BEFORE THE NEBRASKA PUBLIC SERVICE COMMISSION

In the Matter of the Application of Northwestern Bell Telephone Company, Omaha, Nebraska, for authority to adjust its rates and charges for telephone service in the State of Nebraska.	Application No. C-227 GRANTED IN PART Entered: January 11, 1983

APPEARANCES: For the applicant
Richard L. Johnson, Attorney
100 South 19th Street
Omaha, Nebraska

For the Commission
Shanler Cronk, Attorney
2115 State Capitol Building
Lincoln, Nebraska

OPINION AND FINDINGS

BY THE COMMISSION:

By its application filed January 22, 1982, Northwestern Bell Telephone Company, Omaha, Nebraska, seeks authority to adjust its rates and charges for telephone service furnished by it in the State of Nebraska.

Notice of the filing was published on January 27, 1982, and on May 19, 1982, pursuant to the provisions of the Commission's Rules and Regulations. On May 19, 1982, the Commission sent a letter of notification to all Mayors, community clubs and newpapers in the area served by Northwestern Bell advising that the application had been filed and that the increase requested was $42,700,000. A Petition for Leave to Intervene in this application was filed by the Secretary of Defense. Over 2,000 letters of protest and petitions opposing the application were received from throughout the State.

In accordance with policies adopted by this Commission in 1974, a Staff Attorney was assigned to prepare and present the staff case at the hearing. This was done to insure that the Commission would receive all relevant and material evidence on the record, where it would be subject to cross-examination testing its truthfulness. The assigned Staff Attorney was isolated from the decision-making process and placed in the same status as other participants of record. He, as the applicant, presented evidence through witnesses on the record, cross-examined other witnesses and submitted a brief.

Pursuant to notice required by law, public hearing was held on the application on September 15, 16, 17, 20 and 21, 1982 in the Board of Equalization Room, City-County Building, Omaha, Nebraska, with appearances as set forth above.

Additional public hearings were held in Grand Island, Nebraska on September 23, 1982, Ogallala, Nebraska September 30, 1982, O'Neill, Nebraska on October 7, 1982, Tekemah, Nebraska on October 18, 1982, and again in Grand Island, Nebraska on October 26, 1982.

Upon consideration of the application the evidence adduced at the hearings and being fully advised, the Commission is of the opinion and finds that:

GENERAL

1. The Applicant is a corporation existing under the laws of the State of Iowa with its general operating headquarters at Omaha, Nebraska. It is a common carrier furnishing general communications services in Nebraska, Iowa, Minnesota, North Dakota and South Dakota, and is under the jurisdiction of this Commission.

2. Applicant furnishes local and long distance service at 95 telephone exchanges in Nebraska serving approximately 760,000 company-owned telephones and provides long distance connections to 359 exchanges of other telephone companies in the State.

3. The rates and charges of the applicant now in effect were approved by this Commission in its order entered October 20, 1981, in Application C-116.

4. Applicant alleges that its earnings are inadequate and do not provide a fair and reasonable rate of return on its property in Nebraska devoted to intrastate business. Applicant seeks to increase rates in revised amount to produce additional annual revenue of $42,377,321 to Northwestern Bell Telephone Company.

5. Applicant further alleges that it requires a rate of return of 13.5% on its property devoted to intrastate service in the State of Nebraska.

6. For the purpose of determining the results of operations, both applicant and staff have used a test year ending December 31, 1981 and an end of period rate base. Intrastate revenues, expenses and investments were determined in accordance with the NARUC Separations Manual in effect on December 31, 1981.

7. Applicant has included in its testimony the effects of the expensing of station connections. This Commission has in separate proceedings required the continued capitalization of station connections.

RATE BASE

8. Applicant's exhibits reflect its rate base as of December 31, 1981 to be $310,283,807 consisting of the following:

Book Cost of Plant and Equipment	$442,633,858
Materials and Supplies	2,649,022
Working Capital	2,513,248
	$447,796,128
Less: Long Term Plant Under Construction	3,331,380
Depreciation Reserve	85,445,044
Deferred Tax Reserve	46,633,774
Plus Unamortized Portion of Interest During Construction	667,553
Less Capital Recovery Items	2,769,676
	$310,283,807

9. Staff originally proposed seven adjustments to this rate base, however the staff has withdrawn its proposed adjustment relating to equal life group depreciation. The remaining six adjustments are:

a.	Furniture expensed which should have been capitalized	$ 8,369
b.	To disallow working capital	(2,614,248)
c.	To disallow pre-1971 investment tax credit	(576,543)

d.	To reflect capitalization of station connections	$ 2,323,543
e.	To disallow unamortized interest during construction	(667,553)
f.	To disallow short-term plant under construction	(6,949,872)

The foregoing adjustments reduce applicant's rate base by $8,476,221 to $301,807,586.

10. Staff witness, Daniel Selby, presented testimony and an exhibit (#46) concerning the company's need for working capital which indicates that applicant's corporate balance sheet contains no investor supplied funds which are not already earning a return. Applicant has developed its working capital using a formula developed in A-31200 including lead-lag studies. While this formula is appropriate to determine the amount of working capital to be allowed, it still must be demonstrated that any working capital allowance is necessary. The staff adjustment is accepted.

11. Pre-1971 investment tax credit should be disallowed as proposed by the staff. This treatment is consistent with that adopted in other recent cases.

12. In application No. C-33605, applicant and the staff stipulated that a rate base adjustment should be made to include interest during construction from January 1, 1979 through April, 1980. The purpose for this adjustment was to allow the company to earn a return on its short term construction investment until such time as that investment could be included in the rate base for rate making purposes. Investors were given adequate notice of the FCC rule change to allow them to consider investment decisions. It should also be pointed out that the FCC rule change did not require any particular intrastate rate base treatment of plant under construction. The staff adjustment is appropriate.

13. Staff has proposed the disallowance of all short term plant under construction. The reason for this proposal was that the balance included in the company's rate base was inaccurate because experience had shown that a considerable number of projects were not actually completed in twelve months and should thus have been classified as long term plant under construction. Applicant's evidence indicates that, of the $6,949,872 classified as short-term plant under construction, only $53,226 will not be put into service within 12 months. An adjustment for these projects is proper and $6,896,646 of short-term plant under construction should be allowed in the rate base.

14. We find that the appropriate rate base to be used in this case is $308,704,232.

RESULTS OF OPERATIONS

15. Applicant's exhibits show intrastate operating income for the year ended December 31, 1981, adjusted for known changes and Capital Recovery items, in the amount of $25,257,249. Adjustments include compensation and benefit changes, amortization of short term interest during construction, the exclusion of tax payments not applicable to the test period, the exclusion of identified expenses related to subsidiary formation, the exclusion of overhead loadings related to the sale of customer premise equipment, the effect of the 1981 rate increase and a state income tax rate adjustment.

16. The staff proposed additional adjustments and found intrastate net operating income to be $30,731,043. This amount is revised to $30,679,987 with the withdrawal by staff of its proposed equal life group depreciation adjustment.

17. Staff proposes and we concur in an adjustment to continue capitalization of station connections, an adjustment increasing net earnings by $1,253,739.

18. Staff proposes and we find reasonable the exclusion of a number of out-of-period and non-ratepayer expenses increasing earnings by $235,591.

19. Staff proposes an adjustment reducing federal income taxes by $1,043,916. Applicant participates in the filing of a consolidated federal income tax return along with AT&T and members of the Bell System. Applicant does, however, record income tax liability on its books as though it filed an individual income tax return. We concur with the Staff proposal however adjustment of the rate base as set forth above changes the depreciation adjustment to $1,168,952.

20. Staff proposes to disallow wage increases included in applicant's operating results which occurred on April 1 and August 8, 1982. The staff adjustment would increase earnings by $1,616,472. We find the staff adjustment reasonable.

21. Staff proposes and we find reasonable the exclusion of a number of non-Nebraska and non-ratepayer expenses increasing earnings by $46,911.

22. Staff proposes and we find reasonable the exclusion of certain advertising, Telephone Pioneer and lobbying expenses, charitable contributions and tuition reimbursements increasing earnings by $139,068.

23. Exclusion of the amortization of short-term interest during construction would reduce expenses by $95,364 and, after taxes, would increase earnings by $48,614. We find this adjustment to be reasonable as previously stated.

24. Staff has proposed that license contract expenditures be limited to 1% of revenues which would increase net earnings by $991,677. Staff contends that this adjustment is appropriate because of the lack of probative evidence supporting the license contract payments, the concern evidenced by the operating companies about the level of expenditures, and their lack of control over such expenditures. We accept the staff adjustment.

25. We find after all of the above adjustments and the tax effect that applicant's net earnings for the year 1981 are $30,805,023.

RATE OF RETURN

26. The evidence indicates that applicant's rate of return for the test year 1981 on its original cost rate base was 9.98%.

27. Rate of return testimony was offered by both the applicant and the Commission staff. Applicant offered the testimony of three witnesses, Dr. Robert L. Johnson, Professor of Finance at the University of South Dakota, Cornelius B. Pryor, Jr., Vice President of Kidder, Peabody & Co. and John L. Trygg, Assistant Treasurer of applicant. Their testimony and recommended cost of equity was 17.5-18.0%. Using the Bell System consolidated capital structure applicant proposed an overall rate of return of 13.37-13.63%.

28. Staff's witness on rate of return, Dr. John W. Wilson, President of J. W. Wilson & Associates, Inc., also used the discounted cash flow model and comparable earnings to determine his recommended cost of equity capital which he found to be 14%. He however used the AT&T corporate capital structure and that of Northwestern Bell to arrive at an overall return for Northwestern Bell of 10.95%. He further adjusted the ratios of equity, preferred stock and debt to arrive at a capital structure applicable to the Nebraska jurisdictional rate base. His resulting overall rate of return is 10.43%.

29. Having duly considered all of the evidence presented, we find that the appropriate capital structure to be used in this proceeding is that of Northwestern Bell Telephone Company as set forth in Dr. Wilson's exhibit, Exhibit No. 17 (J.W. 13 page 3). We find the evidence insufficient to allow the further adjustment of the capital structure proposed by Dr. Wilson. The Commission also finds that it cannot consider the high end of a range in determining the appropriate rate of return, when the Company has not exercised certain cost controls which other businesses and governmental bodies have had to

observe. The salary increases shown in late-filed Exhibit 164 show that Company officials, on average, have received 13% increases during this test year, when the economy is facing umemployment, plant closings, and renegotiated labor contracts. We further find that a reasonable and appropriate return on common equity is 14.09%. This is fair and reasonable and will allow applicant to continue to attract capital. The resulting overall rate of return is 11%.

SERVICE

30. Testimony was presented by Commission Engineer M. G. Hand on the results of central office service tests conducted in twenty of the applicant's exchanges. The percentage of test calls that completed properly from the selected central offices, in general, was good.

31. Information provided by the company revealed that by the end of 1982 sixteen exchanges will still be utilizing operator number identification (ONI). However under the current conversion schedule the remaining exchanges will be converted to automatic number identification (ANI) by July 1984.

32. Trouble indices in two of the company's exchanges exceeded the Commission's objective of 8 reports per 100 stations per month, based on a six month period. The company should file quarterly trouble indices for the Crookston and Litchfield exchange until July 1, 1984 or further order of the Commission.

33. Fifty-two exchanges had repeated trouble report percentages exceeding 15 percent. Of these fifty-two exchanges, nineteen had repeated trouble report percentages exceeding 20 percent. The company should investigate the conditions in the nineteen exchanges where the repeated trouble report percentages exceed 20 percent and make whatever adjustments are required to reduce the repeated reports.

34. Mr. Hand (T-889) testified that the current Commission rules and regulations defines a customer trouble report as any oral or written report from a subscriber relating to a physical defect in the operation of the telephone company's facilities. Mr. Hand feels that in today's environment the number of trouble reports should be related to the number of access lines rather than the number of telephone in service.

CONCLUSION

35. We have found that applicant is entitled to a rate of return of 11% on its rate base. To produce this rate of return will require an increase in revenues of $8,032,684. This increase in revenue will allow applicant to attract capital and will enable it to continue to provide satisfactory telephone service to is Nebraska customers.

36. Applicant should be directed to file with the Commission for its approval a schedule of rates and charges which will produce additional annual revenue of $8,032,684 in accordance with the following directions.

BASIC SERVICE

37. The company proposed an increase of the basic flat rates by amounts ranging from $2.70 to $4.65 per month for residence individual lines, $1.85 to $3.60 per month for residence party line offerings, and $8.15 to $17.45 per month for business individual lines. These proposed rates would raise over $27 million from basic service.

38. The Commission concludes from testimony and protest letters that the proposed basic service increase must be drastically reduce. Local service increases shall be limited to a revenue increase of not more than $1,609,822.

39. It is further directed that in order to reduce the disparity between rate groups, that increases for each class of service shall be the same for all rate groups.

HOURLY RATE PLAN FOR INSIDE WIRE

40. The Company proposes to replace the non-recurring installation charges consisting of wiring, travel, equipment connection, and jack with an hourly charge for work done. The proposal includes a charge for each 15 minute increment. The charge for the first increment would be $18.00 and the charge for each additional increment $9.75. Under this plan, customers would pay only for the work requested, rather than an average flat rate.

41. The Commission agrees with the applicant's proposed hourly rate plan for installation. We believe it will be more easily understood by the customer and be more equitable since those who benefit from the work done will pay the cost. The Commission also agrees to allow customer provided inside wire. We support an optional maintenance charge for inside wire and authorize a charge of $ .35 per month rather than the $ .50 per month proposed by the company.

42. The Commission denies an increase in the charges for the service order and the central office line.

DIRECTORY ASSISTANCE

43. The Company proposed the introduction of a charging plan for calls to its directory assistance operators. The Company's plan provides for three calls to be provided at no charge. Calls over the allowance will be charged 20¢.

44. The Commission finds that this plan to charge for directory assistance service provided to those subscribers who frequently use it is fair and reasonable. However, the Commission orders that the applicant amend the offering to allow 8 calls at no charge, rather than the 3 call allowance that was proposed.

OPERATOR SERVICES

45. The applicant proposes to charge for local operator assistance, busy verify, and interrupt. Local operator assistance would add features such as local credit card calls, a written record of local calls made through the operator, and the added security of being able to call from pay telephone locations, in a remote area for example, without coins.

46. The Commission agrees with the proposed local operator assistance charge and the charge for busy verification and interrupt. No charge, however, shall be applied to the local operator assistance call from a handicapped person, or to or from emergency agencies for local assistance calls, and calls for busy verify and interrupt.

MESSAGE TELEPHONE SERVICE

47. The applicant proposed a restructure of its long distance rates to provide a one minute charge for all calls and an operator charge for all operator handled calls. The Company proposed no increase in long distance message rates.

48. The Commission agrees with the proposed restructure in operator charges but does not agree with the Company's proposal not to increase long distance rates in this application, considering the fact that Nebraska's intrastate rates are substantially under the interstate rates and, having considered the testimony presented by all parties in this case, the Commission concludes that toll revenues should be adjusted to raise an additional $1,774,862. The proposed adjustment will keep basic services as low as possible. Message toll rates shall be increased as well as the Company proposed adjustments on operator services, WATS, and Telpak.

25¢ COIN

49. Applicant has requested the Commission to approve the increase of a local coin telephone call from the present rate of 10¢ to 25¢. This rate would apply to all coin and coinless public telephones and semi-public coin telephones in the Nebraska exchanges served by the applicant.

50. The Commission finds it fair and reasonable to increase the coin telephone rate to 25¢ only in the following locations: airports, bus terminals, hotels and motels.

SUMMARY

51. The following is a list of the approved additional revenues by product or service:

Basic Service	$1,609,822
Hourly Rate Plan	1,621,000
Directory Assistance	1,379,000
Premise Equipment	407,000
Custom Calling and Hunting	891,000
Toll and Operator Services	1,774,862
Coin Telephone Increase at selected Locations	350,000
	$8,032,684

ORDER

IT IS THEREFORE ORDERED by the Nebraska Public Service Commission that Application No. C-227 be and it is hereby granted in part and the Northwestern Bell Telephone Company be and it is hereby authorized to revise its rates and charges to produce additional annual revenue of $8,032,684.

IT IS FURTHER ORDERED that applicant file with the Commission for its approval a schedule of rates and charges that will produce additional annual revenue of $8,032,684 in accordance with the directions specified herein.

IT IS FURTHER ORDERED that applicant's conversion from operator number identification (ONI) to automatic number identification (ANI) be completed by July 1984; the Company file quarterly with the Commission trouble indices for the Crookston and Litchfield exchanges until July 1, 1984 or until further order of this Commission; Northwestern Bell investigate repeated trouble reports and make whatever adjustments are required in each exchange to reduce the repeated report percentage to 20 percent or below; the applicant shall in the future maintain records that will allow the Commission to receive trouble index information which is developed by using the number of access lines rather than the number of stations as the denominator in the trouble index formula.

MADE AND ENTERED at Lincoln, Nebraska this 11th day of January, 1983.

NEBRASKA PUBLIC SERVICE COMMISSION

Harold D. Simpson

Chairman

COMMISSIONERS CONCURRING:

ATTEST:

John E. [illegible]

Executive Secretary

Acting