Ex. _____ (MLT-Testimony)
Docket No. UT-971140
Witness: Maurice L. Twitchell

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

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| WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION, | ) | |
| | ) | DOCKET NO. UT-971140 |
| Complainant, | ) | |
| vs. | ) | |
| WASHINGTON EXCHANGE CARRIER ASSOCIATION, et al., | ) | |
| Respondent. | ) | |
| . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . | ) | |

TESTIMONY OF MAURICE L. TWITCHELL

STAFF OF THE
WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION

April 8, 1998

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**Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS**.

A. My name is Maurice L. Twitchell. My business address is 1300 South Evergreen Park Drive Southwest, P.O. Box 47250, Olympia, Washington 98504.

**Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?**

A. I am employed by the Washington Utilities and Transportation Commission as a Program Manager/Consultant.

## I. QUALIFICATIONS

**Q. WHAT ARE YOUR EDUCATION AND EXPERIENCE QUALIFICATIONS?**

A. I am a graduate of Brigham Young University, holding a Bachelor of Science degree with a major in Accounting and a minor in Business Administration and Economics, having been graduated in June, 1970. I was employed by the Washington Utilities and Transportation Commission in September of 1970. While in the employment of the Commission, I have participated in or been in charge of several staff studies and accounting examinations, including telephone cases involving U S WEST (Pacific Northwest Bell Company), General Telephone Company of the Northwest, Inc., United Telephone Company of the Northwest, Pacific Telecom, Inc., and many of the other local exchange companies operating in this state. I have also participated in examinations of The Washington Water Power Company, Washington Natural Gas Company, Pacific Power & Light Company, and Puget Sound Power and Light Company. I have also participated in examinations of water and transportation companies.

## II. DESCRIPTION OF FILING AND THIS CASE

**Q. WHAT IS THE NATURE OF THE FILING IN THIS CASE?**

A. This case resulted from a tariff filing by the Washington Exchange Carrier Association (WECA) proposing revisions to the Washington Intrastate Carrier Common Line (CCL) and Universal Service Fund (USF) rate elements. These are commonly referred to as the Non-Traffic Sensitive, or NTS, rate elements. The CCL and USF rate elements are designed to recover the collective intrastate non-traffic sensitive revenue requirements of the companies participating in the WECA pools. The filing of these NTS and USF rate elements are required by the Commission's Eighteenth Supplemental Order in U85-23 (12/30/98). The purpose of these tariffed rates or access charges was to replace the then existing settlements contracts with a system based on the use of tariffed access charges.

**Q. BY WHAT AUTHORITY DOES THE WASHINGTON EXCHANGE CARRIER ASSOCIATION OPERATE?**

A. WECA receives its authority to file tariffs from the Washington Administrative Code (WAC) 480-80-048.

> (1) Upon approval by the commission of its rules of procedure, the Washington Exchange Carrier Association (WECA) may file with the commission tariffs and may represent before the commission those of its members that authorize it to do so. WECA's rules of procedure may provide for joint or collective consideration of proposals for changes in intrastate toll, interexchange and/or access rates, tariffs or conditions of service.
>
> (5) To the extent that WECA is involved in the collection and redistribution of funds pursuant to commission orders authorizing certain revenue sharing arrangements under common tariff, it shall maintain and provide to the commission monthly and annual financial reports relating to such arrangements. These reports shall include actual fund collections and distributions to each member local exchange company and the basis upon which the collection and distribution is made.
>
> (6) Each local exchange telecommunication company serving less than one million access lines in the state of Washington has the option of utilizing the

Washington Exchange Carrier Association as its filing agent/tariff bureau. Companies utilizing WECA may file collectively non-traffic sensitive, traffic sensitive, special access and/or billing and collection revenue and revenue requirement computations and/or tariffs.

**Q. WILL YOU EXPLAIN THE WECA FILING AS YOU UNDERSTAND IT?**

A. The individual member companies submitted figures to WECA, and WECA prepared a joint filing. The rate set for NTS common line access charges in this filing is a pooled rate. Each member company concurs in charging that tariffed NTS access rate.

The USF tariffed rate is collected on all Washington state originating and terminating minutes of use by the local exchange companies and paid to WECA. WECA then distributes the USF fund to WECA member companies that have average loop cost greater than 115 percent of the state average loop cost.

**Q. WERE YOU INSTRUCTED TO MAKE AN ACCOUNTING EXAMINATION OF THE TARIFF FILING OF THE WASHINGTON EXCHANGE CARRIER ASSOCIATION IN DOCKET NUMBER UT-971140?**

A. Yes, I have been instructed to review this filing and to determine the revenue requirement of the WECA companies. I have also been instructed to make a recommendation for tariff rates for access charges for the Carrier Common Line Charge and the Universal Service Fund.

## III. SUMMARY OF FINDINGS AND RECOMMENDATIONS

**Q. WILL YOU SUMMARIZE YOUR FINDINGS AND RECOMMENDATIONS FOR THIS FILING?**

A. Yes, my findings are that the Washington Exchange Carrier Association companies experienced excess revenues of $ 9,598,642. Exhibit C___(MLT C-7) page 20 of 20, line 11, column C. I am recommending that:

- The Universal Service Fund access rate be filed as $0.00147.
- I am recommending the access rate for 1998 for Premium Terminating rate be $0.04182;
- The Non-premium Terminating rate be $0.02091,
- The Premium Originating rate be $0.0100 and
- The Non-premium Originating rate be $0.005.

The comparison of these different rates is shown on Exhibit C-___(MLT C-3) lines 11 thru 15. This exhibit shows a comparison of the proposed staff, proposed company and current rates.

## A. STAFF'S REVIEW AND METHODOLOGY

**Q. WHAT DID YOU REVIEW IN THE COURSE OF YOUR EXAMINATION?**

A. Staff has reviewed the Washington Exchange Carrier Association proposed revisions to its Tariff WN U-1, the workpapers supporting the filing, responses to data requests, cost studies provided to the National Exchange Carrier Association for actual 1996 and projected 1997, data collected by the National Exchange Carrier Association for the last 10 years, the incomplete financial reports filed with this Commission by the WECA member companies for last ten years, workpapers, and testimony filed by each of the WECA member companies in support of the filing.

The staff audited each company's calculations of these NTS access charges. The staff then based its calculations beginning with each company's total state results of operations taken from the National Exchange Carrier Association's (NECA) actual 1996 cost studies (part 36 and 69). The staff then removed from the rate base expenses, and revenue requirement items that are included in the federal cost studies, but are not allowed for state rate-making purposes. The commission staff then made adjustments to depreciation expense, to accounts 6710 and 6720, and to allocations.

The WECA companies based the filing on projected 1997 results of operations. The staff did not receive adequate support to audit the projected 1997 results and concluded that they were incomplete. The projection included increases in expenses and rate base but did not adjust revenues for growth or productivity. Without support for the accuracy of such a projection the staff used actual 1996 data. The actual 1997 data was not available.

**B. ACCESS TO DATA TO AUDIT FILING**

**Q. HAVE YOU EXPERIENCED ANY DIFFICULTIES IN COMPLETING YOUR INVESTIGATION?**

A. Yes. The Order in Cause No. U85-23, et al., Eighteenth Supplemental Order page 6, in the summary of the Commission Order item 7, the Commission states:

> All filings should be accompanied by sufficient work papers to allow full analysis by the Commission staff.

The filing in this case was not accompanied by sufficient work papers to allow full analysis by the Commission staff. Therefore, in August 1996, shortly after receiving the filing, staff submitted written questions to WECA through its legal counsel, Mr. Richard A. Finnigan. Although data and information were provided in response to staff's questions, the data was made available for staff's review only at the offices of the Washington Independent Telephone Association (WITA) and staff was not allowed to make copies of any data, nor to remove any copies from the premises. It was also staff's understanding at that time that the conditions of reviewing the data prohibited staff from entering the data into laptop computers while at the WITA offices. Obviously, these conditions delayed our ability to process and analyze the information efficiently.

After the filing was suspended, staff submitted formal data requests to WECA, allowing a liberal interpretation of the response time to allow copies of the requests to be sent out to the individual companies, and for responses to be submitted and compiled by WECA's attorney, Mr. Finnigan. Responses from some of the companies came in fairly promptly, but others did not. After the intervention of individual companies, some represented by Mr. Finnigan and some represented by Mr. Robert S. Snyder, we requested the responses through the company's attorney. Most responses from the companies represented by Mr. Snyder were not received until January 21, 1998, and some were not received until later. In addition, the companies all refused to provide the interstate data requested in the data requests, instead filing objections to those questions. After a motion was filed to compel responses, we reached an agreement whereby the information would be made available for our review at Mr. Finnigan's offices. The National Exchange Carrier Association cost studies were only allowed to be reviewed in Mr. Finnigan's office during his working hours. During the month of March, Mr. Finnigan did allow the staff the opportunity to bring some of the studies to the Commission office as long as they were picked up at his office each morning and returned by 4:30 the same day. If we could not contact Mr. Finnigan on a given day because he was not in the office, or we could not anticipate on an earlier day what studies we wished to review, the data was not made available. We have continued to receive updated and supplemental responses to data requests, including responses from several of the companies represented by Mr. Snyder, received on April 6, 1998.

## IV. EXPLANATION OF EXHIBIT C-___ (MLT C-2), CALCULATION OF USF & NTS RATES

**Q. HAVE YOU PREPARED EXHIBITS SIMILAR TO EXHIBIT C- ____(CP C-2), WECA'S CALCULATION OF THE USF AND NTS RATES?**

A. Yes, Exhibit C-___(MLT C-2) is entitled "WASHINGTON EXCHANGE CARRIER ASSOCIATION; CALCULATION OF USF AND NTS RATES; TWELVE MONTHS ENDING DECEMBER 31, 1996".

Column A lists the access line count for each of the companies as of December 31, 1996. These amounts are taken from Mr. Craig Phillips' Exhibit C-____(CP C-2).

Columns B, C, D, E, and F are taken from the same exhibit of Mr. Phillips except for lines 5, 7, 8, 10, 14, 15, 17, and 19. The access minutes for these lines are taken from a letter dated March 12, 1998 from Mr. Richard A. Finnigan to Ms. Mary Tennyson, Senior Assistant Attorney General. This letter is attached as Exhibit C-___(MLT C-9). Exhibit C-___(MLT C-9) clearly indicates the 1997 reported minutes of use for Hood Canal, Kalama, Lewis River, McDaniel, St. John, Tenino, Western Wahkiakum and Yelm had been understated. A review of this exhibit by comparing the "1997 reported access MOU" with the "MOU per 1997 tariff projection" it is apparent that the "MOU per 1997 tariff projection" are understated for the companies listed above. The companies used the "MOU per 1997 tariff projections" in calculating the rates proposed in the filing. As can be seen from Exhibit C-___(MLT C-9) Tenino's 1997 projected MOU are _______ minutes less than the 1997 reported minutes. By making this adjustment the staff is sending the message to more accurately report minutes in this filing. The effect of understating the minutes of use in the filing would be to require rates to be set at a higher level to recover the revenue requirement of the companies.

I have used the 1997 actual minutes of use for those companies listed above as provided by the above mentioned letter from Mr Richard A. Finnigan.

## A. USE OF 1997 ACTUAL MINUTES OF USE

**Q. WHY HAVE YOU USED THE 1997 MINUTES OF USE?**

A. I have used the 1997 minutes of use because they best represent what the rates filed in this case will generate. After reviewing the 1997 minutes use I have found many discrepancies in minutes reported to the commission. The 1997 minutes of use also reflect the changes in minutes of use caused by GTE and United becoming Primary Toll Carriers. Because of the transition into competition the minutes of use are constantly changing. ELI and MFS are now providing toll services. US WEST claims the loss of minutes of use because of dial around. Because of the potential difficulty of matching 1996 results of operations with 1997 minutes of use I will provide the 1996 minutes of use. I have not been able to verify the 1996 minutes of use and am not certain that they have been adjusted for Extended Area Services changes, optional calling plans and the new Primary Toll Carriers we have as of April 6, 1998.

**Q. PLEASE LIST THE 1996 MINUTES OF USE OF EACH OF THE COMPANIES.**

A.
Asotin
Cowiche
Ellensburg
Hat Island
Hood Canal
Inland
Kalama
Lewis River
Mashell
McDaniel
PTI
Pend Oreille
Pioneer
St. John
Tenino
Toledo
Western Wahkiakum
Whidbey
Yelm

ELI
GTE-NW
United
US WEST

MFS

## B. USE OF INTERSTATE ALLOCATION FACTOR

**Q. PLEASE CONTINUE YOUR EXPLANATION OF EXHIBIT C-___(MLT C-2).**

A. Column G is the Intrastate Non-Traffic Sensitive revenue requirement for the Common Line Charge taken from my Exhibit C-___(MLT C-5) Column K line 11. This column is calculated using the interstate allocation factor for part 36 and 69.

**Q. WHY HAVE YOU USED THE INTERSTATE ALLOCATION FACTOR FOR THE INTRASTATE CALCULATION OF THE CCL AND NTS RATES?**

A. I used the interstate allocation factor for the intrastate factors for the following reasons:

1) The order in U-85-23 stated that the "availability of the local loop to interexchange companies is an asset equal in value to interstate carriers as it is to intrastate carriers."

2) The WECA companies have had twelve years to transition to the interstate factor and have not done so.

3) The allocation of interstate and intrastate allocations used by the WECA companies could result in allocating the same expenses to interstate and intrastate, thus the same expenses could be recovered twice, once by interstate rates and second by the intrastate rates.

4) The U85-23 Order states that: "Where the said charges vary from those approved by the FCC, the LECS should be prepared to justify the variance." This filing does not justify the variance from the approved FCC procedures.

5) The interstate factors use Part 36 and 69 and are approved by the FCC.

**Q. WILL YOU CONTINUE YOUR EXPLANATION OF EXHIBIT C-___(MLT C-2)?**

A. Column H is the amount in Column G divided by the access lines in column A divided by twelve (12) months.

Column I, entitled "USF REQUIREMENT" is the intrastate Universal Service Fund requirement. It is calculated by taking Column H, monthly loop cost, minus 115% of the state wide average loop cost(column H line 30) times the number of access lines, Column A, times twelve (12). The amount shown in Column I line 30 of $9,685,334 is to be recovered through the Universal Service Fund rate element.

Column J displays the residual revenue requirement of $16,038,879 to be recovered through the carrier common line element.

## C. CALCULATION OF USF RATES

**Q. HOW IS THE PROPOSED ACCESS RATE FOR THE UNIVERSAL SERVICE FUND CALCULATED?**

A. The Universal Service Fund rate element is calculated by adding the budgeted administrative costs to the USF revenue requirement and dividing by the total statewide access minutes. The administrative cost of $235,000 is shown on line 18 of my Exhibit C-_____(MLT C-3). The calculation of the rate of $0.00147 is shown on Exhibit C-___(MLT C-4) line 19.

**D. CALCULATION OF CCL RATES**

**Q. HOW ARE THE PROPOSED ACCESS RATES FOR THE COMMON LINE CHARGE CALCULATED?**

A. The staff has used the method testified to by Mr. Phillips, the WECA administrator who prepared the tariff filing. The proposed access rates are Premium Terminating, Non-premium Terminating, Premium Originating, and Non-premium Originating. The originating rates are set at one cent per minute for premium originating minutes and 0.5 cents per minute for non-premium originating minutes as proposed by WECA in the filing. The non-premium terminating rate is fifty percent of the premium terminating rate.

The premium terminating rate is calculated by taking the summation of the WECA Total Residual Common Line Charge revenue requirement Exhibit C-___(MLT C-2) line 21 column J of $16,038,879 less the premium originating revenues Exhibit C-___(MLT C-4) line 15 of $3,317,711 less the non-premium revenue Exhibit C-___(MLT C-4) line 16 of $9,115 and divided by the total state terminating equivalent minutes of use Exhibit C-___(MLT C-3) line 5 of 3,743,125,000 ((000) have been omitted on the exhibit). The proposed premium terminating rate is 0.04182 cents per minute Exhibit C-____(MLT C-4) line 3.

**Q. HOW IS YOUR CALCULATION OF THE PROPOSED ACCESS RATES DIFFERENT THAN THE CALCULATION PRESENTED BY WECA?**

A. The staff's calculation differs from the company's in the following areas:

- Mirrored FCC allocations
- Adjusted minutes of use

•Used 1996 actual results of operations

•Adjusted Depreciation Expense

•Adjusted Accounts 6710 and 6720

•Adjusted McDaniel Telephone Company from average schedule to cost study

•Did not make an adjustment to USF rate for capping the CCL revenue requirement

•Adjusted the rate of return to 10.3 per cent

**Q. IS YOUR CALCULATION OF THE RATES SET FORTH IN THIS DOCKET IN CONFORMANCE WITH THE INTENDED REQUIREMENTS OF THE COMMISSION ORDER IN DOCKET NO. U-85-23?**

A. Yes. The Order in Cause No. U85-23, et al. Eighteenth Supplemental Order page 5 item 3, states the following:

> The Commission adopts an allocation of NTS costs based upon a division of 50 percent to local exchange services, 25 percent to interstate toll and 25 percent to intrastate toll.

On page 20 and 21 of the same order the following is stated:

> The availability of the local loop to interexchange companies is an asset equal in value to interstate carriers as it is to intrastate carriers. An allocation of NTS costs 50 percent to local exchange, 25 percent to interstate toll, and 25 percent to intrastate toll, as proposed by Commission staff is reasonable.

The Washington Exchange Carrier Association has not filed this tariff based on the direction of the Commission. The intent of the Commission was to mirror the Federal Communications Commission's directive in allocating non-traffic sensitive costs. My testimony and exhibits have allocated the intrastate non-traffic sensitive cost as directed by this Commission by mirroring the allocation of interstate non-traffic sensitive cost using Part 69 of the Code of Federal Regulations. The Commission in its Eighteenth Supplemental Order in U85-23, page 22, states the following:

> 17. It is appropriate for each LEC to file intrastate Traffic Sensitive Access Charges and Special Access charges using FCC Part 67 and 69 allocations procedures. Where said charges vary from those approved by the FCC, the LECs should be prepared to justify the variance.

Part 67 was changed to Part 36 after the signing of the Order in U85-23.

**Q. ARE THERE VARIANCES IN THE WECA FILING, FROM THE METHODS REQUIRED BY THE ORDER IN U 85-23?**

A. There are variances in the WECA filing, from the methods required by the order in U85-23. One area the companies are not in compliance with the order is stated in Mr. Phillips' testimony page 6 beginning on line 12; "...the exception of capping the amount of CCL revenue requirement at a 25% allocator and assigning the difference to the USF rate element". The WECA companies have been directed by the Commission to have the access charge allocations mirror the Interstate allocations. The intrastate access charges allocations do not mirror the interstate allocations. I have made this adjustment to mirror the interstate allocations. The WECA companies have not transitioned to the interstate allocations even though it has been twelve years since the Commission published the Order in U85-23. The Washington Exchange Carrier Association's filing does not state or justify the variances.

## V. CALCULATION OF NTS REVENUE REQUIREMENT

**Q. DOES YOUR EXHIBIT C-___(MLT C-5) ENTITLED "WASHINGTON EXCHANGE CARRIER ASSOCIATION; CALCULATION OF NTS REVENUE REQUIREMENT; TWELVE MONTHS ENDING DECEMBER 31, 1996"**

**SUPPORT YOUR CALCULATION OF COLUMN G HEADED "1996 NTS REV. REQ. CCL" OF EXHIBIT C-___(MLT C-2) ENTITLED "WASHINGTON EXCHANGE CARRIER ASSOCIATION; CALCULATION OF USF AND NTS RATES; TWELVE MONTHS ENDING DECEMBER 31, 1996"?**

A. Yes, Exhibit C-___(MLT-C-5) is a twenty (20) page exhibit which shows the calculation of the Washington intrastate non-traffic sensitive carrier common line revenue requirement for each of the companies. Page 20, line 11, column K is the total for all of the companies.

Column B is the 1996 actual results of operation for each company taken from cost studies the companies provided to the National Exchange Carrier Association as support for their 1996 actual interstate carrier common line charge.

Column C is the adjustments the staff made to the 1996 actual results of operation for known and measurable changes. These adjustment include

1) removing Working Capital from the Rate Base,

2) removing Material and Supplies from the rate base,

3) adjustments to federal income taxes to reflect the 35 percent rate,

4) removing excess salary and associated expenses from results of operations,

5) increasing the depreciation expense relating to the Commission Order in UT-961195,

6) removing expenses that are not allowed for rate-making in Washington state,

7) removing revenues that are not allowed for rate-making in Washington state,

8) removing Plant Under Construction from the rate base,

9) removing Customer Deposits from the rate base,

10) removing Allowance for Funds Used During Construction from determination of Revenue Requirement, and

11) removing non-operating expenses and rate base items from the results of operations.

Column D is the sum of Columns B and C resulting in the 1996 actual results of operations after adjustments.

Column E contains the allocation factors used for determining the interstate toll results of operations using Part 36.

Column F is Column B times Column E. Column F is the actual 1996 interstate toll results of operations using Part 36.

Column G is Column E times Column C. Column G is the interstate portion of the adjustments in Column C.

Column H is Column F plus Column G. Column H is the adjusted 1996 interstate toll results of operations.

Column I is Column D less Column H. Column I is the adjusted 1996 intrastate results of operations.

Column J is the allocation factors used for determining the interstate carrier common line charge. I used the interstate allocation factor as a surrogate for the intrastate allocation factor by mirroring the FCC allocations. These factors were developed using the Code of Federal Regulations Part 36 and 69.

Column K is the product of multiplying Column H by Column J. Column K is the adjusted Washington intrastate carrier common line charge revenue requirement using 10.3 percent rate of return. The amount on line 11 of Column K is the support for the amount shown on Exhibit C-__(MLT C-2) Column G.

## VI. DESCRIPTION OF ADJUSTMENTS

### A. ADJUSTMENT TO CONVERT McDANIEL TELEPHONE CO. TO COST STUDY BASIS

**Q. HAVE YOU MADE ANY OTHER ADJUSTMENTS FOR PURPOSES OF THIS FILING?**

A. Yes. McDaniel Telephone Company reports to the NECA as an average schedule company instead of submitting cost studies for Part 36 and 69. The FCC defined average schedule companies as telephone companies that participated in average schedule settlements on December 1, 1982. The Commission maintained the average schedule status of these independent local exchange companies(ILEC) based on the assumption that these small carriers lacked sufficient financial resources or expertise to justify a requirement that they perform jurisdictionally separated cost studies (FCC Docket DA 962008, paragraphs 3 and 4). In McDaniel's case, the company was purchased in 1994 by Telephone and Data Systems, Inc. (TDS), which performs jurisdictional cost studies for other LECS that it owns, including Lewis River and Asotin. Therefore, I have concluded that McDaniel is capable of filing cost studies. I have adjusted the NTS and USF calculation for McDaniel as if it filed cost studies.

## B. RATE OF RETURN ADJUSTED TO 10.3 PERCENT

**Q. HOW WAS THE 10.3 PERCENT RATE OF RETURN USED IN COLUMN K DETERMINED?**

A. For purposes of the WECA filing, staff and WECA have agreed to the use of a rate of return of 10.3 percent. This number was arrived at by looking at PTI's capital structure and cost of debt and determining a reasonable return on equity. PTI filed its analysis, staff reviewed it and the company updated the numbers based on discussions with the staff.

## C. WORKING CAPITAL REMOVED FROM RATE BASE

**Q. WHY DID YOU REMOVE WORKING CAPITAL FROM THE RATE BASE?**

A. Most of the companies removed this item from the rate base in their state cost studies. Since I started with the Federal cost studies I had to remove this item. If the companies provided a study to support this item in the rate base and the study was found to be correct this item would be placed in the rate base. The addition of this item in the rate base has no effect on rates proposed by the staff in this filing. If a company files for a review of its results of operations this item will be audited.

**Q. WHY DID YOU REMOVE MATERIAL AND SUPPLIES FROM THE RATE BASE?**

A. The Commission has never allowed Material and Supplies as a component of the rate base. Most of the companies had only included this component in the Federal studies but removed them from the State studies. Since I began with the Federal studies I had to remove this item.

**D. ADJUSTMENT TO FEDERAL INCOME TAX**

**Q. HOW DID YOU ADJUST FEDERAL INCOME TAXES FOR THIS FILING?**

A. I adjusted each company's results of operations for the composite tax of 35 percent. The companies used different rates in different jurisdictions. I held the Federal Income Tax rate constant in all jurisdictions.

**E. ADJUSTMENTS TO SALARY AND ADMINISTRATIVE EXPENSES**

**Q. YOU MADE ADJUSTMENTS TO REMOVE EXCESS SALARY AND ASSOCIATED EXPENSES, WILL YOU NOW EXPLAIN THOSE ADJUSTMENTS?**

A. Yes. In previous Washington Exchange Carrier Association tariff filings the staff removed from results of operations excess salaries for Whidbey Telephone Company and Inland Telephone Company. In this case the staff reviewed the expenses in Accounts 6710 and 6720 for each of the companies represented by the Washington Exchange Carrier Association. This included a review of a document obtained from the National Exchange Carrier Association. The document is entitled "Universal Service Fund 1997 Data Collection Instructions". The date of the document is May 1997. The data required for this document is the unseparated regulated amounts, i.e., state and interstate actual or calculated amounts as of the end-of-period and is in accordance with FCC Rules. The data collection period is the twelve months ending December 31, 1996. I reviewed Accounts 6710 and 6720 from this document.

Account 6710 is executive and planning expenses. It also includes Payroll Benefits of executive and planning salaries expense. Account 6720 is general and administrative expense and includes payroll benefits of general and administrative salaries expense. An adjustment was made to reduce the expenses in accounts 6710 and 6720 for the companies which had above average expenses in these accounts.

**Q. HAVE YOU PREPARED AN EXHIBIT SHOWING YOUR CALCULATION FOR THIS ADJUSTMENT?**

A. Yes. Exhibit C-__(MLT C-6) is entitled; "Washington Exchange Carrier Association; Adjustment to Accounts 6710 and 6720."

This exhibit has a list of the companies included in this Docket UT-971140. I have grouped the companies according to their number of access lines, in the following categories; 1)100,000 to 499,999 access lines; 2) 20,000 to 49,999 access lines; 3) 10,000 to 19,999 access lines; 4)1,000 to 4,999 access lines; 5) 500 to 999 access lines; and 6) 0 to 499 access lines.

Once the companies were grouped, I calculated from the NECA report the national average expense per loop per month for Accounts 6710 and 6720 for each group. This nationwide average was then compared to each Washington state company's average expense for these accounts as provided in the 1996 NECA cost studies.

The adjustment for each account was calculated by subtracting the individual company average loop cost from the national average loop cost and multiplying by the 1996 loops times 12. The adjustment is made when the company average loop cost exceeds the national average loop cost in each category. This adjustment is consistent with similar adjustments made in previous access charge filing for excess salaries and benefits.

**Q. WHY DID YOU USE EACH COMPANY'S ACCESS LINES FOR COMPARISON?**

A. The use of access lines reflects the size of the companies in relation to the number of customers served. A better way to make a comparison, in the future, may be to use the total corporate access lines for those companies that are affiliated with other companies. One purported benefit of corporate buy out and mergers is that a larger company can benefit from increased efficiency, and reduce overhead. When a company is merged into a larger system, normally the overhead and executive compensation expense is reduced.

**Q. FROM YOUR ANALYSIS OF THIS WORK SHEET WHY HAVE YOU RECOMMENDED AN ADJUSTMENT TO REDUCE EXPENSES IN ACCOUNTS 6710 AND 6720?**

A. This study supports the wage adjustments made in other WECA filings for Inland Telephone Company and Whidbey Telephone Company. It also demonstrates that other company's salaries are excessive.

Telephone Utilities of Washington's average loop cost for Account 6710 (executive compensation) is 107 percent greater than the national average for similar group companies for this account.

I find it disturbing that Whidbey's average loop cost per customer/access line/per month for Account 6710 is $____ while the national average cost for this account for similarly grouped companies is only $2.16. This is an enormous amount of cost for executive compensation compared with the average costs for companies serving similar number of access lines.

Mashell's average loop cost for Account 6710 is ____ Toledo's is $____, Western Wahkiakum's is $____ and Hood Canal's is $_____while the national average cost for this account for similarly grouped companies is only $5.86.

St. John's average loop cost for Account 6710 is $____ while the national average cost for this account for similar grouped companies is only $8.45.

I also find it incredible that Inland's average loop cost/customer/access line/month for Account 6720 (general and administrative expenses) is $____, Toledo's is $____, Western Wahkiakum's is $____, and Hood Canal's is $____ while the national average cost for this account for similarly grouped companies is only $11.01. Making an adjustment to disallow these expenses that exceed the average cost for similar sized companies is a fair way of making sure that companies do not take advantage of their customers by paying excessive amounts to their executives or inflating their overhead expenses.

## F. ADJUSTMENT TO DEPRECIATION EXPENSES

**Q. DO YOU HAVE A RECOMMENDATION TO MODIFY THIS ADJUSTMENT IF THE COMMISSION DOES NOT AGREE WITH YOUR APPROACH?**

A. Another approach for making a salary adjustment would be to not make an adjustment if the individual company cost/access line/month is within twenty five percent of the national average.

**Q. WILL YOU EXPLAIN YOUR ADJUSTMENT TO INCREASE THE DEPRECIATION EXPENSE?**

A. Yes. In Docket UT-961195, Order Granting Petition for Depreciation Accounting Standards, October 25, 1996, on page 4 states the following findings:

> 2. The use of ceiling rates for small companies is appropriate because small companies lack the resources to preform detailed remaining life depreciation studies such as those required of larger companies. Despite this lack of remaining life depreciation studies, it is important that depreciation rates and reserves reflect the economic value of plant; this could not be accomplished if identical rates were established for all companies.
>
> 3. It appears, upon investigation, that the petition is reasonable and consistent with the public interest and should therefore be granted.

I have increased the depreciation expense for each company to the level of the NECA projected 1997 level so this increased depreciation expense could be recognized in this filing.

## G. ADJUSTMENTS TO RATEMAKING EXPENSES

**Q. WHY DID YOU REMOVE EXPENSES THAT ARE NOT ALLOWED FOR RATE-MAKING IN WASHINGTON STATE?**

A. The companies removed these expenses in their WECA cost studies. Since I used NECA cost studies that included these expenses, I removed the expenses to be consistent with the companies' WECA cost studies. These types of expenses have not been traditionally included in results of operations in this state. I did not identify all of these expenses but one such item was contributions. This Commission has determined that contributions should not be included for rate-making purposes in this state.

**Q. WHY DID YOU MAKE ADJUSTMENTS TO TOTAL REVENUE REQUIREMENTS?**

A. I made adjustments to the revenue requirements to be consistent with the adjustments the companies made to the WECA cost studies. WECA had made these adjustments to revenues so the studies would be consistent with the Washington commission rate-making in previous filings.

**Q. WHY DID YOU REMOVE PLANT UNDER CONSTRUCTION FROM THE RATE BASE?**

A. I removed this item from the rate base to be consistent with the WECA cost studies. Also the Commission has determined that, for state rate-making purposes, plant under construction should not be included in rate base.

**Q. WHY DID YOU REMOVE CUSTOMER DEPOSITS FROM THE RATE BASE?**

A. This should only be included in the rate base after an evaluation of the investor supplied working capital calculation has been made. Since I did not evaluate the study and most companies did not request this item in the rate base I removed it so all the companies would be treated consistently.

**Q. WHY DID YOU REMOVE ALLOWANCE FOR FUNDS USED DURING CONSTRUCTION FROM THE DETERMINATION OF THE REVENUE REQUIREMENT?**

A. This should only be used in the determination of revenue requirement if plant under construction is included in the rate base. I did not include plant under construction in the rate base so it would be inappropriate to include the allowance for funds used during construction.

**Q. YOU ALSO STATE THAT YOU MADE ADJUSTMENTS TO REMOVE NON OPERATING EXPENSES AND RATE BASE ITEMS FROM THE RESULTS OF OPERATIONS, IS THAT CORRECT?**

A. Yes. The WECA studies have adjustments not included in the NECA studies. The purpose of the adjustments made by WECA is so the WECA studies are consistent with Washington rate-making theory. I have made these same adjustments to the NECA studies.

**CALCULATION OF WASHINGTON INTRASTATE EARNINGS IN EXCESS OF 10.3 PERCENT**

**Q. HAVE YOU PREPARED AN EXHIBIT WHICH SHOWS YOUR CALCULATION OF THE WASHINGTON INTRASTATE EARNINGS IN EXCESS OF 10.3%?**

A. Yes. Exhibit C-__(MLT C-7) is entitled; "Washington Exchange Carrier Association; Calculation of Excess Earnings @ 10.3%". This is a twenty (20) page exhibit which illustrates the earnings in excess of 10.3% for each of the companies. Page 20 of this exhibit shows the aggregate excess earnings $9,598,642 for all of the companies.

Column A is the description for each line. Column B is the Washington Intrastate adjusted results of operations. This column is taken from Exhibit C-___(MLT C-5) column I.

Column C is the difference between column B and D.

Column D adjusted line 2 entitled "Rate of Return" to 10.3 percent. The column reflects the effects on each line associated with the change in the rate of return.

**Q. HAVE YOU MADE AN ADJUSTMENT TO REMOVE PAY PHONE INVESTMENT, EXPENSES AND ASSOCIATED REVENUES FROM THE RESULTS OF OPERATIONS?**

A. No. I have not been able to identify the pay phone items for each company so such an adjustment could be made. This adjustment needs to be made so the WECA companies will be in compliance with the Federal Communications Commission. The staff does not want to appear to disagree with the FCC on this matter, so states that the adjustment to remove pay phone results of operations is a required adjustment.

**Q. PLEASE EXPLAIN YOUR EXHIBIT C__(MLT C-8) ENTITLED "WASHINGTON EXCHANGE CARRIER ASSOCIATION; COMPARISON OF STAFF AND COMPANY; TWELVE MONTHS ENDING DECEMBER 31, 1996".**

A. Column A of this exhibit lists each of the companies.

Column B is the revenue to be collected by each company using the staff proposed USF rate.

Column C is the revenue to be collected by each company using the staff proposed CCL rate.

Column D is the revenue to be collected by each company using the company proposed USF rate.

Column E is the revenue to be collected by each company using the company proposed CCL rate.

Column F is the difference for each company between the staff and company proposed USF rates.

Column G is the difference for each company between the staff and company proposed CCL rates.

**Q. HAVE NEGOTIATIONS FOR A SETTLEMENT OF THIS FILING BEEN COMPLETED?**

A. No. The staff and companies are still working on a settlement as of the filing of this testimony.

**Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

A. Yes.