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U S WEST, Inc.
1801 California Street, Suite 5100
Denver, Colorado 80202
303 672-2791
Facsimile 303 296-4576

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[redacted]

Richard A. Karre
Senior Attorney

September 2, 1997

Mr. William F. Caton
Acting Secretary
Federal Communications Commission
Room 222, SC-1170
1919 M Street, N.W.
Washington, DC 20554

RECEIVED
SEP 2 1997
FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

RE: Request for Confidential Treatment -- CC Docket No. 97-149

Dear Mr. Caton:

Pursuant to 47 C.F.R. Section 0.459 of the Federal Communications Commission's Rules, U S WEST Communications, Inc. hereby requests confidential treatment of Exhibit 10 which has been submitted in response to the Commission's Order Designating Issues for Investigation, CC Docket No. 97-149. This Exhibit is marked "Limited Distribution -- Confidential Information Disclose Solely To Authorized U S WEST Communications Employees Having A Need To Know." A copy of this request has also been delivered to the Chief of the Common Carrier Bureau.

Exhibit 10 contains competitively sensitive information which is used in preparing business forecasts that is not public record. Employees of U S WEST review this information only on a need-to-know basis as it is competitively sensitive. If one of U S WEST's competitors were to obtain access to this information, it would give that competitor an unwarranted competitive advantage.

U S WEST removed Exhibit 10 from the Direct Case, filed September 2, 1997 and a redacted version was submitted in its place. A complete version of U S WEST's Direct Case including Exhibit 10 is attached for your consideration under the Commission's confidentiality rules.

Sincerely,

Richard A. Karre

[redacted]

Richard A. Karre (RV)

c: Acting Head -- Common Carrier Bureau

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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

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In the Matter of	)	
	)	
1997 Annual Access	)	CC Docket No. 97-149
Tariff Filings	)	Transmittal No. 847
	)	
U S WEST Communications, Inc.	)	
Tariff F.C.C. Nos. 4 and 5	)	

DIRECT CASE

James T. Hannon
Richard A. Karre
Suite 700
1020 19th Street, N.W.
Washington, DC 20036
303 672-2860
303-672-2791

Attorneys for

U S WEST COMMUNICATIONS, INC.

Of Counsel,
Dan L. Poole

September 2, 1997

[redacted]

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DIRECT CASE

U S WEST Communications, Inc. ("U S WEST"), through counsel and pursuant to the Federal Communications Commission's ("Commission") Investigation Order,[1] hereby files its Direct Case on Transmittal No. 847, U S WEST's 1997 Annual Access Charge filing.

I. INTRODUCTION AND SUMMARY

On June 27, 1997, the Commission released its 1997 Annual Access Order[2] which suspended local exchange carriers' ("LEC") annual access tariffs for one day and initiated an investigation into the lawfulness of certain aspects of U S WEST's tariff. In a subsequent Order designating issues for investigation,[3] the Commission

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[1] In the Matter of 1997 Annual Access Tariff Filings, CC Docket No. 97-149, Order Designating Issues for Investigation, Memorandum Opinion and Order on Reconsideration, ("Investigation Order" or "Order"), DA 97-1609, rel. July 28, 1997.

[2] In the Matter of 1997 Annual Access Tariff Filings, National Exchange Carrier Association Universal Service Fund and Lifeline Assistance Rates, CC Docket No. 97-149, Transmittal No. 759, Memorandum Opinion and Order, DA 97-1350, rel. June 27, 1997 ("Suspension Order").

[3] Note 1, supra.

raised numerous questions and requested extensive data on the issues that were the focus of its investigation. With respect to U S WEST, these issues focused on development of Subscriber Line Charge ("SLC") and Carrier Common Line ("CCL") rates, including Base Factor Portion ("BFP") and line forecasts, the treatment of Other Billing and Collection ("OB&C") expenses, and equal access exogenous cost adjustments.

The issue that received the most attention by far in the Commission's Investigation Order was that of BFP forecasts. The Commission has requested a huge array of data associated with the BFP and the projection of this variable. As the Commission mentioned in its Suspension Order, the issue of BFP forecasts was first raised in challenges to LECs' price cap filings by AT&T Corp. ("AT&T") and MCI Telecommunications Corporation ("MCI").[4] This is not surprising given the enhanced importance of the BFP as a result of the Commission's recent Access Reform Order which permits higher SLCs on multi-line business lines beginning July 1, 1997.[5]

Prior to the adoption of the Access Reform Order, BFP projections received little attention from either the Commission or interexchange carriers ("IXC") because the $6.00 limit on multi-line business SLCs insured that minor variations in BFP forecasts would have little if any impact on the CCL charge assessed on

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[4] Suspension Order ¶¶ 12-17.

[5] In the Matter of Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Transport Rate Structure and Pricing, End User Common Line Charges, First Report and Order, 7 Comm. Reg. (P&F) 1209, 1234 ¶ 78 (1997), appeals pending sub noms. 97-2618, et al. (8th Cir.) ("Access Reform Order").

carriers. With access reform and higher limits on SLCs for multi-line business customers beginning July 1, 1997, over- or under-forecasting of the BFP will be directly translated into higher or lower multi-line SLCs and CCL charges. The net effect on price cap LECs is zero -- it is only a question of which group (i.e., IXCs or multi-line business customers) common line costs are recovered from -- since the overall common line revenue requirement does not change. As such, price cap LECs have nothing to gain from over- or understating BFP forecasts as some parties implied in their earlier comments. While U S WEST and other LECs have a great interest in ensuring that their BFP forecasts are as accurate as possible since these forecasts will affect customers differently, it should be recognized that it is impossible to evaluate the accuracy of any given BFP forecast until after the end of the tariff year. With the one-day suspension of Transmittal No. 847 and the establishment of an accounting order, payors of both SLCs and CCL charges will be affected back to July 1, 1997 if the Commission prescribes changes in U S WEST's BFP projections. Thus, any prescribed changes in BFP projections will result in both positive and negative retroactive adjustments to SLCs and CCL rates under the existing Accounting Order. In order to avoid such unnecessary impacts on customer rates, U S WEST urges the Commission to accept BFP forecasts as filed.

The other variable which can have an effect on SLC and CCL ratio is the access line forecast. U S WEST demonstrates that its 97/98 forecast is quite reasonable. The Commission should accept the access line forecast as filed.

The Commission has not found it necessary to prescribe a methodology for forecasting BFP and access lines in the past and should not do so now. It appears from the Commission's Investigation Order that it is operating under the impression that the BFP and access lines are variables that can be accurately forecast once historical data is "cleaned-up" to remove the impacts of past rule changes and changes to other variables which affect the BFP. U S WEST does not share this same optimism. BFP is a revenue requirement and as such it is closely intertwined with company budgets[6] and future Commission rule changes. U S WEST does not forecast the BFP by using a historical BFP time series nor does it believe that it is appropriate to do so.[7] Furthermore, it is all but impossible to forecast future Commission rule changes and their ultimate impacts on the BFP. If the Commission is greatly concerned about the impact of forecasting errors on SLC

[6] U S WEST's budgets are prepared on a calendar year, not on a tariff year basis. As a result, in preparing BFP forecasts for the Annual Access filing U S WEST uses relatively "firm" budget data for the current year and very general numbers for the following year which will inevitably be subject to major revisions. Thus, the use of forecasts for a split tariff year introduces another element of variability into BFP forecasts. In U S WEST's case the issue is further complicated by the fact that U S WEST significantly modified its budget process beginning with the 1994 calendar year. The new process provided much less detail than had been available in prior years for use in calculating the BFP revenue requirement.

[7] The starting point for U S WEST's BFP forecast is preliminary BFP data for the most recent calendar year. The ARMIS data that the Commission has referenced in its Investigation Order is not yet available when U S WEST must prepare its BFP forecast for the upcoming tariff year. U S WEST adjusts the prior year's BFP to reflect anticipated changes in budgets, Commission rules, and other variables over the next tariff year to arrive at a projected BFP. U S WEST does not develop its BFP projection on an unseparated basis. While this approach does not employ any sophisticated forecasting techniques, U S WEST believes that it produces reasonable results in light of the close tie between budget expenditures, productivity and the BFP revenue requirement.

and CCL rates, it should seriously consider using historical data for BFP calculations rather than forecasts.[8]

The use of forecast data was adopted to produce a SLC which attempted to anticipate the actual costs of the LEC during the tariff year. As the Commission changes the process to shift costs to the end user by increasing the caps, the use of a verifiable method to calculate the BFP/Line is imperative. Use of prior year access line demand and BFP provides a verifiable method.

U S WEST's assignment of OB&C expense to the interstate jurisdiction is also the subject of investigation in this Direct Case. This is surprising given that U S WEST has used a consistent approach to assign OB&C expense and given that billing and collection service was deregulated prior to the inception of price cap regulation. Throughout the period under investigation, U S WEST has employed a consistent method for counting users and messages and has assigned less than 5 percent of total OB&C expenses to the End User Common Line ("EUCL") BFP. Given that the Commission has provided no specific guidance on the assignment of OB&C costs to end users and that assignments up to 5 percent routinely have been found to be acceptable for tariff purposes, U S WEST believes that its assignment of OB&C expenses is both reasonable and lawful. U S WEST also believes that its 1997 OB&C exogenous cost adjustment is appropriate. This exogenous change was dictated by Commission rule changes and should be allowed to remain in effect.

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[8] U S WEST has recommended that historical data be used to develop price cap rates rather than forecasts. See U S WEST's Comments on Access Reform.

Lastly, U S WEST believes that it has fully eliminated any equal access costs from its price cap indices. U S WEST's method of adjusting the amount by the changes in price cap indexes is appropriate. To increase the amount by the change in the "R" value overstates the impact on the current year and is contrary to the method used for making other exogenous changes such as reserve deficiency amortization and inside wiring costs. The exogenous change needs to be adjusted by the price cap index changes to reflect the overall reduction in the recovery that the productivity factor less inflation has had over the intervening years. The Commission should affirm the methodology used by U S WEST.

II. ISSUES DESIGNATED FOR INVESTIGATION/DATA SUBMISSION

In its Investigation Order, the Commission suspended U S WEST's Annual Access filing for one day and designated for investigation issues related to common line costs, equal access exogenous cost changes, and OB&C expense.[9] U S WEST responds to the Commission's inquiries and data requests in this section of its Direct Case.

A. BFP Revenue Requirements

Issue/Submission No. 1
Calculate actual interstate BFP revenue requirement for calendar years 1991-1996, using data from ARMIS report 43-01, columns k and m.[10]

Response
See Exhibit 1.
Issue/Submission No. 2
Calculate actual interstate BFP revenue requirement for tariff years 1991-

[9] Order ¶ 2.

[10] Id. ¶ 17.

1996 (beginning with 1991-92 tariff year) using data from ARMIS report 43-01, columns k and m.[11]

Response
See Exhibit 2.

Issue/Submission No. 3
Submit projected BFP revenue requirements filed in each year's TRP since tariff year 1991-92.[12]

Response
See Exhibit 3.

Issue/Submission No. 4
Explain fully any significant differences between each annual BFP revenue requirement projection and actual BFP revenue requirements.[13]

Response
The 1992/1993 tariff year actual BFP growth rate of 4.6% is different than BFP projected growth rate of -2.8%. The difference of $57M, computed by comparing actual calendar year results with tariff year projections, is primarily due to an understatement of the budget for the year. Analysis of the budget used to forecast 1992/1993 tariff year explains most of the difference. The Subscriber Plant Factor ("SPF") rule change was taken into account in the forecast BFP.

The 1993/1994 actual BFP growth rate of 17.8% is different than BFP projected growth rate of 12.2%. Most of the difference appears to be in the forecast of costs for the tariff year. The difference between the actual BFP revenue requirement and projected revenue requirement is $45M. Actual budget variances of $37M explain most of the difference in the revenue requirements. The General Support Facilities ("GSF") rule change was the major separations change in this period and was taken into account in the forecast.

[11] Id.

[12] Id.

[13] Id.

The 1994/1995 actual BFP growth rate of 14.2% is different than BFP projected growth rate in the 1994/1995 tariff year of 6.9%. Comparing forecasted BFP to actual BFP results in a $70M difference. Budgeted costs were slightly higher than actual expenditures. The 1994 depreciation simplification and technical update authorized by the Commission was not included in the forecast. This explains only $3M of the difference. Most of the change can be attributed to the methodology used to forecast the tariff period and an increase in the loop plant being installed to serve customers.

Actual BFP growth rate for the 1995/1996 tariff year of 7.2% is different than the projected growth rate of -5.2%. This translates into approximately $135M difference of the revenue requirement. The budget under forecast explains $78M of this difference. Most of the remaining under-run can be explained by the significant growth in loop plant being installed to provide customer service.

In the 1996/1997 tariff year, the actual BFP growth rate of 9.0% is different than the -.5% projection. Budget differences do not account for the $111M under forecast of the BFP. The difference can be attributed to the significant growth in loop plant being installed to provide customer service in our vast serving area.

These consistent differences in actual and forecasted revenues are the result of several factors. First, U S WEST has been even more successful than it budgeted in reducing expenses. This is directly related to the incentives and pressures driven by the Commission's price cap model. Second, unprecedented growth in U S WEST' service territory has led to unexpected growth in cable and wire and circuit investment. It is difficult to anticipate the swings in demand and we have expected growth to return to historical levels. For BFP forecasts from 1994 on, an aggressive program of selling local exchanges was included in the budgeted figures. All of these sales have taken longer than expected. Consequently, BFP forecasts included decreases in BFP prior to when those reductions actually occurred.

Issue/Submission No. 5

Explain fully any consistent over-or-under estimation of BFP revenue requirements.[14]

Response

See Response No. 4 above.

[14] Id.

Issue/Submission No. 6
For each change in the Commission's rules that became effective on or before December 31, 1996, and that affected U S WEST's BFP revenue requirement, identify the change, state its effective date, and calculate the effect, in dollars, that the change had on its BFP revenue requirement.[15]

Response
See Exhibit 4.

Issue/Submission No. 7
Calculate the effect each rule change would have had on BFP requirements in previous years, back to 1991, had the revised rule then been in effect.[16]

Response
See Exhibit 5.

Issue/Submission No. 8
For each change in the Commission's rule that became effective after December 31, 1996, and that affected U S WEST's BFP revenue requirement, identify the change, state the effective date, and submit data that show the effect, in dollars, that these changes had on projected BFP revenue requirements prepared for U S WEST's annual access tariff revisions filed to become effective July 1, 1997.[17]

Response
See Exhibit 4.

Issue/Submission No. 9
After determining the effect that changes in the Commission's rules had on their BFP revenue requirements, LECs must report the calculation of their

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[15] Id. ¶ 20.

[16] Id.

[17] Id.

adjusted BFP revenue requirements for the calendar years 1991-1996 in two series as follows. The first series must be adjusted for (1) changes to the allocation of GSF expenses; (2) the phase-in of the SPF and [Dial Equipment Minutes of Use] DEM separations allocation rule changes; and (3) revision of the allocation of Other Billing and Collection expenses to reflect a five percent allocation to the common line revenue requirement, if the LEC has not consistently allocated five percent of these expenses to the common line revenue requirement in the past. The second series must be adjusted for all changes to the Commission's rules identified above. These series must be constructed to allow for year-to-year comparisons of BFP revenue requirements. These BFP revenue requirements must be calculated in a manner consistent with the Commission's rules on December 31, 1996.[18]

Response
Exhibit 5, page 6, line 2 identifies the summary of calculations for the first series. Exhibit 5, Page 6, Line 4 provides the figures for the second series. The second series includes the effects of the RAO 20 effective date and rescission.

Issue/Submission No. 10
LECs must file all data underlying their revenue requirements, and must fully explain the data assumptions and methodology used to compute the BFP revenue requirement and projections and to adjust the revenue requirement for changes in Commission rules. This documentation shall include an explanation of all calculations, including a list of all equations used, and an explanation of the methodology used to compute the actual revenue requirements.[19]

Response
In order to set the SPF to 25% in the adjusted calendar year series of actual revenue requirements, U S WEST used the methodology found in Exhibit 5, Page 1. Since the phase down occurred in approximately equal steps in 1991 and 1992, U S WEST used an average Common Line revenue requirement filed in the TRP for the Tariff Years 1991 and 1992 to determine the adjustment to the 25% level. This 1992 revenue requirement was reduced to the BFP level using the BFP expense to total Common line expense relationship from ARMIS.

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[18] Id. ¶ 22.

[19] Id. ¶ 23.

The 1991 SPF adjustment used a similar method but the impact was approximately doubled because of the equal step phase down process. A ratio of the 1992 SPF adjustment to the total unadjusted 1992 was determined. This represents a one year phase down of SPF. In order to set the prior year to the 25% level, the ratio for 1992 was doubled and multiplied by the actual BFP revenue requirement for the year of 1991. This is similar to the method recommended by the Commission for the GSF adjustment.

The GSF revenue requirement change was filed in the 1993 TRP. The calculations are described in Exhibit 5, page 2. This revenue requirement represented a full year impact of this rule change. Since one-half of the change was reflected in the 1993 actual BFP revenue requirement, the other one-half was added to the revenue requirement to determine the BFP for 1993. The BFP revenue requirement was also removed from the actual revenue requirement in order to report the GSF adjustment described in Appendix B of the Commission's <u>Order</u>. The relationship of the adjusted BFP revenue requirement to the unadjusted BFP revenue requirement was determined. This ratio of approximately 115% was multiplied by the BFP revenue requirement for 1991 and 1992 to determine the rule change impact.

The DEM adjustment is found in Exhibit 5, page 3 and the same methodology was used as for the SPF adjustment. The impacts of the DEM change on the common line element were filed in the 1991 and 1992 TRP's. These were averaged and the BFP portion determined for 1992.

A ratio of the DEM adjustment to the total BFP revenue requirement for 1992 was developed and was used to determine the 1991 DEM rule change impact. The 1991 adjustment was assumed to be approximately double the adjustment for 1992 because of the change in the DEM rules that occurred in 1991. This ratio was multiplied by the actual 1991 BFP revenue requirement to determine the adjustment.

OB&C was set to 5% using the method located in Exhibit 5, page 4. This adjustment was determined using the ARMIS 43-04 for the years 1991 through 1996. U S WEST assigned between 3.6% to 4.6% of these costs to the BFP in the years under review. The difference between actual expense level and the 5% level was grossed up by a factor of 1.6546 (developed on the basis of a sample) in order to determine the proper revenue requirement level because of secondary revenue requirement impacts of this change. The allocations of Corporate Operations Expense and GSF costs assigned to the interstate jurisdiction increased because of these secondary impacts.

U S WEST assigned less than 5% of OB&C costs to the BFP in all Tariff Years. A recent Order[20] issued by the Commission would indicate that an assignment of less than 5% is acceptable. The Commission cites numerous disallowances for tariff purposes for companies exceeding the 5% guideline but did not order increases if the BFP assignment was less than the 5% guideline. U S WEST is not aware of circumstances where an assignment factor of under 5% was questioned for tariff purposes. The Commission also concludes, "We also reaffirm our finding that the Bureau's use of non-binding guidelines such as the 5 percent guideline is a legitimate means of evaluating rates and their underlying cost allocations during the tariff review process."[21] The Commission language implies that an assignment of less than 5% is acceptable for cost and tariff purposes. U S WEST will address the cost issues associated with this issue in a later portion of this direct case.

The impact of RAO 20 (Liability booked to Account 4310) on the BFP was calculated each year using an average of the liability for the year using the Company's MR booked amounts. RAO 20 was effective in 1992. The revenue requirement development is displayed in Exhibit 5, pages 5 and 6 and displays the actual calculations of the revenue requirement. Page 5 of the RAO adjustment depicts the two adjusted series of revenue requirements as suggested by the Commission's Order in paragraph 22.[22]

Each of the Workpapers in Exhibit 5 build off the previous pages "adjusted actual BFP Revenue Requirement." Exhibit 5, page 6, at the line identified as "BFP, including Account 4310 Liability as a Rate Base Reduction," summarizes all adjustments with the exception of the 1994 depreciation adjustment.

Issue/Submission No. 11

LECs should identify and explain in detail any relatively "large" year-to-year changes that emerge in each adjusted series of actual BFP revenue requirements.[23]

Response

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[20] In the Matter of National Exchange Carrier Association, Inc., Order on Reconsideration, 11 FCC Rcd. 4087, 4089 ¶ 14 (1996) ("Order on Reconsideration").

[21] Id. at 4098 ¶ 60 (emphasis added).

[22] Investigation Order ¶ 22.

[23] Id. ¶ 24.

See Exhibit 5A.

BFP revenue requirement trends for the adjusted series yielded the following results.

Calendar Year	Annual Changes
1992	8.5%
1993	6.5%
1994	10.0%
1995	9.1%
1996	9.0%

Growth rates for 1993 and 1994 from the adjusted series of revenue requirements deviate most from the average. Investments and expenses for these years were analyzed to determine a reason for the variation. Expense per dollar of investment in cable and wire facilities and circuit equipment trended normally over this time period with the exception of 1994. In 1994 overall expenses trended upward which drives the BFP revenue requirement higher. Most of the growth in 1994 can be attributed to an increase in depreciation expense. See Exhibit 5, page 7 for the normalization of this item. Booked Depreciation increased 17.8% in 1994 over 1993. Normal growth in depreciation is in the 8-9% range. The Commission awarded the company $154 M in the three-way meeting and an additional $25M in the technical/simplification update. Normalizing the adjusted series for this unusual event of $179M, assuming a 10.6% common line assignment, would yield a normal growth rate in the adjusted BFP series for 1994 of 8.0%.

A simple average of adjusted growth rates yields an 8.6% average growth rate excluding the normalized impact of the unusual 1994 depreciation award. The growth rate of the BFP for 1993 is the low point of the adjusted series. The reason for this is not apparent. Operating expenses of the business increased from 1992 to 1993 by 5.9%. The 6.4% actual growth in this year is similar to this 5.9% growth rate in operating expenses.[24]
U S WEST believes this is a representative data point and reflects the normal operations of the business.

Issue/Submission No. 12

[24] ARMIS 43-01 Subject to Separations, Operating Expenses plus State and Local Taxes, for 1993 and 1992 respectively equals $6,788,537 and $6,412,311 or a 5.9% increase.

If a particular percentage change in actual BFP revenue requirements is the result of a one-time event or other isolated occurrence, the LECs must explain the event and its impact, and calculate BFP revenue requirements, excluding the effects of the event.[25]

Response
See Exhibit 5, page 7 and Response to Submission No. 11 on depreciation.

Issue/Submission No. 13
The Commission seeks comments on alternative methods to forecast BFP revenue requirements.[26]

Response
U S WEST recommends adopting the use of access line base period demand and actual BFP to calculate the BFP/line costs for the EUCL rates.

Using base period actuals would eliminate confusion and wasted energy and would produce an easily verified result. As the submissions for this direct case will show, the level of accuracy that the Commission desires will not occur and will not produce results that are any more capable of meeting the Commission's goals than base period actuals. The current rules use base period (actual) lines to calculate the revenue from SLCs with the remainder of the Common Line revenue to be recovered by carrier charges. Using forecasted data to calculate a BFP/access line amount adds little to the process. It does cause much wasted effort by the Commission, LECs, and IXCs.

As local competitors begin to provide service, historical trends, however, will become a less accurate measure for forecasting access line growth. Even economic data such as unemployment or building permits will not be useful because there is no process or data to determine how local competition will impact LEC access line growth. Since we do not know the plans of local competitors, it would be very difficult to forecast the market impact of their presence.

Issue/Submission No. 14
Explain and document fully the data, assumptions, and methodology to

[25] Investigation Order ¶ 24.

[26] Id. ¶ 25.

derive BFP revenue requirement projections contained in U S WEST's access tariff revisions filed to become effective July 1, 1997.[27]

Each price cap LEC shall indicate whether it has followed the same methodology to derive its BFP revenue requirement for each year between 1991 and 1997, and, if not, must (1) explain why it changed methodologies in each case; (2) provide complete explanations of the ways in which any previous methodologies differ from the methodology used in preparing the BFP revenue requirement projection for the 1997 annual access tariff filing, and (3) explain the effect these changes had on their projections for the 1997-98 tariff year.[28]

Response
See Exhibit 6.

U S WEST projected its 1997/1998 BFP using the best information available to the company in the first quarter of 1997. ARMIS 43-04 data was not available for 1996 at the time of the projection. Preliminary Part 69 interstate company results were used to estimate the 1996 actual BFP revenue requirement. Operating expenses and capital expenditures were forecasted for the calendar years 1997 and 1998 by company budget experts. This forecast was on a "subject to separations basis" (total company budget adjusted for Part 64 exclusions). The forecast was then averaged to determine an equivalent tariff year (1997/1998). The forecast tariff year was then compared to the actual subject to separations expenses and average net investment to determine a growth rate.

Adjustments to the preliminary 1996 actuals were made to add the Pay Telephone loop pursuant to the Commission's Order on Pay Telephone released September 20, 1996 and its Order on Reconsideration released November 8, 1996. OB&C exogenous cost changes were not taken into account. The OB&C impact to the BFP was approximately $1M which is insignificant on a forecasted base of 1.251B. After adjustments to the base period data for anticipated separations changes, the growth rate, explained above, was then applied to the adjusted 1996 calendar year actual BFP interstate amounts to determine the forecasted BFP.

The 1997 forecast is inconsistent with the historical pattern. This is due to the prediction by budget experts that expense levels to be generated by the Company would come in at a different level in 1997 and 1998 than the historical pattern.

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[27] Id. ¶ 26.

[28] Id. ¶ 27.

The 1991 through 1993 BFP was calculated using the Company's Part 36 and Part 69 models. Most recent historical interstate results were adjusted for anticipated separations changes. The resulting interstate factors were used to separate the forecasted subject to separations budget.

Subject-to-separations budget detail, provided by Company subject matter experts, was input to the separations model. Demographics, growth in lines, changes in business operating procedures and a variety of other factors were taken into account when building the budgets. Budgets reflected the best estimate of company regulated financial reserves, investment, expenses and taxes for the tariff period. The Part 36 Model produced interstate separated results which had been adjusted to show the Company's best estimate for the tariff year. These separated interstate results were input to the Interstate Part 69 Model to determine the portion of the interstate costs to be allocated to the BFP.

In 1994, U S WEST changed its budget forecasting process, methodology, and level of forecast detail. These process changes were the impetus for the changed BFP forecasting methodology used to forecast the 1994-1997 BFP projections. Budgets were prepared at a higher level of detail, which did not facilitate running the models described above. Instead, total expenses, taxes, tax adjustments, surplus deferred taxes, miscellaneous revenues, uncollectibles and average net investment components were forecast at a subject to separations level for the two calendar years overlapping the tariff year. An average of these subject-to-separations forecasted expenses, average net investment, etc. was calculated. This average projected tariff year was divided by the prior calendar year subject to separations amounts to determine a growth rate by component. Next, preliminary actual BFP expenses, Average Net Investment, etc., were retrieved from the Company's Part 36/69 Models for the calendar year immediately preceding the annual access tariff filing. These actuals were then adjusted for expected tariff year separations rule changes. The subject to separations budget growth rate was then applied to the BFP costs to determine the forecasted BFP revenue requirement for the prospective tariff period. An 11.25% rate-of-return was applied to the forecasted average net investment and federal and state income taxes were calculated.

The change in methodology in 1994 was driven by a change in business practices and was not intended as an attempt to change BFP forecasting methods. It is not apparent at this time that the 1994 change in BFP forecasting methodology altered 1997 tariff year projections in any way.

Issue/Submission No. 15
Show separately the adjustments for the OB&C Order and the Payphone Reconsideration Order that are reflected in U S WEST's recent BFP revenue requirement projection.[29]

Response
See Exhibits 7 and 7A for payphone adjustments. No adjustments for OB&C are reflected in U S WEST's 1997-98 BFP projection.

Issue/Submission No. 16
If a LEC uses unseparated company data, it must demonstrate with a thorough explanation containing clear evidence that such a calculation produces a result that is more accurate than that produced by the use of separated, interstate data.[30]

Response
U S WEST believes that the use of separated data instead of total company data in forecasting 1997/1998 BFP revenue requirement would be no greater or lesser a predictor of the future competitive environment. In fact, deriving a separated forecast would introduce a new set of assumptions and estimates that would add little precision to the result. In today's dynamic industry, with a multitude of new and potential competitors, it is impossible to derive precise forecasts that would not overstate or understate what will happen. A method that produced a result closer to actuals today will not guarantee that it will produce the most accurate result in the future. The result will either be too high or too low. Market dynamics will determine how accurate forecasts will ultimately be.

U S WEST used the forecasting methodology described in Response No. 14 above. Prior to 1994, U S WEST used its Part 36 and Part 69 Models along with budget forecasts to project BFP revenue requirements. Effective with the 1994 tariff filing, U S WEST used the projected growth in the Company's subject-to-separations tariff year budget compared to the actual calendar year subject-to-separations results to forecast the growth for the tariff period. This growth rate was applied to the interstate BFP results for the most recent annual period to derive next tariff year BFP forecast.

[29] Id. ¶ 27 and Appendix B, "Payphone Adjustment."

[30] Id. ¶ 28.

Issue/Submission No. 17
Carriers using a "bottoms-up" methodology must fully explain their methodology and explain their basis for the conclusion that this method produces results that are at least as accurate as projections developed using historical trends.[31]

Response
U S WEST used a bottoms-up methodology for the tariff years 1991 through 1993. When comparing the actual BFP projections to the tariff year actuals located in Exhibit 3, the evidence is not conclusive that this methodology is better than the method used by U S WEST in later years.

Issue/Submission No. 18
LECs that have adjusted their methodology over time must provide the same information regarding their projection methodology for 1995-96 and 1996-97 tariff years as for the 1997-98 BFP revenue requirement projections.[32]

Response
U S WEST adjusted its projection methodology in 1994. Therefore, U S WEST used the same methodology for 1995-96 and 1996-97 as for 1997-98. See Exhibits 6 and 8 for detail to replicate projections.

Issue/Submission No. 19
Provide the past actual average number of total billable access lines, multi-line business lines, residential and single-line business lines, for the past six tariff years (beginning with the 1991-92 tariff years), using ARMIS data and projections of these lines filed for each of these tariff years.[33]

Response
See Exhibit 9.

Issue/Submission No. 20
Explain any significant differences between projected lines and the actual

[31] Id. ¶ 29.

[32] Id. ¶ 30.

[33] Id. ¶ 31.

number of lines and identify the variables used to forecast end-user demand and the weight given to each variable for each class of lines for each year where there was a significant difference between actuals and projected demand.[34]

Response

The differences between forecasted access lines and actual access lines are quite small and well within established U S WEST tolerances. As shown in Exhibit 9, actual total access lines have been within 1 - 2% of the forecast for each of the last six tariff years. Residence, single line business and multi-line business forecasts are quite accurate in most of the tariff years, particularly in the later years. In the later years U S WEST has been forecasting a little too conservatively and not anticipating the growth the Company has experienced.[35]

U S WEST and the other Price Cap companies are required to forecast access lines for the upcoming tariff year as part of the process of developing the SLC levels. For the 1997 filing, internal work on the filing started in January, 1997, with the actual filing made mid-June, 1997. The access line forecast which was developed for the filing was for July, 1997 through June, 1998. When work started on the filing, no actual results on 1997 access lines were available. Therefore, the forecasting process involved the development of a forecast for 1997 as well as six months of 1998 (an 18-month prospective period). Because the current rules require the development of this prospective, 18-month forecast, any number of changes can occur, and, in many cases, do occur.

U S WEST develops forecasts for access lines, by state and by type of customer, utilizing the following economic indicators, anticipated changes in the market, and company plans relative to strategic initiatives:

Key Economic Indicators:
Labor Market Trends
Nonfarm employment
Personal Income
Population
Housing Permits
Households
Market Influences:
Competition

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[34] Id. ¶ 32.

[35] It should be noted that under-forecasting the access lines tends to overstate the SLC and accordingly the carrier charge is understated.

Changes driven by Technology (e.g., Internet)
Strategic Initiatives:
Promotions (e.g., stimulation of second lines)
Home Business Campaigns

As a partial demonstration of the process U S WEST uses, a copy of the U S WEST 1997 Access Line Forecast dated April, 30, 1997 is attached as Exhibit 10.

The actual billable lines vary from the forecast for any number of reasons, and in many cases, for more than one reason. However, the largest differences are usually driven by changes in the economic indicators, especially employment and population.

The Commission is requiring that U S WEST determine tolerances based on differences between actual growth rates and forecasted growth rates, rather than on actual access lines as compared to forecasted access lines. The use of differences in growth rates is not a valid measurement of forecasting accuracy. U S WEST develops a detailed view of access lines, by state, by customer group, based on key economic, market, and strategic variables. The forecast of access lines is not related, in any way, to the previous year's growth rate. In fact, a growth rate in a particular state for one year has absolutely no bearing on the anticipated growth rate for the following year. The use of a comparison of growth rates, rather than actual access lines, serves to cosmetically inflate the perceived "problem" and make it appear that huge disparities and problems exist, when, in fact, there is no access line forecasting problem.

Issue/Submission No. 21
Each LEC is required either to: (1) demonstrate that the projection for the 1997-98 tariff year is consistent with the value predicted by the historical trend of end-user demand; or (2) state specifically the underlying factor or factors that they expect will change, and the projected effect of the change, expressed in a numerical prediction.[36]

Response
U S WEST believes that the total access line projection for the 1997-98 tariff year is consistent with the value predicted by the historical trend. As noted in Exhibit 9, the year by year actual demand and growth rate is

[36] Id. ¶ 33.

91/92	3.36%
92/93	3.20%
93/94	4.29%
94/95	4.25%
95/96	4.75%

The projected growth for the 97/98 period over the previous year's actuals is 4.89%. As graphically portrayed in Exhibit 11, the projected access lines for 97/98 appears to be well within the overall trend. It is also important to note that the growth rate for U S WEST has been increasing over the Price Cap period and U S WEST has reflected that increase in the access line forecast for 97/98. It is also interesting to note that U S WEST has slightly under-forecasted the access lines for the 95/96 and the 96/97 tariff years. A slight increase in the growth rate would indicate an effort to more accurately anticipate the actual access lines for 97/98.

Issue/Submission No. 22
LECs must provide trend analyses using the actual number of lines and the natural logarithm of the number of lines, as reported in ARMIS, for total billable lines, residential lines, multi-line business lines, and single-line business lines, using calendar year data from 1991-96.[37]

Response
See Exhibit 12.

These charts were prepared using the Excel spreadsheet to calculate the natural logarithmic regression analysis for the billable access lines in each category; i.e., total access lines, residential line, etc. The logarithmic regression line uses the equation: $y = c \ln x + b$, where c and b are constants and ln is the natural logarithm.

Issue/Submission No. 23
LECs that are unable to demonstrate that their projections for the 1997-98 tariff year are consistent with the historical trend must explain and document the data and methodology used to derive EUCL demand projections filed in their 1997-98 TRP.[38] All worksheets used to derive these projections must also be filed.

[37] Id. ¶ 33.

[38] Id.

Response

As noted in Response No. 21, U S WEST believes that the access line projection for the 97/98 tariff year is consistent with the prior year actuals and trends. As such, no other data or supporting material is being supplied other than that in Response No. 20.

Issue/Submission No. 24

Indicate the number of semi-public payphones that U S WEST charged single-line business EUCL charges, prior to the Payphone Reconsideration Order, that will now be charged multi-line business EUCL charges. These projections must be compared with historical counts of public and semi-public payphones. Also show explicitly how the most recent multi-line business and single line end-user demand projections are affected by the Payphone Order.[39]

Response

See Exhibit 13. Semi-public lines were formerly charged the SLB rate and are now charged the MLB rate. This resulted in a migration of 16,772 lines to the MLB access line count from SLB. 79,654 of the total public access lines were not charged a SLC previously and are now charged an MLB and have moved into the MLB Access Line count. The remaining public lines were already being charged a MLB rate and were included in previous MLB Access Line counts.

Issue/Submission No. 25

Explicitly show how ISDN lines are treated in U S WEST's 1997-98 projections of lines.

Response

Prior to the Access Reform Order, released May 7, 1997, which changed the application of subscriber line charges to primary ISDN lines, U S WEST assessed two (2) times the multi-line business SLC for each T-1 Primary ISDN trunk. In the 1997 Annual filing, the new threshold of 5 multi-line business SLCs was used. Consequently, approximately 4,500 lines were added to the multi-line business access line count to account for the additional three SLCs assessed. Similar adjustments were made to 1995 and 1996 actual demand to have an accurate assessment of MLB growth.

Issue/Submission No. 26

[39] Id. and Appendix B.