Q.Please state your name and business address?

A.My name is Kathleen L. Stockton.  My business address is 472 West Washington Street, Boise, Idaho.

Q.By whom are you employed and in what capacity?

A.I am employed as an Auditor by the Idaho Public Utilities Commission.

Q.Are you the same Kathleen L. Stockton who previously filed direct testimony in this proceeding?

A.Yes, I am.

Q.What is the purpose of this surrebuttal testimony?

A.The purpose of my surrebuttal testimony is to respond to U S WEST witness Wright’s rebuttal testimony pertaining to the following adjustments: Telephone Concessions, President’s Club, Chart of Accounts, Documents of Originating Entry, and Advertising.

TELEPHONE CONCESSIONS

Q.In the last general rate case (Case

No. U-1000-63), how were telephone concessions handled, and what specific guidelines were given in Order

No. 18188?

A.Order No. 18188 gave Mountain Bell, now

U S WEST, specific guidelines to follow with respect to

the provision of free local service as a concession for employees and retirees.  The Company was directed to either include in its tariff or file with the Commission a statement of the concessions enjoyed by its employees so that this information is available to the public.

Q.Did U S WEST follow the Commission's directive given in Order No. 18188?

A.No tariff or statement of the concessions enjoyed by its employees and retirees could be located, or any evidence that such a tariff or statement had been filed.

Q.What objection does the Company have regarding the imputation of revenues for telephone concessions?

A.The Company contends that to impute revenues for telephone concessions is a punishment for not following prior Commission Order No. 18188.  Company witness Wright, on page 47, line 18, states, “It is not

appropriate to punish the Company for a minor oversight.”Q.Did the Company object to the amount of the imputed revenues, or the way in which they were calculated?

A.No.  The rebuttal testimony was silent on the subject of the amount of the revenue imputation, as well as the calculation method of the revenue imputation.

Q.Please explain the reasons for imputing revenues for employee and retiree telephone concessions.

A.I included a revenue imputation to match the expenses included in the revenue requirement.  When recording transaction data, an accountant follows certain fundamental principles.  The principles relate to how assets, liabilities, revenues, and expenses are to be

identified, measured, recorded and reported.  One of those principles is the “Matching Principle.”  This key approach, in recognizing expenses, is to “let the expense follow the revenues.”  U S WEST has not included any revenues to justify the inclusion of the expenses.  Staff proposes to match the benefits (revenues) with the appropriate costs (expenses).

Q.Is it reasonable for U S WEST to provide extra benefits or bonuses to employees or retirees of that Company?

A.Not for its regulated activities.  Basic local telephone service is viewed as a necessity.  As such, the expenses necessary to provide reliable telephone service are those that are included for ratemaking purposes.  I included imputed revenues because the concession service represents an expense that is unnecessary for the provision of reliable utility service.  Including this revenue offsets the expenses incurred for the telephone concessions.  Therefore, Title 61 customers will not be paying expenses that are not necessary to provide reliable Title 61 services.  Telephone concessions should not be charged to Title 61 customers.

Q.Should the telephone concessions be viewed as part of the compensation package?

A.No.  The telephone concessions are not recorded as compensation expense by U S WEST.

Q.Are you recommending that telephone concessions be eliminated?

A.No.  I am not advocating that they be eliminated, rather that the expenses included in the Title 61 revenue requirement be matched with the inclusion of the appropriate amount of revenues to offset those expenses.  Revenues are imputed to offset the expenses of the telephone concessions.  Doing so properly matches the benefits(revenues) with the costs (expenses).

PRESIDENT’S CLUB

Q.Why have you recommended that the expenses for the President’s Club not be allocated to the Title 61 revenue requirement for ratemaking purposes?

A.I have recommended that the southern Idaho Intrastate portion of the expenses for the 1994 President’s Club, held in 1995, be disallowed because

U S WEST has failed to show that the President’s Club is beneficial to Title 61 customers, and that the expenses for the President’s Club are necessary for the provision of basic local telephone service.

Q.What is the President’s Club as it has been characterized to you?

A.The President’s Club is a recognition event that singles out individuals whose performance has exceeded certain benchmarks.  This recognition event is not unlike a paid vacation.  It is held in a resort setting, with daily events and meetings scheduled, but the meetings are short, and are not the primary purpose of the President’s Club.  The event gives the outward appearance of an all-expense-paid vacation for the employee and spouse, of about a week in duration.  It is my opinion that an all-expense paid vacation for a Company employee is not directly beneficial to Title 61 customers.  I suspect that the performance benchmarks have significantly more to do with enhancing shareholder value than they have to do with enhancing services for

Title 61 customers.  However, U S WEST has not provided the records and documents supporting the accounting entries to verify the expenses, or the benefit of the President’s Club to Title 61 customers.  Consequently, I have eliminated the expenses attributed to the President’s Club.

Q.What was U S WEST's response to your recommendation that the expenses for the President’s Club not be included in the Title 61 revenue requirement calculation?

A.U S WEST continues to assert that the President’s Club expenses should be included in the Title 61 revenue requirement calculation.  The Company says that the President’s Club is a form of employee recognition.  It does not justify the need for the expenses or their benefit to Title 61 customers.

Q.Did you examine sufficient records to verify the expenses of the President’s Club?

A.No.  I attempted to audit these records while in Denver, and subsequently, but the documents were not available.  The records provided were not sufficient to verify the expenses of the President’s Club.

Q.Did Staff attempt to determine the benefit of the President’s Club to Title 61 customers?

A.Yes, but the information provided was not for the President's Club.

Q.Company witness Wright states in her rebuttal testimony on page 48, line 19, that “This recognition is not given to any performance above an adequate performance level as portrayed by the Staff.”  Did the Staff make this statement?

A.No.  I did not imply or portray that the recognition was given to any employee who performed above average.  What I did say is that Title 61 customers should not have to pay a premium for any performance above adequate.  My adjustment to expenses, at the Idaho intrastate level, is $90,409.  Including expenses such as those for the President’s Club in the Title 61 revenue

requirement calculation implies that the customer can expect only an adequate level of performance, and that to motivate the Company to perform economically, efficiently, and with a high degree of quality and customer satisfaction, the customer must pay an additional premium over the compensation package already included in the Title 61 revenue requirement calculation.

CHART OF ACCOUNTS

Q.What is the ‘Chart of Accounts’ adjustment, and what are the issues surrounding this adjustment?

A.My adjustment called ‘Chart of Accounts’ is from my examination of the 6000-series and 7000-series expense accounts from the Uniform System of Accounts (USOA) that are included above the line.  I examined each expense sub-account title and categorized each sub-account as either a Title 61, Title 62, or combination (both Title 61 and Title 62) expense.  Those accounts that I categorized as Title 62, I directly assigned to Title 62.  Title 61 accounts are directly assigned to the Title 61 revenue requirement, and the combination accounts are allocated between Title 61 and Title 62 based on the allocation factors developed by Staff witness Baldwin.

Q.According to U S WEST, you have a basic flaw in your analysis.  What is this basic flaw, according to U S WEST?

A.U S WEST asserts that there is a basic flaw in my analysis of the Chart of Accounts because I am attempting to assign costs, which are identified at a total state level for allocation to Title 61 and 62.  This arises from a mischaracterization of my starting point.

Q.What is the starting point for your Chart of Accounts adjustment?

A.My starting point is the FR (Financial Report) books, specifically, the U S WEST Communications, Inc., FR Basis Area Ledger, Idaho.

Q.Why did you start at the FR books?

A.I started at the FR books because the FR books were readily available, subject to audit, and I could trace all sub-accounts back to this set of books.  The FR books, adjusted for closing and post-closing entries can be tied back to Company witness Elder’s Exhibit 44B.  Company witness Wright’s revenue requirement numbers are Title 61 intrastate numbers that are not auditable.

Q.Company witness Wright, in her rebuttal testimony, page 50, line 8, states that you “persist in removing” costs which are not included in intrastate results.”  Could you please explain?

A.Yes.  Company witness Wright’s Title 61 numbers may exclude some of these same numbers but this cannot be verified for most accounts.  As I stated before, Ms. Wright’s numbers start at the Title 61 level after these adjustments have been made, but we are unable to directly identify the adjustments by account since Ms. Wright completed three steps in one process.  My adjustment starts before the three steps that Ms. Wright combined.  My adjustment starts at the FR books prior to removing the federal regulated amounts and the Idaho off-book adjustments.  It is also prior to the interstate/intrastate separations.  I adjust the FR

sub-account balances using the appropriate intrastate percentages to arrive at the Idaho intrastate Title 62 amounts that should be excluded.

Q.Does the Uniform System of Accounts (USOA) preclude the Commission from examining individual postings to an account to determine proper Idaho regulatory treatment of the various entries?

A.No.  This Commission adopted by IDAPA 31.12.01.103 the UNIFORM SYSTEM OF ACCOUNTS FOR TELEPHONE UTILITIES.  Rule 103 states in part - “The accounts adopted by reference are adopted for convenience of establishing uniform systems of accounts only and do not bind the Commission in any manner to any particular ratemaking treatment of items in those accounts.”

Company witness Wright in her discussion of the Chart of Accounts (page 49 through 51 of her rebuttal testimony) indicates that the USOA is not designed to distinguish between Title 61 and Title 62.  It is true that the USOA is not designed to distinguish between Title 61 and Title 62.  The USOA makes requirements for the federal jurisdiction, but is silent about any specific requirements of a state jurisdiction.  This Commission recognizes that the USOA is not designed specifically for Idaho.  Therefore, the Commission has made provisions in Rule 103 to examine the accounts for content and establish the proper Idaho ratemaking treatment for whatever the content may be.  U S WEST did not allow me to examine the accounts for content, therefore, I made my adjustment based on the Uniform System of Accounts, disallowing those expenses that are not Title 61 and allocating the amounts that are a combination of Title 61 and Title 62 expenses.  I found no amounts that were totally Title 61 expenses in the accounts I adjusted.

DOCUMENTS OF ORIGINATING ENTRY

Q.What specifically did U S WEST say in rebuttal to your direct assignment of Title 61 and Title 62 expenses in your adjustment titled ‘Documents of Originating Entry’?

A.Company witness Wright maintains that I unfairly criticized the Company in my statement that the documents provided in response to my data requests relating to documents of originating entry were unsatisfactory.

Q.Why is it important to see the documents of originating entry?

A.As I previously stated in my direct testimony on page 19, it is important to see original documents to verify the reasonableness of expenses, the accuracy of entries, and the benefits to the Title 61 customers.  Another reason for examining the documents of original entry is to determine if direct assignment is taking place.

Q.Is it reasonable to expect that direct assignment of costs is possible?

AYes, and beginning at the federal jurisdiction, telephone utilities are required to directly assign costs whenever possible.  U S WEST has not shown that it is impossible to directly assign costs when it is appropriate and reasonable to do so.

Q.Company witness Wright states on page 54 of her rebuttal testimony that “it would not be a simple matter to modify journal entries to reflect direct assignment to Title 61 services.”  Company witness Wright also states that “Title 61 is a classification of service which is unique to the State of Idaho.  The classifica-

tion has no relevance in the other thirteen states in which we do business.”  Are ‘Title 61' services unique to Idaho?

A.Yes and no.  Yes, no other state has a classification of service SPECIFICALLY called “Title 61.”  However, at least two states in U S WEST’s territory do have a classification of service extremely similar to the types of services under the blanket name of “Title 61.”  Those two states are North Dakota and Minnesota.

Q.What does North Dakota call its similar “Title 61" services?

A.North Dakota has a similar basic local service category which they refer to as “essential service.”  They also have a statutory mechanism for non-essential services.  The North Dakota statute, Chapter 49-21-01 defines essential telecommunications service as “service that is necessary for switched access to interexchange telecommunications companies and necessary for two-way switched communications for both residential and business service within a local exchange area.”

Q.What does Minnesota call its similar “Title 61" services?

A.Chapter 237 of the Minnesota Statutes allows for an elective system of regulation which allows for telecommunications services to be classified into three possible categories: non-competitive, subject to emerging competition, and subject to effective competition.  In Docket No. P-421/EM-89-694, U S WEST Communications, the Minnesota Department of Public Service, and the other parties of record, reached an agreement which determined a classification of either “non-competitive” or “subject to emerging competition” for each of U S WEST Communication’s services under Minnesota Statute §237.59 (1994).  The classifications in North Dakota and Minnesota show that the bifurcation of services into two or more classifications is not unique to Idaho.

ADVERTISING

Q.Has Image and Corporate advertising traditionally been allowed in the revenue requirement for utilities?

A.No.  The Commission has held that this type of advertising is not beneficial to ratepayers or customers of public utilities in Idaho.

Q.In the last general rate case for U S WEST (formerly Mountain Bell), how were advertising expenses handled?

A.Advertising expenses other than informational advertising were to be paid by the shareholders, and not the ratepayers or customers.

Q.Why is U S WEST now asking that image and corporate brand advertising be allocated to the Title 61 revenue requirement?

A.U S WEST asserts that it is time for the Idaho Public Utilities Commission to change its historical position on advertising due to the advent of competition.  U S WEST maintains that it will be necessary for Title 61 customers to now pay for this type of advertising that traditionally had been disallowed for ratemaking purposes.  U S WEST asserts that it must now advertise to “attract and retain” Title 61 customers and therefore, these expenses traditionally disallowed should now be allowed for ratemaking.

Q.Should promotional, image and corporate advertising be included in the Title 61 revenue requirement?

A.This type of advertising should be disallowed in Title 61 rates, as it traditionally has.  While it is true that the telecommunications industry is entering a new age, competition is not present in Idaho at this time, as Staff witness Lee Selwyn testifies.  Therefore, there is no reason for still captive Title 61 customers to begin paying for advertising that has historically been disallowed for ratemaking because no benefits accrue to Title 61 customers from this kind of expense.

QHave you examined advertising from the 1995 test year?

A.Yes.  In Staff Production Request No. 398, I asked the Company to provide copies or make available in Boise all 1995 advertising efforts designed specifically “to attract and retain” Title 61 customers.  U S WEST has provided Staff the opportunity to examine and view these advertising efforts from the 1995 test year.

Q.What have you concluded as a result of your examination of the advertising materials provided in response to Staff Production Request No. 398?

A.I have concluded that the advertising I saw was not specifically designed to attract and retain

Title 61 customers.  While there were three advertisements for additional lines, a Title 61 service, the majority of the video, print and radio advertising I examined was designed to sell Title 62 services, primarily services offered through U S WEST’s “Home Office Consultant.”  Such services include, for example, Voice Messaging, Paging, Caller ID, Caller Services, Forwarding Services, and Enhanced Fax Services.  Although these advertisements might indirectly attract and retain Title 61 customers, the primary goal of this marketing effort is to sell additional, primarily Title 62, services to residential and small business customers.  It appears that the marketing strategy to “attract and retain” Title 61 customers is to sell them Title 62 services.

Q.Is it appropriate to include these expenses in the test year Title 61 revenue requirement?

A.No.  Including expenses of this nature, where the products and goals are enhancing and selling Title 62 services, is inappropriate.  The Title 61 revenue requirement should include only Title 61 revenues and expenses.  To include these advertising expenses would be including Title 62 expenses, meaning that the Title 61 customer is subsidizing Title 62 services.

Q.You had the opportunity to view two videos that are an example of corporate image advertising.  Should this type of advertising expense be included in the Title 61 revenue requirement?

A.Corporate image advertising has traditionally been disallowed for ratemaking purposes.  It has not been shown that this type of advertising is necessary for the provision of Title 61 services.  The theme of the two videos that I viewed was “Dependability.”  These two videos did not specifically mention Title 61 services, but stressed that U S WEST was dependable, with phrases like “service that works, no matter what service you have,” “always there for you,” “cause you’re all depending on us,” “with products and services you’ve come to depend on,” and “count on our ability of dependability.”  This type of advertising expense is not necessary for the provision of basic local telephone service, and should continue to be excluded from the Title 61 revenue requirement.

Q.Company witness Wright states in her rebuttal testimony on page 58, beginning at line 3, “It is simply not realistic that USWC will operate successfully in a competitive environment unless it too makes effective use of advertising.”  Are you advocating

that U S WEST not be allowed to advertise in this manner?

A.I am not advocating that U S WEST should not be allowed to advertise.  In Idaho, U S WEST may charge the costs of the advertising to three places:  Title 61 for the Title 61 products and services, Title 62 for Title 62 products and services, and to the shareholders as is reasonable.  I am not taking the position that

U S WEST should not be allowed to advertise, rather that U S WEST match the advertising expenses with the proper revenue source.

Q.Does this conclude your surrebuttal testimony in this proceeding?

A.Yes, it does.