

Results Using Commission Ordered Inputs

Q. Have you calculated US West's depreciation using Staff inputs with ELG and without truncation?

A. Yes. I have calculated the Company's annual depreciation using the same model used by US West in this proceeding. I have not truncated Staff's curves, and have used the following projection lives, as presented in Staff's October 1, 1999 Report.

Table 1

Account	Description	Projection Life
2232.3	Circuit - Digital	10.0
2232.1	Circuit - Analog	11.0
2421.1	Aerial Cable - Metallic	15.7
2422.1	Underground Cable - Metallic	18.0
2423.1	Buried Cable - Metallic	19.5
2424.1	Submarine Cable - Metallic	17.2
2426.1	Intrabuilding Cable - Metallic	21.0

As shown on page 2 of Schedule 1, Staff's inputs without truncation results in an annual increase in depreciation expense of approximately \$29.2 million.

Q. Have you prepared any calculations which show the impact of a \$29.2 million increase in depreciation expense?

A. Yes. In US West's rate case, Docket No. T-01051B-99-0105, the Company filed financial statements that include depreciation expense of \$244.8 million for the test year ending June 30,

1 1998. If the Commission increases the level of depreciation expense by \$29.2 million, this
2 annual depreciation expense would increase to approximately \$274 million.

3 By dividing depreciation (and/or amortization) expense by investment, one can better
4 understand how quickly a firm's investment is being depreciated (and/or amortized). There are
5 several ways this can be done: one can look at individual accounts, groups of accounts, or the
6 firm as a whole, on either a gross or net basis. For example, depreciation expense can be
7 divided by gross plant and equipment (ignoring depreciation accumulated in prior years), or it
8 can be divided by net plant in service (taking into account the effect of prior depreciation). As
9 shown in the table below, as of June 30, 1998, US West had gross plant in service of \$3,390.9
10 million and it had net plant in service of \$1,767.2 million. If the Commission were to increase
11 US West's depreciation expense to \$275 million, this would equate to a composite
12 depreciation rate of 8.1 percent, (annual depreciation of \$275 million divided by gross plant of
13 \$3,390.9 million equals 8.1 percent). Dividing the same level of expense by net plant of
14 \$1,767.2 million results in a figure of 15.5 percent.

15 Both of these calculations measure the rate at which the firm is recovering its capital
16 investment. The second calculation (dividing by net plant) is more relevant in the present
17 context, since it reflects the net effect of prior years' depreciation, and it provides a clearer
18 picture of how quickly the existing capital investment will be recovered if depreciation expense
19 is increased to a specified level. Thus, for example, if the Commission increases US West's
20 depreciation expense to approximately \$274 million per year, the Company's existing
21 investment in plant and equipment in Arizona will be recovered from ratepayers within
22 approximately 6.4 years (the reciprocal of 15.5 percent).

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24 **Q. Are there other methods for measuring the rate at which a company is recovering its**
25 **capital?**

1 A. Yes. One can use a broader measure of capital recovery, and a broader measure of capital
2 investment. In particular, the overall rate at which a firm is recovering its capital can be
3 measured by dividing the firm's annual depreciation and amortization expense by its total net
4 assets. As shown in the following table, as of June 30, 1998, US West had net assets of
5 \$2,212 million. Since the Company has no amortization expense, total depreciation and
6 amortization is the same as depreciation alone. Depreciation and amortization of \$274 million
7 divided by total net assets of \$2,212 equals 12.4 percent.

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9 **Table 2**

Assets	End of Test Year at June 30, 1998
Plant in Service	3,390,674
Less: Depreciation Reserve	1,623,672
Plant Under Construction	84,019
Plant Held for Future Use	0
Plant Acquisition Adjustment	1,192
Net Plant	1,852,413
Material & Supplies	16,275
Current Assets & Other Investments	283,352
Prepaid Expenses & Deferred Charges	59,919
Total Assets	2,211,959

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22 **Q. Up to this point, you have only discussed the effect of using the Staff inputs in**
23 **conjunction with ELG, without truncation. For comparison purposes, have you analyzed**
24 **the effect of using other inputs?**

25 A. Yes. Although the Commission did not expressly reverse its prior decision to rely upon Staff's
26 inputs for the seven accounts remaining under discussion, it appears that the Commission has

1 not made a final decision concerning the appropriate inputs to use for these accounts. In
2 particular, the Commission asked the parties to provide evidence concerning the impact of DSL
3 technology on these accounts, and it asked the parties to provide evidence concerning the
4 depreciation practices of other carriers. Both types of evidence could be helpful to the
5 Commission in making a final decision concerning the appropriate inputs to use for the
6 remaining seven accounts.

7 For comparison purposes, I have prepared calculations which use ELG, Staff's
8 survivor curves and Staff's salvage values in conjunction with the low and high ends of the
9 generic range of projection lives established by the FCC for these accounts¹. These lives are
10 shown below:

11 **Table 3**

12 Account	13 Description	14 Low Projection Life	15 High Projection Life
16 2232.3	17 Circuit - Digital	18 11.0	19 13.0
20 2232.1	21 Circuit - Analog	22 8.0	23 11.0
24 2421.1	Aerial Cable - Metallic	20.0	26.0
2422.1	Underground Cable - Metallic	25.0	30.0
2423.1	Buried Cable - Metallic	20.0	26.0
2424.1	Submarine Cable - Metallic	25.0	30.0
2426.1	Intrabuilding Cable - Metallic	20.0	25.0

20 As shown on page 2 of Schedule 2, if the Commission were to use the low end of the range of
21 FCC projection lives, depreciation expense would increase by approximately \$14.5 million.
22 Thus, US West's total annual depreciation expense would be approximately \$259.2 million. As
23 shown on page 2 of Schedule 3, using the high end of the range of FCC projection lives results
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¹[See, Report and Order, CC Docket 98-137, December 17, 1999]

1 in an annual decrease in depreciation expense of approximately \$11.7 million, and thus total
2 expense would be approximately \$233 million.

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4 **Q. What depreciation rates result from using the low and high FCC generic lives for the**
5 **seven remaining accounts?**

6 A. Dividing depreciation expenses of \$259.2 million and \$233 million by net plant of \$1,767.2
7 million results in composite depreciation rates of 14.7 and 13.2, respectively. Similarly, dividing
8 depreciation (and amortization) of \$259.2 million and \$233 million by net assets of \$2,212
9 equals 11.7 and 13.2 percent, respectively.