

STATE OF MISSOURI
PUBLIC SERVICE COMMISSION

Jefferson City

December 20, 1983

CASE NO. TR-83-253 and TR-83-288

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Enclosed find certified copy of ORDER in the above numbered case.

Sincerely,

Harvey G. Hubbs

Harvey G. Hubbs
Secretary

uncertified copy:

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BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the matter of the filing by)
Southwestern Bell Telephone Company)
of new intrastate tariffs, rates,)
tolls and charges applicable to)
intrastate telecommunication)
services furnished within the State)
of Missouri.)
_____)

CASE NO. TR-83-253

In the matter of Southwestern Bell)
Telephone Company for authority to)
file tariffs offering a Rate)
Stability Plan for Centrex C.O.)
Customers.)
_____)

CASE NO. TR-83-288

REPORT AND ORDER - PART II:
REVENUE REQUIREMENT, RATE DESIGN,
ACCESS CHARGE RATE LEVELS AND QUALITY OF SERVICE

Date Issued: December 20, 1983

Date Effective: January 1, 1984

SOUTHWESTERN BELL TELEPHONE COMPANY

Cases No. TR-83-253 and TR-83-288

REPORT AND ORDER, PART II:
REVENUE REQUIREMENT, RATE DESIGN
ACCESS CHARGE RATE LEVELS AND QUALITY OF SERVICE

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Stability Plan for Centrex C.O.
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REPORT AND ORDER - PART II:
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ACCESS CHARGE RATE LEVELS AND QUALITY OF SERVICE

Procedural Background: The procedural history of this case is summarized in considerable detail in Report and Order, Part I, issued by the Commission on November 22, 1983. Additional hearings on accounting issues were held in this case on November 21-23, 1983, and a final reconciliation was filed by the parties as Exhibit No. 245 on Friday, December 2, 1983. Late-filed testimony was submitted by AT&T Communications (ATTCOM) and the Staff concerning ATTCOM's rate design as Exhibits No. 246 and 247, and ATTCOM's Rate Design Packages were filed as Exhibit No. 248 on December 13, 1983. On the day of issuance of this Report and Order, Part II, Staff caused to be filed as Exhibit No. 249 a final reconciliation showing the revenue requirements, rate design, local exchange rates and other results which flow from a series of assumptions which reflect the Commission's decisions on contested issues herein. As of December 6, 1983, all issues presented to the Commission in this case had been briefed by the parties. Exhibits No. 245, 246, 247, 248 and 249 are hereby received in evidence.

On December 2, 1983, a document entitled a "Statewide Pooling Joint Memorandum of Understanding" was filed by Southwestern Bell and some twenty-nine (29) independent telephone companies, stating their understanding of the intention of the Commission in its Report and Order, Part I, as to certain particulars of the pools which the Commission ordered established in that Report and Order. The Commission notes that said Joint Memorandum of Understanding does accurately reflect the intent of the Commission.

On December 5, 1983, the Staff filed a "Motion to Compel SWB to File Certain Information and to Clarify Matters Necessary to the Implementation of the Commission's Report and Order, Part I." In its motion, Staff sets forth three (3) illustrations of ways in which the Commission could design rates in this case to make up the \$9.4 million access charge pool deficiency which would result under Staff's access charge proposal, since the Commission has previously rejected the establishment of an End User Common Line Charge (EUCLC) in Missouri. Staff's illustrations concern the options of recovering the toll and access charge pool deficiency by increasing intraLATA toll rates, or increasing access charge rate levels, or by distributing the pool deficiency between intraLATA toll rates and access charge rate levels. In addition, Staff requested that the Commission enter an order requiring Southwestern Bell to file a late-filed exhibit in this case showing the level of Missouri jurisdictional operational revenues which would result from setting access charges at parity with the rate levels which will become effective at the interstate jurisdiction pursuant to the "Interstate Access Compensation Agreement", entered into between AT&T and the Bell Operating Companies (BOCs). That agreement establishes an interim compensation system during the time subsequent to January 1, 1984 when the proposed federal Exchange Carriers Association (ECA) access tariffs are under suspension by the FCC. The necessity of such an agreement arose from the action of the FCC suspending said tariffs on October 18, 1983, as discussed in Report and Order, Part I.

On December 8, 1983, Southwestern Bell filed a response to the Staff motion, asserting that the interim plan is not expected to be finalized prior to December 23, 1983 and arguing that it would be unreasonable and inappropriate for the Commission to employ or adopt the interim plan for intrastate ratemaking purposes. The Company also responded to Staff's illustrated alternatives for the recovery of the toll and access charge pool deficiency, and urged the Commission not to fund said deficiency since even the identified deficiency would result in a positive rate of return to pool participants. Company also reiterated its position in opposition to any increase in intraLATA toll rates in this case.

Also on December 8, 1983, AT&T Communications filed a response to the Staff motion, agreeing with Southwestern Bell that it would be inappropriate to utilize the interim agreement as the reference point for establishing Missouri intrastate access charges at "parity" with federal access charges. ATTCOM also opposes increasing carrier access charges in order to make the toll and access charge pool whole. ATTCOM suggests that the exchange carriers be ordered to mirror ATTCOM's new toll rate schedule in order to produce additional revenues to reduce the intraLATA toll deficiency and preserve, for at least a while longer, uniform statewide toll rates. The balance of the deficiency, says ATTCOM, should be recovered from other services.

On or about December 12, 1983, the following independent telephone companies filed responses to the staff's motion of December 5, 1983: Eastern Missouri, Kingdom, Continental, MoKan, CrawKan, and the Independent Telephone Company Group. MoKan and CrawKan suggested that the access charge rate levels in the interim plan agreement between SWB and AT&T be utilized for intrastate purposes for the three (3) month duration of said plan. The Independent Telephone Company Group did not address that point, while Eastern Missouri, Kingdom, and Continental opposed the use of the interim plan's rate levels on an intrastate basis. Concerning the pool deficiency, MoKan, CrawKan, Eastern Missouri and Kingdom all recommend that said

deficiency be recovered by an increase to carrier access charges, and the Independent Telephone Company Group recommends that carrier access charges be relied upon to recover as much of the revenue deficiency as possible without pressuring interexchange carriers into seeking higher toll rates. Continental believes that the pool deficiency should be recovered by increasing rates for both intraLATA toll and carrier access charges, but not necessarily by assigning half of the deficiency to each of those sources.

If Southwestern Bell experiences a significant revenue excess in 1984 as a result of the interim agreement with AT&T, that situation could result in a true-up proceeding and SWB could be ordered to make a refund to its customers. (See Section IV., "Test Year and 1985 Investigatory Proceeding ('True-Up')," below). Company's response to Staff's motion indicates that it seems unlikely that the interim agreement will have a substantial effect upon the Company's performance on an annualized 1984 basis. In any event, the details of the interim agreement cannot be submitted to the Commission until after the instant Report and Order, Part II is required by law to be issued, and therefore will be of no service to the Commission in the establishment of access charge rate levels for SWB for 1984. Any use of that data by the Commission in the establishment of access charges in this case would also require additional cross-examination, the time for which does not exist within the operation of law schedule in this case. For these reasons, the Commission determines that the Staff motion relating to the interim agreement between AT&T Communications and the BOCs should be denied. The reference point for "parity" of access charge rates in this case refers to the proposed federal ECA tariffs which are currently under suspension by the FCC.

The issue of the funding of the toll and access charge pool deficiency will be discussed further below in Section VIII., C.

The requirements of Section 536.080, RSMo 1978, have not been waived by the parties.

Findings of Fact

The Public Service Commission of Missouri makes the following findings of fact, based upon the competent and substantial evidence upon the whole record:

I. Report and Order.

This Report and Order, Part II, and the entirety of Report and Order, Part I (issued in this case on November 22, 1983, effective January 1, 1984), including all findings of fact, conclusions and "Ordered" sections contained therein, shall constitute the entire Report and Order of the Commission in these cases, and shall be considered one (1) document, unless otherwise amended or supplemented by the Commission. Report and Order, Part I, issued on November 22, 1983 and effective on January 1, 1984, is hereby incorporated by reference into the instant Report and Order, Part II.

II. The Company (Southwestern Bell), and AT&T Communications.

Southwestern Bell Telephone Company (hereinafter referred to as SWB, Southwestern Bell or Company) is a public utility corporation duly organized and existing under the laws of the State of Missouri. Southwestern Bell is a telephone corporation as defined in Chapters 386 and 392, RSMo 1978, with its headquarters and principal place of business located at 1010 Pine Street, St. Louis, Missouri. Southwestern Bell is a wholly-owned subsidiary of American Telephone & Telegraph Company (AT&T) and is one of the Bell System's twenty-three (23) operating companies. However, as of January 1, 1984, Southwestern Bell will become a separate and distinct entity from AT&T and be publicly held, under the terms of the Modified Final Judgment (MFJ) in the antitrust suit filed by the United States Department of Justice against AT&T, Bell Laboratories and Western Electric Company in 1974 (see discussion in Report and Order, Part I). SWB provides telecommunications services throughout the states of Missouri, Kansas, Arkansas, Oklahoma and Texas. Southwestern Bell's Missouri intrastate operations are subject to the jurisdiction of this Commission.

As of January 1, 1984, pursuant to the MFJ, Southwestern Bell will be prohibited from providing interLATA toll service. Instead, that service will be provided by AT&T through its new subsidiary, AT&T Communications of the Southwest (ATTCOM). ATTCOM is a Delaware corporation presently owned by Southwestern Bell, which will transfer ATTCOM to AT&T at divestiture. The Commission considers ATTCOM to have intrastate Missouri interLATA toll authority without the specific necessity of authority from this Commission, by virtue of Southwestern Bell's Missouri intrastate authority and the operation of the MFJ. No party has suggested to the contrary, although comments on that point were solicited by the Commission in its Report and Order, Part I.

Therefore, AT&T Communications of the Southwest (ATTCOM) will, at January 1, 1984, be a Delaware corporation, wholly-owned by American Telephone & Telegraph Company, with authority to provide intrastate interLATA toll services within the State of Missouri. As such, ATTCOM will be a public utility corporation under the jurisdiction of this Commission pursuant to Chapters 386 and 392, RSMo 1978. The headquarters and principal place of business of ATTCOM are located at 1100 Main, Kansas City, Missouri 64105. Since ATTCOM is being created out of Southwestern Bell, and will exist as a separate regulated entity as of January 1, 1984 for the first time, the Commission must establish in this case a revenue requirement (including an appropriate rate of return on equity) and rate design for ATTCOM, in addition to Southwestern Bell.

The Commission notes that the inherited operating authority of ATTCOM does not extend to any services other than interLATA toll. Any additional services which ATTCOM would wish to offer would have to be subject to a grant of a Certificate of Public Convenience and Necessity by this Commission.

III. Elements of Cost of Service.

Southwestern Bell's authorized rates, and those of ATTCOM, are generally based on their cost of service or "revenue requirement". As elements of its revenue

requirement, a utility company is authorized to recover all of its reasonable and necessary operating expenses and, in addition, a reasonable rate of return on the value of its property used in public service (rate base). It is necessary, therefore, to establish the value of SWB's (and ATTCOM's) rate base (less accumulated depreciation) and to establish a reasonable rate of return to be applied to the value of that rate base. The total revenue requirement of each company is calculated by adding the operating expenses to the rate of return as applied to the value of the company's rate base. By calculating the company's reasonable level of earnings, it is possible to determine the existence and extent of any deficiency between the present earnings and the company's revenue requirement, which deficiency should be allowed as additional revenue in any rate proceeding.

IV. Test Year and 1985 Investigatory Proceeding (True-up).

A. Test Year. The purpose of using a test year is to construct a reasonably expected level of expenses, revenues and investment during the future period for which the rates to be determined herein will be in effect. Aspects of the test year operations may be adjusted upward or downward in order to arrive at a proper allowable level for all of the elements of the Company's operations.

All parties have agreed to utilize calendar year 1984 as the test year in this case, based upon the Company's 1984 budget as modified by agreement of the parties in the course of Staff's and Public Counsel's audits. Conceptually, the case is based on 1984 projected results.

In Case No. TR-82-199, the Commission directed the parties to make every effort to develop and present alternative methodologies to the traditional historic test year approach, such as the use of a true-up procedure or forward looking data, in SWB's next rate case. The Commission emphasized the importance of maintaining a careful matching of revenues, expenses and plant in whatever test year was used. That directive in TR-82-199, combined with the extreme uniqueness and complexity of the issues presented in the instant case, were instrumental in Staff's and Public

Counsel's decision to agree to utilize a budgeted test year. Barring events equal to divestiture and the various FCC decisions, Staff and Public Counsel do not at this time endorse the use of a budgeted test year in future proceedings.

Public Counsel's position is that the agreement to utilize the Company's 1984 budget does not in any way constitute an agreement among the parties to accept the reasonableness or accuracy of the Company's budget nor is it intended to prohibit the parties from contesting the revenue requirement amounts indicated by the budget.

B. 1985 Investigatory Proceeding (True-up). Staff, Public Counsel and Company initially agreed to calculate Southwestern Bell's revenue requirement by use of a 1984 budgeted test year on the basis that Company's local exchange rates set by the Commission in this proceeding would be authorized on an interim, subject-to-refund basis, with a true-up to occur in 1985 after actual results from calendar year 1984 were available.

Staff's position as reflected in the "Hearing Memorandum-Accounting Issues, Management Efficiency and Complex Wire" (Exhibit 150) has changed, and is now that the rates set by the Commission in this proceeding should be set on a permanent basis, rather than interim, subject-to-refund depending upon the results of a 1985 true-up. The change in Staff's position is a result of Staff's belief that Company will institute a 1984 proceeding that will constitute a rate case and thus require an audit. The rates set in the 1984 proceeding will supersede the rates set in this proceeding. Further, Staff is of the opinion that the productivity target injected into the case as filed by Public Counsel, Staff and Company, provides a sufficient degree of protection for Missouri ratepayers to substantially lessen the need for a 1985 investigatory proceeding. In short, Staff's position is that a true-up or investigatory proceeding in 1985 is not practical.

Public Counsel and Company's positions remain essentially unchanged. However, Public Counsel and Company disagree as to the scope of the proposed 1985 proceeding. Public Counsel asserts that as a result of its agreement with Company,

) parties to the investigatory proceeding would have the right to challenge the reasonableness or appropriateness of Company's actual 1984 operating results. Staff supports in theory the type of investigatory proceeding proposed by Public Counsel.

Company asserts that the investigatory proceeding should be based upon the Company's actual financial results for calendar year 1984, which financial results should be used as the basis for determining whether Company has earned more or less than the Commission authorized return on net plant rate base in this proceeding.

) The Commission is of the opinion and finds that the local exchange rates established in this proceeding should be implemented on an interim, subject-to-refund basis until otherwise ordered by the Commission. The Commission is further of the opinion that an investigatory proceeding need not be scheduled at this time. If, at any time during the period that the rates are subject to refund, any party believes an investigatory proceeding is necessary, that party may come forward and request the Commission to open a docket for that purpose. The Commission would strongly suggest that before initiating such a request, all persons who appear to be proper parties (including all parties to the instant case) should be contacted for the purpose of discussing and possibly recommending how to proceed in the most orderly and expeditious manner.

V. Net Operating Income.

) A. Embedded Base Organization (EBO). In the "Hearing Memorandum-Accounting Issues (Phase II)" designated as Exhibit 231, Public Counsel recommended the disallowance of \$107 million of the Company's projected revenue requirement which Public Counsel associates with the cost of divestiture on the basis that aside from the effects of changes in capital structure, Southwestern Bell has failed to meet its burden of proof with respect to the reasonableness of costs Company has identified as relating to lost contribution from toll and terminal equipment and lost economies of scale and corporate consolidation. Subsequently, Public Counsel modified its position to recommend that the Commission disallow \$20.3 million of Company's revenue

requirement which the Company has identified as relating to lost contributions from the transfer of its terminal equipment operations to the Embedded Base Organization (EBO) or AT&T Information Systems (AT&T-IS) as it is now called.

In support of its proposal, Public Counsel sponsored the testimony of Mr. Allen G. Buckalew. Mr. Buckalew presented an impact analysis which he had performed in order to test the reasonableness of the Company's contention that divestiture would increase its revenue requirement by removing the contribution or subsidy which the Company claims has been provided by its terminal equipment services which will be transferred to AT&T-IS upon divestiture. Mr. Buckalew's study purportedly shows that the transfer of terminal equipment will result in a reduction of Southwestern Bell's net revenue requirement.

Public Counsel argues that given the uncertainty inherent in using a budgeted test year for purposes of reflecting the revenue requirement effects of an event such as divestiture, an analysis of the type performed by Mr. Buckalew is a valuable tool for testing the reasonableness of Company's "divestiture claims" and should be afforded considerable weight in determining whether the Company has met its burden of proving the reasonableness of its divestiture related revenue requirement. In particular, Public Counsel asserts that Mr. Buckalew's analysis should be relied upon as a strong indication that the Company has failed to demonstrate the validity of its contention that the transfer of terminal equipment to AT&T-IS will result in a significant revenue deficiency.

Company contends that its revenue requirement should be determined based on the budget view which it has filed in this case pursuant to the agreement of Staff, Public Counsel and Company to use a budgeted test year. It is the Company's position that the cost of divestiture is irrelevant to the determination of the Company's revenue requirement in this case. Company also contends that its direct evidence fully supports its proposed revenue requirement.

Company further asserts that Public Counsel's proposed disallowance is inappropriate since (1) it is based on an unwarranted criticism of the budgeted test year concept to which Public Counsel agreed, (2) it bears no relationship to the specific items of expense, revenue and rate base implicit in the Company's revenue requirement, (3) it is based on a flawed 1982 fully distributed cost study which does not incorporate separations principles, assumes that arbitrarily allocated common costs actually depart with the terminal equipment line of business, and fails to take into account a significant reduction in expense related to the implementation of the FCC's decision in Computer Inquiry II.

The Commission is not persuaded on the record herein that Public Counsel's proposed adjustment should be made.

B. Wage and Salary Expenses. Staff recommends that the Commission order Southwestern Bell to perform a future wage and salary compensation study which will compare the Company's wage and salary levels with those of the Company's competitors. Staff asserts such a study is necessary if the Commission desires Staff to assess in future proceedings whether the Company's wages and salaries are fair and reasonable.

Company opposes Staff's recommendation and asserts that it is paying a competitive, fair amount for its employees' services. Company indicated that it is opposing Staff's recommendation for two major reasons. First, Company objects to Staff's suggestion that the study be limited to examining companies that are "competitors" of Southwestern Bell. Company believes that for such a study to be meaningful the Commission should not limit the comparison companies to Southwestern Bell's competitors but should include a variety of other industries which seek to attract the same types of employees as Southwestern Bell. Second, Company argues that the Commission is constrained by federal law in the area of wages, which are the subject of collective bargaining. Company further submits that employees' salaries and expenses are a matter of management prerogative and cannot be adjusted without a showing of abuse of discretion on the part of management.

The Commission is concerned that it not transgress the provisions of federal labor law, particularly those governing the collective bargaining process. Nonetheless, the Commission can see no reason why it would be preempted from examining the reasonableness of wage and salary-related expenses for ratemaking purposes.

Based on the foregoing, the Commission finds that Staff's recommendation, that Southwestern Bell perform or have performed a future wage and salary compensation study, should be adopted. However, the Commission believes that the comparison companies should not be limited to competitors of Southwestern Bell. Furthermore, the Company should submit evidence relating to the reasonableness of wage and salary expenses in its next rate proceeding.

C. Inflation Adjustment. In formulating its 1984 budget, the Company has incorporated projected inflation rates of 4.7 percent and 5.0 percent for 1983 and 1984, respectively. These projected inflation rates were then applied to the non-wage expense portion of the Company's budget including materials, rents and services (MRS). The inflation projections incorporated in Company's budget were taken from the July 10, 1983 issue of Blue Chip Economic Indicators. The Blue Chip publication represents a consensus of forecasts by 46 separate firms engaging in economic analysis.

Public Counsel contends the Blue Chip forecasts relied upon by Company should be adjusted downward by one percent (1%) for purposes of determining the appropriate level of inflation to include in the MRS category of Company's budget. The corresponding dollar adjustment to budgeted MRS for 1984 would be \$3.4 million. Public Counsel argues that recent Blue Chip forecasts have indicated a tendency to overestimate the rate of inflation and that the suggested one percent (1%) downward adjustment is in fact conservative.

Company agrees with the quantification of the proposed adjustment, but disagrees with the adjustment in principle. Company argues that the Commission

should reject the proposed adjustment since the clear majority of economists believe inflation in 1984 will exceed four percent (4%), the Blue Chip forecast represents a stable consensus which has been historically accurate, and there is no competent evidence upon the record to support the proposed adjustment.

The Commission is of the opinion and finds that Public Counsel has demonstrated recent Blue Chip forecasts have tended to overestimate the rate of inflation. The Commission further finds that Public Counsel's proposed adjustment to the level of inflation to be included in the MRS category of Company's budget is just and reasonable and should be adopted.

D. Rate Case Expense Adjustment. Public Counsel has proposed the disallowance of \$134,742 in potentially avoidable rate case expense which has been incorporated in the Company's 1984 budget. Public Counsel proposes disallowance of these costs on the premise that there is currently no basis for concluding that the Company will actually file a rate case in 1984.

Company opposes the proposed adjustment. Company argues that the need to file a rate case in 1984 will be affected by the Commission's Report and Order in this case and by the actual operating results for the first portion of 1984.

The Commission is of the opinion that there is a substantial likelihood that Company will institute a rate proceeding in 1984. Therefore, Company's inclusion of avoidable rate case expense in its 1984 budget is reasonable, and Public Counsel's proposed adjustment will be rejected.

E. Conversion of Arrears-Billed Customers to Advance-Billed. The majority of Southwestern Bell's customers are billed for local service in advance of the receipt of their service. However, some 472,000 customers residing in a group of exchanges in the St. Louis metropolitan area are billed for local service in arrears. This situation has existed since the smaller telephone companies serving this area were bought by or merged with Southwestern Bell with their billing practices intact. Staff's position is that the current practice is discriminatory. Noting the "time

value of money" concept, Staff asserts that it costs more to serve customers that are billed in arrears than customers that are billed in advance. Company's Missouri customers who are billed their local recurring service charges in arrears are being subsidized by Missouri customers who are billed their local recurring service charges in advance. If Staff's suggestion is accepted, composite revenue lag would be reduced by 6.0 days and Company's revenue requirement would decrease by approximately \$2.5 million.

Company is not opposed in principle to Staff's recommendation. However, Company does not believe the financial impact is worth the customer confusion and irritation which would result from such a billing change at this time. In short, Company asserts that the disadvantages outweigh the advantages. Therefore, Company opposes Staff's proposed change in Company's current billing practices.

The Commission finds that Company's current billing practices at issue here are discriminatory. The Commission is of the opinion and finds that those customers currently billed in arrears should be converted to advance billing over a ten-month phase-in period, to be completed no later than the end of 1984.

F. Depreciation Expense. Company and Staff have included an agreed upon level of depreciation expense in their respective cases. The depreciation expense includes the increase resulting from the triennial represcription process involving the Company, Staff and the FCC Staff. The agreed upon depreciation rates are set forth in the testimonies of Staff witness J. Richey and Company witness E. J. Peters.

Company and Staff have included the level of depreciation expense for central office switching - analog ESS machines which the Staff and the FCC staff recommended during the represcription process. Company has requested the FCC to review the depreciation expense applicable to this account and a decision on the application is expected in December, 1983. Any increase in the depreciation expense applicable to this account will be booked beginning January 1, 1984.

Staff and Public Counsel agreed to the inclusion of the additional depreciation expense to the extent authorized by the FCC if the decision was received prior to the completion of the November, 1983 true-up. If the FCC rendered its decision after the November, 1983 true-up but prior to the Report and Order in this case, Staff and Public Counsel would not object to the inclusion of the additional expense subject to the Company conducting a review of the 1984 budget with an offset for expense reductions in non-depreciation categories and any other significant item affecting the Company's revenue requirement need. Staff and Public Counsel believe it would be improper to solely consider a single change in one expense item without considering contemporaneous changes in other items affecting revenue requirement.

Company requests the inclusion of any additional depreciation expense authorized by the FCC if the decision is received prior to the issuance of the Report and Order in this case. Company does not believe it necessary to conduct an additional investigation as to its expense levels. Instead, the appropriate expense levels should be determined from the record evidence in this case, in Company's view.

Since the Commission has received no notice of any FCC action with respect to the subject account, the Commission finds that the agreed upon depreciation rates shall be used for purposes of this case.

G. Tax Normalization. Company has excluded the revenue requirement associated with the normalization of tax timing differences related to the cost of removal and salvage for 1980 and prior vintages, vacation pay accruals, capitalized social security and relief and pensions from this case. Company has also excluded the revenue requirement effects of matching the income tax interest deduction for plant under construction with the consumption of the plant. These exclusions are consistent with the Commission's Order in Case No. TR-82-199 which established a generic proceeding, Case No. 00-83-220, to examine current policy relative to the normalization of tax timing differences. Subsequently, this has been changed to a

rulemaking docket No. AX-84-3. In the event the Commission were to conclude that normalization is the most appropriate accounting method and issue an order authorizing normalization in the rulemaking docket or otherwise prior to the conclusion of the 1985 investigatory proceeding hereinafter referred to, Company asserts that the revenue requirement associated with the tax timing differences for which normalization is authorized should be included for purposes of determining Company's 1984 realized return.

Company has calculated the revenue requirement associated with normalization of these timing differences as follows:

	<u>Southwestern Bell</u>	<u>AT&T Communications</u>
1) Cost of Removal and Salvage 1980 and Prior Vintages	\$5,256,000	\$190,000
2) Vacation pay accrued	\$1,165,000	\$ 52,000
3) Capitalized social security and relief and pensions	\$8,126,000	\$ 78,000
4) Interest deduction related to TPUC	\$ 869,000	\$ 32,000

Staff and Public Counsel maintain that the flow-through treatment of the aforementioned nonprotected tax timing differences is appropriate. Staff intends to participate in the rulemaking docketed as Case No. AX-84-3 and therein will address the question of the lawfulness of setting rates by Commission rule. Furthermore, Case Nos. TR-83-253 and AX-84-3 have not been consolidated. Therefore, Staff contends that a determination in Case No. AX-84-3 prior to the operation-of-law date in Case No. TR-83-253 cannot lawfully be applied in Case No. TR-83-253 either in the Report and Order to be issued herein or in the 1985 investigatory proceeding should the Commission order such a proceeding.

Public Counsel opposes consideration in the 1985 investigatory proceeding of the above revenue requirement amounts associated with normalization treatment regardless of any Commission decision reached in Case No. AX-84-3.

The Company's proposal seeks to adjust revenue requirement retroactively from the date any tariffs would be approved following the effective date of any order in AX-84-3, to the operation of law date in this case. The Commission concludes that the Company's proposal thus contemplates unlawful retroactive ratemaking. Further, the Commission notes that the proposed rule in Case No. AX-84-3 would, under its own terms, be applicable beginning with the effective date of the Commission's Report and Order in a regulated company's rate application or tariff case next following the effective date of the rule.

Based on the foregoing, the Commission finds and concludes that the Company's proposal should be rejected.

H. Central Staff Organization. The Central Staff Organization (CSO) expense issue was set for hearing in early November, 1983. Prior to the date of hearing, the parties stipulated and agreed that the intrastate revenue requirement associated with the Central Staff Organization is \$10,986,000 for 1984. Exhibit No. 230 more fully sets forth the matters of agreement between the parties and is hereby incorporated herein by reference.

The Commission finds that the stipulation and agreement entered into by Staff, Public Counsel and Company on this issue is just and reasonable and should be approved.

VI. Rate Base

A. Original Cost Rate Base. Upon the competent and substantial evidence in this case, and adjusting for the Commission's determination with respect to the arrears billing issue, the Commission finds and concludes that the Company's net original cost rate base is \$1,288,482,000.

B. Fair Value Rate Base. The Company and the Staff have submitted to the Commission a Stipulation and Agreement as to the fair value rate base to be applied in this case (Hearing Memorandum, Joint Exhibit No. 150, pp. 7 and 8). As a result the Commission finds that the Company's fair value rate base is \$1,976,600,000.

VII. Rate of Return.

A. Capital Structure and Embedded Cost of Debt. The Company and the Staff agree to the following capital structure and embedded cost of debt to be used in determining Southwestern Bell's total cost of capital:

SOUTHWESTERN BELL TELEPHONE COMPANY
CAPITAL STRUCTURE AND EMBEDDED COSTS
FOR USE IN DETERMINING
SOUTHWESTERN BELL'S TOTAL COST OF CAPITAL

<u>Capital Component</u>	<u>Capitalization Ratio</u>	<u>Embedded Cost</u>	<u>Weighted Cost of Capital</u>
Debt	45%	9.37	4.2165
Common Equity	55%		
TOTAL	100%		

Department of Defense proposes a capital structure of 50 percent equity and 50 percent debt. Department of Defense also took the position that the cost of debt should be that of the senior securities of the Bell system which it calculates to be 8.85 percent. However, Department of Defense now accepts 9.37 percent as the embedded cost of debt.

The Commission rejects the proposals of the Department of Defense with respect to capital structure, since DOD's proposal is not based on the SWB capital structure actually required under the MFJ, which provides that SWB be spun off with a debt ratio no greater than forty-five percent (45%). Department of Defense has presented no adequate justification for using a hypothetical capital structure. Therefore, the Commission finds that the capital structure and cost of debt as agreed to by Company and Staff is appropriate for purposes of this case.

B. Return on Common Equity. Having determined the appropriate capital structure and cost of debt, the Commission must determine the return on common equity in order to arrive at the overall rate of return to be used in this case.

The Company proposes a cost of equity in the range of 16 to 17 percent with a recommended return of 16.5 percent. Staff contends that the Company's cost of equity is in the range of 13.16 to 14.65 percent. Staff recommends that the Commission adopt a return at the high end of its range, 14.65 percent. Department of Defense calculates a return on equity of 13 to 14 percent. Public Counsel supports the low end of Staff's range. In addition, the Public Counsel recommends that issuance costs be excluded from the cost of equity calculation. MoPIRG supports a 13 to 14 percent range.

In arriving at their respective recommendations, all parties utilized the discounted cash flow formula (DCF). The DCF model has consistently been approved by this Commission in rate case proceedings and the Commission continues to approve the method for purposes of determining a reasonable return on equity.

For the dividend yield portion of the formula Staff utilized 8.18 percent, the Company utilized 8.5 percent and Department of Defense utilized 7.5 percent to 9.5 percent. The differences in the dividend yield are attributable to the stock price utilized by the respective parties. The Company originally utilized a market price for AT&T stock of \$68.00 but updated its testimony to reflect a more recent market price of \$63.00. Staff utilized \$65.99, the average market price for AT&T during the first seven months of 1983. The dividend yield utilized by the Department of Defense does not appear to be based on recent AT&T stock prices. The Commission determines that the Staff's dividend yield is the most reasonable since it is based on a seven-month average of 1983 prices during a year of fluctuating prices.

For the growth rate portion of the formula, the Company utilized 7 to 8 percent, Staff utilized 5.27 percent to 6.27 percent and Department of Defense utilized 3 percent to 4.5 percent.

The Company's growth rate is based on three analyses: a review of past AT&T growth rates compared to the Gross National Product (GNP); the implied growth method which is based on the expected retention of future earnings; and a survey of investor expectations.

The Company's comparison of AT&T growth rates to the GNP resulted in expected growth rates ranging from 6.1 to 6.9 percent. However, the Company determined that Southwestern Bell's expected growth rate is at least 7 percent post divestiture. Based on its implied growth method Company calculated transition growth rates for AT&T ranging from 6.0 to 9.9 percent. Based on these figures the Company concludes that the expected growth rate of AT&T is at least 7 percent. Finally, inquiry was made to professional investors and analysts which led the Company to conclude that the investor expected growth rate is 7.5 percent.

Staff's growth rate is based on the earnings retention method and a review of past trends in AT&T earnings and dividends per share. AT&T's retention rate multiplied by Southwestern Bell's current authorized return for Missouri produced a 5.35 percent growth rate. Staff utilized a 5.77 percent plus or minus .50 percent which is based on the application of the retention rate to this Commission's most recent determination of AT&T's cost of equity. Staff's growth rate estimate was then compared to historic growth rates for the most recent five and ten year periods.

The Department of Defense's growth rate is based on a projection of the 12-month increase in book value for AT&T.

The Commission finds that the range of growth rates estimated by the Staff is reasonable and appropriate for purposes of this case. Staff's analysis recognizes to some degree the differences between Southwestern Bell and AT&T post divestiture. In addition, the range of Staff's growth rate is consistent with AT&T's historic growth rates in that it exceeds the growth rate for the most recent five years. In contrast, the Company's 7.8 percent growth rate is not based on either of the Company's first two analyses. Rather, it results from an upward adjustment to those values. With respect to the Company's investor survey, the Commission does not find such evidence to be persuasive. Further, the Commission finds the Department of Defense's growth rate to be inappropriate since it does not appear to bear any reasonable relationship to investor expected growth rates.

Both Staff and Company performed an upward adjustment to the required return to account for issuance costs. The Company recommends a 50 basis point adjustment to reflect the dilution to book value of existing shareholders when equity is issued based upon the actual experience of AT&T in its last five public offerings and in recognition of the five percent discount provided to the present shareholders for participation in the dividend reinvestment plan. Staff proposed a three percent adjustment to the required return on equity to reflect the cost incurred in the issuance of equity. The three percent value utilized by Staff is based on the issuance costs experienced by AT&T in six public offerings over the 1975-1982 period which was 2.68 percent of the issuing price.

The Commission finds that it is appropriate to adjust for issuance costs and that 3 percent should be allowed as proposed by Staff since that figure is consistent with historic issuance costs for AT&T.

Staff's DCF analysis utilized the infinite growth DCF formula (Formula I) and the finite growth DCF formula (Formula II). The current annual dividend in the finite growth model is multiplied by one plus the estimated growth rate while the infinite model does not adjust the dividend for growth. Staff asserts that the finite model is appropriate where the stock under consideration is growth oriented rather than income oriented, since Formula II takes into account capital appreciation in the finite future. In Staff's opinion AT&T stock reflects both growth and income, therefore, it has used the two calculations to arrive at its range of returns.

Staff also applies a market to book adjustment which multiplies the cost of equity after applying issuance costs by the market to book ratio. This results in a cost of equity applicable to book value. Although Staff originally applied the market to book adjustment to both DCF Formula I and Formula II, it now asserts that the adjustment should only be applied to Formula II and that Formula I should not be utilized unless the market to book adjustment is also applied.

The Commission is not persuaded that the market to book adjustment is necessary to ensure that overrecovery does not occur where market price is below book value or to ensure that underrecovery does not occur where market price is above book value. Further, the Staff has not adequately explained its contention that the market to book adjustment is necessary for the finite DCF Formula but is not appropriate for the infinite DCF formula. The market to book adjustment is designed to adjust for differences in market price and book value, which difference exists under either formula. Thus, it is unclear how the market to book adjustment relates to the period of time the stock is held. The Commission is of the opinion that the Company's cost of equity should be the investor required return on equity. Therefore, the Commission finds that the Staff's market to book adjustment should be rejected.

The Commission finds that the infinite DCF formula should be used for determining Southwestern Bell's cost of equity since the stock of Southwestern Bell, a regulated utility, will likely be regarded by investors as an income rather than a growth stock.

Based on the foregoing, the Commission finds that a reasonable return on equity for Southwestern Bell falls within a range of 13.87 percent to 14.90 percent. This range is also supported by Staff's comparable earnings analysis which the Commission finds to be reasonable. Staff's analysis estimates book equity returns of unregulated business to be in the range of 14.5 to 15.5 percent in 1984. Considering the risk differential of Bell and unregulated business the range herein found to be reasonable for Bell is comparable to the range of expected return for unregulated business.

C. Management Efficiency. As has been the procedure in recent rate cases, the Commission by Order of March 2, 1983, directed Company to provide evidence and argument sufficient for the Commission to determine: (1) the degree to which Southwestern Bell has efficient and economical management, and (2) whether a

Commission determination on this point should be utilized in setting Company's authorized return on equity or rate base. In an effort to comply with the Commission's directive, the Company sponsored the direct and supplemental direct testimony of Mr. R. D. Barron. Company's position is that its Missouri operation has been managed in an extremely efficient and economical manner for the past several years, and therefore requests that the Commission make an upward adjustment to its rate of return.

Mr. Barron's testimony touched upon several areas which Company perceived as being prime determinants for evaluation of management efficiency. Among the factors Company considered to be most important were: (1) the quality or level of service, and (2) the cost of providing that service. In addition to the evidence relating generally to quality and cost of providing service, Mr. Barron also listed several specific programs or items he believed demonstrated that Company is efficiently operated.

Company argues in its reply brief that the amount of adjustment to be granted is entirely within the informed discretion of the Commission based on the evidence before it in the record. The Company is of the opinion it deserves at least a forty basis point upward adjustment, such as was received by two other Missouri utility companies in their recent rate cases. Company believes that failure to grant Southwestern Bell such an award would indicate to the investment community that the Commission believes Southwestern Bell does not have efficient and economical management.

Staff contends that a determination of the degree to which the Company has efficient and economical management overall cannot be made based upon the evidence in this record. Staff asserts that Company's evidence concerning its cost-reducing programs, procedures and systems does not prove the Company is economically and efficiently managed; nor do work force reductions, quality of service or total factor productivity, in and of themselves. Staff's position is that the Commission should

be concerned with the quality of the Company's management and should pursue the development of methods for analysis of management efficiency. Staff also believes the Commission should look into the possibility of developing an incentive/disincentive program that would have a positive effect on how utilities are managed.

Staff asserts that, for Southwestern Bell, a comprehensive management audit is the best alternative available for evaluating management efficiency as it relates to all areas of Company operations. Staff notes that a single comprehensive management audit will not provide a quantitative measure of the Company's overall efficiency or economy. However, Staff further notes that it is not aware of any reliable quantitative method by which to determine and measure the overall efficiency and economy of management.

Public Counsel's position is that there is no evidence on the record which would support the reasonableness of a rate of return adjustment for management efficiency in this case. Public Counsel contends that in order to lawfully and successfully implement the Commission's management efficiency policy, certain information and evidence must be presented. First, Public Counsel believes there must be a showing by the utility that its management efforts are not only efficient and economical, but clearly superior to the prevailing standards governing such efforts. In order to determine whether a particular utility's management has performed in a superior manner, however, Public Counsel asserts there must be reliable standards and criteria established which the Commission can apply. Public Counsel contends that the evidence presented herein clearly indicates that no such standards or criteria currently exist. Second, Public Counsel argues that even if there existed reliable standards by which the Commission could measure various degrees of management efficiency, there must still be presented information and evidence which quantifies the appropriate amount to be included in any incentive award. Absent some positive showing on the record that the cost of the incentive is

less than the benefits which the Commission expects to be produced as a result of the incentive, the purpose of an upward adjustment for management efficiency would be defeated. Further, Public Counsel argues that, absent evidence as to what the appropriate amount of the adjustment should be, the Commission would "simply have to pick a number out of the air", and that such a decision would be undeniably arbitrary and capricious.

The Commission is not persuaded that the evidence presented herein is sufficient to support an adjustment to Company's rate of return. By so finding, the Commission does not intend to suggest or imply that it believes Southwestern Bell has inefficient management. The only inference to be appropriately drawn from the Commission's decision on this matter is that there was not presented sufficient and substantial evidence upon which to base a rate of return adjustment for management efficiency.

The Commission rejects Staff's recommendation that Company retain a private consulting firm for the purpose of conducting a comprehensive management audit at the present time. The Commission is of the opinion that although such an audit would be beneficial, Company should operate for at least one year in the post-divestiture environment before it is commenced.

The Commission would note that it anticipates initiating an investigatory proceeding in early 1984 for the purpose of examining methods for monitoring and encouraging management efficiency.

D. Summary. Based on the competent and substantial evidence presented by all of the parties, the Commission finds that the return on equity for Southwestern Bell to be used for purposes of this case shall be 14.70 percent, resulting in an overall rate of return of 12.30 percent.

VIII. Access Charge Rate Levels.

A. Overall. The rate structure and rate level methodology for access charges to be paid by interexchange carriers to local exchange telephone companies were the

principal subjects of the Commission's Report and Order, Part I in this case, issued on November 22, 1983.

The Company proposes access charge rate levels which are designed to produce revenues of \$60,216,000 to Southwestern Bell. This amount excludes the Egan adjustment, which is addressed below.

Staff proposed statewide access charge rate levels of ten percent (10%) above those proposed by the Company. Staff's original proposed access charge rate levels are designed to produce revenues of \$65,219,000 for Southwestern Bell. Staff later proposed to set access charges at ten percent (10%) above the levels set by the interim AT&T-SWB agreement, a proposal discussed and rejected above under "Procedural Background." Under Staff's statewide pooling proposal, which was approved by this Commission in Report and Order, Part I of this proceeding, Staff calculated a statewide toll pool revenue deficiency. Staff proposed that the toll pool deficiency be recovered through an End User Common Line Charge (EUCLC) of 33 cents per line. In the Commission's Report and Order, Part I of this proceeding, the Commission rejected any proposed EUCLC. Public Counsel recommended that access charges be set at rate levels "to generate the largest practical level of revenues from interexchange carriers . . .", but did not provide specific evidence from which to determine those levels other than indicating that they should be set at least ten percent (10%) above parity.

Having considered all of the evidence with respect to access charge rate levels, the Commission determines that access charge rate levels of ten percent (10%) above the Company's proposed access charge rate levels shall be used as a starting point for setting statewide access charge rate levels. The Commission further finds that the access charge rate levels should then be adjusted upward from the ten percent (10%) level in order to recover a portion of the estimated combined access charge pool and toll pool revenue deficiency in the manner described in Section VIII. C. below.

B. Egan Adjustment. Company witness Egan performed an adjustment which decreases the Company's access charge revenues. The final reconciliation filed by the parties (Exhibit 245) reflects that a downward adjustment to Company's estimated access charge revenues of \$3,893,000, and a downward adjustment to Staff's access charge rate level revenues of \$4,709,000, would occur as a result of applying the "Egan Adjustment".

The Company's adjustment attempts to quantify the extent to which access charge revenues will decrease as a result of bypass and customer shift from switched access to special access services.

Having considered the Company's adjustment and its underlying assumptions, the Commission finds that the Company has not shown that the assumptions contained in its customer demand study are reasonable. For example, toll service growth and the cost of bypass contained in the study are likely to be understated. Therefore, the Commission finds that the Company's adjustment should be rejected.

C. Toll and Access Charge Pool Deficiency. Based on Staff's pooling proposals and a 12.3 percent rate of return herein found to be reasonable, the estimated revenues to be derived from statewide interLATA access charge rate levels (set at ten percent (10%) above Company's proposed levels) and statewide intraLATA toll rates (set at existing levels) result in an estimated statewide revenue deficiency of \$9.4 million for the combined access charge and intraLATA toll pools.

The Commission determines that the toll pool should be made whole and that the deficiency should be recovered by increasing both access charges and intraLATA toll rates, but in a manner which will produce uniform statewide toll rates. That is, intraLATA toll rates shall be set equal to interLATA toll rates. In order to accomplish statewide uniform toll rates, the Commission determines that statewide access charge rate levels shall be set at 12.91 percent above the Company's proposed access charge rate levels, and that statewide interLATA and intraLATA toll rates (including MTS and WATS) shall be increased by 5.06 percent. This determination also

assumes a ten percent (10%) private line increase for ATTCOM which is addressed in Section XIII below.

The Commission is of the opinion that the access charge rate levels and toll rates approved herein result in the most reasonable and equitable solution to the problem of recovering the combined access charge pool and intraLATA toll pool deficiency. In addition, the Commission's determination herein is consistent with the Commission's goal of preserving the status quo to the extent possible during the first year of divestiture. This goal was enunciated by the Commission in Report and Order, Part I of this proceeding, in support of Commission's adoption of Staff's pooling proposals. See Report and Order, Part I, p. 65.

D. Ending Date of InterLATA Toll and Access Charge Pools. In Report and Order, Part I of this case, the Commission approved the access charge services tariff structure, to be effective for an interim one year period. The mandatory intraLATA and toll access charge pools were also established for an interim one year period.

Upon further consideration, the Commission determines that the access charge services tariff structure and the intraLATA toll and access charge pools, ordered in Report and Order, Part I, shall be in effect for an interim period which shall end no later than June 30, 1985, unless otherwise ordered by the Commission. This modification to the interim period set forth in Report and Order, Part I, will allow sufficient time for the independent companies to develop cost studies in an effort to allow a review of one full year's experience under the pools. This modification in no way relieves the independent average schedule Companies of the obligation to develop actual cost data during 1984 for use in determining rates to be in effect after 1984, as required by the Commission in its Report and Order, Part I, in this case.

IX. Access Services

A. Billing and Collection Services and Rates; Disconnection Authority. Under its proposed access services tariffs, Southwestern Bell would offer a number of ancillary

billing and collection services for interexchange carriers, including preparation and mailing of the bills for long distance services and collections of such bills from end user customers ("Bill Processing"). Southwestern Bell proposes to purchase the accounts receivable of interexchange carriers for bills rendered on their behalf by Southwestern Bell, at a discount from face value of the bills. The discount would be based on the uncollectible experience of the particular interexchange carrier involved. The proposed access services tariffs would empower Southwestern Bell to disconnect local exchange service for failure by customers to pay charges for services rendered by interexchange carriers where Southwestern Bell is performing billing and collection services for the interexchange carrier.

Approval of the disconnect provision of the proposed access services tariffs would also require that the Commission amend its rule 4 CSR 240-33.070(2), which currently provides as follows: "The failure to pay charges not subject to commission jurisdiction shall not constitute cause for a discontinuance." In P.S.C. Case No. TX-83-348, Re: Southwestern Bell Telephone Company Petition for Rulemaking, SWB proposes that the rule be amended to provide as follows: "The failure to pay charges not subject to commission jurisdiction shall not constitute cause for a discontinuance unless specifically authorized in telephone utility tariffs approved by the Commission." [Emphasis added]. The proposed amendment, which was published in the Missouri Register on August 1, 1983 (Volume 8, No. 8, Page 749), would permit the Commission to consider specific tariffs on a case by case basis authorizing disconnection of residential telephone service for nonpayment of, for example, interstate long distance charges and the interstate End User Common Line Charge (EUCLC) mandated by the Federal Communications Commission in its Docket No. 78-72. Southwestern Bell asserts that it will not be able to attract billing services business from interexchange carriers unless it has authority to disconnect for nonpayment for the services provided by those carriers. In addition, SWB would not be able to disconnect service for nonpayment of interstate, intraLATA charges

without the proposed rule change. Two of the Missouri LATAs cross state lines. (See Report and Order, Part I, Section I, p. 15).

The Company conducted cost studies concerning its billing services, and proposes to set its rates for those services at a level which is not only compensatory but which maximizes contribution to joint and common costs and basic exchange rates, to the highest level reasonably possible in an increasingly competitive market. Southwestern Bell has agreed to Staff's request that it perform a study of the incremental costs which SWB's principal billing customer, ATTCOM, would incur if it were to develop its own billing capability.

Staff initially opposed Southwestern Bell's disconnection proposal but, prior to the taking of testimony in this case concerning that proposal, Staff and Southwestern Bell reached a proposed settlement whereby the Staff withdrew its opposition. The Staff-Company agreement provides that the jurisdictional issue would be addressed in the briefs in this case, which subsequently did occur. Staff's primary motivation for withdrawing its opposition to the SWB disconnection proposal is the desire to avoid possibly jeopardizing Southwestern Bell's ability to market its billing and collection services to interexchange carriers and to retain AT&T Communications as a billing customer.

Public Counsel opposes the Company's proposals concerning discontinuance of service for nonpayment of bills, asserting that adoption of those proposals would constitute an abdication by this Commission to the FCC of its statutory duty to ensure that local telephone service is available to Missouri citizens at just and reasonable rates. The Commission will not abdicate to the FCC any of its statutory responsibilities. However, the ability of Southwestern Bell to disconnect local exchange service for failure to pay charges for interstate long distance service and interstate End User Common Line Charges is a feature which should be attractive to interexchange carriers and should be advantageous to Southwestern Bell in its attempt to attract and retain customers of its billing and collection services. Because

there should be little or no short-run incremental costs associated with Southwestern Bell's provision of billing and collection services for interexchange carriers, significant levels of contribution should be generated by the provision of this service. Such contribution ultimately benefits the general body of ratepayers and enhances the continued goal of universal service. Some ninety-three percent (93%) of Southwestern Bell's customers currently pay their bills, including toll charges, in a timely manner. To the extent that customers do not pay their bills, the result is higher uncollectible expense which, in turn, raises the level of rates paid by the general body of ratepayers.

The Commission finds and concludes that it is not preempted by any federal action or agency from authorizing the disconnection of service for failure by customers to pay interstate charges; that the proposed amendment to 4 CSR 240-33.070(2) in Case No. TX-83-348 is just and reasonable and should be approved in a separate order of rulemaking; and that Southwestern Bell Telephone Company's proposed billing and collection services tariffs in this case, including the rates and the proposed disconnection authority contained therein, are just and reasonable and should be approved.

B. Universal Service Fund. As stated in its Report and Order, Part I (Section XII., Pages 68-69), several parties to this case have proposed the establishment of a Missouri Universal Service Fund (USF). The Staff submits that the establishment of an intrastate USF may be necessary in order to maintain universal service at reasonable rates throughout Missouri.

The Federal Communications Commission has determined in its Docket No. 78-72 that an interstate USF will be established beginning on January 1, 1986. The interstate USF is to be funded by a minute-of-use charge imposed on interexchange carriers based on interstate usage. In FCC Docket No. 80-286, the Federal-State Joint Board recommended the establishment of an interstate high cost factor (HCF), geared to an exchange carrier's level of NTS costs per loop. Only carriers with NTS

costs per loop in excess of one hundred fifteen percent (115%) of the nationwide average will receive any benefits from the interstate USF.

Although no party to this proceeding has recommended the establishment of a Missouri USF prior to January 1, 1986, the Commission is very concerned that such a fund may be necessary and desirable in order to promote and preserve universal service by maintaining local exchange rates at reasonable levels. As the Missouri intrastate telecommunications industry moves toward the deaveraging of prices in the new competitive era, it will be increasingly difficult for the companies to maintain reasonable levels of basic exchange rates. This is true even without adopting the FCC's ill-advised program of shifting all NTS costs to the end user customer.

However, before a Missouri Universal Service Fund could be established, more specific information would be required concerning the need for an intrastate USF, and methods of funding and distributing same. In assessing the need for a Missouri USF on an on-going basis, the type of notification requested by the Commission concerning Southwestern Bell's local measured service (LMS) proposals hereinbelow could be significant. (See Section XII. L. 3., "LMS/Budget LMS", where the Commission requests information from the Company should SWB become aware that a significant number of local exchange customers are leaving the system.) If any telephone company or other interested party perceives a more immediate need for a Universal Service Fund in Missouri, that company or party should file an appropriate pleading with the Commission and be prepared to present recommendations as to reasonable methods for financing, and for distributing the proceeds of, such a fund. In the meantime, the Commission will closely monitor (1) the impact of the rates authorized in this case on universal service in Missouri; (2) the progress of the federal USF; (3) the effects on high cost companies of the shift of interstate NTS costs to end user customers; and (4) the effects on Missouri telephone companies of the deaveraging of intrastate rates.

C. Notice to Customers Concerning Federal End User Common Line Charge. Under the orders of the Federal Communications Commission in Docket No. 78-72, an End User Common Line Charge (EUCLC) is to be established in 1984 at the level of \$2.00 per month per residential customer and \$6.00 per month per business customer. This federal EUCLC is designed to implement an FCC policy of shifting, over a six (6) year period, virtually all non-traffic-sensitive (NTS) local loop costs out of usage-sensitive toll rates to end user customers on a flat rate basis. In its Report and Order, Part I, in this case, this Commission has rejected Southwestern Bell's proposal to establish an intrastate Missouri EUCLC and has expressly rejected the policy of the FCC to shift all NTS local loop costs to the end user customer. The federal Exchange Carriers Association (ECA) tariffs implementing the FCC's access charge plan, including the EUCLC, are currently under suspension by the FCC until April 3, 1984.

The Commission determines that Southwestern Bell should include with its bills on which the federal EUCLC first appears, a special notice to all of the Company's Missouri customers advising those customers that the federal EUCLC is required by the Federal Communications Commission and not the Missouri Public Service Commission. In addition, the Company's bills shall clearly designate the EUCLC itemized charge as a "Federal" End User Common Line Charge, not merely as an End User Common Line Charge.

X. Quality of Service.

For purposes of this case Staff reviewed quarterly reports submitted by the Company to the Commission regarding quality of service criteria established by 4 CSR 240-32.080; investigated the level of service being provided by selected central office facilities; and investigated the level of service being provided by outside plant facilities in selected exchanges. Staff states that its quality of service investigation in this case involves a review of facilities in selected exchanges and

Staff does not assert that the exchanges and facilities reviewed are necessarily representative of Southwestern Bell's statewide operations. Based upon its continuing review, Staff believes that the statewide quality of service being provided by Southwestern Bell in Missouri is generally good.

Southwestern Bell believes that it is providing excellent, high quality service to its customers, and notes that there were virtually no service complaints voiced by those individuals testifying at the five public hearings conducted around the State in connection with this case.

For purposes of this case, Staff and Southwestern Bell stipulate and agree as follows:

1. Southwestern Bell agrees to investigate the situations in its Climax Springs and Gravois Mills exchanges regarding recent deficiencies in meeting the Commission's surveillance levels for the category "Percentage of regular service or installations completed within five working days", and shall report to the Commission, within 30 days of the effective date of the Report and Order in this case, regarding actions Southwestern Bell intends to take in order to correct the situation;
2. Southwestern Bell agrees to investigate the situation in its Paynesville exchange regarding recent deficiencies in meeting the Commission's surveillance level for the category, "Trouble reports per 100 telephones", and shall report to the Commission within 30 days of the effective date of the Report and Order in this case, regarding actions Southwestern Bell intends to take in order to correct the situation;
3. Southwestern Bell agrees to take action to clear all major cable pair faults as identified in the prefiled direct testimony of Staff witness LeBlanc. Southwestern Bell and Staff recognize that, due to the sensitivity of the testing equipment used, a finding of cable pair fault is not necessarily indicative of an out of service condition or even perceptible to the customer. Said major cable pair faults shall be cleared within six (6) months of the effective date of the Report and Order in this case, except in instances where extraordinary circumstances require the granting of additional time. Southwestern Bell shall file monthly status reports with the Commission, beginning 30 days after the effective date of the Report and Order in this case, detailing the progress made in clearing said major faults. The monthly status reports shall be filed with the Commission until all said major faults are cleared. Further,

Southwestern Bell agrees to report to the Commission within 30 days of the effective date of the Report and Order in this case, regarding the development of a method to clear the major faults identified in Staff investigations.

The Commission finds that Southwestern Bell provides high quality service, and that the agreements between Southwestern Bell and Staff are reasonable and should be adopted. Therefore, the Commission finds that Southwestern Bell shall perform the investigations and file the designated reports with regard to the three matters set forth above.

XI. Revenue Requirement For Southwestern Bell.

Based upon the determinations of the Commission herein, Southwestern Bell's total net operating income requirement is \$158,483,000. The net operating income available for purposes of this proceeding is \$66,232,000, leaving a net operating income deficiency of \$92,251,000. After applying a factor for income tax and adding the amount related to uncollectibles Southwestern Bell's total revenue deficiency in this proceeding is found to be \$181,612,000.

XII. Rate Design.

The parties have submitted to the Commission differing proposals for the distribution of the revenue requirement determined in this case among the various classifications and categories of customers of the Company. This distribution of the revenue requirement among customer classes is referred to as "rate design." The specific rate design issues presented to the Commission in this case, some stipulated and some contested, are set out below.

A. Toll. Company has proposed several minor changes in the way toll rates are applied. Specifically, Company is proposing to implement rate specific billing, so that a toll customer will pay the rate applicable to the time of day during which a toll call actually takes place, rather than just the rate applicable when the call is initiated. For example, a call which begins at 7:45 a.m. and lasts until 8:15 a.m. would presently be billed entirely at the discounted night rate, which is in effect

until 8:00 a.m. Under Company's proposal, the first fifteen (15) minutes of that call would be billed at the night rate, but the last fifteen (15) minutes would be billed at the day rate. The Company asserts that this type of rate application is more closely related to the costs actually caused by a particular call.

In addition, the Company proposes to eliminate the holiday discount for resultant legal holidays. That discount is currently available when certain holidays are observed on days other than their actual date. Company's experience shows that the current practice has failed to stimulate additional toll calling on the designated holidays.

The third SWB proposed toll change concerns the rate treatment for calls billed to special billing numbers. This change will result in customers who utilize such service paying the operator station-to-station service charge per call (\$1.05), rather than the charge applicable to dial credit card station-to-station calls (\$.30). Special billing number calls must be handled by an operator and the procedures involved are more similar to operator station-to-station calls than dial credit card station-to-station calls.

The aggregate revenue impact of the three (3) proposed changes is approximately \$64,000. Staff supports these proposals, and no other party opposes them.

The Commission determines that Southwestern Bell's proposed changes in toll rate structure are just and reasonable and should be approved.

Public Counsel recommends a general increase in intraLATA toll rates, and suggests the desirability of maintaining uniform statewide toll rates. An increase in intraLATA toll rates is one of the options available to the Commission for making whole the mandatory pools established pursuant to the Commission's access charge decision in Report and Order, Part I, in this case. The Commission has determined that intrastate toll rates should be increased in this case, as discussed above. (See Section VIII. C., "Toll and Access Charge Pool Deficiency").

B. Service Connection Charges. Staff, Public Counsel and the Company entered into a Stipulation and Agreement on this issue which is embodied in Exhibit No. 100. Under the terms of the agreement, those three (3) parties recommend approval of the Company's proposed rates for service and equipment (S & E) service connection functions, with the exception of the proposed S & E for residence access. S & E functions include the cost of service ordering and central office work (not premises work) associated with service connection activities for the Company's various services. With regard to residence S & E, Company and Public Counsel have agreed to recommend a rate of \$32.15, while Staff supports a rate of \$39.00. SWB's identified cost associated with the residence S & E function is \$49.25, and the current rate is \$21.90.

The proposed S & E rates for other services are set at a level equal to the costs identified in the Company's S & E cost studies. This is consistent with this Commission's Report and Order in Case No. TR-82-199 (Page 83) in which SWB was directed to file fully compensatory service connection charges in this case.

Public Counsel and Staff have also agreed to support the introduction of time sensitive premises work charges as proposed by SWB. These time sensitive charges will replace the current flat rate trip and premises wiring charges which apply to service connection functions performed on the customer's premises. The proposed time sensitive charges are based on a cost study which analyzes the cost of providing such services in fifteen (15) minute increments. The proposed rates are set at levels equal to the costs identified in Company's study. The recommended rates for both residence and simple business are \$27.25 for the initial fifteen (15) minutes, and \$9.50 for each additional fifteen (15) minutes. The initial fifteen (15) minutes includes the costs associated with travel, labor, material and dispatch; while subsequent fifteen (15) minute increments include only labor and material. This proposal allows a disaggregation of the current flat rate premises work charges and will result in individual customers paying only for the actual time an installer is required to spend on their premises.

The Commission determines that the matters agreed to by Company, Staff and Public Counsel are just and reasonable and should be approved. In addition, the Commission determines that the Staff's proposed residence S & E rate of \$39.00 should be approved. The revenue effect of this decision is \$11,992,000.

C. Complex Inside Wire. Complex inside wire is used by complex customers, such as key and PBX, to connect their station equipment with the common equipment on the premises. Under its proposed tariffs in this case, Southwestern Bell would not own or install any new complex inside wire, nor maintain any existing wire for complex business customers in the future. The personnel who previously did this work for Southwestern Bell will be transferred to AT&T Information Systems (AT&T-IS) at the time of divestiture, pursuant to the requirements of the Modified Final Judgment (MJF), and AT&T-IS anticipates providing maintenance for both embedded and new complex wire.

Under the Company's proposal, such customers could obtain the wiring in the future from the vendor of their terminal equipment or from an independent contractor. Although Company would no longer install or maintain complex inside wire under its proposals, it would continue to install and maintain simple inside wire for residential and business customers. No party has opposed this portion of the Company's proposal, and Staff supports it.

Under the MJF, Southwestern Bell will also transfer to AT&T-IS at the time of divestiture all of SWB's embedded base customer premises equipment (CPE), including the common and station equipment currently served by complex inside wire. The transfer of such common and station equipment to AT&T-IS without the transfer of the complex inside wire which serves that equipment will leave Southwestern Bell in the position of being interposed between the CPE supplier and the supplier's customer. Southwestern Bell has to change the basis for its charges for complex wire, since it will no longer have records indicating the type of common equipment or the number of stations attached to that equipment with Southwestern Bell's complex inside wire.

Therefore, Southwestern Bell proposes to implement a monthly charge for the use of existing complex inside wiring which has been capitalized on the books of the Company. The proposed monthly charge would be applied to each access line for each complex customer which utilizes Company wiring, and would be billed to the owner of the customer premises equipment. The proposed charge would continue to apply only until the embedded base of complex wire has been amortized. If station equipment and common equipment are not owned by the same person or entity, the owner of the common equipment would be billed for the complex inside wire. Customers would be able to avoid the monthly charge by buying the complex wire from the Company or installing their own wiring. In conjunction with this proposal, Company proposes elimination of the extension station line charge currently billed to Centrex C.O. customers, due to the fact that SWB will be billing the owner (AT&T-IS) a monthly charge for the complex wire associated with such stations.

The revenue requirement associated with SWB's complex inside wire proposal is \$18,179,000. AT&T-IS opposes Southwestern Bell's proposal to charge the owner of the customer premises equipment for the use of the complex inside wire, and contends that the revenue should be allocated to the general body of ratepayers. This proposal could increase each individual ratepayer's monthly bill by approximately \$.95, assuming that the approximately \$18.2 million were spread equally among all access lines.

Southwestern Bell does not generally own the wire associated with terminal equipment supplied by non-Bell companies. Rather, SWB generally owns wire only in its own terminal equipment installations, which are to be transferred to AT&T-IS at the time of divestiture. The Company's proposal that the monthly charge for the use of existing complex inside wire should be based upon the number of access lines leading to the common equipment is supported by the fact that there is a direct relationship between the number of access lines and the amount of wire used on the premises of a complex customer.

AT&T-IS raises a series of factual and legal arguments in opposition to Southwestern Bell's proposal. The Commission finds those arguments to be lacking in merit. Staff and Public Counsel support the Company on this issue.

The Commission finds and concludes that Southwestern Bell's proposals concerning complex inside wire are just and reasonable and should be approved.

D. Joint User Service. Joint user service involves a directory listing provided in connection with business exchange services which are shared by two (2) or more customers. SWB proposes to convert all joint user customers to the current business additional listing charge due to the fact that after January 1, 1984 the Company will have no practical way of knowing how many businesses are sharing telephone equipment and services. The annual revenue impact of this proposal is a negative \$32,000. Staff supports Company's proposal, and no party has expressed any opposition to it.

The Commission finds and concludes that the Company's proposal is just and reasonable and should be approved.

E. Elimination of Special Message Rates. Special message rate service, which includes one hundred (100) local messages for a flat rate and a charge of \$.10 for each call over the allowance, has been utilized by business customers at exhibitor locations, temporary locations, booth locations, etc. Similar rates have also been utilized by hotels and motels in exchanges where Message Rate Service was not available. Southwestern Bell at one time required that trunks furnished for hotel branch exchange service for the use of hotel/motel guests be on a message rate basis. That practice ceased in 1975. Business customers who previously utilized Special Message Rate Service options will now be required to choose from one of the local exchange options utilized by other customers. The annual revenue impact of this proposal is \$87,000. Staff supports this proposal, and it was not opposed by any party.

The Commission finds and concludes that the Company's proposal is just and reasonable and should be approved.

F. Elimination of No-Charge Trunk Arrangements from Hotels/Motels to Long Distance Operator for Handling Hotel/Motel Guest Toll Calls. Concurrent with

divestiture, Southwestern Bell has proposed to discontinue the practice of providing, without charge, special trunks from hotels/motels to long distance telecommunications operator positions for handling hotel/motel guests calls. Such trunks were provided to hotels/motels to facilitate guests' long distance calling. Since effective with divestiture SWB will cease providing a significant portion of its long distance services, this practice is no longer deemed appropriate. This proposal will impact approximately three hundred twenty (320) customers. Staff concurs in the proposal, and it was not opposed by any party. The Missouri Hotel/Motel Association intervened in the instant case, but withdrew its intervention prior to hearing.

The Commission determines that the Company's proposal is just and reasonable and should be approved.

G. Announcement Distribution Services. Pursuant to the rate structure approved by this Commission for announcement distribution services in Case No. TR-83-52 (Report and Order issued April 13, 1983), most announcement system customers pay the 1FB (flat rate business line) rate for each line they utilize in the provision of announcement services. A few customers pay usage-sensitive rates on a "grandfathered" basis. Southwestern Bell has proposed increases in its 1FB rates in this case, and any approved increase in such rates will apply to announcement system customers. To provide equitable treatment among all announcement system customers, Company is proposing to increase the grandfathered usage-sensitive rates proportionally to the 1FB rates. All parties to Case No. TR-83-52 were made aware of this proposal. The additional annual revenue impact is approximately \$110,000, which is included in the residual revenues associated with local exchange service. Staff concurs in this proposal, and it was not opposed by any party.

The Commission determines that the Company's proposal is just and reasonable and should be approved.

H. Private Line. Company, Staff and Public Counsel reached substantial agreement as to a joint recommendation regarding private line services in this case, as set forth in Exhibit No. 100. Those three (3) parties all support Commission approval of Southwestern Bell's proposal to increase less-than-a-mile private line local channel rates up to the full local channel rate approved by the Commission in Case No. TR-82-199. Company cost studies demonstrate that all local channels cost the same to provide. The annual revenue impact of this proposal is in excess of \$7,000,000. Missouri Alarm Association (MAA) opposes this recommendation unless the Commission uses the cost study submitted by MAA in this case for private line services.

Although the Company initially proposed no increases for other intralATA private line services in this case, Company did reach agreement with Public Counsel to recommend a ten percent (10%) increase for all private line services which the Company will continue to provide after divestiture, with the exception of One Hundred (100) Series private line services. Staff substantially concurs in that recommendation, except that Staff also recommends that the proposed ten percent (10%) increase to private line services be applied to One Hundred (100) Series services. Applying the ten percent (10%) increase to One Hundred (100) Series private lines would further increase private line revenues in this case by \$727,000. The total revenue effect of the Public Counsel-Company stipulation would be \$10,127,000. The total revenue impact of Staff's recommendation would be \$10,854,000.

MAA proposes a decrease in currently approved One Hundred (100) Series private line rates in this case, based upon certain cost studies requested by MAA and directed by the Commission in Case No. TR-82-199, as modified by agreement of the Company and MAA due to the time constraints of this proceeding. MAA asserts that this "compromise" embedded cost study shows that private line rates are currently overstated by at least two to one. MAA insists that the proposed elimination of the rate differential for less-than-a-mile local channels should be rejected unless all

loop rates, on an interim basis, are set at the embedded rate indicated by Method II of Mr. Zubkus' "compromise" embedded cost study endorsed for purposes of this case by MAA.

Company's incremental private line studies, as presented in Case No. TR-82-199, indicate that current One Hundred (100) Series private line rates are just recovering cost. In addition, the Company's 1982 EDA indicates that intraexchange subvoice private line revenues (which include One Hundred [100] Series services) fail to fully recover embedded costs. Thus, Company opposes any decreases in any One Hundred (100) Series rates in this case, and asserts that a decrease of One Hundred (100) Series private line rates on the basis of MAA's suggested cost methodology would produce a discriminatory result as to other private line customers.

Upon the evidence of record in this case, the Commission cannot conclude either that the less-than-a-mile rate differential is cost justified and reasonable, or that the cost study upon which MAA urges that private line rates be set is reasonable and should be relied upon. Rather, the Commission finds and concludes upon the evidence herein that the Stipulation and Agreement of the Company, Staff and Public Counsel to increase less-than-a-mile private line local channel rates to the full local channel rate is just and reasonable and should be approved. In addition, the Commission finds and concludes that all private line rates, including those for One Hundred (100) Series services, should be increased by ten percent (10%), as recommended by the Staff.

Southwestern Bell also proposes in this case to cease providing installation of on-premises private line channels, and to obsolete on-premises private line channels to existing installations at existing locations for existing customers. No opposition was stated to this proposal, and the Commission determines that it is just and reasonable and should be approved.

Finally, Southwestern Bell proposes that carriers should not be allowed to order facilities from the Private Line Tariff in connection with their provision of

MTS (toll) type services, but should order those services from SWB's Access Services Tariff. This proposal of SWB has already been approved by the Commission in its Report and Order, Part I, in this case.

I. Centrex C.O. Southwestern Bell's proposals for Centrex C.O. (Central Office) services are before the Commission in Case No. TR-83-288, which has been consolidated with Case No. TR-83-253. Southwestern Bell proposes the institution of a Rate Stability Plan (RSP) for its Centrex C.O. Customers. Under the terms of the plan, customers could choose to enter into a three (3) year contract under which a portion of the Centrex station rate would become "fixed" (i.e., not subject to Company-initiated change) for the contract period. The exchange access portion of the Centrex station rate, which is based on a relationship to the PBX trunk rate, would not be fixed under the contract and would remain subject to change initiated by the Company. At the end of the contract period, the customer could enter into a new contract at the then-effective rate, or opt for the month-to-month payment option. Customers who do not wish to enter into the RSP contract can subscribe to or continue with the current month-to-month option, the rates for which would continue to be subject to Company-initiated change. The Company has proposed a stabilized rate which represents a reduction in a portion of the Centrex C.O. station rate, on the basis of updated cost studies. This reduction was approved on an interim basis by the Commission on June 20, 1983 in Case No. TR-83-288.

Southwestern Bell asserts that it requires an even lower rate than it is currently proposing in order to maintain Centrex C.O. service at a competitive rate level. However, at the present time, SWB asserts that it cannot recover its incremental costs plus any contribution from a lower rate than has been proposed in this case. SWB will continue to study ways to reduce its costs of providing Centrex C.O. service. The Company submits that the Rate Stability Plan will make continued use of Centrex C.O. service more attractive to Centrex customers, thereby strengthening SWB's competitive position. McDonnell Douglas Aircraft Corporation,

which was SWB's largest Centrex C.O. customer, recently announced plans to leave Centrex C.O. in favor of service offered by an SWB competitor.

Staff and the State of Missouri support the Rate Stability Plan, although the State argues that the RSP should also apply to the exchange access portion of the Centrex station line rate. This, however, would insulate Centrex C.O. customers from rate increases which would apply to all other customers for access to the network. The State would also like the protection of the RSP without binding itself to a three (3) year commitment, which it is precluded by law from doing. While the Commission regrets the State's legal infirmity in this regard, it is not persuaded that it would be just and reasonable to give the State the protection of the RSP without a firm three (3) year commitment by the State to the RSP.

Public Counsel asserts that Centrex C.O. rates do not recover their embedded costs, as calculated by Public Counsel's fully distributed cost study submitted in this case. Therefore, Public Counsel believes it is inappropriate to exempt portions of the Company's Centrex services from Company-proposed increases for a three (3) year period, particularly in light of the significant rate increases being requested by the Company for local exchange service.

The Commission determines that the Company's Rate Stability Plan, and its proposed rates for Centrex C.O. services in this case, are just and reasonable and should be approved.

SWB also proposes to eliminate the extension station line charge for Centrex C.O. customers, if the Commission approves the monthly complex wire charge proposed by SWB in this case. As discussed hereinabove, the Commission has approved that monthly complex inside wire charge. (See Section XII. C., "Complex Inside Wire," above). The Company's proposal to eliminate the extension station line charge for Centrex C.O. customers is also hereby approved.

J. Coin Calls. Southwestern Bell has proposed no increase in the current \$.20 charge for calls placed from coin telephones. Pursuant to Commission order, the

Company did file a new cost study on coin service which demonstrates that the provision of coin telephone service would lose money even at a \$.25 per call rate. A \$.25 coin rate would increase gross annual revenues of the Company by approximately \$813,000. No party has proposed or expressed support of such an increase, however.

The Staff originally proposed a \$.20 surcharge for each intrastate toll call from a coin telephone. Due to perceived problems of implementation of such a proposal, however, Staff withdrew that recommendation and requested Southwestern Bell to perform a study, which the Company has agreed to do.

The Commission determines that no change in current coin telephone rates should be ordered in this case.

K. Custom Calling. Pursuant to an order of the Commission, Southwestern Bell performed an updated long-run incremental analysis (LRIA) for its custom calling services in this case. Although Company had initially proposed no increases in custom calling rates, Staff and Company ultimately entered into a joint recommendation to increase the rate for call waiting service from \$4.35 to \$8.00 per month for residence service, and from \$5.50 to \$10.10 for business, while maintaining existing rates for call forwarding, three-way calling and speed calling. This proposal is consistent with the updated LRIA which indicates that increases in the latter three (3) services would actually decrease contribution, while increases in the rates for call waiting would increase contribution levels.

The Commission determines that the joint recommendation of the Staff and Company is just and reasonable and should be approved.

L. Local Exchange. The Company has proposed significant increases in all local exchange and Outside Base Rate Area (OBRA) mileage rates. Company asserts that its studies (Embedded Direct Analysis or EDA, Rate Group Analysis or RGA, and Exchange Class of Service Study or ECS), indicate that on an embedded basis the cost of providing local exchange services greatly exceeds the revenue from such services. In addition, the Company points out, the revenues associated with terminal equipment

and interLATA toll, which have traditionally been used to hold down local exchange rates under residual pricing, will be lost to the Company upon divestiture. It is the Company's position that local exchange rates must increase in order to recover a greater portion of the cost of providing such services. Company also proposes a new "budget" local measured service (LMS) offering, and an "interim" LMS rate plan, in addition to its currently existing LMS offering, which SWB asserts are designed to mitigate the impact of necessary increases upon residential customers.

1. 1FB, PBX Trunk, Multiline, Mobile Access. The rates for PBX trunks, multilines and mobile access are currently established on the basis of a relationship to the flat rate business line rate (1FB). Company has proposed to substantially increase the rates for all these services and to change the rate relationships as follows:

	<u>RELATIONSHIP TO 1FB</u>	
	<u>Present</u>	<u>Proposed</u>
PBX Flat Rate Trunks	155%	130%
Multiline	105%	130%
Mobile Access	50%	55%

Currently, the determining factor in application of either the PBX trunk or multiline rate is whether the facilities terminate in switching equipment which is used for the random access of outgoing calls (PBX trunk), or in equipment which allows pickup by associated stations (multiline). The distinction as to whether multiline or PBX trunk rates should apply to a given customer has always been difficult to administer in the past, and will become virtually impossible to administer upon divestiture when Southwestern Bell will no longer have a record of what equipment is terminated at the end of the local exchange facility. The Company also proposes that the rate for mobile access be set on the same basis as the rates for business LMS access, since mobile customers, like LMS customers, receive only access for a flat rate and then must pay a usage charge for each call. The mobile usage rate, however, is based on a LRIA, and is significantly higher than the current usage rates for LMS.

These proposed revisions in rate relationships are supported by the Staff, and are not opposed by any party. The Commission determines that the Company's proposals are just and reasonable and should be approved.

The Company and Staff also recommend a modification of the current rate relationship between 1FB and 1FR (residence flat rate) service in this case. This recommendation is discussed below in Section XII. L. 7., "Business/Residence Relationship."

2. One Party Flat Rate (1FR/OBRA). Company proposes to increase the one party flat rate by \$4.40 per month in each rate group. Company's \$4.40 figure includes the \$1.00 per month which would have been designated as an End User Common Line Charge (EUCLC) rate component if that component had been approved by the Commission in its access charge rate structure order (Report and Order, Part I, in this case issued on November 22, 1983). Company and Staff both propose to increase OBRA mileage rates. Staff also agrees with the Company that any increase in the 1FR rates should be applied in the same amount to each rate group. This proposal would result in larger percentage increases in the smaller rate groups, which currently recover a smaller percentage of their costs than the larger rate groups.

Public Counsel contends that local exchange rates, including 1FR, should increase only residually, if necessary, and that SWB's recurring argument that local rates have long been subsidized by toll and terminal equipment charges is a "myth". Public Counsel's witness testified that local exchange revenues exceed their costs and provide a positive return to the Company of 11.5%. That determination was based upon a 1982 fully allocated cost study. That cost study allocated fifty percent (50%) of access line investments and costs to toll, allocated traffic sensitive central office costs from local to toll, and allocated all Yellow Pages advertising revenues to local exchange service. The study also ignored certain expenses of providing access to the network such as marketing, the handling of service requests, accounting costs, and operators' wages.

The Company submits that its rate group analysis (RGA) and its ECS study both indicate that even the Company's proposed 1FR rates would not fully compensate the Company for the cost of access to the network and unlimited local calling.

There is no evidence upon the record of this case of the incremental cost of local exchange service. Of the several economists who testified in this case, only Public Counsel's economic witness concluded that existing local exchange rates fully recover costs. That conclusion is based upon a cost study which may have inherent defects, however, such as the failure to consider certain expenses as stated above.

The Commission need not determine whether existing or proposed local exchange rates recover the exact cost of providing local exchange service. All parties agree that local exchange rates should be increased residually in this case. The Commission concurs, and also agrees that any increase in local exchange rates should apply in the same amount to each rate group, as proposed by the Staff and the Company. The Commission also determines that OBRA mileage rates should be increased residually, also as proposed by Company and Staff.

3. Local Measured Service. The Company presently has a permanent local measured service offering which has been referred to in this case as "Standard LMS". The rate structure for "Standard LMS" consists of an access line charge and a usage charge which is based on the following rate elements: time of day, duration, distance, and occurrence. The access line charge for "Standard LMS" is 55 percent of the one-party flat rate "1FR" residential charge.

a. Budget LMS. The Company is proposing to offer "Budget LMS" in addition to its "Standard LMS" offering. The access line charge for "Budget LMS" is proposed to be set at 30 percent of the "1 FR" rate. The usage rate would be the same as the rate for "Standard LMS", but a 20-cent charge would be imposed on each outgoing call. Staff, Public Counsel and MoPIRG oppose this proposal.

b. Interim LMS. The Company also proposes to offer "Interim LMS" to customers located in exchanges where LMS is not available. "Interim LMS" offers a discounted one-party flat rate service (an approximate \$6.00 discount) until LMS is available. The customer would agree to initiate LMS where it becomes available and maintain LMS for a period of time at least equal to the length of time over which the customer utilized the "Interim LMS", or 12 months, whichever period is shorter. The customer would be assessed a \$6.00 per month penalty for the number of months by which the customer's use of LMS falls short of the period of "Interim LMS" service. Staff, Public Counsel and MoPIRG oppose the Company's proposed "Interim LMS" offering.

c. Waiver of Service and Equipment Charges. The Company is requesting an additional waiver of service and equipment (S&E) charges associated with LMS. Presently S&E charges are waived when a customer switches to or from LMS during a 180-day period subsequent to the initiation of LMS in the customer's area. In addition to this existing waiver, the Company proposes that S&E charges be waived for customers switching to or from LMS for a 90-day period following the effective date of each general increase in the Company's local exchange rates. The Staff, Public Counsel and MoPIRG oppose the Company's proposed 90-day waiver.

d. Discount Periods. The present discount periods for LMS match the discount periods for intrastate toll rates. The Company proposes to change the LMS usage discount periods such that there are two time-of-day periods, 9:00 a.m. to 9:00 p.m., and 9:00 p.m. to 9:00 a.m. The Company proposes a 50-percent discount for its night/weekend discount period. Staff, Public Counsel and MoPIRG oppose the Company's proposed change of discount periods.

e. Commission Determinations. The Commission determines that all of the above proposals (Budget LMS, Interim LMS, extension of the waiver of S&E charges, and the change in the discount periods) should be rejected. Absent evidence that the Budget LMS is necessary to accommodate customers who would otherwise leave the system, the Company's proposed offering could create a shortfall in revenues which could result

in increases to flat rate local service. Interim LMS also results in a loss of revenues to the Company which is unwarranted at this time. Similarly, the extension of S&E waivers as proposed by the Company results in additional costs being imposed on the general body of the ratepayers which otherwise would be imposed on those requesting the service. Finally, the Commission finds that a change in the LMS usage rate discount period does not appear to be cost justified and will promote customer confusion because of the disparity with the toll discount period.

In arriving at its conclusion, the Commission has considered the fact that both the Public Counsel and MoPIRG, who represent the general body of ratepayers and low income ratepayers respectively, and Staff, oppose additional LMS offerings. The Commission continues to be concerned with the goal of universal service and, therefore, if the Company should become aware that a significant number of local exchange customers are leaving the system, the Company should inform the Commission. In the event of such an occurrence, the Company should continue to assess variations to the LMS offering which would promote universal service, if the present LMS offering does not appear to be accomplishing that purpose. Such variations could include the use of less than all four rate elements. To this end, the Company should submit such proposals to the Commission. Finally, the Commission determines that the Company shall refer to the existing LMS offering as "Local Measured Service" and not "Standard Local Measured Service" as it has been used in this case.

4. Optional Measured Metropolitan Exchange Service (OMMES). Southwestern Bell and the Staff have agreed both that the monthly rate for OMMES should be increased and that, because this service is essentially a discounted toll service for those customers who subscribe to it, the percentage increase should be 8.4% (which is equal to the percentage increase in toll services which occurred in Case Nos. TO-82-3 and TR-82-199), plus any percentage increase in toll rates ordered in this case.

The Commission determines that the joint recommendation of the Company and Staff concerning OMMES monthly rates is just and reasonable and should be approved.

5. Arrears Billing. Staff has proposed to eliminate arrears billing for the group of customers in the St. Louis metropolitan area who are billed for local service in arrears. The majority of Southwestern Bell's customers are billed for local service in advance of the receipt of their service. This issue is discussed hereinabove in Section V. E., "Arrears Billing." The Commission has found above that the Company's current billing practices at issue here are discriminatory, and that those customers who are currently billed in arrears should be converted to advance billing over a ten-month phase-in period.

6. EAS Studies. Company has agreed to undertake, and to complete within nine (9) months of the effective date of the Report and Order in this case, if possible, certain extended area service (EAS) studies described in Staff's testimony. Such studies may form the basis of a Company and/or Staff recommendation regarding EAS rates or service in future proceedings.

7. Business/Residence Relationship, 1FB to 1FR. The Company has proposed a change in the current rate relationship between 1FB (flat rate business line rate) and 1FR (flat rate residential line rate) service rates in this case. Under the Company's original proposal, 1FB rates in Rate Group D would have been set at 2.5 times the 1FR rate, instead of the current 2.97 times. The Staff originally opposed any change in the current relationship of 1FB to 1FR rates. However, in the Hearing Memorandum on rate design (Exhibit No. 1), Staff agreed not to take issue with a lesser reduction in the Group D relationship, from 2.97 to 2.87. Southwestern Bell now states that it is willing to accept a change from 2.97 to 2.87 for purposes of this case. Company and Staff agree that all other existing business/residence rate relationships should be maintained at approximately the existing levels.

Public Counsel opposes a reduction in the rate relationship between 1FB and 1FR service on the grounds that there is no competent and substantial evidence upon the record of this case to support such a reduction. Company's original proposal would have shifted approximately \$25.5 million of the Company's revenue requirement from business flat rate customers to residential flat rate customers.

The Commission finds and concludes that there is insufficient evidence before it upon the record of this case to justify any reduction in the existing relationship of LFB to LFR rates. Therefore, the Company's original proposal, and the joint Company-Staff recommendation, are disapproved. Instead, the existing relationships should be maintained to the greatest extent possible while assuring recovery (but not overrecovery) of Company's residual revenue requirement.

M. Detariffing of Embedded Customer Premises Equipment (CPE). Southwestern Bell has proposed that embedded customer premises equipment (CPE) be detariffed as a part of this case. Effective January 1, 1984, Company will be required under the terms of the MFJ to transfer its embedded base CPE to an AT&T subsidiary (Embedded Base Organization or EBO, which will become part of AT&T Informations Systems or AT&T-IS). Company proposes that this AT&T subsidiary be permitted to provide embedded CPE on a deregulated basis. CPE is now part of a competitive market and customers have alternative vendors of equipment readily available to them. The Staff agrees with the Company proposal, and no party opposes that proposal. The Commission determines the Company's proposal to detariff embedded CPE is just and reasonable and should be approved.

N. Cost Study Methodology/Pricing. In Case No. TR-82-199, the Commission raised questions regarding the continued efficacy of the costing and rate design framework established by P.S.C. Case No. 18,309. The latter case authorized the use of Long Run Incremental Analysis (LRIA) for the pricing of services subject to substantial competitive pressure, in order to generate the largest "practical level of contribution" to "joint and common costs and to basic services based on LRIA." (Report and Order, Case No. 18,309, p. 3). Non-basic services not subject to substantial competition are also priced, under 18,309, using LRIA as a foundation and adjusting for social or economic factors related to the provision or receipt of those services. Basic telephone services (primarily local exchange flat rate service) are priced residually after rates are set for the other two categories of service.

In the instant case, Public Counsel has submitted a 1982 fully allocated cost study which it urges the Commission to adopt as the "centerpiece" for its rate design and access charge determinations in this proceeding. Public Counsel asserts, based upon that study and the Company's 1982 Embedded Direct Analysis (EDA), that it appears that a number of competitive and non-basic services of Southwestern Bell are not recovering their embedded costs under the pricing framework adopted in Case No. 18,309. Thus, in Public Counsel's view, residually priced local exchange service does not appear to be receiving any benefits from 18,309, but rather is used to insure recovery of the Company's embedded revenue requirement. Public Counsel recommends that the Commission seriously consider the abandonment, or significant modification, of the pricing framework announced in Case No. 18,309, particularly in light of the dramatic changes that have occurred in the telecommunications industry within the past two (2) years. Public Counsel further suggests that the Commission utilize the results of fully allocated cost studies (including allocation of the joint access line costs) as guidance in determining the revenue requirements for broad categories of services before designing specific service rates. Public Counsel also recommends that the Commission direct the Company to perform a "demand analysis" with respect to carrier access services. Other recommendations include that long-run incremental analyses be done for these services.

The Commission declines to adopt Public Counsel's fully allocated cost study for purposes of this case, for reasons set out above in Section XII. L. 2., "One-party flat rate (1FR/OBRA)", and further declines to order demand or incremental analyses. However, the Commission expects that fully allocated cost studies, among other cost studies, will be submitted in Southwestern Bell's next general rate case, and that it will be necessary for the Commission to consider Public Counsel's proposed methodologies more fully in that case, particularly in light of the fundamental changes in the telecommunications industry referred to by Public Counsel. Should any party believe that the Commission should order Company to

perform any specific studies before or during its next general rate case, then they should enter their requests with the Commission at the earliest possible time.

O. Rate Design Summary. Based upon the competent and substantial evidence on the whole record of this case, and upon its decisions concerning the contested rate design issues set out hereinabove, the Commission determines that the appropriate rate design to be applied to the revenue requirement deficiency found by the Commission in this case is as follows:

OMMES Increase	\$	72,000	
Private Line Increase		10,127,000	
10% Increase 100 Series P.L.		727,000	
Custom Calling Services		4,722,000	
Service Connection Charges		9,836,000	
Additional S.C.C. Increase		2,156,000	
Joint User		(32,000)	
Elimination of Special Message Rates		87,000	
Toll Charges		7,063,000	
Complex Inside Wire		18,179,000	
Eliminate Centrex C.O. Extension Line Rate		(20,000)	
Carriers Access Charges		<u>66,676,000</u>	
TOTAL SPECIFIC RATE ADJUSTMENTS		\$119,593,000	
TOTAL REVENUE DEFICIENCY (See Section XI above)			<u>\$181,612,000</u>
Remainder			<u>\$ 62,019,000</u>

The remainder of the revenue deficiency as determined herein for Southwestern Bell shall be recovered through an increase to all categories of local exchange service, including OBRA mileage charges, and announcement services, in accordance with the Commission's findings hereinabove, and consistent with the recommendations of all parties, including Staff, Company and Public Counsel, that increases to local exchange service be recovered on a residual basis.

The residual increase in this case will raise residential monthly one-party flat rates by \$2.05. It appears to the Commission that a substantial part of that increase is related to the divestiture by AT&T of SWB, an occurrence which, among other things, caused various increases in the Company's expenses, various losses of

revenues to the Company, and the adoption by the Commission of the budgeted test year in this case at the suggestion of the Staff, Public Counsel and Company.

XIII. AT&T Communications.

A. AT&T Management Expenses (Cost of Divestiture). Public Counsel and Staff recommend the disallowance of \$12,779,000 in costs associated with AT&T Communications (ATTCOM) management expenses which Public Counsel and Staff assert are an unexplained "cost of divestiture". The \$12,779,000 in costs represents the difference between the amount of management costs which Southwestern Bell has allocated out of its 1984 budget in connection with interLATA toll service, which it will no longer provide post-divestiture, and the additional amount of management costs which ATTCOM claims it will incur to provide the same service. Public Counsel and Staff assert that ATTCOM's budget is unreliable, and that these unexplained ATTCOM management costs should not be allowed by the Commission.

With respect to Public Counsel's and Staff's "cost of divestiture" allegation, it is ATTCOM's position that no such allocation can properly be performed. ATTCOM further asserts that such allegations have no relation whatsoever to ATTCOM's demonstrated revenue requirement. ATTCOM argues that through the testimony of witnesses Donat, LeMay, Vrooman and Mueller, it has fully supported its revenue requirement.

The Commission is of the opinion that ATTCOM has failed to establish the reasonableness of the projected management expenses at issue here. ATTCOM has the ultimate burden of proof and persuasion that the proposed rates are just and reasonable. Although ATTCOM has produced some evidence in the form of budget projections as to the reasonableness of its management expenses, the Commission is not persuaded as to the accuracy of those projections.

Based on the foregoing, the Commission finds that \$12,779,000 in costs associated with ATTCOM's management expenses should be disallowed as recommended by Public Counsel and Staff.

B. Rate Base.

1. Original Cost Rate Base. Upon the competent and substantial evidence in this case and based on the Commission's findings and conclusions herein, the Commission finds that AT&T Communications' Missouri net original cost rate base is \$74,170,000.

2. Fair Value Rate Base. The Commission finds that AT&T Communications' Missouri fair value rate base is \$113,779,000.

C. Rate of Return.

1. Capital Structure and Embedded Cost of Debt. ATTCOM and Staff agree that the capital structure for AT&T Communications to be used in this case is comprised of 45 percent debt, 55 percent common equity and that the embedded cost of debt for AT&T Communications is 7.81 percent. The Commission finds the agreement between Staff and AT&T Communications to be reasonable and, therefore, the agreed upon capital structure and cost of debt shall be utilized in this case.

2. Return on Common Equity. AT&T Communications proposes a cost of equity in the range of 16 percent to 17 percent and it recommends a return of 16.5 percent. Staff proposes a range of 13.88 percent to 15.42 percent. The return recommended by Staff is 15.42 percent.

ATTCOM utilizes the same analysis to determine a return on equity for AT&T Communications as it uses to determine the return on equity for Southwestern Bell. That analysis is discussed in Section VII hereinabove.

Staff also utilizes the same analysis as it uses for determining return on equity for Southwestern Bell except that Staff includes a different growth rate in the DCF formula for AT&T than it does for Southwestern Bell. Staff's growth rate for its AT&T DCF formula is in the range of 6 percent to 7 percent. This range of growth rates is based on AT&T's retention rate multiplied by the FCC currently authorized return on equity, which calculation results in a growth rate of 6.50 percent. Staff's range is based on plus or minus .50 percent applied to the 6.50 percent

growth rate estimate. As it has done for Southwestern Bell, Staff performs both the infinite and the finite DCF calculation and proposes a 3 percent adjustment to the required return on equity to reflect issuance costs. Staff also applies a market to book adjustment to arrive at the return on book common equity for AT&T Communications.

For the same reasons set forth hereinabove, the Commission finds Staff's dividend yield and growth components of its DCF formula to be appropriate and reasonable. Therefore, the Commission rejects those values as proposed by AT&T Communications. The Commission finds Staff's three percent (3%) value for issuance costs to be reasonable, and the Commission rejects Staff's market to book adjustment. Finally, the Commission finds that the infinite DCF model should be used for purposes of this case.

Based on the foregoing, the Commission finds that a reasonable return on equity for AT&T Communications is in the range of 14.62 percent to 15.65 percent. This range is supported by Staff's comparable earnings analysis taking into account the likelihood that AT&T Communications will be similar in risk to unregulated business.

3. Summary. Having considered all of the evidence, the Commission finds that the return on equity to be used for purposes of this case for AT&T Communications shall be 15.3 percent, resulting in an overall rate of return of 11.93 percent.

D. Revenue Requirement. Based upon the determinations of the Commission herein AT&T Communications' total net operating income requirement is \$8,848,000. The net operating income available for purposes of this proceeding is \$6,095,000, leaving a net operating income deficiency of \$2,753,000. After applying a factor for income tax and adding the amount related to uncollectibles, AT&T Communications' total revenue deficiency in this proceeding is found to be \$5,311,000.

E. Rate Design.

1. Rate Design Packages. Based on ATTCOM's proposed revenue requirement of \$6,214,000 and Staff's proposed revenue requirement of \$2,998,000, ATTCOM proposed the following rate design package:

	<u>Company</u>	<u>Staff</u>
Dial Credit Card Surcharge	\$ 184,000	\$ 184,000
Private Line Increase	276,000	276,000
Combination of First Three MTS Rate Steps	482,000	- 0 -
InterLATA Toll Rates	<u>5,272,000</u>	<u>2,538,000</u>
	\$6,214,000	\$2,998,000

2. Dial Credit Surcharge. ATTCOM proposes to increase the dial credit surcharge from 30 cents to 50 cents. Staff supports ATTCOM's proposal. The Commission finds that ATTCOM's proposal to increase the dial credit surcharge is reasonable and should be allowed.

3. Private Line Increase. ATTCOM proposes to modify the private line tariff to reflect access costs associated with private line service. Staff supports ATTCOM's proposal.

The Commission finds that ATTCOM's proposal to modify the private line tariff to reflect access costs is reasonable and should be allowed. In addition, the Commission finds that ATTCOM's private line rates should be increased by ten percent (10%). This finding is consistent with the Commission's goal of preserving state uniform rates for 1984 and is consistent with the ten percent (10%) private line increase authorized for Southwestern Bell.

4. Combination of the First Three MTS Rate Steps. ATTCOM proposes to combine the first three rate steps into one rate step in the MTS interLATA toll schedule. Staff opposes this proposal.

The Commission finds that the Company's proposal to combine the first three rate steps into one rate step should be rejected. The Company has not shown the reasonableness of this proposal which would result in a severe increase to the first two rate steps.

5. InterLATA Toll Rates. ATTCOM proposes to recover its revenue deficiency by residually increasing interLATA toll rates. Staff supports the Company's proposal.

Based on the Commission's findings with respect to access charge rate levels and uniform toll rates, the Commission finds that interLATA toll rates, including WATS, shall be increased by 5.06 percent.

6. Summary. Based on the Commission's findings and conclusions herein, the Commission finds the following rate design to be appropriate for ATTCOM:

Dial Credit Card Surcharge	\$ 184,000
Private Line Increase	1,276,000
InterLATA Toll Rates	<u>3,851,000</u>
TOTAL	\$ 5,311,000

Conclusions

The Missouri Public Service Commission has arrived at the following conclusions:

Southwestern Bell Telephone Company and AT&T Communications of the Southwest, Inc., are public utilities subject to the jurisdiction of this Commission pursuant to Chapters 386 and 392, RSMo 1978. The tariffs filed by Southwestern Bell which are the subject matter of this proceeding were suspended pursuant to the authority vested in this Commission by Section 392.230, RSMo 1978. The burden of proof to demonstrate that the proposed increased rates are just and reasonable is upon the Company.

The Commission, after notice and hearing, may order a change in any rate, charge or rental, and it may determine and prescribe the lawful rate, charge or rental, or regulations or practices affecting said rate, charge or rental thereafter to be observed. Section 392.230, RSMo 1978.

The Commission may consider all facts which, in its judgment, have any bearing upon a proper determination of the price to be charged with due regard, among other things, to a reasonable average return upon the value of the property actually used in the public service, and to the necessity of making reservation out of income for surplus and contingencies. Section 392.240, RSMo 1978.

When a public utility's existing rates and charges for telephone service are found to be insufficient to yield reasonable compensation for the service rendered, the Commission shall authorize revisions to the Company's applicable tariffs which will yield an appropriate fair return on the Company's property. The resulting rates shall be fair, just, reasonable and sufficient, and shall not be unduly discriminatory or unduly preferential. When tariffs filed by a public utility are designed to produce revenues in excess of those found to be just and reasonable, said tariffs should not be allowed to become effective as requested.

Based upon the Commission's findings herein, the tariffs filed by Southwestern Bell in Case No. TR-83-253 should be disallowed and Southwestern Bell should be authorized to file revised tariffs in conformance with the findings of this Report and Order. In addition, AT&T Communications of the Southwest, Inc., should be authorized to file revised tariffs in conformance with the findings of this Report and Order.

It is, therefore,

ORDERED: 1. That the revised tariffs filed by Southwestern Bell Telephone Company in Case No. TR-83-253 be, and the same are, hereby disapproved, and the Company is authorized to file in lieu thereof, for approval by this Commission, revised tariffs designed to increase gross annual revenues by \$181,612,000, exclusive of gross receipts and franchise taxes; and that said revised tariffs shall be in conformance with the rate design and other findings contained in this Report and Order; provided further that the local exchange rates established herein shall be subject to refund until otherwise ordered by the Commission.

ORDERED: 2. That the access charge services tariff structure and the intraLATA toll and access charge pools ordered in Report and Order, Part I, of this proceeding shall be in effect for an interim period which shall end no later than June 30, 1985, unless otherwise ordered by the Commission.

ORDERED: 3. That the independent average schedule telephone companies shall develop actual cost data during 1984 for use in determining rates to be in effect after 1984. Such companies shall promptly notify the Commission if problems arise in the development of such cost data.

ORDERED: 4. That the revised tariffs filed by Southwestern Bell Telephone Company in Case No. TR-83-288 which have been approved on an interim basis are hereby made permanent.

ORDERED: 5. That the Company shall convert customers currently billed in arrears to advance billing over a 10-month phase-in period to be completed no later than the end of 1984.

ORDERED: 6. That if any party believes an investigatory proceeding is necessary with respect to determine whether a refund should be ordered by this Commission, that party shall come forward and request the Commission to open a docket in the manner set forth in this Report and Order.

ORDERED: 7. That the Company shall perform or have performed a wage and salary compensation study as set forth in this Report and Order.

ORDERED: 8. That the Company shall promptly notify the Commission if it should become aware that a significant number of local exchange customers are leaving the system.

ORDERED: 9. That if any telephone company or other interested party perceives an immediate need for a Universal Service Fund in Missouri, that company or party shall file an appropriate pleading with the Commission containing its recommendations as set forth in this Report and Order.

ORDERED: 10. That if any party desires the Company to perform specific studies to be submitted in the Company's next rate case, such request should be filed with the Commission in a timely manner to allow sufficient time for the performance of such studies.

ORDERED: 11. That the Company shall book depreciation expense based upon the agreed upon depreciation rates which have been approved in this Report and Order.

ORDERED: 12. That Southwestern Bell Telephone Company shall investigate the situations in its Climax Springs and the Gravois Mills exchanges regarding recent deficiencies in meeting the Commission's surveillance levels for the category, "Percent of regular service order installations completed within five working days", and shall report to the Commission, within thirty (30) days of the effective date of this Report and Order, regarding actions Southwestern Bell intends to take in order to correct the situation.

ORDERED: 13. That Southwestern Bell shall investigate the situation in its Paynesville exchange regarding recent deficiencies in meeting the Commission's surveillance level for the category, "Trouble reports per 100 telephones", and shall report to the Commission within thirty (30) days of the effective date of this Report and Order, regarding action Southwestern Bell intends to take in order to correct the situation.

ORDERED: 14. That Southwestern Bell shall take action to clear all major cable pair faults referenced in Section X of this Report and Order. Said major cable pair faults shall be cleared within six (6) months of the effective date of this Report and Order, except in instances where extraordinary circumstances require the granting of additional time. Southwestern Bell shall file monthly status reports with the Commission, beginning thirty (30) days after the effective date of this Report and Order, detailing the progress made in clearing said major faults. The monthly status report shall be filed with the Commission until all said major faults are cleared. Southwestern Bell shall report to the Commission within thirty (30)

days of the effective date of this Report and Order, regarding the development of a method to clear the major faults referenced above.

ORDERED: 15. That the Company shall complete within nine (9) months of the effective date of this Report and Order, extended area service (EAS) studies as set forth in this Report and Order.

ORDERED: 16. That Southwestern Bell, AT&T Communications and Staff shall closely monitor the quality of telephone and customer service provided by SWB and ATTCOM. SWB, ATTCOM and Staff shall also monitor the level of customer understanding of the changes in the telephone system resulting from federal actions as well as the effect on customers of those changes. Any party that believes further specific Commission action is required in these respects should file an appropriate pleading with the Commission.

ORDERED: 17. That in the event the FCC approves a federal EUCLC, Southwestern Bell shall provide special notice to its Missouri customers advising those customers that the federal EUCLC is required by the Federal Communications Commission and not the Missouri Public Service Commission. The Company's bills shall clearly designate the EUCLC itemized charge as a "federal" End User Common Line Charge.

ORDERED: 18. That the Commission recognizes the authority of AT&T Communications of the Southwest, Inc. to provide interLATA toll service within the State of Missouri to the extent such service has been heretofore provided by Southwestern Bell Telephone Company.

ORDERED: 19. That the tariffs filed by Southwestern Bell Telephone Company in Case No. TR-83-253 on behalf of AT&T Communications of the Southwest, Inc., be, and the same are, hereby disapproved and AT&T Communications of the Southwest, Inc., is authorized to file in lieu thereof, for approval by this Commission, revised tariffs designed to increase gross annual revenues by \$5,311,000, exclusive of gross receipts and franchise taxes; and that said revised tariffs shall

be in conformance with the rate design and other findings contained in this Report and Order.

ORDERED: 20. That the objections to Exhibits 195, 196, 197 and 198 are hereby sustained and those exhibits are not received in evidence.

ORDERED: 21. That any exhibits previously offered and not ruled upon are hereby received in evidence, except as otherwise specifically provided herein.

ORDERED: 22. That all objections not previously ruled upon are hereby overruled, and that all motions not previously ruled upon are hereby denied, except as otherwise specifically provided herein.

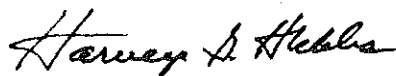
ORDERED: 23. That the rates to be established through revised tariffs conforming to the Commission's findings and conclusions in this Report and Order may become effective for service rendered on and after the effective date of this Report and Order.

ORDERED: 24. That the Secretary of the Commission shall serve a copy of this Report and Order upon all independent telephone companies doing business within the State of Missouri.

ORDERED: 25. That any party who believes that any matter necessary to implementation of this Report and Order requires further guidance from the Commission shall request the same at the earliest possible date.

ORDERED: 26. That this Report and Order shall become effective on the 1st day of January, 1984.

BY THE COMMISSION



Harvey G. Hubbs
Secretary

(S E A L)

Shapleigh, Chm., Musgrave, Mueller
and Hendren, CC., Concur and certify compliance with
the provisions of Section 536.080, RSMo, 1978.

Dated at Jefferson City on this 20th day of
December, 1983.