Q.Please state your name and address for the record.

A.My name is Kent Schneider and my business address is 472 West Washington Street, Boise, Idaho.

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

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

Q.Are you the same Kent Schneider who previously filed Direct Testimony in this proceeding?

A.Yes, I am.

Q.What is the purpose of this Surrebuttal Testimony?

A.The purpose is to respond to the Rebuttal Testimony of U S WEST Communications, Inc. witnesses regarding my Direct Testimony and my Deposed Testimony on the following proposed adjustments:

PENSION ASSET

1801 CALIFORNIA LEASE EXPENSE

COMPENSATED ABSENCES

CURTAILMENT LOSSES

TRANSITION BENEFIT OBLIGATION AMORTIZATION

RESTRUCTURING CHARGES AND EMPLOYEE REDUCTION    BENEFITS

PENSION ASSET

Q.Do you agree with Ms. Wright's Rebuttal Testimony page 34, lines 18 through 21 that Staff ignored the fact that 1FR rates were reset in 1989 in reaching its conclusion that the Pension Asset was supplied by customers?

A.No.  Exhibit No. 141 shows Staff's decision memorandum based on a preliminary investigation into     U S WEST's Idaho earnings as part of Case No. MTB-T-88-7.  In this investigation, 1987's “actual” results were used as the starting point for this investigation.  The last four pages of this exhibit represent a spread sheet with Columns “a” through “e” being the actual Company results for 1987 and adjustments proposed by the Company.  In the line item “net pensions and benefits” there does not appear to be a credit for pensions proposed.  Nor does there appear any discussion of implementing SFAS-87.

The Commission's Final Order No. 22738 in Case No. MTB-T-88-7 reflects the revenue reductions agreed to by the Company and the Staff that totaled about $8.5 million.  There was no reconciliation between the revenue reductions and expense reductions.  The final order addressed the rationale as to why the rate case investigation was stopped and the revenue adjustments were accepted.  There is no mention of pension benefits.

(See Exhibit No. 142.)

Exhibit No. 143 is USWC witness Wozniak's Direct Testimony in Case No. MTB-T-88-13 concerning the proposed Revenue Sharing Plan and Staff's preliminary rate case findings.  His testimony does not mention pension benefits.  Pension accounting was probably not discussed because the Staff did not raise the issue of the accounting change associated with SFAS-87.

I did not ignore the 1989 review in anticipation of development of the Revenue Sharing Plan.  There is no evidence in Order No. 22738 that the Pension Asset or any pension credits were considered when the Commission adjusted rates at the time the Revenue Sharing Plan was implemented.

Q.Have other jurisdictions disallowed the Pension Asset from rate base?

A.Yes.  Arizona, Illinois (GTE), Missouri (United Telephone Company), Texas (Central Telephone Company of Texas), and Utah.  It appears that the reason the Pension Asset is allowed in rate base in Washington and Oregon is related to prior stipulations where pension credits were allowed as reductions in rates in prior years.

Q.On page 36, lines 8-11 of Ms. Wright's Rebuttal Testimony she states “The rate base should include a pension asset to reflect the fact that pension

credits have been recorded in U S WEST's regulated books of accounts with no corresponding decrease in the pension fund.”  Do you agree with this statement?

A.No.  While pension credits may have been recorded in U S WEST's regulated books of accounts with no corresponding decrease in the pension fund, this has been due to accounting entries.  Unless rate relief has been granted due to these credits, the ratepayers have not benefited from these accounting entries.  The pension fund was created by cash contributions that equaled the expenses charged to ratepayers and recovered in rates over the years.  No shareholder contributions have been required.

Q.On page 36, lines 11-15 of Ms. Wright's Rebuttal Testimony she further states not allowing the Pension Asset in rate base “...creates a situation where the customer benefits from the cash in the pension fund in the form of lower expenses in the future from the earnings on these funds while the shareholder is not allowed to earn on the cash left in the pension fund.  It is only fair and equitable for the shareholder to be allowed to earn on the pension asset that was created by these pension credits.”  Do you agree with this statement?

A.The statement that the customer benefits from the cash in the pension fund in the form of lower

expenses in the future is true.  However, this is only fair considering the overfunding is due to customer overpayments in the past.  The earnings of the fund were made possible by the customer-contributed funds being available to invest, not shareholder funds.

Another consideration concerning who will benefit in the future by the overfunding of pension expense relates to the direction of U S WEST toward unregulated activities.  The pension fund was not split between Communications and Media when the recapital-ization occurred.  If Inc.'s entry into cable, interLATA long distance and other nonregulated activities continues to outpace the growth of regulated activities, pension benefits for personnel hired for these activities will be funded by the pension fund created by ratepayers.

Therefore, it is not fair or equitable to allow shareholders to earn on an asset contributed by the ratepayers.  (See Exhibit No. 144.)

Q.Do you agree with Ms. Wright's contention that accumulated deferred taxes related to the Pension Asset should be excluded if the asset is excluded.

A.I agree in theory that the accumulated deferred taxes related to the pension asset should be

reflected.  Sufficient information to calculate the associated number was not available.  If USWC provides the calculation with workpapers, Staff will review it prior to the hearing.

Q.Do you agree with Ms. Wright's contention that “an unjustified...benefit...is that the ratepayer will have lower rates in this case by having the pension asset which is not currently included in rate base deducted from the rate base”?

A.No.  This pension asset is a ratepayer-contributed asset.  This asset, as noted above, will benefit the shareholders as deregulation progresses and  U S WEST expands its activities in nonregulated areas.  A return on this ratepayer contribution by reducing rate base by the amount of the pension asset is not a penalty to the shareholder but a fair return to the ratepayer.

1801 CALIFORNIA LEASE EXPENSE

Q.On pages 45 and 46 of Ms. Wright's Rebuttal Testimony she argues that the Arthur Andersen independent third party study supports the lease rates paid by USWC for 1801 California Street in Denver.  Do you agree?

A.No.  This study was used by USWC in the

Arizona rate case Docket No. E-1051-93-183 Decision No. 58927 dated January 3, 1995.  In this Arizona case, the Company used the Arthur Andersen study to refute the

Arizona staff-commissioned Real Estate Investigation Report performed by an independent team of five real estate analysts headed by Thomas Irvine.  (This report has come to be referred to as “The Irvine Report”.)  In its decision the Arizona Commission did not adopt either report in its entirety as the preparers of the two studies were not available for cross examination.

A compromise decision disallowing half of the amount recommended by the Irvine study was entered in the Arizona case.  Docket No. E-1051-93-183, Decision No. 58927 (85780) PUR4th Jan 3 (1995) (See an excerpt from the case in Exhibit No. 138.)

Q.What did your review determine?

A.The fair rate, determined prior to the sale and leaseback arrangement was determined by the Irvine study to be $12.50 per square foot.  This rate was reinforced by the Oregon study developing a fair rate at $12.46 per square foot.  I used the Irvine rate as being more conservative.  For the current lease rate I used $18.24 per square foot because the Irvine study, the Arthur Andersen study, and the Oregon staff study all agreed to this rate.  This rate was also referenced in

USWC witness Wright's Rebuttal Testimony on page 44.  The difference between the two rates times the total square footage leased was factored to Idaho-South using Company

allocation factors to develop my adjustment.

Q.The Arthur Andersen study went a step further and removed parking garage estimated revenues from the lease rate to develop a lower lease rate of $17.11 per square foot.  Did you consider this?

A.Yes.  In my opinion the operating revenue from the parking garage should be used to offset the operating costs of the leased property, not to lower the net lease rate.  For example, if the garage was closed for repairs or renovation to develop extra spaces, the net lease rate would continue and the revenue would be reduced or eliminated.  Therefore the $18.24 rate best reflects the “net” lease rate.

Q.Have other state Commissions examined these studies?

A.Yes.  These two independent studies were recently reviewed by the Oregon PUC staff in its review of the reasonableness of lease rates.  In the Oregon case U S WEST argued the square-foot rate should be set at $17.11 while the staff argued it should be $12.46.  The Oregon's PUC Order No. 96-179 entered July 16, 1996 concluded that the proper lease rate for 1801 California

should be $12.46 per square foot.  Without actual data for a build-to-suit analysis or more detailed explanation of the assumptions underlying growth rate estimates, the

Commission couldn't confirm the reliability of the Company's lease rate analysis.  The Commission recognized the limitations in Staff's proposed lease rate of $12.46, but, this rate reflected the last arm's-length transaction regarding this property.  (See Exhibit No. 139, pages 10-12.)

Q.In Ms. Wright's Rebuttal Testimony on    page 44 she states “Staff is ignoring three critical components of lease comparability:  the term of the lease (number of years); the size of the square footage; and

the time frame when the lease arrangement is being negotiated.”  Are you ignoring these factors?

A.Not at all.  My point in my Direct Testimony was that the time frame when the lease was renegotiated was a factor in the unreasonableness of the lease rates.  The price paid by the buyer to U S WEST required a lease-back of the amount and duration by USWC to make the purchase price reasonable.  As noted above both the Irvine study and the Oregon staff study found that the lease rate was unreasonable, and that the $12.46 per square foot found by Oregon or the $12.50 per square foot noted in the Irvine study is the reasonable rate.

a. Term and size

Ms. Wright in her Rebuttal Testimony on lines 9 and 10 of page 44 acknowledges that a three to

five-year lease is the most common in the market.  The lease that USWC had before the sale and lease-back transaction was for 600,000 square feet for ten years at $12.50 per square foot, according to the Irvine study.  Had the sale and lease-back transaction not occurred, USWC would have had to negotiate a lease in 1994.  My Exhibit No. 110 shows that while the “A” class leasing market had improved, the square-footage rate increase was minor.  My proprietary Exhibit No. 111 (Direct Testimony) shows that a smaller square foot space at 1801 California was leased for only $12.40 per square foot in 1994.

b. Sale and lease-back unusual duration

The duration of the lease executed by USWC

upon the sale and leaseback was 20.5 years.  This is very atypical of the lease market and significantly reduced the Company's flexibility just as it was planning to start laying off significant numbers of personnel.

c. The lease rate and length of the lease agreement.  Immediately prior to the sale and lease-back agreement, USWC was leasing this same amount of space for $12.50 per square foot.  In this situation the parent company caused USWC to change from leasing from an affiliate to acquiring a longer term lease from a third party, after the parent company sold the building to that third party, they increased the rent per square foot USWC

had to pay.  Because of this change I believe, as I have stated before, that the affiliate transactions

were not to the benefit of USWC and Title 61 ratepayers should not be disadvantaged.

The study provided by Arthur Andersen has not met the burden of proof required to show that this affiliate transaction is reasonable.  My original adjustment is reasonable and necessary.

COMPENSATED ABSENCES

Q.On pages 41 through 43 of Ms. Wright's Rebuttal Testimony, she uses examples of pending accounting changes that may occur in the period between 1995 (the test year) and 1997 (the year in which rates based on the test year will become effective) that could offset the ending of the five-year amortization of the

catch-up expense calculated at the time of the change in accounting for compensated absences.  Do you agree with this argument?

A.No.  This is comparing a possible future event not yet analyzed and accepted by the Idaho Commission to a one-time event that has already occurred and the amortization of which is nearly complete.  I believe that proforma rate setting allows for those events that have occurred and have been accepted, or at least are known and measurable rather than for those

events that may or may not occur.

CURTAILMENT LOSS

Q.In Ms. Wright's Rebuttal Testimony concerning your amortization of the curtailment loss associated with the remaining portion of the twenty-year amortization of the transition benefit obligation (TBO) for the Post-retirement Benefits Other than Pensions (PBOPs), she made two points:

(1) That “Adjustments should be made on their appropriateness or their inappropriateness in the test period.” and (2) that “Staff admits that curtailment losses will probably occur in 1996 and 1997 and that they may occur in the future.”  Do you agree with these two points?

A.I agree with her first point, but not the second point.  In my Direct Testimony on pages 7 and 8, I stated:

Rather than record a rare if not

unique event in the test year, I

propose two possible alternative

treatments.  First, because this

could be considered as a one-time

non-recurring expense, the entire

amount could be removed from the

test year.  Alternatively, because

USWC is not quite half finished

withits re-engineering efforts

another adjustment may be required

in 1997 or 1998, when the Restruc-

turing Plan is complete and its

effects are known and measurable....

Staff suggests that the second

option be accepted since it would

also provide the amortiza-

tionmechanism if future curtailment

losses are incurred and would have

little impact on the test year.

(Emphasis added.)

I was referring in the last sentence of the quote above to the possible need for an adjustment in 1997 or 1998.  Therefore, due to the uniqueness or extreme rarity of these events this curtailment loss cannot be considered an ongoing event.

Also, in the Washington UTC Order issued in April 1996, the Washington Commission eliminated Washington's portion of U S WEST's 1995 curtailment loss. (See Exhibit No. 140, pages 40-41.)

TRANSITION BENEFIT OBLIGATION AMORTIZATION

Q.The issue you present concerning SFAS 106 is that the amortization period for the transition benefit obligation should be increased from 17.3 years as calculated by the Company to 20 years.  In her Rebuttal Testimony, Ms. Wright states that once established at 17.3 years SFAS 106 does not allow for changes to the amortization period.  Who is right?

A.Perhaps I should clarify my position.       U S WEST Communications established a 17.3-year amortization.  Since the Company was not obligated to

consult with or acquire Commission approval when SFAS 106

was adopted, this is the first opportunity that this Commission has had to review this amortization period for

regulatory purposes.

According to SFAS 106 paragraph 112 “If delayed recognition is elected, the transition obligation or asset shall be amortized on a straight-line basis over the average remaining service period of active plan participants, except that...if the average service period is less than 20 years, the employer may elect to use a

20-year period,....”  (Emphasis added.)  Obviously, the longer amortization period benefits the ratepayers, as noted in my adjustment.

I proposed to use the longer amortization period  for ratemaking purposes instead of the Company's calculated period.  The uncertainty of the significant events occurring during and soon after the calculation was made were further justifications on my part for using the allowed, 20-year amortization.

In the Case No. WWP-G-92-2, this Commission authorized a 20-year TBO amortization period (Order No. 24673, page 1).  Also, in Case No. IPC-E-94-5, the Commission authorized a 20-year TBO amortization period (Order No. 25880, pages 9-10).

RESTRUCTURING CHARGES AND EMPLOYEE REDUCTION BENEFITS

Q.In his Rebuttal Testimony USWC witness

Inouye focuses on the contention that the Restructuring Plan expenses are ongoing and are therefore ordinary

business expenses to be included in the year they are incurred.  Do you agree with this contention?

A.No.  USWC was asked to justify the accounting treatment utilized to record expenses for the Restructuring Plan on the Company's financial statements for SEC and shareholder reporting.  The Company's response in Staff Audit Request STFO5-361 was:

The 1993 Restructuring Reserve:

When USWC recorded its restructuring

charge, research of accounting liter-

ature and prevailing practice showed

that prevailing accounting practice

was to accrue the cost of restruc-

turing at the appropriate measurement

date.

However, the accounting literature

did not definitively address account-

ing for corporate restructurings.

The SEC staff addressed restructuring

charges when it issued SAB 67 in 1989.

SAB 67 states:

Facts:  The staff had noted a recent increase in the number of registrants

recording what are commonly referred

to as “restructuring charges.”  While

the events or transactions triggering

the recognition of such provisions vary, they typically result from the consoli-dation and/or relocation of operations

the abandonment of operations or produc-

tive or other long-lived assets.  The

components of these charges also vary,

but generally include the reduction in

the carrying value of long-lived assets

and provisions for the termination and

relocations of operations and employees.

While SAB 67 addressed only the financial reporting of restructuring charges on the

income statement, that is, restructuring

charges must be reported as a component of

continuing operations, USWC restructuring

actions are consistent with both the words

and the spirit of SAB 67.

Because the accounting literature did not

definitively address accounting for cor-

porate restructurings, USWC looked to prevailing accounting practice and an

analogy to APB (Accounting Principles Board) 30 to record its restructuring charge.  In 1993, over 400 companies included charges for corporate restruc-turing actions.  The practice of recog-nizing the financial effect of major corporate restructuring was a wide-

spread and commonly accepted account-

ing practice in the United States.

Analogies to APB 30 fit the comprehensive

nature of a restructuring plan.  Although

APB 30 applies directly to dispositions of

a segment, its concepts are also appropriate

for corporate restructurings.  Dispositions

are the result of management's decision to refocus its business.  So too, is a cor-porate restructuring the result of manage-

ment's decision to refocus its business.

APB 30 requires a company to record the

impact of a disposition on...

...the date on which the management having

authority to approve the action commits

itself to a formal plan to dispose of a

segment of the business...

On September 16, 1993, the Board of Direc- tors of U S WEST, Inc. committed USWC to a

formal plan to restructure USWC's business.

As a result, USWC reflected a charge of $880

million in its financial statements.

APB 30 also provided guidance in determining what types of costs to include in a restruc-

turing.  Paragraph 16 of APB states:

...costs, and expense which (a) are clearly a direct result of the decision to dispose

of the segment and (b) are clearly not the

adjustments of carrying amounts or costs,

or expenses that should have been recognized

on a going-concern basis prior to the meas-

urement date should be included in the gain

or loss on disposal.

The title to APB 30 is “Reporting the Results of Operations-Reporting the Effects of Disposal

of a Segment of a Business, and Extraordinary, Unusual,

and Infrequently Occurring Events and Transactions”.

The Company is treating the 1993 Restructuring Plan like a disposal of a business segment.  Also in the reference to SAB 67 the “restructuring charges” typically result from the consolidation and/or relocation of operations.  The components of the restructuring charges generally include provisions for the termination and relocation of operations and employees.

The consolidation of 560 customer service centers into 26 centers in 10 cities and the reduction of its work force by approximately 10,000 employees, as noted in my Direct Testimony on page 10, is a one-time event that will not recur.  By its scope and purpose this

is a rare if not unique event.  It definitely is not

business as usual as USWC witness Inouye would like to portray.

While a plan of this magnitude could not be accomplished in one year (it was originally planned to start in 1994 and ultimately planned to be completed by the end of 1997) it was management's intent, based on their justifications for the accounting treatment in their financial statements, as noted above, that this is a significant and rare event.

Q.USWC witness Inouye's claims that Staff did

not give consideration to predictions by industry analysts that USWC would have to do further restructuring, streamlining and systems development (lines 7-9, page 4 Inouye Rebuttal Testimony).  Please explain the level of consideration given to this information?

A.I reviewed the information but adhered to my position that restructuring costs did not belong in the test year, but should be amortized over a reasonable future period, for several reasons.  First, my proposed adjustment deals with a business event that Company management considers of significant size and rarity to record for financial purposes as a one-time expense.  Second, my proposed adjustment deals with the effects of

this particular restructuring plan on the test year.

Future predicted events are too vague to be measurable or even known to occur at this point in time.  Third, I was

aware that USWC doesn't have any future plans for restructuring like the one announced by management in 1993.  Staff Production Request No. 360 asks if any restructuring plans of the type announced in 1993 were being planned.  As of February 12, 1997 the answer, in short, was no.  Fourth, the trade articles dealing with what is going to happen in the telephone industry and when they may occur are not always consistent.  For example, in USWC witness Inouye's Exhibit No. 33d, page 2 of Morgan Stanley's comments, dated January 16, 1996,  Morgan Stanley states the following:

 In fact, cost cutting is not as easy

as it sounds.  U S WEST, for one, can

attest to this.  U S WEST embarked

on a costreduction plan two years

ago in which it consolidated service operating centers and reduced its

work force by nearly 4,000 of the

planned reductions.  The result was an inability to meet customer demand,

an erosion in service quality, and

significant fines from regulators.

Reducing work force as competition is increasing is nearly counterintuitive.

Fifth, the magnitude of the effort undertaken in 1993 may never be experienced again.

U S WEST claims that on-going system improvements, cost reduction efforts and streamlining will continue.  This is consistent with all businesses trying to stay up with if not ahead of their competition.  These efforts will most likely be different than what has occurred in 1994

and 1995.

Q.Do you agree with USWC witness Inouye's comparison made between one-time customer charges referred to as being non-recurring and the non-recurring restructuring expenses?  (Inouye Rebuttal Testimony

pages 4-5.)

A.No.  This argument is trying to show how regulatory records and accounting records bookkeep for different activities.  While he focuses on the term “non-recurring”, both the accounting records and the

regulatory records account for one-time customer charges

the same way, as on-going business revenue.  However, the Restructuring Plan created in 1993 is accounted for on the financial books because of the rarity and magnitude of this plan as a one-time expense and associated reserve.  To include these restructuring expenses in the test year for setting rates when benefits are planned to be recognized after the test year is unfair to Title 61 customers.  These restructuring expenses are not normal, recurring operating expenses and they should be amortized over a period of time when benefits from the plan are experienced.

Q.Do you agree with USWC witness Inouye's claim that restructuring and employee severance expenses have well established historical trends and thus are

on-going business expenses?  (See Inouye Rebuttal Testimony, pages 6-8.)

A.No.  First, Mr. Inouye's reference to USWC Rebuttal witness Plummer implies that Mr. Plummer will provide new insight to the discussion of significant restructuring projects, such as the Restructuring Plan, as compared to on-going reengineering, streamlining, and computer hardware and software enhancements.  Mr. Plummer's Rebuttal Testimony does not provide this

additional information.  Second, Mr. Inouye presents separate tables for paid exits, and total personnel, then states on page 8 that the change in total personnel each year does not equal the paid exits primarily because of new hires.  This is misleading.  Staff Exhibit No. 145, which reflects the Staff analysis based on the tables presented in Inouye's Rebuttal Testimony reveals that another very significant factor affecting separations is personnel leaving without being paid to leave.

Significant changes in personnel can be attributed to management intervention.  For example, the decrease in 1990 relates to an early retirement program in which approximately 4000 employees elected to retire

effective February 28, 1990.  The lump sum pension benefits to retiring managers reduced the pension plan assets by $642 million according to footnote 10 to the

U S WEST audited financial statements for 1990.  In 1992 and 1993 management's announced personnel reduction plan was in effect, and 5000 of the 6000 planned personnel cuts were accomplished.  In 1993, the Restructuring Plan was announced and in 1994 over 2000 additional employees left.

On page 7 of Inouye's Rebuttal Testimony he states “In particular, there was nothing abnormal in 1995 as compared to other years.”  However, as can be seen from my Exhibit No. 145 several abnormal events occurred in 1995:  The total number of USWC personnel went up 443 compared to a three year trend of personnel decreases of

over 2000; the new hires were the highest they had seen in the eight years analyzed, more than double the average for the prior seven years; and the new hires were more than three times the number needed to replace the unpaid exits.  Therefore, as far as 1995 is concerned I believe that the quote from Morgan Stanley on pages 18-19 above reflects what happened after the restructuring plan started in 1994 and service problems developed.  This caused U S WEST to rehire personnel until the problems were under control.

Q.Do you agree with USWC Rebuttal witness Inouye's depiction that U S WEST has had an evolutionary history of redesigning computerized systems and

developing new systems.

A.Yes, but this evolution has occurred in nearly all service industries, increasing productivity and decreasing “back-office” costs.  This evolutionary change from manual to more and more sophisticated computerized systems has little or nothing to do with the special Restructuring Plan commenced in 1994.  As Inouye stated on page 10 of his testimony, 38% of the total expense for the current restructure expense is for computer systems.  This 38% represents $360 million of the total 1993 reserve.  The amounts charged against this reserve were $118 in 1994 and $129 in 1995.  Comparing

these expenditures against the total systems development expense for 1994 and 1995 of $472 and $464 shows that the

Restructuring Plan expenses for computers was about 25% of total computer expenses for these years.  (See page 11, line 18 of Inouye's Rebuttal Testimony.)  The source for the restructuring expenses for computers is management's discussion and analysis of the activity affecting the restructuring reserve on page C-9 of       U S WEST, Inc.'s 10-K Report.  Obviously, in dealing with the Restructuring Charge we are not talking about the

on-going, evolutionary improvement to the computer systems.

Again, the issue is whether the expenses of

a particular project, the Restructuring Plan, should be allowed in the test year when the offsetting economic benefits are going to be received in the future.

Q.Have other states addressed this issue?

A.Yes, in the Utah rate case Docket No. 95-049-05 dated November 27, 1995 (UT.PSC\*11/27/95\*[75348]-PUR4th-\*U S WEST Communications, Inc.) the re-engineering costs incurred in 1994 were deferred and amortized over five years to match the expenses to when the ratepayers will at least begin to receive the benefits.  (See Exhibit No. 146, page 30.)  In the Washington UTC decision in Docket No. UT-950200 (See Exhibit No. 147, page 40.) the costs were eliminated from the test year.   In the Oregon rate case, the case is not final, but the PUC Staff's Opening Brief states the Restructuring Program expenses contained in the test year should be eliminated from the rate case (Exhibit No. 148).

Q.USWC witness Inouye claims Staff is not aware of the economic benefits planned for the Restructuring Plan and has not provided evidence that the benefits have not been obtained.  Do you agree?

A.No.  The 1993 U S WEST, Inc. Annual Report and 10-K Report talk mostly about the Restructuring Charges.  The 1993 10-K Report states:

Restructuring.  On September 17, 1993,

U S WEST announced that U S WEST Communications would implement a plan

(the “Restructuring Plan”) designed to provide faster, more responsive customer services while reducing the costs of providing these services.  Pursuant to

the Restructuring Plan, U S WEST Communications will develop new systems

that will enable it to monitor networks to reduce the risk of service interruptions, activate telephone service on demand, provide automated inventory systems and centralize its service centers so that customers can have their telecommunica-

tions needs resolved with one phone call.

U S WEST Communications will also gradually reduce its work force by approximately 8000 employees by the end of 1996 (in addition

to a remaining reduction of 1000 employees pursuant to a restructuring plan announced in 1991) and consolidate the operations of its existing 560 customer centers into 26 customer centers in ten cities.  U S WEST expects cost reductions will be realized as

these components of the Restructuring plan are implemented.  In connection with the

Restructuring Plan, U S WEST recognized a pretax restructuring charge of $1 billion, the components of which are described under “Costs and Expenses” in Management's

Discussion and Analysis of Financial Condition and Results of Operations on page 17 of the 1993 Annual Report, which is incorporated by reference herein.

On page 17 of the 1993 Annual Report, the Company savings were:  “The 1993 restructuring plan is estimated to reduce cumulative total employee and related costs by approximately $525 (million) during the next

three years, starting in 1994.  These savings are expected to be largely offset by higher employee salaries and wages for the remainder of the work force.”

However, this original plan was revised to include an additional 1000 employee paid departures when 1000 employees planned to be relocated decided to be paid to leave instead.  Mathematically, if the original 9000 employees leaving could have justified a savings of $525 million, 10,000 employees leaving would generate $583 million in planned savings.  In reality, it doesn't matter what the exact estimated savings were going to be. The important factor is that the savings were going to come from reducing employee and related costs.  Expenses were going to be incurred to obtain these savings.  After the inception of the original plan, the completion date was delayed a year and the 1000 paid departures were added to the plan.

Q.USWC witness Inouye states that Staff's evidence does not prove that the planned expense benefit was not achieved or that no benefit was achieved.  Do you agree?

A.Of course not.  First, I believe the burden of proof is USWC's to show a special project's expenses benefit to the ratepayers.  However, Exhibit No. 145

reflects that the employee and related costs savings

could not have been achieved when the plan was to reduce the number of employees and the change was an addition of personnel.  I provided USWC Exhibit No. 145 in Production

Requests STF05-360 and STF05-361 and asked them to explain the apparent net additional exits without pay (column 6), the apparent net increase in total employees, and the significant increase in new hires in 1995.  USWC objected to the questions, provided data that did not tie into Inouye's originally provided data and were otherwise largely nonresponsive.  Therefore, I believe I have shown that the economic benefits planned could not have been achieved in 1995 and, in conjunction with Staff witnesses Hart and Cooper, have shown that customer service has suffered in 1994 and 1995.

Q.USWC witness Inouye states that by using USWC Group's audited financial data; that data also includes unregulated subsidiaries and deregulated operations, (i.e., total Company data) as opposed to Idaho.  Do you agree?

A.Only to a limited extent.  Of all the affiliates in the USWC Group, telephone operations is by far the largest, page C-4 of the 1995 10-K Report, states that, “Approximately 97 percent of the revenues of the Communications Group are attributable to the operations

of U S WEST Communications, Inc.”, the telephone

operations.

Q.USWC witness Inouye states in his Rebuttal Testimony that the data that Staff used cannot determine

if restructuring benefits were achieved because (a) the expense attributed to contract workers was included in the data, (b) the effects of pay increases and increased payroll taxes were included in the data and (c) Employee increases were included in the data yet were due to growth and new business opportunities.  Do you agree?

A.No.  I will address each factor in order:  (a) Inouye states that over time the Company has increased its reliance on contract workers.  That may be true, but in the Company's 1995 10-K Report in footnote (2) on page C-7 the Company stated, “A significant number of the employee reductions originally scheduled for 1996 will be delayed while the Communication Group focuses on overtime and contract-labor expenses.”  (Emphasis added.)  This statement was repeated in the Company's March 31, 1996 10-Q Report on page 21.  Obviously management was not satisfied with these expenses increasing in 1995 and was willing to delay the employee reductions called for in the Restructuring Plan to address contract labor issues.  This supports why these costs should be included in my adjustment relating to the restructuring costs and

potential benefits.

(b) In Staff Production Request No.

STF05-363 I asked:

In the 1993 Form 10-K, page 11 the last

two sentences on that page state:  “The restructuring plan is estimated to reduce total employee and related costs by approximately $525 (million) during the

nextthree years, starting in 1994.  Thesesavings are expected to be largely offset

by higher employee salaries and wages forthe remainder of the work force.”  (underline added)  Did management ignore growth and other business opportunities in this statement?  What does the Company mean when it uses the term “largely offset”?

USWC objected to these questions and was generally unresponsive.  As an alternative calculation for the savings to be realized if the Company's 1993 estimate of $50,000 per employee savings were used above, and that this savings only included salaries as I was told:

$50,000 salary

    +$11,250 22.5% benefit load used by the Company

       in 1994 and 1995

$61,250 x 1.055 salary increase in 1994=

$64,619 x 1.055 salary increase in 1995=

$68,817 Employee costs to be saved in 1996

Therefore, personnel costs to be saved in 1996 would be at least $68,817 per employee terminated including

benefits and salary increases.  However, this calculation has flaws tied to lower-salaried staff replacing higher-salaried employees who leave and numerous other factors.

Nonetheless, it provides a rough estimate of the validity

of the amounts I have used in my testimony.

(c)  The employee increases due to growth

and new business were previously addressed on page 18.

Q.USWC witness Inouye asserts that the

Restructuring Plan expenses incurred since 1992 have

produced benefits in 1995 which have exceeded expenses.  Do you agree with this analysis?

A.No.  The 1991 “Restructuring Charge” Plan dealt largely with U S WEST Inc.'s departure from the real estate market.  Of the $915 million pretax charge taken as a restructuring charge, $675 million dealt with projected losses associated with exiting the real estate business and the write-off of certain intangible assets.  The remaining $240 million charge related to workforce reductions of 6000 personnel of USWC.  (Source: page

A-24 of USW Inc.'s 1991 10-K Report.)  On page 25 of USWC's 1992 10-K Report “Approximately $160.0 million of the reserve is unused at December 31, 1992.  Total workforce reductions attributable to both restructuring and attrition was approximately 2300 employees.”

On Exhibit No. 145, Inouye's total net employee reduction for 1992 is shown as 2523 or 4063 depending on whether the offsetting effect of new hires is considered.  The 10% or 77% difference undermines

Inouye's Rebuttal Testimony which is unaudited versus the 10-K Report financial statements which are audited.

My earlier Direct and Deposed Testimony references to prior restructuring efforts was to provide

perspective and some of the history leading to, and

including, the 1993 Restructuring Plan.  However, the

1993 Restructuring Plan is a unique event, separate from on-going operations and prior restructuring efforts.  The expenses of the 1991 employee reduction plan ceased when the 1993 Restructuring plan was started in 1994.  Staff has never indicated that the employee reduction efforts of the 1991 plan were not successful.  However, to use the benefits of one restructuring plan (the 1991 Plan) to offset the expenses of another restructuring plan which is quite unique (the 1993 Plan) is misleading and inappropriate.  In the test year, we are dealing only with whether the expense incurred in the test year of the 1993 Restructuring Plan, which is not expected to be completed until 1997, should be included in the test year.  Inouye's attempts to portray this unique project as an on-going effort are inaccurate, inappropriate and misleading.

Q.USWC witness Inouye refers to USWC witness Jones' testimony as evidence that Title 61 ratepayers have benefited from restructuring and resystemization.

Do you agree?

A.It would appear that customer access to the

service center has improved due to the changes mentioned by witness Jones.  Ms. Jones does not distinguish between

changes due to on-going re-engineering efforts and changes related to the Restructuring Plan.  Jones also mentions further changes that are yet to be completed.  These future expenses are not separated between the Restructuring plan and on-going re-engineering efforts.  Customer service issues will be discussed by Staff witnesses Hart and Cooper.

Q.USWC witness Inouye states that the appropriate ratemaking principle is to establish rates which reflect the on-going level of expenses.  He then uses a simplified example of Staff's proposed

amortization of expenses incurred in 1995 for the 1993

Restructuring Plan as to why the amortization would not be fair.  Do you agree?

A.No.  In steps (3) and (4) of his example on pages 22 and 23 Inouye states that the regulators amortize the disallowed expense over 15 years and then during the period rates are in effect only a 15th of the revenue is allowed to cover the expense but the expense continues to be incurred during the period.  This is not an accurate depiction of the 1993 restructuring

adjustment proposed by Staff.  Simply, the expenses of the Restructuring Plan are going to end soon after new

rates come into effect, so the amortization of the 1995 expenses will not be layered on top of continuing

expenses.  Inouye continues to combine “one-time” expenses with “on-going expenses”.

Q.USWC witness Inouye contends his Exhibit USW/38g depicting the historical trend of expense per access line depicts a relatively consistent expense level per access line and that the proposed Staff expense per line is so far off of this consistent historical trend it must be distortive.  Is this reasonable?

A.If the Company's cost-cutting efforts have only enabled management to keep costs increasing at only the growth rates of access lines, this graph would fairly depict the historical trend.  Unfortunately, this graph has not been audited so its accuracy has not been able to be verified.  I understand that one of the primary allocation factors for expenses to the states is

the number of access lines.  Therefore as access lines

increase in the state the allocated expense would also increase.  Perhaps a better graph to use would be USWC in total.  The graph at Exhibit No. USW/38g should not be given much weight.

Q.USWC witness Inouye states that in determining the amortization period that your Direct

Testimony and your deposed testimony are contradictory.  Do you agree?

A.No.  In my Direct Testimony I presented two

alternatives for treatment of the one-time restructuring expense incurred in the test year but which would not yield benefits in the test year because of temporary service problems encountered.  One approach would be to disallow the expenses as one-time expenses not resulting in benefits in the test year.  The other approach is to

match the one-time expenses incurred with the future benefits to be received to best depict the on-going operations.  As mentioned above the expenses are “one-time”, not to be incurred again.  The benefits are annual, to be received every year once the employees are terminated and their salaries and related costs are not to be incurred again.  Ignoring growth and salary increases for the remaining employees, an annual benefit could be theoretically assumed to last forever offset by a one-time expense.  However, this theoretical “annual benefit forever” yields an infinite amortization period, which is illogical and would result in the write-off of the one-time expense in the test year, because the amortization amount would be infinitely small.  Therefore, I elected to use the time between rate cases rounded up to 15 years.  My explanation of this reasoning in my deposition may have been misconstrued.

Q.USWC witness Inouye contends that Staff's

post year adjustment for workforce reductions distorts

the test year.  Do you agree?

A.No.  Rolling the future benefits expected to be received annually from the one-time expense of the 1993 Restructuring Plan into the test year is a continuation of the reasoning behind amortizing the

restructuring expense into the future.  The Restructuring

Plan is a one-time unique event with significant future benefits.  These benefits should start being received soon after the test year, through 1997 and beyond.  To best reflect the on-going activities appropriately for the test year these benefits should be included.  Inouye's continued concern about growth, salary increases, and other business opportunities are normal on-going business activities and shouldn't be considered when dealing with this one-time event.  I believe that by amortizing the one-time expense and including the offsetting benefit planned to be achieved is proper test year accounting.

Q.Does this conclude your Surrebuttal Testimony in this proceeding?

A.Yes, it does.