Commission and intervenors are free to file a complaint at any time. Public Counsel supported the incentives contained in the plan and the proposed rate of return range and sharing bands. Public Counsel disagreed with the intervenors' suggestions that rate

caps should also be placed upon private line services and that all capped services should be increased equally if rate increases are required. On the subject of rate reductions, Public Counsel pointed out that permanent rate reductions were generally not contemplated by the settlement, except that they could be implemented as part of a rate restructure if done carefully. Public Counsel argued that the EAS concerns of some of the intervenors and the suggested uniform costing methodology should not be addressed by the Commission in this proceeding. Public Counsel did not oppose reasonable changes in the filing dates contained in the agreement, as long as unnecessary delay is avoided.

D. DEPARTMENT OF DEFENSE

The Department of Defense (DOD) presented testimony and evidence from Charles W. King, president of an economic consulting firm.

Mr. King did not evaluate the propriety of the \$65 million rate reduction. As to the distribution of the \$65 million among services and customer classes, he believed it to be, on balance, a favorable package, although containing some objectionable features. One specific point mentioned was that the proposal further reduces residential exchange access rates which he believes are already priced substantially below cost.

Mr. King described incentive regulation proposals as the telephone industry's reaction to the recent reversal in the economics of telephone service from a condition of increasing costs to one of declining costs. He also set forth his views on traditional rate of return regulation. After describing what he considered to be the deficiencies of the settlement agreement proposed by USWC, Mr. King suggested that, at a minimum, the plan should be changed to require that any ratepayer refunds take the form of a permanent rate reduction. He suggested that a far more effective means to convey efficiency incentives would be to require the company to dissect its excess earnings and to identify their causes. He believes USWC should be required to demonstrate the extent and degree that its greater efficiency accounted for the increased rate of return if it wished to keep any of the excess earnings. The company should also have to justify retention of excess earnings due to marketing efforts and the effects of any price reductions by USWC's suppliers should be excluded from sharing. Mr. King believes the company should have the burden of proving it is entitled to keep any excess earnings. Any sharing of earnings should be determined on a case-by-case basis. Mr. King further questioned how ratepayers benefit from increases in depreciation reserves. He suggested that it would take many years before ratepayers would receive a benefit

through depreciation reserve adjustments equivalent to the dollars that they had given up in the year of the company's overearnings.

Mr. King suggested that paragraph 14 be modified so that any revenues to be flowed to ratepayers initially take the form of a negative surcharge applied on an equal proportion basis to all rates and charges and that the parties may then propose alternative distributions before the Commission determines, after hearings, the permanent distribution. He further disagreed with the rate spread for revenue deficiency provisions in paragraph 16 and recommended that the agreement remain silent on the subject of the distribution of rate increases, which are to be later determined as usual in rate increase proceedings.

In its brief, DOD argued that the Commission should accept the rate reductions proposed in the agreement and should further reduce complex business line rates by \$380,000 to reflect a doublecounting identified by TRACER witness, Dr. Zepp. DOD argued for Commission acceptance of the proposed plan with the suggested minimum modifications to paragraphs 14 and 16.

E. MCI

MCI presented testimony from Dr. Nina W. Cornell, an economist who specializes in microeconomic analysis of regulatory and antitrust issues.

In its brief, MCI stated that it has no objection to the proposed settlement of the complaint case against USWC that calls for a rate reduction of \$65 million, but that it does object to the plan for an alternative form of regulation as proposed. It argued that the incentive plan as proposed has little or no ratepayer benefits and was not shown to be in the public interest. MCI further objected to the procedures followed in this case, alleging as flaws: the fact that alleged "secret" negotiations took place among the parties to the agreement (i.e., that MCI and other potential intervenors were not included); the fact that the agreement was submitted to the Commission before other prospective parties had an opportunity to review it and present their positions; the fact that the alternative plan is tied to the complaint settlement; and that this tying together "taints" the alternative form of regulation proceeding.

Dr. Cornell recommended that a uniform cost methodology docket be established to govern future tariff filings under the agreement. She argued that this was necessary in view of the variety of different costing methodologies that

are currently being used. Dr. Cornell felt that some of the terms of the agreement were vague and recommended that the agreement be modified to define what would determine permissible rate increases should there be a change in EAS. She further suggested that the definition of "new service" in the agreement require some functionality not previously provided as opposed to the current definition that allows for bundling and unbundling of existing services to qualify as new services. Lastly, Dr. Cornell recommended that the definition of "traditional miscellaneous filings" be specified and defined to avoid confusion and potential abuse. Dr. Cornell was concerned that the Commission might not adequately scrutinize filings by the company under the agreement. Without specific reference to a provision of the agreement, she testified that the agreement would change the "milieu" and the approach the Commission would take on such filings. Unless its recommendations were adopted, MCI argued that the Commission should reject the incentive regulatory plan.

F. TRACER/DIS

TRACER and the State of Washington Department of Information Services (DIS) presented testimony and evidence from Dr. Thomas M. Zepp, vice president and co-founder of Utility Resources, Inc.

Despite alleged flaws in the rate proposal, Dr. Zepp did not recommend that the proposed rates be changed, except for the errors and omissions which he identified. The first error is the result of double-counting a rate decrease which occurs in the change of the definition of complex service; these customers receive a reduction in basic exchange rates and then receive another rate decrease by being charged the lower price for simple basic exchange service. This error overstates the actual rate decrease from the redefinition of complex service by \$380,000. In order to get the full proposed revenue decrease, rates need to be reduced accordingly. It was suggested that this further reduction of \$380,000 be applied to complex business line rates. The other requested change involves the proposal's failure to consider the revenues from stimulation of sales, which Dr. Zepp suggested should require an additional price reduction to offset additional revenues of \$900,000. Included in Dr. Zepp's criticism was his assertion that the proposed differential between the prices for simple and complex business exchange was too large.

Dr. Zepp criticized the proposed alternative regulation plan alleging: that it fails to correct the "perverse" incentive of rate base, rate of return (RB/ROR) regulation, but instead provides a greater incentive to increase costs in 1990; that it establishes new incentives for USWC to

increase prices for noncompetitive services; that it eliminates the major protection of traditional RB/ROR regulation, the lid on profits, without providing a mechanism to ensure that USWC does not have the opportunity to exercise substantial market power over noncapped, noncompetitive services; that it places the bulk of the risk of revenue shortfalls on business and switched access customers; that it creates a possibility that business and switched access customers will lose the benefits of the proposed rate reductions; and that it creates a new conflict between customer groups.

Dr. Zepp recommended the following changes to the proposed plan: that USWC should be denied the right to increase any prices without reducing others and that the miscellaneous filings provision should be eliminated (only revenue neutral filings should be permitted); that private lines should be included as a capped service in paragraph 9; that prices for noncompetitive new services should be constrained to keep USWC from overcharging for those services and that "new services" should be defined to exclude the unbundling of existing services; that the plan should require that all interested parties should be permitted to participate in any future settlement negotiations involving changes in rates permitted by the plan; that all customers who received rate decreases should be at risk for rate increases with respect to paragraph 16; that if basic exchange rates or switched access charges are increased in a revenue deficiency filing, at the next annual accounting, rates for those services should be reduced to the average level which existed prior to the increase, or by the percentage required to put USWC at a 9.25% return; that provisions for annual review should be changed to three months, that the plan should be modified to permit adjustments for extra-ordinary increases in expenses and rate base; and that staff and intervenors should be given more time to review annual filings.

In its brief, TRACER criticized the procedure followed in this case. It argued that the agreement was not a true settlement in that it did not involve all parties. It was also argued that the agreement improperly tied the alternative regulation proposal to the proposed complaint settlement, thus "tainting" the proceeding to consider the alternative plan.

In its brief, DIS argued for the correction of the errors and omissions identified by Dr. Zepp. It further recommended that private line service be included in the rate cap provisions of paragraph 9. DIS asks that the Commission eliminate the alleged unfair and discriminatory preference. DIS also criticized the procedure. It argued that the linking of the complaint settlement with the alternative regulation proposal created a public expectation and deprived interested

parties of meaningful opportunity to present issues and recommendations to the Commission. DIS specifically pointed to the fact that it and other interested parties were not included in the settlement process and requested as a condition of any negotiated settlement, that the negotiations be open to all interested parties from the inception of the negotiations.

G. AT&T

AT&T did not present any witnesses, but did participate in the hearings. In its brief, AT&T took no position on the appropriateness of the portion of the agreement providing rate reductions or the alternative regulatory framework. AT&T pointed out that it and other intervenors are not parties to the agreement and thus are not bound by it; it requested that this be recognized, as well as the right of intervenors to file complaints against USWC or petition for relief from the agreement.

AT&T urged the Commission to take steps necessary to continue its policy of cost-based rate reductions for carrier access charges by confirming: that increased minutes of use and cost changes should be reflected in annual reductions in switched access charges, without rate rebalancing or reference to other rates; that EAS expansions should occur only if costs are properly shifted from toll to local rates; and that all parties remain free to argue that proposed rates are below cost, discriminatory, or excessive in relationship to the cost of the service.

AT&T argued for the following amendments to the agreement: that if USWC falls below the minimum rate of return, resulting rate increases should be spread equally to all services; that unbundled or bundled rate filings should not be allowed as new service filings, but should be subject to specific rules for such filings; and that USWC should not be permitted to make revenue neutral filings by offsetting regulated service rate increases with decreases in prices for competitively classified services.

H. WITA

WITA did not present any witnesses, but did participate in the hearings. In its brief, WITA first addressed the settlement process used in this case and could find no procedural problem. WITA pointed out that the proposed settlement, after having been reached by USWC, Commission Staff, and Public Counsel, was then published for public comment and review. It argued that settlements should be encouraged and that the process used in this proceeding where the proposed

settlement of a complex case was reached among the principal parties, and then a proceeding was initiated to allow other interested parties to comment on the settlement, is an effective mechanism to resolve issues short of a full, prolonged and expensive adjudicative proceeding. WITA went on to add that there is no statutory or constitutional right for possible intervenors to become involved in the settlement discussions. It pointed out that all parties expressed their views about the proposed settlement.

The only modification that WITA believed was necessary to the proposed settlement is to modify paragraph 14 to allow toll customers, who make a substantial contribution to USWC revenues, to share in any excess revenues that may be generated. It suggested that the paragraph could be modified by including toll within the services that can benefit from a negative surcharge.

I. GTE-NW

GTE-NW did not present any witnesses, but did participate in the hearings. In its brief, GTE-NW argued against the establishment of a NYNEX-type rate moratorium, but that if the Commission does approve the settlement, it should require USWC to compensate independent telephone companies for their costs of implementing the proposed toll timing change in paragraph 27 of the agreement. GTE-NW further argued that the Commission should not approve the proposal unless it is modified to provide that an appropriate portion of any earnings subject to sharing be returned to independent telephone company toll customers.

J. US SPRINT

US Sprint did not present any witnesses, but did participate in the hearings. In its brief, US Sprint stated that it is unable to support the settlement, but that it does not oppose it. U S Sprint explained that it was not invited to participate in the negotiation discussions, and that by its exclusion, it was denied an opportunity to meaningfully participate. U S Sprint took the view that it and other intervenors were thus left without a means of influencing the contents of the settlement.

K. THREE SEATTLE RATEPAYERS

These ratepayers did not present any witnesses, but did participate in the hearings. In their brief, they argued that the evidence did not show that the proposed plan encourages innovation and efficiency. They argued that the proposed ranges for sharing are excessive and that the Commission should place

a cap on the earnings bands. They also argued that the five-year agreement period is too lengthy and that the window for review is too constricted; in this regard, they alleged as troublesome that the review places the burden of proof on the Commission. These intervenors also argued for a refund provision to be included in the agreement.

L. OTHER INTERVENORS

The other intervenors (Contel, PTI Companies, United and Whidbey) did not file briefs and did not take positions on the issues.

IV. PUBLIC PARTICIPATION

As indicated above, hearings for members of the public were held in Seattle on November 27, in Olympia on November 29, and in Yakima and Spokane on November 30, 1989. In addition to the members of the public who attended the hearings to testify, others wrote letters in which they expressed their views.

The Commission was favorably impressed with the quality of the participation from the public. Many of the issues discussed above were addressed by members of the public, who presented the Commission with additional perspectives on these matters. The public comments demonstrated thoughtful examination of the issues and were, in large part, favorable to the settlement agreement. Public participation in such matters is appreciated by the Commission.

V. COMMISSION DISCUSSION

A. Procedural Matters

At the outset, the Commission wishes to briefly address criticisms leveled by some of the parties concerning procedures in this case. A settlement agreement from the statutory parties of record was filed with the Commission following discussions among these parties. The Commission does not find fault with this procedure. Settlements are encouraged. Settlements are subject to Commission approval and will be evaluated to determine whether the public interest is being served.

Following the filing of the settlement, ample time was allowed for all interested persons to examine the agreement. Hearings were then held. Interventions were granted to numerous interested persons. Some of the intervenors believed that the process was tainted by the fact that the agreement combined the settlement of the earnings complaint with the proposed

alternative form of regulation (AFR) and also tainted by the fact that they were not involved in the settlement talks. The Commission does not agree. There is no requirement that all potentially interested persons who may wish to intervene in a given matter be involved in settlement negotiations between a regulated utility and Commission Staff. Such a requirement would not be workable and might be counterproductive. The intervenors were not harmed or prejudiced. The procedure afforded the parties' due process. Reasonable discovery was allowed, full cross-examination of staff and company witnesses was exercised and all intervenors were given the opportunity to present testimony and evidence on the complaint settlement issues and on the AFR issues. A full and complete record was developed. One of the intervenors, WITA, noted that settlements can and do reduce the expense of the regulatory process and, after analyzing the procedural matters, stated that it could find no procedural problem with the settlement process that was followed in this case. The fact that the agreement settled the earnings complaint and also stipulated to an alternative form of regulation did not deprive the intervenors of meaningful review of the alternative plan. In fact, the Commission believes the parties did an outstanding job in analyzing the issues and presenting their perspectives. The Commission appreciates the parties' efforts and looks forward to ongoing comment from all parties as it monitors the progress of the alternative form of regulation.

B. Settlement of Complaint in Docket No. U-89-2698-F

Upon review of the proposed settlement as well as the record in this matter, the Commission accepts the agreement with the modifications noted hereafter. The agreement provides for rate decreases of \$337.75 million over the next five years, with a \$65 million revenue reduction in 1990. Mr. Damron, the Staff revenue requirement witness, presented the results of Staff's accounting investigation. He explained the underlying assumptions and adjustments and demonstrated the reasonableness of the settlement from a revenue requirement standpoint. The parties did not oppose the proposed \$65 million rate reduction, an amount which this Commission finds to be reasonable. The proposed agreement settling the Commission's complaint against USWC is in the public interest.

Distribution of Revenue Reduction

The proposed distribution of the \$65 million revenue reduction reasonably benefits all classes of customers and is found to be in the public interest. However, the company will be directed to make an additional \$380,000 rate reduction to remedy the double-counting error identified by Dr. Zepp. The correction of this error was not opposed and will be ordered

by the Commission. Upon considering the suggestions of record, the Commission will order that this additional rate reduction, needed to maintain the \$65 million 1990 reduction, be applied to complex business line rates. Dr. Zepp's recommendation for a further reduction of \$900,000 to account for stimulation of sales due to the price decreases will be rejected. Repression adjustments are not customarily made to reduce revenues when basic exchange rates are increased, so it would be inconsistent to make such a stimulation adjustment to increase revenues in a rate reduction situation.

The remaining rate spread provisions in the settlement are accepted by the Commission. A summary will be provided for the sake of discussion. Under the agreement, basic exchange rates for most residential and business customers will be reduced (no existing customers' basic exchange rates will be increased) and USWC will file tariffs to eliminate the EAS additives and to reduce the number of rate groups from six to three. This constitutes a more rational structure for basic exchange rates. These rate restructures benefit all classes of USWC's customers.

The company will offer Enhanced 911 service without installation charge in communities it serves for a maximum monthly charge of twenty-five cents per line. The availability of Enhanced 911 is in the public interest.

One-party universal service is also in the public interest; under the agreement USWC will file tariffs to eliminate suburban mileage charges in all areas and will make one-party service available in all areas of the state. The Commission has recently restated its commitment to strive for one-party service availability on a statewide basis by January 1, 1993. The agreement provides for this goal to be achieved by 1995. The Commission recognizes this as part of a total plan and accepts it while still encouraging the company to accelerate this program wherever possible.

The company will reduce traffic sensitive access charges and the carrier common line rates paid to the company by interexchange carriers. Remaining Touch Tone charges for business and complex lines will be eliminated. The agreement also provides that USWC will file tariffs to remove from the definition of complex business lines those customers with fewer than five lines with trunk hunting or call forward-busy features.

The company will change the toll timing method so that, after the initial minute, increments will be rounded up to the next one-tenth of a minute. As pointed out by GTE-NW, this will involve some expense to independent telephone

companies; the Commission agrees, and deems it appropriate that USWC shall reimburse the independent companies for the reasonable costs of reprogramming their billing systems to accommodate this new method of toll timing.

Some of the intervenors complained that the agreement failed to include rate reductions for toll service and excluded toll from sharing benefits of excess earnings. The Commission finds that toll customers will directly benefit from the change in toll timing; as provided in the agreement. The 1990 benefit of this change is \$11.2 million. Also, toll rates should decrease as a result of the access charge reductions provided for in the agreement. The provisions of the agreement are deemed appropriate and no toll rate modifications will be ordered.

Dr. Zepp contended that the proposed rate differential between complex and simple business lines was not justified by cost differences and that the proposal thus discriminated against the business customer who subscribed to more than four lines. Commission Staff pointed to the absence of a definitive basic exchange cost study in this record and further argued that even though the difference between basic and complex service is increased under the proposal, both rates are decreased from current levels. This is not an appropriate record on which to order a reduction in the ratio of complex to simple business rates; the further step of reducing this ratio will be considered in the company's next rate restructure.

The Commission is sympathetic to the position of the three Seattle ratepayers with respect to refunds on this complaint. However, given the legal arguments surrounding refunds, and given the various benefits of this settlement, the Commission is satisfied that the public interest has been protected.

As indicated above, the agreement with the modifications set forth in this order settles all issues of the Commission's earnings complaint against USWC, provides for a reasonable revenue reduction of \$65 million (\$337 million over the five-year settlement period) and for a fair distribution of those rate reductions.

C. ALTERNATIVE FORM OF REGULATION, DOCKET NO. U-89-3245-P

As set forth earlier, the Legislature recognized the changes in technology and the structure of the telecommunications industry and specifically authorized the Commission to employ alternative forms of regulation as long as the stated policy goals are met, 1989 Wash. Laws, Ch. 101, Sec. 1. The Commission also recently issued an Open Letter on Incentive

Regulation on October 7, 1988, identifying Commission policy goals and guidelines. As stated in its Open Letter, the Commission's ultimate criteria in judging incentive regulation proposals would be whether they serve the public interest and generate real benefits for consumers. Although provision is made in Subsection 5, 1989 Wash. Laws, Ch. 101, Sec. 1 for waivers of regulatory requirements under Title 80 RCW, the company did not request any such waivers in its proposal. The proposed plan, as modified below, meets both the statutory criteria and the Commission's Open Letter guidelines. The differences in telecommunications companies are specifically recognized and the Commission acknowledges that this alternative plan may not necessarily be appropriate for other companies. Each such proposal will be evaluated on its own merits. The Commission agrees with staff's position that the appropriate starting point for an alternative form of regulation proposal is a re-examination of the company's revenue requirement, such as was done in this case in Docket No. U-89-2698-F.

The Commission has weighed and considered the benefits and various criticisms of the proposed alternative form of regulation and concludes that the plan should be approved with the modifications set forth below. Various intervenors criticized the plan claiming that the incentive plan is not beneficial to ratepayers, is not in the public interest, and falls short of legislative intent. It was argued that the proposed plan either be rejected or modified. Others, including a number of public witnesses claimed that the plan will improve upon the existing regulatory framework in providing proper incentives to USWC to provide better service, reduce costs, provide for just, fair and reasonable rates, and prevent market abuse. These parties allege that the incentive plan satisfies statutory requirements and should be accepted.

Subject to the modifications set forth below, the Commission agrees that the plan is in the public interest. Much has been said about this proposal. Some of the statements are accurate and others are inaccurate. It is the Commission's view that this plan is a modified form of rate base regulation coupled with incentive regulation, which we believe is better suited to achieving the policy goals of this state and the needs of its citizens than the traditional form of rate of return, rate base regulation. The Commission finds that the proposed plan, as modified by the Commission, ensures that ratepayers will benefit from efficiency gains and cost savings arising out of regulatory change and will afford ratepayers the opportunity to benefit from improvements in productivity due to technological change. The modified plan will not result in a degradation of the quality or availability of efficient telecommunications services. It will produce fair, just, and reasonable rates and will not unduly or unreasonably prejudice

or disadvantage any particular customer class. In short, the modified plan meets statutory requirements and should be accepted. Key portions of the agreement will be discussed below.

Agreement Period and Review

The period covered by the agreement is from the date of Commission approval to December 31, 1994. A two-month "window" period beginning July 1, 1992 is provided during which time the Commission could institute a proceeding to determine whether the agreement should be terminated prior to the end of the agreement period. Contrary to a suggestion of one of the intervenors, this provision does not act to shift the statutory burden of proof. Complaints by other parties can be brought at any time. Under the agreement, the Commission will continue receiving reports from the company and from its staff. At any time, upon petition by any person, or upon its own motion, the Commission may rescind its approval of the alternative form of regulation.

Rate Cap

During the settlement period, there will be no increase in the monthly recurring rates for exchange residence or business access service or the carrier common line charge (CCLC) above the levels that existed on September 25, 1989.

The agreement also provides that the Commission may approve a basic rate increase above the cap for customers who receive the benefits of corresponding EAS arrangements created subsequent to September 25, 1989. Intervenors MCI and AT&T expressed concern regarding the impact of an EAS expansion on the level of the CCLC, i.e., that it could lead to an increase in the CCLC. MCI argued for a prohibition against the use of CCLC revenue to fund an EAS proposal and AT&T suggested that NTS costs be transferred at the same time minutes of use are transferred from toll to local. These modifications are not necessary. The agreement does provide that the CCLC is capped and cannot be increased above the September 25, 1989 rate. The parties are mistaken in assuming that the Commission will not carefully investigate any future EAS action and consider all relevant evidence from all parties before taking action. The Commission will continue to be vigilant in such matters. The proposal does not change the status quo with respect to EAS. It does not require any change in switched access rates due to EAS changes. The agreement does not limit Commission flexibility or discretion with respect to future EAS actions. We perceive no need for including these requested provisions in this order. Such matters are best left to a separate EAS docket.

Intervenors TRACER and MCI argued that private line rates should also be capped under the agreement, subject to changes in special access rates charged by the independent telephone companies. It was Dr. Zepp's view that private line customers are paying rates well above costs and that private line ratepayers are at the mercy of USWC. Dr. Zepp's views were not established on this record as matters of fact; there were contrary opinions. The Commission deems it appropriate to leave the provisions of the agreement alone in this regard. Any attempt to increase private line rates will continue to be subject to the same Commission review and suspension procedures that exist today. The Commission is not inclined to limit its ability to review such filings individually.

Permitted Rate Changes

As provided in paragraph 10 of the agreement, USWC can file with the Commission for rate changes as follows:

Price list changes, changes to the universal service fund increment to carrier access charges, changes to the lifeline tariff additive, municipal tax changes, rate changes within an approved tariff band, revenue neutral filings; and new service filings, are permitted. Traditional miscellaneous filings with annual revenue effects of less than \$950,000 each, which is less than a .08% rate of return impact, that are made for such reasons as to update a tariff to cover current cost, or correct a tariff anomaly, are also permitted subject to limitations in Paragraph 9.

Several of the intervenors criticized this paragraph despite that fact that it goes on to provide that, "Each of these permitted tariff filings is subject to the normal tariff suspension and hearing provisions contained in Title 80 RCW." MCI witness Dr. Cornell offered her opinion that the agreement changes the regulatory "milieu" and suggested that the Commission staff may not adequately scrutinize filings under the agreement. Staff argued on the contrary that filings under paragraph 10 will likely receive heightened scrutiny, rather than lessened scrutiny. It also bears repeating that customer complaint procedures are still available.

MCI's suggestion that the Commission establish a uniform costing methodology will not be adopted in the case. The search for the "proper" method of allocating costs is an

effort that has consumed literally decades of work by both the FCC and state regulatory commissions -- with no concrete results. There are a vast number of methodologies available to allocate costs among services.¹ In FCC Docket 18128, for example, the agency spent ten years trying to choose among seven different fully distributed costing methodologies in order to establish guidelines for separating costs of AT&T's regulated and unregulated activities. The FCC later abandoned its efforts and imposed structural separation for AT&T's unregulated enterprises.²

As part of its effort to implement the 1985 Washington Telecommunications Regulatory Flexibility Act this Commission issued a notice of inquiry into cost of service issues and costing methodologies (Docket No. U-85-58). After considering the comments and reply comments filed in that docket, the Commission determined that a cost of service standard for telecommunications was not appropriate. The Commission found that no simple prescription of "cost of service ratemaking" can satisfy the diverse regulatory purposes pertinent to the many services and companies of the modern telecommunications industry. The Commission concluded that it would continue to monitor cost of service methodologies on a case-by-case basis.

The Commission is always receptive to receipt of such cost of service information. Dr. Cornell and others are free to provide their input to the Commission at any time. Concerning specific situations, complaint procedures remain available to aggrieved parties. The Commission will take no action on a costing docket at this time.

The new service filings under this paragraph could include either the bundling or unbundling of existing services, to which several of the intervenors objected. TRACER suggested that new services be limited to those that materially increase the range of available options, whereas MCI and AT&T contend that new services should involve a new functionality. AT&T further suggested that USWC be required to maintain the old service at the old rates and also be required to make certain

¹ In a footnote to its decision in MCI Communications vs. American Tel. and Tel., the court related that in one electric utility rate case a witness testified to the existence of at least 29 different methods of apportioning costs among services on a fully distributed basis. 708 F 2d. 1081, at 1116 n. 48 (7th Cir. 1983).

² Private Line Rate Case (TELPAK) 61 FCC 2d 595 (1976) and Second Computer Inquiry, Final Decision, 7 FCC 2d 384, 1980, modified on reconsideration, 84 FCC 2d 50, 238 (1980).

cost demonstrations. The Commission is not convinced that any action needs to be taken on this issue. Adequate protections already exist. The rate discrimination statute will continue to apply and any such filings will be subject to the Commission's review and suspension process. The Commission also agrees with staff that flexibility is needed in this area to deal with possible future developments, such as those related to open network architecture (ONA).

The "traditional miscellaneous filings" are "made for such reasons as to update a tariff to cover current cost, or to correct a tariff anomaly." (Settlement Agreement p.5 of 28). TRACER and MCI contend that the plan does not offer effective criteria upon which to judge such filings. Suggested remedies include requiring such filings to be revenue neutral; requiring a side account with revenue generated from price increases being returned to ratepayers; or placing a cap on miscellaneous filings. Having considered the matter, the Commission has decided that if the \$950,000 annual revenue lid is not reached in a given filing, the company shall keep a record of the revenue impacts of each subsequent filing so that when the aggregate annual revenue impact of two or more filings exceeds \$950,000, a "revenue neutral" offsetting rate reduction shall be included. The suggestion for a precise definition of a "traditional miscellaneous filing" is rejected. The Commission also notes our traditional procedural protections remain for these miscellaneous filings as well.

Revenue neutral filings, in general, involve filings in which net revenues stay the same. AT&T argued for a provision against USWC offsetting price list reductions with regulated service rate increases. The Commission perceives no need to modify the terms of the agreement regarding such filings. The rate increase would be subject to review and suspension; again, the protections discussed above apply.

Authorized Rate of Return Range

The Commission agrees with the 9.25% bottom of the authorized rate of return on investment, but believes the proposed top of the rate of return range is too high and should be reduced to 11%. Thus the threshold for ratepayer sharing will be 11% instead of the proposed 11.25%. This modification is necessary because the only credible evidence as to the reasonableness of current rates establishes a 10.53% top range. While the Commission has previously accepted a range of reasonableness 50 basis points above a target rate of return, the 72 point difference between 10.53% and 11.25% is simply too great. It would create the possibility of unshared excess earnings. The 11% threshold will provide greater assurance that rates will be fair, just and reasonable. This is

especially important given the lack of any "ceiling" on the company's potential achieved return.

Excess Revenues Defined

As provided in the agreement, if the company's achieved rate of return exceeds the top of the authorized range, excess revenues are to be shared between ratepayers and the company. Additionally, the ratepayers' share will be 100% of the revenue in excess of the top of the authorized range due to any net decrease in the mandatory cost factors of tax, accounting, and separations changes as defined in WAC 480-80-390, plus a percentage of the additional excess revenue due to all other factors. The Commission accepts staff's clarification that the excess earnings due to mandatory cost changes are to be measured over the first year the change was in effect. In view of the Commission's modification of the top of the authorized rate of return on investment range, a corresponding .25% adjustment will be made in the sharing bands. Thus, if the company's achieved rate of return exceeds the top of the authorized range, 60% of the additional excess revenues in the band of greater than 11% but less than or equal to 11.625% shall be the ratepayers' share. (Additional excess revenue in a band is revenue in the band that does not flow 100% back to ratepayers because of mandatory cost factors). Fifty percent of the additional excess revenues in the band of greater than 11.625% but less than or equal to 12.25% shall be the ratepayers' share. Forty percent of the additional excess revenues in the band of greater than 12.25% shall be the ratepayers' share. The suggestion that some upper cap be imposed will be rejected by the Commission; no need was demonstrated for such action at this time.

Disposition of Excess Revenues

As set forth in the agreement, excess revenues to be flowed to the ratepayer are to be available for Commission directed service improvements or rate restructures, Commission directed adjustments to increase the depreciation reserve, and/or a negative surcharge, at the Commission's discretion. Any negative surcharge is to be applied on an equal percentage basis, applicable to the rates for exchange access lines and the carrier common line charge. If any portion of the excess revenues to be shared are directed toward the increase of the depreciation reserve, the company is required under the plan to contribute an equal proportion of its shared revenues to an additional increase in the reserve.

Staff witness Mr. Damron and several of the intervenors, such as TRACER, DOD, and MCI, expressed reservations as to whether the four sharing applications will in fact produce

benefits for ratepayers. The principal concern is the "circularity issue" with regard to the negative surcharge. That is, if USWC is in a continuing excess earnings posture, the company will, in effect, collect excess earnings from ratepayers, then return a portion to ratepayers, only to recollect excess revenues the next year. The thrust of the concern is based on the fact that the negative surcharge would not be accompanied by a permanent rate reduction. DOD witness, Mr. King, also expressed reservations as to the ratepayer benefit to be derived from reductions in the depreciation reserve. It was asserted that it would take many years for ratepayers to receive a benefit through depreciation reserve adjustments equivalent to the dollars that they may have given up in the year of the company's overearnings.

The Commission agrees with staff that the use of rate restructure and service improvement options can accomplish permanent ratepayer benefits and are ways to use excess earnings that can avoid the circularity problem. However, rather than limit itself solely to these options, the Commission will retain its full discretion to consider all four options. Without limiting that discretion, the Commission intends to apply the ratepayers' share of excess earnings in the following order of priority: (1) rate restructures, (2) service improvements, (3) adjustments to increase the depreciation reserve, and (4) negative surcharges applicable to exchange access lines and the carrier common line charge. This approach also addresses the concern relating to the disposition of "flow-through" mandatory cost changes after the year immediately subsequent to such mandatory changes.

Under the agreement, the company will be filing regular service reports and the Commission will be monitoring service quality during the agreement period. Also, the Commission intends to adopt explicit service quality standards in the near future. The Commission will also maintain flexibility relating to depreciation rules as new technological developments appear.

Revenue Deficiency and Rate Spread for Revenue Deficiency

Under paragraph 15, if the company's achieved rate of return falls below the bottom of the authorized range, USWC is permitted to file for rates pursuant to WAC 480-80-390 or file a make-whole rate case for additional rates to bring it to the bottom of the range. All usual ratemaking issues can be addressed in a make-whole rate case, except that the company, staff and Public Counsel cannot propose a rate of return different from the bottom of the range. Deficiencies resolved under WAC 480-80-390 are spread according

to that rule, subject to the rate cap limitations of paragraph 9. The agreement provides that in make-whole filings, the deficiency is to be spread first to business exchange access lines up to their cap, and the CCLC up to its cap, then to residence access lines up to their cap. Any additional deficiencies would be made to other services as approved by the Commission. This order of priority was criticized by some of the intervenors. DOD witness Mr. King complained that this contradicted the alleged "distorted" cost/revenue relationships in exchange access line service. DIS characterized it as an "inequitable" treatment. AT&T argued that any such rate increases should be spread equally among all services. The Commission adopts the rate spread as set forth in paragraph 16. It agrees with staff that most of the rate reductions resulting from the complaint settlement in Docket No. U-89-2698-F go to the business class. Paragraph 16 reflects a proper balance of benefits and burdens.

Measurement Period Filing Dates

The Commission accepts Staff's position that the filing dates set forth in paragraph 17 are achievable. Staff will be monitoring USWC's results throughout the year. As pointed out by staff, the paragraph 18K adjustments need not be resolved in the three-week period. However, because of the concern expressed by some of the intervenors, Subsection D of paragraph 17 will be modified in order to provide interested persons an additional week within which to file comments; such comments are to be filed with the Commission on or before May 15.

Accordingly, the Commission approves the proposed alternative form of regulation, subject to the modifications discussed above. All other arguments and suggested changes are rejected. As provided in Subsection 4, 1989 Wash. Laws, Ch. 101, Sec. 1, if the company elects not to proceed with this modified plan as authorized by the Commission, it can file such election with the Commission not later than 60 days from the entry of this order.

FINDINGS OF FACT

Having discussed in detail the evidence and having stated findings and conclusions thereto, the Commission now makes the following summary of facts as found. Portions of the preceding detailed findings pertaining to the ultimate facts are incorporated herein by this reference.

1. The Washington Utilities and Transportation Commission is an agency of the State of Washington vested by

statute with the authority to regulate rates, rules, regulations, practices, accounts, securities and transfers of public service companies, including telecommunications companies.

2. Pacific Northwest Bell Telephone Company, d/b/a U S West Communications (USWC), is engaged in the business of furnishing telecommunications services within the state of Washington, and, as such, is a public service company subject to regulation by the Washington Utilities and Transportation Commission.

3. On February 21, 1989, in Docket No. U-89-2698-F, the Commission, on its own motion, issued a complaint, later amended, against USWC for the purpose of investigating the propriety of rates and charges applicable to the services it provides.

4. On September 26, 1989, a proposed settlement of all disputed issues of the complaint and stipulation to an alternative form of regulation was filed with the concurrence of the respondent, the Office of the Attorney General on behalf of the Commission Staff, and the Public Counsel Division of the Office of the Attorney General. The settlement agreement is attached to this order as Appendix A and is incorporated herein by this reference.

5. On October 4, 1989, USWC filed a petition pursuant to section 1, chapter 101, Laws of 1989, seeking approval of an alternative form of regulation, Docket No. U-89-3245-P.

6. Because the proposed alternative form of regulation in Docket No. U-89-3245-P was related to the proposed settlement in Docket No. U-89-2698-F, the matters were consolidated by Commission order dated October 27, 1989.

7. Interventions were granted by the Commission, followed by an allowance of ample and reasonable discovery to all parties of record. Pursuant to due and proper notice to all parties of record, hearings on the proposed settlement agreement as it related to the complaint in Docket No. U-89-2698-F and as it related to the proposed alternative form of regulation in Docket No. U-89-3245-P were held at various locations on October 23 and 24, November 27, 28, 29, and 30, 1989. Testimony on these issues was received from USWC, Commission Staff, various intervenors and members of the public. A full and complete record was developed and all parties were given a reasonable opportunity to be heard on all issues.

8. The agreement provides for a first year rate decrease of \$65 million (totalling \$337.75 million over the

next five years) and provides for the distribution of the revenue reduction. Both provisions are found to be reasonable, except for a \$380,000 double-counting error related to the redefinition of complex lines; the company shall correct this error with an additional rate reduction applied to complex business line rates. Also, as discussed earlier, USWC shall reimburse the independent companies for the reasonable costs of reprogramming their billing systems to accommodate the new method of toll timing. Except for the changes indicated above, the agreement satisfactorily settles the Commission's complaint against USWC and is in the public interest.

9. The agreement includes a proposed plan for an alternative form of regulation for the company. The Commission finds the plan to be in the public interest, subject to the modifications set forth in this order.

10. The modified plan for an alternative form of regulation will reduce regulatory delay and costs. During the five-year term, lengthy and expensive traditional, contested rate cases will be avoided to a large degree, which is an improvement over the traditional rate of return, rate base process. The \$65 million rate reduction will be implemented without delay. The yearly sharing provisions provide that excess revenues will promptly be available for the benefit of ratepayers.

11. The modified plan will encourage innovation in services. The fact that USWC would have the potential to increase its earnings in the state of Washington creates an incentive for the company to bring new services to the market. The terms of the plan also provide that the company will offer several innovative service improvements in Washington, such as the expanded provision of Enhanced 911 service.

12. The modified plan will promote efficiency. Under the plan, the company will be encouraged to operate as efficiently as possible to increase its earnings to reach the sharing levels. These efficiency gains will be shared with the ratepayers under the sharing provisions of the plan. The increase in the company's share as excess earnings increase eliminates a disincentive to avoid earning into the next sharing band. Insofar as the plan lessens the current disincentives for efficiency embodied in traditional rate of return, rate base regulation, it benefits the company as well as ratepayers.

13. The modified plan facilitates the broad dissemination of technological improvements to all classes of ratepayers. Under the plan, USWC agrees to provide numerous service improvements and/or price reductions to all classes of its

customers. These service improvements allow for current technology to benefit all classes of ratepayers. The plan provides for needed flexibility and discretion on the part of the Commission. The plan allows the Commission to direct the use of ratepayers' share of excess revenues to service improvements as it deems appropriate

14. The efficiency incentives of the modified plan will allow USWC to respond more readily to competition.

15. The modified plan will ensure that USWC does not have the opportunity to exercise substantial market power absent effective competition or effective regulatory constraints. The plan does not result in any price listing, detariffing, rate banding, or deregulation of any services. Under the plan, the Commission will still consider petitions to have particular services classified as competitive services subject to the statutory safeguards of RCW 80.36.330 before any price listing is authorized. The rate cap provisions of the plan provide protections against market power abuse. Furthermore, under the plan, current regulatory oversight is maintained and strengthened.

16. The modified plan will result in fair, just, and reasonable rates for all ratepayers. The rate reductions involved have been set forth earlier in this order. The plan further provides for the immediate sharing of future excess revenues with ratepayers.

17. The modified plan is also consistent with the public policy goals of RCW 80.36.300 and the guidelines set forth in the Commission's Open Letter on Incentive Regulation.

18. The traditional miscellaneous filings provision of the proposed plan shall be modified. If the \$950,000 annual revenue lid is not reached in a given filing, USWC shall keep a record of the revenue impact. When the aggregate revenue impact of two or more filings exceeds \$950,000, a "revenue neutral" offsetting rate reduction filing shall be included.

19. The proposed authorized rate of return range shall be modified so that the top of the range is 11%. This represents a more equitable sharing between ratepayers and shareholders than the proposed 11.25% threshold.

20. Consistent with the modification in Finding of Fact No. 19, the proposed excess revenue sharing bands shall be adjusted down by a corresponding .25%. Thus, if the company's achieved rate of return exceeds the top of the authorized range, 60% of the additional excess revenues in the band of greater than 11% but less than or equal to 11.625%

shall be the ratepayers' share. (Additional excess revenue in a band is revenue in the band that does not flow 100% back to ratepayers because of mandatory cost factors.) Fifty percent of the additional excess revenues in the band of greater than 11.625% but less than or equal to 12.25% shall be the ratepayers' share. Forty percent of the additional excess revenues in the band of greater than 12.25% shall be the ratepayers' share. Furthermore, excess earnings due to mandatory cost changes are to be measured over the first year the change was in effect.

21. Concerning paragraph 14 of the agreement, which provides for the disposition of excess revenues, the Commission favors applying the ratepayers' share of excess earnings in the following order of priority: (1) rate restructures, (2) service improvements, (3) adjustments to increase the depreciation reserve, and (4) negative surcharges applicable to exchange access lines and the carrier common line charge. The Commission reserves full discretion to choose among these options.

22. Subsection D of paragraph 17 of the agreement shall be modified so that interested persons will be given an additional week within which to file comments; such comments are to be filed with the Commission on or before May 15.

23. Subject to the modifications set forth in this order, the Commission approves the proposed alternative regulatory plan, and finds the modified plan to be in the public interest, necessary to respond to occurring changes in technology and the structure of the intrastate telecommunications industry, and better suited to achieving the policy goals of this state than traditional rate of return, rate base regulation. The modified plan ensures that ratepayers will benefit from efficiency gains and cost savings arising out of the regulatory change and will afford ratepayers the opportunity to benefit from improvements in productivity due to technological change. The modified plan will not result in a degradation of the quality or availability of efficient telecommunications services. It will produce fair, just, and reasonable rates and will not unduly or unreasonable prejudice or disadvantage any particular customer class. In short, the plan as modified meets statutory requirements. All other arguments and suggested changes to the plan are rejected. The motion of Commission Staff to correct the transcript shall be granted.

CONCLUSIONS OF LAW

1. The Washington Utilities and Transportation Commission has jurisdiction over the subject matter of this proceeding and the parties thereto.

2. Subject to the modifications set forth in this order, the settlement agreement resolving the complaint in Docket No. U-89-2698-F and providing for an alternative form of regulation in Docket No. U-89-3245-P is in the public interest and is acceptable to the Commission. As modified, it will produce fair, just, and reasonable rates for telecommunications services.

3. All motions made in the course of this proceeding which are consistent with the findings, conclusions and decision herein should be granted, and those inconsistent therewith should be denied.

O R D E R

WHEREFORE, THE COMMISSION HEREBY ORDERS:

1. The settlement agreement, as modified in this order, is approved by the Commission.

2. The terms of the settlement agreement contain a stipulated settlement of the Commission's complaint filed in Docket No. U-89-2698-F and, as modified, provides for rate decreases which are herein approved. The company shall file tariff revisions in accordance with the terms of the agreement, as modified herein.

3. The settlement agreement, as modified, further provides for an alternative form of regulation for USWC, which modified plan is herein approved. Should the company elect not to proceed with this modified plan as authorized by the Commission, it shall file such election with the Commission not later than sixty days from the entry of this order.

4. All motions consistent herewith are granted and those inconsistent herewith are denied.

5. Jurisdiction is retained by the Washington Utilities and Transportation Commission to effectuate the provisions of this order.

DATED at Olympia, Washington, and effective this 16th
day of January, 1990.

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION



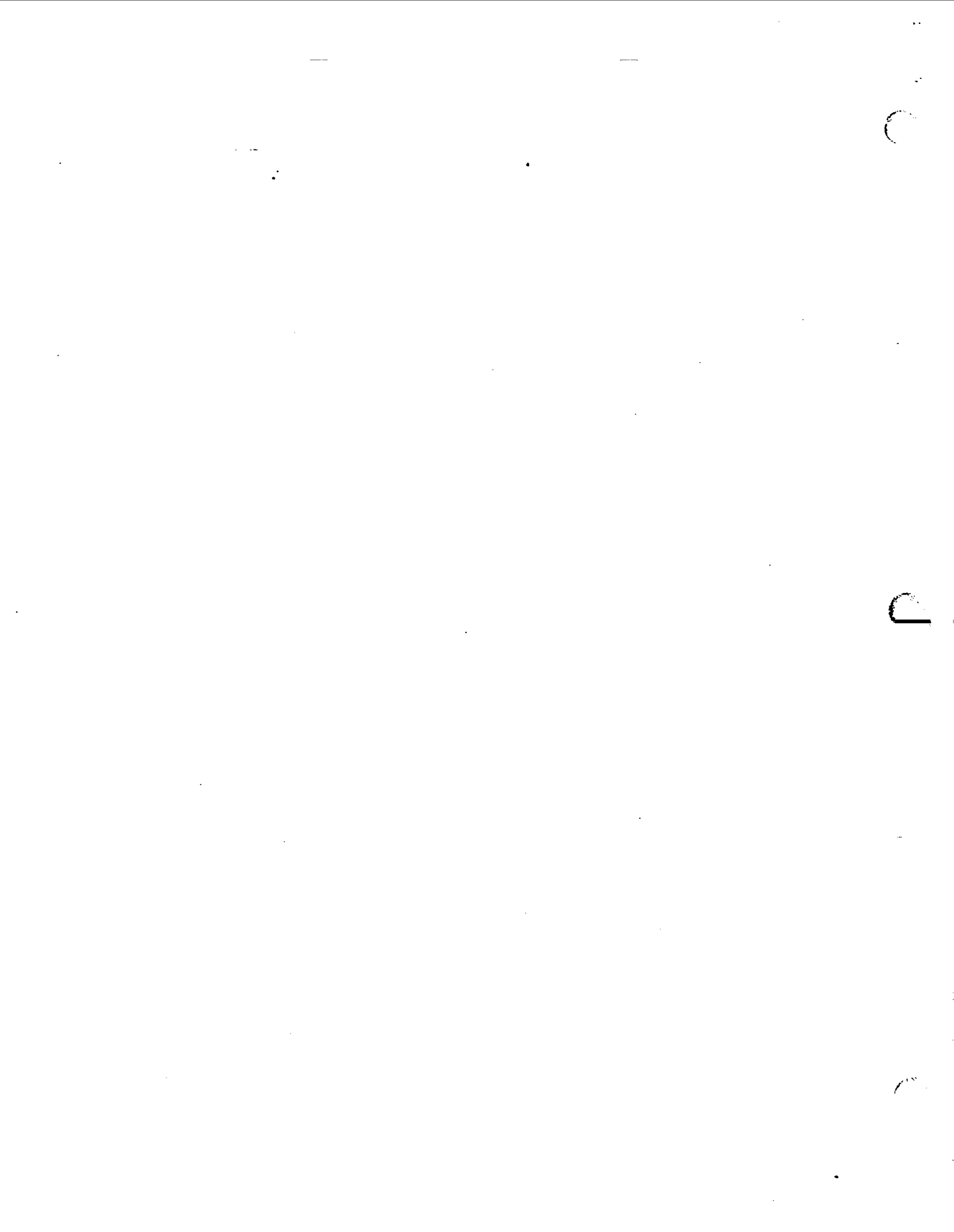
SHARON L. NELSON, Chairman



RICHARD D. CASAD, Commissioner

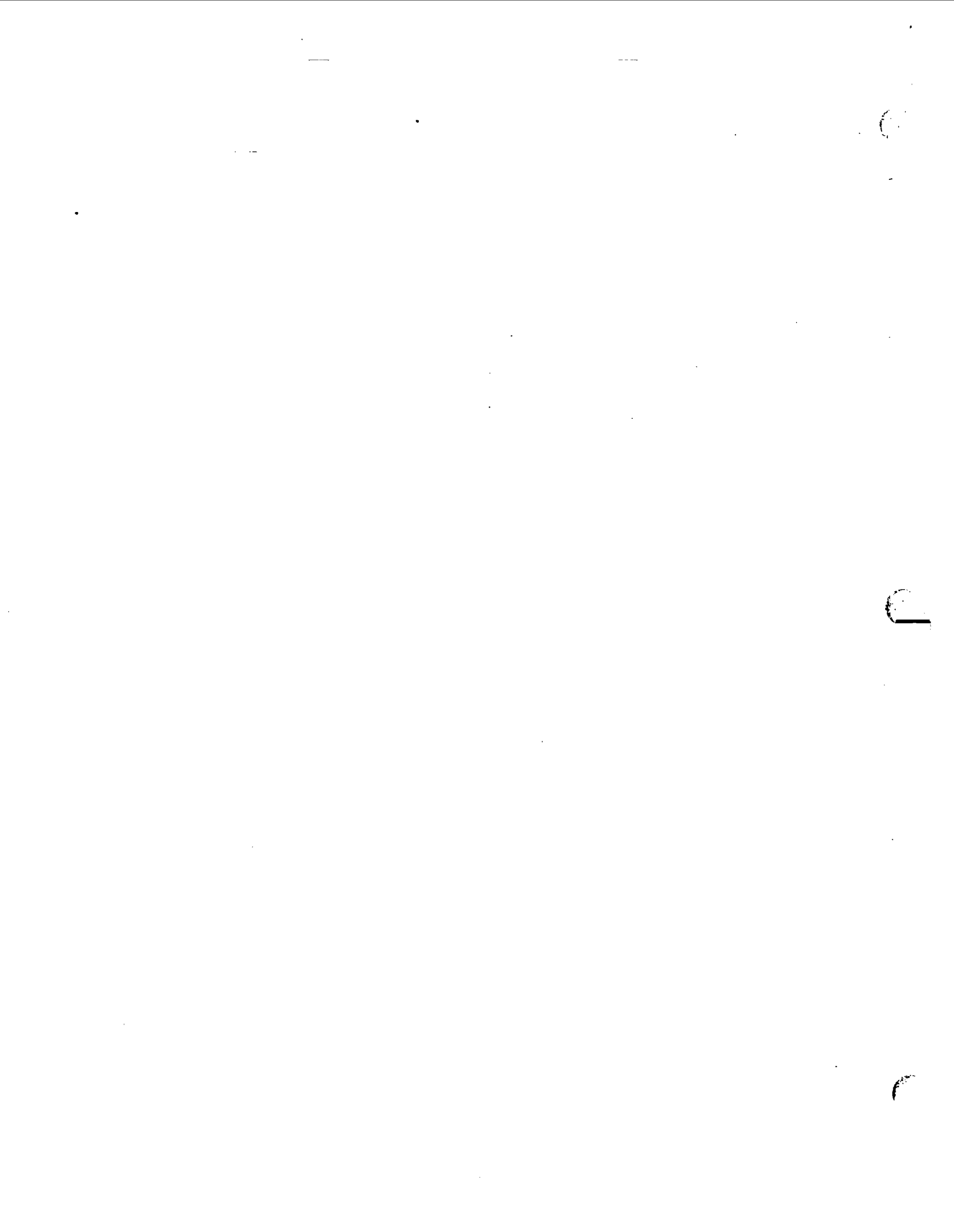


A. J. PARDINI, Commissioner



SETTLEMENT AGREEMENT
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1 1. **GENERAL.** The purpose of this Settlement Agreement
2 (here-after "Agreement") is to stipulate to an alternative
3 form of regulation to be presented to the Commission pursuant
4 to Section 1 of Chapter 101, Laws of 1989, and to stipulate a
5 settlement of the Commission's complaint filed in Docket No.
6 U-89-2698-F against Pacific Northwest Bell Telephone Company
7 d/b/a U S WEST Communications' (hereafter "the Company")
8 rates. The alternative form of regulation is a five-year in-
9 centive regulation plan that provides for a sharing of excess
10 revenues if the Company earns above an authorized rate of re-
11 turn range, and for a cap on basic exchange rates and the car-
12 rier common line charge. The settlement of the Commission's
13 complaint provides for a series of rate decreases which the
14 Company estimates will total \$337.75 million over the next
15 five years. The first year rate decrease effect is \$65.00
16 million. Certain rate increases are allowed if the Company
17 earns at a level below the bottom of the authorized rate of
18 return range.

19
20 2. **EFFECT OF AGREEMENT AS PRECEDENT.** Nothing in this
21 Agreement shall be construed as precedent or shall be binding
22 on any party in any proceeding before the Commission other
23 than those proceedings described in this Agreement. The par-
24 ties recognize that this Agreement is the product of negotia-

1 tion and shall not be construed against any party on the basis
2 that it was the drafter of this Agreement.
3

4 3. **NO EARNINGS COMPLAINTS/LIMITED RATE CHANGES.** The Com-
5 mission and Public Counsel agree not to initiate any com-
6 plaints relating to earnings applicable to the agreement
7 period against the Company. The parties agree that the
8 acceptance of this Agreement by the Commission resolves the
9 issues contained in the Commission's Complaint herein and the
10 Complaint should be dismissed. During the agreement period
11 the Company agrees to limit rate change filings as described
12 in Paragraphs 10 and 15. The Commission is not prevented by
13 this section from instituting a proceeding to change rate
14 design. Rate changes resulting from such a proceeding would
15 be handled in accordance with Paragraph 10.

16 4. **DETARIFFING NOT INCLUDED.** Nothing in this Agreement
17 gives the Company any authority to detariff, rate band, or
18 deregulate any services. The Company reserves the right to
19 pursue price listing or rate banding by making appropriate
20 filings before the Commission as prescribed in Chapter 80.36
21 RCW.

22
23 5. **MANDATORY MEASURED SERVICE PROHIBITED.** The Company
24 agrees not to propose mandatory measured service during the
25 agreement period in the event that the existing statutory
26

1 prohibition on basic exchange mandatory measured service con-
2 tained in RCW 80.04.130 is repealed or is not extended.
3

4 6. **AGREEMENT NOT SEVERABLE.** The parties may present tes-
5 timony in support of this Agreement. In the event the Commis-
6 sion disapproves or modifies this Agreement, the parties shall
7 not be bound by any provision in this Agreement. If the
8 Commission does not approve this Agreement, no party shall be
9 precluded from offering evidence on any and all matters at
10 issue in any hearings that may subsequently be held in this
11 docket, without regard to whether that evidence was or could
12 have been filed in support of, or in opposition to, this
13 Agreement, nor shall any evidence in support of or opposition
14 to this Agreement be part of the decisional record in any sub-
15 sequent hearings on matters remaining at issue, nor shall such
16 testimony be used to the prejudice of any party.
17

18 **ALTERNATIVE FORM OF REGULATION**

19
20
21 7. **AGREEMENT TO FILE A PETITION.** Pursuant to Section 1
22 of Chapter 101, Laws of 1989, the Company agrees to file a pe-
23 tition within ten days of the signing of this Agreement by the
24 aforementioned parties to the Commission for the alternative
25 form of regulation described herein. The Commission Staff and
26

1 Public Counsel agree to support the alternative forms of
2 regulation as described herein.
3

4 8. AGREEMENT PERIOD AND REVIEW. The period covered by
5 this Agreement shall be from the date of approval by the Com-
6 mission to December 31, 1994, and shall be called the agree-
7 ment period unless modified by the Commission pursuant to this
8 paragraph. On or after July 1, 1992 and before August 31,
9 1992, the Commission, on its own motion, or upon petition, may
10 institute a proceeding to determine whether the public inter-
11 est justifies termination of this Agreement prior to December
12 31, 1994. Public Counsel and the Company agree not to appeal
13 the Commission's determination.

14 9. RATE CAP. During the settlement period, there will be
15 no increase in the monthly recurring rates for exchange resi-
16 dence or business access service or the carrier common line
17 charge above the levels that existed at September 25, 1989,
18 provided that the Commission may approve a basic rate increase
19 above the cap for customers who receive the benefits of corre-
20 sponding extended area service arrangements created subsequent
21 to September 25, 1989. Residence and business exchange access
22 service includes all the exchange access lines and network
23 access facilities included in tariff WN U-14, Schedule 1. The
24 carrier common line charge includes originating and
25

1 terminating, premium and non-premium rates included in
2 WN U-19, Sheet 3-18. As provided for in this Agreement, rates
3 for these services may decrease and subsequently increase, but
4 no subsequent increase shall take the rates for these services
5 above the September 25, 1989 levels. In the event that rates
6 for a service are decreased and restructured subsequent to
7 September 25, 1989, subsequently permitted rate increases may
8 be structured so that the average for the service does not ex-
9 ceed the cap, but individual subcategories of rates exceed the
10 cap, provided that the subsequent increases are applied on an
11 equal percentage basis to the entire service.
12

13 10. PERMITTED RATE CHANGES. During the settlement period
14 the Company will not file tariff changes to produce an in-
15 crease in existing tariffed rates except as specifically pro-
16 vided for in this Agreement. Price list changes, changes to
17 the universal service fund increment to carrier access
18 charges, changes to the lifeline tariff additive, municipal
19 tax changes, rate changes within an approved tariff band, rev-
20 enue neutral filings, and new service filings, are permitted.
21 Traditional miscellaneous filings with annual revenue effects
22 of less than \$950,000 each, which is less than a .08% rate of
23 return impact, that are made for such reasons as to update a
24 tariff to cover current cost, or correct a tariff anomaly, are
25 also permitted subject to the limitations in Paragraph 9.
26

1 Each of these permitted tariff filings is subject to the nor-
2 mal tariff suspension and hearing provisions contained in Ti-
3 tle 80 RCW. The Company may also file for rate decreases with
4 no offsetting increases pursuant to RCW 80.04.130. The rev-
5 enue effect of such filings are given special treatment as de-
6 scribed in Paragraph 18G.
7

8 11. AUTHORIZED RATE OF RETURN RANGE. The authorized rate
9 of return on investment shall be the range 9.25% to 11.25%.

10 12. MEASUREMENT PERIODS. The measurement periods shall
11 be defined as the calendar years 1990 through 1994, unless the
12 Agreement is terminated by the Commission pursuant to Para-
13 graph 8.
14

15 13. EXCESS REVENUES DEFINED. If the Company's achieved
16 rate of return, measured on the basis described herein for a
17 measurement period exceeds the top of the authorized range,
18 excess revenues shall be available for sharing between the
19 ratepayers and the Company. The ratepayers' share will be
20 equal to 100% of the revenue in excess of the top of the
21 authorized range due to any net decrease in the mandatory cost
22 factors of tax, accounting, and separations changes as defined
23 in WAC 480-80-390 plus a percentage of the additional excess
24 revenue due to all other factors. If the Company's achieved
25 rate of return exceeds the top of the authorized range, 60% of
26

1 the additional excess revenues in the band of greater than
2 11.25% but less than or equal to 11.875% shall be the ratepay-
3 ers' share. (Additional excess revenue in a band is revenue in
4 the band that does not flow 100% back to ratepayers because of
5 mandatory cost factors). Fifty percent of the additional
6 excess revenues in the band of greater than 11.875 but less
7 than or equal to 12.50% shall be the ratepayers' share.
8 Forty percent of the additional excess revenues in the band of
9 greater than 12.50% shall be the ratepayers' share.
10

11 14. DISPOSITION OF EXCESS REVENUES. Any excess revenues
12 to be flowed to the ratepayer shall be available for Commis-
13 sion directed service improvements or rate restructures, Com-
14 mission directed adjustments to increase the depreciation re-
15 serve, and/or a negative surcharge, at the Commission's dis-
16 cretion. Any negative surcharge shall be payable on or before
17 May 15 or over any time interval in the year following the
18 measurement period, applied on an equal percentage basis, ap-
19 plicable to the rates for exchange access lines and the car-
20 rier common line charge. If any portion of the excess rev-
21 enues that are available on a shared basis are directed toward
22 the increase of the depreciation reserve, the Company shall
23 contribute an equal proportion of its shared revenues to an
24 additional increase in the reserve. Nothing in this Agreement
25 shall prevent the Commission from disposing of any undisputed
26

1 amount of excess revenues prior to the completion of any pro-
2 ceeding in which a disputed adjustment is at issue.

3
4 15. REVENUE DEFICIENCY. If the Company's achieved rate
5 of return measured as described herein falls below the bottom
6 of the authorized range, the Company may file pursuant to
7 WAC 480-80-390 for recovery of certain expense increases iden-
8 tified therein. If the recovery of these expenses is not suf-
9 ficient to bring the Company's rate of return up to the bottom
10 of the range, the Company may, in addition to a pass-through
11 filing pursuant to WAC 480-80-390, file a make-whole rate case
12 for additional rates to bring it to the bottom of the range.
13 If such a make-whole rate case is filed, the Company, the Com-
14 mission Staff, and Public Counsel agree not to propose a rate
15 of return different from the bottom of the range, and the Com-
16 mission Staff and Public Counsel agree not to oppose a Company
17 request that the Commission give the filing expedited
18 treatment.

19 16. RATE SPREAD FOR REVENUE DEFICIENCY. Increased rates
20 resulting from a revenue deficiency filing pursuant to
21 WAC 480-80-390 shall be spread according to that rule, subject
22 to the limitations stated in Paragraph 9. Increased rates
23 resulting from any other revenue deficiency filing shall first
24 be applied to business exchange access lines (including com-
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plex lines as discussed in Paragraph 26) and the carrier com-
mon line charge until these rates are equal to their rate lev-
els as of September 25, 1989 pursuant to the procedures
described in Paragraph 9. Increases will then be applied to
residence access lines until these rates are equal to their
rate levels as of September 25, 1989 pursuant to the
procedures described in Paragraph 9. Additional increases
necessary to recover the approved deficiency will be made to
other services as approved by the Commission.

11 17. **MEASUREMENT PERIOD FILING DATES.** The following dates
12 relate to the year following any measurement period.

13 A. **MARCH 15.** On or before March 15, the Company shall
14 file its Annual Item 14 report.

15
16 B. **APRIL 1.** On or before April 1, the Company shall file
17 its calculation of the achieved rate of return for the
18 measurement period and excess revenues, if any, due
19 the ratepayers pursuant to the procedures described
20 herein, and the Company's proposal for the disposition
21 of any excess revenues.

22 C. **MAY 1.** On or before May 1, the Commission Staff shall
23 file its report on the accuracy of the Company's
24 calculation and appropriate adjustments, and its re-
25

1 port of the appropriateness of the Company's proposed
2 disposition of the ratepayers' share of excess rev-
3 enues. Commission Staff audit adjustments may be made
4 to the Item 14 report as provided for in Paragraph 19.
5

6 D. MAY 8. On or before May 8, comments may be filed with
7 the Commission by any interested person.
8

9 E. DEFICIENCY FILING. If the Company determines that its
10 earnings will fall below the authorized range, it may
11 file for recovery of cost changes pursuant to
12 WAC 480-80-390 or a make-whole rate case at any time
13 after the close of the measurement period.

14 18. MEASUREMENT OF ACHIEVED RATE OF RETURN. For deter-
15 mining the Company's achieved rate of return during the mea-
16 surement period, the following calculations shall be made:

17 A. STARTING POINT. The starting point to calculate the
18 Company's achieved rate of return shall be the Com-
19 pany's actual regulated intrastate rate of return as
20 reported as Column K less Column L of the Item 14 re-
21 port covering the measurement period.
22

23 B. REVENUE SHARING BOOKINGS. An adjustment to the start-
24 ing point shall be made to remove any accruals in the
25
26

1 measurement period made in anticipation of revenue
2 sharing associated with the results of that measure-
3 ment period. An adjustment shall also be made to re-
4 move the impact of the disposition of excess revenues
5 related to the performance of a previous measurement
6 period.

7
8 **C. OUT-OF-PERIOD TRANSACTIONS.** An adjustment to the mea-
9 surement period Item 14 report shall be made to remove
10 the effect of any transaction properly applicable to
11 periods prior to 1990. Adjustments to the starting
12 point shall be made for transactions that are applica-
13 ble to the measurement period booked in the first
14 quarter following a measurement period. These shall
15 be called late-filed adjustments. To avoid dou-
16 ble-counting the transactions associated with the
17 late-filed adjustments, counter late-filed adjustments
18 shall be made to any subsequent measurement period
19 containing transactions that are late-filed adjust-
20 ments. Transactions applicable to the measurement pe-
21 riod, but booked after the first quarter of the subse-
22 quent measurement period shall be reflected in the
23 next measurement period.

1 D. TRADITIONAL ADJUSTMENTS. Adjustments to the starting
2 point shall be made for the following items, calcu-
3 lated in the traditional Commission approved manner.
4 The rate of return used in the calculation of the ad-
5 justments shall be the midpoint of the authorized rate
6 of return range.
7

8 a) Capitalized right to use fees amortized at the
9 currently authorized depreciation rate for
10 analog central office equipment in effect dur-
11 ing each year of the Agreement period.

12 b) Cross boundary adjustment.

13 c) Capitalized interest during construction.

14 d) Lobbying expenses and political action semi-
15 nars.
16

17 e) Charitable contributions.

18 f) U-82-19 refund amortization.

19 g) Jurisdictional differences relating to depre-
20 ciation methods and estimates.
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1 h) Lower of normalization versus flow through for
2 tax timing differences where federal law does
3 not mandate normalization.
4

5 E. **POST-RETIREMENT MEDICAL BENEFITS.** Effective on the
6 tenth calendar day following Commission approval of
7 this Agreement, the Company will cease to accrue post
8 retirement medical benefits. If either the Federal
9 Communications Commission (FCC) or the Financial Ac-
10 counting Standards Board (FASB) approves or mandates
11 the accrual of post retirement medical benefits, the
12 Company may petition the Commission for approval to
13 make the appropriate accruals. The Commission Staff
14 and Public Counsel reserve the right to oppose the
15 accrual in principle, and in methods, including the
16 disposition of the previously accrued post retirement
17 medical benefits during 1988 and 1989. If both the
18 FCC and the FASB approve and/or mandate the accrual of
19 post retirement medical benefits, the Commission Staff
20 agrees not to oppose accruals in principle. The Com-
21 mission Staff then reserves only the right to oppose
22 the Company's proposed accrual methods and its pro-
23 posed disposition of the post retirement medical bene-
24 fits accrued during 1988 and 1989. If the Commission
25 approves the accruals, they will be treated as a
26

1 mandatory cost change pursuant to WAC 480-80-390. Any
2 accrued amounts not deposited in a Voluntary Employee
3 Benefit Association (VEBA) will be deducted from the
4 measurement period rate base.
5

6 F. PRO-FORMA DEBT. Pro-forma debt will be calculated in
7 the traditional approved manner to recognize the addi-
8 tional interest federal income tax deduction for a hy-
9 pothetical capital structure of 47% long term debt,
10 provided the Company's actual long term debt ratio is
11 below 47%.

12 G. RATE DECREASES NOT SUBJECT TO COMMISSION SUSPENSION.
13 An adjustment shall be made to remove the measurement
14 period effect of rate decreases, for the twelve months
15 following the decrease, made during the measurement
16 period or a prior measurement period that were not
17 subject to suspension by the Commission.
18

19 H. U S WEST DIRECT REVENUES. A portion of U S WEST Di-
20 rect's directory advertising revenues (hereafter U S
21 WEST Direct revenues) associated with Washington will
22 be imputed to regulated revenues, calculated based on
23 measurement period data as follows:
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25
26

1 a) U S WEST DIRECT OPERATING REVENUE. U S WEST
2 Direct's actual adjusted operating revenue as-
3 sociated with the publication of telephone di-
4 rectories for U S WEST Communications will be
5 calculated by subtracting from gross revenues:
6 uncollectible expense, cost of service and
7 general and administrative expenses, and
8 adding back in any publishing fees paid to U S
9 WEST Communications included in the general
10 and administrative expenses.

11
12 b) U S WEST DIRECT INVESTMENT BASE. The U S WEST
13 Direct investment base will include the aver-
14 age net book value of fixed assets plus the
15 average value of other current assets, less
16 the end of period value of deferred federal
17 income taxes.

18 c) PRE-TAX IMPUTED U S WEST DIRECT RATE OF RETURN
19 ON INVESTMENT. The pre-tax imputed U S WEST
20 Direct rate of return on investment shall be
21 calculated by giving appropriate effect to the
22 cost of debt equal to the embedded cost of
23 debt for the Washington regulated operations,
24 a debt ratio of 47% long term debt, the cur-
25

1 rent federal income tax rates, and a post-tax
2 rate of return on investment of 12.50%.

3
4 d) **IMPUTED U S WEST DIRECT OPERATING REVENUE.**

5 The imputed U S WEST Direct operating revenue
6 shall be calculated by multiplying the U S
7 WEST Direct pre-tax imputed rate of return on
8 investment obtained in c) by the U S WEST Di-
9 rect investment base calculated in b).

10 e) **U S WEST DIRECT EXCESS OPERATING INCOME.** The
11 U S WEST Direct excess operating income shall
12 be calculated by subtracting the imputed oper-
13 ating revenue calculated in d) from the ad-
14 justed actual operating revenue calculated in
15 a).

16
17 f) **WASHINGTON IMPUTED OPERATING REVENUE.** The
18 Washington imputed operating revenue shall be
19 calculated by multiplying the U S WEST Direct
20 excess operating revenue in e) by a Washington
21 apportionment factor of U S WEST Direct rev-
22 enues for Washington divided by total U S WEST
23 Direct revenues.

1 The parties agree that the foregoing treatment shall
2 continue throughout the entire period of this Agree-
3 ment without regard to any decision that a court may
4 render in the pending yellow page contract litigation.
5 Furthermore, the parties agree that the implementation
6 of a decision of the court in this matter shall not be
7 made retroactive to any portion of the time period
8 covered by this Agreement.
9

10 I. COMMISSION APPROVED AFFILIATED INTEREST CONTRACTS.

11 The Commission has procedures to monitor the expendi-
12 tures associated with these contracts. No adjustment
13 shall be made for these expenses unless the Commission
14 so orders pursuant to the procedure set forth in Para-
15 graph 18K. If the Commission so orders, an adjustment
16 for the expenditure shall be made in an appropriate
17 measurement period calculation. The Company reserves
18 the right to appeal the decision of the Commission.
19 If an appeal of a Commission decision is pending at
20 the time of a measurement period calculation, an
21 amount of ratepayer share of excess revenue associated
22 with the appeal shall be calculated and made subject
23 to refund. If the Commission position prevails on ap-
24 peal, refunds, including interest charged at the rate
25 used for interest on customer deposits, shall be made
26

1 back to the implementation date of the appropriated
2 measurement period calculations. If the Company pre-
3 vails on appeal, the excess revenues associated with
4 the adjustment shall no longer be subject to refund.
5 Nothing in this section shall restrict the rights of
6 any interested person or party to appeal the Commis-
7 sion's determination.
8

9 **J. NOT-YET-APPROVED AFFILIATED INTEREST CONTRACTS.** No
10 adjustments shall be made for any expenses associated
11 with not-yet-approved affiliated interest contracts
12 unless the Commission shall order such an adjustment
13 in an adjudicative proceeding where the Company has
14 the opportunity to be heard, and the rights to appeal
15 are preserved as described above in Paragraph 18I
16 herein.

17 **K. OTHER COMMISSION ORDERED ADJUSTMENTS.** No adjustments
18 for other revenues, expenses, or rate base shall be
19 made unless ordered by the Commission in an adju-
20 dicative proceeding or proceedings where the Company
21 has the right to be heard. Such adjudicative proceed-
22 ings may commence prior to the filing dates specified
23 in Paragraph 17. The Company's right to appeal the
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1 Commission's decision in any such proceeding is pre-
2 served as described in Paragraph 18I herein.
3

4 19. **AUDIT PROVISIONS.** This Agreement does not alter the
5 statutory right of the Commission to inspect and audit all of
6 the Company's books and records or the books and records of
7 the Company's affiliates whose books and records relate to
8 transactions with the Company. The Company agrees to respond
9 expeditiously to reasonable Commission Staff and Public
10 Counsel data requests related to the audit of the Item 14
11 reports in any measurement period. It is understood that an
12 audit of the Item 14 report includes an audit of data
13 underlying the report. The Commission Staff may make
14 appropriate audit adjustments to the Item 14 for the
15 measurement period. The Company has the right to challenge
16 any audit adjustment before the Commission and appeal to the
17 courts. In the case of an appeal, the process pending appeal
18 shall be as set forth in Paragraph 18I herein. Public Counsel
19 shall have access to all audit work papers of the Commission
20 Staff. Further, Public Counsel has the right to make an
21 independent audit of the Company during the period beginning
22 January 1, 1992 and ending on August 31, 1992, or the close of
23 discovery in a Commission instituted formal proceeding on
24 termination, if it is a later date. The Company agrees to ex-
25 peditiously respond to data requests by Public Counsel during
26

1 this audit period pursuant to WAC 480-09-208. Public Counsel
2 and any experts retained by it agree to sign a Protective
3 Agreement not to disclose material designated as confidential.
4

5 20. REPORTING REQUIREMENTS. The Company shall continue
6 to file those periodic and annual reports as required by the
7 Commission. Nothing in this Agreement prevents the Commission
8 from changing the current reporting requirements.

9 21. SERVICE REPORTS. During the period of the Agreement
10 the Company agrees to file the following reports on a monthly
11 and cumulative monthly basis related to the quality of cus-
12 tomer service:
13

14 A. CENTRAL OFFICE. Network Service Performance Summary
15 Plan for individual offices.

16 B. OUTSIDE PLANT. Report of Held Orders for Primary Ser-
17 vice and report on "temporizing" of plant facilities
18 to meet service dates.

19 C. OUT-OF-SERVICE. Report of major service outages and
20 report of trunks and equipment turned down by switch-
21 ing machines or by maintenance personnel for trouble.

22 D. CUSTOMER ACCEPTANCE. Report of quality of service as
23 measured by regular customer surveys.
24
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1 E. TROUBLE REPORT RATE. The total trouble reports per
2 100 access lines.

3
4 In addition to the formal reporting, the Commission
5 Staff will have the right to supplement the reports
6 with inspections of central offices and outside plant
7 facilities.

8
9
10 **REVENUE REDUCTIONS AND SERVICE IMPROVEMENTS**

11
12 22 ENHANCED 911 SERVICE IN SMALL COMMUNITIES. The Com-
13 pany recognizes that it is in the public interest that En-
14 hanced 911 service be available in rural areas, and that the
15 existing \$.50 per month tax is often not sufficient to finance
16 a system. To assist in the development of this service the
17 Company will offer ENHANCED 911 service to any community in
18 which it offers local service for a maximum of \$.25 per line
19 per month. There will be no installation charge. The esti-
20 mated cumulative revenue requirement effect in millions of
21 dollars for this Agreement period is:

22

<u>1990</u>	<u>1991</u>	<u>1992</u>	<u>1993</u>	<u>1994</u>	<u>Total</u>
\$0.36	\$1.36	\$0.75	\$0.44	\$0.35	\$3.26

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1 23. **ONE-PARTY UNIVERSAL SERVICE.** The Company will file
 2 tariffs within ten calendar days of the Commission approval of
 3 this Agreement to be effective ten days following the filing
 4 to eliminate the suburban mileage charge in all areas, and
 5 will make one-party service available, in all areas of the
 6 state. Where facilities for one-party service are available,
 7 suburban party service will be frozen. After one year from
 8 the effective date of the approval of this Agreement by the
 9 Commission, the Company may file tariff changes proposing the
 10 elimination of suburban, two, and four party service. The es-
 11 timated cumulative revenue requirement effect in millions of
 12 dollars for this tariff change for this Agreement period is:

13	14	15	16	17	18	19
	<u>1990</u>	<u>1991</u>	<u>1992</u>	<u>1993</u>	<u>1994</u>	<u>Total</u>
	\$5.53	\$6.42	\$7.09	\$7.81	\$8.41	\$35.26

16 The tariffs filed pursuant to this Paragraph shall be subject
 17 to Commission approval, and bear the notation "By Authority of
 18 the Commission Order in Docket No. U-89-2698-F."
 19

20 24. **CARRIER SWITCHED ACCESS CHARGES REDUCTIONS.** The Com-
 21 pany will file tariffs for an \$8.27 million dollar reduction
 22 within ten calendar days of the Commission approval of this
 23 Agreement to be effective ten days following the filing to up-
 24 date traffic sensitive access charges and carrier common line
 25 rates to reflect the estimated changes in costs and volumes
 26

1 for 1988. The Company agrees to file tariffs based on the
2 procedures prescribed in Cause No. U-85-23 to update access
3 charges on March 1 in each of the years 1990 to 1994, provid-
4 ing the net effect of the changes is a revenue reduction. Ad-
5 justments will be made to cost-derived Carrier Common Line
6 rate to preserve the effect of increases and decreases, and
7 the rate cap pursuant to Paragraphs 9, 14, and 16. If the up-
8 date produces an increase, it will not be filed unless the
9 Company's rate of return during a measurement period falls be-
10 low the bottom of the authorized range. The estimated cumula-
11 tive revenue requirement effect in millions of dollars for
12 this Agreement period is:

<u>1990</u>	<u>1991</u>	<u>1992</u>	<u>1993</u>	<u>1994</u>	<u>Total</u>
\$8.56	\$9.00	\$9.45	\$9.73	\$9.78	\$46.51

16 The tariffs filed pursuant to this Paragraph shall be subject
17 to Commission approval and bear the notation "By Authority of
18 the Commission Order in Docket No. U-89-2698-F."
19

20 25. REMOVAL OF TOUCHTONE CHARGES FROM COMPLEX BUSINESS
21 LINES. The Company agrees to file tariffs within ten calendar
22 days of the Commission approval of this Agreement to be effec-
23 tive ten days following the filing to remove TouchTone charges
24 from complex lines. The estimated cumulative revenue require-
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ment effect in millions of dollars for this Agreement period
is:

<u>1990</u>	<u>1991</u>	<u>1992</u>	<u>1993</u>	<u>1994</u>	<u>Total</u>
\$2.60	\$2.60	\$2.60	\$2.60	\$2.60	\$13.00

The tariffs filed pursuant to this Paragraph shall be subject to Commission approval, and bear the notation "By Authority of the Commission Order in Docket No. U-89-2698-F."

26. **COMPLEX LINE DEFINITION.** The current criteria for a complex line is that it is either part of a system containing more than four lines, or it is part of a system of any size that also includes trunk hunting or the call forward - busy feature on any line. The Company agrees to file tariffs within ten calendar days of the Commission approval of this Agreement to be effective on January 1, 1990 to eliminate the portion of the complex line criteria related to trunk hunting and the call forward - busy feature. Because of the necessary time required to reprogram the Company's billing system to accommodate this change, the tariff will have an effective date of January 1, 1990, but the customer billing will be changed at a later date prior to June 1, 1990. At the time the customer billing is changed, the customer's bill will be credited for the change back to January 1, 1990. The estimated cumula-

1 tive revenue requirement effect of this change in millions of
2 dollars for this Agreement period is:
3

4	<u>1990</u>	<u>1991</u>	<u>1992</u>	<u>1993</u>	<u>1994</u>	<u>Total</u>
5	\$12.76	\$12.76	\$12.76	\$12.76	\$12.76	\$63.80

6 The tariffs filed pursuant to this Paragraph shall be subject
7 to Commission approval, and bear the notation "By Authority of
8 the Commission Order in Docket No. U-89-2698-F."
9

10 27. TOLL TIMING. The current method of timing toll calls
11 for additional minutes (all minutes subsequent to the initial
12 minute are additional minutes) provides for rounding up to the
13 next whole minute. The Company agrees to change the timing
14 method so that additional minutes are rounded up to the next
15 one-tenth minute. Because of the billing system programming
16 changes necessary for the Company and the Independent Tele-
17 phone Companies necessary to implement this change, the Com-
18 pany agrees to file a tariff within ten calendar days of the
19 Commission approval of this Agreement to be effective January
20 1, 1990 to implement a temporary toll reduction of \$11.2 mil-
21 lion. The tariff will further state that on July 1, 1990 the
22 temporary toll reduction will expire and the new method of
23 timing for additional minutes to round up to the next one-
24 tenth of a minute will be implemented. If the billing systems
25 of all of the companies can be changed prior to July 1, 1990,
26

1 the Company will file a subsequent tariff changing the imple-
2 mentation to an earlier date. The estimated cumulative rev-
3 enue requirement effect in millions of dollars for this change
4 for the Agreement period is:

5

<u>1990</u>	<u>1991</u>	<u>1992</u>	<u>1993</u>	<u>1994</u>	<u>Total</u>
\$11.20	\$11.20	\$11.20	\$11.20	\$11.20	\$56.00

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8 The tariffs filed pursuant to this Paragraph shall be subject
9 to Commission approval, and bear the notation "By Authority of
10 the Commission order in Docket No. U-89-2698-F."
11

12 28. BASIC EXCHANGE RATE RESTRUCTURE. The Company will
13 file tariffs within ten calendar days of the Commission ap-
14 proval of this Agreement to be effective ten days following
15 the filing to eliminate the EAS additives to basic exchange
16 rates, and reduce the number of exchange rate groups from 6 to
17 3, and to make various rate decreases to residence and busi-
18 ness exchange rates. Details of the basic exchange rate
19 restructure are included in appendix 1 to this Agreement. The
20 estimated cumulative annual revenue requirement effect in mil-
21 lions of dollars for the basic rate restructure is:

22

<u>1990</u>	<u>1991</u>	<u>1992</u>	<u>1993</u>	<u>1994</u>	<u>Total</u>
\$23.98	\$23.98	\$23.98	\$23.98	\$23.98	\$119.92

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1 The tariffs filed pursuant to this Paragraph shall be subject
2 to Commission approval, and bear the notation "By Authority of
3 the Commission Order in Docket No. U-89-2698-F."
4

5 28. TOTAL REVENUE EFFECT OF STIPULATION. The estimated
6 total cumulative revenue requirement impact in millions of
7 dollars for all of the items above is:

<u>1990</u>	<u>1991</u>	<u>1992</u>	<u>1993</u>	<u>1994</u>	<u>Total</u>
\$65.00	\$67.32	\$67.83	\$68.52	\$69.09	\$337.75

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11 This impact assumes that the Company earns within the autho-
12 rized range during the entire period of this Agreement and
13 that this Agreement remains in force until December 31, 1994.
14 To the extent that the Company achieves earnings in excess of
15 the authorized range, there will be additional revenue
16 reductions during the period. To the extent that the
17 Company's earnings fall below the authorized range, there may
18 be increases in rates that will be an offset to the revenue
19 reductions due to earnings above the authorized range in pre-
20 vious measurement periods, and may in addition, offset some of
21 the specific revenue reductions described above.
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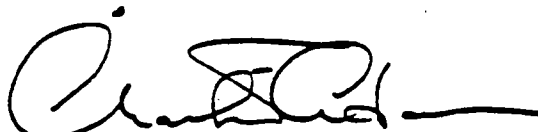
DATED this 25th day of September, 1989

WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION STAFF
by



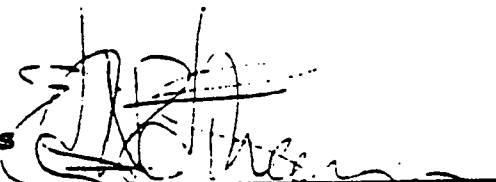
DONALD T. TROTTER
ASSISTANT ATTORNEY GENERAL

PUBLIC COUNSEL SECTION
Office of the Attorney General
by



CHARLES F. ADAMS
ASSISTANT ATTORNEY GENERAL

Pacific Northwest Bell Telephone
Company d/b/a U S WEST Communications
by



EDWARD T. SHAW
CHIEF COUNSEL - WASHINGTON

APPENDIX 1.

PACIFIC NORTHWEST BELL TELEPHONE CO. d/b/a USBC PROPOSED LOCAL RATES BASED ON COMBINING
DOCKET NO. U-89-2698-F ALL RATE GROUPS INTO ONLY 3 BASIC RATE GROUPS, ADJUSTS RATIOS.

RATE GROUP	1FB	FBK	IRK	IMB	MBK	MTK	TYT	2FB	SUB	1FR	IMR	LMR	2FR	2MR	4FR	SUB
1	18.40	26.65	26.65	12.85	12.85	23.90	23.90	15.60	12.75	8.75	6.15	4.15	7.15	MA	6.25	7.00
2	18.40	26.65	26.65	12.85	12.85	23.90	23.90	15.60	12.75	8.75	6.15	4.15	7.15	MA	6.25	7.00
3	24.10	35.15	35.15	16.20	16.20	31.30	31.30	20.70	12.75	9.75	6.60	4.60	8.45	5.80	7.25	8.05
4	24.10	35.15	35.15	16.20	16.20	31.30	31.30	20.70	12.75	9.75	6.60	4.60	8.45	5.80	7.25	8.05
5	28.20	42.25	42.25	19.20	19.20	36.65	36.65	MA	13.00	10.75	7.35	5.35	9.40	5.85	7.95	8.65
6	28.20	42.25	42.25	19.20	19.20	36.65	36.65	MA	13.00	10.75	7.35	5.35	9.40	5.85	7.95	8.65

NEW RG
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NEW RG
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NEW RG
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PACIFIC NORTHWEST BELL TELEPHONE CO. d/b/a USBC
DOCKET NO. U-89-2698-7 AMOUNT OF PROPOSED RATE REDUCTION BY EXISTING RATE GROUP

RATE GROUP	178	FBK	TRK	1MB	MRK	NTK	TTT	2FB	SUB	1FR	1MR	LMR	2FR	2MR	4FR	SUB
1	1.00	0.00	0.00	6.15	6.15	MA	3.05	3.90	0.00	0.00	0.00	0.00	0.00	MA	0.00	0.00
1-E.0	1.35	0.50	0.50	6.15	6.15	MA	3.75	4.20	0.25	0.25	0.15	0.20	0.20	MA	0.15	0.15
1-E.1	1.70	1.00	1.00	6.15	6.15	MA	4.45	4.50	0.50	0.50	0.25	0.40	0.40	MA	0.25	0.25
1-E.2	2.20	1.45	1.45	6.15	6.15	MA	5.45	4.75	0.80	0.80	0.45	0.70	0.70	MA	0.50	0.50
2	3.90	4.00	4.00	6.15	6.15	6.90	6.90	3.90	0.00	1.00	0.00	0.00	0.00	MA	0.55	0.65
2-E.0	4.25	4.50	4.50	6.35	6.35	7.60	7.60	4.20	0.25	1.25	0.15	1.00	1.00	MA	0.70	0.75
2-E.1	4.60	5.00	5.00	6.50	6.50	8.30	8.30	4.50	0.50	1.50	0.25	1.20	1.20	MA	0.80	0.85
2-E.2	5.10	5.65	5.65	6.65	6.65	9.30	9.30	4.75	0.80	1.85	0.45	1.50	1.50	MA	1.05	1.10
2-E.3	6.30	7.55	7.55	7.00	7.00	11.70	11.70	5.50	1.20	2.60	0.80	1.95	1.95	MA	1.30	1.35
3	0.25	(0.50)	(0.50)	2.80	2.80	3.05	3.05	0.00	0.00	0.25	0.00	0.00	0.00	0.00	0.00	0.00
3-E.0	0.60	0.00	0.00	3.00	3.00	3.75	3.75	0.30	0.25	0.50	0.15	0.20	0.20	0.15	0.15	0.15
3-E.1	0.95	0.50	0.50	3.15	3.15	4.45	4.45	0.60	0.50	0.75	0.25	0.40	0.40	0.25	0.25	0.25
3-E.2	1.45	1.15	1.15	3.30	3.30	5.45	5.45	0.85	0.80	1.10	0.45	0.70	0.70	MA	0.50	0.50
3-E.3	2.65	3.05	3.05	3.65	3.65	7.85	7.85	1.60	1.20	1.85	0.80	1.15	1.15	MA	0.75	0.75
3-E.4	5.05	6.40	6.40	4.45	4.45	12.65	12.65	3.25	2.05	3.40	1.60	2.30	2.30	MA	1.50	1.50
4	3.05	3.50	3.50	2.80	2.80	5.90	5.90	0.00	0.00	0.55	0.55	0.55	0.55	0.05	0.35	0.35
4-E.0	3.40	4.00	4.00	3.00	3.00	6.60	6.60	0.30	0.25	0.60	0.70	0.70	0.70	0.20	0.50	0.50
4-E.1	3.75	4.50	4.50	3.15	3.15	7.30	7.30	0.60	0.50	1.05	0.80	0.95	0.95	0.30	0.60	0.60
4-E.2	4.25	5.15	5.15	3.30	3.30	8.30	8.30	0.85	0.80	1.40	1.00	1.25	1.25	MA	0.85	0.85
4-E.4	7.85	10.40	10.40	4.45	4.45	15.50	15.50	3.25	2.05	3.70	2.15	2.85	2.85	MA	1.85	1.85
5	2.45	0.40	0.40	(0.20)	(0.20)	0.55	0.55	MA	(0.25)	(0.05)	0.00	(0.01)	(0.01)	0.00	(0.01)	(0.01)
5-E.0	2.80	0.90	0.90	0.00	0.00	1.25	1.25	MA	0.00	0.20	0.15	0.19	0.19	0.15	0.14	0.14
5-E.1	3.15	1.40	1.40	0.15	0.15	1.95	1.95	MA	0.25	0.45	0.25	0.39	0.39	0.25	0.24	0.24
5-E.2	3.65	2.05	2.05	0.30	0.30	2.95	2.95	MA	0.55	0.80	0.45	0.69	0.69	MA	0.49	0.49
5-E.3	4.85	3.95	3.95	0.65	0.65	5.35	5.35	MA	0.95	1.35	0.80	1.14	1.14	MA	0.74	0.74
5-E.4	7.25	7.30	7.30	1.45	1.45	10.15	10.15	MA	1.80	3.10	1.60	2.29	2.29	MA	1.49	1.49
5-E.5	12.05	12.90	12.90	3.05	3.05	19.75	19.75	MA	3.00	5.20	2.65	3.74	3.74	MA	2.64	2.64
6	6.55	4.35	4.35	(0.20)	(0.20)	0.55	0.55	MA	(0.25)	0.50	0.00	0.35	0.35	0.00	0.10	0.20
6-E.0	6.90	4.85	4.85	0.00	0.00	1.25	1.25	MA	0.00	0.75	0.15	0.55	0.55	0.00	0.25	MA
6-E.1	7.25	5.35	5.35	0.15	0.15	1.95	1.95	MA	0.25	1.00	0.25	0.75	0.75	0.00	0.35	0.45
6-E.2	7.75	6.00	6.00	0.30	0.30	2.95	2.95	MA	0.55	1.35	0.45	1.05	1.05	0.00	0.60	0.70
6-E.3	8.95	7.90	7.90	0.65	0.65	5.35	5.35	MA	0.95	2.10	0.80	1.50	1.50	0.00	0.85	0.95

PACIFIC NORTHWEST BELL TELEPHONE CO. d/b/a USMC
DOCKET NO. U-89-2698-F PERCENT REDUCTION

RATE GROUP	1FB	FBK	TRK	1MB	MBK	MTK	ITT	ZFB	SUB	1FR	1MR	LMR	ZFR	ZMR	4FR	SUB
1	5.2%	0.0%	0.0%	32.4%	32.4%	MA	11.3%	20.0%	0.0%	0.0%	0.0%	0.0%	0.0%	MA	0.0%	0.0%
1-E-0	6.8%	1.6%	1.6%	32.4%	32.4%	MA	13.6%	21.2%	1.9%	2.8%	2.4%	3.5%	2.7%	MA	2.3%	2.1%
1-E-1	8.5%	3.6%	3.6%	32.4%	32.4%	MA	15.7%	22.4%	3.8%	5.4%	3.9%	5.7%	5.3%	MA	3.6%	3.1%
1-E-2	10.7%	5.8%	5.8%	32.4%	32.4%	MA	18.6%	23.3%	5.9%	8.9%	6.8%	9.8%	8.9%	MA	7.4%	6.2%
2	17.5%	13.1%	13.1%	32.4%	32.4%	22.4%	22.4%	20.0%	0.0%	10.3%	0.0%	0.0%	10.1%	MA	8.1%	7.9%
2-E-0	18.8%	14.4%	14.4%	33.1%	33.1%	24.1%	24.1%	21.2%	1.9%	12.5%	2.4%	3.5%	12.3%	MA	10.1%	9.7%
2-E-1	20.0%	15.8%	15.8%	33.6%	33.6%	25.8%	25.8%	22.4%	3.8%	14.6%	3.9%	5.7%	14.4%	MA	11.3%	10.8%
2-E-2	21.7%	17.5%	17.5%	34.1%	34.1%	28.0%	28.0%	23.3%	5.9%	17.5%	6.8%	9.8%	17.3%	MA	14.4%	13.6%
2-E-3	25.5%	22.1%	22.1%	35.3%	35.3%	32.9%	32.9%	26.1%	8.6%	22.9%	11.5%	16.2%	21.4%	MA	17.2%	16.2%
3	1.0%	-1.4%	-1.4%	14.7%	14.7%	8.9%	8.9%	0.0%	0.0%	2.5%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
3-E-0	2.4%	0.0%	0.0%	15.6%	15.6%	10.7%	10.7%	1.4%	1.9%	4.9%	2.2%	3.2%	2.3%	2.5%	2.0%	1.8%
3-E-1	3.8%	1.4%	1.4%	16.3%	16.3%	12.4%	12.4%	2.6%	3.6%	7.1%	3.6%	5.2%	4.5%	4.1%	3.3%	3.0%
3-E-2	5.7%	3.2%	3.2%	16.9%	16.9%	14.8%	14.8%	3.9%	5.9%	10.1%	6.4%	8.9%	7.7%	MA	6.5%	5.8%
3-E-3	9.9%	8.0%	8.0%	18.4%	18.4%	20.1%	20.1%	7.2%	8.6%	15.9%	10.8%	14.8%	12.0%	MA	9.4%	8.5%
3-E-4	17.3%	15.4%	15.4%	21.5%	21.5%	28.8%	28.8%	13.6%	13.9%	25.9%	19.5%	25.8%	21.4%	MA	17.1%	15.7%
4	11.2%	9.1%	9.1%	14.7%	14.7%	15.9%	15.9%	0.0%	0.0%	5.3%	7.7%	10.7%	6.1%	0.9%	4.6%	4.2%
4-E-0	12.4%	10.2%	10.2%	15.6%	15.6%	17.4%	17.4%	1.4%	1.9%	7.6%	9.6%	13.2%	8.2%	3.3%	6.5%	5.8%
4-E-1	13.5%	11.3%	11.3%	16.3%	16.3%	18.9%	18.9%	2.8%	3.8%	9.7%	10.8%	14.8%	10.1%	4.9%	7.6%	6.9%
4-E-2	15.0%	12.8%	12.8%	16.9%	16.9%	21.0%	21.0%	3.9%	5.9%	12.6%	13.2%	17.9%	12.9%	MA	10.5%	9.6%
4-E-4	24.6%	22.8%	22.8%	21.5%	21.5%	33.1%	33.1%	13.6%	13.9%	27.5%	24.6%	31.9%	25.2%	MA	20.3%	18.7%
5	8.0%	0.9%	0.9%	-1.1%	-1.1%	1.5%	1.5%	MA	-2.0%	-0.5%	0.0%	0.0%	-0.1%	0.0%	-0.1%	-0.1%
5-E-0	9.0%	2.1%	2.1%	0.0%	0.0%	3.3%	3.3%	MA	0.0%	1.8%	2.0%	2.7%	2.0%	2.5%	1.7%	1.6%
5-E-1	10.0%	3.2%	3.2%	0.8%	0.8%	5.1%	5.1%	MA	1.9%	4.0%	4.5%	4.5%	4.0%	4.1%	2.9%	2.1%
5-E-2	11.5%	4.6%	4.6%	1.5%	1.5%	7.4%	7.4%	MA	4.1%	6.9%	7.8%	7.8%	6.8%	MA	5.8%	5.4%
5-E-3	14.7%	8.5%	8.5%	3.3%	3.3%	12.7%	12.7%	MA	6.8%	12.6%	13.0%	13.0%	10.8%	MA	8.5%	7.9%
5-E-4	20.5%	14.7%	14.7%	7.0%	7.0%	21.7%	21.7%	MA	12.2%	22.4%	23.0%	23.0%	19.6%	MA	15.6%	14.7%
5-E-5	29.9%	23.4%	23.4%	13.7%	13.7%	35.0%	35.0%	MA	18.8%	32.6%	33.1%	33.1%	28.5%	MA	24.9%	23.4%
6	18.8%	9.3%	9.3%	-1.1%	-1.1%	1.5%	1.5%	MA	-2.0%	4.4%	0.0%	0.0%	3.6%	0.0%	1.2%	2.3%
6-E-0	19.7%	10.3%	10.3%	0.0%	0.0%	3.3%	3.3%	MA	0.0%	6.5%	2.0%	2.7%	5.5%	0.0%	3.0%	MA
6-E-1	20.5%	11.2%	11.2%	0.8%	0.8%	5.1%	5.1%	MA	1.9%	8.5%	3.3%	4.5%	7.4%	0.0%	4.2%	4.9%
6-E-2	21.6%	12.4%	12.4%	1.5%	1.5%	7.4%	7.4%	MA	4.1%	11.2%	5.8%	7.8%	10.0%	0.0%	7.0%	7.5%
6-E-3	24.1%	15.8%	15.8%	3.3%	3.3%	12.7%	12.7%	MA	6.8%	16.3%	9.8%	13.0%	13.8%	0.0%	9.7%	9.9%

