SEVENTY-THIRD REPORT

OF THE

NORTH CAROLINA UTILITIES COMMISSION

ORDERS AND DECISIONS

ISSUED FROM
JANUARY 1, 1983 THROUGH DECEMBER 31, 1983

SEVENTY-THIRD REPORT

OF THE

NORTH CAROLINA

UTILITIES COMMISSION

ORDERS AND DECISIONS

Issued from

January 1, 1983, through December 31, 1983

Robert K. Koger, Chairman

Dr. Leigh H. Hammond, Commissioner

Sarah Lindsay Tate, Commissioner

John W. Winters,* Commissioner

Edward B. Hipp, Commissioner

A. Hartwell Campbell, Commissioner

Douglas P. Leary, Commissioner

Ruth E. Cook,** Commissioner

NORTH CAROLINA UTILITIES COMMISSION

Office of the Chief Clerk

Mrs. Sandra J. Webster
Post Office Box 991
Raleigh, North Carolina 27602

The Statistical and Analytical Report of the North Carolina Utilities Commission is printed separately from the volume of Orders and Decisions and will be available from the Office of the Chief Clerk of the North Carolina Utilities Commission upon order.

* John W. Winters, term expired June 30, 1983
** Ruth E. Cook, appointed July 1, 1983

LETTER OF TRANSMITTAL

December 31, 1983

The Governor of North Carolina
Raleigh, North Carolina

Sir:

Pursuant to the provisions of Section 62-17(b) of the General Statutes of North Carolina, providing for the annual publication of the final decisions of the Utilities Commission on and after January 1, 1983, we hereby present for your consideration the report of the Commission's decisions for the 12-month period beginning January 1, 1983, and ending December 31, 1983.

The additional report provided under G.S. 62-17(a), comprising the statistical and analytical report of the Commission, is printed separately from this volume and will be transmitted immediately upon completion of printing.

Respectfully submitted,

NORTH CAROLINA UTILITIES COMMISSION

Robert K. Koger, Chairman

Dr. Leigh H. Hammond, Commissioner

Sarah Lindsay Tate, Commissioner

Edward B. Hipp, Commissioner

A. Hartwell Campbell, Commissioner

Douglas P. Leary, Commissioner

Ruth E. Cook, Commissioner

Sandra J. Webster, Chief Clerk

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North Carolina Utilities Commission

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DOCKET NO. M-100, SUB 90

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of	
Rulemaking Proceeding Concerning the Appropriate Cost-Study Group(s) for the Southern Motor Carriers Rate Conference, Inc., North Carolina Motor Carriers Association, Inc., and Motor Carriers Traffic Association, Inc., and the Proper Utilization of the Continuing Traffic Study	ORDER ADOPTING RULE R1-17(j)

BY THE COMMISSION: The Commission issued "Notice of Proposed Rule R1-17(j); Order Allowing Comments" on November 23, 1982. The Southern Motor Carriers Rate Conference filed "Additional Comments on Proposed Rule" on January 5, 1983. On February 11, 1983, the Public Staff filed a request that Super Motor Lines be substituted by South Atlantic Bonded Warehouse Company, as a Motor Carrier Traffic Association (MCTA) cost-study carrier, due to Super's withdrawal from the MCTA. Based on the entire record in this matter, the Commission concludes that the Proposed Rule R1-17(j) should be approved, with the exception that Super should be replaced by South Atlantic in the MCTA cost-study group.

IT IS, THEREFORE, ORDER as follows:

1. That Rule R1-17(j), attached hereto as Appendix A, be, and hereby is, effective upon the date of this Order.

ISSUED BY ORDER OF THE COMMISSION.
This the 14th day of September 1983.

NORTH CAROLINA UTILITIES COMMISSION
Sandra J. Webster, Chief Clerk

(SEAL)

Appendix A
RULE R1-17(j):
Additional Procedures for Filings Under G.S. 62-146(g)

(j) Additional Procedures for Collective General Commodities Rate Filings. -

In any general rate case involving one or more groups of common carriers of general commodities acting pursuant to agreement(s) approved under G.S. 62-152.1, the Commission, upon petition of the parties, will conduct public hearings to the extent possible upon a consolidated record for the purpose of rendering appropriate findings of fact and conclusions of law, subject to the following conditions:

1. Each respective group of cost-study carriers shall submit individual carrier data and a consolidated comparison of revenues-to-costs based upon the operating and financial results of designated cost-study carriers for the most current 12-month period for which data is available as of the time of the filing of the request for rate relief. The applicants shall not be precluded from updating the prefiled evidence to reflect current operating conditions.

2. The designated cost-study carriers shall be as follows:

A. Southern Motor Carriers Rate Conference cost-study carriers:

(1) Blue Ridge Trucking Company, Inc.
(2) Bruce Johnson Trucking Co., Inc.
(3) Dixie Trucking Co., Inc.
(4) Estes Express Lines
(5) Fredrickson Motor Express Corp.
(6) Standard Trucking Company

B. North Carolina Motor Carriers Association cost-study carriers:

(1) Carpenter Trucking Co., Inc.
(2) A V Dedmon
(3) Ed Mac Trucking Company, Inc.
(4) Sherman & Boddie, Inc.
(5) Wicker Service, Inc.

C. Motor Carriers Traffic Association cost-study carriers:

(1) DeHart Motor Lines, Inc.
(2) Shippers Freight Lines, Inc.
(3) South Atlantic Bonded Warehouse Company
(4) Western Carolina Express, Inc.
(5) Terminal Trucking Co.

3. In a consolidated rate case, the Commission shall fix and approve the operating ratio of the carriers, as required by G.S. 62-146(g), based upon the composite operating results of all the designated cost-study carriers which participate in the tariffs under investigation. For the purpose of presenting consolidated operating results, study carriers which do not possess a practical means of separating revenues and expenses among the various weight groups for which rate adjustments are proposed may allocate said revenues and expenses so as to reflect the identical relationship of revenues and expenses in each weight group as demonstrated for the remaining study carriers participating in the tariffs under investigation.

4. Upon petition of any person demonstrating a substantial change in the operations of any designated cost-study carrier, the Commission, after affording the parties notice and opportunity for comment, may reopen this proceeding to consider any proposed modifications in the study-carrier Frame(s).

5. The preparation and introduction of evidence in conformity with the requirements of this Rule establishes the presumption that the operating statistics and financial data of the cost-study carriers are representative of operating conditions experienced on North Carolina intrastate general commodities traffic. Nothing contained in this subsection shall limit the right of an applicant or applicants to introduce additional testimony and exhibits in support of the statutory burden of proving the adjustment to be just and reasonable.

DOCKET NO. E-100, SUB 41

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Determination of Rates for Purchase and Sale of Electricity Between Electric Utilities and Qualifying Cogenerators or Small Power Producers) RECOMMENDED ORDER) RELATING TO CAROLINA) POWER & LIGHT COMPANY

HEARD IN: The Commission Hearing Room, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina, on December 14-17, 1982

BEFORE: Robert Gruber, Hearing Examiner

APPEARANCES:

For the Respondents:

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For: Carolina Power & Light Company

Robert W. Kaylor, Associate General Counsel, Carolina Power & Light Company, P.O. Box 1551, Raleigh, North Carolina 27602
For: Carolina Power & Light Company

Steve C. Griffith, Jr., Senior Vice President and General Counsel, and W. Edward Poe, Jr., Assistant General Counsel, Duke Power Company, P.O. Box 33189, Charlotte, North Carolina 28242
For: Duke Power Company

Edgar M. Roach, Jr., Hunton & Williams, P.O. Box 109, Raleigh, North Carolina 27602
For: Virginia Electric and Power Company

Douglas M. Palais, Hunton & Williams, P.O. Box 1535, Richmond, Virginia 23212
For: Virginia Electric and Power Company

For the Intervenors:

William R. White and Tony C. Dalton, White and Dalton, Attorneys at Law, P.O. Box 1589, Brevard, North Carolina 28712
For: Carrasan Power Company and California Hydro-Systems, Inc.

Wells Eddleman, 718-A Iredell Street, Durham, North Carolina 27705
For: Himself

Robert H. Bennink, Jr., Assistant Attorney General, North Carolina Department of Justice, P.O. Box 629, Raleigh, North Carolina 27511
For: The Using and Consuming Public

G. Clark Crampton, Staff Attorney, Legal Division, Public Staff - North Carolina Utilities Commission, P.O. Box 991, Raleigh, North Carolina 27602
For: The Using and Consuming Public

ROBERT P. GRUBER, EXAMINER: The proceedings to which this Order relates were had for the purpose of determining the rates, terms, and conditions upon which Duke and the other regulated electric utility parties will be required to purchase electricity from certain "qualifying" generating facilities in the manner required and contemplated by Section 210 of the Public Utilities Regulatory Policies Act (PURPA).

The instant proceedings are only the second such proceedings held by this Commission since Section 210 of PURPA was enacted by the Congress. The first such proceedings consisted of hearings which were held in the fall and winter of 1980. Various Orders resulted therefrom (and from collaterally related hearings held with respect to wheeling). Those earlier Orders were issued during 1981, and are recapped hereinafter.

Section 210(a) of PURPA required the Federal Energy Regulatory Commission (FERC), after hearing and consultation with representatives of federal and state agencies, to prescribe and revise periodically rules which require electric utilities to sell (on a nondiscriminatory basis) electric energy to, and, more significantly, to purchase electric energy from, certain generating facilities which meet certain "qualifying" criteria. Such generating facilities fall into two broad categories. The first type of utilities required to purchase electricity under the federal law are those defined as "qualifying cogeneration" facilities. Cogeneration facilities are generally those which simultaneously produce two forms of useful energy, such as electric power and steam. An example would be a furniture manufacturing plant which not only uses process steam in its manufacturing activities, but also uses the same steam in order to generate electricity. The dual use of such energy has the obvious potential of producing substantial and significant savings in the cost of producing electricity, and also the potential for reducing the cost of electricity to ratepayers if such savings can be passed on to the ratepayers.

The second general type of generating facility from which Duke and other regulated electric utilities are required to purchase the electricity generated by it are "qualifying small power production" facilities. Such, by definition in the pertinent statutes and FERC regulations, include electric generating facilities which use waste, biomass, or "renewable resources" for energy. Such "renewable resources" are specifically defined to include wind, solar, and water energy. Such energy sources also have the obvious potential of resulting in significantly cheaper electricity. For example, the sun's rays or flowing water have no cost, as contrasted with the generally increasing costs of fossil fuels or nuclear fuel typically used by regulated utilities in their generating plants.

Such generating facilities are qualifying facilities under Section 201 of PURPA if they meet the requirements of Subchapter K, Part 292, Subpart B of Chapter I, Title 18, Code of Federal Regulations. Reference to such regulations points up that the qualifying criteria and the procedures to obtain "qualifying" status for a given generating facility are relatively simple, clear cut, and easy to apply. That aspect of this matter is not here in issue. It is merely mentioned in passing as helpful background.

As permitted by the applicable provisions of federal law (PURPA), the Federal Energy Regulatory Commission in its wisdom, by regulation, has delegated to state regulatory authorities, such as this Commission, the power and duty to implement, regulate, and oversee the implementation of Section 210 of PURPA relating to purchases and sales of electricity between and among "qualifying" electric generating facilities within the jurisdiction of such state regulatory authorities, on the one hand, and the electric utilities regulated by each such state regulatory authority, on the other hand. That delegation took place soon after the enactment of PURPA by the Congress.

Specifically, the Federal Energy Regulatory Commission (FERC), pursuant to Title II of the Public Utility Regulatory Policies Act of 1978 (PURPA), was empowered to promulgate rules and regulations to implement the act provisions, including Section 210. The FERC promulgated such rules and regulations in the form of the provisions of Subchapter K, Part 292, Subparts A, C, D, and F of Chapter I, Title 18, Code of Federal Regulations. Those regulations were amended on February 19, 1980, effective on March 20, 1980. Those regulations, as thus amended, require each regulated electric utility to collect and make available to its state regulatory authority on a biannual basis data from which each regulated utility's avoided costs may be derived. Such avoided costs are to be essentially the basis for such state regulatory authority to establish the rates to be paid to qualifying facilities by such regulated electric utilities. The FERC regulations also require generally, inter alia, each regulated electric utility to purchase electric energy from qualifying facilities; to sell electric energy on a nondiscriminatory basis to qualifying facilities (i.e., on the same basis such would be sold to any other customer which was not a generator of electricity); to interconnect with qualifying facilities; and to supply supplementary, back-up, maintenance, and interruptible power to qualifying facilities on a nondiscriminatory standard basis.

It should be further noted that this Commission has a separate duty under state law which parallels in some respects its duty to set rates for certain types of purchase transactions which are also covered by PURPA. The North Carolina General Assembly enacted in 1979 what has now been codified as North Carolina G.S. 62-156. Also certain definitions used in that section were enacted and are now codified as North Carolina G.S. 62-3(27a). That legislation provides a separate state law basis, as is specifically permitted by the FERC regulations promulgated with respect to PURPA Section 210, for this Commission to regulate and biannually review and revise the rates, and terms and conditions upon which the regulated electric utilities purchase electricity from certain types of nonpublic utility generating facilities. Essentially, such generating facilities are hydroelectric generating facilities having a generating capacity of under 80 megawatts. The Commission is to "encourage" the development of such.

With the foregoing overview, it is now appropriate to briefly examine and recap the proceedings which have been heretofore had before this Commission which relate to its powers and duties under the FERC delegation of powers and duties to it, and under the delegation by the North Carolina General Assembly pursuant to G.S. 62-156, in regulating the types of transactions here involved.

This Commission's first action with respect to implementing Section 210 of PURPA was its Order dated June 3, 1980. The Commission there scheduled a two-phase public hearing. The Phase I hearing was held on July 22, 1980, for the purpose of defining issues and procedures involved in this Commission's first attempt to deal with its duties in regulating the types of transactions involved. By Order dated September 19, 1980, the Commission directed the electric utilities to file direct testimony on or before December 15, 1980. The Phase II Public Hearing was held on January 6, 7, 8, and 26, 1981, for the purpose of resolving the issues identified in the Phase I hearings. The nature and extent of those Phase I and II hearings are set out in this Commission Order issued September 21, 1981, at pp. 5-9, incorporated herein by reference.

After the conclusion of those Phase II hearings, on March 10, 1981, the Hearing Examiner issued a Recommended Order setting standard rates and terms and conditions for the purchase and sale of electricity between utilities and qualifying cogenerators and small power producers. Exceptions to that Recommended Order were filed by Duke and Vepco. At the request of those two utilities, the Commission granted reconsideration, and oral argument was held in June 1981. This procedural history and the positions of Duke and Vepco at that time are set out in detail at pages 12-16 of this Commission Order issued September 21, 1981, in this docket, also incorporated herein by reference.

A second Recommended Order was issued on September 21, 1981, which superseded the earlier March 10, 1981, Recommended Order. No exceptions were filed with respect to that second Recommended Order, and it became final in October 1981. No appeals were taken or perfected with respect to it. That Order, inter alia, specified the avoided cost rates to be paid to qualifying facilities and approved for each regulated utility proposed terms and conditions of service to, and purchases from, such facilities.

Some mention should be made at this point of the collateral matter of wheeling. On November 17, 1981, a hearing was held to consider the cost and necessity of requiring utilities to provide wheeling services for qualifying facilities. The Hearing Examiner issued a Recommended Order relating to the wheeling matters which were there at issue on January 11, 1982. That Order, thru oversight, did not become final until December 2, 1982, its finalization having been postponed at the request of one or more of the involved utilities.

The hearings here involved ultimately arise out of this Commission Order of August 27, 1982, wherein the Commission ordered a public hearing to establish avoided cost rates and other related matters as required by the FERC regulations earlier cited. The Commission's August 27, 1982, Order generally required the regulated electric utilities in this proceeding to file with the Commission: (1) a set of its proposed "standard" avoided cost rates for purchases from qualifying facilities and to do so in a format similar to that which had been utilized by the Commission in the Appendices to the Commission Order of September 21, 1981, referred to earlier in this Order; (2) a description and information regarding the methodology and data used to calculate its proposed "standard" avoided cost rates; and (3) any proposed changes to the currently approved standard form contracts between qualifying facilities and the utility.

By Order dated October 19, 1982, the Commission rescheduled the public hearing in this proceeding for December 14, 1982.

At various times prior to the December 1982 proceedings here involved, various parties became intervenors. Those intervenors, fully recognized by the Commission to be such, are: the Public Staff, the Attorney General of North Carolina, Carrasan Power Company and California Hydro Systems, Inc., and Wells Eddleman. By ruling of the Examiner from the Bench, Mr. Eddleman's intervention was limited to the Duke Power case.

The hearing in the instant matter was held in the Commission Hearing Room in the Dobbs Building, Raleigh, North Carolina, on December 14, 15, 16, and 17, 1982. The following public witnesses appeared and testified: Tom Dorais, Steven Berkowitz, Representative John Jordan, Charles Mierek, Jane Sharp, Daniel F. Reed, and Bill Hohlman. Nantahala presented the testimony of its officer, Ed Tucker. Carolina Power & Light Company presented the testimony of its employees Dr. James N. Kimball, David R. Hostetler, and Robert W. Carney.

Duke Power Company presented the direct testimony of its employees John N. Freund and Joe Price. Duke presented also the rebuttal testimony of its Vice President Donald H. Denton, Jr.

Carrasan presented initial and additional direct testimony of its expert witness William Marcus.

The Public Staff - North Carolina Utilities Commission presented the direct testimony of its expert witness Dr. Robert Weiss.

Wells Eddleman testified on behalf of himself, but consideration of his testimony was limited to the Duke Power case.

Separate Orders are today being issued for Duke, CP&L, Vepco, and Nantahala since the issues and the findings and conclusions vary between the companies.

Based upon the evidence adduced at the subject December 1982 hearings and the entire record in this matter, the Examiner now makes the following

FINDINGS OF FACT

1. CP&L has encouraged cogeneration and small hydroelectric generation in its service territory by offering variable and fixed rates determined on an avoided-cost basis, by sending representatives to various small hydro conferences, by having the goal of attaining an additional 240 megawatts of cogeneration and small power producer capacity by the year 1995, and by cooperating and negotiating in good faith with potential customers.

2. CP&L's prefiled testimony and exhibits (dated November 8, 1982), including proposed cogeneration and small power production schedule CSP-6, are in compliance with Ordering Paragraph 3 of this Commission's August 27, 1982 Order. The proposed rate meets the requirements of North Carolina G.S. 62-156 and satisfies the rules promulgated under Federal Energy Regulatory Commission (FERC) Order No. 69 which implements the Public Utility Regulatory Policies Act (PURPA), Section 210.

3. CP&L's existing Contract Terms and Conditions are unreasonable in certain respects and should be modified as hereinafter ordered.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 1

Evidence supporting this finding is found in the testimony of public witness Tom Dorias and John Jordan and CP&L witness Wayne King. Witness Dorias stated that CP&L had supported various hydroelectric workshops by sending Company representatives to make presentations and to answer questions. Public witness Jordan commended CP&L for its cogeneration rate. Witness King testified that it was CP&L's policy to encourage customer-owned generation and that various types of incentives were offered through the proposed rate schedule CSP-6. This proposed schedule provides for both variable and fixed credits and various combinations thereof and is based on full avoided cost. Witness King further stated that the Company had made contracts with approximately 22 cogenerators and small power producers and that it was the Company's goal to have an additional 240 megawats of customer-owned generation on line by 1995. Two hydroelectric customers are served under avoided-cost rates, one on a special contract, and one on the existing standard rate.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 2

Ordering Paragraph 3 of the Commission's August 27, 1982 Order ordered CP&L to file information, as outlined in Appendix A. Appendix A required in part:

> These rates shall be designed in complete conformity with the guidelines, practices, and procedures utilized by the Commission in conjunction with development of the rates which were heretofore approved for CP&L, Duke, and Vepco pursuant to the Order entered in this docket on September 21, 1981.
>
> Said proposed standard rates shall be presented in a format identical to that utilized by the Commission in the Appendices to the Order entered herein on September 21, 1981.

King Exhibit No. 8 presents the above required information which was calculated in accordance with the required procedures. Witness King also presented several wording changes for schedule CSP-6 which were devised to clarify various aspects of administering the variable and fixed provisions of the rate.

The Commission takes judicial notice of FERC Order No. 69 and North Carolina G.S. 62-156. The Commission understands that full avoided cost rates satisfy the requirements of Order 69 as stated by Section 292.304 and by G.S. 62-156. It is also noted that G.S. 62-156 prohibits payments in excess of avoided cost. CP&L's supporting testimony and exhibits indicate that the proposed CSP-6 schedule is based on full avoided cost and therefore, by definition, satisfies the requirements under the above-cited regulations and law.

Capacity Credits

In calculating its proposed avoided capacity costs, CP&L used a combustion turbine for five-year and 10-year contract periods, and it used a base load unit for 15-year contract periods. This was the same method previously approved by the Commission in the previous proceeding in this docket.

CP&L witness King testified that although the 15-year capacity credit proposed by CP&L was based on a base load unit, CP&L preferred that the capacity credit be based on the cost of a combustion turbine. Duke witness Freund also preferred using the combustion turbine.

The Examiner recognizes that there are many methods, each having certain merits, of calculating capacity credits. It would seem that the procedure for calculating avoided capacity costs should be consistent whether such costs are being calculating for a five-year period, a 10-year period, or a 15-year period. The various parties to this proceeding calculated avoided capacity costs for five- and 10-year periods based on a peaking unit, and there was little controversy regarding the cost of constructing a peaking plant. Yet where the various parties calculated avoided capacity costs for a 15-year period based on a base load unit, there was a great deal of controversy regarding (1) the cost of constructing a base load plant, (2) regarding whether or not such plant should be a nuclear plant, and (3) regarding the amount of fuel savings applicable to the plant.

Calculation of avoided capacity credits for 15-year periods based on peaking units would be consistent with similar calculations for 5- and 10-year periods, and it would provide a more conservative approach until such time as other critical questions discussed herein are resolved in future proceedings.

Nevertheless, the procedures and rates proposed for CP&L by witness King were essentially uncontested in this proceeding, and therefore, the record does not provide the Commission with an adequate basis in this proceeding of using a combustion turbine for calculating rates for a 15-year contract period for CP&L. Accordingly, the Examiner will approve the rates proposed herein by CP&L, with the admonition that the matter of using combustion turbines for calculating 15-year capacity credits should be discussed in detail in the next proceeding in this docket.

Variable O&M

In calculating energy credits, CP&L includes some variable O&M expenses in addition to the variable O&M expenses already in its PROMOD simulation. Such additional O&M alone is approximately 0.265¢ per kWh (in 1983 dollars) while Duke only includes 0.084¢ per kWh total variable O&M (in 1983 dollars).

Therefore, CP&L includes at least three times as much variable O&M per kWh as Duke does in its calculation of energy credits. The Commission is not persuaded that the variable O&M expenses of CP&L are three times as great as Duke's. There may be a discrepancy between CP&L and Duke as to which expenses should be classified as variable O&M expenses for purposes of calculating the energy credits. The record in this proceeding offers little to no help in this regard.

In order to resolve this problem in future proceedings, CP&L whould furnish for the record:

(a) The line items (by account number) which are included in the variable O&M expenses utilized for calculating energy credits;

(b) The line items (by account number) which are included in the fixed O&M expenses utilized for calculating capacity credits;

(c) Descriptions of each line item utilized for calculating energy and capacity credits;

(d) The dollar amount of each line item;

(e) The kWh utilized for calculating the variable O&M expenses per kWh; and

(f) The kW utilized for calculating the fixed O&M expenses per kWh.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 3

CP&L witness King testified that CP&L's Terms and Conditions for the Purchase of Electric Power has proven to be reasonable and appropriate in light of the Company's experience in having made approximately 22 contacts with potential small power producers. Witness King emphasized, and the Examiner generally concurs, that a considerable amount of flexibility is necessary to encourage each potential project because of the often unique characteristics associated with individual generating sites and facilities.

In comments filed on March 2, 1983, the Public Staff proposed that CP&L's standard form agreements be revised and modified. The Public Staf contends that the agreements are illegal and illusory, and will tend to discourage cogenerators from entering into contracts with CP&L and will inhibit their ability to obtain financing. On March 15, 1983, CP&L filed comments in which it specifically addressed each of the Public Staff's comments. Having reviewed and considered these comments, the Examiner makes the following conclusions relating to the standard form agreements and terms and conditions:

THE APPLICATION

1. The title of the application should be changed from "Application For Purchase of Electric Power" to "Application For Standard Contract By a Qualifying Cogenerator or Small Power Producer." This title will better identify the document.

2. The Examiner declines to adopt the Public Staff's recommended note to be shown in bold type under the title which states that CP&L is required to offer the standard form contract to all qualifying cogenerators or such power production facilities. Such a note leaves a strong negative conotation that CP&L is not willingly entering into standard contracts or otherwise encouraging cogeneration. The Examiner has found CP&L is actively and vigorously encouraging cogeneration.

3. The Examiner agrees with the Public Staff that some revision of paragraph 4 is needed for clarification. It should be revised to read as follows:

> "4. Upon the acceptance hereof by the Company, evidenced by the signature of its authorized representative in the block provided below, this document together with attachments shall become an agreement for Seller to deliver and sell to Company and for Company to service and purchase from Seller the electricity generated and declared by Seller from its above described qualifying generating facility at the rates,

in the quantities, for the term, and upon the terms and conditions set forth herein."

4. The Public Staff recommends that paragraph 8 be deleted. Paragraph 8 reads as follows:

"8. This Agreement and the attached applicable Schedule, Riders, and Terms and Conditions are subject to changes or substitutions, either in whole or in part, made from time to time by a legally effective filing of the Company with, or by order of, the regulatory authority having jurisdiction, and each party to this Agreement reserves the right to seek changes or substitutions, in accordance with law, from such regulatory authority. Unless specified otherwise, any such changes or substitutions shall become effective immediately and shall nullify all prior provisions in conflict therewith."

The Public Staff's reason for the proposed change reads as follows:

"Reason for Change: This paragraph, as presently written, renders the entire contractual arrangement illusory. The thrust of it is to provide that any aspect of the contractual arrangements are subject to being changed. That simply means that there is no stability or certainty at all in the arrangements. Thus, such matters as the rates, term, and even the obligation by CP&L to purchase the output of the QF are neither established or certain by virtue of this paragraph 8. Those crucial matters are, of course, the ones which lenders and investors will reasonably and logically insist be certain and established. What lender on the strength of such a contract would even consider lending money? What investor would even consider investing? Lenders and investors simply will not provide capital for projects which are subject to such uncertainty and change. Moreover, as drafted, in order to effectuate even the most major changes (e.g., withdrawal of the applicable rate schedule or filing altogether) all CP&L must do is to make a "legally effective filing." This obviously renders the entire contract subject to being terminated or substantially modified without even Commission approval."

In its response CP&L states: "Paragraph 8 is intended strictly for informational purposes to appraise and identify a regulatory agency's (the North Carolina Utilities Commission) right under one to regulate utility companies. To our knowledge, this paragraph has never been questioned by any Qualifying Facilities and has not proved detrimental to a Seller obtaining financing. The Public Staff's complaint seems to center on the phrase "legally effective filing"; therefore substitute language may be appropriate to alleviate this concern."

The Examiner concludes that paragraph 8 should be deleted. This paragraph would allow the Commission to change the agreed upon rate or essential terms at any time upon petition of either party to the contract. A contract which would allow the Commission to modify the contract at any time is indefinite. Such a provision would have little more value than a "day-to-day" contract and would seriously inhibit the ability of cogenerators to obtain long-term financing, and would thereby, discourage long-term contracts and levelized rates.

TERMS AND CONDITIONS FOR THE PURCHASE OF ELECTRIC POWER

The Public Staff also contends that the paragraph 1(c) set forth below should be modified to delete the last two lines:

"(c) Application of Terms and Conditions, Schedules, and Riders - All Purchase Agreements in effect at the approval hereof or that may be entered into in the future, are expressly subject to these terms and conditions, and subject to all applicable Schedules and Riders, and any changes therein, substitutions thereby, or additions thereto lawfully made.

The Examiner concludes that this provision adds uncertainty to the contract. Since a schedule or rider may relate to a rate, it could be argued that this language would make both annual long-term rates subject to revision by the Commission. As stated above, such a provision makes it difficult to obtain financing. The Examiner concludes that this provision should be amended to include the underlined proviso:

(c) Application of Term and Conditions, Schedules, and Riders - All Purchase Agreements in effect at the approval hereof or that may be entered into in the future, are expressly subject to these terms and conditions, and subject to all applicable Schedules and Riders, and any changes therein, substitutions thereby, and additions thereto lawfully made, provided no change may be made in rates or in essential terms and conditions of this contract except by agreement of the parties to this contract.

2. The Public Staff recommends that subparagraph (6) of (h) on page 2 of the terms and conditions be deleted in its entirety. This paragraph reads as follows:

"(6) at any time when Company would incur additional cost from making such purchase above that which Company would incur from generating its own electricity or purchasing electricity from other available sources."

The Public Staff states that such a termination provision is inconsistent, as a matter of law, with the provisions of North Carolina G.S. 62-156 and the FERC regulations authorizing levelized long term contractual managements. Levelized rates inherently involve the utility paying more at first than its "avoided cost" and less than its avoided cost in the later part of the term.

CP&L's response and proposed change is as follows:

"CP&L's Response: CP&L has received comments from Qualifying Facilities that paragraph 1.(h).(6). adversely affects financing. We appreciate this opportunity to clarify the intentions of this paragraph and to propose a revision to this paragraph.

CP&L's system load is temperature sensitive. There are times, including the mild spring and fall seasons, holidays, weekends, etc., when the system load requirement is met entirely with low fuel cost base load (nuclear and large coal plants) generation. Since there are no size limitations on our proposed standard contract, during CP&L low load periods a large cogenerator (and we are negotiating with several in the 30-80 mW range) could necessitate that CP&L substantially reduce generation from low fuel

cost base load units. It is not desirable to cycle or to substantially reduce base load generation since both of these situations could require several days to restore normal operation. Clearly, the purchase of higher priced nonutility generated electricity in lieu of the lower priced CP&L generated electricity and the possibility of operating problems with CP&L's base load units are not in the best interest of CP&L or its retail customers.

This operating constraint is recognized in PURPA, Section 210, which includes the following provision:

Section 292.304 (f) Periods during which purchases not required.

(1) Any electric utility which gives notice pursuant to subparagraph (2) will not be required to purchase electric energy or capacity during any period during which, due to operational circumstances, purchases from qualifying facilities will result in costs greater than those which the utility would incur if it did not make such purchases, but instead generated an equivalent amount of energy itself.

While paragraph 1.(h).(6). has not unduly discouraged the development of cogeneration and small power production, CP&L recognized the initial reaction to this paragraph could be negative.

CP&L's Proposed Change: Delete item 1.(h).(6). and all references to item 1.(h).(6). contained in paragraph 1.(h). and other locations throughout the Terms and Conditions for the Purchase of Electric Power, and substitute a new paragraph 1.(i). as follows:

1. (i) Suspension of Purchases at Company's Request

If Seller has a Contract Capacity of 5,000 kW or greater, company will contract for a maximum number of hours annually during which Company may suspend purchases. Company will exercise reasonable and diligent effort to notify Seller, and provide maximum prior notice, prior to a request for suspension to allow for Seller's proper planning and coordination of such suspension."

The Examiner concludes that CP&L's proposed change is necessary and reasonable and consistent with relevant statutes and regulations, and should be approved.

3. The Public Staff recommends that the first two full paragraphs in "Section 12, Governmental Restrictions," be deleted. These read as follows:

"This Agreement is subject to the jurisdiction of those governmental agencies having control over either party or over this Agreement. This Agreement shall not become effective until all required governmental authorizations, such as approval of qualifying status, and permits are first obtained and copies thereof are submitted to Company; provided, that this Agreement shall not become

> effective unless it and all provisions thereof are authorized and permitted by such governmental agencies without change or conditions.
>
> This Agreement shall at all times be subject to changes by such governmental agencies, and the parties shall be subject to conditions and obligations, as such governmental agencies may, from time to time, direct in the exercise of their jurisdiction. Both parties agree to exert their best efforts to comply with all of the applicable rules and regulations of all governmental agencies having control over either party or this Agreement. The parties shall take all reasonable action necessary to secure all required governmental approval of this Agreement in its entirety and without change."

As stated earlier, it is not necessary or appropriate that long-term rates and the essential terms of agreements once entered into be made subject to changes by governmental agencies. It is reasonable that the contract be subject to minor technical amendments and clarifying amendments. It is also is appropriate that the parties agree that the agreement shall not become effective until all governmental authorizations are obtained, and that the parties agree to make good faith efforts to comply with all reasonable governmental rates and regulations. Therefore the first sentence in paragraph 2 should be amended to add the underlined proviso: "This agreement shall at all times be subject to changes by such governmental agencies, and the parties shall be subject to conditions and obligations, as such governmental agencies may, from time to time, direct in the exercise of their jurisdiction, <u>provided no change may be made in rates or in essential terms and conditions of this contract except by agreement of the parties to this contract.</u>"

<u>REVISIONS IN CP&L's RATE SCHEDULE CSP-6</u>

The Public Staff points out that the <u>Contract Period</u> provision of the rate does not clearly indicate that an annual contract is available when only energy purchases are desired by a qualifying facility. The Examiner accepts and approves CP&L's recommendation that present Contract Period Provisions be deleted and replaced by the following:

> "The Contract Period for Qualifying Facilities who desire a capacity credit shall be at least five years with minimum one-year renewal periods. One-year contracts are available to Qualifying Facilities who desire an energy credit only. Qualifying Facilities classified as New Capacity with five-year or longer contract terms may choose different lengths for Energy Credits and Capacity Credits, except that the Rate Term of the Energy Credit."

Except for the modification herein required, CP&L's standard terms and conditions are approved.

IT IS, THEREFORE, ORDERED as follows:

1. That CP&L's proposed cogeneration and small power producer schedule, CSP-6, is hereby approved as filed.

2. That the existing Contract Terms and Conditions shall be modified in accordance with Finding of Fact No. 3 and supporting conclusions, and a copy

of such revised contract be filed with the Commission within 10 days of the effective date of this Recommended Order.

3. That CP&L shall furnish for the record in future proceedings in this docket:

(a) The line items (by account number) which are included in the variable O&M expenses utilized for calculating energy credits;

(b) The line items (by account number) which are included in the fixed O&M expenses utilized for calculating capacity credits;

(c) Descriptions of each line item utilized for calculating energy and capacity credits;

(d) The dollar amount of each line item;

(e) The kWh utilized for calculating the variable O&M expenses per kWh; and

(f) The kW utilized for calculating the fixed O&M expenses per kWh.

ISSUED BY ORDER OF THE COMMISSION.
This the 1st day of April 1983.

NORTH CAROLINA UTILITIES COMMISSION
Sharon Credle Miller, Deputy Clerk

(SEAL)

DOCKET NO. E-100, SUB 41

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Determination of Rates for Purchase and Sale of Electricity Between Electric Utilities and Qualifying Cogenerators or Small Power Producers) RECOMMENDED ORDER RELATING TO DUKE POWER COMPANY

HEARD IN: The Commission Hearing Room, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina, on December 14-17, 1982

BEFORE: Robert Gruber, Hearing Examiner

APPEARANCES:

For the Respondents:

John Bode, Bode, Bode & Call, Attorneys at Law, P.O. Box 391, Raleigh, North Carolina 27602
For: Carolina Power & Light Company

Robert W. Kaylor, Associate General Counsel, Carolina Power & Light Company, P.O. Box 1551, Raleigh, North Carolina 27602
For: Carolina Power & Light Company

Steve C. Griffith, Jr., Senior Vice President and General Counsel, and W. Edward Poe, Jr., Assistant General Counsel, Duke Power Company, P.O. Box 33189, Charlotte, North Carolina 28242
For: Duke Power Company

Edgar M. Roach, Jr., Hunton & Williams, P.O. Box 109, Raleigh, North Carolina 27602
For: Virginia Electric and Power Company

Douglas M. Palais, Hunton & Williams, P.O. Box 1535, Richmond, Virginia 23212
For: Virginia Electric and Power Company

For the Intervenors:

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For: Carrasan Power Company and California Hydro-Systems, Inc.

Wells Eddleman, 718-A Iredell Street, Durham, North Carolina 27705
For: Himself

Robert H. Bennink, Jr., Assistant Attorney General, North Carolina Department of Justice, P.O. Box 629, Raleigh, North Carolina 27511
For: The Using and Consuming Public

G. Clark Crampton; Staff Attorney, Legal Division, Public Staff - North Carolina Utilities Commission, P.O. Box 991, Raleigh, North Carolina 27602
For: The Using and Consuming Public

ROBERT P. GRUBER, EXAMINER: The proceedings to which this Order relates were had for the purpose of determining the rates, terms, and conditions upon which Duke and the other regulated electric utility parties will be required to purchase electricity from certain "qualifying" generating facilities in the manner required and contemplated by Section 210 of the Public Utilities Regulatory Policies Act (PURPA).

The instant proceedings are only the second such proceedings held by this Commission since Section 210 of PURPA was enacted by the Congress. The first such proceedings consisted of hearings which were held in the fall and winter of 1980. Various Orders resulted therefrom (and from collaterally related hearings held with respect to wheeling). Those earlier Orders were issued during 1981, and are recapped hereinafter.

Section 210(a) of PURPA required the Federal Energy Regulatory Commission (FERC), after hearing and consultation with representatives of federal and state agencies, to prescribe and revise periodically rules which require electric utilities to sell (on a nondiscriminatory basis) electric energy to, and, more significantly, to purchase electric energy from, certain generating facilities which meet certain "qualifying" criteria. Such generating facilities fall into two broad categories. The first type of utilities required to purchase electricity under the federal law are those defined as

"qualifying cogeneration" facilities. Cogeneration facilities are generally those which simultaneously produce two forms of useful energy, such as electric power and steam. An example would be a furniture manufacturing plant which not only uses process steam in its manufacturing activities, but also uses the same steam in order to generate electricity. The dual use of such energy has the obvious potential of producing substantial and significant savings in the cost of producing electricity, and also the potential for reducing the cost of electricity to ratepayers if such savings can be passed on to the ratepayers.

The second general type of generating facility from which Duke and other regulated electric utilities are required to purchase the electricity generated by it are "qualifying small power production" facilities. Such, by definition in the pertinent statutes and FERC regulations, include electric generating facilities which use waste, biomass, or "renewable resources" for energy. Such "renewable resources" are specifically defined to include wind, solar, and water energy. Such energy sources also have the obvious potential of resulting in significantly cheaper electricity. For example, the sun's rays or flowing water have no cost, as contrasted with the generally increasing costs of fossil fuels or nuclear fuel typically used by regulated utilities in their generating plants.

Such generating facilities are qualifying facilities under Section 201 of PURPA if they meet the requirements of Subchapter K, Part 292, Subpart B of Chapter I, Title 18, Code of Federal Regulations. Reference to such regulations points up that the qualifying criteria and the procedures to obtain "qualifying" status for a given generating facility are relatively simple, clear cut, and easy to apply. That aspect of this matter is not here in issue. It is merely mentioned in passing as helpful background.

As permitted by the applicable provisions of federal law (PURPA), the Federal Energy Regulatory Commission in its wisdom, by regulation, has delegated to state regulatory authorities, such as this Commission, the power and duty to implement, regulate, and oversee the implementation of Section 210 of PURPA relating to purchases and sales of electricity between and among "qualifying" electric generating facilities within the jurisdiction of such state regulatory authorities, on the one hand, and the electric utilities regulated by each such state regulatory authority, on the other hand. That delegation took place soon after the enactment of PURPA by the Congress.

Specifically, the Federal Energy Regulatory Commission (FERC), pursuant to Title II of the Public Utility Regulatory Policies Act of 1978 (PURPA), was empowered to promulgate rules and regulations to implement the act provisions, including Section 210. The FERC promulgated such rules and regulations in the form of the provisions of Subchapter K, Part 292, Subparts A, C, D, and F of Chapter I, Title 18, Code of Federal Regulations. Those regulations were amended on February 19, 1980, effective on March 20, 1980. Those regulations, as thus amended, require each regulated electric utility to collect and make available to its state regulatory authority on a biannual basis data from which each regulated utility's avoided costs may be derived. Such avoided costs are to be essentially the basis for such state regulatory authority to establish the rates to be paid to qualifying facilities by such regulated electric utilities. The FERC regulations also require generally, inter alia, each regulated electric utility to purchase electric energy from qualifying facilities; to sell electric energy on a nondiscriminatory basis to

qualifying facilities (i.e., on the same basis such would be sold to any other customer which was not a generator of electricity); to interconnect with qualifying facilities; and to supply supplementary, back-up, maintenance, and interruptible power to qualifying facilities on a nondiscriminatory standard basis.

It should be further noted that this Commission has a separate duty under state law which parallels in some respects its duty to set rates for certain types of purchase transactions which are also covered by PURPA. The North Carolina General Assembly enacted in 1979 what has now been codified as North Carolina G.S. 62-156. Also certain definitions used in that section were enacted and are now codified as North Carolina G.S. 62-3(27a). That legislation provides a separate state law basis, as is specifically permitted by the FERC regulations promulgated with respect to PURPA Section 210, for this Commission to regulate and biannually review and revise the rates, and terms and conditions upon which the regulated electric utilities purchase electricity from certain types of nonpublic utility generating facilities. Essentially, such generating facilities are hydroelectric generating facilities having a generating capacity of under 80 megawatts. The Commission is to "encourage" the development of such.

With the foregoing overview, it is now appropriate to briefly examine and recap the proceedings which have been heretofore had before this Commission which relate to its powers and duties under the FERC delegation of powers and duties to it, and under the delegation by the North Carolina General Assembly pursuant to G.S. 62-156, in regulating the types of transactions here involved.

This Commission's first action with respect to implementing Section 210 of PURPA was its Order dated June 3, 1980. The Commission there scheduled a two-phase public hearing. The Phase I hearing was held on July 22, 1980, for the purpose of defining issues and procedures involved in this Commission's first attempt to deal with its duties in regulating the types of transactions involved. By Order dated September 19, 1980, the Commission directed the electric utilities to file direct testimony on or before December 15, 1980. The Phase II Public Hearing was held on January 6, 7, 8, and 26, 1981, for the purpose of resolving the issues identified in the Phase I hearings. The nature and extent of those Phase I and II hearings are set out in this Commission Order issued September 21, 1981, at pp. 5-9, incorporated herein by reference.

After the conclusion of those Phase II hearings, on March 10, 1981, the Hearing Examiner issued a Recommended Order setting standard rates and terms and conditions for the purchase and sale of electricity between utilities and qualifying cogenerators and small power producers. Exceptions to that Recommended Order were filed by Duke and Vepco. At the request of those two utilities, the Commission granted reconsideration, and oral argument was held in June 1981. This procedural history and the positions of Duke and Vepco at that time are set out in detail at pages 12-16 of this Commission Order issued September 21, 1981, in this docket, also incorporated herein by reference.

A second Recommended Order was issued on September 21, 1981, which superseded the earlier March 10, 1981, Recommended Order. No exceptions were filed with respect to that second Recommended Order, and it became final in October 1981. No appeals were taken or perfected with respect to it. That

Order, inter alia, specified the avoided cost rates to be paid to qualifying facilities and approved for each regulated utility proposed terms and conditions of service to, and purchases from, such facilities.

Some mention should be made at this point of the collateral matter of wheeling. On November 17, 1981, a hearing was held to consider the cost and necessity of requiring utilities to provide wheeling services for qualifying facilities. The Hearing Examiner issued a Recommended Order relating to the wheeling matters which were there at issue on January 11, 1982. That Order, thru oversight, did not become final until December 2, 1982, its finalization having been postponed at the request of one or more of the involved utilities.

The hearings here involved ultimately arise out of this Commission Order of August 27, 1982, wherein the Commission ordered a public hearing to establish avoided cost rates and other related matters as required by the FERC regulations earlier cited. The Commission's August 27, 1982, Order generally required the regulated electric utilities in this proceeding to file with the Commission: (1) a set of its proposed "standard" avoided cost rates for purchases from qualifying facilities and to do so in a format similar to that which had been utilized by the Commission in the Appendices to the Commission Order of September 21, 1981, referred to earlier in this Order; (2) a description and information regarding the methodology and data used to calculate its proposed "standard" avoided cost rates; and (3) any proposed changes to the currently approved standard form contracts between qualifying facilities and the utility.

By Order dated October 19, 1982, the Commission rescheduled the public hearing in this proceeding for December 14, 1982.

At various times prior to the December 1982 proceedings here involved, various parties became intervenors. Those intervenors, fully recognized by the Commission to be such, are: the Public Staff, the Attorney General of North Carolina, Carrasan Power Company and California Hydro Systems, Inc., and Wells Eddleman. By ruling of the Examiner from the Bench, Mr. Eddleman's intervention was limited to the Duke Power case.

The hearing in the instant matter was held in the Commission Hearing Room in the Dobbs Building, Raleigh, North Carolina, on December 14, 15, 16, and 17, 1982. The following public witnesses appeared and testified: Tom Dorais, Steven Berkowitz, Representative John Jordan, Charles Mierek, Jane Sharp, Daniel F. Reed, and Bill Hohlman. Nantahala presented the testimony of its officer, Ed Tucker. Carolina Power & Light Company presented the testimony of its employees Dr. James N. Kimball, David R. Hostetler, and Robert W. Carney.

Duke Power Company presented the direct testimony of its employees John N. Freund and Joe Price. Duke presented also the rebuttal testimony of its Vice President Donald H. Denton, Jr.

Carrasan presented initial and additional direct testimony of its expert witness William Marcus.

The Public Staff - North Carolina Utilities Commission presented the direct testimony of its expert witness Dr. Robert Weiss.

Wells Eddleman testified on behalf of himself, but consideration of his testimony was limited to the Duke Power case.

Separate Orders are today being issued for Duke, CP&L, Vepco, and Nantahala since the issues and the findings and conclusions vary between the companies.

Based upon the evidence adduced at the subject December 1982 hearings and the entire record in this matter, the Examiner now makes the following:

FINDINGS OF FACT

1. Duke is a public utility corporation organized and existing under the laws of the State of North Carolina, is fully authorized to transact business in the State of North Carolina and is subject to the jurisdiction of this Commission including its jurisdiction with respect to all matters and issues here involved.

2. Duke's present and proposed energy rates are as follows:

Contract Terms	Present Rate	Proposed Rate
5-year fixed rate		
on peak hours	2.87 cents	2.96 cents
off peak hours	2.15 cents	2.01 cents
10-year fixed rate		
on peak hours	3.93 cents	3.67 cents
off peak hours	2.96 cents	2.31 cents
15-year fixed rate		
on peak hours	5.02 cents	4.28 cents
off peak hours	3.78 cents	2.56 cents
5-year variable rate		
on peak hours	2.2239 cents	2.74 cents
off peak hours	1.6784 cents	1.89 cents

3. The proposed energy and capacity credits filed by Duke Power Company in Schedule PP(NC) Purchased Power do not fully reflect the Company's avoided costs and should be supplemented, adjusted, and revised in the manner and to the extent hereinafter set out in this Order. (See Appendix A for summary.)

4. Duke's proposed energy credits should be increased because Duke's PROMOD analysis contains overly optimistic nuclear powerplant performance assumptions. The adjustments should be as follows (in ¢/kWh):

Variable Rate	0.10
5-Year Rate	0.10
10-Year Rate	0.15
15-Year Rate	0.20

5. Duke's proposed energy credits should be increased to include line losses. The adjustments should be as follows (in ¢/kWh):

	On Peak Hours	Off Peak Hours
Variable Rate	0.10	0.08
5-Year Rate	0.11	0.08
10-Year Rate	0.14	0.09
15-Year Rate	0.17	0.10

6. Duke's proposed energy credits should be increased to reflect a greater working capital allowance than was proposed by Duke. The adjustments should be as follows (in ¢/kWh):

	On Peak Hours	Off Peak Hours
Variable Rate	0.09	0.06
5-Year Rate	0.10	0.06
10-Year Rate	0.12	0.08
15-Year Rate	0.14	0.09

7. Duke's present and proposed capacity credits are as follows (¢/kWh):

Contract Terms	Present Credit	Proposed Credit
5-Year Fixed Rate		
Peak Month	1.11	1.34
Base Month	0.66	0.81
10-Year Fixed Rate		
Peak Month	1.11	1.55
Base Month	.66	0.94
15-Year Fixed Rate		
Peak Month	1.17	1.67
Base Month	0.69	1.01
5 Year Variable Rate		
Peak Month	1.11	1.25
Base Month	0.66	0.76

8. Duke's proposed capacity credits for all periods should be increased to include line losses. The adjustments should be as follows (¢/kWh):

Peak Month	Base Month
0.05	0.02
0.05	0.03
0.06	0.04
0.07	0.04

9. Duke's proposed capacity credit for the 15-year period should be based on use of a peaking unit which adds to Duke's proposed capacity credit the amount of .09¢/kWh during the peak season and .05¢/kWh during the off-peak season or base month.

10. The record in this proceeding is incomplete with regard to variable operating and maintenance expenses and general plant expenses, and these costs should be more fully examined in future proceedings.

11. Duke's proposed amendments to Paragraphs 5 and 8 are unreasonable. It would have the effect of discouraging small power production and cogeneration projects.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 1

These findings are essentially jurisdictional and do not involve matters here at issue or in dispute. The evidence or basis for these findings are contained in the provisions of Chapter 62 of the North Carolina Utilities Commission (including N.C.G.S. 62-156), the provisions of the Public Utilities Regulatory Policy Act, the Rules and Regulations of the Federal Energy Regulatory Commission which have been promulgated and published in the Federal Register in order to implement Section 210 of PURPA, and other Orders by this Commission in this docket and Duke's filings, appearances, and evidence in the December 1982 hearings, indicating its recognition of this Commission's jurisdiction in the premises.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 2 AND 3

Five witnesses presented expert testimony on the proper avoided cost energy credits for Duke Power Company. The Company presented John Freund, Carrasan Power Company presented William Marcus, and the Public Staff presented Dr. Robert Weiss. The Company also presented Donald Denton, Jr. Mr. Eddleman testified on his own behalf.

The rate schedule proposed by Duke is given in Freund Exhibit 1. It is in the format which was proposed by the Commission in the one earlier "avoided cost" rate proceedings earlier described in this Order. Duke's proposed rates include a five-year variable rate, a five-year fixed rate, a 10-year fixed rate, and a 15-year fixed rate. At the conclusion of the hearings, however, Duke's Vice President Donald Denton requested that the Commission not approve any 15-year fixed rate for Duke to the end that Duke simply would not offer or be required to offer any such long-term rate.

Duke's proposed energy credits for contracts up to 10 years were based on PROMOD calculations, a method which this Commission on one prior occasion found acceptable. Duke's proposed 15-year energy credits, however, were not based on PROMOD, but rather on a regression analysis performed by Duke based on PROMOD results for the 10-year forecast and upon Duke's assumption of a 20% reserve margin for the 1993-1997 period.

The results of Duke's methodology were criticized on several grounds by several parties. Witness Marcus, the expert witness for Intervenor Carrasan, made adjustments to both Duke's proposed energy and capacity credits. Witness Marcus' energy adjustments were designed and intended to reflect the proper treatment of the 1993-1997 period, reasonable assumptions relating to the future performance of Duke's nuclear plants, reasonable working capital requirements and assumptions, and consideration of line losses.

Witness Marcus' major adjustment related to treatment of the 1993-1997 period. As stated previously, Duke used a regession analysis technique in order to estimate short-run avoided costs in the period 1993-1997 and further assumed that sufficient capacity would be built up to keep the reserve margin at 20%. Witness Marcus contended that the fact that Duke had none of such capacity as was assumed by Duke in its current construction or resource plan

and therefore Duke should not assume that any such new capacity will be available. He contended Duke should derive its avoided energy costs without assuming any capacity that is not in Duke's own resource plan. This method was used in Duke's PROMOD runs dated October 11 and October 12, 1982, to reflect the 1993-97 period. This method raises on-peak prices by 0.88¢/kWh and off-peak prices by 0.35¢/kWh.

Witness Freund testified that to assume no capacity additions to the Duke system beyond Catawba Unit 2 would necessarily result in a situation of fixed capacity during a period of increasing load which would require Duke to operate its cost efficient generating units more and more frequently as its reserve margin is exhausted. Under this scenario, Duke's avoided energy costs would sprial upward dramatically.

The main question raised by witness Marcus is whether capacity additions not now in the resource plan should be considered in deriving avoided energy costs. (The phrase "energy costs" should be taken to mean all variable operating costs such as operation and maintenance, working capital adjustments, etc.) The Examiner agrees that Duke's general approach, which is to assume that the Company would meet its load and preserve an appropriate reserve margin by constructing base loaded plants, is correct. In order to calculate avoided costs it is proper to look at what the Company can reasonably be expected to do to provide service at the lowest possible cost; i.e., construct fuel efficient base loaded plants. The marginal costs associated with that expansion path are the utility's avoided costs. It is not correct to assume, as does witness Marcus, that the utility will not minimize its costs, but will meet its load by operating plants with high marginal energy costs.

Duke has asked the Commission not to approve a 15-year rate based on any method. Duke contends all methods are inherently speculative. The Examiner believes that it is Commission policy to establish a 15-year rate, and Duke's methodology using a regression model is the only reasonable basis in the record for establishing avoided costs and rates 15 years hence.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 4

Carrasan's witness Marcus testified that in developing avoided energy costs using the PROMOD computer model, a utility must input the following data into the model:

1. Forced outage ratios (both full and partial) for all units,

2. Maintenance schedules on an annual basis for all units,

3. Scheduled in-service dates for new power plants,

4. Demand forecasts and load duration curves,

5. Fuel price forecasts, and

6. Incremental heat rates for all units at full and partial load.

He stated that of particular importance is the reasonableness of nuclear availability assumptions and the in-service dates of nuclear units. If

nuclear units are unavailable, there will be increased use of less efficient coal, oil, and gas plants, and overly optimistic assumptions as to nuclear availability cause an understatement of avoided energy costs.

Witness Marcus concluded that Duke has overstated nuclear availability. He based his conclusions on his study comparing Duke's power plant performance assumptions included in its PROMOD model with the historical experience of Duke and other North Carolina utilities. Witness Marcus testified Duke's overly optimistic estimate of nuclear performance underestimated avoided costs by 0.1¢/kWh for a 5-year contract, 0.15¢/kWh for a 10-year contract, and 0.2¢/kWh for a 15-year contract.

Duke did not dispute witness Marcus' estimates of nuclear performance. The only evidence contesting witness Marcus' estimates was provided in the testimony of witness Eddleman and his cross-examination of witness Marcus. Witness Eddleman asserted that problems with Westinghouse steam generators at the McGuire nuclear plants have depressed its performance below Duke's projections, and witness Marcus agreed that the inclusion of such steam generator problems, if warranted, would increase the avoided cost above his estimates.

In sum, witness Marcus' estimates are conservative; the only evidence in the record which does not support them would suggest that they should be higher, not lower. His adjustment for nuclear powerplant performance is the minimum adjustment which should be adopted by the Commission.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 5

Witness Marcus pointed out that Duke has failed to include line losses in its pricing formula. Duke did not contest this point.

Failure to include line losses contravenes the Commission's September 24, 1981, Order which indicates that they should be included. It also violates the Commission's August 27, 1982, Order that rates "shall be designed in complete conformity" with past Commission Orders. CP&L includes these loss factors.

In the absence of specific evidence relating to Duke's losses, the Commission should apply CP&L's loss factors to Duke's rates before losses. These factors are 3.53% on-peak and 2.62% off-peak. As described in the cross-examination testimony of witness King, the correct way to apply these factors is to divide the on-peak rate before losses by 0.9647 (1 minus 3.53%) and to divide the off-peak rate by 0.9738 (1 minus 2.62%).

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 6

Duke includes an allowance of 5.4% of fuel costs for fuel inventory. No additional working capital allowance is included. Duke's narrow definition, which excludes working capital other than fuel inventories, was utilized despite the Commission's September 1981 Order requiring utilities to include additional components of working capital in addition to fuel inventories.

CP&L, by comparison, included a 9% allowance for working capital containing not only fuel inventory but cash working capital from a lead-lag study. Witness Marcus testified that Duke's allowance is overly limited.

If cash working capital should include one-eighth (1/8) of avoided fuel costs as well as fuel inventory, then Duke's annual carrying charges would be approximately 8.4%. The 8.4% is comparable to the 9.0% utilized by CP&L. Therefore, Duke's calculation of energy credits should utilize an 8.4% allowance for working capital instead of 5.42%.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 7 AND 8

The adjustments for line losses to capacity credits are the same as to adjustments for line losses to the energy credits, and are set forth in Evidence and Conclusions for Finding of Fact No. 5.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 9

In calculating its proposed avoided capacity costs Duke used and assumed a combustion turbine (as the basis for the "avoided cost") for the shorter contract periods and used and assumed a baseload plant for the calculation of Duke's proposed avoided capacity costs for the 15-year period. This was a methodology previously suggested or approved by this Commission in its last Order. In applying the methodology, Duke used the cost of its McGuire Nuclear Unit 2 as the base load plant. This cost as asserted by Duke was $828 per kilowatt.

Both witness Marcus and Dr. Weiss criticized Duke's use of the cost of its McGuire nuclear unit as the basis for Duke's calculated avoided capacity cost. Dr. Weiss used a figure of $995 per kilowatt, as the realistic present cost of a nuclear plant. This was approximately 20% higher than the cost used by Duke. Witness Marcus recommended that a figure of $1279 per kilowatt, Duke's estimate for Catawba, be used.

Witness Freund testified that although the 15-year capacity credit proposed in Freund Exhibit 2 was based upon a nuclear unit, Duke preferred and recommended that the credit be based on the cost of a combustion turbine. CP&L witness King also preferred this method.

The Examiner recognizes that there are many methods, each having certain merits, of calculating capacity credits. However, it would seem that the procedure for calculating avoided capacity costs should be consistent whether such costs are beng calculated for a five-year period, a 10-year period, or a 15-year period. There is no apparent reason for using a peaking unit to develop avoided costs for the 5- and 10-year periods, and a base loaded plant for the 15-year period.

The various parties to this proceeding calculated avoided capacity costs for five- and 10-year periods based on a peaking unit, and there was little controversy regarding the cost of constructing a peaking plant. Yet where the various parties calculated avoided capacity costs for a 15-year period based on a base load unit, there was a great deal of controversy regarding (1) the cost of constructing a base load plant, (2) regarding whether or not such plant should be a nuclear plant, and (3) regarding the amount of fuel savings applicable to the plant.

Calculation of avoided capacity credits for 15-year periods based on peaking units would be consistent with similar calculations for 5- and 10-year periods, and it would place less arguments as to the accuracy of projections of future construction costs.

Carrasan witness Marcus presented calculations showing capacity credits for Duke for a 15-year period based on peaking units, which resulted in 1.76¢/kWh during the peak season and 1.06¢/kWh during the base season.These calculations utilize the same method adopted by Duke for the 5-year and 10-year capacity credits, and yield higher capacity credits for the 15-year period than those proposed by Duke. The Examiner is of the opinion that the 15-year capacity credits presented by witness Marcus based on a peaking plant should be adopted herein.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 10

Variable O&M

Duke includes 0.084¢/kWh total variable O&M (in 1983 dollars). By comparison, CP&L includes some variable O&M expenses in addition to the variable O&M expenses already in its PROMOD simulation. Such additional O&M alone is approximately 0.265¢/kWh (in 1983 dollars).

Therefore, CP&L includes at least three times as much variable O&M per kWh as Duke does in its calculation of energy credits. The Examiner is not persuaded that the variable O&M expenses of CP&L are three times as great as Duke's. There may be a discrepancy between CP&L and Duke as to which expenses should be classified as variable O&M expenses for purposes of calculating the energy credits. The record in this proceeding offers little to no help in this regard.

In order to resolve this problem in future proceedings, Duke should furnish for the record:

(a) The line items (by account number) which are included in the variable O&M expenses utilized for calculating energy credits;

(b) The line items (by account number) which are included in the fixed O&M expenses utilized for calculating capacity credits;

(c) Descriptions of each line item utilized for caclulating energy and capacity credits;

(d) The dollar amount for each line item;

(e) The kWh utilized for calculating the variable O&M expense per kWh; and

(f) The kW utilized for calculating the fixed O&M expense per kW.

General Plant

Duke did not add an allowance for general plant associated with avoided generating units in its calculation of capacity credits. CP&L adds a 2% allowance.

The Examiner is not persuaded that general plant necessarily varies in proportion to generating plant, or that avoiding or delaying construction of a generating unit will also avoid or delay construction of general plant. The record in this proceeding is of little or no help in this regard, and the subject should be explored further in future proceedings.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 11

Through its witness Freund, Duke proposed that Paragraphs No. 5 and 8 of its standard agreements be amended to include the language underlined below:

"5. Term. The term of this Agreement shall be _____ year(s), and thereafter until terminated. The Parties shall have the right of termination provided in the attached Rate Schedule, as from time to time amended; and in the absence of any such provision, either party may terminate this Agreement upon written notice to the other delivered at least thirty (30) months in advance of the termination of the original term or any then existing additional term. In addition, should the existing law or regulations be altered by court or Commission decision or should the Commission change or withdraw the availability of Schedule PP offered under this contract, this contract shall be null and void."

"8. In the event that this contract is terminated by either party prior to the expiration of the initial term as set forth in paragraph 5 hereof, except in the case where existing laws or regulations are altered by court or Commission decision or if the Commission changes or withdraws the availability of Schedule PP offered under this contract, the Supplier will reimburse the Company for the total energy credits received in excess of that which would have been received under variable rates and capacity credits received in excess of that which would have been received..."

In its proposed order Duke shows that it has appropriately sought to condition its obligations in the event American Electric Power Service Corp. v. Federal Energy Regulatory Commission, 668 F. 2d 880, 45 PUR 4th 364 is upheld by the U.S. Supreme Court. That decision rejected the full avoided cost standard and interconnection provisions of the FERC rules set forth in Order No. 69. This case is presently on appeal to the United States Supreme Court.

During the hearing and in its proposed order, the Public Staff, the Attorney General, and Carrasan challenged the propriety and validity of these provisions and, basically, contended that these provisions rendered the contract indefinite, uncertain, and illusory. The Public Staff contends that potential investors or lendors will not risk lending or investing upon the basis of such unstable contractual arrangements.

Witness Marcus, testifying for Carrasan, stated that this language adds so much uncertainty to the contract that it is doubtful projects can be financed. He states:

"This means that the 15-year contract has no more value to the financial community than a day-to-day contract. Small power producers cannot finance their projects if there is no certainty that Duke will even buy tomorrow at all or that it will honor its current contract commitments if a court or the Commission changes its mind. Duke is thus attempting to negate the Commission's decision that '... fixed, long-term levelized rates are appropriate complementary alternatives to short-term purchase rates which change over time.'"

In its proposed order, in an effort "to strike a balance between these competing interests," Duke proposed that the following language be substituted in Paragraphs 5 and 8 in lieu of the language originally proposed by Duke"

"If after this Agreement becomes effective any legislative or judicial body or governmental agency having jurisdiction requires any changes in this Agreement, or modifies any law or regulation that would affect any provision of this Agreement affecting the payment by the utility of avoided costs to the qualifying facility, the utility may require that the Agreement be amended to comply with the changes or modifications and that the changes or modifications be effective as of the date the changes are required or the date of the modifications in the law or regulations."

Duke explains that "[t]his language simply provides that upon a change in the law or regulations under which it contracts to purchase power from the qualifying facility, the utility has the right to amend the existing contract."

The Examiner concludes that the proposed amendments offered by Duke, including the compromise proposal, all cast such uncertainty on the stability of the standard contract that it will be difficult, if not impossible, for small power producers to obtain long-term financing. If contracts signed today can be amended to comply with future changes in law or regulation, these contracts are indeed little more than day-to-day agreements. Investors or lenders wishing to commit to a long-term project will have no assurance that there will be adequate "cash flow" to cover the investment or loan under Duke's proposed terms.

Current federal regulations, legislative policy, and the clearly stated policy of this Commission support the encouragement of small power production. These amendments are inconsistent with these policies and should not be approved.

IT IS, THEREFORE, ORDERED as follows:

1. That Duke Power Company shall offer through published tariffs and shall pay the avoided cost rates shown in Appendix A, page 5 of 5, hereto attached.

2. That Duke Power Company shall within 10 days of the effective date of this Order file for approval tariffs and standard contract terms and conditions as directed to be modified by the findings, conclusions, and rates allowed in this Order.

3. That Duke's proposed amendment to its standard contract is denied.

4. That Duke shall furnish for the record in future proceedings in this docket:

(a) The line items (by account number) which are included in the variable O&M expenses utilized for calculating energy credits;
(b) The line items (by account number) which are included in the fixed O&M expenses utilized for calculating capacity credits;
(c) Descriptions of each line item utilized for calculating energy and capacity credits;
(d) The dollar amount of each line item;

(e) The kWh utilized for calculating the variable O&M expenses per kWh; and
(f) The kW utilized for calculating the fixed O&M expenses per kWh.

ISSUED BY ORDER OF THE COMMISSION.
This the 1st day of April 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sharon Credle Miller, Deputy Clerk

APPENDIX A
SUMMARY OF AVOIDED COST ADJUSTMENTS
(Variable Rate - ¢/kWh)

	On-Peak Hours		
	Peak	Base	
Energy Credits	Month	Month	Off-Peak Hours
Duke's Existing Rate	2.2239	2.2239	1.6784
Duke's Proposed Rate	2.74	2.74	1.89
Adjustments:			
1. Nuclear performance	0.10	0.10	0.10
2. Working capital	0.09	0.09	0.06
3. Line losses	0.10	0.10	0.08
Total Energy Credits	3.03	3.03	2.13
Capacity Credits			
Duke's Existing Rate	1.11	0.66	0.00
Duke's Proposed Rate	1.22	0.74	0.00
Adjustments:			
1. Line losses	0.05	0.03	0.00
Total Capacity Credits	1.27	0.77	0.00

SUMMARY OF AVOIDED COST ADJUSTMENTS
(5-Year Rate - ¢/kWh)

	On-Peak Hours		
	Peak	Base	
Energy Credits	Month	Month	Off-Peak Hours
Duke's Existing Rate	2.87	2.87	2.15
Duke's Proposed Rate	2.96	2.96	2.01
Adjustments:			
1. Nuclear performance	0.10	0.10	0.10
2. Working capital	0.10	0.10	0.06
3. Line losses	0.11	0.11	0.08
Total Energy Credits	3.27	3.27	2.25
Capacity Credits			
Duke's Existing Rate	1.11	0.66	0.00
Duke's Proposed Rate	1.34	0.81	0.00
Adjustments:			
1. Line losses	0.05	0.03	0.00
Total Capacity Credits	1.39	0.84	0.00

SUMMARY OF AVOIDED COST ADJUSTMENTS
(10-Year Rate - ¢/kWh)

	On-Peak Hours		
Energy Credits	Peak Month	Base Month	Off-Peak Hours
Duke's Existing Rate	3.93	3.98	2.96
Duke's Proposed Rate	3.67	3.67	2.31
Adjustments:			
1. Nuclear performance	0.15	0.15	0.15
2. Working capital	0.12	0.12	0.08
3. Line losses	0.14	0.14	0.09
Total Energy Credits	4.08	4.08	2.63
Capacity Credits			
Duke's Existing Rate	1.11	0.66	0.00
Duke's Proposed Rate	1.55	0.94	0.00
Adjustments:			
1. Line losses	0.06	0.04	0.00
Total Capacity Credits	1.61*	0.98*	0.00

*Corrected by Errata Order dated April 14, 1983.

SUMMARY OF AVOIDED COST ADJUSTMENTS
(15-Year Rate - ¢/kWh)

	On-Peak Hours		
Energy Credits	Peak Month	Base Month	Off-Peak Hours
Duke's Existing Rate	5.02	5.02	3.78
Duke's Proposed Rate	4.28	4.28	2.56
Adjustments:			
1. Nuclear performance	0.20	0.20	0.20
2. Working capital	0.14	0.14	0.09
3. Line losses	0.17	0.17	0.10
Total Energy Credits	4.79	4.79	2.95
Capacity Credits			
Duke's Existing Rate	1.17	0.69	0.00
Duke's Proposed Rate	1.67	1.01	0.00
Adjustments:			
1. Peaking Unit	0.09	0.05	0.00
2. Line Losses	0.07	0.04	0.00
Total Capacity Credits	1.83	1.10	0.00

DUKE POWER COMPANY

	Standard Cogeneration and Small Power Producer Rates (Cents/kWh)			
	Variable Annual Rate	Fixed Long-Term Rates 5 yr.	10 yr.	15 yr.
Energy Credits				
Peak kWh	3.03*	3.27	4.08	4.79
Off-peak kWh	2.13*	2.25	2.63	2.95

*Annual rate energy credits will be updated every two years. In the interim, Fuel Cost Adjustment Factors will apply to the annual rate energy credits.

	Variable Annual Rate	5 yr.	10 yr.	15 yr.
Capacity Credits				
Peak kWh - peak months	1.27	1.39	1.39	1.83**
Peak kWh - off-peak months	0.77	0.84	0.84	1.10**

**Applies to contracts of 11 years or longer.

On-Peak Hours
The hours beginning 7:00 a.m. and ending 11:00 p.m. Monday-Friday.

Off-Peak Hours
All other hours.

Peak Months
The peak months are the billing months of June-September and December-March.
Off-peak months are the billing months of April, May, October, and November.

Note: Capacity credits shall be constant at the initial level for the life of a long-term contract. Capacity credits for annual contracts shall be at the initial level but shall be updated once every five years.

DOCKET NO. E-100, SUB 41

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Determination of Rates for Purchase and Sale of Electricity Between Electric Utilities and Qualifying Cogenerators or Small Power Producers) RECOMMENDED ORDER RELATING TO NANTAHALA POWER AND LIGHT COMPANY

HEARD IN: The Commission Hearing Room, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina, on December 14-17, 1982

BEFORE: Robert Gruber, Hearing Examiner

APPEARANCES:

For the Respondents:

John Bode, Bode, Bode & Call, Attorneys at Law, P.O. Box 391, Raleigh, North Carolina 27602
For: Carolina Power & Light Company

Robert W. Kaylor, Associate General Counsel, Carolina Power & Light Company, P.O. Box 1551, Raleigh, North Carolina 27602
For: Carolina Power & Light Company

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For: Duke Power Company

Edgar M. Roach, Jr., Hunton & Williams, P.O. Box 109, Raleigh, North Carolina 27602
For: Virginia Electric and Power Company

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For: Virginia Electric and Power Company

For the Intervenors:

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For: Carrasan Power Company and California Hydro-Systems, Inc.

Wells Eddleman, 718-A Iredell Street, Durham, North Carolina 27705
For: Himself

Robert H. Bennink, Jr., Assistant Attorney General, North Carolina Department of Justice, P.O. Box 629, Raleigh, North Carolina 27511
For: The Using and Consuming Public

G. Clark Crampton, Staff Attorney, Legal Division, Public Staff - North Carolina Utilities Commission, P.O. Box 991, Raleigh, North Carolina 27602
For: The Using and Consuming Public

ROBERT P. GRUBER, EXAMINER: The proceedings to which this Order relates were had for the purpose of determining the rates, terms, and conditions upon which Duke and the other regulated electric utility parties will be required to purchase electricity from certain "qualifying" generating facilities in the manner required and contemplated by Section 210 of the Public Utilities Regulatory Policies Act (PURPA).

The instant proceedings are only the second such proceedings held by this Commission since Section 210 of PURPA was enacted by the Congress. The first such proceedings consisted of hearings which were held in the fall and winter

of 1980. Various Orders resulted therefrom (and from collaterally related hearings held with respect to wheeling). Those earlier Orders were issued during 1981, and are recapped hereinafter.

Section 210(a) of PURPA required the Federal Energy Regulatory Commission (FERC), after hearing and consultation with representatives of federal and state agencies, to prescribe and revise periodically rules which require electric utilities to sell (on a nondiscriminatory basis) electric energy to, and, more significantly, to purchase electric energy from, certain generating facilities which meet certain "qualifying" criteria. Such generating facilities fall into two broad categories. The first type of utilities required to purchase electricity under the federal law are those defined as "qualifying cogeneration" facilities. Cogeneration facilities are generally those which simultaneously produce two forms of useful energy, such as electric power and steam. An example would be a furniture manufacturing plant which not only uses process steam in its manufacturing activities, but also uses the same steam in order to generate electricity. The dual use of such energy has the obvious potential of producing substantial and significant savings in the cost of producing electricity, and also the potential for reducing the cost of electricity to ratepayers if such savings can be passed on to the ratepayers.

The second general type of generating facility from which Duke and other regulated electric utilities are required to purchase the electricity generated by it are "qualifying small power production" facilities. Such, by definition in the pertinent statutes and FERC regulations, include electric generating facilities which use waste, biomass, or "renewable resources" for energy. Such "renewable resources" are specifically defined to include wind, solar, and water energy. Such energy sources also have the obvious potential of resulting in significantly cheaper electricity. For example, the sun's rays or flowing water have no cost, as contrasted with the generally increasing costs of fossil fuels or nuclear fuel typically used by regulated utilities in their generating plants.

Such generating facilities are qualifying facilities under Section 201 of PURPA if they meet the requirements of Subchapter K, Part 292, Subpart B of Chapter I, Title 18, Code of Federal Regulations. Reference to such regulations points up that the qualifying criteria and the procedures to obtain "qualifying" status for a given generating facility are relatively simple, clear cut, and easy to apply. That aspect of this matter is not here in issue. It is merely mentioned in passing as helpful background.

As permitted by the applicable provisions of federal law (PURPA), the Federal Energy Regulatory Commission in its wisdom, by regulation, has delegated to state regulatory authorities, such as this Commission, the power and duty to implement, regulate, and oversee the implementation of Section 210 of PURPA relating to purchases and sales of electricity between and among "qualifying" electric generating facilities within the jurisdiction of such state regulatory authorities, on the one hand, and the electric utilities regulated by each such state regulatory authority, on the other hand. That delegation took place soon after the enactment of PURPA by the Congress.

Specifically, the Federal Energy Regulatory Commission (FERC), pursuant to Title II of the Public Utility Regulatory Policies Act of 1978 (PURPA), was empowered to promulgate rules and regulations to implement the act provisions,

including Section 210. The FERC promulgated such rules and regulations in the form of the provisions of Subchapter K, Part 292, Subparts A, C, D, and F of Chapter I, Title 18, Code of Federal Regulations. Those regulations were amended on February 19, 1980, effective on March 20, 1980. Those regulations, as thus amended, require each regulated electric utility to collect and make available to its state regulatory authority on a biannual basis data from which each regulated utility's avoided costs may be derived. Such avoided costs are to be essentially the basis for such state regulatory authority to establish the rates to be paid to qualifying facilities by such regulated electric utilities. The FERC regulations also require generally, inter alia, each regulated electric utility to purchase electric energy from qualifying facilities; to sell electric energy on a nondiscriminatory basis to qualifying facilities (i.e., on the same basis such would be sold to any other customer which was not a generator of electricity); to interconnect with qualifying facilities; and to supply supplementary, back-up, maintenance, and interruptible power to qualifying facilities on a nondiscriminatory standard basis.

It should be further noted that this Commission has a separate duty under state law which parallels in some respects its duty to set rates for certain types of purchase transactions which are also covered by PURPA. The North Carolina General Assembly enacted in 1979 what has now been codified as North Carolina G.S. 62-156. Also certain definitions used in that section were enacted and are now codified as North Carolina G.S. 62-3(27a). That legislation provides a separate state law basis, as is specifically permitted by the FERC regulations promulgated with respect to PURPA Section 210, for this Commission to regulate and biannually review and revise the rates, and terms and conditions upon which the regulated electric utilities purchase electricity from certain types of nonpublic utility generating facilities. Essentially, such generating facilities are hydroelectric generating facilities having a generating capacity of under 80 megawatts. The Commission is to "encourage" the development of such.

With the foregoing overview, it is now appropriate to briefly examine and recap the proceedings which have been heretofore had before this Commission which relate to its powers and duties under the FERC delegation of powers and duties to it, and under the delegation by the North Carolina General Assembly pursuant to G.S. 62-156, in regulating the types of transactions here involved.

This Commission's first action with respect to implementing Section 210 of PURPA was its Order dated June 3, 1980. The Commission there scheduled a two-phase public hearing. The Phase I hearing was held on July 22, 1980, for the purpose of defining issues and procedures involved in this Commission's first attempt to deal with its duties in regulating the types of transactions involved. By Order dated September 19, 1980, the Commission directed the electric utilities to file direct testimony on or before December 15, 1980. The Phase II Public Hearing was held on January 6, 7, 8, and 26, 1981, for the purpose of resolving the issues identified in the Phase I hearings. The nature and extent of those Phase I and II hearings are set out in this Commission Order issued September 21, 1981, at pp. 5-9, incorporated herein by reference.

After the conclusion of those Phase II hearings, on March 10, 1981, the Hearing Examiner issued a Recommended Order setting standard rates and terms

and conditions for the purchase and sale of electricity between utilities and qualifying cogenerators and small power producers. Exceptions to that Recommended Order were filed by Duke and Vepco. At the request of those two utilities, the Commission granted reconsideration, and oral argument was held in June 1981. This procedural history and the positions of Duke and Vepco at that time are set out in detail at pages 12-16 of this Commission Order issued September 21, 1981, in this docket, also incorporated herein by reference.

A second Recommended Order was issued on September 21, 1981, which superseded the earlier March 10, 1981, Recommended Order. No exceptions were filed with respect to that second Recommended Order, and it became final in October 1981. No appeals were taken or perfected with respect to it. That Order, inter alia, specified the avoided cost rates to be paid to qualifying facilities and approved for each regulated utility proposed terms and conditions of service to, and purchases from, such facilities.

Some mention should be made at this point of the collateral matter of wheeling. On November 17, 1981, a hearing was held to consider the cost and necessity of requiring utilities to provide wheeling services for qualifying facilities. The Hearing Examiner issued a Recommended Order relating to the wheeling matters which were there at issue on January 11, 1982. That Order, thru oversight, did not become final until December 2, 1982, its finalization having been postponed at the request of one or more of the involved utilities.

The hearings here involved ultimately arise out of this Commission Order of August 27, 1982, wherein the Commission ordered a public hearing to establish avoided cost rates and other related matters as required by the FERC regulations earlier cited. The Commission's August 27, 1982, Order generally required the regulated electric utilities in this proceeding to file with the Commission: (1) a set of its proposed "standard" avoided cost rates for purchases from qualifying facilities and to do so in a format similar to that which had been utilized by the Commission in the Appendices to the Commission Order of September 21, 1981, referred to earlier in this Order; (2) a description and information regarding the methodology and data used to calculate its proposed "standard" avoided cost rates; and (3) any proposed changes to the currently approved standard form contracts between qualifying facilities and the utility.

By Order dated October 19, 1982, the Commission rescheduled the public hearing in this proceeding for December 14, 1982.

At various times prior to the December 1982 proceedings here involved, various parties became intervenors. Those intervenors, fully recognized by the Commission to be such, are: the Public Staff, the Attorney General of North Carolina, Carrasan Power Company and California Hydro Systems, Inc., and Wells Eddleman. By ruling of the Examiner from the Bench, Mr. Eddleman's intervention was limited to the Duke Power case.

The hearing in the instant matter was held in the Commission Hearing Room in the Dobbs Building, Raleigh, North Carolina, on December 14, 15, 16, and 17, 1982. The following public witnesses appeared and testified: Tom Dorais, Steven Berkowitz, Representative John Jordan, Charles Mierek, Jane Sharp, Daniel F. Reed, and Bill Hohlman. Nantahala presented the testimony of its officer, Ed Tucker. Carolina Power & Light Company presented the testimony of its employees Dr. James N. Kimball, David R. Hostetler, and Robert W. Carney.

Duke Power Company presented the direct testimony of its employees John N. Freund and Joe Price. Duke presented also the rebuttal testimony of its Vice President Donald H. Denton, Jr.

Carrasan presented initial and additional direct testimony of its expert witness William Marcus.

The Public Staff - North Carolina Utilities Commission presented the direct testimony of its expert witness Dr. Robert Weiss.

Wells Eddleman testified on behalf of himself, but consideration of his testimony was limited to the Duke Power case.

Separate Orders are today being issued for Duke, CP&L, Vepco, and Nantahala since the issues and the findings and conclusions vary between the companies.

Based upon the evidence adduced at the subject December 1982 hearings and the entire record in this matter, the Examiner now makes the following:

FINDINGS OF FACT

1. Nantahala is a public utility corporation organized and existing under the terms of the State of North Carolina and is subject to the jurisdiction of this Commission including its jurisdiction with respect to all matters and issues here involved.

2. On November 17, 1982, Nantahala filed for approval "Schedule CG, Cogeneration" which is the schedule previously approved by the Commission updated for the latest TVR rate increase.

CONCLUSIONS

No other party offered any testimony or argument relating to Nantahala's proposed rate. The Examiner therefore concludes that the proposed cogeneration rate "Schedule CG" should be approved as filed subject to being updated for purchased power adjustments.

IT IS THEREFORE ORDERED that Nantahala Schedule CG is approved as filed.

ISSUED BY ORDER OF THE COMMISSION.
This the 1st day of April 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sharon Credle Miller, Deputy Clerk

DOCKET NO. E-100, SUB 41

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Determination of Rates for Purchase and Sale of Electricity Between Electric Utilities and Qualifying Cogenerators or Small Power Producers) RECOMMENDED ORDER RELATING TO VIRGINIA ELECTRIC AND POWER COMPANY

HEARD IN: The Commission Hearing Room, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina, on December 14-17, 1982

BEFORE: Robert Gruber, Hearing Examiner

APPEARANCES:

For the Respondents:

John Bode, Bode, Bode & Call, Attorneys at Law, P.O. Box 391, Raleigh, North Carolina 27602
For: Carolina Power & Light Company

Robert W. Kaylor, Associate General Counsel, Carolina Power & Light Company, P.O. Box 1551, Raleigh, North Carolina 27602
For: Carolina Power & Light Company

Steve C. Griffith, Jr., Senior Vice President and General Counsel, and W. Edward Poe, Jr., Assistant General Counsel, Duke Power Company, P.O. Box 33189, Charlotte, North Carolina 28242
For: Duke Power Company

Edgar M. Roach, Jr., Hunton & Williams, P.O. Box 109, Raleigh, North Carolina 27602
For: Virginia Electric and Power Company

Douglas M. Palais, Hunton & Williams, P.O. Box 1535, Richmond, Virginia 23212
For: Virginia Electric and Power Company

For the Intervenors:

William R. White and Tony C. Dalton, White and Dalton, Attorneys at Law, P.O. Box 1589, Brevard, North Carolina 28712
For: Carrasan Power Company and California Hydro-Systems, Inc.

Wells Eddleman, 718-A Iredell Street, Durham, North Carolina 27705
For: Himself

Robert H. Bennink, Jr., Assistant Attorney General, North Carolina Department of Justice, P.O. Box 629, Raleigh, North Carolina 27511
For: The Using and Consuming Public

G. Clark Crampton, Staff Attorney, Legal Division, Public Staff - North Carolina Utilities Commission, P.O. Box 991, Raleigh, North Carolina 27602
For: The Using and Consuming Public

ROBERT P. GRUBER, EXAMINER: The proceedings to which this Order relates were had for the purpose of determining the rates, terms, and conditions upon which Duke and the other regulated electric utility parties will be required to purchase electricity from certain "qualifying" generating facilities in the manner required and contemplated by Section 210 of the Public Utilities Regulatory Policies Act (PURPA).

The instant proceedings are only the second such proceedings held by this Commission since Section 210 of PURPA was enacted by the Congress. The first such proceedings consisted of hearings which were held in the fall and winter of 1980. Various Orders resulted therefrom (and from collaterally related hearings held with respect to wheeling). Those earlier Orders were issued during 1981, and are recapped hereinafter.

Section 210(a) of PURPA required the Federal Energy Regulatory Commission (FERC), after hearing and consultation with representatives of federal and state agencies, to prescribe and revise periodically rules which require electric utilities to sell (on a nondiscriminatory basis) electric energy to, and, more significantly, to purchase electric energy from, certain generating facilities which meet certain "qualifying" criteria. Such generating facilities fall into two broad categories. The first type of utilities required to purchase electricity under the federal law are those defined as "qualifying cogeneration" facilities. Cogeneration facilities are generally those which simultaneously produce two forms of useful energy, such as electric power and steam. An example would be a furniture manufacturing plant which not only uses process steam in its manufacturing activities, but also uses the same steam in order to generate electricity. The dual use of such energy has the obvious potential of producing substantial and significant savings in the cost of producing electricity, and also the potential for reducing the cost of electricity to ratepayers if such savings can be passed on to the ratepayers.

The second general type of generating facility from which Duke and other regulated electric utilities are required to purchase the electricity generated by it are "qualifying small power production" facilities. Such, by definition in the pertinent statutes and FERC regulations, include electric generating facilities which use waste, biomass, or "renewable resources" for energy. Such "renewable resources" are specifically defined to include <u>wind</u>, <u>solar</u>, <u>and</u> <u>water</u> energy. Such energy sources also have the obvious potential of resulting in significantly cheaper electricity. For example, the sun's rays or flowing water have no cost, as contrasted with the generally increasing costs of fossil fuels or nuclear fuel typically used by regulated utilities in their generating plants.

Such generating facilities are qualifying facilities under Section 201 of PURPA if they meet the requirements of Subchapter K, Part 292, Subpart B of Chapter I, Title 18, Code of Federal Regulations. Reference to such regulations points up that the qualifying criteria and the procedures to obtain "qualifying" status for a given generating facility are relatively simple, clear cut, and easy to apply. That aspect of this matter is not here in issue. It is merely mentioned in passing as helpful background.

As permitted by the applicable provisions of federal law (PURPA), the Federal Energy Regulatory Commission in its wisdom, by regulation, has delegated to state regulatory authorities, such as this Commission, the power and duty to implement, regulate, and oversee the implementation of Section 210 of PURPA relating to purchases and sales of electricity between and among "qualifying" electric generating facilities within the jurisdiction of such state regulatory authorities, on the one hand, and the electric utilities regulated by each such state regulatory authority, on the other hand. That delegation took place soon after the enactment of PURPA by the Congress.

Specifically, the Federal Energy Regulatory Commission (FERC), pursuant to Title II of the Public Utility Regulatory Policies Act of 1978 (PURPA), was empowered to promulgate rules and regulations to implement the act provisions, including Section 210. The FERC promulgated such rules and regulations in the form of the provisions of Subchapter K, Part 292, Subparts A, C, D, and F of Chapter I, Title 18, Code of Federal Regulations. Those regulations were amended on February 19, 1980, effective on March 20, 1980. Those regulations, as thus amended, require each regulated electric utility to collect and make available to its state regulatory authority on a biannual basis data from which each regulated utility's avoided costs may be derived. Such avoided costs are to be essentially the basis for such state regulatory authority to establish the rates to be paid to qualifying facilities by such regulated electric utilities. The FERC regulations also require generally, inter alia, each regulated electric utility to purchase electric energy from qualifying facilities; to sell electric energy on a nondiscriminatory basis to qualifying facilities (i.e., on the same basis such would be sold to any other customer which was not a generator of electricity); to interconnect with qualifying facilities; and to supply supplementary, back-up, maintenance, and interruptible power to qualifying facilities on a nondiscriminatory standard basis.

It should be further noted that this Commission has a separate duty under state law which parallels in some respects its duty to set rates for certain types of purchase transactions which are also covered by PURPA. The North Carolina General Assembly enacted in 1979 what has now been codified as North Carolina G.S. 62-156. Also certain definitions used in that section were enacted and are now codified as North Carolina G.S. 62-3(27a). That legislation provides a separate state law basis, as is specifically permitted by the FERC regulations promulgated with respect to PURPA Section 210, for this Commission to regulate and biannually review and revise the rates, and terms and conditions upon which the regulated electric utilities purchase electricity from certain types of nonpublic utility generating facilities. Essentially, such generating facilities are hydroelectric generating facilities having a generating capacity of under 80 megawatts. The Commission is to "encourage" the development of such.

With the foregoing overview, it is now appropriate to briefly examine and recap the proceedings which have been heretofore had before this Commission which relate to its powers and duties under the FERC delegation of powers and duties to it, and under the delegation by the North Carolina General Assembly pursuant to G.S. 62-156, in regulating the types of transactions here involved.

This Commission's first action with respect to implementing Section 210 of PURPA was its Order dated June 3, 1980. The Commission there scheduled a two-phase public hearing. The Phase I hearing was held on July 22, 1980, for the purpose of defining issues and procedures involved in this Commission's first attempt to deal with its duties in regulating the types of transactions involved. By Order dated September 19, 1980, the Commission directed the electric utilities to file direct testimony on or before December 15, 1980. The Phase II Public Hearing was held on January 6, 7, 8, and 26, 1981, for the purpose of resolving the issues identified in the Phase I hearings. The nature and extent of those Phase I and II hearings are set out in this Commission Order issued September 21, 1981, at pp. 5-9, incorporated herein by reference.

After the conclusion of those Phase II hearings, on March 10, 1981, the Hearing Examiner issued a Recommended Order setting standard rates and terms and conditions for the purchase and sale of electricity between utilities and qualifying cogenerators and small power producers. Exceptions to that Recommended Order were filed by Duke and Vepco. At the request of those two utilities, the Commission granted reconsideration, and oral argument was held in June 1981. This procedural history and the positions of Duke and Vepco at that time are set out in detail at pages 12-16 of this Commission Order issued September 21, 1981, in this docket, also incorporated herein by reference.

A second Recommended Order was issued on September 21, 1981, which superseded the earlier March 10, 1981, Recommended Order. No exceptions were filed with respect to that second Recommended Order, and it became final in October 1981. No appeals were taken or perfected with respect to it. That Order, inter alia, specified the avoided cost rates to be paid to qualifying facilities and approved for each regulated utility proposed terms and conditions of service to, and purchases from, such facilities.

Some mention should be made at this point of the collateral matter of wheeling. On November 17, 1981, a hearing was held to consider the cost and necessity of requiring utilities to provide wheeling services for qualifying facilities. The Hearing Examiner issued a Recommended Order relating to the wheeling matters which were there at issue on January 11, 1982. That Order, thru oversight, did not become final until December 2, 1982, its finalization having been postponed at the request of one or more of the involved utilities.

The hearings here involved ultimately arise out of this Commission Order of August 27, 1982, wherein the Commission ordered a public hearing to establish avoided cost rates and other related matters as required by the FERC regulations earlier cited. The Commission's August 27, 1982, Order generally required the regulated electric utilities in this proceeding to file with the Commission: (1) a set of its proposed "standard" avoided cost rates for purchases from qualifying facilities and to do so in a format similar to that which had been utilized by the Commission in the Appendices to the Commission Order of September 21, 1981, referred to earlier in this Order; (2) a description and information regarding the methodology and data used to calculate its proposed "standard" avoided cost rates; and (3) any proposed changes to the currently approved standard form contracts between qualifying facilities and the utility.

By Order dated October 19, 1982, the Commission rescheduled the public hearing in this proceeding for December 14, 1982.

At various times prior to the December 1982 proceedings here involved, various parties became intervenors. Those intervenors, fully recognized by the Commission to be such, are: the Public Staff, the Attorney General of North Carolina, Carrasan Power Company and California Hydro Systems, Inc., and Wells Eddleman. By ruling of the Examiner from the Bench, Mr. Eddleman's intervention was limited to the Duke Power case.

The hearing in the instant matter was held in the Commission Hearing Room in the Dobbs Building, Raleigh, North Carolina, on December 14, 15, 16, and 17, 1982. The following public witnesses appeared and testified: Tom Dorais, Steven Berkowitz, Representative John Jordan, Charles Mierek, Jane Sharp, Daniel F. Reed, and Bill Hohlman. Nantahala presented the testimony of its

officer, Ed Tucker. Carolina Power & Light Company presented the testimony of its employees Dr. James N. Kimball, David R. Hostetler, and Robert W. Carney.

Duke Power Company presented the direct testimony of its employees John N. Freund and Joe Price. Duke presented also the rebuttal testimony of its Vice President Donald H. Denton, Jr.

Carrasan presented initial and additional direct testimony of its expert witness William Marcus.

The Public Staff - North Carolina Utilities Commission presented the direct testimony of its expert witness Dr. Robert Weiss.

Wells Eddleman testified on behalf of himself, but consideration of his testimony was limited to the Duke Power case.

Separate Orders are today being issued for Duke, CP&L, Vepco, and Nantahala since the issues and the findings and conclusions vary between the companies.

Based upon the evidence adduced at the subject December 1982 hearings and the entire record in this matter, the Examiner now makes the following

FINDINGS OF FACT

1. Virginia Electric and Power Company is a public utility corporation organized and existing under the laws of the State of Virginia and authorized to transact business in the State of North Carolina and is subject to the jurisdiction of this Commission including its jurisdiction with respect to all matters and issues here involved.

2. Vepco's projections of avoided energy costs and avoided capacity costs are reasonable and accurate.

3. The energy and capacity rates contained in Vepco's proposed Schedule 19 reflect Vepco's avoided costs and are appropriate to encourage the development of cogeneration and small power production in Vepco's North Carolina service territory. Schedule 19 is approved as filed.

4. Vepco's long-term levelized five-, 10-, and 15-year rates, which are limited in applicability to small scale hydroelectric facilities as defined in G.S. 62-156, are just and reasonable.

5. Vepco should continue to study the possible implementation in the future of a method of payment for energy supplied by qualifying facilities based on <u>actual</u> avoided costs.

6. Vepco's standard form contracts for qualifying facilities are reasonable and are approved.

7. The waiver of payment of capacity credits for facilities on which construction began before November 9, 1978, is apropriate unless the operator of such facility demonstrates the financial need for the payment of capacity credits to continue the operation of such facility and to continue the benefits from such facility over the foreseeable future.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 1

The evidence supporting this finding of fact is contained in prior Commission Orders in this docket of which the Commission takes notice. This finding is essentially informational, procedural, and jurisdictional in nature and the matters which it involves are essentially uncontested.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 2

The evidence for this finding of fact can be found in the testimony of Dr. James N. Kimball and Vepco Revised Exhibit DRH-1, Schedule 3. Dr. Kimball testified as to both the total marginal costs of energy and capacity and the components of such costs. Dr. Kimball's marginal energy costs were derived by use of a production cost computer model known as PROMOD. Using the results of PROMOD, Dr. Kimball calculated an avoided energy cost of 3.88¢/kWh off-peak. These marginal energy costs are lower than those previously submitted by Vepco in this proceeding on December 15, 1980, due to changes in forecasted load levels, planned unit conversions from oil to coal, expected unit capacity factors, expected levels of cogeneration, and forecasted fuel prices.

In addition, Dr. Kimball calculated levelized marginal energy costs to be used for small-scale hydroelectric facilities pursuant to G.S. 62-156. Dr. Kimball's five-year costs are 5.23¢/kWh on-peak and 3.53¢/kWh off-peak. For 10 years, the costs are 6.16¢/kWh on-peak and 4.38¢/kWh off-peak. On January 14, 1983, pursuant to a request by the Public Staff, Vepco filed a late-filed exhibit (Vepco Revised Exhibit DRH-1, Schedule 3) that included 15-year levelized energy and capacity rates for hydroelectric facilities. The 15-year energy rates for small-scale hydroelectic facilities are 7.10¢/kWh on-peak and 5.15¢/kWh off-peak. The 15-year capacity rate is 2.511¢/kWh on-peak.

Dr. Kimball's calculation of avoided capacity costs included the marginal cost of generation and excluded costs associated with transmission and distribution. In accordance with the methodology previously approved by the Commission in this proceeding, Dr. Kimball calculated an annual avoided capacity cost of $40.21 per kilowatt for contracts for less than five years. For contracts five years or longer, Dr. Kimball calculated avoided capacity costs at the annual rate of $62.74 per kilowatt. Dr. Kimball's avoided capacity calculations do not take into account Vepco's recent cancellation of the construction of North Anna Unit 3. Dr. Kimball testified that the Company intends to rerun its analyses as soon as practicable in order to determine any potential changes in capacity and or energy costs as a result of the cancellation. There has been no showing that the capacity or energy costs calculated by Dr. Kimball will change significantly because of the cancellation of North Anna Unit 3. The Examiner accepts the costs and methodology used by Dr. Kimball, but asks that Vepco in the next phase of this proceeding take into account the effects, if any, on avoided costs resulting from the cancellation of North Anna Unit 3.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 3

The evidence for this finding of fact can be found in the testimony of David R. Hostetler, Manager - Rates of Vepco, and the Final Order of January 11, 1983, of the State Corporation Commission of Virginia in Case No. PUE800102, of which this Commission takes judicial notice. Witness Hostetler

testified as to the applicability of Schedule 19 - Power Purchases from Cogeneration and Small Power Production Qualifying Facilities. This schedule, which is attached as Appendix A, is hereby approved by the Commission. Schedule 19 is applicable to all "new" qualifying facilities and to "old" qualifying facilities with a design capacity of 100 kilowatts or less. Under this tariff Vepco proposes to pay variable annual energy rates and, where appropriate, capacity payments to qualifying facilities.

The rates contained in Schedule 19 are based on the marginal costs calculated by Dr. Kimball. Witness Hostetler testified that Vepco proposes to evaluate the energy payments in Schedule 19 each year in conjunction with Vepco's annual fuel factor proceeding before the State Corporation Commission of Virginia and update those payments accordingly. In addition, witness Hostetler testified that Vepco proposes to update capacity payments every two years in conjunction with the revision of those payments in Vepco's Virginia service territory.

The Commission concludes in its Order of September 21, 1981, that:

> "The standard rates paid by Vepco to qualifying facilities [in North Carolina] should be annual rates only and should be reasonably identical to those filed by the Company in Virginia."

Vepco's Schedule 19 filed in Virginia was approved by the State Corporation Commission of Virginia on January 11, 1983. The substantive provisions of Schedule 19 filed herein are identical to those contained in Schedule 19 as approved in Virginia. The rates for Schedule 19 submitted in this proceeding are based on more recent avoided cost projections utilizing the same methodology as approved by the Virginia Commission. The Examiner finds it reasonable that Schedule 19 as filed herein be approved.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 4

The evidence for this finding of fact is found in the testimony of Dr. Kimball and witness Hostetler and in the Commission Order of September 21, 1981. Dr. Kimball and witness Hostetler testified concerning Vepco's lack of 15-year avoided cost data and the potential problems associated with any long-term projections. Witness Hostetler presented in his direct testimony and exhibits levelized five- and 10-year rates applicable to small-scale hydroelectric facilities pursuant to G.S. 62-156. Witness Hostetler subsequently revised his exhibit to include 15-year levelized rates that were extrapolated from his five- and 10-year levelized rates.

Witness Hostetler testified that due to the large quantities of cogeneration and small power production in Vepco's North Carolina service territory, long-term levelized rates for other than hydroelectric facilities would have a severely detrimental impact on the Company's North Carolina ratepayers. Due to these circumstances, the Commission declined to set such rates for Vepco in its Order of September 21, 1981. In its Order of September 21, 1981, the Commission stated:

> "The Commission concludes that long-term standard rate options are not appropriate for Nantahala or Vepco at this time...Vepco has a small service area in North Carolina and the additional costs of long-term credits above short-term contract could as much as double

> the current rates. The Commission does not preclude, however, the negotiation of limited long-term rates by these utilities if such contracts are not detrimental to the welfare of their North Carolina consumers."

The record in the current phase of this proceeding reveals that the relevant circumstances for Vepco have not changed since September 21, 1981. Consequently, the Commission continues to decline to set long-term levelized rates for Vepco, except with respect to small-scale hydroelectric qualifying facilities. G.S.62-156 provides that the Commission should encourage long-term contracts for small-scale hydroelectric facilities. The Examiner approves the five-, 10-, and 15-year long-term rates offered by witness Hostetler to be applicable for small-scale hydroelectric facilities only. These rates are set forth in Schedule 19H, attached hereto as Appendix B. Schedule 19H is hereby approved.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 5

The evidence for this finding is found in the testimony of Dr. Kimball and witness Hostetler, in FERC Order No. 69 and in the Commission's prior Orders in this docket. The Commission, in its September 21, 1981, Order stated:

> ".... It was suggested by Dr. Weiss, the witness for the Public Staff, that qualifying facilities have the option of being paid according to actual avoided energy costs...[This approach] would provide a means of giving qualifying facilities the highest payments during the times when the costs of the utilities would be highest... The Commission concludes, however, that the demand for such a rate has not been shown to be great enough to require the setting up of its costly administrative procedure at this time... However, the Commission also concludes that the utilities and qualifying facilities should be allowed to contract for an after-the-fact rate based on the actual costs avoided as a result of the qualifying facility operation. In that case, however, such contracting qualifying facility should pay the costs of administering the data gathering process which would determine such rates."

Dr. Kimball testified that Vepco is currently studying the possibility of developing a computer program that will record on an hourly basis the actual cost of marginal energy for the Vepco system. Witness Hostetler testified that after the program has been reviewed and if it is found to be accurate, Vepco plans to ask the Commission to allow it to pay qualifying facilities for current energy costs on the basis of that approach. Payment based on actual avoided costs is a method approved by the FERC in Order No. 69. The Examiner encourages Vepco to continue to investigate suitable methodologies to allow payments for energy based on actual avoided costs. However, the Commission cannot rule on the validity of such a methodology until a detailed proposal is made by Vepco.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 6

The evidence supporting this finding is found in the testimony of Robert W. Carney, Supervisor - Cogeneration and Support Services for Vepco. Witness Carney testified regarding Vepco's activities in negotiating with potential qualifying cogeneration and small power production facilities. Witness Carney

testified that Vepco has entered into agreements with cogeneration facilities in Vepco's Virginia service territory with a combined generation of approximately 65 megawatts, with two hydroelectric facilities with a combined capacity of 700 killowatts and with a two-kilowatt wind generator in North Carolina. Witnes Carney testified that this new capacity is in addition to some 450 megawatts (approximately 150 megawatts of which is in North Carolina) of customer-owned generation that has operated in parallel with the Vepco system for several years. Vepco expects two additional qualifying facilities with a capacity of 24 megawatts to come into service during the first quarter of 1983. Finally, witness Carney testified that Vepco is in the process of ongoing negotiations with several other potential qualifying facilities with a total capacity of approximately 80 megawatts.

Mr. Carney testified that Vepco has changed its standard form power purchase agreements to be used for qualifying facilities in order to reflect its experience in negotiating with such facilities in the last two years. Witness Carney presented two different contractual documents to be used for qualifying facilities. One contract (Vepco Exhibit RWC-1, Schedule 1) applies to qualifying facilities that do not exceed 1,000 kilowatts (1 megawatt) in design capacity. The other contract (Vepco Exhibit RWC-1, Schedule 2) is more detailed and is applicable to facilities with a design capacity in excess of 1,000 kilowatts. Witness Carney testified that the larger qualifying facilities desired the lengthier, more detailed contract form in order to accommodate the more complicated interconnection and other problems associated with purchases and sales to and from these facilities and Vepco. The Commission finds the standard form contracts proposed by Vepco to be acceptable. The Commission recognizes that actual contractual agreements may vary in some respects, due to individual needs and characteristics of qualifying facilities.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 7

The evidence for this finding can be found in the testimony of witness Hostetler, FERC Order No. 69, and the Commission's September 21, 1981, Order in this docket. In his testimony, witness Hostetler noted that the Commission, in its Order of September 21, 1981, concluded that standard rates should apply only to existing qualifying facilities with a design capacity of 100 kilowatts or less and to all new qualifying facilities. The Commission, consistent with FERC Order No. 69, concluded that old qualifying facilities are not entitled to capacity payments unless they demonstrate a need for such payments in order to remain viable.

The Examiner concludes that "old" qualifying facilities are not entitled to capacity payments in the absence of an affirmative showing of need. There is no evidence in the record to support a departure by the Commission from this finding. The Commission will accordingly continue to differentiate between "new" and "old" capacity as described in its Order of September 21, 1981.

IT IS, THEREFORE, ORDERED as follows:

1. Vepco shall offer through proposed Schedule 19 the avoided cost rates proposed by it in this proceeding. Schedule 19 is hereby approved.

2. Vepco's Schedule 19H, which contains five-, 10-, and 15-year levelized rates, and which is applicable only to small scale hydroelectric facilities pursuant to G.S. 62-156, is hereby approved.

3. Vepco's standard form power purchase agreements were uncontested and are hereby approved.

ISSUED BY ORDER OF THE COMMISSION.
This the 1st day of April 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sharon Credle Miller, Deputy Clerk

DOCKET NO. E-100, SUB 41

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Determination of Rates for Purchase and Sale of Electricity Between Electric Utilities and Qualifying Cogenerators or Small Power Producers and Rulemaking Concerning Conditions and Requirements for Such Services) ORDER OVERRULING EXCEPTIONS, AFFIRMING RECOMMENDED ORDERS, AND AMENDING ORDER RELATING TO DUKE POWER COMPANY

BY THE COMMISSION: On April 1, 1983, Hearing Examiner Robert P. Gruber issued separate Recommended Orders in this docket relating to Carolina Power & Light Company, Duke Power Company, Virginia Electric and Power Company, and Nantahala Power and Light Company.

On April 15, 1983, Charles B. Mierek filed exceptions to the Recommended Orders relating to Duke Power Company and Carolina Power & Light Company.

On April 18, 1983, Wells Eddleman filed exceptions to the four Recommended Orders issued April 1, 1983, in this docket.

On April 19, 1983, Carolina Power & Light Company filed responses to the exceptions to the Recommended Order relating to Carolina Power & Light Company which were filed on behalf of Mr. Mierek and Mr. Eddleman. With respect to Mr. Mierek, Carolina Power & Light alleged that Mr. Mierek was not a party to this proceeding and has no standing to file exceptions to the Recommended Order. With respect to Mr. Eddleman, Carolina Power & Light Company stated that Mr. Eddleman was not an intervenor or party with respect to Carolina Power & Light Company and has no standing to file exceptions to the Recommended Order relating to Carolina Power & Light Company. Carolina Power & Light Company asked that the Commission dismiss the exceptions relating to Carolina Power & Light Company which were filed by Mr. Mierek and Mr. Eddleman.

On May 2, 1983, the Commission issued an Order scheduling the exceptions of Mr. Eddleman and Mr. Mierek, and the response of Carolina Power & Light Company thereto for oral argument before the full Commission on May 13, 1983.

On May 9, 1983, Charles B. Mierek filed a response to the response of Carolina Power & Light Company stating that he was granted intervenor status in a North Carolina Utilities Commission Order Allowing Intervention dated July 22, 1982.

The exceptions and responses came on for oral argument as scheduled on May 13, 1983. The parties were present and made oral argument with respect to the exceptions.

Upon consideration of the exceptions, the oral argument of the parties, the Recommended Orders of April 1, 1983, and the entire record in this docket, the Commission is of the opinion and so concludes that except as hereinafter set forth the exceptions to the Recommended Orders should be overruled and that the Recommended Orders of Hearing Examiner Gruber issued April 1, 1983, should be affirmed and adopted as the final orders of the Commission. In so deciding, the Commission finds and concludes that all the findings and conclusions and ordering paragraphs contained in the Recommended Orders are fully supported by the records.

With respect to the Recommended Order relating to Duke Power Company, the Commission makes the following amendment to page 5 of Appendix A relating to the 15-year, fixed, long-term rates by substituting the folling rates:

Energy Credits	
Peak kWh	4.82¢ per kWh
Off-peak kWh	2.97¢ per kWh
Capacity Credits	
Peak kWh - peak months	1.83**¢ per kWh
Peak kWh - off-peak months	1.10**¢ per kWh

**Applies to contracts of 11 years or longer.

In so deciding the Commission estimates that the 15-year rates granted in the Recommended Order for purchases by Duke from qualifying facilities are approximately 5.28¢ per kWh on a composite basis, whereas the rates in effect prior to the Recommended Order were approximately 5.31¢ per kWh. Although various adjustments to the rates were made by the Hearing Examiner based on testimony and evidence from many sources, the Commission recognizes that such rates are still an imperfect reflection at best of the avoided costs, and that quantifying the actual avoided costs is an imprecise exercise involving a great deal of judgment. The Commission is of the opinion that a decrease in overall rates from the 5.31¢ per kWh previously approved to 5.28¢ per kWh would not be desirable from the standpoint of encouraging more cogeneration activity, particularly when such decrease is based on premises over which there is so little agreement. The Commission therefore concludes that the 15-year rates should remain at 5.31¢ per kWh on a composite basis; and that the largest component in said composite rates, the energy credits, should be adjusted in order to achieve the 5.31¢ per kWh.

The Commission also calls attention to the exceptions of Mr. Eddleman relating to the ruling of Examiner Gruber which limits Mr. Eddleman's intervention in this docket to Duke Power Company and denying Mr. Eddleman's intervention and participation in the CP&L portion of the docket. The Commission has carefully considered these exceptions and the ruling of Mr. Gruber. The Commission is of the opinion that Examiner Gruber properly acted within his discretion as Hearing Examiner by limiting the participation of Mr. Eddleman in this docket to the portion relating to Duke Power Company. The record discloses that Mr. Eddleman was a customer of Duke Power Company and was allowed participation with respect to Duke Power Company, including

the opportunity to cross-examine Duke's witnesses. Mr. Eddleman was not a customer of CP&L, and the Examiner properly ruled that Mr. Eddleman's status as a shareholder in CP&L would not authorize his intervention and participation in the CP&L portion of the case.

IT IS, THEREFORE, ORDERED as follows:

1. That each of the exceptions filed by Wells Eddleman on April 18, 1983, and Charles B. Mierek on April 15, 1983, to the Recommended Orders issued in this docket on April 1, 1983, be and the same are hereby denied.

2. That the Recommended Orders issued in this docket on April 1, 1983, by Hearing Examiner Gruber be, and the same hereby are, affirmed and adopted as the final orders of the commission except as in the paragraph 3 below.

3. That with respect to the Recommended Order relating to Duke Power Company, the Commission makes the following amendment to page 5 of Appendix A relating to the 15-year, fixed, long-term rates by substituting the following rates:

Energy Credits	
Peak kWh	4.82¢ per kWh
Off-peak kWh	2.97¢ per kWh
Capacity Credits	
Peak kWh - peak months	1.83**¢ per kWh
Peak kWh - off-peak months	1.10**¢ per kWh

ISSUED BY ORDER OF THE COMMISSION.
This the 3rd day of June 1983.

NORTH CAROLINA UTILITIES COMMISSION
Sandra J. Webster, Chief Clerk

(SEAL)

DOCKET NO. E-100, SUB 41

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of

Determination of Rates for Purchase and Sale of Electricity Between Electric Utilities and Qualifying Cogenerators or Small Power Producers) ORDER REGARDING APPLICATION REQUIREMENTS AND PROCEDURES FOR QUALIFYING COGENERATORS AND SMALL POWER PRODUCERS

BY THE COMMISSION: G. S. 62-110.1(a) provides, in pertinent part, as follows:

"[N]o public utility or other person shall begin the construction of any steam, water, or other facility for the generation of electricity to be directly or indirectly used for the furnishing of public utility service, even though the facility be for furnishing the service already being rendered, without first obtaining from the Commission a certificate that public convenience and necessity requires, or will require, such construction.

In order to insure that potential cogenerators and small power producers in North Carolina are made aware of the certification requirements of this statute, the Commission issued an Order on August 17, 1983, requiring that each regulated electric utility in the State give notice of the statutory requirements to each potential cogenerator and small power producer that contacts the utility regarding the possible sale of electricity to the utility.

The Commission encourages the development of cogeneration and small power producer projects in the interest of facilitating the regulated electric utilities' load management programs and the conservation of the nation's natural resources. Therefore, the Commission has determined that it would be appropriate to enter a further Order establishing and clarifying the application requirements of G. S. 62-110.1(a) as it relates to cogenerators and small power producers and the procedures that the Commission will follow in order to process such applications in an expeditious manner.

The Commission has concluded that an application for a certificate of public convenience and necessity for the construction of a facility for the generation of electricity under G. S. 62-110.1(a) by a qualifying cogenerator or small power producer should include, but not be limited to, allegations of the following nature:

1. The correct name and business address of the applicant.

2. Whether the applicant is an individual, a partnership, or a corporation and, if a partnership, the name and business address of each general partner and, if a corporation, the state and date of incorporation and the name and business address of an individual authorized to act as corporate agent for the purpose of the application.

3. The site and nature of the generating facility, including the geographic location, the ownership of the site (if other than by the applicant), the source of power, a brief description of the buildings and equipment comprising the generating facility, and the expected generation capacity of the facility.

4. The projected cost of the project.

5. The projected date of project completion and operation.

6. The applicant's plans for sale and distribution of the electricity generated.

7. The federal and state permits and exemptions that are required for the project and whether they have been obtained or applied for.

The application should be verified by the applicant or by an individual authorized to act on behalf of the applicant for purposes of the application and may be accompanied by such supporting exhibits as the applicant choses to provide.

The Commission has determined that, in the interest of expediting the processing of such an application while still observing the requirements

imposed upon the Commission by the General Assembly, the procedures set forth in G.S. 62-82(a) should be observed. More specifically, such an application will be processed in the following manner:

1. Upon the filing of an application appearing to meet the requirements set forth above, the Commission shall promptly issue an Order requiring the applicant to publish a notice (which will be provided along with the Order) once a week for four successive weeks in a daily newspaper of general circulation in the county where the generating facility is proposed to be constructed and, if the generating facility is a hydroelectric facility, mail a copy of the notice to the Dam Safety Administrator, Land Quality Section, Division of Land Resources, Department of Natural Resources and Community Development, P. O. Box 27687, Raleigh, North Carolina 27611.

2. The applicant shall be responsible for filing with the Commission (a) an affidavit of publication (which can be obtained from the newspaper in which the notice is printed) and (b), if the generating facility is a hydroelectric facility, a certificate of service which shall simply state that the notice has been mailed to the Dam Safety Administrator and shall be signed and verified by the applicant or its agent.

3. If no complaint is received within ten days after the last date of publication of the notice and the affidavit of publication and certificate of service (if required) have by that time been filed with the Commission, the Commission shall promptly enter an Order awarding the certificate.

4. If a complaint is received within ten days after the last date of publication of the notice, the Commission shall promptly schedule a public hearing on the application and shall give reasonable notice of the time and place thereof to the applicant and to each complaining party. Such a hearing shall be held as soon as reasonably possible, and the procedure for rendering a decision pursuant to the hearing shall be given priority over all other cases on the Commission's calendar of hearings and decisions, except rate cases.

5. If time is of the essence, the Commission may, upon the applicant's request, schedule a hearing by the Order requiring public notice of the application. A hearing so scheduled may be cancelled if no complaints are received within ten days after the last date of publication of the notice, and the notice shall so specify.

6. If time is of the essence, the applicant may request temporary operating authority either before or at the time the application is filed.

IT IS, THEREFORE, ORDERED as follows:

1. That the requirements and procedures outlined herein be observed by the Commission.

2. That each regulated electric utility subject to this Order be, and hereby is, required to advise each potential cogenerator and small power

producer which contacts the utility regarding the possible sale of electricity to the utility of the substance of the application requirements and procedures provided herein at the same time as the notice required by Commission Order of August 17, 1983, in this docket: Notice of the present requirements and procedures shall be in clear and simple terms and shall state that the Commission encourages the development of cogeneration and small power producer projects and has established these guidelines in order to clarify and expedite the application process required by statute.

3. That each regulated electric utility subject to the requirements of this Order shall file with the Commission within one month after the date of this Order a copy of the written notice to be utilized by the company in conformity with decretal paragraph number 2 above.

ISSUED BY ORDER OF THE COMMISSION.
This the 7th day of October 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sharon Credle Miller, Deputy Clerk

DOCKET NO. E-100, SUB 46

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of

Investigation, Analysis and Estimation of Future Growth in the Use of Electricity and the Need for Future Generating Capacity for North Carolina	) ORDER ADOPTING UPDATED) FORECAST AND PLAN FOR) MEETING LONG-RANGE NEEDS) FOR ELECTRIC GENERATION) FACILITIES IN NORTH) CAROLINA - 1982/1983

HEARD IN: Commission Hearing Room, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina, on March 15-17 and on March 23, 1983

BEFORE: Commissioner Sarah Lindsay Tate, Presiding, Chairman Koger, Commissioners Edward B. Hipp, John W. Winters, Leigh H. Hammond, A. Hartwell Campbell, and Douglas P. Leary (Commissioner Winters did not participate in this decision)

APPEARANCES:

For Duke Power Company:
George W. Ferguson, Jr., and William Larry Porter, Duke Power Company, Post Office Box 33189, Charlotte, North Carolina 28242

For Carolina Power & Light Company:
Robert W. Kaylor and H. Hill Carrow, Carolina Power & Light Company, Post Office Box 1551, Raleigh, North Carolina 27602

For Virginia Electric and Power Company:
Edgar M. Roach, Jr., Hunton & Williams, Post Office Box 109, Raleigh, North Carolina 27602

For North Carolina Public Interest Research Group:
Wilbur P. Gulley, Gulley & Eakes, Post Office Box 3573, Durham, North Carolina 27702

For Kudzu Alliance:
M. Travis Payne, Edelstein & Payne, Post Office Box 12607, Raleigh, North Carolina 27602

For the Using and Consuming Public:
Theodore C. Brown, Jr., Karen E. Long, and Antoinette R. Wike, Staff Attorneys, Public Staff - North Carolina Utilities Commission, Post Office Box 991, Raleigh, North Carolina 27602

BY THE COMMISSION: In 1975 the North Carolina General Assembly enacted G. S. 62-110.1(c), which directs the Utilities Commission to "develop, publicize, and keep current an analysis of the long-range needs for expansion of facilities for the generation of electricity in North Carolina, including its estimate of the probable future growth of the use of electricity, the probably needed generating reserves, the extent, size, mix, and general location of generating plants and arrangements for pooling power . . ." The statute requires the Commission to conduct public hearings in the course of making the analysis and developing the plan and each year to submit a report of its analysis and plan to the Governor and to the appropriate committees of the General Assembly.

On December 1, 1982, the Commission issued an Order scheduling a hearing in this docket. The Order required the Public Staff, Carolina Power & Light Company, Duke Power Company, Virginia Electric and Power Company, and Nantahala Power and Light Company to file their forecast reports and supporting testimony and exhibits on or before February 4, 1983. The Order also established a schedule for other interested parties to file petitions of intervention, testimony, and exhibits. It further directed CP&L, Duke, Vepco, and Nantahala to publish notice of the hearing in newspapers in their respective service areas once a week for two consecutive weeks. Proof of publication has been filed with the Commission as required by the Order.

Notice of intervention from the Public Staff was filed and recognized by the Commission. The Commission also received and granted petitions to intervene from the following parties: CP&L, Duke, Vepco, Kudzu Alliance, and the North Carolina Public Interest Research Group (N. C. PIRG).

The 1983 Public Staff Report entitled Analysis of Long Range Needs for Electric Generating Facilities in North Carolina was filed with the Commission on February 4, 1983, as were testimony and exhibits of CP&L, Duke, Vepco, and Nantahala. The Public Staff also moved to file testimony on February 18, 1983, which Motion was allowed by the Commission. Testimony and exhibits of the Kudzu Alliance and N.C. PIRG were filed on February 28, 1983.

On March 10, 1983, Duke filed additional testimony and exhibits, and on March 15, 1983, Kudzu Alliance filed supplemental testimony.

The matter came on for hearing as scheduled on March 15, 1983. Vepco presented the testimony and exhibits of the following witnesses: Jack H. Ferguson, Executive Vice President and Chief Operating Officer of Vepco, and Samuel M. Laposata, Director of Forecasting at Vepco.

The Public Staff presented the testimony and exhibits of the following witnesses: Hsin-Mei Hsu, Economist in the Economic Research Division of the Public Staff; Thomas S. Lam, Utilities Engineer in the Electric Division of the Public Staff; Dennis J. Nightingale, Director of the Electric Division of the Public Staff; Richard N. Smith, Jr., Utilities Engineer in the Electric Division of the Public Staff; and Robert A. Weiss, Economist in the Economic Research Division of the Public Staff.

Nantahala presented the testimony and exhibits of N. Edward Tucker, Jr., Vice President - Finance and Treasurer of Nantahala.

CP&L presented the testimony and exhibits of the following witnesses: Archie W. Futrell, Jr., Director of Economic & Energy Forecastng & Special Studies for CP&L; John S. Monroe, Jr., Manager of the Conservation and Load Management Department of CP&L; and Bobby L. Montague, Vice President, Planning & Coordination for CP&L.

Duke presented the testimony and exhibits of the following witnesses: Donald H. Denton, Senior Vice President, Marketing & Rates for Duke; David Rea, Manger of Forecasting for Duke; Donald H. Sterrett, Manager of System Planning for Duke; and Warren H. Owen, Executive Vice-President, Engineering & Construction for Duke.

CP&L also presented rebuttal testimony of Mr. Futrell and Mr. Monroe. Duke presented rebuttal testimony of Robert H. Spann, a Principal of ICF Incorporated.

The Public Staff presented surrebuttal testimony of Mr. Lam and Dr. Weiss.

Kudzu Alliance and N.C. PIRG presented separate testimony and exhibits of Wells Eddleman, an energy and pollution control consultant.

At the night hearing in Raleigh, the Commission also heard testimony from two public witnesses: Henry S. Cole and Eliza Wolper.

Based upon the foregoing, the evidence adduced at the hearing, and the entire record in this matter, the Commission makes the following

FINDINGS OF FACT

1. The two largest electric utilities in North Carolina are Duke Power Company and Carolina Power and Light Company, which together provide 95% of the electricity consumed in the state. Virginia Electric and Power Company and Nantahala Power and Light Company supply the remaining 5%.

2. The probable future rates of growth in the peak demand for electricity through the year 1997 for CP&L and Duke, taking into account the effects of additional load management and conservation, are as follows:

CP&L	1.9% to 3.4%
Duke	1.4% to 3.5%

3. With respect to the Harris 2 nuclear unit, CP&L should be required to file a comprehensive study showing economic justification for the continued construction and the funding of its Harris 2 nuclear unit.

4. Duke's Bad Creek hydroelectric project is under limited construction with no scheduled completion date. Duke should file a report showing the role of such project in its current construction schedule and capacity plan.

5. Vepco's generation expansion plan, which was outlined in the testimony of Vepco witness Jack H. Ferguson, will be adequate to meet Vepco's projected growth in demand and to provide dependable service to Vepco's customers.

6. The probable needed generating reserves for planning purposes, through the year 1997, for CP&L, Duke, and Vepco continues to be 20%.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 1

This finding is based on information contained in the files and records of the Commission, testimony presented at the hearing, and findings of the Commission in previous Orders.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 2, 3, AND 4

The forecasting of the demand for electricity, and the design of systems to meet that demand at minimum cost, are formidable tasks. The demand for electricity is related to factors such as economic activity, the price of electricity, and the price of competitive fuels which are themselves difficult to forecast. In addition, the relationship between these factors and the demand for electricity can change over time as new technologies are developed and commercialized.

The long lead time required to bring capacity on line also makes planning difficult. A power plant which appears to be state-of-the-art and economical when ordered may, as conditions change, become instead a heavy financial burden to both investors and ratepayers.

The Commission has heard substantial testimony in this proceeding on estimated growth rates in demand and the companies' load management programs. The Commission has also heard testimony on what the construction schedules should be given the uncertainties inherent in the above. Yet, it is the construction schedules that are really the basis for G. S. 62-110.1(c).

The Commission, therefore, has considered all of the evidence in terms of the companies' expansion plans and construction schedules as they currently exist and as they should or should not be modified.

The Public Staff witnesses Hsu, Lam, Nightingale, Smith, and Weiss testified as a panel and discussed the conclusions of the Public Staff Report. This Report showed expected annual growth rate of demand for electricity, after additional conservation and load management programs, as 2.0% for CP&L and 1.7% for Duke. Based upon this growth, the Public Staff stated, Duke and CP&L will need to add only three generating facilities each between 1983 and 2000 in order to provide electricity in the most economic and reliable manner. The Public Staff Report stated that the power from Harris 1, Mayo 2, Catawba 1, and Catawba 2 would not be needed until several years after the currently expected completion dates of these units.

Taking into account the possibility that its forecasts might be low, the Public Staff also considered what construction would be needed at higher

growth rates in electricity demand. Using the Public Staff econometric peak demand forecasts and the Company's own load management and conservation estimates, the Public Staff found that for CP&L an additional plant (beyond Harris 1, Mayo 1, and Mayo 2) would be needed in 1995 and that this plant should be fueled by coal and not by uranium. For Duke, the Public Staff found that a construction schedule based on a higher growth rate indicated that any other power plants required by the year 2000 should also be coal plants rather than nuclear.

CP&L offered the testimony of witnesses Futrell, Monroe, and Montague. Mr. Futrell described the Company's usage forecast, which uses regression analysis on monthly or quarterly data. He stated that the Company's models forecast sales growth before load management and conservation of 3.1% per year from 1981-2000. After load management and additional conservation, the growth rates are 2.7% from 1981 to 1991 and 2.9% from 1991 to 2001. He stated:

> "This reflects a slightly slower growth rate in electric energy usage in the Company's service area for the first ten years than in our previous forecast due primarily to the lingering effect of the recession of 1981-82." (Tr. Vol. 2, p. 53)

Mr. Monroe described the Company's conservation and load management program stating:

> "It is the policy of Carolina Power and Light Company to pursue cost-effective conservation and load management programs which permit good service and support sound economic growth within our service area." (Tr. Vol. 2, p. 111)

He noted the Company's goal of 1750 megawatts of peak load reduction by 1995, about half from conservation due to price and the other half due to load management or things the customers would not do by themselves, such as appliance control.

Mr. Montague discussed the forecast of peak load and the Company's Generation Additions Schedule. He stated that the load forecast is developed by determining future coincident peak load factors for each sales classification and applying them to a separate energy forecast to derive future peak loads. He explained that a coincident peak load factor is the ratio of the average hourly load for a class to the load for that class at the time of the system peak.

Mr. Montague stated that the Company is forecasting peak load to grow at an annual rate of 2.9% for the 1981-1995 period. This is after the effects of load management. To meet this growth in peak demand the Company is planning the addition of the following units:

Mayo 1 (Coal)	1983
Harris 1 (Nuclear)	1986
Harris 2 (Nuclear)	1990
Mayo 2 (Coal)	1992

He stated that the Company will need additional capacity in 1996 to maintain a 20% reserve margin.

The testimony of Duke was given by witnesses Denton, Rea, Sterrett, and Owen. Mr. Denton described the Duke Load Management Program, one of the goals of which is to reduce the winter 1997 peak by 6056 megawatts. He concluded that "even with this aggressive load management program, Duke Power currently sees system peak demand growing 2.8 percent annually, which must be met by new generation facilities." (Tr. Vol. 2, p. 225)

Mr. Rea described the Company's peak load forecasting methodology, which is based primarily on the growth in real personal income in the service area. Mr. Rea noted that one of Duke's assumptions was that the real price of electricity would increase by 2.5% per year in the period 1981-1997.

Mr. Sterrett discussed the Company's construction schedule and prospective reserve margins. At the time of the hearing, the Company had the following units planned:

McGuire 2	(Nuclear)	March 1984
Catawba 1	(Nuclear)	Summer 1985
Catawba 2	(Nuclear)	Summer 1987
Bad Creek and	(Pumped Storage)	limited construction -
Cherokee 1	(Nuclear)	no completion date

Mr. Sterrett's exhibit showed that without Bad Creek and Cherokee, Duke's reserve margin would fall below 20% in the summer of 1993, under the Company's forecast.

Mr. Owen also testified on the Company's construction schedule, noting that he felt it was insufficient to meet the electricity demand in the Duke service area. He also pointed out that the Company forecast of need for capacity did not allow for any unit retirements, even though 45% of the Company's present generating capacity would be at least 25 years old in 1995.

The Commission notes that on April 30, 1983, Duke announced cancellation of Cherokee 1, saying the unit would not be needed until 1995 and had lost its "cost advantage" over other types of power plants the Company might build to meet power demand.

In its consideration of the evidence presented in this proceeding, the Commission finds itself confronted by different forecasts of electricity demand for the future as well as differences in the accounting for additional load management and conservation. With respect to the economic forecasts, the Commission concludes that sophisticated techniques were competently applied by all parties. The assumptions used by each party about such variables as personal income and the future price of electricity were reasonable, although certainly not in agreement. Therefore, the Commission concludes that the forecasts presented constitute a range over which the future growth in demand for electricity can be expected to be found.

Using the actual peak load in the summer of 1982 as the base, and each party's forecast of peak load after conservation and load management, the Commission concludes that growth rates from 1982 to 1997 can be expected to fall in the range of 1.4% to 3.5% for Duke and 1.9% to 3.4% for CP&L. (Because these growth rates are calculated from 1982 actual to 1997 forecast, they are not the same as other growth rates cited. Those other growth rates were computed using different starting and/or ending points.)

Given the uncertainties inherent in any forecast of capacity expansion schedules, the important question then becomes: what facilities should Duke and CP&L be building to meet the probable demand? In the following tables the current construction schedules for Duke (recognizing the cancellation of Cherokee) and for CP&L are compared to the schedules the Public Staff presented showing when that power would be needed:

	Duke	Public Staff
McGuire 2	1984	1984
Catawba 1	1985	1996
Catawba 2	1987	1999
Bad Creek	?	not needed

Witnesses for Duke discussed various reasons, including contractual obligations relating to the sale of the units, which would make it impractical to delay the in-service dates of the Catawba units. The Public Staff witnesses stated that their schedule showed when the power from the units would be needed to keep reserve margins at 20% or above, but the Public Staff did not actually recommend delaying construction. Also, the Public Staff concluded that any additional baseload plants after Catawba should be coal-fired.

After considering the evidence relating to Duke, the Commission finds essentially no difference in what Duke is currently building and what the Public Staff proposed Duke should be building. The major difference is that Duke believes the current program is inadequate and that more capacity will be needed in 1993. The Public Staff believes that view is pessimistic and that the reserve margin will be adequate for several years past that. The other difference concerns Bad Creek, a pumped storage facility. That facility is not mentioned in the Public Staff Report and the Company did not refer to the economics of this type of unit. Presumably the economic justification for Bad Creek will have changed since the cancellation of Cherokee, as the Company will have less nuclear power to operate in conjunction with the pumped storage facility.

With the cancellation of Cherokee, the Commission is left without any guidance from Duke on what is the appropriate type of generation to come on line, if necessary, in the period from 1993 to 2000. Therefore, the Commission concludes that Duke should file comments or studies showing its current preferred alternative or the type of capacity it should build if such construction becomes necessary.

With respect to CP&L, the situation is similar. The Company's program is shown, and compared to that shown by the Public Staff, in the following table:

CP&L		Public Staff	
Mayo 1	1983	Mayo 1	1983
Harris 1	1986	Harris 1	1990
Harris 2	1990		
Mayo 2	1992	Mayo 2	1998
Other	1996		

Again, the Public Staff stated that the dates shown were its estimates of when the power from the plants would be needed but it did not recommend that Harris 1 or Mayo 2 be postponed.

The difference between CP&L and the Public Staff is Harris 2. CP&L witness Montague stated that the Company still considered Harris 2 a "viable option," subject only to the Company's concerns about financing the unit. Mr. Montague also testified that even under the Company's low forecast scenario, Harris 2 would still be needed, although its completion date could be moved to 1992. Mr. Montague testified that for the years 1982 and 1983 the Company has not had a really active effort underway on Harris 2. (Tr. Vol. 2, pp. 189-190) Except for items relating directly to Harris 1, construction has not been taking place on Harris 2.

Again, the Company thinks the unit will be necessary and useful, while the Public Staff does not, but the current construction program of CP&L (work ongoing at Harris 1) is, in fact, in accord with the recommendations of the Public Staff. The question remaining is: Which unit should be built next? The Company says Harris 2 and the Public Staff says Mayo 2. The Public Staff Report makes the point that "NRC 'ratcheting' of nuclear plant design technology makes Harris 2 and Cherokee 1 less of a viable alternate (sic) than a plant of new design." The Commission notes that Cherokee 1 has been cancelled and concludes that CP&L should file studies showing an analysis of the economics of completing Harris 2 versus constructing a coal plant. Given the evidence presented by the Public Staff, the Commission concludes that further expenditures on Harris 2 may not be considered prudent in the absence of a demonstration that Harris 2 is the most efficient way to expand the CP&L system in the face of uncertain demand growth.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 5

The Public Staff offered no forecast for Vepco. Vepco, through the testimony of Witness Laposata, presented a description of the modeling process used by Vepco to project its sales and peak load.

In addition to discussing the official forecast, Dr. Laposata also described Vepco's development of a new forecast model. The preliminary results of the new forecast model are as follows:

(1) The growth rate of the winter peak, 1983-1997, will be in the range of 2.5 to 3.0 percent.

(2) The growth rate of the summer peak, 1983-1997, will be in the range of 1.9 to 2.4 percent.

(3) The growth rate of energy output, 1983-1997, will be in the range of 2.5 to 3.0 percent.

The preliminary projections from the new model do not differ significantly from those of the current forecast. Vepco is now in the process of conducting a number of studies necessary for finalizing the new load forecast.

Vepco Witness Ferguson presented Vepco's schedule of capacity additions as follows:

Type	Commercial Operation Date	Capability (MW) Summer	Winter
Bath County 1, 2, 4	Fall 1985	525*	525*
Bath County 3, 5, 6	Fall 1986	525*	525*
Replacement Purchase	Fall 1989	907	907
Undesignated	Fall 1993	550	550
Undesignated	Fall 1994	550	550
Undesignated	Fall 1995	550	550

*Vepco share

Vepco's capacity addition program includes the Bath County Pumped Storage Project (Bath County). Bath County consists of six 350 megawatt units, with three to be completed in the fall of 1985 and three in 1986. Vepco has agreed to a partial sale of Bath County to Allegheny Power System (APS). In its generation expansion plan, Vepco has assumed that APS purchases 20 percent of the Project's assets and makes a ten-year capacity purchase of 30 percent of the Project's capacity, and that Vepco recovers the 30 percent capacity purchase after the tenth year of commercial operation.

Vepco's plans for unit additions for the period past 1990 have not been completed. Vepco is performing an on-going evaluation of the types of generation that may be added to its system to provide an optimum mix in the 1990s. The evaluation encompasses conventional as well as alternative energy sources.

Vepco offered testimony in this proceeding regarding the decision to cancel North Anna Unit 3. Vepco Witness Ferguson testified that Vepco's decision was based on months of detailed and thorough evaluations regarding estimated completion costs of North Anna Unit 3. These evaluations showed that recent changes in regulatory requirements have resulted in large increases in completion cost estimates for future nuclear units. Mr. Ferguson testified that in light of the new cost estimates for North Anna Unit 3, completing the unit is no longer the least costly alternative for meeting future electric needs.

The cancellation of North Anna Unit 3 did not result from any reduction in Vepco's forecast for load growth. The capacity which would have been supplied by North Anna Unit 3 will have to be replaced from other sources. Vepco is now investigating several possibilities for replacing that capacity. Vepco, in its investigations, has found that imbalances exist between slow growth of electricity demand and the pace of capacity development in some of its neighboring utility systems. Vepco is now negotiating with other utilities concerning specific combinations of asset purchases and/or long-term capacity purchases. Vepco also expects the development of conservation and load management techniques and the implementation of cogeneration and non-conventional generating methods will contribute to replacement of the capacity which was planned from North Anna Unit 3.

The Commission concludes that Vepco is taking reasonable steps toward meeting the future demand for electricity in an economical manner.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 6

The Commission has used, in previous cases, a reserve margin criterion of 20%. No party presented evidence that this was too high or too low or otherwise inappropriate, and the Commission concludes that 20% reserves remain a legitimate goal.

IT IS, THEREFORE, ORDERED as follows:

1. That the findings and conclusions of this Order are hereby adopted as the Commission's current analysis and plan for the expansion of facilities to meet future requirements for electricity in North Carolina.

2. That, within ninety (90) days after the date of this Order, CP&L shall file with the Commission a comprehensive study showing economic justification for the continued construction and funding of its Harris 2 nuclear unit; provided, however, that no such study shall be required if, within the same ninety (90) day period, CP&L shall have notified the Commission in writing that the Harris 2 unit has been cancelled.

3. That within ninety (90) days after the date of this Order, Duke shall file with the Commission comments and/or studies showing the role of Bad Creek in its current construction schedule and capacity expansion plan.

ISSUED BY ORDER OF THE COMMISSION.
This the 1st day of December 1983.

NORTH CAROLINA UTILITIES COMMISSION
Sandra J. Webster, Chief Clerk

(SEAL)

DOCKET NO. P-100, SUB 61
DOCKET NO. P-134

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of		
Resale of Intrastate	)	ORDER APPROVING CURRENT TARIFF RESTRICTIONS AGAINST
Telecommunications	)	THE RESALE OF INTRASTATE TELECOMMUNICATIONS
Services	)	SERVICES

HEARD IN: The Commission Hearing Room, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina, on November 16, 1982, at 2:00 p.m.

BEFORE: Chairman Robert K. Koger and Commissioners Edward B. Hipp,

Presiding, Douglas P. Leary, Sarah Lindsay Tate, Leigh H. Hammond, and A. Hartwell Campbell

APPEARANCES:

For the Applicant:

Charles C. Meeker, Sanford, Adams, McCullough and Beard, Attorneys at Law, Post Office Box 389, Raleigh, North Carolina 27602, and

Walter E. Daniels, Attorney at Law, Post Office Box 13039, Research Triangle Park, North Carolina 27709
For: Data Utilities, Inc.,
Heins Systems, Inc., and
U.S. Telephone Communications, Inc.

For the Protestants:

Thomas K. Austin, Staff Attorney, Public Staff - North Carolina Utilities Commission, Post Office Box 991, Raleigh, North Carolina 27602
For: The Using and Consuming Public

Jerry B. Fruitt, Eller and Fruitt, Attorneys at Law, Post Office Drawer 27866, Raleigh, North Carolina 27611
For: Tarheel Radio Telephone Association, Inc.

Gary K. Shipman, Shipman and Lea, Attorneys at Law, Post Office Box 1428, Wilmington, North Carolina 28402
For: Econowats, Inc.

For the Respondents:

Robert Carl Voigt, Attorney, Carolina Telephone and Telegraph Company, 720 Western Boulevard Tarboro, North Carolina 27886
For: Carolina Telephone and Telegraph Company

Dale E. Sporleder, Vice President and General Counsel, and Joe E. Foster, Attorney, General Telephone Company of the Southeast, 4100 N. Roxboro Road, Durham, North Carolina 27704
For: General Telephone Company of the Southeast

R. Frost Branon, Jr., General Attorney, Southern Bell Telephone and Telegraph Company, Post Office Box 30188, Charlotte, North Carolina 28230, and

Gene V. Coker, Southern Bell Telephone and Telegraph Company, 4300 Southern Bell Center, Atlanta, Georgia 30375
For: Southern Bell Telephone and Telegraph Company

BY THE COMMISSION: On July 20, 1982, Data Utilities, Inc., a Tennessee corporation certified by the FCC to provide nationwide interstate resale of telephone services, filed an application with this Commission seeking a Certificate of Public Convenience and Necessity to Provide Resale of Telecommunications Services and Facilities within North Carolina. In its application, Data proposes to provide on an intrastate basis voice and data telecommunications services originating and terminating in North Carolina. The Applicant initially intends to resell Wide Area Telecommunications Service (WATS) at rates equal to or more than approved WATS rates but equal to or less than approved MTS rates. Applicant further proposes that as a nondominant common carrier, its tariff should be deemed presumptively lawful.

The Commission concluded that prior to considering applications for certificates to engage in the resale process, a general investigation should be conducted to determine whether currently approved tariff restrictions against the resale of telecommunications services should be modified or rescinded. Moreover, the Commission should consider under relevant statutory and case law the extent of its authority to issue certificates of public convenience and necessity for additional toll service along with the existing toll service, whether a certificate is required to engage in resale, and such other issues as deemed appropriate. Data Utilities, along with all regulated telephone companies, were made parties to the proceeding. The companies, the Public Staff, and other interested persons were invited to file testimony and/or legal briefs regarding this matter.

The hearing commenced as scheduled November 16, 1982, in the Commission Hearing Room, Raleigh, North Carolina. Upon calling of the case for hearing, counsel for all parties were allowed an opportunity to make brief opening statements.

POSITION OF THE PARTIES
THE PUBLIC STAFF

The Public Staff stated that the matter involves a two-fold legal question: (1) Is the proposed service a public utility function, and (2) can this Commission issue a certificate of public convenience and necessity to resellers? The Public Staff contended that the proposed service is a public utility service and that a certificate cannot be granted as a matter of law. Since the Public Staff contends the issue is legal, it presented no evidence.

TARHEEL RADIO TELEPHONE ASSOCIATION, INC.

Tarheel Radio Telephone Association, Inc. (TARS), concurred with the Public Staff's position that whether or not the resale of WATS should be allowed in the public interest is immaterial since resale is prohibited by law. TARS went further to say that this matter is for the legislature to address rather than this Commission. TARS asserted that there is no statute conferring any

authority upon this Commission to require any regulated utility to interconnect its facilities so that somebody can compete against them.

DATA UTILITIES, INC.

Data (Applicant) defined the scope of the application to include WATS, private line and other services by the telephone companies. Data asserted that substantial public benefits will flow from the resale of telecommunication services and that due to this benefit the Commission has the discretion to grant or deny certificate of convenience and necessity. Data relied on the following paragraph in Utilities Commission v. Coach Company, 260 N.C. 43, which says:

> "Whether there shall be competition in any given field and to what extent is largely a matter committed to the sound discretion and judgment of the Commission."

Data further asserted that because resellers do not intend to establish duplicate transmission and other telephone facilities the general policies concerning duplication of facilities do not apply here, and that the only competition involved is in the marketing of telecommunications services and not in the transmission of such services.

CAROLINA TELEPHONE AND TELEGRAPH COMPANY

Carolina stated that existing law does not allow competition among utilities. Carolina also expressed its concern that the term "telecommunications services," was too broad noting that message toll service, foreign exchange service, local exchange service, private line exchange service and terminal equipment services could all be included in the term. Carolina stated that if resale were permitted it should be limited to WATS.

EVIDENCE

For the Applicant

Dr. Nina Cornell, President of Cornell, Pelcanito, and Brenner Economists, Inc., testified regarding the public interest benefits of removing existing tariff provisions that prohibit resale of telecommunications services within North Carolina. Dr. Cornell recommended that this Commission allow resale of MTS, WATS, and private line services. She stated that to do so would open up to the residents of North Carolina significant public benefits from new service combinations, much wider availability of specialized services, more efficient utilization of existing facilities, and additional assistance in monitoring the basis for telephone tariff rates. Dr. Cornell emphasized that granting resale of all services involves virtually no duplication of any facilities, meaning that no questions of competitive routes or systems with possible diversion of traffic and reduction in service levels should be raised. In essence, she stated that resale offers large public benefits, particularly to smaller businesses and residential customers, without imposing higher costs.

Royce Bell, President of Data Utilities, Inc., testified that Data has operated as an interstate resale common carrier since December 1, 1981, and seeks to resell intrastate telephone services in North Carolina. He stated

that consumers would benefit from the resale services because they would have a choice of long distance service at competitive rates and to obtain additional service offerings that are not generally available from the regulated carriers. Mr. Bell indicated that the small independent-reseller will also be in a position to more rapidly take advantage of new technologies and to make new offerings of needed services. Data's interest is in leasing transmission facilities from dominant carriers rather than install any duplicative transmission or termination facilities.

Mr. Bell suggested minimal regulation by this Commission such as a streamlined certification procedure which will allow North Carolina to approve only reputable resellers. He stated that tariff control is unnecessary and believes that the resellers pricing structure will, in effect, be regulated by the tariffed dominant carrier rates as well as the competitive nature of the business. Mr. Bell did suggest that reseller should be made subject to the Commission's complaint procedures.

Mr. Edward Watts, General Manager of Heins System, Inc., testified that Heins operates out of the research triangle area and is engaged in interstate resale of WATS services. He stated that Heins does not offer intrastate resale services. He stated that a number of companies are reselling intrastate telecommunications services facilities without a certificate of authority from the North Carolina Utilities Commission, and some of these companies are taking intrastate calls and switching them across state lines and back into North Carolina. Mr. Watts asserted that Heins and other resellers who only resell interstate traffic in compliance with the tariff prohibition are placed at an unfair competitive disadvantage.

Mr. James Pridemore is President of Sound Telephone Systems and Econowats, Inc. He stated that Econowats has been formed for the purpose of offering resale communications services, but is not yet offering any resale services. Mr. Pridemore would like the Commission to allow intrastate resale of WATS and private line service. He presented charts to illustrate the monetary savings which he believes customers would experience if the intrastate resale of telecommunications services is allowed. Mr. Pridemore indicated that the resale of WATS is beneficial to the small businessman and that he does not feel it is detrimental to the telephone company.

For the Respondents

Southern Bell Telephone and Telegraph Company

Mr. David B. Denton, a Southern Bell Telephone and Telegraph Company Division Staff Manager in Rates and Costs, testified that no resale should be allowed until rate levels and rate structures are cost based. MTS needs "Rate Period Specific Billing." According to Mr. Denton the present level of nonrecurring charges for WATS does not cover nonrecurring costs. Private lines are presently priced below cost whereas MTS and WATS are priced above cost. Significant contribution would be lost as WATS and MTS messages are diverted to the reseller's private lines that are used as a substitute for MTS and WATS. Therefore, Southern Bell opposed using "private line service" for resale. In addition, Denton suggested that flat rates should be used for PBX trunks (as opposed to business line rates). Denton stated that this is appropriate charge from the serving central office to the reseller's switch because the reseller's usage of the network is expected to resemble PBX trunk usage.

General Telephone Company of the Southeast

Mr. Joe Wareham, Business Relations Director for General Telephone Company, testified that if the Commission certificates resellers, the rate structures should be cost based in order to fully recover costs and make an additional contribution where appropriate, and that "customers in metropolitan areas, business customers and residence customers with high usage will be the primary beneficiary (of resale). He testified that a loss of contribution from resold services will result in increased rates for basic services, and that this upward pressure on basic services will adversely impact those customers who do not have need for high volumes of usage or sophisticated services."

Carolina Telephone and Telegraph Company

Mr. Warren Hannah, Cost of Service Supervisor for Carolina Telephone Company testified that the present statutes prohibit certification of intrastate telecommunications resellers, and that no order allowing intrastate resale should be issued until the General Assembly revises the relevant statutes. Further, modification or recission of existing tariffs should be required even if the Commission should decide resale is allowable as a matter of law.

United States Telephone Communications, Inc.

Comments of counsel were allowed to be read into the record and in essence United States Telephone Communications, Inc., recommended limiting regulation by the North Carolina Utilities Commission; i.e., review legal and financial status of applicants, require no certification unless applicant is not certified by the FCC and keep tariffs only as record of services and automatically approve rates. In addition, the Commission should establish oversight procedures to resolve any complaints against resellers.

After review of the evidence here presented and consideration of the entire record in this proceeding, the Commission makes the following

FINDINGS OF FACT

1. That the Applicant, Data Utilities, Inc., is a Tennessee corporation which presently holds a certificate from the FCC to resell interstate telecommunications services throughout the continental United States.

2. Data seeks an order from this Commission which would allow it and other federallv certificated resellers to be "automatically" certificated to engage in intrastate resale of telecommunications services in North Carolina.

3. The proposed resale of intrastate telecommunications services would involve the transmission of messages or communications by telephone where such services would be offered to the public for compensation.

4. Current approved tariffs subscribed to by all regulated telephone companies prohibit resale of telecommunications services.

5. The Commission takes judicial notice of the fact that there are presently 26 telephone companies certificated to provide telephone services in

North Carolina within their respective territorial boundaries and that these utilities have a monopoly to provide telecommunications services within said boundaries.

6. The proposed resale would allow resellers to compete for customers now being served by existing utilities.

7. Resellers would provide no service that is not being offered or could not be offered by any of the presently certificated telephone utilities.

8. Competition from resellers would cause a loss of revenue contribution from resold services to general intrastate revenues and thereby result in increased rates for basic service.

CONCLUSIONS

The Commission concludes that Data's request that it and other federally certificated resellers be permitted to resell intrastate telecommunications services should be denied. The Commission further concludes that all tariffs restricting or prohibiting intrastate resale should remain in full force and effect.

Currently approved tariffs restricting resale should remain in effect since they carry out the legislative policy that state certificated monopolies generally should be protected from competition, from other certificated utilities.

If the Commission were to grant Data's request and certificate resellers [as public utilities pursuant to G. S. 62-3(23)a.1. and N.C.G.S. 62-110] and allow them to actively compete with existing telephone utilities, the Commission would be acting contrary to the policy enunciated in State ex rel. Utilities Commission v. Carolina Telephone and Telegraph Co., 267 N.C. 257, 271, 148 S.E. 2d 100 (1966).

> "G.S. 62-262(f) expressly provides as to motor carriers of passengers that no certificate shall be granted to an applicant proposing to serve a route already served by a previously authorized motor carrier unless and until the Commission shall find from the evidence that the service rendered by such previously authorized carrier is inadequate, and the certificate holder has been given reasonable time to remedy the inadequacy. See Utilities Commission v. Coach Co., supra; Utilities Commission v. Coach Co., 233 N.C. 119, 63 S.E. 2d 113.
>
> "There is no such express provision as to utilities engaged in the communications field. Nevertheless, the basis for the requirement of a certificate of public convenience and necessity, as a prerequisite to the right to serve, is the adoption, by the General Assembly, of the policy that, nothing else appearing, the public is better served by a regulated monopoly than by competing suppliers of the service. Utilities Commission v. Coach Co., 224 N.C. 390, 30 S.E. 2d 328; Citizens Valley View Co. v. Illinois Commerce Commission, 28 Ill. 2d 294, 192 N.E. 2d 392, Mo., Kan. & Okla. Coach Lines, Inc. v. State, 183 Okla. 3, 81 P. 2d 664. There is, however, inherent in this requirement the concept that, once a certificate is granted which authorizes the holder to render the proposed service

within the geographic area in question, a certificate will not be granted to a competitor in the absence of a showing that the utility already in the field is not rendering and cannot or will not render the specific service in question."

Inasmuch as the evidence indicates that existing utilities are providing or can provide the proposed services and that by allowing resale the Commission would promote upward pressure on basic local rates, the Commission cannot conclude that the public would be better served by allowing resale, or that the utilities in the field cannot or will not render the specific service in question.

Having found that resale is not permitted under North Carolina law, and the findings of fact herein, tariffs restricting resale should remain in effect and Data's application to be certificated as a reseller of intrastate telecommunications services should be dismissed.

IT IS, THEREFORE, ORDERED:

1. That all tariffs prohibiting or restricting resale of intrastate telecommunications services shall remain in effect.

2. That the application of Data Utilities, Inc., for a certificate of public convenience and necessity is dismissed.

ISSUED BY ORDER OF THE COMMISSION.
This the 18th day of March 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sharon Credle Miller, Deputy Clerk

DOCKET NO. P-100, SUB 64

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of	
Investigation of Intrastate Long Distance WATS and	) ORDER DENYING
Interexchange Private Line Rates of All Telephone	) MOTION TO
Companies under the Jurisdiction of the North	) DISMISS
Carolina Utilities Commission	) APPLICATION

HEARD IN: Commission Hearing Room, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina, May 30, 1983, at 3:00 p.m.

BEFORE: Commissioner Edward B. Hipp, Presiding, Commissioner Lindsay Tate and Chairman Robert K. Koger

APPEARANCES:

For Southern Bell Telephone and Telegraph Company:
Robert C. Howison, Jr., Hunton & Williams, Attorneys at Law, P.O. Box 109, Raleigh, North Carolina

R. Frost Branon, Jr., General Attorney, Southern Bell Telephone and Telegraph Company, P.O. Box 30188, Charlotte, North Carolina

For Citizens Telephone Company:
Thomas R. Eller, Jr., Attorney at Law, P.O. Drawer 27866, Raleigh, North Carolina 27611

For Carolina Telephone and Telegraph Company:
Dwight Allen, General Counsel, Carolina Telephone and Telegraph Company, 720 Western Boulevard, Tarboro, North Carolina 27886

For Continental Telephone Company of North Carolina and Mid-Carolina Telephone Company:
F. Kent Burns, Boyce, Mitchell, Burns & Smith, P.A., Attorneys at Law, P.O. Box 2479, Raleigh, North Carolina

For North Carolina Textile Manufacturers Association:
Jerry B. Fruitt, Attorney at Law, P.O. Box 2507, Raleigh, North Carolina 27602

BY THE PANEL: This docket is before the Commission and concerns an investigation of all intrastate long distance WATS and interexchange private lines of all telephone companies under the jurisdiction of the Commission.

On May 10, 1983, the North Carolina Textile Manufacturers Association filed a Motion to Dismiss the Application in the docket without prejudice. The Commission scheduled oral argument on the motion to be heard on May 20, 1983. The matter came on for hearing as scheduled.

Based on the argument of able counsel, the Commission concludes that the intervenors and independents have raised grave issues regarding the future regulation of telecommunications in North Carolina, but these issues do not go to the question of dismissal but instead, should be addressed in the hearing on the merits. Moreover, the Panel concludes that it is illogical to consolidate this toll rate case with a generic rule-making investigation into access charges. Thus, the Panel concludes that good cause does not appear to dismiss or consolidate the application.

IT IS, THEREFORE, ORDERED:

1. That the Motion to Dismiss the Application in this docket is denied.

2. That the oral motion of Carolina Telephone Company to consolidate this docket with Docket No. P-100, Sub 65, is denied.

3. That the hearing in Docket No. P-100, Sub 64, shall commence in Raleigh on Wednesday, June 1, 1983, at 10:00 a.m., as scheduled in the Commission Order issued March 7, 1983.

ISSUED BY ORDER OF THE PANEL.
This the 26th day of May 1983.

NORTH CAROLINA UTILITIES COMMISSION
Sandra J. Webster, Chief Clerk

(SEAL)

DOCKET NO. P-100, SUB 64

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of Investigation of Intrastate Long Distance, WATS, and Interexchange Private Line Rates of All Telephone Companies Under the Jurisdiction of the North Carolina Utilities Commission	) RECOMMENDED ORDER) ALLOWING PARTIAL) INCREASE AND) REQUIRING THE FILING) OF RATES FOR) INTRASTATE TOLL) SERVICE

HEARD IN: The Commission Hearing Room, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina, on June 1, 2, 3, and 6, 1983

BEFORE: Commissioner Edward B. Hipp, Presiding; and Chairman Robert K. Koger and Commissioner Sarah Lindsay Tate

APPEARANCES:

For the Applicant:

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R. Frost Branon, Jr., General Attorney, Southern Bell Telephone and Telegraph Company, P.O. Box 30188, Charlotte, North Carolina 28232

Robert W. Sterrett, Jr., and J. Billie Ray, Jr., Southern Bell Telephone and Telegraph Company, 4300 Southern Bell Center, Atlanta, Georgia 30375
For: Southern Bell Telephone and Telegraph Company

For the Respondents:

Dwight W. Allen, Carolina Telephone and Telegraph Company, 720 Western Boulevard, Tarboro, North Carolina 27886
For: Carolina Telephone and Telegraph Company

John R. Boger, Jr., Williams, Boger, Grady, Davis and Tuttle, P. A., P. O. Box 810, Concord, North Carolina 28025
For: Concord Telephone Company

F. Kent Burns, Boyce, Mitchell, Burns and Smith, P.A., P.O. Box 2479, Raleigh, North Carolina 27602
For: Continental Telephone Company of North Carolina and Mid-Carolina Telephone Company

Thomas R. Eller, Jr., P.O. Box Drawer 27866, Raleigh, North Carolina 27611
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For: Central Telephone Company

Thomas K. Parker, and Dale E. Spoleder, Attorneys at Law, General Telephone Company of the Southeast, P.O. Box 1412, Durham, North Carolina 27712
For: General Telephone Company of the Southeast

For the Intervenors:

Charles J. Beck, P.A., 820 Irma Avenue, Orlando, Florida 32803
For: North Carolina Alarm Association

Jerry B. Fruitt, Attorney at Law, P.O. Box 2507, Raleigh, North Carolina 27602
For: North Carolina Textile Manufacturers Association

Robert H. Bennink, Jr., Assistant Attorney General, North Carolina Department of Justice, P.O. Box 629, Raleigh, North Carolina 27602
For: The Using and Consuming Public

Antoinette R. Wike, and Thomas K. Austin, Staff Attorneys, Public Staff, P.O. Box 991, Raleigh, North Carolina 27602
For: The Using and Consuming Public

BY THE COMMISSION: On February 8, 1983, Southern Bell Telephone and Telegraph Company (Southern Bell or Applicant) filed an application with the Commission for authority to increase intrastate rates and charges to produce increases in total annual revenues of $144,974,447. The Commission being of the opinion that the matter constituted a general rate case under G.S. 62-137, issued an Order on March 7, 1983, in Docket Nos. P-55, Sub 816 and P-100, a general rate case proceeding,
suspending the proposed rates for 270 days from the date the rates were to become effective, and establishing the test period as the 12 months ended October 31, 1982. Further, in its March 7, 1983, Order, the Commission found that the public interest required intrastate long-distance message toll service (MTS), wide-area telephone service (WATS), and interexchange private line rates to be uniform among all telephone companies operating in North Carolina. Accordingly Southern Bell's request to adjust long-distance MTS, WATS, and interexchange private line rates was separated from Docket No. P-55, Sub 816, and placed in Docket No. P-100, Sub 64, for investigation and hearing with all other telephone companies under the jurisdiction of the Commission being made parties thereto.

The following parties intervened: the Public Staff by Notice of Intervention filed on March 28, 1983; the North Carolina Textile Manufacturers Association by Order Allowing Petition to Intervene issued April 1, 1983; the Attorney General by Notice of Intervention filed April 13, 1983; and the North Carolina Alarm Association by Order Allowing Petition to Intervene issued April 19, 1983.

The matter came on for hearing at the time and place shown above.

Southern Bell offered the direct testimony of the following witnesses: Robert C. Hart, Jr., District Staff Manager in Service Costs; Robert L. Savage, Division Staff Manager - Rates and Service Costs; and B.A. Rudisill, District Manager - Bell Independent Relations. W. Whitard Jordan, District Staff Manager - Rates and Costs, testified as a rebuttal witness for Southern Bell.

Carolina Telephone and Telegraph Company offered the testimony of T.G. Allgood, Jr., Toll Revenue Requirements Manager; William H. Collins, Associate Professor of Decision Sciences, East Carolina University; and T.P. Williamson, Vice-President - Administration.

Appearing and offering testimony on behalf of the other Independent telephone companies (Independents) operating in North Carolina were: Felix L. Boccucci, Jr., Analyst with Contel Service Corporation - Eastern Region for Continental Telephone Company of North Carolina; Stuart M. Rutter, General Manager - Regulatory and Operational Planning, for Central Telephone Company; Harold W. Shaffer, Regional Settlement Supervisor for the Southern Region of the Mid-Continent Telephone Service Corporation for Mid-Carolina Telephone Company and for the Sandhill Telephone Company; Larry J. Sparrow, Vice President - Revenue Requirements for General Telephone Company of the Southeast; and Phil W. Widenhouse, Executive Vice President and Treasurer, for Concord Telephone Company.

The prefiled statement of David O. Albertson, Secretary-Treasurer and Controller of Citizens Telephone Company, was copied into the record.

The Public Staff offered the testimony and exhibits of Millard N. Carpenter, Engineer - Communications Division, and of Hugh L. Gerringer, Engineer - Communications Divisions.

Based on the foregoing, the evidence adduced at the hearings, and the entire record in this matter, the Commission makes the following

FINDINGS OF FACT

1. Southern Bell and the Independents made parties to this docket are duly franchised public utilities lawfully incorporated and licensed to do business in North Carolina, are providing telephone services in their respective North Carolina service areas, are subject to the jurisdiction of the Commission, and are lawfully before this Commission to establish rates for intrastate MTS, WATS, and interexchange private line services.

2. The public interest requires that intrastate MTS, WATS, and 800 service and interexchange private line service rates and charges be uniform for all telephone companies operating in North Carolina.

3. Southern Bell's proposed changes in the intrastate MTS rate schedules are just and reasonable.

4. Southern Bell's proposed changes in the nonrecurring intrastate WATS rates and charges are just and reasonable except the "Time and Materials" charging basis proposed for premises wiring (installation and maintenance) items, which are inappropriate.

5. Certain increases proposed by Southern Bell in interexchange private line service and foreign exchange service are excessive and unreasonable. Increases in rates and charges for these services should be approved under the recommendations and limitations proposed by the Public Staff.

6. The estimated annual amount of additional gross end-of-test-period intrastate toll revenues subject to toll settlements that will be produced for Southern Bell and the Independents (including the Telephone Membership Corporations - TMCs) combined related to Southern Bell's proposed changes in all intrastate toll rates (MTS, WATS, and interexchange private line) excluding toll directory assistance is $26,030,145. This amount includes 25% of the total effect of repression and associated cost savings as proposed by the Company for the MTS and interexchange private line rates.

7. The method used by both Southern Bell and the Public Staff for distributing the annual additional gross intrastate toll revenues subject to toll settlements resulting from this proceeding among Southern Bell and the Independents is proper and reasonable, resulting in additional gross toll revenues of $14,055,644 for Southern Bell and $11,974,501 for the Independents, including the Telephone Membership Corporations.

8. The increase in nonsettlement revenues resulting from the herein approved rates and charges for interexchange private line service and foreign exchange service is $144,996. Appropriate distribution of these revenues among the jurisdictional companies is shown on Appendix A under the column entitled "Nonsettlement Revenues."

9. Southern Bell's proposal to eliminate the matching plan related to intrastate toll directory assistance (DA) calls should be granted. A rate of $0.20 for each intrastate toll DA request for MTS and WATS with no free allowance calls is just and reasonable and should produce approximately $2,280,701 of additional revenues for Southern Bell. Such amount reflects the effects of the Commission's decision with respect to the DA rate and the recognition of 25% of the Company's associated recommendation on repression and cost savings revenues. All Independent telephone companies should be required to file concurrence tariffs and provide Southern Bell with the necessary data on which Southern Bell can calculate the projected revenue increase which will inure to each company through the settlement pool.

10. The increases derived from the rate changes herein shall be handled as follows: (a) In the pending rate cases for Southern Bell, Continental of North Carolina, Mid-Carolina, and Heins; (b) Increases in toll revenues of $0.25 or less per access line shall be deemed de minimis for North State, Lexington, Ellerbe, Mebane, Pineville, Randolph, Saluda, Service, and Sandhill; and (c) The remaining five companies shall be required to establish a deferred account in which the revenues shall be placed for Barnardsville, Carolina, Central, Citizens, and Concord.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 1

This finding is essentially procedural in nature, was not contested by the parties, and warrants no additional discussion in this Order.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 2

The need for uniform toll rates in North Carolina was not an issue in this docket. This finding is consistent with previous Commission practice and policy.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 3

Southern Bell witness Savage and Public Staff witness Gerringer presented testimony and exhibits regarding Southern Bell's proposed changes in the intrastate MTS rate schedules. Witnesses appearing for the Independents also presented testimony regarding Southern Bell's proposed MTS changes.

Witness Savage testified that the proposed changes in the MTS rates and charges were both fair and reasonable and were designed to more nearly approximate or achieve parity with the interstate MTS rates and charges.

Witness Gerringer testified that Southern Bell proposed the following four changes regarding the intrastate MTS rate schedules:

1. Increasing the add-on charges that apply to all types of operator-handled (OPH) intrastate calls. For Station-to-Station calls, the Customer Dialed Credit (Calling) Card add-on charge is proposed to be increased from $0.30 to $0.50 and the All Other add-on charge is proposed to be increased from $0.70 to $1.25. For all Person-to-Person calls, the add-on charge is proposed to be increased from $1.70 to $2.50. No changes are proposd in the DDD rates which constitute a portion of the rate for OPH calls.

2. Eliminating the present MTS discount that applies on resulting legal holidays. A resulting legal holiday occurs when one of the holidays falls on a Saturday or Sunday and the preceding Friday or following Monday is observed as the legal holiday.

3. Instituting a feature called Rate Period Specific Billing (RPSB). In this proposed feature, the minutes of an MTS call that span two or more rate periods are charged based upon the specific rate period (discounted or nondiscounted) in which those minutes of use occur.

4. Restructuring the MTS Conference Service to simplify the charge plan by charging for each leg of a conference call as a person-to-person call.

Public Staff witness Gerringer testified that the Public Staff was not opposed to Southern Bell's proposed intrastate MTS rate schedule changes since they result in an increase in revenues, which provides a desired contribution to maintain local service rates at a lower level than otherwise would be possible.

Witnesses for the Independents testified in general regarding the toll rate charges proposed by Southern Bell. While the majority of the Independents did not oppose the specific rate change proposals, several questioned the timing of the proposed changes. Carolina Telephone recommended that no toll rate changes be made at this time because of the extensive changes now taking place in the telephone industry such as the divestiture of the Bell System and the F.C.C's adoption of a system of interstate toll access charges and the uncertainties concerning the provision of toll services and future

arrangements for dividing toll revenues. Further, Carolina Telephone recommended that if the Commission did not deny Southern Bell's toll rate proposals, it should continue any decision about the requested increases and their impacts within or after the conclusion of the Commission's investigation in Docket No. P-100, Sub 65 regarding intrastate access charges.

The Commission, having previously denied a motion to consolidate this toll rate proceeding into Docket No. P-100, Sub 65, concludes, based on the evidence and testimony presented in this proceeding, that the changes proposed by Southern Bell in the MTS rate schedules are just and reasonable and, therefore, should be approved.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 4

Southern Bell witness Savage and Public Staff witness Gerringer presented testimony and exhibits regarding Southern Bell's proposed changes in the nonrecurring intrastate WATS rates and charges for both outward WATS and 800 Service (Inward WATS) arrangements. In addition, witnesses for the Independents presented testimony which did not oppose the specific proposed changes.

Witness Savage testified that the nonrecurring WATS charges should be set at levels at least equal to their costs so that the customers whose orders cause the costs to be incurred will be the source of the revenues needed to recover these costs. Therefore, the proposed changes were designed to increase certain of the nonrecurring charges and revise others to a Time and Materials basis. All premises wiring (installation and maintenance) items were to be charged on a Time and Materials basis with a recurring monthly rate option proposed for wiring maintenance for business WATS.

Witness Gerringer testified that the Public Staff opposed only the Time and Materials charging basis proposed for premises wiring items. This opposition was consistent with the Public Staff's position in recent general rate cases for Independent companies regarding similar proposals to charge for local service items on a Time and Materials basis. Witness Gerringer recommended that the present nonrecurring charge for all premises wiring of $8.00 per activity be increased to $20.00, which was in line with other charges proposed in the nonrecurring WATS charges and in line with similar premises wiring charges for private lines and local business lines.

Under cross-examination, witness Savage indicated that premises wiring maintenance charges are presently built into the recurring rate structure on an average basis. However, witness Savage argued that because customers presently have a choice of having maintenance done by Southern Bell, doing the maintenance themselves or having the maintenance done by a contractor other than Southern Bell, it is necessary to get away from an average maintenance price so that Southern Bell will not become the contractor doing all the high cost maintenance jobs at an average rate. In witness Savage's view, a Time and Materials charging basis will solve this potential problem.

Under cross-examination, witness Gerringer offered reasons for opposing the proposed Time and Materials charging basis for premises wiring maintenance. He indicated that the proposal is ill-timed in that the service is still subject to regulation, with potential complaints being directed to the Commission and Public Staff if the Company repairman is not efficient or for

any reason takes more time to complete a job than the customer may think is reasonable. Witness Gerringer further stated that the cost causer is difficult to identify. Even though a problem may occur at a particular residence, the cause of the problem may have been beyond the control of the customer at that residence. Therefore, recovering maintenance costs on average from all customers through recurring rates appears to be more equitable.

Based on the evidence and testimony presented in this proceeding and considering the Commission's decisions in the most recent Carolina Telephone and Central Telephone general rate cases, the Commission concludes that the changes proposed by Southern Bell in the nonrecurring WATS rate schedules, with the exception of the proposed Time and Materials charging for premises wiring items, are just and reasonable and should be approved. In lieu of the proposed Time and Materials Charges, the present $8.00 nonrecurring charge for all premises wiring items should be increased to $20.00.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 5

The Commission's finding on the reasonableness of the proposed rates for interexchange private line service is based on the testimony of Southern Bell witnesses Savage, Hart, and Jordan and Public Staff witness Carpenter.

Witness Savage presented the Company's proposals on interexchange private line services. Witness Savage stated that the proposed rates and charges were based on current cost and that current cost is the appropriate basis for setting rates for these services.

Witness Hart presented the results of the current direct cost study on which the proposed rates were based and described the methodology used in the study. Witness Jordan presented a demand model for private line services. The model apparently covered both intraexchange and interexchange services and all types of private lines on an aggregate basis.

Witness Carpenter presented testimony regarding his review of the Applicant's proposals for interexchange private line service and foreign exchange service. Witness Carpenter concluded that in a number of categories of service Southern Bell's proposed percentage increases in recurring rates were excessive and that the increases in those categories should be limited to a reasonable level, he recommended a limitation of 30%. This 30% ceiling was to be applied to several categories of service which witness Carpenter identified in his exhibits.

Witness Carpenter recommended that, with the exception of the proposed Time and Materials Charges, the increases proposed by Southern Bell in nonrecurring charges be approved. Witness Carpenter concluded that the Time and Materials Charges were unnecessary and would cause uncertainty and inconvenience for the customer and recommended that the proposed charges be rejected.

Witness Carpenter cited lack of adequate support for the proposed increase in the cross-boundary foreign exchange rate and recommended that the present rate of $8.85 per mile remain unchanged.

Regarding Series 5000 channels (Telpak), witness Carpenter recommended that Southern Bell's proposals to obsolete the service immediately and discontinue the service after two years be rejected. Witness Carpenter pointed out that there was no evidence in the record to justify single-channel rates for Telpak offerings and stated that it seemed reasonable to expect that the per channel cost of Telpak would be lower than the cost of a single channel. He also pointed out that the elimination of Telpak in two years as proposed would produce an additional $9.5 million which was not reflected in Southern Bell's proposed revenue to be obtained from private line services. Witness Carpenter concurred in Southern Bell's proposed increases in the Telpak rates which averaged approximately 46%.

Witness Carpenter's testimony indicated that his calculations of the revenue which would be produced by his proposed increases in rates and charges were made without reflecting repression.

The Commission finds that some of the Company's proposed increases in monthly private line rates are excessive and may cause unreasonable burdens on subscribers to these services. The Commission concludes that the recommendation by witness Carpenter to limit to 30% the increase in revenues from witness Carpenter's specifically identified recurring charge categories is reasonable and is required in order to moderate the increases in monthly rates proposed by Southern Bell. The Commission also concludes that witness Carpenter's recommendations on rates for nonrecurring charges, cross-boundary foreign exchange service, and Telpak services are reasonable and should be adopted. The total additional revenue increase resulting from these increases is approximately $7,063,654 which reflects the Commission's decision with regard to the treatment of repression as discussed in the Evidence and Conclusions for Finding of Fact No. 6.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 6

Southern Bell witnesses Savage, Rudisill, Hart, and Jordan and Public Staff witnesses Gerringer and Carpenter presented testimony and exhibits regarding the determination of the estimated annual amount of additional end-of-test-period gross intrastate toll revenues subject to toll settlements that would be produced for Southern Bell and the Independents, including the TMCs, based on Southern Bell's proposed rate changes excluding toll directory assistance charges.

The following tabular summary shows a comparison of the total increase in intrastate toll revenues subject to toll settlements estimated by Southern Bell with those estimated by the Public Staff:

Item	Southern Bell	Public Staff
MTS (OPH add-on, resulting legal holiday, RPSB)	$329,883,573	$345,037,487
	x4.1056858%	x5.85%
Conference service	13,543,983	20,184,693
	(60,558)	(60,558)
MTS total	13,483,425	20,124,135
WATS	276,102	346,982
Interexchange private line	6,253,082	7,517,906
Total for Southern Bell and the Independents combined	$ 20,012,609	$ 27,989,023

Southern Bell's estimate of the additional MTS revenues was presented by witness Savage. Company witness Jordan offered rebuttal testimony concerning price repression and cost savings. Witness Savage used an intrastate toll message sample (including messages for both Southern Bell and the Independents) in order to determine the aggregate percentage increase in intrastate MTS revenues due to three of the four proposed changes in the MTS rate schedules, excluding the restructuring of the MTS Conference Service charges. This increase was determined by comparing the revenues the message sample would produce when priced at the current rates with those when priced at the proposed rates and charges. The results showed a 5.85% aggregate revenue increase. This percentage increase did not take into account the effect of the Company's expectation that a decline in consumer demand would be caused by the higher prices (repression) nor the associated reduction in expenses that would occur when the level of demand for a service is lowered (cost savings). Thus, the Company used an econometric disaggregated repression model to forecast elasticity of demand for the various services. The model produced a result which showed that the proposed rates would yield only a 4.11% increase in revenues, assuming that the increased prices would be in effect during the test year. Southern Bell applied the 4.11% revenue increase determined from the message sample to the actual gross intrastate MTS revenues of $329,883,573 billed during the test period for Southern Bell and the Independents combined, resulting in an annual increase in MTS revenues of $13,543,983. This amount was reduced by $60,558 to reflect the impact of the MTS Conference Service restructuring, resulting in a final annual increase in MTS revenues of $13,483,425.

Public Staff witness Gerringer testified that his estimate of the additional MTS revenues was based on taking the 5.85% increase from Southern Bell's basic message sample approach, excluding the effects of repression and cost savings, and applying it to an end-of-test-period level of gross billed intrastate toll revenues to arrive at an annual increase. According to witness Gerringer, the Company's use of actual gross billed revenues for the test period, is not the same thing as using an end-of-test-period annual amount of MTS revenues and thus Southern Bell's revenue level would be improper. Witness Gerringer testified that, using regression analysis, he determined the end-of-test-period level of gross billed annual revenues for Southern Bell and the Independents combined to be $345,037,487 which, when multiplied by the 5.85% increase, resulted in an annual increase in MTS revenues of $20,184,693. This amount was reduced by the $60,558 related to the restructuring of the MTS Conference Service with the resulting amount of $20,124,135 being the Public Staff's recommendation as to the final annual increase in MTS revenues.

The difference between the WATS amounts shown for Southern Bell and the Public Staff results from differences between the parties proposed rates for the premises wiring nonrecurring charges. The Public Staff's amount of $346,982 includes the revenue impact of increasing the present $8.00 premises wiring charge to $20.00. Southern Bell's amount of $276,102 reflects the revenue impact of that $8.00 charge going to zero. Furthermore, Southern Bell failed to include as part of its WATS revenue increase the revenues associated with its proposal to charge for premises wiring on a Time and Materials basis.

The difference in the parties' amounts of revenue shown for interexchange private lines results from (1) the Public Staff's recommendation of limiting

the amount of revenue increase to be obtained from several categories of service to 30%, (2) other modifications to the proposed rates and charges which the Public Staff recommended including continuation of existing rates for cross-boundary foreign exchange service, and continuation of present charges for installation of premises wiring in lieu of Time and Materials charges proposed by Southern Bell, and (3) the Public Staff's use of a direct priceout for the calculation of the increased revenues due to the proposed changes without estimating, as Southern Bell did, the repression effects due to the proposed increases as used by Southern Bell. The interexchange private line limitations and modifications recommended by the Public Staff are more thoroughly discussed in Evidence and Conclusions for Finding of Fact No. 5.

Regarding the Public Staff's treatment of the effects of repression and cost savings, witness Gerringer stated that his exclusion of these two effects was consistent with the Commission's decisions in preceding toll rate cases. Under cross-examination, witness Gerringer acknowledged that Southern Bell used a disaggregated econometric modeling approach in this case to determine the price repression effects. Apparently this approach was taken in an effort to satisfy the Commission's criticism of the use of an aggregate model in previous toll rate proceedings. Witness Gerringer indicated that the use of the Company's disaggregated models satisfied only one of several criticisms made by the Commission in past cases. According to witness Gerringer, these criticisms related to considering only a price repression effect and not a total repression effect. Nevertheless, the Public Staff did not deny absolutely that repression in fact exists.

The Commission Order in Docket No. P-100, Sub 57 contains an extensive discussion on the subject of repression wherein the Commission expressed a concern that the model used therein was not disaggregated and thus disallowed the effects of repression. The model was said to be disaggregated since there were no specific provisions in the model at that time for the recognition of the various customer classes - residential, commercial, and industrial - nor for the differing aspects of the service such as distance, time of day, and level of operator assistance. In the present case, Southern Bell has developed several disaggregated models, four which are related to MTS specifically addressed concerns voiced by the Commission in the past. For example, one model observed residence service/person-to-person. Another observed business service/person-to-person. A third model was developed and run for residence service/all-station calling. A fourth observed business service/all-station calling. The Company also developed an econometric model to estimate the demand elasticity for interexchange private line services which are proposed for repricing in this proceeding. The Commission concludes that the models used in this proceeding have partially satisfied the criticisms upon which the Commission based its decisions in previous toll rate proceedings. Furthermore, in Docket No. P-100, Sub 57, the Commission expressed concern that "adjustments to the test year for only a price increase overlooks the impacts of other variables...." However, upon examination of the methodology used in the present case, there is a reflection in the actual billed revenue during the test period of other variables reflecting economic activity including the Consumer Price Index, personal income levels, housing starts, gas tax receipts, and so forth.

Cost savings associated with repression have not been included by Southern Bell in preceding toll rate cases; however, cost savings have been included in this proceeding to recognize the changes in expenses that would occur if the

level of demand for a service changed. Maintenance and administrative expenses for toll private line services, operator expenses related to directory assistance and message telecommunications service and gross receipts taxes which will be saved as a result of the estimated repression have been calculated and included in the revenue development by Southern Bell.

Based upon the evidence, the Commission finds that it cannot in this proceeding deny the fact that repression does in fact exist; however, the Commission concludes that Southern Bell has not shown that its determination of the quantification of repression is completely reasonable. Thus, the Commission finds that only 25% of the total effect of repression and associated cost savings as proposed by the Company for the MTS and interexchange private line rates is appropriate for use in this proceeding. Further, having accepted the Public Staff's recommendations regarding proposed changes in MTS, WATS, and interexchange private line rates and charges in Findings of Fact Nos. 3, 4, and 5, agreeing that witness Gerringer's approach for determining end-of-test-period additional MTS revenues is reasonable and recognizing 25% of the effects of repression and cost savings determined based upon the Commission's rate design decisions, the Commission concludes that the total annual additional gross intrastate toll revenues subject to toll settlements that will be produced by the approved changes in intrastate toll rates for Southern Bell and the Independents is $26,030,145, excluding the toll revenue impact of the Commission's DA plan (see Finding of Fact No. 9).

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 7

Southern Bell witness Rudisill and Public Staff witness Gerringer presented testimony regarding the distribution among Southern Bell and the Independents of the estimated annual additional gross intrastate toll revenues subject to toll settlements resulting from this proceeding. Witnesses for several of the Independents settling on an actual cost basis presented testimony regarding this distribution and the amount of additional intrastate toll revenues that each would expect to receive through additional toll settlements. Some of the Independents who presented testimony based their estimates on expectations regarding the impact of the proposed toll rate changes on the intrastate toll settlement ratio along with other changes, including the growth in expenses and pending changes related to merging competition and divestiture of the Bell System, that would affect the settlement ratio and the settlements process.

Company witness Rudisill testified that in estimating the amount of additional toll settlement revenues which would result for each company from the toll rate changes, it was necessary first to estimate the effect on the standard schedule settlement companies of the proposed changes in the MTS and WATS rates. Witness Rudisill indicated that changes in the rates for interexchange private line services would not affect the settlements for the standard schedule settlement companies, since private line settlements for them are determined based on nationwide average cost tables that are related to facility units rather than to billed revenues. Based on Southern Bell's proposals, the total annual settlement increase for all standard schedule settlement companies was $46,793.

Regarding the toll settlement revenue effect of the proposed toll rate changes for cost settlement companies, including Southern Bell, witness Rudisill testified that he had estimated the effect by spreading the balance of the estimated total revenue increase, after settlement effects for the

standard schedule settlement companies had been removed, among the cost settlement companies based on the percent of total net intrastate toll investment each company had as of October 31, 1982. Under Southern Bell's proposals, the annual intrastate toll settlement revenue increase for all cost settlement companies was $19,965,816, of which $10,877,376 was Southern Bell's portion.

During cross-examination, witness Rudisill defended his methodology for distributing the additional gross revenues among the cost settlement companies based on relative net intrastate toll investment versus some other method of distribution, such as that suggested by Carolina Telephone, using relative total intrastate toll revenues received by each cost settlement company during the test period. Witness Rudisill indicated that a representative stable basis was necessary for distributing the additional gross toll revenues and that net toll investment over time provided that degree of stability, whereas using total toll revenues may not be representative for a given period if these total toll revenues happen to be impacted by a large one-time accounting adjustment. Further, witness Rudisill testified that even though his distribution method suggested that the additional revenues for each company would end up as profit, he did not expect that to be the case due to increased expenses and inflation eroding the additional revenues flowing to the bottom line and lowering the settlement ratio. However, witness Rudisill stated that he knew of no precise method to allow for this erosion effect, and thus maintained that distributing the additional gross revenues on net investment was presently the most representative means of determining each company's share of the additional revenues.

Public Staff witness Gerringer testified that he used the same methods used by Company witness Rudisill in distributing the additional toll settlement revenues among Southern Bell and the Independents. However, witness Gerringer's results differed from those of witness Rudisill due to his use of the Public Staff's estimate rather than Southern Bell's estimate of the total additional intrastate toll revenues subject to toll settlements that would be produced by the changes in toll rates proposed by Southern Bell (See Evidence and Conclusions for Finding of Fact No. 6). Applying the distribution methods used by witness Rudisill, witness Gerringer first estimated the increase in intrastate toll settlements for the standard schedule settlement companies to be approximately $287,190 with the qualification that a more accurate determination of this amount should be made based on the Commission's final decision regarding the adjustments and recommendations proposed by the Public Staff.

Witness Gerringer then took the Public Staff's estimate for the total additional intrastate toll revenues of $27,989,023 as indicated in Finding of Fact No. 6 and reduced it by $287,190, leaving a total of $27,701,833. This amount was distributed between Southern Bell and the other cost settlement companies based on relative net intrastate toll investments, resulting in additional intrastate toll settlements of $15,091,959 (54.48%) for Southern Bell and of $12,609,874 (45.52%) for the cost settlement companies.

During cross-examination, witness Gerringer disagreed with the Company's proposition that the cost settlement companies would not necessarily receive the additional gross toll revenues distributed to them by the net investment base method as a result of the erosion of the settlement ratio due to increased expenses and inflation. Witness Gerringer indicated that the

increased expenses may be offset by growth in the toll revenues prior to the toll rate changes. To the extent that the toll rate changes caused no or only a minimal expense increase, witness Gerringer stated there was no reason to conclude that the companies would not receive the additional toll revenues, particularly at a time when the settlement ratio appears to be increasing absent the impact of the proposed toll rate changes. Further, witness Gerringer stated that this proceeding is for the purpose of determining the impact of the proposed intrastate toll rate changes and addresses only changes in the toll revenue factor for determining the division of the toll settlement pool and not changes in the other major factors of expenses and net investment.

Based upon the testimony and evidence presented in this proceeding, the Commission concludes that only additional gross intrastate toll settlement revenues resulting from the proposed toll rate changes are to be considered as a basis for distribution between Southern Bell and the Independents and that the method of distribution as presented by the testimony of witness Rudisill and witness Gerringer is proper and reasonable for use herein resulting in additional gross toll revenues of $14,055,644 for Southern Bell and $11,974,501 for the Independents combined ($11,743,995 - cost settlement companies and $230,506 - standard schedule settlement companies). The Commission further concludes that reductions in these additional gross intrastate toll settlement revenues to reflect the speculation of increased expenses, as presented in the testimony of the witnesses for the Independents settling on an actual cost basis, are not appropriate in this proceeding. Thus, the Commission finds that the additional gross intrastate toll settlement revenues shown for each company in Appendix A are consistent with and result from the application of the distribution methods herein concluded to be proper and reasonable and reflect the effects of the Commission's allowance for 25% of the total effects of repression and associated cost savings.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 8

Public Staff witness Carpenter testified regarding the amount of additional nonsettlement revenue which each independent company would bill and retain as a result of the proposed changes in rates and charges for interexchange private line service and foreign exchange service. Witness Carpenter stated that Southern Bell estimated in Item 31-d of the Minimum Filing Requirements the additional recurring revenue not included in settlements which would result if its proposed rates and charges were approved. Southern Bell did not include estimates of the increase in nonsettlement nonrecurring revenue in Item 31-d. Neither of these amounts was included by Company witness Rudisill in his testimony.

Witness Carpenter estimated the full amount of increase in Independent to Independent (I-I) revenues not included in settlements excluding repression effects. The sum of these nonsettlement revenues for all companies under witness Carpenter's recommendations is $154,321.

The Commission finds that the Public Staff's rate proposals and methodology for estimating the total nonsettlement revenues which the Independents will receive is reasonable and appropriate for use in this proceeding; however, the Commission does not agree with the Public Staff's position on repression and associated cost savings. The Commission concludes that the full amount of

additional nonsettlement annual toll revenue which will result from changes in interexchange private line and foreign exchange rates and charges is $144,996 which reflects the same level of repression as used in the Commission's other private line revenue calculations. The amount of nonsettlement revenue for each jurisdictional company is shown in Appendix A.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 9

Southern Bell witnesses Savage and Rudisill, Public Staff witness Gerringer and witnesses for the Independents presented testimony and exhibits regarding Southern Bell's proposed changes regarding requests for toll (MTS and WATS) directory assistance (DA).

Witness Savage testified that the Company was proposing a charge of $0.35 for each intrastate toll DA request for MTS and WATS. The Company proposed this charge as a nonconcurrence tariff item chargeable only to Southern Bell subscribers and not as an element for inclusion in the revenue settlements pool. Currently, usage associated with WATS DA calls is billed under the WATS recurring charges. Southern Bell proposes to discontinue this billing for WATS DA calls and charge the $0.35 rate per call. Under Southern Bell's proposal, the $0.35 DA charge for MTS and WATS would apply whether or not there were offsetting long-distance calls, and no allowance would apply to these calls. Witness Savage stated that the proposed DA charging plan was necessary to recognize the cost of such requests plus the expected rapid emergence of competitive suppliers for long-distance service. Under cross-examination, witness Savage indicated that there was no DA charging plan for interstate toll DA requests.

Public Staff witness Gerringer testified that, for Southern Bell and all telephone companies in North Carolina, no toll DA charge currently applies for requests from a 919 area code number for a 704 area code number and vice-versa. For toll DA requests within the 919 and 704 home area, no charge applies if the total number of requests is matched by a corresponding number of sent paid home area code toll calls made by the subscriber making the toll DA requests. Presently, if such DA requests are not matched and not covered by the five free call allowance that applies to toll and local DA requests combined, a $0.20 charge per request applies.

Witness Gerringer stated that, since DA changes were not proposed as a concurrence item, no revenues had been developed for the Independents, however Southern Bell did compute a revenue increase based on its subscribers of $3,839,751 which includes the effects of repression and cost savings. Consistent with the Public Staff's position of excluding repression and cost savings, the resulting DA revenue increase would be $3,916,929.

Witness Gerringer recommended that the proposed toll DA charging plan be made a concurrence item for the Independents, that the unrepressed revenue impact of the proposed plan for the Independents be developed and that those revenues plus the unrepressed revenues already developed for Southern Bell of $3,916,929 be subjected to toll settlements.

Under cross-examination, witness Rudisill testified that Southern Bell and the other cost settlement companies presently recover toll DA costs from the settlement pool. Further, witness Rudisill indicated that Southern Bell would not object to making the proposed toll DA charging plan a uniform concurrence

tariff for all the Independents with the resulting revenues being reported to the settlement pool to be distributed. The majority of the witnesses for the Independents also did not oppose this approach. However, Carolina Telephone did oppose the plan, contending that it would create new complaints from customers similar to the high complaint level that resulted at the time the $0.20 charging for DA calls was approved.

Based upon the evidence and testimony presented in this proceeding, the Commission concludes that a rate of $0.20 for each intrastate toll DA request for MTS and WATS with no allowance or matching plan to apply to these calls is the appropriate DA charge for use by Southern Bell. Further, the Commission concludes that the DA plan as approved for Southern Bell should be made a concurrence item for the Independents with the associated toll revenues being reported to the settlement pool for distribution. The Commission finds that the amount of DA toll revenues expected to be collected by Southern Bell from its customers is $2,280,701; such amount reflects the effects of the Commission's decisions with respect to the DA rate and the recognition of 25% of the Company's associated recommendation on repression and cost savings revenues. In order to establish the full revenue impact of this approved DA plan, the Commission is requiring that all affected Independents determine and report the additional partially repressed (25%) toll revenues that would be collected from their customers to be included with Southern Bell's already developed additional toll revenues of $2,280,701 for reporting to the settlement pool. Consequently, these additional total toll revenues will be included with those already developed in Finding of Fact No. 6 to be distributed in like manner among all companies according to the procedures approved by the Commission in Finding of Fact No. 7.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 10

Public Staff witness Gerringer and witnesses for the Independents presented testimony and exhibits regarding the flow-through of the additional intrastate toll revenues estimated to be realized from the changes in the rates and charges approved herein.

Witness Gerringer testified that after the resulting additional intrastate toll revenues, both those subject to toll settlements and those not subject to toll settlements have been accurately determined for each company, the following guidelines should be applied:

1. For each company that has a rate case pending before the Commission or that has filed a rate case before the issuance of the Commission's final decision in this proceeding, the additional revenues for such company should be considered in its rate case. Presently, the following companies have rate cases before the Commission: Southern Bell, Continental of North Carolina, Mid-Carolina, and Heins.

2. An increase in toll revenues of $0.25 or less per access line per month is considered de minimis. Based on this guideline the following companies, provided that they do not qualify under Condition No. 1, are deemed to have de minimis additional revenues and no flow-through is recommended: North State, Lexington, Ellerbe, Mebane, Pineville, Randolph, Saluda, Service, and Sandhill.

The Commission concludes that these guidelines are proper and should be followed.

The Commission considered carefully the following options proposed by Independent Telephone Company witnesses:

1. Allowing no flow-through to local rate reductions,

2. Delaying decisions on the flow-through issue by transferring or considering it in the access charge Docket No. P-100, Sub 65, or

3. Effecting flow-through by rate reductions in other MTS and WATS rates.

The bases for these three options were manifold, including the uncertainty surrounding the divestiture of the Bell System expected to be implemented January 1, 1984, the implementation of access charges and the implication of changes to the existent toll settlements process, and the fear that the settlement ratio increase due to the additional toll revenues would be offset by increasing toll expenses. Witnesses for Carolina Telephone testified that the additional toll revenue estimated to be generated by the toll rate changes approved in Docket No. P-100, Sub 57, did not materialize. One explanation was that poor economic conditions prevailing since the approval of the last toll rate changes have adversely affected toll revenue growth. Regarding the option of flowing through the additional toll revenues by reducing other MTS and WATS rates, these witnesses indicated such flow-through would recognize the fact of competitive pressures and the deloading of toll which is now taking place and will increasingly be necessary.

Under cross-examination, witness Gerringer testified that the Public Staff would not close the door on the option of flowing through the additional toll revenues by reducing other MTS and WATS rates. He indicated that if the Commission approved this approach, the Public Staff would need to study it further. Regarding the fear of whether the estimated additional toll revenues would materialize, witness Gerringer referred to the toll rate proceeding in Docket No. P-100, Sub 45, wherein the additional toll revenues realized exceeded everyone's expectation. Finally, witness Gerringer testified that flow-through for certain companies was necessary to keep the status quo and that only a general rate proceeding could provide a basis for not flowing through significant additional toll revenues resulting from this case.

The Commission concludes that due to the uncertainties posed by deregulation of the telecommunications industry, Barnardsville, Carolina, Central, Citizens, and Concord shall not be required to flow-through at this time. But, within 10 days from the issuance of this Order, each of these companies shall establish a deferred account in which the intrastate toll revenues derived from the rate increase approved herein shall be placed. The deferred account revenues will be considered in any rate case filed within the next 12 months. Approximately one year from the date of this Order, the Commission shall schedule a further hearing to determine the appropriate disposition of the deferred account funds. Each of the aforementioned companies shall file with this Commission a bond or undertaking sufficient to cover the projected additional intrastate toll revenues as set forth in Appendix A.

Moreover, it is the Commission's view that to the extent a company receives less toll or toll related revenue subsequent to December 31, 1983, due solely to changes in the toll settlements process, such company shall be allowed to retain an equivalent amount of revenue arising from the increase approved herein. The Commission will also take into account earnings of the Company. However, as noted above, this issue may be resolved subsequently with respect to an individual company in the context of a general rate case proceeding or collectively by further Order of this Commission.

IT IS, THEREFORE, ORDERED as follows:

1. That Southern Bell Telephone and Telegraph Company and the other telephone companies in North Carolina under the Commission's jurisdiction are hereby authorized to adjust the rates, charges, rules, and regulations of the North Carolina intrastate message toll, WATS, interexchange private line, and foreign exchange services to produce, based upon a test year ended October 31, 1982, additional annual gross revenues of approximately $26,030,145 ($14,055,644 - Southern Bell, $11,974,501 - Independents Combined) in accordance with the conclusions reached herein by the Commission. The Independents combined amount includes revenues to be received by telephone membership corporations concurring in rates and charges herein revised. In addition to Southern Bell being granted a revenue increase of $14,055,644, the Commission has approved $2,280,701 of directory assistance revenues resulting in a $16,336,345 annual gross revenue increase for Southern Bell in this proceeding. As soon as a determination has been made of the amount of the total revenue increase resulting from the DA charges flowing to all regulated telephone companies and TMCs, the revised annual gross revenue total shall be reflected in a further Order of the Commission.

2. That within ten (10) days from the date of this Order Southern Bell shall file the tariffs necessary to reflect the revisions in rates and charges in accordance with Paragraph 1 above. Directory Assistance tariffs applicable to toll services should be filed in Section A18. Work papers supporting such proposals should be provided to all parties of record (formats such as Item 30 of the minimum filing requirements, NCUC Form P-1 are suggested).

3. That all other proposed changes in rates, rate structure, and revenues as proposed by Southern Bell are hereby denied.

4. That the Public Staff and any other intervenor may file written comments concerning the Company's tariffs within ten (10) days of the date upon which the tariffs are filed with the Commission.

5. That the rates, charges, and regulations necessary to reflect the changes authorized herein shall be effective upon the issuance of a further Order approving the tariffs filed pursuant to Paragraph 2 above.

6. That within thirty (30) days from the date of this Order, all Independents shall file with the Commission and Southern Bell, for the purpose of revising the total annual gross revenue increase and finalizing Appendix A, the partially repressed (25%) estimated toll revenue which would be reported to the settlements pool as a result of applying the DA charging plan herein approved by the Commission. All TMCs which will concur in the DA plan are requested to file this information also.

7. That within thirty-five (35) days from the date of this Order, Southern Bell shall file with this Commission the additional settlements revenue for each independent telephone company resulting from the application of the DA charges approved herein.

8. That Barnardsville, Carolina, Central, Citizens, and Concord telephone companies shall establish deferred accounts in which the intrastate revenues derived from the rate increase approved herein shall be placed. That within sixty (60) days from the issuance of this Order, each of the aforementioned companies shall file with this Commission a bond or undertaking sufficient to cover the projected additional intrastate toll revenues as will be reflected in the further Order of this Commission.

9. That for each company that has a rate case pending before the Commission or that has filed a rate case before the issuance of the Commission's final decision in this proceeding, the additional revenues shall be considered in its rate case. Presently, the following companies have filed rate cases: Southern Bell, Continental of North Carolina, Mid-Carolina, and Heins.

10. That provided they do not file rate applications prior to the final decision in this proceeding, the additional revenues of the companies listed below shall be deemed de minimis (i.e., an increase in toll revenues of $0.25 or less per access line per month) and shall not be subject to further investigation: North State, Lexington, Ellerbe, Mebane, Pineville, Randolph, Saluda and Service.

11. That the Public Staff and any other intervenors may file written comments concerning the Companies' DA tariffs within fifteen (15) days of the date upon which the tariffs are filed with the Commission. The changes required herein shall be effective upon the issuance of a further Order approving the tariffs filed pursuant to Paragraph 7 above.

ISSUED BY ORDER OF THE COMMISSION.
This the 14th day of September 1983.

NORTH CAROLINA UTILITIES COMMISSION
Sandra J. Webster, Chief Clerk

(SEAL)

COMMISSIONER TATE DISSENTING

APPENDIX A
Southern Bell Telephone & Telegraph Company

INCREASE IN ANNUAL INTRASTATE TOLL REVENUES RESULTING FROM CHANGES IN MTS, WATS AND INTEREXCHANGE PRIVATE LINE SERVICE* BASED ON TEST YEAR ENDING 10-31-1982

Company	Increase in Settlement Revenues	Increase in Nonsettlement Revenues (I-I Private Line)	Total Revenue Increase
Barnardsville	$ 15,479	$ -	$ 15,479
Carolina	6,581,487	-	6,581,487
Central	1,563,457	80,943	1,644,400
Citizens	98,038	-	98,038
Concord	332,818	28,395	361,213
Continental of N. C.	910,727	-	910,727
Ellerbe	2,161	-	2,161
General	1,166,144	-	1,166,144
Heins	172,857	2,010	174,867
Lexington	31,753	6,113	37,866
Mebane Home	7,428	-	7,428
Mid-Carolina	552,112	19,476	571,588
North State	123,508	8,059	131,567
Pineville	765	-	765
Randolph	4,013	-	4,013
Saluda	-	-	-
Sandhill	6,534	-	6,534
Service	1,465	-	1,465
Southern Bell**	14,055,644	-	14,055,644
Total	25,626,390	144,996	25,771,386
Non-regulated TMCs	403,755	-	403,755
Total all companies	$26,030,145	$144,996	$26,175,141

* Does not include additional revenues resulting from Commission approval of toll D.A. charge plan.

** The Commission has approved $2,280,701 of directory assistance revenues for Southern Bell resulting in a $16,336,345 annual gross revenue increase for Southern Bell in this proceeding.

COMMISSIONER TATE, DISSENTING. I dissent because the revolutionary changes in the telecommunications industry make it impossible for this Commission to set rates that are reasonable and justified for the time period during which the rates are scheduled to be effective.

Due to the introduction of competition in the interstate interexchange services area, the court-ordered divestiture by American Telephone and Telegraph Company of its local operating companies in early 1984, and rapidly developing technology, the telecommunications industry in North Carolina is in early stages of fundamental change, with ultimate results and impacts not fully predictable. These changes render obsolete the partnership between Bell and the "independents" as it has heretofore existed. The settlement agreements, investments, expenses, and the settlement ratio which existed in the test year are not reliable guides for estimating conditions likely to exist when the proposed rates are in effect. It is certainty that the

"settlors" as well as their settlements and the settlement methods in the immediate future will be significantly different from those in the test year. In fact, the majority's treatment of toll revenues as between Bell and the independents differs from past cases and is patently discriminatory.

In the future, it will be required that interexchange services, interstate as well as intrastate, will be cost based, thereby reducing if not eliminating subsidies to local exchange services. Although the benevolent practices of the past have admirably fostered universal service, the Federal Communications Commission and the Federal Courts in their infinite wisdom have decreed that the public will be better served by competition. However distasteful this Commission finds these decisions, federal authority has created an entirely new ball game with new rules and new players. I cannot ignore the consequences that flow from these federal actions and pretend that nothing has changed, as the majority does in this decision. Due to the immeasurable universe of changes which are certain to occur, uniform rates for the immediate future cannot be fixed with any certainty that they will be fair, just, reasonable or even lawful during the time they are to be effective.

In the post-divestiture environment, Southern Bell will be prohibited from providing many of the interexchange private line services it currently provides. Although these services may well be provided by another company, the Commission does not know who that company is or whether that company's cost of providing interexchange private line services will be substantially the same or radically different from the costs of Southern Bell. Accordingly, it is unreasonable to impose rate increases, at this time, on users of interexchange private line services, when those rates are based on costs which, even if valid today, will only be valid for a few short months.

Neither Southern Bell, the Public Staff nor any other party to this proceeding could give the Commission any assurance that the rates proposed for change in this proceeding would be appropriate beyond the January 1, 1984, divestiture deadline. Although rates in this state are based on historical test period operations, rate schedules are set with an eye no less toward the future than to the past. The General Statutes contemplate that the Commission will consider probable future revenues and expenses in setting rates for the future. Utilities Commission v. Edmisten, 291 NC 327, 230 SE 2d 651 (1976). All amounts utilized in this docket are annualized numbers designed to be recovered over the next twelve months after the tariffs take effect. However, the existing settlement process will be terminated as of the date of divestiture, which could result in all revenue numbers used herein being overestimated by approximately 75%.

Ratemaking is by its very nature a balancing act requiring the Commission always to balance the interest of the companies against the interest of the public. This case is no exception. On the one hand, the majority desires to maximize intrastate toll revenues, to the extent practicable, since this tends to reduce local service rates for Southern Bell's local subscribers. On the other hand, the majority cannot now know what the impact of its decisions will be on the independent companies and their customers particularly in view of the anticipated cancellation of existing settlement contracts before the end of 1983 and the revenue uncertainty which that produces.

It may well be that the intrastate toll rates will need to be adjusted, upward or downward, in the future but the public interest requires that those

decisions be postponed until the divestiture is finalized and the access charge and division of revenue questions are resolved. At that time the Commission will be able to ascertain the appropriate costs for setting rates. The majority has adopted the maxim of Justice Holmes: "We have no concern with the future. It has not come yet." Union Trust Co. v. Grosman, 245 U.S. 412, 417 (1918). But the revolution in telecommunications has already begun and I believe we are bound by the law to take it into account. I agree with Justice Frankfurter: "We cannot as judges be ignorant of that which is common knowledge to all men." Sherrer v. Sherrer, 334 U.S. 343, 366 (1948).

Sarah Lindsay Tate, Commissioner

DOCKET NO. P-100, SUB 64

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Investigation of Intrastate Long Distance, WATS, and Interexchange Private Line Rates of All Telephone Companies Under the Jurisdiction of the North Carolina Utilities Commission) ORDER SETTING RATES

BY THE COMMISSION: On September 14, 1983, the Commission issued an Order Allowing Increase and Requiring the Filing of Rates for Intrastate Toll Service in this docket. The Order required Southern Bell Telephone and Telegraph Company to file appropriate revised tariffs reflecting additional gross revenues of $26,030,145. The Public Staff and other intervenors were allowed ten (10) days to file written comments concerning the revised tariffs.

On September 15, 1983, Southern Bell filed tariffs reflecting the revised rates and charges allowed in the September 14, 1983, Order. On September 20, 1983, the Public Staff filed a letter to the Chairman stating that the proposed tariffs comply with the Commission's guidelines as set forth in the September 14, 1983, Order.

On September 16, 1983, Southern Bell filed an Undertaking, a Notice to Customers and a Motion for Approval of same. The Undertaking and Notice in pertinent part provides that "Southern Bell has notified the Commission that it will place into effect so much of the proposed schedules of rates and charges which are set forth in Attachment A of Southern Bell's Application of February 8, 1983; as allowed by G.S. 62-135, such rates and charges to be placed into effect being those approved by the Commission in its Recommended Order of September 14, 1983, in this proceeding which, in fact, do not result in an increase of any more than twenty percent (20%) for any single rate classification, i.e., MTS, Interexchange Private Line, and WATS and like service." Southern Bell proposed to make the rates efffective on and after September 24, 1983.

On September 19, 1983, the Public Staff filed a motion asserting that the Commission should follow its long-standing practice and policy of implementing uniform toll rates statewide. To maintain this uniformity, the Public Staff's motion requested that pursuant to G.S. 62-130 and G.S. 62-134, the Commission authorize all regulated telephone companies to place into effect the same rates and charges approved in its Recommended Order issued September 14, 1983, effective at 12:01 a.m., September 27, 1983.

The Commission is of the opinion that good cause exists to grant the Public Staff's motion.

IT IS, THEREFORE, ORDERED as follows:

1. That the rates and charges filed in this docket by Southern Bell on September 15, 1983, are herein approved to become effective at 12:01 a.m., September 27, 1983.

2. That all regulated telephone companies are authorized to place into effect the rates herein approved effective at 12:01 a.m., September 27, 1983.

3. That all regulated telephone companies, except those whose revenues were designated de minimis in the September 14, 1983, Order, shall file within five (5) days from the issuance of this Order a bond or undertaking sufficient to cover the projected additional revenues.

4. That all regulated telephone companies shall give public notice of the approved rate change within 45 days of the effective date of the Commission Order or in the next billing cycle.

5. That all rates and charges collected under the provisions of this Order shall be subject to refund pending a final order in this docket.

ISSUED BY ORDER OF THE COMMISSION.
This the 20th day of September 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sandra J. Webster, Chief Clerk

DOCKET NO. P-100, SUB 64

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Investigation of Intrastate Long-Distance WATS and Interexchange Private Line Rates of all Telephone Companies Under the Jurisdiction of the North Carolina Utilities Commission) ORDER

BY THE COMMISSION: On September 14, 1983, the Commission issued a Recommended Order Allowing Partial Increase and Requiring the Filing of Rates for Intrastate Toll Service in the above-captioned docket. Ordering paragraph number 1 concluded that as soon as a determination had been made of the amount of the total revenue increase resulting from the Directory Assistance charges flowing to all regulated telephone companies and the Telephone Membership Corporation, the revised annual gross revenue total would be reflected in a further Order of the Commission. On November 28, 1983, Southern Bell Telephone and Telegraph Company filed with the Commission for each independent telephone company and for the Telephone Membership Corporation the additional settlements revenue resulting from the application of the directory assistance charges approved in this docket.

It is the conclusion of this Commission that good cause exists to accept the $4,065,447 estimated Intrastate Toll Directory Assistance Revenues for test period ending October 31,1982.

IT IS, THEREFORE, ORDERED that the estimated directory assistance revenues as submitted in the Southern Bell Report filed in the above-captioned docket on November 28, 1983, are hereby accepted.

ISSUED BY ORDER OF THE COMMISSION.
This the 6th day of December 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sandra J. Webster, Chief Clerk

DOCKET NO. P-100, SUB 65

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Investigation to Consider the Implementation of a Plan for Intrastate Access Charges for All Telephone Companies Under the Jurisdiction of the North Carolina Utilities Commission) ORDER ESTABLISHING INTERIM OPERATING PROCEDURES

HEARD IN: Commission Hearing Room 217, Dobbs Building, Raleigh, North Carolina, on October 11-14, October 18-21, 1983, and November 3 and 4, 1983

Superior Courtroom, Fifth Floor, Buncombe County Courthouse, Courthouse Plaza, Asheville, North Carolina; Commissioners Board Room, Fourth Floor, County Office Building, Charlotte, North Carolina; Commission Hearing Room 217, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina; Superior Courtroom, New Hanover County Courthouse, Corner of Third and Princess Streets, Wilmington, North Carolina; and Council Chambers, Third Floor, Administrative Offices Complex, One Governmental Plaza, Rocky Mount, North Carolina, on Monday, October 17, 1983

BEFORE: Chairman Robert K. Koger, Presiding; and Commissioners Sarah Lindsay Tate, Edward B. Hipp, A. Hartwell Campbell, Douglas P. Leary, and Ruth E. Cook

APPEARANCES:

For Southern Bell Telephone and Telegraph Company:

R. Frost Branon, Jr., General Attorney, Southern Bell Telephone and Telegraph Company, P.O. Box 30188, Charlotte, North Carolina 28230

Hubert F. Owens, Solicitor, Southern Bell Telephone and Telegraph Company, 675 West Peachtree Street, N.E., Atlanta, Georgia 30375

Robert C. Howison, Jr., Hunton & Williams, Attorneys at Law, P.O. Box 109, Raleigh, North Carolina 27602

For Carolina Telephone and Telegraph Company:

Dwight W. Allen, Vice President, General Counsel, and Secretary, Carolina Telephone and Telegraph Company, 720 Western Boulevard, Tarboro, North Carolina 27886

Robert C. Voigt, Senior Attorney, Carolina Telephone and Telegraph Company, 720 Western Boulevard, Tarboro, North Carolina 27886

For General Telephone Company of the Southeast:

Dale Sporleder, Vice President - General Counsel and Secretary; Wayne L. Goodrum, Associate General Counsel; and Joe W. Foster, Attorney, General Telephone Company of the Southeast, P.O. Box 1412, Durham, North Carolina 27702

For Continental Telephone Company of North Carolina and Mid-Carolina Telephone Company:

F. Kent Burns, Boyce, Mitchell, Burns & Smith, P.A., Attorneys at Law, P.O. Box 2479, Raleigh, North Carolina 27602

For Central Telephone Company:

James M. Kimzey, Kimzey, Smith, McMillan & Roten, Attorneys at Law, 506 Wachovia Bank Building, P.O. Box 150, Raleigh, North Carolina 27602

For AT&T Communications of the Southern States, Inc.:

Wade H. Hargrove, Tharrington, Smith & Hargrove, Attorneys at Law, P.O. Box 1151, Raleigh, North Carolina 27602

Gene V. Coker, General Attorney, AT&T Communications of the Southern States, Inc., 1200 Peachtree Street, N.E., Atlanta, Georgia

For Concord Telephone Company:

John R. Boger, Jr., Williams, Boger, Grady, Davis & Tuttle, P.A., Attorneys at Law, P.O. Box 810, Concord, North Carolina 28025

For the Public Staff:

James D. Little, Chief Counsel; Paul L. Lassiter, Staff Attorney; Vickie L. Moir, Staff Attorney; Antoinette R. Wike, Staff Attorney, Public Staff - North Carolina Utilities Commission, P.O. Box 991, Raleigh, North Carolina 27602
For: The Using and Consuming Public

For The Attorney General:

Karen E. Long, Assistant Attorney General, and Jo Anne Sanford, Special Deputy Attorney General, North Carolina Department of Justice, P.O. Box 629, Raleigh, North Carolina 27602
For: The Using and Consuming Public

For Bernice Dill, et al.

Margot Roten, North Carolina Legal Services Resource Center, Inc., P.O. Box 1658, Raleigh, North Carolina 27602

Daniel V. Besse, Pamlico Sound Legal Services, Inc., P.O. Box 1045, New Bern, North Carolina 28560

Douglas A. Scott, Central Carolina Legal Services, Inc., P.O. Box 3467, Greensboro, North Carolina 27401

Richard M. Klein, Farmworkers Legal Services of North Carolina, P.O. Box 1229, Raleigh, North Carolina 27602

For Citizens Telephone Company and Tarheel Association of Radiotelephone Systems, Inc.:

Thomas R. Eller, Jr., Attorney at Law, Suite 205, Crabtree Center, 4600 Marriott Drive, Raleigh, North Carolina 27612

For North Carolina Textile Manufacturers Association, Inc.:

Jerry B. Fruitt, Attorney at Law, P.O. Box 2507, Raleigh, North Carolina 27602

BY THE COMMISSION: On April 19, 1983, the Commission issued an Order Instituting Investigation in this docket to consider the implementation of a plan for intrastate access charges. This Order made Southern Bell and the Independent Telephone Companies under the Commission's jurisdiction parties, requested AT&T and ATTIX to participate, required Southern Bell along with ATTIX to file a detailed statement of their intentions, required the filing of comments by other jurisdictional companies, the Public Staff, and other interested parties by the dates set therein, and noted that the Commission would issue such further Orders as required, including the scheduling of evidentiary hearings.

Pursuant to the Commission's April 19, 1983, Order, statements or comments were filed by the following: Southern Bell Telephone and Telegraph Company, Bell System Southern Interexchange Organization, the Town of Pineville, Central Telephone Company, General Telephone Company of the Southeast, Carolina Telephone and Telegraph Company, Lexington Telephone Company, Concord Telephone Company, Barnardsville Telephone Company, Service Telephone Company, Mebane Home Telephone Company, Randolph Telephone Company, Saluda Mountain Telephone Company, Citizens Telephone Company, Ellerbe Telephone Company, the Carolina-Virginia Telephone Membership Association, Inc., Mid-Carolina Telephone Company, Sandhill Telephone Company, MCI Telecommunications Corporation, Heins Telephone Company, the Combined Network, Inc., GTE Sprint, and the Public Staff.

The following Motions for Intervention were also filed with the Commission: North Carolina Textile Manufacturers Association, Inc. (NCTMA), Carolina-Virginia Telephone Membership Association, Inc., Bernice Dill, et al., and Tarheel Association of Radiotelephone Systems, Inc. (TARS).

The Commission issued Orders on various dates in response to these petitions to intervene. Any such motion for intervention not previously ruled upon is hereby allowed.

The Public Staff and the Attorney General filed Notices of Intervention, which are deemed recognized. By Motions filed on July 20 and 25, 1983, the Public Staff requested the Commission to schedule an evidentiary hearing in this matter, establish filing dates, and require public notice.

On July 28, 1983, the Commission issued an Order Scheduling Hearing and Requiring Public Notice. By that Order the Commission: set the matter for evidentiary hearing as a complaint proceeding to develop an intrastate access charge plan and establish guidelines for the implementation of such a plan; scheduled the hearing to begin on Tuesday, October 11, 1983; scheduled a pre-trial conference for Monday, October 3, 1983; set a date for Southern Bell and the Bell System Southern Interexchange Organization to file testimony and tariffs; set dates for the Independent Telephone Companies, the Public Staff, and other intervenors to file testimony; and required the giving of public notice.

On September 6, 1983, a letter was filed with the Commission, giving notice that the name of the Bell System Southern Interexchange Organization had been changed to AT&T Communications (ATTCOM).

By motion filed on September 15, 1983, the Attorney General requested that night hearings be held in Raleigh and Asheville and that adequate public notice of the hearings be required.

On September 22, 1983, the Commission issued an Order scheduling public hearings at night on Monday, October 17, 1983, in Asheville, Charlotte, Raleigh, and Wilmington and requiring public notice. By Commission Order issued September 27, 1983, an additional night hearing was scheduled to be held in Rocky Mount simultaneously with the other night hearings previously scheduled and the public notice was required to be amended accordingly.

A pre-trial conference was held on October 3, 1983, and a Pre-Trial Order was issued by the Commission on October 7, 1983.

Prior to and during the course of the hearings, motions were made and orders entered relating thereto, all of which are a matter of record.

Public hearings were held as scheduled by the Commission for the specific purpose of receiving testimony from public witnesses. The following persons appeared and testified:

Charlotte: C. T. White, Marshall Howard, and Monroe T. Gilmer

Rocky Mount: Katie Roberson, Minerva Banks, Walter Williams, Joe Moody, Norma Bryan, Cynthia Arnold, Josephine Garris, and Sarah May

Wilmington: John Fitzpatrick, Robert Richard Hughes, Sr., Ernest F. Yott, Jr., and Beasley Harry

Asheville: Ed Bradley, Fred Sealey, Horace Reeves, Grace McElreath, Henry Suthard, Madeline Brookshire, George Ingle, Juanita Jones, Mary Hensley, Calvin W. McCurry, Sidney L. Hodges, Jr., Scott Dedman, Helen T. Reed, and Joe Morgan

Raleigh: Ada J. Hooker, Ellen Winston, Lula Chambers, Doris Hanford, Fannie Graves, Gale Hawks, Elisha Wolper, Maria Cuttina, Michael Soehnlein, Jane Rogers Montgomery, David B. Stevens, and Joseph Reinckens

As previously ordered, the case in chief was heard in Raleigh beginning on October 11, 1983.

Southern Bell presented the testimony and exhibits of the following witnesses: Allen K. Price - District Staff Manager; Harold M. Raffensperger - District Staff Manager in Service Costs; Robert C. Hart, Jr. - District Staff Manager in Service Costs; O. Lee Prather, Jr. - District Staff Manager in Service Costs; W. Whitard Jordan - District Staff Manager - Rates and Costs; Donald L. Eargle - District Staff Manager - Network Planning; and Robert T. Burns - Division Staff Manager, Bell - Independent Relations.

Carolina Telephone and Telegraph Company presented the testimony and exhibits of T. P. Williamson, Vice President - Administration for the Company.

Central Telephone Company presented the testimony and exhibits of R. Chris Harris, Manager - Operations Planning.

Concord Telephone Company presented the testimony of Phil W. Widenhouse, Executive Vice-President.

Continental Telephone Company presented the testimony and exhibits of Earle A. Mackenzie, Revenue Requirements Manager for Contel Service Corporation.

General Telephone Company of the Southeast presented the testimony and exhibits of Joseph W. Wareham, Business Relations Director.

Mid-Carolina Telephone Company and Sandhill Telephone Company presented the testimony of Harold W. Shaffer, Regional Settlements Supervisor - Southern Region of Mid-Continent Service Corporation.

ATTCOM presented the testimony and exhibits of James A. Tamplin, Jr., Staff Supervisor in the Engineering Department of Southern Region of AT&T Long Lines; Lawrence R. Weber, Vice President - External Affairs for Southern Bell and designated Vice President - External Affairs for the Southern Region of ATTCOM; and Marion R. McTyre, District Manager.

The Attorney General presented the testimony of Dr. John W. Wilson, President of J. W. Wilson & Associates, Inc.

The Public Staff presented the testimony and exhibits of Gene A. Clemmons, Director - Communications Division; Millard N. Carpenter, III, Engineer -

Communications Division; and Hugh L. Gerringer, Engineer - Communications Division.

The Carolina/Virginia Telephone Membership Corporation presented the testimony of A. William McDonald, General Manager of Yadkin Valley Telephone Membership Corporation.

The NCTMA presented the testimony and exhibit of Louis R. Jones, Telecommunications Analyst, Corporate Communications Department, Burlington Industries, Inc.

TARS presented the testimony and exhibits of Allen L. Guin, President of Two-Way Radio of Carolina at Charlotte.

Based upon a careful consideration of the foregoing and the entire record in this proceeding, the Commission makes the following

FINDINGS OF FACT

1. The telephone companies which have participated as parties in this docket are subject to the jurisdiction of this Commision.

2. AT&T Communications of the Southern States, Inc., has applied for a certificate of public convenience and necessity in Docket No. P-140 to provide telecommunications services in North Carolina. ATTCOM is subject to the jurisdiction of this Commission.

3. At the present time, 20 regulated telephone companies and nine unregulated telephone membership corporations (TMCs) furnish equipment and facilities jointly to provide an integrated statewide toll network in North Carolina. The major services provided by this toll network are message telephone service (MTS), WATS, and private line service.

4. Under the present partnership arrangement, intrastate toll revenues collected from customers are pooled for division among the telephone companies to recognize the costs incurred by each in participating in the partnership. These divided toll revenues are known as toll settlements.

5. Southern Bell Telephone and Telegraph Company has acted historically as a clearing house for toll settlements. The Independent Telephone Companies and the TMCs settle with Southern Bell on either a standard schedule basis or an actual cost basis.

6. Each "actual cost" company's revenues, investment, expenses, taxes, and reserves are allocated to the intrastate toll and local jurisdictions through what are known as separations procedures. These procedures are set out in the February 1971 Separations Manual published by the Federal Communications Commission (FCC) and adopted by the FCC as Part 67 of its Rules in Docket No. 18866, Report and Order of October 27, 1970, and revised in Docket No. 80-286, Decision and Order adopted February 24, 1982. Each company receives settlements to cover its cost of providing toll service plus a return, referred to as the settlement ratio, on its net toll investment.

7. Each "standard schedule" company receives toll settlements based on sample cost studies performed by companies throughout the United States using

the accepted separations procedures. These studies result in a schedule of settlements related to average revenue per message.

8. The present intrastate toll arrangement in North Carolina has provided telephone subscribers with efficient and reliable toll service at reasonable, uniform rates. In addition, it has provided a contribution to overall telephone company revenue requirements which has allowed local rates to remain affordable to the majority of subscribers.

9. In compliance with the Modification of Final Judgment (MFJ) in United States v. American Telephone and Telegraph Co., 552 F. Supp. 131 (D.D.C. 1982), affirmed per curium sub nom. Maryland v. United States, ____ U.S. ____, 103 S. Ct. 1240 (1983), and in accordance with the Plan of Reorganization (POR) submitted to the U.S. District Court, Southern Bell will transfer its assets used to provide interexchange (interLATA) service in North Carolina to a wholly owned subsidiary, AT&T Communications of the Southern States, Inc., which will itself become a wholly owned subsidiary of American Telephone and Telegraph Company (AT&T).

10. Under the MFJ, Southern Bell will only be permitted to provide exchange or interexchange service within a LATA. LATAs or Local Access and Transport Areas define the geographical areas in which Bell operating companies, such as Southern Bell, are permitted by the MFJ to conduct business. There are five court-approved Southern Bell LATAs in North Carolina, with which the Independent Telephone Companies have been associated for purposes of classifying Bell-Independent traffic in order to determine the proper division of Bell System assets. No pooling of revenues or costs between Southern Bell and ATTCOM will be allowed. Instead, ATTCOM will provide interLATA service and Southern Bell will bill ATTCOM through a system of tariffed access charges for exchange access or intraLATA facilities used to complete a call.

11. The decision of the Federal Communications Commission in Docket No. 78-72, Third Report and Order issued February 28, 1983, requires the determination and use of access charges for access to the local network provided by the local telephone companies for interstate traffic of interexchange carriers but does not dictate charges in the provision of North Carolina intrastate toll or local service; nor does it dictate the use of end-user access charges of any kind for intrastate service.

12. The implementation date of the FCC's decision in Docket 78-72 has been extended until April 3, 1984, by FCC Order No. 83-1145, issued October 19, 1983.

13. There is no requirement to mirror the FCC end-user access charge tariff in North Carolina at this time.

14. The MFJ approving divestiture of the Bell Operating Companies (BOCs) from AT&T does not require imposition of an end-user access charge in North Carolina.

15. Presently Southern Bell, AT&T, and the Independents have contracts with the radio common carriers (RCCs) which set the rates to be charged, subject to Commission approval, and which recognize the RCCs as local common carriers. These arrangements have worked well in the past and are not prohibited by either the MFJ or the FCC's order in Docket 78-72 from continuing in the future.

16. The Fayetteville and Rocky Mount areas of the Carolina Telephone and Telegraph Company's service area should be recognized as separate and distinct Geographic Market Areas (GMAs or LATAs in Bell System terminology).

Whereupon, the Commission reaches the following

CONCLUSIONS

1. North Carolina has historically been well served by the present arrangement of uniform intrastate toll rates for the reason that intrastate toll rates contribute to the overall revenue requirements of the telephone companies operating in North Carolina, thus allowing local rates to remain affordable to most North Carolina telephone subscribers. Toll service, at the same time, has remained reasonably priced, efficient, and reliable. The present system, therefore, should be changed no more than absolutely necessary in order to implement divestiture.

2. The evidence clearly shows in this case that there is presently great uncertainty at the federal level concerning the implementation of interstate access charges and how interstate toll settlements will be handled in the post divestiture period. Originally, the FCC ordered interstate access charges to become effective on January 1, 1984. However, by order issued October 19, 1983, in FCC Docket 83-1145, the FCC suspended the effective date of all access and divestiture related tariffs until April 3, 1984, set the matter for notice, comment and investigation, and also continued the existing toll settlement agreement and division of revenues procedure during the period of delay. On December 1, 1983, Judge Greene issued an order stating that the FCC-ordered delay of the implementation of interstate access charges and the continuation of the existing settlement arrangement was in violation of the MFJ but that he would permit a waiver until April 3, 1983. Meanwhile, numerous bills have been introduced in Congress that would delay or prohibit the implementation of interstate access charges on residential and small business customers. As it now stands, no one can be sure what access charge tariffs will be approved by the FCC on April 3, 1984, even assuming Congress does not act to prohibit such charges. In addition, no one knows how interstate toll settlements between AT&T, the BOCs, and the Independents will be handled in the post-divestiture period.

3. All of the telephone companies offering testimony contended that the access charge tariffs approved by this Commission should mirror those approved for them by the FCC; in other words, that their intrastate and interstate access charges should be the same. No company presented evidence that its interstate and intrastate access costs are identical. Testimony given by witness Price suggests that for Southern Bell, at least, interstate costs are higher.

The Commission recognizes the administrative burdens on all of the telephone companies which will follow from implementation of our ultimate decision regarding access charges. It is the Commission's intention that the plan we adopt should be fair and workable and that its benefits should justify its costs. Nevertheless, factors which may warrant a particular level and structure of access charges in the interstate arena may well have little relevance to telecommunicatins in North Carolina. For instance, we note the absence of lawful competition in the North Carolina intrastate toll market.

It is clear, moreover, that this Commission's objectives in establishing an intrastate carrier access charge plan are certainly not shared by the FCC. Nor are the FCC orders which have been entered in FCC Docket 78-72 providing for interstate toll end-user access charges binding upon or determinative of North Carolina intrastate toll rates or local service tariffs.

As to the other elements related to the proposed access charge plans presented in this hearing, the Commission will rule on these matters in a further Order prior to April 3, 1983.

4. After considering the evidence in this case, the Commission concludes that intrastate end-user access charges are not justified for implementation in North Carolina nor are they otherwise warranted. The basic theory offered by the proponents of end-user access charges is that such charges are needed to generate revenues to cover the cost of local service that toll revenues are now allegedly subsidizing so that toll rates can be reduced, thereby allowing toll carriers to meet competition. This theory is invalid for a number of reasons. The law in North Carolina does not presently permit or authorize competition in the intrastate toll market. In addition, the record in this case clearly shows that toll revenues have been constantly increasing. It is also important to note that many of the companies in this proceeding have not proposed intrastate end-user access charges. Based on the evidence, therefore, the Commission concludes that intrastate end-user charges should not be imposed. Such conclusion is consistent with the Commisison's objective to make only the minimum changes required by the MFJ. Certainly nothing in the MFJ or orders of the FCC requires intrastate end-user access charges. Finally, in making our decision, the Commission is also influenced by the possibility that end-user charges could drive certain marginal income customers off the telephone system, thereby undermining universal service. The Commision is unwilling to take such a drastic step as imposing end-user access charges until it is adequately demonstrated that such charges are needed.

5. Accordingly, the Commission is of the opinion and concludes that as of the beginning date of divestiture of the Bell System and continuing until the actual implementation of intrastate carrier access charges by this Commission, toll settlements should be conducted on an interim basis under a contractual arrangement as done presently but including ATTCOM. The Commission makes this conclusion in recognition of the fact that all companies cannot have appropriate carrier access charges filed for implementation on January 1, 1984. In fact, it is clear that additional time is required for the Commission to develop guidelines which will be sufficient to assist in the development of such charges. (The Commission again notes the FCC's order delaying the implementation of interstate access charges until April 3, 1984.) Some method of settlements, therefore, must be used in the interim period immediately following divestiture on January 1, 1984, and prior to the implementation of intrastate carrier access charges. The Commission is of the opinion that a continuation of the present settlement arrangement, with the inclusion of ATTCOM, is the easiest and best way of handling such settlements. This conclusion is based on the fact that the present settlement process is already in effect, is understood by all the companies, and can be modified to deal with toll settlements in the interim period. Such an interim arrangement is also consistent with the MFJ.

The Commission will soon enter a further Order in this docket with regard to the design and implementation of intrastate carrier access charges.

6. The Commission has given much consideration to the issue, put forth by Carolina Telephone and Telegraph Company (Carolina), as to whether or not Carolina's service area should be recognized as two separate GMAs. Criteria for establishing LATAs within the Bell System, such as population centers, the number of telephones, geographic size, the distance between cities, and existing telephone network configuration serve to establish the conclusion that the Carolina service area should be recognized as two separate and distinct GMAs. The Commission further notes that Carolina's existing network tends to center on Rocky Mount and Fayetteville, and that there is substantial distance separating Rocky Mount and Fayetteville from the core cities of the adjacent Southern Bell LATAs (i.e., Raleigh and Wilmington). Therefore, based on the foregoing, and the entire record, the Commission concludes that Carolina's service area should be considered to be comprised of two distinct GMAs, exceept those exchanges associated with Southern Bell LATAs.

7. Southern Bell Telephone and Telegraph Company, through its proposed access charge tariff, proposes to classify certificated radio common carriers as interLATA long-distance carriers, terminate existing privately negotiated interconnections and traffic interchange contracts, and thus make RCCs subject to new tariff offerings for Switched Access Service offerings (available only to RCCs) and Special Access Offerings for connections between RCC terminals and base station transmitters.

Based on the evidence in this case, the Commission concludes that the RCCs should not be charged access charges at this time. Further, the Commission concludes that the RCCs' interconnection rates should be determined for the future using the same parameters and concepts that are currently applied under the Commission's rules and procedures.

IT IS, THEREFORE, ORDERED as follows:

1. That, beginning on the date of divestiture of the Bell System and continuing until the implementation of intrastate carrier access charges by this Commission no later than April 3, 1984, toll settlements shall be conducted under a contractual arrangement as done presently, but including ATTCOM in the toll settlement process.

2. That intrastate carrier access charges shall be implemented upon further Order of this Commission.

3. That all intrastate access charges filed heretofore in this and associated dockets be, and hereby are, suspended, pending further Commission Order.

4. That access charges shall not be applicable to RCCs at this time.

5. That RCC interconnection rates should be determined consistent with decretal paragraph 4 above and past Commission procedures and practices concerning this issue.

6. That Carolina Telephone's service area (except those associated with a Southern Bell LATA) shall be divided into two geographic market areas, as proposed by Carolina Telephone.

7. That intrastate toll rates presently in effect shall remain in effect, consistent with decretal paragraph 1 above, until further Commission Order.

ISSUED BY ORDER OF THE COMMISSION.
This the 16th day of December 1983.

NORTH CAROLINA UTILITIES COMMISSION
Sharon A. Credle, Deputy Clerk

(SEAL)

DOCKET NO. E-22, SUB 274

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Town of Kill Devil Hills,)
Complainant,)
v.) ORDER
Virginia Electric and Power Company,)
Respondent)

HEARD IN: Meeting Room, Municipal Building, U.S. 158 By-Pass, Kill Devil Hills, North Carolina, on February 7 and 8, 1983

Commission Hearing Room, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina, on February 9 - 11, and February 15 - 17, 1983

BEFORE: Commissioner A. Hartwell Campbell, Presiding; and Commissioners Edward B. Hipp and Leigh H. Hammond

APPEARANCES:

For the Complainant:

John G. Gaw, Jr., Attorney at Law, P.O. Box 1895, Kill Devil Hills, North Carolina 27948
For: The Town of Kill Devil Hills

For the Respondent:

Odes L. Stroupe, Jr., and John R. McArthur, Hunton and Williams, Attorneys at Law, P.O. Box 109, Raleigh, North Carolina 27602
For: Virginia Electric and Power Company

For the Intervenors:

Robert W. Lehrer, N.C. Department of Natural Resources and Community Development, Office of Legal Affairs, P.O. Box 27687, Raleigh, North Carolina 27611
For: North Carolina Department of Natural Resources and Community Development

Norman W. Shearin, Jr., Shearin and Archbell, Attorneys at Law, P.O. Box 269, Kitty Hawk, North Carolina 27949
For: The Nature Conservancy

Robert H. Bennink, Jr., Assistant Attorney General, and Jo Anne Sanford, Special Deputy Attorney General, North Carolina Department of Justice, P.O. Box 629, Raleigh, North Carolina 27602
For: The Using and Consuming Public

James D. Little, Chief Counsel and G. Clark Crampton, Staff Attorney, Public Staff - North Carolina Utilities Commission,

P.O. Box 991, Raleigh, North Carolina 27602
For: The Using and Consuming Public

On January 27, 1983, the Town of Kill Devil Hills (the Town), filed a complaint with the North Carolina Utilities Commission seeking a temporary restraining order to prevent Virginia Electric and Power Company (Vepco) from construction of Vepco's new 115 Kv transmission line through the Town. The Complainant also sought an order requiring (1) a relocation of Vepco's new transmission line from its proposed route along the sound side portion of the Town to a right of way along U.S. 158 by-pass, and (2) a permanent injunction against Vepco's constructing its new transmission line anywhere within the Town limits except within the U.S. 158 by-pass right of way. As grounds for such relief, the Town alleged that Vepco was in violation of a Town zoning ordinance and that Vepco had acted in an arbitrary and unreasonable manner in constructing its new transmission line on its proposed route.

Also on January 27, 1983, the North Carolina Attorney General (the Attorney General), and the Public Staff of the North Carolina Utilities Commission (the Public Staff), filed notices of intervention on behalf of the using and consuming public. Both the Attorney General and the Public Staff filed pleadings supporting the Town's request for immediate injunctive relief.

On that same day, the North Carolina Department of Natural Resources and Community Development (NRCD), filed a petition to intervene alleging that Vepco was constructing its new transmission line through the Nags Head Woods National Landmark, which has been designated a Natural Heritage Area under a program administered by NRCD's Division of Parks and Recreation. The NRCD joined in the Town's request for immediate injunctive relief.

On January 28, 1983, the Nature Conservancy, which is a non-profit corporation organized to preserve significant natural areas, and which owns part of the area known as Nags Head Woods, petitioned to intervene in the complaint proceeding and joined in the Town's and the two other Intervenors' request for immediate injunctive relief. Also, on that date, Vepco filed a petition to remove the action to the United States District Court for the Eastern District of North Carolina. In its petition, Vepco asserted diversity of citizenship as the basis for federal subject matter jurisdiction.

On Sunday, January 30, 1983, the Town and each of the Intervenors - the Attorney General, the Public Staff, the NRCD, and the Nature Conservancy - filed with the clerk of the federal district court and served on Vepco's counsel motions to remand the action back to the Utilities Commission. These motions were heard by United States District Judge Franklin T. Dupree, Jr., on February 1, 1983.

At the hearing, Vepco filed with the court and served on the parties motions to consolidate the proceeding with a cause of action filed by the Town in Dare County Superior Court, motions to dismiss the NRCD and the Nature Conservancy as parties and/or strike their motions to remand, and motions to dismiss the Public Staff and the Attorney General as parties. Also at this time the Nature Conservancy filed an amendment to its petition to intervene.

After arguments from all parties, Judge Dupree ruled from the bench that he would remand the action to the North Carolina Utilities Commission. He issued a written order to that effect the same afternoon.

On the morning of February 2, 1983, Vepco filed a response to the Town's and the Intervenors' motions for a temporary restraining order. That afternoon the Commission issued orders granting the NRCD's and the Nature Conservancy's petitions to intervene and denying the Town's and the Intervenors' motions for a temporary restraining order. The Commission denied the motions for a temporary restraining order because based upon the documents before it, the Commission could not find that immediate and irreparable injury, loss, or damage would result to the Town or the Intervenors before notice could be served and a hearing could be conducted. Based on the extraordinary circumstances before it, however, the Commission scheduled a hearing before a panel of three Commissioners at 9:00 a.m. on February 7, 1983, in Kill Devil Hills so that the panel could view the sites and the construction at issue in the proceeding.

On February 3, 1983, the Town and the Intervenors jointly filed a motion for an order directing Vepco to produce certain documents and witnesses. Vepco filed its response to the Town's and the Intervenors' motion on February 4, 1983, and stated that it was willing to make a diligent, good faith effort to produce the requested documents which are relevant and material to the issues raised in the proceeding and that the Commission should not order Vepco to produce all of documents requested because some of them were immaterial. Vepco delivered a large amount of documents to Mr. Crampton, Attorney for the Public Staff, on Sunday morning and Sunday afternoon, February 6, 1983.

At the hearing in Kill Devil Hills, the following public witnesses from the Outer Banks area testified: Mike Riddick, Bryan Newman, Lowell Perry, Robert Rollason, John Burch, Joseph Deneke, Chris Payne, Fred Hutchins, Doug Langford, Nancy Aycock, Lucie Wickman, Doug Foran, Keith Ferrin, Denise Benkne and Fred Bear. The Commissioners conducted an on-site inspection of the completed portion of the transmission line as well as the rest of the proposed route. Representatives of each party accompanied the panel during the inspection.

The Public Staff called Mr. William W. Proffitt, Senior Vice President for Vepco, as an adverse witness and offered as rebuttal testimony and exhibits from Thomas S. Lam, Engineer in the Public Staff's Electric Division.

The Town offered testimony and exhibits from the following witnesses: Clare Waterfield, Town Clerk for the Town of Kill Devil Hills; Jim Lee, licensed professional photographer, Kill Devil Hills; Craig Clark, Fire Inspector and Assistant Building Inspector, Town of Kill Devil Hills; Lloyd Balance, Town Manager, Town of Kill Devil Hills; and David Menaker, Commissioner and Mayor Pro Tem, Town of Kill Devil Hills.

The Nature Conservancy presented Dr. Vincent Bellis, Professor of Biology, East Carolina University; and Henrietta and Jim List, managers of the Nags Head Woods Preserve for the Nature Conservancy.

The NRCD presented testimony from the following witnesses: Joseph W. Grimsley, Secretary, North Carolina Department of Natural Resources and Community Development and Julie Hackney Moore, Inventory Specialist and Botonist, NRCD Natural Heritage Program.

Vepco presented testimony and exhibits from the following witnesses: R.D. McIver, Vice President, Southern Division for Vepco; James E. Harden, District Manager, Outer Banks District for Vepco; Richard John Gutleber, director of Transmission and Distribution Engineering for Vepco; Richard Weaver, Supervisor, Transmission Engineering for Vepco, and Jim Claypool, Division Engineer for the Southern Division for Vepco.

Based on the foregoing, the testimony and exhibits received in evidence at the hearings, and the entire record in this proceding, the Commission makes the following

FINDINGS OF FACT

1. That Vepco is engaged in the business of developing, generating, transmitting, distributing, and selling electric power and energy to the general public in northeastern North Carolina including the Outer Banks area, and Vepco has its principal office and place of business in Richmond, Virginia.

2. That Vepco is duly organized as a public utility company under the laws of North Carolina and is subject to the general jurisdiction of this Commission.

3. That the Town of Kill Devil Hills is a municipal corporation existing under the laws of the State of North Carolina with the power, inter alia, to enter into franchise agreements with a public utility company, adopt and enforce land use regulations, and bring a complaint before this Commission against a public utility erecting transmission poles within the Town's corporate limits.

4. That the Nature Conservancy is a nonprofit corporation with a principal place of business in Arlington, Virginia, which is organized and existing for the purpose, inter alia, of acquiring, protecting, and preserving significant natural areas within the United States and within the State of North Carolina

5. That the Nature Conservancy owns and manages a 350 acre portion of an ecologically sensitive and unique area known generally as the Nags Head Woods, (the Woods), which is wholly within the corporate limits of the Town of Kill Devil Hills in Dare County, North Carolina and that the property owned by the Nature Conservancy has been designated by it as the Nags Head Woods Ecological Preserve. The Nature Conservancy also manages approximately 300 additional acres of the Woods for the Town of Nags Head, these acres being located within the corporate limits of Nags Head. Vepco has owned a right of way through the Nags Head Woods, including that portion owned and managed by the Nature Conservancy, since 1954, and has maintained a 34.5 Kv combination transmission/distribution line in that right of way since approximately 1957. The Conservancy was aware of Vepco's use of and legal right to use this right of way when it bought its property in several purchases between 1978 and 1982.

6. That the North Carolina Department of Natural Resources and Community Development is organized and existing under the laws of North Carolina for the purpose, inter alia, of aiding in the promotion of conservation and development of the natural resources in North Carolina and for the purpose of

aiding in the promotion of more profitable use of the State's lands and forests.

7. That the North Carolina Attorney General and the Public Staff of the North Carolina Utilities Commission are organized and existing under the laws of North Carolina for the purpose, inter alia, of representing the using and consuming public in matters properly before this Commission.

8. That as early as 1972, Vepco began considering the feasibility of upgrading one of its two existing 34.5 Kv combination transmission/distribution lines which run from its Kitty Hawk substation through Kill Devil Hills to a substation located in Nags Head. The lines can be considered to be combination transmission/distribution lines because they serve both to transmit power south from Kitty Hawk and they also serve to distribute power along the way by use of step-down transformers. One of the lines (Circuit 406) runs south from the Kitty Hawk substation down the east side of Highway 158 by-pass, across the highway and in front of the Wright Brothers Memorial, through the business district of Kill Devil Hills, and into a substation in Nags Head. The second line (Circuit 405), known as the sound side line, runs westward out of the Kitty Hawk susbstation along Kitty Hawk Bay, through the sound front area of Kill Devil Hills, through the Nags Head Woods in Kill Devil Hills and Nags Head, behind Jockey's Ridge State Park, and into the Nas Head substation.

9. That Vepco's load growth projections in the 1970s indicated that upgrading transmission capacity south of Kitty Hawk substation would be necessary in order to ensure reliable service and that Vepco's load projections in 1979 showed that the new line was needed by the summer of 1981. Peak loads in the Outer Banks service area generally occur on the hottest days in the summer.

10. That in late 1978 and early 1979, Vepco had a preliminary plan to build the new 115 Kv transmission line down the west side of U. S. 158 by-pass. The completion date for this project was May 1981 so that the new line would be operational for the peak load periods during the summer of 1981.

11. That in February of 1979, Vepco officials made a presentation to the Board of Commissioners of the Town of Kill Devil Hills at one of the Board's regularly scheduled by-weekly meetings. Vepco had had preliminary discussions with the North Carolina Department of Transportation for a permit to build on the west side of the by-pass. The Department of Transportation apparently informed the Commissioners of Kill Devil Hills that they had been contacted by Vepco. The Commissioners asked Vepco to appear at their board meeting to explain their plans. At this presentation Vepco officials told the Board that their preliminary plan was to build the new line on the west side of U.S. 158 by-pass from Kitty Hawk substation to the Nags Head substation. Although Vepco had not yet designed a pole for the new line at that time, the Vepco spokesmen presented to the Board a drawing of a "typical pole" of 65 feet in height. After the Vepco officials answered questions from the Commissioners and listened to their comments, it was apparent to the Vepco representatives (and the Town minutes of the meeting reflect the fact) that all members of the Board preferred that the new line be placed underground. When the Vepco spokesmen responded that placing the new line underground was cost prohibitive, the Board requested orally (though not by duly adopted motion or resolution) that if the line could not economically be placed underground, that Vepco build the line on the sound side rather than along the by-pass.

The Commissioners expressed their concerns about the undersirable aesthetic impact of placing the large poles along the Town's main transportation and commercial route and about the safety risks of placing the poles along the main evacuation route for the island.

12. That Vepco made numerous presentations to the Boards of Commissioners of the affected local governments in the spring and summer of 1979 and that the consensus of the representatives of the political subdivisions affected, including the Boards of Commissioners of the Towns of Kill Devil Hills, Kitty Hawk, and Nags Head, and the Dare County Board of Commissioners, was that they preferred that the new line be placed underground, but when faced with the prohibitive costs of underground construction and maintenance, they all asked Vepco to consider alternatives to the by-pass route. The elected officials did not want the tall poles to be erected along their major commercial and transportation corridor because of adverse aesthetic and safety consequences.

13. That in order to build the new line down the west side of the by-pass and to avoid the costly and dangerous procedure of overbuilding the new line over the existing 34.5 Kv line on the east side of the by-pass, Vepco would have to obtain a permit from the North Carolina Department of Transportation. In July 1979, however, Vepco was informed by the departmnent that it would not be able to get a permit to build the new line down the west side of the U.S. 158 by-pass. Thus, in order to route the new line down the by-pass Vepco would have to build the new line over the existing 34.5 Kv line on the east side of the by-pass. Vepco also learned that it would be necessary to get an environmental impact statement and a permit from the National Park Service before crossing a 100-foot strip of land from Colleton Road to the beach road that was owned by the National Park Service, and Vepco was apprised that this would consume a lot of time. Finally, Vepco operations personnel had now had input into the issue of the location of the line and had determined that from a construction and maintenance point of view, the sound side route was preferable because substantial construction and operation problems associated with the route on the east side of the by-pass, including insulation contamination from salt spray and difficulty of access to the new line for repairs, would not be present on the sound side.

14. That based on the opposition to its proposed preliminary route and because of the operation, construction and permit problems, Vepco changed its plans and began pursuing the feasibility of building the new line in the right of way of the 34.5 line on the sound side.

15. That because of the difficulties with the by-pass route and the change to the sound side route, Vepco realized it would not be able to have the 115 Kv line operational by May 1981, so it decided to add capacitor banks and to reconductor the sound side 34.5 Kv line (circuit 405) with a larger conductor that could be used later for the 115 Kv line. The reconductoring and the adddition of capacitor banks increased the amperage and the thermal capacity of circuit 405 so that some of the load from circuit 406 could be switched to the sound side enabling Vepco to provide adequate and reliable service to the Outer Banks with the existing 34.5 Kv lines until the early summer of 1983.

16. That in order to build the new line along the sound side route of the then existing 34.5 Kv line, Vepco needed an easement across approximately 1,700 feet on the western edge of Jockey's Ridge State Park

because it was not feasible to place the new 115 Kv line underground and because poles for an above ground line in the existing right of way would not have satisfied National Electric Safety Code standards because they would have been too close to existing buildings in the Villas condominium complex. Secretary Joseph Grimsley of NRCD, however, did not have the authority to negotiate with Vepco for or grant Vepco such an easement. As a result, a meeting of local government officials, including representatives of the Town of Kill Devil Hills, Vepco and Representative Charles Evans, was held on September 24, 1981, and Rep. Evans was asked to introduce a bill in the North Carolina House of Representatives giving Secretary Grimsley such authority. Rep. Evans introduced the bill and on October 9, 1981, the North Carolina General Assembly ratified the bill by a required two-thirds majority vote. On November 6, 1981, however, Secretary Grimsley denied granting Vepco the requested easement.

17. That in April 1982 Vepco met again with the Board of Commissioners of the Town of Kill Devil Hills to update them on the status of the new line and to inform them that a route totally on the sound side was impossible because a right of way through Jockey's Ridge State Park could not be obtained. At this time the Board included five new Commissioners out of six available positions who had taken office in December 1981. The Board indicated that they were still interested in Vepco's placing the line underground. That in June of 1982, the Town attorney for Kill Devil Hills reported to the Board that after several conversations with the Public Staff of the Utilities Commission, he was satisfied that contrary to what Vepco had told the Board (that the customers requesting lines to be placed underground would have to bear the increased costs), all of Vepco's North Carolina taxpayers would bear the cost of placing the line underground. That in July of 1982 the Nature Conservancy appeared before the Kill Devil Hills Board to persuade the Board to try to get Vepco to move the proposed route of the new line out of the Nags Head Woods. The convergence of these two events appears to have given the impetus for the new Board's opposition to the sound side route by late summer of 1982.

18. That Vepco investigated several alternatives for coming from the sound side out to the by-pass north of Jockey's Ridge and that the most feasible route was to build down the sound side from Kitty Hawk through Kill Devil Hills largely in the existing 34.5 Kv line right of way, to cross over east to the by-pass north of Jockey's Ridge State Park at Dowdey's Amusement Park and then down the east side of the by-pass to Nags Head substation. A cross over to the by-pass farther north was undesirable because of problems with congestion and a conflict with the flight path of the First Flight Airport behind the Wright Memorial.

19. That between 1978 and 1982, the Nature Conservancy acquired in separate transactions a total of approximately 350 acres of land in the Nags Head Woods and in 1980 began negotiating with Vepco for a management agreement under which the Conservancy would largely manage the right of way containing the existing 34.5 Kv line which ran through the Conservancy's property. Although at least two proposed agreements were exchanged by the parties, in the spring of 1982, the Nature Conservancy began seeking support among local officials on the Outer Banks to block Vepco's planned 115 Kv transmission line through the Nags Head Woods and to relocate to the by-pass the existing 34.5 Kv line located through their property.

20. Thatby the late spring of 1982, Vepco had obtained the necessary rights of way and highway permits for the combination route for the new line and that in July 1982 Vepco actually learned that at least the Towns of Kill Devil Hills and Nags Head had changed their positions to oppose the sound side route through the Nags Head Woods.

21. That during the summer and fall of 1982, the Nature Conservancy, NRCD, and several local elected officials contacted Vepco about changing the route for the new transmission line back to the U. S. 158 by-pass. That high ranking Vepco officials who had the authority to make any necessary decisions on this matter met with representatives from each of these groups and that Vepco considered the proposals presented by the various parties and was willing to make another change in the route of the line if: (1) the Company be made whole for all investment in the present routing that is lost as a result of the change, (2) agreement is obtained from all of the governing bodies of the affected political subdivisions, and (3) the governing bodies of each of the affected areas publicly inform the citizens of the Outer Banks that the relocation is at their request and they understand that service curtailments are likely to occur.

22. That under the circumstances, the conditions Vepco placed on another change in the location of the new line were reasonable and that no party has ever come forward and offered to meet any of the conditions.

23. That load projections made by Vepco in 1980 and 1981 indicated that the load on the Outer Banks, after the capacity-increasing procedures completed in May 1981 (reconductoring and the addition of capacitor banks), would again reach the critical stage in the summer of 1983. These projections also indicated that the winter of 1982-1983 was the last winter the load could be carried on one 34.5 Kv line while the new line was being constructed.

24. That Vepco waited until September 1982 to begin construction of the new 115 Kv line to allow the Nature Conservancy, the Towns of Kill Devil Hills and Nags Head, and state NRCD officials to satisfy the conditions Vepco had placed upon another relocation of the line. Based upon Vepco's load forecasts and its opinion that the winter of 1982-1983 was the last winter in which one of the 34.5 circuits would handle the winter load, Vepco could delay construction no longer and still be assured it could handle adequately the anticipated load of the Outer Banks during the summer of 1983.

25. That prior to entering onto the Nags Head Woods Preserve to begin construction, Vepco notified the manager of the Preserve in order to minimize the damage to the Preserve and that Vepco agreed to many of the manager's wishes, including utilizing certain routes for vehicles and equipment, substantially reducing the number of trees and amount of vegetation to be cut from the right of way, moving two poles to new locations, building several osprey nests, and instructing its employees and the construction subcontractors generally to attempt to cooperate with the Nature Conservancy as much as possible consistent with performance of their tasks.

26. That at the time the Town of Kill Devil Hills filed its complaint on January 27, 1983, Vepco was already erecting poles within the corporate limits of the Town and that by the conclusion of these hearings, two-thirds of the new line had been completed beginning at Nags Head substation and running north along U.S. 158 by-pass to Dowdy's Amusement Park. New poles are

in place from that point across to the sound side right of way and north through Nags Head Woods. Thus, at the time of the hearings, one-third of the poles to be placed within the corporate limits of the Town of Kill Devil Hills were in place.

27. There is no evidence that the ordinance has ever been enforced against any structure other than a building even though there is substantial evidence in the record that Vepco has many poles greater than 40 feet in height in the Town of Kill Devil Hills other than these poles in issue herein. Whether Vepco's new poles would be "structures" within the meaning of the zoning ordinance was discussed initially by the Kill Devil Hills Board of Commissioners at a regularly scheduled Board meeting on February 27, 1979, at which time the former building inspector for the Town stated his view that the ordinance did not apply to utilities and their structures. Thereafter, apparently, the matter was never raised again until Mr. Gaw, the Town Attorney, was instructed by the Town Board at the January 11, 1983, regular Board meeting to use every means available to stop Vepco from building the new line.

28. That although it may be possible for the 115 Kv line to be built on 40-foot poles and meet National Electric Saftey Code clearances, such a line would have a picket fence like appearance and would be more expensive and aesthetically undesirable.

29. That the existing franchise agreement between the Town of Kill Devil Hills and Vepco does not mention any height restriction on any of Vepco's structures even though the height ordinance was in existence at the time the franchise agreement was executed, and that the franchise agreement provides that any other ordinances inconsistent with its provisions are repealed.

30. That the Outer Banks is one of the fastest growing areas in Vepco's service territory, that the growth in population and economic activity has increased demand for electricity to a critical point and that completion of the 115 Kv transmission line project by the summer of 1983 is necessary and essential to the pulic interest in maintaining adequate and reliable electric service on the Outer Banks.

31. That construction of the new line is on schedule but that if any substantial delay in construction would occur, Vepco may not be able to have the line in service for the summer load of 1983 and, as a result, reliability of electric service on the Outer Banks could not be assured.

32. That replacement of the old dismantled 34.5 Kv line on the sound side in order to provide more time for a hearing on the merits is not a reasonable alternative because Vepco could not assure reliability of service this summer without the new 115 Kv line and because there is no evidence that Vepco could reconnect the old 34.5 Kv line any sooner than the 115 Kv line can be made operational.

33. That the existence of the old 34.5 Kv line since the 1950s, the reconductoring of the 34.5 Kv line in 1980 and 1981, and the construction of the new 115 Kv line through the Nags Head Woods has affected adversely the unique ecological system in proximity to the right of way through the Woods. That such damage had already been done by the construction and maintenance of the old 34.5 Kv line, the reconductoring work, and the present construction

completed in the Nags Head Woods and that removal of the new poles already erected through the Woods would cause further damage to the area. Maintenance of the new line in the right of way under a reasonable management agreement between Vepco and the Nature Conservancy, however, can substantially minimize any further adverse impact on the Woods.

34. That the construction of the new line along its present route through Kill Devil Hills does not require any substantial widening or changing of the 1954 right of way and the poles will be substantially less visible to the majority of the population of the area and to the majority of tourists and other visitors than the poles would be if located along the by-pass.

35. That over-building; i.e., building the 115 Kv line on new poles over the existing 34.5 Kv line on the east side of U.S. 158 by-pass, would increase the congestion in that residential and light comnmercial area and would cause much greater visual intrusion to a far greater number of people, including visitors to the Wright Brothers National Memorial, than would building the line along the combination route.

36. That over-building a new 115 Kv line on new poles along U.S. 158 by-pass in Kill Devil Hills would result in shorter span lengths, would be more difficult to build, and would present greater maintenance problems than the new 115 Kv line along the sound side in Kill Devil Hills.

37. That the poles supporting the new 115 Kv line are designed and are being constructed to withstand sustained wind speeds of up to 145 m.p.h. and that these poles are safer than the existing poles carrying the two 34.5 Kv lines. The new poles through the greater density of residential and commercial development along the highway and because the highway is the main evacuation route for the Outer Banks area.

38. That from an engineering, operational, safety, and aesthetic point of view, Vepco's decision to construct its new line along the combination route was a just and reasonable one.

CONCLUSIONS OF LAW

1. That all of the parties to this proceeding are properly before this Commission and that this Commission has general jurisdiction over this Complaint proceeding.

2. That this Commission does not find it necessary at this stage of the proceedings to determine whether it has jurisdiction to entertain the issues in this litigation arising from the Town's attempted enforcement of its 40-foot height limitation to Vepco's poles. Nevertheless, in the event it later determines that it has such jurisdiction, the following conclusions would appear to be warranted from the evidence presented thus far and as such have a bearing on the Town's likelihood of success on the merits without regard to whether this Commission has such jurisdiction:

a. The ordinance would appear not to have any application to "utility structures";

b. If indeed the ordinance is applicable then the Town of Kill Devil Hills by its conduct or behavior as set forth in the record may have granted to Vepco a variance, either expressly or impliedly;

c. If indeed the ordinance is applicable and if no express or implied variance has been granted by the town to Vepco, then and in that event, it would appear that the ordinance may consitute an unreasonable burden on Interstate Commerce which would prohibit Vepco from fulfilling its obligations as a public utility; and

d. Even if the ordinance were to apply to utility structures, there being no variance, express or implied, and even if it did not constitute an unreasonable burden on Interstate Commerce, all of which the Commission doubts, then the franchise agreement between Vepco and the City of Kill Devil Hills probably controls over the ordinance. The franchise agreement contains no height limitation on utility poles and, in fact, it indicates that it is intended to repeal all city ordinances in conflict therewith. It should be noted, again, that it appears from the record herein that at the time of the signing of the franchise ordinance the town's height limitation ordinance was in effect.

Therefore, without regard to this Commission's jurisdictional authority to determine these matters, it appears that the Complainant Town of Kill Devil Hills has little likelihood of prevailing on the merits herein as far as the ordinance is concerned.

3. That to be entitled to a preliminary injunction, the Complainant and the Intervenors must show that (1) there is probable cause that they will prevail on the merits, (2) there is reasonable apprehension of irreparable loss without injunctive relief or that an injunction is reasonably necessary to protect the Complainants' and Intervenors' rights pending a hearing on the merits. Waff Bros., Inc. v. Bank of North Carolina, N.A., 289 N.C. 198, 221 S.E.2d 273 (1975).

4. That in order to prevail on the merits the Complainant and Intervenors must show that Vepco has acted unjustly and unreasonably in locating and constructing the new 115 Kv line. G.S. 62-73 and G.S. 62-75. That the Complainants and Intervenors have failed to meet their burden of proof on this issue and, in fact, the overwhelming weight of the evidence supports the conclusion that the Complainants and Intervenors will not be able to prevail on the merits.

5. That the Complaint and Intervenors have failed to show that there is a reasonable apprehension of irreparable loss to them or that a preliminary injunction is reasonably necessary to protect their rights pending hearing on the merits. In fact, the evidence indicates that the controversy raised by the Complainant and Intervenors is almost moot because of Vepco's substantial completion of the project at the time of the hearings and that the risk to reliable electric service to the Outer Banks, which would result from delay in construction of the new line, is a reasonable apprehension of loss to the general public.

6. That under the facts in this case, where the new line has been built through the unique ecological system of the Nags Head Woods and where Vepco

and the Nature Conservancy have evidenced a willingness to reach a reasonable management agreement for that portion of the right of way which runs through land which the Conservancy either owns or manages for the Town of Nags Head, it is reasonable to require Vepco to enter into a management agreement designed to protect the Woods to the maximum extent possible consistent with safe operation and maintenance of the new transmission line.

IT IS, THEREFORE, ORDERED as follows:

1. That the Complainants' and Intervenors' request for a preliminary injunction to stop Vepco from constructing its new 115 Kv transmission line be denied.

2. That Vepco and the Nature Conservancy enter into, within a reasonable period of time, a management agreement for management of the right of way through property owned and managed by the Nature Conservancy. Said management agreement shall be designed to protect the vegetation and ecology in and around the right of way to the maximum extent possible consistent with safe operation and maintenance of the transmission line.

3. That hearings on the merits of this case shall be heard beginning at 2:00 p.m., May 9, 1983, in the Commission Hearing Room at which time all parties will be given an opportunity to present any new and additional evidence relevant to the issues in the case pursuant to the parties' stipulation that evidence already presented in the hearings on the preliminary injunction shall constitute the record on the merits subject to each parties' right to object to the admissibility of such evidence.

ISSUED BY ORDER OF THE COMMISSION.
This the 22nd day of April 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sandra J. Webster, Chief Clerk

DOCKET NO. E-2, SUB 461

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of	
Application of Carolina Power & Light Company for an Adjustment in Its Rates and Charges Applicable to Electric Service in North Carolina	) ORDER GRANTING PARTIAL) INCREASE IN RATES AND) CHARGES

HEARD IN: Superior Courtroom, 5th Floor, Buncombe County Courthouse, Courthouse Plaza, Asheville, North Carolina, on May 16, 1983

Superior Courtroom, New Hanover County Courthouse, Third and Princess Streets, Wilmington, North Carolina, on May 25, 1983

The Wayne Center, Corner of George and Chestnut Streets, Goldsboro, North Carolina, on May 26, 1983

The Commission Hearing Room, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina, on June 28-July 1, July 5-8, July 18-22, and July 25-26, 1983

BEFORE: Commissioner Leigh H. Hammond, Presiding; and Chairman Robert K. Koger and Commissioner A. Hartwell Campbell

APPEARANCES:

For the Applicant:

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Richard E. Jones, Vice President and Senior Counsel; Robert W. Kaylor, Associate General Counsel; and Margaret S. Glass, Associate General Counsel, Carolina Power & Light Company, P. O. Box 1551, Raleigh, North Carolina 27602
For: Carolina Power & Light Company

For the Intervenor State Agencies Representing the Using and Consuming Public:

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For: Public Staff - North Carolina Utilities Commission

Steven F. Bryant, Assistant Attorney General, North Carolina Department of Justice, P. O. Box 629, Raleigh, North Carolina 27602
For: The Attorney General of the State of North Carolina

For the Other Intervenors:

Ralph McDonald and Carson Carmichael, III, Bailey, Dixon, Wooten, McDonald & Fountain, Attorneys at Law, P. O. Box 2246, Raleigh, North Carolina 27602
For: Carolina Industrial Group for Fair Utility Rates - Weyerhaeuser Company; Federal Paper Board Company, Inc.; Riegelwood Operations; Monsanto North Carolina, Inc.; Union Carbide Corporation; Clark Equipment Company; Huron Chemicals of America, Inc.; LCP Chemicals and Plastics, Inc.; Masonite Corporation; and The Firestone Tire & Rubber Company

Thomas R. Eller, Jr., Attorney at Law, P. O. Box 27866, Raleigh, North Carolina 27611 For: The North Carolina Textile Manufacturers Association, Inc.

David A. McCormick, Attorney, Regulatory Law Office (JALS-RL), U. S. Army Legal Services Agency, 5611 Columbia Pike, Falls Church, Virginia 22041
For: The Consumer Interest of the United States Department of Defense and Other Affected Executive Agencies

M. Travis Payne, Edelstein & Payne, Attorneys at Law, P. O. Box 12607, Raleigh, North Carolina 27605
For: The Kudzu Alliance

BY THE COMMISSION: On February 11, 1983, Carolina Power & Light Company (Applicant, the Company, or CP&L) filed an application with the North Carolina Utilities Commission seeking authority to adjust and increase electric rates and charges for its retail customers in North Carolina. The requested increase in rates and charges was designed to produce approximately $164.9 million of additional annual revenues from the Company's North Carolina retail operations when applied to a test period consisting of the 12 months ended September 30, 1982, or approximately a 14.9% increase in total North Carolina retail rates and charges. The Company requested that such increased rates be allowed to take effect for service rendered on and after March 13, 1983.

The Company alleged in its application that the $164.9 million additional annual revenues was necessary because present rates would be insufficient to: (1) produce either an overall rate of return or a rate of return on common equity which would be just and reasonable, (2) enable the Company to continue to attract capital on reasonable terms, and (3) permit it to finance its operations and construction program. Included among the reasons set forth in the application as necessitating the rate relief requested were the addition of Mayo Unit No. 1 on the Company's system, the ongoing construction at the Shearon Harris Nuclear Power Plant, and the increased expense of overall operations of the entire system.

The Company filed its letter of intent to file a general rate case with the Commission on January 11, 1983. Subsequently, upon the Company's motions and pursuant to Orders issued January 21, 1983, and February 1, 1983, the Commission permitted the Company to modify certain filing requirements which would have otherwise been applicable to its rate request filing.

On January 21, 1983, the Public Staff of the North Carolina Utilities Commission filed its Notice of Intervention. The intervention of the Public Staff in this proceeding is deemed recognized pursuant to Commission Rule R1-19(e).

On February 11, 1983, the Company filed its rate case application and an Undertaking wherein it agreed to make refunds with interest of the amount, if any, by which any rates and charges put into effect pursuant to G.S. 62-135(a) exceeded the amounts finally determined to be just and reasonable herein.

On March 7, 1983, the Secretary of Defense, on behalf of the Department of Defense of the United States, filed a petition requesting leave to intervene. That request was granted by Order issued March 17, 1983.

On March 7, 1983, the Commission issued an Order declaring the Company's application to be a general rate case pursuant to G.S. 62-137, suspending the rate increase for a period of up to 270 days as permitted by the provisions of G.S. 62-134, scheduling public hearings and directing the Company to give public notice thereof, establishing the test period for use in the case, and establishing certain dates for testimony and petitions to intervene to be filed.

On March 11, 1983, a Petition to Intervene was filed on behalf of Public Service Company of North Carolina, Inc., which was allowed by Commission Order issued March 17, 1983.

On March 22, 1983, a Petition was filed on behalf of the North Carolina Textile Manufacturers Association, Inc. (NCTMA), seeking leave to intervene and participate in the proceedings. By Order issued March 24, 1983, that intervention was allowed.

On April 21, 1983, the Attorney General of the State of North Carolina filed a Notice of Intervention in this proceeding.

On May 3, 1983, a Petition to Intervene was filed with the Commission on behalf of the Kudzu Alliance. That intervention was allowed by Order issued May 16, 1983.

On May 5, 1983, the Commission issued an Order scheduling an initial pretrial conference for June 1, 1983, which was subsequently rescheduled for and held on June 13, 1983, at which time it was determined that there would be no necessity for the additional pretrial conference which had been scheduled for June 24, 1983. A Pretrial Order was issued on June 17, 1983.

On May 5, 1983, the Commission issued its Order relating to an inspection tour of CP&L's Brunswick Nuclear Plant to be conducted by CP&L for the Commission and for representatives of all parties of record who wished to participate. The inspection tour of CP&L's Brunswick Nuclear Power Plant was held as scheduled. All parties of record were permitted to send a representative. The following persons attended: Chairman Robert K. Koger and Commissioners Leigh H. Hammond and A. Hartwell Campbell; Karen E. Long and G. Clark Crampton, Staff Attorneys - Public Staff; S. R. Kirby, Staff Attorney - NCUC, and D. F. Creasy, Chief Engineer - NCUC; and Richard E. Jones, Norris L. Edge, and Ronnie M. Coats - CP&L.

On June 1, 1983, a Petition to Intervene and Motion for Extension of Time to File Testimony was filed on behalf of the Carolina Industrial Group for Fair Utility Rates, "CIGFUR II," consisting of: Federal Paper Board Company, Inc.; Huron Chemicals of America, Inc.; LCP Chemicals and Plastics, Inc.; Monsanto Company; Union Carbide Corp.; and Weyerhaeuser Company. That Petition and Motion was allowed by Order issued June 6, 1983.

On June 9, 1983, a Petition to Intervene was filed on behalf of Clark Equipment Company, Masonite Corporation, and The Firestone Tire and Rubber Company, alleging that those corporations had become members of "CIGFUR II." That petition was allowed by Order issued June 15, 1983.

On June 10, 1983, the Commission issued its Order directing the Public Staff to file certain data, exhibits, and schedules identified therein. The time initially set in that Order for the subject data to be filed was subsequently extended by the Commission, upon verbal motion by the Public Staff, and said data, exhibits, and schedules were timely filed and served pursuant to such extension.

Prior to and during the course of the hearings, various other procedural and discovery motions were made and Orders were entered relating thereto, all of which are a matter of record. Further, pursuant to various Commission Orders or requests, also of record, various parties were directed or permitted to file and serve certain late filed exhibits, either during or subsequent to the hearings held in this matter.

The proceeding came on for public hearings in the territory served by CP&L as noted herein. Night hearings were scheduled and held by the Commission for the specific purpose of receiving testimony from public witnesses in Asheville, on Monday, May 16, 1983; in Wilmington on Wednesday, May 25, 1983; in Goldsboro, on Thursday, May 26, 1983; and in Raleigh, on Wednesday, June 29, 1983. Public witnesses also appeared and testified in Raleigh, on June 28, 1983. The following persons appeared and testified at these hearings:

Asheville: David Spicer, Frank Fishburne, Jr., Richard N. Barber, Jr., L. W. Kraft, Kitty Boniske, Keith Thomson, Rebecca Williams, Carroll Rogers, Jr., Fred Sealey, and Charles Brookshire;

Wilmington: R. F. Warrick, Llewellyn Bestal, Ron Shackleford, Jerry Cabot, Larry Vestal, Stanley R. Addlemann, Herbert Slack, John Fitzpatrick, and William S. Conner;

Goldsboro: Jim Barnwell, Fred Lutz, Marie Grant, Ron Staton, Lou Colombo, Henry L. Stewart, Jr., Sylvester F. Lane, D. J. Pelt, George Mitchell, Ernest Smith, Craig Kennedy, John N. Walker, Rachel Jefferson, Steve L. Herring, Edwin H. Allen, Allen J. Griffin, Ralph Carraway, Karl Best, Gladys Thornton, and Debbie Jones; and

Raleigh: Lonnie Knott, Christopher Scott, R. H. Beatty, William T. Fuller, J. Franklin Drake, Jane Sharp, Gene Furr, Joseph Reinchens, Joseph R. Overby, William Parrish, John Currin, Jr., Rex Paramore, F. R. Robinson, William Winston Sears, Alfred Compton, Joe R. Ellen, Jr., Curtis Sapp, Clarence Knight, Elisha Wolper, Carolyn Moore, John M. Green, William Bell, Elliot Winit, and Johnny Lee Williams.

The case in chief came on for hearing as ordered on June 28, 1983, for the purpose of presenting the Applicant's evidence. The Applicant presented the testimony and exhibits of the following witnesses:

1. Sherwood H. Smith, Jr., President, Chief Executive Officer, and Chairman of the Board of Directors of CP&L (direct testimony);

2. Edward G. Lilly, Executive Vice President and Chief Financial Officer of CP&L (direct, supplemental, and additional supplemental testimony);

3. Dr. James Vander Weide, Professor of Finance, Fuqua School of Business, Duke University (direct and supplemental testimony);

4. R. A. Watson, Vice President - Fuel in the Fuel and Materials Management Group of CP&L (direct and supplemental testimony);

5. Lynn W. Eury, Senior Vice President - Power Supply (direct testimony);

6. M. A. McDuffie, Senior Vice President - Engineering and Construction (direct testimony);

7. Steven S. Faucette, Director of Regulatory Accounting (direct and supplemental testimony);

8. Paul S. Bradshaw, Vice President - Accounting Department and Controller of CP&L (direct and supplemental testimony);

9. Dr. Robert M. Spann, Principal and Member of Board of Directors of ICF, Incorported (direct testimony);

10. David R. Nevil, Manager - Rate Development and Administration in the Rates and Service Practices Department of CP&L (direct, supplemental, and additional supplemental testimony);

11. Joe A. Chapman, Supervisor - Rate Support in the Rates and Service Practices Department of CP&L (direct and supplemental testimony);

12. Norris L. Edge, Vice President - Rates and Service Practices Department of CP&L (direct, supplemental, and additional supplemental testimony);

13. Archie W. Futrell, Director of Economic and Energy Forecasting and Special Studies for CP&L (rebuttal testimony); and

14. John D. McClellan, Partner and Regulatory Specialist with Deloitte Haskins & Sells (rebuttal testimony).

The Public Staff presented the testimony and exhibits of the following witnesses:

1. Dennis J. Nightingale, Director of the Electric Division of the Public Staff (direct and supplemental testimony);

2. William E. Carter, Assistant Director of the Accounting Division of the Public Staff (direct and supplemental testimony);

3. Timothy J. Carrere, Engineer with the Electric Division of the Public Staff (direct testimony);

4. Benjamin R. Turner, Jr., Engineer with the Electric Division of the Public Staff (direct testimony);

5. George E. Dennis, Supervisor of the Water Section of the Accounting Division of the Public Staff (direct testimony);

6. Richard N. Smith, Engineer with the Electric Division of the Public Staff (direct testimony);

7. William W. Winters, Supervisor of the Electric Section of the Accounting Division of the Public Staff (direct and additional testimony);

8. Thomas S. Lam, Engineer with the Electric Division of the Public Staff (direct testimony);

9. Nancy B. Bright, Director of the Accounting Division of the Public Staff (direct testimony); and

10. Dr. Caroline M. Smith, Senior Consultant, J. W. Wilson and Associates, Inc. (direct testimony).

The Attorney General of the State of North Carolina presented the testimony and exhibits of the following witnesses:

1. Dr. John K. Stutz, Senior Research Scientist with Energy Systems Research Group, Inc.; and

2. Dr. Richard A. Rosen, Executive Vice President and Senior Research Scientist with Energy Systems Research Group, Inc.

The Intervenor Department of Defense presented the testimony and exhibits of John William McCabe III, of the consulting firm of McCabe Associates, Inc.

The Intervenor Kudzu Alliance presented the testimony and exhibits of Wells Eddleman.

The Intervenor Carolina Industrial Group for Fair Utility Rates presented the testimony and exhibits of Maurice E. Brubaker, Vice President, and Nicholas Phillips, Jr., Consultant, Drazen - Brubaker and Associates, Inc., and those of Dr. Jay B. Kennedy, Executive Director of the Electricity Consumers Resource Council.

Based upon the verified application, the testimony and exhibits received into evidence at the hearings, and the record as a whole of these proceedings, the Commission now makes the following

FINDINGS OF FACT

1. CP&L is engaged in the business of developing, generating, transmitting, distributing, and selling electric power and energy to the general public within a broad area of eastern and western North Carolina, with its principal office and place of business in Raleigh, North Carolina.

2. CP&L is a public utility corporation organized and existing under the laws of the State of North Carolina and is subject to the jurisdiction of this Commission. CP&L is lawfully before this Commission based upon its application for a general increase in its North Carolina retail rates and charges pursuant to the jurisdiction and authority conferred upon the Commission by the Public Utilities Act.

3. The test period for purposes of this proceeding is the 12-month period ended September 30, 1982, adjusted for certain known changes based upon circumstances and events occurring up to the time of the close of the hearings in this docket.

4. CP&L, by its application, is seeking an increase in its basic rates and charges to its North Carolina retail customers of $164,912,650.

5. The overall quality of electric service provided by CP&L to its North Carolina retail customers is adequate.

6. The "summer/winter peak and average" method as discussed herein is the most appropriate method for making jurisdictional allocations and for making fully distributed cost allocations between customer classes in this proceeding. Consequently each finding of fact appearing in this Order which deals with the overall level of rate base, revenues, and expenses for North Carolina retail service has been determined based upon the summer/winter peak and average cost allocation method.

7. The appropriate treatment in this case to reflect the sale of assets to North Carolina Eastern Municipal Power Agency (NCEMPA) include: (a) a three-year amortization of the gain flowed through to the ratepayers, (b) a reduction from rate base for the unamortized portion of the gain on the sale, (c) an additional rate base deduction of $50,383,000 related to Accumulated Deferred Income Taxes associated with sale, (d) an allocation of 68.7% of the gain to the North Carolina retail customers, and (e) the treatment of Investment Tax Credits associated with property sold to NCEMPA as an addition to the gain on the transaction.

8. The Company should be allowed to recover its abandonment loss sustained as the result of the Company having terminated construction on, and having abandoned, its Shearon Harris Nuclear Units Nos. 3 and 4. The recovery of the Company's investment in those units should be over a 10-year amortization period. It is neither fair nor reasonable to include any portion of the unamortized balance of this investment in rate base, and no adjustment which would have the effect of allowing the Company to earn a return on the unamortized balance of this investment should be ordered.

9. The Company should be allowed to continue the recovery of its abandonment loss sustained as the result of the Company having terminated construction on, and having abandoned, the South River Project and the Brunswick cooling towers, as previously allowed by the Commission; however, the unamortized balance of these investments should no longer be included in rate base nor should any adjustment be ordered which should have the effect of allowing the Company to earn a return on the unamortized balance on these investments.

10. CP&L has mistakenly interpreted and applied prior Orders of this Commission which specified and directed the methodology to be used to compute the amounts charged to North Carolina retail ratepayers for coal purchased from CP&L's affiliated coal mines. It is appropriate that such mistakes be corrected by this Commission.

11. Seventy-eight days of outages at CP&L's Brunswick Unit Nos. 1 and 2 in the Summer of 1982 largely resulted from past inefficiency in nuclear plant management practices. This inefficiency increased the cost of service to CP&L's customers. For these reasons, a rate of return penalty should be imposed on CP&L.

12. A normalized test period generation mix is appropriate for determining the base fuel component in the rates.

13. A base fuel component of 1.686¢ per kWh excluding gross receipts tax is appropriate for this proceeding, reflecting a reasonable fuel cost of $317,286,400 for North Carolina retail service. The 1.686¢ per kWh base fuel component in the rates does not reflect an "experience factor."

14. A $76,079,959 working capital allowance for fuel inventory is appropriate for North Carolina retail service in this proceeding, consisting of $69,489,429 for coal inventory, $6,507,444 for liquid fuel inventory, and $83,086 miscellaneous fuel stock.

15. The reasonable working capital allowance and deferred debits and credits is $98,087,000.

16. The proper amount of reasonable and prudent expenditures for construction work in progress (CWIP) to allow in rate base pursuant to G.S. 62-133 is $539,781,000. Inclusion of this amount of CWIP in rate base is in the public interest and is necessary to insure the financial stability of CP&L. This leaves a North Carolina retail amount of approximately $582 million CWIP not included in the rate base.

17. CP&L's reasonable original cost rate base used and useful in providing service to the public within the State of North Carolina is $2,222,090,000; consisting of electric plant in service of $2,431,733,000, net nuclear fuel of $25,172,000, and construction work in progress of $539,781,000, a working capital allowance of $98,087,000, reduced by accumulated depreciation of $559,362,000 and accumulated deferred income taxes of $313,321,000.

18. Appropriate gross revenues for CP&L for the test year, under present rates and after accounting and pro forma adjustments, are $1,105,194,000.

19. The reasonable level of test year operating revenue deductions for the Company after normalized and pro forma adjustments is $904,407,000.

20. The reasonable capital structure to be employed as a basis for setting rates in this proceeding is composed as follows:

Debt	49.5%
Preferred stock	12.5%
Common stock	38.0%
Total capitalization	100.0%

21. That the Company's embedded cost of debt and preferred stock are 9.59% and 8.96%, respectively. In view of the poor nuclear performance resulting from past management inefficiency and imprudence as described herein, the rate of return for CP&L to be allowed to earn on its common equity is 14.5%. In absence of its poor nuclear performance, CP&L would have been entitled to a 15.25% rate of return on common equity. Using a weighted average for the Company's cost of long-term debt, preferred stock, and common equity, with reference to the reasonable capital structure heretofore determined, yields an overall fair rate of return of 11.38% to be applied to the Company's original cost rate base. Such rate of return will enable CP&L, by sound management, to produce a fair return for shareholders, to maintain its facilities and service in accordance with the reasonable requirements of its customers, and to compete in the market for capital on terms which are reasonable and fair to its customers and to existing investors.

22. Based upon the foregoing, CP&L should increase its annual level of gross revenues under present rates by $90,855,000. The annual revenue requirement approved herein is $1,196,049,000, which will allow CP&L a reasonable opportunity to earn the rate of return on its rate base which the Commission has found just and reasonable. The revenue requirement approved herein is based upon the original cost of CP&L's property used and useful in providing service to its customers and its reasonable test year operating revenues and expenses as previously set forth in these findings of fact.

23. Further study and discussion is needed with regard to quantifying an appropriate cost differential between summer and winter months for residential service and between on-peak and off-peak hours for all customer classes.

24. It is appropriate that the Company reduce the on-peak hours in its Residential Time of Use rate schedule R-TOU from 10:00 p.m. to 9:00 p.m. during the summer months.

25. It is not appropriate that the Company expand its load control program to include customers with thirty (30) gallon water heaters at this time.

26. It is appropriate that Large General Service Time of Use rate Schedule LGS-TOU and Customer Generation Rider 55 exclude a billing demand ratchet, and that such exclusion be without prejudice to the Company seeking a ratchet at a later date which would recover distribution fixed costs only.

27. The rate designs, rate schedules, and service rules proposed by the Company, except for the modifications thereto as described herein, are appropriate and should be adopted.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 1 AND 2

The evidence supporting these findings of fact is contained in the Company's verified application, in prior Commission Orders in this docket of which the Commission takes notice, and G.S. 62-3(23)a.1 and G.S. 62-133. These findings of fact are essentially informational, procedural, and jurisdictional in nature and the matters which they involve are essentially uncontested.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 3 AND 4

The evidence supporting these findings of fact is contained in the Company's verified application, the Commission Order issued March 7, 1983, and the testimony and exhibits of Company witnesses Smith, Lilly, Bradshaw, Nevil, Faucette, Watson, and Edge.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 5

The evidence for this finding of fact is found in the testimony of Company witness Smith and that of various public witnesses who testified at the hearings which were held in this matter in Asheville, Wilmington, Goldsboro, and Raleigh. Careful consideration of such evidence leads the Commission to conclude that the quality of electric service which the Company is providing to its North Carolina retail customers is adequate.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 6

The evidence for this finding of fact consists primarily of the testimony and exhibits of Company witness Chapman; Public Staff witness Turner; Department of Defense (DOD) witness McCabe; Carolina Industrial Group for Fair Utility Rates (CIGFUR) witnesses Brubaker, Phillips, and Kennedy; and Kudzu Alliance witness Eddleman.

CP&L provides retail service in two states, as well as wholesale service. For this reason, it is necessary to allocate the cost of service among jurisdictions and among customer classes within each jurisdiction. In its four previous rate cases in North Carolina, the Company proposed the "summer peak and average" method for allocation of production level costs. The Commission did not change from the summer coincident peak method to the peak and average method in the first case, Docket No. E-2, Sub 366. However, in the next two cases, Docket Nos. E-2, Sub 391, and E-2, Sub 416, the Commission adopted the peak and average method. In the Company's last rate case, Docket No. E-2, Sub 444, the Commission modified the peak portion of the peak and average method to reflect the average of the summer and winter coincident peaks rather than the summer peak only.

In this case, the Company proposed the "summer/winter peak and average" (SWP&A) approved by the Commission in Docket No. E-2, Sub 444. The SWP&A allocates approximately 40% of production plant and related expenses based on peak responsibility, in this case the average of the summer and winter peak demands, and the remaining approximately 60% based on kWh consumption. The 60/40 split is determined by the system load factor calculated using the average of the summer and winter peaks.

Public Staff witness Turner recommended that the SWP&A method be utilized for the purpose of assigning costs to the North Carolina retail jurisdiction. He recommended that the "summer/winter peak and base," or modified peak and base (MPB), methodology be utilized for the purpose of assigning costs to the retail rate classes. The MPB allocation method allocated 65% of production plant and related expenses on an average of summer and winter coincident peak demand (kW) and the remaining 35% based on energy (kWh). The MPB method differs from the SWP&A method proposed by CP&L in that the MPB method allocates 35% of production costs by energy.

Witness Turner stated that the Company's proposed use of the summer/winter peak and average method for rate design purposes may be unfair to certain customer classes because, in his opinion, it does not recognize the possibility that the costs of fuel may vary among classes. For example, if a particular customer class is assigned base load plant costs, witness Turner contended that it should also be assigned the lower fuel costs associated with the base load plant. Conversely, if a class is assigned primarily peaking plant costs, witness Turner contended that it should also be assigned the higher fuel costs associated with the peaking plant.

Witness Turner cited a Public Utilities Fortnightly article entitled "Bias in Traditional Capacity and Energy Cost Allocation" which pointed out that there can be significant differences in costs among customer classes if the higher load factor customer is not assigned the lower fuel costs associated with base load plant. Witness Turner also stated that a recent NRRI Workshop which he attended concentrated on a method of allocating capital costs and fuel costs based on actual loads, which tended to show that the assignment of energy or fuel costs by the energy allocation factor may overcharge some customers for fuel and undercharge others. Therefore, witness Turner recommended that the Commission adopt the summer/winter peak and base method for rate design purposes as a more conservative step in the recognition of energy-related production plant costs.

CIGFUR witness Brubaker proposed to allocate production costs based on the one-hour coincident peak (CP) allocation method. Brubaker contended that it is primarily the system peak demand that drives the need for the addition of capacity. He contended that said capacity cost should be allocated to each customer class by each class's kilowatt contribution to the system peak. Witness Brubaker contended that allocating the fuel cost to each customer class based on energy usage is not "symmetrical" with the peak and average approach. The result, in his opinion, is that the SWP&A method fails to give the high load factor customers the benefit of the lower fuel costs associated with the production plant investment assigned to them.

CIGFUR witness Phillips also testified that the Company's SWP&A allocation method lacked "symmetry" between allocation of production plant investment and allocation of fuel costs. In support of the CP method, Phillips argued that allocation of plant investment on the basis of the single annual peak and allocation of fuel on the basis of energy usage did not suffer the same problems with "symmetry."

Witness Eddleman testified that the most appropriate way to allocate costs is to use the coincident peak method with the summer/winter contribution of each customer class averaged.

The Commission concluded in previous rate cases, for reasons explained extensively in Docket No. E-2, Sub 444, that the cost allocation method utilized for rate-making purposes should recognize the energy related portion of fixed costs. Essentially, the Commission reasoned that not all fixed costs represent the cost of meeting system peak demand, and that a significant portion of fixed costs represents the cost of producing kWh during many hours of the year and of producing such kWh at a lower fuel cost per kWh. The Commission continues to be persuaded in this proceeding that the cost allocation method utilized herein should recognize the energy related portion of fixed costs.

CIGFUR witness Phillips presented an exhibit showing declining system load factors in more recent years and contended that the exhibit demonstrated the detrimental effect of using the peak and average method for cost allocation during the past three years. However, upon closer examination of the exhibit by the Commission, it appears that the load factors are calculated using a mixture of summer peaks and winter peaks. If the exhibit is recalculated using annual summer peaks only, the resulting system load factors in recent years will be very consistent with all system load factors over the past 10 years. On the other hand, if the exhibit is recalculated using annual winter peaks only, the resulting system load factors in recent years will decline in comparison with all system load factors over the past 10 years. Therefore, any decline in system load factor appears to be the result of the winter peak, not the summer peak, and appears to call for a cost allocation method which places more emphasis on usage during the winter peak and less emphasis on usage during the summer peak.

The Commission concluded in the previous rate case, for reasons explained extensively in Docket No. E-2, Sub 444, that it is not persuaded that system capacity is installed to meet a single system peak, and that both the summer peak and the winter peak should be recognized in the cost allocation process. The evidence presented in this proceeding continues to persuade the Commission that the summer/winter peak as proposed by the Company is appropriate for use as a part of the cost allocation process.

DOD witness McCabe testified that he preferred the 12-month coincident peak allocation method. The Commission has reviewed the rates of return resulting from various cost allocation methods in this proceeding and notes that the rates of return are very similar when comparing: (1) the 12-month peak and average method with the summer/winter peak and average method; (2) the 12-month peak and base method with the summer/winter peak and base method; and (3) the 12-month coincident peak method with the summer/winter coincident peak method. Therefore, the Commission is of the opinion that the summer/winter peak (i.e., average of summer and winter peaks) produces results which are as satisfactory as the 12-month peak (i.e., average of 12 monthly peaks) for cost allocation purposes in this proceeding.

The Company presented two cost allocation studies in this proceeding based on variations of a "stacking" methodology. The "stacking" method used for the studies is the same used for similar studies presented in the previous rate case in Docket No. E-2, Sub 444. The Commission concluded in the previous rate case that the "production stacking" method, one of the two variations presented, demonstrated that the energy-related portion of fixed costs might well be as much as 60% of total fixed costs (of production plant).

For this proceeding, Public Staff witness Turner pointed out several inconsistencies in the "production stacking" methodology, including the problem of different dollar vintages associated with the embedded cost of each of the generating units. While the Commission recognizes the limitations of the "production stacking" method as a cost allocation method, it is of the opinion that said method still represents a good faith effort to quantify the amount of fixed costs which might be classified as energy related, and as such it represents a useful tool for comparing the cost allocation methods proposed by the various parties to this proceeding. The Commission would welcome any improvements in the studies or any alternative studies which might be useful in quantifying the energy-related portion of fixed costs.

The Commission concludes that the summer/winter peak and average method for allocating costs is appropriate for this proceeding. The Commission further concludes that the Company should continue to file alternative cost allocation studies in future general rate proceedings in order to facilitate further discussion of the many issues raised regarding cost allocation.

Another area for discussion is the assertion by several parties to this proceeding that allocation of energy-related fixed costs (of production plant) by means of kWh usage, as provided by the summer/winter peak and average method, will cause high load factor customers to bear a greater share of responsibility for such fixed costs, and that such high load factor customers will not at the same time be given a greater share of credit for the lower fuel costs associated with the fixed costs.

The summer/winter peak and average method allocates energy-related fixed costs for base load plants by kWh usage in the same proportions as the low cost fuel for said base load plants is allocated by kWh usage. The Commission must reject any assertion that such allocation of energy-related fixed cost is not consistent with allocation of low cost fuel, because both types of costs are allocated in exactly the same proportions.

The summer/winter peak and average method allocates demand-related fixed costs (for base load plants and for peaking plants) by means of peak responsibility (i.e., by one or more system peaks). There has not been any serious assertion by proponents of the peak responsibility methods that the fuel costs for said peaking plants (or for base load plants) should also be allocated by peak responsibility.

Witness Turner suggested that the problem of quantifying the energy-related portion of fixed costs (of production plant) might be resolved by means of a cost allocation study which assigns both fixed costs and variable costs to each of the 8760 hours of the year, and he recommended that such a study be undertaken. The study could also resolve limitations found in the Company's attempts to determine appropriate cost differentials between summer usage versus winter usage and between on-peak usage versus off-peak usage as discussed elsewhere herein.

The Company pointed out that a study which would assign costs to the hours during which those costs were incurred, and which would also allocate the costs in each given hour to customer classes based on their kWh usage during the given hour, would be a very large undertaking and could require a significantly larger load survey effort in order to be statistically valid. The Company suggested that it be allowed to work with the Public Staff to develop a study which would be responsive to the concerns discussed herein and would also be a reasonable undertaking from a cost and a technical standpoint. The Commission concludes that the Company's suggestion represents the best course to follow in this proceeding.

Finally, the Commission would point out that the matter of assigning costs is not an exact science, and therefore that further review and study is an appropriate matter for continuing consideration. Some members of the Commission prefer that the matter not be considered as a final judgment based on the evidence presented in this case. For instance, the assigning of class cost responsibilities may have a significant effect or impact on the assignment of jurisdictional cost responsibilities. Thus, the Commission will

follow with interest the methodologies adopted by regulatory bodies in other jurisdictions. In any event the Commission, in adopting the summer/winter peak and average allocation method in this proceeding, does not preclude the possibility that additional data may indicate the need for considering and possibly adopting some other methodology in future proceedings.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 7

The evidence supporting this finding of fact is found in the testimony and exhibits of Company witnesses Smith, Lilly, Faucette, Bradshaw, Nevil, Chapman, and McClellan; Public Staff witnesses Dennis and Winters; and DOD witness McCabe.

During 1981, CP&L concluded negotiations with the North Carolina Eastern Municipal Power Agency (NCEMPA) for the sale of interests in certain of the Company's generating units. The agreements between CP&L and NCEMPA provided for a series of closings to effect this transaction, with each closing increasing the percentage ownership of assets by NCEMPA until 100% of the agreed-upon share was transferred. The first closing of a 33% ownership share took place in April 1982. After additional closings in August, October, and November 1982, a final closing took place in April 1983, which brought NCEMPA ownership to 100% of the agreed-upon share of facilities.

Company witness Chapman testified that as of the final closing, NCEMPA owned generating capacity equal to approximately 52% of its present load requirements. Until the completion of the purchased units, which are still under construction, CP&L will provide for service to meet the remainder (presently 48%) of the NCEMPA requirements under the provisions of the Power Coordination Agreement (PCA). In addition, the Company will provide NCEMPA with backstand power during periodswhen its share of owned units is unavailable due to maintenance, modification, or forced outages. Sales by CP&L to NCEMPA under the PCA are termed Supplemental Sales. Revenues related to these sales are determined in accordance with pricing mechanisms specified in the PCA.

A number of Company witnesses testified regarding the benefits of the sale to NCEMPA. Witness Smith testified that these benefits included reduction of the need for outside financing during 1982, reduction of future construction expenditures, increased financial strength which prevented a further lowering of the Company's security ratings, and the added assurance that adequate generating capacity can be completed to provide for future growth. Company witness Smith testified that NCEMPA has paid the Company approximately $700 million during the 1982-1983 time period. Company witness Lilly testified that NCEMPA will contribute another $670 million over the next 10 years toward its share of new construction. Witness Lilly indicated that these funds would slow the rise of embedded capital costs and thus hold down customer rates.

Company witness Bradshaw testified that the customer would also benefit from the Company's proposal to flow the majority of the profit realized above book value back to the customer; from provisions for the buy-back of power from NCEMPA at prices below CP&L's cost; and by the lower AFUDC rate that would result due to reduced capital costs. Company witness Chapman testified that an ongoing benefit to the customer of the sale is the additional load portion of NCEMPA, comprised of load not previously served by CP&L which reduces the portion of fixed costs each customer must pay.

As a result of the CP&L sale to NCEMPA and the associated agreements, the Company has incorporated in its filing in this docket a number of adjustments. These relate to the specific treatment of the various costs and revenues on which the sale had an impact, including: profit above book value realized from the sale, revenues from supplemental sales to NCEMPA, and adjustments to pro forma test year results to exclude 100% of NCEMPA's ownership. The Company contends that the overall result of its treatment of the NCEMPA sale is a benefit to the North Carolina retail customers. This is due primarily to the improvement in the Company's financial condition and a reduction in future need for capital which lowers capital costs, the flow-back of the profit or gain to the customers, and provisions for buy-back of power at a discount from NCEMPA's portion of generating units. The Company believes that its treatment of the elements of the NCEMPA transaction should be viewed as a negotiated package and that, as such, it results in a substantial net benefit to the ratepayer.

The Company and certain of the parties are in disagreement with respect to:

1. The time period for flowing back the gain;
2. The treatment of the unamortized balance of the gain;
3. The allocation of the gain;
4. The treatment of accumulated deferred taxes associated with the gain;
5. The time period for flowing back investment tax credits associated with plant sold to NCEMPA; and
6. The calculation of Supplemental Revenues.

The first specific item for discussion is the profit or gain received by CP&L as a result of the sale. This gain of $37,327,000 is the amount by which the price paid for shares of generating units exceeds the proportional original cost of those units. There are three issues to be resolved arising from this gain. These are:

1. Over what time period should the gain be flowed through to the customer?

2. If the period is longer than one year, how should the unamortized portion of the gain be treated?

3. What is the proper allocation of the gain to North Carolina retail customers?

Regarding the time period for flowing the gain to the customers, the Company has proposed three years. The Company accomplishes the flow-back by an adjustment which increases Income for Return and, thereby, because of associated taxes, decreases the North Carolina retail revenue requirement by approximately twice the amount of the income for return adjustment. Company witness Bradshaw testified that in his opinion the gain, under normal accounting procedures, belongs to the stockholder but that the Company is flowing it through to its customers to offset the costs of cancelled plants. Since the flow-through is a benefit to the ratepayer, it is being amortized over only three years. Witness Bradshaw testified that if the gain had been an expense of comparable magnitude, the Company would have requested a longer amortization period.

Public Staff witness Winters recommended that the entire gain be flowed through to the ratepayer in the current rate case because the Company presently has the proceeds from this sale available to it. Witness Winters testified that if the Company's position is accepted, the revenue requirement in this case will be $35,838,000 greater than his recommendation. Witness Winters additionally stated that the Company, in its last rate case had proposed flowing through the entire gain that had been realized at that time.

Company witness Bradshaw testified that the Company's position has been consistent between rate cases because in the last case the Company proposed flowing back one-third of the gain, which was the gain that had been realized at that time. The Company is again recommending that one-third of the gain be flowed through per year.

The Commission, having reviewed the evidence in this case, believes that a three-year amortization of the gain is reasonable. The Commission recognizes that an extraordinary event of this amount, whether a profit or an expense, should be amortized over some period of time. The Commission believes it is appropriate to adopt the amortization period proposed by the Company of three years. Therefore, the three-year amortization period recommended by the Company is found to be reasonable.

The second issue relating to the gain is the proper treatment of the unamortized balance of the gain. The Company has included an adjustment to increase Income for Return by $742,008 which represents a return on the debt portion of the unamortized gain. The Company thereby reduces the revenue requirement based on the debt portion of the gain. Company witness Bradshaw testified that this is consistent with the Commission treatment of the Harris Units No. 3 and 4 loss in Docket No. E-2, Sub 444, and the Company's requested treatment of the Harris Units No. 3 and 4 unamortized balance in this case. In Docket No. E-2, Sub 444, the Commission allowed the Company to earn a return on only the debt portion of the loss by decreasing Income for Return by such amount.

Public Staff witness Winters recommended that if the gain is amortized over a three-year period, the entire unamortized balance should be treated as cost-free capital and be deducted from rate base. Witness Winters testified that the Company's position on this issue allows the Company to earn preferred and common equity returns on funds which were not provided by the equity investors and have no costs to the Company. Witness Winters recommended that these funds be treated in a similar manner to other cost-free capital.

After careful consideration of this issue, the Commission finds it appropriate to deduct the unamortized gain on the sale to NCEMPA from the rate base in this proceeding. The unamortized gain on the NCEMPA sale represents cost-free capital to the Company and in the Commission's opinion it is unreasonable and improper to expect the ratepayers of the Company to pay a return on capital which has no costs to the Company.

The final issue related to the gain for consideration by the Commission involves the proper allocation of the gain on the NCEMPA sale to the North Carolina retail jurisdiction. Both the Company and the Public Staff used a production plant allocation factor to allocate the total company gain to the North Carolina jurisdiction. However the Company used an allocation factor which reflected how production plant was allocable to this jurisdiction prior to the sale of that production plant which gave rise to the gain in question.

The Public Staff, on the other hand, used an allocation factor which reflected how production plant was allocable to this jurisdiction after the sale in question.

Public Staff witness Winters presented an explanation of why and how the sale in question changed the production plant allocation factor. Witness Winters' testimony in that regard was as follows:

> "Immediately prior to the sale in question, CP&L was serving the customers of the N. C. Eastern Municipal Power Agency as wholesale customers of CP&L. However, by virtue of the sale itself those customers were eliminated as CP&L wholesale customers. The interest in the generating units sold to the Power Agency is now owned by it -- not CP&L -- and used by it -- not CP&L -- to serve its member customers. Thus, the sale reduced the relative percentage of the remaining production plant allocable to CP&L's post-sale wholesale customers. Concomitantly the sale increased the amount of CP&L's post-sale production plant which is properly allocable to its N. C. retail customers."

The evidence indicates that if the total Company gain of $37,327,000 is allocated based upon CP&L's method, then only 62.8% of that gain is allocated to North Carolina retail customers. However, the evidence indicates that after the sale, the Company's production plant allocable to this jurisdiction is actually 68.7%.

Presumably, under CP&L's allocation method the 5.9% of the gain in controversy would either go to its shareholders or would be flowed back to its post-sale wholesale customers. If that portion of the gain were flowed back to CP&L's post-sale wholesale customers, it would constitute a "windfall" to them. Nor does there appear to be any logical reason why that portion of the gain should inure to the benefit of CP&L's shareholders. In any event, neither treatment would be fair to the North Carolina retail ratepayers. This is true because those retail ratepayers must now pay a return on a higher percentage of the production plant remaining on the CP&L system after the sale to the Power Agency than they would have paid on the same plant prior to the sale. Based upon a careful consideration of the evidence on this issue the Commission concludes that the post-sale allocation factor proposed by the Public Staff and the Department of Defense should be used for allocating the gain on the sale to the North Carolina retail customers.

The next area for consideration is the rate base treatment for the Deferred Taxes associated with the gain from the sale to NCEMPA. The Company, in its filing, made an adjustment to its per books values to reverse the booking of Deferred Taxes in Account 190 associated with the gain from the sale to NCEMPA. The effect of this adjustment was to reduce North Carolina retail rate base by $36,500,247.

The Public Staff made an adjustment to Accumulated Deferred Income Taxes which results in an additional rate base deduction of $50,383,000 on a North Carolina retail basis. The difference of $50,383,000 results from the adjustment made by witness Winters regarding the deferred income taxes related to the sale of certain generating plant and transmission lines to the North Carolina Eastern Municipal Power Agency. Witness Winters testified in this regard as follows:

"The gain on the sale to the Power Agency was reduced approximately $88,000,000 for taxes which will not have to be paid until years into the future. The Company has already received the funds to pay these taxes through proceeds from the Power Agency. The Company has proposed not to include these deferred income taxes as a rate base deduction in this case; and, if these deferred income taxes are not deducted from rate base, the ratepayers will be required to pay a return on funds which were not provided by the debt and equity investors. I recommend that the N. C. retail portion of these deferred income taxes be deducted from rate base in this proceeding as cost-free capital just as other deferred income taxes are deducted as cost-free capital.

As part of my adjustment for deferred income taxes I have increased rate base by approximately $15,000,000 to reflect the elimination of deferred income taxes which the Company treats as cost-free capital. This adjustment is necessary because these same deferred taxes were reflected as an increase in the gain on the sale."

The Company, through witness Bradshaw, takes the view that the ratepayer did not provide the funds associated with these deferred taxes and should not, therefore, benefit from a rate base reduction resulting from them. Rather, NCEMPA, which purchased from the Company's investors certain generating facilities, provided the funds associated with these deferred taxes to the Company's investors. Witness Bradshaw contended that the property that created the deferred taxes is not in rate base, has not been requested to be in rate base, and, therefore, the related deferred taxes should not be deducted from rate base.

The Commission, after reviewing the evidence on this issue, recognizes that the deferred taxes associated with the sale to NCEMPA represent cost-free funds to the Company since these funds have been contributed to CP&L by NCEMPA. CP&L has the use of these funds until such time as the taxes must be paid. The Commission concludes that deferred taxes associated with the NCEMPA sale should be treated as other cost-free capital to the Company and deducted from rate base. Thus, the Commission concludes that deferred income taxes should be increased by $50,383,000 and that the appropriate level of deferred income taxes for use in this proceeding is $313,321,000.

The next area for consideration relating to the sale to NCEMPA is the proper treatment of Investment Tax Credits which are related to property sold to NCEMPA. The Company has continued to treat these Investment Tax Credits as it does all others and flows them back ratably over the life of the property.

Public Staff witness Winters recommended that the Investment Tax Credits associated with property sold to NCEMPA be flowed back currently. Witness Winters' opinion is that current flow-through of these amounts would not be in violation of IRS regulations since the applicable Code provision refers to the useful life of property. Witness Winters further contends that the useful life has terminated when the plant has been sold.

Company witness McClellan testified that a current flow-through of the Investment Tax Credits associated with the sale would be in violation of Section 46(f)(2) of the Internal Revenue Code. In witness McClellan's opinion, current flow-through will exceed the ratable flow-through mandated. Witness McClellan testified that if the Company is found in violation of this provision, it stands to lose Investment Tax Credits retroactively to 1975.

The total projected loss for the period 1975-1984 would approximate $300,000,000 on a total system basis. Witness McClellan supported his interpretation of the IRS Code with a legal opinion from tax counsel.

The Commission finds that the Job Development Investment Tax Credits relating to the portion of the generating and transmission plant sold to NCEMPA should properly be treated as an addition to the gain on the sale of property to NCEMPA and should therefore be accorded rate-making treatment similar to that previously discussed herein regarding the gain on the sale. Specificially the Commission finds it reasonable to amortize accumulated JDITC related to the NCEMPA sale to the cost of service over a three-year period and to deduct the unamortized portion of accumulated JDITC from the rate base as cost-free capital. The Commission is aware that the accumulated investment tax credits adjusted for recapture provisions of the Internal Revenue Code represents permanent reductions in income tax expense; however, for legal reasons these credits are deferred for regulated utilities and are amortized to operations over the useful life of the property. In the Commission's opinion, the property sold to NCEMPA has no remaining life to CP&L. Thus it is both reasonable and proper to amortize the investment tax credit related to property sold to the cost of service over a three-year period.

The final area for consideration, which relates to the NCEMPA transactions, is the proper treatment of the revenues from NCEMPA for supplemental sales. The Commission will hereafter discuss this issue in Evidence and Conclusions for Finding of Fact No. 18.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 8 AND 9

Evidence with respect to the rate-making treatment of abandonment losses can be found in the testimony of Company witness Paul S. Bradshaw and Public Staff witness William W. Winters. The Public Staff takes the position that the abandonment loss should be amortized over a 10-year period and that the unamortized balance of the loss should be excluded from rate base and the Company should not be allowed to earn any return on it. The Public Staff argues that G. S. 62-133 only allows a utility to earn a return on property which is "used and useful" in providing utility service or which is construction work in progress that meets the standards set forth in the statutes. The Public Staff argues that abandonment losses qualify under neither category, that they must be excluded from the rate base, and that the Company must not be allowed to earn any return on them. In previous proceedings before the Commission, the Company has been allowed to amortize the cost of the South River Project and the Brunswick cooling towers and to include the unamortized balance of the projects in rate base. See Docket Nos. E-2, Sub 391 and E-2, Sub 416. In the last CP&L rate case before the Commission, the Commission allowed the Company to amortize the cost of Harris Units Nos. 3 and 4 over a 10-year period, and allowed that portion of the unamortized balance supported by long-term debt to be included in rate base. See Docket No. E-2, Sub 444. The Company argues that these treatments should be continued.

The proper rate-making treatment of abandonment losses has been before the Commission in several cases and will continue to arise in many future cases. The Commission has, therefore, undertaken to re-examine this important issue in order to develop a more consistent and equitable approach to it. The Commission's ultimate responsibility with respect to ratemaking is to fix

rates for the service provided which are fair and reasonable both to the utility and to the consumer. G. S. 62-133(a); State ex rel Utilities Commission vs. Morgan, 277 NC 255, 177 SE 2 405 (1970); State ex rel Utilities Commission vs. Carolina's Committee, 257 NC 560, 126 SE 2d 325 (1962).

Although parties may disagree as to the amortization period, they agree that the Company should be allowed to recover the prudently invested cost of its abandonment losses through amortization over some period of time. The Commission, based upon the evidence presented, must determine what is a fair amortization period in order to fairly allocate the loss between the utility and the consumer. In the last CP&L rate case, the Commission determined that a 10-year amortization period for abandonment losses resulting from cancellation of Harris Units No. 3 and 4 "will more reasonably and equitably serve to share the burden of the cancellation of Harris Units No. 3 and 4 between present and future ratepayers. Furthermore, use of a ten-year amortization period is also consistent with previous decisions of the Commission regarding amortization of similar property losses set forth in Orders." Amortization of these abandonment losses should be continued as previously ordered. Similarly, the Commission believes that the amortization of the losses resulting from cancellation of the South River Project and the Brunswick cooling towers should continue as previously ordered by the Commission.

Pursuant to the Commission's reexamination of the proper ratemaking treatment of abandonment losses, the Commission has determined that it is neither fair nor reasonable to include any portion of the unamortized balance of such investments in rate base and, furthermore, that no adjustment should be allowed which would have the effect of allowing the Company to earn a return on the unamortized balance. The Commission has concluded that this treatment provides the most equitable allocation of the loss between the utility and the consumer. It would be inequitable to place the entire loss of expenditures that were prudent when made on the utility. Thus, amortization should be allowed. However, on the other hand, the ratepayer must not bear the entire risk of the Company's investment. A middle ground must be found on which the Company bears some of the risk of abandonment and the ratepayer is protected from unreasonably high rates. The losses resulting from cancellations of utility plants will inevitably be borne by one or a combination of three groups: the utility investors, the ratepayers, and the income taxpayer. A recent study prepared by the United States Department of Energy indicates that a 10-year amortization of such losses will distribute costs in proportions that the Commission considers fair and equitable. NUCLEAR PLANT CANCELLATIONS: CAUSES, COSTS, AND CONSEQUENCES, United States Department of Energy, Washington, D. C. (April 1983). The Commission believes this will result in a fair and reasonable treatment of both the utility and the consumer. In the last CP&L rate case, the Commission allowed that portion of the unamortized balance in Harris Units No. 3 and 4 that was supported by a long-term debt to be included in rate base. Based upon the examination of the issue, the Commission believes it more fair and reasonable to exclude this element from the rate base. Similarly, the Commission has excluded from the rate base herein the unamortized balance of the Company's investment in the South River Project and the Brunswick cooling towers.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 10

Company witness Watson and Public Staff witness Carter presented testimony concerning the cost of coal produced by Leslie Coal Mining Company (Leslie) and McInnes Coal Mining Company (McInnes), and the appropriate fair market value of such coal. Leslie and McInnes are affiliated companies of CP&L, by virtue of the fact that CP&L owns 80% of the common stock of these coal companies. The remaining 20% of the common stock of Leslie and McInnes is owned by Pickands and Mather & Company (Pickands Mather).

Company witness Watson asserted that charges including transportation costs for coal delivered to the CP&L system from Leslie and McInnes have been determined in accordance with the Commission Order in Docket No. E-2, Sub 233, which approved the Company's participation in the mining venture and specified the coal-pricing mechanism for regulatory purposes. Witness Watson testified that the "fair market value" for the coal was determined as specified in Exhibit E (the Coal Purchase agreement between CP&L and Leslie) of CP&L's application in Docket No. E-2, Sub 233, which states that "fair market value" shall mean the market price at the time of delivery of coal of the same or comparable grade and quality being sold by a manager on the open market at arm's length in bona fide transactions. (The term "manager" under the definition which was contained in the various agreements submitted for Commission approval in early 1974 in Docket No. E-2, Sub 233, refers to Robert Coal Company, a wholly owned subsidiary of Pickands Mather.) Witness Watson testified that Pickands Mather has periodically provided CP&L with its opinion of the "fair market value" of the Leslie and McInnes coal in accordance with the language contained in Exhibit E. Witness Watson further testified that CP&L has continually monitored the "fair market value" amount provided to CP&L by Pickands Mather by comparing such data to information contained in FERC Form 423 concerning the delivered cost of coal of comparable grade and quality to Leslie and McInnes coal. Witness Watson further testified that the delivered cost of the coal from Leslie and McInnes, using the "fair market value" provided to CP&L by Pickands Mather has always been less than the delivered cost of comparable quality coal shown in FERC Form 423. Further witness Watson stated that the FERC Form 423 "fair market value" amounts have been included in exhibits filed by the Company in previous rate cases and fuel clause proceedings. According to witness Watson, the Commission has in prior proceedings established rates based upon coal costs reflecting the fair market value of the Leslie and McInnes coal as submitted by CP&L. Finally, witness Watson testified that operations at the Leslie and McInnes mines were suspended in mid-February of 1983, due to economic considerations. Witness Watson testified that at the time of the hearing the affiliated coal mining operations continue to be suspended.

Public Staff witness Carter testified that CP&L's methodology for determining fair market value does not in his opinion comply with the Commission's intent in its Order in Docket No. E-2, Sub 233. Witness Carter testified that it is his understanding and belief that the term "fair market value," as is used in the Commission Order in Docket No. E-2, Sub 233, means the price which CP&L is paying for coal of the same or comparable grade and quality which it is purchasing at arm's length from nonaffiliated long-term contract suppliers. Witness Carter stated that the Public Staff's position is based upon the language contained in conclusion (g) and the last paragraph of the Order in Docket No. E-2, Sub 233, which states in part that:

"CP&L is being put on notice that the Seller's cost of producing its coal under these referenced agreements must be closely monitored by CP&L and should they get out of line to the point that coal being supplied CP&L under these agreements is substantially higher than the fair market value of coal of the same or comparable grade and quality being purchased from non-affiliated other sources the excess cost would be disallowed for ratemaking purposes." (Emphasis added), and

"Carolina Power & Light Company is also required to include as a part of the report its own comparative analysis of the price of the coal purchased from Leslie Coal Mining Company to that coal it has purchased during the same report period from its other non-affiliated sources." (Emphasis added)

Witness Carter further testified that the language in the Order requires that reports be submitted by CP&L to the Commission reflecting prices which CP&L is paying for coal purchased from CP&L's nonaffiliated sources and that the Commission does not require CP&L to submit any reports or information concerning the prices which CP&L, or any parties other than CP&L, are paying for coal purchased from U. S. Bureau of Mines, District 8.

Witness Carter also testified as follows:

"In my opinion, if the Commission had intended for CP&L to determine "fair market value" from what either CP&L or other parties were paying for coal purchased from U. S. Bureau of Mines, District 8, the Commission would have required CP&L to submit reports concerning those prices. However, as the order reflects, no such reports are required. Reports reflecting prices which CP&L was paying for coal purchased from its non-affiliated suppliers were required. That fact leads me to the conclusion that the Commission clearly intended for CP&L to determine "fair market value" based on prices it is paying non-affiliated suppliers for comparable quality coal."

Witness Carter testified that CP&L has four nonaffiliated long-term contracts with quality requirements comparable to the quality requirements (similar sulfur content, BTU/LB, ash, and moisture content) of the Leslie and McInnes contracts. The highest cost paid for coal of similar sulfur content, BTU/LB, ash, and moisture content purchased from nonaffiliated long-term contract suppliers is according to witness Carter considerably less than the "fair market value" booked by CP&L.

CP&L has been recording the difference between the production cost of Leslie and McInnes coal and the "fair market value" of that coal, determined by CP&L, in a deferred account. The deferred account which reflects the excess of cost over fair market value has been understated in witness Carter's opinion due to the Company's method of determining fair market value. According to witness Carter's original testimony, the use of a fair market value, which equates to the price of CP&L's highest nonaffiliated long-term contract with quality requirements comparable to the Leslie and McInnes contracts, would have resulted in a decrease in coal costs of $13,065,581, on a total company basis, and $8,250,707 for North Carolina retail operations in the Company's fuel expenses. Such amounts were computed for the time period January 1979 through April 1983. Based on revised data from CP&L, witness Carter modified the aforementioned amounts to $10,329,720 on a total company basis and to $6,519,808 on a North Carolina retail basis. Based on the

foregoing, witness Carter recommended that the Commission reduce CP&L's operating revenue deductions by the $6,519,808 to recognize previous charges in excess of fair market value. It was witness Carter's recommendation that the Company's cost of service be reduced by $6,519,808 in this proceeding and that the adjustment be made separate from any adjustment to fuel expense.

Witness Carter stated that his recommendation in this regard is consistent with the methodology used by the Commission in the recent Duke Power Company (Duke) rate case, Docket No. E-7, Sub 338, to eliminate the excess of cost over market value of coal purchased by Duke from its affiliated coal mines. In witness Carter's opinion his recommendation is a very reasonable and conservative interpretation of the language which appears in the Commission Order in Docket No. E-2, Sub 233, since he proposes using the highest price of comparable quality nonaffiliated long-term contract coal rather than the average price of all comparable non-affiliated long-term contract coal. Further, witness Carter believes that the recommended adjustment does not constitute retroactive ratemaking since the Company's departure from the Commission's ordered methodology of determining "fair market value" was an error which must be corrected to comply with the Commission Order in Docket No. E-2, Sub 233.

The Commission has carefully reviewed all the evidence in this regard, including the Commission Order in Docket No. E-2, Sub 233, the testimony and exhibits presented on the production costs and "fair market value" of Leslie and McInnes coal filed and presented in previous rate case and fuel clause proceedings, as well as the Commission Order in Docket No. E-2, Sub 391, which authorized the establishment of a deferred account to record differences between production cost and fair market value of Leslie and McInnes coal. The Commission concludes that CP&L has not determined "fair market value" of the Leslie and McInnes coal as required by the Order in Docket No. E-2, Sub 233, and consequently, has overcharged the ratepayers for the coal the Company has received from Leslie and McInnes. Although the term "fair market value" appears throughout the Order in Docket No. E-2, Sub 233, it is never specifically defined. It is the Commission's opinion that the term "fair market value" as used in the Order means the price which CP&L is paying for coal of the same or comparable grade and quality which it is purchasing at arm's length from its nonaffiliated long-term contract suppliers. This is strongly suggested by the language contained in conclusion (g) and the last paragraph of the Order in Docket No. E-2, Sub 233.

Based on the foregoing, the Commission concludes that operating revenue deductions should be reduced by $6,519,808 in this proceeding. This is the amount by which CP&L, through a mistaken interpretation of the prior, final Orders of this Commission issued in Docket Nos. E-2, Sub 233, and E-2, Sub 391, has overcharged its North Carolina retail ratepayers for coal purchased from its affiliated coal mines. Such amount is calculated based on the methodology described by Public Staff witness Carter in his prefiled testimony using the difference between the average annual cost of coal per ton received by CP&L under its highest nonaffiliated contract coal supplier and the average annual "fair market value" per ton used by CP&L to charge the Leslie and McInnes coal to fuel inventory and fuel expense.

The Commission recognizes that the mining operations at the Leslie and McInnes coal mines are currently suspended. However, should the mining operations at these mines be resumed in the future, the Commission concludes

that the fair market value of coal purchased from these mines by CP&L shall be determined based on the highest price which CP&L pays for coal of comparable grade and quality purchased from a currently existing nonaffiliated long-term contract supplier. Work papers showing a calculation of the amount added to or deducted from the nonearning reserve established as a result of the Commission Order in Docket No. E-2, Sub 391, shall be filed with the Commission on a monthly basis.

EVIDENCE AND CONCLUSIONS FOR OF FINDING OF FACT NO. 11

The evidence for this finding of fact is found in the testimony and exhibits of Public Staff witnesses Thomas S. Lam and Caroline M. Smith and Company witness Lynn Eury.

In CP&L's last general rate case, Docket No. E-2, Sub 444, the Commission issued an Order on September 24, 1982, that found that:

> "CP&L's nuclear performance has been declining since 1978 and the Company's Brunswick Nuclear Units have not been available to meet the system load at periods of peak summer usage for the past four summers. Such nuclear performance is clearly unsatisfactory and is related to mismanagement with respect to outage planning, preventive maintenance, spare parts and inventory and control, and quality control and assurance."

The Commission further stated in that Order:

> "The Commission strongly believes that the sooner Company management faces up to inefficiencies and problems in its own nuclear program, the sooner nuclear production will improve. Specifically, the Commission concludes that the rate of return allowed in this docket should provide an incentive for the Company to do better. To that end, the Commission concludes that a rate of return penalty is appropriate in this case . . ."

The Commission imposed a rate of return penalty of 1% in its Order of September 24, 1982.

In the present case, witness Lam testified that 78 days of outages at the Brunswick nuclear site, 43 days at Unit 1, and 35 days at Unit 2, were avoidable. Unit 1 was shut down on June 28, 1982, because of undervoltage relays. The Unit returned to service on June 29, 1982; however, the Company's post-shutdown evaluation indicated that the undervoltage relays on the emergency electrical distribution systems had not been tested as required by the Technical Specifications which are part of the plant's license from the NRC. The Company assured the NRC that it would review all Technical Specifications surveillance requirements to insure plant safety. The review revealed three additional surveillances that were not being performed. The four surveillance requirements involved were the following:

1. Periodic checks, tests, and calibrations of the emergency electrical distribution system undervoltage relays. This system insures that the nuclear reactor does not run unless there is sufficient back-up power to operate the emergency core cooling system. Channel checks are to be performed every eight hours, channel

function tests once each month, and channel calibrations once each 18 months. The tests, checks, and calibrations had not been performed at either unit for two years.

2. Visual inspection of containment penetration to insure that radioactive contaminants do not escape. These inspections are required every 31 days. The inspections had not been performed at either unit for 55 months.

3. Check of operability of reactor water cleanup system isolation instrumentation. The standby liquid control system dumps a boran solution into the water cooling the reactor core when there is no other way to slow the nuclear reaction, and the reactor water cleanup system must be separated at that time so that it does not remove the boran. The check should be performed every 18 months. The check had never been performed at either of the Brunswick units until July 1982.

4. Tests for leaks in the transversing in-core probe guide tube isolation valve and electrical penetrations of the containment vessel to insure against leaks of radioactive contaminants. The valves should be tested for leaks every 24 months. They had not been tested for 39 months and the electrical penetrations had not been tested for 29 months.

After the Company discovered that these surveillance requirements were not being met, the NRC issued a Confirmation of Action letter outlining the work that CP&L was to complete before the Brunswick units could return to service. Witness Lam concluded that 43 days of outages at Brunswick Unit 1 were avoidable since these were the days that the unit was out while the Technical Specifications were being reviewed for compliance. For Brunswick Unit 2, 35 days of outages could have been avoided if surveillance tests had been carried out in a proper and timely manner in compliance with the plant's operating license from the NRC.

The NRC fined CP&L $600,000 for the violations described above. On February 12, 1983, the NRC sent a letter to CP&L proposing the fine in which it stated, "The cause of these violations appears to be a breakdown in corporate and facility management controls in the areas of corporate oversight, facility management and operations and problem identification and correction." In its May 2, 1983, Response to Notice of Violation and proposed imposition of civil penalties, CP&L admitted the violations and stated, in part:

"The reasons for the violations can be contributed to procedures and administrative controls that have become difficult to implement and unduly burdensome as a result of numerous amendments and modifications to plant systems and applicable regulatory requirements. Personnel errors, which were the cause of the violations, were not detected by administrative controls in place."

The NRC has otherwise expressed concern with management at the Brunswick nuclear site. In its evaluation of the Company's performance for the period January 1, 1982, through January 31, 1983, the NRC stated in its Systematic Assessment of Licensee Performance dated June 14, 1983, the following:

"Poorly stated or ill-understood procedures, identified the previous review period, continued to degrade the effectiveness of the operating staff and contributed to the substantial numbers of the reported personnel errors. Inadequate management involvement, indicated by a demonstrated laxness in discipline of operations and adherence to procedures, also had an adverse effect on operation's performance. These weaknesses were key elements in each of the violations identified below, in the civil penalties issued in June 1982 and February 1983, and in the 65 Licensee Event Reports (LER) attributable to personnel error that were issued during this review period. NRC concerns in the area of management and supervisory controls were discussed at each of five enforcement conferences held during this review period. A procedure upgrade program, renewed emphasis on discipline of operations and adherence to procedures are commitments contained in the licensee's long-range improvement program, confirmed by NRC Order on December 22, 1982."

In September 1982, CP&L made certain changes with respect to the management of the Brunswick nuclear units. All operating and maintenance, engineering, and construction activities for the plant were consolidated under the control of the Vice President of Brunswick Nuclear Project who reports directly to the Executive Vice President of Operations, Engineering, and Construction. Witness Eury testified that this reorganization was undertaken in order to increase senior management oversight of the Brunswick nuclear plant; to improve communications and coordination by consolidating operations, engineering, and construction; to insure sufficient and timely support to the plant to meet engineering and construction requirements; and to improve organizational accountability and strengthen management control. He further stated that these initiatives have resulted in certain operational efficiencies at the nuclear plant; however, the Commission finds that Brunswick's capacity factor remains unsatisfactorily low.

While the Commission recognizes that a recognized national management consulting firm recently judged CP&L to be "in many respects... one of the best-managed utilities that we have audited in the past several years" and while the Commission recognizes that CP&L has undertaken reorganization of the management of the Brunswick nuclear units in an effort to solve their problems there, the Commission nonetheless finds that a rate of return penalty should be continued. A penalty is being continued because the management problems at the Brunswick nuclear units continued to have adverse consequences on nuclear performance, such as the 78-day outage and low capacity factors, during the present test year. CP&L has now undertaken steps to eliminate the problem, but the consequences of the problem in the test year cannot be discounted. The amount of the penalty will be discussed in a later section of this Order.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 12

Company witness Nevil, Public Staff witness Nightingale, and Attorney General witness Rosen provided testimony and exhibits regarding the use of a normalized generation mix in determining fuel costs for this proceeding.

The Company contended in the previous general rate proceeding that the proper way to determine the base fuel component in the rates is by using actual test year fuel costs adjusted for known and measurable changes in kWh usage and in unit fuel prices. In this proceeding, the Company contends that

the proper way to determine the base fuel component in the rates is by using a normalized generation mix (based on the Company's own historical operating experiences and adjusted for known changes in kWh usage and unit fuel prices) plus an "experience factor." Under cross-examination, witness Nevil recommended that the actual test year fuel costs be utilized if the "experience factor" is not adopted by the Commission.

The Public Staff contends that the proper method to determine the base fuel cost for general rate case proceedings is by using a normalized generation mix (based on national averages for the nuclear plant operations and adjusted for known and measurable changes in system usage and in unit fuel prices). Witness Nightingale testified that the use of a normalized generation mix for calculating fuel costs would result in periods when the Company would over-recover its actual fuel expenses and in periods when the Company would under-recover its actual fuel expenses.

Witness Rosen testified that a normalized generation mix (based on national averages for operating experience) would be desirable so that reasonable target levels of technical and economic performance could be reflected by the base fuel component in the rates. Kudzu witness Eddleman and DOD witness McCabe also supported the use of a normalized generation mix.

The Commission concludes, as it did in the previous general rate proceeding in Docket No. E-2, Sub 444, that the general concept of utilizing a normalized test period generation mix is appropriate for establishing the base fuel component in the rates.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 13

Company witnesses Nevil and Futrell, Public Staff witness Nightingale, Attorney General witness Rosen, Department of Defense (DOD) witness McCabe, and Kudzu witness Eddleman presented testimony and evidence regarding the appropriate base fuel component in the rates.

In his original prefiled testimony, Company witness Nevil proposed a base fuel component of 1.867¢ per kWh based on actual test year generation mix (as adjusted for weather, customer growth, the addition of Mayo No. 1, and the additional load portion of NCEMPA). In his supplemental prefiled testimony, witness Nevil proposed a base fuel component of 1.818¢ per kWh based on a normalized generation mix plus an "experience factor." He stated that the actual test period generation mix should be utilized unless the "experience factor" is adopted.

In calculating his normalized generation mix, witness Nevil utilized a computerized production simulation model (PROMOD) to recreate the test year generation mix which would have occurred if the test year were adjusted to reflect: weather normalization, customer growth, addition of Mayo No. 1, additional load portion of NCEMPA, the lifetime average capacity factor of each of the Company's nuclear units, the five-year average equivalent availability of each of the Company's fossil steam units, the average hydro generation over the last 22 years, and purchased power and IC turbine generation "at levels which maintained reasonable levels of supply from both sources." His normalization of the nuclear generation resulted in a total nuclear capacity factor of approximately 52%.

To determine the portion of net fuel costs associated with NCEMPA, the Company utilized its own computer model (ECAP) to determine the kWhs and fuel costs to be charged to Power Agency under each of the five supply and pricing classifications contained in the agreement with Power Agency.

Witness Nevil utilized March 1983 unit fuel prices to compute a total Company fuel cost (subject to fuel charge adjustments) of $429,299,900. He then multiplied the fuel cost by his proposed "experience factor" of 1.1588 to obtain a requested fuel cost of $497,472,700 total Company (or $342,140,000 for North Carolina retail service) yielding a base fuel component of 1.818¢ per kWh excluding gross receipts tax.

The "experience factor" was presented to the entire Commission in Docket No. E-100, Sub 47, concerning fuel charge adjustments, and the Commission has not yet made a determination in that proceeding. The "experience factor" is computed based on the ratio of three years actual fuel costs per kWh to three years estimated fuel costs per kWh (utilizing any specific estimating methodology), and is intended to compensate for estimating errors. The Company multiplied the 1.569¢ per kWh base fuel component it estimated in this proceeding (based on its historic normalization methodology) by the 1.1588 "experience factor" it calculated (based on actual and estimated fuel costs for 1980, 1981 & 1982), to derive its recommended 1.818¢ per kWh base fuel component.

Public Staff witness Nightingale recommended that the base fuel component be derived by a methodology which does not involve the use of a complex computer program. His analysis normalizes the generation mix by: utilizing the 10-year average capacity factor for each type of nuclear plant as reported by the National Electric Reliability Council (NERC), Ten Year Review - Report on Equipment Availability (1972-1981); setting hydro generation equal to the median reported in the Company's most recent Power System Statement (Form 12); and prorating the remaining fossil fuel generation and outside purchases and sales in proportion to their actual test period generation mix. His normalization of the nuclear generation resulted in a total nuclear capacity factor of approximately 57%. No account was taken of the planned extended outage for the Robinson nuclear unit in this figure.

Witness Nightingale utilized March 1983 unit fuel prices to compute a total Company fuel cost (subject to fuel charge adjustments) of $412,515,200, or $283,709,700 for North Carolina retail service, yielding a base fuel component of 1.508¢ per kWh excluding gross receipts tax. DOD witness McCabe also accepted the Public Staff's position on fuel expenses.

Attorney General witness Rosen advocated the determination of nuclear capacity factors by means of a regression analysis equation developed by his Company, Energy Systems Research Group (ESRG). Witness Rosen selected several characteristics of a nuclear unit and he utilized data from the national data base concerning those characteristics, and he performed a multiple regression analysis of the data to determine an appropriate capacity factor for each individual nuclear unit. He testified that the average normal Maximum Dependable Capacity factor for Brunswick No. 1, Brunswick No. 2, and Robinson No. 2 should be 60%, 63% and 73%, respectively, resulting in a total nuclear capacity factor of approximately 65% for the Company. Witness Rosen took no account of the actual experience factor for the CP&L units except to include them in his national average statistics.

Kudzu witness Eddleman computed a range for the base fuel component by simply assuming a 60% nuclear capacity factor (NCUC Rule R8-46, level for signaling a need for examination of outage problems) and a 70% nuclear capacity factor (design level). His procedure yielded a base fuel component of 1.312¢ per kWh to 1.429¢ per kWh (reflecting the 70% to 60% capacity factors, respectively).

Witness Nevil testified that the Company projects its actual fuel costs to be 1.838¢ per kWh for the period during which the rates established herein are expected to be in effect. The Company's testimony indicated that the steam generator at the Robinson nuclear unit must be replaced and that the Company has planned a nine-month outage of the unit beginning in March 1984. If the rates established herein are in effect for the period September 1983 to September 1984, an outage beginning in March 1984 would last for 6 months of the period. The Commission is of the opinion that the base fuel component in the rates established herein should be normalized to reflect a six-month outage of Robinson in order to reflect a just and reasonable level of base fuel costs.

The Company filed data showing that the base fuel component which results from incorporating a six-month outage of the Robinson nuclear unit into the historic normalization methodology would be 1.686¢ per kWh excluding gross receipts tax. The calculation reflects March 1983 unit fuel prices and an overall nuclear capacity factor of approximately 42%. The overall nuclear capacity factor is impacted significantly by the six months planned outage of the Robinson nuclear unit. The national average capacity factor for nuclear units has generally averaged approximately 60%, and the theoretical maximum nuclear capacity factor is about 80% if no down time for maintenance is required except for annual fuel reloading. The 1.686¢ per kWh does <u>not</u> include the proposed "experience factor."

The Commission is of the opinion that the "experience factor" proposed by the Company should not be adopted for this proceeding in order to reserve judgment regarding use of the "experience factor" for the entire Commission in Docket No. E-100, Sub 47. The Commission is also of the opinion that it should adopt a 1.686¢ per kWh base fuel component in the rates for this proceeding in order to recognize a normalized generation mix which includes the necessary outage of the Robinson nuclear unit for major repairs. The 1.686¢ per kWh will reflect a total Company fuel cost (subject to fuel charge adjustments) of $461,335,900 (or $317,286,400 for North Carolina retail service), which level of fuel costs is concluded to be just and reasonable for the period of time the rates approved herein are expected to be in effect.

In evaluating the 1.686¢ per kWh base fuel component adopted herein, the Commission has carefully considered each element in the generation mix, including generation by nuclear fuel, fossil fuels and hydro, and including intersystem purchases and sales. The contribution by each element of the generation mix which was utilized to produce the 1.686¢ per kWh base fuel component is judged to be just and reasonable.

In setting the base fuel component of CP&L's rates in this case, the Commission has established a reasonable normalized level of fuel expenses which it anticipates to occur during the period of time the rates set herein are expected to be in effect. The Commission recognizes that the Robinson outage will have a distinctly adverse impact on the Company's operations and

earnings. However, the Commission acknowledges the fact that the level of fuel revenues contained herein may exceed the level of fuel expense incurred by the Company prior to the time the Robinson plant is actually shut down for modifications and repairs. Likewise due to the use of a six-month outage, the level of fuel expense incurred by the Company subsequent to the outage is likely to exceed the level of fuel revenues contained herein. In recognition of these facts the Commission finds it appropriate to authorize the Company to establish a deferred account for purposes of levelizing fuel revenues prior to and subsequent to the scheduled Robinson outage for modifications and repairs. The status of such deferred account shall be reported to the Commission no later than one year or thirty days prior to the beginning of the hearings in CP&L's next general rate proceeding. The status of this account is to be made available to the Public Staff at any time.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 14

The evidence for this finding is found in the testimony and exhibits of Company witnesses Watson and Nevil, and Public Staff witnesses Carrere and Winters.

Company witness Watson recommended a system coal inventory, as further adjusted by Company witness Nevil to exclude Power Agency ownership, of 2,104,956 tons. Public Staff witness Carrere recommended a system coal inventory level of 1,593,516 tons. Both parties relied upon the maximum drawdown method, variations of which have been utilized by the Public Staff and/or the Company in previous rate cases and have been adopted by the Commission in Docket Nos. E-2, Subs 391, 416 and 444.

The Company used the 110-day period from December 6, 1977, to March 26, 1978, having a maximum drawdown of 1,260,000 tons in its coal inventory. The 110-day period utilized by the Company represents the longest period during which coal deliveries were interrupted by a coal strike.

The Public Staff used the 130-day period from March 29, 1981, to August 2, 1981, having a maximum drawdown of 1,399,528 tons in the Company's coal inventory. The 130-day period utilized by the Public Staff included a 76-day U.M.W.A. miners strike followed by 54 days of miners' vacation. The 130-day period represents the longest period during which coal deliveries were interrupted by a coal strike or otherwise.

The Company translated the 1,260,000 tons drawdown during the 110-day period to current levels by means of daily burn rates for coal. The Company utilized 16,326 tons per day to represent the daily burn rate during the 110-day period, and it utilized 27,274 tons per day to represent the current daily burn rate. Multiplying the 1,260,000 ton drawdown by the ratio of 27,274 tons/day to 16,326 tons/day yields the 2,104,956-ton coal inventory recommended by the Company.

The Public Staff translated the 1,399,528 ton drawdown during the 130-day period to current levels by means of coal-fired generating capacity. The Public Staff utilized the 4,473 mW coal generating capacity available during the 130-day period and the current coal generating capacity of 5,093 mW including Mayo. Multiplying the 1,399,528 ton drawdown by the ratio of 5,093 mW to 4,473 mW yields the 1,593,516 ton coal inventory recommended by the Public Staff.

At the March 1983 coal inventory price of $48 per ton, the Company's requested 2,104,956-ton coal inventory represents an investment of $101,037,888 total Company (or $69,489,429 for North Carolina retail service). At the same prices, the Public Staff's recommended 1,593,516-ton coal inventory represents an investment of $76,488,768 total Company (or $52,605,624 for North Carolina retail service). DOD witness McCabe supported the Public Staff position.

Witness Carrere contended that daily burn rates can be highly volatile due to changes in system generation mix, availability of alternative fuels or sources of supply, and fluctuations in system load. The Commission is of the opinion that actual daily burn rates must be considered in establishing the proper level of coal inventory for the system, even though said daily burn rates tend to be unstable from month to month. The Commission observes that neither the Company nor any other party to this proceeding attempted to normalize the daily burn rates utilized in the calculations.

The Commission concludes that the coal inventory requested by the Company, representing an investment of $69,489,429 for North Carolina retail service, is appropriate for this proceeding.

Company witness Watson requested a total liquid fuels inventory, as adjusted by Company witness Nevil to exclude Power Agency ownership of $9,461,848 total Company (or $6,507,444 for North Carolina retail service). The inventory would consist of 9,413,000 gallons of No. 2 oil at 86.14¢ per gallon, plus 2,365,000 gallons of propane at 57.23¢ per gallon. The 9,413,000 gallons of No. 2 oil represents a maximum two-month drawdown during 1977-78.

Public Staff witness Carrere recommended a No. 2 oil inventory of $6,408,988 total Company (or $4,407,821 for North Carolina retail service). The inventory would consist of 7,440,200 gallons of No. 2 oil at 86.14¢ per gallon representing a one-year supply at 1979 daily burn rate levels. The currently allowed oil inventory was established in 1979.

In the prior rate proceeding in Docket No. E-2, Sub 444, the Commission allowed a 23,000,000-gallon oil inventory. The actual oil inventory at the end of the test period in this proceeding was 14,448,144 gallons. The Commission concludes that the No. 2 oil inventory requested by the Company, representing an investment of $8,108,358 total Company (or $5,576,573 for North Carolina retail service) is appropriate for this proceeding.

The Commission further concludes that a $76,079,959 working capital allowance for fuel inventory is appropriate for North Carolina retail service in this proceeding, consisting of the $69,489,429 coal inventory, the $6,507,444 liquid fuel inventory, and $83,086 miscellaneous fuel stock.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 15

Company witnesses Bradshaw, Faucette, Watson, Nevil, and McClellan and Public Staff witnesses Winters and Carrere offered testimony regarding the reasonable working capital allowance. The following chart summarizes the North Carolina retail amounts the Company and Public Staff contend are the proper levels of the components of CP&L's working capital allowance to be used in this proceeding:

(000's Omitted)

Item	Company	Public Staff
Cash	$ 3,467	$ 3,467
Materials and supplies - fuel stock	76,080	57,896
Materials and supplies - other	19,991	19,991
Prepayments	6,594	6,594
Investor funds advanced for operations	32,567	17,413
Miscellaneous projects	9,921	4,943
Other rate base deductions	(8,187)	(6,626)
Customers deposits	(5,898)	(5,898)
Total allowance for working capital	$134,535	$97,780

The parties are in disagreement over the proper amount of materials and supplies - fuel stock, investor funds advanced for operations, miscellaneous projects, and other rate base deductions. The Commission will now analyze the testimony regarding these differences.

The first difference between the parties is the level of materials and supplies - fuel stock recommended for use in this proceeding. This difference of $18,184,000 is discussed in the Evidence and Conclusions for Finding of Fact No. 14. Consistent with the determinations made by the Commission in Finding of Fact No. 14 regarding this issue, materials and supplies--fuel stock of $76,080,000 is included as the reasonable level of fuel stock to be included in the working capital allowance in this proceeding.

The next difference between the parties is the level of investor funds advanced for operations recommended for use in this proceeding. The $15,154,000 difference between the amounts proposed by the Company and Public Staff results from the adjusted versus per books lead-lag study, the treatment of federal income tax lag differences and the treatment of average employee and use taxes held.

The first issue the Commission must resolve is whether to use the lead-lag study adjusted for pro forma adjustments and the proposed rate increase as recommended by the Company or the per books lead-lag study as recommended by the Public Staff. The Public Staff contends that the per books lead-lag study, adjusted to reflect 100% of the closings related to the Power Agency sale and the removal of the Leslie and McInnes coal mine loss from the cost of service, provides a reasonable level of investor-supplied funds before reduction for any incidental collections. Public Staff witness Winters testified as follows regarding the use of the per books study of average employee and use taxes held.

> "The Commission, in Docket Nos. E-2, Sub 444, 416, and 391, CP&L's last three general rate cases, has ruled, `...a lead-lag study, applied to the per books amounts of cost of service, is the more reasonable approach to use in determining the investor funds advanced for operations.' The Commission has also ruled in Docket No. G-5, Sub 157, a general rate case involving Public Service Gas Company, that `...a lead-lag study applied to the per books cost of service results in a fair and reasonable analysis of the subject company's cash working capital needs.' I believe the per books computation provides a reasonable representation of investor funds because it is based upon the Company's actual experience for the test-year."

Company witness McClellen presented rebuttal testimony and contended that accounting and pro forma adjustments should be considered, because the end-of-period level of revenues and expenses adjusted for the proposed increase more nearly reflects the cost of service for the period in which the rates will be in effect. Witness McClellen also criticized the Public Staff for adjusting the per books cost of service to reflect 100% closings for the Power Agency sale and to eliminate the Leslie and McInnes coal mining losses.

Public Staff witness Winters testified that the adjustments to the per books study proposed by the Public Staff increased working capital by approximately $500,000 and that if the working allowance had been calculated based upon the Public Staff's cost of service after proposed rates, the working capital allowance would have been substantially the same.

The Commission has evaluated and reviewed the results of the Company's end-of-period lead-lag study and finds that the results of the study are inappropriate. The main problem area of CP&L's end-of-period lead-lag study is its classification of federal income taxes. As can be seen by examining McClellan Rebuttal Exhibit No. 2, line 34, columns (f) and (h), CP&L has assigned 90% of the income taxes associated with the proposed rate increase to investment tax credits. This is inappropriate since no adjustment has been made to adjust deferred income taxes to an end-of-period basis. The difference between end-of-period book depreciation expense and end-of-period income tax depreciation expense has not been determined. If this were done, deferred income taxes would increase and both investment tax credits and current income taxes would decrease. Also, if deferred income taxes were increased, it would not be appropriate to assign zero lag days to the increased amount unless the increased amount of deferred income taxes were deducted from rate base.

In addition, CP&L's treatment has the effect of recognizing a level of investment tax credits which have not been utilized and which will in all probability not be recognized in the future. The additional level of investment tax credits based on 90% of federal income taxes associated with the proposed rate increase will probably not be recognized in the future because of the increased level of deferred income taxes which is likely to be recognized in the future. Based on a certain level of federal income tax expense, the higher the level of deferred tax expense the lower the level of investment tax credits utilized. The Company's level of deferred income taxes as well as its level of interest expense, both operating interest expense and nonoperating interest expense, continue to increase. All these items will contribute to the likelihoood that CP&L's level of investment tax credits in the coming year will be less than the $92,644,000 adjusted amount as shown of McClellan Rebuttal Exhibit No. 2. This seems especially likely since investment tax credits of only $30,234,000 were utilized during the test year. Based on the likelihood that in the coming year the level of investment tax credits will be less than the end-of-period level indicated by CP&L, and the like likelihood that deferred income taxes will be greater than the end-of-period level indicated by CP&L, the Commission concludes that the per books level of income tax expense, as well as all other per books components of cost of service, with the exception of the adjustments for Leslie and McInnes coal mine losses and 100% Power Agency closing, is the appropriate level to use in determining investor funds advanced for operations.

The Commission finds witness Winters' adjustments to the per books lead-lag study of the 100% Power Agency closing and the cumulative write-off of the Leslie and McInnes coal mine losses appropriate. The adjustment for the 100% Power Agency closing represents a permanent change in operations which did not exist during the test year, but which will exist continuously from the final closing. In the Commission's opinion, the adjustment to remove the effect of Leslie and McInnes coal mine losses incurred since 1979 and written-off during the test year is appropriate because these losses are nonrecurring and it is not anticipated that losses of this magnitude will be incurred in the future. The Commission, therefore, finds that the per books method viewed in its entirety produces a reasonable level of working capital. The Commission concludes that the preponderance of the evidence in this case indicates that a lead-lag study applied to the per books cost of service, adjusted only for abnormal events, results in a fair and reasonable analysis of the Company's cash working capital needs.

The next item which the Commission must decide regarding investor funds advanced for operations is the proper federal income tax lag to be used in this proceeding. The Company proposed a 38-day lag based on the assumption that estimated income tax payments would be made in equal quarterly installments. Public Staff witness Winters proposed a 58.45-day lag based on the statutory requirements for filing estimated income tax payments. Witness Winters testified in that regard as follows:

> "I do not believe that the Company should pay its taxes faster than is legally required. Working capital requirements which arise from early payments of income taxes, in my opinion, should not be borne by the ratepayers. After all, the ratepayers have paid in through rates the funds used by the Company to pay those taxes. The Company's election to give those funds to the Federal Government earlier than is legally required diminishes the benefit which the ratepayers should receive from having paid them."

The Commission finds that the working capital calculation based on an early payment of income taxes as proposed by the Company is inappropriate and concludes that the appropriate lag for federal income taxes is 58.45 days.

The final item the Commission must decide regarding investor funds advanced for operations is whether incidental collections should be deducted in the calculation. Public Staff witness Winters deducted $1,296,000 for employee tax withholdings and $273,000 of North Carolina sales and use tax collections. Witness Winters testified in regard to this issue as follows:

> "After determining investor funds advanced for operations by multiplying the average daily cost of service by the net interval between the revenue lag and the expense lag, I have deducted the average amount retained before payment of employee tax withholdings and the North Carolina sales and use tax collections. These employee tax withholdings and sales tax collections represent funds which the Company has collected for later remittance to governmental agencies. Until they are remitted to the governmental agencies the Company has unrestricted use of these funds. They are, therefore, cost-free funds and should be deducted from investor funds advanced for operations in determining the total amount of investor funds which should be included in the working capital allowance."

The Company agrees as to the propriety of treating such deductions as cost-free capital. However the Company classifies these items as other rate base deductions to be discussed hereinafter.

The Commission finds that these incidental collections are in the nature of cost-free capital and are properly used as a reduction in the calculation of investor funds advanced for operations. The Commission further finds and concludes that the appropriate level of investor funds advanced for operations to be used in this proceeding is $17,413,000.

The next difference between the parties is the level of miscellaneous projects to be used in this proceeding. The Company included $4,978,000 in this account for the Brunswick cooling towers and the South River Project. Public Staff witness Winters removed these projects and testified regarding them as follows:

> "I have excluded the unamortized balance of the Brunswick cooling towers and the South River Project losses from the working capital allowance, because, in my opinion, these items are not used and useful in providing electric service. Counsel for the Public Staff has advised me that these abandoned projects do not meet the legal requirements for inclusion in rate base."

The Commission discusses this issue fully in the Evidence and Conclusions for Findings of Fact Nos. 8 and 9. Based on the conclusions reached therein the Commission finds it inappropriate to include the unamortized balance of the Brunswick cooling towers and the South River Project losses in rate base. Thus the Commission concludes that the appropriate level of miscellaneous projects is $4,943,000.

The final difference between the parties is the appropriate level of other rate base deductions. The $1,561,000 difference consists of $1,569,000 relating to differing categorization of average employee and use taxes by the Company and Public Staff. The Commission for purposes of this Order finds it appropriate to treat average employee and use taxes as a reduction in investor funds advanced for operations. The remaining difference relates to an adjustment made by Public Staff witness Winters to include $246,000 in other rate base deductions representing the accrual of an expense which was never paid by the Company. Although the Company agrees that the Public Staff's proposed adjustment is proper, the Company advocates using a production allocation factor to allocate the item to North Carolina retail operations. The Commission finds that it is proper to include this element of cost-free capital in other rate base deductions and that the Company's proposed allocation is proper.

In Evidence and Conclusions for Finding of Fact No. 7, the Commission discusses the treatment of the gain on the sale of property by CP&L to NCEMPA and the treatment of accumulated JDITC related to the sale. Consistent with the decisions made therein, the Commission finds that the unamortized portion of the gain on the sale of $17,105,000 and the unamortized portion of accumulated JDITC related to the sale of assets to NCEMPA of $781,000 should be included in other rate base deductions. Based upon the foregoing the Commission finds other rate base deductions of $24,503,000 appropriate for use in this proceeding.

The parties are in agreement as to appropriate levels of cash, materials and supplies - other, prepayments, and customer deposits; therefore, the Commission concludes that the appropriate level of allowance for working capital to be used for setting rates in this proceeding is $98,087,000 as shown in the chart below:

(000's Omitted)

Item	Amount
Cash	$ 3,467
Materials and supplies	96,071
Prepayments	6,594
Investor funds advanced for operations	17,413
Miscellaneous projects	4,943
Other rate base deductions	(24,503)
Customer deposits	(5,898)
Total allowance for working capital	$ 98,087

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 16

Company witnesses Spann, Vander Weide, Bradshaw, and Lilly, Public Staff witness Bright, Attorney General witness Stutz, Department of Defense witness McCabe, and Kudzu Alliance witness Eddleman presented evidence as to the proper level of construction work in progress (CWIP) to be included in rate base. In 1977, North Carolina G.S. 62-133(b)(1) was amended to provide for reasonable and prudent expenditures of CWIP after July 1, 1979, to be included in rate base. Since the effective date of that amendment, the Commission has approved the inclusion of CWIP in CP&L's rate base in four proceedings: NCUC Docket Nos. E-2, Sub 366; E-2, Sub 391; E-2, Sub 416; and E-2, Sub 444.

On June 17, 1982, G.S. 62-133(b)(1) was further amended to provide that reasonable and prudent expenditures for CWIP may be included in rate base to the extent the Commission considers such inclusion to be in the public interest and necessary to the financial stability of the utility involved. The current amount of CWIP included in CP&L's North Carolina retail rate base is $392,199,000. Of this amount, $173,865,000 is attributable to Mayo Unit No. 1 which began commercial operation in March 1983. The remaining amount of $218,334,000 is applicable to Harris Unit No. 1. The Company is requesting in this proceeding that $539,780,749 of CWIP relating to Harris Unit No. 1, net of Power Agency ownership, be included in its North Carolina retail rate base.

As the Commission has noted in previous Orders, the amount of CWIP in rate base determined to be appropriate results from the application of the following criteria: (1) the expenditure must be reasonable and prudent, (2) the inclusion must be in the public interest, and (3) the inclusion must be necessary to the financial stability of the utility in question.

Company witness McDuffie presented evidence indicating that the expenditures made for construction of Harris Unit No. 1 to date have been both reasonable and prudent. Company witness Sherwood Smith testified that the audit of the Company performed at the request of the Commission by the firm of Cresap, McCormick and Paget found that productivity at the Harris site appeared good and that the Company had a sound management approach to the Harris project. Public Staff witness Bright testified that there is no reason to believe expenditures on Harris Unit No. 1 to date have not been reasonable.

Attorney General witness Stutz testified on cross-examination that he had no evidence to offer that the expenditures for Harris Unit No. 1 CWIP were unreasonable.

A number of witnesses offered testimony on the public interest criterion. Company witness Spann presented a quantitative study and testimony that the inclusion of the Company's requested amount of CWIP would benefit ratepayers by minimizing the net present value of revenue requirements through the end of the century. Witness Spann pointed out that although the percentage difference was small, with and without CWIP in rate base, the magnitude of the dollars resulted in a net savings of approximately $350 million. Witness Spann testified that it is less costly on a present value basis to place CWIP in rate base in order to maintain an "A" bond rating than not to place CWIP in rate base and have CP&L's bonds downgraded with a commensurate increase in interest expense. Finally, Dr. Spann testified that inclusion of CWIP in rate base would help to smooth rates and minimize rate shock as new plants go into service.

Company witness Edge testified that 84% of the Company's residential customers and 87% of the Company's commercial and industrial customers have been on the Company's system for over seven years. Consequently, the Company expects that the majority of current Company customers would still be receiving service from the Company in 1986, the expected in-service date of Harris Unit No. 1. Witness Edge also testified that CWIP in rate base provides better pricing signals to consumers and reduces rate shock when a new generating unit is placed in service. Finally, witness Edge testified that assurance of adequate service in the future attracts industry to the area and benefits ratepayers through more and higher paying jobs, broader tax base, and improved economic outlook.

Public Staff witness Bright testified that inclusion of CWIP in rate base could result in lower future rates for ratepayers remaining in the service area, but that, in her opinion, such inclusion is seldom in the public interest due to the involuntary nature of the ratepayers' investment in a utility's construction program. Witness Bright recommended that $309,519,000 of Harris Unit No. 1 CWIP be included in rate base.

Attorney General witness Stutz took the position that CWIP inclusion should be considered in light of the inter-generational equity issue, the used and useful concept, and the relative cost/benefit to ratepayers. Witness Stutz recommended that only $218 million of CWIP for Harris Unit No. 1 be included in rate base.

Department of Defense witness McCabe stated that all CWIP should be excluded from rate base except for that amount previously authorized by the Commission of Harris Unit No. 1. Witness McCabe contended that inclusion of CWIP violated the traditional used and useful concept since customers would be paying for plants not yet in operation. Witness McCabe testified that in his opinion placing CWIP in rate base would not reduce the costs of construction.

Kudzu Alliance witness Eddleman testified that no CWIP should be included in rate base. Witness Eddleman stated that inclusion of CWIP is not cost effective and in reality is a forced loan from consumers to the Company.

The Commission finds that in determining whether the public interest is served, it is appropriate to consider a number of factors. Although the near term impact on present ratepayers is certainly an important factor, it is not totally dispositive of the issue. When the public interest is viewed in a broader sense, it becomes clear that CWIP in rate base may serve the public interest even if rates will be somewhat higher in the near term.

Evidence introduced in the proceeding has shown the relative importance of the inter-generational equity issue to be slight when the CWIP in question relates to a plant which will go into service in just a few years. Witness Edge's testimony that 84% of residential customers and 87% of the industrial and commercial customers are still receiving service from CP&L after seven years shows that the Commission can reasonably expect the vast majority of present ratepayers to be ratepayers on the system in 1986 when Harris Unit No. 1 goes into service.

In this proceeding, the quantitative evidence presented supports a finding that inclusion of CWIP at the level requested by the Company would result in lower revenue requirements on a net present value basis through the year 2000. This is consistent with the policy of providing power at the lowest cost over the life of the plant. The Commission is also of the opinion that ratepayers would benefit from the smoothing of rate increases to avoid rate shock and from the pricing signals that the Company's requested level of CWIP in rate base can provide. The Commission notes that $582 million of CWIP consisting primarily of pre-1979 construction expenditures on Harris Unit #1 is not included in the rate base. This amount in itself will cause a significant rate shock in 1986 when Harris #1 is completed and placed in rate base. Finally, the Commission finds that the public interest is served by the attraction of new industry through the assurance of adequate service in the future.

In considering the financial stability criterion, the Commission has examined the record with regard to the financial condition of the Company, the impact of CWIP inclusion, and the appropriateness of such inclusion versus some other method of ensuring the financial stability of the Company. Company witness Lilly testified that CP&L's fixed charge coverage at the end of the test year was 1.9 times, and its ratio of AFUDC included in return for common equity was almost 78% at the end of 1982. Witness Lilly further testified that the Company's forecast of construction expenditures from 1983 through 1985 is substantially greater than the industry average. Witness Lilly concluded that these factors contributed to the recent downrating of the Company's bonds and that absent considerable improvement in the Company's financial condition in the near future, another downrating is possible.

Company witness Spann testified that including approximately $500 million of CWIP in North Carolina rate base would result in improving some but not all of CP&L's financial indicators to the levels normally achieved by an average "A" rated utility. Witness Spann also stated the present value of revenue requirements is less if CP&L's cash earnings are improved by placing CWIP in rate base than by granting signficantly higher rates of return than those sought by CP&L in this case.

Public Staff witness Bright supported inclusion of $309,519,000 of CWIP in North Carolina rate base in that such inclusion was necessary to the financial stability of the Company. Ms. Bright stated that the relatively high (60%)

ratio of construction to net plant and large amount of AFUDC (78%) as a percent of income created such necessity. Witness Bright stated that this amount of CWIP would result in the Company receiving a 2.3 times pretax interest coverage ratio excluding AFUDC, a ratio that would be indicative of financial stability.

Attorney General witness Stutz testified that CWIP should be reserved for utilities in dire financial situations, and CP&L did not meet this standard of financial instability. Witness Stutz recommended that only the continued allowance of $218 million of CWIP for Harris Unit No. 1 be authorized.

With regard to the financial stability criteria relating to the inclusion of CWIP in rate base, the Commission has considered a comparison of various financial ratios of CP&L relevant to this issue to similar financial ratios of the 100 electric utilities, reported by Salomon Brothers. The data was obtained from the March 31, 1983, issue of Salomon Brothers Electric Utility Quality Measurements.

Comparison of Various Financial Ratios
(March 31, 1983)

	CP&L	Average of 100 Electric Utilities	Average of 25 A-Rated Electric Utilities
Pretax coverage			
Including AFUDC	2.5	3.0	3.1
Excluding AFUDC	1.9	2.5	2.7
Equity Ratio	38%	40%	40%
AFUDC as a percentage of earnings	78%	49%	37%
Construction as a percentage of gross plant	62%	43%	44%
Internal cash generation	38%	62%	63%

It is obvious to the Commission based on the preceding analysis that the magnitude of CP&L's construction budget is placing the Company in an adverse financial position relative to other electric utilities in the country. Specifically CP&L's percentage of construction to gross plant is 62% as compared to 43% for the 100 electric utilities and 44% for the 25 "A" rated electric utilities. Similarly AFUDC as a percentage of earnings of 78% for CP&L materially exceeds the average of the 100 electric utilities of 49% and to the average of the 25 electric utilities with an "A" bond rating of 37%.

It is also noted by the Commission that due to the magnitude of the Company's construction budget relative to its total plant investment, the determination of this issue may be more critical to CP&L than other major electric utilities under the Commission's jurisdiction.

Based upon the foregoing, the Commission concludes that inclusion of some level of CWIP in the rate base of CP&L is imperative to the Company's financial stability and to its continued maintenance of an "A" bondrating. The Commission believes that the preponderance of the evidence in this case exemplifies the necessity of including some level of CWIP in rate base. Indeed with the exception of the Kudzu Alliance, all intervenors in the proceeding advocated the inclusion of some level of CWIP in rate base. The Commission recognizes that the amount of CWIP to be included in rate base is

somewhat judgmental since the Commission must determine what level of reasonable and prudent expenditures for CWIP in rate base is necessary to CP&L's financial stability and what level is in the best interest of the ratepayer.

It is the finding of this Commission from the evidence presented that the financial stability of CP&L requires the inclusion of the Company's requested amount of CWIP in rate base. The Commission has determined that inclusion of $539,780,749 of CWIP associated with Harris Unit No. 1 represents reasonable and prudent expenditures, is in the public interest, and is necessary for the Company's financial stability.

Another issue raised by the Public Staff was the treatment of AFUDC on pre-July 1, 1979, CWIP balances. Public Staff witness Bright testified that she had been advised by counsel that it was not legally permissible to include in rate base any CWIP which represented AFUDC accrued since July 1, 1979, on any pre-July 1, 1979, CWIP balances. As the Commission has stated in the past, AFUDC on CWIP expenditures is as much a part of the cost of construction as the cost of bricks and mortar or labor. Therefore, even though a portion of the AFUDC accrued since July 1, 1979, relates to CWIP balances created prior to July 1, 1979, it is the Commission's opinion that AFUDC is a current cost of construction just like any other cost that occurred after July 1, 1979, on a project that was begun prior to that date. AFUDC on pre-July 1, 1979, property which accrued after July 1, 1979, is therefore found by the Commission to be proper for inclusion in CWIP receiving rate base treatment.

The Public Staff also raised an issue during cross-examination of Company witness Bradshaw concerning the derivation of the AFUDC rate used by the Company subsequent to the Commission Order in Docket No. E-2, Sub 444. Company witness Bradshaw indicated that the Company has used a rate for equity of 15.5% based on the Commission Order in that case. The Public Staff disputes this equity rate and believes instead that a rate of 14.5% should have been used. The Commission found in the last case that the appropriate rate of return on equity for CP&L was 15.5% but reduced such return to 14.5% as a penalty for the 1981 Brunswick outage for the purposes of calculating the revenue requirements of the Company. In the Commission's opinion, reducing the AFUDC rate which would penalize the Company into the future for past performance, would be a greater penalty than the Commission intended in its last general rate Order. The Commission believes that any further penalty in the allowed AFUDC rate would be clearly inappropriate and, therefore, finds the Company's computation of its AFUDC rate appropriate. Further in Evidence and Conclusions for Findings of Fact Nos. 20 and 21, the Commission finds a return on equity of 15.25% fair and reasonable for CP&L under prudent management but has imposed a rate of return penalty for the reason stated therein of .75% on the Company. Consistent with its previous findings the Commission finds that 15.25% is the appropriate rate of return on equity to be used by the Company in calculating its AFUDC rate in the future.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 17

Company witnesses Bradshaw and Faucette, Department of Defense witness McCabe, Kudzu Alliance witness Eddelman, and Public Staff witness Winters presented testimony regarding the reasonable original cost of the Company's investment in electric plant. The following chart summarizes the amounts which the Company and the Public Staff contend are the proper levels of the original cost of CP&L's electric plant to be used in this proceeding.

(000's Omitted)

Item	Company	Public Staff
Electric plant in service	$2,432,859	$2,431,733
Net nuclear fuel	25,172	25,386
Construction work in progress	539,781	309,519
Working capital	134,535	97,780
Accumulated depreciation	(557,168)	(558,731)
Accumulated deferred income taxes	(263,249)	(313,632)
Total	$2,311,930	$1,992,055

As is reflected above, the total net difference between the Company and the Public Staff is $319,875,000. The first item on which the parties disagree is the appropriate amount of electric plant in service. A difference of $1,126,000 exists between the amounts proposed by the Company and Public Staff and results from an adjustment made by Public Staff witness Winters to remove the allowance for funds used during construction (AFUDC) accrued on Roxboro Unit No. 4 during the period September 15, 1980, to September 24, 1982.

Public Staff witness Winters testified regarding this adjustment as follows:

> "In CP&L's last general rate case the Commission determined that the AFUDC accrued on 4.97% of Roxboro Unit 4 should not be included in rate base. That determination was made based on the Commission's decision in the preceding case, Docket No. E-2, Sub 391, that CP&L should not be allowed to earn a return on 4.97% of Roxboro Unit 4. However, CP&L accrued AFUDC on that portion of Roxboro during the period it was not allowed in rate base and is again attempting in this case to put that accrued AFUDC into rate base. If the Company is allowed to do this, the Commission's earlier adjustment will be negated. Consequently, I have made an adjustment to remove this AFUDC from rate base and to remove the related depreciation expense from the cost of service. The impact of my adjustment is to reduce gross revenue requirements by approximately $264,000."

Company witness Bradshaw testified that, in his opinion, the Commission should reconsider its decision; because it, in effect, made the stockholders guarantors that vendors will meet design specifications without having to perform warranty work.

The Commission carefully considered this issue in CP&L's last general rate proceeding. In making its decision in that case the Commission considered the context in which the Company undertook to remedy the problems at Roxboro Unit 4 and the fact that such remedies may have only been rigorously pursued upon the prompting of the Commission. Based upon the considerations made in the Company's last general rate proceeding, the Commission concludes that AFUDC accrued on Roxboro Unit No. 4 in the amount of $1,126,000 should be excluded from electric plant in service in this proceeding.

The next item on which the Company and Public Staff disagree is net nuclear fuel. The $214,000 difference between the Company's and Public Staff's position relates solely to an adjustment proposed by the Company to eliminate the Power Agency ownership from net nuclear fuel. The Commission finds it

appropriate to exclude from net nuclear fuel that portion owned by the Power Agency and thus finds net nuclear fuel of $25,172,000 reasonable and proper.

The next item of disagreement between the Company and Public Staff is Construction Work in Progress (CWIP). Consistent with the decision made in this regard in Finding of Fact No. 16, the Commission finds CWIP of $539,781,000 appropriate for use herein.

The next item of difference between the Company and Public Staff relates to the working capital allowance. In Finding of Fact No. 15, the Commission finds it reasonable to include in rate base a working capital allowance of $98,087,000.

The Company and the Public Staff are in disagreement regarding the proper amount of accumulated depreciation to be used for setting rates in this proceeding. The difference between the Company's and Public Staff's position of $1,563,000 consists of an adjustment related to AFUDC accrued on Roxboro Unit No. 4 during the period September 15, 1980, through September 24, 1982, of $41,000 and an adjustment proposed by Public Staff witness Winters of $1,604,000 regarding the Brunswick plant augmented off-gas system.

The Commission, having previously found that the AFUDC accrued on the Roxboro Unit No. 4 plant from September 15, 1980, to September 24, 1982, should be excluded from plant in service, correspondingly finds that the related accumulated depreciation should be adjusted accordingly.

The Commission will now discuss the adjustment made by Public Staff witness Winters regarding the Brunswick plant augmented off-gas system.

> "In its final order in CP&L's last general rate case, Docket No. E-2, Sub 444, this Commission ruled that the Brunswick plant augmented off-gas system should not be included in rate base. In its Order of September 24, 1982, the Commission stated:
>
> > 'Witness Jacobstein testified that the Augmented Off Gas System (AOG) is a system designed to remove radioactive gases which are sometimes produced from atomic fission and released through the main condenser at the Brunswick plant. These radioactive gases must be filtered and allowed to decay before release from the plant. Witness Jacobstein further testified that the AOG was of an experimental design which was plagued by explosions during its testing phase. The Company abandoned testing of the system in approximately 1976 and did not repair or replace it. The AOG has thus never functioned during the plant's history.'
>
> During the test period in this case the Company retired this equipment. In doing so the Company accounted for it as an ordinary retirement by crediting electric plant in service and by debiting the depreciation reserve. The net effect of the Company's proposed treatment of this item leaves the rate base at the same level after the retirement as before. If the Company's treatment of the item is not adjusted, the Company will now be allowed to earn a return on funds which the Commission ruled in the last general rate case should be 'removed' from rate base as property not used and useful in the

production of electricity.' Thus, I have made an adjustment reducing rate base for this item."

The Commission has carefully reviewed the testimony regarding this issue and concludes that the retirement of the augmented off-gas system should be treated as an extraordinary retirement and that the balance of accumulated depreciation be increased by $1,604,000. However, the Commission believes that it is entirely reasonable and proper for the Company to recover its investment in the Brunswick augmented off-gas system while excluding the investment from rate base. Thus the Commission finds it appropriate to amortize to test period operating revenue deductions the extraordinary retirement of the Brunswick plant augmented off gas system. Further the Commission finds a three-year amortization period for the retirement appropriate.

The Commission finds it necessary to make a further adjustment to accumulated depreciation relating to decommissioning costs. The methodology used by the Company to adjust for future decommissioning of its nuclear units utilizes in part CP&L's capital structure, embedded cost of debt and preferred stock, and return on common equity. In Findings of Fact Nos. 20 and 21 contained herein the Commission establishes the capital structure, cost rates, and return on equity appropriate for setting rates for CP&L in this proceeding. Since the decisions made by the Commission in this regard differ from that proposed by the Company, it is necessary to modify the Company's proposed adjustments for decommissioning cost to reflect the decisions made herein. The Commission, therefore finds it appropriate to increase depreciation expense and accumulated depreciation by $631,000 and to decrease deferred income taxes and accumulated deferred taxes by $311,000. Based upon the foregoing, the Commission finds accumulated depreciation of $559,362,000 proper for setting rates in this proceeding.

The final area of disagreement between the Company and the Public Staff relates to the amount that should be reflected for accumulated deferred taxes. The $50,383,000 difference between the Company's and the Public Staff's proposals relates to the accumulated deferred taxes associated with the gain on the sale of property to NCEMPA. As discussed in Evidence and Conclusions for Finding of Fact No. 7, the Commission finds it appropriate to increase accumulated deferred taxes by $50,383,000.

The Commission concludes, based upon the foregoing, and the decisions made in Findings of Fact Nos. 15 and 16 that the proper level of the Company's investment in electric plant in service for use herein is $2,124,003,000; that the reasonable allowance for working capital is $98,087,000, including deferred debits and credits; and that the proper rate base for use herein is $2,222,090,000 as detailed below:

(000's Omitted)

Item	Amount
Electric plant in service	$2,431,733
Construction work in progress	539,781
Net nuclear fuel	25,172
Working capital	98,087
Less: Accumulated depreciation	(559,362)
Accumulated deferred taxes	(313,321)
Total rate base	$2,222,090

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 18

Company witness Chapman and Public Staff witness Dennis presented testimony relative to the appropriate level of revenues under present rates to be included in this proceeding. The difference between the revenues proposed by the Company and the revenues proposed by the Public Staff relates solely to the amount of supplemental revenues from NCEMPA. The Company includes $1,103,090,000 as the end-of-period level of operating revenues whereas the Public Staff included $1,101,548,000. The difference of $1,542,000 is due solely to the different levels of NCEMPA supplemental revenues and consists of both a fuel-related adjustment and a nonfuel related adjustment.

The Company has treated the supplemental revenues from NCEMPA as properly allocable to current customers of the Company. Allocation of these revenues to North Carolina retail customers has the effect of lowering the revenue increase that would otherwise be requested. However, any expenses incurred by the Company in providing this service are also allocated to current customers. The net result is that any difference between expenses and revenues related to supplemental sales will be allocated to present customers. This means that retail customers could benefit if revenues exceed expenses or incur additional costs if expenses exceed revenues. The Public Staff did not take issue with the Company's treatment of NCEMPA Supplemental Revenues and related expenses as properly allocable to the current customer of the Company. Indeed, the Public Staff's methodology in this regard is identical to that of the Company. The Commission finds it appropriate to treat the NCEMPA supplemental revenues and related expenses as proper components of the Company North Carolina retail operations for purposes of setting rates in this proceeding.

The Company has calculated the test year Supplemental Revenues in accordance with the Power Coordination Agreement but has made adjustments for known changes including: the rate of return requested in this case, the inclusion in plant in service of Mayo Unit No. 1 on an annualized basis, and fuel expenses equal to the Company's proposed base fuel cost.

Public Staff witness Dennis testified that the Company should have priced the supplemental revenues using end-of-period balances rather than test year 13-month balances for investment, accumulated depreciation, accumulated deferred income taxes, and plant held for future use, as well as adjusted test year expense levels. Witness Dennis maintained that the Company's methods are inconsistent with the traditional rate-making process followed by the Commission.

The Company makes the argument that the methodology followed by the Public Staff also fails to correspond completely to the rate-making methodology

adhered to by the Commission since components of the investment base for the NCEMPA differ from components of the rate base determined by this Commission. The Company further argues that although neither the Company nor the Public Staff has strictly followed the Power Coordination Agreement (PCA) and neither made all of the adjustments that could be made, the Company's treatment is substantially closer to the provisions of that agreement.

The Commission concludes that it is appropriate to calculate supplemental revenues utilizing end-of-period investment balances in the manner advocated by the Public Staff. In making its decision the Commission recognizes that the Power Coordination agreement is a negotiated contract between the NCEMPA and CP&L. However, the Commission can find no plausible reason for not adjusting NCEMPA supplemental revenues and related expenses to an end-of-period level which can be anticipated to occur in the future.

The Commission notes that this issue is directly analogous to the establishment of end-of-period toll service revenues in telephone company rate proceedings where the telephone company is settling on an actual cost basis. As the investment base in the PCA differs from that used by this Commission, it is likewise true that the investment base for toll settlement purposes differs from that used by this Commission to set rates for telephone companies under its jurisdiction. Likewise average investment balances and actual expenses are used in the toll settlement process as in the PCA. The Commission has followed a methodology for many years in telephone rate proceedings, of adjusting toll settlement revenues to an end-of-period level using end-of-test period level of investment. The Commission thus finds it proper to adjust NCEMPA supplemental revenues to an end-of-period level that can be anticipated to occur on an ongoing basis in the future.

Both parties spoke of the difficulty and the time required to adjust the per books amounts of supplemental revenues. Undoubtedly much of the difficulty involved results from the newness of the contract and lack of familiarity in dealing with this issue for rate-making purposes. The Commission finds that the Company should in its next general rate proceeding file all data and information necessary to make the end-of-period calculations similar to those found fair herein by the Commission. Company witness Chapman suggested that an alternative to the process of adjustments would be to allocate the NCEMPA supplemental sales separately as a class and to assign directly the supplemental revenues to that class consistent with the treatment of any retail rate class. The result of this separate allocation would be that any difference between revenues and expenses would no longer fall to North Carolina retail customers. Instead, any excess or shortfall would fall to the Company stockholders. The Company did not file sufficient information to make such determinations in this proceeding. However, should the Company find it prudent to use such methodology in its next general rate proceeding, the Commission directs the Company to file such information in addition to the information previously required herein.

The next issue to be resolved regarding supplemental revenues relates to the proper rate of return on common equity to be used in calculating supplemental revenues. Witness Dennis testified that the contracts between NCEMPA and CP&L provide that NCEMPA pay CP&L a return on certain investments in utility property. The common equity portion of that return to be paid by NCEMPA is specified to be the common equity rate of return granted by this Commission in the Company's most recent general rate proceeding minus .75%.

The Company is requesting a 15.5% of return on common equity in this proceeding. Alternatively, the Public Staff is recommending a 13.5% return on common equity.

The Commission, in agreeing with the end-of-period concept of calculating an ongoing level of supplemental revenues, also agrees that the common equity rate found fair in this proceeding, less .75%, as specified in the contract between NCEMPA and CP&L, should be used in calculating those supplemental revenues. In accordance with Finding of Fact No. 21, that 14.50% is the reasonable rate of return on common equity, the Commission concludes that 13.75% (14.50 - .75%) is the correct rate of return to use in calculating NCEMPA supplemental revenues.

The final issue to be resolved regarding operating revenues relates to the fuel-related supplemental revenues. Public Staff witness Nightingale presented testimony on the impact of the Power Agency on CP&L's system fuel cost. Basically, witness Nightingale used the actual test period Power Agency impact ratio as a proxy for the impact in his fuel normalization discussed in Evidence and Conclusions for Finding of Fact No. 13. Witness Nightingale stated that the overall impact of the Power Agency as a ratio of the Company's total system "fuel only" cost remained relatively constant over a wide range of possible generation mixes.

As noted by witness Nightingale the proportions of the Power Agency relative to CP&L's "fuel only" fuel cost remained fairly constant over a varied range of generation mixes. The Commission finds the Public Staff's position in this regard reasonable. However, for purposes of this case the Commission has utilized the Company's methodology with regard to fuel expenses. The Commission therefore concludes that it is proper to adjust supplemental revenues to reflect the impact of changes in fuel costs that are associated with the adjusted fuel factor found appropriate in this proceeding. The base fuel factor of $.01686 found proper by the Commission is fully discussed in Evidence and Conclusions for Finding of Fact No. 13. Based on the Commission's findings therein, a fuel adjustment to increase supplemental revenues of $1,527,000 is found to be proper. In summary, the Commission finds that the rate-making treatment of both nonfuel related supplemental revenues from NCEMPA advocated by the Public Staff and the fuel supplemental revenues adjusted to reflect the fuel factor previously found fair herein is proper. The Commission finds test period operating revenues of $1,105,194,000 appropriate for use herein.

In addition to the issues discussed above which were contested among the parties to this docket, the Company included in its filing a number of adjustments to reflect a 100% closing of the sale to NCEMPA. No objection has been made to these adjustments, and they are hereby approved.

The Commission recognizes that the sale of assets to the NCEMPA, when viewed as an overall package, has and will be of substantial benefit to the ratepayers of North Carolina. Although there is disagreement among the parties on the handling of certain aspects of the sale, no party has contested the substantial overall benefit of the sale to the Company's ratepayers.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 19

The evidence for this finding of fact is found in the testimony and exhibits of Company witnesses Bradshaw, Nevil, Chapman, and McClellen, and Public Staff witnesses Nightingale, Lam, Winters, and Carter.

The following schedule sets forth the amounts proposed by the Company and the Public Staff.

(000's Omitted)

Item	Company	Public Staff
Operation and maintenance expenses	$649,145	$598,366
Depreciation expense	91,755	91,714
Taxes other than income	82,223	81,892
Income taxes	92,917	122,306
Total operating revenue deductions	$916,040	$894,278

As the above chart indicates, the parties are in disagreement over all of the items of operating revenue deductions. The Commission will now analyze the reasons for these differences.

The first difference between the parties is the level of operation and maintenance expenses recommended for use in this proceeding. The chart below summarizes the components of this difference of $50,779,000.

(000's Omitted)

Item	Amount
Leslie and McInnes coal losses	$ 6,520
Fuel expenses	44,259
Total	$50,779

The first component of the difference arises from an adjustment made by Public Staff witness Carter regarding the proper amount of losses attributable to the purchases of coal from affiliated coal mines. The Commission fully discussed this issue under Evidence and Conclusions for Finding of Fact No. 10 contained herein and concludes that operation and maintenance expenses should be reduced by $6,519,808 for this item.

The next area of disagreement concerns the proper level of fuel expense that should be included in operating expenses. Consistent with the conclusions contained in Evidence and Conclusions for Finding of Fact No. 13, wherein the proper base cost of fuel was determined to be $.01686 per kWh, the Commission finds total fuel expense of $352,616,000 consisting of base fuel expense and handling and analysis charges appropriate for use herein.

Based upon the foregoing discussion, the Commission finds operation and maintenance expenses of $618,932,000 just and reasonable.

The next item on which the parties disagree is depreciation expense. The $41,000 difference in the party's proposals results from the adjustment made by the Public Staff to remove the depreciation expense related to the AFUDC accrued on Roxboro Unit No. 4 from September 15, 1980, through September 24, 1982. The Commission has previously concluded in Evidence and Conclusion for

Finding of Fact No. 17 that AFUDC relating to Roxboro Unit 4 should not be included in rate base; therefore, the Commission finds and concludes that depreciation should be reduced by $41,000 for this item.

In Evidence and Conclusions for Finding of Fact No. 17, the Commission also discussed the appropriate rate-making treatment of the retirement of the Brunswick augmented off-gas system. Consistent with the previous decision made in this regard, the Commission finds it appropriate to increase depreciation expense by $535,000 for amortization expense related to the Brunswick augmented off-gas system.

The Commission finds it necessary to make a further adjustment to depreciation expense relating to decommissioning expense. The calculation of test period decommissioning expense proposed by the Company and approved by this Commission in previous general rate proceedings is dependent in part upon the capital structure, embedded cost of debt, and preferred and rate of return on equity found fair by this Commission. Since the findings of the Commission differ from that proposed by the Company, it is necessary to adjust decommissioning expense to reflect the impact of the capital structure, embedded cost of debt and preferred and rate of return on equity found fair by this Commission in Findings of Fact Nos. 20 and 21. Thus the Commission finds it appropriate to increase the decommissioning expense proposed by the Company by $631,000.

Based upon the foregoing, the Commission finds depreciation expense of $92,880,000 appropriate for use herein.

The next item on which the parties disagree is the proper level of taxes other than income which should be used in this proceeding. The chart which follows summarizes the components of this difference of $330,000.

Item	Amount
Property taxes on Roxboro No. 4 AFUDC	$ 7,000
Property taxes related to Public Staff	323,000
Total	$330,000

The $7,000 component of the difference results from an adjustment made by the Public Staff to remove property taxes from the cost of service related to the AFUDC accrued on Roxboro Unit No. 4 from September 15, 1980, through September 24, 1982. The Commission has concluded in another section of this Order that this amount of AFUDC should not be included in rate base; therefore, the Commission concludes that property tax expense should be reduced by $7,000.

The other area of disagreement between the parties with respect to year-end property taxes relates to the appropriate property tax rate to use in the calculation of property taxes allowable as an expense. Public Staff witness Winters used a property tax factor for the calendar year ended December 31, 1982; whereas Company witness Faucette used a property tax factor for the calendar year ended December 31, 1981. Both factors were calculated using Plant in Service balances before full NCEMPA ownership is excluded. The result is an adjustment proposed by witness Winters to decrease property taxes by $449,000.

This Commission concludes that the property tax factor used should be determined on the most recent calendar year figures as proposed by the Public Staff. It should, however, be adjusted to exclude full Power Agency ownership to be consistent with all other amounts in this case. Therefore, the Commission has calculated a property tax rate using calendar year-end December 31, 1982, taxes paid and property investment, but excluding full NCEMPA ownership. This rate is .06565 and results in a decrease in property taxes of $126,000 from the amount calculated by the Company. The Commission finds taxes other than income of $82,215,000 appropriate for use herein.

The next difference relates to state and federal income taxes. Since the Commission has not accepted all of either the Company's or the Public Staff's components of taxable income, it is necessary to calculate state and federal income taxes based on the findings heretofore and herein made by the Commission. The only substantial differences between the parties, with respect to the level of income tax expenses, relate to two adjustments made by Public Staff witness Winters: an adjustment to eliminate the Company's adjustment as related to the job development investment tax credit (JDITC) in calculating interest expense and an adjustment to eliminate the accumulated investment tax credits with respect to property which CP&L sold to the NCEMPA.

The Public Staff's adjustment to include JDITC imputed interest in the interest expense deduction decreases taxes and has the effect of reflecting JDITC at less than the overall rate of return. The Public Staff has taken this position in the last four rate cases, and the Commission in those cases has ruled that the Public Staff's position is improper. The Commission has been upheld by the North Carolina Court of Appeals. State ex. rel. Utilities Commission v. Carolina Telephone & Telegraph Co., 61 N.C. App. 42 (1983). The Commission is aware of no new evidence presented in this case which would warrant a change and, therefore, concludes that the JDITC imputed interest should not be used as a deduction for purposes of calculating income taxes.

The second JDITC adjustment proposed by the Public Staff relates to property sold to NCEMPA. This issue was fully discussed in Evidence and Conclusions for Finding of Fact No. 7 wherein the Commission found it appropriate to treat JDITC related to property sold to NCEMPA as an addition to the gain on the sale. Thus the Commission finds the adjustment to income tax expense proposed by the Public Staff inappropriate. The Commission finds income tax expense of $110,380,000 reasonable for use herein.

Based on the previous findings, the Commission concludes that total operating revenue deductions are $904,407,000 as shown on the chart below.

(000's Omitted)

Item	Amount
Operation and Maintenance Expenses	$618,932
Depreciation expense	92,880
Taxes other than income	82,215
Income taxes	110,380
Total operating revenue deductions	$904,407

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 20 AND 21

Three witnesses testified in the area of capital structure and cost of capital. The Company offered the testimony of Sherwood H. Smith, Chief Executive Officer and Chairman of the Board of Directors of CP&L, Edward G. Lilly, Jr., Senior Vice-President and Chief Financial Officer of CP&L, and Dr. James H. Vander Weide, Professor at the School of Business Administration at Duke University. The Public Staff offered the testimony of Dr. Caroline M. Smith, Senior Economist with the firm of J. W. Wilson & Associates, and consultant to the Public Staff. The Department of Defense offered the testimony of John W. McCabe III regarding this issue. In addition, the Company offered rebuttal testimony of Archie W. Futrell, Jr., Director of the Economic and Energy Forecast and Special Studies of CP&L, on the subject of Public Staff witness Smith's growth estimates for determining CP&L's cost of equity.

Company witness Lilly testified on the financial plans of CP&L. In his original testimony, witness Lilly recommended that rates be set in this proceeding upon a hypothetical or "normalized" capital structure consisting of 49.5% debt at a cost of 9.59%, 12.5% preferred and preferenced stock at a cost of 8.96%, and 38% common equity with a required return of 15.5%. Witness Lilly testified that the actual capital structure at September 30,1983, was comprised of 48.98% long-term debt, 13.15% preferred stock, and 37.87% common equity.

Public Staff witness Smith testified that the overall rate of return which CP&L should be allowed to earn was 11.00%. Witness Smith's recommendation was derived using the Company's requested hypothetical capital structure and senior security costs rates, and included a common equity return of 13.50%.

After considering all of the evidence presented by the parties on these issues, the Commission concludes that the appropriate capital structure to be used in this proceeding is as follows:

Item	Percent
Long-term debt	49.5%
Preferred stock	12.5%
Common equity	38.0%
Total	100.0%

Consistent with the evidence supporting the above capital structure, the Commission concludes that the appropriate reasonable embedded costs of long-term debt and preferred stock are 9.59% and 8.96%, respectively.

Company witness Vander Weide testified that the cost of equity capital for CP&L ranges from 16.5% to 17.0%. However, the Company's filing in this proceeding recognizes a requested equity return of 15.5%. Company witness Sherwood Smith testified that the Company requested a return on equity in this case of only 15.5% in recognition of the current economic conditions experienced by ratepayers, although in his opinion the Company can only do so on a short-term basis.

Company witness Vander Weide conducted two studies consisting of a discounted cash flow (DCF) study and a historical yield spread study in arriving at his recommended cost of equity capital for CP&L. The DCF method

utilized by witness Vander Weide assumes that the current market price of the firm's stock is equal to the discounted value of all expected future dividends. The DCF formula equates the investors' required return on equity capital to dividend yield plus expected growth in dividends per share.

Witness Vander Weide reviewed the past growth in CP&L's earnings and dividends per share for the last five- and 10-year periods. Additionally witness Vander Weide testified that he had reviewed published security analysts' projections of CP&L's future dividends and earnings growth. On the basis of his examination of the past growth rates, his review of analysts' projections, and his knowledge of current economic conditions, witness Vande Weide estimated the Company's expected growth rate to be in the range of 5% - 6% which, when added to his dividend yield, produced a cost of equity by the DCF method of 16.45% - 17.45%, centering on 17%.

The second study performed by Company witness Vander Weide was the historical yield spread study. The yield spread study equates investors' current expected return on equity to the sum of current bond yield plus the past differences or spread between the yields on stocks and the yields on bonds. Based upon the yield spread study, witness Vander Weide arrived at a cost of equity capital for CP&L of 18%.

In updating and summarizing his testimony from the witness stand, witness Vander Weide reevaluated his recommended return on an equity capital in the light of changes in economic and financial conditions subsequent to the time his prefiled testimony was prepared. On this basis Dr. Vander Weide determined the cost of CP&L's equity to be the range of 16.5% and 17.0%.

Company witnesses Vander Weide and Lilly testified regarding the erosion of the Company's financial integrity, its poor earnings quality in the perspective of current economic events, the present unfavorable environment of financial markets, and the serious need for adequate regulatory relief. Witness Lilly further pointed out that since 1977, CP&L fixed charge coverage, excluding allowance for funds used during the construction (AFUDC), has fallen from 2.9 times in 1978 to 1.9 times for the 12 months ended September 30, 1982. Moreover, AFUDC as a percentage of income for common equity during the same time period increased from 46% in 1978 to 78% in 1982.

Witness Lilly further testified that the forecast of construction expenditures for the period 1983-1985 for CP&L is substantially greater than the industry average for the same period. Comparison of these forecasts indicates greater construction risk in CP&L than in the industry generally. Witness Lilly also testified that while the sale of assets to the Power Agency has temporarily reduced somewhat the need for outside financing of required construction, the Company will continue to face substantial outside financing requirements. Additionally, Witness Lilly testified that the Company had suffered a downgrading of its bonds after the last North Carolina retail rate Order and that another downgrading is possible if CP&L's financial stability does not improve.

Public Staff witness Smith derived the Public Staff's recommended return on common equity of 13.5% on the basis of a DCF analysis for CP&L and the electric utility industry as a whole. Witness Smith testified that CP&L's dividend yield was 11.5%, as compared to the industry average dividend yield of 10.7%. Witness Smith stated further that actual historical growth

indicators for CP&L were smaller than the industry average, ranging between 0.7% to 2.9% for the Company and 1.2% to 3.8% for the industry. Witness Smith derived an estimate of the long-term dividend growth anticipated by investors of 1.5% to 2.5%, which she stated is somewhat higher than CP&L's own experienced growth and below the industry average historical experience. Based upon her study, witness Smith concluded that the current cost of common equity to CP&L is in the 13% to 14% range, and proposed that the midpoint of that range of 13.5% be used for setting the allowed rate of return.

Additionally witness Smith presented data concerning the historical earnings of utilities and non-regulated companies. According to witness Smith electric utilities equity earnings have ranged from 11% to 13% over the past decade. Alternatively witness Smith testified that unregulated companies, which are less risky than CP&L and the other electric utilities on any conventional measure, earned 11% on common equity in 1982.

Public Staff witness Smith testified that the study conducted by herself assumes like the classic DCF model that a company's cost of equity capital is determined by its dividend yield and the long-term dividend growth anticipated by investors. Witness Smith also explained that, although the electric utilities are similar, there are risk differences within the industry. Variations in risk measures include equity ratios, price volatility, management quality, and the nature of resource supply contracts. However, witness Smith stated that the problem with attempting to test these risk variations is that no measureable risk indicators exist which completely explain the variability in dividend yields remaining after growth expectations are accounted for. Specifically, it is not possible to build a perfectly specified model of relationships between dividend yields and the combination of growth and individual risk factors.

However, witness Smith testified that it is possible to measure the collective effect of all the risks investors associate with an individual utility. Witness Smith explained that, while in her opinion the individual effect of each risk factor cannot be measured with precision, it is possible to measure their combined effects by comparing a company's actual dividend yield with the yield that would prevail if expected growth were only determinant of variations in the stock's price and yield. The difference in the actual dividend yield and the yield that would prevail if expected growth were the only determinant of variations in the stocks price and yield is unexplained variability, or the E term, in witness Smith's regression equations.

Company witness Futrell testified in rebuttal to the testimony of Public Staff witness Smith specifically with regard to statistical analyses performed by Dr. Smith. Witness Futrell stated as acknowledged by Public Staff witness Smith that the specific risk variations for CP&L as compared to other electric utilities were not measurable. In witness Futrell's opinion it is impossible due to the lack of specification of a parameter in witness Smith's model namely unknown risk variation to determine the cost of equity capital for CP&L using witness Smith's methodology. Witness Futrell stated that Dr. Smith performed an ordinary least squares regression analysis to solve for the unknown risk variable. An ordinary least squares regression analysis has a dependent variable and one or more independent variables. Witness Smith's independent variable was growth rate, and her dependent variable was dividend yield. Witness Futrell stated that Dr. Smith's regression analysis simply

determined the line of best fit between various growth rates and various dividend yields. According to witness Futrell, Dr. Smith erroneously used the error term contained in the ordinary least square regression analysis as a substitute for the risk variable of CP&L. However, in witness Futrell's opinion the risk variation should properly have been treated as an independent variable, in addition to dividend growth. The omission of the independent variable risk variation in witness Futrell's opinion makes it impossible to determine the dividend yield which would best fit a regression with both independent variables utilized. According to Company witness Futrell, Dr. Smith simply attempted to substitute the error of the regression for the independent variable risk variation. In witness Futrell's opinion this cannot be done because regression analysis minimizes the error of the regression, rather than solving for it. Hence, witness Futrell maintains that the use of the error of the regression as a risk variable is erroneous since a minimized level of risk variation rather than the actual value of risk variation is obtained. Consequently, witness Futrell concludes that the analysis performed by witness Smith should not be relied upon to determine the cost of equity capital for CP&L.

Department of Defense witness McCabe recommended a return on equity of 14.75%. Witness McCabe's recommendation was not based on any specific statistical analyses but rather equates the return on equity to that found in the last rate case less 75 basis points comparable to the treatment prescribed in the return component of CP&L's Power Coordination Agreement with the North Carolina Eastern Municipal Power Agency.

The determination of the appropriate fair rate of return for the Company is of great importance and must be made with great care because whatever return is allowed will have an immediate impact on the Company, its shareholders, and its customers. In the final analysis the determination of a fair rate of return must be made by this Commission, using its own impartial judgment and guided by the testimony of expert witnesses and other evidence of record. Whatever return is allowed must balance the interest of the ratepayers and investors and meet the test set forth in G.S. 62-133(b)(4):

> "...(to) enable the public utility by sound management to produce a fair return for its shareholders, considering changing economic conditions and other factors, as they then exist, to maintain its facilities and services in accordance with the reasonable requirements of its customers in the territory covered by its franchise, and to compete in the market for capital funds on terms which are reasonable and which are fair to its customers and to its existing investors."

The return allowed must not burden ratepayers any more than is necessary for the utility to continue to provide adequate service. The North Carolina Supreme Court has stated that the history of G.S. 62-133(b):

> "...supports the inference that the Legislature intended for the Commission to fix rates as low as may be reasonably consistent with the requirements of Due Process Clause of the Fourteenth Amendment to the Constitution of the United States..." State ex rel. Utilities Commission v. Duke Power Co., 285 N.C. 377, 206 S.E. 2d 269 (1974).

The nature of the evidence in a case such as this makes it extremely difficult to balance all of the opposing interests, since much, if not all, of

the evidence is based on individual witnesses' perceptions and interpretations of trends and data from the capital market. The Commission has considered carefully all of the relevant evidence presented in this case, with the constant reminder that whatever return that is allowed will have an immediate impact on the Company, its stockholders and its customers. The Commission must use its impartial judgment to insure that all the parties involved are treated fairly and equitably. In coming to a final decision on this matter, the Commission is not unmindful of the upward pressure of capital costs generally present in the economy over recent years.

Based upon a careful consideration of all of the foregoing, including the statistical procedures used by witness Smith, the Commission concludes that, in the absence of any consideration of CP&L's history of poor nuclear performance and the inefficiency and imprudence of CP&L's management in the area of nuclear plant performance, a 15.25% rate of return upon equity would be the fair rate of return for CP&L in this case. However, when CP&L's poor nuclear plant performance and the past history of inefficiency and imprudence of CP&L's management in the area of nuclear plant performance is taken into consideration, the Commission concludes that it cannot allow that level of return upon equity. It is clear, based upon Finding of Fact No. 11 set forth above and the matters set forth and discussed in connection with the Evidence and Conclusions section for said finding of fact, that CP&L's inefficiency and mismanagement in the past resulted in the Company not achieving reasonable operation of its nuclear units during the test year. The Commission recognizes that considerable changes in organization and procedure have now been made but concludes that a penalty should remain in effect for the Company because of its test year nuclear performance. The Commission therefore concludes that CP&L should be allowed an opportunity to earn no more than a 14.5% rate of return on equity.

This Commission operates under a legislative mandate that requires it to fix rates which will allow a utility "by sound management" to pay all of its reasonable operating costs, including maintenance, depreciation, and taxes, and to earn a fair return on its investment. G.S. 62-133(b)(4); State of North Carolina ex rel. Utilities Commission vs. Duke Power Company, 285 NC 377, 206 SE 2nd 269 (1974). However, upon a finding that a utility is not soundly managed, it may be penalized by being authorized to earn less than a "fair return." State of North Carolina ex rel. Utilities Commission vs. General Telephone Company of the Southeast, 285 NC 671, 208 SE 2nd 681 (1974). In order to penalize a utility on rate of return, the Commission must make specific findings showing the effect upon its decision of the poor management it has found. Utilities Commission v. Morgan, Attorney General, 277 N.C. 255, 177 S.E.2d 405 (1970). The penalty must not result in a confiscatory rate of return. 285 NC 671.

In this case, the Commission has concluded that if CP&L's Brunswick nuclear units had been properly managed and reasonably operated, said Company would be entitled to a 15.25% rate of return on its common equity. The Commission has found, however, that CP&L's nuclear performance continues to be unsatisfactory and that the cost of service to CP&L's customers has been significantly increased as a result. In Finding of Fact No. 11 above and the Evidence and Conclusions set forth in support thereof, the Commission has determined that CP&L's nuclear performance during the test year was unsatisfactory. Considering the evidence of corporate mismanagement with respect to the Brunswick nuclear plant, the Commission concludes that CP&L should be

penalized by not being allowed to earn the rate of return that it would have been allowed if its Brunswick nuclear plant had been soundly managed.

Public Staff witness Thomas S. Lam testified that the 78 days of outages at the Brunswick nuclear unit resulted in approximately $26.5 million purchase power requirement, fuel cost expense, and calculated replacement power costs. Public Staff witness Caroline M. Smith testified that this figure would translate into a penalty of 150 basis points or 1.5%. While Company witness Lynn Eury agreed that the $26.5 million figure was a reasonable estimate, he noted that improvements have been made in the management of the Brunswick units since the time of these outages. He also noted that NRC has found performance "at the plant level" at the Brunswick units to be "acceptable" and has identified "major strengths" at the plant in the areas of emergency preparedness, security and safeguards. Eury further testified that the Company's fossil plants' performance compares quite favorably with appropriate industry indicators. The Commission must consider all material evidence that will help it determine what are reasonable and just rates. Further evidence presented shows that in September 1982 CP&L made certain changes with respect to the management of the Brunswick nuclear units. Reorganization of management was made to increase senior management oversight of the plant, to improve communications and coordination, and improve organizational accountability and strengthen management control. In recognition of these initiatives and the evidence as a whole, the Commission has determined that a rate of return penalty of 0.75% is appropriate.

The penalty imposed above will not result in a confiscatory rate of return. The Commission has determined that allowing a 14.5% rate of return on common equity and a 11.38% rate of return on the Company's rate base will allow CP&L to pay its operating expenses, including maintenance, depreciation, taxes, and interest on long-term debts, and still pay $24,887,000 to its preferred shareholders and $122,437,000 to its common shareholders. This is not confiscatory.

The Commission cannot guarantee that the Company will, in fact, achieve the level of returns herein found to be just and reasonable. In fact, it should be noted that the revenue requirements established in this case reflect the Commission's disallowance of CP&L's cost of debt and equity funds associated with the Company's abandoned plant facilities. These unrecognized costs would serve to reduce the Company's ability to earn the allowed returns stated above. Indeed, the Commission would not guarantee it if it could. Such a guarantee would remove necessary incentives for the Company to achieve the utmost in operational and managerial efficiency. The Commission believes, and thus concludes, that the level of return approved herein will afford the Company a reasonable opportunity to earn a reasonable return for its stockholders while providing adequate and economical service to ratepayers.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 22

The Commission previously has discussed its findings and conclusions regarding the rate of return which CP&L should be given the opportunity to earn.

The Company is being granted rates which will produce total operating revenues of $1,196,049,000 based on adjusted test period sales of 18,660,082,846 kWh. This represents an increase in operating revenues of

$90,855,000 based on the adjusted test period kWh sales and the rates previously in effect as of the date of this order. The Commission notes that a major factor contributing to CP&L's need for rate relief was the addition to CP&L's system of Unit No. 1 of the Mayo generating plant. The increased revenue requirements associated with Mayo Unit No. 1 being placed into service is approximately $41 million.

The following schedules summarize the gross revenues and the rates of return which the Company should have a reasonable opportunity to achieve based upon the increases approved herein. Such schedules, illustrating the Company's gross revenue requirements, incorporate the findings and conclusions heretofore and herein approved by the Commission.

SCHEDULE I
CAROLINA POWER & LIGHT COMPANY
NORTH CAROLINA RETAIL OPERATIONS
DOCKET NO. E-2, SUB 461
STATEMENT OF OPERATING INCOME
TWELVE MONTHS ENDED SEPTEMBER 30, 1982
(000'S OMITTED)

Item	Present Rates	Approved Increase	Approved Rates
Operating revenues	$1,105,194	$ 90,855	$1,196,049
Operating revenue deductions:			
Operation and maintenance expenses	618,932	-	618,932
Depreciation expense	92,880	-	92,880
Taxes other than income	82,215	5,451	87,666
Income taxes	110,380	42,053	152,433
Total	904,407	47,504	951,911
Operating income before adjustments	200,787	43,351	244,138
Adjustments to operating income	8,670	-	8,670
Net operating income	$ 209,457	$ 43,351	$252,808

SCHEDULE II
CAROLINA POWER & LIGHT COMPANY
NORTH CAROLINA RETAIL OPERATIONS
DOCKET NO. E-2, SUB 461
STATEMENT OF RATE BASE AND RATE OF RETURN
TWELVE MONTHS ENDED SEPTEMBER 30, 1982
(000'S OMITTED)

Item	Amount
Investment in Electric Plant:	
Electric plant in service	$2,431,733
Net nuclear fuel	25,172
Construction work in progress	539,781
Accumulated depreciation	(559,362)
Accumulated deferred income taxes	(313,321)
Net investment in electric plant	2,124,003
Allowance for Working Capital:	
Cash	3,467
Materials and supplies	96,071
Prepayments	6,594
Investor funds invested for operations	17,413
Miscellaneous projects	(24,503)
Customer deposits	(5,898)
Total	98,087
Original cost rate base	$2,222,090
Rates of Return	
Present	9.43%
Approved	11.38%

SCHEDULE III
CAROLINA POWER & LIGHT COMPANY
NORTH CAROLINA RETAIL OPERATIONS
DOCKET NO. E-2, SUB 461
STATEMENT OF CAPITALIZATION AND RELATED COSTS
TWELVE MONTHS ENDED SEPTEMBER 30, 1982
(000'S OMITTED)

Item	Capital-ization Ratio (%)	Original Cost Rate Base	Embedded Cost (%)	Net Operating Income
	Present Rates - Original Cost Rate Base			
Long-term debt	49.50	$ 1,099,935	9.59	$105,484
Preferred stock	12.50	277,761	8.96	24,887
Common equity	38.00	844,394	9.37	79,086
Total	100.00	$2,222,090	-	$209,457
	Approved Rates - Original Cost Rate Base			
Long-term debt	49.50	$ 1,099,935	9.59	$105,484
Preferred stock	12.50	277,761	8.96	24,887
Common equity	38.00	844,394	14.50	122,437
Total	100.00	$2,222,090	-	$252,808

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 23 THROUGH 27

Evidence for these findings of fact is found primarily in the testimony and exhibits of Company witness Edge, Public Staff witnesses Richard Smith and Turner, DOD witness McCabe, and Kudzu witness Eddleman. The following discussion of the rate designs proposed by the various parties is arranged by rate schedule or by topic.

Summer/Winter Rate Differentials

In its residential rate Schedule RES, the Company proposes to retain the summer/winter rate differential for all over 800 kWh. None of the rates proposed for the nonresidential rate schedules (excluding time-of-day rate schedules) contain summer/winter rate differentials for the energy charges. In fact, the seasonal rate differential does not apply to all energy blocks for residential service.

In the previous general rate cases in Docket Nos. E-2, Sub 416 and Sub 444, the Commission concluded that the summer/winter differentials in the residential rates should not be increased until such time as it can be determined what size summer/winter differential would be appropriate for each rate block of each rate schedule. The Commission further concluded that the Public Staff and CP&L should examine in depth the appropriate level of seasonal differentials and present their results in a docket as soon as possible.

The cost allocation study presented by the Company in this proceeding includes an attempt to quantify an appropriate summer/winter rate differential for residential service. The study results indicate that almost all of the summer/winter rate differential is due to the difference in unit demand cost between summer and winter. A review of the study methodology indicates that the major factor affecting the difference in unit demand cost between summer and winter is the fact that 50% of demand related fixed costs are allocated to four summer months and 50% are allocated to eight winter months. Such an allocation would produce a higher summer rate and a lower winter rate even if there were not other cost differences.

The Commission is of the opinion that further study of summer/winter rate differentials is needed. Such studies might consider the fixed plant mix during summer months versus winter months, and the number of months associated with summer peaks versus winter peaks.

TOD Rates for Residential Service

Public Staff witness Richard Smith testified that the customer response to the Company's time-of-use rate Schedule R-TOU has been poor to date. In order to make the schedule more attractive for the customer and more effective in reducing system demand, he recommended that the on-peak hours in that schedule be reduced. From the customer's standpoint, shorter on-peak hours would give more flexibility in scheduling baths and in the use of dishwashers and clothes washers. Shorter on-peak hours would also permit pre-cooling of the residence on summer mornings, earlier use of air conditioning in the evenings, and more satisfactory heating opportunities in the winter.

With respect to reducing system demand, witness Smith stated that with rates which are revenue neutral it is necessary to increase the demand charge to compensate for decreased on-peak hours. That increased demand charge then becomes an added incentive for customers to reduce demand.

The reduced on-peak hours recommended by the Public Staff compared to the present on-peak hours for Schedule R-TOU are as follows:

	Schedule R-TOU On-Peak Hours	
	April-September	October-March
Present hours	10:00 A.M. - 10:00 P.M.	6:00 A.M. - 1:00 P.M.
Hours proposed by Public Staff	Noon - 9:00 P.M.	6:30 A.M. - 1:00 P.M.

Witness Smith's testimony indicated that the proposed reduced hours would permit demand reductions up to 7.73% in the Company's system load curves and that less than 6% demand reduction is forecast by the Company from time-of-use rates and load control measures by the year 1995.

Chairman Koger asked the Company to determine what the effect would be in 1995 of shortening the summer on-peak period from 10:00 p.m. to 9:00 p.m. Company witness Edge testified that he was concerned with customers cutting back on appliances at the end of the on-peak period, but that the Company does not have a lot of difficulty with the idea of shortening the summer on-peak period from 10:00 p.m. to 9:00 p.m.

The Commission concluded in the previous general rate case (in Docket No. E-2, Sub 444) that the Company should embark on an experimental trial program to ascertain the effectiveness of an all-energy TOD rate (i.e., two-part rate) for residential customers, and that such all-energy TOD rate, if proved valid, could replace the present demand type TOD rate (i.e., three-part rate) or could be offered as an alternative TOD rate for residential service. The Commission also concluded that such all-energy TOD rate should include the same on-peak/off-peak hours recommended by the Public Staff in that proceeding, which are also the same hours recommended by the Public Staff in this case. The Company therefore implemented the experimental rate as directed by the Commission.

Given the evidence presented in this proceeding, the need for successful load management, and the agreement by all parties that moving the residential summer on-peak hours from 10:00 a.m. - 10:00 p.m. to 10:00 a.m. - 9:00 p.m. would have no detrimental effect at this time, the Commission accepts the principle of shifting the April-September residential on-peak boundary from 10:00 p.m. to 9:00 p.m. Due to the uncertainties inherent in future predictions, i.e., load forecasts, anticipated customer response, and overall load management and conservation program success, the shift in on-peak hours should apply to the Residential TOU rate schedule only.

Since the Commission believes the changes to meters and communication of the change to consumers will take some time, the change should be made effective by April 1, 1984. Present rating periods for all TOU rates should remain unchanged through March 31, 1984, new rating periods for the Residential TOU rate should become effective on April 1, 1984, and the Company should notify the Commission when the necessary changes and communications have been accomplished.

In another matter affecting TOD rates, the cost allocation study presented by the Company in this proceeding includes an attempt to quantify a cost differential between on-peak hours and off-peak hours. A review of the study methodology indicates that demand-related fixed costs are allocated to on-peak hours only. The Public Staff recommended that CP&L conduct further study of the allocation of fixed costs between on-peak and off-peak periods in conjunction with the cost allocation issues. The Commission is not convinced that the rate differential between on-peak and off-peak hours should be established, based on the study presented in this proceeding, and concludes that further study and discussion is needed.

Residential Water Heater Load Control Program

CP&L's residential water heater load control program currently applies to water heaters which have a storage capacity of 40 gallons or more. Public Staff witness Richard Smith recommended that 30-gallon water heaters also be eligible for the program. Witness Smith stated that including 30-gallon water heaters in the program could increase the number of eligible heaters by 60% and thereby expand by a like amount the potential demand reduction achievable by the load control program.

Witness Smith offered water heater manufacturer's test data which showed that the temperature of the water withdrawn from a water heater did not decline in direct proportion to the water used as assumed by both the Company and the consultant's study, but that 75% of a water heater's capacity was available before the temperature of the hot water outflow dropped 30 degrees. Witness Smith suggested that this test data indicated that almost three times more hot water was available than calculated.

Witness Smith stated that the Company had made no drawdown tests on 30-gallon water heaters nor had it interrupted any 30-gallon water heaters on its load control program. He also pointed out that the 8,434 customers on the Raleigh test program in 1981, which was limited to water heaters 40 gallons and larger, registered only 71 complaints in the winter and 17 complaints in the summer. Witness Smith indicated that less than one percent had withdrawn from the program, and that few, if any, had withdrawn as a result of the Company's test.

Witness Smith stated that the load control program was a voluntary one and that customers who are dissatisfied with the interruptions could withdraw from the program. Witness Smith stated that the majority of customers with 30-gallon water heaters should find the program satisfactory and that this large segment of customers should not be discriminated against but should be offered the program. Commissioner Campbell inquired whether or not a fact-finding determination could be made by placing 100 or 500 customers on the load control program and then observing the complaints. Witness Smith stated that such a test could be satisfactory, provided the customers were treated normally and left completely alone without receiving any questions or comments from the Company.

CP&L witness Edge testified that the Company is opposed to the inclusion of the 30-gallon capacity water heaters in the load control program. Witness Edge testified that there would be increased customer dissaticluded and that such dissatisfaction could negatively affect the present effort to expand the

water heater control program. In addition, the Company incurs an expense in installing and then removing the control device. Witness Edge testified that information contained in a Public Staff Exhibit filed in Docket No. M-100, Sub 78, showed that the control of the 30-gallon water heater would be satisfactory during peak hours of the day, provided that the length of the interruption was no more than one hour. Also, 40 and 50-gallon water heaters could be interrupted beyond two and three hours, respectively. Witness Edge testified that the Company findings support the findings set forth in the Public Staff Exhibit in Docket No. M-100, Sub 78. Witness Edge testified that the current interruption period of two and three hours in the winter and summer, respectively, would probably have to change to one and two hours in order to minimize customer dissatisfaction if the 30-gallon water heaters are allowed on the program. This would have the effect of substantially reducing the benefits of the program.

The Commission concludes that the addition to the Company's load control program of 30-gallon water heaters is not in the best interests of that program at this time. The Commission recognizes that CP&L is currently expanding the load control program into new locations and that increased customer dissatisfaction could negatively affect that effort. This does not mean, however, that the Company should not continue to seek ways to expand the scope of its water heater control program. The Company should continue to expand into new areas of its territory and once the program becomes well accepted consideration should be given to conducting an experiment using the 30-gallon water heater.

Revenue Requirement for Small General Service

The Commission has generally attempted to establish rates in prior proceedings which would produce rates of return for each class that were within 10% ± of the overall North Carolina retail rate of return. In comparing the rates of return for each rate class resulting from three of the cost allocation methods discussed herein (summer/winter coincident peak, summer/winter peak and base, summer/winter peak and average), the Commission notes that the small general service class is overpriced (i.e., has a high rate of return) using all three methods. Furthermore, in making the same comparison for the small general service class in the previous rate case, Docket No. E-2, Sub 444, the Commission noted that the SGS class was overpriced in that proceeding. Therefore, the Commission concludes that any increase for the small general service rate class should be less than that proposed by the Company in this proceeding.

On the other hand, a comparison of the rates of return for the small general service class versus the rates of return for overall North Carolina retail service since 1972 (based on the annual cost of service studies filed with the Commission) indicates that the small general service class was overpriced in some years and underpriced in some years.

The Company proposed to increase the rates for SGS class by 14.5% in this proceeding versus a 14.9% increase for North Carolina retail service overall. If the rates for the SGS class were increased 10.8% instead of the proposed 14.4%, it would result in a rate of return which would be within 10% of the North Carolina retail rate of return. The difference between a 14.5% increase and a 10.8% increase for the SGS class is approximately $13,354,000 revenue requirement.

However, the Commission is of the opinion that a $13,354,000 reduction in revenue requirement for the SGS class, in addition to the same percentage reduction applied to the other rate classes as described in Appendix A attached to this order, would be too large for this single proceeding. It would also be an extreme correction in view of the unstable relationship since 1972 between the rates of return for the SGS class and overall North Carolina retail service. The Commission concludes that an additional $3,000,000 reduction in revenue requirement for the SGS class would be appropriate for this proceeding.

Small General Service Schedule SGS Rate Blocks

In its small general service rate schedule SGS, the Company proposes to retain a declining block rate for its energy charge. The declining block rate consists of the middle block (second block) and the tail block (third block). In prior general rate cases, the Commission concluded that multiple rate blocks should be combined and that declining block rates should be eliminated where possible. In this proceeding, the Company proposes to increase the tail block by a considerably larger percentage than the middle block, thereby closing the differential that exists between the middle and the tail block. The Commission concludes that reduction of said differential between the middle and tail blocks is appropriate for this proceeding and should be continued in its future general rate proceedings.

"Closed" Rate Schedules RFS, CSG, CSE, AHS & SCS

In Docket No. E-2, Sub 366, the Commission directed the Company to take steps to withdraw its "closed" rate schedules. Subsequently, in Docket No. E-2, Sub 391, the Company added a proviso to its "closed" rate schedules (RFS, CSG CSE, AHS, SCS and MPS) which requires that a customer serviced under any of the "closed" rate schedules be automatically tranferred to another available rate schedule (probably SGS) whenever the Company determines that the customer would have paid less revenues over the previous 12 months for service under the alternative rate schedule than he actually paid under his current rate schedule.

As a supplement to this proviso, the Company proposed to apply greater than average rate increases to the "closed" rate schedules in each successive rate case. Each time rates for the "closed" rate schedules are increased more than the rates for alternative rate schedules, an additional number of customers will be required to transfer to alternate rate schedules pursuant to the proviso just described. The greater than average increases will continue until all of the customers served under the "closed" rate schedules have been transferred to alternate rate schedules. In this manner, "closed" rate schedule MPS was eventually withdrawn in a prior general rate proceeding.

In this proceeding, the Company proposed to increase the rates for four of the remaining "closed" rate schedules (RFS, CSG, CSE, and AHS) by approximately 24% to 26%, while increasing the rates for the other major rate schedules by approximately 14% to 16%. This is really nothing more than giving the four "closed" rate schedules a 10% increase relative to the other rate schedules. The Commission concludes that the Company's proposed rate increase for the four (4) "closed" rate schedules should be approved.

The Company also proposes to withdraw "closed" rate schedule SCS (shopping center service) in this proceeding as a result of the program described above. The proposal was unopposed and the Commission concludes that it should be approved.

Demand Ratchets and TOD Rates for Large General Service

In its previous general rate order in Docket No. E-7, Sub 444, the Commission noted that voluntary TOD rates were not available to large general service customers unless they had thermal storage equipment, and that the large general service class was the only major class of customers which did not have a voluntary TOD rate available to all of the customers in the class. The Commission further observed that TOD rates might be a reasonable alternative to demand ratchets, and it concuded that the next general rate case should include a discussion of voluntary TOD rates for LGS customers as well as a discussion of alternatives to demand ratchets for LGS customers.

In this proceeding, the Company proposes to replace the present large general service TOD rate schedule (LGS-TS) with a new large general service TOD rate schedule (LGS-TOU). The new rate schedule LGS-TOU will be available on a voluntary basis to all LGS customers.

The proposed new schedule LGS-TOU will include a billing demand ratchet based on the highest of: (1) the current month's demand; or (2) 80% of the maximum on-peak demand during the summer or winter season in the preceding 11 months. None of the Company's other TOD rate schedules (for residential service or small general service) contains a billing demand ratchet. Public Staff witness Turner and DOD witness McCabe proposed to eliminate the ratchet from rate schedule LGS-TOU. The Company also proposes that Customer Generation Service Rider No. 55 be revised to include a billing demand ratchet in conjunction with rate schedule LGS-TOU.

Witness Turner recommended that the demand ratchet not be included in rate schedule LGS-TOU or in Rider No. 55. He gave several reasons for his proposal. First, at the time it was introduced, ratcheting was a peak load pricing mechanism designed to discourage peak demand at the time of system peak or to place the cost of the system peak upon those that caused it. Today, however, in the presence of sophisticated time-of-use metering technology, it is a poor second choice as a peak load pricing mechanism. The ratchet without time-of-use metering increases the demand portion of a customer's bill regardless of when the customer's peak occurred -- on the system's peak or off it. Time-of-use rates by design charges a higher rate per KW for on-peak demand and lower rate for off-peak demand. With properly designed time-of-use rates there is no need for a ratchet. Second, the ratchet allows the Company to present a weakened price signal. This occurs because the ratchet increases the number of billing units that will be divided into the revenue requirement when establishing the unit price. As a result, the ratchet favors those customers who maintain a high load factor and who levelize their demand requirements throughout the year.

Witness Turner further stated that he realized the ratchet grants the Company some measure of revenue stability because it requires customers to pay a fixed amount for demand per month independent of their actual monthly demand. However, he testified that this reason does not justify giving customers incorrect price signals in a time-of-use rate.

Kudzu witness Eddleman opposed the ratchet in either rate form indicating that once the maximum demand is established, there is no incentive to conserve. DOD witness McCabe opposed the ratchet in the LGS Time-of-Use rate but proposed that the ratchet in the standard LGS rate be revised to conform to the seasonal nature of the ratchet proposed by the Company for rate Schedule LGS-TOU. He supported this proposal based on the nature of the summer and winter peaks included in the summer/winter peak and average allocation factor. CIGFUR witness Brubaker, while opposing the SWP&A allocation method, indicated that the demand ratchet was a useful tool and supported its continuation.

Company witness Edge pointed out that to abruptly eliminate the ratchet could cause significant changes in the amount of individual customer's bills with high load factor customers receiving large increases and low load factor customers receiving substantial reductions. Witness Edge also indicated that the ratchet promoted conservation and load management and related the dramatic increase in the number of customers employing load control devices since the implementation of the ratchet. He indicated that the ratchet enabled the Company to recover the fixed costs related to distribution plant in an equitable manner.

The Commission concludes that TOD rates should not include a billing demand ratchet and that the demand ratchet should be eliminated from the proposed Large General Service (time-of-use) rate schedule and from Rider 55, without prejudice to the Company seeking a ratchet at a later date which would recover distribution fixed costs only. However, the Commission also concludes that the Company's billing demand ratchets for its non-TOD large general service customers should remain as they are proposed by the Company. Finally, the Commission concludes that the proposed new rate schedule LGS-TOU, excluding a billing demand ratchet, should be approved as modified.

Coincident Demand Billing for LGS or Wholesale Customers

Another rate design issue addressed by parties in this proceeding is the use of coincident demand for billing purposes for resale (wholesale) customers. Public Staff witness Richard Smith testified that the Company should institute coincident demand billing for its resale customers. DOD witness McCabe suggested that coincident demand billing be applied to DOD customers of the Company. Witness Smith supported his position with the argument that coincident demand billing would provide an incentive for resale customers to reduce their demand at the time of the system peak, thereby reducing that system peak and potentially the need for additional generation facilities in the future. Witness McCabe had the same argument but also presented data which indicated that defense facilities peak at times other than the system peak. Presumably coincident demand billing for DOD would have the effect of reducing their cost.

The Commission has noted the evidence in the record in this case that the Company is presently working with its resale customers in order to establish coincident demand billing for those customers. Although the Commission is concerned about the amount of generating capability that will be required in the future of this Company, it is of the opinion that the Company's dealings with its resale customers on this issue are not within the purview of this Commission.

Concerning the DOD request for coincident demand billing, the Commission notes that allocation of demand related production costs between rate classes has always been based on coincident demands, for reasons discussed extensively in this and prior general rate orders. Furthermore, allocation of demand related costs between customers in a given rate class has always been based on the assumption that customers in the rate class are similar in some respects, and that allocation of such costs by individual maximum demand billing reflects an appropriate distribution of cost responsibility within the class. The Commission, therefore, concludes that it is improper at this time to order a change in the Company's use of individual billing demand.

DOD witness McCabe has raised the issue that the composition of the LGS rate class is inappropriate and recommended that this rate be broken into different categories by voltage levels. He indicates that line losses differ by voltage level of service and that a customer should be responsible only for its specific line losses.

With perfect information, it would be theoretically possible to develop a different rate for each of the utility's customers. However, as a practical matter, it is necessary to group customers with other customers having similar load characteristics in order to have a manageable number of rate schedules for the utility to administer. In this grouping of customers into rate classes, there will inevitably be differences between individual customers within a given rate class. Line losses would potentially be one of the sources of those differences. The Commission is not convinced in this proceeding that this particular example is more worthy of distinction than other potential differences. The Commission is also of the opinion that DOD has available to it the option of applying for service under CP&L's wholesale rates, whereby it would then be grouped with other similarly constituted users of electricity. The Commission, therefore, finds no reason to restructure the LGS rate class.

Sports Field Lighting Service

The Commission has generally attempted to establish rates in prior proceedings which would produce rates of return for each rate class that were within 10% ± of the overall North Carolina retail rate of return. In comparing the rates of return for each rate class resulting from three of the cost allocation methods discussed herein (summer/winter coincident peak, summer/winter peak and base, summer/winter peak and average), the Commission notes that the sports field lighting class is underpriced (i.e., has a low rate of return) using all three methods. However, the Commission also notes that said low rates of return occur even after a 21.4% increase proposed by the Company in this proceeding for the rate class versus a 14.9% increase proposed for North Carolina retail service overall. Therefore, the Commission concludes that the rates proposed for rate schedule SFLS (Sports Field Lighting Service) should be reduced by the same percentage as the other rates proposed by the Company, in the manner described on Appendix A attached to this order.

General

In addition to those revisions already discussed herein, the Company proposes various miscellaneous rate changes, administrative changes, and clarifications on its rate schedules and in its terms and conditions for

service which were not opposed by any party. Such changes and clarifications include in part: provisions to list base fuel costs on tariffs and riders; provisions to exclude availability of residential rate schedules from service which is metered separately from residence; provisions to restrict availability of Rider 7 (Standby Service) to retail rate schedules only; provisions to add a customer charge during non-usage months for service under Rider 5 (Seasonal Service); provisions to increase off-peak demand charges for service under Rider 55 (Customer Generation); provisions to include power factor adjustments on LGS Tariffs for clarity; provisions to increase the attractiveness of Rider 5 (Curtailable Load); provisions to add a new 5800 lumen S.V. fixture to the lighting rate schedules; and provisions to restrict 12,000 and 38,000 lumen S.V. Retrofit fixtures to existing applications only.

The Commission concludes that the rate designs, rate schedules and terms and conditions for service as proposed by the Company should all be approved, except as discussed herein.

IT IS, THEREFORE, ORDERED as follows:

1. That Carolina Power & Light Company shall adjust its electric rates and charges so as to produce an increase in gross annual revenues from its North Carolina retail operations of $90,855,000, said increase to be effective for service rendered on and after the date of this Order.

2. That within five (5) working days after the date of this Order, Carolina Power & Light Company shall file with this Commission five (5) copies of rate schedules designed to produce the increase in revenues set forth in Decretal Paragraph No. 1 above in accordance with the guidelines set forth in Appendix A attached hereto. Said rate schedules shall be accompanied by a computation showing the level of revenues which said rate schedules will produce by rate schedule, plus a computation showing the overall North Carolina retail rate of return and the rates of return for each rate schedule which will be produced by said revenues.

3. That Carolina Power & Light Company shall prepare cost allocation studies for presentation with its next general rate application which allocate production plant based on the following methodologies: (1) summer/winter peak and average; (2) summer/winter peak and base; (3) summer/winter coincident peak; (4) summer coincident peak; and (5) summer peak and average. Both jurisdictional and fully distributed cost allocation studies shall be made using each method, and the studies shall be included in items 31 and 37, respectively, of Form E-1 of the minimum filing requirements for general rate applications.

4. That Carolina Power & Light Company work with the Public Staff during the six (6) months following the date of this Order to develop a mutually agreeable study which could be done at a reasonably limited cost and would be responsive to the concerns discussed in this proceeding regarding: (1) allocation of fixed costs and variable costs to each hour of the year, and (2) allocation of costs incurred during a given hour to customer classes based on usage during the given hour. The Company shall report to the Commission on the details of the study from time to time as necessary, but not later than six (6) months following the date of this Order.

5. That Carolina Power & Light Company shall take the steps necessary to reduce the on-peak hours for residential TOD rate schedule R-TOU during the summer months from 10:00 p.m. to 9:00 p.m. effective April 1, 1984, as discussed herein.

6. That Carolina Power & Light Company shall give appropriate notice of the rate increase approved herein by mailing a copy of the notice attached hereto as Appendix B by first class mail to each of its North Carolina retail customers during the next normal billing cycle following the filing of the rate schedules described in Decretal Paragraph No. 2.

7. That anv motions heretofore filed in this proceeding and not previously ruled upon are hereby denied.

ISSUED BY ORDER OF THE COMMISSION.
This the 19th day of September 1983.

NORTH CAROLINA UTILITIES COMMISSION
Sandra J. Webster, Chief Clerk

(SEAL)

APPENDIX A
GUIDELINES FOR DESIGN OF RATE SCHEDULES

Step 1: Determine the amount of rate schedule revenues and other revenues, respectively, which are necessary to produce the overall revenue requirement established by the Commission in this proceeding.

Step 2: Decrease the rate schedule revenues proposed by the Company for each rate schedule by the same percentage to produce the total rate schedule revenues determined in Step 1, except as follows:

(a) Reduce the revenue requirement for rate schedule SGS by $3,000,000 in addition to the percentage reduction described above.

(b) Reduce the revenue requirement for each of the four (4) "closed" rate schedules RFS, AHS, CSG, and CSE by the same percentage as rate schedule SGS.

Steo 3: Reduce the individual prices in a given rate schedule by the same percentage to reflect the decrease in revenue requirement for the rate schedule as determined in Step 2, except as follows:

(a) Hold the basic customer charge for each rate schedule at the level proposed by the Company.

(b) Revise new schedule LGS-TOU and Rider 55 in order to exclude the billing demand ratchet.

(c) Decrease prices in the TOD rate schedules in such a manner that they will remain basically revenue neutral with comparable non-TOD rate schedules, considering projected peak demand savings for the TOD rates.

(d) Hold miscellaneous service charges and extra charges at the same level proposed by the Company.

Step 4: Round off individual prices to the extent necessary for administrative efficiency, provided said rounded off prices do not produce revenues which exceed the overall revenue requirement established by the Commission in this proceeding.

DOCKET NO. E-2, SUB 461

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Application of Carolina Power & Light Company for an Adjustment in Its Rates and Charges Applicable to Electric Service in North Carolina) SUPPLEMENTAL ORDER

BY THE COMMISSION: On September 19, 1983, the Commission issued its Order Granting Partial Increase In Rates and Charges for Carolina Power & Light Company. It has come to the Commission's attention that certain information was inadvertently excluded from the Order. The Appendix B, Notice to Customers, referred to in ordering paragraph 6 and the last line of page 55 were erroneously omitted from the Commission Order. The Commission therefore concludes that the Order issued September 19; 1983, should be modified to correct for the aforementioned omissions.

IT IS, THEREFORE, ORDERED as follows:

1. That page 55 of the Commission Order Granting Partial Increase In Rates and Charges issued September 19, 1983, shall be modified to include the last line as follows: "a confiscatory rate of return. 285 NC 671."

2. That the September 19, 1983, Order of the Commission shall be modified to include Appendix B attached hereto.

ISSUED BY ORDER OF THE COMMISSION.
This the 20th day of September 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sandra J. Webster, Chief Clerk

APPENDIX B

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Application of Carolina Power & Light Company for an Adjustment in Its Rates and Charges Applicable to Electric Service in North Carolina) NOTICE TO CUSTOMERS

The North Carolina Utilities Commission on September 19, 1983, after months of investigation and following hearings held throughout the State, denied CP&L's request for an increase of $164,913,000 in current rates and approved an increase of $90,855,000. If CP&L's full rate request had been granted, rates would have increased by 14.92% above current rates. The Commission Order allows an increase of 8.22% above current rates.

The Commission estimates that the bill of a typical residential customer using 1000 kWh per month will increase from approximately $65.00 per month to approximately $71.00 per month.

In allowing the 8.22% increase, the Commission found that the approved rates would provide CP&L under efficient management, an opportunity to earn an approximate 11.38% rate of return on the original cost of its property. In its application, CP&L had sought rates which would allow it to earn an 11.74% rate of return on the original cost of its property based on a return to its stockholders of 15.5%. The Commission's Order found that in the absence of any consideration of CP&L's history of poor plant performance and the inefficiency and imprudence of CP&L's management in the area of nuclear plant performance, a 15.25% rate of return upon stockholders equity would be the fair rate of return for CP&L in this case. However, when CP&L's history of poor nuclear plant performance was taken into consideration the Commission found that only a return on stockholders equity of 14.50% was warranted.

It should be noted that the revenue requirements established in this case reflect the Commission's disallowance of CP&L's cost of debt and equity funds associated with the Company's abandoned plant facilities. These unrecognized costs would serve to reduce the Company's ability to earn the allowed returns stated above.

The Commission imposed a rate of return penalty of 1% in CP&L's last general rate proceeding, Docket No. E-2, Sub 444, which became effective September 24, 1982. In continuing to impose a rate of return penalty on the Company, the Commission found that CP&L's nuclear plant performance continues to be unsatisfactory and that the cost of service to CP&L's customers has been significantly increased as a result. However in reducing the penalty from 1.0% to .75% in its Order, the Commission recognized the initiatives taken by management to reorganize the senior management oversight of the Brunswick plant, to improve communications and coordination, to improve organization accountability, and to strengthen management control. In support of the rate of return penalty, the Commission concludes that 78 days of outage at CP&L's Brunswick Units 1 and 2 during the summer of 1982 were largely the result of past inefficiency in nuclear management practices.

One of the major factors contributing to the Company's need for rate relief was the addition to CP&L's system of Unit No. 1 of the Mayo generating plant which began commercial operation in March 1983. The increased cost associated with the Mayo Unit No. 1 being placed into service is approximately $41 million of the $90.9 million increase granted CP&L. The total cost of the new Mayo plant was approximately $488 million.

The Commission also directed that more steps be taken to improve customer participation in time-of-day (TOD) rates. A voluntary TOD rate was introduced for large general service customers, and the number of on-peak hours was reduced for the residential TOD rates.

DOCKET NO. E-2, SUB 461

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Application of Carolina Power & Light Company for an) ORDER ON
Adjustment in Its Rates and Charges Applicable to) RECONSIDERATION
Electric Service in North Carolina)

HEARD IN: Superior Courtroom, 5th Floor, Buncombe County Courthouse, Courthouse Plaza, Asheville, North Carolina, on May 16, 1983

Superior Courtroom, New Hanover County Courthouse, Third and Princess Streets, Wilmington, North Carolina, on May 25, 1983

The Wayne Center, Corner of George and Chestnut Streets, Goldsboro, North Carolina, on May 26, 1983

The Commission Hearing Room, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina, on June 28-July 1, July 5-8, July 18-22, and July 25-26, 1983

BEFORE: Commissioner Leigh H. Hammond, Presiding; and Chairman Robert K. Koger and Commissioner A. Hartwell Campbell

APPEARANCES:

For the Applicant:

R. C. Howison, Jr., and Edward S. Finley, Jr., Hunton & Williams, Attorneys at Law, P. O. Box 109, Raleigh, North Carolina 27602

Richard E. Jones, Vice President and Senior Counsel; Robert W. Kaylor, Associate General Counsel; and Margaret S. Glass, Associate General Counsel, Carolina Power & Light Company, P. O. Box 1551, Raleigh, North Carolina 27602
For: Carolina Power & Light Company

For the Intervenor State Agencies Representing the Using and Consuming Public:

G. Clark Crampton and Karen E. Long, Staff Attorneys, Public Staff - North Carolina Utilities Commission, P. O. Box 991, Raleigh, North Carolina 27602
For: Public Staff - North Carolina Utilities Commission

Steven F. Bryant, Assistant Attorney General, North Carolina Department of Justice, P. O. Box 629, Raleigh, North Carolina 27602
For: The Attorney General of the State of North Carolina

For the Other Intervenors:

Ralph McDonald and Carson Carmichael, III, Bailey, Dixon, Wooten, McDonald & Fountain, Attorneys at Law, P. O. Box 2246, Raleigh, North Carolina 27602
For: Carolina Industrial Group for Fair Utility Rates - Weyerhaeuser Company; Federal Paper Board Company, Inc.; Riegelwood Operations; Monsanto North Carolina, Inc.; Union Carbide Corporation; Clark Equipment Company; Huron Chemicals of America, Inc.; LCP Chemicals and Plastics, Inc.; Masonite Corporation; and The Firestone Tire & Rubber Company

Thomas R. Eller, Jr., Attorney at Law, P. O. Box 27866, Raleigh, North Carolina 27611
For: The North Carolina Textile Manufacturers Association, Inc.

David A. McCormick, Attorney, Regulatory Law Office (JALS-RL), U. S. Army Legal Services Agency, 5611 Columbia Pike, Falls Church, Virginia 22041
For: The Consumer Interest of the United States Department of Defense and Other Affected Executive Agencies

M. Travis Payne, Edelstein & Payne, Attorneys at Law, P. O. Box 12607, Raleigh, North Carolina 27605
For: The Kudzu Alliance

BY THE COMMISSION: On February 11, 1983, Carolina Power & Light Company (Applicant, the Company, or CP&L) filed an application with the North Carolina Utilities Commission seeking authority to adjust and increase electric rates and charges for its retail customers in North Carolina. The requested increase in rates and charges was designed to produce approximately $164.9 million of additional annual revenues from the Company's North Carolina retail operations when applied to a test period consisting of the 12 months ended September 30, 1982, or approximately a 14.9% increase in total North Carolina retail rates and charges. The Company requested that such increased rates be allowed to take effect for service rendered on and after March 13, 1983.

The Company alleged in its application that the $164.9 million additional annual revenues was necessary because present rates would be insufficient to: (1) produce either an overall rate of return or a rate of return on common equity which would be just and reasonable, (2) enable the Company to continue to attract capital on reasonable terms, and (3) permit it to finance its operations and construction program. Included among the reasons set forth in the application as necessitating the rate relief requested were the addition of Mayo Unit No. 1 on the Company's system, the ongoing construction at the Shearon Harris Nuclear Power Plant, and the increased expense of overall operations of the entire system.

The Company filed its letter of intent to file a general rate case with the Commission on January 11, 1983. Subsequently, upon the Company's motions and pursuant to Orders issued January 21, 1983, and February 1, 1983, the Commission permitted the Company to modify certain filing requirements which would have otherwise been applicable to its rate request filing.

On January 21, 1983, the Public Staff of the North Carolina Utilities Commission filed its Notice of Intervention. The intervention of the Public Staff in this proceeding is deemed recognized pursuant to Commission Rule R1-19(e).

On February 11, 1983, the Company filed its rate case application and an Undertaking wherein it agreed to make refunds with interest of the amount, if any, by which any rates and charges put into effect pursuant to G.S. 62-135(a) exceeded the amounts finally determined to be just and reasonable herein.

On March 7, 1983, the Secretary of Defense, on behalf of the Department of Defense of the United States, filed a petition requesting leave to intervene. That request was granted by Order issued March 17, 1983.

On March 7, 1983, the Commission issued an Order declaring the Company's application to be a general rate case pursuant to G.S. 62-137, suspending the rate increase for a period of up to 270 days as permitted by the provisions of G.S. 62-134, scheduling public hearings and directing the Company to give public notice thereof, establishing the test period for use in the case, and establishing certain dates for testimony and petitions to intervene to be filed.

On March 11, 1983, a Petition to Intervene was filed on behalf of Public Service Company of North Carolina, Inc., which was allowed by Commission Order issued March 17, 1983.

On March 22, 1983, a Petition was filed on behalf of the North Carolina Textile Manufacturers Association, Inc. (NCTMA), seeking leave to intervene and participate in the proceedings. By Order issued March 24, 1983, that intervention was allowed.

On April 21, 1983, the Attorney General of the State of North Carolina filed a Notice of Intervention in this proceeding.

On May 3, 1983, a Petition to Intervene was filed with the Commission on behalf of the Kudzu Alliance. That intervention was allowed by Order issued May 16, 1983.

On May 5, 1983, the Commission issued an Order scheduling an initial pretrial conference for June 1, 1983, which was subsequently rescheduled for and held on June 13, 1983, at which time it was determined that there would be no necessity for the additional pretrial conference which had been scheduled for June 24, 1983. A Pretrial Order was issued on June 17, 1983.

On May 5, 1983, the Commission issued its Order relating to an inspection tour of CP&L's Brunswick Nuclear Plant to be conducted by CP&L for the Commission and for representatives of all parties of record who wished to participate. The inspection tour of CP&L's Brunswick Nuclear Power Plant was held as scheduled. All parties of record were permitted to send a representative. The following persons attended: Chairman Robert K. Koger and Commissioners Leigh H. Hammond and A. Hartwell Campbell; Karen E. Long and G. Clark Crampton, Staff Attorneys - Public Staff; S. R. Kirby, Staff Attorney - NCUC, and D. F. Creasy, Chief Engineer - NCUC; and Richard E. Jones, Norris L. Edge, and Ronnie M. Coats - CP&L.

On June 1, 1983, a Petition to Intervene and Motion for Extension of Time to File Testimony was filed on behalf of the Carolina Industrial Group for Fair Utility Rates, "CIGFUR II," consisting of: Federal Paper Board Company, Inc.; Huron Chemicals of America, Inc.; LCP Chemicals and Plastics, Inc.; Monsanto Company; Union Carbide Corp.; and Weyerhaeuser Company. That Petition and Motion was allowed by Order issued June 6, 1983.

On June 9, 1983, a Petition to Intervene was filed on behalf of Clark Equipment Company, Masonite Corporation, and The Firestone Tire and Rubber Company, alleging that those corporations had become members of "CIGFUR II." That petition was allowed by Order issued June 15, 1983.

On June 10, 1983, the Commission issued its Order directing the Public Staff to file certain data, exhibits, and schedules identified therein. The time initially set in that Order for the subject data to be filed was subsequently extended by the Commission, upon verbal motion by the Public Staff, and said data, exhibits, and schedules were timely filed and served pursuant to such extension.

Prior to and during the course of the hearings, various other procedural and discovery motions were made and Orders were entered relating thereto, all of which are a matter of record. Further, pursuant to various Commission Orders or requests, also of record, various parties were directed or permitted to file and serve certain late filed exhibits, either during or subsequent to the hearings held in this matter.

The proceeding came on for public hearings in the territory served by CP&L as noted herein. Night hearings were scheduled and held by the Commission for the specific purpose of receiving testimony from public witnesses in Asheville, on Monday, May 16, 1983; in Wilmington on Wednesday, May 25, 1983; in Goldsboro, on Thursday, May 26, 1983; and in Raleigh, on Wednesday, June 29, 1983. Public witnesses also appeared and testified in Raleigh, on June 28, 1983. The following persons appeared and testified at these hearings:

Asheville: David Spicer, Frank Fishburne, Jr., Richard N. Barber, Jr., L. W. Kraft, Kitty Boniske, Keith Thomson, Rebecca Williams, Carroll Rogers, Jr., Fred Sealey, and Charles Brookshire;

Wilmington: R. F. Warrick, Llewellyn Bestal, Ron Shackleford, Jerry Cabot, Larry Vestal, Stanley R. Addlemann, Herbert Slack, John Fitzpatrick, and William S. Conner;

Goldsboro: Jim Barnwell, Fred Lutz, Marie Grant, Ron Staton, Lou Colombo, Henry L. Stewart, Jr., Sylvester F. Lane, D. J. Pelt, George Mitchell, Ernest Smith, Craig Kennedy, John N. Walker, Rachel Jefferson, Steve L. Herring, Edwin H. Allen, Allen J. Griffin, Ralph Carraway, Karl Best, Gladys Thornton, and Debbie Jones; and

Raleigh: Lonnie Knott, Christopher Scott, R. H. Beatty, William T. Fuller, J. Franklin Drake, Jane Sharp, Gene Furr, Joseph Reinchens, Joseph R. Overby, William Parrish, John Currin, Jr., Rex Paramore, F. R. Robinson, William Winston Sears, Alfred Compton, Joe R. Ellen, Jr., Curtis Sapp, Clarence Knight, Elisha Wolper, Carolyn Moore, John M. Green, William Bell, Elliot Winit, and Johnny Lee Williams.

The case in chief came on for hearing as ordered on June 28, 1983, for the purpose of presenting the Applicant's evidence. The Applicant presented the testimony and exhibits of the following witnesses:

1. Sherwood H. Smith, Jr., President, Chief Executive Officer, and Chairman of the Board of Directors of CP&L (direct testimony);

2. Edward G. Lilly, Executive Vice President and Chief Financial Officer of CP&L (direct, supplemental, and additional supplemental testimony);

3. Dr. James Vander Weide, Professor of Finance, Fuqua School of Business, Duke University (direct and supplemental testimony);

4. R. A. Watson, Vice President - Fuel in the Fuel and Materials Management Group of CP&L (direct and supplemental testimony);

5. Lynn W. Eury, Senior Vice President - Power Supply (direct testimony);

6. M. A. McDuffie, Senior Vice President - Engineering and Construction (direct testimony);

7. Steven S. Faucette, Director of Regulatory Accounting (direct and supplemental testimony);

8. Paul S. Bradshaw, Vice President - Accounting Department and Controller of CP&L (direct and supplemental testimony);

9. Dr. Robert M. Spann, Principal and Member of Board of Directors of ICF, Incorporated (direct testimony);

10. David R. Nevil, Manager - Rate Development and Administration in the Rates and Service Practices Department of CP&L (direct, supplemental, and additional supplemental testimony);

11. Joe A. Chapman, Supervisor - Rate Support in the Rates and Service Practices Department of CP&L (direct and supplemental testimony);

12. Norris L. Edge, Vice President - Rates and Service Practices Department of CP&L (direct, supplemental, and additional supplemental testimony);

13. Archie W. Futrell, Director of Economic and Energy Forecasting and Special Studies for CP&L (rebuttal testimony); and

14. John D. McClellan, Partner and Regulatory Specialist with Deloitte Haskins & Sells (rebuttal testimony).

The Public Staff presented the testimony and exhibits of the following witnesses:

1. Dennis J. Nightingale, Director of the Electric Division of the Public Staff (direct and supplemental testimony);

2. William E. Carter, Assistant Director of the Accounting Division of the Public Staff (direct and supplemental testimony);

3. Timothy J. Carrere, Engineer with the Electric Division of the Public Staff (direct testimony);

4. Benjamin R. Turner, Jr., Engineer with the Electric Division of the Public Staff (direct testimony);

5. George E. Dennis, Supervisor of the Water Section of the Accounting Division of the Public Staff (direct testimony);

6. Richard N. Smith, Engineer with the Electric Division of the Public Staff (direct testimony);

7. William W. Winters, Supervisor of the Electric Section of the Accounting Division of the Public Staff (direct and additional testimony);

8. Thomas S. Lam, Engineer with the Electric Division of the Public Staff (direct testimony);

9. Nancy B. Bright, Director of the Accounting Division of the Public Staff (direct testimony); and

10. Dr. Caroline M. Smith, Senior Consultant, J. W. Wilson and Associates, Inc. (direct testimony).

The Attorney General of the State of North Carolina presented the testimony and exhibits of the following witnesses:

1. Dr. John K. Stutz, Senior Research Scientist with Energy Systems Research Group, Inc.; and

2. Dr. Richard A. Rosen, Executive Vice President and Senior Research Scientist with Energy Systems Research Group, Inc.

The Intervenor Department of Defense presented the testimony and exhibits of John William McCabe III, of the consulting firm of McCabe Associates, Inc.

The Intervenor Kudzu Alliance presented the testimony and exhibits of Wells Eddleman.

The Intervenor Carolina Industrial Group for Fair Utility Rates presented the testimony and exhibits of Maurice E. Brubaker, Vice President, and Nicholas Phillips, Jr., Consultant, Drazen - Brubaker and Associates, Inc., and those of Dr. Jay B. Kennedy, Executive Director of the Electricity Consumers Resource Council.

The Commission issued an Order Granting Partial Increase in Rates and Charges in this docket on September 19, 1983.

On September 30, 1983, Carolina Power & Light Company filed a Motion for Reconsideration asking the Commission to reconsider that portion of Finding of Fact No. 7 in the September 19, 1983 Order which requires treatment of investment tax credits associated with property sold to the North Carolina Eastern Municipal Power Agency as an addition to the gain from the sale. On October 7, 1983, the Public Staff filed a response to CP&L's Motion for Reconsideration urging that reconsideration be denied or, if reconsideration

be undertaken, that no amendment or change be ordered. On October 4, 1983, the Attorney General filed a Motion for Reconsideration asking the Commission to reconsider Finding of Fact No. 13 in the September 19, 1983 Order dealing with fuel costs. On October 11, 1983, the Public Staff filed a Motion for Reconsideration also asking the Commission to reconsider Finding of Fact No. 13.

On that same date, October 11, 1983, the Public Staff filed a Motion pursuant to G. S. 62-90, as amended, asking for an extension of time within which any party may appeal from the September 19, 1983 Order. The Commission issued an Order on October 14, 1983, allowing an extension of time within which any party may appeal the September 19, 1983 Order for an additional thirty days, up to and including November 18, 1983, and scheduling an oral argument on the outstanding motions for reconsideration for October 24, 1983. The oral argument was convened as scheduled, and the Commission heard argument on behalf of Carolina Power & Light Company, the Public Staff, the Attorney General, the Carolina Industrial Group for Fair Utility Rates, and the North Carolina Textile Manufacturers Association.

On November 17, 1983, the Public Staff filed Exceptions and Notice of Appeal, and on November 18, 1983, the Attorney General filed Exceptions and Notice of Appeal. As of November 18, 1983, the deadline for parties to appeal the September 19, 1983 Order, the Commission had not reached its decision on reconsideration. However, the time for cross appeals having not yet expired, the Commission continued its reconsideration pursuant to the authority of G. S. 62-80. See State ex rel. Utilities Commission v. Edmisten, 291 N.C. 575, 581-82 (1977). The Supreme Court wrote in that case, "We think it clear that G. S. 62-80 is broad enough to permit the Commission to modify and amend its order, even substantially, for the reason that, upon further consideration of the record before it, the Commission comes to the opinion that its order was due to the Commission's misapprehension of the facts, or disregard of facts, shown by the evidence received at the original hearing." Id. at 584. See also G. S. 62-90(c), which provides that the Commission may on its own motion set exceptions filed along with a notice of appeal for further hearing before the Commission. On November 29, 1983, the Commission issued an Order requesting that certain data be filed by the Company on or before December 1, 1983. The Company filed such data on December 1, 1983.

Upon reconsideration of Findings of Fact Nos. 7 and 13 of the September 19, 1983, Order pursuant to G. S. 62-80 on the basis of the record already compiled, the Commission now issues the present Order on Reconsideration.

Based upon the verified application, the testimony and exhibits received into evidence at the hearings, and the record as a whole of these proceedings, the Commission now makes the following

FINDINGS OF FACT

1. CP&L is engaged in the business of developing, generating, transmitting, distributing, and selling electric power and energy to the general public within a broad area of eastern and western North Carolina, with its principal office and place of business in Raleigh, North Carolina.

2. CP&L is a public utility corporation organized and existing under the laws of the State of North Carolina and is subject to the jurisdiction of this Commission. CP&L is lawfully before this Commission based upon its application for a general increase in its North Carolina retail rates and charges pursuant to the jurisdiction and authority conferred upon the Commission by the Public Utilities Act.

3. The test period for purposes of this proceeding is the 12-month period ended September 30, 1982, adjusted for certain known changes based upon circumstances and events occurring up to the time of the close of the hearings in this docket.

4. CP&L, by its application, sought an increase in its basic rates and charges to its North Carolina retail customers of $164,912,650.

5. The overall quality of electric service provided by CP&L to its North Carolina retail customers is adequate.

6. The "summer/winter peak and average" method as discussed herein is the most appropriate method for making jurisdictional allocations and for making fully distributed cost allocations between customer classes in this proceeding. Consequently each finding of fact appearing in this Order which deals with the overall level of rate base, revenues, and expenses for North Carolina retail service has been determined based upon the summer/winter peak and average cost allocation method.

7. The appropriate treatment in this case to reflect the sale of assets to North Carolina Eastern Municipal Power Agency (NCEMPA) include: (a) a three-year amortization of the gain flowed through to the ratepayers, (b) a reduction from rate base for the unamortized portion of the gain on the sale, (c) an additional rate base deduction of $50,383,000 related to Accumulated Deferred Income Taxes associated with the sale, and (d) an allocation of 68.7% of the gain to the North Carolina retail customers.

8. The Company should be allowed to recover its abandonment loss sustained as the result of the Company having terminated construction on, and having abandoned, its Shearon Harris Nuclear Units Nos. 3 and 4. The recovery of the Company's investment in those units should be over a 10-year amortization period. It is neither fair nor reasonable to include any portion of the unamortized balance of this investment in rate base, and no adjustment which would have the effect of allowing the Company to earn a return on the unamortized balance of this investment should be ordered.

9. The Company should be allowed to continue the recovery of its abandonment loss sustained as the result of the Company having terminated construction on, and having abandoned, the South River Project and the Brunswick cooling towers, as previously allowed by the Commission; however, the unamortized balance of these investments should no longer be included in

rate base nor should any adjustment be ordered which should have the effect of allowing the Company to earn a return on the unamortized balance on these investments.

10. CP&L has mistakenly interpreted and applied prior Orders of this Commission which specified and directed the methodology to be used to compute the amounts charged to North Carolina retail ratepayers for coal purchased from CP&L's affiliated coal mines. It is appropriate that such mistakes be corrected by this Commission.

11. Seventy-eight days of outages at CP&L's Brunswick Unit Nos. 1 and 2 in the Summer of 1982 largely resulted from past inefficiency in nuclear plant management practices. This inefficiency increased the cost of service to CP&L's customers. For these reasons, a rate of return penalty should be imposed on CP&L.

12. A normalized test period generation mix is appropriate for determining the base fuel component in the rates.

13. A base fuel component of 1.677¢ per kWh excluding gross receipts tax is appropriate for this proceeding, reflecting a reasonable fuel cost of $315,593,000 for North Carolina retail service. The 1.677¢ per kWh base fuel component in the rates does not reflect an "experience factor."

14. A $76,079,959 working capital allowance for fuel inventory is appropriate for North Carolina retail service in this proceeding, consisting of $69,489,429 for coal inventory, $6,507,444 for liquid fuel inventory, and $83,086 miscellaneous fuel stock.

15. The reasonable working capital allowance and deferred debits and credits is $98,868,000.

16. The proper amount of reasonable and prudent expenditures for construction work in progress (CWIP) to allow in rate base pursuant to G. S. 62-133 is $539,781,000. Inclusion of this amount of CWIP in rate base is in the public interest and is necessary to ensure the financial stability of CP&L. This leaves a North Carolina retail amount of approximately $582 million CWIP not included in the rate base.

17. CP&L's reasonable original cost rate base used and useful in providing service to the public within the State of North Carolina is $2,222,871,000; consisting of electric plant in service of $2,431,733,000, net nuclear fuel of $25,172,000, and construction work in progress of $539,781,000, a working capital allowance of $98,868,000, reduced by accumulated depreciation of $559,362,000 and accumulated deferred income taxes of $313,321,000.

18. Appropriate gross revenues for CP&L for the test year, under present rates and after accounting and pro forma adjustments, are $1,104,072,000.

19. The reasonable level of test year operating revenue deductions for the Company after normalized and pro forma adjustments is $902,976,000.

20. The reasonable capital structure to be employed as a basis for setting rates in this proceeding is composed as follows:

Debt	49.5%
Preferred stock	12.5%
Common stock	38.0%
Total capitalization	100.0%

21. That the Company's embedded cost of debt and preferred stock are 9.59% and 8.96%, respectively. In view of the poor nuclear performance resulting from past management inefficiency and imprudence as described herein, the rate of return for CP&L to be allowed to earn on its common equity is 14.5%. In absence of its poor nuclear performance, CP&L would have been entitled to a 15.25% rate of return on common equity. Using a weighted average for the Company's cost of long-term debt, preferred stock, and common equity, with reference to the reasonable capital structure heretofore determined, yields an overall fair rate of return of 11.38% to be applied to the Company's original cost rate base. Such rate of return will enable CP&L, by sound management, to produce a fair return for shareholders, to maintain its facilities and service in accordance with the reasonable requirements of its customers, and to compete in the market for capital on terms which are reasonable and fair to its customers and to existing investors.

22. The Commission in its September 19, 1983, Order found that CP&L should increase its annual level of gross revenues under the then current rates by $90,855,000. The Commission further found that the annual revenue requirement approved in the September 19, 1983, Order of $1,196,049,000, would allow CP&L a reasonable opportunity to earn the rate of return on its rate base which the Commission has found just and reasonable. The revenue requirement approved therein was based upon the original cost of CP&L's property used and useful in providing service to its customers and its reasonable test year operating revenues and expenses as previously set forth in these findings of fact. The Commission recognizes that the annual gross revenue increase reflected herein on reconsideration of $91,211,000 exceeds by $356,000 the annual gross revenue increase established by the Commission's Order Granting Partial Increase in Rates and Charges issued September 19, 1983. However, due to the lack of materiality of such an increase relative to the Company's total revenue requirements (less than .0003) the Commission finds it unreasonable for CP&L to increase the rates and charges which became effective on September 19, 1983, in order to recover such a <u>de minimus</u> amount. The Commission therefore finds it reasonable for CP&L to maintain without change the rates and charges which became effective September 19, 1983.

23. Further study and discussion is needed with regard to quantifying an appropriate cost differential between summer and winter months for residential service and between on-peak and off-peak hours for all customer classes.

24. It is appropriate that the Company reduce the on-peak hours in its Residential Time of Use rate schedule R-TOU from 10:00 p.m. to 9:00 p.m. during the summer months.

25. It is not appropriate that the Company expand its load control program to include customers with thirty (30) gallon water heaters at this time.

26. It is appropriate that Large General Service Time of Use rate Schedule LGS-TOU and Customer Generation Rider 55 exclude a billing demand ratchet, and that such exclusion be without prejudice to the Company seeking a ratchet at a later date which would recover distribution fixed costs only.

27. The rate designs, rate schedules, and service rules filed by the Company in response to the Commission's September 19, 1983, Order, except for the modifications thereto as described herein, are appropriate and should be maintained by the Company.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 1 AND 2

The evidence supporting these findings of fact is contained in the Company's verified application, in prior Commission Orders in this docket of which the Commission takes notice, and G.S. 62-3(23)a.1 and G.S. 62-133. These findings of fact are essentially informational, procedural, and jurisdictional in nature and the matters which they involve are essentially uncontested.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 3 AND 4

The evidence supporting these findings of fact is contained in the Company's verified application, the Commission Order issued March 7, 1983, and the testimony and exhibits of Company witnesses Smith, Lilly, Bradshaw, Nevil, Faucette, Watson, and Edge.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 5

The evidence for this finding of fact is found in the testimony of Company witness Smith and that of various public witnesses who testified at the hearings which were held in this matter in Asheville, Wilmington, Goldsboro, and Raleigh. Careful consideration of such evidence leads the Commission to conclude that the quality of electric service which the Company is providing to its North Carolina retail customers is adequate.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 6

The evidence for this finding of fact consists primarily of the testimony and exhibits of Company witness Chapman; Public Staff witness Turner; Department of Defense (DOD) witness McCabe; Carolina Industrial Group for Fair Utility Rates (CIGFUR) witnesses Brubaker, Phillips, and Kennedy; and Kudzu Alliance witness Eddleman.

CP&L provides retail service in two states, as well as wholesale service. For this reason, it is necessary to allocate the cost of service among jurisdictions and among customer classes within each jurisdiction. In its four previous rate cases in North Carolina, the Company proposed the "summer peak and average" method for allocation of production level costs. The Commission did not change from the summer coincident peak method to the peak and average method in the first case, Docket No. E-2, Sub 366. However, in the next two cases, Docket Nos. E-2, Sub 391, and E-2, Sub 416, the Commission adopted the peak and average method. In the Company's last rate case, Docket No. E-2, Sub 444, the Commission modified the peak portion of the peak and average method to reflect the average of the summer and winter coincident peaks rather than the summer peak only.

In this case, the Company proposed the "summer/winter peak and average" (SWP&A) approved by the Commission in Docket No. E-2, Sub 444. The SWP&A allocates approximately 40% of production plant and related expenses based on peak responsibility, in this case the average of the summer and winter peak

demands, and the remaining approximately 60% based on kWh consumption. The 60/40 split is determined by the system load factor calculated using the average of the summer and winter peaks.

Public Staff witness Turner recommended that the SWP&A method be utilized for the purpose of assigning costs to the North Carolina retail jurisdiction. He recommended that the "summer/winter peak and base," or modified peak and base (MPB), methodology be utilized for the purpose of assigning costs to the retail rate classes. The MPB allocation method allocated 65% of production plant and related expenses on an average of summer and winter coincident peak demand (kW) and the remaining 35% based on energy (kWh). The MPB method differs from the SWP&A method proposed by CP&L in that the MPB method allocates 35% of production costs by energy.

Witness Turner stated that the Company's proposed use of the summer/winter peak and average method for rate design purposes may be unfair to certain customer classes because, in his opinion, it does not recognize the possibility that the costs of fuel may vary among classes. For example, if a particular customer class is assigned base load plant costs, witness Turner contended that it should also be assigned the lower fuel costs associated with the base load plant. Conversely, if a class is assigned primarily peaking plant costs, witness Turner contended that it should also be assigned the higher fuel costs associated with the peaking plant.

Witness Turner cited a Public Utilities Fortnightly article entitled "Bias in Traditional Capacity and Energy Cost Allocation" which pointed out that there can be significant differences in costs among customer classes if the higher load factor customer is not assigned the lower fuel costs associated with base load plant. Witness Turner also stated that a recent NRRI Workshop which he attended concentrated on a method of allocating capital costs and fuel costs based on actual loads, which tended to show that the assignment of energy or fuel costs by the energy allocation factor may overcharge some customers for fuel and undercharge others. Therefore, witness Turner recommended that the Commission adopt the summer/winter peak and base method for rate design purposes as a more conservative step in the recognition of energy-related production plant costs.

CIGFUR witness Brubaker proposed to allocate production costs based on the one-hour coincident peak (CP) allocation method. Brubaker contended that it is primarily the system peak demand that drives the need for the addition of capacity. He contended that said capacity cost should be allocated to each customer class by each class's kilowatt contribution to the system peak. Witness Brubaker contended that allocating the fuel cost to each customer class based on energy usage is not "symmetrical" with the peak and average approach. The result, in his opinion, is that the SWP&A method fails to give the high load factor customers the benefit of the lower fuel costs associated with the production plant investment assigned to them.

CIGFUR witness Phillips also testified that the Company's SWP&A allocation method lacked "symmetry" between allocation of production plant investment and allocation of fuel costs. In support of the CP method, Phillips argued that allocation of plant investment on the basis of the single annual peak and allocation of fuel on the basis of energy usage did not suffer the same problems with "symmetry."

Witness Eddleman testified that the most appropriate way to allocate costs is to use the coincident peak method with the summer/winter contribution of each customer class averaged.

The Commission concluded in previous rate cases, for reasons explained extensively in Docket No. E-2, Sub 444, that the cost allocation method utilized for rate-making purposes should recognize the energy related portion of fixed costs. Essentially, the Commission reasoned that not all fixed costs represent the cost of meeting system peak demand, and that a significant portion of fixed costs represents the cost of producing kWh during many hours of the year and of producing such kWh at a lower fuel cost per kWh. The Commission continues to be persuaded in this proceeding that the cost allocation method utilized herein should recognize the energy related portion of fixed costs.

CIGFUR witness Phillips presented an exhibit showing declining system load factors in more recent years and contended that the exhibit demonstrated the detrimental effect of using the peak and average method for cost allocation during the past three years. However, upon closer examination of the exhibit by the Commission, it appears that the load factors are calculated using a mixture of summer peaks and winter peaks. If the exhibit is recalculated using annual summer peaks only, the resulting system load factors in recent years will be very consistent with all system load factors over the past 10 years. On the other hand, if the exhibit is recalculated using annual winter peaks only, the resulting system load factors in recent years will decline in comparison with all system load factors over the past 10 years. Therefore, any decline in system load factor appears to be the result of the winter peak, not the summer peak, and appears to call for a cost allocation method which places more emphasis on usage during the winter peak and less emphasis on usage during the summer peak.

The Commission concluded in the previous rate case, for reasons explained extensively in Docket No. E-2, Sub 444, that it is not persuaded that system capacity is installed to meet a single system peak, and that both the summer peak and the winter peak should be recognized in the cost allocation process. The evidence presented in this proceeding continues to persuade the Commission that the summer/winter peak as proposed by the Company is appropriate for use as a part of the cost allocation process.

DOD witness McCabe testified that he preferred the 12-month coincident peak allocation method. The Commission has reviewed the rates of return resulting from various cost allocation methods in this proceeding and notes that the rates of return are very similar when comparing: (1) the 12-month peak and average method with the summer/winter peak and average method; (2) the 12-month peak and base method with the summer/winter peak and base method; and (3) the 12-month coincident peak method with the summer/winter coincident peak method. Therefore, the Commission is of the opinion that the summer/winter peak (i.e., average of summer and winter peaks) produces results which are as satisfactory as the 12-month peak (i.e., average of 12 monthly peaks) for cost allocation purposes in this proceeding.

The Company presented two cost allocation studies in this proceeding based on variations of a "stacking" methodology. The "stacking" method used for the studies is the same used for similar studies presented in the previous rate case in Docket No. E-2, Sub 444. The Commission concluded in the previous

rate case that the "production stacking" method, one of the two variations presented, demonstrated that the energy-related portion of fixed costs might well be as much as 60% of total fixed costs (of production plant).

For this proceeding, Public Staff witness Turner pointed out several inconsistencies in the "production stacking" methodology, including the problem of different dollar vintages associated with the embedded cost of each of the generating units. While the Commission recognizes the limitations of the "production stacking" method as a cost allocation method, it is of the opinion that said method still represents a good faith effort to quantify the amount of fixed costs which might be classified as energy related, and as such it represents a useful tool for comparing the cost allocation methods proposed by the various parties to this proceeding. The Commission would welcome any improvements in the studies or any alternative studies which might be useful in quantifying the energy-related portion of fixed costs.

The Commission concludes that the summer/winter peak and average method for allocating costs is appropriate for this proceeding. The Commission further concludes that the Company should continue to file alternative cost allocation studies in future general rate proceedings in order to facilitate further discussion of the many issues raised regarding cost allocation.

Another area for discussion is the assertion by several parties to this proceeding that allocation of energy-related fixed costs (of production plant) by means of kWh usage, as provided by the summer/winter peak and average method, will cause high load factor customers to bear a greater share of responsibility for such fixed costs, and that such high load factor customers will not at the same time be given a greater share of credit for the lower fuel costs associated with the fixed costs.

The summer/winter peak and average method allocates energy-related fixed costs for base load plants by kWh usage in the same proportions as the low cost fuel for said base load plants is allocated by kWh usage. The Commission must reject any assertion that such allocation of energy-related fixed cost is not consistent with allocation of low cost fuel, because both types of costs are allocated in exactly the same proportions.

The summer/winter peak and average method allocates demand-related fixed costs (for base load plants and for peaking plants) by means of peak responsibility (i.e., by one or more system peaks). There has not been any serious assertion by proponents of the peak responsibility methods that the fuel costs for said peaking plants (or for base load plants) should also be allocated by peak responsibility.

Witness Turner suggested that the problem of quantifying the energy-related portion of fixed costs (of production plant) might be resolved by means of a cost allocation study which assigns both fixed costs and variable costs to each of the 8760 hours of the year, and he recommended that such a study be undertaken. The study could also resolve limitations found in the Company's attempts to determine appropriate cost differentials between summer usage versus winter usage and between on-peak usage versus off-peak usage as discussed elsewhere herein.

The Company pointed out that a study which would assign costs to the hours during which those costs were incurred, and which would also allocate the

costs in each given hour to customer classes based on their kWh usage during the given hour, would be a very large undertaking and could require a significantly larger load survey effort in order to be statistically valid. The Company suggested that it be allowed to work with the Public Staff to develop a study which would be responsive to the concerns discussed herein and would also be a reasonable undertaking from a cost and a technical standpoint. The Commission concludes that the Company's suggestion represents the best course to follow in this proceeding.

Finally, the Commission would point out that the matter of assigning costs is not an exact science, and therefore that further review and study is an appropriate matter for continuing consideration. Some members of the Commission prefer that the matter not be considered as a final judgment based on the evidence presented in this case. For instance, the assigning of class cost responsibilities may have a significant effect or impact on the assignment of jurisdictional cost responsibilities. Thus, the Commission will follow with interest the methodologies adopted by regulatory bodies in other jurisdictions. In any event the Commission, in adopting the summer/winter peak and average allocation method in this proceeding, does not preclude the possibility that additional data may indicate the need for considering and possibly adopting some other methodology in future proceedings.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 7

The evidence supporting this finding of fact is found in the testimony and exhibits of Company witnesses Smith, Lilly, Faucette, Bradshaw, Nevil, Chapman, and McClellan; Public Staff witnesses Dennis and Winters; and DOD witness McCabe.

During 1981, CP&L concluded negotiations with the North Carolina Eastern Municipal Power Agency (NCEMPA) for the sale of interests in certain of the Company's generating units. The agreements between CP&L and NCEMPA provided for a series of closings to effect this transaction, with each closing increasing the percentage ownership of assets by NCEMPA until 100% of the agreed-upon share was transferred. The first closing of a 33% ownership share took place in April 1982. After additional closings in August, October, and November 1982, a final closing took place in April 1983, which brought NCEMPA ownership to 100% of the agreed-upon share of facilities.

Company witness Chapman testified that as of the final closing, NCEMPA owned generating capacity equal to approximately 52% of its present load requirements. Until the completion of the purchased units, which are still under construction, CP&L will provide for service to meet the remainder (presently 48%) of the NCEMPA requirements under the provisions of the Power Coordination Agreement (PCA). In addition, the Company will provide NCEMPA with backstand power during periods when its share of owned units is unavailable due to maintenance, modification, or forced outages. Sales by CP&L to NCEMPA under the PCA are termed Supplemental Sales. Revenues related to these sales are determined in accordance with pricing mechanisms specified in the PCA.

A number of Company witnesses testified regarding the benefits of the sale to NCEMPA. Witness Smith testified that these benefits included reduction of the need for outside financing during 1982, reduction of future construction expenditures, increased financial strength which prevented a further lowering

of the Company's security ratings, and the added assurance that adequate generating capacity can be completed to provide for future growth. Company witness Smith testified that NCEMPA has paid the Company approximately $700 million during the 1982-1983 time period. Company witness Lilly testified that NCEMPA will contribute another $670 million over the next 10 years toward its share of new construction. Witness Lilly indicated that these funds would slow the rise of embedded capital costs and thus hold down customer rates.

Company witness Bradshaw testified that the customer would also benefit from the Company's proposal to flow the majority of the profit realized above book value back to the customer; from provisions for the buy-back of power from NCEMPA at prices below CP&L's cost; and by the lower AFUDC rate that would result due to reduced capital costs. Company witness Chapman testified that an ongoing benefit to the customer of the sale is the additional load portion of NCEMPA, comprised of load not previously served by CP&L which reduces the portion of fixed costs each customer must pay.

As a result of the CP&L sale to NCEMPA and the associated agreements, the Company has incorporated in its filing in this docket a number of adjustments. These relate to the specific treatment of the various costs and revenues on which the sale had an impact, including: profit above book value realized from the sale, revenues from supplemental sales to NCEMPA, and adjustments to pro forma test year results to exclude 100% of NCEMPA's ownership. The Company contends that the overall result of its treatment of the NCEMPA sale is a benefit to the North Carolina retail customers. This is due primarily to the improvement in Company's financial condition and a reduction in future need for capital which lowers capital costs, the flow-back of the profit or gain to the customers, and provisions for buy-back of power at a discount from NCEMPA's portion of generating units. The Company believes that its treatment of the elements of the NCEMPA transaction should be viewed as a negotiated package and that, as such, it results in a substantial net benefit to the ratepayer.

The Company and certain of the parties are in disagreement with respect to:

1. The time period for flowing back the gain;
2. The treatment of the unamortized balance of the gain;
3. The allocation of the gain;
4. The treatment of accumulated deferred taxes associated with the gain;
5. The time period for flowing back investment tax credits associated with plant sold to NCEMPA; and
6. The calculation of Supplemental Revenues.

The first specific item for discussion is the profit or gain received by CP&L as a result of the sale. This gain of $37,327,000 is the amount by which the price paid for shares of generating units exceeds the proportional original cost of those units. There are three issues to be resolved arising from this gain. These are:

1. Over what time period should the gain be flowed through to the customer?

2. If the period is longer than one year, how should the unamortized portion of the gain be treated?

3. What is the proper allocation of the gain to North Carolina retail customers?

Regarding the time period for flowing the gain to the customers, the Company has proposed three years. The Company accomplishes the flow-back by an adjustment which increases Income for Return and, thereby, because of associated taxes, decreases the North Carolina retail revenue requirement by approximately twice the amount of the income for return adjustment. Company witness Bradshaw testified that in his opinion the gain, under normal accounting procedures, belongs to the stockholder but that the Company is flowing it through to its customers to offset the costs of cancelled plants. Since the flow-through is a benefit to the ratepayer, it is being amortized over only three years. Witness Bradshaw testified that if the gain had been an expense of comparable magnitude, the Company would have requested a longer amortization period.

Public Staff witness Winters recommended that the entire gain be flowed through to the ratepayer in the current rate case because the Company presently has the proceeds from this sale available to it. Witness Winters testified that if the Company's position is accepted, the revenue requirement in this case will be $35,838,000 greater than his recommendation. Witness Winters additionally stated that the Company, in its last rate case had proposed flowing through the entire gain that had been realized at that time.

Company witness Bradshaw testified that the Company's position has been consistent between rate cases because in the last case the Company proposed flowing back one-third of the gain, which was the gain that had been realized at that time. The Company is again recommending that one-third of the gain be flowed through per year.

The Commission, having reviewed the evidence in this case, believes that a three-year amortization of the gain is reasonable. The Commission recognizes that an extraordinary event of this amount, whether a profit or an expense, should be amortized over some period of time. The Commission believes it is appropriate to adopt the amortization period proposed by the Company of three years. Therefore, the three-year amortization period recommended by the Company is found to be reasonable.

The second issue relating to the gain is the proper treatment of the unamortized balance of the gain. The Company has included an adjustment to increase income for return by $742,008 which represents a return on the debt portion of the unamortized gain. The Company thereby reduces the revenue requirement based on the debt portion of the gain. Company witness Bradshaw testified that this is consistent with the Commission treatment of the Harris Units No. 3 and 4 loss in Docket No. E-2, Sub 444, and the Company's requested treatment of the Harris Units No. 3 and 4 unamortized balance in this case. In Docket No. E-2, Sub 444, the Commission allowed the Company to earn a return on only the debt portion of the loss by decreasing Income for Return by such amount.

Public Staff witness Winters recommended that if the gain is amortized over a three-year period, the entire unamortized balance should be treated as cost-free capital and be deducted from rate base. Witness Winters testified that the Company's position on this issue allows the Company to earn preferred and common equity returns on funds which were not provided by the equity

investors and have no costs to the Company. Witness Winters recommended that these funds be treated in a similar manner to other cost-free capital.

After careful consideration of this issue, the Commission finds it appropriate to deduct the unamortized gain on the sale to NCEMPA from the rate base in this proceeding. The unamortized gain on the NCEMPA sale represents cost-free capital to the Company and in the Commission's opinion it is unreasonable and improper to expect the ratepayers of the Company to pay a return on capital which has no costs to the Company.

The final issue related to the gain for consideration by the Commission involves the proper allocation of the gain on the NCEMPA sale to the North Carolina retail jurisdiction. Both the Company and the Public Staff used a production plant allocation factor to allocate the total Company gain to the North Carolina jurisdiction. However the Company used an allocation factor which reflected how production plant was allocable to this jurisdiction prior to the sale of that production plant which gave rise to the gain in question. The Public Staff, on the other hand, used an allocation factor which reflected how production plant was allocable to this jurisdiction after the sale in question.

Public Staff witness Winters presented an explanation of why and how the sale in question changed the production plant allocation factor. Witness Winters' testimony in that regard was as follows:

> "Immediately prior to the sale in question, CP&L was serving the customers of the N. C. Eastern Municipal Power Agency as wholesale customers of CP&L. However, by virtue of the sale itself those customers were eliminated as CP&L wholesale customers. The interest in the generating units sold to the Power Agency is now owned by it -- not CP&L -- and used by it -- not CP&L -- to serve its member customers. Thus, the sale reduced the relative percentage of the remaining production plant allocable to CP&L's post-sale wholesale customers. Concomitantly the sale increased the amount of CP&L's post-sale production plant which is properly allocable to its N. C. retail customers."

The evidence indicates that if the total Company gain of $37,327,000 is allocated based upon CP&L's method, then only 62.8% of that gain is allocated to North Carolina retail customers. However, the evidence indicates that after the sale, the Company's production plant allocable to this jurisdiction is actually 68.7%.

Presumably, under CP&L's allocation method the 5.9% of the gain in controversy would either go to its shareholders or would be flowed back to its post-sale wholesale customers. If that portion of the gain were flowed back to CP&L's post-sale wholesale customers, it would constitute a "windfall" to them. Nor does there appear to be any logical reason why that portion of the gain should inure to the benefit of CP&L's shareholders. In any event, neither treatment would be fair to the North Carolina retail ratepayers. This is true because those retail ratepayers must now pay a return on a higher percentage of the production plant remaining on the CP&L system after the sale to the Power Agency than they would have paid on the same plant prior to the sale. Based upon a careful consideration of the evidence on this issue the Commission concludes that the post-sale allocation factor proposed by the Public Staff and the Department of Defense should be used for allocating the gain on the sale to the North Carolina retail customers.

The next area for consideration is the rate base treatment for the Deferred Taxes associated with the gain from the sale to NCEMPA. The Company, in its filing, made an adjustment to its per books values to reverse the booking of Deferred Taxes in Account 190 associated with the gain from the sale to NCEMPA. The effect of this adjustment was to reduce North Carolina retail rate base by $36,500,247.

The Public Staff made an adjustment to Accumulated Deferred Income Taxes which results in an additional rate base deduction of $50,383,000 on a North Carolina retail basis. The difference of $50,383,000 results from the adjustment made by witness Winters regarding the deferred income taxes related to the sale of certain generating plant and transmission lines to the North Carolina Eastern Municipal Power Agency. Witness Winters testified in this regard as follows:

"The gain on the sale to the Power Agency was reduced approximately $88,000,000 for taxes which will not have to be paid until years into the future. The Company has already received the funds to pay these taxes through proceeds from the Power Agency. The Company has proposed not to include these deferred income taxes as a rate base deduction in this case; and, if these deferred income taxes are not deducted from rate base, the ratepayers will be required to pay a return on funds which were not provided by the debt and equity investors. I recommend that the N. C. retail portion of these deferred income taxes be deducted from rate base in this proceeding as cost-free capital just as other deferred income taxes are deducted as cost-free capital.

As part of my adjustment for deferred income taxes I have increased rate base by approximately $15,000,000 to reflect the elimination of deferred income taxes which the Company treats as cost-free capital. This adjustment is necessary because these same deferred taxes were reflected as an increase in the gain on the sale."

The Company, through witness Bradshaw, takes the view that the ratepayer did not provide the funds associated with these deferred taxes and should not, therefore, benefit from a rate base reduction resulting from them. Rather, NCEMPA, which purchased from the Company's investors certain generating facilities, provided the funds associated with these deferred taxes to the Company's investors. Witness Bradshaw contended that the property that created the deferred taxes is not in rate base, has not been requested to be in rate base, and, therefore, the related deferred taxes should not be deducted from rate base.

The Commission, after reviewing the evidence on this issue, recognizes that the deferred taxes associated with the sale to NCEMPA represent cost-free funds to the Company since these funds have been contributed to CP&L by NCEMPA. CP&L has the use of these funds until such time as the taxes must be paid. The Commission concludes that deferred taxes associated with the NCEMPA sale should be treated as other cost-free capital to the Company and deducted from rate base. Thus, the Commission concludes that deferred income taxes should be increased by $50,383,000 and that the appropriate level of deferred income taxes for use in this proceeding is $313,321,000.

The next area for consideration relating to the sale to NCEMPA is the proper treatment of Investment Tax Credits which are related to property sold to NCEMPA. The Company has continued to treat these Investment Tax Credits as it does all others and flows them back ratably over the life of the property.

Public Staff witness Winters recommended that the Investment Tax Credits associated with property sold to NCEMPA be flowed back currently. Witness Winters' opinion is that current flow-through of these amounts would not be in violation of IRS regulations since the applicable Code provision refers to the useful life of property. Witness Winters further contends that the useful life has terminated when the plant has been sold.

Company witness McClellan testified that a current flow-through of the Investment Tax Credits associated with the sale would be in violation of Section 46(f)(2) of the Internal Revenue Code. In witness McClellan's opinion, current flow-through will exceed the ratable flow-through mandated. Witness McClellan testified that if the Company is found in violation of this provision, it stands to lose Investment Tax Credits retroactively to 1975. The total projected loss for the period 1975-1984 would approximate $300,000,000 on a total system basis. Witness McClellan supported his interpretation of the IRS Code with a legal opinion from tax counsel.

The Commission concludes that the determination of the appropriate rate-making treatment for the Job Development Investment Tax Credits relating to the portion of the generating and transmission plant sold to NCEMPA should properly be held in abeyance at this time. The Commission finds that the Company should seek to obtain a ruling from the United States Internal Revenue Service (IRS) regarding this matter. The Commission further concludes that it is prudent for the Company to file with the Chief Clerk of the Commission a draft of the Company's proposed letter requesting a ruling on the matter for review by the Commission and Public Staff prior to submitting the request to the IRS. The resultant ruling or findings of the IRS or the current status of the matter should properly be presented to the Commission in the Company's next general rate proceeding for resolution of the issue by the Commission at that time.

The final area for consideration, which relates to the NCEMPA transactions, is the proper treatment of the revenues from NCEMPA for supplemental sales. The Commission will hereafter discuss this issue in Evidence and Conclusions for Finding of Fact No. 18.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 8 AND 9

Evidence with respect to the rate-making treatment of abandonment losses can be found in the testimony of Company witness Paul S. Bradshaw and Public Staff witness William W. Winters. The Public Staff takes the position that the abandonment loss should be amortized over a 10-year period and that the unamortized balance of the loss should be excluded from rate base and the Company should not be allowed to earn any return on it. The Public Staff argues that G. S. 62-133 only allows a utility to earn a return on property which is "used and useful" in providing utility service or which is construction work in progress that meets the standards set forth in the statutes. The Public Staff argues that abandonment losses qualify under neither category, that they must be excluded from the rate base, and that the Company must not be allowed to earn any return on them. In previous

proceedings before the Commission, the Company has been allowed to amortize the cost of the South River Project and the Brunswick cooling towers and to include the unamortized balance of the projects in rate base. See Docket Nos. E-2, Sub 391 and E-2, Sub 416. In the last CP&L rate case before the Commission, the Commission allowed the Company to amortize the cost of Harris Units Nos. 3 and 4 over a 10-year period, and allowed that portion of the unamortized balance supported by long-term debt to be included in rate base. See Docket No. E-2, Sub 444. The Company argues that these treatments should be continued.

The proper rate-making treatment of abandonment losses has been before the Commission in several cases and will continue to arise in many future cases. The Commission has, therefore, undertaken to re-examine this important issue in order to develop a more consistent and equitable approach to it. The Commission's ultimate responsibility with respect to ratemaking is to fix rates for the service provided which are fair and reasonable both to the utility and to the consumer. G. S. 62-133(a); State ex rel Utilities Commission vs. Morgan, 277 NC 255, 177 SE 2 405 (1970); State ex rel Utilities Commission vs. Carolina's Committee, 257 NC 560, 126 SE 2d 325 (1962).

Although parties may disagree as to the amortization period, they agree that the Company should be allowed to recover the prudently invested cost of its abandonment losses through amortization over some period of time. The Commission, based upon the evidence presented, must determine what is a fair amortization period in order to fairly allocate the loss between the utility and the consumer. In the last CP&L rate case, the Commission determined that a 10-year amortization period for abandonment losses resulting from cancellation of Harris Units No. 3 and 4 "will more reasonably and equitably serve to share the burden of the cancellation of Harris Units No. 3 and 4 between present and future ratepayers. Furthermore, use of a ten-year amortization period is also consistent with previous decisions of the Commission regarding amortization of similar property losses set forth in Orders." Amortization of these abandonment losses should be continued as previously ordered. Similarly, the Commission believes that the amortization of the losses resulting from cancellation of the South River Project and the Brunswick cooling towers should continue as previously ordered by the Commission.

Pursuant to the Commission's reexamination of the proper ratemaking treatment of abandonment losses, the Commission has determined that it is neither fair nor reasonable to include any portion of the unamortized balance of such investments in rate base and, furthermore, that no adjustment should be allowed which would have the effect of allowing the Company to earn a return on the unamortized balance. The Commission has concluded that this treatment provides the most equitable allocation of the loss between the utility and the consumer. It would be inequitable to place the entire loss of expenditures that were prudent when made on the utility. Thus, amortization should be allowed. However, on the other hand, the ratepayer must not bear the entire risk of the Company's investment. A middle ground must be found on which the Company bears some of the risk of abandonment and the ratepayer is protected from unreasonably high rates. The losses resulting from cancellations of utility plants will inevitably be borne by one or a combination of three groups: the utility investors, the ratepayers, and the income taxpayer. A recent study prepared by the United States Department of

Energy indicates that a 10-year amortization of such losses will distribute costs in proportions that the Commission considers fair and equitable. NUCLEAR PLANT CANCELLATIONS: CAUSES, COSTS, AND CONSEQUENCES, United States Department of Energy, Washington, D. C. (April 1983). The Commission believes this will result in a fair and reasonable treatment of both the utility and the consumer. In the last CP&L rate case, the Commission allowed that portion of the unamortized balance in Harris Units No. 3 and 4 that was supported by a long-term debt to be included in rate base. Based upon the examination of the issue, the Commission believes it more fair and reasonable to exclude this element from the rate base. Similarly, the Commission has excluded from the rate base herein the unamortized balance of the Company's investment in the South River Project and the Brunswick cooling towers.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 10

Company witness Watson and Public Staff witness Carter presented testimony concerning the cost of coal produced by Leslie Coal Mining Company (Leslie) and McInnes Coal Mining Company (McInnes), and the appropriate fair market value of such coal. Leslie and McInnes are affiliated companies of CP&L, by virtue of the fact that CP&L owns 80% of the common stock of these coal companies. The remaining 20% of the common stock of Leslie and McInnes is owned by Pickands and Mather & Company (Pickands Mather).

Company witness Watson asserted that charges including transportation costs for coal delivered to the CP&L system from Leslie and McInnes have been determined in accordance with the Commission Order in Docket No. E-2, Sub 233, which approved the Company's participation in the mining venture and specified the coal-pricing mechanism for regulatory purposes. Witness Watson testified that the "fair market value" for the coal was determined as specified in Exhibit E (the Coal Purchase agreement between CP&L and Leslie) of CP&L's application in Docket No. E-2, Sub 233, which states that "fair market value" shall mean the market price at the time of delivery of coal of the same or comparable grade and quality being sold by a manager on the open market at arm's length in bona fide transactions. (The term "manager" under the definition which was contained in the various agreements submitted for Commission approval in early 1974 in Docket No. E-2, Sub 233, refers to Robert Coal Company, a wholly owned subsidiary of Pickands Mather.) Witness Watson testified that Pickands Mather has periodically provided CP&L with its opinion of the "fair market value" of the Leslie and McInnes coal in accordance with the language contained in Exhibit E. Witness Watson further testified that CP&L has continually monitored the "fair market value" amount provided to CP&L by Pickands Mather by comparing such data to information contained in FERC Form 423 concerning the delivered cost of coal of comparable grade and quality to Leslie and McInnes coal. Witness Watson further testified that the delivered cost of the coal from Leslie and McInnes, using the "fair market value" provided to CP&L by Pickands Mather has always been less than the delivered cost of comparable quality coal shown in FERC Form 423. Further witness Watson stated that the FERC Form 423 "fair market value" amounts have been included in exhibits filed by the Company in previous rate cases and fuel clause proceedings. According to witness Watson, the Commission has in prior proceedings established rates based upon coal costs reflecting the fair market value of the Leslie and McInnes coal as submitted by CP&L. Finally, witness Watson testified that operations at the Leslie and McInnes mines were suspended in mid-February of 1983, due to economic considerations. Witness Watson testified that at the time of the hearing the affiliated coal mining operations continue to be suspended.

Public Staff witness Carter testified that CP&L's methodology for determining fair market value does not in his opinion comply with the Commission's intent in its Order in Docket No. E-2, Sub 233. Witness Carter testified that it is his understanding and belief that the term "fair market value," as is used in the Commission Order in Docket No. E-2, Sub 233, means the price which CP&L is paying for coal of the same or comparable grade and quality which it is purchasing at arm's length from nonaffiliated long-term contract suppliers. Witness Carter stated that the Public Staff's position is based upon the language contained in conclusion (g) and the last paragraph of the Order in Docket No. E-2, Sub 233, which states in part that:

"CP&L is being put on notice that the Seller's cost of producing its coal under these referenced agreements must be closely monitored by CP&L and should they get out of line to the point that coal being supplied CP&L under these agreements is substantially higher than the fair market value of coal of the same or comparable grade and quality being purchased from non-affiliated other sources the excess cost would be disallowed for ratemaking purposes." (Emphasis added), and

"Carolina Power & Light Company is also required to include as a part of the report its own comparative analysis of the price of the coal purchased from Leslie Coal Mining Company to that coal it has purchased during the same report period from its other non-affiliated sources." (Emphasis added)

Witness Carter further testified that the language in the Order requires that reports be submitted by CP&L to the Commission reflecting prices which CP&L is paying for coal purchased from CP&L's nonaffiliated sources and that the Commission does not require CP&L to submit any reports or information concerning the prices which CP&L, or any parties other than CP&L, are paying for coal purchased from U. S. Bureau of Mines, District 8.

Witness Carter also testified as follows:

"In my opinion, if the Commission had intended for CP&L to determine "fair market value" from what either CP&L or other parties were paying for coal purchased from U. S. Bureau of Mines, District 8, the Commission would have required CP&L to submit reports concerning those prices. However, as the order reflects, no such reports are required. Reports reflecting prices which CP&L was paying for coal purchased from its non-affiliated suppliers were required. That fact leads me to the conclusion that the Commission clearly intended for CP&L to determine "fair market value" based on prices it is paying non-affiliated suppliers for comparable quality coal."

Witness Carter testified that CP&L has four nonaffiliated long-term contracts with quality requirements comparable to the quality requirements (similar sulfur content, BTU/LB, ash, and moisture content) of the Leslie and McInnes contracts. The highest cost paid for coal of similar sulfur content, BTU/LB, ash, and moisture content purchased from nonaffiliated long-term contract suppliers is according to witness Carter considerably less than the "fair market value" booked by CP&L.

CP&L has been recording the difference between the production cost of Leslie and McInnes coal and the "fair market value" of that coal, determined by CP&L, in a deferred account. The deferred account which reflects the excess of cost over fair market value has been understated in witness Carter's opinion due to the Company's method of determining fair market value. According to witness Carter's original testimony, the use of a fair market value, which equates to the price of CP&L's highest nonaffiliated long-term contract with quality requirements comparable to the Leslie and McInnes contracts, would have resulted in a decrease in coal costs of $13,065,581, on a total company basis, and $8,250,707 for North Carolina retail operations in the Company's fuel expenses. Such amounts were computed for the time period January 1979 through April 1983. Based on revised data from CP&L, witness Carter modified the aforementioned amounts to $10,329,720 on a total company basis and to $6,519,808 on a North Carolina retail basis. Based on the foregoing, witness Carter recommended that the Commission reduce CP&L's operating revenue deductions by the $6,519,808 to recognize previous charges in excess of fair market value. It was witness Carter's recommendation that the Company's cost of service be reduced by $6,519,808 in this proceeding and that the adjustment be made separate from any adjustment to fuel expense.

Witness Carter stated that his recommendation in this regard is consistent with the methodology used by the Commission in the recent Duke Power Company (Duke) rate case, Docket No. E-7, Sub 338, to eliminate the excess of cost over market value of coal purchased by Duke from its affiliated coal mines. In witness Carter's opinion his recommendation is a very reasonable and conservative interpretation of the language which appears in the Commission Order in Docket No. E-2, Sub 233, since he proposes using the <u>highest</u> price of comparable quality nonaffiliated long-term contract coal rather than the average price of all comparable non-affiliated long-term contract coal. Further, witness Carter believes that the recommended adjustment does not constitute retroactive ratemaking since the Company's departure from the Commission's ordered methodology of determining "fair market value" was an error which must be corrected to comply with the Commission Order in Docket No. E-2, Sub 233.

The Commission has carefully reviewed all the evidence in this regard, including the Commission Order in Docket No. E-2, Sub 233, the testimony and exhibits presented on the production costs and "fair market value" of Leslie and McInnes coal filed and presented in previous rate case and fuel clause proceedings, as well as the Commission Order in Docket No. E-2, Sub 391, which authorized the establishment of a deferred account to record differences between production cost and fair market value of Leslie and McInnes coal. The Commission concludes that CP&L has not determined "fair market value" of the Leslie and McInnes coal as required by the Order in Docket No. E-2, Sub 233, and consequently, has overcharged the ratepayers for the coal the Company has received from Leslie and McInnes. Although the term "fair market value" appears throughout the Order in Docket No. E-2, Sub 233, it is never specifically defined. It is the Commission's opinion that the term "fair market value" as used in the Order means the price which CP&L is paying for coal of the same or comparable grade and quality which it is purchasing at arm's length from its nonaffiliated long-term contract suppliers. This is strongly suggested by the language contained in conclusion (g) and the last paragraph of the Order in Docket No. E-2, Sub 233.

Based on the foregoing, the Commission concludes that operating revenue deductions should be reduced by $6,519,808 in this proceeding. This is the amount by which CP&L, through a mistaken interpretation of the prior, final Orders of this Commission issued in Docket Nos. E-2, Sub 233, and E-2, Sub 391, has overcharged its North Carolina retail ratepayers for coal purchased from its affiliated coal mines. Such amount is calculated based on the methodology described by Public Staff witness Carter in his prefiled testimony using the difference between the average annual cost of coal per ton received by CP&L under its highest nonaffiliated contract coal supplier and the average annual "fair market value" per ton used by CP&L to charge the Leslie and McInnes coal to fuel inventory and fuel expense.

The Commission recognizes that the mining operations at the Leslie and McInnes coal mines are currently suspended. However, should the mining operations at these mines be resumed in the future, the Commission concludes that the fair market value of coal purchased from these mines by CP&L shall be determined based on the highest price which CP&L pays for coal of comparable grade and quality purchased from a currently existing nonaffiliated long-term contract supplier. Work papers showing a calculation of the amount added to or deducted from the nonearning reserve established as a result of the Commission Order in Docket No. E-2, Sub 391, shall be filed with the Commission on a monthly basis.

EVIDENCE AND CONCLUSIONS FOR OF FINDING OF FACT NO. 11

The evidence for this finding of fact is found in the testimony and exhibits of Public Staff witnesses Thomas S. Lam and Caroline M. Smith and Company witness Lynn Eury.

In CP&L's last general rate case, Docket No. E-2, Sub 444, the Commission issued an Order on September 24, 1982, that found that:

> "CP&L's nuclear performance has been declining since 1978 and the Company's Brunswick Nuclear Units have not been available to meet the system load at periods of peak summer usage for the past four summers. Such nuclear performance is clearly unsatisfactory and is related to mismanagement with respect to outage planning, preventive maintenance, spare parts and inventory and control, and quality control and assurance."

The Commission further stated in that Order:

> "The Commission strongly believes that the sooner Company management faces up to inefficiencies and problems in its own nuclear program, the sooner nuclear production will improve. Specifically, the Commission concludes that the rate of return allowed in this docket should provide an incentive for the Company to do better. To that end, the Commission concludes that a rate of return penalty is appropriate in this case . . ."

The Commission imposed a rate of return penalty of 1% in its Order of September 24, 1982.

In the present case, witness Lam testified that 78 days of outages at the Brunswick nuclear site, 43 days at Unit 1, and 35 days at Unit 2, were

avoidable. Unit 1 was shut down on June 28, 1982, because of undervoltage relays. The Unit returned to service on June 29, 1982; however, the Company's post-shutdown evaluation indicated that the undervoltage relays on the emergency electrical distribution systems had not been tested as required by the Technical Specifications which are part of the plant's license from the NRC. The Company assured the NRC that it would review all Technical Specifications surveillance requirements to insure plant safety. The review revealed three additional surveillances that were not being performed. The four surveillance requirements involved were the following:

1. Periodic checks, tests, and calibrations of the emergency electrical distribution system undervoltage relays. This system insures that the nuclear reactor does not run unless there is sufficient back-up power to operate the emergency core cooling system. Channel checks are to be performed every eight hours, channel function tests once each month, and channel calibrations once each 18 months. The tests, checks, and calibrations had not been performed at either unit for two years.

2. Visual inspection of containment penetration to insure that radioactive contaminants do not escape. These inspections are required every 31 days. The inspections had not been performed at either unit for 55 months.

3. Check of operability of reactor water cleanup system isolation instrumentation. The standby liquid control system dumps a boran solution into the water cooling the reactor core when there is no other way to slow the nuclear reaction, and the reactor water cleanup system must be separated at that time so that it does not remove the boran. The check should be performed every 18 months. The check had never been performed at either of the Brunswick units until July 1982.

4. Tests for leaks in the transversing in-core probe guide tube isolation valve and electrical penetrations of the containment vessel to insure against leaks of radioactive contaminants. The valves should be tested for leaks every 24 months. They had not been tested for 39 months and the electrical penetrations had not been tested for 29 months.

After the Company discovered that these surveillance requirements were not being met, the NRC issued a Confirmation of Action letter outlining the work that CP&L was to complete before the Brunswick units could return to service. Witness Lam concluded that 43 days of outages at Brunswick Unit 1 were avoidable since these were the days that the unit was out while the Technical Specifications were being reviewed for compliance. For Brunswick Unit 2, 35 days of outages could have been avoided if surveillance tests had been carried out in a proper and timely manner in compliance with the plant's operating license from the NRC.

The NRC fined CP&L $600,000 for the violations described above. On February 12, 1983, the NRC sent a letter to CP&L proposing the fine in which it stated, "The cause of these violations appears to be a breakdown in corporate and facility management controls in the areas of corporate oversight, facility management and operations and problem identification and

correction." In its May 2, 1983, Response to Notice of Violation and proposed imposition of civil penalties, CP&L admitted the violations and stated, in part:

> "The reasons for the violations can be contributed to procedures and administrative controls that have become difficult to implement and unduly burdensome as a result of numerous amendments and modifications to plant systems and applicable regulatory requirements. Personnel errors, which were the cause of the violations, were not detected by administrative controls in place."

The NRC has otherwise expressed concern with management at the Brunswick nuclear site. In its evaluation of the Company's performance for the period January 1, 1982, through January 31, 1983, the NRC stated in its Systematic Assessment of Licensee Performance dated June 14, 1983, the following:

> "Poorly stated or ill-understood procedures, identified the previous review period, continued to degrade the effectiveness of the operating staff and contributed to the substantial numbers of the reported personnel errors. Inadequate management involvement, indicated by a demonstrated laxness in discipline of operations and adherence to procedures, also had an adverse effect on operation's performance. These weaknesses were key elements in each of the violations identified below, in the civil penalties issued in June 1982 and February 1983, and in the 65 Licensee Event Reports (LER) attributable to personnel error that were issued during this review period. NRC concerns in the area of management and supervisory controls were discussed at each of five enforcement conferences held during this review period. A procedure upgrade program, renewed emphasis on discipline of operations and adherence to procedures are commitments contained in the licensee's long-range improvement program, confirmed by NRC Order on December 22, 1982."

In September 1982, CP&L made certain changes with respect to the management of the Brunswick nuclear units. All operating and maintenance, engineering, and construction activities for the plant were consolidated under the control of the Vice President of Brunswick Nuclear Project who reports directly to the Executive Vice President of Operations, Engineering, and Construction. Witness Eury testified that this reorganization was undertaken in order to increase senior management oversight of the Brunswick nuclear plant; to improve communications and coordination by consolidating operations, engineering, and construction; to insure sufficient and timely support to the plant to meet engineering and construction requirements; and to improve organizational accountability and strengthen management control. He further stated that these initiatives have resulted in certain operational efficiencies at the nuclear plant; however, the Commission finds that Brunswick's capacity factor remains unsatisfactorily low.

While the Commission recognizes that a recognized national management consulting firm recently judged CP&L to be "in many respects... one of the best-managed utilities that we have audited in the past several years" and while the Commission recognizes that CP&L has undertaken reorganization of the management of the Brunswick nuclear units in an effort to solve their problems there, the Commission nonetheless finds that a rate of return penalty should be continued. A penalty is being continued because the management problems at

the Brunswick nuclear units continued to have adverse consequences on nuclear performance, such as the 78-day outage and low capacity factors, during the present test year. CP&L has now undertaken steps to eliminate the problem, but the consequences of the problem in the test year cannot be discounted. The amount of the penalty will be discussed in a later section of this Order.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 12

Company witness Nevil, Public Staff witness Nightingale, and Attorney General witness Rosen provided testimony and exhibits regarding the use of a normalized generation mix in determining fuel costs for this proceeding.

The Company contended in the previous general rate proceeding that the proper way to determine the base fuel component in the rates is by using actual test year fuel costs adjusted for known and measurable changes in kWh usage and in unit fuel prices. In this proceeding, the Company contends that the proper way to determine the base fuel component in the rates is by using a normalized generation mix (based on the Company's own historical operating experiences and adjusted for known changes in kWh usage and unit fuel prices) plus an "experience factor." Under cross-examination, witness Nevil recommended that the actual test year fuel costs be utilized if the "experience factor" is not adopted by the Commission.

The Public Staff contends that the proper method to determine the base fuel cost for general rate case proceedings is by using a normalized generation mix (based on national averages for the nuclear plant operations and adjusted for known and measurable changes in system usage and in unit fuel prices). Witness Nightingale testified that the use of a normalized generation mix for calculating fuel costs would result in periods when the Company would over-recover its actual fuel expenses and in periods when the Company would under-recover its actual fuel expenses.

Witness Rosen testified that a normalized generation mix (based on national averages for operating experience) would be desirable so that reasonable target levels of technical and economic performance could be reflected by the base fuel component in the rates. Kudzu witness Eddleman and DOD witness McCabe also supported the use of a normalized generation mix.

The Commission concludes, as it did in the previous general rate proceeding in Docket No. E-2, Sub 444, that the general concept of utilizing a normalized test period generation mix is appropriate for establishing the base fuel component in the rates.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 13

Company witnesses Nevil and Futrell, Public Staff witness Nightingale, Attorney General witness Rosen, Department of Defense (DOD) witness McCabe, and Kudzu witness Eddleman presented testimony and evidence regarding the appropriate base fuel component in the rates.

In his original prefiled testimony, Company witness Nevil proposed a base fuel component of 1.867¢ per kWh based on actual test year generation mix (as adjusted for weather, customer growth, the addition of Mayo No. 1, and the additional load portion of NCEMPA). The actual test year nuclear capacity factor for all units averaged 39.5%. For the calendar years 1980, 1981, and

1982, the average nuclear capacity factor, taken over the three-year period, was 43.98%.

Witness Nevil testified that the Company projects its actual fuel costs to be 1.838¢ per kWh for the period during which the rates established herein are expected to be in effect. This estimate gives consideration to other Company witnesses' testimony that the steam generator at the Robinson nuclear unit must be replaced and that the Company has planned a nine-month outage of the unit beginning in March 1984.

In his supplemental prefiled testimony, witness Nevil proposed a base fuel component of 1.818¢ per kWh based on a normalized generation mix plus an "experience factor." He stated that the actual test period generation mix should be utilized unless the "experience factor" is adopted. In calculating his normalized generation mix to use with his experience factor, witness Nevil utilized a computerized production simulation model (PROMOD) to recreate the test year generation mix which would have occurred if the test year were adjusted to reflect: weather normalization, customer growth, addition of Mayo No. 1, additional load portion of NCEMPA, the lifetime average capacity factor of each of the Company's nuclear units, the five-year average equivalent availability of each of the Company's fossil steam units, the average hydro generation over the last 22 years, and purchased power and IC turbine generation "at levels which maintained reasonable levels of supply from both sources." His normalization of the nuclear generation, using each plant's historical average generation, resulted in a total nuclear capacity factor of approximately 52%.

To determine the portion of net fuel costs associated with NCEMPA, the Company utilized its own computer model (ECAP) to determine the kWhs and fuel costs to be charged to Power Agency under each of the five supply and pricing classifications contained in the agreement with Power Agency.

Witness Nevil utilized March 1983 unit fuel prices to compute a total Company fuel cost (subject to fuel charge adjustments) of $429,299,900. He then multiplied the fuel cost by his proposed "experience factor" of 1.1588 to obtain a requested fuel cost of $497,472,700 total Company (or $342,140,000 for North Carolina retail service) yielding a base fuel component of 1.818¢ per kWh excluding gross receipts tax.

The "experience factor" was presented to the entire Commission in Docket No. E-100, Sub 47, concerning fuel charge adjustments, and the Commission has not yet made a determination in that proceeding. The "experience factor" is computed based on the ratio of three years actual fuel costs per kWh to three years estimated fuel costs per kWh (utilizing any specific estimating methodology), and is intended to compensate for estimating errors. The Company multiplied the 1.569¢ per kWh base fuel component it estimated in this proceeding (based on its historic normalization methodology) by the 1.1588 "experience factor" it calculated (based on actual and estimated fuel costs for 1980, 1981 & 1982), to derive its recommended 1.818¢ per kWh base fuel component.

Public Staff witness Nightingale recommended that the base fuel component be derived by a methodology which does not involve the use of a complex computer program. His analysis normalizes the generation mix by: utilizing the 10-year average capacity factor for each type of nuclear plant as reported

by the National Electric Reliability Council (NERC), Ten Year Review - Report on Equipment Availability (1972-1981); setting hydro generation equal to the median reported in the Company's most recent Power System Statement (Form 12); and prorating the remaining fossil fuel generation and outside purchases and sales in proportion to their actual test period generation mix. His normalization of the nuclear generation, utilizing national averages, resulted in a total nuclear capacity factor of approximately 57%.

Witness Nightingale utilized March 1983 unit fuel prices to compute a total Company fuel cost (subject to fuel charge adjustments) of $412,515,200, or $283,709,700 for North Carolina retail service, yielding a base fuel component of 1.508¢ per kWh excluding gross receipts tax. DOD witness McCabe also accepted the Public Staff's position on fuel expenses.

Attorney General witness Rosen advocated the determination of nuclear capacity factors by means of a regression analysis equation developed by his Company, Energy Systems Research Group (ESRG). Witness Rosen selected several characteristics of a nuclear unit and he utilized data from the national data base concerning those characteristics, and he performed a multiple regression analysis of the data to determine an appropriate capacity factor for each individual nuclear unit. He testified that the average normal Maximum Dependable Capacity factor for Brunswick No. 1, Brunswick No. 2, and Robinson No. 2 should be 60%, 63% and 73%, respectively, resulting in a total nuclear capacity factor of approximately 65% for the Company. Witness Rosen took no account of the actual experience factor for the CP&L units except to include them in his national average statistics.

Kudzu witness Eddleman computed a range for the base fuel component by simply assuming a 60% nuclear capacity factor (NCUC Rule R8-46, level for signaling a need for examination of outage problems) and a 70% nuclear capacity factor (design level). His procedure yielded a base fuel component of 1.312¢ per kWh to 1.429¢ per kWh (reflecting the 70% to 60% capacity factors, respectively).

The Commission is of the opinion that the "experience factor" proposed by the Company should not be adopted for this proceeding in order to reserve judgment regarding use of the "experience factor" for the entire Commission in Docket No. E-100, Sub 47. The Commission also concludes that the 1.838¢ projected cost figure as testified to by the Company as well as the estimates made by the Public Staff and intervenors using national average nuclear capacity figures are not representative of CP&L's actual situation. The Commission concludes that a more representative nuclear capacity factor would be 41.74% - an average of the actual test year experience and the last three calendar years. By averaging these factors, we arrive at a slightly higher test year capacity factor than that experienced, but one that hopefully will begin to reflect an improving trend of operations for the Company. The matter of nuclear operations is dealt with further in our discussion of the imposition of a penalty on the Company. Given the evidence presented in this case, we do not anticipate the Company beginning to approach national average capacity factors in the next 12 to 18 months.

Using the above nuclear capacity factor and normalized fossil fuel, hydro, and purchased power costs, the Commission arrives at a 1.677¢ per kWh base fuel cost component.

In evaluating the 1.677¢ per kWh base fuel component adopted herein, the Commission has carefully considered each element in the generation mix, including generation by nuclear fuel, fossil fuels and hydro, and including intersystem purchases and sales. The contribution by each element of the generation mix which was utilized to produce the 1.677¢ per kWh base fuel component is judged to be just and reasonable.

In setting the base fuel component of CP&L's rates in this case, the Commission has established a reasonable normalized level of fuel expenses which it anticipates to occur during the period of time the rates set herein are expected to be in effect.

However, no matter what fuel factor the Commission might find as a fact to be appropriate as reflective of a normalized test year, there are numerous uncertainties, many of which are outside the control of either CP&L or this Commission (e.g., changes in demand and hence costs resulting from weather variations or in economic conditions; NRC decisions on the operation or non-operations of CP&L's nuclear units; changes in fuel prices, etc.), that could cause whatever fuel factor chosen to be in error. This likelihood of error in the fuel factor, regardless of any evidence that could be ascertained in a general rate case or fuel clause procedure, gives the Commission concern because of the large portion of total expenses attributable to fuel costs for electric utilities. For the test year in this case, CP&L expenses $350,922,000 for fuel out of a total O & M expense of $617,238,000; i.e., fuel expenses accounted for 56.85%. As a result, small deviations from a fuel factor can cause enormous swings in earnings of an electric utility such as CP&L.

This State, through its General Assembly, recognized this problem and enacted special legislation for fuel charge adjustment proceedings in 1975. A major revision to the law was passed in June of 1982, G.S. 62-133.2. Given the wide differences in interpretations of the new law, no consensus could be reached as to a set of rules for the practical implementation of G. S. 62-133.2. The Commission has held lengthy evidentiary hearings, and, most recently, has heard oral arguments on the matter of establishing rules for the implementation of the statute. Further public hearings have been scheduled in February on the matter of a report to the General Assembly on the statute. Due to its heavy rate case hearing schedule, which must by law take precedence over all other matters, the Commission has not yet had sufficient time to establish rules for implementing G. S. 62-133.2. The lack of rules troubles this panel since we cannot be sure that sufficient recourse will be available under G. S. 62-133.2 for adjusting for large overcollections or undercollections by CP&L that may result from the fuel factor set herein.

Since minor changes in the normalized test year generation mix and resulting changes in fuel costs can cause overcollections or undercollections of tens of millions of dollars, and in light of CP&L's erratic nuclear operational experience and the absence of Commission rules for implementing G.S. 62-133.2, the panel is reluctant to set a fuel factor without providing some explicit protection for the ratepayers. Therefore, the Commission finds that the 1.677¢ per kWh fuel factor should be considered provisional in the sense that it may be reduced if actual experience demonstrates that it has been set too high, but fixed if actual reasonable fuel costs equal or exceed it. By the Commission taking this approach, CP&L has the burden, and properly so, to maintain its fuel costs at or below the level found to be reasonable

herein. If it is unable to do so, it will have the burden of attempting to institute a proceeding under G. S. 62-133.2, even in the absence of Commission rules, to recover its additional reasonable fuel costs. However, the Commission is not willing to place such a burden on CP&L's customers or their representatives. Accordingly, the Commission directs CP&L to establish a deferred fuel expense account and place any net overcollections in it. The Commission will review the Company's actual fuel costs in its next general rate case or in a G. S. 62-133.2 proceeding and will requferred account shall be reported to the Commission no later than one year from the date of this Order or 30 days prior to the beginning of the hearings in CP&L's next general rate case. The status of this account is to be made available to the Public Staff at any time.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 14

The evidence for this finding is found in the testimony and exhibits of Company witnesses Watson and Nevil and Public Staff witnesses Carrere and Winters.

Company witness Watson recommended a system coal inventory, as further adjusted by Company witness Nevil to exclude Power Agency ownership, of 2,104,956 tons. Public Staff witness Carrere recommended a system coal inventory level of 1,593,516 tons. Both parties relied upon the maximum drawdown method, variations of which have been utilized by the Public Staff and/or the Company in previous rate cases and have been adopted by the Commission in Docket Nos. E-2, Subs 391, 416, and 444.

The Company used the 110-day period from December 6, 1977, to March 26, 1978, having a maximum drawdown of 1,260,000 tons in its coal inventory. The 110-day period utilized by the Company represents the longest period during which coal deliveries were interrupted by a coal strike.

The Public Staff used the 130-day period from March 29, 1981, to August 2, 1981, having a maximum drawdown of 1,399,528 tons in the Company's coal inventory. The 130-day period utilized by the Public Staff included a 76-day U.M.W.A. miners strike followed by 54 days of miners' vacation. The 130-day period represents the longest period during which coal deliveries were interrupted by a coal strike or otherwise.

The Company translated the 1,260,000 tons drawdown during the 110-day period to current levels by means of daily burn rates for coal. The Company utilized 16,326 tons per day to represent the daily burn rate during the 110-day period, and it utilized 27,274 tons per day to represent the current daily burn rate. Multiplying the 1,260,000 ton drawdown by the ratio of 27,274 tons/day to 16,326 tons/day yields the 2,104,956-ton coal inventory recommended by the Company.

The Public Staff translated the 1,399,528 ton drawdown during the 130-day period to current levels by means of coal-fired generating capacity. The Public Staff utilized the 4,473 mW coal generating capacity available during the 130-day period and the current coal generating capacity of 5,093 mW including Mayo. Multiplying the 1,399,528 ton drawdown by the ratio of 5,093 mW to 4,473 mW yields the 1,593,516 ton coal inventory recommended by the Public Staff.

At the March 1983 coal inventory price of $48 per ton, the Company's requested 2,104,956-ton coal inventory represents an investment of $101,037,888 total Company (or $69,489,429 for North Carolina retail service). At the same prices, the Public Staff's recommended 1,593,516-ton coal inventory represents an investment of $76,488,768 total Company (or $52,605,624 for North Carolina retail service). DOD witness McCabe supported the Public Staff position.

Witness Carrere contended that daily burn rates can be highly volatile due to changes in system generation mix, availability of alternative fuels or sources of supply, and fluctuations in system load. The Commission is of the opinion that actual daily burn rates must be considered in establishing the proper level of coal inventory for the system, even though said daily burn rates tend to be unstable from month to month. The Commission observes that neither the Company nor any other party to this proceeding attempted to normalize the daily burn rates utilized in the calculations.

The Commission concludes that the coal inventory requested by the Company, representing an investment of $69,489,429 for North Carolina retail service, is appropriate for this proceeding.

Company witness Watson requested a total liquid fuels inventory, as adjusted by Company witness Nevil to exclude Power Agency ownership of $9,461,848 total Company (or $6,507,444 for North Carolina retail service). The inventory would consist of 9,413,000 gallons of No. 2 oil at 86.14¢ per gallon, plus 2,365,000 gallons of propane at 57.23¢ per gallon. The 9,413,000 gallons of No. 2 oil represents a maximum two-month drawdown during 1977-78.

Public Staff witness Carrere recommended a No. 2 oil inventory of $6,408,988 total Company (or $4,407,821 for North Carolina retail service). The inventory would consist of 7,440,200 gallons of No. 2 oil at 86.14¢ per gallon representing a one-year supply at 1979 daily burn rate levels. The currently allowed oil inventory was established in 1979.

In the prior rate proceeding in Docket No. E-2, Sub 444, the Commission allowed a 23,000,000-gallon oil inventory. The actual oil inventory at the end of the test period in this proceeding was 14,448,144 gallons. The Commission concludes that the No. 2 oil inventory requested by the Company, representing an investment of $8,108,358 total Company (or $5,576,573 for North Carolina retail service) is appropriate for this proceeding.

The Commission further concludes that a $76,079,959 working capital allowance for fuel inventory is appropriate for North Carolina retail service in this proceeding, consisting of the $69,489,429 coal inventory, the $6,507,444 liquid fuel inventory, and $83,086 miscellaneous fuel stock.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 15

Company witnesses Bradshaw, Faucette, Watson, Nevil, and McClellan and Public Staff witnesses Winters and Carrere offered testimony regarding the reasonable working capital allowance. The following chart summarizes the North Carolina retail amounts the Company and Public Staff contend are the proper levels of the components of CP&L's working capital allowance to be used in this proceeding:

(000's Omitted)

Item	Company	Public Staff
Cash	$ 3,467	$ 3,467
Materials and supplies - fuel stock	76,080	57,896
Materials and supplies - other	19,991	19,991
Prepayments	6,594	6,594
Investor funds advanced for operations	32,567	17,413
Miscellaneous projects	9,921	4,943
Other rate base deductions	(8,187)	(6,626)
Customers deposits	(5,898)	(5,898)
Total allowance for working capital	$134,535	$97,780

The parties are in disagreement over the proper amount of materials and supplies - fuel stock, investor funds advanced for operations, miscellaneous projects, and other rate base deductions. The Commission will now analyze the testimony regarding these differences.

The first difference between the parties is the level of materials and supplies - fuel stock recommended for use in this proceeding. This difference of $18,184,000 is discussed in the Evidence and Conclusions for Finding of Fact No. 14. Consistent with the determinations made by the Commission in Finding of Fact No. 14 regarding this issue, materials and supplies--fuel stock of $76,080,000 is included as the reasonable level of fuel stock to be included in the working capital allowance in this proceeding.

The next difference between the parties is the level of investor funds advanced for operations recommended for use in this proceeding. The $15,154,000 difference between the amounts proposed by the Company and Public Staff results from the adjusted versus per books lead-lag study, the treatment of federal income tax lag differences and the treatment of average employee and use taxes held.

The first issue the Commission must resolve is whether to use the lead-lag study adjusted for pro forma adjustments and the proposed rate increase as recommended by the Company or the per books lead-lag study as recommended by the Public Staff. The Public Staff contends that the per books lead-lag study, adjusted to reflect 100% of the closings related to the Power Agency sale and the removal of the Leslie and McInnes coal mine loss from the cost of service, provides a reasonable level of investor-supplied funds before reduction for any incidental collections. Public Staff witness Winters testified as follows regarding the use of the per books study of average employee and use taxes held.

> "The Commission, in Docket Nos. E-2, Sub 444, 416, and 391, CP&L's last three general rate cases, has ruled, `...a lead-lag study, applied to the per books amounts of cost of service, is the more reasonable approach to use in determining the investor funds advanced for operations.' The Commission has also ruled in Docket No. G-5, Sub 157, a general rate case involving Public Service Gas Company, that `...a lead-lag study applied to the per books cost of service results in a fair and reasonable analysis of the subject company's cash working capital needs.' I believe the per books computation provides a reasonable representation of investor funds because it is based upon the Company's actual experience for the test-year."

Company witness McClellen presented rebuttal testimony and contended that accounting and pro forma adjustments should be considered, because the end-of-period level of revenues and expenses adjusted for the proposed increase more nearly reflects the cost of service for the period in which the rates will be in effect. Witness McClellen also criticized the Public Staff for adjusting the per books cost of service to reflect 100% closings for the Power Agency sale and to eliminate the Leslie and McInnes coal mining losses.

Public Staff witness Winters testified that the adjustments to the per books study proposed by the Public Staff increased working capital by approximately $500,000 and that if the working allowance had been calculated based upon the Public Staff's cost of service after proposed rates, the working capital allowance would have been substantially the same.

The Commission has evaluated and reviewed the results of the Company's end-of-period lead-lag study and finds that the results of the study are inappropriate. The main problem area of CP&L's end-of-period lead-lag study is its classification of federal income taxes. As can be seen by examining McClellan Rebuttal Exhibit No. 2, line 34, columns (f) and (h), CP&L has assigned 90% of the income taxes associated with the proposed rate increase to investment tax credits. This is inappropriate since no adjustment has been made to adjust deferred income taxes to an end-of-period basis. The difference between end-of-period book depreciation expense and end-of-period income tax depreciation expense has not been determined. If this were done, deferred income taxes would increase and both investment tax credits and current income taxes would decrease. Also, if deferred income taxes were increased, it would not be appropriate to assign zero lag days to the increased amount unless the increased amount of deferred income taxes were deducted from rate base.

In addition, CP&L's treatment has the effect of recognizing a level of investment tax credits which have not been utilized and which will in all probability not be recognized in the future. The additional level of investment tax credits based on 90% of federal income taxes associated with the proposed rate increase will probably not be recognized in the future because of the increased level of deferred income taxes which is likely to be recognized in the future. Based on a certain level of federal income tax expense, the higher the level of deferred tax expense the lower the level of investment tax credits utilized. The Company's level of deferred income taxes as well as its level of interest expense, both operating interest expense and nonoperating interest expense, continue to increase. All these items will contribute to the likelihoood that CP&L's level of investment tax credits in the coming year will be less than the $92,644,000 adjusted amount as shown of McClellan Rebuttal Exhibit No. 2. This seems especially likely since investment tax credits of only $30,234,000 were utilized during the test year. Based on the likelihood that in the coming year the level of investment tax credits will be less than the end-of-period level indicated by CP&L, and the like likelihood that deferred income taxes will be greater than the end-of-period level indicated by CP&L, the Commission concludes that the per books level of income tax expense, as well as all other per books components of cost of service, with the exception of the adjustments for Leslie and McInnes coal mine losses and 100% Power Agency closing, is the appropriate level to use in determining investor funds advanced for operations.

The Commission finds witness Winters' adjustments to the per books lead-lag study of the 100% Power Agency closing and the cumulative write-off of the Leslie and McInnes coal mine losses appropriate. The adjustment for the 100% Power Agency closing represents a permanent change in operations which did not exist during the test year, but which will exist continuously from the final closing. In the Commission's opinion, the adjustment to remove the effect of Leslie and McInnes coal mine losses incurred since 1979 and written-off during the test year is appropriate because these losses are nonrecurring and it is not anticipated that losses of this magnitude will be incurred in the future. The Commission, therefore, finds that the per books method viewed in its entirety produces a reasonable level of working capital. The Commission concludes that the preponderance of the evidence in this case indicates that a lead-lag study applied to the per books cost of service, adjusted only for abnormal events, results in a fair and reasonable analysis of the Company's cash working capital needs.

The next item which the Commission must decide regarding investor funds advanced for operations is the proper federal income tax lag to be used in this proceeding. The Company proposed a 38-day lag based on the assumption that estimated income tax payments would be made in equal quarterly installments. Public Staff witness Winters proposed a 58.45-day lag based on the statutory requirements for filing estimated income tax payments. Witness Winters testified in that regard as follows:

> "I do not believe that the Company should pay its taxes faster than is legally required. Working capital requirements which arise from early payments of income taxes, in my opinion, should not be borne by the ratepayers. After all, the ratepayers have paid in through rates the funds used by the Company to pay those taxes. The Company's election to give those funds to the Federal Government earlier than is legally required diminishes the benefit which the ratepayers should receive from having paid them."

The Commission finds that the working capital calculation based on an early payment of income taxes as proposed by the Company is inappropriate and concludes that the appropriate lag for federal income taxes is 58.45 days.

The final item the Commission must decide regarding investor funds advanced for operations is whether incidental collections should be deducted in the calculation. Public Staff witness Winters deducted $1,296,000 for employee tax withholdings and $273,000 of North Carolina sales and use tax collections. Witness Winters testified in regard to this issue as follows:

> "After determining investor funds advanced for operations by multiplying the average daily cost of service by the net interval between the revenue lag and the expense lag, I have deducted the average amount retained before payment of employee tax withholdings and the North Carolina sales and use tax collections. These employee tax withholdings and sales tax collections represent funds which the Company has collected for later remittance to governmental agencies. Until they are remitted to the governmental agencies the Company has unrestricted use of these funds. They are, therefore, cost-free funds and should be deducted from investor funds advanced for operations in determining the total amount of investor funds which should be included in the working capital allowance."

The Company agrees as to the propriety of treating such deductions as cost-free capital. However the Company classifies these items as other rate base deductions to be discussed hereinafter.

The Commission finds that these incidental collections are in the nature of cost-free capital and are properly used as a reduction in the calculation of investor funds advanced for operations. The Commission further finds and concludes that the appropriate level of investor funds advanced for operations to be used in this proceeding is $17,413,000.

The next difference between the parties is the level of miscellaneous projects to be used in this proceeding. The Company included $4,978,000 in this account for the Brunswick cooling towers and the South River Project. Public Staff witness Winters removed these projects and testified regarding them as follows:

> "I have excluded the unamortized balance of the Brunswick cooling towers and the South River Project losses from the working capital allowance, because, in my opinion, these items are not used and useful in providing electric service. Counsel for the Public Staff has advised me that these abandoned projects do not meet the legal requirements for inclusion in rate base."

The Commission discusses this issue fully in the Evidence and Conclusions for Findings of Fact Nos. 8 and 9. Based on the conclusions reached therein the Commission finds it inappropriate to include the unamortized balance of the Brunswick cooling towers and the South River Project losses in rate base. Thus the Commission concludes that the appropriate level of miscellaneous projects is $4,943,000.

The final difference between the parties is the appropriate level of other rate base deductions. The $1,561,000 difference consists of $1,569,000 relating to differing categorization of average employee and use taxes by the Company and Public Staff. The Commission for purposes of this Order finds it appropriate to treat average employee and use taxes as a reduction in investor funds advanced for operations. The remaining difference relates to an adjustment made by Public Staff witness Winters to include $246,000 in other rate base deductions representing the accrual of an expense which was never paid by the Company. Although the Company agrees that the Public Staff's proposed adjustment is proper, the Company advocates using a production allocation factor to allocate the item to North Carolina retail operations. The Commission finds that it is proper to include this element of cost-free capital in other rate base deductions and that the Company's proposed allocation is proper.

In Evidence and Conclusions for Finding of Fact No. 7, the Commission discusses the treatment of the gain on the sale of property by CP&L to NCEMPA and the treatment of accumulated JDITC related to the sale. Consistent with the decisions made therein, the Commission finds that the unamortized portion of the gain on the sale of $17,105,000 should be included in other rate base deductions. Based upon the foregoing the Commission finds other rate base deductions of $23,722,000 appropriate for use in this proceeding.

The parties are in agreement as to appropriate levels of cash, materials and supplies - other, prepayments, and customer deposits; therefore, the

Commission concludes that the appropriate level of allowance for working capital to be used for setting rates in this proceeding is $98,868,000 as shown in the chart below:

(000's Omitted)

Item	Amount
Cash	$ 3,467
Materials and supplies	96,071
Prepayments	6,594
Investor funds advanced for operations	17,413
Miscellaneous projects	4,943
Other rate base deductions	(23,722)
Customer deposits	(5,898)
Total allowance for working capital	$ 98,868

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 16

Company witnesses Spann, Vander Weide, Bradshaw, and Lilly, Public Staff witness Bright, Attorney General witness Stutz, Department of Defense witness McCabe, and Kudzu Alliance witness Eddleman presented evidence as to the proper level of construction work in progress (CWIP) to be included in rate base. In 1977, North Carolina G.S. 62-133(b)(1) was amended to provide for reasonable and prudent expenditures of CWIP after July 1, 1979, to be included in rate base. Since the effective date of that amendment, the Commission has approved the inclusion of CWIP in CP&L's rate base in four proceedings: NCUC Docket Nos. E-2, Sub 366; E-2, Sub 391; E-2, Sub 416; and E-2, Sub 444.

On June 17, 1982, G.S. 62-133(b)(1) was further amended to provide that reasonable and prudent expenditures for CWIP may be included in rate base to the extent the Commission considers such inclusion to be in the public interest and necessary to the financial stability of the utility involved. The current amount of CWIP included in CP&L's North Carolina retail rate base is $392,199,000. Of this amount, $173,865,000 is attributable to Mayo Unit No. 1 which began commercial operation in March 1983. The remaining amount of $218,334,000 is applicable to Harris Unit No. 1. The Company is requesting in this proceeding that $539,780,749 of CWIP relating to Harris Unit No. 1, net of Power Agency ownership, be included in its North Carolina retail rate base.

As the Commission has noted in previous Orders, the amount of CWIP in rate base determined to be appropriate results from the application of the following criteria: (1) the expenditure must be reasonable and prudent, (2) the inclusion must be in the public interest, and (3) the inclusion must be necessary to the financial stability of the utility in question.

Company witness McDuffie presented evidence indicating that the expenditures made for construction of Harris Unit No. 1 to date have been both reasonable and prudent. Company witness Sherwood Smith testified that the audit of the Company performed at the request of the Commission by the firm of Cresap, McCormick and Paget found that productivity at the Harris site appeared good and that the Company had a sound management approach to the Harris project. Public Staff witness Bright testified that there is no reason to believe expenditures on Harris Unit No. 1 to date have not been reasonable. Attorney General witness Stutz testified on cross-examination that he had no

evidence to offer that the expenditures for Harris Unit No. 1 CWIP were unreasonable.

A number of witnesses offered testimony on the public interest criterion. Company witness Spann presented a quantitative study and testimony that the inclusion of the Company's requested amount of CWIP would benefit ratepayers by minimizing the net present value of revenue requirements through the end of the century. Witness Spann pointed out that although the percentage difference was small, with and without CWIP in rate base, the magnitude of the dollars resulted in a net savings of approximately $350 million. Witness Spann testified that it is less costly on a present value basis to place CWIP in rate base in order to maintain an "A" bond rating than not to place CWIP in rate base and have CP&L's bonds downgraded with a commensurate increase in interest expense. Finally, Dr. Spann testified that inclusion of CWIP in rate base would help to smooth rates and minimize rate shock as new plants go into service.

Company witness Edge testified that 84% of the Company's residential customers and 87% of the Company's commercial and industrial customers have been on the Company's system for over seven years. Consequently, the Company expects that the majority of current Company customers would still be receiving service from the Company in 1986, the expected in-service date of Harris Unit No. 1. Witness Edge also testified that CWIP in rate base provides better pricing signals to consumers and reduces rate shock when a new generating unit is placed in service. Finally, witness Edge testified that assurance of adequate service in the future attracts industry to the area and benefits ratepayers through more and higher paying jobs, broader tax base, and improved economic outlook.

Public Staff witness Bright testified that inclusion of CWIP in rate base could result in lower future rates for ratepayers remaining in the service area, but that, in her opinion, such inclusion is seldom in the public interest due to the involuntary nature of the ratepayers' investment in a utility's construction program. Witness Bright recommended that $309,519,000 of Harris Unit No. 1 CWIP be included in rate base.

Attorney General witness Stutz took the position that CWIP inclusion should be considered in light of the inter-generational equity issue, the used and useful concept, and the relative cost/benefit to ratepayers. Witness Stutz recommended that only $218 million of CWIP for Harris Unit No. 1 be included in rate base.

Department of Defense witness McCabe stated that all CWIP should be excluded from rate base except for that amount previously authorized by the Commission of Harris Unit No. 1. Witness McCabe contended that inclusion of CWIP violated the traditional used and useful concept since customers would be paying for plants not yet in operation. Witness McCabe testified that in his opinion placing CWIP in rate base would not reduce the costs of construction.

Kudzu Alliance witness Eddleman testified that no CWIP should be included in rate base. Witness Eddleman stated that inclusion of CWIP is not cost effective and in reality is a forced loan from consumers to the Company.

The Commission finds that in determining whether the public interest is served, it is appropriate to consider a number of factors. Although the near

term impact on present ratepayers is certainly an important factor, it is not totally dispositive of the issue. When the public interest is viewed in a broader sense, it becomes clear that CWIP in rate base may serve the public interest even if rates will be somewhat higher in the near term.

Evidence introduced in the proceeding has shown the relative importance of the inter-generational equity issue to be slight when the CWIP in question relates to a plant which will go into service in just a few years. Witness Edge's testimony that 84% of residential customers and 87% of the industrial and commercial customers are still receiving service from CP&L after seven years shows that the Commission can reasonably expect the vast majority of present ratepayers to be ratepayers on the system in 1986 when Harris Unit No. 1 goes into service.

In this proceeding, the quantitative evidence presented supports a finding that inclusion of CWIP at the level requested by the Company would result in lower revenue requirements on a net present value basis through the year 2000. This is consistent with the policy of providing power at the lowest cost over the life of the plant. The Commission is also of the opinion that ratepayers would benefit from the smoothing of rate increases to avoid rate shock and from the pricing signals that the Company's requested level of CWIP in rate base can provide. The Commission notes that $582 million of CWIP consisting primarily of pre-1979 construction expenditures on Harris Unit #1 is not included in the rate base. This amount in itself will cause a significant rate shock in 1986 when Harris #1 is completed and placed in rate base. Finally, the Commission finds that the public interest is served by the attraction of new industry through the assurance of adequate service in the future.

In considering the financial stability criterion, the Commission has examined the record with regard to the financial condition of the Company, the impact of CWIP inclusion, and the appropriateness of such inclusion versus some other method of ensuring the financial stability of the Company. Company witness Lilly testified that CP&L's fixed charge coverage at the end of the test year was 1.9 times, and its ratio of AFUDC included in return for common equity was almost 78% at the end of 1982. Witness Lilly further testified that the Company's forecast of construction expenditures from 1983 through 1985 is substantially greater than the industry average. Witness Lilly concluded that these factors contributed to the recent downrating of the Company's bonds and that absent considerable improvement in the Company's financial condition in the near future, another downrating is possible.

Company witness Spann testified that including approximately $500 million of CWIP in North Carolina rate base would result in improving some but not all of CP&L's financial indicators to the levels normally achieved by an average "A" rated utility. Witness Spann also stated the present value of revenue requirements is less if CP&L's cash earnings are improved by placing CWIP in rate base than by granting signficantly higher rates of return than those sought by CP&L in this case.

Public Staff witness Bright supported inclusion of $309,519,000 of CWIP in North Carolina rate base in that such inclusion was necessary to the financial stability of the Company. Ms. Bright stated that the relatively high (60%) ratio of construction to net plant and large amount of AFUDC (78%) as a percent of income created such necessity. Witness Bright stated that this

amount of CWIP would result in the Company receiving a 2.3 times pretax interest coverage ratio excluding AFUDC, a ratio that would be indicative of financial stability.

Attorney General witness Stutz testified that CWIP should be reserved for utilities in dire financial situations, and CP&L did not meet this standard of financial instability. Witness Stutz recommended that only the continued allowance of $218 million of CWIP for Harris Unit No. 1 be authorized.

With regard to the financial stability criteria relating to the inclusion of CWIP in rate base, the Commission has considered a comparison of various financial ratios of CP&L relevant to this issue to similar financial ratios of the 100 electric utilities, reported by Salomon Brothers. The data was obtained from the March 31, 1983, issue of Salomon Brothers Electric Utility Quality Measurements.

Comparison of Various Financial Ratios
(March 31, 1983)

	CP&L	Average of 100 Electric Utilities	Average of 25 A-Rated Electric Utilities
Pretax coverage			
Including AFUDC	2.5	3.0	3.1
Excluding AFUDC	1.9	2.5	2.7
Equity Ratio	38%	40%	40%
AFUDC as a percentage of earnings	78%	49%	37%
Construction as a percentage of gross plant	62%	43%	44%
Internal cash generation	38%	62%	63%

It is obvious to the Commission based on the preceding analysis that the magnitude of CP&L's construction budget is placing the Company in an adverse financial position relative to other electric utilities in the country. Specifically CP&L's percentage of construction to gross plant is 62% as compared to 43% for the 100 electric utilities and 44% for the 25 "A" rated electric utilities. Similarly AFUDC as a percentage of earnings of 78% for CP&L materially exceeds the average of the 100 electric utilities of 49% and to the average of the 25 electric utilities with an "A" bond rating of 37%.

It is also noted by the Commission that due to the magnitude of the Company's construction budget relative to its total plant investment, the determination of this issue may be more critical to CP&L than other major electric utilities under the Commission's jurisdiction.

Based upon the foregoing, the Commission concludes that inclusion of some level of CWIP in the rate base of CP&L is imperative to the Company's financial stability and to its continued maintenance of an "A" bondrating. The Commission believes that the preponderance of the evidence in this case exemplifies the necessity of including some level of CWIP in rate base. Indeed with the exception of the Kudzu Alliance, all intervenors in the proceeding advocated the inclusion of some level of CWIP in rate base. The Commission recognizes that the amount of CWIP to be included in rate base is somewhat judgmental since the Commission must determine what level of reasonable and prudent expenditures for CWIP in rate base is necessary to

CP&L's financial stability and what level is in the best interest of the ratepayer.

It is the finding of this Commission from the evidence presented that the financial stability of CP&L requires the inclusion of the Company's requested amount of CWIP in rate base. The Commission has determined that inclusion of $539,780,749 of CWIP associated with Harris Unit No. 1 represents reasonable and prudent expenditures, is in the public interest, and is necessary for the Company's financial stability.

Another issue raised by the Public Staff was the treatment of AFUDC on pre-July 1, 1979, CWIP balances. Public Staff witness Bright testified that she had been advised by counsel that it was not legally permissible to include in rate base any CWIP which represented AFUDC accrued since July 1, 1979, on any pre-July 1, 1979, CWIP balances. As the Commission has stated in the past, AFUDC on CWIP expenditures is as much a part of the cost of construction as the cost of bricks and mortar or labor. Therefore, even though a portion of the AFUDC accrued since July 1, 1979, relates to CWIP balances created prior to July 1, 1979, it is the Commission's opinion that AFUDC is a current cost of construction just like any other cost that occurred after July 1, 1979, on a project that was begun prior to that date. AFUDC on pre-July 1, 1979, property which accrued after July 1, 1979, is therefore found by the Commission to be proper for inclusion in CWIP receiving rate base treatment.

The Public Staff also raised an issue during cross-examination of Company witness Bradshaw concerning the derivation of the AFUDC rate used by the Company subsequent to the Commission Order in Docket No. E-2, Sub 444. Company witness Bradshaw indicated that the Company has used a rate for equity of 15.5% based on the Commission Order in that case. The Public Staff disputes this equity rate and believes instead that a rate of 14.5% should have been used. The Commission found in the last case that the appropriate rate of return on equity for CP&L was 15.5% but reduced such return to 14.5% as a penalty for the 1981 Brunswick outage for the purposes of calculating the revenue requirements of the Company. In the Commission's opinion, reducing the AFUDC rate which would penalize the Company into the future for past performance, would be a greater penalty than the Commission intended in its last general rate Order. The Commission believes that any further penalty in the allowed AFUDC rate would be clearly inappropriate and, therefore, finds the Company's computation of its AFUDC rate appropriate. Further in Evidence and Conclusions for Findings of Fact Nos. 20 and 21, the Commission finds a return on equity of 15.25% fair and reasonable for CP&L under prudent management but has imposed a rate of return penalty for the reason stated therein of .75% on the Company. Consistent with its previous findings the Commission finds that 15.25% is the appropriate rate of return on equity to be used by the Company in calculating its AFUDC rate in the future.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 17

Company witnesses Bradshaw and Faucette, Department of Defense witness McCabe, Kudzu Alliance witness Eddelman, and Public Staff witness Winters presented testimony regarding the reasonable original cost of the Company's investment in electric plant. The following chart summarizes the amounts which the Company and the Public Staff contend are the proper levels of the original cost of CP&L's electric plant to be used in this proceeding.

(000's Omitted)

Item	Company	Public Staff
Electric plant in service	$2,432,859	$2,431,733
Net nuclear fuel	25,172	25,386
Construction work in progress	539,781	309,519
Working capital	134,535	97,780
Accumulated depreciation	(557,168)	(558,731)
Accumulated deferred income taxes	(263,249)	(313,632)
Total	$2,311,930	$1,992,055

As is reflected above, the total net difference between the Company and the Public Staff is $319,875,000. The first item on which the parties disagree is the appropriate amount of electric plant in service. A difference of $1,126,000 exists between the amounts proposed by the Company and Public Staff and results from an adjustment made by Public Staff witness Winters to remove the allowance for funds used during construction (AFUDC) accrued on Roxboro Unit No. 4 during the period September 15, 1980, to September 24, 1982.

Public Staff witness Winters testified regarding this adjustment as follows:

"In CP&L's last general rate case the Commission determined that the AFUDC accrued on 4.97% of Roxboro Unit 4 should not be included in rate base. That determination was made based on the Commission's decision in the preceding case, Docket No. E-2, Sub 391, that CP&L should not be allowed to earn a return on 4.97% of Roxboro Unit 4. However, CP&L accrued AFUDC on that portion of Roxboro during the period it was not allowed in rate base and is again attempting in this case to put that accrued AFUDC into rate base. If the Company is allowed to do this, the Commission's earlier adjustment will be negated. Consequently, I have made an adjustment to remove this AFUDC from rate base and to remove the related depreciation expense from the cost of service. The impact of my adjustment is to reduce gross revenue requirements by approximately $264,000."

Company witness Bradshaw testified that, in his opinion, the Commission should reconsider its decision; because it, in effect, made the stockholders guarantors that vendors will meet design specifications without having to perform warranty work.

The Commission carefully considered this issue in CP&L's last general rate proceeding. In making its decision in that case the Commission considered the context in which the Company undertook to remedy the problems at Roxboro Unit 4 and the fact that such remedies may have only been rigorously pursued upon the prompting of the Commission. Based upon the considerations made in the Company's last general rate proceeding, the Commission concludes that AFUDC accrued on Roxboro Unit No. 4 in the amount of $1,126,000 should be excluded from electric plant in service in this proceeding.

The next item on which the Company and Public Staff disagree is net nuclear fuel. The $214,000 difference between the Company's and Public Staff's position relates solely to an adjustment proposed by the Company to eliminate the Power Agency ownership from net nuclear fuel. The Commission finds it appropriate to exclude from net nuclear fuel that portion owned by the Power Agency and thus finds net nuclear fuel of $25,172,000 reasonable and proper.

The next item of disagreement between the Company and Public Staff is Construction Work in Progress (CWIP). Consistent with the decision made in this regard in Finding of Fact No. 16, the Commission finds CWIP of $539,781,000 appropriate for use herein.

The next item of difference between the Company and Public Staff relates to the working capital allowance. In Finding of Fact No. 15, the Commission finds it reasonable to include in rate base a working capital allowance of $98,868,000.

The Company and the Public Staff are in disagreement regarding the proper amount of accumulated depreciation to be used for setting rates in this proceeding. The difference between the Company's and Public Staff's position of $1,563,000 consists of an adjustment related to AFUDC accrued on Roxboro Unit No. 4 during the period September 15, 1980, through September 24, 1982, of $41,000 and an adjustment proposed by Public Staff witness Winters of $1,604,000 regarding the Brunswick plant augmented off-gas system.

The Commission, having previously found that the AFUDC accrued on the Roxboro Unit No. 4 plant from September 15, 1980, to September 24, 1982, should be excluded from plant in service, correspondingly finds that the related accumulated depreciation should be adjusted accordingly.

The Commission will now discuss the adjustment made by Public Staff witness Winters regarding the Brunswick plant augmented off-gas system.

> "In its final order in CP&L's last general rate case, Docket No. E-2, Sub 444, this Commission ruled that the Brunswick plant augmented off-gas system should not be included in rate base. In its Order of September 24, 1982, the Commission stated:
>
> > 'Witness Jacobstein testified that the Augmented Off Gas System (AOG) is a system designed to remove radioactive gases which are sometimes produced from atomic fission and released through the main condenser at the Brunswick plant. These radioactive gases must be filtered and allowed to decay before release from the plant. Witness Jacobstein further testified that the AOG was of an experimental design which was plagued by explosions during its testing phase. The Company abandoned testing of the system in approximately 1976 and did not repair or replace it. The AOG has thus never functioned during the plant's history.'
>
> During the test period in this case the Company retired this equipment. In doing so the Company accounted for it as an ordinary retirement by crediting electric plant in service and by debiting the depreciation reserve. The net effect of the Company's proposed treatment of this item leaves the rate base at the same level after the retirement as before. If the Company's treatment of the item is not adjusted, the Company will now be allowed to earn a return on funds which the Commission ruled in the last general rate case should be 'removed' from rate base as property not used and useful in the production of electricity.' Thus, I have made an adjustment reducing rate base for this item."

The Commission has carefully reviewed the testimony regarding this issue and concludes that the retirement of the augmented off-gas system should be treated as an extraordinary retirement and that the balance of accumulated depreciation be increased by $1,604,000. However, the Commission believes that it is entirely reasonable and proper for the Company to recover its investment in the Brunswick augmented off-gas system while excluding the investment from rate base. Thus the Commission finds it appropriate to amortize to test period operating revenue deductions the extraordinary retirement of the Brunswick plant augmented off gas system. Further the Commission finds a three-year amortization period for the retirement appropriate.

The Commission finds it necessary to make a further adjustment to accumulated depreciation relating to decommissioning costs. The methodology used by the Company to adjust for future decommissioning of its nuclear units utilizes in part CP&L's capital structure, embedded cost of debt and preferred stock, and return on common equity. In Findings of Fact Nos. 20 and 21 contained herein the Commission establishes the capital structure, cost rates, and return on equity appropriate for setting rates for CP&L in this proceeding. Since the decisions made by the Commission in this regard differ from that proposed by the Company, it is necessary to modify the Company's proposed adjustments for decommissioning cost to reflect the decisions made herein. The Commission, therefore finds it appropriate to increase depreciation expense and accumulated depreciation by $631,000 and to decrease deferred income taxes and accumulated deferred taxes by $311,000. Based upon the foregoing, the Commission finds accumulated depreciation of $559,362,000 proper for setting rates in this proceeding.

The final area of disagreement between the Company and the Public Staff relates to the amount that should be reflected for accumulated deferred taxes. The $50,383,000 difference between the Company's and the Public Staff's proposals relates to the accumulated deferred taxes associated with the gain on the sale of property to NCEMPA. As discussed in Evidence and Conclusions for Finding of Fact No. 7, the Commission finds it appropriate to increase accumulated deferred taxes by $50,383,000.

The Commission concludes, based upon the foregoing, and the decisions made in Findings of Fact Nos. 15 and 16 that the proper level of the Company's net investment in electric plant in service for use herein is $2,124,003,000; that the reasonable allowance for working capital is $98,868,000, including deferred debits and credits; and that the proper rate base for use herein is $2,222,871,000 as detailed below:

(000's Omitted)

Item	Amount
Electric plant in service	$2,431,733
Construction work in progress	539,781
Net nuclear fuel	25,172
Working capital	98,868
Less: Accumulated depreciation	(559,362)
Accumulated deferred taxes	(313,321)
Total rate base	$2,222,871

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 18

Company witness Chapman and Public Staff witness Dennis presented testimony relative to the appropriate level of revenues under present rates to be included in this proceeding. The difference between the revenues proposed by the Company and the revenues proposed by the Public Staff relates solely to the amount of supplemental revenues from NCEMPA. The Company includes $1,103,090,000 as the end-of-period level of operating revenues whereas the Public Staff included $1,101,548,000. The difference of $1,542,000 is due entirely to the different levels of NCEMPA supplemental revenues and consists of both a fuel-related adjustment and a nonfuel related adjustment.

The Company has treated the supplemental revenues from NCEMPA as properly allocable to current customers of the Company. Allocation of these revenues to North Carolina retail customers has the effect of lowering the revenue increase that would otherwise be requested. However, any expenses incurred by the Company in providing this service are also allocated to current customers. The net result is that any difference between expenses and revenues related to supplemental sales will be allocated to present customers. This means that retail customers could benefit if revenues exceed expenses or incur additional costs if expenses exceed revenues. The Public Staff did not take issue with the Company's treatment of NCEMPA Supplemental Revenues and related expenses as properly allocable to the current customer of the Company. Indeed, the Public Staff's methodology in this regard is identical to that of the Company. The Commission finds it appropriate to treat the NCEMPA supplemental revenues and related expenses as proper components of the Company North Carolina retail operations for purposes of setting rates in this proceeding.

The Company has calculated the test year Supplemental Revenues in accordance with the Power Coordination Agreement but has made adjustments for known changes including: the rate of return requested in this case, the inclusion in plant in service of Mayo Unit No. 1 on an annualized basis, and fuel expenses equal to the Company's proposed base fuel cost.

Public Staff witness Dennis testified that the Company should have priced the supplemental revenues using end-of-period balances rather than test year 13-month balances for investment, accumulated depreciation, accumulated deferred income taxes, and plant held for future use, as well as adjusted test year expense levels. Witness Dennis maintained that the Company's methods are inconsistent with the traditional rate-making process followed by the Commission.

The Company makes the argument that the methodology followed by the Public Staff also fails to correspond completely to the rate-making methodology adhered to by the Commission since components of the investment base for the NCEMPA differ from components of the rate base determined by this Commission. The Company further argues that although neither the Company nor the Public Staff has strictly followed the Power Coordination Agreement (PCA) and neither made all of the adjustments that could be made, the Company's treatment is substantially closer to the provisions of that agreement.

The Commission concludes that it is appropriate to calculate supplemental revenues utilizing end-of-period investment balances in the manner advocated by the Public Staff. In making its decision the Commission recognizes that the Power Coordination agreement is a negotiated contract between the NCEMPA

and CP&L. However, the Commission can find no plausible reason for not adjusting NCEMPA supplemental revenues and related expenses to an end-of-period level which can be anticipated to occur in the future.

The Commission notes that this issue is directly analogous to the establishment of end-of-period toll service revenues in telephone company rate proceedings where the telephone company is settling on an actual cost basis. As the investment base in the PCA differs from that used by this Commission, it is likewise true that the investment base for toll settlement purposes differs from that used by this Commission to set rates for telephone companies under its jurisdiction. Likewise average investment balances and actual expenses are used in the toll settlement process as in the PCA. The Commission has followed a methodology for many years in telephone rate proceedings, of adjusting toll settlement revenues to an end-of-period level using end-of-test period level of investment. The Commission thus finds it proper to adjust NCEMPA supplemental revenues to an end-of-period level that can be anticipated to occur on an ongoing basis in the future.

Both parties spoke of the difficulty and the time required to adjust the per books amounts of supplemental revenues. Undoubtedly much of the difficulty involved results from the newness of the contract and lack of familiarity in dealing with this issue for rate-making purposes. The Commission finds that the Company should in its next general rate proceeding file all data and information necessary to make the end-of-period calculations similar to those found fair herein by the Commission. Company witness Chapman suggested that an alternative to the process of adjustments would be to allocate the NCEMPA supplemental sales separately as a class and to assign directly the supplemental revenues to that class consistent with the treatment of any retail rate class. The result of this separate allocation would be that any difference between revenues and expenses would no longer fall to North Carolina retail customers. Instead, any excess or shortfall would fall to the Company stockholders. The Company did not file sufficient information to make such determinations in this proceeding. However, should the Company find it prudent to use such methodology in its next general rate proceeding, the Commission directs the Company to file such information in addition to the information previously required herein.

The next issue to be resolved regarding supplemental revenues relates to the proper rate of return on common equity to be used in calculating supplemental revenues. Witness Dennis testified that the contracts between NCEMPA and CP&L provide that NCEMPA pay CP&L a return on certain investments in utility property. The common equity portion of that return to be paid by NCEMPA is specified to be the common equity rate of return granted by this Commission in the Company's most recent general rate proceeding minus .75%. The Company is requesting a 15.5% of return on common equity in this proceeding. Alternatively, the Public Staff is recommending a 13.5% return on common equity.

The Commission, in agreeing with the end-of-period concept of calculating an ongoing level of supplemental revenues, also agrees that the common equity rate found fair in this proceeding, less .75%, as specified in the contract between NCEMPA and CP&L, should be used in calculating those supplemental revenues. In accordance with Finding of Fact No. 21, that 14.50% is the reasonable rate of return on common equity, the Commission concludes that 13.75% (14.50 - .75%) is the correct rate of return to use in calculating NCEMPA supplemental revenues.

The final issue to be resolved regarding operating revenues relates to the fuel-related supplemental revenues. Public Staff witness Nightingale presented testimony on the impact of the Power Agency on CP&L's system fuel cost. Basically, witness Nightingale used the actual test period Power Agency impact ratio as a proxy for the impact in his fuel normalization discussed in Evidence and Conclusions for Finding of Fact No. 13. Witness Nightingale stated that the overall impact of the Power Agency as a ratio of the Company's total system "fuel only" cost remained relatively constant over a wide range of possible generation mixes.

As noted by witness Nightingale the proportions of the Power Agency relative to CP&L's "fuel only" fuel cost remained fairly constant over a varied range of generation mixes. The Commission finds the Public Staff's position in this regard reasonable. However, for purposes of this case the Commission has utilized a method of calculating the change in supplemental revenues necessitated by changes in fuel expenses in a manner similar to that employed by the Company. The Commission therefore concludes that it is proper to adjust supplemental revenues to reflect the impact of changes in fuel costs that are associated with the adjusted fuel factor found appropriate in this proceeding. The base fuel factor of $.01677 per kWh found proper by the Commission is fully discussed in Evidence and Conclusions for Finding of Fact No. 13. In summary, the Commission finds that the rate-making treatment of both nonfuel related supplemental revenues from NCEMPA advocated by the Public Staff and the fuel supplemental revenues adjusted to reflect the fuel factor previously found fair herein is proper. The Commission finds test period operating revenues of $1,104,072,000 appropriate for use herein.

In addition to the issues discussed above which were contested among the parties to this docket, the Company included in its filing a number of adjustments to reflect a 100% closing of the sale to NCEMPA. No objection has been made to these adjustments, and they are hereby approved.

The Commission recognizes that the sale of assets to the NCEMPA, when viewed as an overall package, has and will be of substantial benefit to the ratepayers of North Carolina. Although there is disagreement among the parties on the handling of certain aspects of the sale, no party has contested the substantial overall benefit of the sale to the Company's ratepayers.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 19

The evidence for this finding of fact is found in the testimony and exhibits of Company witnesses Bradshaw, Nevil, Chapman, and McClellen, and Public Staff witnesses Nightingale, Lam, Winters, and Carter.

The following schedule sets forth the amounts proposed by the Company and the Public Staff.

(000's Omitted)

Item	Company	Public Staff
Operation and maintenance expenses	$649,145	$598,366
Depreciation expense	91,755	91,714
Taxes other than income	82,223	81,892
Income taxes	92,917	122,306
Total operating revenue deductions	$916,040	$894,278

As the above chart indicates, the parties are in disagreement over all of the items of operating revenue deductions. The Commission will now analyze the reasons for these differences.

The first difference between the parties is the level of operation and maintenance expenses recommended for use in this proceeding. The chart below summarizes the components of this difference of $50,779,000.

(000's Omitted)

Item	Amount
Leslie and McInnes coal losses	$ 6,520
Fuel expenses	44,259
Total	$50,779

The first component of the difference arises from an adjustment made by Public Staff witness Carter regarding the proper amount of losses attributable to the purchases of coal from affiliated coal mines. The Commission fully discussed this issue under Evidence and Conclusions for Finding of Fact No. 10 contained herein and concludes that operation and maintenance expenses should be reduced by $6,519,808 for this item.

The next area of disagreement concerns the proper level of fuel expense that should be included in operating expenses. Consistent with the conclusions contained in Evidence and Conclusions for Finding of Fact No. 13, wherein the proper base cost of fuel was determined to be $.01677 per kWh, the Commission finds total fuel expense of $350,922,000 consisting of base fuel expense and handling and analysis charges appropriate for use herein.

Based upon the foregoing discussion, the Commission finds operation and maintenance expenses of $617,238,000 just and reasonable.

The next item on which the parties disagree is depreciation expense. The $41,000 difference in the party's proposals results from the adjustment made by the Public Staff to remove the depreciation expense related to the AFUDC accrued on Roxboro Unit No. 4 from September 15, 1980, through September 24, 1982. The Commission has previously concluded in Evidence and Conclusion for Finding of Fact No. 17 that AFUDC relating to Roxboro Unit 4 should not be included in rate base; therefore, the Commission finds and concludes that depreciation should be reduced by $41,000 for this item.

In Evidence and Conclusions for Finding of Fact No. 17, the Commission also discussed the appropriate rate-making treatment of the retirement of the Brunswick augmented off-gas system. Consistent with the previous decision made in this regard, the Commission finds it appropriate to increase depreciation expense by $535,000 for amortization expense related to the Brunswick augmented off-gas system.

The Commission finds it necessary to make a further adjustment to depreciation expense relating to decommissioning expense. The calculation of test period decommissioning expense proposed by the Company and approved by this Commission in previous general rate proceedings is dependent in part upon the capital structure, embedded cost of debt, and preferred and rate of return on equity found fair by this Commission. Since the findings of the Commission differ from that proposed by the Company, it is necessary to adjust decommissioning expense to reflect the impact of the capital structure, embedded cost of debt and preferred and rate of return on equity found fair by this Commission in Findings of Fact Nos. 20 and 21. Thus the Commission finds it appropriate to increase the decommissioning expense proposed by the Company by $631,000.

Based upon the foregoing, the Commission finds depreciation expense of $92,880,000 appropriate for use herein.

The next item on which the parties disagree is the proper level of taxes other than income which should be used in this proceeding. The chart which follows summarizes the components of this difference of $330,000.

Item	Amount
Property taxes on Roxboro No. 4 AFUDC	$ 7,000
Property taxes related to Public Staff	323,000
Total	$330,000

The $7,000 component of the difference results from an adjustment made by the Public Staff to remove property taxes from the cost of service related to the AFUDC accrued on Roxboro Unit No. 4 from September 15, 1980, through September 24, 1982. The Commission has concluded in another section of this Order that this amount of AFUDC should not be included in rate base; therefore, the Commission concludes that property tax expense should be reduced by $7,000.

The other area of disagreement between the parties with respect to year-end property taxes relates to the appropriate property tax rate to use in the calculation of property taxes allowable as an expense. Public Staff witness Winters used a property tax factor for the calendar year ended December 31, 1982; whereas Company witness Faucette used a property tax factor for the calendar year ended December 31, 1981. Both factors were calculated using Plant in Service balances before full NCEMPA ownership is excluded. The result is an adjustment proposed by witness Winters to decrease property taxes by $449,000.

This Commission concludes that the property tax factor used should be determined on the most recent calendar year figures as proposed by the Public Staff. It should, however, be adjusted to exclude full Power Agency ownership to be consistent with all other amounts in this case. Therefore, the Commission has calculated a property tax rate using calendar year-end December 31, 1982, taxes paid and property investment, but excluding full NCEMPA ownership. This rate is .06565 and results in a decrease in property taxes of $126,000 from the amount calculated by the Company. The Commission finds taxes other than income of $82,215,000 appropriate for use herein.

The next difference relates to state and federal income taxes. Since the Commission has not accepted all of either the Company's or the Public Staff's components of taxable income, it is necessary to calculate state and federal income taxes based on the findings heretofore and herein made by the Commission. The only substantial differences between the parties, with respect to the level of income tax expenses, relate to two adjustments made by Public Staff witness Winters: an adjustment to eliminate the Company's adjustment as related to the job development investment tax credit (JDITC) in calculating interest expense and an adjustment to eliminate the accumulated investment tax credits with respect to property which CP&L sold to the NCEMPA.

The Public Staff's adjustment to include JDITC imputed interest in the interest expense deduction decreases taxes and has the effect of reflecting JDITC at less than the overall rate of return. The Public Staff has taken this position in the last four rate cases, and the Commission in those cases has ruled that the Public Staff's position is improper. The Commission has been upheld by the North Carolina Court of Appeals. State ex. rel. Utilities Commission v. Carolina Telephone & Telegraph Co., 61 N.C. App. 42 (1983). The Commission is aware of no new evidence presented in this case which would warrant a change and, therefore, concludes that the JDITC imputed interest should not be used as a deduction for purposes of calculating income taxes.

The second JDITC adjustment proposed by the Public Staff relates to property sold to NCEMPA. This issue was fully discussed in Evidence and Conclusions for Finding of Fact No. 7 wherein the Commission concludes that the determination of the appropriate rate-making treatment for the Job Development Investment Tax Credit relating to the portion of the generating and transmission plant sold to NCEMPA should properly be held in abeyance at this time. Thus the Commission finds the adjustment to income tax expense proposed by the Public Staff inappropriate. The Commission finds income tax expense of $110,643,000 reasonable for use herein.

Based on the previous findings, the Commission concludes that total operating revenue deductions are $902,976,000 as shown on the chart below.

(000's Omitted)

Item	Amount
Operation and Maintenance Expenses	$617,238
Depreciation expense	92,880
Taxes other than income	82,215
Income taxes	110,643
Total operating revenue deductions	$902,976

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 20 AND 21

Three witnesses testified in the area of capital structure and cost of capital. The Company offered the testimony of Sherwood H. Smith, Chief Executive Officer and Chairman of the Board of Directors of CP&L, Edward G. Lilly, Jr., Senior Vice-President and Chief Financial Officer of CP&L, and Dr. James H. Vander Weide, Professor at the School of Business Administration at Duke University. The Public Staff offered the testimony of Dr. Caroline M. Smith, Senior Economist with the firm of J. W. Wilson & Associates, and consultant to the Public Staff. The Department of Defense offered the testimony of John W. McCabe III regarding this issue. In addition, the

Company offered rebuttal testimony of Archie W. Futrell, Jr., Director of the Economic and Energy Forecast and Special Studies of CP&L, on the subject of Public Staff witness Smith's growth estimates for determining CP&L's cost of equity.

Company witness Lilly testified on the financial plans of CP&L. In his original testimony, witness Lilly recommended that rates be set in this proceeding upon a hypothetical or "normalized" capital structure consisting of 49.5% debt at a cost of 9.59%, 12.5% preferred and preferenced stock at a cost of 8.96%, and 38% common equity with a required return of 15.5%. Witness Lilly testified that the actual capital structure at September 30,1983, was comprised of 48.98% long-term debt, 13.15% preferred stock, and 37.87% common equity.

Public Staff witness Smith testified that the overall rate of return which CP&L should be allowed to earn was 11.00%. Witness Smith's recommendation was derived using the Company's requested hypothetical capital structure and senior security costs rates, and included a common equity return of 13.50%.

After considering all of the evidence presented by the parties on these issues, the Commission concludes that the appropriate capital structure to be used in this proceeding is as follows:

Item	Percent
Long-term debt	49.5%
Preferred stock	12.5%
Common equity	38.0%
Total	100.0%

Consistent with the evidence supporting the above capital structure, the Commission concludes that the appropriate reasonable embedded costs of long-term debt and preferred stock are 9.59% and 8.96%, respectively.

Company witness Vander Weide testified that the cost of equity capital for CP&L ranges from 16.5% to 17.0%. However, the Company's filing in this proceeding recognizes a requested equity return of 15.5%. Company witness Sherwood Smith testified that the Company requested a return on equity in this case of only 15.5% in recognition of the current economic conditions experienced by ratepayers, although in his opinion the Company can only do so on a short-term basis.

Company witness Vander Weide conducted two studies consisting of a discounted cash flow (DCF) study and a historical yield spread study in arriving at his recommended cost of equity capital for CP&L. The DCF method utilized by witness Vander Weide assumes that the current market price of the firm's stock is equal to the discounted value of all expected future dividends. The DCF formula equates the investors' required return on equity capital to dividend yield plus expected growth in dividends per share.

Witness Vander Weide reviewed the past growth in CP&L's earnings and dividends per share for the last five- and 10-year periods. Additionally witness Vander Weide testified that he had reviewed published security analysts' projections of CP&L's future dividends and earnings growth. On the basis of his examination of the past growth rates, his review of analysts' projections, and his knowledge of current economic conditions, witness Vande

Weide estimated the Company's expected growth rate to be in the range of 5% - 6% which, when added to his dividend yield, produced a cost of equity by the DCF method of 16.45% - 17.45%, centering on 17%.

The second study performed by Company witness Vander Weide was the historical yield spread study. The yield spread study equates investors' current expected return on equity to the sum of current bond yield plus the past differences or spread between the yields on stocks and the yields on bonds. Based upon the yield spread study, witness Vander Weide arrived at a cost of equity capital for CP&L of 18%.

In updating and summarizing his testimony from the witness stand, witness Vander Weide reevaluated his recommended return on an equity capital in the light of changes in economic and financial conditions subsequent to the time his prefiled testimony was prepared. On this basis Dr. Vander Weide determined the cost of CP&L's equity to be the range of 16.5% and 17.0%.

Company witnesses Vander Weide and Lilly testified regarding the erosion of the Company's financial integrity, its poor earnings quality in the perspective of current economic events, the present unfavorable environment of financial markets, and the serious need for adequate regulatory relief. Witness Lilly further pointed out that since 1977, CP&L fixed charge coverage, excluding allowance for funds used during the construction (AFUDC), has fallen from 2.9 times in 1978 to 1.9 times for the 12 months ended September 30, 1982. Moreover, AFUDC as a percentage of income for common equity during the same time period increased from 46% in 1978 to 78% in 1982.

Witness Lilly further testified that the forecast of construction expenditures for the period 1983-1985 for CP&L is substantially greater than the industry average for the same period. Comparison of these forecasts indicates greater construction risk in CP&L than in the industry generally. Witness Lilly also testified that while the sale of assets to the Power Agency has temporarily reduced somewhat the need for outside financing of required construction, the Company will continue to face substantial outside financing requirements. Additionally, Witness Lilly testified that the Company had suffered a downgrading of its bonds after the last North Carolina retail rate Order and that another downgrading is possible if CP&L's financial stability does not improve.

Public Staff witness Smith derived the Public Staff's recommended return on common equity of 13.5% on the basis of a DCF analysis for CP&L and the electric utility industry as a whole. Witness Smith testified that CP&L's dividend yield was 11.5%, as compared to the industry average dividend yield of 10.7%. Witness Smith stated further that actual historical growth indicators for CP&L were smaller than the industry average, ranging between 0.7% to 2.9% for the Company and 1.2% to 3.8% for the industry. Witness Smith derived an estimate of the long-term dividend growth anticipated by investors of 1.5% to 2.5%, which she stated is somewhat higher than CP&L's own experienced growth and below the industry average historical experience. Based upon her study, witness Smith concluded that the current cost of common equity to CP&L is in the 13% to 14% range, and proposed that the midpoint of that range of 13.5% be used for setting the allowed rate of return.

Additionally witness Smith presented data concerning the historical earnings of utilities and non-regulated companies. According to witness Smith

electric utilities equity earnings have ranged from 11% to 13% over the past decade. Alternatively witness Smith testified that unregulated companies, which are less risky than CP&L and the other electric utilities on any conventional measure, earned 11% on common equity in 1982.

Public Staff witness Smith testified that the study conducted by herself assumes like the classic DCF model that a company's cost of equity capital is determined by its dividend yield and the long-term dividend growth anticipated by investors. Witness Smith also explained that, although the electric utilities are similar, there are risk differences within the industry. Variations in risk measures include equity ratios, price volatility, management quality, and the nature of resource supply contracts. However, witness Smith stated that the problem with attempting to test these risk variations is that no measureable risk indicators exist which completely explain the variability in dividend yields remaining after growth expectations are accounted for. Specifically, it is not possible to build a perfectly specified model of relationships between dividend yields and the combination of growth and individual risk factors.

However, witness Smith testified that it is possible to measure the collective effect of all the risks investors associate with an individual utility. Witness Smith explained that, while in her opinion the individual effect of each risk factor cannot be measured with precision, it is possible to measure their combined effects by comparing a company's actual dividend yield with the yield that would prevail if expected growth were only determinant of variations in the stock's price and yield. The difference in the actual dividend yield and the yield that would prevail if expected growth were the only determinant of variations in the stocks price and yield is unexplained variability, or the E term, in witness Smith's regression equations.

Company witness Futrell testified in rebuttal to the testimony of Public Staff witness Smith specifically with regard to statistical analyses performed by Dr. Smith. Witness Futrell stated as acknowledged by Public Staff witness Smith that the specific risk variations for CP&L as compared to other electric utilities were not measurable. In witness Futrell's opinion it is impossible due to the lack of specification of a parameter in witness Smith's model namely unknown risk variation to determine the cost of equity capital for CP&L using witness Smith's methodology. Witness Futrell stated that Dr. Smith performed an ordinary least squares regression analysis to solve for the unknown risk variable. An ordinary least squares regression analysis has a dependent variable and one or more independent variables. Witness Smith's independent variable was growth rate, and her dependent variable was dividend yield. Witness Futrell stated that Dr. Smith's regression analysis simply determined the line of best fit between various growth rates and various dividend yields. According to witness Futrell, Dr. Smith erroneously used the error term contained in the ordinary least square regression analysis as a substitute for the risk variable of CP&L. However, in witness Futrell's opinion the risk variation should properly have been treated as an independent variable, in addition to dividend growth. The omission of the independent variable risk variation in witness Futrell's opinion makes it impossible to determine the dividend yield which would best fit a regression with both independent variables utilized. According to Company witness Futrell, Dr. Smith simply attempted to substitute the error of the regression for the independent variable risk variation. In witness Futrell's opinion this cannot

be done because regression analysis minimizes the error of the regression, rather than solving for it. Hence, witness Futrell maintains that the use of the error of the regression as a risk variable is erroneous since a minimized level of risk variation rather than the actual value of risk variation is obtained. Consequently, witness Futrell concludes that the analysis performed by witness Smith should not be relied upon to determine the cost of equity capital for CP&L.

Department of Defense witness McCabe recommended a return on equity of 14.75%. Witness McCabe's recommendation was not based on any specific statistical analyses but rather equates the return on equity to that found in the last rate case less 75 basis points comparable to the treatment prescribed in the return component of CP&L's Power Coordination Agreement with the North Carolina Eastern Municipal Power Agency.

The determination of the appropriate fair rate of return for the Company is of great importance and must be made with great care because whatever return is allowed will have an immediate impact on the Company, its shareholders, and its customers. In the final analysis the determination of a fair rate of return must be made by this Commission, using its own impartial judgment and guided by the testimony of expert witnesses and other evidence of record. Whatever return is allowed must balance the interest of the ratepayers and investors and meet the test set forth in G.S. 62-133(b)(4):

> "...(to) enable the public utility by sound management to produce a fair return for its shareholders, considering changing economic conditions and other factors, as they then exist, to maintain its facilities and services in accordance with the reasonable requirements of its customers in the territory covered by its franchise, and to compete in the market for capital funds on terms which are reasonable and which are fair to its customers and to its existing investors."

The return allowed must not burden ratepayers any more than is necessary for the utility to continue to provide adequate service. The North Carolina Supreme Court has stated that the history of G.S. 62-133(b):

> "...supports the inference that the Legislature intended for the Commission to fix rates as low as may be reasonably consistent with the requirements of Due Process Clause of the Fourteenth Amendment to the Constitution of the United States..." State ex rel. Utilities Commission v. Duke Power Co., 285 N.C. 377, 206 S.E. 2d 269 (1974).

The nature of the evidence in a case such as this makes it extremely difficult to balance all of the opposing interests, since much, if not all, of the evidence is based on individual witnesses' perceptions and interpretations of trends and data from the capital market. The Commission has considered carefully all of the relevant evidence presented in this case, with the constant reminder that whatever return that is allowed will have an immediate impact on the Company, its stockholders and its customers. The Commission must use its impartial judgment to insure that all the parties involved are treated fairly and equitably. In coming to a final decision on this matter, the Commission is not unmindful of the upward pressure of capital costs generally present in the economy over recent years.

Based upon a careful consideration of all of the foregoing, including the statistical procedures used by witness Smith, the Commission concludes that, in the absence of any consideration of CP&L's history of poor nuclear performance and the inefficiency and imprudence of CP&L's management in the area of nuclear plant performance, a 15.25% rate of return upon equity would be the fair rate of return for CP&L in this case. However, when CP&L's poor nuclear plant performance and the past history of inefficiency and imprudence of CP&L's management in the area of nuclear plant performance is taken into consideration, the Commission concludes that it cannot allow that level of return upon equity. It is clear, based upon Finding of Fact No. 11 set forth above and the matters set forth and discussed in connection with the Evidence and Conclusions section for said finding of fact, that CP&L's inefficiency and mismanagement in the past resulted in the Company not achieving reasonable operation of its nuclear units during the test year. The Commission recognizes that considerable changes in organization and procedure have now been made but concludes that a penalty should remain in effect for the Company because of its test year nuclear performance. The Commission therefore concludes that CP&L should be allowed an opportunity to earn no more than a 14.5% rate of return on equity.

This Commission operates under a legislative mandate that requires it to fix rates which will allow a utility "by sound management" to pay all of its reasonable operating costs, including maintenance, depreciation, and taxes, and to earn a fair return on its investment. G.S. 62-133(b)(4); State of North Carolina ex rel. Utilities Commission vs. Duke Power Company, 285 NC 377, 206 SE 2nd 269 (1974). However, upon a finding that a utility is not soundly managed, it may be penalized by being authorized to earn less than a "fair return." State of North Carolina ex rel. Utilities Commission vs. General Telephone Company of the Southeast, 285 NC 671, 208 SE 2nd 681 (1974). In order to penalize a utility on rate of return, the Commission must make specific findings showing the effect upon its decision of the poor management it has found. Utilities Commission v. Morgan, Attorney General, 277 N.C. 255, 177 S.E.2d 405 (1970). The penalty must not result in a confiscatory rate of return. 285 NC 671.

In this case, the Commission has concluded that if CP&L's Brunswick nuclear units had been properly managed and reasonably operated, said Company would be entitled to a 15.25% rate of return on its common equity. The Commission has found, however, that CP&L's nuclear performance continues to be unsatisfactory and that the cost of service to CP&L's customers has been significantly increased as a result. In Finding of Fact No. 11 above and the Evidence and Conclusions set forth in support thereof, the Commission has determined that CP&L's nuclear performance during the test year was unsatisfactory. Considering the evidence of corporate mismanagement with respect to the Brunswick nuclear plant, the Commission concludes that CP&L should be penalized by not being allowed to earn the rate of return that it would have been allowed if its Brunswick nuclear plant had been soundly managed.

Public Staff witness Thomas S. Lam testified that the 78 days of outages at the Brunswick nuclear unit resulted in approximately $26.5 million purchase power requirement, fuel cost expense, and calculated replacement power costs. Public Staff witness Caroline M. Smith testified that this figure would translate into a penalty of 150 basis points or 1.5%. While Company witness Lynn Eury agreed that the $26.5 million figure was a reasonable estimate, he noted that improvements have been made in the management of the Brunswick

units since the time of these outages. He also noted that NRC has found performance "at the plant level" at the Brunswick units to be "acceptable" and has identified "major strengths" at the plant in the areas of emergency preparedness, security and safeguards. Eury further testified that the Company's fossil plants' performance compares quite favorably with appropriate industry indicators. The Commission must consider all material evidence that will help it determine what are reasonable and just rates. Further evidence presented shows that in September 1982 CP&L made certain changes with respect to the management of the Brunswick nuclear units. Reorganization of management was made to increase senior management oversight of the plant, to improve communications and coordination, and improve organizational accountability and strengthen management control. In recognition of these initiatives and the evidence as a whole, the Commission has determined that a rate of return penalty of 0.75% is appropriate.

The penalty imposed above will not result in a confiscatory rate of return. The Commission has determined that allowing a 14.5% rate of return on common equity and a 11.38% rate of return on the Company's rate base will allow CP&L to pay its operating expenses, including maintenance, depreciation, taxes, and interest on long-term debts, and still pay $24,896,000 to its preferred shareholders and $122,480,000 to its common shareholders. This is not confiscatory.

The Commission cannot guarantee that the Company will, in fact, achieve the level of returns herein found to be just and reasonable. In fact, it should be noted that the revenue requirements established in this case reflect the Commission's disallowance of CP&L's cost of debt and equity funds associated with the Company's abandoned plant facilities. These unrecognized costs would serve to reduce the Company's ability to earn the allowed returns stated above. Indeed, the Commission would not guarantee it if it could. Such a guarantee would remove necessary incentives for the Company to achieve the utmost in operational and managerial efficiency. The Commission believes, and thus concludes, that the level of return approved herein will afford the Company a reasonable opportunity to earn a reasonable return for its stockholders while providing adequate and economical service to ratepayers.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 22

The Commission previously has discussed its findings and conclusions regarding the rate of return which CP&L should be given the opportunity to earn.

In the Commission's September 19, 1983, Order Granting Partial Increase in Rates and Charges, the Company was granted rates which produce total operating revenues of $1,196,049,000, based on adjusted test period sales of 18,660,082,846 kWh. Said Order reflected an annual increase in operating revenues of $90,855,000. In its September 19, 1983, Order the Commission noted that a major factor contributing to CP&L's need for rate relief was the addition to CP&L's system of Unit No. 1 of the Mayo generating plant. The increased revenue requirements associated with Mayo Unit No. 1 being placed into service was approximately $41 million.

The Commission upon reconsideration has determined that the Company's total gross revenue requirement for its North Carolina retail operations is $1,195,283,000, based upon the adjusted test year ended September 30, 1982,

which reflects an annual increase in operating revenues of $91,211,000. The Commission notes that the gross revenue increase reflected herein of $91,211,000 exceeds by $356,000 the gross revenue increase granted in the Commission's September 19, 1983, Order. However, due to the lack of materiality of such an increase in revenue requirements relative to the Company's total revenue requirements (less than .0003) the Commission finds it unreasonable for CP&L to increase the rates and charges which became effective September 19, 1983, in order to recover such a de minimus amount. Therefore, the Commission finds that CP&L should maintain without change the rate and charges which became effective September 19, 1983.

The following schedules summarize the gross revenues and the rates of return which the Company should have a reasonable opportunity to achieve based upon the increases approved herein. Such schedules, illustrating the Company's gross revenue requirements, incorporate the findings and conclusions heretofore and herein approved by the Commission.

SCHEDULE I
CAROLINA POWER & LIGHT COMPANY
NORTH CAROLINA RETAIL OPERATIONS
DOCKET NO. E-2, SUB 461
STATEMENT OF OPERATING INCOME
TWELVE MONTHS ENDED SEPTEMBER 30, 1982
(000'S OMITTED)

Item	Present Rates	Approved Increase	Approved Rates
Operating revenues	$1,104,072	$ 91,211	$1,195,283
Operating revenue deductions:			
Operation and maintenance expenses	617,238	-	617,238
Depreciation expense	92,880	-	92,880
Taxes other than income	82,215	5,473	87,688
Income taxes	110,643	42,217	152,860
Total	902,976	47,690	950,666
Operating income before adjustments	201,096	43,521	244,617
Adjustments to operating income	8,280	-	8,280
Net operating income	$ 209,376	$ 43,521	$252,897

SCHEDULE II
CAROLINA POWER & LIGHT COMPANY
NORTH CAROLINA RETAIL OPERATIONS
STATEMENT OF RATE BASE AND RATE OF RETURN
TWELVE MONTHS ENDED SEPTEMBER 30, 1982
(000'S OMITTED)

Item	Amount
Investment in Electric Plant:	
Electric plant in service	$2,431,733
Net nuclear fuel	25,172
Construction work in progress	539,781
Accumulated depreciation	(559,362)
Accumulated deferred income taxes	(313,321)
Net investment in electric plant	2,124,003
Allowance for Working Capital:	
Cash	3,467
Materials and supplies	96,071
Prepayments	6,594
Investor funds invested for operations	17,413
Miscellaneous projects	4,943
Other rate base deductions	(23,722)
Customer deposits	(5,898)
Total	98,868
Original cost rate base	$2,222,871
Rates of Return	
Present	9.42%
Approved	11.38%

SCHEDULE III
CAROLINA POWER & LIGHT COMPANY
NORTH CAROLINA RETAIL OPERATIONS
STATEMENT OF CAPITALIZATION AND RELATED COSTS
TWELVE MONTHS ENDED SEPTEMBER 30, 1982
(000'S OMITTED)

Item	Capitalization Ratio (%)	Original Cost Rate Base	Embedded Cost (%)	Net Operating Income
	Present Rates - Original Cost Rate Base			
Long-term debt	49.50	$ 1,100,321	9.59	$105,521
Preferred stock	12.50	277,859	8.96	24,896
Common equity	38.00	844,691	9.35	78,959
Total	100.00	$2,222,871	-	$209,376
	Approved Rates - Original Cost Rate Base			
Long-term debt	49.50	$ 1,100,321	9.59	$105,521
Preferred stock	12.50	277,859	8.96	24,896
Common equity	38.00	844,691	14.50	122,480
Total	100.00	$2,222,871	-	$252,897

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 23 THROUGH 27

Evidence for these findings of fact is found primarily in the testimony and exhibits of Company witness Edge, Public Staff witnesses Richard Smith and Turner, DOD witness McCabe, and Kudzu witness Eddleman. The following discussion of the rate designs proposed by the various parties is arranged by rate schedule or by topic.

Summer/Winter Rate Differentials

In its residential rate Schedule RES, the Company proposes to retain the summer/winter rate differential for all over 800 kWh. None of the rates proposed for the nonresidential rate schedules (excluding time-of-day rate schedules) contain summer/winter rate differentials for the energy charges. In fact, the seasonal rate differential does not apply to all energy blocks for residential service.

In the previous general rate cases in Docket Nos. E-2, Sub 416 and Sub 444, the Commission concluded that the summer/winter differentials in the residential rates should not be increased until such time as it can be determined what size summer/winter differential would be appropriate for each rate block of each rate schedule. The Commission further concluded that the Public Staff and CP&L should examine in depth the appropriate level of seasonal differentials and present their results in a docket as soon as possible.

The cost allocation study presented by the Company in this proceeding includes an attempt to quantify an appropriate summer/winter rate differential for residential service. The study results indicate that almost all of the summer/winter rate differential is due to the difference in unit demand cost between summer and winter. A review of the study methodology indicates that the major factor affecting the difference in unit demand cost between summer and winter is the fact that 50% of demand related fixed costs are allocated to four summer months and 50% are allocated to eight winter months. Such an allocation would produce a higher summer rate and a lower winter rate even if there were not other cost differences.

The Commission is of the opinion that further study of summer/winter rate differentials is needed. Such studies might consider the fixed plant mix during summer months versus winter months, and the number of months associated with summer peaks versus winter peaks.

TOD Rates for Residential Service

Public Staff witness Richard Smith testified that the customer response to the Company's time-of-use rate Schedule R-TOU has been poor to date. In order to make the schedule more attractive for the customer and more effective in reducing system demand, he recommended that the on-peak hours in that schedule be reduced. From the customer's standpoint, shorter on-peak hours would give more flexibility in scheduling baths and in the use of dishwashers and clothes washers. Shorter on-peak hours would also permit pre-cooling of the residence on summer mornings, earlier use of air conditioning in the evenings, and more satisfactory heating opportunities in the winter.

With respect to reducing system demand, witness Smith stated that with rates which are revenue neutral it is necessary to increase the demand charge to compensate for decreased on-peak hours. That increased demand charge then becomes an added incentive for customers to reduce demand.

The reduced on-peak hours recommended by the Public Staff compared to the present on-peak hours for Schedule R-TOU are as follows:

	Schedule R-TOU On-Peak Hours	
	April-September	October-March
Present hours	10:00 A.M. - 10:00 P.M.	6:00 A.M. - 1:00 P.M.
Hours proposed by Public Staff	Noon - 9:00 P.M.	6:30 A.M. - 1:00 P.M.

Witness Smith's testimony indicated that the proposed reduced hours would permit demand reductions up to 7.73% in the Company's system load curves and that less than 6% demand reduction is forecast by the Company from time-of-use rates and load control measures by the year 1995.

Chairman Koger asked the Company to determine what the effect would be in 1995 of shortening the summer on-peak period from 10:00 p.m. to 9:00 p.m. Company witness Edge testified that he was concerned with customers cutting back on appliances at the end of the on-peak period, but that the Company does not have a lot of difficulty with the idea of shortening the summer on-peak period from 10:00 p.m. to 9:00 p.m.

The Commission concluded in the previous general rate case (in Docket No. E-2, Sub 444) that the Company should embark on an experimental trial program to ascertain the effectiveness of an all-energy TOD rate (i.e., two-part rate) for residential customers, and that such all-energy TOD rate, if proved valid, could replace the present demand type TOD rate (i.e., three-part rate) or could be offered as an alternative TOD rate for residential service. The Commission also concluded that such all-energy TOD rate should include the same on-peak/off-peak hours recommended by the Public Staff in that proceeding, which are also the same hours recommended by the Public Staff in this case. The Company therefore implemented the experimental rate as directed by the Commission.

Given the evidence presented in this proceeding, the need for successful load management, and the agreement by all parties that moving the residential summer on-peak hours from 10:00 a.m. - 10:00 p.m. to 10:00 a.m. - 9:00 p.m. would have no detrimental effect at this time, the Commission accepts the principle of shifting the April-September residential on-peak boundary from 10:00 p.m. to 9:00 p.m. Due to the uncertainties inherent in future predictions, i.e., load forecasts, anticipated customer response, and overall load management and conservation program success, the shift in on-peak hours should apply to the Residential TOU rate schedule only.

Since the Commission believes the changes to meters and communication of the change to consumers will take some time, the change should be made effective by April 1, 1984. Present rating periods for all TOU rates should remain unchanged through March 31, 1984, new rating periods for the Residential TOU rate should become effective on April 1, 1984, and the Company should notify the Commission when the necessary changes and communications have been accomplished.

In another matter affecting TOD rates, the cost allocation study presented by the Company in this proceeding includes an attempt to quantify a cost differential between on-peak hours and off-peak hours. A review of the study methodology indicates that demand-related fixed costs are allocated to on-peak hours only. The Public Staff recommended that CP&L conduct further study of the allocation of fixed costs between on-peak and off-peak periods in conjunction with the cost allocation issues. The Commission is not convinced that the rate differential between on-peak and off-peak hours should be established, based on the study presented in this proceeding, and concludes that further study and discussion is needed.

Residential Water Heater Load Control Program

CP&L's residential water heater load control program currently applies to water heaters which have a storage capacity of 40 gallons or more. Public Staff witness Richard Smith recommended that 30-gallon water heaters also be eligible for the program. Witness Smith stated that including 30-gallon water heaters in the program could increase the number of eligible heaters by 60% and thereby expand by a like amount the potential demand reduction achievable by the load control program.

Witness Smith offered water heater manufacturer's test data which showed that the temperature of the water withdrawn from a water heater did not decline in direct proportion to the water used as assumed by both the Company and the consultant's study, but that 75% of a water heater's capacity was available before the temperature of the hot water outflow dropped 30 degrees. Witness Smith suggested that this test data indicated that almost three times more hot water was available than calculated.

Witness Smith stated that the Company had made no drawdown tests on 30-gallon water heaters nor had it interrupted any 30-gallon water heaters on its load control program. He also pointed out that the 8,434 customers on the Raleigh test program in 1981, which was limited to water heaters 40 gallons and larger, registered only 71 complaints in the winter and 17 complaints in the summer. Witness Smith indicated that less than one percent had withdrawn from the program, and that few, if any, had withdrawn as a result of the Company's test.

Witness Smith stated that the load control program was a voluntary one and that customers who are dissatisfied with the interruptions could withdraw from the program. Witness Smith stated that the majority of customers with 30-gallon water heaters should find the program satisfactory and that this large segment of customers should not be discriminated against but should be offered the program. Commissioner Campbell inquired whether or not a fact-finding determination could be made by placing 100 or 500 customers on the load control program and then observing the complaints. Witness Smith stated that such a test could be satisfactory, provided the customers were treated normally and left completely alone without receiving any questions or comments from the Company.

CP&L witness Edge testified that the Company is opposed to the inclusion of the 30-gallon capacity water heaters in the load control program. Witness Edge testified that there would be increased customer dissaticluded and that such dissatisfaction could negatively affect the present effort to expand the

water heater control program. In addition, the Company incurs an expense in installing and then removing the control device. Witness Edge testified that information contained in a Public Staff Exhibit filed in Docket No. M-100, Sub 78, showed that the control of the 30-gallon water heater would be satisfactory during peak hours of the day, provided that the length of the interruption was no more than one hour. Also, 40 and 50-gallon water heaters could be interrupted beyond two and three hours, respectively. Witness Edge testified that the Company findings support the findings set forth in the Public Staff Exhibit in Docket No. M-100, Sub 78. Witness Edge testified that the current interruption period of two and three hours in the winter and summer, respectively, would probably have to change to one and two hours in order to minimize customer dissatisfaction if the 30-gallon water heaters are allowed on the program. This would have the effect of substantially reducing the benefits of the program.

The Commission concludes that the addition to the Company's load control program of 30-gallon water heaters is not in the best interests of that program at this time. The Commission recognizes that CP&L is currently expanding the load control program into new locations and that increased customer dissatisfaction could negatively affect that effort. This does not mean, however, that the Company should not continue to seek ways to expand the scope of its water heater control program. The Company should continue to expand into new areas of its territory and once the program becomes well accepted consideration should be given to conducting an experiment using the 30-gallon water heater.

Revenue Requirement for Small General Service

The Commission has generally attempted to establish rates in prior proceedings which would produce rates of return for each class that were within 10% ± of the overall North Carolina retail rate of return. In comparing the rates of return for each rate class resulting from three of the cost allocation methods discussed herein (summer/winter coincident peak, summer/winter peak and base, summer/winter peak and average), the Commission notes that the small general service class is overpriced (i.e., has a high rate of return) using all three methods. Furthermore, in making the same comparison for the small general service class in the previous rate case, Docket No. E-2, Sub 444, the Commission noted that the SGS class was overpriced in that proceeding. Therefore, the Commission concludes that any increase for the small general service rate class should be less than that proposed by the Company in this proceeding.

On the other hand, a comparison of the rates of return for the small general service class versus the rates of return for overall North Carolina retail service since 1972 (based on the annual cost of service studies filed with the Commission) indicates that the small general service class was overpriced in some years and underpriced in some years.

The Company proposed to increase the rates for SGS class by 14.5% in this proceeding versus a 14.9% increase for North Carolina retail service overall. If the rates for the SGS class were increased 10.8% instead of the proposed 14.4%, it would result in a rate of return which would be within 10% of the North Carolina retail rate of return. The difference between a 14.5% increase and a 10.8% increase for the SGS class is approximately $13,354,000 revenue requirement.

However, the Commission is of the opinion that a $13,354,000 reduction in revenue requirement for the SGS class, in addition to the same percentage reduction applied to the other rate classes as described in Appendix A attached to this order, would be too large for this single proceeding. It would also be an extreme correction in view of the unstable relationship since 1972 between the rates of return for the SGS class and overall North Carolina retail service. The Commission concludes that an additional $3,000,000 reduction in revenue requirement for the SGS class would be appropriate for this proceeding.

Small General Service Schedule SGS Rate Blocks

In its small general service rate schedule SGS, the Company proposes to retain a declining block rate for its energy charge. The declining block rate consists of the middle block (second block) and the tail block (third block). In prior general rate cases, the Commission concluded that multiple rate blocks should be combined and that declining block rates should be eliminated where possible. In this proceeding, the Company proposes to increase the tail block by a considerably larger percentage than the middle block, thereby closing the differential that exists between the middle and the tail block. The Commission concludes that reduction of said differential between the middle and tail blocks is appropriate for this proceeding and should be continued in its future general rate proceedings.

"Closed" Rate Schedules RFS, CSG, CSE, AHS & SCS

In Docket No. E-2, Sub 366, the Commission directed the Company to take steps to withdraw its "closed" rate schedules. Subsequently, in Docket No. E-2, Sub 391, the Company added a proviso to its "closed" rate schedules (RFS, CSG CSE, AHS, SCS and MPS) which requires that a customer serviced under any of the "closed" rate schedules be automatically tranferred to another available rate schedule (probably SGS) whenever the Company determines that the customer would have paid less revenues over the previous 12 months for service under the alternative rate schedule than he actually paid under his current rate schedule.

As a supplement to this proviso, the Company proposed to apply greater than average rate increases to the "closed" rate schedules in each successive rate case. Each time rates for the "closed" rate schedules are increased more than the rates for alternative rate schedules, an additional number of customers will be required to transfer to alternate rate schedules pursuant to the proviso just described. The greater than average increases will continue until all of the customers served under the "closed" rate schedules have been transferred to alternate rate schedules. In this manner, "closed" rate schedule MPS was eventually withdrawn in a prior general rate proceeding.

In this proceeding, the Company proposed to increase the rates for four of the remaining "closed" rate schedules (RFS, CSG, CSE, and AHS) by approximately 24% to 26%, while increasing the rates for the other major rate schedules by approximately 14% to 16%. This is really nothing more than giving the four "closed" rate schedules a 10% increase relative to the other rate schedules. The Commission concludes that the Company's proposed rate increase for the four (4) "closed" rate schedules should be approved.

The Company also proposes to withdraw "closed" rate schedule SCS (shopping center service) in this proceeding as a result of the program described above. The proposal was unopposed and the Commission concludes that it should be approved.

Demand Ratchets and TOD Rates for Large General Service

In its previous general rate order in Docket No. E-7, Sub 444, the Commission noted that voluntary TOD rates were not available to large general service customers unless they had thermal storage equipment, and that the large general service class was the only major class of customers which did not have a voluntary TOD rate available to all of the customers in the class. The Commission further observed that TOD rates might be a reasonable alternative to demand ratchets, and it concuded that the next general rate case should include a discussion of voluntary TOD rates for LGS customers as well as a discussion of alternatives to demand ratchets for LGS customers.

In this proceeding, the Company proposes to replace the present large general service TOD rate schedule (LGS-TS) with a new large general service TOD rate schedule (LGS-TOU). The new rate schedule LGS-TOU will be available on a voluntary basis to all LGS customers.

The proposed new schedule LGS-TOU will include a billing demand ratchet based on the highest of: (1) the current month's demand; or (2) 80% of the maximum on-peak demand during the summer or winter season in the preceding 11 months. None of the Company's other TOD rate schedules (for residential service or small general service) contains a billing demand ratchet. Public Staff witness Turner and DOD witness McCabe proposed to eliminate the ratchet from rate schedule LGS-TOU. The Company also proposes that Customer Generation Service Rider No. 55 be revised to include a billing demand ratchet in conjunction with rate schedule LGS-TOU.

Witness Turner recommended that the demand ratchet not be included in rate schedule LGS-TOU or in Rider No. 55. He gave several reasons for his proposal. First, at the time it was introduced, ratcheting was a peak load pricing mechanism designed to discourage peak demand at the time of system peak or to place the cost of the system peak upon those that caused it. Today, however, in the presence of sophisticated time-of-use metering technology, it is a poor second choice as a peak load pricing mechanism. The ratchet without time-of-use metering increases the demand portion of a customer's bill regardless of when the customer's peak occurred -- on the system's peak or off it. Time-of-use rates by design charges a higher rate per KW for on-peak demand and lower rate for off-peak demand. With properly designed time-of-use rates there is no need for a ratchet. Second, the ratchet allows the Company to present a weakened price signal. This occurs because the ratchet increases the number of billing units that will be divided into the revenue requirement when establishing the unit price. As a result, the ratchet favors those customers who maintain a high load factor and who levelize their demand requirements throughout the year.

Witness Turner further stated that he realized the ratchet grants the Company some measure of revenue stability because it requires customers to pay a fixed amount for demand per month independent of their actual monthly demand. However, he testified that this reason does not justify giving customers incorrect price signals in a time-of-use rate.

Kudzu witness Eddleman opposed the ratchet in either rate form indicating that once the maximum demand is established, there is no incentive to conserve. DOD witness McCabe opposed the ratchet in the LGS Time-of-Use rate but proposed that the ratchet in the standard LGS rate be revised to conform to the seasonal nature of the ratchet proposed by the Company for rate Schedule LGS-TOU. He supported this proposal based on the nature of the summer and winter peaks included in the summer/winter peak and average allocation factor. CIGFUR witness Brubaker, while opposing the SWP&A allocation method, indicated that the demand ratchet was a useful tool and supported its continuation.

Company witness Edge pointed out that to abruptly eliminate the ratchet could cause significant changes in the amount of individual customer's bills with high load factor customers receiving large increases and low load factor customers receiving substantial reductions. Witness Edge also indicated that the ratchet promoted conservation and load management and related the dramatic increase in the number of customers employing load control devices since the implementation of the ratchet. He indicated that the ratchet enabled the Company to recover the fixed costs related to distribution plant in an equitable manner.

The Commission concludes that TOD rates should not include a billing demand ratchet and that the demand ratchet should be eliminated from the proposed Large General Service (time-of-use) rate schedule and from Rider 55, without prejudice to the Company seeking a ratchet at a later date which would recover distribution fixed costs only. However, the Commission also concludes that the Company's billing demand ratchets for its non-TOD large general service customers should remain as they are proposed by the Company. Finally, the Commission concludes that the proposed new rate schedule LGS-TOU, excluding a billing demand ratchet, should be approved as modified.

Coincident Demand Billing for LGS or Wholesale Customers

Another rate design issue addressed by parties in this proceeding is the use of coincident demand for billing purposes for resale (wholesale) customers. Public Staff witness Richard Smith testified that the Company should institute coincident demand billing for its resale customers. DOD witness McCabe suggested that coincident demand billing be applied to DOD customers of the Company. Witness Smith supported his position with the argument that coincident demand billing would provide an incentive for resale customers to reduce their demand at the time of the system peak, thereby reducing that system peak and potentially the need for additional generation facilities in the future. Witness McCabe had the same argument but also presented data which indicated that defense facilities peak at times other than the system peak. Presumably coincident demand billing for DOD would have the effect of reducing their cost.

The Commission has noted the evidence in the record in this case that the Company is presently working with its resale customers in order to establish coincident demand billing for those customers. Although the Commission is concerned about the amount of generating capability that will be required in the future of this Company, it is of the opinion that the Company's dealings with its resale customers on this issue are not within the purview of this Commission.

Concerning the DOD request for coincident demand billing, the Commission notes that allocation of demand related production costs between rate classes has always been based on coincident demands, for reasons discussed extensively in this and prior general rate orders. Furthermore, allocation of demand related costs between customers in a given rate class has always been based on the assumption that customers in the rate class are similar in some respects, and that allocation of such costs by individual maximum demand billing reflects an appropriate distribution of cost responsibility within the class. The Commission, therefore, concludes that it is improper at this time to order a change in the Company's use of individual billing demand.

DOD witness McCabe has raised the issue that the composition of the LGS rate class is inappropriate and recommended that this rate be broken into different categories by voltage levels. He indicates that line losses differ by voltage level of service and that a customer should be responsible only for its specific line losses.

With perfect information, it would be theoretically possible to develop a different rate for each of the utility's customers. However, as a practical matter, it is necessary to group customers with other customers having similar load characteristics in order to have a manageable number of rate schedules for the utility to administer. In this grouping of customers into rate classes, there will inevitably be differences between individual customers within a given rate class. Line losses would potentially be one of the sources of those differences. The Commission is not convinced in this proceeding that this particular example is more worthy of distinction than other potential differences. The Commission is also of the opinion that DOD has available to it the option of applying for service under CP&L's wholesale rates, whereby it would then be grouped with other similarly constituted users of electricity. The Commission, therefore, finds no reason to restructure the LGS rate class.

Sports Field Lighting Service

The Commission has generally attempted to establish rates in prior proceedings which would produce rates of return for each rate class that were within 10% $\pm$ of the overall North Carolina retail rate of return. In comparing the rates of return for each rate class resulting from three of the cost allocation methods discussed herein (summer/winter coincident peak, summer/winter peak and base, summer/winter peak and average), the Commission notes that the sports field lighting class is underpriced (i.e., has a low rate of return) using all three methods. However, the Commission also notes that said low rates of return occur even after a 21.4% increase proposed by the Company in this proceeding for the rate class versus a 14.9% increase proposed for North Carolina retail service overall. Therefore, the Commission concludes that the rates proposed for rate schedule SFLS (Sports Field Lighting Service) should be reduced by the same percentage as the other rates proposed by the Company, in the manner described on Appendix A attached to this order.

General

In addition to those revisions already discussed herein, the Company proposes various miscellaneous rate changes, administrative changes, and clarifications on its rate schedules and in its terms and conditions for

service which were not opposed by any party. Such changes and clarifications include in part: provisions to list base fuel costs on tariffs and riders; provisions to exclude availability of residential rate schedules from service which is metered separately from residence; provisions to restrict availability of Rider 7 (Standby Service) to retail rate schedules only; provisions to add a customer charge during non-usage months for service under Rider 5 (Seasonal Service); provisions to increase off-peak demand charges for service under Rider 55 (Customer Generation); provisions to include power factor adjustments on LGS Tariffs for clarity; provisions to increase the attractiveness of Rider 5 (Curtailable Load); provisions to add a new 5800 lumen S.V. fixture to the lighting rate schedules; and provisions to restrict 12,000 and 38,000 lumen S.V. Retrofit fixtures to existing applications only.

OTHER CONCLUSIONS ON RECONSIDERATION

The Commission recognizes that the annual gross revenue increase reflected herein of $91,211,000 exceeds by $356,000 the annual gross revenue increase established by the Commission's Order Granting Partial Increase in Rates and Charges issued September 19, 1983. However due to the lack of materiality of such an increase in revenue requirements relative to the Company's total revenue requirements (less than .0003) the Commission finds it reasonable for CP&L to maintain without change the rates and charges which became effective on September 19, 1983. The Commission recognizes, however, that it will be necessary for CP&L to file revised tariffs reflecting the new base fuel component established herein.

The Commission concludes that the rate designs, rate schedules and terms and conditions for service as proposed by the Company should all be approved, except as discussed herein.

IT IS, THEREFORE, ORDERED as follows:

1. That Carolina Power & Light Company shall maintain without change the rates and charges established by this Commission in its Order Granting Partial Increase in Rates and Charges issued September 19, 1983; however, the Company shall file with this Commission five (5) copies of rate schedules reflecting the revised base fuel component established herein.

2. That Carolina Power & Light Company shall prepare cost allocation studies for presentation with its next general rate application which allocate production plant based on the following methodologies: (1) summer/winter peak and average; (2) summer/winter peak and base; (3) summer/winter coincident peak; (4) summer coincident peak; and (5) summer peak and average. Both jurisdictional and fully distributed cost allocation studies shall be made using each method, and the studies shall be included in items 31 and 37, respectively, of Form E-1 of the minimum filing requirements for general rate applications.

3. That Carolina Power & Light Company work with the Public Staff during the six (6) months following the date of this Order to develop a mutually agreeable study which could be done at a reasonably limited cost and would be responsive to the concerns discussed in this proceeding regarding: (1) allocation of fixed costs and variable costs to each hour of the year, and (2) allocation of costs incurred during a given hour to customer classes based on usage during the given hour. The Company shall report to the Commission on

the details of the study from time to time as necessary, but not later than six (6) months following the date of this Order.

4. That Carolina Power & Light Company shall take the steps necessary to reduce the on-peak hours for residential TOD rate schedule R-TOU during the summer months from 10:00 p.m. to 9:00 p.m. effective April 1, 1984, as discussed herein.

5. That any motions heretofore filed in this proceeding and not previously ruled upon are hereby denied.

6. That CP&L shall seek to obtain a ruling from the IRS regarding the tax consequences of possible rate-making treatments of the Job Development Investment Tax Credits relating to that portion of the generating and transmission plant sold to NCEMPA. The Company shall file within thirty (30) days from the date of this Order a draft of the Company's proposed letter to the IRS requesting a ruling on the matter for review by the Commission and Public Staff. The Company shall obtain approval of the Commission prior to submitting the request for ruling to the IRS. The resultant ruling or finding of the IRS or the current status of the matter shall be presented to the Commission in CP&L's next general rate proceeding.

ISSUED BY ORDER OF THE COMMISSION.
This the 7th day of December 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sharon Credle Miller, Deputy Clerk

DOCKET NO. E-7, SUB 338

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Application by Duke Power Company for Authority to Adjust and Increase Its Electric Rates and Charges) ORDER UPON RECONSIDERATION

BY THE COMMISSION: On November 4, 1982, Duke Power Company (Duke) filed a motion requesting that the full Commission reconsider and alter or amend its Order of November 1, 1982, entered in this docket (E-7, Sub 358) with respect to Decretal Paragraph 16 appearing on page 147 of said Order and the related findings and conclusions and in support thereof offered the following justification(s):

> "1. On December 21, 1981, the full Commission in Docket No. E-7, Sub 331 entered its Order authorizing and approving Duke Power Company's proposal:
>
> > 'To issue a maximum of 3,750,000 shares of the Company's common stock without nominal or par value during December of 1981 in exchange for certain of the Company's First and Refunding Mortgage Bonds not to exceed $125,000,000 principal amount to be purchased on the open market by Salomon Brothers at a composite weighted average price of 55 to 70 percent of the principal amount of such bonds...'"

"The Commission further ordered that:

> 'The accounting methods and entries as set forth in the Application reflecting the results of and recording of the transaction are hereby authorized, approved and directed as submitted including specifically the inclusion of the stock (at market value) and the nonoperating extraordinary gain in common equity on the books and records of the company.' (Emphasis added)"

On November 9, 1982, the North Carolina Textile Manufacturers Association, Inc. (NCTMA) filed its response in opposition to Duke's Motion for Reconsideration. On November 15, 1982, Great Lakes Carbon Corporation and the Public Staff filed responses to Duke's Motion for Reconsideration and on December 1, 1982, the Kudzu Alliance filed exceptions to the Commission Order entered in this docket which, in part, relate to Duke's Motion for Reconsideration. By Order issued on December 6, 1982, the Commission set this matter for hearing on January 10, 1983, at 11:00 a.m. in Room No. 217, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina. On December 13, 1982, Great Lakes Carbon Corporation requested that the Commission issue an Order clarifying its Order Scheduling Hearing, issued in this docket on December 6, 1982. On December 22, 1982, the North Carolina Attorney General filed Notice of Intervention. On December 23, 1982, the Commission issued an Order clarifying its Order of December 6, 1982. On January 10, 1983, Great Lakes Carbon Corporation filed its brief on rehearing and the hearing in this regard came on as scheduled.

The Commission after having very carefully considered oral argument heard on January 10, 1983, and the entire evidence of record presented in this docket relating to the debt/equity swap, and after having carefully considered the Commission Order issued on December 21, 1981, in Docket No. E-7, Sub 331, and the Panel's Order of November 1, 1982, concludes that Duke's motion filed on November 4, 1982, should be allowed. The Commission believes that its decision in this regard is fully supported by the evidence and is consistent with the Commission's decision in Docket No. E-7, Sub 331. Duke contends that it would not have proceeded with the transaction had the Commission not approved its proposed accounting treatment of the extraordinary gain arising from the debt/equity swap. The Commission recognizes that such approval in no way obviated the need for subsequent evaluation of the propriety of the transaction nor foreclosed the appropriate rate-making treatment to be accorded the transaction in Duke's next rate case. The Commission stated that the appropriate rate-making treatment contemplated by the Commission's Order of December 21, 1981, would involve either an adjustment to the required return on equity and/or an adjustment to capital structure.

Based upon consideration of the evidence, oral argument, and briefs, the Commission concludes that the transaction was beneficial to both the Company and its customers because Duke's financial position was improved significantly. Improvement of Duke's common equity capitalization should result in greater times coverage of its fixed interest charges, thereby tending to lower its cost of capital. The Commission therefore concludes that Decretal Paragraph 16 and related findings and conclusions should be rescinded.

The Panel's decision reduced Duke's annual revenue requirement by approximately $5.9 million dollars to reflect amortization of the gain

realized from the debt/equity swap. Since the findings and Decretal Paragraph relating to this matter have now been rescinded, if Duke is to be allowed the same annual revenue requirement as approved by the Panel, the Commission concludes that it should make an adjustment to the cost of equity from 15.5% to 15.22%. The overall rate of return previously found fair by the Panel of 11.98% is thus reduced to 11.86%. Thus, the return on common equity has been reduced by an amount such that the increase in Duke's gross revenue requirement arising from the accounting treatment accorded the debt/equity swap herein is exactly off-set by a decrease in said revenue requirement related to the reduction in the return on common equity. After modification as described above Duke will be afforded an opportunity to earn a 15.22% return on its common shareholder equity devoted to its North Carolina retail operations based upon rates previously approved by the Commission in this Docket.

IT IS, THEREFORE, ORDERED THAT:

Decretal Paragraph 16 of the Commission Order of November 1, 1982, issued in this docket and the related findings and conclusions be and hereby are rescinded, and the Order modified consistent with the above findings.

ISSUED BY ORDER OF THE COMMISSION.
This the 13th day of January 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sandra J. Webster, Chief Clerk

COMMISSIONER HIPP CONCURRING (OPINION ATTACHED)
COMMISSIONER WINTERS DISSENTING (OPINION ATTACHED)
COMMISSIONER HAMMOND DISSENTS

HIPP, COMMISSIONER, CONCURRING. I concur in the Order issued today to emphasize the importance of the continued ability of North Carolina utilities to finance essential construction programs needed to render adequate service to the public in the future. I dissented from the debt/equity swap order, Docket No. E-7, Sub 331, partly because of the difficulties of implementation, as illustrated in this case. But the securities approved there have been issued, and there must be finality to securities dockets. The intervenors have raised questions regarding the need for additional construction, and this requires extremely careful consideration.

Even under the latest reduction in projected load growth to 2.8% annual growth, Duke will not have adequate reserves to serve North Carolina consumers in the 1990s unless it completes the plants presently included in the construction program. This includes McGuire 2 in 1983, Catawba 1 and 2 in 1985 and 1987, respectively, Cherokee 1, planned for 1990, and the Bad Creek Pumped Storage Plant, planned for 1990 and 1991. It is true that Cherokee 1 and the Bad Creek Pumped Storage projects have been placed on an unscheduled status due, in part to present financial conditions and the uncertain duration of the present recession, but, if North Carolina is to recover from this recession, its industries must resume full employment and adequate electric power must be available when needed.

The load forecast proceeding set for hearing later this year will explore and investigate the latest load growth projections, but until it is completed it is essential to maintain the ability to finance this construction when

needed. This may well require the sale of new debt and equity, and will require full faith and credit and full confidence of prospective capital sources in the North Carolina regulatory process. The amendment and modification approved in this Order is needed to preserve the intent and purpose of the financing plan approved in Docket No. E-7, Sub 331, on December 21, 1981. That Order provided that Duke's next general rate case would fully examine the adjustments warranted on return on equity and to establish a pro forma capital structure, which is accomplished by these modifications to the general rate case Order while leaving intact the accounting methods and entries which were approved in that securities docket. G.S. 62-160, et seq., covering securities regulation under the Public Utilities Act carefully provides for the sanctity of securities issued under that article of the Act, and requires high priority of disposition and handling by the Commission, including the provision in G.S.62-170(b) that the terms and conditions of such securities shall not be affected by regulation of the Commission and other matters preceding such an Order or supplemental thereto.

This amendment and modification to the Order fully protects the benefits authorized in the securities Order and granted to the ratepayers in the original rate case Order, while still preserving the essential full faith and credit of the securities Orders needed for future construction of plants needed to serve the public in North Carolina.

Edward B. Hipp, Commissioner

WINTERS, COMMISSIONER, DISSENTING: I respectfully dissent from the majority Order rescinding the rate-making treatment accorded the gain realized from the debt/equity swap as previously established by Commission Order of November 1, 1982. If the Panel's decision is to be reconsidered and its findings and conclusions relating to the extraordinary gain realized from the debt/equity swap are to be rescinded, I would adopt in lieu thereof the cost of equity capital of 15.22% utilized by the majority in its instant decision; however, I would also adopt the capitalization ratios and the related embedded cost of debt and preferred stock recommended by the Public Staff. Such a modification in the cost of common equity capital is .28% less than the 15.5% return on common equity capital allowed Duke Power Company by the Panel Order issued on November 1, 1982. My proposal would decrease the increase approved in this docket by approximately $11.6 million or from $61.7 million to $50.1 million. Such a reduction in the Company's revenue requirement is modest in view of the significant financial benefits which proponents expect to enure to the Company as a result of the debt/equity swap having been approved by a majority of the Commission. It is noted that the capitalization ratios and the related embedded cost of debt and preferred stock used by the Commission in all aspects of this matter were those sought exclusively by the Company. With respect to use of the Company's proposed capitalization ratios and embedded cost of debt and preferred stock by the Panel in its Order of November 1, 1982, such use came about only after each member of the Panel having made significant compromises with respect to other issues affecting the companies revenue requirement. Such issues included other aspects of the Applicant's case affecting its cost of capital. It was my initial position prior to compromise that the Public Staff's position with respect to capitalization ratios and related costs rates was most appropriate for use by the Commission. As a result of the majority having disturbed such compromises without giving appropriate weight to the capitalization ratios and

embedded cost rates, I can no longer be bound by my earlier commitments. I, therefore, vigorously dissent from the majority's action in this regard.

John W. Winters, Commissioner

DOCKET NO. E-7, SUB 358

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Application by Duke Power Company for Authority to Adjust and Increase Its Electric Rates and Charges) ORDER APPROVING PARTIAL RATE INCREASE

HEARD IN: Courtroom, City Hall, 145 5th Avenue, East, Hendersonville, North Carolina, on August 1, 1983; Commissioners' Board Room, Fourth Floor, County Office Building, 720 East Fourth Street, Charlotte, North Carolina, on August 2, 1983; Courtroom 5-D, Forsyth County Hall of Justice, Liberty Street, WinstonSalem, North Carolina, on August 3, 1983; Courtroom 2-A, Guilford County Courthouse, No. 2 Governmental Plaza, Greensboro, North Carolina, on August 3, 1983; Council Chambers, City Hall, 101 City Hall Plaza, Durham, North Carolina, on August 4, 1983; and Commission Hearing Room, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina, on August 16 - 19, and August 22 - 25, 1983

BEFORE: Commissioner Douglas P. Leary, Presiding; and Commissioners Sarah Lindsay Tate and A. Hartwell Campbell

APPEARANCES:

For Duke Power Company:

Steve C. Griffith, Jr., Senior Vice President and General Counsel, William L. Porter, Associate General Counsel, and George Ferguson, Vice President and Deputy General Counsel, Duke Power Company, 422 South Church Street, Charlotte, North Carolina 28242

Clarence W. Walker, Kennedy, Covington, Lobdell & Hickman, Attorneys at Law, 330 NCNB Plaza, Charlotte, North Carolina 28280

For the Public Staff:

Paul L. Lassiter and Vickie L. Moir, Staff Attorneys, Public Staff, North Carolina Utilities Commission, P.O. Box 991, Dobbs Building, Raleigh, North Carolina 27602
For: The Using and Consuming Public

For the Attorney General:

Karen E. Long and Steven F. Bryant, Assistant Attorneys General, North Carolina Department of Justice, P.O. Box 629, Raleigh, North Carolina 27602

For: The Using and Consuming Public

For the Intervenors:

Thomas R. Eller, Jr., Attorney at Law, P.O. Drawer 27866, Raleigh, North Carolina 27612
For: North Carolina Textile Manufacturers Association, Inc.

Sam J. Ervin, IV, Byrd, Byrd, Ervin, Blanton, Whisnant and McMahon, P.A., Attorneys at Law, P. O. Drawer 1269, Morganton, North Carolina 28655
For: Great Lakes Carbon Corporation

M. Travis Payne, Edelstein & Payne, Attorneys at Law, P.O. Box 12643, Raleigh, North Carolina 27605
For: Kudzu Alliance

Carson Carmichael III, Bailey, Dixon, Wooten, McDonald & Fountain, Attorneys at Law, P.O. Box 2246, Raleigh, North Carolina 27602
For: Carolina Industrial Group for Fair Utility Rates

F. Kent Burns, Boyce, Mitchell, Burns & Smith, Attorneys at Law, P.O. Box 479, Raleigh, North Carolina 27602
For: Public Service Company of North Carolina, Inc.

BY THE COMMISSION: On February 1, 1983, Duke Power Company (Applicant, Company, or Duke) filed an application with the North Carolina Utilities Commission seeking authority to adjust and increase electric rates and charges for its retail customers in North Carolina. Said application seeks rates that produce approximately $112,884,000 of additional annual revenues from the Company's North Carolina retail operations when applied to a test period consisting of the 12 months ended September 30, 1982, an approximate 7.68% increase in total North Carolina retail rates and charges. The Company requested that such increased rates be allowed to take effect for service rendered on and after March 3, 1983. The principal reasons set forth in the application as necessitating the requested increase in rates were: (1) expenditures for construction work in progress applicable to McGuire Nuclear Station Unit 2 since December 31, 1981; (2) the cancellation of Cherokee Nuclear Station Units 2 and 3; (3) increased operating expenses and increased fuel expense; and (4) investment in additional plant not reflected in current rates.

This docket was established with the Commission on December 30, 1982, by Duke's filing of a letter of intent to file an application for a general increase in rates as is required by the provisions of Commission Rule R1-17(a). Moreover, on January 17, 1983, Duke filed a request for waiver of certain of the Commission's filing requirements applicable to general rate increase applications by electric utilities. The Public Staff filed on January 21, 1983, its Letter of Concurrence regarding Duke's requested waiver. On January 25, 1983, the Commission issued its Order specifying which filing requirements would be waived or delayed.

On February 22, 1983, Great Lakes Carbon Corporation filed its Petition to Intervene and Protest. By its Order of February 28, 1983, the Commission allowed that request to intervene.

On February 28, 1983, Duke filed Affidavits of Publication of the notice regarding its application as required by Commission Rule R1-15(1).

On March 2, 1983, the Commission issued an Order declaring Duke's application to be a general rate case pursuant to G.S. 62-137, suspending Duke's proposed rates pursuant to G.S. 62-134 for a period of up to 270 days from the proposed effective date of such rates, scheduling public hearings on the application, establishing the test period, and requiring Duke to give public notice of its application and the hearings scheduled by the Commission.

On March 8, 1983, there was filed in this docket the Petition of Public Service Company of North Carolina, Inc., to Intervene. By Commission Order of March 11, 1983, that request to intervene was allowed.

On March 11, 1983, there was filed in this docket a Petition to Intervene and Participate by the North Carolina Textile Manufacturers Association, Inc. (NCTMA). By Commission Order of March 17, 1983, that request to intervene was allowed.

On May 3, 1983, there was filed in this docket a Petition to Intervene by Kudzu Alliance. By Commission Order of May 16, 1983, that request to intervene was allowed.

On June 22, 1983, there was filed in this docket a Petition to Intervene by Carolina Industrial Group for Fair Utility Rates (CIGFUR). By Commission Order of July 5, 1983, that request to intervene was also allowed.

On July 14, 1983, Duke filed its affidavits of publication of newspaper notice and affidavit of notice by bill insert evidencing that public notice had been given as required by the Commission in its Order issued March 2, 1983.

The Commission, on its own motion, issued an Order on July 5, 1983, scheduling an initial pretrial conference. On that same date, a Motion for Discovery was filed on behalf of Kudzu Alliance to the Company requesting information preparatory to testimony filings. On July 13, 1983, the Kudzu Alliance filed an Amendment to the Motion for Discovery.

On August 4, 1983, there was filed in this docket a Petition to Intervene on behalf of American Cyanamid Corporation, and by Commission Order dated August 11, 1983, that request to intervene was allowed.

Both the Public Staff and the Attorney General intervened in the case by either filing a formal petition and/or by appearing at the hearings. The interventions of the Public Staff and Attorney General are deemed recognized.

On August 11, 1983, Duke filed in Docket No. E-7, Sub 338 (Duke's last general rate case), a proposed extra facilities charge tariff. On August 12, 1983, the Attorney General filed a motion to strike the extra facilities charge filing in Docket No. E-7, Sub 338, and to require that the proposed extra facilities charge tariff be filed in this docket. On that same date, NCTMA filed a motion requesting that the two dockets be consolidated for the purpose of determining the extra facilities charge tariff. The Commission by

Order issued August 15, 1983, denied the two motions and set the extra facilities charge tariff for hearing at another time.

As a result of the August 5, 1983, prehearing conference, the Commission on August 15, 1983, issued a Pretrial Order.

Prior to and during the course of the hearings, motions were made and orders were issued relating thereto, all of which are a matter of record. Additionally, pursuant to various Commission Orders or requests, also of record, various parties were directed or permitted to file and serve certain late exhibits, either during or subsequent to the hearings held in this matter.

Public hearings were held as scheduled by the Commission for the specific purpose of receiving testimony from public witnesses. The following persons appeared and testified:

Hendersonville - Charles Lankford, James Lamberson, Paul Welch, Joseph Oates, Ansley Cope, L.T. Arvidson, William Lapsley, D.O. Thompson, Jr., and Carl Summey.

Winston-Salem - Lee Fay Mack, Lewis Overby, Herschel Redding, Carlos Falk, L.E. Stopper, D. Kelly Almond, Ila Kreeger, John D. Potter, Henry Drexler, William E. Lanford, Mozelle Gibbs, Lorraine Ashburn, Gray Jackson, Betsy Sawyer, and C.E. Robertson.

Durham - Walter Cain, James Tabron, Jane Gaede, J.B. Carlyle Wooten, Robert Brinkmeyer, Norma Cone, Alan Rimer, John Anderson, Janet Irons, Paul Luebke, Elisa Wolper, John Kay, Amy DeHart, C.E. Boulware, Gertrude Cheek, Geoffry Wyckoff, Howard Sherman, Ben Edwards, Johnny Williams, Elena Yott, Lee Barner, Larry Colbert, George Rowe, and Laura Drey.

Greensboro - C.E. Conley, Annie Wagstaff, Ada J. Hooker, George Blair, John Timberlake, David Hill, Hilda Knowles, H.L. Simpson, and Angeline Smith.

Charlotte - H. Y. Kinard, Jim Thomasson, Clifton G. Turner, Ben Vernon, Jack M. Goodnight, Charles A. Hunter, G.B. Bailey, James M. Nolan, Tom Huggins, S.R. Buie, C.R. Tolleson, C.W. Brewer, Jr., Baxter E. McIntosh, Betsy Levitas, Henry Dameron, Marian Priesler, Robert Stegoll, Wilson Maxwell, Vernon Teal, Steven Levitas, Johnny Polk, Mabel Mitchell, and Stephen Rhodes.

Raleigh - Christopher Scott and Jane Sharp.

As previously ordered, the case in chief came on for hearing in Raleigh on August 16, 1983. The Applicant presented the testimony and exhibits of the following witnesses:

1. William S. Lee, Chairman of the Board and Chief Executive Officer of Duke (direct testimony);

2. Dr.Charles E. Olson, President of Olson & Company, Inc. (direct testimony);

3. William R. Stimart, Vice President, Regulatory Affairs of Duke (direct and rebuttal testimony);

4. Richard LaCapra, President of LaCapra Associates (direct testimony);

5. M.T. Hatley, Jr., Vice President, Rates of Duke (direct testimony);

6. John F. Utley, National Director, Regulated Business Practice, Deloitte Haskins & Sells (direct testimony);

7. Dr. Edward W. Erickson, Professor of Economics and Business, North Carolina State University (rebuttal testimony); and

8. Donald M. Jenkins, Manager of Rate Research and Development in the Rate Department of Duke (rebuttal testimony).

The Public Staff presented the testimony and exhibits of the following witnesses:

1. Dennis J. Nightingale, Director of the Electric Division of the Public Staff;

2. Thomas S. Lam, Engineer with the Electric Division of the Public Staff;

3. Richard N. Smith, Engineer with the Electric Division of the Public Staff;

4. James Hoard, Accountant with the Accounting Division of the Public Staff;

5. Dr. Caroline M. Smith, Senior Consultant, J.W. Wilson and Associates, Inc., Washington, D.C.; and

6. Benjamin R. Turner, Jr., Engineer with the Electric Division of the Public Staff.

The Intervenor, Kudzu Alliance, presented the testimony and exhibits of Wells Eddleman.

The Intervenor, Carolina Industrial Group for Fair Utility Rates, presented the testimony and exhibits of Nicholas Phillips, Jr., Consultant with the firm of Drazen-Brubaker and Associates, Inc.

Based upon the verified application, the testimony and exhibits received into evidence at the hearings, and the record as a whole of these proceedings, the Commission now makes the following

FINDINGS OF FACT

1. Duke is engaged in the business of developing, generating, transmitting, distributing, and selling electric power and energy to the general public within a broad area of central and western North Carolina, with its principal office and place of business in Charlotte, North Carolina.

2. Duke is a public utility corporation organized and existing under the laws of the State of North Carolina and is subject to the jurisdiction of this Commission. Duke is lawfully before this Commission based upon its application for a general increase in its North Carolina retail rates and charges pursuant to the jurisdiction and authority conferred upon the Commission by the Public Utilities Act.

3. The test period for purposes of this proceeding is the 12-month period ended September 30, 1982, adjusted for certain known changes based upon circumstances and events occurring up to the time of the close of hearings in this docket.

4. By its application, Duke sought rates to produce jurisdictional revenues of $1,583,484,000 based upon a test year ending September 30, 1982. Revenues under present rates, according to the Company were $1,470,600,000, thereby necessitating an increase of $112,884,000.

5. The overall quality of electric service provided by Duke to its North Carolina retail customers is adequate.

6. The summer coincident peak method as discussed herein is the most appropriate method for making jurisdictional cost allocations and for making fully distributed cost allocations between customer classes in this proceeding. Consequently, each finding of fact appearing in this Order which deals with the overall level of rate base, revenues, and expenses for North Carolina retail service has been determined based upon the summer coincident peak cost allocation method.

7. Duke Power Company should be allowed to recover its abandonment loss sustained as the result of the Company's having terminated construction on, and having abandoned, its Cherokee nuclear generating units 1, 2 and 3. Recovery of the Company's reasonable and prudent investment in those units should be over a 10-year amortization period. It is neither fair nor reasonable to include any portion of the unamortized balance of this investment in rate base, and no adjustment which would have the effect of allowing the Company to earn a return on the unamortized balance of this investment should be allowed.

8. Duke Power Company should be allowed to continue the recovery of its prudently incurred abandonment loss sustained as the result of the Company's having terminated construction on, and having abandoned, its Perkins nuclear generating project in the manner previously authorized by the Commission in Docket No. E-7, Sub 338. Thus, it is fair and reasonable to allow Duke to continue to recover its reasonable and prudent investment in its cancelled Perkins station over a five-year amortization period without the inclusion of the unamortized balance of that investment in rate base. Further, no adjustment which would have the effect of allowing the Company to earn a return on the unamortized balance of this investment would be reasonable for rate-making purposes.

9. A base fuel component of 1.3734¢ per kWh excluding gross receipts tax is appropriate for this proceeding, reflecting a reasonable base fuel cost of $408,542,000 for North Carolina retail service.

10. An $84,604,000 working capital allowance for fuel inventory is appropriate for North Carolina retail service in this proceeding, consisting of $81,482,000 for coal inventory and $3,122,000 for fuel oil inventory.

11. The reasonable allowance for working capital and deferred debits and credits is $190,086,000.

12. Duke's reasonable original cost rate base used and useful in providing service to the public within the State of North Carolina is $2,548,596,000; consisting of electric plant in service of $3,640,170,000, reasonable and prudent expenditures for construction work in progress of $282,481,000, and allowance for working capital of $190,086,000, reduced by accumulated depreciation of $1,263,605,000, accumulated deferred income taxes of $289,937,000, and operating reserves of $10,599,000. Inclusion of $282,481,000 of reasonable and prudent expenditures for CWIP in Duke's rate base is in the public interest and is necessary to the financial stability of the Company.

13. The appropriate gross revenues for Duke for the test year, under present rates and after accounting and pro forma adjustments, are $1,470,600,000.

14. The reasonable level of test year operating revenue deductions for the Company after normalized and pro forma adjustments is $1,205,203,000.

15. The reasonable capital structure to be employed as a basis for setting rates in this proceeding is composed as follows:

Item	Percent
Long-term debt	47.0%
Preferred stock	13.0%
Common equity	40.0%
Total	100.0%

16. The Company's proper embedded costs of debt and preferred stock are 9.83% and 8.62%, respectively. The reasonable rate of return for Duke to be allowed to earn on its common equity is 15.25%. Using a weighted average for the Company's costs of long-term debt, preferred stock, and common equity, with reference to the reasonable capital structure heretofore determined, yields an overall fair rate of return of 11.84% to be applied to the Company's original cost rate base. Such rate of return will enable Duke, by sound management, to produce a fair return for its shareholders, to maintain its facilities and service in accordance with the reasonable requirements of its customers, and to compete in the market for capital funds on terms which are reasonable and fair to customers and existing investors.

17. Based upon the foregoing, Duke should increase its annual level of gross revenues under present rates by $76,235,000. The annual revenue requirement approved herein is $1,546,835,000, which will allow Duke a reasonable opportunity to earn the rate of return on its rate base which the Commission has found just and reasonable. The revenue requirement approved herein is based upon the original cost of Duke's property used and useful in providing service to its customers and its reasonable test year operating revenues and expenses as previously set forth in these findings of fact.

18. The Company should not be required to offer to reset the thermostats on controlled water heaters at this time.

19. The Company should make a detailed study of the matter of including minimum efficiency standards for heat pumps and central air conditioners in the requirements for residential rate schedule RC(NC).

20. Volunteer organizations who promote and install weatherization for customers under the Company's low income weatherization program should not be required to promote and sign up customers for the Company's water heater and air conditioner load control program.

21. The rate blocks in all major rate schedules should be flattened.

22. The summer/winter differential in the residential rate schedules should be held at the levels contained in the present rates.

23. The Hopkinson type demand charge in the major nonresidential rate schedules should be increased to the levels proposed by the Company.

24. The rate designs and rate schedules proposed by the Company, except for the modifications thereto as described herein, are appropriate and should be adopted.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 1, 2, 3 AND 4

The evidence for these findings of fact is contained in the verified application, the Commission's files and records regarding this proceeding, the Commission Order setting hearing, and the testimony of Company witness Stimart and Public Staff witness Hoard. These findings of fact are essentially informational, procedural, and jurisdictional in nature and are, for the most part, uncontested.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 5

The evidence for this finding of fact is found in the testimony of Company witness Lee and the various public witnesses who appeared at the hearings in Hendersonville, Charlotte, Winston-Salem, Greensboro, Durham, and Raleigh. The Commission notes that the record contains little, if any, evidence which would even suggest any problems with respect to the adequacy of Duke's service. A careful consideration of all the evidence relating to this issue leads the Commission to conclude that the quality of service being provided by Duke to its retail customers in North Carolina is adequate.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 6

Company witnesses Hatley, LaCapra, and Jenkins; Public Staff witness Turner; Carolina Industrial Group for Fair Utility Rates (CIGFUR) witness Phillips; and Kudzu Alliance witness Eddleman presented testimony and evidence regarding the proper cost allocation methodology.

The Company provides retail service in two states as well as wholesale service. For this reason, it is necessary to allocate the cost of service among jurisdictions and among customer classes within each jurisdiction.

In previous rate cases in North Carolina, the Company has used the summer coincident peak (summer CP) method for cost allocations. The Company also proposes to utilize the same method for this proceeding. The summer CP method allocates 100% of production plant (and related expenses) based on summer peak responsibility.

Company witness LaCapra stated that the summer CP method reflects the most critical demand on the system, which is the summer peak when loads are most volatile and least manageable and when equipment (plant) ratings are reduced. He also insisted that the Company has not constructed any of its plants to save energy and that every plant was constructed to meet the peak demand.

Witness LaCapra pointed out that selection of an allocation method should reflect the planning criteria of the system and that the system was planned to meet the need for capacity at the time of the summer peak. He contended that evaluation of the type of new capacity needed was only slightly concerned with the system load factor, although he did recommend that duration of demand not be ignored. In fact, he acknowledged that duration of demand should be incorporated into the allocation method, but he contended that the summer CP method does recognize the duration of demand.

Company witness Hatley pointed out that the Company has used the summer CP method for many years, and he concluded that its use has resulted in balanced peak loads in summer and winter. Witness Jenkins testified that the winter peak was an induced peak encouraged by the Company's electric heating program and that the summer peak was a natural peak caused primarily by the air conditioning load. Witness Jenkins pointed out that the summer CP method was used for Duke by the South Carolina Public Service Commission, and that the Catawba agreements specify the summer CP method for allocating plant. He also cited the three criteria for sound rate design (in Bonbright, Principles of Public Utility Rates, 1961) as: (a) producing a fair rate of return, (b) based on cost of service, and (c) promoting economically justified use and discouraging wasteful use; and he contended that the Public Staff's proposals do not meet the criteria.

Public Staff witness Turner recommends the summer/winter peak and base method (S/W P&B) for the assignment of costs to both the North Carolina retail jurisdiction and customer classes. The S/W P&B method allocates 70% of production plant (and related expenses) based on an average of summer and winter peak responsibility and allocates the remaining 30% of production plant (and related expenses) by average demand or energy.

Witness Turner explained that the allocation method should recognize the winter peak because the Company's winter peak has a very significant load. He pointed out that the winter peak has frequently exceeded the summer peak and should be recognized as a factor in the assignment of demand related costs. The S/W P&B method does this by giving equal weight to both peaks.

Witness Turner explained that a portion of production plant should be allocated by energy because the duration of time over which a plant must maintain a given load is as important a design factor as the capacity (KW) of the plant. The Company has three different types of plant upon which it can call to meet demand: base, intermediate, and peaking. The base plant is designed to operate for long periods of time and typically is high in capital cost and low in operating cost. The peaking plant is designed to operate for short periods of time (usually at the time of system peak) and typically is low in capital cost and high in fuel cost. Witness Turner contended that, if demand was the only design consideration, the Company would construct only peaking units and that it builds the higher capital cost base load units when the units must be capable of operating during a high percentage of the hours in a year.

Witness Turner stated that the summer/winter peak and base method for rate design purposes may be unfair to certain customer classes because, in his opinion, it does not recognize the possibility that the costs of fuel may vary among classes. For example, if a particular customer class is assigned base load plant costs, witness Turner contended that it should also be assigned the lower fuel costs associated with the base load plant. Conversely, if a class is assigned primarily peaking plant costs, witness Turner contended that it should also be assigned the higher fuel costs associated with the peaking plant.

To solve this problem, witness Turner recommended that the Commission direct the Company to make a study of the steps required to determine plant and fuel cost by hour of day for a 12-month period by customer class, and that the Company proceed with said study and report on its progress to the Commission and to the Public Staff every six months until the study is completed.

Company witness Jenkins opposed a study to determine the fixed costs and variable costs which are incurred during each hour of the year, contending that such a study would not be useful and would cost too much.

CIGFUR witness Phillips testified that the peak responsibility method should be used to allocate all production plant costs, and that the preferable peak responsibility method is either summer CP or summer/winter CP. He based his recommendation on the assumption that production plant costs are fixed costs, and that fixed costs are demand related.

Kudzu witness Eddleman recommended the summer/winter CP method for allocating production plant costs. The intervenor NCTMA also recommended the summer/winter CP method, while the intervenor Great Lakes Carbon recommended the summer CP method.

The Commission is of the opinion that it should adopt the summer CP method for allocating costs in this proceeding. However, in view of the continuing discussion of cost allocation methodology, it is further of the opinion that it should require at least several of the cost allocation methodologies to be utilized by the Company in its next general rate application. Finally, the Commission is of the opinion that the problem of cost allocations might be resolved or at least greatly alleviated by means of a cost allocation study which assigns both fixed costs and variable costs to each of the 8,760 hours of the year. Such a study could also resolve the problem of determining appropriate cost differentials between summer usage versus winter usage and between on-peak usage versus off-peak usage as discussed elsewhere herein.

The Commission concludes that the Company should be required to work with the Public Staff to develop a study which would be responsive to the concerns discussed herein and would be a reasonable undertaking from a cost and a technical standpoint. The study might assign costs to the hours during which these costs were incurred by utilizing a normalized generation mix and normalized dispatch of generating units, and the study might allocate the costs during a given hour (or hours) to customer classes based on their usage during the given hour.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 7 AND 8

Company witnesses Lee, Stimart, and Utley, Public Staff witness Hoard, and Kudzu Alliance witness Eddleman offered testimony concerning the proper rate-making treatment for the Company's abandoned Cherokee Units 1, 2, and 3.

Company witness Lee testified as to the decision to construct and later cancel Cherokee Units 1, 2, and 3. Company witness Stimart proposed that the loss be amortized over 10 years to the cost of service with an allowance for the ongoing interest and preferred dividend costs associated with the unrecovered balance. Witness Stimart's recommended approach would levelize the annual amortization of the loss and the related interest and preferred dividend costs in a manner similar to a typical fixed-term home mortgage. Witness Stimart offered an alternative position on the loss in his rebuttal testimony of a 10-year amortization with no allowance for any costs of debt, preferred, or common equity.

Company witness Utley proposed that the Commission permit the Company to recover the Cherokee property abandonment costs over a reasonable period of time along with recovery of all associated costs on the unamortized balance. As an alternative to this full recovery option, he stated that he believed that Company witness Stimart's alternate proposal set forth in his rebuttal testimony represented a reasonable partial recovery technique.

Public Staff witness Hoard recommended that the loss be amortized to the cost of service over 12 years without a return on the unamortized balance. Witness Hoard testified that Public Staff counsel had advised him that it would be illegal to allow the Company to include the unamortized balance in rate base since it is neither used and useful nor CWIP. Witness Hoard further testified that the Company's proposal that recovery of a return on the debt and preferred equity portion of the unamortized losses be charged to the cost of service is the same as placing the unamortized balance in rate base and that such transfer of the capital costs to the cost of service is really nothing more than superficial change. Witness Hoard also presented an alternative recommendation which stated that, if the Commission were to determine, contrary to the Public Staff's position, that the Company should be allowed to earn a return on a portion of the abandonment loss, then the Company should only be allowed to recover its debt costs and that the loss should be amortized over 15 years with levelized payments.

The Attorney General has recommended that the abandonment loss of Cherokee should be amortized over 15 years with no rate base treatment or return allowed on the unamortized amount. In this regard, the Attorney General cross-examined Public Staff witness Hoard with respect to a recent report by the United States Department of Energy entitled Nuclear Plant Cancellations: Causes, Costs, and Consequences (April 1983). In response to questions from the Attorney General concerning the report, witness Hoard pointed out that the cost recovery option for abandonment losses followed by most jurisdictions, as cited by the report, is one which excludes the unamortized balance from rate base.

Kudzu Alliance witness Eddleman recommended that the Company not be allowed to charge customers for any of the abandonment costs of Cherokee. In support of his position, witness Eddleman stated that:

"Duke customers played no role in the erroneous decision to go ahead with construction of Cherokee at a time when demand growth was declining and energy alternatives were available to displace Cherokee's output at less cost than it could produce energy for."

The proper rate-making treatment of abandonment losses related to electric generating plants has been before the Commission in several cases and will continue to arise in future cases. The Commission has, therefore, undertaken to reexamine this important issue in order to develop a more consistent and equitable approach to it. The Commission's ultimate responsibility with respect to ratemaking is to fix rates for the service provided which are fair and reasonable both to the utility and to the consumer. G.S. 62-133(a); State ex rel. Utilities Commission v. Morgan, 277 N.C. 255, 177 S.E. 2d 405 (1970); State ex rel. Utilities Commission v. Area Development, Inc., 257 N.C. 560, 126 S.E. 2d 325 (1962).

Although the parties to this proceeding may disagree as to the proper amortization period, they generally agree that the Company should be allowed to recover the prudently invested cost of its abandonment losses through amortization over some period of time. The Commission, based upon the evidence presented, must determine what is a fair amortization period in order to fairly allocate the loss between the utility and the consumer. With regard to the Cherokee Units 1, 2, and 3, the Commission concludes that utilization of a 10-year amortization period is proper and fair in this proceeding for the reason that such an amortization period, particularly when considered in conjunction with the Commission's decision, as subsequently discussed, to allow Duke no return on the unamortized balance, will serve to more reasonably and equitably share the burden of such plant cancellations between the Company's shareholders and its present and future ratepayers.

Furthermore, the Commission has determined that it is neither fair nor reasonable to include any portion of the unamortized balance of the prudently incurred abandonment losses associated with the Cherokee units in rate base and that no adjustment should be allowed which would in fact have the effect of allowing the Company to earn a return on the unamortized balance. The Commission has concluded that this treatment provides the most equitable allocation of the loss between the utility and the consumer. It would be inequitable to place the entire loss of expenditures that were prudent when made on the utility. Thus, amortization should be allowed. However, on the other hand, the ratepayer must not bear the entire risk of the Company's investment. A middle ground must be found on which the Company bears some of the risk of abandonment and the ratepayer is protected from unreasonably high rates. The losses resulting from cancellations of utility generating plants will inevitably be borne by one or a combination of three groups: the utility investors, the ratepayers, and the income taxpayer. The above referenced study on nuclear plant cancellations prepared by the United States Department of Energy indicates that a 10-year amortization of such losses will distribute costs in proportions that the Commission considers fair and equitable, even considering the effects of CWIP in rate base in North Carolina. The Commission believes, and thus concludes, that this will result in a fair and reasonable treatment for both the utility and its customers.

In addition, considerable testimony was rendered by Company witnesses Stimart and Utley and Public Staff witness Hoard concerning the amount of the Cherokee loss and the appropriateness of accounting for the loss on a net of

tax basis. Certain parties appearing in this proceeding were concerned with accounting for the loss on a net of tax basis. As the Company and Public Staff accounting witnesses agreed, the effect on net income of accounting for the loss on a pre-tax or net of tax basis is the same. Since the National Association of Regulatory Utility Commissioners (NARUC) System of Accounts, which this Commission has approved, sets forth net of tax accounting for abandonment losses, the Commission finds net of tax accounting for the loss to be appropriate for both ratemaking and per books purposes.

The Company and Public Staff Cherokee loss amounts differed only because of the different jurisdictional allocation methods. Both parties used the March 31, 1983, Cherokee 1 investment and the November 1, 1982, Cherokee 2 and 3 investment. The Commission recognizes that these amounts are not yet finalized, but finds that it is appropriate to render an Order in this proceeding which addresses the rate-making treatment of the loss. Any adjustments to the Cherokee loss amount can be considered in subsequent rate proceedings. This would also apply to any final determination concerning AFUDC accrued on Cherokee since February 24, 1981. Based on Finding of Fact No. 6 which determines that the proper jurisdictional allocation methodology for use in this case is the summer coincident peak method, and the foregoing, the Commission finds the proper amount of the Cherokee loss to be addressed in this proceeding is $224,464,000 stated on a net of tax basis.

In summary, various proposals for treating the Cherokee abandonment loss have been discussed before the Commission in this proceeding. The proposals discussed vary from no recovery to full recovery of all abandonment costs, with several partial recovery alternatives. In arriving at its determination, the Commission has considered the interests of both ratepayers and shareholders. Accordingly, the Commission concludes that the proper treatment of the Cherokee abandonment loss is to amortize the loss over 10 years without a return on the unamortized balance. Based on the net of tax investment in Cherokee, this treatment results in a $22,447,000 decrease in net income.

With regard to the appropriate rate-making treatment to be utilized concerning Duke's abandonment of its Perkins nuclear generating project, the Commission concludes that it is proper to affirm the decision on this issue previously set forth in Docket No. E-7, Sub 338, as part of the Commission's Order Granting Partial Increase dated November 1, 1982, for the reasons stated in that Order. In addition, the rationale for continuation of such rate-making treatment is further discussed in conjunction with Evidence and Conclusions for Finding of Fact No. 14.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 9

Company witness Stimart, Public Staff witness Nightingale, and Kudzu witness Eddleman presented testimony and evidence regarding the appropriate base fuel component in the rates.

In his original prefiled testimony, Company witness Stimart proposed a base fuel component of 1.4244¢ per kWh excluding gross receipts tax based on a normalized generation mix reflecting a 57% nuclear capacity factor. In his supplemental prefiled testimony, witness Stimart proposed a base fuel component of 1.3971¢ per kWh excluding gross receipts tax based on a normalized generation mix reflecting a 60% nuclear capacity factor.

In calculating his normalized generation mix, witness Stimart utilized a generation mix which would have occurred if the test year were adjusted to reflect: weather normalization, customer growth, a 60% average capacity factor for the Company's nuclear units, 0.415¢ per kWh nuclear fuel pricing, 1.819¢ per kWh coal fuel pricing, 8.282¢ per kWh combustion turbine fuel pricing, median conventional hydro generation, pumped storage generation based on 1980-1982 averages, combustion turbine generation based on a 2.75 - year average, 7.46% test year line losses, exclusion of 113.8 GWH nonrecurring cost-free energy from Yadkin, and test year levels of purchased power and net interchange.

Witness Stimart calculated a total company fuel cost (subject to fuel charge adjustments) of $726,270,750, or $416,034,150 for North Carolina retail service; yielding a base fuel component of 1.3971¢ per kWh excluding gross receipts tax.

Public Staff witness Nightingale normalized the generation mix by utilizing: the same adjustments for weather normalization and customer growth as the Company, 0.391¢ per kWh nuclear fuel pricing based on June 1983 prices, 1.782¢ per kWh coal fuel pricing based on average coal inventory prices in June 1983, 8.846¢ per kWh fuel oil pricing based on average oil inventory prices in June 1983, pumped storage generation based on 7-year lifetime average, median conventional hydro generation, the 10-year average capacity factor for each type of nuclear plant as reported by the National Electric Reliability Council (NERC), 7.40% line losses based on 1978-1982 averages, inclusion of 113.8 GWH cost-free energy from Yadkin, and the remaining fossil fuel generation and outside purchases and sales prorated in proportion to their actual test period generation mix. His normalization of the nuclear generation resulted in a total nuclear capacity factor of approximately 62.7%.

Witness Nightingale calculated a total company fuel cost (subject to fuel charge adjustments) of $686,919,200, or $393,491,900 for North Carolina retail service, yielding a base fuel component of 1.3214¢ per kWh excluding gross receipts tax.

Kudzu witness Eddleman computed a 1.18¢ per kWh base fuel component assuming a 65% nuclear capacity factor for McGuire 1 and a 70% nuclear capacity factor for Oconee. His procedure also incorporated the impact of McGuire 2.

Witness Stimart testified that the Company projects its actual nuclear fuel costs to be 0.412¢ per kWh for the period following the reloading of Oconee 1 (completed in August 1983), and 0.437¢ per kWh for the period following reloading of Oconee 2 (to begin in September 1983). He also testified that the actual coal fuel cost during June 1983 was 1.811¢ per kWh and that it averaged 1.837¢ per kWh during April through June 1983.

The Commission is of the opinion that a 62% nuclear capacity factor would be an appropriate normalization of the Company's nuclear operations for the period during which the rates established herein are expected to be in effect. The Commission is also of the opinion that the attempt by the Company to normalize combustion turbine (CT) generation represents an appropriate projection of the Company's CT operations, and similarly that the Public Staff's normalization of pumped storage generation, purchased power, and net

interchange power represents an appropriate projection of the Company's use of those energy sources. The Commission also concludes that the Company's recommended exclusion of cost-free energy from Yadkin should be adopted in order to reflect the nonrecurring nature of that energy source and that the Public Staff's normalized line losses should be utilized.

The Commission is of the opinion that 0.412¢ per kWh would be an appropriate normalization of the Company's nuclear fuel cost for the period during which the rates established herein are expected to be in effect. The Commission also concludes that it should adopt the 1.811¢ per kWh coal fuel pricing as an appropriate projection of the Company's coal fuel costs, and that the Company's 8.282¢ per kWh fuel oil pricing would be an appropriate normalization of the Company's fuel oil costs.

The Commission concludes that recalculating the fuel costs utilizing the normalization techniques and the unit pricing adopted herein will produce a total company fuel cost (subject to fuel charge adjustments) of $713,959,800, or $408,982,000 for North Carolina retail service, yielding a base fuel component of 1.3734¢ per kWh excluding gross receipts tax.

In evaluating the 1.3734¢ per kWh base fuel component adopted herein, the Commission has carefully considered each element in the generation mix, including generation by nuclear fuel, fossil fuels and hydro, and including intersystem purchases and sales. The contribution by each element of the generation mix which was utilized to produce the 1.3734¢ per kWh base fuel component is judged to be just and reasonable.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 10

Company witness Stimart presented testimony and evidence concerning the level of fuel inventory to be included in the allowance for working capital.

The Company had requested a 90-day supply of coal as its inventory level in the last several general rate proceedings, and it is requesting a 3,143,745-ton level of coal inventory in this proceeding. The 3,143,745 tons at the June 1983 price level of $46.58 per ton results in $145,483,000 coal inventory for total company, or $83,673,000 coal inventory for North Carolina retail service.

Witness Stimart conceded that the 3,143,745 tons would be only a 73-day supply at the test year burn rate of 43,000 tons per day. However, he explained that the Company anticipated that its burn rate for coal would drop to approximately 38,000 tons per day with the increased use of nuclear generation during 1983, and that the Company's reassessment of its coal inventory needs indicated that an 80-day supply would be sufficient in the future instead of a 90-day supply. He pointed out that 38,000 tons per day times 80 days yields approximately 3,143,745 tons (i.e., 3,040,000 tons).

The Commission concludes that the 80-day coal supply at 38,000 tons per day would be appropriate for this proceeding, resulting in 3,040,000 tons at $46.58 per ton, or $141,603,000 total company (or $81,482,000 for North Carolina retail service).

The Company is requesting a 14,078,000-gallon level of fuel oil inventory in this proceeding. The 14,078,500 gallons at the June 1983 price level of

72.33¢ per gallon results in $10,183,000 oil inventory for total company, or $5,857,000 for North Carolina retail service.

Witness Stimart conceded that the Company estimated it would use approximately 2,319,000 gallons of fuel oil during 1983 and 1,967,000 gallons during 1984. However, he explained that the fuel oil was needed not only for combustion turbine operation but also to improve the heat rate for coal operations and for flame stabilization in coal plants. He pointed out that the level of oil inventory should not be based on the average use of the oil, such as a one-year supply, but rather on the use which might have to be made of it in an emergency.

The Commission is of the opinion that the level of fuel oil inventory should not be based on the average use of oil as is done with coal inventory, but that a 14,078,000-gallon fuel oil inventory does seem unreasonably large for rate-making purposes. The Commission concludes that a 7,500,000-gallon fuel oil inventory is appropriate for this proceeding, resulting in $5,425,000 fuel oil inventory for total company, or $3,122,000 for North Carolina retail service.

The Commission further concludes that the North Carolina retail portion of working capital allowance for fossil fuel inventory should be $84,604,000, consisting of $81,482,000 for coal inventory and $3,122,000 for fuel oil inventory.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 11

Company witness Stimart and Public Staff Witness Hoard offered testimony regarding the reasonable working capital allowance. The following chart summarizes the North Carolina retail amounts the Company and the Public Staff contend are the proper levels of the components of Duke's working capital allowance to be used in this proceeding.

(000's Omitted)

Item	Company	Public Staff	Difference
Cash	$ 653	$ 648	$ (5)
Materials and supplies - fuel stock	89,530	75,318	(14,212)
Materials and supplies - other	52,764	52,372	(392)
Investor funds advanced for operations	85,701	57,220	(28,481)
Unamortized Western Fuels, Inc.	5,735	-	(5,735)
Customer deposits	(5,081)	(5,081)	-
Total working capital allowance	$229,302	$180,477	$(48,825)

The parties agree on the proper amount to include for customer deposits. Therefore, the Commission concludes that the proper amount for customer deposits is $5,081,000.

The difference in allocation methods, summer CP for the Company and summer/winter peak and base for the Public Staff, comprises the entire difference between the parties with respect to the cash and materials and supplies - other, components of working capital. Based on the Commission's conclusion that the summer CP allocation methodology is appropriate for use herein as discussed in Finding of Fact No. 6, the Commission finds that cash

of $653,000 and materials and supplies - other of $52,764,000 are the proper amounts for use in this proceeding.

Based on the Commission's conclusion in Finding of Fact No. 10, concerning the proper level for materials and supplies - fuel stock, the Commission finds it appropriate to include $84,604,000 in the allowance for working capital representing materials and supplies - fuel stock.

The next difference between the parties is the level of investor funds advanced for operations. The chart below summarizes the $28,481,000 difference.

(000's Omitted)

Item	Amount
Lag on interest and preferred dividends	$ 22,693
Lag on property taxes	184
Lag on other O & M expenses	3,840
North Carolina retail per books amounts	1,764
Total	$ 28,481

The first investor funds item of difference concerns whether lag days should be assigned to interest on long-term debt and dividends on preferred stock. Public Staff witness Hoard testified that the Company's assignment of zero lag days to these items was improper because, in fact, the Company pays the cost of interest on long-term debt and preferred dividends 80.07 days and 31.13 days, respectively, after those costs are incurred in rendering service to ratepayers. Witness Hoard concluded that the costs of interest on long-term debt and preferred dividends should be accorded the same lead-lag treatment as any other component in the cost of service that is incurred by the Company before it is paid. In rebuttal, Company witness Stimart testified that interest and preferred dividends should be assigned zero lag days since these investors are entitled to their return at the time electric service is provided to the customer.

After considering the evidence presented, the Commission concludes that 80.07 lag days should be assigned to interest on long-term debt and that 31.13 lag days should be assigned to preferred dividends. The Company's contention that bondholders and preferred stockholders are entitled to their return at the time electric service is provided to the customer is improper because these investors receive their interest payment only at six-month intervals and their preferred dividends on a quarterly basis. Bondholders and preferred stockholders know the payment terms for their interest and preferred dividends and expect to receive their interest or dividends on those dates, and no sooner.

The second item of difference in the investor funds advanced for operations calculations is the proper lag on property taxes. The difference in the composite property tax lag is due entirely to the appropriate lag on North Carolina property taxes. Company witness Stimart used 182.5 lag days for North Carolina property taxes based on a December 31 of the taxable year payment due date, whereas Public Staff witness Hoard used 187.5 lag days based on a January 5 date in the year following the taxable year payment due date. Public Staff witness Hoard supported this position on the property tax payment due date with the following excerpt from G.S. 105-360:

"(a) Due date; interest for nonpayment of taxes; discounts for prepayments - (a) all taxes levied by counties and municipalities under the provisions of this subchapter shall be due and payable on the first day of September of the fiscal year for which the taxes are levied. If paid: (1) On or after the due date and before the sixth day of January thereafter, taxes shall be paid at par or fact amount. (2) On or after the sixth day of January following the due date and before the first day of February thereafter, there shall be added to the taxes interest at the rate of two percent (2%). (3) On or after the first day of February following the due date, there shall be added to the taxes, in addition to the two percent (2%) provided in subdivision (a)(2) above, interest at the rate of three-fourths of one percent (3/4%) per month or fraction thereof until the taxes plus penalties and interest have been paid." (Emphasis added)

The Company did not offer any evidence contradicting the January 5 North Carolina property tax payment date, or supporting its December 31 North Carolina property tax payment date.

Based on the foregoing, the Commission finds 187.5 lag days proper for North Carolina property taxes and, consequently, finds 185.35 composite property tax lag days appropriate for use herein.

The third investor funds item of difference concerns the proper lag days assigned to other O&M expenses. Company witness Stimart computed 15.30 lag days, whereas Public Staff witness Hoard utilized 26.23 lag days for other O&M expenses.

Witness Hoard explained the two major problems with the Company O&M expense lag day computation as follows:

"The Company's lag was calculated by computer based upon all test year vouchers expensed to all 500 and 900 series accounts except for fuel, purchased power and employee benefits. The major problem with this procedure was the Company's calculation of each voucher's lag. The Company computed each lag based on the difference between the invoice date and the payment date rather than the difference between the expense incurred date and payment date.

One example of this problem concerns $300,000 of security services performed at the Oconee plant during the period September 25, 1981 to October 23, 1981. Based on an invoice date of November 17, 1981 and a payment date of December 28, 1981 the Company computed a lag of 41 days. This lag should have been computed from the midpoint of the period for which the security service was performed since the vendor (the company performing the security service) has funds tied up in Duke Power and Duke has the use of those funds from the date the service is provided to the date payment is made.

Another problem with the Company's voucher study concerns vouchers which were assigned, for one reason or another, an invoice date the same as the payment date and consequently calculated as zero lag days. Examples of items included in this category are telephone bills for the prior month's service, various materials and supplies invoices grouped together (all received prior to the payment date), line of

> credit billings for the prior quarter and other previously received services grouped together for payment as a single voucher. The assignment of zero lag days to these items by the Company results in a serious distortion of the lag days associated with other O&M expenses."

Company witness Stimart did not rebut witness Hoard on these points.

Witness Hoard recommended that the Commission reject the Company's proposed other O&M expense lag and that the Commission use the 26.23-day other O&M expense lag found reasonable in the Company's last general rate case, Docket No. E-7, Sub 338.

Based on the foregoing, the Commission rejects the Company's 15.30-day other O&M expense lag and finds 26.23 lag days appropriate to assign to other O&M expenses.

The last investor funds item of difference concerns the appropriate North Carolina per books amounts to which the lag days previously determined should be applied. Public Staff witness Hoard explained the difference between his position and the Company's on this item as follows:

> "The Company and I used N.C. retail per books amounts that differed for two reasons. The first reason is that I used the summer and winter peak and base allocation method to arrive at my N.C. retail amounts whereas the Company used the summer CP allocation method. Since the Public Staff's position is presented on a summer and winter peak and base basis, it is entirely consistent that the N.C. retail per books amounts for the investor funds calculation be stated on that same basis.
>
> The other reason that the Company and I differ with respect to the N.C. retail per books amounts is that the Company applied summer CP allocation factors for a period other than the test year to the test year total company amounts. The result of this difference is that the Company's N.C. retail per books amounts used in the investor funds calculation do not agree with the N.C. retail per books amounts used in its cost of service study."

Consistent with the Commission's prior finding regarding the proper jurisdictional allocation method, the Commission finds that it is appropriate to use the North Carolina retail per books amounts as derived using the summer CP allocation method. Further, the Commission finds it proper to use the summer CP allocation factors as derived from the test year per books study rather than factors for a period other than the test year in arriving at the North Carolina retail per books amounts to be used in calculating investor funds advanced for operations.

Based on the conclusions previously discussed, the Commission finds that the reasonable level of investor funds advanced for operations is $57,146,000.

The last area of disagreement concerning working capital involves the Company's unamortized investment in Western Fuels, Inc. The Company proposed to amortize the expenditures in this project over a five-year period and

included the unamortized Western Fuels, Inc., investment in rate base as working capital. Public Staff witness Hoard concurred that these research and development expenditures should be amortized to operations over a five-year period but recommended against inclusion of the unamortized portion in rate base.

Company witness Stimart explained his Western Fuels recommendation in his rebuttal testimony as follows:

"The Commission should not penalize the Company for investing in projects which the Commission has approved and which are designed to explore low-cost sources of fuel. All of the benefits of such experiments will be passed on to ratepayers, as they should be. If the Company is penalized for these experiments by disallowing full recovery of the investments, there will be no incentive to undertake projects designed to provide cheaper means of providing electric service. The Company originally chose, and so reported to this Commission, to capitalize those R & D expenditures instead of charging them off currently to cost of service as the Company does for its other R & D expenditures. Duke's request for recovery of these R & D expenditures is no different from the Commission's decision to CP&L in Docket No. E-2, Sub 366, to include in rate base deferred charges related to the Robinson turbine repairs."

Public Staff witness Hoard testified during cross-examination by the Company on this issue as follows:

"If we had allowed the Company to earn a return on the unamortized balance, we would provide the Company with some sort of incentive to enter into suspect and speculative investments and... they'd (ratepayers would) be forced to bear the entire cost of this loss if we included it in rate base."

Company witness Stimart acknowledged during cross-examination that requiring ratepayers to pay a return on the unamortized investment insulates shareholders from bearing any of the loss.

The Commission recognizes that including the unamortized balance of the Western Fuels investment in working capital as proposed by the Company would allow the Company to earn a return on the unamortized portion of said investment and all the risks of this venture would be transferred from the shareholders to the ratepayers. The Commission does not believe that the Company's shareholders should be entirely insulated from the risk associated with such ventures. Based on the foregoing, the Commission concludes that it would be inappropriate to allow the Company a return on the unamortized portion of the Western Fuels investment by including it in rate base as working capital. However, the Commission concurs with the Company and the Public Staff that the Western Fuels investment should be amortized to the cost of service over a five-year period.

Based on the foregoing findings, the Commission concludes that the reasonable working capital allowance in this proceeding is $190,086,000, as summarized below:

(000's Omitted)

Item	Amount
Cash	$ 653
Materials and supplies - fuel stock	84,604
Materials and supplies - other	52,764
Investor funds advanced for operations	57,146
Customer deposits	(5,081)
Total working capital allowance	$190,086

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 12

Company witness Stimart and Public Staff witness Hoard offered testimony and exhibits regarding Duke's reasonable original cost rate base. The following chart summarizes the amounts which the Company and the Public Staff contend are the proper levels of original cost rate base to be used in this proceeding.

(000's Omitted)

Item	Company	Public Staff	Difference
Electric plant in service	$ 3,640,170	$ 3,619,605	$ (20,565)
Accumulated depreciation	(1,263,605)	(1,257,449)	6,156
Construction work in progress	282,481	281,065	(1,416)
Allowance for working capital	229,302	180,477	(48,825)
Accumulated deferred income taxes	(289,937)	(287,471)	2,466
Operating reserves	(9,204)	(10,529)	(1,325)
Total original cost rate base	$2,589,207	$2,525,698	$(63,509)

The only difference between the Company and the Public Staff concerning the reasonable level of electric plant in service, accumulated depreciation, construction work in progress (CWIP), and accumulated deferred income taxes is due to the difference in the parties' jurisdictional cost allocation methods. Based on the Commission's finding that the summer CP allocation method is proper, the Commission finds that the following amounts: electric plant in service of $3,640,170,000, accumulated depreciation of $1,263,605,000, CWIP of $282,481,000 (McGuire Unit No. 2 - $277,429,000 and Oconee radwaste facility - $5,052,000), and accumulated deferred income taxes of $289,937,000 are appropriate for use herein.

Pursuant to G.S. 62-133(b)(1), the Commission may include reasonable and prudent expenditures for CWIP in rate base to the extent such inclusion is found to be in the public interest and necessary to the financial stability of the utility in question. In this case, Duke proposes to include in rate base a net incremental amount of $6,613,000 of CWIP in addition to the $275,868,000 of CWIP already reflected in rates presently in effect, which would bring the the total CWIP in rate base to $282,481,000. This amount of total CWIP consists of construction expenses recorded on the Company's books since July 1, 1979, for McGuire Unit No. 2 ($277,429,000) and the Oconee radwaste facility ($5,052,000). The increment of CWIP consists of additions of $110,493,000, all applicable to McGuire Nuclear Station Unit No. 2, offset by the elimination from CWIP of $103,880,000 which is the amount previously included for Cherokee Unit No. 1. Company witness Lee testified that McGuire Unit No. 2 is expected to commence operation in early 1984. He further indicated that with this request approximately 50% of Duke's investment in McGuire Unit No. 2 would be included in the Company's rate base.

Company witnesses Lee, Stimart and Olson all testified that the inclusion in rate base of the amount of CWIP proposed herein by the Company was necessary to assure the Company's financial stability in that it would provide essential help to the Company's cash flow and fixed charges coverage and would avoid extremely unfavorable signals to investors. Witness Lee also testified that inclusion of CWIP in rate base with respect to large electric generating units is in the public interest because it gives more accurate price signals to consumers of the real cost of electricity and avoids the shock of huge rate increases that would otherwise be necessary when large generating units are brought into service.

Public Staff witness Hoard proposed only one adjustment to CWIP in the amount of $1,416,000 which resulted from the Public Staff's proposed allocation methodology, which adjustment the Commission has previously found to be inappropriate for use in this proceeding. Furthermore, although he did not propose any adjustment in this case, witness Hoard testified that it continues to be the position of the Public Staff that AFUDC accrued on July 1, 1979, CWIP balances should be excluded from rate base.

Based upon a careful consideration of the entire record in this proceeding, the Commission concludes that the $282,481,000 of CWIP proposed herein by Duke for inclusion in the Company's rate base represents reasonable and prudent construction expenditures and that inclusion of such amount of CWIP, being only a small portion of the Company's total existing CWIP applicable to North Carolina retail operations, is in the public interest and necessary to the continuing financial stability of Duke Power Company. Furthermore, the Commission continues to reject the Public Staff's legal contention that AFUDC accrued since July 1, 1979, on construction expenditures made prior to that time should be excluded from rate base. G.S. 62-133 does not require such treatment. As the Commission has stated in past orders, AFUDC or capital costs accrued in connection with construction projects are as much a part of that construction and no less real than the cost of steel, bricks, mortar and labor. G.S. 62-133 does not require that such capital costs be disallowed for rate-making purposes merely because they relate to construction expenditures made prior to July 1, 1979. Therefore, even though a portion of the AFUDC accrued since July 1, 1979, relates to CWIP balances created prior to July 1, 1979, it is the Commission's opinion that AFUDC is a current cost of construction just like any other cost that occurred after July 1, 1979, on a project that was begun prior to that date. AFUDC on pre-July 1, 1979 property which accrued after July 1, 1979, is therefore found by the Commission to be proper for inclusion in CWIP receiving rate base treatment.

Accordingly, the Commission concludes that the $282,481,000 of reasonable and prudent expenditures for CWIP which Duke proposes to include in rate base in this case is in the public interest and is necessary to the Company's financial stability.

The next area of difference concerns the allowance for working capital. The Commission found in Evidence and Conclusions for Finding of Fact No. 11 that $190,086,000 is the appropriate level and, therefore, includes this amount as the allowance for working capital in determining the rate base.

The last area of difference concerns the proper amount to deduct as operating reserves. The $1,325,000 difference is summarized below:

(000's Omitted)

Item	Amount
Operating reserves per company	$ 9,204
Change to summer/winter peak and base allocation method	(61)
Injuries and damages reserves	1,386
Operating reserves per Public Staff	$10,529

As shown above, the Company includes $61,000 more for operating reserves than the Public Staff due to the different allocation methods. The Commission finds that it is inappropriate to reduce the Company's operating reserves amount by $61,000, based on its previous finding that the summer CP allocation method is proper.

The $1,386,000 injuries and damages reserves adjustment made by the Public Staff was agreed to by Company witness Stimart in his rebuttal testimony; therefore, the Commission finds that it is proper to make such an adjustment. However, due to the Commission's acceptance of the summer CP as the proper allocation method, the Commission finds that an adjustment to the injuries and damages reserve in the amount of $1,395,000 is proper. Consequently, the Commission finds the reasonable level for operating reserves to be $10,599,000.

Based on the foregoing the Commission concludes that the appropriate North Carolina retail original cost rate base for use herein is $2,548,596,000 calculated as follows:

(000's Omitted)

Item	Amount
Electric plant in service	$ 3,640,170
Accumulated depreciation	(1,263,605)
Construction work in progress	282,481
Allowance for working capital	190,086
Accumulated deferred income taxes	(289,937)
Operating reserves	(10,599)
Total original cost rate base	$ 2,548,596

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 13

Company witness Stimart and Public Staff witnesses Hoard and Turner offered testimony on the proper level of operating revenues. The $1,000 difference between the Company's $1,470,600,000 amount and the Public Staff's $1,470,599,000 amount is due solely to the parties' different jurisdictional cost allocation methods. Since the summer coincidental peak allocation method has previously been found to be proper, the Commission concludes that the appropriate level of operating revenues for use herein is $1,470,600,000.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 14

The evidence for this finding of fact is found in the testimony and exhibits of Company witness Stimart and Public Staff witnesses Nightingale, Turner, Lam and Hoard. The following chart sets forth the amounts presented by the Company and Public Staff:

(000's Omitted)

Item	Company	Public Staff	Difference
O&M expenses			
- Fuel used in electric generation	$ 436,998	$415,123	$ 21,875
- Purchased power and net interchange	444	(908)	1,352
- Other	332,435	324,027	8,408
Depreciation and amortization	118,781	118,016	765
General taxes	123,586	122,400	1,186
Interest on customer deposits	372	372	-
Income taxes	178,917	196,900	(17,983)
Amortization of ITC	(3,680)	(3,659)	(21)
Property abandonment expenses			
- Property amortization	19,508	19,273	235
- Interest and preferred dividend costs	7,931	-	7,931
Total operating revenue deductions	$1,215,292	$1,191,544	$23,748

The Company and the Public Staff are in agreement regarding the level of depreciation and amortization expense, interest on customer deposits, and amortization of ITC with the exception of jurisdictional allocation methodology differences. Consequently, the Commission finds depreciation and amortization expense of $118,781,000, interest on customer deposits of $372,000, and amortization of ITC of $3,680,000 appropriate for use herein.

The $21,875,000 difference between the Company and the Public Staff for fuel used in electric generation is comprised of two items. The first item of difference, in the amount of $22,542,000, results from differing fuel cost components proposed by the Company and the Public Staff. The Commission fully discusses this issue in Evidence and Conclusions for Finding of Fact No. 9, wherein the Commission finds a fuel cost component of $.013734 per kWh appropriate. Consistent with such finding by the Commission, an adjustment to decrease the Company's proposed level of fuel expense by $7,052,000 is found to be proper.

The remaining item of difference in the amounts proposed for fuel used in electric generation concerns an adjustment proposed by the Public Staff to increase the Company's cost of service by $667,000 for additional nuclear fuel disposal costs. This proposed adjustment is based upon the Public Staff's recommended level of nuclear generation. As previously discussed in Evidence and Conclusions for Finding of Fact No. 9, the Commission's level of nuclear generation differs from that level proposed by both the Company and the Public Staff. Consequently, the Commission finds it proper to increase the Company's proposed fuel expense used in electric generation by $494,000 related to nuclear fuel disposal costs. Based on the foregoing conclusions of the Commission, the proper level for fuel expense used in electric generation for use in this proceeding is found to be $430,440,000.

The Company and the Public Staff differed by $1,352,000 concerning the appropriate amount of purchased power and net interchange. The $1,352,000 difference results from an adjustment made by Public Staff witness Lam to reduce expenses by the net profit Duke made on the sale and interchange of power during the test year.

Witness Lam testified that Duke filed workpaper D-414 in Item 10 of their E-1 data response filing that showed a profit on the sale of power of $9,186,000 and a nonfuel expense for power purchased of $6,827,000 which results in a net nonfuel component profit of $2,359,000 on a total company basis and a profit of $1,352,000 allocated to North Carolina retail. Witness Lam also testified that in his opinion there would be a market for Duke's excess power in the future due to CP&L's current problems with its nuclear units. Witness Lam further stated that CP&L had purchased large amounts of power from Duke for the 12-month period ending May 1983.

Witness Lam testified that the profit Duke makes as a middleman in transfer transactions was considered in this rate case in a similar manner to the treatment of this item in Duke's last general rate case considered by the Commission in Docket No. E-7, Sub 338. According to witness Lam in Docket No. E-7, Sub 338, when the nonfuel component of power purchased was higher than the profit, the North Carolina ratepayer bore the expense of the purchased power. Consequently, witness Lam testified that it is only fair and correct for the ratepayer to be the beneficiary if the net profit is higher than the expense of purchased power.

Company witness Stimart testified that the level of the nonfuel component profit from the sale of power was due in part to Duke's acting as a middleman in the transfer of power (concurrent in and concurrent out) from the Southern Company to CP&L, and that such profit should not flow through to the North Carolina ratepayers.

The Commission finds the Public Staff's proposal regarding purchase power and net interchange appropriate and concludes that the $1,352,000 net profit on purchases and interchange should be used as a reduction to test period operating revenue deductions in this general rate proceeding.

The next area of disagreement relates to other O&M expenses. The $8,408,000 difference between the Company and the Public Staff is reconciled as follows:

(000's Omitted)

Item	Amount
Other O&M expenses per company	$332,435
Public Staff adjustments:	
Excess nuclear insurance	(522)
End of period payroll	(3,175)
Nonpayroll customer growth expenses	(433)
Nonpayroll employee growth expenses	(1,165)
Post-test year inflation	(1,905)
Officers' salaries	(328)
Lobbying expenses	(74)
Allocated to peak and base methodology	(806)
Other O&M expenses per Public Staff	$324,027

Company witness Stimart stated in rebuttal testimony that he concurred with the Public Staff's excess nuclear insurance adjustment; therefore, the Commission finds the Public Staff's adjustment to reduce other O&M expenses for excess nuclear insurance proper; however, in accordance with the

Commission's decision regarding the summer CP allocation methodology, the proper amount for the adjustment is found to be $525,000.

Three of the remaining areas of difference between the Company and the Public Staff are interrelated. The Company proposed adjustments to (1) annualize wage rate increases during the test year, (2) annualize wage rate increases occurring subsequent to the test year, (3) increase O&M expenses (excluding fuel and purchased power) to reflect customer and employee growth, and (4) annualize payroll and nonpayroll O&M expenses for a full year's operation of McGuire #1. In addressing these same areas of expense, the Public Staff made adjustments to (1) reflect end of test year payroll expense and employee levels, (2) reverse the nonpayroll portion of the Company's employee growth adjustment, and (3) reflect nonpayroll customer growth related expenses. Thus, the Public Staff and the Company are in agreement regarding the Company's proposed adjustments for wage rate increases subsequent to the test year (Company proposed adjustment 2 above) and annualization of nonpayroll O&M expenses for a full year's operation of McGuire #1 (Company proposed adjustment 4 above).

Public Staff witness Hoard determined the end of test year level of payroll expense by annualizing the last monthly and biweekly regular payrolls for the test year ended September 30, 1982, and adding to that amount end-of-period premium pay based on the relationship of actual test year premium pay to regular pay. Witness Hoard assigned the Public Staff's proposed end of test year level to expense based on the ratio of actual test year payroll expense to total payroll as adjusted for a full year of McGuire #1 operations. Based upon the methodology proposed by witness Hoard, the Public Staff recommended that the Company test period adjusted payroll expenses be decreased by $3,175,000.

Company witness Stimart testified in rebuttal that in his opinion the Public Staff's proposed payroll expense estimate was in error for three reasons. The three reasons enumerated by witness Stimart involve the following: (1) In witness Stimart's opinion the Public Staff's methodology effectively eliminates from cost of service the Company's summer and holiday season temporary employment costs, since they are not involved during the month of September; (2) in witness Stimart's opinion the Public Staff's payroll expense estimate involves greater risk of misallocation between electric and nonelectric operations than does the Company's calculation since the Public Staff applied the test year historical average payroll factor to total payroll in arriving at the proposed payroll expense amount; and (3) the methodology used by Duke to reflect wage rate changes has been used and accepted by the Commission for many years.

Public Staff witness Hoard conceded as to the validity of the Company's criticism regarding the omission of summer and holiday season temporary employment costs from the Public Staff's adjusted wage expenses. However, witness Hoard maintains that the Public Staff's methodology, unlike the Company's, includes premium pay based on end-of-period wage rates. In witness Hoard's opinion any understatement in wage expense relative to summer and holiday season temporary employment costs is offset by the additional premium pay considered by the Public Staff.

The Commission has carefully considered the adjustments proposed by the Company and the Public Staff to test period payroll expense, specifically the

propriety of the Public Staff's proposed $3,175,000 decrease in payroll expense. The Company's position regarding this issue is based upon actual payroll experienced during the test period as actually distributed to utility operations, adjusted to reflect the annualization of wage rate increases during the test year. Alternatively, the Public Staff's position attempts to reconstruct Duke's annual electric operating payroll expense by annualizing the September 1982 total payrolls and allocating the results of such calculations between operations and construction on the basis of the ratio of actual work effort assignments and construction for the entire test year. The Commission recognizes that the proposals of the Company and the Public Staff simply reflect alternative methods of arriving at the end-of-test-period level of payroll expense which can be expected to occur on an ongoing basis in the future. The Commission must therefore determine which of the proposed methodologies more accurately reflects the level of payroll expenses which Duke will likely incur during the period of time wherein rates established in this proceeding are in effect. In the Commission's opinion the Company's proposed methodology of arriving at the adjusted level of payroll expenses more accurately reflects this item of cost on an end-of-period basis. Since the base payroll used by the Company represents the actual payroll recorded on the Company's books during the test year and is supported by time reports filled out by each employee, the Company's calculations more accurately reflect the actual test period allocation between electric and nonelectric operations. Further, the Company's methodology is more closely reflective of the methods utilized by the Commission in setting rates for Duke in past rate proceedings. Finally, the Commission notes that the method advocated by the Public Staff erroneously omits any consideration of summer and holiday season temporary employment costs. The Commission therefore finds the adjustment proposed by the Public Staff to decrease payroll expense by $3,175,000 inappropriate.

The parties offered different treatments of customer and employee growth as it effects O&M expenses, excluding fuel. The Company's proposed adjustment to O&M expense (excluding fuel and purchased power) for customer and employee growth is based upon a percentage growth factor of 1.22% comprised of the composite percentage of growth in customers and employees. The Company, in determining its O&M expense adjustment of $3,751,000 of which $1,813,000 is related to payroll expenses included in O&M expenses simply multiplied the composite growth factor of 1.22% times O&M expenses (excluding fuel and purchased power). The Commission notes that O&M expenses (excluding fuel and purchased power) are composed of energy-related expenses, customer related expenses, and demand-related expenses. It is likewise recognized that only customer-related expenses and energy-related expenses vary in relation to the number of customers and their related kWh sales. Further, the sum of customer-related and energy-related expenses (excluding fuel and purchased power) comprise far less than one-half of O&M expenses. Additionally, certain expenses related to the number of employees have already been considered in customer-related expenses.

Alternatively, the Public Staff's proposed adjustment to O&M expenses for customer growth of $433,000 consists of two parts, an adjustment to energy-related expenses (excluding fuel) and an adjustment to customer-related expenses. Public Staff witness Turner calculated total energy-related expenses per kWh to be .1202¢/kWh (excluding fuel and wages). Witness Turner's calculation utilizes energy-related production expenses excluding fuel and wages which includes an allowance for administrative and general

expenses. The total energy-related factor when multiplied by the Company's proposed 112,817,000 kWh adjustment for customer growth, results in an adjustment decreasing energy-related expenses by $135,606 (excluding fuel and wages).

The Public Staff also proposed an adjustment decreasing O&M expenses by $204,548 for customer growth relating to customer-related expenses. Public Staff witness Turner calculated total customer-related expenses, excluding wages of $1.465 per bill utilizing customer accounts expenses and customer service and information expenses, excluding wages and including an allowance for administrative and general expenses. Based upon the proposed adjustment to billings of 139,623 and the customer-related cost of $1.465 per bill, the Public Staff recommends an increase in customer-related expenses of $204,548. Therefore, the Public Staff proposes that the Company's proposed increase for customer growth relating to O&M expenses excluding fuel, purchase power, and wages of $773,000 be decreased by $433,000 to $340,000 ($136,000 + $204,000).

Public Staff witness Hoard recommended that the Company's proposed adjustment for employee growth be decreased by $1,165,000 to exclude the nonpayroll portion of employee growth. According to witness Hoard's testimony it is not necessary to include additional expenses for employee growth since O&M expenses have been adjusted to reflect an end-of-period level of payroll expenses, to reflect the nonpayroll, nonfuel and nonpurchased power related customer growth expenses and to reflect test period price increases.

The Commission has carefully considered the adjustments proposed by the Public Staff regarding nonpayroll customer growth and nonpayroll employee growth adjustments and concludes that these adjustments are proper. The Commission concludes that the adjustments for nonpayroll customer growth expenses and nonpayroll employee growth expenses proposed by the Public Staff more accurately reflect expense increases for customer and employee growth than that proposed by the Company since items of cost adjusted to end-of-period elsewhere are eliminated from such calculations. After adjusting such amounts to reflect the summer coincidental peak allocation method found fair herein, the Commission finds adjustments decreasing the Company's proposed nonpayroll customer growth expenses and the nonpayroll employee growth expenses by $433,000 and $1,171,000, respectively, appropriate.

The next item of difference concerns the Company's adjustment for inflation occurring subsequent to the test year. In its original filing, the Company made an adjustment to increase the cost of service by $19,416,000 in order to provide for forecasted annual inflation occurring after the test year. In his supplemental testimony and exhibits, filed June 28, 1983, Company witness Stimart increased operating revenue deductions for wage increases occurring after the test year through March 1983, for additional CWIP, for the abandonment of Cherokee #1, and for reduced fuel expenses. Witness Stimart directly offset these supplemental adjustments with a $17,511,000 reduction in the Company's post test year inflation adjustment. Thus witness Stimart reduced the Company's inflation adjustment from $19,416,000 to $1,905,000. Public Staff witness Hoard proposed eliminating the remaining $1,905,000 inflation adjustment from operating revenue deductions since there were no specific items of cost supporting the adjustment. The Commission has considered the evidence in this regard and does not believe that it is appropriate to make a specific adjustment to increase the test year cost of

service in order to compensate for the so-called effect of attrition beyond that reflected in the accounting and pro forma adjustments which the Commission has adopted for use herein. Therefore, the Commission finds it proper to exclude the remaining $1,905,000 of the Company's inflation adjustment from the cost of service.

The next area of difference is a reduction in O&M expenses of $328,000 proposed by Public Staff witness Hoard in conformity with the Commission's decision in Docket No. E-7, Sub 338 to exclude from the cost of service one-half of the annual amount of salaries paid to Duke's executive officers earning in excess of $150,000 per year. The Commission has carefully reconsidered this adjustment to wages and salaries related to executive salaries and concludes that salaries paid to the chief officers of the Company represent a prudent and reasonable operating expense. The Commission finds no evidence in the record to indicate that such salaries are excessive or unreasonable or that such officers are not performing their duties prudently or effectively; therefore, no adjustment in this regard is proper.

The Public Staff proposed a further adjustment of $74,000 to eliminate from operating revenue deductions wages and salaries relating to lobbying expenses. The adjustment proposed by the Public Staff relates specifically to the salary of John Hicks, a registered lobbyist for the Company. Consistent with previous decisions of the Commission regarding lobbying activities, the Commission finds that the cost of such activities is not a proper cost of providing service to be recovered from the ratepayers of the Company. The Commission finds that the costs of lobbying activities should properly be borne by the stockholders of the Company.

The final issue to be resolved regarding O&M expenses relates to the clean-up costs associated with Three Mile Island. Company witness Stimart testified under cross-examination by the Attorney General that as of January 1, 1983, the Company began accruing $100,000 a month on a total company basis in anticipation of some ultimate liability associated with the Three Mile Island (TMI) cleanup costs. Test period operating expenses proposed by the Company in this proceeding include $541,000 on a North Carolina retail basis for cleanup costs associated with TMI.

Witness Stimart further testified that no court or government agency has ordered the Company to make the payment nor has the Company made any payments for such cleanup costs. Additionally, on cross-examination, witness Stimart stated that the accrual of TMI cleanup costs had not been specifically identified or mentioned in the Company's testimony and exhibits.

The Commission concludes that amounts accrued by Duke for the possible cleanup costs associated with the TMI accident are not properly includable in test period operating expenses. The Commission concludes that the amount of any possible assessment, the timing of the ultimate payment of such an assessment, and even the certainty of incurring such costs are not known at this time. In the Commission's opinion to charge customers in rates today for what is at best an uncertain future expense is neither just nor reasonable and thus the Commission finds it appropriate to reduce the Company's proposed test period operation and maintenance expenses by $541,000. The Commission further concludes that previous accruals to operating revenue deductions in this regard should be reversed. Such costs shall not be reflected in operating revenue deductions until such time as the Company has received specific Commission approval with respect thereto.

In summation, the Commission concludes that O&M expenses of $757,317,000 using the summer coincidental peak allocation methodology are appropriate for use herein.

The Company and the Public Staff also differ with respect to the level of other operating taxes. The two items comprising the $1,003,000 difference (exclusive of allocation differences) are payroll taxes related to the Public Staff's end-of-period payroll adjustment in the amount of $94,000 and gross receipts taxes of $909,000 related to revenues refunded by the Company.

Consistent with the Commission's prior finding concerning the Public Staff's proposed end-of-period payroll adjustment, the Commission finds the reduction in general taxes of $94,000 improper.

Public Staff witness Hoard explained the $909,000 gross receipts tax adjustment in his testimony as follows:

> "Based on the test year per books revenues, gross receipts taxes per books were overstated. The overstated gross receipts taxes relate to gross receipts taxes computed on revenues that have been refunded. Since the revenues are not included in the Company's per books cost of service computation, it would be improper to include the related gross receipts taxes."

Company witness Stimart stated in rebuttal testimony that he concurred with this adjustment. The Commission, therefore, finds it proper to reduce general taxes by $909,000 for gross receipts taxes relating to operating revenues which have been refunded by the Company. Based on the foregoing and the use of a summer coincident peak allocation methodology, the Commission finds other operating taxes of $122,677,000 appropriate for use herein.

Since the Commission has not adopted all of the components of taxable income proposed by either party, it has made its own calculation of income tax expense of $185,473,000 and concludes that this is the proper amount to include in determining the cost of service in this proceeding.

The last area of difference concerns the proper treatment of the Company's Cherokee and Perkins property abandonment losses. Based on the Commission's conclusions in Findings of Fact Nos. 7 and 8, the Commission has included $23,263,000 net of income taxes, relating to the Cherokee and Perkins abandonment losses as an operating revenue deduction.

Company witness Stimart proposed that the Company be allowed to recover the Perkins-related interest and preferred dividend costs over a ten-year amortization period. In arriving at the unamortized Perkins loss amount upon which the Company computes a return consisting of interest costs and preferred dividend costs, witness Stimart did not deduct out the amount previously recovered from ratepayers for the loss. Thus the Company is requesting that ratepayers pay a return on a portion of the loss that has already been recovered by the Company.

Public Staff witness Hoard recommended that the Commission continue its treatment for Perkins set forth in the Company's prior rate proceeding, Docket No. E-7, Sub 338. Witness Hoard recommended that the loss be amortized over a five-year period without inclusion of the unamortized balance in rate base.

Witness Hoard included $810,000 in the cost of service for the net of tax Perkins property abandonment loss expenses.

The Commission finds the proper treatment of the Perkins loss is to amortize the loss over five years without a return on the unamortized balance, as the Commission found in Docket No. E-7, Sub 338. Based on the foregoing and Finding of Fact No. 6 wherein the Commission found the summer coincidental peak allocation method proper, the Commission finds the proper, net of tax, Perkins property abandonment expenses to include in the cost of service in this proceeding to be $816,000.

In summary, the Commission finds $23,263,000, comprised of $22,447,000 for Cherokee and $816,000 for Perkins, properly includable in the cost of service in this proceeding as property abandonment expenses.

Based on the entire record in this proceeding, the Commission concludes that the proper level of operating revenue deductions for use herein under present rates is $1,205,203,000 calculated as follows:

(000's Omitted)

Item	Amount
Operating and maintenance expense	$ 757,317
Depreciation and amortization	118,781
General taxes	122,677
Interest on customer deposits	372
Income taxes	186,473
Amortization of investment tax credit	(3,680)
Property abandonment loss amortization, net of taxes	23,263
Total operating revenue deductions	$1,205,203

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 15 AND 16

Four witnesses testified in the area of capital structure and cost of capital. The Company offered the testimony of William R. Stimart, Vice President, Regulatory Affairs of Duke, Dr. Charles E. Olson, President of Olson & Company, Inc., and Dr. Edward W. Erickson, Professor of Economics at North Carolina State University. The Public Staff offered the testimony of Dr. Caroline M. Smith, Senior Economist with the firm of J.W. Wilson & Associates, Inc., and consultant to the Public Staff.

There was no disagreement concerning the appropriate capital structure and costs of long-term debt and preferred stock to be used in this proceeding. The capitalization ratios used in this case are identical to those approved by the Commission in Docket No. E-7, Sub 338, and consisted of 47% long-term debt, 13% preferred stock, and 40% common equity. The senior security costs are 9.83% for long-term debt and 8.62% for preferred stock, calculated as of September 30, 1982.

Accordingly, the Commission concludes that the proper capital structure for use in this proceeding is as follows:

Item	Percent
Long-term debt	47.0%
Preferred stock	13.0%
Common equity	40.0%
Total	100.0%

Consistent with the evidence supporting the above capital structure, the Commission concludes that the appropriate embedded costs of debt and preferred stock are 9.83% and 8.62%, respectively.

The evidence relating to the fair rate of return for Duke Power is contained in the testimony and exhibits of Company witnesses Olson and Erickson and Public Staff witness Caroline Smith. The rates proposed by the Company in its application were designed to yield a rate of return of 15.5% on common equity, based upon the test period ended September 30, 1982, as adjusted, and based upon a capital structure containing 40% common equity. The Public Staff, through the testimony of Dr. Smith, recommended that Duke receive a return of 13.0% on its common equity capital, after adjustment to reflect the Commission's previous treatment of the gain attributable to the debt-equity swap.

Company witness Olson relied principally on the discounted cash flow method of estimating the cost of equity and the fair rate of return on equity for Duke Power Company. This method is based on the notion that the price an investor in utility common stock will pay for the stock will generate a current dividend yield which, when added to the investor's expected long-term growth in that utility's dividends, will equal the investor's cost of common equity for that utility. The discounted cash flow method thus can be expressed as the following equation: the cost of equity (K) is equal to the dividend yield (D/p) plus the expected growth in dividends (g), or $K = D/p + g$. Utilization of the DCF method thus requires the determination of the applicable dividend yield for Duke and the estimation of what those investors who are buying Duke's common stock expect the long-term growth rate in its dividends to be.

Dr. Olson concluded that, based on a current dividend yield of 10.7% (calculated by using the current indicated annual dividend of $2.36, and average price for the last 4 1/2 months) and his estimate of investor expectation of long-term dividend growth of 5.0% to 5.5%, the "investor-required" cost of equity is 15.7% to 16.2%.

Dr. Olson's judgment that investors expect a 5.0% to 5.5% growth in Duke's dividends was based upon his analysis of Duke's historical growth in earnings, dividends, and book value and on current circumstances affecting investor's expectations, including Duke's allowed rate of return, its recent earned rates of return and payout ratio and the recent cancellation of its Cherokee Nuclear Station.

Dr. Olson checked his DCF analysis of Duke's cost of equity by the interest premium approach, which he concluded reflects a required investor return on equity to Duke of about 16%. He also conducted a DCF analysis of eight electric companies which, in his judgment, are comparable with Duke in revenues, operating characteristics, and bond ratings. The DCF investor-required return of these eight companies averaged 15.8% to 16.3%.

Dr. Olson testified that the 15.7% to 16.2% investor-required return should be increased by a factor of about 8% to enable Duke's stock to trade at a slight premium over book value, so that future issues of its common stock can generate net proceeds that approximate book value. He therefore concluded that the fair rate of return for Duke's common equity is in the range of 16.9% to 17.4%.

Dr. Caroline M. Smith testified on fair rate of return for the Public Staff. She based her conclusion as to the fair rate of return on equity primarily on the discounted cash flow model, using a regression and correlation analysis of the historic growth rate of 95 electric utilities, including Duke, to derive her estimate of investor growth expectations. Dr. Smith checked the results of her discounted cash flow approach by an examination of the return of "comparable" companies in 1982.

Dr. Smith derived a current dividend yield of 10.2%, using the "indicated" dividend, which is the dividend for the last quarter of 1982, annualized, and the average of the high and low sale prices over the six months ended March 31, 1983. Using her correlation and regression analysis witness Smith examined 30 historical growth rates in relation to the dividend yields of the 95 utilities (10 each in dividends, earnings, and book value) and concluded that the "single best growth rate" to use as a proxy for investor long-term dividend growth expectations is the four-year growth in book value and that the three most important growth rates were the 4-year and 8-year book value growth rates and the 7-year earnings growth rate, each weighted by its related regression coefficient. Dr. Smith also examined the result of all 30 growth rates, weighted by their respective correlation coefficients. She derived an algebraic formula to arrive at what she asserted was the risk differential between Duke on the one hand and the average of her 95-utility group on the other hand. Applying this formula Dr. Smith concluded that investors expect a 1.9% growth in Duke's dividends. She concluded that, on the basis of the "three most important growth rates" investors expect Duke's long-term dividend growth to be 2.8%. Finally, using all 30 growth rates, Dr. Smith concluded that investors expect dividend growth of 4.2% for Duke. Thus, Dr. Smith's regression analysis came up with three different growth rates: 1.9%, 2.8%, and 4.2%. Public Staff witness Smith then arrived at her own growth estimate of 3% which is an average of the three.

Dr. Edward W. Erickson testified in rebuttal to Dr. Smith's regression and correlation methodology. He first established that he had been able to replicate Dr. Smith's model on computer, and he then took issue with certain factual assertions in Dr. Smith's testimony, stating that those assertions were incorrect. Dr. Erickson concluded that Dr. Smith's three-growth rate regression model did not select the three growth rates which in combination are most highly correlated with yield, as she asserts. He also concluded that the selection of growth rates is very unstable in Dr. Smith's methodology, and that the statistical "constant" accounts for more than 97% of the contribution of her statistical analysis so that the effect of individual company data cannot enter meaningfully into her results. Dr. Erickson then analyzed the algebraic development of Dr. Smith's regression model and testified that, because of fatal flaws in that model (especially the "omitted variables" problem), Dr. Smith could not produce a valid cost of equity by such model. As a result of his study of Dr. Smith's regression analysis, Dr. Erickson concluded that "I am convinced that Dr. Smith's methodology does not produce

an accurate or reliable estimate of the cost of capital for Duke Power Company."

The determination of the appropriate fair rate of return for Duke is of great importance and must be made with great care because whatever return is allowed will have an immediate impact on Duke, its stockholders, and its customers. In the final analysis, the determination of a fair rate of return must be made by this Commission, using its own impartial judgment and guided by the testimony of expert witnesses and other evidence of record. Whatever return is allowed must balance the interest of the ratepayers and investors and meet the test set forth in G.S. 62-133(b)(4):

> "...(to) enable the public utility by sound management to produce a fair return for its shareholders, considering changing economic conditions and other factors, as they then exist, to maintain its facilities and services in accordance with the reasonable requirements of its customers in the territory covered by its franchise, and to compete in the market for capital funds on terms which are reasonable and which are fair to its customers and to its existing investors."

The return allowed must not burden ratepayers any more than is necessary for the utility to continue to provide adequate service. The North Carolina Supreme Court has stated that the history of G.S. 62-133(b):

> "...supports the inference that the Legislature intended for the Commission to fix rates as low as may be reasonably consistent with the requirements of the Due Process Clause of the Fourteenth Amendment to the Constitution of the United States..." State ex rel. Utilities Commission v. Duke Power Co., 285 N.C. 377, 206 S.E. 2d 269 (1974).

The nature of the evidence in a case such as this makes it extremely difficult to balance all of the opposing interests, since much, if not all, of the evidence is based on individual witnesses' perceptions and interpretations of trends and data from the capital market. The Commission has considered carefully all of the relevant evidence presented in this case, with the constant reminder that whatever return is allowed will have an immediate impact on the Company, its stockholders and its customers. The Commission must use its impartial judgment to ensure that all the parties involved are treated fairly and equitably.

Based upon the foregoing and the entire record in this docket, including evidence related to the debt-equity swap, the Commission finds and concludes that the fair rate of return that Duke Power Company should have the opportunity to earn on the original cost of its rate base is 11.84%. Such overall fair rate of return will yield a fair and reasonable return on common equity capital of 15.25%.

The Commission cannot guarantee that the Company will, in fact, achieve the level of returns herein found to be just and reasonable. Indeed, the Commission would not guarantee it if it could. Such a guarantee would remove necessary incentives for the Company to achieve the utmost in operational and managerial efficiency. The Commission believes, and thus concludes, that the level of return approved herein will afford the Company a reasonable opportunity to earn a reasonable return for its stockholders while providing adequate and economical service to ratepayers.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 17

The Commission has previously discussed its findings and conclusions regarding the fair rate of return which Duke Power Company should be afforded an opportunity to earn. However, there is one remaining issue concerning the cost of capital to be discussed. This issue concerns the propriety of the cost of capital rate; i.e., the allowance of funds used during construction (AFUDC) rate utilized by the Company during November and December 1982. This question arises as a result of the full Commission's having issued its Order upon Reconsideration in Docket No. E-7, Sub 338, which in part reduced the Company's authorized return on common equity from 15.50% to 15.22%. The Commission sitting as a panel had by Order issued on November 1, 1982, set the Company's authorized return on common equity at 15.50%. Subsequently, by Order issued on January 13, 1983, the full Commission modified the panel Order. Such modification included a reduction of the return on equity from 15.50% to 15.22%. Thus, the question before the Commission is: what is the proper cost of common equity capital to be used in capitalizing AFUDC for the months of November and December 1982?

After having very carefully considered the entire evidence of record in this regard, including the nature and effect of the full Commission's modification to the panel Order and the prospective nature of the January 13, 1983, Order, the Commission concludes that the rate utilized by Duke for the capitalization of AFUDC during the months of November and December 1982, was entirely consistent and proper.

The following schedules summarize the gross revenues and the rates of return which the Company should have a reasonable opportunity to achieve based upon the determination made herein. Such schedules, illustrating the Company's gross revenue requirements, incorporate the findings and the conclusions heretofore and herein made by the Commission.

SCHEDULE I
DUKE POWER COMPANY
NORTH CAROLINA RETAIL OPERATIONS
DOCKET NO. E-7, SUB 358
STATEMENT OF OPERATING INCOME
TWELVE MONTHS ENDED SEPTEMBER 30, 1982
(000'S OMITTED)

Item	Present Rates	Increase Approved	After Approved Increase
Operating revenues			
Net operating revenues	$1,470,600	$ 76,235	$1,546,835
Operating revenue deductions			
Operating and maintenance	757,317	-	757,317
Depreciation and amortization	118,781	-	118,781
Taxes - other than income	122,677	4,574	127,251
Interest on customer deposits	372	-	372
Income taxes	186,473	35,286	221,759
Amortization of investment tax credit	(3,680)	-	(3,680)
Property abandonment amortization	23,263	-	23,263
Total operating revenue deductions	1,205,203	39,860	1,245,063
Net operating income for return	$ 265,397	$ 36,375	$ 301,772

SCHEDULE II
DUKE POWER COMPANY
NORTH CAROLINA RETAIL OPERATIONS
DOCKET NO. E-7, SUB 358
STATEMENT OF RATE BASE AND RATE OF RETURN
TWELVE MONTHS ENDED SEPTEMBER 30, 1982
(000'S OMITTED)

Item	Approved Rates
Investment in Electric Plant	
Electric plant in service	$ 3,640,170
Construction work in progress	282,481
Less: Accumulated depreciation	(1,263,605)
Accumulated deferred income taxes	(289,937)
Operating reserves	(10,599)
Net investment in electric plant	2,358,510
Allowance for Working Capital	
Materials and supplies - fuel stock	84,604
Materials and supplies - other	52,764
Required bank balances	653
Investor funds advanced for operations	57,146
Less: Customer deposits	(5,081)
Total working capital	190,086
Net original cost rate base	$ 2,548,596
Rate of Return:	
- Present	10.41%
- Approved	11.84%

SCHEDULE III
DUKE POWER COMPANY
NORTH CAROLINA RETAIL OPERATIONS
STATEMENT OF CAPITALIZATION AND RELATED COSTS
TWELVE MONTHS ENDED SEPTEMBER 30, 1982
(000'S OMITTED)

Item	Ratio %	Original Cost Rate Base	Embedded Cost %	Net Operating Income
		Present Rates		
Long-term debt	47	$1,197,840	9.83	$117,748
Preferred stock	13	331,318	8.62	28,560
Common equity	40	1,019,438	11.68	119,089
Total	100	$2,548,596	-	$265,397
		Approved Rates		
Long-term debt	47	$1,197,840	8.83	$117,748
Preferred stock	13	331,318	8.62	28,560
Common equity	40	1,019,438	15.25	155,464
Total	100	$2,548,596	-	$301,772

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 18 - 20

Public Staff witness Richard Smith presented testimony and evidence concerning the Company's load management program.

Witness Smith recommended: (1) that the Company's Residential Load Control Rider LC(NC) be amended to provide that the Company offer to set thermostats lower on controlled water heaters; (2) that the Company's rate schedule RC(NC) be amended to include minimum efficiency standards for heat pumps and central air conditioners; and (3) that the Company's low income weatherization program be amended to require that volunteer organizations which promote and install the weatherization must also promote and sign up customers for the Company's water heater and air conditioner load control program.

Resetting Thermostats on Controlled Water Heaters

Witness Smith recommended that the Company offer to reduce the customer's water heater thermostat to 140 degrees if the residence has a dishwasher (or 120 degrees if it does not) whenever the Company installs a water heater load control device at the residence. He contended that the water heater kWh usage would thereby be reduced approximately 6% to 8%, and that VEPCO has successfully implemented such a program in its North Carolina service area.

The Commission notes that the Company does not currently propose to reset thermostats for water heaters and that the contractors who install the load control devices might charge the Company an additional fee to reset the water heater thermostat. The Commission is not persuaded that it should require the Company to offer to reset the thermostats on controlled water heaters at this time.

Efficiency Standards for Heat Pumps and Air Conditioners

Witness Smith recommended that the Company's residential energy conservation rate schedule RC be amended to require, in addition to the current thermal insulation requirements, minimum efficiencies for heat pumps and central air conditioners if such equipment is installed. For heat pumps, he proposed a minimum Seasonal Energy Efficiency Rate (S.E.E.R.) of 8.0 and an S.E.E.R. of 8.5 for air conditioners. He stated that the standards would be applied only to equipment being installed after the standards are in effect, including replacements of original equipment.

The Commission notes that there were a number of questions raised concerning the appropriate forum for minimum efficiency standards of heat pumps and air conditioners, the relative efficiencies of alternative types of furnaces, and the relative cost of alternative sources of space conditioning. The Commission is of the opinion that rate schedule RC might be enhanced by including minimum efficiency standards for heat pumps and central air conditioners and that the matter should be studied in greater detail before a final determination is made by the Commission.

Low Income Weatherization Program

Witness Smith recommended that the Company provide volunteer organizations which are installing the weatherization kits under the Company's low income weatherization program with the necessary information so that they can promote

and sign up customers for the Company's water heater and air conditioner load control program. He indicated that the personal one-on-one contact by volunteers would be more effective in reaching customers under the low income weatherization program than mailers and bill stuffers. Witness Smith envisioned that customers under the low income weatherization program would not be required to sign up for load control and that the Company would install all load control devices and not the volunteers.

The Commission notes that the Company does not currently have residential load control available throughout its system in North Carolina, and it is of the opinion that the volunteer organizations might create some confusion between the low income weatherization program and the residential load control program. The Commission suggests that volunteers could make known to the customers the fact that the residential load control program exists and that they could encourage the customers to check with the Company concerning the program. The Commission concludes that the volunteer organizations should not be required to promote and sign up customers for the residential load control program.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 21 - 24

Company witnesses Hatley and Jenkins, Public Staff witness Turner, CIGFUR witness Phillips, and Kudzu witness Eddleman presented testimony and evidence regarding rate design.

Basic Customer Charges

The Company proposed in this proceeding to increase its basic customer charges for all major rate schedules by the same percentage as the other rate blocks, including a proposed increase in the residential customer charge from $5.40 per month to $5.82 per month. The proposed customer charges were unopposed by any party.

The Commission is of the opinion that the customer charges had been established at a level which was significantly below cost in previous rate cases for reasons discussed in those cases and that such customer charges should now be moved closer to actual customer-related costs. The Commission notes that the proposed residential customer charge is still less than the residential customer charge which this Commission has allowed for CP&L and Vepco. In view of the relative increases for the various residential energy blocks discussed herein, the Commission concludes that the residential customer charge should be increased to $5.80 per month and that the nonresidential customer charges should be approved at the levels proposed by the Company.

Residential Water Heater Discount

In the previous general rate case in Docket No. E-7, Sub 338, the Commission directed that the matter of water heating (WH) discounts in Schedule R be discussed in the next proceeding.

In this proceeding, witness Hatley presented data illustrating the cost differential between customer groups in Schedule R (i.e., with or without the water heating discount). The data shows that rates of return are higher for customers with the WH discount than for customers without the WH discount,

although customers with the WH discount have a higher load factor than do customers without the WH discount (based on demand at time of summer peak).

However, the Commission notes that the customers in Schedule R with WH discounts have a far greater proportion of their total usage in the second block (i.e., 350 to 1300 kWh) vs. the first block (i.e., 0 to 350 kWh) of the rate sechdule than do customers without WH discounts. Since the rate level of the second block is considerably higher than the first block (even with the WH discount), the tendency would be for customers with WH discounts to pay a higher average price per kWh over the first two blocks than customers without WH discounts. The higher average price per kWh over the first two blocks could explain the higher rate of return for customers with WH discounts, especially if it should turn out that there was no cost differential between the two groups of customers. When the rate blocks are flattened as described herein, the average price per kWh over the first two blocks should be closer together for the two groups of customers, and the difference in rates of return between the two groups should be reduced.

The Commission also notes that the data presented in this case does not explain why a discount, if any, should be applied only to the second block of the rate schedule instead of to the entire schedule. Both CP&L and Vepco have eliminated the WH discount from their residential rate schedules for North Carolina retail service.

The Commission is not persuaded that a WH discount is as appropriate as it once was and is of the opinion that the Company's WH discount should be reduced somewhat in this proceeding consistent with the flattening of the rate blocks described herein.

Summer/Winter Differential in Residential Rates

The Company proposes to increase the size of the summer/winter rate differential for all over 1300 kWh in each residential rate schedule while keeping the percentage difference essentially constant.

In the Company's previous general rate proceeding in Docket No. E-7, Sub 338, the Commission concluded that the summer/winter rate differentials should not be increased until such time as it could be determined what size summer/winter differential would be appropriate for each rate block of each rate schedule, and it reduced the summer/winter differential for Schedule R to a level more comparable with Schedules RA and RC.

Public Staff witness Turner pointed out in this proceeding that cost studies supporting summer/winter differentials generally did not indicate a differential for one rate class and not another, and they generally did not indicate a differential for one rate block within a given rate schedule and not another. He recommended that the summer/winter differential continue to be held at the present rate level until a more definitive study of such rate differentials can be made.

Company witness Jenkins responded that the summer/winter rate differential is intended to encourage residential heating load which would help balance the summer and winter peak loads on the system. He contended that residential electric heating customers save the other system customers approximately $58,000,000, such figure representing the fixed costs recovered from the

residential heating customers through the winter rate block (i.e., over 1300 kWh in winter).

The Commission notes that while it can be argued that eliminating the residential heating load would leave $58,000,000 of fixed costs to be recovered from other customers, it can also be argued that eliminating the residential air conditioning load would leave at least $58,000,000 of fixed costs to be recovered from other customers. Certainly no party in this proceeding is advocating a discount for air conditioning load.

A more appropriate basis for comparison is to note that for all practical purposes the elimination of all winter load probably would not eliminate the need for any of the Company's generating plants, and the elimination of all summer load probably would not eliminate the need for any of the Company's generating plants. Summer users of the system benefit winter users of the system by sharing the recovery of fixed costs, and vice versa.

If there is a difference in cost to serve customers during summer versus winter, it would seem more likely to involve differences in generation mix between seasons, and the differences in fixed costs and variable costs associated with such differences in generation mix.

The Commission is not persuaded that a summer/winter rate differential of the magnitude proposed herein is appropriate, or that such rate differential should be applied only to residential customers, or that such rate differential should be applied only for usage over 1300 kWh per month. It would be highly desirable to base a determination of appropriate summer/winter rate differentials on information as to the fixed costs and variable costs incurred by each customer group during each hour of the year (and each season of the year).

The Commission concludes that the summer/winter rate differentials in the residential rates should not be increased until such time as it can be determined what size summer/winter differential would be appropriate for each rate block of each rate schedule.

Multiple Block Rates for Residential Service

The Company proposes to retain three energy blocks in its residential rate schedules. The Commission concluded in previous general rate proceedings that rates should accurately track costs in a manner consistent with the intent of the Public Utility Regulatory Policies Act (PURPA) and that multiple rate blocks and declining block rates should no longer be applied unless it can be demonstrated that such rate features will track costs more accurately than the simple and straightforward single block rate.

Company witnesses Hatley and Jenkins contended in this proceeding that usage in the first block (i.e., 0 to 350 kWh) represented year round usage, such as nonair conditioning and nonheating load. They further contended that usage in the second block (i.e., 350 to 1300 kWh) included air conditioning and heating load associated with additional demand at the time of the system peak, and therefore it contributed to a lower load factor for the system. They contended that usage in the third block (i.e., over 1300 kWh) included primarily heating load which was not accompanied by additional demand at the time of the system peak, and therefore it improved the system load factor.

Late filed data provided by the Company indicates that the load factor for residential customers is generally higher in summer than it is in winter (based on demand at time of system peak), which does not seem consistent with a higher priced second block (reflecting summer air conditioning load?) and a lower priced third block (reflecting winter heating load?). By comparison, the higher prices for General and Industrial customers are applied to lower load factor customers.

Public Staff witness Turner pointed out that it is possible for customer usage in the second block to be off-peak usage and that the Company has not quantified the difference in cost, if any, to serve usage within the second block versus usage outside the second block. He recommended that the rate blocks be reduced to a single block for all usage over 350 kWh per month.

The Commission is not persuaded that the multiple rate blocks proposed herein are appropriate. It would be very desirable to base a determination of the actual cost of service for different ranges of usage on information as to the fixed costs and variable costs incurred by each customer group during each hour of the year. In any event, it is imperative that the cost of service for different customer groups be studied further to determine the differences in cost of service for different ranges of usage in order to justify continued use of multiple rate blocks.

The Commission concludes that the multiple rate blocks should be flattened in this proceeding in order that the number of blocks may be reduced in future proceedings and that such rate blocks should be flattened in such a manner that no customer will receive a rate increase higher than that proposed by the Company herein.

Merger of Residential Rate Schedules R and RA

The three major residential rate schedules are Schedules R, RA, and RC. Schedule RA is applicable to residential customers having all-electric service, Schedule RC is applicable to customers meeting certain thermal requirements for conservation of energy, and Schedule R is applicable to residential customers who are not eligible for Schedules RA and RC.

Schedule RA has been closed to new customers since 1979, and all new residential customers must choose between R and RC. The Company merged a former Schedule RW into Schedule R in a previous proceeding (although merged Schedule R still contains a discount for qualifying water heaters). The Company has not yet proposed merging Schedule RA into Schedule R.

The Commission continues to be of the opinion that merger of Schedules R and RA should be accomplished over a period of time in order to give the RA customers a reasonable opportunity to achieve the benefits of their investment in all-electric facilities. However, such period of time should not remain indefinite, since new customers who would have qualified for Schedule RA are not being offered the same opportunities under the same circumstances.

The Company was directed in its previous rate case in Docket No. E-7, Sub 338, to present a proposal in this proceeding for merging Schedules RA and R over a period of time. The Company's response was to point out that customers who would qualify for Schedule RA would already qualify for the

water heating discount under Schedule R. Witness Hatley suggested that the way to merge Schedules RA and R was to establish a lower rate in the third block of Schedule R which would be comparable, to but not necessarily the same as, the third block of Schedule RA. He did not propose a time table for merging the schedules.

In the previous general rate proceeding in Docket No. E-7, Sub 338, the Commission reduced the summer/winter rate differential in the third block of Schedule R to a level more comparable with Schedule RA. The Commission is of the opinion that flattening the residential rate blocks as described herein would bring the level of all three rate blocks in Schedules R and RA closer together and would be an appropriate step toward merging Schedules R and RA, and it concludes that the matter of merging the rate schedules should continue to receive attention in future rate proceedings.

Nonresidential Declining Block Rates

The Company proposes to retain declining block rates within each section (i.e., three sections, or load factor ranges, per rate schedule) of its major nonresidential rate schedules. As discussed earlier herein concerning residential rate blocks, the Commission has concluded that multiple rate blocks and declining block rates should be eliminated where it cannot be demonstrated that they are cost justified.

Company witness Hatley conceded that the Company does not have a study to show whether the usage within a given rate block of any rate schedule is on-peak. As noted with respect to the residential rate blocks, the Commission is of the opinion that it would be highly desirable to base a determination of the actual cost of service for different ranges of usage on information as to the fixed costs and variable costs incurred by each customer group during each hour of the year.

The Commission concludes that the declining block rates for each section of the nonresidential rate schedules should be flattened in this proceeding in a manner which will ensure that no customer will receive a higher rate increase than that proposed by the Company herein. In the absence of appropriate cost studies as described herein, the Commission also concludes that it should reduce the revenue requirement for each section of a given nonresidential rate schedule by the same percentage in order to preserve the current average rate for each range of load factor until such time as it can be determined what cost differential would be appropriate for each section of each rate schedule.

Hopkinson Type Nonresidential Rates

Company witness Hatley testified that the Company's long-range goals for rate design included placing more emphasis on the separate demand charge (i.e., the Hopkinson type demand charge) in order to enhance customer understanding of demand and to make customers more demand conscious. As discussed in previous general rate decisions involving the Company, the Commission is of the opinion that Hopkinson type rate designs might be beneficial in that they greatly simplify the rates, and they give stronger and clearer price signals to encourage conservation of demand.

Public Staff witness Turner pointed out that the Hopkinson type rate design is more appropriate where customers are classified into homogeneous groups and that the Company does not currently classify its customers into homogeneous groups. He recommended that the separate Hopkinson type demand charge in the Company's nonresidential rate schedules be held at the level of the present rates until such time as it can be determined what is the appropriate difference between a demand charge per kW for high load factor customers versus low load factor customers.

In a previous general rate proceeding in Docket No. E-7, Sub 314, the Commission concluded that the matter of Hopkinson type rate designs for nonresidential customers should be explored thoroughly in a future rate proceeding, and it directed the Company to design rate schedules for the Commission's consideration which would include Hopkinson type rate design features. The Commission's intent was to obtain some understanding of the magnitudes involved in the various elements of a Hopkinson type rate, in order to better assess the possible impact of moving in the direction of Hopkinson type rates.

Unfortunately, the Commission was advised by the Company that the Hopkinson type rate designs subsequently filed with the Commission in February 1983 pursuant to the Order in Docket No. E-7, Sub 314, were not cost justified. Nevertheless, the Commission notes with interest the general relationship between the demand charges and energy charges for different load factor customers in the rate designs. For example, the demand charge per kW is higher for high LF customers than for low LF customers, which would recognize that generally the billing demand for high LF customers carries a greater coincidence factor than for low LF customers (i.e., the billing demand is closer to demand at the time of system peak for high LF customers than for low LF customers). Also, although the demand charge is highest for high LF customers, the combination of demand charges plus energy charges still results in a significantly lower overall charge per kWh for high LF customers than for low LF customers.

The Company did point out that a higher demand charge per kW for high LF customers than for low LF customers would cause an administrative problem by encouraging a high LF customer to increase its demand simply to lower its LF and thereby qualify for the lower demand charge per kW. The Commission notes that this emphasizes the necessity of maintaining customers in homogeneous groups when utilizing the Hopkinson type rate design.

The Commission concludes that the separate demand charge in the major nonresidential rate schedules should be held at the levels proposed by the Company in this proceeding in order to enhance the goal of moving toward Hopkinson type rates. Nevertheless, the Commission is of the opinion that the appropriate differences in demand charges for different customer groups (i.e., different load factor groups, etc.) should be established before moving very far down the path toward Hopkinson type rates. Therefore, the Commission also concludes that the Company should prepare a program for achieving its long range goal of Hopkinson type rates, including a discussion of timetables, implementation steps, makeup of customer groups, etc.

General

In addition to those revisions already discussed herein, the Company proposes various miscellaneous rate changes, administrative changes, and clarifications on its rate schedules which were not opposed by any party. Such changes and clarifications include in part: provisions to clarify the minimum billing requirements of nonresidential rate schedules G, GA, GB, I, and IP; provisions to clarify the description of "suburban" luminaires on lighting rate schedules T and T2; provisions to clarify the applicability of rates in schedules T and T2 to decorative and nonstandard luminaires; provisions to increase extra charges for special type poles in rate schedules T and T2 from $4.40 to $4.75 to reflect current costs; and provisions to reduce the customer charge for schedule RT.

The Commission concludes that the rate designs, rate schedules, and terms and conditions for service as proposed by the Company should all be approved, except as discussed herein.

IT IS, THEREFORE, ORDERED as follows:

1. That Duke Power Company be, and is hereby, allowed to adjust its electric rates and charges so as to produce, based upon the adjusted test year level of operations, an increase in annual gross revenues of $76,235,000 from its North Carolina retail operations. Said increase is effective for service rendered on and after the date of this Order.

2. That within five (5) working days after the date of this Order, Duke Power Company shall file with this Commission rate schedules designed to produce the increase in revenues set forth in Decretal Paragraph No. 1 above in accordance with the guidelines set forth in Appendix A attached hereto. Said rate schedules shall be accompanied by a computation showing the level of revenues which said rate schedules will produce by rate schedule, plus a computation showing the overall North Carolina retail rate of return and the rates of return for each rate schedule which will be produced by said revenues.

3. That Duke Power Company shall prepare cost allocation studies for presentation with its next rate application which allocate production plant based on the following methodologies: (1) summer/winter peak and average; (2) summer/winter peak and base; (3) summer/winter coincident peak; and (4) summer coincident peak. Both jurisdictional and fully distributed cost allocation studies shall be made using each method, and the studies shall be included in items 31 and 37, respectively, of Form E-1 of the minimum filing requirements for general rate applications.

4. That Duke Power Company shall work with the Public Staff during the six (6) months following the date of this Order to develop a mutually agreeable study which could be done at a reasonably limited cost and would be responsive to the concerns discussed in this proceeding regarding: (1) allocation of fixed costs and variable costs to each hour of the year and (2) allocation of costs incurred during a given hour to customer classes based on usage during the given hour. The Company shall report to the Commission on the details of the study from time to time as necessary, but not later than six (6) months following the date of this Order.

5. That Duke Power Company shall prepare a study for presentation to the Commission within 12 months after the date of this Order which addresses the proposal to establish minimum efficiency standards for heat pumps and central air conditioners under residential rate schedule RC(NC) as discussed herein, including cost and efficiency comparisons between alternative heating and cooling systems and the heat pumps/air conditioners subject to the proposed efficiency standards.

6. That Duke Power Company shall file with the Commission within six (6) months after the date of this Order a program outlining specific steps, timetables, makeup of customer classes, etc., associated with the Company's stated long-term goal of implementing Hopkinson type rate design for its major nonresidential customer classes.

7. That Duke Power Company shall give appropriate notice of the rate increase approved herein by mailing a copy of the notice attached hereto as Appendix B by bill insert to each of its North Carolina retail customers during the next normal billing cycle following the filing of the rate schedules described in Decretal Paragraph No. 2.

8. That any motions heretofore filed in this proceeding and not previously ruled upon are hereby denied.

ISSUED BY ORDER OF THE COMMISSION.
This the 30th day of September 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sandra J. Webster, Chief Clerk

APPENDIX A
DOCKET NO. E-7, SUB 358
GUIDELINES FOR DESIGN OF RATE SCHEDULES

Step 1: Determine the amount of rate schedule revenues and other revenues, respectively, which are necessary to produce the overall revenue requirement established by the Commission in this proceeding.

Step 2: Increase the rate schedule revenues produced by the present rates for each rate schedule by the same percentage to produce the total rate schedule revenues determined in Step 1.

Step 3: Increase the individual prices in a given rate schedule by the same percentage to reflect the increase in revenue requirement for the rate schedule as determined in Step 2, except as follows:

(a) Increase the customer charge for residential rate schedules R, RA, and RC to $5.80.

(b) Maintain the same differential between summer and winter rates as is contained in the present rate levels of the third block of residential rate schedules R, RA, and RC (i.e., 0.44¢, 0.49¢, and 0.44¢ for rate schedules R, RA, and RC, respectively).

(c) Increase the first block only (i.e., 0 to 350 kWh) of residential rate schedules R, RA, and RC as necessary to achieve the increase in revenue requirement for each rate scheduled, respectively, except do

not increase the first block above the levels proposed by the Company for said block.

(d) If the increase in revenue requirement is not achieved for residential rate schedules R, RA, and RC, although the first block is increased to the levels proposed by the Company, then hold the first block at the levels proposed by the Company and also increase the third block (i.e., over 1300 kWh summer and winter) as necessary to achieve the revenue requirement for each rate schedule, respectively; except do not increase the third block above the levels proposed by the Company for said block and do not neglect to maintain the same differential between summer and winter rates as is contained in the present rate levels.

(e) If the increase in revenue requirement is not achieved for residential rates schedules R, RA, and RC although the first block is increased to the levels proposed by the Company and the third block is increased to the levels proposed by the Company (or the levels necessary to maintain the appropriate summer/winter rate differential in the case of the third block-summer), then hold the first block at the levels proposed by the Company and also hold the third block at the levels proposed by the Company (or the levels necessary to maintain the appropriate summer/winter rate differential in the case of the third block-summer), and also increase the second block (i.e., 350 to 1300 kWh) as necessary to achieve the revenue requirement for each rate schedule, respectively; except hold the regular rate of the second block of Schedule R at the 6.22¢ per kWh present rate level while increasing only the WH discount rate (i.e., 5.65¢ per kWh at present rate level) in the second block of Schedule R.

(f) Increase the customer charge for nonresidential rate schedules G, GA, GB, I, and IP to the levels proposed by the Company.

(g) Increase the separate demand charge per kW for nonresidential rate schedules G, GA, I, and IP to the levels proposed by the Company.

(h) Increase the revenue requirement for each section (i.e., three sections, or load factor ranges, per rate schedule) for nonresidential rate schedules G, GA, GB, I, and IP by the same percentage in order to maintain the present ratio of revenue recovery between sections.

(i) Increase the third block only (i.e. over 90,000 kWh) of the first section (i.e., first 125 kWh per KW) of schedule G as necessary to achieve the increase in revenue requirement for said first section, except do not increase the third block above the level proposed by the Company for said block.

(j) If the increase in revenue requirement is not achieved for the first section of schedule G although the third block is increased to the level proposed by the Company, then hold the third block at the level proposed by the Company and also increase the second block (ie., 3000 to 90,000 kWh) as necessary to achieve the increase in revenue requirement for the first section of schedule G; except do not increase the second block above the level proposed by the Company for said block.

(k) If the increase in revenue requirement is not achieved for the first section of schedule G although the third block and the second block are increased to the levels proposed by the Company, then hold the third block and the second block at the levels proposed by the Company and also increase the first block (i.e., 0 to 3000 kWh) as necessary to achieve the increase in revenue requirement for the first section of schedule G.

(l) Increase the revenue requirement for each section (i.e., three sections per rate schedule) of nonresidential rate schedules G, GA, GB, I, and IP in the same manner as described for the first section of schedule G in order to flatten the rate blocks in each section, except for the third section (i.e., over 400 kWh per KW) of rate schedule GA.

(m) Increase the revenue requirement for the third section of rate schedule GA in such a manner that the rate blocks will be at the same level.

(n) Increase prices in the TOD rate schedules in such a manner that they will remain basically revenue neutral with comparable non-TOD rate schedules, considering projected peak demand savings for the TOD rates.

(o) Hold miscellaneous service charges and extra charges at the same level proposed by the Company.

Step 4: Round off individual prices to the extent necessary for administrative efficiency, provided said rounded off prices do not not produce revenues which exceed the overall revenue requirement established by the Commission in this proceeding.

APPENDIX B
DOCKET NO. E-7, SUB 358
UTILITIES COMMISSION DISAPPROVES ONE-THIRD OF DUKE POWER COMPANY'S PROPOSED RATE INCREASE REQUEST

The North Carolina Utilities Commission today, after several months of investigation and following three weeks of hearings held throughout the State, denied Duke's request for an increase of $112.9 million over rates currently in effect while approving an increase of $76.2 million. The Company's application for rate relief was filed with the Commission on February 1, 1983. The rate increase allowed by the Commission equates to an increase of 5.18% over rates now in effect as compared to an increase of 7.68% which would have resulted had the Company's full rate increase request been approved.

The Commission estimates that the bill of a typical residential customer using 1000 kWh per month and presently paying approximately $59.45 per month will increase to approximately $62.48 per month. However, the percentage increase will vary for different levels of usage in order to reflect more uniform rates per kWh for all levels of usage.

In allowing the 5.18% increase, the Commission found that the approved rates would provide Duke, under efficient management, an opportunity to earn an approximate 11.84% rate of return on the original cost of its property. In

its application, Duke had sought rates which would allow it to earn a rate of return of 11.94%.

Among the more controversial issues addressed by the Commission in its Order was the appropriate rate-making treatment to be accorded costs associated with Duke's decision to cancel construction of its Cherokee nuclear power production facility. Under the Commission's treatment of the Cherokee cancellation, Duke was denied approximately $9.4 million in annual revenue the Company had sought in order to cover its cost of capital associated with its unrecovered investment in Cherokee. The Commission concluded that its treatment in this regard results in a fair and equitable distribution of the cancellation cost burden between Duke's ratepayers and shareholders.

The increase granted was due principally to the Cherokee cancellation and the impact of general inflation on Duke's costs since its last general rate increase which became effective on November 1, 1982.

In the area of rate design, the Commission directed that additional steps be taken toward more uniform rates per kWh for all levels of usage within each rate schedule.

The rate increase will become effective for service rendered on and after September 30, 1983.

DOCKET NO. E-7, SUB 358

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of		
Application by Duke Power Company for	)	ORDER DENYING MOTIONS
Authority to Adjust and Increase Its	)	FOR RECONSIDERATION
Electric Rates and Charges	)	AND ORAL ARGUMENT; ORDER
	)	OF CLARIFICATION

BY THE FULL COMMISSION: On September 30, 1983, a three-member Commission Hearing Panel entered an Order in this docket entitled "Order Approving Partial Rate Increase."

Motions for Reconsideration were subsequently filed in this proceeding pursuant to G.S. 62-80 by the Attorney General, Great Lakes Carbon Corporation, and the Public Staff on October 6, 1983, October 26, 1983, and October 27, 1983, respectively. By these Motions for Reconsideration, the Full Commission has been requested to reconsider portions of the "Order Approving Partial Rate Increase" entered herein on September 30, 1983, and to schedule oral argument thereon related to the issues of the ten (10) year amortization period authorized by the Commission for the abandonment losses associated with Duke Power Company's cancelled Cherokee nuclear generating station, the fuel component of base rates established by the Commission, and the rate of return of 15.25% on common equity allowed Duke.

On November 10, 1983, Duke Power Company filed its Response in opposition to the above-referenced Motions for Reconsideration, whereby the Commission was requested to deny said motions.

Based upon a careful consideration of the Motions for Reconsideration filed herein by the Attorney General, Great Lakes Carbon Corporation, and the Public Staff, the Response thereto filed by Duke Power Company, and the entire record in this proceeding, the Full Commission concludes that said Motions for Reconsideration and requests for oral argument thereon should be denied.

Notwithstanding this denial of the pending Motions for Reconsideration, the Commission concludes that some clarification is necessary and appropriate with respect to the "Order Approving Partial Rate Increase" entered herein on September 30, 1983, concerning the issue of the fuel component of base rates established therein for Duke Power Company. The Attorney General, Great Lakes Carbon Corporation, and the Public Staff generally assert that the Commission relied upon "projected" fuel expenses rather than test year historical or normalized fuel expenses in establishing Duke's base fuel component and that the use of such "projections" is erroneous as a matter of law (G.S. 62-133) and policy.

Finding of fact number 9 of the "Order Approving Partial Rate Increase" entered herein on September 30, 1983, provides as follows:

> "9. A base fuel component of 1.3734¢ per kWh excluding gross receipts tax is appropriate for this proceeding, reflecting a reasonable base fuel cost of $408,542,000 for North Carolina retail service."

The Commission must regretfully acknowledge and cannot deny that in the "Evidence and Conclusions for Finding of Fact No. 9" set forth on pages 13 through 15 of the "Order Approving Partial Rate Increase" the word "projection" or some form thereof was in fact used on at least four (4) occasions regarding nuclear fuel costs, combustion turbine generation, coal fuel costs, pumped storage generation, purchased power, and net interchange power. Nevertheless, a careful review of the evidence and the entire record in this proceeding clearly indicates that the Commission did not, <u>in any manner</u>, rely upon unlawful "projections" in developing the fuel component of base rates found and established in this proceeding by the "Order Approving Partial Rate Increase." To the contrary, it is clear that the Commission obviously utilized techniques of <u>normalization related to actual historical fuel costs</u> and not "projections" in establishing a base fuel component of 1.3734¢ for Duke Power Company in this proceeding. The Commission further notes that, although the Attorney General, Great Lakes Carbon, and the Public Staff clearly disagree with and object to the normalized level of base fuel cost established herein, said parties do themselves generally advocate, and in fact did advocate in this proceeding, utilization of the technique of normalization by the Commission in establishing a reasonable base fuel cost. The evidence in this case clearly indicates that the Commission's use of the term "projection" or some form thereof in the "Order Approving Partial Rate Increase" was inadvertently substituted for the term "normalization" in referring to the determination of Duke's proper and reasonable level of base fuel costs. The mere fact that the Commission incorrectly used the term "projection" does not, and should not, obscure the fact that the fuel component of Duke's base rates was properly established on the evidence of record utilizing the technique of normalization and not projections.

In this regard, the record clearly indicates that the Commission properly and reasonably normalized Duke's nuclear fuel cost for purposes of setting

rates in this proceeding at 0.412¢ per kWh based upon Duke witness Stimart's testimony that said number reflects the Company's average nuclear fuel expense for all of its nuclear units after the reload or refueling of Oconee Unit 1. (Tr. Vol. 14, p. 271). Mr. Stimart's rebuttal testimony in this proceeding was presented on August 24 and August 25, 1983. Review of Duke Power Company's Base Load Power Plant Performance Report for the month of August 1983 indicates that the refueling of Oconee Unit 1 had in fact been completed and the unit had been returned to service by the time witness Stimart offered his rebuttal testimony herein. Thus, the Commission's normalization of Duke's nuclear fuel cost at a level of 0.412¢ per kWh properly reflects consideration of relevant, material and competent evidence offered by Duke Power Company pursuant to G.S. 62-133(c) tending to show actual changes in its nuclear fuel costs based upon circumstances and events occurring up to the time the hearing in this case was closed. Although the Commission Order dated September 30, 1983, states at page 14 that "Witness Stimart testified that the Company projects its actual nuclear fuel costs to be 0.412¢ per kWh for the period following the reloading of Oconee 1 (completed in August 1983)..." (emphasis added), it is clear from the record that Mr. Stimart did not himself use the terms "projects" in his testimony with reference to the refueling of Oconee Unit 1. To the contrary, Duke witness Stimart testified that "after the reload on Oconee Unit 1, the average nuclear fuel expense for all units is 4.12 mills/kWh. . ." (emphasis added). (Tr. Vol. 14, P. 271). Thus, the Commission appropriately normalized Duke's nuclear fuel costs pursuant to G.S. 62-133(c) and did not base its determination with respect thereto upon "projections" in abrogation of said statute.

In the "Order Approving Partial Rate Increase" entered herein on September 30, 1983, the Commission also adopted a unit cost of 1.811¢ per kWh for Duke's coal fuel costs in establishing the Company's normalized, rather than projected, level of base fuel costs. Here again, the Commission inadvertently used the term "projection," rather than "normalization," in connection with said costs. Nevertheless, the record clearly reflects that the unit cost for coal of 1.811¢ per kWh adopted by the Commission was in fact based upon Duke's actual cost for coal purchased during the month of June 1983, and that such unit price for coal was in fact less than the Company's average cost for coal of 1.837¢ per kWh during the period April through June 1983. (Tr. Vol. 14, p. 272). Thus, the unit cost for coal of 1.811¢ per kWh found reasonable in this case by the Commission is fully supported by the evidence as being based upon and reflecting an appropriate normalization of the Company's representative unit cost for coal for purposes of setting just and reasonable rates in this proceeding. The mere fact that the Commission inadvertently used the term "projection" in conjunction with Duke's coal costs cannot obscure the obvious fact that the unit price for coal found reasonable herein was based upon relevant, material and competent evidence pursuant to G.S. 62-133(c).

The same findings and conclusions set forth hereinabove also apply to the Commission's decision in the "Order Approving Partial Rate Increase" to normalize Duke's level of combustion turbine (CT) generation at 130 million kWh for purposes of establishing the Company's reasonable, normalized level of base fuel expense in this proceeding. Duke witness Stimart testified that said level of combustion turbine generation was based upon the average of such generation over the 2.75 year period ending September 30, 1982. (Tr. Vol. 14, p. 273; Tr. Vol. 15, p. 16). Thus, the Commission clearly established a level of combustion turbine generation for use in this proceeding in determining

Duke's reasonable cost of fuel based upon an historical and a normalized, rather than projected, level of CT generation, notwithstanding any inadvertent use of the term "projection" by the Commission with respect thereto in the "Order Approving Partial Rate Increase." Further, the fact that the 8.282¢ per kWh utilized by the Commission for purposes of normalizing the Company's reasonable level of CT fuel oil costs also contains some costs for natural gas is of no legal significance or consequence since both oil and natural gas are apparently used to fuel Duke's CT generators. Although the Commission specifically concluded that 8.282¢ per kWh was the appropriate normalization of CT fuel oil costs, the evidence of record indicates that such unit fuel cost includes costs for both oil and natural gas, which is entirely appropriate and proper.

In the "Order Approving Partial Rate Increase," the Commission also concluded at page 15 that ". . . the Public Staff's normalization of pumped storage generation, purchased power, and net interchange power represents an appropriate projection of the Company's use of those energy sources..." (emphasis added). Here again, it is obvious that the Commission, upon Public Staff recommendation, was utilizing the technique of normalization with regard to these elements of Duke's reasonable base cost of fuel and was not relying upon "projections." It is also clear that the use of the term "projection" by the Commission with reference to the level of pumped storage generation, purchased power, and net interchange power found to be appropriate for use in this proceeding was really meant to reflect normalization thereof as was in fact advocated by the Public Staff. In this regard, it is interesting to note that none of the parties requesting reconsideration herein made any mention whatsoever in their respective motions of this particular use of the term "projection" by the Commission in the Order of September 30, 1983, whereby the Commission adopted the Public Staff's recommended levels of generation.

Accordingly, the Full Commission concludes that the base fuel component of 1.3734¢ per kWh adopted by the Commission Hearing Panel in the "Order Approving Partial Rate Increase" was properly based upon the principles and techniques of normalization rather than "projections" and was fully and lawfully supported in the record by relevant, material, and competent evidence.

IT IS, THEREFORE, ORDERED as follows:

1. That the Motions for Reconsideration filed herein by the Attorney General, Great Lakes Carbon Corporation, and the Public Staff on October 6, 1983, October 26, 1983, and October 27, 1983, respectively, be, and the same are hereby, denied.

2. That the "Order Approving Partial Rate Increase" entered in this docket on September 30, 1983, be, and the same is hereby, clarified in conformity with this Order.

ISSUED BY ORDER OF THE FULL COMMISSION.
This the 6th day of December 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sandra J. Webster, Chief Clerk

DOCKET NO. E-13, SUB 44

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Application of Nantahala Power and Light Company for Authority to Adjust and Increase Its Electric Rates and Charges) NOTICE OF DECISION AND ORDER

HEARD IN: Swain County Courthouse, Bryson City, North Carolina, on September 27, 1983, and the Commission Hearing Room, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina 27602, on September 29 and 30, 1983 and October 3, 4, 5, 6, 17 and 18, 1983

BEFORE: Commissioner Edward B. Hipp, Presiding; and Commissioners Leigh H. Hammond and Ruth E. Cook

APPEARANCES:

For Nantahala Power and Light Company

Robert C. Howison, Jr., James E. Tucker, Edward Finley, Jr., and Darla B. Tarletz, Hunton and Williams, Attorneys at Law, P. O. Box 109, Raleigh, North Carolina 27602

For Aluminum Company of America and Tapoco, Inc.

Ronald D. Jones, David R. Poe and Dennis P. Harkawik, LeBoeuf, Lamb, Leiby and McRae, Attorneys at Law, 336 Fayetteville Street, 7th Floor, Raleigh, North Carolina 27602

For the Attorney General:

Richard L. Griffin, Assistant Attorney General, and JoAnne Sanford, Special Deputy Attorney General, North Carolina Department of Justice, P. O. Box 629, Raleigh, North Carolina 27602
For: The Using and Consuming Public

For the Public Staff:

James D. Little, Chief Counsel, and Thomas K. Austin, Staff Attorney, Public Staff - North Carolina Utilities Commission, P. O. Box 991, Raleigh, North Carolina 27602
For: The Using and Consuming Public

For the Intervenors:

William Crisp and Robert F. Page, Crisp, Davis, Schwentker and Page, Attorneys at Law, P. O. Box 751, Raleigh, North Carolina 27602
For: Counties of Cherokee, Graham, Jackson, Macon and Swain; Towns of Andrews, Bryson City, Dillsboro, Robbinsville and

Sylva; Tribal Council of Eastern Band of Cherokee Indians; and Henry J. Truett, Howard Paton, Veronica Nicholas, O. W. Hooper, Jr., and Alvin E. Smith

David H. Permar, Hatch, Little, Bunn, Jones, Few and Berry, Attorneys at Law, P. O. Box 527, Raleigh, North Carolina 27608
For: Jackson Paper Manufacturing Company

BY THE COMMISSION: On February 1, 1983, Nantahala Power and Light Company (Applicant, Company or Nantahala) filed an application with the North Carolina Utilities Commission seeking to increase its rates and charges for retail electric service in North Carolina effective March 4, 1983. The application proposed an annual increase in gross annual revenues of the Company of approximately 6.9%.

On February 7, 1983, the Attorney General of the State of North Carolina filed a Notice of Intervention in the case on behalf of the using and consuming public.

On February 16, 1983, the Public Staff filed Notice of Intervention on behalf of the using and consuming public.

On February 21, 1983, Jackson Paper Manufacturing Company filed petition to intervene. By Order issued February 23, 1983, the Commission allowed the intervention of Jackson Paper Manufacturing Company.

On March 1, 1983, the Commission issued an Order suspending the Applicant's proposed rates.

On March 1, 1983, a petition for leave to intervene was filed on behalf of the Counties of Cherokee, Graham, Jackson and Swain; the Towns of Andrews, Bryson City, Billsboro, Robbinsville and Sylva; and by the Tribal Council of the Eastern Band of Cherokee Indians; and by Henry J. Truett, Howard Paton, Veronica Nicholas, O. W. Hooper, Jr. and Alvin E. Smith. On July 19, 1983, said petition was amended to include the County of Macon. The Commission issued an Order allowing the original petition to intervene on March 10, 1983, and issued an Order allowing the intervention of the County of Macon on August 9, 1983.

On April 22, 1983, the Commission issued an Order which scheduled hearings on the application with hearings to be held in the service area in Bryson City on September 27, 1983, and to resume in Raleigh on September 29, 1983.

On August 9, 1983, the Commission issued an Order which joined Aluminum Company of America (Alcoa) and Tapoco, Inc. (Tapoco) as parties.

Other motions, pleadings and Commission Orders filed in this docket may be found in the official file in this matter. The application came on for hearing at the places and times as ordered by the Commission. All parties were present and represented by counsel.

At the hearing held in Bryson City on September 27, 1983, nine members of the public testified. The resumed proceedings came on for hearing in Raleigh as scheduled.

Nantahala offered the testimony of the following witnesses: N. Edward Tucker, Jr., Vice President - Finance and Treasurer of Nantahala; Joseph F. Brennan, President of Associated Utility Services, Inc.; Stuart G. McDaniel, Senior Vice President of Associated Utility Services, Inc.; John K. Carson, Manager - Client Services, for Ebasco Business Consulting Company; and Dale M. Keith, Project Manager - Black and Veatch, Engineers/Architects.

Testifying on behalf of the Intervenors Public Staff, Attorney General and County of Cherokee, et al were: Dr. Robert Weiss, Director of the Economic Research Division of the Public Staff; Benjamin Turner, Engineer - Electric Division of the Public Staff; Candace Paton, Staff Accountant - Accounting Division of the Public Staff; David A. Springs, Senior Vice President of Southern Engineering Company; and J. Bertram Solomon of Southern Engineering Company.

Testifying for Intervenor Jackson Paper Manufacturing Company were Richard J. Rudden, President of R. J. Rudden Associates, Inc., and Donald L. Alexander of Dixie Container Corporation.

The following witnesses testified on behalf of Alcoa and Tapoco: David A. Toof, Manager in the Washington Office of the Ernst and Whinney Utility Group; John Devlin, Manager with Ernst and Whinney; and William W. Lindsay, Vice President of NPS Energy Management, Inc.

Nantahala offered the rebuttal testimony of the following witnesses: Dale Kenneth Hollister, First Vice President in the Regulated Industries Finance Department with Dean Witter Reynolds; Richard C. Crawford, Director of the Division of Energy Use and Distribution Relations with the Tennessee Valley Authority; and Bruce A. Ainsworth, Project Civil Engineer in the Power Division of Black and Veatch.

Alcoa and Tapoco offered rebuttal testimony by Christopher Scott, President of the North Carolina AFL/CIO.

Based on the foregoing, the evidence adduced at the hearing and the entire record in this matter, the Commission makes the following

FINDINGS OF FACT

1. Nantahala is a duly organized public utility company under the laws of the State of North Carolina, subject to the jurisdiction of this Commission, and is holding a franchise to furnish electric power in the western part of North Carolina under rates and services regulated by this Commission as provided by Chapter 62 of the General Statutes.

2. The test period for purposes of this proceeding is the 12-month period ended December 31, 1981, adjusted for certain known changes based upon circumstances and events occurring up to the time of the close of hearings in this docket.

3. By its application, Nantahala is seeking an increase in its basic rates and charges to its North Carolina retail customers of $1,443,283.

4. The overall quality of electric service provided by Nantahala to its North Carolina retail customers is adequate.

5. Both Nantahala and Tapoco, Inc. are wholly-owned subsidiaries of Aluminum Company of America.

6. The 1962 New Fontana Agreement and the 1971 Apportionment Agrement expired by their own terms on December 31, 1982. The New Fontana Agreement was replaced by an Interconnection Agreement negotitated independently by Nantahala with the Tennessee Valley Authority (TVA). Nantahala's entire generating capacity is from hydroelectric stations, two of which have water storage dams and nine of which are run-of-the-river generators. By controlling its water releases under the 1983 Interconnection Agreement, Nantahala can supply most of its customers' needs from its own hydroelectric generation during normal water conditions and average consumption hours and seasons. During low water and peak consumption periods, Nantahala can supplement its available generation by outside purchases of power from TVA or other suppliers at the most advantageous cost available at such times. During high water and flood seasons when consumption is low, Nantahala will have to release water from its storage when its consumers will have no use for the resulting generation, and Nantahala can then sell such surplus power to TVA at the most advantageous price available at such time, and its consumers will get full benefit of the proceeds of such sales in setting Nantahala's rates. The 1983 Interconnection Agreement between Nantahala and TVA provides substantial benefits to the Company's retail ratepayers in North Carolina which were not present under the New Fontana Agreement and the 1971 Apportionment Agreement. Changed conditions reflected in the 1983 Interconnection Agreement, which became effective January 1, 1983, include, but are not limited to, the following: Nantahala now dispatches and controls the operation of all of its hydroelectric generating facilities and retains for itself and its customers all of the Company's hydroelectric generation; Nantahala operates and dispatches said system in order to best meet its load requirements and depends upon TVA only for the purchase of its capacity and energy needs above and beyond that which the Company can generate for itself; Nantahala is assured of a firm supply of supplemental and back-up power and energy from TVA, without limitation, when the Company's own generation cannot meet its load; Nantahala is permitted to utilize, without limitation, any other source of supplemental power which may be available, including the addition of new generating capacity to the Company's system and/or purchases from other suppliers; and Nantahala can sell its excess generation to TVA. Nantahala's North Carolina retail rates should, therefore, be established in this proceeding in recognition of and pursuant to the more favorable terms and benefits of the 1983 Interconnection Agreement.

7. The New Fontana Agreement and 1971 Apportionment Agreement resulted in substantial concealed benefits accruing to Alcoa to the significant detriment of the customers of Nantahala. No direct benefits now accrue to Alcoa as a result of the 1983 Interconnection Agreement to the detriment of Nantahala's customers. Furthermore, if any indirect benefits enure to Alcoa as a result of said agreement, any such indirect benefits do not appear to be the result of unlawful preference having been shown to Alcoa by Nantahala to the significant detriment of Nantahala's customers.

8. The roll-in in methodology proposed herein by the Intervenors for pro forma purposes in fixing Nantahala's rates without any accompanying order from the appropriate federal jurisdiction requiring the physical sale of Tapoco power to Nantahala or a guarantee of Nantahala's financial integrity by Alcoa will ultimately result in insolvency or bankruptcy of Nantahala and an

inability of Nantahala to meet its customers' needs for electric power, and will not serve the best interests of Nantahala's customers or its service area in North Carolina. Further, if and when the federal jurisdiction having authority to allocate Tapoco power to the Nantahala service area should order such allocation, then the Commission can reopen this docket to readjust the rates of Nantahala to reflect the actual cost of such purchases from Tapoco as may be approved by said federal jurisdiction.

9. The Nantahala electric system should be treated independently of Tapoco in this proceeding with respect to all matters affecting the determination of Nantahala's reasonable cost of service applicable to its North Carolina retail operations. Under the 1983 Interconnection Agreement, Nantahala is a stand alone hydroelectric power company which operates its 11 hydroelectric generation stations for the sole benefit of its customers, all of which are in North Carolina, without any obligation to or regard for the TVA or Tapoco hydro stations in North Carolina and Tennessee or for Alcoa's power use in Tennessee. Further, Alcoa receives no power or any other direct benefit from Nantahala's power generation. All of the benefits of the generation from Nantahala's entire hydroelectric system are retained exclusively for the use and benefit of the North Carolina customers of Nantahala, whose entire service is confined to its service area in North Carolina. Thus, the roll-in methodology advocated herein by the Intervenors and previously utilized by the Commission in prior dockets in making cost of service allocations is not appropriate for use in setting Nantahala's retail rates in this proceeding. Consequently, each finding of fact appearing in this Order which deals with a proper level of rate base, revenues, and expenses has been determined based upon Nantahala's stand-alone levels of revenues and costs.

10. Nantahala should actively and thoroughly investigate and pursue alternatives to purchasing power from TVA, including, in particular, power purchases from Tapoco, in order to secure for its retail ratepayers purchase power at the lowest possible cost.

11. Nantahala should continue to adjust its rates through use of the purchase power adjustment (PPA) clause pursuant to G.S. 62-130(d). A base unit cost of 1.132757 ¢/kwh for purchase power (excluding gross receipts tax) is appropriate for use in this proceeding, reflecting a reasonable base cost for purchase power of $6,138,500 for North Carolina retail service. The base unit cost of 1.132757 ¢/kwh for purchase power found reasonable herein shall be utilized by Nantahala in future PPA filings which are proposed to become effective subsequent to the date of this Order and until such time as a new base unit cost for purchase power is set by the Commission.

12. Inclusion of $406,209 of reasonable and prudent expenditures for construction work in progress (CWIP) in Nantahala's rate base is in the public interest and is necessary to the financial stability of the Company.

13. Nantahala's net original cost of electric plant is $24,772,451, consisting of electric plant in service of $61,289,278; construction work in progress of $406,209; reduced by accumulated provision for depreciation of $33,012,528; accumulated deferred income taxes of $3,861,645; and accumulated deferred investment tax credit (pre-1971) of $48,863.

14. The reasonable allowance for working capital is $1,134,937, consisting of cash working capital of $594,010, materials and supplies of $519,025, FERC

license expense of $98,243, unamortized maintenance of $144,516, less customer deposits of $220,857.

15. Nantahala's rate base is $25,907,388. This amount consists of net original cost of electric plant of $24,772,451, plus a reasonable allowance for working capital of $1,134,937.

16. The approximate gross revenues from electric operations for the test year, after accounting and pro forma adjustments, under rates in effect at the time of the application are $20,868,973 and after giving effect to the Company proposed increase, are $22,312

17. The approximate level of test year operating expenses under rates in effect at the time of the application, after accounting and pro forma adjustments, including taxes and interest on customer deposits, is $18,259,159, which includes an amount of $1,863,668 for actual investment currently consumed through reasonable, actual depreciation after annualization to year-end levels.

18. The reasonable capital structure to be employed as a basis for setting rates in this proceeding is composed as follows:

Item	Ratio
Long-term Debt	43.9%
Common Equity	56.1%
Total	100.0%

19. The proper embedded cost of long-term debt is 8.72%. The reasonable rate of return Nantahala should be allowed to earn on common equity is 15.5%. Use of a weighted average for the cost of debt and common equity, with reference to the reasonable capital structure heretofore determined, yields an overall fair rate of return of 12.52% to be applied to the Company's original cost rate base. Such rate of return will enable Nantahala, by sound management, to produce a fair return for its shareholders, to maintain its facilities and service in accordance with the reasonable requirements of its customers, and to compete in the market for capital funds on terms which are reasonable and fair to customers and its existing investors.

20. The approximate annual level of revenue which Nantahala should be authorized to collect through rates charged for its sales of service, based upon the findings of fact set forth hereinabove, is $22,204,830. Such level of revenue reflects a required increase of $1,335,857 over the test year level of revenue ($20,868,973) which would be produced under rates in effect at the time this rate application was filed.

21. Nantahala's proposed rate design and service rules are reasonable and appropriate as modified herein.

22. Nantahala should base all residential customer billings on monthly meter readings as ordered in Docket No. E-13, Sub 35.

23. Nantahala should list the Purchased Power Adjustment as a separate item on each billing.

24. Nantahala should undertake studies, in conjunction with the Public Staff, to determine the feasibility of time-of-use rates, including seasonal rates, and load control of residential water heating and central air conditioning.

25. The proposed rate schedule LIS (Large Industrial Service) should not be approved in this proceeding.

Based upon the findings of fact set forth hereinabove, the Commission concludes that the appropriate annual level of revenues which Nantahala should be authorized to collect through rates charged for its sales of service based upon the adjusted test year level of operations is $22,204,830. The following charts summarize the gross revenues and the rates of return which the Company should have a reasonable opportunity to achieve, based upon the level of revenues approved herein. Such charts, illustrating the Company's gross revenue requirements, incorporate the findings, adjustments and conclusions herein made by the Commission:

SCHEDULE I
NANTAHALA POWER AND LIGHT COMPANY
Docket No. E-13, Sub 44
North Carolina Retail Operations
STATEMENT OF RATE BASE AND RATE OF RETURN

For the Test Year Ended December 31, 1981

Item	Amount
Electric plant in service	$61,289,278
Construction work in progress	406,209
Materials and supplies	519,025
Cash working capital	594,010
Subtotal	62,808,522
Add:	
FERC license adjustment	98,243
Unamortized maintenance	144,516
Less:	
Accumulated depreciation	33,012,528
Accumulated deferred income taxes	3,861,645
Accumulated deferred investment tax credit pre-1971	48,863
Customer deposits	220,857
Total original cost rate base	$25,907,388
Rate of Return:	
Present rates	10.07%
Approved rates	12.52%

SCHEDULE II
NANTAHALA POWER AND LIGHT COMPANY
Docket No. E-13, Sub 44
North Carolina Retail Operations
STATEMENT OF OPERATING INCOME FOR RETURN

For the Test Year Ended December 31, 1981

Item	Present Rates	Approved Increase	After Approved Increase
Operating Revenues:			
Sales of electricity	$20,623,491	$1,335,857	$21,959,348
Other operating revenues	245,482	-	245,482
Total operating revenues	20,868,973	1,335,857	22,204,830
Operating Expenses:			
Purchased power expense	6,138,500	-	6,138,500
Other O&M expenses	7,151,238	5,611	7,156,849
Depreciation & amortization	1,863,668	-	1,863,668
Taxes other than income	1,720,108	79,815	1,799,923
Income taxes:			
State	183,158	75,026	258,184
Federal	1,083,062	540,686	1,623,748
Deferred in prior years	(78,960)	-	(78,960)
Investment tax credits	275,566	-	275,566
Amortization of ITC	(77,181)	-	(77,181)
Total operating expenses	18,259,159	701,138	18,960,297
Net operating income	$ 2,609,814	$ 634,719	$3,244,533

SCHEDULE III
NANTAHALA POWER AND LIGHT COMPANY
Docket No. E-13, Sub 44
North Carolina Retail Operations
STATEMENT OF CAPITALIZATION AND RELATED COSTS

Twelve Months Ended December 31, 1981

Item	Ratio %	Original Cost Rate Base	Embedded Cost %	Net Operating Income
		Present Rates		
Long-term debt	43.9	$11,373,343	8.72	$ 991,756
Common equity	56.1	14,534,045	11.13	1,618,058
Total	100.0	$25,907,388	-	$2,609,814
		Approved Rates		
Long-term debt	43.9	$11,373,343	8.72	$ 991,756
Common equity	56.1	14,534,045	15.50	2,252,777
Total	100.0	$25,907,388	-	$3,244,533

An Order setting forth the evidence and conclusions in support of this decision wil be issued subsequently. The Commission will consider the time for filing exceptions and notice of appeal in this proceeding to run from the date of issuance of such Order.

IT IS, THEREFORE, ORDERED as follows:

1. That the appropriate annual level of revenues which Nantahala is hereby authorized to collect for rates charged for its sales of service, based upon adjusted test year level of operations, is $22,204,830. Rates designed to produce the $1,335,857 annual increase approved herein shall be effective for service rendered on and after the date of this Order.

2. That Nantahala shall file for Commission approval, within ten (10) working days of the issuance date of this Order, rate schedules designed to provide the revenues set forth in Decretal Paragraph No. 1 above. Said rate schedules shall be designed in a manner consistent with that proposed by Nantahala in its application as filed in this docket; provided, however, that such rates shall be scaled downward so as not to exceed the annual level of revenue herein allowed. Such rate filing shall be accompanied by a computation showing the level of revenues which said rate schedules will produce by rate schedule, plus a computation showing the overall retail rate of return and the rate of return for each rate schedule which will be produced by said revenues.

3. That the Large Industrial Service (LIS) Schedule of rates proposed in this proceeding should be, and hereby is, denied.

4. That Nantahala shall begin calculating monthly bills for all residential customers based on monthly meter readings within 90 days after the date of this Order, said 90-day period being the time allowed for acquiring and training the additional staff and equipment necessary to implement such monthly meter readings.

5. That Nantahala shall study the feasibility of offering to its customers rate schedules based on time-of-use and on-peak control of residential customers loads such as water heaters and air conditioners and shall report its findings to the Commission within a reasonable period of time.

6. That Nantahala shall include the Purchased Power Adjustment as a separate item on each customer billing.

7. That any motions heretofore filed in this docket which have not been previously ruled upon be, and the same are hereby, denied.

8. That Nantahala Power and Light Company shall give appropriate public notice of the rate increase approved herein by mailing a copy of the notice attached hereto as Appendix A to each of its North Carolina retail customers during the next normal billing cycle following the filing and acceptance of the rate schedules approved in Decretal Paragraph No. 2 above.

9. That Nantahala shall actively and thoroughly investigate and pursue alternatives to purchasing power from TVA, including, in particular, power purchases from Tapoco, in order to secure for its retail ratepayers purchase power at the lowest possible cost. Further, that Nantahala shall file testimony in conjunction with its next general rate case specifically detailing the action which it has undertaken in compliance with this decretal paragraph.

ISSUED BY ORDER OF THE COMMISSION.
This the 29th day of November 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sandra J. Webster, Chief Clerk

APPENDIX A
DOCKET NO. E-13, SUB 44

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Application of Nantahala Power and Light)
Company for Authority to Adjust and Increase) NOTICE TO CUSTOMERS
Its Electric Rates and Charges)

A three-member panel of the North Carolina Utilities Commission, after months of investigation and following hearings held in Bryson City and Raleigh, issued its Order today allowing Nantahala Power and Light Company (Nantahala) to increase its electric rates and charges currently in effect by 6.40%. The Company's application for rate relief was filed with the Commission on February 1, 1983. Nantahala had requested an increase of $1.4 million annually over rates then in effect. The Commission's Order allows Nantahala an annual increase of $1.3 million.

The Commission estimates that the bill of a typical residential customer using 1,000 kWh per month and presently paying approximately $46.36 per month will increase to approximately $50.24 per month. Such increase reflects a purchased power cost adjustment of 0.8165¢ per kWh for usage in December 1983. The cost of purchased power fluctuates monthly due to a variety of factors, thereby necessitating the continuation of Nantahala's purchased power adjustment clause (PPA). Such rates compare favorably with those of Carolina Power & Light Company (CP&L) and Duke Power Company, the two major electric utilities operating in North Carolina. The bill of a typical CP&L residential customer is currently $69.98 per month and the bill of a typical Duke customer is currently $62.48.

In allowing the 6.40% increase, the Commission found that the approved rates would provide Nantahala, under efficient management, an opportunity to earn an approximate 12.52% rate of return on the original cost of its property. In its application, Nantahala had sought rates which would allow it to earn a rate of return of 12.81%.

In reaching its decision to allow the increase, the Commission ruled that a 1983 Interconnection Agreement between Nantahala and the Tennessee Valley Authority (TVA) provided substantial benefits to the Company's retail ratepayers in North Carolina which were not present under previous agreements between Nantahala, Aluminum Company of America (ALCOA), Tapoco, Inc. (Tapoco), and TVA. The Commission in two previous cases had ruled that the agreements between the parties in effect prior to the 1983 Interconnection Agreement resulted in substantial concealed benefits accruing to Alcoa to the significant detriment of the customers of Nantahala.

The Commission's decision issued today will not affect its earlier decisions relating to two previous Commission rate orders which are now on appeal in the courts, as it is based on changed conditions brought about under

the Nantahala-TVA 1983 Interconnection Agreement. The prior Commission decisions require Nantahala and/or ALCOA to make refunds to Nantahala's North Carolina retail customers in an amount which is now estimated to be in a range from $35 million to $40 million.

Further, the North Carolina Utilities Commission has filed a legal action with the Federal Energy Regulatory Commission (FERC) requesting that Tapoco be required to make low cost hydro generation available to Nantahala for use in serving its public load. FERC has regulatory jurisdiction over Tapoco. Should the N.C. Commission's request be granted, Nantahala's rates will be readjusted to reflel steps
be taken toward more uniform rates of return for each rate schedule. The rate increase will become effective for service rendered on and after November 29, 1983.

DOCKET NO. E-13, SUB 44

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Application of Nantahala Power and Light Company for Authority to Adjust and Increase Its Electric Rates and Charges) ORDER GRANTING PARTIAL RATE INCREASE

HEARD IN: Swain County Courthouse, Bryson City, North Carolina, on September 27, 1983, and the Commission Hearing Room, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina 27602, on September 29 and 30, 1983 and October 3, 4, 5, 6, 17 and 18, 1983

BEFORE: Commissioner Edward B. Hipp, Presiding; and Commissioners Leigh H. Hammond and Ruth E. Cook

APPEARANCES:

For Nantahala Power and Light Company:

Robert C. Howison, Jr., James E. Tucker, Edward Finley, Jr., and Darla B. Tarletz, Hunton and Williams, Attorneys at Law, P. O. Box 109, Raleigh, North Carolina 27602

For Aluminum Company of America and Tapoco, Inc.:

Ronald D. Jones, David R. Poe and Dennis P. Harkawik, LeBoeuf, Lamb, Leiby and McRae, Attorneys at Law, 336 Fayetteville Street, 7th Floor, Raleigh, North Carolina 27602

For the Attorney General:

Richard L. Griffin, Assistant Attorney General, and JoAnne Sanford, Special Deputy Attorney General, North Carolina Department of Justice, P. O. Box 629, Raleigh, North Carolina 27602
For: The Using and Consuming Public

For the Public Staff:

James D. Little, Chief Counsel, and Thomas K. Austin, Staff Attorney, Public Staff - North Carolina Utilities Commission, P. O. Box 991, Raleigh, North Carolina 27602
For: The Using and Consuming Public

For the Intervenors:

William Crisp and Robert F. Page, Crisp, Davis, Schwentker and Page, Attorneys at Law, P. O. Box 751, Raleigh, North Carolina 27602
For: Counties of Cherokee, Graham, Jackson, Macon and Swain; Towns of Andrews, Bryson City, Dillsboro, Robbinsville and Sylva; Tribal Council of Eastern Band of Cherokee Indians; and Henry J. Truett, Howard Paton, Veronica Nicholas, O. W. Hooper, Jr., and Alvin E. Smith

David H. Permar, Hatch, Little, Bunn, Jones, Few and Berry, Attorneys at Law, P. O. Box 527, Raleigh, North Carolina 27608
For: Jackson Paper Manufacturing Company

BY THE COMMISSION: On February 1, 1983, Nantahala Power and Light Company (Applicant, Company or Nantahala) filed an application with the North Carolina Utilities Commission seeking to increase its rates and charges for retail electric service in North Carolina effective March 4, 1983. The application proposed an annual increase in gross annual revenues of the Company of approximately 6.9%.

On February 7, 1983, the Attorney General of the State of North Carolina filed a Notice of Intervention in the case on behalf of the using and consuming public.

On February 16, 1983, the Public Staff filed Notice of Intervention on behalf of the using and consuming public.

On February 21, 1983, Jackson Paper Manufacturing Company filed petition to intervene. By Order issued February 23, 1983, the Commission allowed the intervention of Jackson Paper Manufacturing Company.

On March 1, 1983, the Commission issued an Order suspending the Applicant's proposed rates.

On March 1, 1983, a petition for leave to intervene was filed on behalf of the Counties of Cherokee, Graham, Jackson and Swain; the Towns of Andrews, Bryson City, Billsboro, Robbinsville and Sylva; and by the Tribal Council of the Eastern Band of Cherokee Indians; and by Henry J. Truett, Howard Paton, Veronica Nicholas, O. W. Hooper, Jr. and Alvin E. Smith. On July 19, 1983, said petition was amended to include the County of Macon. The Commission issued an Order allowing the original petition to intervene on March 10, 1983, and issued an Order allowing the intervention of the County of Macon on August 9, 1983.

On April 22, 1983, the Commission issued an Order which scheduled hearings on the application with hearings to be held in the service area in Bryson City on September 27, 1983, and to resume in Raleigh on September 29, 1983.

On August 9, 1983, the Commission issued an Order which joined Aluminum Company of America (Alcoa) and Tapoco, Inc. (Tapoco) as parties.

Other motions, pleadings and Commission Orders filed in this docket may be found in the official file in this matter. The application came on for hearing at the places and times as ordered by the Commission. All parties were present and represented by counsel.

At the hearing held in Bryson City on September 27, 1983, nine members of the public testified. The resumed proceedings came on for hearing in Raleigh as scheduled.

Nantahala offered the testimony of the following witnesses: N. Edward Tucker, Jr., Vice President - Finance and Treasurer of Nantahala; Joseph F. Brennan, President of Associated Utility Services, Inc.; Stuart G. McDaniel, Senior Vice President of Associated Utility Services, Inc.; John K. Carson, Manager - Client Services, for Ebasco Business Consulting Company; and Dale M. Keith, Project Manager - Black and Veatch, Engineers/Architects.

Testifying on behalf of the Intervenors Public Staff, Attorney General and County of Cherokee, et al were: Dr. Robert Weiss, Director of the Economic Research Division of the Public Staff; Benjamin Turner, Engineer - Electric Division of the Public Staff; Candace Paton, Staff Accountant - Accounting Division of the Public Staff; David A. Springs, Senior Vice President of Southern Engineering Company; and J. Bertram Solomon of Southern Engineering Company.

Testifying for Intervenor Jackson Paper Manufacturing Company were Richard J. Rudden, President of R. J. Rudden Associates, Inc., and Donald L. Alexander of Dixie Container Corporation.

The following witnesses testified on behalf of Alcoa and Tapoco: David A. Toof, Manager in the Washington Office of the Ernst and Whinney Utility Group; John Devlin, Manager with Ernst and Whinney; and William W. Lindsay, Vice President of NPS Energy Management, Inc.

Nantahala offered the rebuttal testimony of the following witnesses: Dale Kenneth Hollister, First Vice President in the Regulated Industries Finance Department with Dean Witter Reynolds; Richard C. Crawford, Director of the Division of Energy Use and Distribution Relations with the Tennessee Valley Authority; and Bruce A. Ainsworth, Project Civil Engineer in the Power Division of Black and Veatch.

Alcoa and Tapoco offered rebuttal testimony by Christopher Scott, President of the North Carolina AFL/CIO.

On November 29, 1983, the Commission entered a "Notice of Decision and Order" in this docket.

Based on the foregoing, the evidence adduced at the hearing and the entire record in this matter, the Commission makes the following

FINDINGS OF FACT

1. Nantahala is a duly organized public utility company under the laws of the State of North Carolina, subject to the jurisdiction of this Commission, and is holding a franchise to furnish electric power in the western part of North Carolina under rates and services regulated by this Commission as provided by Chapter 62 of the General Statutes.

2. The test period for purposes of this proceeding is the 12-month period ended December 31, 1981, adjusted for certain known changes based upon circumstances and events occurring up to the time of the close of hearings in this docket.

3. By its application, Nantahala is seeking an increase in its basic rates and charges to its North Carolina retail customers of $1,443,283.

4. The overall quality of electric service provided by Nantahala to its North Carolina retail customers is adequate.

5. Both Nantahala and Tapoco, Inc. are wholly-owned subsidiaries of Aluminum Company of America.

6. The 1962 New Fontana Agreement and the 1971 Apportionment Agreement expired by their own terms on December 31, 1982. The New Fontana Agreement was replaced by an Interconnection Agreement negotitated independently by Nantahala with the Tennessee Valley Authority (TVA). Nantahala's entire generating capacity is from hydroelectric stations, two of which have water storage dams and nine of which are run-of-the-river generators. By controlling its water releases under the 1983 Interconnection Agreement, Nantahala can supply most of its customers' needs from its own hydroelectric generation during normal water conditions and average consumption hours and seasons. During low water and peak consumption periods, Nantahala can supplement its available generation by outside purchases of power from TVA or other suppliers at the most advantageous cost available at such times. During high water and flood seasons when consumption is low, Nantahala will have to release water from its storage when its consumers will have no use for the resulting generation, and Nantahala can then sell such surplus power to TVA at the most advantageous price available at such time, and its consumers will get full benefit of the proceeds of such sales in setting Nantahala's rates. The 1983 Interconnection Agreement between Nantahala and TVA provides substantial benefits to the Company's retail ratepayers in North Carolina which were not present under the New Fontana Agreement and the 1971 Apportionment Agreement. Changed conditions reflected in the 1983 Interconnection Agreement, which became effective January 1, 1983, include, but are not limited to, the following: Nantahala now dispatches and controls the operation of all of its hydroelectric generating facilities and retains for itself and its customers all of the Company's hydroelectric generation; Nantahala operates and dispatches said system in order to best meet its load requirements and depends upon TVA only for the purchase of its capacity and energy needs above and beyond that which the Company can generate for itself; Nantahala is assured of a firm supply of supplemental and back-up power and energy from TVA, without limitation, when the Company's own generation cannot meet its load; Nantahala is permitted to utilize, without limitation, any other source of supplemental power which may be available, including the addition of new generating capacity to the Company's system and/or purchases from other suppliers; and

Nantahala can sell its excess generation to TVA. Nantahala's North Carolina retail rates should, therefore, be established in this proceeding in recognition of and pursuant to the more favorable terms and benefits of the 1983 Interconnection Agreement.

7. The New Fontana Agreement and 1971 Apportionment Agreement resulted in substantial concealed benefits accruing to Alcoa to the significant detriment of the customers of Nantahala. No direct benefits now accrue to Alcoa as a result of the 1983 Interconnection Agreement to the detriment of Nantahala's customers. Furthermore, if any indirect benefits enure to Alcoa as a result of said agreement, any such indirect benefits do not appear to be the result of unlawful preference having been shown to Alcoa by Nantahala to the significant detriment of Nantahala's customers.

8. The roll-in methodology proposed herein by the Intervenors for pro forma purposes in fixing Nantahala's rates without any accompanying order from the appropriate federal jurisdiction requiring the physical sale of Tapoco power to Nantahala or a guarantee of Nantahala's financial integrity by Alcoa will ultimately result in insolvency or bankruptcy of Nantahala and an inability of Nantahala to meet its customers' needs for electric power, and will not serve the best interests of Nantahala's customers or its service area in North Carolina. Further, if and when the federal jurisdiction having authority to allocate Tapoco power to the Nantahala service area should order such allocation, then the Commission can reopen this docket to readjust the rates of Nantahala to reflect the actual cost of such purchases from Tapoco as may be approved by said federal jurisdiction.

9. The Nantahala electric system should be treated independently of Tapoco in this proceeding with respect to all matters affecting the determination of Nantahala's reasonable cost of service applicable to its North Carolina retail operations. Under the 1983 Interconnection Agreement, Nantahala is a stand alone hydroelectric power company which operates its 11 hydroelectric generation stations for the sole benefit of its customers, all of which are in North Carolina, without any obligation to or regard for the TVA or Tapoco hydro stations in North Carolina and Tennessee or for Alcoa's power use in Tennessee. Further, Alcoa receives no power or any other direct benefit from Nantahala's power generation. All of the benefits of the generation from Nantahala's entire hydroelectric system are retained exclusively for the use and benefit of the North Carolina customers of Nantahala, whose entire service is confined to its service area in North Carolina. Thus, the roll-in methodology advocated herein by the Intervenors and previously utilized by the Commission in prior dockets in making cost of service allocations is not appropriate for use in setting Nantahala's retail rates in this proceeding. Consequently, each finding of fact appearing in this Order which deals with a proper level of rate base, revenues, and expenses has been determined based upon Nantahala's stand-alone levels of revenues and costs.

10. Nantahala should actively and thoroughly investigate and pursue alternatives to purchasing power from TVA, including, in particular, power purchases from Tapoco, in order to secure for its retail ratepayers purchase power at the lowest possible cost.

11. Nantahala should continue to adjust its rates through use of the purchase power adjustment (PPA) clause pursuant to G.S. 62-130(d). A base unit cost of 1.132757 ¢/kwh for purchase power (excluding gross receipts tax)

is appropriate for use in this proceeding, reflecting a reasonable base cost for purchase power of $6,138,500 for North Carolina retail service. The base unit cost of 1.132757 ¢/kwh for purchase power found reasonable herein shall be utilized by Nantahala in future PPA filings which are proposed to become effective subsequent to the date of this Order and until such time as a new base unit cost for purchase power is set by the Commission.

12. Inclusion of $406,209 of reasonable and prudent expenditures for construction work in progress (CWIP) in Nantahala's rate base is in the public interest and is necessary to the financial stability of the Company.

13. Nantahala's net original cost of electric plant is $24,772,451, consisting of electric plant in service of $61,289,278; construction work in progress of $406,209; reduced by accumulated provision for depreciation of $33,012,528; accumulated deferred income taxes of $3,861,645; and accumulated deferred investment tax credit (pre-1971) of $48,863.

14. The reasonable allowance for working capital is $1,134,937, consisting of cash working capital of $594,010, materials and supplies of $519,025, FERC license expense of $98,243, unamortized maintenance of $144,516, less customer deposits of $220,857.

15. Nantahala's rate base is $25,907,388. This amount consists of net original cost of electric plant of $24,772,451, plus a reasonable allowance for working capital of $1,134,937.

16. The approximate gross revenues from electric operations for the test year, after accounting and pro forma adjustments, under rates in effect at the time of the application are $20,868,973 and after giving effect to the Company proposed increase, are $22,312,256 ($20,868,973 + $1,443,283).

17. The approximate level of test year operating expenses under rates in effect at the time of the application, after accounting and pro forma adjustments, including taxes and interest on customer deposits, is $18,259,159, which includes an amount of $1,863,668 for actual investment currently consumed through reasonable, actual depreciation after annualization to year-end levels.

18. The reasonable capital structure to be employed as a basis for setting rates in this proceeding is composed as follows:

Item	Ratio
Long-term Debt	43.9%
Common Equity	56.1%
Total	100.0%

19. The proper embedded cost of long-term debt is 8.72%. The reasonable rate of return Nantahala should be allowed to earn on common equity is 15.5%. Use of a weighted average for the cost of debt and common equity, with reference to the reasonable capital structure heretofore determined, yields an overall fair rate of return of 12.52% to be applied to the Company's original cost rate base. Such rate of return will enable Nantahala, by sound management, to produce a fair return for its shareholders, to maintain its facilities and service in accordance with the reasonable requirements of its customers, and to compete in the market for capital funds on terms which are reasonable and fair to customers and its existing investors.

20. The approximate annual level of revenue which Nantahala should be authorized to collect through rates charged for its sales of service, based upon the findings of fact set forth hereinabove, is $22,204,830. Such level of revenue reflects a required increase of $1,335,857 over the test year level of revenue ($20,868,973) which would be produced under rates in effect at the time this rate application was filed.

21. Nantahala's proposed rate design and service rules are reasonable and appropriate as modified herein.

22. Nantahala should base all residential customer billings on monthly meter readings as ordered in Docket No. E-13, Sub 35.

23. Nantahala should list the Purchased Power Adjustment as a separate item on each billing.

24. Nantahala should undertake studies, in conjunction with the Public Staff, to determine the feasibility of time-of-use rates, including seasonal rates, and load control of residential water heating and central air conditioning.

25. The proposed rate schedule LIS (Large Industrial Service) should not be approved in this proceeding.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 1, 2, 3, AND 5

The evidence for these findings of fact is contained in the verified application and in the record as a whole. These findings of fact are essentially procedural and jurisdictional in nature and are not contested.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 4

Company witness Tucker and the various public witnesses who appeared at the hearings in Bryson City presented testimony concerning the quality of service. The Commission notes that the record contains little, if any, evidence which would suggest problems regarding the quality of Nantahala's service to its customers. Therefore, the Commission concludes that the quality of electric service being furnished by Nantahala to its N. C. retail customers is adequate.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 6, 7, 8, 9, AND 10

Company witnesses Tucker, Carson, Keith, Crawford, and Ainsworth; Alcoa-Tapoca witnesses Toof, Devlin, and Lindsay; and Intervenor witnesses Springs and Solomon presented testimony and evidence regarding system operations, relationships between companies, contracts and agreements, cost allocation methodologies and the "roll-in" technique.

<u>Concealed Benefits to Alcoa Flowing From 1962 New Fontana Agreement and 1971 Apportionment Agreement</u>

In two general rate orders establishing rates for Nantahala in Docket Nos. E-13, Sub 29 (Remanded) and E-13, Sub 35 the Commission determined that it was improper to base cost allocations on demand and energy entitlements as

contained in the 1962 New Fontana Agreement and the 1971 Tapoco-Nantahala Apportionment Agreement as proposed by Nantahala. The Commission found that a number of inequities to Nantahala arising out of these agreements resulted in Alcoa receiving concealed benefits. For example, the 1971 Apportionment Agreement credited Nantahala with only 360 million kWh annually, whereas a 1963 agreement with Alcoa provided Nantahala with 360 million kWh minimum production plus Nantahala's actual production in excess of 360 million kWh. Under the 1971 agreement, Nantahala was deprived of 66 million kWh average energy production annually in comparison to the 1963 agreement with Alcoa. Since the production allowance in the TVA return entitlements was jointly shared by Nantahala and Tapoco under the 1962 New Fontana Agreement, the 66 million kWh detriment to Nantahala constituted a benefit to Tapoco that was passed on to Alcoa.

Furthermore, the 1971 apportionment agreement credited Nantahala with an assigned generating capacity of 54,300 kw whereas its actual dependable generating capacity is 81,800 kw. Since the capacity allowance in the TVA return entitlements was jointly shared by Nantahala and Tapoco under the 1962 New Fontana Agreement, any capacity needs of Nantahala between 54,300 kw and 81,800 kw represented an expense to Nantahala and, thus, a saving to Tapoco that was passed on to Alcoa as a concealed benefit.

In addition, Nantahala's loss of the right to control the storage and flow of water for Nantahala's facilities constituted a loss of considerable value for which loss Nantahala was entitled to compensation. Despite the fact that the 1962 New Fontana Agreement included in the TVA return entitlement a reimbursement by TVA for the right to operate Nantahala's projects, the 1971 Apportionment Agreement gave no credit to Nantahala for that reimbursement, and thus said reimbursement represented a savings to Tapoco that was passed on to Alcoa.

In summary, the 1962 New Fontana Agreement and 1971 Apportionment Agreement resulted in direct inequities to Nantahala and concealed benefits to Alcoa. The situation was further aggravated because the TVA return entitlements in the 1962 New Fontana Agreement were entirely designed to meet Alcoa's aluminum production needs and were not suitable for Nantahala's public service needs. Nantahala had energy production capacity and it had peaking capacity from its own generating stations, yet Nantahala gave up that energy production capacity and that peaking capacity with the result that it had to buy higher cost power from TVA to meet its peaking responsibilities and its energy production responsibilities.

Roll-In Rate-Making Technique

In *State of North Carolina ex rel. Utilities Commission v. Edmisten*, 299 N.C. 432 (1980), the North Carolina Supreme Court required the Commission to consider a roll-in method of ratemaking based upon Intervenors' assertion that such method would serve to cancel, or at least to true-up, concealed benefits which allegedly flowed to Alcoa from Nantahala and Tapoco by virtue of the 1971 agreements. The Court found that Nantahala's primary duty as a public utility is to serve its public customers. The Court stated that Nantahala should "not be allowed to structure its economic affairs or physical operations in such a way as to effect an unreasonable preference or advantage to anyone, including its parent Alcoa", and that Nantahala's customers should not be "denied the benefit of their utility's fairly regular harvests of

abundant energy." Id. The Supreme Court remanded the Docket No. E-13, Sub 29, case to the Commission to examine the roll-in rate-making technique and stated that if any "unlawful preferences were indeed accorded to Alcoa to the detriment of Nantahala's customers because of the separate corporate structures and the inter-corporate apportionment agreements, this rate-making device would seem to eliminate them." Id. at 443.

The Commission subsequently utilized the roll-in rate-making technique to establish rates for Nantahala in Docket Nos. E-13, Sub 29 (Remanded) and E-13, Sub 35. As pointed out in said rate orders, the purpose of the roll-in method of ratemaking was to cancel or at least to true-up the concealed benefits to Alcoa.

On December 6, 1983, the North Carolina Court of Appeals entered an opinion affirming the Commission Order of September 2, 1981, in Docket No. E-13, Sub 29 (Remanded) wherein the Commission utilized the roll-in methodology in setting Nantahala's rates. State of North Carolina ex rel. Utilities Commission v. Nantahala Power and Light Company, ___ N.C. App. ___ (1983).

The Intervenors urge the Commission to continue to establish Nantahala's rates through application of the roll-in rate-making technique in this proceeding. Intervenors maintain that the new contractual arrangements between Nantahala and TVA, and between Tapoco and TVA, merely constitute a continuation of the same pattern that existed in the past. Nantahala and Alcoa, on the other hand, argue that the basis for the roll-in applied in Docket Nos. E-13, Sub 29 (Remanded) and E-13, Sub 35 no longer exists, and that under the 1983 Nantahala/TVA Interconnection Agreement, the inequities of the 1962 New Fontana Agreement and 1971 Apportionment Agreement have disappeared.

The 1983 Nantahala/TVA Interconnection Agreement

The 1962 New Fontana Agreement and the 1971 Apportionment Agreement expired by their own terms on December 31, 1982. Effective January 1, 1983, the 1962 New Fontana Agreement and the 1971 Apportionment Agreement were superseded by the 1983 Nantahala/TVA Interconnection Agreement. Under the 1983 Nantahala/TVA Interconnection Agreement, Nantahala serves its own load with the full output of its own generating facilities. Nantahala purchases supplemental and standby power from TVA when its own load exceeds its own generation, such as in the event of adverse water conditions or equipment outages. Under Nantahala's 1983 agreement with TVA, Nantahala purchases capacity at TVA's average capacity costs, and it purchases energy at TVA's hour-by-hour, out-of-pocket energy costs excluding hydro generation. (TVA reserves the benefit of its own hydro generation for residential customers in the TVA service area.) In addition to the hour-by-hour, out-of-pocket energy costs, Nantahala must pay an adder in its energy rate. The adder is the greater of (1) the difference between TVA's projected annual energy charge (excluding hydro generation) to its wholesale customers versus its estimated out-of-pocket, hour-by-hour energy costs (excluding hydro generation); or (2) 15% of the hour-by-hour, out-of-pocket costs (excluding hydro generation). TVA's energy charge to its other wholesale customers contains substantial demand costs in addition to out-of-pocket, hour-by-hour energy costs, and the adder is designed to produce an energy charge to Nantahala comparable to TVA's energy charge to its other wholesale customers.

Intervenor witness Springs acknowledged that unlike the 1962 New Fontana Agreement and the 1971 Apportionment Agreement, the 1983 Nantahala/TVA Interconnection Agreement gives Nantahala full credit for its actual energy generated and almost full credit for its peaking capacity. Intervenors criticize the 1983 Agreement because they maintain that Nantahala is now cut away from the exchange concept, that the energy pricing concept in the 1983 Agreement is not cost-related, and that Alcoa should have bargained with TVA on Nantahala's behalf.

The Commission recognizes that an exchange agreement between Nantahala and TVA, whereby all of Nantahala's hydro generation is dispatched to TVA as it is produced, and whereby in return TVA dispatches power back to Nantahala as Nantahala needs it, would tend to levelize the need for Nantahala to purchase supplemental or standby power from TVA. The Commission is of the opinion that an exchange agreement between TVA and Nantahala would have tended to levelize the impact of increases and decreases in the cost of purchased power over time, but the net impact on rates to Nantahala's customers should be approximately the same in the long run whether Nantahala's actual generation is exchanged with TVA or not.

Witness Springs seems to maintain that a pricing mechanism whereby Nantahala must pay TVA's average capacity costs plus TVA's hour-by-hour energy costs would be harmful to Nantahala because Nantahala would then pay a share of the high capital cost of base load production plants without also getting an equal share of the low cost energy from such base load production plants. The Commission recognizes that TVA's energy charge to Nantahala is designed to approximately equal the energy charge to TVA's other wholesale customers. Nantahala's experience under the contract through the close of the hearing indicates that Nantahala's costs for electricity purchased from TVA have been lower than Alcoa's. The Commission also recognizes that pricing of the high capital cost of base load generating plants in a manner consistent with pricing of the low cost energy from such base load generating plants is a widespread concern affecting many if not most utility companies in the nation, and that such concern does not of itself demonstrate any unreasonable weakness in the Nantahala/TVA agreement.

Intervenors also maintain that Alcoa should have bargained on Nantahala's behalf and that such joint bargaining would have resulted in better terms to Nantahala. However, Intervenors have pointed to nothing in the Tapoco/TVA agreement to demonstrate that Alcoa's presence at the bargaining table resulted in a tangible improvement in the terms of the Tapoco/TVA agreement. Indeed, the client negotiator for TVA, Mr. Crawford, testified that Alcoa's presence or assistance in bargaining for Nantahala would not have affected the Nantahala/TVA agreement results.

Nantahala's entire generating capacity is from hydroelectric stations, two of which have water storage dams and nine of which are run-of-the-river generators. By controlling its water releases under the 1983 Interconnection Agreement, Nantahala can supply most of its customers' needs from its own hydroelectric generation during normal water conditions and average consumption periods. During low water or peak consumption periods, Nantahala can supplement its available generation by outside purchases of power from TVA or other suppliers at the most advantageous cost available at such times. During high water or low consumption periods, Nantahala will have excess generation for which it will have no use, and Nantahala can then sell such

surplus power to TVA or others at the most advantageous price available at such time, and its consumers will get full benefit of the proceeds of such sales in their rates.

The 1983 Interconnection Agreement between Nantahala and TVA provides substantial benefits to the Company's retail ratepayers in North Carolina which were not present under the 1962 New Fontana Agreement and the 1971 Apportionment Agreement. Changed conditions reflected in the 1983 Interconnection Agreement include, but are not limited to, the following: Nantahala now dispatches and controls the operation of all of its own hydroelectric generating facilities and retains for itself and its customers all of its own hydroelectric generation; Nantahala operates and dispatches said system in order to best meet its own load requirements and depends upon TVA only for the purchase of its capacity and energy needs above and beyond that which Nantahala can generate for itself; Nantahala is assured of a firm supply of supplemental and back-up power and energy from TVA, without limitation, when the Company's own generation cannot meet its load; Nantahala is permitted to utilize, without limitation, any other source of supplemental power which may be available, including the addition of new generating capacity to the Company's system and/or purchases from other suppliers; and Nantahala can sell its excess generation to TVA.

Under the 1983 Interconnection Agreement, Nantahala is a stand-alone hydroelectric power company which operates its 11 hydroelectric generation stations for the sole benefit of its customers in North Carolina, without any obligation to or regard for the TVA or Tapoco hydro stations in North Carolina and Tennessee or for Alcoa's power use in Tennessee. Alcoa receives no power or any other direct benefit from Nantahala's power generation. All of the benefits of the generation from Nantahala's entire hydroelectric system are retained exclusively for the benefit of the North Carolina customers of Nantahala, whose entire service is confined to its service area in North Carolina.

The Commission concludes that the 1983 Nantahala/TVA Interconnection Agreement and the control by Nantahala of its own generation facilities is a substantial improvement over Nantahala's previous arrangements, and that the 1983 Nantahala/TVA Interconnection Agreement provides substantial benefits to the Company's retail ratepayers in North Carolina which were not present under the 1962 New Fontana Agreement and the 1971 Apportionment Agreement.

Stand-Alone Rate-Making Technique

In Docket No. E-13, Sub 29 (Remanded) and E-13, Sub 35, this Commission found that the Nantahala and Tapoco electric facilities constituted a single, integrated electric system and were operated as such by TVA as a coordinated part of the TVA system. The Commission based its finding of a single, integrated system upon the facts that Nantahala and Tapoco were wholly-owned by one corporate parent, Aloca; that the facilities of Nantahala and Tapoco were located in contiguous areas in western North Carolina; that the Nantahala and Tapoco electric facilities were physically interconnected with each other; and that both companies were interconnected with TVA. The Commission found that power could be dispatched and transmitted from the facilities of one to the facilities of the other; and that the Original Fontana Agreement and the New Fontana Agreement treated the facilities of Nantahala and Tapoco without discrimination and made them an integral part of, and subjected them to

coordination with, the TVA system. By the terms of these Agreements, TVA received the output of all of the hydro resources of both Nantahala and Tapoco, except for three small projects of Nantahala. By the terms of these Agreements, Tapoco and Nantahala also turned over to TVA control of production and stream flow. Accordingly, TVA determined for Tapoco and Nantahala, as a single entity, both electric generation and stream flow. In turn, Tapoco and Nantahala received back from TVA certain entitlements of power which they divided between themselves in the 1971 Nantahala-Tapoco Apportionment Agreement.

The Commission reaffirms its previous findings and conclusions made in Docket Nos. E-13, Sub 29 (Remanded) and E-13, Sub 35, to the effect that the 1962 New Fontana Agreement and the 1971 Apportionment Agreement resulted in the accrual of substantial concealed benefits to Alcoa to the significant detriment of the customers of Nantahala. However, effective January 1, 1983, Nantahala entered into a separate agreement with TVA under which Nantahala retains, dispatches and controls the generation from its own hydroelectric generating plants, and under which Nantahala purchases supplemental and standby power from TVA. Effective January 1, 1983, Tapoco also entered into a separate agreement with TVA under which Tapoco conveys the generating output of its hydroelectric plants to TVA in return for entitlements from TVA which Tapoco uses to provide power to Alcoa in Tennessee. The execution of these new agreements with TVA substantially removes the underpinnings upon which rested the Commission's previous determinations that the roll-in methodology was appropriate.

Although the New Fontana Agrement and 1971 Apportionment Agreement undoubtedly resulted in substantial concealed benefits accruing to Alcoa to the significant detriment of the customers of Nantahala, no direct benefits now accrue to Alcoa as a result of the 1983 Interconnection Agreement to the detriment of Nantahala's customers. Furthermore, if any indirect benefits enure to Alcoa as a result of said agreement, any such indirect benefits do not appear to be the result of unlawful preference having been shown to Alcoa by Nantahala to the significant detriment of Nantahala's customers.

Under the current Nantahala/TVA contract, Nantahala controls its own generating resources, and Nantahala's customers are assured the full economic benefit of the output of Nantahala's hydroelectric generating projects. Nantahala and Tapoco no longer share joint return entitlements from TVA. The Commission therefore concludes that Nantahala and Tapoco should be treated as separate and independent entities for rate-making purposes and that Nantahala's retail rates in North Carolina should be established in this proceeding in recognition of and pursuant to the more favorable terms and benefits of the 1983 Interconnection Agreement.

Access to Tapoco Hydro Generation

The Commission notes that one implication of the Intervenors' criticism of the new relationship created between Nantahala, Tapoco and TVA by the 1983 agreements is that Tapoco power is not available to Nantahala. In the past, Intervenors have contended that there were concealed benefits flowing from Nantahala to Alcoa, and that Nantahala-Tapoco was a single, integrated system. The roll-in technique applied by the Commission in the previous cases was used to prevent the benefits of Nantahala's generation from improperly flowing to Aloca, and to proform Nantahala's rates as if there had been a

hypothetical roll-in of the two systems. The roll-in technique did not make the benefits of Tapoco's generation available to Nantahala. Intervenors and this Commission have now requested relief before the Federal Energy Regulatory Commission (FERC), regarding the issue of access by Nantahala to Tapoco power, an issue which should properly be decided in that forum by FERC.

Thus, the Commission concludes that without any accompanying order from the appropriate federal jurisdiction requiring the physical sale of Tapoco power to Nantahala, or a guarantee of Nantahala's financial integrity by Alcoa, the roll-in methodology proposed herein by the Intervenors for fixing Nantahala's rates will ultimately result in insolvency or bankruptcy of Nantahala and an inability of Nantahala to meet its customers' needs for electric power, and will not serve the best interests of Nantahala's customers or its service area in North Carolina. Further, if and when the federal jurisdiction having authority to order the sale of Tapoco power to Nantahala should order such sale, then the Commission can reopen this docket to readjust the rates of Nantahala to reflect the actual cost of such purchases from Tapoco.

Notwithstanding the fact that the 1983 Interconnection Agreement between Nantahala and TVA provides substantial benefits to the Company's retail ratepayers in North Carolina which were not present under the 1962 New Fontana Agreement and the 1971 Apportionment Agreement, the Commission concludes that Nantahala should actively and thoroughly investigate and pursue alternatives to purchasing power from TVA, including, in particular, power purchases from Tapoco, in order to secure for its retail ratepayers purchase power at the lowest possible cost.

In reaching all of the conclusions set forth hereinabove in support of Findings of Fact Nos. 6, 7, 8, 9, and 10, the Commission has carefully reviewed and considered the holding of the North Carolina Supreme Court in _State of North Carolina ex rel. Utilities Commission_ v. _Edmisten_, supra, the recent holding of the North Carolina Court of Appeals in _State of North Carolina ex rel. Utilities Commission_ v. _Nantahala Power and Light Company_, supra, the findings of fact and conclusions heretofore reached by the Commission in Docket Nos. E-13, Sub 29 (Remanded) and E-13, Sub 35, regarding utilization of the roll-in methodology, and the entire record in this docket.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 11

Company witnesses McDaniel and Carson and Public Staff witness Paton presented testimony and evidence regarding the purchase power adjustment clause.

Nantahala's rates have, for many years, contained a purchase power adjustment clause as an adjunct to its base rates. Under Nantahala's purchase power adjustment clause, rates are adjusted each month based upon a rolling average of purchase power expense for a prior three-month period. Since 1971, the output from Nantahala's hydroelectric generating resources has been insufficient to serve the complete needs of its customers, and Nantahala has purchased its stand-by and supplemental needs from TVA. Nantahala's monthly purchase power adjustments occur after filing and consideration of Nantahala's request by the Commission. Nantahala has never filed its requests to adjust purchase power expenses in accordance with G.S. 62-134(e), and the nature of its needs could not have been met by use of this statute. Under its 1983 contract with TVA, Nantahala dispatches and controls its own generation.

Under the 1962 New Fontana Agreement and the 1971 Apportionment Agreement, Nantahala received a levelized entitlement each month based upon estimated average stream conditions and purchased its needs in excess of said entitlement from TVA. Therefore, Nantahala's current purchase power costs are more likely to fluctuate as a result of water conditions, extreme weather and equipment unavailability than in the past. Nantahala's purchase power adjustment clause allows Nantahala to recover expeditiously increases in purchase power expense, and likewise allows Nantahala to expeditiously pass on reductions in purchase power expense to its customers.

North Carolina G.S. 62-130(d) states that: "The Commission shall from time-to-time as often as circumstances may require, change and revise or cause to be changed or revised any rates fixed by the Commission, or allowed to be changed by any public utility." Pursuant to the authority of this statutory provision, the Commission is of the opinion that it is appropriate for Nantahala to continue to adjust its rates through changes in the purchase power adjustment clause. In State of North Carolina ex rel. Utilities Commission v. Edmisten, 291 N.C. 327, 230 S.E.2d 651 (1976), the North Carolina Supreme Court authorized use of a Commission-approved automatic fuel adjustment clause pursuant to G.S. 62-130. The Court noted that instead of approving fixed monetary rates for electric service, the Commission may approve rates expressed as a formula which will vary with changes in the different elements that make up the formula.

The Commission finds that based on the above authority, Nantahala's purchase power adjustment clause is in all respects proper and approves same for use as an adjunct to the base rates approved herein.

Further, the Commission finds and concludes that the base unit cost of 1.132757¢/kWh, as advocated by Nantahala witness Carson, is proper for use with respect to the Company's future filings relating to the purchase power adjustment clause.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 12, 13, 14, AND 15

The Commission has previously concluded that it is inappropriate to use the roll-in technique in setting rates in this proceeding; therefore, in discussing the differences in rate base, revenues and expenses between the Company and the Intervenors in this and later sections of this Order, these differences will be based upon the Nantahala stand-alone methodology. There will be no further discussion of the differences between the parties arising solely from the use of the roll-in methodology.

The evidence for these findings of fact is found in the testimony and exhibits of Company witnesses McDaniel and Tucker, Public Staff witness Paton, and Intervenor witness Solomon.

The total difference between the parties under the stand-alone approach with respect to rate base totals $406,209, and results from the exclusion of construction work in progress (CWIP) from Nantahala's rate base by the Public Staff. Nantahala included in rate base current investment in CWIP added subsequent to December 31, 1979. Nantahala witness McDaniel testified that inclusion of CWIP is consistent with and in the public interest and necessary to the financial stability of Nantahala. Witness McDaniel testified that it is appropriate to include CWIP in rate base because of the increased demand

for electric service by present customers. Although customer costs are higher during the construction period of a project when CWIP is included in rate base, electric rates overall will be much less. The capitalized financing charges (AFUDC) that accrue during the construction period when CWIP is not included in rate base result in a significantly higher rate base when the plant becomes used and useful. This causes the customers to pay more return, greater depreciation expense and greater income tax on the additional earnings. Property taxes also increase, and the ability to utilize investment tax credit carry forwards and operating losses on a timely basis is diminished. Inclusion of CWIP in rate base prevents the sudden, precipitous increases in rates that occur when large construction projects become eligible for inclusion in rate base at completion. Customers, especially those who must accurately budget their future expenses, should prefer the gradual, orderly increase in rates that inclusion of CWIP in rate base allows. Inclusion of CWIP is necessary to Nantahala's financial stability. Inclusion of CWIP in rate base, in addition to increasing internal cash generation, improves fixed charge coverages needed to support the issuance of securities.

Public Staff witness Weiss testified that CWIP should not be included in rate base. Dr. Weiss testified that the CWIP issue is most relevant for electric utilities with heavy construction schedules and long lead times. For companies such as Nantahala with small construction projects that are completed quickly, the investors are capable of advancing the necessary funds without assistance from the ratepayers; that financial stability of Nantahala is essentially unaffected by the treatment of CWIP, which represents less than 2% of rate base; that pre-tax interest coverage is more than adequate at approximately 5.0 times and that this coverage is well into the AAA bond rating range according to Standard & Poor's.

The Commission notes that in light of the controversy that has existed since 1979 concerning the manner in which Nantahala's rates should be established, Nantahala has been unable to raise outside capital on any terms. Likewise, Nantahala has paid no dividends since early in 1979. The Commission believes it is essential that Nantahala improve and maintain its financial integrity. Inclusion of CWIP in rate base is one facet of the program adopted by the Commission in this Order that will enhance Nantahala's ability to raise the necessary capital on reasonable terms it needs in order to meet its customers' demand for electric energy.

Based upon the evidence presented on this issue, the Commission concludes that $406,209 of reasonable and prudent expenditures for construction work in progress should be included in Nantahala's rate base and that inclusion thereof is in the public interest and necessary to the financial stabilituy of the Company.

Further, the Commission concludes that the proper rate base for use in this proceeding is $25,907,388.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 16 AND 17

With respect to the test year level of operating revenue and operating revenue deductions, the differences between the parties arise, in all material respects, as a result of the use of different allocation techniques.

The Commission has previously adopted the allocation techniques employed by Nantahala for use herein. The Commission therefore concludes that the proper level of operating revenues, under rates in effect at the time of application, to be used in this proceeding is $20,868,973. Such sum is summarized as follows:

Item	Amount
Operating Revenues	
Sales of electricity	$20,623,491
Other operating revenues	245,482
Total Operating Revenues	$20,868,973

The following chart summarizes the level of operating revenue deductions, under rates in effect at the time of application, that the Commission concludes is appropriate for use herein.

Operating Expenses	Amount
Purchased power expenses	$ 6,138,500
Other operations & maintenance	7,151,238
Depreciation and amortization	1,863,668
Taxes - Other than income	1,720,108
Income taxes:	
State	183,158
Federal	1,083,062
Income taxes deferred in prior years	(78,960)
Investment tax credits normalized	275,566
Amortization of investment tax credit	(77,181)
Total Operating Expenses	$18,259,159

With respect to the proper level of income tax expense included above there is one matter which must be addressed. This matter concerns the propriety of imputing interest to a portion of funds arising from utilization of the Job Development Investment Tax Credit (JDITC).

In numerous rate proceedings before the Commission, the Public Staff has steadfastly maintained that the Revenue Act of 1971, which implemented the JDITC, permits the Commission to impute interest thereto for use in determining the test year level of federal income tax expense. Notwithstanding that, the Commission had consistently found, for reasons which need not be repeated here, that the Public Staff's position in this regard was and is incorrect in its entirety. The North Carolina Court of Appeals in Utilities Commission v. Carolina Telephone, 61 N.C. App. 42 (1983), affirmed the Commission findings in this regard, this matter having been appealed by the Public Staff. In the words of the Court:

> "The issue on appeal, as stated by the Public Staff in its brief, 'is whether the Commission erred as a matter of law in concluding that Section 46(f)(2) of the Internal Revenue Code requires that all effects of JDITC should be excluded from the determination of interest expense.'
>
> G.S. 62-94 sets forth the standard of judicial review of orders of the Utilities Commission and includes the following:. . .

In this appeal we are called upon to interpret the applicable sections of the Internal Revenue Code to determine whether the Commission's order is affected by errors of law. We conclude that the order is not so affected.

Section 46(f)(2) of Title 26 of the Internal Revenue Code provides that JDITC will be disallowed with regard to public utility property in the following two circumstances.

> (A) Cost of service reduction.--If the taxpayer's cost of service for ratemaking purposes or in its regulated books of account is reduced by more than a ratable portion of the credit allowable by section 38 (determined without regard to this subsection), or
>
> (B) Rate base reduction.--If the base to which the taxpayer's rate of return for ratemaking purposes is applied is reduced by reason of any portion of the credit allowable by section 38 (determined without regard to this subsection).

The term 'ratable portion' is explained in Section 46(f)(2):

> For purposes of determining. . .ratable portions under paragraph (2)(A), the period of time used in computing depreciation expense for purposes of reflecting operating results in the taxpayer's regulated books of account shall be used.

The following example of 'ratable portion' appears in Section 1.46-6(g)(2) of the Tresury Regulations:

> (I)f cost of service is reduced annually by an amount computed by applying a composite annual percentage rate to the amount of the credit, cost of service is reduced by a ratable portion.

The Internal Revenue Service has published the following regulations implementing Section 46(f)(2):

> (2) Cost of service. (i) For purposes of this section, 'cost of service' is the amount required by a taxpayer to provide regulated goods or services. Cost of service includes operating expenses. . . maintenance expenses, depreciation expenses, tax expenses, and interest expenses. . .
>
> (ii) In determining whether, or to what extent, a credit has been used to reduce cost of service, reference shall be made to any accounting treatment that affects cost of service. Examples of such treatment include reducing by all or a portion of the credit amount of Federal income tax expense taken into account for ratemaking purposes and reducing the depreciable bases of property by all or a portion of the credit for ratemaking purposes.
>
> (3) Rate base. (i) For purposes of this section, 'rate base' is the monetary amount that is multiplied by a rate of return to determine the permitted return on investment.
>
> (ii) In determining whether, or to what extent, a credit has been used to reduce rate base, reference shall be made to any accounting

> treatment that affects rate base. In addition, in those cases in which the rate of return is based on the taxpayer's cost of capital, reference shall be made to any accounting treatment that affects the permitted return on investment by treating the credit in any way other than as though it were capital supplied by common shareholders to which a `cost of capital' rate is assigned that is not less than the taxpayer's overall cost of capital rate (determined without regard to the credit). What is the overall cost of capital rate depends upon the practice of the regulatory body. Thus, for example, an overall cost of capital rate may be a rate determined on the basis of an average, or weighted average, of the costs of capital provided by common shareholders, preferred shareholders, and creditors.

Treas. Reg. 1.46-6(2)(i), (ii) and (3)(i), (ii) (1979).

Essentially, Section 46(f)(2) and the regulation provided that a utility remains eligible for the credit as long as cost of service is reduced by no more than `a ratable portion of the credit,' and as long as no reduction is made in the rate base. The purpose of this scheme, as revealed by legislative history, is to permit the benefits of the credit to be shared by the consumers and the investors of the utility. H.R. Rep. No. 533, 92d Cong., 1st Sess., reprinted in U.S. Code Cong. & Ad. News 1825, 1839 (1971).

Pursuant to paragraph (A) of Section 46(f)(2), CT&T `flows through' directly to its customers an annual percentage of JDITC based upon the useful life of the property producing the credit and thereby reduces its tax expense, and thus its cost of service, by a ratable portion of the credit. This treatment of JDITC by CT&T is not at issue in the present case.

Pursuant to paragraph (B) of Section 46(f)(2), CT&T makes no reduction in its rate base on account of the credit and assigns the overall cost of capital rate to the capital generated by the credit.

The Public Staff advocates an additional adjustment due to the presence of JDITC. Assuming that, in the absence of JDITC, the capital otherwise supplied by JDITC would be contributed by all capital suppliers, including debt, in the same ratios as those suppliers exist in CT&T's capital structure, the Public Staff maintains that a hypothetical interest expense attributable to that portion of JDITC which would have been provided by debt, in the absence of JDITC, should be deducted from CT&T's income tax expense for ratemaking purposes, in addition to the ratable reduction in taxes already produced by amortization of the credit. The Public Staff asserts that this adjustment to income tax expense for ratemaking purposes is in accord with Section 46(f)(2) based upon the language in Treas. Reg. Section 1.46-6(b)(3)(ii) that JDITC be `assigned a "cost of capital" rate that is not less than the taxpayer's overall cost of capital rate (determined without regard to the credit)'. The Public Staff also maintains that its position has been upheld in three federal court decisions and is therefore the correct one. Finally, the Public Staff contends that the ratepayers are entitled to an additional benefit from the proposed imputed interest on JDITC because they are the source of the cost-free capital provided by JDITC. We reject each of these arguments.

The Public Staff's interpretation of the pertinent regulation completely ignores the words which precede the phrase relied upon by the Public Staff. The regulation clearly states that, to determine whether an improper reduction in rate base has occurred, reference should be made to any accounting treatment which treats JDITC 'in any way other than as though it were capital supplied by common stockholders. . .' The phrase relied upon by the Public Staff refers to the determination of the 'overall cost of capital rate' which must be applied to JDITC under the regulation. As such, the phrase deals with the rate of return which the utility is entitled to receive on JDITC, but does not require that a utility's interest expense be calculated without regard to the credit (i.e., as though capital generated by JDITC were supplied by other sources of capital reflected in the utility's capital structure). Rather, the preceding phrase strongly indicates that in other instances, JDITC is to be treated as 'capital supplied by common shareholders.' The imputation of interest to a portion of JDITC as though supplied by creditors does not treat that portion of JDITC as though supplied by common shareholders and, in addition, reduces the cost of service by more than a 'ratable portion' of JDITC. For these reasons, the adjustment proposed by the Public Staff contravenes Section 46(f)(2) and the regulation thereunder.

The cases cited by the Public Staff do not persuade us to interpret Section 46(f)(2) otherwise because each of the cases completely ignores the clear requirement in the regulation to that Section that JDITC be treated as 'capital supplied by common shareholders.'

In the case of Public Service Company of New Mexico v. Federal Energy Regulatory Commission, 653 F. 2d 681 (D.C. Cir. 1981), the main issue before the court was whether capital provided by JDITC should receive the overall or common equity rate of return. The court concluded that, for purposes of determining the overall rate of return, JDITC could be treated as capital supplied by all capital suppliers in the same proportion as those suppliers existed in the capital structure of the utility, absent the credit. The court further held that excluding JDITC from the capital structure of the utility did not alter the debt/equity ratio such that the utility's interest expense deduction was increased, resulting in an additional, impermissible reduction in cost of service. No issue of imputing interest to JDITC was before the court.

That issue was before the court in New England Power Company v. Federal Energy Regulatory Commission, 668 F. 2d 1327 (D.C. Cir. 1981), cert. denied, ___ U.S. ___, 102 S. Ct. 2928 (1982). However, in determining that the Federal Energy Regulatory Commission could require the utility to impute hypothetical interest to JDITC, the court relied on its earlier decision in Public Service Company of New Mexico, supra. Upon stating that, '(t)he question in this section is whether FERC may properly treat tax credit funds in relation to interest deduction in the same way it treats tax credit funds in relation to rate of return determination,' the court quoted that portion of its earlier opinion in which it had approved the Federal Energy Regulatory Commission's treatment of JDITC as capital supplied by all capital suppliers in a proportionate manner for purposes of determining the overall rate of return on capital. As we have previously stated, the questions of how to treat JDITC for purposes of determining interest expense for rate making purposes are separate issues. The court in New England Power Company did not treat them as such and

failed to analyze in any way the tax laws or the arguments supporting the impermissible nature of the adjustment.

In Union Electric Company v. Federal Energy Regulatory Commission, 688 F. 2d 389 (8th Cir. 1981), the third case cited by the Public Staff, the court again relied upon that portion of the regulation under Section 46(f)(2) which permits a ratemaking agency to assign the 'overall cost of capital rate (determined without regard to credit)' to JDITC and ignored the remainder of the regulation. Reasoning that because the regulation allows JDITC to be 'treated like other capital' in one instance, the court concluded that the regulation should be interpreted to allow such treatment on the interest deduction issue as well. In our opinion, such reasoning contravenes the clear requirement of Section 46(f)(2)(A) that only a 'ratable portion' of JDITC be flowed through to customers and of Treas. Reg. Section 1.46(b)(3)(ii) that JDITC be treated as 'capital supplied by common shareholders,' and we decline to follow it.

The final argument advanced by the Public Staff in support of imputing hypothetical interest to JDITC is that ratepayers are entitled to the additional benefit that would enure to them as a result of imputing interest to a portion of JDITC because they supplied the capital produced by JDITC by paying rates computed without regard to the tax credit (other than the ratable portion flowed through to them). The Commission disagrees. Without regard to the credit, a utility owes a certain amount of taxes at the end of its tax year upon which its rates are based. The credit essentially forgives or returns to the utility a portion of the taxes owed by it if certain capital assets have been purchased during the tax year. As such, the capital generated by JDITC comes from the Treasury of the United States, not the ratepayers of the qualifying utility.

Based upon the express language of Section 46(f)(2) and the regulation thereunder, as well as a consideration of the history and purpose of JDITC, that being primarily to benefit the utility so as to stimulate investment and thereby increase employment and additionally to share a ratable portion of the credit with ratepayers, we affirm the decision of the Commission to exclude all imputed interest expense related to JDITC in determining CT&T's income tax expense for rate making purposes."

Based on the foregoing, including the reasoning set forth in past Commission decisions, the Commission finds and concludes that no interest expense should be imputed to funds arising from utilization of JDITC.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 18 AND 19

Two witnesses were presented in the area of cost of capital and fair rate of return. The Company offered the testimony of Joseph F. Brennan, President of Associated Utility Services, a utility consulting firm. The Public Staff offered the testimony of Dr. Robert Weiss, Director of the Economic Research Division.

Witness Brennan recommended an overall return of 12.81%. This was based on a 16% return on common equity and Nantahala's actual capital structure and empedded cost rates as of December 31, 1982. Witness Brennan testified that the capital structure ratios for the Company as of that date were 43.9% long-term debt, with an embedded cost of 8.72% and 56.1% common equity.

In his testimony, witness Brennan cited what he described as "unusual circumstances" relating to Nantahala. First were the Orders by this Commission and the Federal Energy Regulatory Commission under which refunds would be payable to the customers of Nantahala. Witness Brennan compared the total of these refunds, which he found to be approximately $37.5 million, with the Company's total capitalization of $26.2 million at the end of 1982 and stated that "it is obvious that the prospective risk to which capital is exposed when invested in Nantahala is possibly infinite under these circumstances."

Witness Brennan also made reference to the Company's new agreement with TVA which replaces the New Fontana Agreement and under which Nantahala will dispatch its own system and purchase additional energy from TVA.

Finally, witness Brennan stated that Nantahala needs to spend at least $2.5 million constructing additional transmission facilities so as to assure service to its existing customers over time and about $3 million annually to provide service to new customers. Witness Brennan also stated that Nantahala is in no position to attract capital in the marketplace and must rely on internally generated funds which are insufficient to supply all of its requirements.

Witness Brennan stated that the risk of an investment is significantly increased when the "unusual circumstances" are taken into account but that it is impossible to calculate the added risk. Witness Brennan's opinion as to the cost of equity capital to Nantahala was based on the assumption that Nantahala would be freed of its refund obligations and that its rates would be determined as a stand-alone company.

Witness Brennan reached his conclusion that the cost of equity capital to Nantahala is 16.0% by giving equal weight to a discounted cash flow analysis (DCF) and a risk spread analysis. Because Nantahala stock is not traded, and thus its market price is not known, witness Brennan used two groups of companies he considered comparable. The first group was five eastern utilities which can be considered primarily hydroelectric and the second was the two major North Carolina electric utilities, Duke Power Company and Carolina Power & Light Company. Witness Brennan noted that all of his comparable companies were substantially larger than Nantahala.

For his five company barometer group, witness Brennan obtained a discounted cash flow result of 15.8% and risk spread result of 16.5%. For the two North Carolina utilities, witness Brennan's discounted cash flow result was 15% and his risk spread result was 17%. Witness Brennan's recommendation of 16% for Nantahala is essentially an average of these four numbers.

Dr. Weiss of the Public Staff accepted the capital structure and embedded cost rate for debt proposed by witness Brennan but recommended a return on equity of 15% and an overall return on rate base of 12.24%. Dr. Weiss first determined the expected return of a diversified portfolio of equities, specifically the S&P 500. Using discounted cash flow and risk premium techniques, he estimated the expected return for the S&P 500 as 15% - 16%. Dr. Weiss then compared the risk of the electric utility industry to the risk of the S&P 500 using several measures - Value Line Safety Rank, Standard and Poor's Stock Rating, and Beta (as reported by Value Line). Dr. Weiss concluded that these risk measures showed that electric utilities on average

were less risky than the S&P 500 and therefore their expected return is lower than the 15% - 16% he found for the S&P 500. Taking the current level of interest rates into account, he concluded that 15% is a reasonable estimate of the cost of equity to an average electric utility and that a company with Nantahala's characteristics should not have a cost of equity higher than average.

Dr. Weiss stated that currently Nantahala's cost of capital would be high because its rates and refund obligations are uncertain, pending actions by the courts. However, he said that this aspect of the Compnay's cost of capital should not be recognized in setting rates as it would be the equivalent of allowing any refunds as an expense item in the next rate case. Dr. Wiess stated, on cross examination:

> "If we were to give an added return to reflect these uncertainties, that would necessarily be paid by the ratepayer and if these refund obligations came to pass, it's because the ratepayer was being overcharged for a number of years..."

With respect to the components making up the overall rate of return to be allowed in this case, the parties were in agreement on most issues, including the appropriate capital structure and the embedded cost of debt. With respect to the cost of equity, the difference between the witnesses was small, only one percentage point.

The determination of the appropriate fair rate of return for the Company is of great importance and must be made with great care because whatever return is allowed will have an immediate impact on the Company, its stockholders, and its customers. In the final analysis the determination of a fair rate of return must be made by this Commission, using its own impartial judgment, and guided by the testimony of expert witnesses, and other evidence of record. Whatever return is allowed must balance the interests of the ratepayers and investors, and meet the test set forth in G.S. 62-133(b)(4):

> "Fix such rate of return...as will enable the public utility by sound management to produce a fair return for its shareholders, considering changing economic conditions and other factors, as they then exist, to maintain its facilities and services in accordance with the reasonable requirements of its customers in the territory covered by its franchise, and to compete in the market for capital funds on terms which are reasonable and which are fair to its customers and to its existing investors."

The return allowed must not burden ratepayers any more than is necessary for the utility to continue to provide adequate service. The North Carolina Supreme Court has stated that the history of G.S. 62-133(b):

> "...supports the inference that the Legislature intended for the Commission to fix rates as low as may be reasonably consistent with the requirements of the Due Process Clause of the Fourteenth Amendment to the Constitution of the United States..." State ex rel. Utilities Commission v. Duke Power Company, 285 N.C. 377, 206 S.E.2d 269 (1974).

The nature of the evidence in a case such as this makes it extremely difficult to balance all of the opposing interests, since much, if not all, of the evidence is based on individual witnesses' perceptions, and interpretations of trends and data from the capital markets. The Commission has considered carefully all of the relevant evidence presented, with the constant reminder that whatever return is allowed will have an immediate impact on the Company, its stockholders, and its customers. The Commission must use its impartial judgment to ensure that all the parties involved are treated fairly and equitably. In coming to a final decision on this matter, the Commission is not unmindful of the upward pressure on capital costs generally present in the economy over recent years. The Commission is also aware of the recent downward trend in interest and other capital costs.

Based upon the foregoing and the entire record in this docket, the Commission finds and concludes that the fair rate of return that Nantahala should have the opportunity to earn on the original cost of its rate base is 12.52%. Such fair rate of return will yield a fair return on common equity of 15.50%, after payment of interest obligations.

The Commission cannot guarantee that the Company will, in fact, achieve the level of returns herein found to be just and reasonable. Indeed, the Commission would not guarantee it if it could. Such a guarantee would remove necessary incentives for the Company to achieve the utmost in operational and managerial efficiency. The Commission believes, and thus concludes, that the level of return approved herein will afford the Company a reasonable opportunity to earn a reasonable return for its stockholders while providing adequate and economical service to ratepayers.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 20

Based upon the findings of fact set forth hereinabove, the Commission concludes that the appropriate annual level of revenues which Nantahala should be authorized to collect through rates charged for its sales of service based upon the adjusted test year level of operations is $22,204,830. The following charts summarize the gross revenues and the rates of return which the Company should have a reasonable opportunity to achieve, based upon the level of revenues approved herein. Such charts, illustrating the Company's gross revenue requirements, incorporate the findings, adjustments and conclusions herein made by the Commission.

SCHEDULE I
NANTAHALA POWER AND LIGHT COMPANY
Docket No. E-13, Sub 44
North Carolina Retail Operations
STATEMENT OF RATE BASE AND RATE OF RETURN

For the Test Year Ended December 31, 1981

Item	Amount
Electric plant in service	$61,289,278
Construction work in progress	406,209
Materials and supplies	519,025
Cash working capital	594,010
Subtotal	62,808,522
Add:	
FERC license adjustment	98,243
Unamortized maintenance	144,516
Less:	
Accumulated depreciation	33,012,528
Accumulated deferred income taxes	3,861,645
Accumulated deferred investment tax credit pre-1971	48,863
Customer deposits	220,857
Total original cost rate base	$25,907,388
Rate of Return:	
Present rates	10.07%
Approved rates	12.52%

SCHEDULE II
NANTAHALA POWER AND LIGHT COMPANY
Docket No. E-13, Sub 44
North Carolina Retail Operations
STATEMENT OF OPERATING INCOME FOR RETURN
For the Test Year Ended December 31, 1981

Item	Present Rates	Approved Increase	After Approved Increase
Operating Revenues:			
Sales of electricity	$20,623,491	$1,335,857	$21,959,348
Other operating revenues	245,482	-	245,482
Total operating revenues	20,868,973	1,335,857	22,204,830
Operating Expenses:			
Purchased power expense	6,138,500	-	6,138,500
Other O&M expenses	7,151,238	5,611	7,156,849
Depreciation & amortization	1,863,668	-	1,863,668
Taxes other than income	1,720,108	79,815	1,799,923
Income taxes:			
State	183,158	75,026	258,184
Federal	1,083,062	540,686	1,623,748
Deferred in prior years	(78,960)	-	(78,960)
Investment tax credits	275,566	-	275,566
Amortization of ITC	(77,181)	-	(77,181)
Total operating expenses	18,259,159	701,138	18,960,297
Net operating income	$ 2,609,814	$ 634,719	$3,244,533

SCHEDULE III
NANTAHALA POWER AND LIGHT COMPANY
Docket No. E-13, Sub 44
North Carolina Retail Operations
STATEMENT OF CAPITALIZATION AND RELATED COSTS
Twelve Months Ended December 31, 1981

Item	Ratio %	Original Cost Rate Base	Embedded Cost %	Net Operating Income
		Present Rates		
Long-term debt	43.9	$11,373,343	8.72	$ 991,756
Common equity	56.1	14,534,045	11.13	1,618,058
Total	100.0	$25,907,388	-	$2,609,814
		Approved Rates		
Long-term debt	43.9	$11,373,343	8.72	$ 991,756
Common equity	56.1	14,534,045	15.50	2,252,777
Total	100.0	$25,907,388	-	$3,244,533

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 21, 22, 23, 24, AND 25

Company witness Carson, Public Staff witness Turner, and Jackson Paper Company witness Rudden presented testimony and evidence regarding the Company's proposed rate designs and service rules.

General

The major changes Nantahala proposes for its Service Rules and Regulations include: (1) an extra facilities charge of 2% of installed cost; (2) after hours service connection charge of $15.00; (3) after hours service connection charge of $17.50 if service was suspended by the Company; and (4) trouble call charge if trouble is not related to the Company's equipment of $10.00 during normal business hours and $25.00 during non-business hours.

Generally, Nantahala proposed no major structural changes in its rate design. The amount of increase by rate schedule, however, varies because of an effort to continue the process of equalizing rate class rates of return. Additionally, each rate schedule is adjusted to roll into basic rates the adjusted level of purchased power costs under the new TVA contract.

Nantahala is also proposing to add an RC rate schedule for those customers who achieve certain insulation standards as prescribed in the schedule, limited to the first 100 qualifying homes.

Nantahala further proposes to delete the paragraph pertaining to the funding of the Alternative Energy Corporation from each rate schedule and add a rider which incorporates the level of funding approved by the Commission in Docket No. E-13, Sub 35.

None of the proposals discussed above were opposed by any party herein, and the Commission concludes that they should be approved.

Billing Based on Monthly Meter Readings

In Docket No. E-13, Sub 35, the Commission ordered Nantahala to take monthly meter readings and bill its customers accordingly. The Commission does not believe that merely because certain findings of that docket have been appealed that the requirement for monthly meter readings should be delayed any longer. Witness Tucker of Nantahala testified during the hearing in this proceeding that Nantahala had no objections to monthly meter readings so long as it were allowed to recover the expenses of those meter readings. The Commission concludes that the Company should base its residential billings on monthly meter readings as required in Docket No. E-13, Sub 35.

Separate Listing of Purchased Power Adjustments on Bills

The proposed order filed by the Public Staff in this proceeding recommended that the purchased power adjustment be itemized separately on the monthly bills to customers. The Commission notes that the unit price per kwh representing the purchased power adjustment is already listed separately on the monthly bills, except for those months where the bills are estimated. The Commission is of the opinion that such listing of the unit price per kwh for the purchased power adjustment should be sufficient, and concludes that the Company's present practice is acceptable.

Time of Use Rates and Load Management

Witness Turner testified that the Commission has approved tariffs for other electric utilities in its jurisdiction which are cost justified and promote

efficient use of electric utility resources. These tariffs include time-of-use features, seasonal charges, and various load management provisions and more accurate measurement of electric usage with demand meters as well as energy meters.

The Public Staff takes the position that similar tariffs should be made available on a voluntary basis for the customers of Nantahala whenever these tariffs can be justified, but it is not proposing specific rate tariffs in this proceeding because of the uncertainty of the basis for these tariffs.

On cross-examination, Witness Turner testified that he had made no studies of Nantahala's particular system to determine whether or not rates such as those advocated would be appropriate. Although Witness Turner testified that he had reviewed studies that had been used in applications by other utilities, he testified that those systems were substantially different from Nantahala's. He testified that the studies for the other companies would not be appropriate because Nantahala has only hydroelectric generation. Witness Turner acknowledged that the purpose of time-of-day rates, for example, as to enable a Company to shift load from peak periods to off-peak periods. He acknowledged that Nantahala's 1983 contract with TVA causes Nantahala to attempt to schedule its generation so as to minimize its on peak purchases from TVA. He testified that it would be appropriate for Nantahala to conduct a study with input from the Public Staff to see just how time of day rates, for example, might dovetail with provisions of that contract to make sure that costs indeed are saved. He testified that he would not be opposed to an analysis made of Nantahala's operation in conjunction with the purchases from TVA as a preliminary step to the design of time-of-use rates.

Based upon the foregoing, the Commission determines that Nantahala, in conjunction with the Public Staff, should conduct a study to determine whether rates as advocated by the Public Staff should be implemented. The Commission recognizes that implementation of time-of-use rates entails a considerable expense such as the purchase of meters for that purpose. The Commission requires that Nantahala undertake such studies and report its findings to the Commission within a reasonable time.

Proposed New Rate Schedule LIS

Witness Rudden recommended the establishment of a new class of service, large industrial service (LIS), and offered a proposed rate design for that class. Witness Rudden testified that Jackson Paper will have a peak demand of 6,100 kw and a monthly non-coincident peak load factor in the range of 85 to 90%. The next largest customer of the Nantahala system, Western Carolina University, had a 1981 peak demand of only 3,940 kw, an average monthly demand of about 3,500 kw and an average monthly load factor of less than 62%. Witness Rudden testified that Jackson's load characteristics result in a large difference between the cost of serving Jackson and other customers, and it is therefore appropriate to reflect these differences in the rates charged to Jackson. Nantahala had originally filed an LG rate that would produce 13.61% rate of return on the large general service rate. At the 13.61% return level, the revenue required from the rates charged to Jackson is $891,148, or $123,373 less than the revenue that would be charged to Jackson by Nantahala's proposed LG rate.

Witness Rudden designed a rate for Jackson that will produce revenues of approximately $891,000 and a rate of return of 13.61%. He designed the LIS rate on a cost-based structure that will provide the correct revenue level and rate of return. Witness Rudden structured the demand and energy charges in a way that reflected the higher unit demand cost of the LIS customer relative to the LG customer, and the lower average energy cost associated with higher load factor customers. He selected 5,000 kw as a minimum demand level for the LIS rate. This kw level was selected because it reasonably approximates Jackson's load of 5,800 kw in the non-peak months and is also approximately equal to the midpoint of the difference between Jackson's maximum load and the next largest customer's demand load. Witness Rudden recommended that Nantahala remove the current 4,000 kw in the LG rate and make it available to all large general service customers. The proposed LIS class would be an option to those LG customers with demands exceeding 5,000 kw and whose load factors would make LIS more economical.

On cross-examination, Witness Rudden agreed that, while the LIS schedule would permit Nantahala to sell power at the rate of approximately 2.0¢ per kw, Nantahala must pay TVA 3.4¢ per kw (based on a 100% load factor for purchased power) with the difference being made up by the other customer classes. In fact, Late-Filed Exhibit RJR-8 requested by Dr. Hammond shows that the overall increase in revenue requirement, after including the JPC load, will be $1,599,509; and only 56% of said $1,599,509 increase will be paid by Jackson Paper Company under the LIS rate schedule, leaving a deficit which must be paid by the remaining rate classes.

The Commission is unconvinced that the LIS rate schedule proposed for the Jackson Paper Manufacturing Company is cost justified and concludes that said rate schedule should not be approved.

IT IS, THEREFORE, ORDERED as follows:

1. That the Commission's Notice of Decision and Order dated November 29, 1983, be, and the same is hereby, reaffirmed.

2. That the rate schedules and service rules and regulations filed herein on December 13, 1983, by Nantahala be, and the same are hereby, approved.

ISSUED BY ORDER OF THE COMMISSION.
This the 22nd day of December 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sandra J. Webster, Chief Clerk

DOCKET NO. E-22, SUB 273

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Application of Virginia Electric and Power Company) ORDER GRANTING
for Authority to Adjust and Increase Its Electric) PARTIAL INCREASE
Rates and Charges) IN RATES

HEARD IN: Meeting Room, Municipal Building, Ahoskie, North Carolina, on Monday, August 8, 1983, at 7:00 p.m.

Knob Creek Recreation Center, Elizabeth City, North Carolina, on Tuesday, August 9, 1983, at 7:00 p.m.

Assembly Room, City Hall, Williamston, North Carolina, on Wednesday, August 10, 1983, at 7:00 p.m.

Banquet Hall, Roanoke Rapids Community Center, Roanoke Rapids, North Carolina, Thursday, August 11, 1983, at 10:30 a.m.

Commission Hearing Room, Dobbs Building, Raleigh, North Carolina, on September 7-9 and 14-16, 1983, at 9:00 a.m.

BEFORE: Commissioner Sarah Lindsay Tate, Presiding; and Commissioners Edward B. Hipp and Ruth E. Cook

APPEARANCES:

For Virginia Electric and Power Company:

Guy T. Tripp, III, Hunton & Williams, Attorneys at Law, P.O. Box 1535, Richmond, Virginia 23212

Edward S. Finley, Jr. and Edgar M. Roach, Jr., Hunton & Williams, Attorneys at Law, P.O. Box 109, Raleigh, North Carolina 27602

For the Public Staff:

Antoinette R. Wike and Gisele L. Rankin, Staff Attorneys, Public Staff, North Carolina Utilities Commission, P.O. Box 991, Dobbs Building, Raleigh, North Carolina 27602
For: The Using and Consuming Public

For the Attorney General:

Steven F. Bryant, Assistant Attorney General, N.C. Department of Justice, P.O. Box 629, Raleigh, North Carolina 27602
For: The Using and Consuming Public

For the Intervenors:

Jerry B. Fruitt, Attorney at Law, P.O. Box 2507, Raleigh, North Carolina 27602
For: North Carolina Textile Manufacturers Association, Inc. (NCTMA)

Ralph McDonald and Carson Carmichael, III, Bailey, Dixon, Wooten, McDonald & Fountain, Attorneys at Law, P.O. Box 2246, Raleigh, North Carolina 27602
For: Abbott Laboratories, Inc., Schlage Lock Company, Weyerhauser Company, Champion International Corporation, and Consolidated Diesel (CIGFUR I).

BY THE COMMISSION: On February 7, 1983, Virginia Electric and Power Company (Vepco) filed an application with the North Carolina Utilities Commission seeking authority to adjust and increase its rates and charges for

electric service to its North Carolina retail customers, said proposed rates and charges to become effective on March 9, 1983. The requested increase in rates and charges was designed to produce additional revenue of approximately $18,727,000, based on the 12-month test period ended June 30, 1982.

By Order issued on March 8, 1983, the Commission declared Vepco's application to be a general rate case pursuant to G.S. 62-137, suspended Vepco's proposed rates pursuant to G.S. 62-134 for a period of up to 270 days from the proposed effective date of such rates, scheduled public hearings on the application, established the test period to be used in the proceeding, and required Vepco to give public notice of the application and the hearings scheduled by the Commission, and required protests or interventions to be filed in accordance with the Commission's Rules.

On March 17, 1983, the Public Staff filed a Notice of Intervention in this docket on behalf of the using and consuming public.

On March 30, 1983, the North Carolina Textile Manufacturers Association, Inc., filed a Petition to Intervene in this docket. By Commission Order of April 1, 1983, that request to intervene was allowed.

On May 24, 1983, the Commission issued an Errata Order correcting Appendix A of the Commission Order Declaring General Rate Case, Suspending Proposed Rates, Scheduling Public Hearing, and Requiring Notice which had been issued on March 8, 1983.

On June 10, 1983, Abbott Laboratories, Inc., Schlage Lock Company, and Weyerhaeuser Company (Carolina Industrial Group for Fair Utility Rates, or CIGFUR I) filed a joint petition to intervene in this docket. By Commission Order of June 15, 1983, that request to intervene was granted.

On June 14, 1983, Champion International Corporation and Consolidated Diesel (having become members of CIGFUR I) filed a joint petition to intervene in this docket. By Commission Order of June 17, 1983, the request to intervene was granted.

On June 18, 1983, the Attorney General of North Carolina filed a Notice of Intervention in this docket on behalf of the using and consuming public.

Out of town hearings were conducted by the Commission for the purpose of receiving testimony from members of the using and consuming public with regard to Vepco's proposed rate increase. The first such hearing was held in Ahoskie, North Carolina, at 7:00 p.m., on August 8, 1983; the second in Elizabeth City, North Carolina, at 7:00 p.m., on August 9, 1983; the third in Williamston, North Carolina, at 7:00 p.m., on August 10, 1983; and the fourth in Roanoke Rapids, North Carolina, at 10:30 a.m., on August 11, 1983.

Public witnesses at these hearings included the following persons:

Ahoskie - No witnesses
Elizabeth City - No witnesses
Williamston - Betty Swain, Stanley W. Hege, and Allison Clark
Roanoke Rapids - Uriel Powell, Dock Brown, Joe P. Moody, and Madeline Kruger

The matter came on for hearing in the Commission Hearing Room, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina, on September 7, 1983, at 9:00 a.m. Vepco offered the testimony and exhibits of the following witnesses:

1. William W. Berry, President and Chief Executive Officer of Vepco;
2. Jack H. Ferguson, Executive Vice President and Chief Operating Officer of Vepco;
3. O. James Peterson, III, Vice President and Treasurer of Vepco;
4. B.D. Johnson, Vice President and Controller of Vepco;
5. H.H. Dunston, Jr., Manager-Cost Analysis for Vepco;
6. David R. Hostetler, Manager-Rates for Vepco;
7. James P. Carney, Director-Economic Analysis for Vepco; and
8. Cornelius B. Pryor, Jr., Vice President and Director of Kidder, Peabody & Co., Inc.

The Public Staff offered testimony and exhibits of the following witnesses:

1. Dennis J. Nightingale, Director of the Electric Division of the Public Staff;
2. Richard N. Smith, Engineer in the Electric Division of the Public Staff;
3. Benjamin R. Turner, Jr., Engineer in the Electric Division of the Public Staff;
4. David Kirby, Accountant in the Accounting Division of the Public Staff;
5. Nancy B. Bright, Director of the Accounting Division of the Public Staff; and
6. Dr. Caroline M. Smith, Senior Consultant with J.W. Wilson & Associates, Inc.

Vepco offered testimony and exhibits of the following rebuttal witnesses:

1. Gary L. Edwards, Director-Rate Design for Vepco;
2. David R. Hostetler;
3. B.D. Johnson;
4. James Graham Dynes, Jr., Staff Economist for Vepco; and
5. Dr. Allen P. Mitchem, Staff Economist for Vepco.

All parties to the proceeding were provided an opportunity to file Briefs and Proposed Orders with the Commission. Briefs and Proposed Orders were required to be filed on or before Monday, November 7, 1983.

After the close of the hearing, the Company, at the request of the Commission, prepared and filed on October 14, 1983, a late filed exhibit containing additional cost of service studies plus a proposal for further studies regarding the identification of a portion of production plant which should be allocated based on energy usage. No parties to the proceeding requested the opportunity to cross-examine the Company regarding the late filed exhibit.

Based upon the verified application, the testimony and exhibits received into evidence at the hearings and the record as a whole of this proceeding, the Commission, having duly reviewed such Briefs and Proposed Orders as were filed by the parties, now makes the following

FINDINGS OF FACT

1. Vepco is engaged in the business of developing, generating, transmitting, distributing, and selling electric power and energy to the general public in northeastern North Carolina, and Vepco has its principal office and place of business in Richmond, Virginia.

2. Vepco is duly organized as a public utility company under the laws of North Carolina and is subject to the jurisdiction of this Commission. Vepco is lawfully before this Commission based upon its application for a general increase in its North Carolina retail rates and charges, pursuant to the jurisdiction and authority conferred upon the Commission by the Public Utilities Act.

3. The test period for purposes of this proceeding is the 12-month period ended June 30, 1982, adjusted for certain changes and updates. Vepco, by its application, is seeking an increase in its rates and charges to its North Carolina retail customers of approximately $18,727,000.

4. The overall quality of electric service provided by Vepco to its North Carolina retail customers is adequate.

5. The summer-winter peak and average method as discussed herein is the most appropriate method for making cost allocations between jurisdictions and between customer classes in this proceeding. Consequently, each finding of fact appearing in this Order which deals with the overall level of rate base, revenues, and expenses for N.C. retail service has been determined based upon the summer-winter peak and average cost allocation method.

6. Vepco's decision to cancel its North Anna Unit 3 was reasonable and prudent. Further, Vepco should be allowed to recover its abandonment loss sustained as the result of the Company's having terminated construction on, and having abandoned, its Surry Units 3 and 4 and North Anna Units 3 and 4. Recovery of the Company's reasonable and prudent investment in those units should be amortized over a 10-year period. It is neither fair nor reasonable to include any portion of the unamortized balance of this investment in rate base, and no adjustment which would have the effect of allowing the Company to earn a return on the unamortized balance of this investment should be allowed.

7. The reasonable original cost of Vepco's property used and useful, or to be used and useful within a reasonable time after the test period, in providing service rendered to the public within the State of North Carolina, less that portion of the cost which was being consumed by previous use recovered by depreciation expense, less cost-free capital, plus the original cost of investment in plant under construction (CWIP) is $218,418,000. Inclusion of $18,850,000 of reasonable and prudent expenditures for CWIP in Vepco's rate base is in the public interest and is necessary to the financial stability of the Company.

8. The reasonable allowance for working capital is $15,156,000.

9. Vepco's reasonable original cost rate base is $233,574,000. This amount consists of net utility plant in service and construction work in progress of $218,418,000, plus a reasonable allowance for working capital of $15,156,000.

10. Vepco's appropriate level of gross revenues for the test year under presently approved rates and after accounting and pro forma adjustments is $100,633,000 and after the increase approved herein, it is $118,973,000.

11. A base fuel component of 1.541¢ per kWh excluding gross receipts tax is appropriate for this proceeding, reflecting a reasonable fuel cost of $25,795,763 for N.C. retail service, after reflection of unbilled kWhs.

12. The reasonable level of test year operating revenue deductions is $83,259,000. This amount includes $9,484,000 for investment currently consumed through reasonable actual depreciation on an annual basis.

13. The capital structure for Vepco which is appropriate for use in this proceeding is as follows:

Item	Percent
Debt	53.22
Preferred stock	10.96
Other paid in capital	.38
Common equity	35.44
Total	100.00

14. The Company's embedded costs of debt and preferred stock are 9.09% and 8.51%, respectively. The fair and reasonable rate of return for the Company's common stockholders is 15.25%. Using a weighted average for the Company's cost of debt, preferred stock, and common equity, with reference to the reasonable capital structure heretofore determined, yields an overall fair rate of return of 11.18% to be applied to the Company's original cost rate base.

15. Based upon the foregoing, the Company's annual revenue requirement approved herein is $18,340,000. This increased revenue requirement is based upon the original costs of the Company's property and its reasonable test year operating revenues and expenses as previously determined and set forth in these findings of fact.

16. The rates of return proposed by the Company for each rate schedule relative to the overall N.C. retail rate of return are reasonable. The revenue increases proposed by the Company for each rate schedule relative to the overall revenue increase proposed for N.C. retail service are also reasonable.

17. Each TOD rate schedule subject to the new on-peak hours proposed by the Company should specify that said on-peak hours are clock time.

18. Bimonthly billing should not be available for service under TOD schedules 1P, 1T, or 1DF.

19. The Company's proposal to exclude flats, apartments, boarding houses, etc., from service under TOD schedules 1P and 1T should be denied at this time.

20. The one-year contract provision in rate schedules 1P, 1T, 1DF, and 1W should be eliminated, and the alternative type of provision proposed by the

Company in this proceeding for rate schedules 1P and 1T should be adopted for rate schedules 1P, 1T, 1DF, and 1W.

21. The hours of interruption for rate schedule IW should be revised to the hours between 6:30 a.m. and 11:00 a.m. (EST), and between 12:30 p.m. and 8:30 p.m. (EST), as agreed upon by the Company and by the Public Staff.

22. The revisions to the residential conservation discount program proposed by the Public Staff and agreed upon by the Company should be adopted, including: (1) amending the thermal insulation requirements to conform to the standards of the Company's Energy Saver Home (ESH) program; (2) including efficiency standards for heat pumps and central air conditioners in the conservation discount requirements in order to conform to the standards of the Company's ESH program; (3) extending the conservation discount program to TOD schedules 1P and 1T; and (4) listing the conservation discount requirements on the tariff sheets for rate schedules 1P and 1T as well as schedule 1.

23. The conservation discount applicable to rate schedules 1, 1P, and 1T should be based on a fixed amount per kWh as proposed by the Company.

24. The definitions of maximum and minimum voltage in the Company's proposed terms and conditions should be revised as recommended by the Public Staff to delete reference to a five-minute mean or average voltage.

25. The rate designs, rate schedules, and service rules proposed by the Company, except for the modifications thereto as described herein, should be approved.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 1 AND 2

The evidence supporting these findings of fact is contained in the Company's verified application, in prior Commission Orders in this docket of which the Commission takes notice, and G.S. 62-3(23)a and G.S. 62-133. These findings of fact are essentially informational, procedural and jurisdictional in nature and the matters which they involve are essentially uncontested.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 3

The evidence for this finding of fact is contained in the Company's verified application and the testimony and exhibits of Company witness Johnson. Witness Johnson, in his additional direct testimony filed on August 2, 1983, updated those revenue, expense, and rate base items related to plant-in-service, construction work in progress, and depreciation through April 30, 1983. Customer growth was updated through March 31, 1983. Fuel expenses were updated to the 12-months ended June 30, 1983. Nuclear fuel disposal costs for nuclear fuel burned during the test period were updated to reflect the effect of the Nuclear Waste Disposal Act. The Commission concludes that the Company's updates are proper, and should be considered in determining fair and reasonable rates in this proceeding.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 4

The evidence for this finding of fact is found in the testimony of Company witness Berry and various public witnesses who appeared in these hearings. Certain testimony offered by the public witnesses was devoted to complaints

about the basic rates being charged or proposed to be charged by the Company for its services. A careful consideration of the testimony leads the Commission to conclude that the quality of electric service being provided to retail customers in North Carolina by Vepco is adequate.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 5

Company witness Dunston and Public Staff witness Turner presented testimony and exhibits regarding cost allocation methodologies.

Cost Allocation Method

The Company provides retail electric service in North Carolina and in two other states, and it also provides wholesale electric service. Therefore, it is necessary to allocate the cost of electric service between the North Carolina retail jurisdiction and the other jurisdictions, and also between the customer classes within the North Carolina retail jurisdiction.

Prior to the Company's last general rate case (in Docket No. E-22, Sub 265), the Company had utilized the Summer Coincident Peak method for allocating production plant. The Summer Coincident Peak method allocates all production plant investment and related expenses between the various jurisdictions and customer classes based on contribution to the system peak demand. However, in Docket No. E-22, Sub 265, the Company recommended the Average and Excess method for allocating production plant, recognizing that its summer and winter system peaks had become more nearly balanced, that reliance on a single system peak can result in significantly unstable results from year to year, and that a portion of production plant might be energy related.

The Public Staff recommended in Docket No. E-22, Sub 265, the Summer/Winter Peak and Base method for allocating production plant. The Summer/Winter Peak and Base method utilizes minimum demand instead of average demand to determine that portion of production plant (and related expenses) which should be allocated by energy. The Summer/Winter Peak and Base method also utilizes coincident peak demands instead of noncoincident peak demands to allocate the demand-related portion of production plant.

The industrial intervenors in Docket No. E-22, Sub 265, recommended the Summer/Winter Coincident Peak method for allocating production plant. The Summer/Winter Coincident Peak method assumes that all production plant is peak demand related.

The Commission concluded in Docket No. E-22, Sub 265, that the Average and Excess method suffered from use of noncoincident peak demands instead of coincident peak demands, and that the Summer/Winter Peak and Average method would remedy the defect. The Commission also concluded that average demand (as utilized by the Summer/Winter Peak and Average method) was more appropriate for determining the portion of production plant which should be allocated by energy than minimum demand (as utilized by the Summer/Winter Peak and Base method) until such time as a more convincing method for making such determination was introduced.

In the current general rate case in Docket No. E-22, Sub 273, the Company recommends the Summer/Winter Peak and Average method for allocating production

plant. Although the Company still would prefer the Average and Excess method to all other methods, it also regards consistency in use of an allocation method to be important so it proposes to utilize the method adoped by the Commission in the prior rate case.

The positions of the intervenor parties are essentially the same in the current rate case as they were in the prior rate case, with the Public Staff recommending the Summer/Winter Peak and Base method and the industrial intervenors recommending the Summer/Winter Coincident Peak method.

The Commission concluded in the previous rate cases, for reasons explained extensively therein, that the cost allocation method utilized for rate-making purposes should recognize the energy-related portion of production plant. Essentially, the Commission reasoned that not all fixed costs (for production plant) represent the cost of meeting system peak demand, and that a significant portion of fixed costs represents the cost of producing kWh during many hours of the year and of producing such kWh at a lower fuel cost per kWh. The Commission continues to be persuaded in this proceeding that the cost allocation method utilized herein should recognize the energy-related portion of production plant fixed costs.

The Commission also concluded in the previous rate cases, for reasons explained extensively therein, that the cost allocation method utilized for rate-making purposes should continue to recognize peak responsibility as the basis for allocating the demand-related portion of production plant, and that said peak responsibility should include both the summer peak and the winter peak. Essentially, the Commission reasoned that the most significant capacity requirements placed on the system were heating and cooling season loads, and that while both types of loads were similar in their impact on system capacity needs, the customer mix contributing to the heating season load is significantly different from the customer mix contributing to the cooling season load. The Commission continues to be persuaded in this proceeding that the cost allocation method utilized herein should recognize both the summer peak and the winter peak as a basis for allocating the demand-related portion of production plant fixed costs.

The Commission concludes in this proceeding that the Summer/Winter Peak and Average method will best recognize the requirement that demand-related production plant fixed costs be allocated based on peak responsibility, just as they always have been. The method will also recognize that not all production plant fixed costs are demand-related, and it recognizes the requirement that energy-related production plant fixed costs be allocated by kWh energy.

Study to Determine Energy-Related Portion of Production Plant

Although the Commission is adopting the Summer/Winter Peak and Average method for allocating production plant in this proceeding, it nevertheless recognizes that there is a continuing need to resolve the issue regarding how much production plant fixed cost is energy-related.

Company witness Dunston testified that some production plant ought to be allocated on the basis of energy in recognition of the fact that larger units are built to save energy cost, but that he did not feel it should be as much as the 57% allocated by the Summer/Winter Peak and Average method. Public

Staff witness Turner testified that, in his opinion, when more definitive studies are produced showing the energy-related portion of production plant, the studies would show such portion to be less than the system load factor (i.e., 57% in this instance).

In the two previous general rate cases in Docket Nos. E-22, Sub 257, and E-22, Sub 265, the Company was directed to produce the information necessary to determine the energy-related portion of production plant. In the current rat cost and annual fuel cost of each nonpeaking unit, and also the estimated capital cost (in 1982 dollars) and annual fuel cost of a peaking unit comparable in capacity to each nonpeaking unit. The Public Staff was critical of the data filed, particularly of the fact that the capital cost of the nonpeaking units and comparable peaking units was not in time consistent dollars and so were not comparable. The Company later filed revised data with its October 14, 1983, late filed exhibit showing the original capital cost of each nonpeaking unit in 1982 dollars. The Company cautioned that it did not recommend that the data be used to determine the energy-related portion of production plant.

The Company also proposed in its October 14, 1983, late filed exhibit to undertake a study that would, as a first step, identify what portion of base load generating plant is necessary to serve the minimum system load. The study to identify necessary base load plant would include consideration of area protection requirements, purchased and interchanged power, maintenance schedules and unplanned outages, operation of nonbase load units to avoid cycling, and the effect of the Bath County project coming into service beginning in 1985. The Company proposed to review the progress of the study with the Public Staff and other interested parties in February 1984.

The Commission concludes that the Company should undertake the study outlined in its October 14, 1983, late filed exhibit, and that it should work with the Public Staff in an effort to resolve the issue of identifying the energy-related portion of production plant.

Study to Determine Hourly Costs of Generation

The Public Staff suggested in its testimony that neither the Summer/Winter Peak and Average method nor the Summer/Winter Peak and Base method recognizes the possibility that the unit fuel cost per kWh may vary between customer classes. Witness Turner contended that customer classes which are allocated base load plant fixed costs should also be allocated the lower fuel costs associated with the base load plants. He suggested that a solution to the problem might result from an analysis of hourly plant operating data and from hourly customer loads to match actual total costs (fixed plus variable costs) during each hour with actual customer loads during each hour. Such a study would confirm whether or not the various cost allocation methods under consideration assign base load plant fixed costs in a manner consistent with assignment of the lower fuel costs associated with the base load plants. Such study would also provide valuable data for designing time of day rates.

The Company proposed in its October 14, 1983, late filed exhibit to undertake a study to identify a portion of base load generating plant as necessary to serve the minimum system load, as discussed elsewhere herein. As a part of that study, the Company proposes to analyze time differentiated fuel costs to see what type and magnitude of credit might be appropriate if base

load plant fixed costs are allocated to customer classes based on energy usage.

The Commission concludes that the study proposed by the Company in its October 14, 1983, late filed exhibit would be an appropriate response to the Public Staff's concerns regarding allocation of base load plant fixed costs consistent with allocation of the lower fuel costs associated with the base load plants, and that the Company should work with the Public Staff in an effort to resolve the issues addressed by the study.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 6

The evidence for this finding of fact is found in the testimony of Company witnesses Berry, Ferguson, and Johnson, Public Staff witness Kirby, and in prior Commission Orders in this docket of which the Commission takes notice.

In November 1982, Vepco cancelled the construction of North Anna Unit 3, a 907 megawatt nuclear unit. Company witness Berry testified that recent changes in Nuclear Regulatory Commission regulations and other factors resulted in such large projected cost increases that the unit was no longer economically justified. Company estimates completed in the fall of 1982 showed total projected costs for North Anna Unit 3 of between $4.1 and $5.1 billion (depending on the date of expected commercial operation), which is twice the level of previous estimates. Completion of North Anna Unit 3 would have required an investment of roughly a third of the Company's total assets by 1990 in a unit that would have represented less than 10 percent of Vepco's total generating capacity. Vepco witness Berry testified that completion of the unit would have resulted in higher rates than will result from cancellation of the unit, with a 10-year write-off and full rate base treatment of the unamortized balance, and purchase by Vepco of replacement capacity from another utility. The Company asserted that its investigations have found that long-term capacity purchases are possible and attractive.

No evidence was offered in opposition to the Company's decision to cancel North Anna Unit 3. Accordingly, a careful consideration of the evidence presented at the hearing leads the Commission to conclude that Vepco's decision to cancel North Anna Unit 3 was reasonable and prudent.

With regard to the issue of the proper rate-making treatment which should be accorded to plant abandonment losses, the abandoned plant projects at issue in this proceeding are Surry Units 3 and 4 and North Anna Units 3 and 4. The Company, the Public Staff, and the Attorney General agreed that the abandonment losses were prudently incurred and therefore should be amortized to the cost of service over a reasonable period. However, the Public Staff disagreed with the Company's proposed 10-year amortization period for the North Anna 3 abandonment loss and recommended instead a 12-year period. The Attorney General recommended a 15-year amortization period for all of the units in question. The parties also proposed different rate base treatments for unamortized plant abandonment losses. Vepco witness Johnson proposed that the Company be allowed to recover debt and preferred stock costs, but no common equity costs, related to the unamortized losses on North Anna Unit 4 and Surry Units 3 and 4, and that the full overall rate of return be permitted for the unamortized North Anna 3 loss. The Public Staff and Attorney General contend that no recovery of capital costs associated with unamortized abandoned plant losses should be allowed.

The rate-making treatment of the North Anna 4 and Surry 3 and 4 abandonment losses was at issue in the Company's last general rate case, Docket No. E-22, Sub 265. Vepco's proposal to allow recovery only of the senior capital costs related to those abandonment losses is based on the approach found reasonable by the Commission in that case. The rate-making treatment of the loss on the North Anna 3 project, which the Company cancelled in November 1982, has not been considered in any previous case. Vepco witness Johnson contended that the circumstances of the North Anna 3 abandonment loss justify a rate-making treatment of that loss more favorable to the Company than that which he proposed for the earlier cancelled projects. In his rebuttal testimony, witness Johnson stated that the North Anna 3 project was cancelled not because of a decline in the projected load growth, as was the case with the first three cancelled projects, but because of escalating construction costs. He testified that the cost to customers of purchased power to meet future load growth, together with the cost of amortizing the North Anna 3 abandonment loss with full inclusion of unamortized amounts in rate base, would be less than the cost of completing the North Anna 3 plant. According to witness Johnson, this cost savings justifies granting the full overall rate of return on the unamortized North Anna 3 abandonment loss.

In recommending that no rate base inclusion be allowed for plant abandonment losses, Public Staff witness Kirby cited the effects of such inclusion on the allocation of the financial risks of construction projects between investors and ratepayers. He stated that including the North Anna 3 loss in rate base "ignores the principle that those who choose to invest in the common stock of an electric utility assume, or should assume, some of the financial risks, such as plant abandonment losses, that are inherent in the electric utility business." To insulate investors from such risks, contended witness Kirby, would diminish management's incentive to avoid future abandonment losses. He concluded that the most logical basis for effecting an equitable sharing of plant abandonment losses between investors and ratepayers would be to allow amortization of prudently incurred losses but to exclude unamortized losses from rate base.

The proper rate-making treatment of abandonment losses related to electric generating plants has been before the Commission in several cases and will continue to arise in future cases. The Commission has, therefore, undertaken to re-examine this important issue in order to develop a more consistent and equitable approach to it. The Commission's ultimate responsibility with respect to ratemaking is to fix rates for the service provided which are fair and reasonable both to the utility and to the consumer. G.S. 62-133(a); _State ex rel. Utilities Commission_ v. _Morgan_, 277 N.C. 255, 177 S.E. 2d 405 (1970); _State ex rel. Utilities Commission_ v. _Area Development, Inc._, 257 N.C. 560, 126 S.E. 2d 325 (1962).

Although the parties to this proceeding may disagree as to the proper amortization period to be utilized with regard to plant abandonment losses, they generally agree that Vepco should be allowed to recover the prudently invested cost of its abandonment losses through amortization over some period of time. The Commission, based upon the evidence presented, must determine what is a fair amortization period in order to fairly allocate the loss between the utility and the consumer. Thus, the Commission finds no appropriate basis for requiring an amortization period greater than 10 years for North Anna Unit 3. This Commission in Docket No. E-22, Sub 224, approved a 10-year amortization of Surry Units 3 and 4; in Docket E-22, Sub 257, the

Commission continued the 10-year write-off of Surry Units 3 and 4 and approved the write-off of North Anna Unit 4 over a 10-year period; in Docket No. E-22, Sub 265, the Commission continued to allow Vepco a 10-year write-off for all three of said units. This Commission has consistently used a write-off period of 10 or fewer years for all major plant cancellations.

Based upon a careful consideration of the evidence of record in this case, the Commission finds and concludes that a 10-year period is a reasonable period and should be used for the amortization of the North Anna Unit 3 cancellation costs. Furthermore, the Commission concludes that amortization of the losses resulting from Vepco's cancellation of its Surry Units 3 and 4 and North Anna Unit 4 should be continued over 10 years as previously ordered by the Commission. Utilization of a 10-year amortization period is proper and fair in this proceeding for the reason that such an amortization period, particularly when considered in conjunction with the Commission's decision as subsequently discussed, to allow Vepco no return on the unamortized balance, will serve to more reasonably and equitably share the burden of such plant cancellations between the Company's shareholders and its present and future ratepayers.

Pursuant to the Commission's reexamination of the proper rate-making treatment of abandonment losses, the Commission has determined that it is neither fair nor reasonable to include any portion of the unamortized balance of such investments in rate base and, furthermore, that no adjustment should be allowed which would in fact have the effect of allowing the Company to earn a return on the unamortized balance. The Commission has concluded that this treatment provides the most equitable allocation of the loss between the utility and the consumer. It would be inequitable to place the entire loss of expenditures that were prudent when made on the utility. Thus, amortization should be allowed. However, on the other hand, the ratepayer must not bear the entire risk of the Company's investment. A middle ground must be found on which the Company bears some of the risk of abandonment and the ratepayer is protected from unreasonably high rates. The losses resulting from cancellations of utility generating plants will inevitably be borne by one or a combination of three groups: the utility investors, the ratepayers, and the income taxpayer. A recent study prepared by the United States Department of Energy indicates that a 10-year amortization of such losses will distribute costs in proportions that the Commission considers fair and equitable, even considering the effects of CWIP in rate base in North Carolina. NUCLEAR PLANT CANCELLATIONS: CAUSES, COSTS, AND CONSEQUENCES, United States Department of Energy, Washington, D.C. (April 1983). The Commission believes this will result in a fair and reasonable treatment of both the utility and its consumers.

In the last Vepco rate case, the Commission allowed that portion of the unamortized balance in Surry Units 3 and 4 and North Anna Unit 4 that was supported by senior capital to be included in rate base. Based upon the Commission's reexamination of this issue, the Commission believes it fairer and more reasonable to exclude this element from the Company's rate base. Similarly, the Commission has excluded from the rate base herein the entire unamortized balance of the Company's investment in its North Anna Unit 3.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 7

The evidence for this finding of fact is found in the testimony of Company witnesses Johnson and Peterson and Public Staff witnesses Kirby and Bright. The following table summarizes the amounts which the Company and the Public Staff witnesses contend are the proper levels of Vepco's investment in electric plant for use in this proceeding:

(000's Omitted)

Item	Company Witness Johnson	Public Staff Witness Kirby
Electric plant in service including nuclear fuel	$ 293,579	$ 293,579
Less: Accumulated depreciation	(72,115)	(72,115)
Nuclear fuel amortization	(7,566)	(7,566)
Net electric plant	213,898	213,898
Construction work in progress	18,850	0
Less: Cost-free capital	(14,330)	(14,330)
Total net original cost of Investment in electric plant	$ 218,418	$ 199,568

The Company and the Public Staff disagree as to only one item relating to the total net original cost of investment in electric plant: construction work in progress (CWIP). The Company in this proceeding has requested that $18,850,000 of expenditures for construction work in progress be included in rate base. All of these expenditures were made on the Company's Bath County project and two related transmission lines. In accordance with the Commission Order in Docket No. E-22, Sub 265, the Company has requested inclusion of only 60% of the expenditures after June 30, 1979, for these projects. No CWIP related to other projects is included in the requested $18,850,000, even though the Company had approximately $45 million of qualifying North Carolina retail jurisdiction CWIP on its books at the end of June 1983.

Public Staff witness Bright proposed that no CWIP expenditures be included in rate base in this case. Witness Bright testified that it is not in the public interest or necessary to the financial stability of the Company to include any CWIP in rate base. Additionally, Public Staff witness Bright objected to $2,428,000 of the requested CWIP based on advice of counsel that it is not permissible to include in rate base any CWIP which represents allowances for funds used during construction (AFUDC) which have been accrued since July 1, 1979, on any pre-July 1, 1979, CWIP balance.

Addressing this latter issue first, the Commission notes that the Public Staff has repeatedly and unsuccessfully advanced this position in several previous cases before this Commission. As the Commission has stated in the past, AFUDC accrued on CWIP expenditures is as much a part of the cost of construction as the cost of bricks and mortar or labor. Therefore, AFUDC accrued after July 1, 1979, on pre-July 1, 1979, construction expenditures is once again found by the Commission to be proper for inclusion in CWIP receiving rate base treatment.

The Commission turns next to the question of the amount of CWIP expenditures that should properly be included in rate base in this proceeding. In 1977, North Carolina G.S. 62-133(b)(1) was amended to provide

for reasonable and prudent expenditures of CWIP after July 1, 1979, to be included in rate base. Effective June 17, 1982, G.S. 62-133(b)(1) was further amended to provide that reasonable and prudent expenditures for CWIP may be included in rate base to the extent the Commission considers such inclusion to be in the public interest and necessary to the financial stability of the utility involved. The current amount of CWIP included in Vepco's North Carolina retail rate base is $17,377,000, as established in Vepco's last general rate case proceeding.

Company witness Johnson testified that the requested inclusion of CWIP expenditures in rate base is in the public interest and is necessary to the financial stability of the Company. Witness Johnson testified that the inclusion of CWIP in rate base results in lower costs to the customer. Witness Johnson further stated that while the cost to the customer is slightly higher during the construction period of a project, the benefits of lower costs that accrue to the customer during the many years that the project will be in service are far greater.

Exclusion of CWIP from rate base causes a disproportionate impact on customers at the time a new plant is placed in service, creating a major problem for the utility and its customers. The regular inclusion of construction expenditures in rate base avoids this sudden increase in rates when the facility is completed and placed in service.

The Commission also notes that a substantial portion of Vepco's construction program involves expenditures to convert oil-fired generation to coal-fired generation, resulting in major reductions in fuel costs which lower electric bills for customers. Vepco's fuel costs have reflected reductions in 1981, 1982, and 1983 from previous years. Witness Johnson testified that the inclusion of CWIP related to the Bath County project in rate base will materially enhance the Company's ability to continue this program on schedule and achieve resulting fuel savings sooner.

Company witnesses Johnson and Peterson testified that the requested inclusion of CWIP expenditures in rate base is necessary to the Company's financial stability. Witness Peterson provided an analysis of key financial data for Vepco and other "A" rated utilities and for "Baa" rated utilities. That data showed that Vepco data is, in all cases, below the average standards of "A" rated utilities. Witness Peterson testified that Vepco's present "A" rating is in jeopardy, and that Vepco has been so informed by Standard & Poor's. Witness Peterson concluded that Vepco's financial situation will be materially affected by the treatment of CWIP by the commissions which regulate it.

The inclusion of CWIP in rate base provides the Company with a cash return on its investment in plant facilities not yet in service. The cash return provided by inclusion of CWIP in rate base increases the amount of funds generated internally by the Company, thereby reducing the amount of financing required from outside sources. Inclusion of CWIP in rate base also increases coverage of fixed charges and is viewed favorably by investors and the rating agencies.

Public Staff witness Bright testified that she did not believe the inclusion of CWIP expenditures in rate base was necessary to the financial stability of the Company. In support of this position she isolated three

financial factors: pre-tax interest coverage without AFUDC, CWIP as a percentage of net utility plant, and AFUDC as a percentage of net income for common. Witness Bright found that Vepco's pre-tax interest coverage without AFUDC was below the industry median but that Vepco was slightly above the industry median for the other two factors.

Company witness Johnson, in rebuttal to Public Staff witness Bright, testified that the three factors Ms. Bright utilized do not fairly represent the true level of Vepco's financial position. When one considers other relevant financial data, such as market-to-book ratios and achieved return on common equity, it is clear that the Company's financial position remains below average. Vepco's common stock has continued to sell at a substantial discount below book value, despite the most significant increase in stock prices in recent years, an increase that has generally carried the electric utility industry, but not Vepco, to a point where its stock is selling at about book value. Industry data published by Kidder, Peabody & Company indicate that, based on market prices at June 17, 1983, the average market price as a percent of book value was 98.21% for the 106 utility group studied by Kidder, Peabody. Vepco's (Dominion Resources) market-to-book ratio as of June 17, 1983, was 77.90%, which ranked the Company 104 of the 106 utilities in the group. Only Consumer's Power Company at 77.80% and General Public Utilities at 39.51% had lower market-to-book ratios.

It is clear that Vepco's financial position is stronger than in the recent past, but the Company's financial indicators are still below the industry average. Therefore, a careful consideration of the entire record in this proceeding leads the Commission to conclude that the $18,850,000 of CWIP proposed herein by Vepco for inclusion in the Company's rate base represents reasonable and prudent construction expenditures and that inclusion of such amount of CWIP, being less than one-half of the Company's total existing CWIP applicable to its North Carolina retail operations, is in the public interest and necessary to the continuing financial stability of Vepco. The Commission further notes that three of the six units which comprise Vepco's Bath County pumped storage project are presently planned to come on-line in October 1985, less than two years hence. Thus, inclusion of $18,850,000 of CWIP applicable to the Bath County project in Vepco's rate base is appropriate in this proceeding.

Accordingly, the Commission concludes, based on the foregoing discussion, that the proper level of net original cost of electric plant in service to be used in setting fair and reasonable rates this proceeding is $218,418,000.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 8

The evidence for this finding of fact is found in the testimony of Company witness Johnson and Public Staff witness Kirby. The Company has requested the inclusion in rate base of $34,991,000 of working capital. The Public Staff has proposed $15,156,000. The difference between the Company and the Public Staff as to working capital is attributable to the Public Staff's proposal that no portion of the unamortized balances of cancellation costs for Surry Units 3 and 4 and North Anna Units 3 and 4 should be included in rate base. In Finding of Fact No. 6, the Commission rejected the Company's proposed inclusion of the requested portions of the unamortized balances in rate base. Accordingly, the Commission finds that $15,156,000 constitutes the proper level of working capital which should be included in the Company's rate base.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 9

The Commission, having previously determined the reasonable original cost of the Company's investment in electric plant which should be used in this case is $218,418,000, as determined in Finding of Fact No. 7, and that the reasonable allowance for working capital is $15,156,000, as determined in Finding of Fact No. 8, concludes that the proper original cost rate base for use in setting rates in this case is $233,574,000.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 10

Company witnesses Johnson, Hostetler, and Mitchem presented testimony showing that the end-of-period revenues should be $98,892,000, and Public Staff witnesses Kirby and Turner presented testimony showing that the end-of-period revenues should be $100,706,000. The difference between end-of-period revenues calculated by the Company and the Public Staff is the difference between customer growth and usage adjustments.

The Company and the Public Staff both proposed an adjustment to test year operating revenues to reflect customer growth. The customer growth adjustment typically consists of two adjustments: one adjustment reflects the difference between test year bills and normalized end-of-period bills; the other adjustment reflects the difference between test year average kWh per bill and normalized end-of-period kWh per bill. The adjustment to reflect normalized end-of-period bills is priced at average revenues per bill, and the adjustment to reflect normalized end-of-period kWh per bill is priced at incremental revenues per kWh. Each adjustment also produces an adjustment to test year kWh sales and therefore to related test year variable expenses (including fuel).

In general, both the Company and the Public Staff used regression analysis in this proceeding to determine normalized end-of-period bills, but they both used a simple ratio method to determine normalized end-of-period kWh per bill. Regression analysis is a procedure for removing the month-to-month variability inherent in the actual historical data in order to develop a representative trend of the data over a period of time. Use of regression analysis to determine the normalized end-of-period level has previously been adopted by the Commission in a number of electric and telephone rate cases, including the last rate case for Vepco in docket No. E-22, Sub 265. The Commission continues to be persuaded that regression analysis is the most appropriate method available for determining normalized end-of-period bills where such procedure is statistically valid.

On the other hand, neither the Company nor the Public Staff has proposed to utilize regression analysis to determine normalized end-of-period kWh per bill in previous electric rate cases or in this proceeding. Since none of the parties in this proceeding propose to utilize regression analysis to determine the normalized end-of-period kWh per bill, and since the regression analysis calculations are usually quite voluminous, the Commission will not attempt such calculations in this proceeding. Nevertheless, the Commission is of the opinion that regression analysis to determine the normalized end-of-period bills could very well be statistically valid for determining the normalized end-of-period kWh per bill, and that such procedure should be explored in future rate proceedings.

In applying regression analysis to determine the normalized end-of-period bills, the Public Staff utilized regression analysis for all rate schedules while the Company utilized regression analysis for all rate schedules except Schedule 5 (small general service) and Schedule 6 (large general service). The Company contended that regression analysis was not appropriate for Schedules 5 or 6 because the month-to-month variability in the historical data for Schedules 5 and 6 was not due to seasonality. However, the Commission is of the opinion that month-to-month variability in the historical data should still be removed, if possible, in order to determine the representative trend of the data over a period of time whether or not such month-to-month variability is due to seasonality, weather, economic conditions, etc.

Nevertheless, the Commission is disturbed by the fact that the average kWh per bill is so high for Schedule 5 (industrial) and for Schedule 6 (industrial and commercial) that even a small adjustment to end-of-period bills results in a very large adjustment to kWh sales for those rate schedules, which can cause the kind of problems pointed out by the Company in this proceeding regarding rounding off the fractional number of customers for Schedule 6. The Commission concludes that it should utilize the actual end-of-period bills for Schedule 5 (industrial) and for Schedule 6 (industrial and commercial) rather than normalized end-of-period bills in this proceeding, in view of the leverage associated with the large kWh per bill for said rate schedules and the problems discussed elsewhere herein regarding the simple ratio method to determine normalized end-of-period kWh per bill.

The Company criticized the Public Staff's method of applying the regression analysis whereby the Public Staff selected 12, 24, or 36 months of data for its trend line depending on the highest R-square value obtained. The Commission is of the opinion that the Public Staff approach is a reasonable attempt to ensure that the trend line developed from the historical data will represent the most recent general trend possible while at the same time giving equal weight to data representing each season of the year, and that the Public Staff's methodology should be approved.

The Company also criticized the Public Staff's method of calculating its adjustment to kWh sales resulting from its adjustment to reflect the normalized end-of-period bills. The Company contends that the Public Staff multiplied annual average kWh per bill times an adjustment to annual average bills, whereas it would be more accurate to multiply monthly average kWh per bill times an adjustment to monthly bills for each of the 12 months and then add the 12 products together. The Commission notes that the total adjustment to kWh sales using the Company's procedure and the Public Staff's procedure do not differ significantly and concludes that the Public Staff's procedure should be adopted for simplicity.

Therefore, the Commission concludes that the Public Staff's adjustments to reflect the difference between the actual test year bills and the normalized end-of-period bills for rate schedules 1, 5 (commercial), 7, 26, 27, 30, and 42 should be adopted herein, resulting in positive adjustments of 17,277,000 kWh and 18,312 bills and $1,203,810 revenues. The Commission further concludes that the Company's adjustments to reflect the difference between the actual test year bills and the normalized end-of-period bills for rate schedules 5 (industrial), 6 (commercial) and 6 (industrial) should be adopted herein, and should be modified to reflect the simplified Public Staff calculation procedure adopted herein regarding annual average kWh per bill

times adjustment to annual average bills, resulting in negative adjustments of 147,522,000 kWh and 245 bills and $6,946,951 revenues.

As discussed earlier herein, the Company and the Public Staff both utilized a simple ratio method to determine the normalized end-of-period kWh per bill in this proceeding. The Commission has already concluded herein that regression analysis is the most appropriate method available for determining the normalized end-of-period bills where such procedure is statistically valid, and that regression analysis could very well be statistically valid for determining the normalized end-of-period kWh per bill. The Commission is concerned about the statistical validity of the simple ratio method utilized by both the Company and the Public Staff, since it appears to determine a trend line using nothing more than two "data points" (i.e., previous year average kWh per bill versus current year average kWh per bill). While the Commission recognizes that the shortcomings of the simple ratio method increase the probability of producing an unrepresentative trend line, it also recognizes that the voluminous calculations required for regression analysis make it impractical to attempt such calculations for this proceeding. Therefore, the Commission concludes that the simple ratio method should be utilized herein.

The Public Staff calculated the change in kWh per bill over time based on the average kWh per bill for the 12 months ended March 31, 1982, versus the average kWh per bill for the 12 months ended March 31, 1983; whereas the Company calculated the change in kWh per bill over time based on the average kWh per bill for the 12 months ended June 30, 1981, versus the average kWh per bill for the 12 months ended June 30, 1982, plus the average kWh per bill for the nine months ended March 31, 1982, versus the average kWh per bill for the nine months ended March 31, 1983. The Public Staff contended that the Company's calculations are biased by giving unequal weight to each season of the year, since the Company uses 21 months of data instead of multiples of 12 months. The Commission agrees with the Public Staff.

However, a close review of the Company's calculations implementing the simple ratio method, and the Public Staff testimony that its comparable calculations are performed the same way as the Company's, indicates that both the Company and the Public Staff may have overstated their adjustments to reflect the difference between the average test period kWh per bill and the normalized end-of-period kWh per bill by a factor of two.

To illustrate the problem, we refer to Company exhibit DRH-8, page 15 of 84, which shows calculations to determine the difference between annual kWh per customer during the test year and annual kWh per customer prior to the test year. The 9816 kWh per customer represents the average annual kWh per customer at approximately January 1, 1982 (i.e., midpoint of year ended June 30, 1982). The 10107 kWh per customer represents the average annual kWh per customer at approximately January 1, 1981 (i.e., midpoint of year ended June 30, 1981). The 291 kWh per customer represents the decrease in average annual kWh per customer from approximately January 1, 1981, to approximately January 1, 1982. The objective of the calculation should be to determine the normalized annual kWh per customer at June 30, 1982. Since the decrease in annual kWh per customer is 291 kWh over 12 months, the decrease in annual kWh per customer over six months (from January 1, 1982, to June 30, 1982) is one-half of 291 kWh, or 146.5 kWh per customer. The total adjustment to kWh sales in the illustration should be 9,251,326 kWh (i.e., 146.5 kWh per

customer times 63,583 customers) instead of 18,502,653 kWh; and the total adjustment to revenues in the illustration should be $574,127 (or one-half of $1,148,254).

By applying the same reasoning to the calculations for each rate schedule, the total adjustment to reflect the difference between average annual kWh per customer and normalized end-of-period kWh per customer would be 12,328,000 kWh instead of the 24,814,000 kWh calculated by the Public Staff. The 12,328,000 kWh also reflects the normalized end-of-period bills calculated by the Company instead of the Public Staff for Schedule 5 (industrial) and Schedule 6 (commercial and industrial). The Commission concludes that the Public Staff's adjustments to reflect the difference between the actual test year bills and the normalized end-of-period bills should be adopted as modified herein, resulting in a positive adjustment of 12,328,000 kWh and a negative adjustment of $726,844 revenues.

Finally, the Commission concludes that the reasonable level of test year revenues under presently approved rates and after accounting and pro forma adjustments is $100,633,000.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 11

Company witness Hostetler and Public Staff witness Nightingale provided testimony and exhibits regarding the appropriate fuel component to be included in the base rates.

In his original prefiled testimony, witness Hostetler proposed a base fuel component of 1.803¢ per kWh excluding gross receipts tax based on the actual generation mix for the test year ending June 30, 1982, and reflecting a nuclear capacity factor of approximately 66%. In his additional prefiled testimony, he updated his proposed base fuel component to 1.666¢ per kWh excluding gross receipts tax based on the actual generation mix for the year ending June 30, 1983, and reflecting a nuclear capacity factor of approximately 55%. The Company subsequently computed a reduction of 0.125¢ per kWh in its proposed base fuel component in order to eliminate the nonfuel portion of purchased power which had been included therein, resulting in a final recommended base fuel component of 1.541¢ per kWh.

In his original prefiled testimony, Public Staff witness Nightingale proposed a base fuel component of 1.626¢ per kWh excluding gross receipts tax based on a normalized generation mix reflecting a 62.7% nuclear capacity factor. In his revised prefiled testimony witness Nightingale corrected his normalization calculations and updated his unit fuel prices to June 1983 levels, resulting in a recommended base fuel component of 1.663¢ per kWh excluding gross receipts tax. During cross-examination, witness Nightingale further revised his recommended base fuel component to 1.687¢ per kWh to incorporate the Company's July 1983 nuclear fuel cost. Subsequently, the Public Staff pointed out in its recommended order that correction of an error in witness Nightingale's computation of the unit coal price would result in a base fuel component of 1.675¢ per kWh excluding gross receipts tax. The Public Staff also pointed out in its recommended order that a reduction in its recommended base fuel component to eliminate the nonfuel portion of purchased power (utilizing the same unit prices as the Company used for said nonfuel portion of purchased power) would result in a recommended base fuel component of 1.543¢ per kWh excluding gross receipts tax.

The principal difference between the Company's final recommended base fuel component of 1.541¢ per kWh and the Public Staff's final recommended base fuel component of 1.543¢ per kWh is the use of actual generation mix versus normalized generation mix. The Company recognizes that normalization might well be appropriate under different circumstances, but asserted that an attempt to normalize fuel expenses in this proceeding would be an unnecessary exercise because fuel costs and plant performance are within reasonable ranges. The Company is also critical of certain aspects of the normalization methodology utilized by the Public Staff.

The Commission notes that the final results of the Company's calculations based on actual generation mix and the Public Staff's calculations based on a normalized generation mix are very close. The Commission also notes that the Company calculated its base fuel component based on actual generation mix in the prior general rate case in Docket No. E-22, Sub 265, and the Public Staff agreed to the Company's recommended base fuel component in that proceeding.

The Commission is of the opinion that a normalized generation mix would be appropriate under most circumstances for determining the base fuel component. However, since the results of utilizing a normalized generation mix are so close to the results of utilizing actual generation mix in this case, and since the methodology utilized to normalize the generation mix in this proceeding is not universally accepted, the Commission concludes that the actual generation mix would be a just and reasonable approach for determining the base fuel component herein.

The Commission concludes that the appropriate base fuel component excluding the nonfuel component of purchased power for this proceeding would be the 1.541¢ per kWh excluding gross receipts tax recommended by the Company. The 1.541¢ per kWh multiplied by the Commission end-of-period kWh sales level of 1,673,962,530 yields $25,795,763, based on total kWh billed less total kWh unbilled.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 12

The evidence for this finding of fact is found in the testimony and exhibits of Company witnesses Johnson and Hostetler and Public Staff witnesses Turner, Nightingale, and Kirby. The following schedule shows the operating revenue deductions proposed by the Company and the Public Staff:

(000's Omitted)

Item	Company	Public Staff
Operation and maintenance expenses	$54,831	$54,006
Depreciation expense	9,484	9,484
Amortization of property losses	2,483	2,859
Gain or loss on disposition of property	(3)	(3)
Taxes other than income	9,108	8,978
Income taxes	6,442	8,246
Interest on customer deposits	47	47
Commitment fees	69	69
Contributions	12	-
Gain on Bath County sale	-	(178)
Totals	$82,473	$83,508

The $825,000 difference between the parties with respect to operation and maintenance expenses is analyzed as follows:

(000's Omitted)

	Item	
1.	Base fuel expense	$ (683)
2.	Nonfuel decrease in customer growth and usage expenses	(11)
3.	Nuclear fuel disposal cost	(98)
4.	Officers' salaries	(33)
		$ (825)

The difference in base fuel expense of $683,000 is the result of two functions. First, the Public Staff has excluded consideration of unbilled kWh's in calculating the appropriate level of base fuel expense to be used in setting rates in this proceeding. However, the Public Staff has not excluded the effects of unbilled kWh's in calculating the level of end-of-period revenues recommended herein in this proceeding. After careful consideration of this matter, the Commission concludes that consistency dictates that the unbilled kWh's should be considered in determining an appropriate level of base fuel expense, and therefore the Public Staff adjustment should not be made.

Second, the Public Staff has adjusted base fuel expense to reflect the Public Staff's adjustment to kWh sales resulting from the customer growth and usage adjustment, spoken to hereinabove, under Evidence and Conclusions for Finding of Fact No. 10. Since the Commission's adjustment to kWh's sales resulting from the customer growth and usage adjustment is different from that sponsored by either party, as spoken to under Evidence and Conclusions for Finding of Fact No. 10, then the base fuel expense derived from the end-of-period kWh sales adjusted for customer growth and usage is necessarily different from that presented by either party. In addition, the Commission notes that the Public Staff did not consider the nonfuel portion of purchased power in computing its total adjustment due to the customer growth and usage adjustment. The Commission concludes that this procedure is inconsistent with past Commission decisions and should be rejected.

Since the Commission has adopted a customer growth and usage adjustment different from that promulgated by either party, the Commission must consistently apply this adjustment to determine the appropriate level of end-of-period nonfuel expense. Based on this, the Commission concludes that the adjustment to nonfuel expense for customer growth and usage should be $(118,578).

The next issue involving operation and maintenance expenses is the level of nuclear fuel disposal cost of in-reactor fuel. Public Staff witness Kirby proposed a $98,000 reduction in the Company's proposed nuclear disposal cost. Mr. Kirby stated that his adjustment was necessary because of the Public Staff's lower proposed level of nuclear generation, and based his proposed cost per kWh on the 1.17 mills per kWh cost found in Company witness Ferguson's testimony. The 1.17 mills per kWh resulted from the 1.0 mill per kWh contract rate for nuclear fuel disposal charged by the U.S. Department of Energy, plus a .17 mill increment for the Company's cost of interim storage of spent fuel. Company witness Johnson testified in rebuttal that Mr. Kirby's calculation of nuclear disposal cost is incorrect because it applies the 1.17

mill factor to the net nuclear generation proposed by Public Staff witness Nightingale. According to Mr. Johnson, this is improper because the Energy Department contract specifies that kWh's are to be measured at the generator, which results in a gross nuclear generation amount before reduction for internal Company power usage. However, Mr. Johnson agreed on cross-examination that Mr. Nightingale had based his nuclear generation level on a capacity factor obtained from a North American Electric Reliability Council (NERC) study which indentified the factor as a "gross" capacity factor. The Commission, in Evidence and Conclusions for Finding of Fact No. 11, concluded that the nuclear generation level proposed by the Company was reasonable. The Commission concludes that the preponderance of evidence in this proceeding dictates that witness Kirby's factor of 1.17 mill per kWh cost rate is appropriate, to be used in determining end-of-period nuclear fuel disposal costs. Therefore, the Commission concludes that a $43,000 adjustment to reduce nuclear fuel disposal cost for in-reactor fuel is proper.

Another disagreement arose concerning the Public Staff's adjustment to remove from the cost of service the salaries of the Company's Chairman of the Board, President, and Executive Vice President. Witness Kirby testified that the adjustment would prevent ratepayers from paying for costs properly related to shareholders and that his methodology was based on that found reasonable by the Commission in Docket No. E-22, Sub 265. Mr. Johnson, in his rebuttal testimony, rejected the Public Staff's adjustment on the ground that the Public Staff produced no evidence linking those three officers' salaries with shareholders' interests. The Company's Executive Vice President, Jack H. Ferguson, is Chief Operating Officer of the Company and his primary duty is to ensure that customers receive adequate and reliable service. The Commission has found that the quality of the Company's service is adequate and notes that the Company's fuel costs have been reduced for the last three years and that the performance of its generating system has improved significantly.

The Commission has, therefore, carefully reconsidered the issue of officers' salaries under the facts of this case and concludes that no adjustment to reduce officers' salaries expense is appropriate in this proceeding.

The Commssion, upon review of the record and consistent with past rate-making practices, has reduced the Applicant's uncollectible expense by $4,000 to reflect the Commission's adjustment to the Applicant's end-of-period revenue, spoken to under Evidence and Conclusions for Finding of Fact No. 10.

Based on the foregoing, the Commission concludes that the reasonable level of operation and maintenance expense is $53,754,000.

The parties disagree as to the proper level of amortization of property losses. The Company proposed that the North Anna 3 abandonment loss be included in rate base and amortized over 10 years with the annual amortization calculated to produce a "levelized" North Anna 3 related revenue requirement for each of the 10 years. The Public Staff proposed a $376,000 higher first-year amortization of the North Anna 3 loss because of the Staff's position that the loss should be excluded from rate base and amortized over 12 years on a "straight-line" basis. Since the Commission adopted, in Finding of Fact No. 6, a 10-year amortization of the North Anna 3 loss without rate base incusion, the Commission concludes that $3,215,000 is the proper level of amortization of property losses.

The parties differed by $130,000 on the proper level of taxes other than income. This difference results from a normalization adjustment to gross receipts tax made by Mr. Kirby and from the gross receipts tax effect of the difference in level of revenues supported by the parties. Witness Kirby recommended that the gross receipts tax expense be reduced by $239,000 in order to normalize that tax to the statutory six percent of end-of-period revenued net of uncollectibles. The Commission concludes this adjustment is appropriate.

The remainder of the difference in taxes other than income results from a $109,000 increase proposed by the Public Staff resulting from its adjustment to increase end-of-period revenues over the level sponsored by the Company. Based on the Public Staff's normalizing adjustment and the level of revenues determined in Finding of Fact No. 10, the Commission concludes that the proper level of taxes other than income is $8,974,000.

The difference in income taxes is related to the different expense and revenue levels proposed by the parties except for witness Kirby's adjustment to tax-deductible interest resulting from his update to April 30, 1983, of accumulated investment tax credits. The Company did not dispute that adjustment. Based on all of the above conclusions associated with end-of-period revenues, expenses, and investment, the Commission determines that the proper level of income tax expense is $7,778,000.

Whether the Company's charitable contributions are properly includable in the cost of service was also an issue between the parties. Mr. Johnson contended that in order to be a good corporate citizen a utility company is expected to contribute to charities in its service area. Charitable contributions should, therefore, be considered a cost of doing business and included in the cost of service, according to Mr. Johnson. Mr. Kirby recommended that charitable contributions be excluded from the cost of service in order that ratepayers not be forced to contribute through rates to charities of the Company's choosing.

After giving this issue due consideration, the Commission reaffirms its long standing policy of excluding charitable contributions from the cost of service. Although such contributions may be prompted by commendable motives, they cannot properly be considered costs necessary for the production and sale of electricity. Accordingly, the Commission agrees with the $12,000 adjustment to reduce operating revenue deductions as proposed by the Public Staff.

The final difference in operating income deductions results from the Public Staff's adjustment to increase operating income by the gain on the sale of 20% of the Bath County project. Evidence related to this issue is found in the testimony and exhibits of Company witness Johnson and Public Staff witness Kirby.

According to Mr. Kirby, net operating income under present rates should be increased by $178,000 in order to give ratepayers the benefit of the nonoperating gain realized by the Company's sale of 20% of the Bath County Pumped Storage project to Allegheny Power System during the test year. He contended that, since ratepayers will be required to absorb the losses incurred by the Company on plant abandonments, it would be inequitable and inconsistent to ignore gains on the sale of other plant assets. Mr. Kirby

recommended that the proper amnortization period for the gain is one year, since the gain is relatively small compared to the annual cost of service and would not cause undesirable fluctuations in rates if amortized over a short period.

In his rebuttal testimony, Mr. Johnson argued that the Bath County gain is not analogous to losses on plant cancellations and that the two issues should be considered separately. He asserted that the ratepayers have already benefited from the Bath County sale through lower financing costs. He also observed that, for rate-making purposes, the Commission has traditionally disregarded gains or losses on property sales. Although Mr. Johnson emphasized his opposition to flowing the gain to ratepayers, he contended that, if the Commission does allocate the gain to ratepayers, the amortization period should be longer than one year. A longer period is appropriate, according to Mr. Johnson, because both the useful life of the Bath County project and the financing cost savings resulting from the sale will occur over many years.

The Commission has considered all evidence relating to this issue and concludes that the appropriate rate-making treatment to be afforded this item is to amortize the gain over a period of three years.

The parties are in agreement that the appropriate level of depreciation expense is $9,484,000, the appropriate level of gain on disposition of property is $(3,000), the appropriate level of interest on customer deposits is $47,000, and the appropriate level of commitment fees is $69,000; therefore, the Commission concludes that these amounts are reasonable.

As the result of the foregoing conclusions, the Commission finds that $83,259,000 is the reasonable level of operating income deductions to be used in setting fair and reasonable rates in this proceeding.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 13 AND 14

Five witnesses testified in the area of capital structure and cost of capital. The Company offered the testimony of O. James Peterson III, Vice President and Treasurer of Vepco, James P. Carney, Director of Economic Analysis of Vepco, and Eugene Meyer, Vice President of Kidder, Peabody & Co. The Public Staff offered the testimony of Dr. Caroline M. Smith, Senior Economist with the firm of J.W. Wilson & Associates, Inc., and consultant to the Public Staff. James Graham Dynes, Jr., Staff Economist of Vepco, testified on rebuttal to Dr. Smith.

Though on the surface there appears to be no disagreement between Vepco and the Public Staff as to the proper capital structure in this proceeding, according to their respective proposed orders, there is an area that needs to be noted here. In its original filing, the Company assigned zero cost to that portion of common equity designated as "other paid in capital." This is consistent with past treatment of this item by the Commission, the Company, and the Public Staff. In its testimony and exhibits, it is not entirely clear how the Public Staff proposes to treat this item. In any event, in its operating income for return schedules presented in the record in this proceeding, the Public Staff has computed the Applicant's net income available for common equity by applying a cost rate of 13% to the Applicant's entire common equity component, including the other paid in capital portion. In its

proposed order, the Company applied its cost of equity to the entire common equitry component, including the other paid in capital, in determining net income available for common equity. Based on the entire record in this matter, the Commission concludes that the other paid in capital portion of Vepco's capital structure should not be included in the common equity portion receiving a return in this proceeding. This decision is consistent with the Commission's decision in Docket No. E-22, Sub 265.

Since, with the exception spoken to above, the parties agreed in the record that the Company's capital structure at June 30, 1982, is proper to be used in this proceeding, the Commission concludes that the proper capital structure for use in this proceeding is as follows:

Item	Percent
Long-term debt	53.22
Preferred stock	10.96
Other paid in capital	.38
Common equity	35.44
Total	100.00

Consistent with the evidence supporting the above capital structure, the Commission concludes that the appropriate embedded costs of debt and preferred stock are 9.09% and 8.51%, respectively, as supported by the Public Staff and the Company.

The evidence concerning the fair rate of return for Vepco is found in the testimony of Company witness Carney and Public Staff witness Smith. Mr. Carney, in his original prefiled testimony, testified that the Company should be allowed an equity return between 17.0% and 17.5%. Dr. Smith proposed an equity return of 13%.

In his analysis of the cost of equity, Mr. Carney relied on the results of his DCF analysis, which resulted in an equity cost rate of 15.9% to 16.6%. In his initial direct testimony, his DCF results were in the range of 14.05% to 17.01%. Mr. Carney relied upon his quarterly DCF model, increased the result for floation costs and attrition, and concluded that the cost of equity to Vepco was 16% to 17%. In his additional testimony, he updated the yield and growth value and proposed an equity return in the 15.9% to 16.6% range.

Dr. Smith derived her equity cost estimate on the basis of a DCF analysis for Vepco and the electric utility industry as a whole. Dividend calculations were done with market prices over the six months ended March 31, 1983, and indicated dividend rates at the end of the pricing period. Vepco's dividend yield was 11.2%, as compared to the industry average dividend yield of 10.7%. Actual historical growth indicators for Vepco were somewhat lower than industry averages, ranging between .7% to 3.2% for Vepco and 1.2% to 3.8% for the industry. Dr. Smith's estimate of the long-term dividend growth investors expect for Vepco is between 1.5% and 2.0%, somewhat higher than Vepco's own experienced growth and below the industry average historical experience. Based upon a dividend yield of 11.2% for Vepco and a growth estimate of 1.5% to 2.5% for Vepco, Dr. Smith's estimate of the current cost of common equity capital to Vepco is 13%.

The determination of the appropriate fair rate of return for Vepco is of great importance and must be made with great care because whatever return is

allowed will have an immediate impact on Vepco, its shotkholders and its customers. In the final analysis the determination of a fair rate of return must be made by this Commission, using its own impartial judgment and guided by the testimony of expert witnesses and other evidence of record. Whatever return is allowed must balance the interest of the ratepayers and investors and meet the test set forth in G.S. 62-133(b)(4):

> "Fix such rate of return ... as will enable the public utility by sound management to produce a fair return for its shareholders, considering changing economic conditions and other factors, as they then exist, to maintain its facilities and services in accordance with the reasonable requirements of its customers in the territory covered by its franchise, and to compete in the market for capital funds on terms which are reasonable and which are fair to its customers and to its existing investors."

The return allowed must not burden ratepayers any more than is necessary for the utility to continue to provide adequate service. The North Carolina Supreme Court has stated that the history of G.S. 62-133(b):

> "...supports the inference that the Legislature intended for the Commission to fix rates as low as may be reasonaly consistent with the requirements of the Due Process Clause of the Fourteenth Amendment to the Constitution of the United States..." State ex rel. Utilities Commission v. Duke Power Company, 285 N. C. 377, 206 S.E. 2d 269 (1974)

The nature of the evidence in a case such as this makes it extremely difficult to balance all of the opposing interests, since much, if not all, of the evidence is based on individual witnesses' perceptions and interpretations of trends and data from the capital market. The Commission has considered carefully all of the relevant evidence presented in this case, with the constant reminder that whatever return is allowed will have an immediate impact on the Company, its stockholders, and its customers. The Commission must use its impartial judgment to ensure that all the parties involved are treated fairly and equitably. In coming to a final decision on this matter, the Commission is not unmindful of the upward pressure on capital costs generally present in the economy over recent years. The Commission is also aware of the recent downward trend in interest and other capital costs.

Based upon the foregoing and the entire record in this docket, the Commission finds and concludes that the fair rate of return that Vepco should have the opportunity to earn on the original cost of its rate base is 11.18%. Such fair rate of return will yield a fair return on all of Vepco's common equity capital of 15.25%, after payment of interest obligations.

The Commission cannot guarantee that the Company will, in fact, achieve the level of return herein found to be just and reasonable. Indeed, the Commission would not guarantee it if it could. Such a guarantee would remove necessary incentives for the Company to achieve the upmost in operational and managerial efficiency. The Commission believes, and thus concludes, that the level of return approved herein will afford the Company a reasonable opportunity to earn a reasonable return for its stockholders while providing adequate and economical service to ratepayers.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 15

This Commission has previously discussed its findings of fact and conclusions concerning the fair rate of return which Vepco should be given the opportunity to earn.

The following schedules summarize the gross revenues and the rates of return which the Company should have a reasonable opportunity to achieve based on the increases approved herein. The schedules illustrating the Company's gross revenue requirements incorporate the findings and the conclusions heretofore and herein made by the Commission.

SCHEDULE I
VIRGINIA ELECTRIC AND POWER COMPANY
North Carolina Retail Operations
STATEMENT OF OPERATING INCOME

Twelve Months Ended June 30, 1982
(Adjusted for Known Changes Occurring Subsequent to the End of the Test Year)

(000"s Omitted)

	Present Rates	Approved Increase	After Approved Rates
Operating Revenues:			
New operating revenues	$100,633	$18,340	$118,973
Operating Revenue Deductions:			
Operation and maintenance expenses	53,754	46	53,800
Depreciation	9,484		9,484
Amortization of property losses	3,215		3,215
Gain or loss on disposition of property	(3)		(3)
Taxes other than income	8,974	1,098	10,072
Deferred income taxes	1,787		1,787
Current federal and state income taxes	4,531	8,467	12,998
Investment tax credits	2,047		2,047
Investment tax credit amortization	(587)		(587)
Interest on customer deposits	47		47
Commitment fees	69		69
Gain on Bath County sale	(59)		(59)
Total operating revenue deductions	83,259	9,611	92,870
Net operating income	$ 17,374	$ 8,729	$ 26,103

SCHEDULE II
VIRGINIA ELECTRIC AND POWER COMPANY
North Carolina Retail Operations
STATEMENT OF RATE BASE AND RATE OF RETURN

Twelve Months Ended June 30, 1982
(Adjusted for Known Changes Occurring Subsequent to the End of the Test Year)

(000's Omitted)

Item	Amount
Investment in Electric Plant:	
Gross electric plant in service, including nuclear fuel	$293,579
Deduct: Accumulated provision for depreciation	(72,115)
Amortization of nuclear fuel assemblies, front-end costs	(7,566)
Construction Work in Progress	18,850
Plant investment less acumulated depreciation and amortization	232,748
Deduct: Cost-free capital	(14,330)
Total net investment in electric plant before working capital allowance	218,418
Working capital and deferred debits and credits	15,156
Original cost rate base	$233,574

SCHEDULE III
VIRGINIA ELECTRIC AND POWER COMPANY
North Carolina Retail Operations
STATEMENT OF CAPITALIZATION AND RELATED COSTS

Twelve Months Ended June 30, 1982

Item	Ratio %	Original Cost Rate Base	Embedded Cost %	Net Operating Income
	Present Rates - Original Cost Rate Base			
Long-term debt	53.22	$124,308	9.09	11,300
Preferred stock	10.96	25,600	8.51	2,179
Other paid-in capital	.38	887		-0-
Common equity	35.44	82,779	4.71	3,895
Total	100.00	$233,574		$17,374
	Approved Rates - Original Cost Rate Base			
Long-term debt	53.22	$124,308	9.09	$11,300
Preferred stock	10.96	25,600	8.51	2,179
Other paid-in capital	.38	887		-0-
Common equity	35.44	82,779	15.25	$12,624
Total	100.00	$233,574		$26,103

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 16 THRU 25

Company witnesses Hostetler and Edwards and Public Staff witnesses Turner and Smith presented testimony and evidence concerning conservation, load management and rate design.

Miscellaneous Service Charges

The Company proposes to increase its service charges for the following purposes in order to reflect current costs: (1) initial connection charge from $11.75 to $17.75; (2) reconnection charge from $11.75 to $17.75; (3) temporary connection charge from $11.75 to $17.75; (4) service charge for after hours repairs of outdoor lighting from $11.75 to $17.75; and (5) service charge for supplying a temporary connection from overhead lines (from $74.50 to $79.75) or from an underground transformer (from $115.75 to $123.75) or from underground lines (from $178.50 to $192.00). The Company calculates that the proposed increases described above will produce approximately $103,406 additional revenue.

The Company also proposes to modify the options available to customers for extra facility charges to: (a) customer pays initial installation cost, plus replacement cost, plus actual O&M costs as they occur; or (b) customer pays initial installation cost, plus 0.73% per month of installation cost for O&M and replacement.

The proposed revisions to the service charges and the extra facilities charges were unopposed, and the Commission concludes that said revisions should be approved.

Class rates of Return

Public Staff witness Turner pointed out in his prefiled testimony that the class rates of return for Small General Service (Schedules 5 and 7) and for County/Muncipal (Schedules 30 and 42) would not be within 10% of the overall N.C. retail rate of return under the Company's proposed rates, and he recommended that the rates of return for those customer classes be adjusted so that they are within 10% of the overall N.C. retail rate of return.

Company witness Edwards pointed out in his rebuttal testimony that the Small General Service class and the County/Municipal class were combined for rate design purposes, and that the rate of return for the combined classes will be within 10% of the overall N.C. retail rate of return. He also pointed out that the services provided under the schedules for each class are very similar, and that the unit prices are practically identical.

The Commission notes that the Company proposes a 29.7% increase for the County/Municipal class (including a 42.0% increase for Schedule 42 and a 20.2% increase for Schedule 30) versus a 20.2% increase for the Small General Service class (including a 29.7% increase for Schedule 7 and a 19.9% increase for Schedule 5). Such increases will still produce rates of return under the Company's proposed rates of 13.9% for the Small General Service class versus 10.9% for the County/Municipal class. This indicates that the Company is in the process of bringing the rates of return for the Small General Service class and the County/Municipal class closer together, and that such process will obviously require more than one rate proceeding in order to restrain the

impact on the customers to an acceptable level. Therefore, the Commission concludes that the relative rates of return proposed by the Company for the two classes should be approved.

Revenue Increases for Schedules 5, 7, 30, and 42

Schedule 7 is combined with Schedule 5 for purposes of making cost of service allocations and calculating rates of return. However, Schedule 7 offers significantly lower rates in winter than Schedule 5 for customers having separately metered water heating or separately metered space heating. Since no separate cost allocation study is made of Schedule 7, there is no firm basis for establishing rates for Schedule 7 which are so different from Schedule 5. Schedule 7 was closed to new applications for service after November 1, 1981.

The Commission is of the opinion that Schedule 7 should be merged into Schedule 5 over a period of time in such a way as to maintain the impact on customers at an acceptable level. In this proceeding, the Company proposes to increase Schedule 7 revenues by 29.7% versus 19.9% for Schedule 5. Therefore, the Commission concludes that the relative increases proposed by the Company for Schedules 5 and 7 should be approved.

Schedule 42 is combined with Schedule 30 for purposes of making cost of service allocations and calculating rates of return. However, Schedule 42 offers significantly lower rates in winter than Schedule 30 for customers having all electric service. Since no separate cost allocation study is made of Schedule 42, there is no firm basis for establishing rates for Schedule 42 which are so different from Schedule 30. Schedule 42 is not closed to new applications for service.

In this proceeding, the Company proposes to increase Schedule 42 revenues by 42.0% versus 20.2% for Schedule 30. The Commission is of the opinion that moving Schedule 42 rates closer to Schedule 30 rates is appropriate and consistent with moving Schedule 7 rates closer to Schedule 5 rates. Schedule 30 rates are identical to Schedule 5 rates, and Schedule 42 rates are practically identical to Schedule 7 rates. Therefore, the Commission concludes that the relative increases proposed by the Company for Schedules 30 and 42 should be approved.

The Commission further concludes that the process of moving the rates for Schedules 7 and 42 closer to the rates for Schedules 5 and 30 should be continued in future rate cases in order to remove the discrepancy between the rates of return for the Small General Service class (Schedules 5 and 7) and the County/Municipal class (Schedules 30 and 42).

Time of Day Rates - General

The Company proposes in this proceeding to revise the on-peak/off-peak hours applicable to time of day (TOD) rate schedules 1P, 5P, 6P, and 9. TOD schedule 1T (all energy schedule for residential service) will be unaffected.

The proposed new on-peak hours for energy charges will be 7:00 a.m. to 10:00 p.m. (clock time) versus the old on-peak hours of 10:00 a.m. to 10:00 p.m. (EDT).

The proposed new on-peak hours for demand charges for Schedule 1P will be 12:00 noon to 10:00 p.m. (clock time) during June through September, and 7:00 a.m. to 11:00 a.m. plus 5:00 p.m. to 10:00 p.m. (clock time) during October through May, versus the old on-peak hours of 10:00 a.m. to 10:00 p.m. (EDT).

The proposed new on-peak hours for demand charges for Schedules 5P, 6P, and 9 will be 10:00 a.m. to 10:00 p. m. (clock time) during June through September, and 7:00 a.m. to 10:00 p.m. (clock time) during October through May, versus the old on-peak hours of 10:00 a.m. to 10:00 p.m. (EDT).

The Company also proposes to modify its provisions for controlling migration of customers between Schedules 5P and 6P by eliminating load factor as a criteria for qualifying for service under each schedule, and by replacing said criteria with maximum demand. Schedule 5P will be available to customers having less than 500 kW demand, and Schedule 6P will be available to customers having greater than 500 kW demand.

The Company also proposes to eliminate the RKVA charge from Schedule 5P, since high demand customers will no longer be eligible for service under Schedule 5P.

The Company also proposes to limit the availability of Schedules 5P and 6P to the first 50 volunteers each, and to limit the availability of Schedules 1P and 1T to the first 200 volunteers each.

None of the proposals discussed above were opposed by any party, and the Commission concludes that they should be approved. However, the Commission is also of the opinion that some confusion could result from the change to on-peak hours (clock time) versus the old on-peak hours (EDT or EST). Therefore, the Commission further concludes that each TOD rate schedule should specify that the on-peak hours are clock time.

Bimonthly Billing for TOD Schedules

The Company proposed to extend the bimonthly billing option currently available under Schedule 1 (residential service) to TOD Schedules 1P and 1T and to dual fuel schedule 1DF. The proposal was opposed by the Public Staff, and Company witness Edwards agreed in his rebuttal testimony that bimonthly billing need not be extended to the TOD schedules at this time.

The Commission is of the opinion that bimonthly billing would not be consistent with giving customers appropriate price signals based on time of usage, since it would create a longer time lapse between the time usage occurs and the time the customer sees the price signals resulting from such usage. Therefore, the Commission concludes that bimonthly billing should not be available for service under rate schedules 1P, 1T, or 1DF.

Availability of TOD Schedules

The Company proposed that TOD Schedules 1P and 1T be limited to single family residences, and that they no longer be available to flats, apartments, boarding houses, etc. The Public Staff opposed the proposal on grounds that apartments, flats, etc., are a growing segment of the residential customer class and offer a significant opportunity for increased utilization of TOD rates. The Company offered no rebuttal to these objections.

Nevertheless, the Commission is of the opinion that apartment dwellers might be expected to be more transient, and that the utilization of a TOD meter at a given apartment location might be expected to be of shorter duration. One of the reasons for placing limitations on the number of volunteers for TOD rates is that the effectiveness and impact of such rates have not yet been evaluated, and such evaluation would best be accomplished by utilizing longer term volunteers (i.e., those identified as single family residences). The Commission concludes that the Company's proposal should be denied in this proceeding, and that further discussion of this issue would be appropriate in the Company's next general rate case, including a report on any problems with turnover of volunteers for the TOD rates.

Minimum Contracts for TOD Schedules

The Public Staff proposed eliminating the one-year minimum contract provision in Schedules 1P, 1T, 1W, and 1DF in this proceeding. Company witness Edwards testified upon rebuttal that the one-year contract provision could be eliminated from Schedules 1P and 1T by substituting in its place a provision that customers who switch from said schedules to another schedule could not be served again under the previous schedule within one year of such switch. The Public Staff did not oppose the alternative suggested by the Company, and the Commission concludes that the Company's alternative proposal should be approved.

However, the Company also expressed its preference for retaining the current one-year contract provision for Schedules 1W and 1DF. The commission is of the opinion that the alternative provision adopted herein for Schedules 1P and 1T should also resolve the Company's concerns regarding Schedules 1W and 1DF, and concludes that the alternative provision discussed herein should also be adopted for Schedules 1W and 1DF for the sake of consistency.

Schedule 1W

Schedule 1W is an interruptible TOD rate for electric storage water heating and electric storage space heating whereby service is interrupted 12 hours daily, five days per week, by means of time clocks.

The Public Staff has pointed out in previous rate proceedings that the current 9:00 a.m. to 9:00 p.m. hours of interruption do not include the hours of the system peak during winter months. In this proceeding, the Company proposed to extend the hours of interruption to include the time of the winter peak. The Public Staff recommended that such hours of interruption also include a mid-day reheating period which would alleviate the loss of hot water resulting from extended interruptions. The Company and the Public Staff agreed that the new hours of interruption should be between 6:30 a.m. and 11:00 a.m. (EST), and between 12:30 p.m. and 8:30 p.m. (EST).

The Commission is of the opinion that the hours of interruption agreed upon by the Company and the Public Staff should be adopted herein.

Schedule 1

In the previous general rate case in Docket No. E-22, Sub 265, the Company proposed in Schedule 1 to eliminate the declining block rate for its winter energy charge, and to extend the summer/winter rate differential to all kWh

usage. The Public Staff agreed with the Company's proposal, but recommended that a more gradual transition be implemented. The Commission adopted the Public Staff's recommendation in that proceeding by extending the size of the first block from 800 kWh to 1500 kWh.

In this proceeding the Company proposes to retain the 1500 kWh first block in Schedule 1, and the proposal is unopposed by the Public Staff. The Commission is of the opinion that the size of the first block need not be revised in this proceeding, but that consideration should be given to further revision in future proceedings.

The Company also proposed to increase its basic customer charge for residential service from $6.64 to $7.70 in order to move closer to the $11.11 it contended was the true customer-related cost of service per billing. The Commission is of the opinion that there is still merit in maintaining the basic customer charge for residential service below the actual customer-related cost per billing at the present time, and it concludes that said basic customer charge should be increased to $6.85 in this proceeding.

Conservation Discounts

Public Staff witness Smith recommended that the conservation discount applicable to Schedule 1 customers be amended so that the thermal insulation requirements conform to the standards of the Company's Energy Saver Home (ESH) program, and that said requirements include efficiency standards for heat pumps and central air conditioners as in the ESH program.

Witness Smith also recommended that the conservation discount available to Schedule 1 customers also be made available to customers under TOD Schedules 1P and 1T. He also recommended that the standards for the conservation discount be listed directly on the tariff sheets for Schedules 1P and 1T as well as for Schedule 1.

The Company agreed with the Public Staff's proposals regarding the conservation discount, and said proposals were unopposed by any other party. Therefore, the Commission concludes that they should be approved.

Public Staff witness Smith also recommended in his prefiled testimony that the conservation discount be based on an across-the-board percentage of the monthly bill, or at least a percentage of the monthly energy charge. Company witness Edwards testified upon rebuttal that the discount was based on calculations showing the savings per kWh, not savings as a percent of expenses per kWh. Therefore, the Commission concludes that the conservation discount should remain as currently applied by the Company.

Schedule 6

The Commission's general rate Order in Docket No. E-22, Sub 257, required the Company to modify its proposed rate design for Schedule 6 (large general service) in order to better reflect the ratio between demand charge revenues and energy charge revenues as indicated by the Company's cost allocation study.

In the previous general rate case in Docket No. E-22, Sub 265, the Company increased its energy charges in Schedule 6 without increasing its separate

demand charge, thereby further correcting the ratio between demand charge revenues and energy charge revenues.

In the current general rate case in Docket No. E-22, Sub 273, the Company again proposes to increase its energy charges in Schedule 6 without increasing its separate demand charge in order to further correct the ratio between demand charge revenues and energy charge revenues. The Company's proposal was questioned by NCTMA.

In order to complete its review of the appropriate ratio between demand charge revenues and energy charge revenues, the Commission's Order in Docket No. E-22, Sub 265, required the Company to prepare a study showing how much demand charge revenue is included in each block of the energy charges in Schedules 5 and 6. The Company filed the study with its application in the current rate case as requested by the Commission. Although the rate case load currently facing the Commission leaves insufficient time for fully evaluating the study in this proceeding, it does indicate that under the rate design proposed by the Company for Schedule 6 in this proceeding, the demand charge revenues will now recover almost all of the demand-related costs, and the energy charges will now contain relatively little demand-related costs. Therefore, the Commission concludes that the rate design proposed by the Company for Schedule 6 in this proceeding is appropriate and should be adopted.

Outdoor Lighting Schedules 26 and 27

The Company proposes to merge Schedule 27 into Schedule 26 in order to reflect that prices are identical on both schedules for most fixture sizes. In addition, the Company proposes to add a new category of fixtures ("Ultra Style") to Schedule 26.

The Company's proposed revisions to the outdoor lighting schedules were unopposed by any party, and the Commission concludes that they should be approved.

Maximum and Minimum Voltages

Public Staff witness Turner recommended that the provision in the Company's terms and conditions for service defining maximum and minimum voltages be revised from a maximum or minimum "five-minute mean or average" voltage to a maximum or minimum actual voltage. He cited the concern that such a definition could include short duration voltages so high that serious damage to the customers' equipment could result.

The Company cited NCUC Rule R8-17 which states that voltages in excess of those specified in the rules do not constitute a violation of the rule if they are caused by infrequent and unavoidable fluctuations of short duration due to various causes. The Company contended that the "five-minute mean or average" in its terms and conditions simply defines the short duration contained in NCUC Rule R8-17. The Company pointed out that the tariff provision has been in effect for at least 25 years, and that there is no evidence that it has been a source of problems to the customers or the Company, and that the issue would probably have not been raised if the Company had not proposed rearranging its terms and conditions for clarity.

The Commission notes that both Carolina Power & Light Company and Duke Power Company appear to define maximum or minimum voltages as maximum or minimum actual voltage, and there have been no adverse complaints regarding such definition. The Commission concludes that the Company's proposed definitions of maximum and minimum voltages should be revised as recommended by the Public Staff to delete reference to a five-minute mean or average.

General

In addition to those revisions already discussed herein, the Company proposes various miscellaneous rate changes, administrative changes, and clarifications on its rate schedules and in its terms and conditions for service which were unopposed by any party.

Proposed changes and clarifications to the rate schedules include in part: provisions to clarify calculation of bi-monthly billings; provisions to exclude residential customers from Schedule 5 (small general service); provisions to add a summer/winter rate differential to the first block of Schedule 5; and provisions to revise the demand charges in Schedules 7 and 42 consistent with Schedules 5 and 30.

Proposed changes and clarifications to the terms and conditions for service include in part: provisions to include definitions for cogeneration and small power production; provisions to clarify the applicability and/or administration of connection charges and extra facility charges; provisions to clarify customer responsibility for site preparation prior to installation of new connections; provisions to clarify location and administration of metering; provisions to clarify the characteristics and voltages of electric supply; provisions to clarify billing of customers for location or relocation of underground facilities; and provisions to clarify the options available for temporary service.

The Commission concludes that the rate designs, rate schedules, and terms and conditions for service as proposed by the Company should all be approved except as discussed herein.

IT IS, THEREFORE ORDERED, as follows:

1. That Virginia Electric and Power Company shall adjust its electric rates and charges so as to produce an increase in gross annual revenues from its North Carolina retail operations of $18,340,000, said increase to be effective for service rendered on and after the date of this Order.

2. That within five (5) days after the date of this Order, Virginia Electric and Power Company shall file with this Commission rate schedules designed to produce the increase in revenues set forth in Decretal Paragraph No. 1 above in accordance with the guidelines set forth in Appendix A attached hereto.

3. That the interim rates and charges which Virginia Electric and Power Company placed into effect pursuant to G.S. 62-135 on September 9, 1983, subject to an undertaking to refund, are found to be unjust and unreasonable and are hereby disapproved to the extent that such rates and charges were in excess of those approved herein. Vepco shall refund all amounts which may have been thus overcollected from its North Carolina retail ratepayers since

September 9, 1983, together with interest thereon at the rate of 10.0% per annum as specified in the Commission Order heretofore entered in this docket on August 12, 1983. Such refunds shall be made as promptly as possible by appropriate credits to customer bills. Vepco shall submit a plan for making such refunds and showing the calculation thereof within five (5) days after the date of this Order.

4. That the rate design, rate schedules, and service rules proposed by the Company, except for the modifications thereto as described herein, are hereby approved.

5. That Virginia Electric and Power Company shall prepare cost allocation studies for presentation with its next general rate application which allocate production plant based on the following methodologies: (1) Summer/Winter Peak and Average; (2) Summer/Winter Peak and Base; (3) Summer/Winter Coincident Peak; and (4) Average and Excess. Both jurisdictional and fully distributed cost allocation studies shall be made using each method, and the studies shall be included in Items 31 and 37, respectively, of Form E-1 of the minimum filing requirements for general rate applications.

6. That Virginia Electric and Power Company shall undertake the study outlined in its October 14, 1983, late filed exhibit and discussed herein to identify the energy-related portion of production plant and to analyze the time diffrentiated costs associated with production plant; and that the Company shall work with the Public Staff and other interested intervenors in an effort to resolve any differences as to the study procedures.

7. That Virginia Electric and Power Company shall give public notice of the rate increase approved herein by mailing a notice by first-class mail to each of its North Carolina retail customers during the next normal billing cycle following the filing of the rate schedules specified in Decretal Paragraph No. 2.

8. That any motions heretofore filed in this proceeding and not previously ruled upon are hereby denied.

ISSUED BY ORDER OF THE COMMISSION.
This the 5th day of December 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sandra J. Webster, Chief Clerk

APPENDIX A
Virginia Electric and Power Company
Docket No. E-22, Sub 273
Guidelines for Design of Rate Schedules

Step 1: Determine the amount of rate schedule revenues and other revenues, respectively, which are necessary to produce the overall revenue requirement established by the Commission in this proceeding.

Step 2: Reduce the revenue requirement proposed by the Company for each rate schedule by the same percentage to produce the total rate schedule revenues determined in Step 1.

Step 3: Reduce the individual prices in a given rate schedule by the same percentage to reflect the required reduction in revenue requirement for the rate schedule as determined in Step 2, except as follows:

a. Set basic customer charge for residential Schedule 1 at $6.85.

b. Hold miscellaneous service charges and RKVA charges at the same level proposed by the Company.

Step 4: Round off individual prices to the extent necessary for administrative efficiency, provided said rounded-off prices do not produce revenues which exceed the overall revenue requirement established by the Commission in this proceeding.

DOCKET NO. E-22, SUB 273

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Application by Virginia Electric and Power Company) ORDER AMENDING
for Authority to Adjust and Increase Its Electric) RATE DESIGN
Rates and Charges)

BY THE COMMISSION: On December 5, 1983, the Commission Order Granting Partial Increase in Rates was issued in the above-captioned matter specifying that rates should be designed in accordance with guidelines contained in Appendix A to said Order.

It has now been made to appear that rates designed in accordance with said guidelines would not produce the total revenues authorized by said Order, in that the basic customer charge of $6.85 for residential service authorized in the Order would reduce overall revenues to such an extent that other rates would need to be set higher than the levels proposed by the Company in order to achieve the overall revenues authorized in the Order.

On December 7, 1983, the Company filed a Petition to Amend Order Granting Partial Increase in Rates in the above-captioned matter requesting that rates be designed to produce the overall revenues authorized in said Order by establishing the basic customer charge for residential service at $7.17 such that no other change in the Company's proposed rates and charges would be necessary.

The Commission is of the opinion that the final rate design should result in no customer paying a greater rate than that proposed by the Company, and furthermore that every effort should be made in this proceeding to reduce the rates applicable to residential customers. Therefore, the Commission concludes that the entire reduction in the revenues proposed by the Company should be reflected in the basic customer charge for residential service, and that such reduction would result in a basic customer charge of $7.17 for Schedule 1 and no change in the other rates and charges proposed by the Company.

IT IS, THEREFORE, ORDERED as follows:

That Appendix A of the Commission Order of December 5, 1983, in the above-captioned matter is hereby amended to delete steps 1, 2, 3, and 4 of the guidelines for design of rate schedules contained in said Appendix A, and by substituting therefor the following:

"Set basic customer charge for residential Schedule 1 at $7.17."

ISSUED BY ORDER OF THE COMMISSION.
This the 8th day of December 1983.

NORTH CAROLINA UTILITIES COMMISSION
Sandra J. Webster, Chief Clerk

(SEAL)

DOCKET NO. SP-1, SUB 1

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of	
Application of Cox Lake-Carbonton Associates for Certificate of Public Convenience and Necessity Pursuant to G.S. 62-110.1 Authorizing Carbonton Hydro Project on the Deep River	) RECOMMENDED ORDER) GRANTING CERTIFICATE) OF PUBLIC CONVENIENCE) AND NECESSITY PURSUANT) TO G.S. 62-110.1

HEARD IN: Commission Hearing Room, Second Floor, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina, on May 17, 1983

BEFORE: Sammy R. Kirby, Hearing Examiner

APPEARANCES:

For the Applicant:

Edgar M. Roach, Jr., Hunton & Williams, P.O. Box 109, Raleigh, North Carolina 27602
For: Cox Lake-Carbonton Associates

For the Public Staff:

Gisele L. Rankin, Staff Attorney, Public Staff - North Carolina Utilities Commission, P.O. Box 991, Raleigh, North Carolina 27602
For: The Using and Consuming Public

KIRBY, HEARING EXAMINER: This proceeding was instituted on March 30, 1983, by the filing of an application by Cox Lake-Carbonton Associates (hereinafter Applicant) for a certificate of public convenience and necessity pursuant to G.S. 62-110.1 to renovate and construct a hydroelectric generating facility at Carbonton on the Deep River in Lee County.

By Order of the Commission dated April 12, 1983, the matter was set for public hearing on May 17, 1983, at 10:00 a.m., in the Commission Hearing Room in the Dobbs Building in Raleigh. By this same Order, Cox Lake-Carbonton Associates was ordered to: (a) publish a notice of this hearing once a week for four successive weeks in a daily newspaper of general circulation in Lee County; and (b) notify Steve McEvoy, Dam Safety Administrator, Land Quality Section, Division of Land Resources, Department of Natural Resources and Community Development, of the hearing. A certificate of service upon Steve McEvoy was filed with the Commission on April 15, 1983; and an affidavit of publication was filed on May 19, 1983.

On May 17, 1983, at 10:00 a.m., the public hearing was convened in the Commission Hearing Room. Making appearances were Edgar M. Roach, Jr., Attorney for the Applicant, and Gisele L. Rankin, Staff Attorney for the Public Staff. The Applicant offered the testimony and exhibits of Ruben S. Brown, Chairman of Carolina Hydro, Inc., the corporate general partner of Cox Lake-Carbonton Associates.

Based upon a careful examination of the entire record in this proceeding, the Hearing Examiner makes the following

FINDINGS OF FACT

1. The Applicant, Cox Lake-Carbonton Associates, is a limited partnership organized under the laws of New York State. The corporate general partner is Carolina Hydro, Inc., a North Carolina corporation.

2. The Applicant is a Small Power Producer as defined in G.S. 62-3(27a) and is within the purview of G.S. 62-156. The Applicant also comes within the definition of public utility in G.S. 62-3(23).

3. The Applicant seeks a certificate of convenience and necessity pursuant to G.S. 62-110.1 for a hydroelectric facility to be located at Carbonton on the Deep River in Lee County. This project will be known as the Carbonton Hydro Project. All electric power generated at the site will be sold to Carolina Power & Light Company, pursuant to a contract embodying 15-year power purchase rates.

4. The Carbonton Hydro Project will consist of: (a) an existing slab and buttress dam 211 feet long and 18 feet high; (b) an existing reservoir with a surface area of 116 acres; (c) installation in the existing powerhouse of two generator and turbine units with an installed capacity of one megawatt; (d) proposed transmission lines less than 200 yards long; and (e) appurtenant facilities. The average annual generation is expected to be 4.2 gigawatt hours. Flashboards may be added, thereby raising the head of the dam. The Carbonton site was licensed to John M. Jordan, and he has optioned his rights to Carolina Hydro, Inc. The Carbonton site is now owned by Carolina Power & Light Company.

5. The total estimated cost of the Carbonton Hydro Project is $917,000.

6. The Applicant estimates that the generating facility will be placed into operation between December 1, 1983, and April 1, 1984.

7. Public convenience and necessity require construction and installation by the Applicant of the hydroelectric facility which is the subject of this application, in that such facility will provide Applicant with a generating capacity dependent upon the naturally renewing flow of the Deep River, with no fuel costs to the Applicant, while reducing the reliance of this State upon power generated through the burning of fossil fuels.

8. The proposed facility will not affect the Commission's load forecast due to the small size increment established therein.

Whereupon, the Hearing Examiner reaches the following

CONCLUSIONS

1. The public convenience and necessity require construction of the Carbonton Hydro Project in that such facility will provide a generating capacity dependent upon the natural flow of the Deep River, with no fuel costs, while reducing the reliance of this State upon power generated by the burning of fossil fuels.

2. Although the Applicant is a public utility as defined in G.S. 62-3(23), it should, pending further order of the Commission, be regulated as hereinafter provided.

IT IS, THEREFORE, ORDERED as follows:

1. Cox Lake-Carbonton Associates is hereby authorized to renovate, construct, and operate the aforementioned Carbonton Hydro Project.

2. This Order shall itself constitute a Certificate of Public Convenience and Necessity for the construction and operation of said facility.

3. Cox Lake-Carbonton Associates shall file such information and reports as required by G.S. 62-110.1(f).

4. Cox Lake-Carbonton Associates shall file an annual report with the Commission setting forth the certificate docket number and date of last report, the owner's name and address, the type of facility, the location and site of the facility, the name of the interconnected utility, and the present rates and schedule number. In addition, each such annual report shall set forth for the period since the issuance of the certificate or since the last report information as to revenues, expenses, modifications to the facility, generation in kWh, sales, type of fuel consumed, and cost and quantity of fuel, plus general comments.

ISSUED BY ORDER OF THE COMMISSION.
This the 16th day of June 1983.

(SEAL)

NORTH CAROLINA UTILITIES COMMISSION
Sandra J. Webster, Chief Clerk

DOCKET NO. G-21, SUB 235
DOCKET NO. G-21, SUB 237

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Application of North Carolina Natural Gas Corporation) NOTICE OF DECISION
for an Adjustment of Its Rates and Charges) AND ORDER

HEARD IN: Auditorium, Willis Building, Greenville, North Carolina, on October 25, 1983; Council Room, City Hall, Fayetteville, North Carolina, on October 26, 1983; Commission Hearing Room, Dobbs Building, Raleigh, North Carolina, on October 27 and 28, 1983; and Room 213, Dobbs Building, Raleigh, North Carolina, on October 31, and November 1 and 2, 1983

BEFORE: Commissioner Edward B. Hipp, Presiding; and Commissioner Ruth E. Cook and Chairman Robert K. Koger

APPEARANCES:

For the Applicant:

Donald W. McCoy and Alfred E. Cleveland, McCoy, Weaver, Wiggins, Cleveland & Raper, Attorneys at Law, P.O. Box 2129, Fayetteville, North Carolina 28302
For: North Carolina Natural Gas Corporation

For the Public Staff:

Antoinette R. Wike and Vickie L. Moir, Staff Attorneys, Public Staff - North Carolina Utilities Commission, P.O. Box 991, Raleigh, North Carolina 27602
For: The Using and Consuming Public

For the Intervenors:

Ernie K. Murray, Spruill, Lane, Carlton, McCotter & Jolly, Attorneys at Law, P.O. Drawer 353, Rocky Mount, North Carolina 27801, and

David R. Straus and John M. Adragna, Spiegel and McDiarmid, Attorneys at Law, 2600 Virginia Avenue, N.W., Suite 312, Washington, D.C. 20037
For: The Cities of Wilson, Rocky Mount, Monroe, and Greenville, North Carolina

Henry S. Manning, Jr., Hunton and Williams, Attorneys at Law, P.O. Box 109, Raleigh, North Carolina
For: Aluminum Company of America

Jerry B. Fruitt, Attorney at Law, P.O. Box 2507, Raleigh, North Carolina 27602
For: North Carolina Textile Manufacturers Association, Inc.

BY THE COMMISSION: On April 27, 1983, North Carolina Natural Gas Corporation (NCNG, Applicant, or Company) filed an application with the Commission in Docket No. G-21, Sub 235, for authority to adjust its rates and charges for natural gas service in North Carolina..

By Order dated May 25, 1983, the Commission declared the matter to be a general rate case pursuant to G.S. 62-137, suspended the proposed rates for a period of 270 days from the effective date of May 27, 1983, set the matter for hearing, declared the test period to be the 12 months ended December 31, 1982, and required the Company to give notice to its customers of the proposed increase and the hearings.

On June 10, 1983, in Docket No. G-21, Sub 237, the Company filed an application for approval of revisions in its Transportation Rate Schedule No. T-1. By Order issued July 12, 1983, the Commission consolidated the matter with Docket No. G-21, Sub 235, for investigation and hearing, suspended the proposed rates for a period of 270 days from the effective date of June 15, 1983, and required that the Company give public notice to its municipal customers and those customers considered as being in NCUC Priorities 2.5-9.

On August 22, 1983, the Cities of Wilson, Rocky Mount, Monroe, and Greenville (Cities) filed a Petition to Intervene in Docket No. G-21, Sub 235. On September 2, 1983, a Petition to Intervene was filed in both dockets on behalf of the North Carolina Textile Manufacturers Association (NCTMA). The Petition of Aluminum Company of America for Leave to Intervene was filed on September 7, 1983. On September 9, 1983, a Motion for Limited Admission to Practice was filed by James N. Horwood, David R. Straus, and John Michael Adragna seeking to represent the Cities in Docket No. G-21, Sub 235. Federal Paper Board Company, Inc., filed in both dockets a Petition to Intervene in both dockets on September 15, 1983. By Orders of the Commission on various dates, all of these petitions and motions were allowed.

On October 6, 1983, the Commission issued an Order in Docket No. G-21, Sub 238 and Sub 235, stating that the Public Staff in its investigation had found that $132,389 of the exploration and development (E&D) refunds had been allocated to C.F. Industries, Inc. (CFI). As a part of the negotiated settlement of liability between CFI and NCNG, CFI had assigned all rights to these refunds to NCNG. The Public Staff's proposal has been that the refund plan be amended to require that the refunds allocated to CFI be distributed to NCNG's other customers. The Commission requested the parties to the Docket No. G-21, Sub 235 proceeding to offer testimony during said proceeding as to the proper rate-making treatment to be accorded the E&D refunds in question and any future E&D refunds to be paid to CFI and assigned to the Company. The Order further required that the $132,389 be placed in a deferred account pending consideration of the matter in Docket No. G-21, Sub 235.

Prior to and during the course of the hearings, motions were made and Orders were entered relating thereto, all of which are a matter of record. Additionally, pursuant to various Commission Orders or requests, also of record, various parties were directed or permitted to file and serve certain late filed exhibits, either during or subsequent to the hearings held in this matter.

The matter came on for hearing at the places and on the dates scheduled in the Order Setting Hearing. Mrs. Margaret Wirth, Chairman of the Greenville Utilities Commission, appeared at the Greenville hearing on October 25, 1983, and offered testimony on the City's behalf. The following public witnesses appeared at the hearing in Fayetteville, North Carolina, on October 26, 1983: Patricia Keller, Mark J. Bullock, John Mobley, Philip Harrington, and Glen Ross.

The case in chief was heard in Raleigh beginning on October 27, 1983. The applicant presented the testimony and exhibits of the following witnesses:

1. Frank Barragan, Jr., President and Director of NCNG (direct and rebuttal testimony);

2. Calvin B. Wells, Executive Vice President and Director of NCNG (direct and rebuttal testimony);

3. Gerald A. Teele, Vice President - Rates and Budget (direct and rebuttal testimony);

4. Raymond A. Ranson, consultant with Ransom Engineers, P.C. (direct testimony);

5. Jerome C. Weinert, Supervising Appraiser in the Regulated Industries Division, The American Appraisal Company (direct testimony);

6. James H. Vander Weide, Professor of Finance and Associate Dean at the Fuqua School of Business of Duke University; and

7. Eugene W. Meyer, Vice President and Director of Kidder, Peabody & Co., Inc. (direct testimony).

The cities of Wilson, Rocky Mount, Monroe, and Greenville presented the testimony and exhibits of the following witnesses:

1. Fred R. Saffer, Director of the Rate Department of R.W. Beck and Associates, Engineers and Consultants, Orlando, Florida, regional office;

2. Daniel J. Lawton, Supervising Economist, R.W. Beck and Associates; and

3. Robert J. Ori, Supervising Analyst, Rate Department, R.W. Beck and Associates.

Aluminum Company of America presented the testimony of Maynard F. Stickney, Chief Industrial Engineer of its Badin Works.

The Public Staff presented the testimony and exhibits of the following witnesses:

1. R. J. Nery, Director, Natural Gas Division;

2. John T. Garrison, Jr., Engineer, Natural Gas Division;

3. William W. Winters, Supervisor of the Electric Section, Accounting Division;

4. Hsin-Mei C. Hsu, Economist, Economic Research Division; and

5. Elise Cox, Supervisor of the Natural Gas Section, Accounting Division.

Based upon the foregoing, the evidence adduced at the hearing and the entire record in this proceeding, the Commission makes the following

FINDINGS OF FACT

1. North Carolina Natural Gas Corporation is a corporation organized under the laws of the State of Delaware and authorized to do business in the State of North Carolina and is a franchised public utility providing natural gas service to its customers in North Carolina. The Company is properly before the Commission in this proceeding, pursuant to Chapter 62 of the General Statutes of North Carolina, for a determination of the justness and reasonableness of its rates and charges.

2. The test period for purposes of this general rate case is the 12 months ended December 31, 1982, adjusted for actual changes based on circumstances and events occurring through the close of the hearing, including the inclusion of plant in service and other rate base items at June 30, 1983.

3. The Applicant originally requested an annual increase in operating revenues of $8,373,361. In the update filed on September 21, 1983, the Company sought to show that an increase of $8,577,027 was justified.

4. NCNG is providing adequate gas service to its customers in North Carolina.

5. The reasonable allowance for working capital for the Company is $5,504,533.

6. NCNG's reasonable original cost rate base used and useful in providing service to its customers is $53,273,671. This rate base consists of plant-in-service of $89,141,608 plus a working capital allowance of $5,504,533 less accumulated depreciation of $31,115,023, customer advances for construction of $6,264, accumulated deferred income taxes of $9,718,540 and cost-free capital of $532,643.

7. The refunds and cash payments received through the close of hearings by NCNG pursuant to the January 26, 1983 Settlement Agreement between C.F. Industries, Inc. (CFI) and NCNG in settlement of the obligations of CFI to NCNG under the Service Agreement of November 10, 1967, should be divided so that one-half of them goes to reduce the cost of service over a five-year period, the approximate remaining life of the Service Agreement, and one-half of them is retained by the Company as below-the-line income. The remaining $200,000 cash payment due NCNG pursuant to the settlement agreement and any future Transco refunds, curtailment compensation, curtailment tracking rate refunds, E & D refunds and any other future amounts otherwise due and payable to CFI should be placed in a deferred account pending future disposition by the Commission.

8. The appropriate level of revenues associated with completed construction not classified is $109,498. The appropriate level of purchased natural gas costs associated with completed construction not classified is $69,957.

9. NCNG's end-of-period operating revenues for the test period, after engineering and accounting adjustments, are $167,773,665.

10. The depreciation rates proposed by the Company are reasonable and proper with the exception of the rates proposed for Account 367 - Transmission Mains, Account 376 - Distribution Mains and Account 380 - Services. The appropriate annual depreciation rate for Account 367 - Transmission Mains is 2.74%, for Account 376 - Distribution Mains is 2.40%, and for Account 380 - Services is 3.71%.

11. NCNG's method of calculating per books current deferred income taxes does not reflect the appropriate level of utility income tax expense for reporting purposes.

12. The reasonable level of test year operating revenue deductions for NCNG after accounting, pro forma, and end-of-period adjustments is $161,341,143 which includes an amount of $2,593,159 for actual investment currently consumed through reasonable actual depreciation after annualization to year-end levels.

13. The capital structure for NCNG which is reasonable and proper for use in this proceeding is as follows:

Item	Ratio
Short-term debt	18%
Long-term debt	27%
Common equity	55%
Total	100%

14. The proper cost of short-term and long-term debt for use in this proceeding is 11.00% and 9.52%, respectively. The reasonable rate of return for NCNG to be allowed on its common equity is 15.5%. Using a weighted average for the cost of debt and common equity, with reference to the reasonable capital structure heretofore determined, yields an overall just and reasonable rate of return of 13.08% to be applied to the Company's original cost rate base. Such rate of return will enable NCNG, by sound management, to produce a fair return for its stockholders, to maintain its facilities and service in accordance with the reasonable requirements of its customers, and to compete in the market for capital funds on terms which are reasonable and fair to the customers and to existing investors.

15. Based upon the foregoing, NCNG should increase its annual level of gross revenues under present rates by $1,117,531. The annual revenue requirement approved here is $168,891,196, which will allow NCNG a reasonable opportunity to earn the rate of return on its rate base which the Commission has found just and reasonable. The revenue requirement approved herein is based upon the original cost of NCNG's property used and useful in providing service to its customers and its reasonable test year operating revenues and expenses as previously set forth in these findings of fact.

16. The margin on sales of compressed natural gas (CNG) should be placed into the deferred account for refunding to NCNG's customers and the rate charged for sales of CNG should be subject to prior Commission approval.

17. The curtailment tracking adjustment formula or rate (CTR) heretofore approved for use by NCNG, during a period of serious gas supply shortages is outmoded and therefore should be terminated.

18. An Industrial Sales Tracker (IST) is reasonable and should be included in the rates of NCNG. The IST is applicable to sales volumnes and margin for sales to existing customers served under Rate Schedules 4, 5, 6, and S-1 including the negotiated volumnes applicable to municipal sales normally made under Rate Schedule RE-1. New customers added after June 30, 1983, are specifically excluded from the IST.

19. The rate design proposed by the Public Staff for NCNG as modified herein is appropriate. The rate schedules and tariffs to be filed pursuant to this Order shall be just and reasonable.

Based upon the findings of fact set forth hereinabove, the Commission concludes that the appropriate annual level of revenues which NCNG should be authorized to collect through rates charged for its sales of service based upon the adjusted test year level of operations is $168,891,196. The following charts summarize the gross revenues and the rates of return which the Company should have a reasonable opportunity to achieve, based upon the level of revenues approved herein. Such charts, illustrating the Company's gross revenue requirements, incorporate the findings, adjustments, and conclusions herein made by the Commission.

SCHEDULE I
NORTH CAROLINA NATURAL GAS CORPORATION
STATEMENT OF OPERATING INCOME

Twelve Months Ended December 31, 1982

Item	Present Rates	Increase Approved	After Approved Increase
Operating Revenues:			
Natural gas sales	$167,095,707	$1,117,531	$168,213,238
Revenues - completed construction not classified	109,498	-	109,498
Miscellaneous revenues	568,460	-	568,460
Total operating revenues	$167,773,665	$1,117,531	$168,891,196
Operating Revenue Deductions:			
Cost of gas	$133,965,008	$ -	$133,965,008
Cost of gas - completed construction not classified	69,957	-	69,957
Operation and maintenance	9,643,735	-	9,643,735
Depreciation	2,593,159	-	2,593,159
Taxes other than income	11,143,744	67,052	11,210,796
Interest on customer deposits	66,325	-	66,325
Income taxes	3,859,215	517,256	4,376,471
Total operating revenue deductions	$161,341,143	$ 584,308	$161,925,451
Net operating income	$ 6,432,522	$ 533,223	$ 6,965,745

SCHEDULE II
NORTH CAROLINA NATURAL GAS CORPORATION
Docket No. G-21, Sub 235
STATEMENT OF RATE BASE AND RATE OF RETURN

Twelve Months Ended December 31, 1982

Item	Amount
Investment in Gas plant	
Gas utility plant in service	$89,141,608
Accumulated depreciation	31,115,023
Net plant in service	58,026,585
Allowance for working capital	5,504,533
Accumulated deferred income taxes	(9,718,540)
Customer advances for construction	(6,264)
Cost-free capital - Transco refund	(125,377)
Cost-free capital - Gain on CFI settlement	(407,266)
Original cost rate base	$53,273,671
Rate of Return	
Present rates	12.07%
Approved rates	13.08%

SCHEDULE III
NORTH CAROLINA NATURAL GAS CORPORATION
STATEMENT OF CAPITALIZATION AND RELATED COSTS

Twelve Months Ended December 31, 1982

Item	Ratio %	Original Cost Rate Base	Embedded Cost %	Net Operating Income
		Present Rates - Original Cost Rate Base		
Short-term debt	18.00	$ 9,589,261	11.00	$1,054,819
Long-term debt	27.00	14,383,891	9.52	1,369,346
Common equity	55.00	29,300,519	13.68	4,008,357
Total	100.00	$ 53,273,671	-	$6,432,522
		Approved Rates - Original Cost Rate Base		
Short-term debt	18.00	$ 9,589,261	11.00	$1,054,819
Long-term debt	27.00	14,383,891	9.52	1,369,346
Common equity	55.00	29,300,519	15.50	4,541,580
Total	100.00	$ 53,273,671	-	$6,965,745

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 18

The evidence for this finding is found in the testimony of Company witnesses Wells and Teele and Public Staff witness Garrison.

Both the evidence of the Company and the Public Staff reflect that the Company has lost substantial markets and customers because the price of gas for industrial use is in excess of the cost of competitive fuels in some cases. In addition, a substantial part of the Company's remaining large commercial and industrial sales are being made at negotiated rates which are lower than the Company's filed tariff rates which were last adjusted in NCNG's general rate proceeding in 1978. Most of these negotiated sales are to customers using heavy fuel oils. This situation has made it difficult to determine with reasonable accuracy the Company's sales volumes and revenues under both present and proposed rates.

Public Staff witness Garrison presented testimony regarding the propriety of establishing an Industrial Sales Tracker (IST) for NCNG. The purpose of the IST is to stabilize the Company's margins while maintaining as large a sales base as possible. Under the Public Staff's proposal, the Commission will establish a margin for industrial and large commercial sales with revenues above or below the established margin being tracked through adjustments to the rates of NCNG's other customers.

In supplemental direct testimony, Company witness Wells presented a proposal for an IST which is, in principle, similar to Public Staff witness Garrison's proposed IST. Witness Garrison's proposed IST would include all Rate S-1 customers plus any existing industrial and large commercial customers being served under Rate Schedules 4, 5, and 6.

Public Staff witness Garrison proposed to increase industrial and municipal sales volumes to a level that was 622,520 dt greater than the sales volumes proposed by the Company. Also, witness Garrison proposed to price end-of-period sales volumes under Rate Schedule S-1 (negotiated sales) at a rate of $.19 per dt higher than the rate used by the Company. At the hearings, Company witness Teele agreed to accept those Public Staff adjustments because the Transco November 1, 1983 PGA increase turned out to be only $.055 per dt rather than the $.291 per dt increase contained in Transco's original PGA filing dated September 30, 1983, and because Public Staff witness Garrison's adjustments are reasonable, particularly in light of the implementation of the IST which, as stated, helps to stabilize the Company's margin attributable to industrial sales in a general rate case.

With the implementation of the IST, therefore, the Company and the Public Staff are in agreement as to industrial sales volumes and general rate design with respect to industrial and municipal customers. The Commission concludes that the IST is reasonable and should be adopted as a tariff item by NCNG. The Commission further concludes that the terms of the IST should be similar to those presented by Public Staff witness Garrison, with the following modifications to Exhibit No. JTG-9(R), entitled "Industrial Sales Tracker":

1. In Paragraph 4, the section which reads, "Rate Schedule No. RE-1 shows a rate of $.49711/therm which will be used by the Company for sales which are not negotiated," should be revised to show the rate as $.49912/therm, because the Commission is making no change in the RE-1 base rate;

2. To add in Paragraph 4, Line 7, after "on RE-1 less" the words "the 6% gross receipts tax and the then current CD-2 commodity cost of gas" and to delete the words "the cost of gas (calculated by multiplying the quantity sold by the test period cost of gas of $0.3898/therm";

3. To add in Paragraph 7, Line 8, after the word "uniformly" the words "a surcharge"; and

4. In Paragraph 10, Public Staff witness Garrison presents a table of base period monthly margins which he labels as "Including Gross Receipts Tax." The Commission finds that these amounts are improper for purposes of the IST because what these amounts represent, in fact, are margins plus the additional gross receipts taxes in excess of the gross receipts tax applicable to the cost of gas witness Garrison used in designing his proposed rates to recover the Public Staff's proposed cost of service. As an illustration, witness Garrison calculates the Rate 4 Margin as follows:

Sales rate	$5.0614 per dt
Cost of gas rate	3.8980[1/]
Margin per witness Garrison	$1.1634 per dt

[1/] CD-2 Commodity Rate $3.664 ÷ .94 = $3.898 with gross receipts tax

The actual margin, after considering that gross receipts taxes are paid by the Company on revenues, not cost of gas, is as follows:

Sales rate	$5.0614 per dt
Gross receipts tax at 6%	.3037
Net revenue rate	4.7577
Cost of gas at CD-2 Commodity rate	3.6640
Actual margin	$1.0937 per dt
Excess margin in witness Garrison's IST amounts ($1.1634 - $1.0937)	$ .0697 per dt
Reconciled as follows:	
Actual gross receipts tax	$ .3037
Gross receipts tax applicable to cost of gas ($3.898 - $3.664)	.2340
Additional gross receipts tax	$ .0697

While witness Garrison's methodology is acceptable for purposes of designing rates in the manner he has chosen, it is not appropriate to use an inflated margin for purposes of the IST. The effect of what the Public Staff's proposed methodology is to treat part of the Company's gross receipts tax expense as if it were margin, which is not the case. To the extent that prices of negotiated sales increase in the future, witness Garrison's base period IST margin would cause NCNG subsequently to underrecover its margin if gross receipts taxes are not fully accounted for in the base period margin determination. This would occur because NCNG would have to pay the higher gross receipts tax to the State but witness Garrison's method would require that the increase in gross receipts also be paid to NCNG's customers as "margin" through the IST. The monthly base period margins are as follows:

Test Period Month/Year	Per Public Staff Witness Garrison	Per Commission
7/82	$ 1,135,794	$ 1,067,801
8/82	1,200,949	1,129,058
9/82	1,080,266	1,015,597
10/82	1,119,573	1,052,554
11/82	1,094,208	1,028,706
12/82	1,074,625	1,010,295
1/83	1,103,755	1,037,683
2/83	1,056,487	993,248
3/83	1,142,015	1,068,207
4/83	1,116,167	1,045,521
5/83	1,075,506	1,011,124
6/83	1,109,283	1,042,878
Total	$13,308,628	$12,502,672

With these modifications, the Commission accepts the IST proposed by witness Garrison.

Both the Public Staff and the Company propose to exclude from the IST any new customers added after June 30, 1983, in order to offer the Company the incentive to add new industrial loads which will benefit the Company and its

customers by expanding its sales base while permitting the Company to earn some return on new plant investments it will make to attach new customers to its system. The Cities proposed that the IST be inclusive of new customers added after June 30, 1983. The Commission concludes that it is fair and reasonable to exclude customers added after June 30, 1983, from the IST.

The Commission fully recognizes that the level of sales volumes and the negotiated sales loss provided for in the IST approved herein are based on a normalized level. However, a provision has been made for undercollections or overcollections to be trued-up on an annual basis. Further, the Commission believes and so concludes that the time value of money should be considered in the IST mechanism and thus finds that any such under or over collections should carry the overall rate of return found fair herein.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 19

The evidence for these findings is contained in the testimony and exhibits of Company witness Ransom and Teele, Public Staff witness Garrison, and Municipal Intervenor witness Saffer.

Facilities Charges

The Company and the Public Staff are in agreement regarding the appropriate facilities charge for rate schedules 3A and 3B. The Commission therefore finds facilities charges of $50.00 and $100.00 appropriate for rate schedules 3A and 3B, respectively. The Company and the Public Staff disagree however with regard to the appropriate facilities charges for rate schedules 1 and 2. The facilities charges proposed by the Company and the Public Staff for rate schedules 1 and 2 are listed below.

Rate Schedule	Company	Public Staff
1 - Residential		
Heat only	$ 7.00	$4.00
Other	$ 5.00	$3.00
2 - Commercial and small industrial	$10.00	$6.00

The Commission finds the facilities charges proposed by the Public Staff reasonable and proper. In the Commission's opinion the level of increase in gross revenues approved herein does not justify an increase in facilities charges of the magnitude proposed by the Company.

Rate Blocks

The Company and the Public Staff also are in disagreement with regard to the proper rate blocks for rate schedules 1 and 2. The Company's proposal provides for rate blocks which contain three steps while the Public Staff's proposal provides for rate blocks of two steps. The Commission finds the Public Staff's proposal in this regard reasonable. The Commission notes that the two-step rate blocks proposed by the Public Staff and approved herein are more representative of those approved by this Commission for other gas companies in the State in recent general rate proceedings than those proposed by the Company.

Rate Schedules 4, 5, 6, and E-1

The Company and the Public Staff are in agreement that the present base tariff rates for NCNG's customers in rate groups 4, 5, 6, and E-1 should remain unchanged. The Commission therefore finds that the rates proposed by the Company and agreed upon by the Public Staff for the aforementioned rate schedules are just and reasonable.

Transportation Rate

The Company proposed an increase in its transportation service rate in Docket No. G-21, Sub 237. The Commission consolidated the matter with the Company's general rate proceeding. The Company and the Public Staff agreed that the proposed rates are just and reasonable. However, the NCTMA opposes the increase in the T-1 rate. The Commission finds that the T-1 rate proposed by the Company is just and reasonable and therefore should be implemented by the Company.

Rate Schedule RE-1

The Company proposed that the RE-1 rate to municipals remain unchanged. Alternatively in accordance with the decrease in revenues proposed by the Public Staff, witness Garrison recommended a decrease in the RE-1 base rate. The Commission finds that the base tariff rate for rate schedule RE-1 should remain unchanged as proposed by the Company.

Municipal Intervenor witness Saffer proposed a rate design for the four municipal customers of NCNG in which NCNG's rates to the municipalities would be based on the NCUC priority system on which NCNG's own retail rates are based. While witness Saffer's proposal has some merit, the Commission finds that cities proposed rate design must be rejected at this time due to the administrative difficulties it could possibly create. The Commission notes that the Company sells gas to each of the municipalities at their city gates; from that point on, NCNG has no control over how and to whom the cities distribute their gas. In order to bill the municipalities under a rate based on end use, NCNG would be dependent on the cities to accurately meter and then report end use to NCNG. The possibilities exist that, without verifiable test period data which only the cities could provide NCNG and this Commission, serious problems for NCNG and the municipalities with respect to billings and revenues could result.

Turn-on and Reconnection Fees

The Company proposed that turn-on and reconnection fees be increased from $15.00 to $25.00 for residential customers and from $25.00 to $30.00 for commercial customers. The Public Staff agreed with the turn-on and reconnection fees proposed by the Company. The Public Staff proposed to adjust operating revenues under present rates to reflect the annual increase in revenues associated with the turn-on and reconnection fees proposed by the Company.

The Commission concludes that a turn-on and reconnection fee of $20 is appropriate for residential customers and concurs with the Company and the Public Staff that a fee of $30 for commercial customers is proper. The Commission has excluded the proposed annual increase in revenues relating to

turn-on and reconnection fees from operating revenues for purposes of establishing the end-of-period level of operating revenues under present rates in this proceeding.

The Commission concludes that such increase is properly considered in the rate design of the Company since it reflects revenues associated with proposed rates of the Company rather than present rates.

Other Rate Design Conclusions

The Commission concludes that it is appropriate for NCNG to file tariffs based upon the revenue requirements and rate design guidelines reflected herein and an adjusted sales volume of 329,130,750 therms.

Since no revenues from emergency sales (which are erratic) or transportation revenues have been reflected in cost of service in this proceeding, it is appropriate that any such revenues generated from present customers should be credited to the IST account for the benefit of all other customers. Based on the fact that NCNG's cost of service is being recovered only from sales volumes included in this proceeding and given the protection the IST affords the Company for possible loss of sales in the industrial market, the Commission concludes that such accounting treatment is fair and reasonable.

An Order setting forth the evidence and conclusions in support of this decision will be issued subsequently. The Commission will consider the time for filing exceptions and notice of appeal in this proceeding to run from the date of issuance of such Order.

IT IS, THEREFORE, ORDERED as follows:

1. That North Carolina Natural Gas Corporation is hereby required to adjust its rates and charges in a manner so as to produce an annual level of revenues no greater than $168,891,196 from its North Carolina retail customers based upon the Commission's adjusted test year level of operations. Said amount represents an increase of $1,117,531 from the level of revenues that would have resulted from rates currently in effect based upon the test year level of operations. Said increase shall be effective for service rendered on and after the date of this Order.

2. That the Curtailment Tracking Rate (CTR) mechanism be, and is hereby, terminated and eliminated from the Company's rates effective on the date of this Order.

3. That the Industrial Sales Tracker (IST) mechanism is approved as discussed herein and shall be effective for service rendered on and after the date of this Order.

4. That NCNG's Rate Schedule T-1 approved to reflect the margins, net of distribution costs, in Rate Schedules 4, 5, and 6 as approved in this docket for the blocks shown in the Company's filing in Docket G-21, Sub 237.

5. That North Carolina Natural Gas Corporation be, and hereby is, ordered to file appropriate tariffs in conformity with the guidelines set forth in Evidence and Conclusions for Finding of Fact No. 19 properly adjusted for the

current Transco rates and for the current cost of alternate fuel considered in the IST mechanism and in conformity with the provisions of this Order not later than two (2) days from the date of this Order. Upon the Company filing such tariffs the Commission will allow two (2) days for intervenor comment.

6. That the depreciation rates proposed by NCNG herein be, and hereby are, approved with the exception of those for Account 367 - Transmission Mains, Account 376 - Distribution Mains and Account 380 - Services. The approved rates for those accounts are 2.74%, 2.40% and 3.71%, respectively.

7. That NCNG be, and hereby is, ordered to notify its customers of the rates and of the Industrial Sales Tracker (IST) mechanism approved herein by appropriate bill insert in the next billing cycle following the effective date of the new tariffs.

8. That NCNG be, and hereby is, ordered to file a monthly report with the Commission's Chief Clerk showing the IST volumes sold and the margin earned compared to the base period IST monthly volumes and margin.

9. That the tariffs filed in response to Ordering Paragraph 5 above shall be approved upon further Order of the Commission.

10. That North Carolina Natural Gas Corporation be, and is hereby, authorized to retain for its general corporate purposes one-half of all refunds and cash payments received prior to the close of hearings in this proceeding from its settlement of all contractual matters with its former customer, CF Industries, Inc. (CFI). Furthermore, one-half the funds now being held by NCNG in deferred accounts under Commission Order in Docket No. G-21, Sub 238, and all of the funds now being held by NCNG in deferred accounts under Commission Order No. G-21, Sub 239, be, and are hereby, authorized to be transferred from such deferred accounts for the general corporate purposes of NCNG.

11. That any such future refunds and cash payments received by NCNG from the CFI settlement shall, upon receipt, be placed in a deferred account for future disposition by the Commission.

ISSUED BY ORDER OF THE COMMISSION.
This the 12th day of December 1983.

NORTH CAROLINA UTILITIES COMMISSION
Sandra J. Webster, Chief Clerk

(SEAL)

DOCKET NO. G-21, SUB 235
DOCKET NO. G-21, SUB 237

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Application of North Carolina Natural Gas Corporation) ORDER SETTING
for an Adjustment of Its Rates and Charges) RATES

BY THE COMMISSION: On December 12, 1983, in Docket No. G-21, Sub 235 and Docket No. G-21, Sub 237, the Commission issued its Notice of Decision and Order for North Carolina Natural Gas (NCNG, Company) wherein the Company was

allowed to increase its rates and charges to produce additional revenues of $1,117,531 annually.

The Company was called upon to file specific rate schedules designed to produce the increase in revenues approved by the Commission. Upon the filing of such rate schedules the Commission Order allowed two days for intervenor comment. On December 14, 1983, pursuant to the Commission Order of December 12, 1983, NCNG filed specific rate schedules designed to produce approximately $1,117,531 in additional operating revenues on an annual basis. No intervenor comments were filed in response to the rate schedule filings of NCNG.

The Commission having carefully reviewed and considered the rate schedules proposed by the Company concludes that such rate schedules are proper and consistent with the guidelines enumerated in Evidence and Conclusions for Finding of Fact No. 19 contained in the Commission Order of December 12, 1983.

IT IS, THEREFORE, ORDERED as follows:

1. That the rate schedules filed by NCNG on December 14, 1983, which will produce an increase in annual revenues from its North Carolina operations of approximately $1,117,531 be, and hereby are, approved to be charged and implemented by the Company.

2. That the increase in rates and charges as approved herein shall become effective on service rendered on and after December 12, 1983.

ISSUED BY ORDER OF THE COMMISSION.
This the 19th day of December 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sandra J. Webster, Chief Clerk

DOCKET NO. G-3, SUB 114

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Application of Pennsylvania and Southern Gas Company (North Carolina Gas Service Divison) for an Adjustment of Its Rates and Charges) RECOMMENDED ORDER GRANTING PARTIAL INCREASE IN RATES

HEARD IN: Wrenn Room, Rockingham Public Library System, Reidsville, North Carolina, at 11:00 a.m., on May 17,1983

BEFORE: Hearing Examiner Jim Panton

APPEARANCES:

For the Applicant:

James T. Williams, Jr., and G. Garner Pullaman, Jr., Brooks, Pierce, McLendon, Humphrey and Leonard, P.O. Box Drawer U, Greensboro, North Carolina
For: Pennsylvania and Southern Gas Company

For the Public Staff:

Antoinette R. Wike, Staff Attorney, Public Staff - North Carolina Utilities Commission, P.O. Box 991, Raleigh, North Carolina 27602
For: The Using and Consuming Public

BY THE HEARING EXAMINER: This matter is before the Commission on the application of Pennsylvania and Southern Gas Company (North Carolina Gas Service Division, hereafter noted as Applicant or Company), filed on February 1, 1983, for authority to increase its rates and charges for gas utility service in its service area in North Carolina. The increase sought in the Company's original application was $534,000.

By Order of March 1, 1983, the Commission set the Company's application for investigation and hearing in this docket, suspended the proposed rates, and required the Company to give notice of this application to the public.

The Public Staff - North Carolina Utilities Commission filed Notice of Intervention on March 17, 1983.

On April 22, 1983, the Company filed Amendment to Petition wherein the proposed increase was reduced to $412,300.

On April 26, 1983, the Public Staff filed Response to Amendment and stated therein that the Public Staff did not intend to file testimony and exhibits on this matter since the Company had made certain adjustments in its amendment that were recommended by the Public Staff after its investigation of the Company's rate case filing and supporting books and records. The public hearing came on as sheduled in the Commission Order of March 1, 1983.

At the hearing, the Applicant entered into evidence the testimony and exhibits of Bernard L. Smith, Assistant Secretary and Controller of the Company, and James W. Carl, Applicant's Coordinator of Regulatory Matter. No public witness testified at the hearing.

After due consideration of the testimony offered during the hearing and a review of the entire record in this proceeding, the Hearing Examiner now makes the following

FINDINGS OF FACT

1. Pennsylvania and Southern Gas Company (North Carolina Gas Service Division), is duly franchised to provide gas utility service to its service area in North Carolina and is properly before the North Carolina Utilities Commission seeking an increase in its rates and charges for gas utility service.

2. The total increase in rates and charges under the Applicant's amended application will produce $412,300 in additional annual gross revenues.

3. The test period used in this proceeding and established by Commission Order is the 12-month period ended September 30, 1982.

4. The Applicant's reasonable original cost rate base is $4,751,813, consisting of net utility plant in service of $3,824,946, working capital of $1,361,541, and deferred income taxes of $434,674.

5. The Applicant's end-of-period operating revenues under present rates is $12,474,160 and under proposed rates is $12,866,460.

6. The Applicant's end-of-period operating revenue deductions under present rates is $12,124,164, and under proposed rates is $12,340,481. The operating revenue deductions include $160,971 for annual depreciation expense.

7. The Company should be allowed a rate of return on original cost rate base of 11.49%.

8. Based on the foregoing, Applicant should be allowed an increase in annual gross revenues not to exceed $412,300.

9. The rate structure presented by the Applicant in its amended application will produce the $412,300 additional gross revenues approved herein, and therefore should be approved.

10. The Applicant's quality of service is adequate.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 1 - 10

The evidence supporting these findings of fact is found in the verified application, the verified amended application, and in the record as a whole. This evidence is uncontroverted in the record.

IT IS, THEREFORE, ORDERED as follows:

1. That Pennsylvania and Southern Gas Company (North Carolina Gas Service Division) be, and hereby is, authorized to increase its rates and charges in order to produce $412,300 additional annual gross revenues, effective upon the date this Order becomes final.

2. That Pennsylvania and Southern Gas Company (North Carolina Gas Service Division) be, and hereby is, required to file tariff sheets reflecting the rates approved herein, in order to achieve the increase approved in Ordering Paragraph No. 1.

ISSUED BY ORDER OF THE COMMISSION.
This the 18th day of May 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sandra J. Webster, Chief Clerk

DOCKET NO. G-3, SUB 114

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Application of Pennsylvania and Southern Gas Company (North Carolina Gas Service Division) for an Adjustment of Its Rates and Charges) FINAL ORDER) ADOPTING) RECOMMENDED ORDER

BY THE COMMISSION: Pursuant to the parties of record stipulation that the Recommended Order issued by the Hearing Examiner would not be contested, provided said Recommended Order reflected the agreed upon facts of records, and pursuant to Commission's conclusion that said Recommended Order reflects the facts of record, the Commission further concludes that the Recommended Order should be adopted as the Final Order and that the increase granted therein should be effective upon the date of this Order.

IT IS, THEREFORE, ORDERED as follows:

That the Recommended Order issued in the docket be, and hereby is, ordered to be effective upon the date of this Order.

ISSUED BY ORDER OF THE COMMISSION.
This the 18th day of May 1983.

NORTH CAROLINA UTILITIES COMMISSION
Sandra J. Webster, Chief Clerk

(SEAL)

DOCKET NO. G-5, SUB 181

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Application of Public Service Company of North Carolina, Inc., for an Adjustment of Its Rates and Charges) ORDER GRANTING PARTIAL RATE INCREASE

HEARD IN: Buncombe County Courthouse, Asheville, North Carolina, on June 7, 1983; City Council Chambers, City Hall, Gastonia, North Carolina, on June 8, 1983; Commission Hearing Room, Dobbs Building, Raleigh, North Carolina, on June 9, 10, and 14, 1983

BEFORE: Commissioners A. Hartwell Campbell, Presiding; and Commissioners Edward B. Hipp and Douglas P. Leary

APPEARANCES:

For the Applicant:

J. Mack Holland, Mullen, Holland & Cooper, P.A., 316 S. Marietta Street, P.O. Box 488, Gastonia, North Carolina 28052

F. Kent Burns, James M. Day, Boyce, Mitchell, Burns & Smith, P.A., P.O. Box 2479, Raleigh, North Carolina 27602

For the Intervenor:

Thomas R. Eller, Jr., P.O. Box 27866, Raleigh, North Carolina 27611
For: North Carolina Textile Manufacturers Association, Inc.

For the Public Staff:

Vickie Moir and Gisele Rankin, Staff Attorneys, Public Staff - North Carolina Utilities Commission, P.O. Box 991, Raleigh, North Carolina 27602
For: The Using and Consuming Public

BY THE COMMISSION: On January 19, 1983, Public Service Company of North Carolina, Inc. (Public Service, Applicant, or the Company), filed an application with this Commission seeking authority to adjust its rates and charges for retail natural gas service in North Carolina.

On February 15, 1983, the Commission issued an Order suspending the proposed rates for a period of 270 days from the proposed effective date of February 18, 1983, setting hearings, and requiring that public notice be given.

On March 11, 1983, a Petition to Intervene and Protest was filed with the Commission by the North Carolina Textile Manufacturers Association, Inc. (NCTMA). This Petition was allowed by Order dated March 17, 1983.

The matter came on for hearing as scheduled.

No public witnesses appeared at the hearings in Asheville, Gastonia, or Raleigh.

The Company presented the testimony and exhibits of the following witnesses in support of its application:

Charles E. Zeigler, President and Chief Executive Officer of the Company, who testified about the Company's service area, organization, customers, its shareholders, and its need for rate relief.

C. Marshall Dickey, Vice President-Gas Supply Services of the Company, who testified about the Company's gas supply, market requirements, competition, fully allocated cost of service, rate design, and the weather adjustment.

Allen J. Schock, Vice President-Rates of the Company, who testified about the Company's accounting exhibits.

E. L. Flanagan, Jr., Senior Vice President-Finance and Treasurer of the Company, who testified about the Company's financing, the financial condition of the Company, future financing needs, and the Company's need for rate relief.

Robert S. Jackson, Senior Vice President of Stone & Webster Management Consultants, Inc., who testified as to the proper capital structure, cost of capital, and required rate of return for Public Service.

The Public Staff offered the testimony and exhibits of the following witnesses:

Eugene H. Curtis, Jr., Public Utilities Engineer, Public Staff, who testified as to sales volumes, growth factor, cost of gas purchased, rate design, and the Industrial Sales Tracker.

Elise Cox, Staff Accountant of the Public Staff, who testified as to the accounting exhibits of the Public Staff.

Hsin-Mei C. Hsu, Economist with the Economic Research Division of the Public Staff, who testified as to the cost of capital and recommended rate of return for Public Service.

Based upon a careful consideration of the entire record in this proceeding, the Commission makes the following

FINDINGS OF FACT

1. Public Service is a corporation organized and existing under the laws of the State of North Carolina and is a franchised public utility providing natural gas service in 80 cities, towns, and communities in North Carolina. It is properly before the Commission in this proceeding for a determination of the justness and reasonableness of its proposed rates and charges under Chapter 62 of the General Statutes of North Carolina.

2. The test period established by the Commission and utilized by all parties is the 12 months ended September 30, 1982, adjusted for certain changes to March 31, 1983.

3. The additional gross revenues sought by Public Service under the rates and volumes originally proposed herein by the Company was $7,126,265.

4. Public Service is providing adequate natural gas service to its existing customers.

5. The original cost of Public Service's plant in service used and useful in providing natural gas service in North Carolina is $185,780,497. From this amount should be deducted accumulated depreciation of $56,426,323, resulting in a reasonable original cost, less depreciation or a net gas plant in service of $129,354,174.

6. The appropriate amount of accumulated deferred income taxes is $15,064,708.

7. The reasonable allowance for working capital for use in this case for Public Service is $13,392,666.

8. The reasonable original cost less depreciation of the natural gas plant in service of Public Service of $129,354,174, less the appropriate amount of accumulated deferred income taxes of $15,064,708, plus the reasonable allowance for working capital of $13,392,666 minus cost-free capital of $258,000 yields an original cost of the property of Public Service used and useful in providing service to the public in this State of $127,424,132.

9. Public Service's operating revenues after appropriate accounting and pro forma adjustments under present rates are $247,298,168 and under the Company's proposed rates as revised at the hearing would have been $252,005,744.

10. The test period level of Public Service's operating revenue deductions under present rates after accounting and pro forma adjustments is $232,942,376

which includes the amount of $5,402,750 for actual investment currently consumed through reasonable actual depreciation.

11. The appropriate level of the net income adjustment associated with the purchase of the Hendersonville property is $334,490.

12. The capital structure which is proper for use in this proceeding is the following:

Item	Percent
Long-term debt	49.75%
Preferred stock	7.28%
Common equity	42.97%
Total	100.00%

13. The Company's embedded cost of debt and preferred stock are 10.35% and 7.15%, respectively. The rate of return which should be applied to Public Service's original cost rate base is 12.24%. This return is reasonable and will allow the Company the opportunity to earn a return on its common equity of 15.30% after recovery of the embedded cost of debt and preferred stock. This return on common equity is just and reasonable.

14. Public Service's pro forma return on its rate base at the end of the test year was 11.53% which is less than the Commission has determined to be just and reasonable. Therefore, in order to have the opportunity to earn the returns which the Commission has determined to be just and reasonable, Public Service should be allowed to increase its rates and charges so as to produce an additional $1,916,396 of annual gross revenues based on its operations during the test year.

15. An Industrial Sales Tracker (IST) is reasonable and should be included in the rates of Public Service.

16. The rates set forth in Appendix A attached hereto and approved herein will generate the appropriate level of revenue and afford the Company an opportunity to achieve the overall return of 12.24% approved herein, but that said rates should be adjusted for any changes in Public Service's base rates since December 1982 and to reflect the current price of the alternate fuel considered in the IST.

17. Emergency gas sales revenues of $22,398 during the test period, which reflect the amount in excess of the revenues generated if the emergency volumes had been sold at the filed tariff rate schedule, should be placed in a deferred account for future disposition by the Commission.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 1 THROUGH 4

The evidence for these findings of fact is contained in the verified application, the Commission Order Setting Hearing and Investigation, and the testimony of Company witnesses Zeigler and Schock and Public Staff witness Cox. The evidence was uncontradicted and uncontested. These findings are essentially informational, procedural, and jurisdictional in nature.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 5 THROUGH 8

The evidence for these findings of fact is found in the testimony and exhibits of Company witness Schock and Public Staff witness Cox. The following table sets forth the net original cost rate base as proposed by these witnesses; and reflected in the parties proposed orders:

Item	Company	Public Staff	Difference
Plant in service	$185,780,497	$185,375,637	($404,860)
Accumulated depreciation	56,426,323	56,426,323	-
Net plant in service	$129,354,174	$128,949,314	($404,860)
Allowance for working capital	13,392,666	13,392,666	-
Deferred income taxes	(15,064,708)	(15,064,708)	-
Cost-free capital	-	(258,000)	(258,000)
Original cost rate base	$127,682,132	$127,019,272	($662,860)

The Company and the Public Staff agree that the proper amount for accumulated depreciation is $56,426,323, that the proper allowance for working capital is $13,392,666, and that the proper amount of deferred income taxes is $15,064,708. There being no evidence to the contrary, the Commission concludes that these amounts are reasonable and proper.

The difference between the Company and the Public Staff over the amount of plant in service of $404,860 is brought about by the inclusion by the Company in the rate base of the unamortized portion of the acquisition adjustment of the property acquired by the Company from United Cities Gas Company at Hendersonville. The Public Staff excluded this amount on the grounds that the customers would pay higher rates because Public Service increased its service area through the purchase. The Company responded that the average cost of acquiring the Hendersonville customers, both industrial and residential, including all the backbone plant and the acquisition adjustment was $1,203 per customer, whereas it cost the Company $1,440 to add a new residential customer just by extending the main 100 feet, installing the service, and setting the meter. By adding these customers, Public Service increased its customer base over which to spread its fixed costs. Public Service also pointed out that other benefits flowed to all customers including lower rates at Hendersonville, more reliable service to customers, and making the Company's Asheville division a more efficient operation.

While it clearly is the policy of the Commission to look at acquisition adjustments on a case-by-case basis, the evidence here shows benefits from the acquisition accruing to the existing customers of Public Service, the customers in the Hendersonville area, as well as to the Company. Under these circumstances, the Commission believes that it is reasonable to allow the treatment of the acquisition in the way sought by the Company. The Commission therefore approves the inclusion of the unamortized amount of $404,860 in the rate base.

The remaining difference between the parties as to rate base arises from the exclusion of $258,000 as cost-free capital by the Public Staff.

Public Staff witness Elise Cox offered testimony regarding the treatment of Transco refunds. The Company has accorded no specific treatment of the refunds, thus allowing the refunds to receive the overall rate of return. Witness Cox argued that the refunds, net of taxes, should be deducted from rate base as cost-free capital, thereby allowing no return on the refunds.

She further stated that the refunds should be treated as cost-free capital since Public Service's ratepayers paid in rates to cover the excessive producer-supplier costs related to the Transco refunds considered herein this matter.

There is no dispute as to the following facts: Transco received these monies from producer-suppliers as a result of orders of the Federal Energy Regulatory Commission. Transco, in turn, flowed the refunds through to its customers, including the North Carolina natural gas distribution companies. At the time the companies received the refunds, the Public Staff contended that the refunds should be flowed through to their North Carolina retail customers. The companies claimed that refunds were not required and that they should be permitted to retain these monies. Docket No. G-100, Sub 37, was established to determine the proper disposition of these Transco refunds. As a result of proceedings in that docket, the Commission ordered Public Service and several of the other companies to refund these monies to their customers.

Public Service and one other company appealed this decision to the North Carolina Court of Appeals. The Court of Appeals reversed the Commission's decision on the grounds that G.S. 62-136(c) required that it must be practicable to make the refunds to the customers who paid the charges and such a refund would be impracticable in this case. This reversal was upheld by the North Carolina Supreme Court. State ex rel. Utilities Commission v. Public Service Co., 56 N.C. App. 448, 289 S.E.2d 82, (1982) aff'd, 307 N.C. 474, __S.E.2d__ (1983). As a result of this affirmance, Public Service will permanently retain this capital.

The Company tried to show, through cross-examination of witness Cox, that the Public Staff's treatment is erroneous because the Supreme Court reversed the Commission's decision in its entirety. However, a judgment of reversal is not necessarily an adjudication by the appellate court of any question other than those which were in terms discussed and decided. Chas. Wolff Packing Co. v. Court of Industrial Relations of Kansas, 267 U.S. 552, 69 L.Ed. 785, 45 S. Ct. 441 (1925); 5 AM JUR 2d, Appeal and Error Sec. 955. Further, a decision of the North Carolina Supreme Court is authority only as to matters therein decided. In re West, 212 N.C. 189, 193 S.E. 134 (1937). Review of the Supreme Court's opinion in State ex rel. Utilities Commission v. Public Service, supra, shows that the Court reversed as a matter of law on the limited grounds discussed above and did not discuss the remaining assignments of error since its first holding required reversal. By its action, the Supreme Court in effect held that the companies did not have to refund the dollars in question. It did not address the appropriate rate-making treatment to be accorded these dollars. That issue was not before the Court and the Company's argument that the Court intended its holding to be determinative of this issue is unpersuasive. The Commission, therefore, finds and concludes that since the customers paid in rates to cover the excessive supplier costs which were refunded by Transco and since these dollars cannot be refunded because the Supreme Court held as a matter of law that the practicability requirement contained in G.S. 62-136(c), prior to amendment, had not been met, it is proper to reduce the rate base by that portion of capital supplied by the ratepayers which has no cost to the Company.

Based upon the foregoing, the Commission finds and concludes that the appropriate level of net original cost rate base for use in this proceeding is $127,424,132.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 9

The evidence supporting this finding of fact is found in the evidence and exhibits of Company witnesses Dickey and Schock and Public Staff witnesses Curtis and Cox.

After the Company's acceptance at the hearing of certain Public Staff adjustments, the parties are in agreement that the appropriate end-of-period level of operating revenues under present rates is $247,298,168, calculated as follows:

Natural gas sales	$246,785,703
Miscellaneous revenues	512,465
Total operating revenues	$247,298,168

Since there is no disagreement as to the level of end-of-period present operating revenues, the Commission adopts this amount of $247,298,168 for determining fair and reasonable rates in this proceeding.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 10 AND 11

The following table sets forth the differences between the Company and the Public Staff with respect to operating revenue deductions:

Item	Company	Public Staff	Difference
Purchased gas	$184,065,291	$184,065,291	$ -
Operation and maintenance	19,216,986	18,925,684	(291,302)
Depreciation and amortization	5,402,750	5,357,765	(44,985)
General taxes	17,227,909	17,227,909	-
State income taxes	908,168	897,194	(10,974)
Federal income taxes	6,524,616	6,445,528	(79,088)
Amortization of ITC	(315,293)	(315,293)	-
Total operating expenses	$233,030,427	$232,604,078	($426,349)

The Public Staff and the Company agreed to the proper level of purchased gas expense, general taxes, and amortization of ITC. Since there is no evidence of record to the contrary, the Commission concludes that these levels are appropriate for determining fair and reasonable rates herein. The purchase gas level is based on purchase of 43,808,530 dekatherms. This level of gas supply is necessary to generate the end-of-period sales volume upon which the Commission's end-of-period level of natural gas sales revenues is based, and included elsewhere herein. The Commission further notes that all parties of record recognized the reasonableness of this supply level, to be included herein this proceeding, and therefore the Commission concludes that the Applicant's appropriate level of natural gas supply is 43,808,530 dekatherms.

The difference in operations and maintenance expense of $291,302 is made up of two Public Staff adjustments. The first adjustment is in the amount of $139,696 and relates to advertising expense.

This adjustment of $139,696 is comprised of two items, as shown in the chart below:

	Item	Amount
1.	Gas Appliance Manufacturers Association Costs in Account 909	$ 16,809
2.	Advertising expenses including Gas Appliance Manufacturers Association Costs in Account 913	122,887
	Total	$139,696

Public Staff witness Cox testified that the Public Staff had examined advertising copy, vouchers, and invoices associated with the Company's entries in Account 909 and 913. Witness Cox further testified that $33,614 of costs associated with the Gas Appliance Manufacturers Association (GAMA) were removed from Accounts 909 and 913 in the Company's cost of service presented in this proceeding, because these costs were related to promotion of gas appliance sales.

The Company responded that it has adequate gas supplies to increase sales and it is no longer the policy to deny service to new customers as it was when the advertising restrictions were adopted. Additional sales mean that fixed costs will be spread over a greater volume to the benefit of all of the Company's customers. The Company also said that it has a responsibility to let the public know that gas is still a bargain, and generally the least expensive source of energy for domestic use. Finally, the Company witnesses stated that the advertising informs the public that more efficient gas appliances not only aid in conservation but that these more efficient appliances can save the customer a substantial amount of money in annual operating costs.

The record here disclosed that Public Service has an allocation or supply from Transco of some 57 million dekatherms and it is presently selling only about 42 million dekatherms. It is axiomatic if more units are sold, there are more units available over which to spread fixed costs.

Based on the foregoing, and the entire record in this matter, the Commission concludes that the expenses associated with GAMA should be removed from the Company's cost of service for the reason that the Company has failed to prove that these advertising expenditures directly benefit the using and consuming public in North Carolina. However, based in part on the current supply of natural gas available to the Company for resale to its North Carolina customers, and in part on the undisputed efficiency of natural gas as a domestic source of energy, as presented in this record, the Commission concludes that inclusion of a <u>representative</u> end-of-period level of advertising expenses in the Company's cost of service for use in setting fair and reasonable rates is justified in this proceeding and requires the Commission to disallow the remainder of the Public Staff adjustment to advertising expenses. Accordingly, the Commission is including the Company's advertising expenditures minus GAMA costs as a <u>representative</u> level of advertising expense for inclusion in the Applicant's cost of service in this proceeding. This <u>representative</u> level is the appropriate level necessary for the Applicant to effectively present to the public the fact that it offers an efficient energy source that is available for sale.

In making this determination, the Commission has carefully considered the entire record in this matter and Commission Rule R12-13 relating to advertising by natural gas utilities. Based on the undisputed evidence of record that the Applicant's natural gas service is both energy efficient and adequately available to meet potential growth in demand, the Commission

concludes that the representative level of advertising expenditures found to be reasonable hereinabove satisfies the conditions of Rule R12-13(d), that reads as follows:

> (d) Expenditures made by an electric or natural gas utility for advertising of a type or nature other than that described in subsections (b), (c), or (d) of Rule R12-12 or for other nonutility advertising shall be considered by the Commission to represent reasonable operating expenses to the extent that it can be established on a case-by-case basis, that -
>
> (1) the advertising is of benefit to the using and consuming public, or
>
> (2) the advertising enhances the ability of the public utility to provide efficient and reliable service.

The Commission wishes to emphasize the fact that the decision herein concerning the appropriate level of advertising expenditures is based on the evidence of record in the proceeding, and that this decision is not, and it should in no way be construed as, a departure from the fundamental principles of Commission Rule R12-13. Simply put, the facts in <u>this case</u> have been considered and the appropriate decision has been derived <u>solely</u> on the basis thereof.

Further, the Commission would be remiss if it did not emphasize to Public Service that any advertising whose related costs are <u>included</u> by the Company in its cost of service should <u>not</u> include the following statement:

> THIS MESSAGE IS NOT PAID FOR BY THE CUSTOMERS OF (the natural gas utility sponsoring the advertisement).

The remaining difference in operations and maintenance expense is $151,606 and relates to the amount of increased insurance premiums the Company estimates it would have to pay for hospitalization and life insurance for its employees, effective August 1983.

Public Staff witness Cox stated that she had included the March 1983 insurance rates in her calculation of the reasonable level of end-of-period hospitalization and life insurance expense. Witness Cox testified that the increase proposed by the Company was an estimate and not an actual known change at the close of the hearing.

The Commission has considered this adjustment carefully. Unlike an adjustment for increased wages, where the amount of increase is known, and is simply the products of a mathematical calculation using known numbers, the Company has presented no evidence to show what the <u>actual</u> dollar amount of the expected insurance increase will be. Therefore, the Commission concludes that the Public Staff adjustment is fair and reasonable and should be adopted in determining fair and reasonable rates in this proceeding.

After a review of the record, the Commission concludes that the level of uncollectible expense supported by both parties and presented in their proposed Orders should be adjusted to reflect the inclusion of the test period emergency gas sales revenues in the appropriate deferred account, as spoken

elsewhere herein. This results in an adjustment to the parties' uncollectible expense of $69.

Therefore, the Commission concludes that the reasonable level of operations and maintenance expense for use in this proceeding is $19,031,697.

The next difference between the parties' respective levels of operating revenue deductions of $44,985 is related to depreciation and amortization expense. This difference is caused by the elimination by the Public Staff of the Company's amortization of the acquisition adjustment relating to the purchase of the Hendersonville property.

The Company included in its cost of service annual amortization of $44,985 based on a 10-year amortization period of the purchase of the Hendersonville property. Consistent with the Commission's decision under Evidence and Conclusions for Findings of Fact Nos. 5 - 8, the Commission concludes that the inclusion of the acquisition adjustment amortization in the Applicant's cost of service is reasonable to be used in setting appropriate rates in this proceeding.

Consistent with the Commission's decision concerning the appropriate level of uncollectible expense to be included in the Applicant's cost of service, the Commission concludes that the emergency gas sales should not be included in the gross receipts tax calculation. Therefore, the Commission concludes that the Applicant's fair and reasonable end-of-period level of general taxes is $17,226,569.

In regard to state and federal income taxes, the position of the parties differs in two respects: First, the Public Staff imputed interest expenses related to the Job Development Investment Tax Credit (JDITC) in determining the Company's income tax expense; and second, the Public Staff in its revised exhibits included short-term debt in its proposed capital structure for use in this proceeding.

The Public Staff proposal to impute interest expense related to JDITC in computing income taxes has been presented to the Commission in many prior cases, including the Company's last general rate case in Docket No. G-5, Sub 168. In each case, the Commission has rejected the Public Staff's position. Recently, the North Carolina Court of Appeals in State ex rel. Utilities Commission v. Carolina Telephone and Telegraph Company, 61 N.C., App. 42, ___ S.E.2d ___ (1983), affirmed the position the Commission has taken of excluding this imputed interest in determining income tax expense. The Court of Appeals said:

> "Based upon the express language of Section 46(f)(2) and the regulations thereunder, as well as a consideration of the history and purpose of JDITC, that being primarily to benefit the utility so as to stimulate investment and thereby increase employment and additionally to share a ratable portion of the credit with rate payers, we affirm the decision of the Commission to exclude all imputed interest in determining CT&T's income tax expense for rate-making purposes."

Based on the foregoing, the entire record, and consistent with prior Commission decisions, the Commission concludes that the Company's treatment of the JDITC issue is appropriate for determining rates in this proceeding.

The final area of disagreement in regard to income taxes is the use of interest on short-term debt in the Public Staff's proposed capital structure as an expense in determining the appropriate level of income taxes.

Consistent with Evidence and Conclusions for Findings of Fact Nos. 12 - 13, the Commission concludes that interest associated with short-term debt should not be considered in determining the Applicant's reasonable level income tax expense to be used in setting rates in this proceeding. Therefore, and after considering all other components of the Applicant's cost of service, presented elsewhere herein, the Commission concludes that the reasonable level of state income taxes for use in this proceeding is $920,180 and the reasonable level of federal income taxes is $6,611,182.

In summary, the Commission concludes that the appropriate level of operating revenue deductions under present rates is $232,942,376 which is calculated as follows:

Purchased gas	$184,065,291
Operations and maintenance	19,031,697
Depreciation amd amortization	5,402,750
General taxes	17,226,569
State income taxes	920,180
Federal income taxes	6,611,182
Amortization of ITC	(315,293)
Total	$232,942,376

Both the Company and Public Staff used the same net income growth factor of 2.33% to properly reflect the effects of the purchase of the Hendersonville property. Therefore, the Commission concludes that this factor is appropriate and that when this factor is applied to the net income found reasonable herein results in a proper net income adjustment related to the purchase of the Hendersonville property of $334,490.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 12 AND 13

Two witnesses testified for the Company regarding the cost of capital, capital structure, and the need for rate relief. They were Robert S. Jackson, Senior Vice President of Stone & Webster Management Consultants, Inc., and E. L. Flanagan, Jr., Senior Vice President-Finance and Treasurer of Public Service. Cathy Hsu, Economist of the Public Staff, testified on these subjects on behalf of the Public Staff.

The witnesses who testified as to the appropriate capital structure to be used in this proceeding filed initial testimony and exhibits supporting the use of the Company's actual permanent capital structure at the end of the test year. At the time of the hearing, both witness Jackson and witness Hsu suggested that the structure should be updated to reflect the March 31, 1983, structure. Witness Jackson and witness Flanagan further recommended use of the actual permanent capital structure at March 31, 1983. Witness Hsu recommended inclusion of actual short-term debt at March 31, 1983, in the capital structure.

In determining a representative capital structure to be used in setting rates in this proceeding, the Commission must give appropriate consideration to the degree of permanence of each component of the capital structure and the

degree of permanence of the relationships between said components. The Public Staff asserts that the short-term debt included in the Company's capital structure at March 31, 1983, is needed to support the Company's end-of-period rate base. In addition, the Public Staff presented testimony that tended to show that the Company used short-term debt to finance stored natural gas.

The Company presented testimony that short-term debt was only an interim step in the Company's capital formation process. The record shows that during the test year the Company's short-term debt balance fluctuated during the test year from a high of $24,500,000 in February 1982 to a low of zero in September 1982. Based on this wide variance in the levels of short-term debt, the Commission concludes it is difficult to ascertain a fair and reasonable representative level of short-term debt to be used in the Applicant's capital structure in this proceeding. This problem is accentuated by the fact that in August 1982 the Company replaced its short-term debt by selling $18,000,000 principal amount of First Mortgage Bonds.

Based on the foregoing and consistent with the Commission's decision in Piedmont Natural Gas Company's general rate case in Docket No. G-9, Sub 219, the Commission concludes that short-term debt should not be used in the Applicant's representative capital structure to be used in setting rates in this proceeding. However, the Commission further concludes that the Commission and the Public Staff should monitor the short-term debt balances maintained by Public Service for consideration in future proceedings before this Commission.

The Commission concludes that the appropriate capital structure to be used in this proceeding is as follows:

Item	Percent
Long-term debt	49.75%
Preferred stock	7.28%
Common equity	42.97%
Total	100.00%

There is no substantial disagreement between the parties as to the appropriate and reasonable cost of long-term debt and preferred stock. These costs are 10.35% and 7.15%, respectively. The Commission therefore concludes that these costs are reasonable and should be used in this proceeding.

Witness Flanagan testified as to the total capital requirements over the period 1982-1986 and as to the need for large amounts of outside capital to finance the Company's construction program. He further testified as to the need to improve earnings to enable the Company to raise capital at the lowest reasonable cost.

The determination of the appropriate fair rate of return for the Company is of great importance and must be made with great care because whatever return is allowed will have an immediate impact on the Company, its stockholders, and its customers. In the final analysis, the determination of a fair rate of return must be made by this Commission, using its own impartial judgment and guided by the testimony of expert witnesses and other evidence of record. Whatever return allowed must balance the interests of the ratepayers and investors and meet the test set forth in G.S. 62-133(b)(4): "to enable the public utility by sound management to produce a fair profit for

its stockholders, considering changing economic conditions and other factors, as they then exist, to maintain its facilities and services in accordance with the reasonable requirements of its customers in the territory covered by its franchise, and to compete in the market for capital funds on terms which are reasonable and which are fair to its customers and to its existing investors."

The return allowed must not burden ratepayers any more than is necessary for the utility to continue to provide adequate service. The North Carolina Supreme Court has stated that the history of G.S. 62-133(b):

> "...supports the inference that the Legislature intended for the Commission to fix rates as low as may be reasonably consistent with the requirements of the Due Process Clause of the Fourteenth Amendment to the Constitution of the United States..." State ex rel. Utilities Commission v. Duke Power Co., 285 N.C. 377, 206 S.E.2d 269 (1974).

Based on the foregoing and the entire record in this proceeding, the Commission is of the opinion that a 15.30% return on common equity is fair and reasonable. When this return is weighed with the other elements of the capital structure and the other cost rates the Commission has deternmined to be reasonable, the Commission finds and concludes that an overall return on the original cost net investment rate base of 12.24% is reasonable.

In setting the approved rates of return at the foregoing levels, the Commission has considered all of the relevant testimony and the tests of a fair return. The Commission concludes that the revenues herein allowed should enable the Company, given efficient management, to attract sufficient debt and equity capital to discharge its obligations and to achieve and maintain adequate natural gas service.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 14

The Commission has previously discussed the finding and conclusions regarding the fair rate of return the Company should be afforded an opportunity to earn.

The following schedules summarize the gross revenues and the rates of return which the Company should have a reasonable opportunity to achieve based upon the increases approved herein. Such schedules, illustrating the Company's gross revenue requirements, incorporate the findings and conclusions heretofore and herein made by the Commission.

SCHEDULE I
PUBLIC SERVICE COMPANY OF NORTH CAROLINA, INC.
STATE OF NORTH CAROLINA
STATEMENT OF OPERATING INCOME
Twelve Months Ended September 30, 1982

Item	Present Rates	Increase Approved	After Approved Increase
Operating Revenues:			
Natural gas sales	$246,785,703	$1,916,396	$ 248,702,099
Miscellaneous	512,465	-	512,465
Total	$247,298,168	1,916,396	249,214,564
Operating Revenue Deductions:			
Cost of gas	$184,065,291	$ -	$ 184,065,291
Operation and maintenance	19,031,697	5,864	19,037,561
Depreciation	5,402,750	-	5,402,750
Taxes other than income	17,226,569	114,632	17,341,201
State income taxes	920,180	107,754	1,027,934
Federal income taxes	6,611,182	776,547	7,387,729
Amortization	(315,293)	-	(315,293)
Total operating revenue deductions	$232,942,376	$1,004,797	$ 233,947,173
Net operating income	14,355,792	911,599	15,267,391
Hendersonville adjustment	334,490	-	334,490
Net operating income for return	$ 14,690,282	$ 911,599	$ 15,601,881

SCHEDULE II
PUBLIC SERVICE COMPANY OF NORTH CAROLINA, INC.
STATE OF NORTH CAROLINA
STATEMENT OF RATE BASE AND RATE OF RETURN
Twelve Months Ended September 30, 1982

Item	Amount
Investment in Gas plant	
Gas utility plant in service	$185,780,497
Depreciation reserve	(56,426,323)
Working capital	13,392,666
Accumulated deferred income taxes	(15,064,708)
Cost-free capital	(258,000)
Original cost rate base	$127,424,132
Rate of Return	
Present rates	11.53%
Approved rates	12.24%

SCHEDULE III
PUBLIC SERVICE COMPANY OF NORTH CAROLINA, INC.
STATE OF NORTH CAROLINA
STATEMENT OF CAPITALIZATION AND RELATED COSTS
Twelve Months Ended September 30, 1982

Item	Ratio %	Original Cost Rate Base	Embedded Cost %	Net Operating Income
	Present Rates - Original Cost Rate Base			
Long-term debt	49.75%	$ 63,393,505	10.35%	$ 6,561,228
Preferred stock	7.28%	9,276,477	7.15%	663,268
Common equity	42.97%	54,754,150	13.64%	7,466,460
Total	100.00%	$127,424,132	-	$14,690,282
	Approved Rates - Original Cost Rate Base			
Long-term debt	49.75%	$ 63,393,505	10.35%	$ 6,561,228
Preferred stock	7.28%	9,276,477	7.15%	663,268
Common equity	42.97%	54,754,150	15.30%	8,377,385
Total	100.00%	$127,424,132	-	$15,601,881

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 15 AND 16

The evidence for this finding is found in the testimony of Public Staff witness Curtis and Company witness Dickey.

Both the evidence of the Company and the Public Staff reflect that the Company has lost substantial markets and customers because the price of gas is in excess of the cost of competitive fuels. In addiition, a substantial part of the Company's remaining large commercial and industrial sales are being made at negotiated rates which are lower than the rates approved in the last general rate case. Most of these negotiated sales are to customers using heavy fuel oils. This situation has made it difficult to determine with reasonable accuracy the Company's sales volumes and revenues under both present and proposed rates.

The Public Staff presented an Industrial Sales Tracker (IST) at the hearing. The purpose of the IST is to stabilize the Company's margins while maintaining as large a sales base as possible. Under the proposal, the Commission will establish a margin for industrial and large commercial sales with revenues above or below this margin being tracked through adjustments to rates for other customers. With the implementation of this tracker, the Company and Public Staff are in agreement as to sales volumes and general rate design. The Commission concludes that the IST is reasonable and should be adopted as a tariff item by Public Service. The Commission further concludes that the terms of the IST should be similar to those presented by the Public Staff at the hearing.

Based on the revenue requirements and sales volumes found reasonable elsewhere herein, the Commission concludes that the rates reflected on Appendix A attached hereto will generate said revenue requirements. However, the Commission further concludes that the rates on Appendix A should be properly adjusted to reflect changes in Transco's rates since December 31, 1983, and to reflect the current price of alternate fuel, to be considered under the IST mechanism, approved herein above.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 17

The evidence for this finding of fact is contained in the testimony of Public Staff witness Curtis. The revenue figure provided originally to Public Staff witness Cox by witness Curtis reflected the additional monies generated from emergency sales. Witness Curtis reflected the additional monies generated from emergency sales. Witness Curtis recommended that this amount should be placed in a deferred account for future refunding to customers other than those who paid in this amount rather than placing these dollars in operating revenues. These emergency sales are random in nature and it is possible that none may be made within an annual period. Based on the foregoing, and the entire evidence of record, the Commission concludes that the $22,398 related emergency sales should be placed in a deferred account for future refunding and that all future transactions of emergency gas sales should be treated in the same manner.

IT IS, THEREFORE, ORDERED as follows:

1. That Public Service Company of North Carolina, Inc., be, and is hereby, authorized to adjust and increase its rates and charges based upon the Company's level of test year operations by $1,916,396.

2. That the Industrial Sales Tracker (IST) mechanism is approved as discussed herein and shall be effective for service rendered on and after the first day of the month following the effective date of this Order.

3. That Public Service be, and hereby is, ordered to file appropriate tariffs in conformity with the base rates set forth in Appendix A properly adjusted for the current Transco rates and for the current cost of alternate fuel considered in the IST mechanism and in conformity with the provisions of this Order not later than ten (10) days from the date of this Order.

4. That Public Service be, and hereby is, ordered to notify its customers of the increased rates and of the Industrial Sales Tracker (IST) mechanism approved herein by appropriate bill insert in the next billing cycle following the effective date of the new tariffs.

5. That Public Service be, and hereby is, ordered to file a monthly report with the Commission's Chief Clerk showing the IST volumes sold and the margin earned compared to the base period IST monthly volumes and margin.

6. That the tariffs filed in response to Ordering Paragraph 3 above shall be approved upon further Order of the Commission.

ISSUED BY ORDER OF THE COMMISSION.
This the 18th day of August 1983.

NORTH CAROLINA UTILITIES COMMISSION
Sandra J. Webster, Chief Clerk

(SEAL)

APPENDIX A
PUBLIC SERVICE COMPANY OF NORTH CAROLINA, INC.
DOCKET NO. G-5, SUB 181

Rate Schedule	Number Bills	Facilities Charge ($)	Sales Volume (Th.)	Proposed Rate ($Th.)	Total Sales Revenues ($)
50	1,446,453	$ 4.50			$ 6,509,039
50			114,570,294	$.61843 1/	70,853,707
55	179,856	7.50			1,348,920
55			77,556,478	.60885 1/	47,220,262
60	1,272	75.00			95,400
60			49,872,694	.57708 1/	28,780,534
65 & 67	2,529	75.00			189,675
65 & 67			74,525,853	.57305 1/	42,707,040
70 & 72	944	250.00			236,000
70 & 72			110,330,044	.4600 1/	50,751,820
85	537	-			
85			18,252	-	8,000

1/ These rates must be adjusted to reflect current Transco rates and the current price of alternate fuel to be used in the Industrial Sales Tracker.

DOCKET NO. G-5, SUB 181

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Application of Public Service Company of North Carolina, Inc., for an Adjustment of Its Rates and Charges) ORDER AMENDING ORDER OF AUGUST 18, 1983, AND APPROVING RATES

BY THE COMMISSION: The Commission issued Order Granting Partial Rate Increase on August 18, 1983. Said Order approved a gross revenue increase of $1,916,396, for Public Service Company of North Carolina, Inc. (Applicant), based upon the test year ended September 30, 1982.

On August 23, 1983, the Public Staff - North Carolina Utilities Commission filed a letter stating that the Order of August 18, 1983, established rates based in part on consideration of the Applicant's Company use volumes in both the cost of gas account and the operation and maintenance expense account. This overstatement resulted in the Applicant's gross revenue requirements being overstated by $388,290. On August 24, 1983, the Applicant filed a letter that likewise stated that the Applicant's gross revenue requirements were overstated due to the inclusion of the Company use volumes in both the cost of gas and operation and maintenance expense. The Commission considers the above-referenced letters filed herein by the Public Staff and Public Service to be a stipulation by said parties regarding the appropriate cost of Company use volumes.

On August 29, 1983, Public Service filed rates in this docket for Commission approval designed to produce approximately $1,527,476 of additional annual revenues.

After a careful consideration of the foregoing and the entire record in this matter, the Commission concludes that the Order of August 18, 1983, should be amended pursuant to G.S. 62-80 in order to reflect the $388,290 reduction in the Applicant's fair and reasonable revenue requirements in this proceeding.

In view of the above-referenced letters of stipulation filed herein by the Company and the Public Staff, it is clear that this Order of amendment does not constitute an arbitrary or capricious abuse of the discretionary power granted to this Commission by G.S. 62-80 to rescind, alter, or amend a prior order or decision. State of North Carolina ex rel. Utilities Commission v. Carolina Coach Company, 260 N.C. 43, 132 S.E.2d 249 (1963); State of North Carolina ex rel. Utilities Commission v. Edmisten, 291 N.C. 575, 232 S.E.2d 177(1977). To the contrary, the Commission is merely exercising its statutorily mandated duty to fix just and reasonable rates in North Carolina. Accordingly, the Commission concludes that the Findings of Fact 10, 11, 14, and 16 as set forth in its Order of August 18, 1983, in this docket should be amended to read as follows:

10. The test period level of Public Service's operating revenue deductions under present rates after accounting and pro forma adjustments is $232,761,585, which includes the amount of $5,402,750 for actual investment currently consumed through reasonable actual depreciation.

11. The appropriate level of the net income adjustment associated with the purchase of the Hendersonville property is $338,702.

14. Public Service's pro forma return on rate base at the end of the test year was 11.67% which is less than that which the Commission has determined to be just and reasonable. Therefore, in order to have the opportunity to earn the returns which the Commission has determined to be just and reasonable, Public Service should be allowed to increase its rates and charges so as to produce an additional $1,527,476 of annual gross revenues based on its operations during the test year.

16. The rates set forth in Appendix A attached hereto and approved herein will generate the appropriate level of revenue and afford the Company an opportunity to achieve the overall return of 12.24% approved herein, but that said rates should be adjusted for any changes in Public Service's base rates since December 1982 and to reflect the current price of the alternate fuel considered in the IST. In addition, said rates should be adjusted to reflect the reduced revenue requirements of $388,290 related to the cost of gas adjustment.

Further, the Commission is also of the opinion that the schedules set forth in the Order in this docket dated August 18, 1983, should be amended as follows in order properly to reflect the adjustments made herein:

SCHEDULE I
PUBLIC SERVICE COMPANY OF NORTH CAROLINA, INC.
STATE OF NORTH CAROLINA
STATEMENT OF OPERATING INCOME
Twelve Months Ended September 30, 1982

Item	Rates	Approved	Increase
Operating Revenues:			
Natural gas sales	$246,785,703	$1,527,476	$ 248,313,179
Miscellaneous	512,465	-	512,465
Total	$247,298,168	1,527,476	248,825,644
Operating Revenue Deductions:			
Cost of gas	$183,709,123	$ -	$ 183,709,123
Operation and maintenance	19,031,697	4,674	19,036,371
Depreciation	5,402,750	-	5,402,750
Taxes other than income	17,226,569	91,368	17,317,937
State income taxes	941,550	85,886	1,027,436
Federal income taxes	6,765,189	618,952	7,384,141
Amortization	(315,293)	-	(315,293)
Total operating revenue deductions	$232,761,585	$ 800,880	$ 233,562,465
Net operating income	14,536,583	726,596	15,263,179
Hendersonville adjustment	338,702	-	338,702
Net operating income for return	$ 14,875,285	$ 726,596	$ 15,601,881

SCHEDULE II
PUBLIC SERVICE COMPANY OF NORTH CAROLINA, INC.
STATE OF NORTH CAROLINA
STATEMENT OF RATE BASE AND RATE OF RETURN
Twelve Months Ended September 30, 1982

Item	Amount
Investment in Gas plant	
Gas utility plant in service	$185,780,497
Depreciation reserve	(56,426,323)
Working capital	13,392,666
Accumulated deferred income taxes	(15,064,708)
Cost-free capital	(258,000)
Original cost rate base	$127,424,132
Rate of Return	
Present rates	11.67%
Approved rates	12.24%

SCHEDULE III
PUBLIC SERVICE COMPANY OF NORTH CAROLINA, INC.
STATE OF NORTH CAROLINA
STATEMENT OF CAPITALIZATION AND RELATED COSTS
Twelve Months Ended September 30, 1982

Item	Ratio %	Original Cost Rate Base	Embedded Cost %	Net Operating Income
	Present Rates - Original Cost Rate Base			
Long-term debt	49.75%	$ 63,393,505	10.35%	$ 6,561,228
Preferred stock	7.28%	9,276,477	7.15%	663,268
Common equity	42.97%	54,754,150	13.98%	7,650,789
Total	100.00%	$127,424,132	-	$14,879,285
	Approved Rates - Original Cost Rate Base			
Long-term debt	49.75%	$ 63,393,505	10.35%	$ 6,561,228
Preferred stock	7.28%	9,276,477	7.15%	663,268
Common equity	42.97%	54,754,150	15.30%	8,377,385
Total	100.00%	$127,424,132	-	$15,601,881

Review of the proposed rates filed herein by Public Service on August 29, 1983, leads the Commission to find and conclude that such rates will produce approximately $1,527,476 of additional annual revenues based on test year operations before consideration of changes in Transco's rates since December 31, 1982, and that such rates, being just and reasonable, should be approved effective for service rendered on and after September 1, 1983.

IT IS, THEREFORE, ORDERED as follows:

1. That the Order of August 18, 1983, be amended as denoted herein in this Order. Further, that except as modified herein, the Commission Order entered in this docket on August 18, 1983, shall remain in full force and effect.

2. That the rates filed by Public Service on August 29, 1983, be, and hereby are, approved, effective for service rendered on or after September 1, 1983.

ISSUED BY ORDER OF THE COMMISSION.
This the 31st day of August 1983.

NORTH CAROLINA UTILITIES COMMISSION
Sandra J. Webster, Chief Clerk

(SEAL)

DOCKET NO. B-69, SUB 135

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Trailways Southeastern Lines, Inc. - Suspension and Investigation of Proposed Increases in Intercity Bus Passenger Fares and Bus Package Service Rates and Charges, Scheduled to Become Effective March 7, 1983) ORDER APPROVING PARTIAL INCREASE IN RATES AND CHARGES

HEARD IN: Commission Hearing Room, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina 27602, on May 6, 1983

BEFORE: Commissioner Leigh H. Hammond, Presiding; Chairman Robert K. Koger and Commissioner A. Hartwell Campbell

APPEARANCES:

For the Respondent:

Edward S. Finley, Jr., Hunton & Williams, Attorneys at Law, P.O. Box 109, Raleigh, North Carolina 27602

For the Public Staff:

Theodore C. Brown, Jr., Staff Attorney, Public Staff - North Carolina Utilities Commission, P.O. Box 991, Raleigh, North Carolina 27602
For: The Using and Consuming Public

BY THE COMMISSION: On February 3, 1983, the Commission received tariff filings publishing increased rates and charges from National Bus Traffic Association (NBTA) for and on behalf of Trailways Southeastern Lines, Inc. (Trailways, Company), proposing to increase North Carolina intrastate intercity bus passenger fares and package express rates as follows:

1. Passenger fares increased by 25% adjusted to nearest "0" or "5."

2. Express rates increased by 27% adjusted to nearest "0" or "5."

The proposed revisions in bus passenger and express tariff schedules are published as follows:

<u>NATIONAL BUS TRAFFIC ASSOCIATION, INC., AGENT</u>

1. North Carolina Local and Joint Master Table Tariff, N.C.U.C. No. 308;

2. North Carolina Intrastate Supplement No. 790 to National Busing Fare Tariff, Being Supplement No. 33 to N.C.U.C. No. 4;

3. North Carolina Intrastate Supplement No. 721 to National Passenger Tariff, Being Supplement No. 30 to N.C.U.C. No. 31;

4. Twelfth Revised Pages F-1 and F-2 Bearing Correction No. 258A to National Express Tariff, N.C.U.C. No. 243;

TRAILWAYS SOUTHEASTERN LINES, INC.

5. Supplement No. 4 to Local Passenger Tariff, Being Supplement No. 1 to N.C.U.C. No. 8; and

6. Supplement No. 1 to Local Passenger Tariff, N.C.U.C. No. 10.

On March 1, 1983, the Commission by Order suspended the proposed tariff schedules for a period of 270 days from March 7, 1983, and declared the filing a general rate case. The Commission requested the Public Staff to investigate and analyze the proposed tariff filing and make a recommendation to the Commission with respect to the reasonableness of the proposed tariff filing.

On February 3 and 9, 1983, Maria U. Hensley, Director of Financial Reporting and Analysis for Trailways, Inc., filed an Affidavit and Testimony and Exhibits in support of the proposed tariff.

On April 26, 1983, Phillip W. Cooke, Rate Specialist, Public Staff, Transportation Rates Division, filed testimony and exhibits in this docket for and on behalf of the using and consuming public.

On May 6, 1983, at 10:00 a.m., in Raleigh, North Carolina, Commission Hearing Room, Dobbs Building, 430 North Salisbury Street, the ordered hearing was held. Witness Hensley presented testimony and exhibits for Trailways, Inc., and witness Cooke presented testimony and exhibits for the Public Staff.

Based on the foregoing, the evidence adduced at the hearing, and the entire record in this matter, the Commission makes the following

FINDINGS OF FACT

1. The Respondent, Trailways Southeastern Lines, Inc., is engaged in the intercity transportation of passengers for compensation in North Carolina intrastate commerce, and is subject to the jurisdiction of this Commission under the Public Utilities Act.

2. The test period in this docket is the 12 months ended September 30, 1982, adjusted for known changes occurring through the close of the hearing.

3. The test period North Carolina intrastate end-of-period expenses of the Company are $4,015,439 under present rates.

4. The total test period North Carolina intrastate issue traffic revenues under present rates are $3,857,152, consisting of passenger revenues of $2,650,564, special bus revenues of $130,644, mail revenues of $2,113, express revenues of $1,036,719, newspaper revenues of $107, miscellaneous station revenues of $25,426, and other revenues of $11,579; and under proposed rates are $4,799,707.

5. The test period present level operating ratio prior to the proposed increase is 104.10%. With the approved increase in revenues of $653,929 an 18% increase in passenger fares and an 18% increase in express rates, the operating ratio of all rates and charges will be 90.1%, the same operating ratio level proposed by Trailways found to be reasonable herein.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 1 AND 2

The evidence for these findings comes from the verified application. The findings are essentially informational, procedural, and jurisdictional in nature and are not contested.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 3

The only difference between the parties with respect to operating expenses concerns the factor to be applied to expenses to bring them to the present level. Witness Hensley, testifying on behalf of Trailways, computed a 15.4% factor which she applied to test year expenses. Witness Hensley determined the total system expenses and expenses per bus mile for each year from 1978 through 1981, from which she determined that the average percentage increase in the unit price (cost per bus mile) from 1978 through 1981 was 15.4%. The 15.4% average unit cost increase was then applied to the actual test year expenses to determine the end-of-period level of expenses for purposes of this case.

Witness Cooke, for the Public Staff, took issue with the 15.4% factor computed by Trailways. Witness Cooke divided the cost per bus mile at March 31, 1983, of $1.89 by the average cost per bus mile for the test year of $1.86 to calculate his end-of-period adjustment factor of 1.6%.

In his testimony, witness Cooke stated that the 15.4% factor utilized by Trailways is improper because Trailways was granted rate relief in Docket No. B-105, Subs 38, and 39, and Docket No. B-69, Sub 133. Consequently, Trailways has requested and has been granted rate relief that took into consideration increases in cost per bus mile in prior years. Those increases in cost per bus mile have again been considered in the calculation to derive the 15.4% pro forma adjustment used in this docket.

The Commission has given much consideration to the appropriate expense growth factor that should be used to establish the proper end-of-period level of operating expenses to be used in determining fair and reasonable rates in this proceeding. The Commission concludes that the company's factor must be determined inappropriate due to its reliance on a historical period (1978-1981), that is <u>unrepresentative</u> of current economic conditions affecting the Company's ongoing level of operating expenses. Likewise, the Commission rejects the Public Staff's facts due to the limited data base upon which the factor was developed. Therefore, the Commission concludes that the most appropriate end-of-period expense factor to be used in determining fair and reasonable rates in this proceeding is 6.28%, which is based on data from a represented period of 1980 to the first quarter, 1983. This period is longer than that used by the Public Staff, thereby providing more data points upon which to produce the fair and reasonable end-of-period expense factor, and is more current than that used by the Company, thereby providing more <u>representative</u> data.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 4

The evidence supporting Finding of Fact No. 4 is contained in the testimony of Public Staff witness Cooke and was adopted by the Company in its Proposed Order. There being no dispute concerning this matter, the Commission concludes that the appropriate end-of-period revenue under present rates is $3,857,152 and under proposed rates is $4,799,707.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 5

Based upon the Commission's findings and conclusions under Findings of Fact Nos. 3 and 4, the Commission concludes that Trailways' end-of-test-period operating ratio under present rates is 104.10% and that the Company's proposed operating ratio of 90.1% found to reasonable for setting rates in this proceeding can be obtained by an equitable 18% increase on passenger fares and an 18% increase on express rates, resulting in an annual increase in revenues of $653,929, consisting of $470,829 in passenger revenue and $183,100 in express revenue. Trailways' proposal of 25% increase in passenger fares and a 27% increase in express rates is excessive in order to obtain the 90.1% proposed operating ratio, and therefore their increases are denied.

IT IS, THEREFORE, ORDERED as follows:

1. That the Respondent be, and the same hereby is, authorized to increase North Carolina intrastate passenger fares by 18% and express rates by 18%.

2. That the Commission Order of Suspension and Investigation in this proceeding be, and the same is, vacated and set aside.

3. That the Respondent hereby is ordered to cancel the tariff publications under suspension in this docket and is authorized to publish appropriate tariff schedules providing for the increase set forth in Ordering Paragraph No. 1 above, and that the publications may be made effective on one day's notice to the Commission and to the public.

4. That upon the publications herein authorized, the investigation in this matter be discontinued and the docket closed.

ISSUED BY ORDER OF THE COMMISSION.
This the 3rd day of June 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sandra J. Webster, Chief Clerk

DOCKET NO. B-7, SUB 99

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of

Petition of Greyhound Lines, Inc., to Discontinue Intrastate Motor Bus Transportation	) RECOMMENDED ORDER ALLOWING DISCONTINUANCE OF PASSENGER SERVICE

HEARD IN: Courtroom D, First Floor, Randolph County Courthouse, Worth Street, Asheboro, North Carolina, on Monday, March 21, 1983, at 10:00 a.m.

Commissioners' Board Room, Fourth Floor, County Office Building, 720 East Fourth Street, Charlotte, North Carolina, on Monday March 21, 1983, at 3:00 p.m.

Council Room, Governmental Services Facilities Center, 101-103 West Gold Street, Kings Mountain, North Carolina, on Monday, March 21, 1983, at 7:30 p.m.

Courtroom 906, 9th Floor, Buncombe County Courthouse, Courthouse Plaza, Asheville, North Carolina, on Tuesday, March 22, 1983, at 11:00 a.m.

Council Chambers, Second Floor, City Hall, 101 North Main Street, Winston-Salem, North Carolina, on Tuesday, March 22, 1983, at 7:00 p.m.

Board Room, Municipal Bulding, 111 Masonic Street, Creedmoor, North Carolina, on Wednesday, March 23, 1983, at 2:00 p.m.

Commission Hearing Room, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina, on Tuesday, March 29, 1983, at 9:30 a.m.

Superior Courtroom, Second Floor, Duplin County Courthouse, Kenansville, North Carolina, on April 8, 1983, at 10:00 a.m.

Meeting Room, Buies Creek Fire Department, Buies Creek, North Carolina, on April 8, 1983, at 2:00 p.m.

BEFORE: Wilson B. Partin, Jr., Hearing Examiner

APPEARANCES:

For the Applicant:

J. Ruffin Bailey, Ralph McDonald, and Gary K. Joyner, Bailey, Wooten, McDonald & Fountain, Attorneys at Law, P. O. Box 2246, Raleigh, North Carolina 27602
Appearing for: Greyhound Lines, Inc.

For the Public Staff:

Theodore C. Brown, Jr., Staff Attorney, Public Staff - North Carolina Utilities Commission, P. O. Box 991, Raleigh, North Carolina 27602
Appearing for: The Using and Consuming Public

PARTIN, HEARING EXAMINER: On December 30, 1982, Greyhound Lines, Inc., filed a petition with the Commission proposing to discontinue North Carolina intrastate motor bus transportation over seventeen (17) routes located throughout North Carolina.

The routes proposed to be discontinued by Greyhound are as follows:

ROUTE 1 - That portion between Asheville, North Carolina, and Hendersonville, North Carolina, via U.S. Highway 25 via Fletcher and that portion of U.S. Highway 25 serving Tuxedo;

ROUTE 2 - Between Charlotte, North Carolina, and the North Carolina-South Carolina State Line (west of Pineville) via U.S. Highway 21 through Pineville;

ROUTE 3 - Between Pineville, North Carolina, and the North Carolina-South Carolina State Line (south of Pineville) via U.S. Highway 521;

ROUTE 4 - That portion between junction Interstate Highway 85 and U.S. Highway 74 and the North Carolina-South Carolina State Line over U.S. Highway 74 to Kings Mountain, thence over N.C. Highway 216 to its junction with U.S. Highway 29, thence over U.S. Highway 29 through Grover;

ROUTE 12 - That portion between Charlotte and Mooresville over U.S. Highway 21 to its junction with N.C. Highway 115, thence over N.C. Highway 115 through Huntersville;

ROUTE 14 - That portion between Mocksville and Winston-Salem via U.S. Highway 158 through Clemmons;

ROUTE 16 - That portion between Winston-Salem and junction Old U.S. Highway 52 (northwest of Pilot Mountain) via Old U.S. Highway 52 through Rural Hall and Dalton to its junction with U.S. Highway 52, Business, thence over U.S. Highway 52, Business, through Pilot Mountain to its junction with U.S. Highway 52;

ROUTE 22 - Between Winston-Salem and Kernersville via N.C. Highway 150;

ROUTE 23 - Between Winston-Salem and Greensboro over U.S. Highway 421 through Kernersville and Friendship;

ROUTE 28 - Between Winston-Salem and Raleigh via U.S. Highway 52 through Eller and Welcome to Lexington, thence via U.S. Highway 64 through Asheboro, Ramseur, Siler City and Pittsboro to junction U.S. Highway 64 and N.C.Highway 55 to Apex, thence over Old U.S. Highway 1 to junction of U.S. Highway 64 (approximately 2 miles north of Apex),

thence via U.S.Highway 64 through Cary (that portion between Winston-Salem and Asheboro is currently dormant);

ROUTE 29 - Between Durham and North Carolina-Virginia State Line (north of Bullock) via U.S. Highway 15 through Creedmoor, Oxford, Lewis, and Bullock, also between Creedmoor and Camp Butner over Granville County Road 1111 (that portion between Oxford and the North Carolina-Virginia State Line is currently dormant);

ROUTE 32 - Between the junction of U.S. Highway 401 and N.C. Highway 217 (west of Linden) and the junction of U.S. Highway 401 and N.C. Highway 55 (north of Angier) over N.C. Highway 217 through Linden to its junction with N.C. Highway 82, thence over N.C. Highway 82 to Erwin, thence over N.C. Highway 55 through Coats and Angier;

ROUTE 34 - Between the junction of Harnett County Road 1532 and N.C. Highway 55 (near Angier) and the junction of U.S. Highway 421 and N.C. Highway 55 (at Erwin) over County Road 1532 to Buies Creek, thence over U.S. Highway 421 to Erwin and return over the same route;

ROUTE 36 - Between the junction of Wake County Road 2030 and County Road 2000 (south of Millbrook) and Wake Forest, via County Road 2000 through Falls to its junction with N.C. Highway 98, thence N.C. Highway 98;

ROUTE 41 - Between Warsaw and the junction of N.C. Highway 11 and U.S. Highway 117 (south of Tin City) over N.C. Highway 24 to Kenansville, thence over N.C. Highway 11 through Tin City;

ROUTE 43 - Between the junction of U.S. Highway 70 and Johnston County, County Road 1900 (approximately 5 miles southeast of Clayton) and the junction of U.S. Highway 70 and County Road 1913 (approximately 1 mile northwest of Smithfield) over County Road 1900 to a point just east of Wilson Mills, thence over County Road 1913;

ROUTE 44 - Between Asheboro and Charlotte via N.C. Highway 49, combining such operations with operations now conducted by applicant between Asheboro and Raleigh and other points, so as to provide through service over said route between Raleigh and Charlotte via Asheboro.

Greyhound's petition also cited and quoted from a provision of the recently enacted Bus Regulatory Reform Act of 1982, 49 U.S.C. Sec. 10935, which provides as follows:

"When a motor common carrier of passengers having intrastate authority under the laws of a State, and interstate authority under a certificate issued under section 10922 of this subchapter, to provide transportation over any route to any points in such State has proposed to discontinue providing transportation over such route to such point or to reduce its level of service over such route to such point to a level which is less than one trip per day (excluding Saturdays and Sundays) and the carrier has requested the department, agency, or instrumentality of such State having jurisdiction over granting such discontinuance or reduction for permission to discontinue such

intrastate transportation or to reduce its level of service to a level which is less than one trip per day (excluding Saturdays and Sundays) and the request has been denied (in whole or in part) or such department, agency, or instrumentality has not acted finally (in whole or in part) on the request by the 120th day after the carrier made the request, the carrier may petition the Commission for such permission.

On January 28, 1983, the Public Staff filed a motion for investigation, hearing, and request for data in this docket. In its motion the Public Staff alleged that the Petition of Greyhound was a matter affecting the public interest and that the petition should be set for hearing throughout the State in the areas to be affected by the discontinuance and that Greyhound should be required to give notice of its petition and of the scheduled hearings by newspaper publication and by notices along its routes and in its buses. The Public Staff further alleged that since the petition was filed pursuant to the Bus Regulatory Reform Act of 1982, the Commission should institute the proceeding immediately in order that all matters may be disposed of prior to the expiration of 120 days from the date of Greyhound's filing. The motion of the Public Staff also contained a data request to be answered by Greyhound.

By Orders issued on February 9 and 15, 1983, the Commission instituted an investigation into Greyhound's petition and scheduled hearings beginning the week of March 21, 1983, in Asheboro, Charlotte, Kings Mountain, Asheville, Winston-Salem, Creedmoor, Buies Creek, Kenansville, and Raleigh. Greyhound was required to give notice of the time and place and purpose of these hearings by appropriate newspaper publication and by the posting of notices in its buses, bus stations, and public places along the routes proposed to be discontinued. By subsequent order issued February 17, 1983, the Commission ordered Greyhound to comply with the data request of the Public Staff on or before March 11, 1983, and fixed the times for filing testimony and exhibits.

Because of snow which occurred on March 24, 1983, the Commission was forced to cancel the hearings scheduled in Buies Creek and Kenansville on that date. The Commission issued an Order rescheduling hearings in Kenansville and Buies Creek on April 8, 1983, and required Greyhound to give notice thereof.

The petition came on for hearing at the time and places set forth above. The Company and the Public Staff were present at each of these hearings and were represented by counsel. The following public witnesses testified at the following places:

Asheboro:	Thomas J. McIntosh Ralph Bulla
Charlotte:	Nancy MacCormac, Mayor of Davidson
Kings Mountain:	John Henry Moss, Mayor of Kings Mountain
Asheville:	No witnesses
Winston-Salem:	Kenneth Kroosh, City Planning Manager of Winston-Salem
Creedmoor:	Paula W. Ellington, Creedmoor Chamber of Commerce Thomas B. Currin, Executive Director of the Granville County Chamber of Commerce

Anthony Selton, President of the Butner Chamber of Commerce

Raleigh: Merle Edwards, Clerk, City of Creedmoor
Thomas H. Edwards
Julian Mangum

Buies Creek: No witnesses
Kenansville: No witnesses

At the hearing in Raleigh, Greyhound presented the testimony and exhibits of Eugene Given, Director of Traffic, Greyhound Lines, Inc., Phoenix, Arizona. The Public Staff presented the testimony of David King, Director of the Public Transporation Division of the North Carolina Department of Commerce, Raleigh, North Carolina; and Phillip Cooke, a member of the Transporation Rates Division, Public Staff; and J. Phillip Lee, a member of the Transportation Division of the Commission Staff.

During the hearings in this proceeding, Greyhound and the Public Staff entered into the following stipulation, which was set forth in an Order of the Examiner issued on April 7, 1982, and served on the parties:

1. The hearings originally scheduled in Buies Creek and Kenansville on March 24, 1983, would be rescheduled to Friday, April 8, 1983, at a time and place to be set by Commission Order.

2. The Hearing Examiner would announce his decision either at the conclusion of the hearings on April 8, 1983, or at least no later than April 11, 1983.

3. The party in whose favor the decision was rendered would prepare and submit on or before April 15, 1983, a proposed order to the Hearing Examiner for consideration and adoption by him.

4. The Hearing Examiner would issue his Recommended Order in this docket on or before April 18, 1983.

5. Any Exceptions to the Examiner's Recommended Order must be filed with the Commission on or before April 21, 1983.

6. If Exceptions are filed to the Recommended Order, the Commission will hear oral argument on Exceptions on Monday, April 25, 1983, at a time to be announced by subsequent Order.

7. The Commission will issue its Final Order in this docket on or before Friday, April 29, 1983.

On April 15, 1983, the Public Staff filed a letter in this docket stating that, with respect to the seventeen (17) requested abandonments by Greyhound, that significant public interest was shown in resistance to the proposed change and abandonment of Route 29 (Creedmoor and Butner). The Public Staff further stated that service to the Butner area is very much needed and that the Commission should order such service to be continued.

Upon consideration of the petition of Greyhound, the testimony and exhibits presented at all the hearings in this docket, including the public witnesses, the Examiner makes the following

FINDINGS OF FACT

1. Greyhound Lines, Inc., is a common carrier of passengers by bus in North Carolina intrastate commerce and is subject to the jurisdiction of the Commission.

2. Greyhound proposes to discontinue motor bus transportation under its Certificates of Public Convenience and Necessity issued by the Commission as follows:

ROUTE 1 - That portion between Asheville, North Carolina, and Hendersonville, North Carolina, via U.S. Highway 25 via Fletcher and that portion of U.S. Highway 25 serving Tuxedo;

ROUTE 2 - Between Charlotte, North Carolina, and the North Carolina-South Carolina State Line (west of Pineville) via U.S. Highway 21 through Pineville;

ROUTE 3 - Between Pineville, North Carolina, and the North Carolina-South Carolina State Line (south of Pineville) via U.S. Highway 521;

ROUTE 4 - That portion between junction Interstate Highway 85 and U.S. Highway 74 and the North Carolina-South Carolina State Line over U.S. Highway 74 to Kings Mountain, thence over N.C. Highway 216 to its junction with U.S. Highway 29, thence over U.S. Highway 29 through Grover;

ROUTE 12 - That portion between Charlotte and Mooresville over U.S. Highway 21 to its junction with N.C. Highway 115, thence over N.C. Highway 115 through Huntersville;

ROUTE 14 - That portion between Mocksville and Winston-Salem via U.S. Highway 158 through Clemmons;

ROUTE 16 - That portion between Winston-Salem and junction Old U.S. Highway 52 (northeast of Pilot Mountain) via Old U.S. Highway 52 through Rural Hall and Dalton to its junction with U.S. Highway 52, Business, thence over U.S. Highway 52, Business, through Pilot Mountain to its junction with U.S. Highway 52;

ROUTE 22 - Between Winston-Salem and Kernersville via N.C. Highway 150;

ROUTE 23 - Between Winston-Salem and Greensboro over U.S. Highway 421 through Kernersville and Friendship;

ROUTE 28 - Between Winston-Salem and Raleigh via U.S. Highway 52 through Eller and Welcome to Lexington, thence via U.S. Highway 64 through Asheboro, Ramseur, Siler City and Pittsboro to junction U.S. Highway 64 and N.C.Highway 55 to Apex, thence over Old U.S. Highway 1 to junction of U.S. Highway 64 (approximately 2 miles north of Apex),

thence via U.S. Highway 64 through Cary (that portion between Winston-Salem and Asheboro is currently dormant);

ROUTE 29 - Between Durham and North Carolina-Virginia State Line (north of Bullock) via U.S. Highway 15 through Creedmoor, Oxford, Lewis, and Bullock, also between Creedmoor and Camp Butner over Granville County Road 1111 (that portion between Oxford and the North Carolina-Virginia State Line is currently dormant);

ROUTE 32 - Between the junction of U.S. Highway 401 and N.C. Highway 217 (west of Linden) and the junction of U.S. Highway 401 and N.C. Highway 55 (north of Angier) over N.C. Highway 217 through Linden to its junction with N.C. Highway 82, thence over N.C. Highway 82 to Erwin, thence over N.C. Highway 55 through Coats and Angier;

ROUTE 34 - Between the junction of Harnett County Road 1532 and N.C. Highway 55 (near Angier) and the junction of U.S. Highway 421 and N.C. Highway 55 (at Erwin) over County Road 1532 to Buies Creek, thence over U.S. Highway 421 to Erwin and return over the same route;

ROUTE 36 - Between the junction of Wake County Road 2030 and County Road 2000 (south of Millbrook) and Wake Forest, via County Road 2000 through Falls to its junction with N.C. Highway 98, thence N.C. Highway 98;

ROUTE 41 - Between Warsaw and the junction of N.C. Highway 11 and U.S. Highway 117 (south of Tin City) over N.C. Highway 24 to Kenansville, thence over N.C. Highway 11 through Tin City;

ROUTE 43 - Between the junction of U.S. Highway 70 and Johnston County, County Road 1900 (approximately 5 miles southeast of Clayton) and the junction of U.S. Highway 70 and County Road 1913 (approximately 1 mile northwest of Smithfield) over County Road 1900 to a point just east of Wilson Mills, thence over County Road 1913;

ROUTE 44 - Between Asheboro and Charlotte via N.C. Highway 49, combining such operations with operations now conducted by applicant between Asheboro and Raleigh and other points, so as to provide through service over said route between Raleigh and Charlotte via Asheboro.

3. On each of the routes that Greyhound proposes to discontinue, the traffic carried by the Company is greatly insufficient to make the routes profitable for the Company. On every route the Company's variable costs in providing service greatly exceed the revenue generated from the traffic. In fact, on almost every route the revenue generated was not even sufficient to pay for that part of the variable costs related to drivers' wages and fuel and oil expenses.

4. In most instances, the ridership on the routes proposed to be abandoned by Greyhound averaged less than one passenger per bus.

5. The number of passengers carried by Greyhound over these routes has been declining during the past decade, and there is no prospect that the decline will be reversed. This decline is caused by the competition which Greyhound

receives from other means of transportation, including the privately-owned automobile.

6. The Commission scheduled hearings throughout the State in those localities most affected by Greyhound's petition. Greyhound gave public notice of these hearings as required by the Orders of the Commission. In addition, the Public Staff wrote approximately 200 letters to state senators and representatives, county commissioners, mayors, and chambers of commerce in the areas affected by the Petition. These letters of the Public Staff advised that Greyhound was discontinuing bus service in the area and that the Commission would hold a public hearing in the area at a stated time and place in order to hear testimony from the public. The places of hearing, the date of the hearing, and the number of public witnesses who attended and testified are as follows:

Place	Date	Public Witnesses
Asheboro	March 21, 1983	2
Charlotte	March 21, 1983	1
Kings Mountain	March 21, 1983	1
Asheville	March 22, 1983	0
Winston-Salem	March 22, 1983	1
Creedmoor	March 23, 1983	3
Raleigh	March 29, 1983	3
Kenansville	April 8, 1983	0
Buies Creek	April 8, 1983	0
		11

7. Greyhound in 1982 experienced its first loss ever on its systemwide passenger bus operations.

8. Greyhound is not receiving any subsidy for operations conducted over the routes proposed to be discontinued. By letter dated March 4, 1983, Greyhound offered to maintain service over the affected routes at a level of service to be established by the State of North Carolina, or any financially responsible person, provided there is a subsidy or financial assistance for providing the service which is equal to the fully allocated cost per bus mile plus 20% profit less any operating revenues generated by service. This offer expires on June 29, 1983. Greyhound's offer has not been accepted as of the date of this Order.

9. During the past decade the State of North Carolina has been attempting to coordinate all passenger transportation which might be available at the county level throughout the State. The transportation needs of any person affected by the discontinuances approved herein could possibly be met by such county-level means of transportation. Greyhound should be required to give its passengers affected by the discontinuances notice of any alternative means of transportation that might be available to them.

10. Congress has enacted the Bus Regulatory Reform Act of 1982. This legislation, which became effective on November 19, 1982, permits an intercity bus carrier, such as Greyhound, to seek direct review by the Interstate Commerce Commission of a decision by a state regulatory agency, such as this Commission, which denies, in whole or in part, the application of the carrier to discontine services on routes <u>within</u> the state that are part of

interstate routes regulated by the ICC. The carrier may also seek review where the state agency has failed to act on the carrier's application within 120 days after the application was filed.

11. Greyhound's Petition to discontinue the routes set forth therein should be allowed, except as set forth hereinafter with respect to the Creedmoor/Butner community.

12. Community leaders in the Butner/Creedmoor community expressed their strong concern that Greyhound retain some type of service for the community. There are institutions at Butner, such as the Alcoholic Rehabilitation Center, whose patients may need bus service to and from Butner in order to obtain treatment. Butner and Creedmoor are four miles apart and are joined by N. C. Highway 56, which crosses over Interstate Highway 85. There is a shopping center at the interchange of I-85 and N. C. 56 which could serve as a stop for Greyhound. There is no reasonable alternative bus service to the Creedmoor/Butner community if Greyhound were permitted to discontinue service. Greyhound should be required to provide service at this interchange twice a day on a 12-month trial basis.

CONCLUSIONS

1. The Examiner concludes that Greyhound Lines, Inc., should be allowed to discontinue the routes set forth in its Petition filed in this docket on December 30, 1982, except as to certain service to the Creedmoor/Butner community.

G. S. 62-262(j) provides:

> "(j) After the issuance of a certificate or permit for the transportation of passengers, as provided in this section, such certificate or permit may thereafter be amended, changed or modified, by requiring the holder to furnish more or less transportation service, or by changing the routes over which service has been authorized, or by imposing other reasonable terms, conditions, restrictions, and limitations <u>as public convenience and necessity</u> or reasonable regulation of traffic upon the highways <u>may require</u>; provided, that the procedure in all such cases as to notice and hearing shall be the same as provided in this section for the issuance of a certificate or permit." (emphasis added)

"What constitutes 'public convenience and necessity' is primarily an administrative question with a number of imponderables to be taken into consideration . . ." <u>Utilities Commission</u> v. <u>Trucking Co</u>., 223 N.C. 687."

In <u>Utilities Commission</u> v. <u>Coach Co</u>., 260 N.C. 43 (1963), the Supreme Court further elaborated on the doctrine of public convenience and necessity:

> " . . . The doctrine of convenience and necessity is a relative or elastic theory. The facts in each case must be separately considered and from those facts it must be determined whether public convenience and necessity requires a given service to be performed or dispensed with. <u>The convenience and necessity required are those of the public and not of an individual or individuals</u>. . . ." (emphasis added)

In deciding that Greyhound's Petition should be allowed, the Examiner has carefully considered the following:

a. Lack of adequate passenger ridership. The uncontradicted evidence in this proceeding discloses that the number of passengers riding on Greyhound's buses is greatly insufficient to make the routes in question profitable for Greyhound. In most instances the ridership on the routes proposed to be discontinued averaged less than one passenger per bus. On the route with the most ridership - Raleigh to Charlotte - the ridership averaged less than six passengers per bus.

b. The unprofitability of the Greyhound routes in question. The uncontradicted evidence in this proceeding discloses that Greyhound's passenger revenues on each of these routes are substantially less than the variable costs incurred by Greyhound in providing service over the routes. (Variable costs include maintenance expense, drivers' wages, fuel and oil expense, depreciation, and fuel and social security taxes.) In fact, the revenue earned on most routes was insufficient even to pay for those costs related to drivers' wages and fuel expense.

c. Little or no attendance of public witnesses at the public hearings. The Commission scheduled hearings at nine localities across the State in order to take the testimony of the public. These locations were chosen to accommodate those persons who would be affected by Greyhound's Petition. The hearings were at Asheboro, Charlotte, Kings Mountain, Asheville, Winston-Salem, Creedmoor, Raleigh, Kenansville, and Buies Creek. A total of 11 public witnesses appeared at these hearings and testified.

Greyhound was required by the Commission to give notice of its Petition and the scheduled hearings by newspaper publication and by notices placed in the Company's buses and along its routes. The Petition and the hearings received considerable publicity in the media. (See Greyhound's exhibits of newspaper articles from the Winston-Salem area.) Attention is also especially called to the efforts of the Public Staff to ensure that the Petition and the scheduled hearings received widespread notice. The Staff wrote approximately 200 letters to members of the legislature, county commissioners, mayors, and officials at the chambers of commerce in the areas affected by the Petition.

Only in the Creedmoor area was there sufficient interest shown in the loss of bus service. This interest is more fully discussed below in Conclusion No. 2. Except for the Creedmoor area, the Examiner must conclude that there was insufficient public interest shown in the routes proposed to be abandoned by Greyhound.

d. The Bus Regulatory Reform Act of 1982. Greyhound's petition filed with the Commission on December 30, 1982, cited and quoted from a provision of the recently enacted Bus Regulatory Reform Act of 1982, 49 U.S.C. Sec. 10935. This legislation, which became effective on November 19, 1982, would permit Greyhound to seek direct review by the Interstate Commerce Commission of a decision of this Commission which denied, in whole or in part, the petition of Greyhound to discontinue service on the routes set forth in its petition of December 30, 1982.

The Act provides that the Interstate Commerce Commission must give "great weight" to the extent to which Greyhound's revenues from service on the routes proposed to be abandoned are less than the variable cost of providing the transportation. The Act also requires the Interstate Commerce Commission to consider whether the carrier is receiving or has an offer for financial evidence to continue the transportation, and whether there is any alternative bus transportation.

The Bus Regulatory Reform Act allows the State, within 120 days from the date the Petition is filed, to decide the Petition. This Commission must recognize the Act as an expression of national policy by the Congress with respect to the discontinuance of routes wholly within one state. In view of the uncontradicted evidence in this proceeding, and the overall lack of public interest in Greyhound's petition for discontinuance of service, the Examiner must conclude that Greyhound's petition should be allowed, except as provided hereafter for the Creedmoor/Butner community.

2. The Examiner concludes that Greyhound should provide service, on a 12-month trial basis, to the Creedmoor/Butner community by making a stop twice a day, in the morning and in the afternoon, at a suitable place in the shopping center at the interchange of I-85 and N. C. 56.

A number of community leaders in the Creedmoor/Butner area appeared at the hearings in Creedmoor and Raleigh and testified about the continued need for some type of Greyhound service in the community. These witnesses were Paula W. Ellington, representing the Creedmoor Chamber of Commerce; Thomas B. Curin, Executive Director of the Granville County Chamber of Commerce; Anthony Selton, President of the Butner Chamber of Commerce; and Merle Edwards, Clerk of the City of Creedmoor. In addition, the Commission also received letters opposing the Greyhound discontinuance from Senator William G. Hancock, Jr., 13th District; and John T. Stallings, Mayor of Creedmoor.

The witnesses generally expressed their concern about the effect the discontinuance of bus service would have on the institutions located at Butner, particularly the Alcoholic Rehabilitation Center. The witnesses also spoke of the general need for bus service between Creedmoor and Durham. No witness, however, testified about the number of passengers that would be expected to use Greyhound's buses into and out of the Creedmoor/Butner community. The witnesses did propose an alternative in the event the Commission approved the discontinuance of service to Creedmoor: that service be provided by Greyhound at the shopping center located at the interchange of I-85 and N. C. 56, which is two or three miles from Creedmoor. Butner is located adjacent to the interchange, and Greyhound's buses travel on I-85.

On April 15, 1983, the Public Staff filed a letter in this docket pointing out the significant public interest in resistance to the discontinuance of Route 29 relating to Creedmoor and Butner. The Public Staff further pointed out that service to the Alcoholic Rehabilitation Center and the surrounding communities is much needed and the Public Staff requested the Commission to direct that such service be continued.

In view of the considerable testimony from the Creedmoor/Butner area, and the support of the Public Staff as stated in its letter filed April 15, 1983, the Examiner is of the opinion that Greyhound should be required to provide

service, on a 12-month trial basis, to the Creedmoor/Butner community by making a stop twice a day, in the morning and in the afternoon, at a suitable place in the shopping center at the interchange of I-85 and N.C. 56.

3. The Examiner further concludes that Greyhound should give notice to its passengers affected by this Order of the discontinuances authorized herein and of any alternative transportation that may be available to them.

David King, the Director of the Public Transportation Division of the North Carolina Department of Transportation (NCDOT), attended the hearings scheduled by the Commission throughout the State and testified at the hearing in Raleigh. Mr. King advised the Commission of the programs administered by NCDOT and the counties that might be available to passengers adversely affected by the discontinuances authorized by this Order. Mr. King stated, in part:

> "The other point I would like to make for the record is that State government as a whole in the last half dozen years has been attempting to coordinate all of the human service transportation which is available usually at the county-wide level throughout North Carolina. Virtually every county in the State has some transportation being provided by organizations such as Council on Aging, Department of Social Service, Sheltered Workshops, Community Action Organization and so forth. The policy of the State and this administration in particular has been to get those organizations to provide that transportation jointly, cooperatively and in a number of cases that transportation service is provided by one entity on behalf of all the others in the county. Those situations offer us perhaps some possibilities for dealing with some of the problems that might result should these abandonments in some cases be allowed to occur."

Mr. King offered to work with Greyhound in preparing notices which would advise the passengers of possible alternative transportation in their communities.

The Examiner recognizes that, notwithstanding of the overall lack of public interest in Greyhound's petition to discontinue service, as evidenced by the sparse attendance at the hearings, there will be some individuals throughout the State who will be adversely affected by the discontinuance. For example, Thomas H. Edwards, Jr., Route 3, Wake Forest, North Carolina, appeared at the Raleigh hearing and testified that he used Greyhound service to come to Raleigh and purchase groceries and see his doctor. Mr. Edwards stated that he had been riding the Greyhound buses once or twice a week for more than 30 years and that the bus service was his only means of transportation. Julian Mangum, also of Route 3, Wake Forest, North Carolina, testified that he has been riding the Greyhound buses to his work in Raleigh since 1950 and that he has no other means of transportation. (These two witnesses were the only witnesses at any of the nine hearings in this proceeding who testified that they regularly rode Greyhound's buses and depended on them for transportation.) Mr. King suggested that Wake County may have a transportation program available for these two witnesses.

The Examiner concludes that Greyhound should seek the assistance of Mr. King and his agency in preparing notices advising those Greyhound passengers affected by this Order of any alternative transportation that may be available to them.

The Examiner will also request Mr. Randy Royal, Transportation Administrator for Wake County, to look into the transportation needs of Mr. Edwards and Mr. Mangum and determine if any alternative transportation is available for these two regular users of Greyhound service.

IT IS, THEREFORE, ORDERED as follows:

1. That, except as provided in Ordering Paragraph 2 below, the petition to discontinue intrastate motor bus transportation filed by Greyhound Lines, Inc., on December 30, 1982, be, and the same is hereby, allowed, such discontinuance to become effective on 60 days notice to the Commission from and after the final and effective date of this Order.

2. That Greyhound Lines, Inc., shall provide bus passenger and package express service, on a 12-month trial basis, to the Creedmoor/Butner community by making two stops a day, once in the morning in a southerly direction and once in the afternoon in a northerly direction, at some suitable place in the shopping center located at the interchange of Interstate Highway 85 and North Carolina Highway 56 in Granville County, North Carolina. Greyhound shall file with the Commission, no later than 20 days after the effective date of this Order, its proposed timetable and stopping point with respect to the service ordered herein. The service ordered herein shall not begin later than at the expiration of the discontinuance of service authorized by ordering paragraph No. 1 above. In complying with this paragraph, Greyhound should give particular consideration to the use of its southerly schedule 1011 and its northerly schedule 1040 or times comparable thereto. Greyhound shall not discontinue the service ordered by this paragraph without first obtaining approval of the Commission to do so. Greyhound's request to discontinue service shall be accompanied by operating statistics for the 12-month period, including ridership and express revenue.

3. That, within 5 days from the effective date of this Order, Greyhound shall call upon David T. King, Director of the Public Transportation Division of the North Carolina Department of Transportation, and seek the assistance of Mr. King and his office in preparing notices advising Greyhound's passengers of the discontinuance of service authorized by this Order and describing alternative transportation services that may be available to these passengers. Greyhound shall distribute these notices to passengers boarding or alighting its buses at locations at which service will be discontinued, such distribution to begin at least 30 days prior to the date that service is to be discontinued under this Order. The expense of preparing and distributing these notices shall be borne by Greyhound.

4. That the Transportation Administrator of Wake County, Mr. Randy Royal, is requested to investigate the transportation needs of Mr. Thomas H. Edwards, Jr., and Mr. Julian Mangum, both of whom are residents of Wake County and who will lose bus service under this Order, and determine if alternative transportation services are available for these two persons. The address of Mr. Edwards is as follows:

Mr. Thomas H. Edwards, Jr.
Route 3, Box 278
Wake Forest, North Carolina 27587

The address of Mr. Mangum and the telephone number at which he can be reached is as follows:

Mr. Julian Mangum
Route 3, Box 218
Wake Forest, North Carolina 27587

Telephone Number: (919) 556-2741

5. That exceptions to this Recommended Order shall be filed with the Commission as stipulated to by the parties on or before Thursday, April 21, 1983.

6. That this Recommended Order shall become effective and final on Friday, April 29, 1983.

7. That a copy of this Order shall be mailed to the following persons:

The Honorable John T. Stallings
Mayor of Creedmoor
P. O. Box 765
Creemoor, North Carolina 27522

Ms. Annette Jordan
Courier Tribune
P. O. Box 340
Asheboro, North Carolina 27203

Mr. Phil Gurkin
P. O. Box 1448
Dunn, North Carolina 28334

ISSUED BY ORDER OF THE COMMISSION.
This the 19th day of April 1983.

NORTH CAROLINA UTILITIES COMMISSION
Sandra J. Webster, Chief Clerk

(SEAL)

DOCKET NO. T-192, SUB 8

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of		
Pilot Freight Carriers, Inc., Post Office Box 27153, Winston-Salem, North Carolina 27153-0000 - Application to Amend Certificate No. C-1146	)))	ORDER RULING ON EXCEPTIONS AND AFFIRMING RECOMMENDED ORDER

HEARD IN: The Commission Hearing Room, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina 27603 on Monday, March 7, 1983, at 2:00 p.m.

BEFORE: Chairman Robert K. Koger and Commissioners Leigh H. Hammond, Sarah Lindsay Tate, John W. Winters, Edward B. Hipp, A. Hartwell Campbell, and Douglas P. Leary

APPEARANCES:

For the Applicant:

Ralph McDonald, Bailey, Dixon, Wooten, McDonald & Fountain, Attorneys at Law, Post Office Box 2246, Raleigh, North Carolina 27602
For: Pilot Freight Carriers, Inc.

For the Protestants:

Thomas W. Steed, Jr., Moore, Van Allen & Allen, Attorneys at Law, Post Office Box 2058, Raleigh, North Carolina 27602
For: Fredrickson Motor Express Corporation
Bruce Johnson Trucking Company, Inc.
Estes Express Lines
Overnite Transportation Company

BY THE COMMISSION: On June 26, 1982, Pilot Freight Carriers, Inc. (Applicant) filed an application seeking to amend the description of territory in its common carrier certificate No. C-1146 to read as follows:

"Transportation of general commodities, except those requiring special equipment and except commodities in bulk, in tank vehicles, over irregular routes, statewide."

On October 5, 1982, a joint protest and motion for intervention was filed by Fredrickson Motor Express Corporation; Bruce Johnson Trucking Company, Inc.; Estes Express Lines; and Overnite Transportation (Protestants). An Order was entered permitting intervention on October 11, 1982.

The application was heard on October 28, 1982, before Hearing Examiner Robert P. Gruber; and a Recommended Order Granting Application was issued by the Hearing Examiner on January 5, 1983.

On January 19, 1983, Protestants filed Exceptions to Recommended Order Granting Authority setting forth Exceptions 1 - 21 and various reasons and arguments in support thereof. Protestants requested oral argument and counsel

For the parties presented oral argument to the Commission at the time and place indicated above.

Upon consideration of the entire record in this proceeding, the Commission is of the opinion that the Exceptions of the Protestants should be decided as follows:

1. Exception 1 should be upheld, and the last sentence of Finding of Fact No. 11 should be modified to read:

"At one time it used Estes, Fredrickson, and Overnite, but it stopped using Fredrickson and Overnite because of service problems and Estes has not solicited Torpedo Wire's freight in the past two years."

However, sustaining this Exception does not require reversal of the Recommended Order.

2. Several findings of fact are to the effect that Protestants have not solicited the business of the shippers supporting the Applicant. Exceptions 3, 5, 8, 9, 11, and 14 challenge these findings. Protestants argue that so long as they participate in published tariffs, actively engage in transportation business and conduct "reasonable marketing activities," shippers should be required to seek out them, rather than they be required to solicit the shippers.

Initially, we note that there is sufficient evidence in the record to support each of the findings of fact challenged by these Exceptions. Indeed, the Protestants do not challenge the sufficiency of the evidence. Instead, their Exceptions raise the issue of whether such findings may properly be considered in determining whether additional authority should be granted. We overrule the Exceptions. First, we note that the protestants' attorney did not object at the hearing to the evidence that supports these findings. Second, we believe that the shipping public's awareness of available service is relevant to whether there is a public need for additional service. We cannot fix any flat rule establishing the extent of the carriers' duty to solicit shippers or the shippers' duty to seek out carriers. Evidence of both types might be presented and considered. To rule on the present Exceptions, we need only hold that the level of existing carriers' solicitation programs - as well as the level of their advertising - is relevant evidence, to be considered along with other evidence bearing on the public need for additional service. See Masters v. Public Utilities Commission, 45 Ohio St. 2d 207 (1976).

It is clear from examining the transcript and the Recommended Order herein, that the Hearing Examiner did not rely solely upon the findings of fact now challenged in granting the application. We hold that he properly considered these findings, along with other factors bearing on the public convenience and necessity, and that the present Exceptions should be overruled.

3. The remaining Exceptions should be overruled and denied.

4. The Recommended Order should be affirmed.

IT IS, THEREFORE, ORDERED:

1. That Exception 1 should be upheld and Finding of Fact 11 should be modified as indicated above.

2. That the Recommended Order, as so modified, should be, and the same hereby is, affirmed.

ISSUED BY ORDER OF THE COMMISSION.
This the 1st day of April 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sharon Credle Miller, Deputy Clerk

DOCKET NO. T-1287, SUB 37

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of	
Harper Trucking Company, Inc., Post Office Box 25868, Raleigh, North Carolina 27611 - Complaint against Fredrickson Motor Express Corporation and Standard Trucking Company	) ORDER REVERSING RECOMMENDED ORDER IN PART AND DEFERRING RULING IN PART

HEARD IN: The Hearing Room of the Commission, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina on Monday, August 23, 1983, at 11:00 a.m.

BEFORE: Chairman Robert K. Koger, Presiding, and Commissioners Leigh H. Hammond, Sarah Lindsay Tate, John W. Winters, Edward B. Hipp, A. Hartwell Campbell, and Douglas P. Leary

APPEARANCES:

For the Complainant:

Ralph McDonald, Bailey, Dixon Wooten, McDonald & Fountain, Attorneys at Law, P.O. Box 2246, Raleigh, North Carolina 27602
For: Harper Trucking Company

For the Respondents:

Joseph W. Eason, Allen, Steed and Allen, P.A., Attorneys at Law, Suite 701 BB&T Building, Post Office Box 2058, Raleigh, North Carolina 27602
For: Fredrickson Motor Express Corporation
Standard Trucking Company

BY THE COMMISSION: On July 2, 1982, Robert P. Gruber, Hearing Examiner, issued a Recommended Order in this docket dismissing the Complaint of Harper Trucking Company, Inc., and Intervenor Estes Express Lines. (Estes was permitted to intervene in this docket upon its assertion that its interests in this proceeding were identical to those of Harper.)

On July 19, 1982, Harper Trucking Company, Inc., filed its Exceptions to the Recommended Order of Hearing Examiner Gruber and requested that the Exceptions be set for Oral Argument before the full Commission. These Exceptions were scheduled for Oral Argument before the full Commission on August 23, 1982. At the oral argument, the Commission heard argument from counsel for the Complainant and the Defendants.

After considering the Recommended Order of July 2, 1982, the Exceptions, and the evidence of record, and the Oral Argument of counsel on Exceptions, the Commission is of the opinion and so concludes that the Recommended Order should be reversed and modified to the extent hereinafter set out.

The Commission finds and concludes that the following Conclusions of Law made by the Examiner are in error: Conclusions No. 3 and No. 5. These

Conclusions were challenged by Harper's Exceptions numbered 11, 12, 13, and 17. Conclusion No. 3 reads as follows:

"3. A public utility has the right to complain to this Commission on any of the grounds upon which complaints are allowed to be filed by other parties. However, complaints may be made by any person having an interest in any act or thing done or omitted to be done by any public utility, if and only if such person has a direct interest in the subject matter of the act or thing done or omitted by the public utility, or if such person is acting as a representative of any person having such a direct interest in the subject matter of the complaint. N.C. Gen. Stat. 62-73; 62-74; 62-136. The Commission, in its discretion, may investigate allegedly discriminatory rates of motor carriers on its own motion or the complaint of any person, but only persons with 'direct interests' are entitled to adjudication on that issue. Carolina Motor Service, Inc. v. Atlantic Coastline Railroad Co., 210 N.C. 36, 185 S.E. 479 (1936); N.C. Gen. Stat. 62-146(e) and 147(c)."

Conclusion No. 5 reads as follows:

"5. Neither Harper nor Estes has a direct interest as to whether the rates charged or services rendered by Fredrickson or Standard constitute an unreasonable preference or advantage to any person or subject any person to any unreasonable prejudice or disadvantage, nor do Harper or Estes have a direct interest as to whether the issue tariffs of Fredrickson or Standard establish or maintain any unreasonable difference as to rates or services either as between localities or as between classes of service. Estes and Harper, therefore, are not real parties in interest and are not entitled to an adjudication of this issue. It is shippers and not competing carriers who would be the parties aggrieved by discriminatory rates. Carolina Motor Service, Inc. v. Atlantic Coastline Railroad Co., 210 N.C. 36, 185 S.E. 479 (1936).

In lieu of Conclusions Nos. 3 and 5, the Commission makes the following

CONCLUSION OF LAW

The Complainants Harper Trucking Company, Inc., and Estes have standing to complain with respect to the Respondents' revenue incentive discount tariffs. G.S. 62-146(e) provides that any person may complain to the Commission in writing that a proposed or existing rate violates the provisions of the Public Utilities Act. G.S. 62-3(21) defines "person" to include, *inter alia*, a corporation.

Furthermore, this Commission has plenary authority under G.S. 62-146(e), G.S. 62-30, G.S. 62-32, G.S. 62-73, G.S. 62-80, and G.S. 62-136, upon its own motion, to investigate proposed or existing rates of any public utlity subject to its jurisdiction. By issuing its Order of January 20, 1982, scheduling a hearing in this docket, this Commission exercised such authority.

In any event, Respondents have had adequate notice and a full and fair hearing. As this proceeding originated as a complaint

proceeding, Complainants rather than Respondents have been charged with the burden of proof. All parties have had the opportunity to present evidence and arguments with respect to the issues in this proceeding - whether the rates in question violate the provisions of G. S. Chapter 62.

The remaining Exceptions of the Complainants relate to the Findings and Conclusions of the Examiner with respect to the issue whether the revenue incentives discount tariffs of Fredrickson and Standard under consideration in this docket violate any of the provisions of G.S. Chapter 62. These Exceptions are numbered 1 -10, 14 - 16, and 18. The Examiner had found and concluded that the tariffs did not violate Chapter 62 and the Complaint was accordingly dismissed. The Commission is of the opinion that a ruling on these Exceptions should be deferred for the reasons hereafter set forth.

There is now pending before the Commission the application of the North Carolina intrastate motor common carriers of general commodities for general increases in rates and charges. Docket No. T-825, Sub 275. On February 1, 1983, the Commission issued in this docket its Order of Suspension and Investigation - Notice of Hearing. Paragraph 8 of that Order directed the respondent carriers to furnish certain information and data as follows:

"8. That respondents be, and the same are hereby, instructed to furnish, on or before April 28, 1983, the Commission with information showing earned revenue dollars and the revenue dollars, identified by specific categories, which have been allowed, returned or granted to shippers due to all rate and revenue incentive discounts by volume, aggregate tender, promotional, handling allowances and any other revenue reduction provisions initiated by all carriers participants in the tariffs publishing the increases proposed in this proceeding and of respondent carriers parties to any and all other tariffs of a similar nature involving North Carolina intrastate transportation of general commodities for the calendar years 1981, 1982, and for the months of January, February, and March of 1983."

The scope of the information required by Ordering Paragraph 8 would include the tariffs of Fredrickson and Standard under consideration in the Harper complaint docket, T-1287, Sub 37.

It appearing to the Commission that the revenue and volume incentive discount tariffs of the general commodity carriers, including Standard and Fredrickson, are to be a matter of investigation in the general commodities rate increase docket, the Commission is of the opinion, and so concludes, that it should defer ruling on the rest of Harper's exceptions pending the final determination of the issues in the general commodities rate docket.

IT IS, THEREFORE, ORDERED as follows:

1. That the Exceptions of Harper Trucking Company filed July 19, 1982, and numbered 11, 12, 13, and 17, all of which relate to the standing of the Complainants to institute the Complaint, are hereby allowed, as hereinabove set forth.

2. That a determination of the remaining Exceptions of Harper Trucking Company, which are numbered 1 - 10, 14 - 16, and 18, is hereby deferred

pending the final determination of the general commodities rate case, Docket No. T-825, Sub 275.

ISSUED BY ORDER OF THE COMMISSION.
This the 1st day of April 1983.

NORTH CAROLINA UTILITIES COMMISSION
Sharon Credle Miller, Deputy Clerk

(SEAL)

DOCKET NO. T-825, SUB 248

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of	
Intrastate Fuel Surcharges Applicable to Transportation Rates and Charges of North Carolina Motor Carriers of Passengers and Property	) ORDER ADJUSTING) SURCHARGE AND) PERMITTING ROLL-IN

HEARD IN: Commission Hearing Room, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina, on March 25, 1983

BEFORE: Commissioner Edward B. Hipp, Presiding; Chairman Robert K. Koger and Commissioner Leigh H. Hammond

APPEARANCES:

For the Applicant:

Joseph W. Eason, Moore, Van Allen, and Allen, Attorneys at Law, P.O. Box 2058, Raleigh, North Carolina 27602
For: North Carolina Motor Carriers Association

For the Intervenors:

Theodore Brown, Staff Attorney, Public Staff - North Carolina Utilities Commission, P.O. Box 991, Raleigh, North Carolina 27602
For: The Using and Consuming Public

BY THE COMMISSION: On March 1, 1983, the Public Staff, North Carolina Utilities Commission filed Motion for Hearing requesting hearing for the purpose of determining the appropriate fuel surcharge requirements for the asphalt, petroleum, and bulk commodity carriers. On March 10, 1983, the Commission set the matter for hearing on Friday, March 25, 1983. Thereafter, the North Carolina Motor Carriers Association, Inc. (NCMCA), on behalf of those such carriers which participate in the NCMCA's tariffs, moved that the Commission adjust their intrastate fuel surcharge, that the Commission permit the bulk carriers to roll-in the adjusted fuel surcharge into the permanent rates, and that the Commission revise provisions of NCUC Rule R2-16.1 to permit the bulk carriers' future fuel surcharges to be expressed on a per mile basis rather than as a percentage of rate revenue. The matter came on for hearing before the Commission at the time and place scheduled above. Based upon all matters of record and the stipulations of parties at the aforesaid hearing, the Commission makes the following:

FINDINGS OF FACT

1. The bulk carriers are currently charging and collecting a 12.5% intrastate fuel surcharge pursuant to this Commission's Orders in this Docket dated June 14 and 15, 1982.

2. On April 1, 1983, federal fuel taxes are scheduled to increase by $.05 per gallon.

3. The verified fuel surcharge reports applicable to bulk carriers establish that the bulk carriers' fuel surcharge should be adjusted to 8.2%, as computed by the Public Staff in accordance with NCUC Rule R2-16.1, after taking the federal tax increase into consideration.

4. The bulk carriers request to roll their presently effective fuel surcharge into their general rates uniformly across all mileage brackets is just and reasonable.

5. The roll-in of the bulk carriers' fuel surcharge into their general rates does not require a determination of the entire rate structure or their overall rate of return.

6. The procedures adopted by the Commission for determining a fuel surcharge should be retained in the event emergency situations develop in the future requiring this Commission to act promptly in establishing a new fuel surcharge for bulk carriers or other carriers.

7. That representatives of the Public Staff and the bulk carriers should submit a proposed revision of NCUC Rule R2-16.1 which will permit the bulk carriers to express their intrastate fuel surcharge as a per mile charge in the future.

8. The bulk carriers should not be required to file fuel surcharge reports after the roll-in referred to hereinabove until such time as it becomes necessary for the bulk carriers to actually charge and collect a fuel surcharge.

9. The roll-in of the bulk carriers' adjusted fuel surcharge should be allowed to become effective on April 1, 1983, on one day's notice to the public, after appropriate tariffs, supplements, or reissues thereof are filed with this Commission in accordance with its rules and the Public Utilities Act.

Upon the foregoing Findings of Fact, the Commission makes the following:

CONCLUSIONS OF LAW

1. This proceeding is not a general rate case and does not involve questions which require a determination of the entire rate structure and overall rate of return. (North Carolina G.S. 62-137)

2. Under NCUC Rule R2-16.1, the bulk carriers' present fuel surcharge of 12.5% should be adjusted to 8.2%, taking into consideration the $.05 per gallon federal fuel tax increase to become effective on April 1, 1983. This conclusion was supported by both the carriers and the Public Staff at the hearing.

3. The bulk carriers should be permitted to roll the adjusted fuel surcharge of 8.2% into their general rates as supported by both the Public Staff and the carriers at the hearing.

4. The Public Staff and the bulk carriers both supported a change in any future fuel surcharge mechanism for the bulk carriers. The change would result in the fuel surcharge being calculated on a per mileage basis. The

Commission concludes that this is an appropriate modification and that the Public Staff and the bulk carriers should develop and propose to this Commission a revision to NCUC Rule R-2-16.1, incorporating this modification.

IT IS, THEREFORE, ORDERED as follows:

1. That the North Carolina intrastate fuel surcharge applicable to motor carriers of asphalt, petroleum, cement, and other bulk commodities be, and hereby is, adjusted from 12.5% to 8.2%.

2. That the North Carolina intrastate carriers of asphalt, petroleum, cement, and other bulk commodities be, and hereby are, authorized to roll the intrastate fuel surcharge of 8.2% into their general rates as a uniform percentage increase across all mileage brackets.

3. That the adjustment and roll-in of the North Carolina intrastate fuel surcharge as described above shall become effective on April 1, 1983, on one day's notice to the public upon filing of appropriate tariffs, supplements, or reissues thereof with this Commission in accordance with the Public Utilities Act and the rules of this Commission.

4. That the Public Staff and the North Carolina intrastate carriers of asphalt, petroleum, cement, and other bulk commodities be, and hereby are, reuqested to develop and propose to this Commission a revision of NCUC Rule R2-16.1 which will permit such carriers to express any future intrastate fuel surcharges on a per mile basis in lieu of expressing such a surcharge as a percent of revenue.

ISSUED BY ORDER OF THE COMMISSION.
This the 31st day of March 1983.

NORTH CAROLINA UTILITIES COMMISSION
Sharon Credle Miller, Deputy Clerk

(SEAL)

DOCKET NO. T-825, SUB 248

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Intrastate Fuel Surcharge Applicable to Transportation Rates and Charges of North Carolina Motor Carriers of Passengers and Property) RECOMMENDED ORDER APPROVING 8.6% FUEL SURCHARGE, APPROVING CHANGE IN RULE R2-16.1 AND APPROVING FORMS

HEARD IN: The Commission Hearing Room, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina, on Tuesday, February 2, 1983

BEFORE: Wilson B. Partin, Jr., Hearing Examiner

APPEARANCES:

For the Applicant:

David H. Permar, Hatch, Little, Bunn, Jones, Few & Berry, Attorneys at Law, Post Office Box 527, Raleigh, North Carolina
For: Tobacco Transporters Association

For the Public Staff:

Theodore C. Brown, Jr., Staff Attorney, Public Staff - North Carolina Utilities Commission, Post Office Box 991, Raleigh, North Carolina 27602
For: The Using and Consuming Public

PARTIN, HEARING EXAMINER: On September 2, 1982, the Tobacco Transporters Association (TTA) filed a motion to revise the fuel surcharge reports. Thereafter, on October 18, 1982, the Public Staff filed a reply and requested that a hearing be set. On October 21, 1982, the Tobacco Transporters Association filed a reply to the motion for a hearing also requesting that a hearing be set. There is also pending in this docket a motion by the Tobacco Transporters Association that Rule R2-16.1(k) be modified to allow a roll-in of the fuel surcharge in the context of a general rate case proceeding for tobacco carriers.

After several continuances, the matter came on for hearing on February 1, 1983. At the hearing, the tobacco carriers requested that their pending roll-in motion be considered in this hearing. The Public Staff indicated that although they opposed the motion, they did not object to the matter being heard at this time.

Thereafter, the Public Staff presented the testimony of David A. Poole, Staff Accountant with the Transportation Rates Division, Public Staff - North Carolina Utilities Commission. The tobacco carriers presented the testimony of Harvie A. Carter, Traffic Manager for Epes Transport System and the coordinator for the fuel surcharge reports for the Tobacco Transporters Association, and Douglas E. Leckie, III, Treasurer of Burton Lines, Inc.

The tobacco carriers' witnesses testified that the present report forms were inadequate, chiefly because of the lack of data in the report forms relative to Owner/Operators, who transport the majority of the traffic. On this point, the Public Staff agreed that Owner/Operators should be included, but disagreed as to the methodology to be used and the exact form of a new revised fuel surcharge report. The tobacco carriers and the Public Staff agreed to meet within two weeks following the hearing to see if they could work out their differences relating to the form of the fuel surcharge reports and jointly submit proposed modifications.

The tobacco carriers presented evidence indicating that in November 1982 the required percentage for the fuel surcharge utilizing currently approved forms produced a percentage fuel surcharge requirement of 11.6% and with the changes in form suggested by the tobacco carriers, the percentage should be 12.3%.

The Public Staff presented evidence showing that utilizing the current form for the month of December 1982, the required fuel surcharge is 8.6¢ after the pro forma adjustment provided for in the existing rule. Further, the Public Staff presented evidence which showed that fuel surcharge needs, based strictly on Commission Rule R2-16.1, the Tobacco Transporters Association proposed forms, and the forms proposed by the Public Staff, have not amounted to 15% since June 1982 when the Commission order was issued approving the 15% fuel surcharge.

At the conclusion of the hearing, the Hearing Examiner asked the parties to meet and attempt to decide on a fuel surcharge report form for the tobacco carriers. On February 16, 1983, James C. Turner of the Public Staff and Harvey Carter, Secretary-Treasurer of the Tobacco Transporters Association, filed a joint report on the results of their meeting. The parties agreed on the forms to be used by the carriers in filing for a fuel surcharge. The parties also recommended that the language in paragraph (a) of Rule R2-16.1 be amended to read as follows:

> "(a) The cost study carriers set forth in Attachment C to this rule, except tobacco carriers, during any period a fuel surcharge is in effect for such group, shall file on or before the 25th day of each month a fuel surcharge report in the form of Attachments A and B to this rule. The tobacco carriers, during any period a fuel surcharge is in effect for its group, shall file a fuel surcharge report each month in the form of Attachments A (Tobacco) and B (Tobacco) to this rule on or before the 5th day of the second month following the reported month."

A copy of the entire report filed by the parties is attached to this Order. The parties also agreed that the Commission defer any decision on the feasibility of the proposed fuel surcharge roll-in" until such time as the Tobacco Transporters Association files its next rate increase.

Based upon the evidence presented at the hearing, and the entire record in this docket, the Commission now reaches the following

FINDINGS OF FACT

1. The Tobacco Transporters Association, through its member carriers, is currently engaged in the transportation of traffic under Tariff 8 in North Craolina intrastate commerce.

2. The tobacco carriers in North Carolina are currently assessing a 15% fuel surcharge on Tariff 8 traffic.

3. The determination of the appropriate fuel surcharge for the tobacco transporters in this proceeding is governed by the present NCUC Rule R2-16.1.

4. The current fuel surcharge need, as properly determined by the application of Rule R2-16.1, is 8.6%.

5. The present Rule R2-16.1 and the tobacco carrier forms required therein should be revised pursuant to Exhibit A attached hereto.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NOS. 1, 2, AND 3

The evidence supporting these Findings of Fact is contained in the parties' motions and in prior Commission Orders in this docket of which the Commission takes judicial notice. These Findings of Fact are essentially informational, procedural, and jurisdictional in nature and the matter which they involve are essentially uncontested. The 15% fuel surcharge on Tariff 8 Traffic was set by Order dated June 16, 1982, in this docket.

The methodology used by the Interstate Commerce Commission (ICC) to set its fuel surcharge is not the same as is found in NCUC Rule R2-16.1. It would be inappropriate to set North Carolina fuel surcharge rates based upon ICC's fuel surcharge justification. The Commission concludes that the use of NCUC Rule R2-16.1 to set current fuel surcharges is proper in this proceeding.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NOS. 4 AND 5

At the February 1, 1983, hearing the Public Staff presented evidence that the current fuel surcharge requirement, based on the appliction of Rule R2-16.1, was 8.6%. The 8.6% requirement was based on fuel surcharge data filed by the tobacco carriers for the month of December 1982 adjusted according to the provisions of paragraph (i) of said rule. The Commission agrees with Public Staff testimony that the original intent of the paragraph (i) adjustment was to provide a mechanism of updating the reported fuel price to the most recent fuel price conditions at the time of an application for adjustment or at the time of a hearing set to determine appropriate rate levels. The current procedures used by R2-16.1 for determining fuel surcharge requirements are the most reliable and accurate procedures at this time, even though there was evidence presented by the Public Staff and the Tobacco Transporters Association at the hearing that the rule has some inequities.

Based on the evidence presented by the Public Staff and the TTA at the hearing, the Commission concludes that the current 15% rate is excessive.

The Commission further concludes that the 15% rate should immediately be reduced to 8.6%, which is the level determined by proper application of Rule R1-16.1. Rule R1-16.1 is the only authority by which this Commission can adjust fuel surcharge.

Further, the Commission concludes that the rule and its attachments should be revised only as to the tobacco carriers for future applications of said rule.

Upon consideration of the joint recommendations filed by the parties on February 16, 1983, pursuant to the Hearing Examiner's request, the Commission concludes that the recommendations and the forms set forth in Appendix A attached hereto should be adopted for use in future tobacco carrier fuel surcharge determinations and that Rule R2-16.1 should be amended accordingly.

IT IS, THEREFORE, ORDERED as follows:

1. That the tobacco carriers shall issue tariff supplements within three (3) days of the effective date of this Order reflecting a reduction of the fuel surcharge percentage from 15% to 8.6%, said tariff to become effective on one day's notice on June 1, 1983.

2. That Rule R2-16.1 be and the same hereby is amended to read as follows:

"(a) The cost study carriers set forth in Attachment C to this rule, except tobacco carriers, during any period a fuel surcharge is in effect for such group, shall file on or before the 25th day of each month a fuel surcharge report in the form of Attachments A and B to this rule. The tobacco carriers, during any period a fuel surcharge is in effect for its group, shall file a fuel surcharge report each month in the form of Attachments A (Tobacco) and B (Tobacco) to this rule on or before the 5th day of the second month following the reported month."

3. That the forms and recommendations agreed to by the parties in their report of February 16, 1983, which is attached to this Order as Appendix A, and incorporated herein by reference, is hereby approved.

ISSUED BY ORDER OF THE COMMISSION.
This the 5th day of May 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sandra J. Webster, Chief Clerk

*NOTE: Corrected by Errata Order dated May 11, 1983.

NOTE: Please refer to the official files in the office of the Chief Clerk for Exhibit A and Attachments A and B.

DOCKET NO. T-825, SUB 275

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Motor Common Carriers - Proposed General Increases in Rates and Charges Applicable on Shipments of General Commodities, Including Minimum Charges) ORDER GRANTING INCREASE

HEARD IN: The Hearing Room of the Commission, Dobbs Building, Raleigh, North Carolina, on June 21 and 22, 1983

BEFORE: Commissioner Sarah Lindsay Tate, Presiding; and Commissioners A. Hartwell Campbell and Douglas P. Leary

APPEARANCES:

For the Applicants:

Thomas W. Steed, Jr., and Joseph W. Eason, Moore, Van Allen and Allen, Attorneys at Law, P.O. Box 2058, Raleigh, North Carolina 27602
For: Motor Carriers Traffic Association, Inc., North Carolina Motor Carriers Association, Inc., and Southern Motor Carriers Rate Conference, Inc., and their respective motor common carrier participants

John W. Joyce and Sherman D. Schwartzberg, 1307 Peachtree Street, N. E., Atlanta, Georgia 30309
For: Southern Motor Carriers Rate Conference, Inc., and participants in Tariff NCUC SMC 304-C

For the Intervenors:

Theodore C. Brown, Jr., Public Staff Attorney, Public Staff - North Carolina Utilities Commission, P.O. Box 991, Raleigh, North Carolina 27602
For: The Using and Consuming Public

BY THE COMMISSION: The motor common carriers of general commodities which participate in tariffs issued by Motor Carriers Traffic Association, Inc. (MCTA), North Carolina Motor Carriers Association, Inc. (NCMCA), and Southern Motor Carriers Rate Conference, Inc. (SMCRC), have filed with the Commission the following tariff publications:

1. Supplement No. 26 to Tariff No. 304-D N.C.U.C. No. 304-D issued by Southern Motor Carriers Rate Conference, Inc., on behalf of its participating carriers, said supplement bearing an issue date of December 30, 1982, with a scheduled effective date of February 14, 1983.

2. Supplement No. 38 to Motor Freight Tariff No. 10-I, N.C.U.C. No. 129 issued by North Carolina Motor Carriers Association, Inc., Agent on behalf of its participating carriers, said supplement bearing an issue date of January 14, 1983, with a scheduled effective date of February 14, 1983.

3. Supplement No. 66 to Tariff No. 3-K, N.C.U.C. No. 47 issued by Motor Carriers Traffic Association, Inc., on behalf of its participating carriers, bearing an issue date of January 14, 1983, with a scheduled effective date of February 14, 1983.

Each of the above-described tariff publications reflect proposed increases on all rates and charges on North Carolina Intrastate Class, Commodity, Distance or Mileage Commodity, Exception Rates, Minimum Charges, Accessorial Charges and Accessorial Rates as follows:

Category	Increase (See Note A)
Minimum charges	$2.00 per shipment
LTL or AQ rates:	
On shipments weighing less than 5,000 pounds	8 percent
On shipments weighing 5,000 pounds or more	4 percent
Volume or TL rates	3 percent
Accessorial charges or accessorial rates	8 percent

NOTE A - Minimum increase of 3 cents. Fractions to be disposed of in accordance with Item 565 of NMFC.

Simultaneously with the filing of its tariff publication, SMCRC filed its Application and Justification for the proposed increased rates and charges setting out evidence and data justifying the need of the North Carolina intrastate general commodity traffic carriers for rate relief. The cost-update ratios and cost-revenue analysis and comparisons supporting the proposed increases are based upon 1981 traffic study data of six cost study carriers, five of which participate in the SMCRC Continuing Traffic Study.

Simultaneously with the filing of their respective tariff publications, NCMCA and MCTA each filed an Application and Motion for Intervention and Consolidation requesting that the three tariff publications be consolidated in a single docket for the purpose of investigation and hearing. In addition, NCMCA and MCTA both adopted and incorporated into each of their Applications the justification data filed on behalf of SMCRC in its Application and Justification, and advised this Commission that each was in the process of compiling cost-revenue comparisons based upon the operating and financial results of the designated cost-study carriers for NCMCA and MCTA identified in this Commission's proposed Rule R1-17(j) promulgated on November 23, 1982, in Docket No. M-100, Sub 90, which cost-revenue comparisons would be filed in further justification and support of the proposed increased rates and charges.

On February 1, 1983, the Commission issued its Order of Suspension and Investigation - Notice of Hearing in which it suspended the operation of the three tariff schedules, declared the matter to constitute a general rate case under N. C. General Statute 62-137, requested the Public Staff to investigate and analyze the proposed tariff filings, made the motor carrier parties to the proposed tariff publications Respondents in the proceeding, instructed the Respondents to furnish the information required by Commission Rule R1-17 on or before April 28, 1983, and set the matter for hearing on June 28, 1983. By Order issued on March 4, 1983, the Commission changed the hearing date until June 21, 1983.

In its Order of Suspension and Investigation of February 1, 1983, the Commission had in paragraph No. 8 instructed the Respondents to furnish on or before April 28, 1983, certain data and information relating to incentive discounts involving North Carolina intrastate transportation of general commodities. On April 5, 1983, SMCRC filed a Petition for Modification of Commission Order requesting that said paragraph No. 8 be rescinded for reasons stated therein. The Public Staff filed a Reply to the SMCRC petition on April 22, 1983, and by Order dated April 28, 1983, the Commission set the matter for oral argument on May 9, 1983. Oral argument was held as scheduled, and on May 19, 1983, the Commission entered its Order rescinding said paragraph No. 8 as it relates to the general rate case in this docket and ordered the parties to appear in a separate proceeding in Docket No. T-825, Sub 278, for the purpose of determining the appropriate parameters for data associated with rate discount filings to be filed in future general rate case proceedings.

A Petition to Intervene filed on April 18, 1983, by Harper Trucking Company, Inc., in this docket was allowed by Commission Order issued on May 6, 1983.

A Motion for Continuance filed by the Public Staff on May 25, 1983, requesting that the hearing in this docket be continued for one hundred and twenty (120) days, which Motion was responded to by SMCRC by letter dated June 3, 1983, was denied by Order of the Commission issued on June 7, 1983.

The matter was called for hearing before Commissioner Sarah Lindsay Tate, presiding, and Commissioners A. Hartwell Campbell and Douglas P. Leary on June 21, 1983, and continued over to June 22, 1983, in the Hearing Room of the Commission, Dobbs Building, Raleigh, North Carolina, during which time the Respondents and the Public Staff were all present and represented by counsel.

The Respondents presented the testimony and exhibits of the following witnesses in support of their applications:

Leajar A. Brooks, Manager Rate and Research Department, Southern Motor Carriers Rate Conference, Inc.; Richard T. White, Manager, Continuing Traffic Study Department, Southern Motor Carriers Rate Conference, Inc.; Charles R. McGowan, Senior Cost Analyst, Southern Motor Carriers Rate Conference, Inc.; Harvie A. Carter, Traffic Manager, Epes Transport System, Inc.; Daniel M. Acker, Manager, Cost and Statistical Department, Southern Motor Carriers Rate Conference, Inc.; L. E. Forrest, Consultant, Former Traffic Manager, North Carolina Motor Carriers Association, Inc.; Charlie Finley, Director of Traffic, Fredrickson Motor Express Corporation; Robert E. Fitzgerald, Vice President of Traffic, Estes Express Lines; and Kenneth D. Angell, President, Edmac Trucking Company, Inc.

The Public Staff presented the testimony and exhibits of the following witness:

H. L. Woody, Executive Vice President, North Carolina Traffic League, Inc., and David A. Poole, Staff Accountant, Public Staff, Transportation - Rates Division, North Carolina Utilities Commission.

Based upon the complete record in this docket, including the testimony and exhibits presented at the hearing, late-filed testimony and exhibits subsequently allowed into the record, and matters of which judicial notice may be taken, the Commission makes the following

FINDINGS OF FACT

1. The motor carriers of general commodities participating in the tariff publications which are the subject of this docket, all of whom hold certificates from this Commission for operating authority, are property before this Commission for an increase in their rates and charges pursuant to Chapter 62 of the General Statutes of the State of North Carolina.

2. The SMCRC, NCMCA and MCTA cost-study groups utilized in making the cost-revenue analysis and comparisons supporting the proposed rate increases are reasonably representative of the general commodity carriers that participate in each respective issue tariff, and the combined results of the cost-revenue comparisons of such cost-study groups are reasonably representative of all of the general commodity carriers participating in the issue tariffs.

3. Under present rates, the overall operating ratio of all subject tariff categories for the three rate bureaus included in this proceeding is 108.42%

4. Under rates approved herein, the operating ratio of all subject tariff categories for the three rate bureaus included in this proceeding is 100.52%.

5. The operating ratio of $100.52% is the result of the approval of the rates requested herein by the Respondents and is not unfair and unreasonable.

6. The approved increase will result in an increase in gross revenues of $3,586,617 for the study carriers used in setting rates in this proceeding.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 1

The evidence for this finding of fact comes from the verified applications. This finding of fact is essentially informational, procedural, and jurisdictional in nature.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 2

Respondents, pursuant to proposed Rule R1-17(j) promulgated by the Commission in its Docket No. M-100, Sub 90, used the following carriers as cost-study carriers based on this Commission's prior determinations that the data from such carriers is reasonably representative of the experiences of carriers participating in the respective issue tariffs and that the combined data of all three groups of carriers reasonably represents the experiences of all motor carriers of general commodities which participate in the issue tariffs:

SMCRC	NCMCA	MCTA
Fredrickson Motor Express Corp.	Edmac Trucking Co., Inc.	DeHart Motor Lines, Inc.
Estes Express Lines, Inc.	Sherman & Boddie, Inc.	Shippers Freight Lines, Inc.
Standard Trucking Co.	Wicker Services, Inc.	Terminal Trucking Co., Inc.
Bruce Johnson Trucking Co., Inc.	Carpenter Trucking Co., Inc.	Western Carolina Express, Inc.
Blue Ridge Trucking Co., Inc.	A. V. Dedmon Trucking, Inc.	South Atlantic Bonded Warehouse Corp.
Dixie Trucking Co., Inc.		

The Public Staff, a party to the proceedings in Docket No. M-100, Sub 90, did not dispute the representativeness of the cost-study carriers used by Respondents, and therefore the Commission concludes that the cost-study groups utilized by Respondents in this proceeding are appropriate for use in in setting fair and reasonable rates in this proceeding.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 3

The evidence for this finding of fact is found primarily in the testimony and exhibits of Respondents' witnesses Acker and Forrest, and Public Staff witness Poole. The Public Staff did not contest the Respondents' level of present revenues, before consideration of any alleged overcollections of fuel surcharge revenues.

The Public Staff contended that the Respondents' study carrier groups included herein in this proceeding have overcollected fuel surcharge revenues during the test year as follows:

Carrier Bureau	Amount
1. SMCRC	$898,418
2. NCMCA	15,584
3. MCTA	42,986
4. Composite	$956,988

The Public Staff contends that revenues from fuel surcharges collected under authority of Orders entered in Docket T-825, Sub 248 (hereinafter "the Fuel Surcharge Docket"), during 1981 exceeded the increases in fuel expenses over the base price during that period, and argue that the amount of such "over collections" should be subtracted from the additional revenues requested by the Respondents. The Respondents deny that any significant over collection has occurred, arguing that the so-called "over collections" calculated by the Public Staff are due to (1) differences in the cost-study carrier frame in this and the Fuel Surcharge Docket; (2) differences in the cost allocation methods used in this and the Fuel Surcharge Docket; and (3) the emphasis on test year figures in this docket, rather than comparisons of revenues and expenses since the inception of fuel surcharges as occurs in the Fuel Surcharge Docket. Respondents also argue these issues should be resolved in the Fuel Surcharge Docket. Finally, Respondents argue that the proposed increases should be allowed even if the Commission adopts the Public Staff's contentions, because the proposed increase in revenues under the issue tariffs together with the "over collections" of fuel surcharge revenues would produce issue operating ratios exceeding 95 for each carrier group, which would not be an unjust and unreasonable operating ratio for each.

After a careful review of the entire record in this matter, the Commission concludes that the position of the Public Staff should be rejected for the reason the Commission Order of November 7, 1980, establishing Rule R1-16.1(k), clearly states that the appropriate method for preventing an overcollection of fuel revenues is to adjust the fuel adjustment factor in fuel surcharge proceedings. Based on this statement and review of Final Orders entered in prior general rate case proceedings concerning the Respondent motor carriers' issue traffic of which the Commission hereby takes judicial notice, the Commission concludes that the fuel surcharge proceeding is the proper docket to measure and to determine whether or not and to what extent fuel surcharge overcollections should be considered for rate-making purposes.

The Commission further notes that the Respondent carriers' fuel surcharge in effect and collected during the test year was that established pursuant to lawful Commission Orders entered in Docket No. T-825, Sub 248, and that no appeal was taken with respect to those Orders by any party to those proceedings.

Therefore, based on the foregoing, the Commission concludes that the Respondents' level of present revenues is $45,628,517, as calculated below:

Carrier Bureau	Amount
1. SMCRC	$37,997,863
2. NCMCA	1,810,663
3. MCTA	5,819,991
Composite	$45,628,517

The Public Staff and the Respondents agree to the present level of expenses for the NCMCA and the MCTA study carriers, and therefore the Commission

concludes that the proper level of present expenses for these carriers is $1,893,090 and $6,291,082, respectively.

The Public Staff disagreed on three items concerning the appropriate present level of expenses for the SMCRA study group. First, the Public Staff allocated certain expenses based on hundredweight platformed as opposed to man-minutes per hundredweight. Consistent with its decision in the Respondents' last general rate case concerning issue traffic, the Commission concludes that the Respondents' position on this issue is appropriate.

The Public Staff took issue with the Respondents' methodology used in updating of the Continuing Tariff Study to derive the present level of expenses for the SMCRC carriers. The Commission concludes that the preponderance of evidence on this issue supports the Respondents' expense updating procedures to be used in setting fair and reasonable rates in this proceeding.

Finally, the Public Staff adjusted the SMCRC present expense level by $100,000 to properly reflect present wage expense levels. The Respondents did not contest this adjustment and therefore the Commission concludes this adjustment is appropriate. Consequently, based on the foregoing, the Commission concludes that the SMCRC study carriers' present level of expenses, to be used in setting rates in this proceeding, is $41,284,773.

The Commission further concludes that the operating ratios on issue traffic under present rates for the study carriers included in this proceeding are as follows:

Carrier Group	Operating Ratio
1. SMCRC	108.65%
2. NCMCA	104.55%
3. MCTA	108.09%
Composite	108.42%

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 4 AND 5

The evidence for this finding of fact is found primarily in the testimony and exhibits of Respondents' witnesses Forrest and Acker and Public Staff witness Poole. There is no material diffference in the record between the Respondents' proposed revenue increase and the Public Staff's recommended increase when added to the Public Staff's calculations of alleged fuel surcharge overcollections. Therefore, consistent with the Commission's decision concerning the appropriate operating ratio under present rates under Evidence and Conclusions for Finding of Fact No. 3, the Commission concludes that the requested revenue increase should be granted. The Commission further concludes that the appropriate operating ratios for the Carrier Groups after the requested increase approved herein is the following:

Carrier Group	Operating Ratio
1. SMCRC	100.26%
2. NCMCA	100.62%
3. MCTA	102.18%
Composite	100.52%

The Commission concludes that these operating ratios, resulting from the requested increase being approved herein, is not unfair and unreasonable.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 6

The evidence for this finding of fact is based on the evidence and conclusions found elsewhere in this Order and is caluclated as follows:

Carrier Group	Present Revenues	Approved Increase	Revenues After Approved Increase
SMCRC	$37,997,863	$ 3,179,250	$41,177,113
NCMCA	1,810,663	70,747	1,881,410
MCTA	5,819,991	336,620	6,156,611
Composite	$45,628,517	$ 3,586,617	$49,215,134

IT IS, THEREFORE, ORDERED as follows:

1. That the Respondents be, and the same are hereby, authorized to increase their North Carolina intrastate class, commodity, distance, or mileage commodity, and exception rates, minimum charges, accessorial charges, and accessorial rates applying on the transportation of general commodities, involved in these proceedings, as proposed in their respective issue tariffs.

2. That the proposed increases are hereby approved and may become effective after appropriate tariff publications in accordance with the Commission's rules and regulations governing the construction, filing, and posting of transportation tariff schedules, upon not less than five (5) days' notice to the Commission and to the public.

3. That the Respondent motor common carriers participating in the involved tariff publications shall revise and reissue or require their respective tariff publishing agents to revise and republish their present general commodity tariffs so that all rates and charges contained in said tariffs, with the exception of fuel surcharge adjustments authorized by this Commission under Docket No. T-825, Sub 248, will be the rates authorized by this Order.

ISSUED BY ORDER OF THE COMMISSION.
This the 8th day of September 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sandra J. Webster, Chief Clerk

DOCKET NO. T-825, SUB 276

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Infinger Transportation Co., Inc., P.O. Box 70698, Charleston, South Carolina 29405 - Investigation of Proposed Tariff Filing Publishing Increases and Reductions in Transportation Rates Applying on North Carolina Intrastate Transportation of Asphalt, in Tank Vehicles, Scheduled to Become Effective March 13, 1983, and Complaint Thereto Filed by A.C. Widenhouse, Inc., and Eastern Oil Transport, Inc.

ORDER GRANTING EXCEPTIONS AND DENYING PROPOSED RATE ADJUSTMENTS

ORAL ARGUMENT
HEARD IN: Commission Hearing Room, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina 27602, on Monday, September 19, 1983

BEFORE: Chairman Robert K. Koger, Presiding; and Commissioners Leigh H. Hammond, Sarah Lindsay Tate, A. Hartwell Campbell, Douglas P. Leary, and Ruth E. Cook

APPEARANCES:

For the Respondent:

Ralph McDonald, Bailey, Dixon, Wooten, McDonald, and Fountain, P.O. Box 2246, Raleigh, North Carolina 27602
For: Infinger Transportation Co., Inc.

For the Intervenors:

Joseph W. Eason, Moore, Van Allen and Allen, P.O. Box 2058, Raleigh, North Carolina 27602
For: A.C. Widenhouse, Inc.
Eastern Oil Transport, Inc.

BY THE COMMISSION: This matter was heard on oral argument by the Commission on September 19, 1983. The oral argument was scheduled by Commission Order of August 24, 1983, in response to exceptions filed by Intervenors Widenhouse and Eastern to the Recommended Order issued by Hearing Examiner Sammy R. Kirby on August 5, 1983. The Recommended Order of August 5, 1983, approved the rate adjustments requested by Infinger.

The record of this matter shows that on February 10, 1983, the North Carolina Motor Carriers Association, Inc. (NCMCA), as agent on behalf of Infinger Transportation Co., Inc. (Infinger or Respondent), filed Supplement No. 3 to Local Motor Freight Tariff No. 16-H applying on shipments of asphalt in bulk, in tank trucks. Supplement No. 3, which was scheduled to become effective on March 13, 1983, constituted an independent action by Infinger to adjust its rates and charges applicable to asphalt shipments originating at Wilmington.

On March 4, 1983, A.C. Widenhouse, Inc. (Widenhouse), and Eastern Oil Transport, Inc. (Eastern), (collectively, Complainants), filed a complaint requesting that Infinger's tariff filing be suspended, that the proceeding be declared a general rate case, and that an investigation of the proposed rates and charges be undertaken.

On March 11, 1983, the Commission isued an Order suspending the tariff for 270 days, instituted an investigation, and scheduled a public hearing. After investigation by the Intervenors, the matter was heard by Hearing Examiner Sammy R. Kirby.

On June 7, 1983, the Public Staff - North Carolina Utilities Commission intervened in this matter, appeared at the hearing on June 7, 1983, but did not file exceptions to the Hearing Examiner's Order of August 5, 1983. Nor did the Public Staff appear at the September 19, 1983, oral argument.

Based upon a careful consideration of the entire record in this proceeding, the Commission concludes that the Recommended Order Approving Rate Adjustments entered herein on August 5, 1983, should be reversed. Further, the Commission now makes the following

FINDINGS OF FACT

1. The Commission has jurisdiction over the subject matter of this proceeding and over the motor common carriers of property and their agents which are parties hereto.

2. The Respondent, Infinger Transportation Company, Inc., is a motor common carrier of property operating under authority evidenced by Certificate No. C-1032 issued by this Commission, which among other things authorizes the transportation of asphalt in tank trucks moving in intrastate commerce to points and places throughout the state from the origins of Wilmington, Morehead City, Beaufort, River Terminal, Thrift, Friendship, Salisbury, or Washington, North Carolina. Infinger also has authority from this Commission to transport other commodities, including petroleum and petroleum products, in intrastate commerce within North Carolina, and also possesses interstate authorities on various commodities issued by the Interstate Commerce Commission and intrastate authority in jurisdictions other than North Carolina. Infinger is a member of the NCMCA, and has participated in Tariff 16-H prior to the filing and during the suspension of Supplement No. 3.

3. A.C. Widenhouse, Inc., is a motor common carrier of property operating under the authority evidenced by Certificate No. C-400 issued by this Commission, and pursuant to said authority is actively engaged in providing intrastate transportation services on shipments of various commodities, including asphalt, moving in intrastate commerce to points and places in North Carolina. Widenhouse is a member of the NCMCA, and participates in Tariff 16-H.

4. Eastern Oil Transport, Inc., is a motor common carrier of property holding authority evidenced by Certificate No. C-161 issued by this Commission, and pursuant to said authority is effectively engaged in providing transportation services on shipments of various commodities, including asphalt, moving in intrastate commerce to points and places in North Carolina. Eastern is a member of the NCMCA, and participates in Tariff 16-H.

5. Tariff 16-H contains rates and charges applicable to intrastate shipments of asphalt which were established by this Commission after a hearing and a final Order in a general rate proceeding in Docket No. T-825, Sub 264. Tariff 16-H became effective on July 13, 1981. Tariff 16-H contains several separate sections and items, including point-to-point rates for shipments of asphalt except roofing and culvert asphalt, mileage scales for shipments of asphalt except roofing and culvert asphalt, and mileage scales applicable on roofing and culvert asphalt. The separate sections and items in Tariff 16-H relate to several different origin points. Supplement No. 1 to Tariff 16-H, which became effective on May 18, 1982, was cancelled by Supplement No. 2 effective on June 19, 1982.

6. Supplement No. 3 to Tariff 16-H, the result of an independent action by Infinger, proposes adjustments from the rates and charges published in Tariff 16-H solely for the account of Infinger on intrastate shipments of asphalt

originating in the City of Wilmington, North Carolina. The rates of other carriers and the rates via Infinger on asphalt moving intrastate from other origins are not directly affected by Supplement No. 3. Supplement No. 3, which was suspended by the Commission, was scheduled to become effective on March 13, 1983. Infinger proposed adjustments in the point-to-point rates applicable on asphalt except roofing and culvert asphalt, adjustments in the mileage scales applicable on asphalts except roofing and culvert asphalt, and adjustments in the mileage scales applicable on roofing and culvert asphalt.

7. Supplement No. 3 essentially proposes to increase the rates on shipments of asphalt from Wilmington to points within 42 counties, to decrease the rates on shipments of asphalt from the same origin to points within 52 counties, and to leave unchanged the rates on shipments of asphalt from Wilmington to points within six counties. The proposed adjustments are not uniform, with increases ranging from 3.6 percent to 45.5 percent, and reductions ranging from 1.0 percent to 8.9 percent. Except for five counties approximately 145 to 150 miles one way from Wilmington, the proposed reductions apply to shipments of asphalt moving less than 200 miles one-way from Wilmington, whereas the rates on shipments of asphalt moving one-way in excess of 200 miles are proposed to be increased.

8. In preparing justification data and testimony in support of Supplement No. 3, Infinger did not use the uniform allocation method attached to the Order of this Commission issued on April 2, 1981, in Docket No. T-825, Sub 257 (hereinafter "the Uniform Allocation Method"), which Order concluded that the Uniform Allocation Method was "approved to be used by the asphalt common carriers engaged in intrastate commerce in the State of North Carolina for use in compiling financial data in future tariff filings."

9. Infinger has failed to prove that the adjustments proposed in Supplement No. 3 are just and reasonable.

Whereupon, the Commission reaches the following

CONCLUSIONS

There are two key points at the heart of this matter, and upon which the exceptions of Widenhouse and Eastern are generally based. First, there is the point of whether or not Infinger used the appropriate cost allocation methodology in calculating operating ratios associated with its proposed rates. Second, there is the point whether or not the present rates for issue traffic involved herein should be changed, based on evidence of record.

As to the proper cost allocation methodology issue, Eastern and Widenhouse contend that the method used by Infinger is inappropriate. Eastern and Widenhouse assert that Infinger should have used the Uniform Allocation Method approved by the Commission in Docket No. T-825, Sub 257, dated April 2, 1981, for use in determining fair and reasonable rates for the issue traffic involved herein in this proceeding. Complainants further assert that the system unit cost methodology employed by Infinger in this proceeding is applied to a base that includes not only issue traffic involved herein, but interstate traffic and other intrastate traffic, such as petroleum. The Commission is mandated to fix fair and reasonable rates for the issue traffic in this proceeding, and a key component necessary to achieve this mandate is the determination of the appropriate allocation methodology to be used in

establishing a proper level of operating expenses. Indeed, this component is a key ingredient to any decision involving appropriate rates for utilities engaged in more than one jurisdiction or having more than one type of operation. Based upon the entire record in this matter, the Commission is unpersuaded that the cost allocation methodology incorporated by Infinger in this proceeding is appropriate for determining fair and reasonable rates for the issue traffic involved in this matter.

By seeking to adjust the issue traffic rates in this proceeding, Infinger is in effect seeking to change the rate structure approved for said traffic in the last general rate case for said traffic, Docket No. T-825, Sub 264, by Order dated July 10, 1981. Said rate structure approved by the July 10, 1981, Order was the rate structure requested by the NCMCA in that proceeding, and recommended by the Public Staff - North Carolina Utilities Commission after their investigation into the matter. In addition, by virtue of its participation in the NCMCA's tariff filing in Docket No. T-825, Sub 264, Infinger's current rates for issue traffic involved herein were those proposed and approved in Docket No. T-825, Sub 264.

The Complainants assert that the instant proceeding is an investigation of a proposed change in rates previously established by the Commission and that, therefore, according to North Carolina General Statutes 62-132 and G.S. 62-134(c), the burden is on Infinger to show that the proposed rate change is just and reasonable. Further, G.S. 62-132 provides that rates approved and established under this Chapter, as is the case for the rates associated with the issue traffic resulting from Docket No. T-825, Sub 264, shall be deemed just and reasonable. Based on a careful review of the entire record, the Commission concludes that the current rates for the issue traffic are in fact just and reasonable, and that Infinger has not carried the burden of proof to show otherwise in order to justify approval of its proposed rates.

Based on the foregoing, the Commission concludes that the Recommended Order of August 5, 1983, should not be adopted by the Commission, and further, that the Supplement No. 3 to Local Motor Freight Tariff No. 16-H, filed March 11, 1983, by Infinger, should not be approved.

IT IS, THEREFORE, ORDERED as follows:

1. That Supplement No. 3 to NCMCA Tariff No. 16-H, NCUC No. 134 be, and hereby is, denied approval.

2. That Infinger Transportation Co, Inc., and North Carolina Motor Carriers Association, as its agent, be, and hereby are, ordered to file appropriate supplements to Tariff No. 16-H NCUC No. 134, cancelling Supplement No. 3.

3. That the Recommended Order Approving Rate Adjustments entered herein on August 5, 1983, be, and the same is hereby, reversed.

ISSUED BY ORDER OF THE COMMISSION.
This the 27th day of October 1983.

NORTH CAROLINA UTILITIES COMMISSION
Sandra J. Webster, Chief Clerk

(SEAL)

DOCKET NO. T-2193

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of	
Sale and Transfer of Certificate No. C-972 from Steve Strickland, d/b/a Strick's Transporters, to Clyde Dean Haugen and Boyce Rhymer, d/b/a Atlantis Transporters	) ORDER OVERRULING) EXCEPTIONS AND AFFIRM-) ING RECOMMENDED ORDER) APPROVING TRANSFER

HEARD IN: Commission Hearing Room 217, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina, on March 28, 1983, at 2:00 p.m.

BEFORE: Commissioner Edward B. Hipp, Presiding; Chairman Robert K. Koger, Commissioners Leigh H. Hammond, Sarah Lindsay Tate, John W. Winters, and Douglas P. Leary

APPEARANCES:

For the Applicants:

Peter Reynolds, Attorney at Law, 309 Law Building, Charlotte, North Carolina 28202

For the Protestants:

Carson Carmichael, III, Bailey, Dixon, Wooten, McDonald & Fountain, Attorneys at Law, P.O. Box 2246, Raleigh, North Carolina 27602

BY THE COMMISSION: By joint application filed on February 24, 1982, Steve Strickland, d/b/a Strick's Transporters, as transferor, and Clyde Dean Haugen and Boyce Rhymer, d/b/a Atlantis Transporters, as transferees, filed an application seeking authority to sell and transfer the operating authority set forth in Certificate No. C-972, as follows:

> "Transportation of Group 21, mobile homes between points and places in southeastern North Carolina bounded on the west by U.S. Highway 301, on the south by the South Carolina State Line, on the east by the Atlantic Ocean, and the North by U.S. Highway 264, the Pamlico River, and the Pamlico Sound, excepting from said authority, however, points and places in the following counties: Onslow, Cumberland, Wayne, and Robeson."

The application was heard on July 23, 1982, before Hearing Examiner Robert P. Gruber, and a Recommended Order Granting Application was issued by the Hearing Examiner on November 22, 1982.

On December 7, 1983, Protestants filed Exceptions to the Recommended Order setting forth Exceptions 1 - 4 and supporting reasons and arguments. Protestants requested oral argument on their Exceptions, and counsel for the Applicants and the Protestants presented oral argument to the Commission at the time and place indicated above.

Upon consideration of the entire record in this proceeding, the Commission concludes that each of the Exceptions 1 - 4 should be overruled and denied and that the Recommended Order should be affirmed.

IT IS, THEREFORE, ORDERED by action of the Full Commission at a meeting on March 28, 1983, following the oral argument, that the Recommended Order Granting Application issued in this docket on November 22, 1982, be, and the same hereby is, affirmed.

ISSUED BY ORDER OF THE COMMISSION.
This the 11th day of April 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sandra J. Webster, Chief Clerk

DOCKET NO. T-2143, SUB 3

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Merritt Trucking Company, Inc., Post Office Box 18346, Greensboro, North Carolina 27419-8346 - Application for Sale and Transfer of a Portion of Certificate No. C-417 from Everette Truck Line, Inc.
) FINAL ORDER MODIFYING RECOMMENDED ORDER, OVERRULING EXCEPTIONS, AFFIRMING RECOMMENDED ORDER AS MODIFIED

HEARD IN: Commission Hearing Room, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina, on Monday, March 7, 1983, at 2:00 p.m.

BEFORE: Chairman Robert K. Koger and Commissioners Leigh H. Hammond, Sarah Lindsay Tate, John W. Winters, Edward B. Hipp, A. Hartwell Campbell, and Douglas P. Leary

APPEARANCES:

For the Applicants:

Ralph McDonald, Bailey, Dixon, Wooten, McDonald & Fountain, Attorneys at Law, Post Office Box 2246, Raleigh, North Carolina 27602
For: Merritt Trucking Company, Inc.
Everette Truck Lines, Inc.

For the Protestants:

Thomas W. Steed, Jr., Moore, Van Allen & Allen, Attorneys at Law, Post Office Box 2058, Raleigh, North Carolina 27602
For: Fleet Transport Company, Inc.
Chemical Leaman Tank Lines, Inc.
Central Transport, Inc.
Kenan Transport Company

BY THE COMMISSION: By joint application filed with the North Carolina Utilities Commission on June 25, 1982, Merritt Trucking Company, Inc. (Merritt), and Everette Truck Lines, Inc. (Everette), seek authority for

Everette to transfer and sell to Merritt a portion of Everette's motor carrier operating authority evidenced by Certificate No. C-417. The portion of the authority to be sold and transferred reads as follows:

"The transportation of brick, tile, grain, chemicals, and syrup over irregular routes in North Carolina on and east of U.S. Highway 29."

On October 1, 1982, a joint protest and motion for intervention was filed by Fleet Transport Company, Inc.; Chemical Leaman Tank Lines, Inc.; Central Transport, Inc.; and Kenan Transport Company (Protestants). By Order of October 11, 1982, Protestants were permitted to intervene.

The application was heard before Hearing Examiner Robert P. Gruber on November 17, 1982; and the Recommended Order Granting Application was issued by the Hearing Examiner on January 20, 1983.

On February 4, 1983, Protestants filed Exceptions to Recommended Order Granting Application setting forth Exceptions 1 - 10 and supporting reasons and arguments. Protestants requested oral argument on their exceptions, and counsel for the Applicants and the Protestants presented oral argument to the Commission at the time and place indicated above. During oral argument and in response to a point made by the Protestants, Applicant Merritt stipulated that the authority sold and transferred to it could be limited to read as follows:

"The transportation of chemicals and syrup in bulk over irregular routes in North Carolina on and east of U.S. Highway 29."

The Commission recognizes and accepts this stipulation and will so modify the authority sold and transferred by the Recommended Order.

Upon consideration of the entire record in this proceeding and in light of the stipulation made during oral argument, the Commission concludes that each of the Exceptions 1 - 10 should be overruled and denied and that the Recommended Order, as modified above, should be affirmed.

IT IS, THEREFORE, ORDERED:

1. That the Recommended Order Granting Application issued in this docket on January 20, 1983, be, and the same hereby is, modified to limit the authority sold and transferred to the Applicant Merritt as follows:

"The transportation of chemicals and syrup in bulk over irregular routes in North Carolina on and east of U.S. Highway 29."

2. That each of the Exceptions 1 - 10 filed herein by Protestants be, and the same hereby are, overruled and denied.

3. That the Recommended Order issued on January 20, 1983, as modified herein, be, and the same hereby is, affirmed.

ISSUED BY ORDER OF THE COMMISSION.
This the 18th day of March 1983.

NORTH CAROLINA UTILITIES COMMISSION
Sandra J. Webster, Chief Clerk

(SEAL)

DOCKET NO. T-825, SUB 277

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of

Filing of Tariff by North Carolina Movers Association, Inc. - Independent Announcement of Lentz Transfer and Storage Company Independently Annoucning a New Rule Providing for a "Guaranteed Price Move," Scheduled to Become Effective April 1, 1983	) RECOMMENDED) ORDER) ALLOWING) MOTION TO) DISMISS

HEARD IN: Commission Hearing Room No. 217, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina 27602, on Thursday, September 22, 1983, at 9:30 a.m.

BEFORE: Sammy R. Kirby, Hearing Examiner

APPEARANCES:

For the Respondents:

Wesley Bailey, Bailey and Thomas, Attorneys at Law, P. O. Box 52, Winston-Salem, North Carolina 27102
For: Yarborough Transfer Company

D. Blake Yokley, Yokley and Teeter, Attorneys at Law, 405 1st Home Federal Building, 120 West 3rd Street, Winston-Salem, North Carolina 27101
For: Lentz Transfer and Storage Company

For the Public Staff:

Theodore C. Brown, Jr., Staff Attorney, Public Staff - North Carolina Utilities Commission, P. O. Box 991 - Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina 27602
For: The Using and Consuming Public

KIRBY, HEARING EXAMINER: On March 2, 1983, the North Carolina Movers Association, Inc., filed Supplement No. 38 to Tariff No. 3 naming local rates on household goods between points within the State of North Carolina, said supplement to be effective April 1, 1983. The supplement provided for a "guaranteed price move" and was made applicable to Yarborough Transfer Company, Lentz Transfer and Storage Company, and other named carriers.

On March 22, 1983, the Commission issued an Order suspending the tariff provided by the supplement, requiring the Public Staff to investigate the filing and make a recommendation, and scheduling a hearing. By subsequent Order of May 2, 1983, the Commission rescheduled the hearing for the time and place indicated above.

On August 5, 1983, the Public Staff filed a motion to dismiss the proceeding without prejudice and to close the docket. By Order of September 2, 1983, the Commission scheduled oral argument on the motion to dismiss as a part of the hearing already scheduled.

The hearing came on as scheduled and oral argument was presented on the Public Staff's motion to dismiss. The Respondents, the carriers party to the "guaranteed price move" supplement, were allowed an extension of time in which to file a written response to the motion to dismiss, and such a response was subsequently filed with the Commission on October 6, 1983. Testimony was presented on behalf of the Respondents and the Public Staff; however, the Hearing Examiner has concluded that the merits of the supplement can be decided on the basis of the motion to dismiss, the response thereto, and the oral argument thereon.

The motion to dismiss asserts, among other grounds for dismissal, that the "guaranteed price move" supplement cannot be approved under applicable law since it is actually a request for deregulation of the household goods moving industry, since it is not governed by specific approved tariff rates and thus allows the carriers to usurp the Commission's statutory ratemaking responsibility, since it provides no means by which the Utilities Commission can determine whether charges thereunder are just and reasonable or whether carriers are discriminating among shippers, and since it violates various other statutes cited in the motion. The Respondents deny that the supplement would deregulate the household goods moving industry, argue that carriers would continue to use the tariff rates approved by the Commission in figuring the "guaranteed price move" charges (although the Examiner notes that the supplement does not require such), maintain that the Commission could impose rules and regulations on "guaranteed price move" carriers in order to protect shippers and provide incentives to carriers, and argue that the Commission would continue to have authority to police the carriers and prevent discrimination.

Based upon the motion to dismiss, the response thereto, and the argument thereon, the Hearing Examiner finds and concludes as a matter of law that the "guaranteed price move" supplement as filed in this docket on March 2, 1983, is not permissible under the present statutes governing the motor carrier industry in this state, on the grounds argued in the Public Staff's motion to dismiss and summarized above, and that the Public Staff's motion to dismiss should be allowed.

IT IS, THEREFORE, ORDERED that the motion to dismiss this proceeding without prejudice and to close this docket filed by the Public Staff on August 5, 1983, should be, and the same hereby is, allowed.

ISSUED BY ORDER OF THE COMMISSION.
This the 13th day of October 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sandra J. Webster, Chief Clerk

DOCKET NO. T-2218

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of

Jerry T. Johnson and Wife, Helen H. Johnson, d/b/a Jerry Johnson Mobile Home Movers, 1870 Garland Street, Henderson, North Carolina 27536 - Application for Common Carrier Authority, Group 21, Mobile Homes, Bulk Barns and Mobile Offices	)	FINAL ORDER OVERRULING EXCEPTIONS AND AFFIRMING RECOMMENDED ORDER

HEARD IN: The Commission Hearing Room, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina on January 24, 1983, at 2:45 p.m.

BEFORE: Chairman Robert K. Koger, and Commissioners Sarah Lindsay Tate, John W. Winters, Edward B. Hipp, Presiding, A. Hartwell Campbell, and Douglas P. Leary

APPEARANCES:

For the Applicant:

F. Kent Burns, Boyce, Mitchell, Burns & Smith, P.A., Attorneys at Law, 107 Fayetteville Street Mall, Raleigh, North Carolina
For: Jerry Johnson Mobile Home Movers

For the Respondents:

Robert Catherwood, Edmondson and Catherwood, Post Office Box 428, Oxford, North Carolina 27565
For: Pop's Trailer Towing Company, Inc.
Joe Lewis, t/a Joe Lewis Mobile Home Moving Service

BY THE COMMISSION: On November 30, 1982, the Protestants, Pop's Trailer Towing Company, Inc., and Joe Lewis, t/a Joe Lewis Mobile Home Moving Service, filed exceptions to the Recommended Order of Hearing Examiner Partin which was issued in this docket on November 10, 1982. On December 3, 1982, the Commission issued an Order scheduling the exceptions for oral argument before the full Commission on January 17, 1983. The hearing date was subsequently rescheduled to January 24, 1983.

The matter came on for oral argument as scheduled on January 24, 1983. The Applicant, Jerry Johnson Mobile Home Movers, and the Protestants were present and represented by counsel and made oral argument.

Based upon a careful consideration of the Recommended Order of November 10, 1982, the exceptions of the Protestants filed November 30, 1983, the oral argument of the parties before the full Commission on January 24, 1983, and the entire record in this proceeding the Commission is of the opinion, finds, and concludes that all the findings, conclusions, and ordering paragraphs contained in the Recommended Order of November 10, 1982, are fully supported by the record and that the Recommended Order dated November 10, 1982, should be affirmed and adopted as the Final Order of the Commission, and that each of the exceptions thereto should be overruled and denied.

IT IS, THEREFORE, ORDERED:

1. That each and every exception of the Protestants to the Recommended Order of November 10, 1982, be, and the same are hereby, overruled.

2. That the Recommended Order of November 10, 1982, be, and the same is hereby, affirmed and adopted as the Final Order of the Commission.

ISSUED BY ORDER OF THE COMMISSION.

This the 12th day of April 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sandra J. Webster, Chief Clerk

DOCKET NO. T-2143, SUB 4

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Merritt Trucking Company, Inc., P. O. Box 18346, Greensboro, North Carolina 27419-8346 - Application for Authority to Transport Group 21, Soybean Oil, Statewide) FINAL ORDER OVERRULING EXCEPTIONS AND AFFIRMING RECOMMENDED ORDER

HEARD IN: The Commission Hearing Room, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina 27602, on May 9, 1983, at 11:00 a.m.

BEFORE: Chairman Robert K. Koger, Presiding; and Commissioners Sarah Lindsay Tate, Edward B. Hipp, A. Hartwell Campbell, and Douglas P. Leary

APPEARANCES:

For the Applicant:

Ralph McDonald, Bailey, Dixon, Wooten, McDonald & Fountain, Attorneys at Law, P.O. Box 2246, Raleigh, North Carolina 27602
For: Merritt Trucking Company, Inc.

For the Protestants:

Joseph W. Eason, Moore, Van Allen & Allen, Attorneys at Law, P.O. Box 2058, Raleigh, North Carolina 27602
For: Fleet Transport Company, Inc.

BY THE COMMISSION: On April 1, 1983, Protestant Fleet Transport Company, Inc., filed exceptions to the Recommended Order of Hearing Examiner Kirby which was issued in this docket on March 17, 1983. On April 26, 1983, the Commission issued an Order scheduling the exceptions for oral argument before the full Commission on May 9, 1983.

The matter came on for oral argument as scheduled on May 9, 1983. The Applicant Merritt Trucking Company, Inc., and the Protestant were present and represented by counsel and made oral argument.

Based upon a careful consideration of the Recommended Order of March 17, 1983, the oral argument of the parties before the full Commission on May 9, 1983, and the entire record in this proceeding, the Commission is of the opinion, finds and concludes that all the findings, conclusions, and ordering paragraphs contained in the Recommended Order of March 17, 1983, are fully supported by the record and that the Recommended Order dated March 17, 1983, should be affirmed and adopted as the Final Order of the Commission, and that each of the exceptions thereto should be overruled and denied.

IT IS, THEREFORE, ORDERED as follows:

1. That each and every exception of the Protestant to the Recommended Order of March 17, 1983, be, and the same are hereby, overruled.

2. That the Recommended Order of March 17, 1983, be, and the same is hereby, affirmed and adopted as the Final Order of the Commission.

ISSUED BY ORDER OF THE COMMISSION.
This the 18th day of May 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sandra J. Webster, Chief Clerk

DOCKET NO. P-140

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of	
Application of AT&T Communications of the Southern States, Inc., for a Certificate of Public Convenience and Necessity to Provide Intrastate Telecommunications Services and for Approval of Proposed Rates Charges, Rules and Regulations	ORDER GRANTING CERTIFICATE

HEARD IN: Commission Hearing Room, Dobbs Building, Raleigh, North Carolina, on December 1, 2, and 15, 1983

BEFORE: Commissioner Sarah Lindsay Tate, Presiding; and Chairman Robert K. Koger and Commissioners Edward B. Hipp, Leigh H. Hammond, A. Hartwell Campbell, Douglas P. Leary, and Ruth E. Cook

APPEARANCES:

For the Applicant:

Gene V. Coker, General Attorney, AT&T Communications of the Southern States, Inc., 1200 Peachtree Street, N. E., Atlanta, Georgia 30357,

and

Wade H. Hargrove and Mark J. Prak, Tharrington, Smith and Hargrove, Attorneys at Law, P. O. Box 1151, Raleigh, North Carolina 27602
For: AT&T Communications of the Southern States, Inc.

For the Intervenors:

R. Frost Branon, Jr., General Attorney, and Robert Sterrett, Attorney, Southern Bell Telephone and Telegraph Company, P. O. Box 30182, Charlotte, North Carolina 28230
For: Southern Bell Telephone and Telegraph Company

Dwight W. Allen, Vice President, General Counsel, and Secretary, Carolina Telephone and Telegraph Company, 720 Western Boulevard, Tarboro, North Carolina 27886
For: Carolina Telephone and Telegraph Company

Dale E. Sporleder, General Counsel and Secretary, and Thomas R. Parket, Attorneys, General Telephone Company of the Southeast, 4100 North Roxboro Road, Durham, North Carolina 27704
For: General Telephone Company of the Southeast

James M. Kimzey, Kimzey, Smith, McMillan & Roten, Attorneys at Law, 506 Wachovia Bank Building, P. O. Box 150, Raleigh, North Carolina 27602
For: Central Telephone Company

Thomas R. Eller, Jr., Attorney at Law, Crabtree Center - Suite 205, 4500 Marriott Drive, Raleigh, North Carolina 27612
For: Citizens Telephone Company

Jerry B. Fruitt, Attorney at Law, P. O. Box 2507, Raleigh, North Carolina 27602
For: Carolina Utility Customers Association, Inc.

For the Public Staff:

Paul L. Lassiter, Antoinette R. Wike, and Vickie L. Moir, Staff Attorneys, Public Staff - North Carolina Utilities Commission, P. O. Box 991, Raleigh, North Carolina 27602
For: The Using and Consuming Public

For the Attorney General:

Karen E. Long, Assistant Attorney General, North Carolina Department of Justice, P. O. Box 629, Raleigh, North Carolina 27602
For: The Using and Consuming Public

BY THE COMMISSION: This proceeding arises on the application of AT&T Communications of the Southern States, Inc. ("ATTCOM" or "Applicant"), filed pursuant to G. S. 62-110 on October 31, 1983. The application seeks a certificate of public convenience and necessity authorizing ATTCOM to provide end-to-end intrastate telecommunications service throughout the State of North Carolina, i.e, on a statewide basis, and seeks approval of tariffs providing regulations, rates, and charges applicable thereto.

On November 3, 1983, the Commission suspended the proposed tariffs, set public hearings on the application and tariffs beginning December 1, 1983, and required public notice of the hearings. The Public Staff, the Attorney General, Carolina Telephone and Telegraph Company, Central Telephone Company, Citizens Telephone Company, General Telephone Company of the Southeast, Southern Bell Telephone and Telegraph Company, and Carolina Utility Customers Association, Inc. (CUCA), were permitted to intervene in this proceeding.

ATTCOM presented the testimony and exhibits of the following witnesses: Robert E. Fortenberry, designated as Vice President in ATTCOM's regulatory relations organization; Marion R. McTyre, District Manager for Southern Bell; Robert Friedlander, District Staff Manager - Rates for Southern Bell and designee for ATTCOM with responsibility for rates and tariffs.

Carolina Telephone Company presented the testimony of T. A. Norman, Assistant Vice President of Network Service for the Company.

General Telephone Company presented the testimony of Joseph W. Wareham, Business Relations Director for the Company.

The Public Staff presented the testimony of Millard N. Carpenter, III, Engineer - Communications Division.

During the course of the hearing, the Commission ordered Southern Bell to file three complete sets of the revised tariffs which the Company proposes to place into effect on January 1, 1984.

Two of the Intervenors, Carolina Telephone and Telegraph Company and Citizens Telephone Company, pleaded jurisdictional and constitutional bars to the granting of the application as filed. All Intervenors in the case with the exception of Southern Bell Telephone and Telegraph Company and General Telephone Company of the Southeast moved in substance that ATTCOM's application for a certificate of public convenience and necessity be treated as a proposed sale and transfer of the operating authority, assets, and operations of Southern Bell. Intervenors have further moved that the tariffs proposed by ATTCOM be specifically limited and applied to such intrastate long distance service and operating authority as presently owned and operated by Southern Bell in rendering long-distance telephone service between LATAs in North Carolina.

All parties were given ample opportunity for cross-examination and were afforded time for filing briefs and proposed orders. Based upon the evidence presented, relevant law, and the entire record in this proceeding, the Commission makes the following

FINDINGS OF FACT

1. On January 1, 1984, pursuant to the decision in United States v. Western Electric Company, Inc., and American Telephone and Telegraph Company, Civil Action No. 82-0192 (D.D.C. 1983), Southern Bell and the other Bell operating companies will be divested from AT&T. On that date, as a result of that order and without further leave of court, Southern Bell will not be permitted to offer interLATA toll services in North Carolina; that authority will reside with AT&T Communications, assuming it is granted the certificate requested in this proceeding.

On January 1, 1984, also pursuant to the Modification of Final Judgment (MFJ) entered in the above-captioned case, Southern Bell will transfer its interLATA facilities to AT&T. AT&T Communications has been created for the purpose of receiving such assets and offering legally permitted toll services.

2. AT&T Communications of the Southern States, Inc., seeks a certificate of public convenience and necessity to provide statewide end-to-end intrastate telecommunications service and seeks approval of tariffs providing regulations, rates, and charges applicable thereto.

3. Southern Bell Telephone and Telegraph Company is a duly franchised telephone utility corporation providing intrastate services in North Carolina. The application and the testimony of ATTCOM witness Fortenberry establish that the authority requested by ATTCOM is statewide in nature. The request is not limited to interLATA toll services; rather, if granted, the certificate would permit the offering of toll services throughout North Carolina by AT&T Communications, including those service territories exclusively within or affiliated with a Southern Bell LATA, or within a Carolina Telephone Company Geographical Marketing Area (GMA).

4. There was no evidence presented by any party that the existing toll service rendered by Southern Bell or any other telephone company in this State is not adequate. Existing telephone companies are presently meeting the public convenience and necessity for total telecommunications services and,

with the exception of Southern Bell, the ability of those same utilities to satisfy the public convenience and necessity will not be diminished by the MFJ after the effective date of divestiture.

5. The Commission has fully considered all of the evidence presented in this docket _in pari materia_ with Docket P-100, Sub 65, and finds that the request of AT&T Communications, _as it relates to intraLATA authority_, should not be granted. Under the existing North Carolina law, each telephone franchise is exclusive for the telephone service area designated; experience in a post-divestiture environment must be gained and the effects on basic subscribers fully studied before this Commission can determine the desirability of issuing competing intraLATA certificates. We do find, however, that to the extent ATTCOM seeks a toll certificate for the operating authority being simultaneously divested from Southern Bell pursuant to the MFJ, such a request is in the public interest and necessary to continue uninterrupted interLATA intrastate toll services on and after January 1, 1984.

6. Only that portion of Southern Bell's operating authority in North Carolina which has been actively operated by said Company in the provision of intrastate long-distance interLATA service as identified and ruled upon by the federal court should be acquired by ATTCOM. After acquisition, Southern Bell's operating authority shall be amended to delete that portion of the Bell operating authority acquired by ATTCOM. Any long-distance tariffs to be filed by ATTCOM should be clearly marked to show that the service offered is joint-line or through service applicable exclusively to interLATA services as defined and identified by the federal court. Conversely, the long distance intrastate tariffs of Southern Bell must be clearly marked to show that the service offered is applicable exclusively to calls originating and terminating within specifically designated LATAs in North Carolina in compliance with the federal court ruling.

7. Tariffs filed in this docket by ATTCOM must be modified to reflect only intrastate interLATA toll services performed over the North Carolina toll network acquired from Southern Bell; that during the interim period January 1, 1984, to April 3, 1984, the service shall be performed in connection with existing telephone utilities and cooperatives as presently provided, and after the Commission approves carrier access charges in Docket No. P-100, Sub 65, such service shall be in accordance therewith, with origination and termination of such service performed through franchised exchange carriers under carrier access charge tariffs.

8. The tariffs filed by AT&T Communications with its application in this proceeding, subject to Findings of Fact 6 and 7 above and other modifications specified herein, should go into effect on January 1, 1984, subject to further review by the Commission, if necessary. The tariffs filed by Southern Bell to implement divestiture, as modified herein, should also go into effect on January 1, 1984, in the same manner.

9. The intrastate message toll, WATS, TELPAK, and interexchange private line tariffs, including terminal equipment offerings for private line services, presently in effect for Southern Bell and the independent telephone companies should remain in effect on an interim basis and, to the extent necessary, should be made applicable to ATTCOM until April 3, 1984, pending further Order of the Commission.

10. The transfer of Southern Bell's intrastate joint-line, interLATA operating authority, assets, and operations to ATTCOM is for a lawful object, pursuant to the MFJ, and not only is within the corporate purposes of Southern Bell, but is in furtherance of the public policies of this State.

11. ATTCOM has excluded from its tariffs all offerings of premises wiring and continuous property channels. Further, ATTCOM has excluded references to the applicable local rate and FX extension rates from its foreign exchange tariff.

12. There is a need for ATTCOM to offer premises wiring associated with continuous property channels when such services involve interLATA service.

13. ATTCOM has included only the interexchange portion of interLATA foreign exchange service in its proposed tariffs.

14. There is a need for ATTCOM to serve as the single customer contact for interLATA foreign exchange related services.

15. ATTCOM shall provide MTS, WATS, TELPAK, FX, and Private Line Service only over the facilities acquired from Southern Bell and through access to the franchised area of the local exchange carriers under carrier access charge tariffs which shall be approved by further Order of the Commission in Docket No. P-100, Sub 65.

16. For an interim period not to exceed 120 days from January 1, 1984, Southern Bell shall retain all embedded equipment tariffs which are concurred in by the independent telephone companies.

17. Southern Bell shall retain specific rates and regulations in its tariffs applicable to equipment used with emergency services.

18. Southern Bell and ATTCOM shall file to be effective January 1, 1984, interim tariffs for provision of joint WATS offerings and joint TELPAK offerings which require no change in rates or charges to any subscribers. The TELPAK offering shall include the availability of a split package on interLATA and intraLATA channels.

19. Southern Bell shall perform all Directory Assistance (D.A.) billing at a charge of 20¢ per request in accordance with presently approved tariffs and shall furnish ATTCOM the revenues for interLATA D.A. requests.

Whereupon, the Commission reaches the following

CONCLUSIONS

On its face, ATTCOM's application seeks a certificate of public convenience and necessity within a service scope, i.e., "end-to-end" telecommuncations service, which is not supported by the evidence; and on its face, the application also seeks a certificate for a territorial scope, i.e., the entire State of North Carolina (service between all points and places in the State), which is not supported by the evidence. The only "end-to-end" telecommunications service permitted under North Carolina law is illustrated by local exchange service wherein the franchised carrier provides end-to-end basic local service and long-distance "end-to-end" service between its

franchised local service areas. Within the several local exchange areas in the State, there is no legal distinction between whether a subscriber is a basic local customer or a long-distance customer. Each company serves and bills its own customers, both for local and long-distance service. The only statutory reference to long-distance service is in G.S. 62-44, which in pertinent part provides:

> "The Commission may, upon its own motion or upon written complaint by any person, after notice and hearing, require any two or more telephone or telegraph utilities to establish and maintain through lines within the State between two or more localities, which cannot be communicated with or reached by the lines of either utility alone, where the lines or wires of such utilities form a continuous line of communication, or could be made to do so by the construction and maintenance of suitable connections or the joint use of equipment, or the transfer of messages at common points..."

Moreover, North Carolina law clearly holds as to all utilities--not merely telephone utilities--that no certificate shall be granted to an applicant to provide the same or similar service as an authorized utility in the same territory being served by the previously authorized utility unless and until the Commission shall find from the evidence that the service rendered by such previously authorized utility is inadequate, and the previously authorized carrier has been given reasonable time to remedy the inadequacy. See Utilities Commission v. Carolina Telephone and Telegraph Company, 267 N.C. 257, 148 S.E. 2d 100 (1966) for the leading case as to telephone utilties.

It is incontrovertible that: (1) This Commission has only those powers specifically granted it by the General Assembly; and (2) Where the meaning of a statute is clear and unambiguous, the Utilities Commission is without authority to construe or interpret it differently. The evidence in this case does not support a grant to ATTCOM of a telephone utility certificate with a scope of service which permits end-to-end telephone service of any type, whether characterized as "interLATA," "intraLATA, "interexchange" or "local exchange" telephone service. All long-distance intrastate telephone utility service in North Carolina must be "jointline" as it relates to independents, or for Southern Bell under the MFJ, by carrier access charge tariffs in all instances where the service crosses the service area boundary lines of two or more telephone utilities.

By casting its application under G.S. 62-110, and seeking an entirely new certificate for almost unlimited service and territory, ATTCOM assumed the burden in this case of establishing by competent, material, and substantial evidence that the local exchange and long-distance service--not merely of one telehone utility in the State, but all telephone utilities including Southern Bell--is inadequate and cannot, after reasonable notice, be made adequate.

At various times and through various wording, all parties to the proceeding except ATTCOM and Southern Bell moved the Commission to limit the operating authority sought by the application to that which Southern Bell is forced to give up in compliance with the Consent Decree to which AT&T bound itself and Southern Bell. Although ATTCOM elected not to amend its application, the Commission can only grant such authority as the evidence shows the Applicant is entitled to receive. The Commission, thus, must consider whether the application should be construed as limited to the existing interLATA

intrastate telephone utility operating authority being divested from Southern Bell pursuant to the MFJ.

The Commission considers indisputable the following facts: (a) Both Southern Bell and ATTCOM are wholly owned subsidiaries of AT&T; (b) As parent, AT&T has consented through MFJ that Southern Bell be disqualified from rendering interLATA long-distance telephone service, whether intrastate or interstate in character, and has created and designated ATTCOM as the entity to acquire such plant and system subject to approval of the Commission under G. S. 62-110.

The evidence presented in this docket is interwoven with the subject matter and record in Docket No. P-100, Sub 65. Therefore, the Commission has considered the evidence in this docket _in pari materia_ with Docket No. P-100, Sub 65, as it has bearing on the issues to be determined in this docket pursuant to G.S. 62-110, and further concludes that:

The proceedings properly are in the nature of a proposal by Southern Bell to sell and transfer and for ATTCOM to acquire, accept, and thereafter operate under and with that portion of the present intrastate telephone utility operating plant, assets, facilities, and appurtenances presently owned and actively used by Southern Bell in the provision of intrastate long-distance telephone services between LATAs as identified by the MFJ, all pursuant to the orders and decisions of the federal court requiring Southern Bell and AT&T to make a full and complete separation between them in the provision of long distance telephone service effective January 1, 1984. This proceeding should, therefore, be treated as in the nature of an application for sale and transfer pursuant to G.S. 62-110. The issues upon which the Applicant has the burden of proof pursuant to G.S. 62-75 are those set forth in G.S. 62-110. It is upon these issues that the Commission should make the salient determinations on the relief to which the evidence shows ATTCOM and Southern Bell to be entitled.

Southern Bell is authorized to file tariffs pursuant to G. S. 62-134 for WATS and/or TELPAK services which are confined to origination and termination within a single LATA, do not duplicate other telephone utility facilities and service, and do not have the capability of systematic multiLATA service as defined by the court.

The tariffs of rates and charges filed by ATTCOM in this docket are inappropriate and must be denied approval as filed in that said tariffs in various respects constitute an unlawful and unilateral restructuring of rates concurred in by all telephone companies in the State, are unnecessarily duplicative of presently approved long-distance telephone services in the State, and do not clearly specify and delineate the type and scope of long distance service to be provided thereunder as limited and defined in this Order. Upon completion of the transactions herein approved, ATTCOM should file and concur in the presently approved MTS, WATS, and Private Line Channel long-distance rates. Such tariffs shall expressly limit and separately delineate ATTCOM's services under its tariffs so that it participates in joint-line service or tariffed carrier access charges in interLATA long-distance service only to the extent participated in by Southern Bell prior to the granting of ATTCOM's certificate.

IT IS, THEREFORE, ORDERED as follows:

1. That the application in this docket be, and it is hereby, approved and granted to the extent that AT&T Communications of the Southern States, Inc., is authorized to acquire from Southern Bell Telephone and Telegraph Company, and thereafter operate under and through the use of that portion of Southern Bell's intrastate telephone utility operating authority, utility plant and assets, and operating appurtenances now operated under, owned, and employed by Southern Bell in rendering intrastate, interLATA, joint-line, MTS, WATS, TELPAK, and Private Line Channel Service within contemplation of G. S. 62-44. In all other respects, the application is denied and disapproved. This Order shall constitute ATTCOM's Certificate of Public Convenience and Necessity.

2. That the tariffs of rates and charges proposed by ATTCOM in this docket be, and are hereby, disapproved and denied, and required to be cancelled. ATTCOM is authorized to file and make effective without further notice on January 1, 1984, or the date of consummation of all transactions herein authorized, whichever is later, intrastate North Carolina tariffs providing rates for MTS, WATS, and Private Line Channel (including "Dimension 5000," or TELPAK) Services which are identical to those finally approved on November 9, 1983, in Docket No. P-100, Sub 64, for all telephone utilities in the State. Such tariffs shall be clearly marked and limited to a classification designated "INTERLATA LONG DISTANCE SERVICES." The definitions, delineations and restrictions provided by this Order shall be specifically stated and observed.

3. That ATTCOM shall not offer "end-to-end" service; all service shall be interLATA only. The service provided by ATTCOM shall not exceed the scope of service provided by Southern Bell to the interLATA classification at the time the application herein was filed. The provisions of G. S. 62-44 and all present methods of settlements of revenues derived from rates pursuant to G. S. 62-44, shall govern the services and divisions of revenues except that upon approval of access charges by later Order of the Commission the through service shall be performed under tariffed carrier access charges for service in the intraexchange carriers franchise area.

4. That effective on January 1, 1984, or the date of consummation of the transactions approved, whichever is later, Southern Bell Telephone and Telegraph Company's authority to provide intrastate interLATA long-distance telephone service as identified and defined by MFJ and this Commission in this docket and in Docket No. P-100, Sub 65, shall cease and determine and be regarded as cancelled. Southern Bell shall cease and desist from providing such service on and after said date and shall file its tariffs to become effective on said date. Southern Bell's tariffs shall provide the identical long-distance rates finally approved by this Commission on November 9, 1983, except that the Company shall not offer WATS or TELPAK services except as herein authorized after filing pursuant to G. S. 62-134. Southern Bell's tariffs for long-distance service shall contain a section clearly identified as "INTRALATA MTS and PRIVATE LINE RATES" and the LATAs in which service is proposed shall be clearly identified.

5. That the terms "Interexchange Long Distance Service" and "Local Exchange Area" shall not be used interchangeably with the terms "InterLATA," or "IntraLATA," or "LATA," said terms retaining their traditional meaning and usage in this State.

6. That Southern Bell's intrastate operating authority in the State of North Carolina is hereby modified to restrict said Company from rendering interLATA toll telecommunications services on and after January 1, 1984, except as hereinafter provided and subject to any necessary waivers.

7. That Southern Bell and AT&T shall provide, for an interim period, WATS on a statewide basis as a joint offering with the independent telephone companies, and the Telephone Membership Corporations.

8. That Southern Bell and AT&T shall provide, for an interim period, TELPAK (Series 5000 channels) on a statewide basis as a joint offering with the independent telephone companies.

9. That Southern Bell and AT&T shall determine whether a waiver from any authority is needed in order to comply with decretal paragraphs 7 and 8 above and shall earnestly seek any needed waivers for those interim arrangements.

10. That Southern Bell and AT&T shall file to be effective January 1, 1984, tariffs for the interim provision of the joint WATS offerings and joint TELPAK offerings and separate billings which require no change in rates or charges to any subscriber. The TELPAK offering shall include the availability of a split package on interLATA and intraLATA channels.

11. That Southern Bell shall retain offerings of equipment for the disabled in its tariffs and shall continue to offer those services which are available today under present rates and regulations.

12. That ATTCOM shall be totally responsible for interLATA foreign exchange service; that ATTCOM shall modify its tariffs accordingly; and that the present rates for those services shall be billed by or for ATTCOM.

13. That Southern Bell shall retain specific rates and regulations in its tariffs applicable to equipment used with emergency services.

14. That Southern Bell shall retain all equipment in its Private Line Services Tariff for an interim period until the independent telephone companies can provide their own tariff, not to exceed 120 days from January 1, 1984.

15. That each independent telephone company shall revise its tariffs to reflect concurrence in ATTCOM's tariffs. The concurrence provisions should be added to the same sections of the tariffs in which the Southern Bell concurrence provisions presently appear. The revised tariffs shall be filed not later than 30 days from the date of this Order with an effective date of January 1, 1984. The ATTCOM tariff sections with which the independent telephone companies shall concur are as follows:

AT&T Communications of the Southern States, Inc.
General Services Tariff

A7 - Foreign Exchange Service
A11 - Message Telecommunications
A12 - Wide Area Telecommunications Service
A112 - Obsolete Service Offerings-Wide Area Telecommunications Service.

Channel Service Tariff

All Sections

16. That specific language shall be added to ATTCOM's tariffs for the purpose of limiting the application of said tariffs to interLATA services (except for the joint offerings on an interim basis of WATS and TELPAK services).

17. That language shall be added to ATTCOM's tariffs to reflect that the tariffed services are furnished on a joint basis with the independent telephone companies and the telephone membership corporations.

18. That the tariffs of Southern Bell which are proposed to become effective on January 1, 1984, shall be allowed to become effective on January 1, 1984, after modification as directed herein, subject to further review.

19. That the tariffs which were filed herein by ATTCOM with its application on November 1, 1983, after modification as directed herein, shall be allowed to become effective on January 1, 1984, subject to further review.

20. That ATTCOM shall not offer any telecommunications service in by-pass of the franchised intraexchange carriers or telephone membership corporations.

21. That neither this Order nor the Certificate granted hereby shall be construed as authorizing the furnishing of local exchange service.

22. That, except for Southern Bell, the granting of this Certificate to AT&T Communications of the Southern States, Inc., shall not be construed as diminishing or affecting the rights of any telephone firms under their existing authority in this State.

23. That ATTCOM, Southern Bell, and the independent telephone companies shall perform the service to the public after issuance of the Certificate herein in accordance with the findings of fact and conclusions set forth above.

24. That to the extent not granted herein, all motions still pending in this docket are hereby denied.

ISSUED BY ORDER OF THE COMMISSION.
This the 22nd day of December 1983.

NORTH CAROLINA UTILITIES COMMISSION
Sandra J. Webster, Chief Clerk

(SEAL)

DOCKET NO. P-118, SUB 28

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of	
Mid-Carolina Telephone Company, Complainant	) RECOMMENDED ORDER
v.	) DENYING COMPLAINT
Southern Bell Telephone and Telegraph Company, Respondent	)

HEARD IN: Room 217, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina, on Wednesday, April 6, 1983, at 9:30 a.m.

BEFORE: Donald R. Hoover, Hearing Examiner

APPEARANCES:

For the Complainant:

F. Kent Burns, Boyce, Mitchell, Burns & Smith, P.A., Attorneys at Law, P.O. Box 2479, Raleigh, North Carolina 27602
For: Mid-Carolina Telephone Company

For the Respondent:

R. C. Howison, Jr., Hunton and Williams, P.O. Box 109, Raleigh, North Carolina 27602
For: Southern Bell Telephone and Telegraph Company

R. Frost Branon, Jr., General Attorney, Southern Bell Telephone and Telegraph Company, P.O. Box 30188, Charlotte, North Carolina 28239
For: Southern Bell Telephone and Telegraph Company

HOOVER, HEARING EXAMINER: On February 8, 1983, Mid-Carolina Telephone Company (Mid-Carolina) filed with this Commission a Complaint against Southern Bell Telephone and Telegraph Company (Southern Bell). In its Complaint Mid-Carolina alleged that it no longer had an agreement with Southern Bell as to the proper division of toll revenue. Mid-Carolina requested that the Commission order it and Southern Bell to begin determining the toll revenue to which Mid-Carolina is entitled, effective April 1, 1983, by use of the average schedule methodology as opposed to the cost-based methodology which had been in effect prior to April 1, 1983.

On March 7, 1983, an Answer of Southern Bell Telephone and Telegraph Company was filed with the Commission. In its Answer, Southern Bell urged the Commission to find Mid-Carolina's cancellation of the aforementioned contract and its proposed change to the average schedule toll settlement methodology to be unfair and unreasonable. In addition, Southern Bell moved the Commission to order Mid-Carolina to continue to remit toll settlement payments to Southern Bell utilizing the cost-based methodology pending final disposition of this matter.

On March 16, 1983, the Commission set the matter for hearing and ordered Mid-Carolina to continue to remit settlement payments to Southern Bell utilizing the cost-based methodology pending final disposition of the case.

The Complaint was heard on Friday, April 6, 1983, in Raleigh. The Complainant and Southern Bell were represented by counsel. Archie Thomas, President of Mid-Carolina, and Harold Shaffer, Regional Settlements Supervisor for Mid-Carolina, testified on behalf of Complainant. Southern Bell presented the testimony and exhibits of B. A. Rudisill, District Manager - Bell Independent Relations.

Upon consideration of the testimony and exhibits presented at the hearing and the entire record in this docket, the Hearing Examiner makes the following

FINDINGS OF FACT

1. The provision of intrastate toll telephone service to North Carolinians is accomplished through a joint effort by the various telephone companies operating in the State, including the parties to this proceeding. This joint enterprise receives compensation for its services in accordance with a uniform toll rate schedule established by this Commission.

2. The division of revenues produced by the joint rendition of intrastate toll telephone service is accomplished pursuant to contractual arrangements (Traffic Agreements) between and among the providers of such service.

3. Complainant, Mid-Carolina Telephone Company, is one of 27 independent companies providing telephone service to the citizens of North Carolina in conjunction with Southern Bell Telephone and Telegraph Company.

4. Mid-Carolina, as it is constituted now, resulted from the purchase and merger of six independent companies. As of December 31, 1977, Mid-Carolina combined company exchanges totalled 89,855 stations. Over 70% (63,129 stations) of Mid-Carolina's combined company operations has employed the cost-based toll settlement methodology for a period of seven years or longer. Hence, Mid-Carolina and Southern Bell executed a Traffic Agreement which, inter alia, provided for cost-based settlements.

5. For those companies that do not have the ability to make an individual cost study for purposes of toll settlement, one is made on a nationwide basis. The study uses a representative sample of telephone exchanges from throughout the country. Utilizing data from these exchanges, a nationwide average composite cost which ultimately takes the form of a "national average schedule" is determined and is used in the toll settlement process for non-cost companies.

6. The average schedule method is generally intended for smaller companies which are unable, as a practical matter, to develop individual cost studies. However, in the event revenues received under this method are determined not to fairly and accurately reflect costs and expenses for a given company, that company is prospectively required to settle on the cost basis.

7. Those companies which do not settle on the average schedule basis make studies of their own costs. After revenues are distributed to those companies

which settle on the basis of the "national average schedule," the remainder of the toll revenue pool is disbursed to the cost companies.

8. Approximately 90 percent (90%) of the total intrastate toll revenues collected in North Carolina go to companies that determine their toll settlements on the basis of cost studies.

9. Revenue that Mid-Carolina would gain by converting to the average schedule method would result in a direct reduction in revenues to other cost companies.

10. Should Mid-Carolina be allowed to convert to the national average method of settlement, it would earn a return greater than that of the cost companies.

SUMMARY OF EVIDENCE FOR FINDINGS OF FACT

The provision of intrastate toll telephone services to North Carolinians is accomplished through a joint effort by the various telephone companies operating in this State. This joint enterprise receives compensation for its toll services in accordance with a uniform toll rate schedule established by this Commission. Thus, a methodology is required to equitably divide the resultant revenue among the companies who participate in this endeavor. In North Carolina, the division of revenues produced by the joint rendition of intrastate toll telephone service has been accomplished pursuant to traffic agreements between and among the providers of such services.

Complainant, Mid-Carolina, is one of 27 independent companies providing telephone toll services to the citizens of North Carolina in conjunction with Southern Bell. Southern Bell acts as administrator of the intrastate settlement fund. Settlements are multistep in nature. First, revenues are distributed to those companies which settle on the basis of the "national average schedule." Distributions to these companies are determined on the basis of averages obtained by correlating nationwide data obtained from actual cost companies. This method is generally reserved for smaller companies which are unable, as a practical matter, to develop individual cost studies. Once average schedule companies receive their settlement, the remainder of the pool is disbursed to the cost companies. Initially, as provided by the traffic agreements, each company recovers from the fund revenues sufficient to cover costs and taxes as determined under the NARUC-FCC Separations Manual. The residue is distributed among the cost companies so that each receives the same return on its toll-related investment. In the event revenues received under the average schedule method are determined not to fairly and accurately reflect toll-related costs and expenses for a given company, that company is contractually required to settle prospectively on the cost basis.

Since 1978, Mid-Carolina and Southern Bell have agreed to settle on the cost basis.

In December 1982, Mid-Carolina notified Southern Bell of its desire to convert from the cost basis to the average schedule basis of settlement effective March 31, 1983. Southern Bell has not agreed to this conversion.

As previously stated, Mid-Carolina has petitioned the Commission to issue an order allowing it to adopt the average schedule toll settlement method.

Mid-Carolina offers as grounds for the relief it seeks its contention that a traffic agreement between itself and Southern Bell dated July 1, 1978, which provides for the division of toll revenue between the companies on a cost basis is unjust and unreasonable and is imposing a substantial adverse economic burden on its ratepayers and stockholders. Mid-Carolina has determined that it would receive a greater share of toll network revenue if it were permitted to employ the average schedule basis of toll revenue settlement as compared to the cost-based method of toll revenue settlement which is currently in use. Mid-Carolina further contends that the existing cost-based settlement methodology does not reflect its actual cost of providing intrastate toll telephone service.

Southern Bell replied to this complaint on March 7, 1983, answering the specific averments thereof, as well as setting forth affirmative reasons for denying the relief sought. Specifically, Southern Bell requested that the relief sought be denied because the use of actual cost data, where such data is available, is just, fair, and reasonable. In addition, Southern Bell alleged that Mid-Carolina's actual toll costs are below those recompensed under the average schedule methodology. Accordingly, Southern Bell contended it would be unjust, unreasonable, and unfair to require the toll network to reimburse Mid-Carolina on the basis of artificial and nonexistent costs. Southern Bell further responded that the average schedule basis of settlements negotiated between the Bell System and the Independent Telephone Association was never intended to be used by a company, such as Mid-Carolina, which is in a position to, and has determined for many years its actual toll provisioning costs.

CONCLUSIONS

The law of this State clearly provides that the Commission has the authority not only to establish the rates for toll service but to "declare the portion thereof to which each utility affected thereby is entitled" (G.S. 62-44). Apparently the Commission has not heretofore determined what method shall be employed by the utilities in the division of toll revenue. In the past, the division has been made by a method agreed on by the utilities.

Here, there is no longer an agreement between the parties as to how toll revenues should be divided, and both Southern Bell and Mid-Carolina ask in their pleadings that the Commission determine the method which should be used by them after April 1, 1983. Thus, the issue is whether Mid-Carolina has presented facts sufficient to justify the relief it seeks. In deciding this matter the Commission is to be guided by principles of equity and fairness. The Commission must focus on all the surrounding circumstances and judge Mid-Carolina's request in that light. In such determinations, maximum profit is not the proper benchmark; the proper benchmark is parity in treatment among all who share in the toll revenue pool.

The settlement and separations-related procedures utilized by Mid-Carolina and Southern Bell are neither novel nor new. Such methods, including the 1971 Ozark plan changes to the Separations Manual, have been approved by this Commission, the FCC and the USITA. Each of these bodies recognizes that cost-based determinations are preferable to the national average method. In their joint reports, USITA and AT&T have consistently and continually taken the position that, if and when, the return received by any company under the national average schedule fails to be representative of that company's cost, that individual company's actual cost basis should be applied.

In North Carolina the vast majority of revenues are distributed to cost companies with each receiving exactly the same percentage rate of return on each company's net investment devoted to providing toll service. Mid-Carolina has presented no evidence to overcome the presumption of fairness and equity in the cost-based settlement procedures. In short, the present settlement system utilized by the North Carolina companies, although not perfect, is a long-standing, well-settled method which ensures a reasonable, fair, and equitable toll settlement among the various companies. Accordingly, the Hearing Examiner makes the following conclusions:

1. The use of actual cost data as the basis in determining the division of toll revenues, where such data is reasonably available, is just, fair, and reasonable.

2. The methodologies for determining costs outlined in the NARUC-FCC Manual are accepted and used between these and other parties and have been for a number of years.

3. Mid-Carolina has made no showing which justifies a departure from the present cost-based method of settlement.

Based upon the entire evidence of record including reasons set forth herein, the Hearing Examiner concludes that the parties should continue to operate under the terms of the Traffic Agreement entered into in 1978 and, as amended or supplemented from time to time, and continue to settle on the basis of actual costs as determined under that agreement with reference to the NARUC-FCC Separations Manual. Consequently, the Hearing Examiner is of the opinion, and so further concludes, that the Complaint should be denied.

IT IS, THEREFORE, ORDERED as follows:

1. That the Complaint of Mid-Carolina Telephone Company be, and hereby is, denied.

2. That the Traffic Agreement as executed by and between the parties be reinstated and that the parties continue to provide service and divide toll revenues based on the terms of said Traffic Agreement as if never terminated.

ISSUED BY ORDER OF THE COMMISSION.
This the 7th day of July 1983.

NORTH CAROLINA UTILITIES COMMISSION
Sandra J. Webster, Chief Clerk

(SEAL)

DOCKET NO. P-10, SUB 407

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Investigation of the Need to Establish EAS Between Danbury and Walnut Cove to Winston-Salem and Danbury to Sandy Ridge) ORDER

BY THE COMMISSION: The original investigation in this matter was initiated on March 7, 1980, after Attorney Jerry Rutledge transmitted to the Public Staff petitions bearing 2,153 signatures along with a Resolution passed by the Stokes County Board of Commissioners. The petitioners requested Extended Area Service (EAS), involving Stokes, Surry, Rockingham, and Forsyth Counties; three regulated telephone companies, Central Telephone Company, Mid-Carolina Telephone Company, Southern Bell Telephone and Telegraph Company; and one telephone membership corporation, Surry Telephone Membership Corporation.

The petitions and Resolution specifically requested the following EAS arrangement:

1. Between Danbury and the exchanges of Winston-Salem, King, Rural Hall, Sandy Ridge, Madison, Pilot Mountain, Westfield, and Shoals. (Danbury already had EAS to Walnut Cove and Quaker Gap.)

2. Between Walnut Cove and the exchanges of Winston-Salem, King, Rural Hall, Madison, and Sandy Ridge. (Walnut Cove already had EAS to Danbury, King, Walnut Cove, and Winston-Salem.)

3. Between Madison and the Exchange of Quaker Gap. (Madison already had EAS to Sandy Ridge and Quaker Gap had EAS to Danbury, King, Walnut Cove, and Winston-Salem.)

4. Between Pilot Mountain and the exchanges of King and Quaker Gap. (Pilot Mountain already had EAS to Westfield and Shoals.)

5. Between the exchanges of King and Westfield.

Based on the interest in this EAS matter and the extensive nature of the requested EAS, the Commission set the request for investigation and public hearing in Docket No. P-10, Sub 391. All affected telephone customers were notified of the time and place of the hearing through bill inserts which included the requested EAS arrangements and the proposed monthly rate increases associated with providing the service. The stated purpose of the hearing was to determine the following: (a) The need for the requested EAS, (b) the extent of the public's interest in the requested EAS, (c) whether or not an EAS poll should be conducted of the affected subscribers.

The matter came on for hearing before a Panel of Commissioners on February 24, 1983, in Danbury. Public witnesses, company witnesses and the Public Staff were present and stated their respective positions. On March 25, 1981, the Public Staff filed Comments and Recommendations moving the Commission to issue an interim Order finding, inter alia, that further consideration of EAS is justified as follows:

a. Between the Danbury and Winston-Salem exchanges.
b. Between the Danbury and Sandy Ridge exchanges.
c. Between the Walnut Cove and Winston-Salem exchanges.

On April 13, 1981, the Comments of Southern Bell Telephone and Telegraph Company were filed with the Commission. Southern Bell requested that the Winston-Salem exchange be excluded from any further consideration in this docket since no known Winston-Salem subscribers attended the hearing or requested the EAS. Additionally, the Southern Bell witness had testified that 98.6% of the Winston-Salem subscribers made no calls to Danbury, and 95.7% of the Winston-Salem subscribers made no calls to Walnut Cove.

After considering the evidence in its entirety, the Panel concluded that the record did not reflect a sufficient community of interest to justify the increase in subscriber rates which would be necessary to provide all of the services requested. Thus, by Order issued May 27, 1981, the request to implement the proposed EAS arrangement was denied. However, the Commission ordered Central Telephone Company to file proposed Optional Toll Calling Plan (OTCP), rates for the exchanges Danbury to Winston-Salem and Danbury to Sandy Ridge. Subsequently, the Commission suspended Central's proposed OTCP pending a decision in Docket P-10, Sub 400 (Central Telephone Company's Application for a General Rate Increase.)

On August 27, 1981, the Commission issued a Notice of Decision and Order in Docket No. P-10, Sub 400. The EAS Panel then issued an Order establishing OTCP rates from Danbury to Sandy Ridge and from Danbury to Winston-Salem. The Panel then closed Docket No. P-10, Sub 392.

On October 8, 1981, Mr. Jerry Rutledge, Attorney, submitted a copy of a resolution passed by the Stokes County Commissioners urging the Commission to establish Extended Area Service between the following exchanges:

1. Danbury and Winston-Salem
2. Danbury and Sandy Ridge
3. Walnut Cove and Winston-Salem

The Commission, on March 29, 1982, issued an Order setting the matter to be heard on May 12, 1982, in Danbury and requiring that Public Notice of the hearing be published in newspapers having general coverage in Winston-Salem and Danbury. The hearing was held as scheduled. Central Telephone Company offered the direct testimony of Jerry G. Harris, Southern Bell Telephone and Telegraph Company offered the direct testimony of Robert Freidlander and the Public Staff represented approximately 23 public witnesses who testified regarding the proposed EAS in Stokes County. Subsequently, the Commission issued an Order requiring that all affected subscribers be polled to determine their interest in the proposed EAS and their willingness to pay the basic monthly increase necessary to offset some of the costs of the service.

On September 16, 1982, Central Telephone Company and Southern Bell Telephone and Telegraph Company filed the following polling results:

Walnut Cove to Winston-Salem

1.	Number of eligible customers	2,056
2.	Number of ballots returned	1,101 or 53.6% of eligible
3.	Number of customers voting for EAS	913 or 82.9% of Ballots returned
4.	Number of customers voting against EAS	172 or 15.6% of Ballots returned
5.	Number of invalid ballots	16 or 1.5% of Ballots returned

Sandy Ridge to Danbury

1.	Number of eligible customers	894
2.	Number of ballots returned	479 or 53.6% of eligible
3.	Number of customers voting for EAS	344 or 71.8% of Ballots returned
4.	Number of customers voting against EAS	123 or 25.7% of Ballots returned
5.	Number of invalid ballots	12 or 2.5% of Ballots returned

Danbury to Winston-Salem and Sandy Ridge

1.	Number of eligible customers	1,199
2.	Number of ballots returned	632 or 52.7% of eligible
3.	Number of customers voting for Winston-Salem and Sandy Ridge	293 or 46.4% of Ballots returned
4.	Number of customers voting for Sandy Ridge only	58 or 9.2% of Ballots returned
5.	Number of customers voting for Winston-Salem only	124 or 19.6% of Ballots returned
6.	Number of customers voting against EAS	152 or 24.1% of Ballots returned
7.	Number of invalid ballots	5 or .8% of Ballots returned

Southern Bell Telephone and Telegraph Company

	Winston-Salem to Danbury		Winston-Salem to Walnut Cove	
	#	%	#	%
1. Number of Lines Voting	14,626	100.0	14,626	100.0
2. Number in Favor of EAS	2,023	13.8	2,041	14.0
3. Number Not in Favor of EAS	12,461	85.2	12,484	85.3
4. Number Returned No Vote	142	1.0	101	.7

On November 23, 1982, the Panel, having analyzed the polling results and all other evidence in this docket, issued an Order concluding that EAS should be implemented between the Danbury and Sandy Ridge exchanges. On the other hand, the Panel stated that due to the magnitude of Winston-Salem subscribers voting against the proposed EAS, the Commission could not in good conscience impose EAS upon those subscribers. Instead, the Commission ordered Central Telephone Company to offer optional toll calling plan charges calculated so as not to exceed 50% of the day-time toll rate.

By letter filed December 20, 1982, Central Telephone Company notified the Commission that the projected date to establish EAS between Danbury and Sandy Ridge is July 1, 1983.

On February 23, 1983, the Public Staff filed a Motion for Reconsideration and Oral Argument which was granted by Order of the Commission issued March 3, 1983.

Following the oral argument held on March 23, 1983, the Commission reviewed the evidence in its entirety and having carefully considered the argument of able counsel, concludes that the Order issued November 23, 1982, in this docket should be affirmed. The requested EAS involved the following exchanges, (1) Danbury and Winston-Salem, (2) Danbury and Sandy Ridge, (3) Walnut Cove and Winston-Salem. Moreover, the result of the poll of affected subscribers revealed that of the 14,626 Winston-Salem customers responding, 82.9% opposed the EAS. Furthermore, of the 632 Danbury respondents, only 46.4% voted for the total EAS between Danbury, Winston-Salem, and Sandy Ridge.

The Public Staff indicates that only 16% of the eligible Winston-Salem subscribers returned ballots and 14% of the respondents were against the EAS. The Commission finds unpersuasive the Public Staff's deduction that the opposition of 12,000 Winston-Salem respondents should be disregarded because more Winston-Salem subscribers did not respond. A vote was held and a great majority (82.9%) voted against the proposal even at the slight charge of 3¢ to Danbury, 9¢ to Walnut Cove or 12¢ combined.

IT IS, THEREFORE, ORDERED that the November 23, 1982, Order issued in this docket Granting in Part and Denying in Part the EAS Petition, is hereby affirmed.

ISSUED BY ORDER OF THE COMMISSION.
This the 26th day of April 1983.

NORTH CAROLINA UTILITIES COMMISSION
Sharon Credle Miller, Deputy Clerk

(SEAL)

Dissenting:

Chairman Robert K. Koger
Commissioner Leigh H. Hammond
Commissioner Edward B. Hipp

DOCKET NO. P-7, SUB 670

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of	
Application of Carolina Telephone and Telegraph Company for Adjustments and Changes in its Rates and Charges Applicable to Intrastate Telephone Service	) ORDER GRANTING) PARTIAL INCREASE) IN RATES

HEARD IN: Knob Creek Recreation Center, Elizabeth City, North Carolina, on January 25, 1983, at 7:00 p.m.

Administration Building, Auditorium, Tarboro, North Carolina, on January 26, 1983, at 11:00 a.m.

City Hall Courtroom, New Bern, North Carolina, on January 26, 1983, at 7:30 p.m.

City Hall, City Council Room, Fayetteville, North Carolina, on January 28, 1983, at 10:00 a.m.

Commission Hearing Room, Second Floor, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina, on February 1 - 4, February 8, and February 10, 1983

BEFORE: Commissioner Douglas P. Leary, Presiding; Chairman Robert K. Koger and Commissioner Sarah Lindsay Tate

APPEARANCES:

For the Applicant:

Robert C. Howison, Jr., and Edward S. Finley, Jr., Hunton & Williams, Attorneys at Law, The Branch Banking and Trust Building, Post Office Box 109, Raleigh, North Carolina 27602

Dwight W. Allen and Robert C. Voight, Attorneys at Law, Carolina Telephone and Telegraph Company, 720 Western Boulevard, Tarboro, North Carolina 27886

For the Using and Consuming Public:

Antoinette R. Wike and Karen E. Long, Staff Attorneys, Public Staff - North Carolina Utilities Commission, Post Office Box 991, Raleigh, North Carolina 27602

Robert H. Bennink, Jr., Assistant Attorney General, North Carolina Department of Justice - Attorney General, Post Office Box 629, Raleigh, North Carolina 27602

BY THE COMMISSION: On August 30, 1982, Carolina Telephone and Telegraph Company (hereinafter called Carolina, the Company, or the Applicant) filed an application with the Commission for authority to increase certain elements of its intrastate rates and charges. The Company's initial application, which asked that the rates become effective on September 30, 1982, proposed an

annual increase in gross revenues of $37,764,716 based upon the 12 months ended March 31, 1982. In supplemental testimony filed with the Commission on January 3, 1983, and amended at the hearing, the Company indicated that the increase in gross revenues needed to give the Company an opportunity to earn its requested rate of return had decreased from $37,764,716 to $33,949,398, due primarily to increases in the expected level of intrastate toll revenues and changes in capital costs.

On September 4, 1982, the Commission issued its Order declaring the matter to be a general rate case under G.S. 62-137, suspending the effective date of the proposed rates for 270 days pending investigation and hearing, and requiring the Company to give public notice of the hearings which were scheduled for Elizabeth City, Tarboro, New Bern, Fayetteville, and Raleigh.

On September 30, 1982, the Public Staff filed Notice of Intervention on behalf of the using and consuming public. A Notice of Intervention was also filed by the Attorney General on October 8, 1982.

The matter came on for hearing as scheduled in the Commission's Order Setting Hearing. During the course of the hearings, the Commission heard from the following public witnesses:

Elizabeth City - Raleigh Carver, Bill Cox, Shirley Perry, Paul Kraeuter, Gerald Tyler, Vincent Lucente, Walter Tatum, Macon Johnson, and Frank Swindell.

Tarboro - Bobby Shelton Cross, Steve Randolph Jones, Barbara Heilbroner Bone, Samuel Bruce Petteway, D.D. Garrett, and Thayer D. Forsht, Jr.

New Bern - Joshua T. Jones, Tom White, and Ann Tiernan.

Fayetteville - John Corbett, Charley Brindel, R.H. Beatty, George Erwin, Albert J. Guihani, Eloise Haggard, Charles Davis, Carolyn Weaver, Caletha Powell, Tom Scanlan, Lt. Col. Jochen H. Ewing, Katie Fouchee, George R. Horace, Louis Spillman, and James Warner.

Raleigh - John Redmond, Robert Brooks, and Frank Sinnott.

At the hearings in Raleigh, Carolina offered testimony from the following witnesses: T.P. Williamson, Vice President-Administration for Carolina, concerning the Company's overall operations, effect of federal regulatory changes, representative level of intrastate toll revenues, and the need for additional revenues; J.B. Teal, Vice President-Operations for Carolina, concerning the quality of service provided by the Company and the need for more and better grades of service; James H. Vander Weide, Professor of Finance at the Fuqua School of Business at Duke University, concerning the appropriate capital structure, cost of capital, and fair rate of return; and Kenneth F. Tarleton, Assistant Controller for Carolina, concerning intrastate operating results and the appropriate levels of revenues, expenses, and investments. The Company also offered testimony from the following witnesses: Robert E. Baker, Jr., Assistant Vice President-Rate Case Matters, United Telephone System, Inc., concerning the various support services provided by United Telephone System, Inc., to Carolina, the purchase of materials and supplies from North Supply Company, and the use of subsidiary rather than the consolidated capital structure; J. Richard Owen, Local

Revenue Requirements Manager for Carolina, concerning the revenue effect of and philosophy utilized in developing the Company's rate design proposals; and Warren D. Hannah, Cost of Service Supervisor for Carolina, concerning time and materials charges for service connection work functions performed on the customers' premises.

Testimony on behalf of the Public Staff was presented by the following witnesses: Thi-Chen Hu, Communications Engineer, relating to the Public Staff's evaluation of the service being provided by the Company; Karyl J. Lam, Staff Accountant, Accounting Division, Communications Section, relating to the appropriate levels of revenue, expenses, and investments; Curtis Toms, Jr., Supervisor, Accounting Division, Communications Section, relating to the allocation of certain Phone Shop and business office investments, accumulated depreciation, and operating expenses between regulated and unregulated operations; Jocelyn M. Perkerson, Accountant, Accounting Division, relating to the exclusion of certain general service and license contract expenses from the Company's cost of service; Robert Weiss, Economist, Economic Research Division, relating to capital structure, cost of capital, and fair rate of return; William J. Willis, Jr., Engineer, Communications Division, relating to rate design proposals and end-of-period local and miscellaneous revenues, and Hugh L. Gerringer, Engineer, Communications Division, relating to the apportionment of the Company's operations between interstate and intrastate jurisdictions and the representative level of intrastate toll revenues.

Following presentation of the Public Staff's testimony, the Company offered rebuttal testimony from Dr. Vander Weide, witness Baker, and witness Tarleton, all of whom had testified previously on behalf of the Company.

Based on the foregoing, the verified application, the testimony and exhibits admitted at the hearing, and the entire record in this proceeding, the Commission makes the following

FINDINGS OF FACT

1. Carolina is a duly franchised public utility serving all or part of fifty (50) counties in North Carolina, subject to the jurisdiction of the Commission, and is properly before the Commission for a determination of the justness and reasonableness of its proposed rates and charges.

2. The test period used by the parties to this proceeding and established by the Commission is the 12 months ended March 31, 1982, adjusted for known certain changes based on events and circumstances occurring prior to the close of the hearings. Carolina initially filed for an increase in its intrastate rates and charges of $37,764,716 which was ultimately amended by the Company in its Proposed Order to $24,725,023.

3. The overall quality of service provided by Carolina to its customers is adequate.

4. The reasonable original cost of Carolina's plant used and useful, or to be used and useful within a reasonable time after the test period, in providing service to its customers, less that portion of the cost consumed by previous use recovered through depreciation expense, less cost-free capital, plus the reasonable cost of investment in plant under construction is $426,347,717.

5. The reasonable allowance for working capital is $6,466,219.

6. The reasonable original cost rate base is $432,813,936. This amount consists of net telephone plant in service and short-term construction work in progress of $426,347,717 plus a reasonable allowance for working capital of $6,466,219.

7. The reasonable level of test year operating revenues after accounting, pro forma, and end-of-period adjustments is $252,549,082 net of uncollectibles under present rates and under rates proposed by Carolina in its originally filed application would have been $290,242,045. The representative level of intrastate toll revenues under existing rates amounts to $95,125,295.

8. The reasonable level of test year operating revenue deductions after accounting, pro forma, and end-of-period adjustments is $208,057,732. This amount includes $46,570,255 for actual investment currently consumed through reasonable actual depreciation on an annual basis.

9. The capital structure appropriate for use in this proceeding is as follows:

Long-term debt	50.25%
Preferred stock	1.35%
Common equity	48.40%
Total	100.00%

10. The reasonable overall rate of return which Carolina should have the opportunity to earn is 11.82%. Such fair rate of return is based on an embedded cost of debt of 8.51%, an embedded cost of preferred stock of 11.7%, and a return on common equity of 15.25% weighted by the capitalization ratios hereinabove found fair.

11. Based on the foregoing, it is just and reasonable to allow Carolina to increase its rates and charges to produce $13,956,465 additional annual gross revenues. The increase is required in order for the Company to have a reasonable opportunity to earn the 11.82% rate of return on its rate base which the Commission has found just and reasonable.

12. The schedule of rates and charges proposed by Carolina is unjust and unreasonable. Rates, charges, and regulations to be filed in accordance with the guidelines contained herein will be just and reasonable.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 1 AND 2

The evidence for these findings is found in the verified application, testimony and exhibits, and the record as a whole. These findings are essentially informational, procedural, and jurisdictional in nature and were not contested at the hearing.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 3

The evidence for this conclusion is contained in the testimony of four public witnesses, the testimony and exhibits of Company witness Teal, and the testimony and exhibits of Public Staff witness Hu.

Company witness Teal reviewed the numerous service measurements that the Company utilizes in evaluating its overall quality of service. Witness Teal testified that previous studies indicated that the Company's overall quality of service met or surpassed the standards used by the Public Staff in its evaluations and that recent studies indicate that high levels of service are being maintained. Witness Teal offered a series of exhibits showing a number of service indicators used by the Company and Public Staff and, in his opinion, the exhibits revealed that the Company continues to maintain a consistent level of good service.

Witness Teal also reviewed a number of technological innovations which the Company has established to assure the continued good quality of its service. He noted that a computer controlled maintenance information system (called 4-Tel) has been in use since 1978 and will be available throughout the Company by the end of 1983. The system, which is used for preventive maintenance and repair of subscriber plant, performs nightly testing of access lines so that, in many instances, troubles are detected and cleared before the customer is aware that anything is wrong. Other systems which have been implemented include, but are not limited to, a Centralized Automatic Reporting on Trunk System (called CAROT) for automatic transmission and operational testing of trunks between central offices and an Individual Circuit Usage and Peg Count System (ICUP) for studying usage of individual circuits and selected items of equipment in central offices.

The service testimony of the Public Staff was presented by witness Hu. His review of the Company's quality of service included field inspections and tests of switching and trunking facilities; measurements of answer time for operators, directory assistance, repair and business offices; an analysis of statistics relating to the Company's service; and a review of subscriber complaints received by the Commission and the Public Staff. Witness Hu then compared his findings with the service criteria followed by the Public Staff and presented his conclusions concerning the Company's overall quality of service.

Witness Hu summarized the results of his evaluation of the Company's quality of service in a series of exhibits. Although the exhibits revealed isolated instances where a particular service objective was not met for a given exchange at a specific moment in time, witness Hu's testimony revealed that, generally, the Company's overall quality of service met or surpassed the service objectives used by the Public Staff.

During public hearings, four public witnesses testified concerning service problems which they had experienced. Prior to the close of the hearings, the Company conducted a service investigation of each service complaint and presented a report to the Commission detailing the results of its investigation. In those instances where a trouble was found, repairs were made. In those instances where tests revealed no service problems, the customer was asked to contact the Company in the event of a future service problem.

Based on the foregoing evidence, the Commission concludes that the overall quality of service provided by the Company is adequate.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 4

Company witness Tarleton and Staff witness Lam presented testimony and exhibits concerning the original cost of Carolina's intrastate net telephone plant in service. The following chart summarizes the amount which each of the witnesses contends properly represent those costs:

Item	Company Witness Tarleton	Staff Witness Lam
Telephone plant in service	$707,437,171	$707,491,949
Telephone plant under construction	7,546,187	-
Plant acquisition adjustment	384,594	384,594
Less: Accumulated Depreciation & amortization	212,142,134	212,155,290
Unamortized investment tax credit (Pre-1971)	736,472	736,472
Accumulated deferred income taxes	74,565,543	74,565,543
End of period customer deposits	1,617,708	1,617,708
Net telephone plant in service	$426,306,095	$418,801,530

The first difference between the amounts presented by the two witnesses relates to investment in telephone plant in service and amounts to $54,778. This difference arises from two adjustments. The first difference amounts to $102,323 and arises solely from the adjustment made by the Public Staff to reinstate investment associated with the yellow pages section of the Company's telephone directory. The Company in its original filing made adjustments in this case to remove investments, revenues, and expenses associated with advertisements in the yellow pages section of its telephone directories. Company witness Williamson testified that the advertising section of the directory is not essential to the provision of good telephone service, and that without directory advertising a fully adequate and efficient service would still exist. Witness Williamson testified that directory advertising exists in a market that is fully open to competition. Examples of this competition given by witness Williamson include newspapers and other publications, radio, television, cable television, billboards, advertising specialties, and yellow page type classified telephone directories published by others in the Company's service area. The Company also maintained that the costs of advertisements in the yellow pages should be treated in the same manner as those of other nonregulated activity such as the Company's sale of terminal equipment, which the Commission excludes in determining the Company's appropriate cost of service.

Public Staff witness Lam made adjustments reinstating the investments, revenues, and expenses associated with the yellow pages. The Public Staff maintains that the yellow pages are an integral part of providing telephone service. Witness Lam stated that the origination of, the use of, and the market for the yellow pages are directly related to providing telephone service.

The issue of whether the investments, revenues, and expenses arising from advertising in the yellow pages should be included in the cost of service has been litigated in the Company's last case, Docket No. P-7, Sub 662, and in cases of other telephone companies. During the hearing in this case the North Carolina Supreme Court issued its decision in North Carolina ex rel. Utilities Commission v. Southern Bell, ---- N.C. --- (February 8, 1983).

In that case, the Supreme Court ruled that it is permissible for the Utilities Commission to include investments, expenses, and revenues arising from yellow pages advertising in setting rates for Southern Bell.

In light of the Supreme Court ruling, the Company included investments, revenues, and expenses arising from yellow page advertising in their calculation of gross revenue requirements, as presented in their Proposed Order. Hence, the Commission concludes that investments, revenues, and expenses associated with yellow pages advertising should be included in the Applicant's calculation of revenue requirements used in establishing fair and reasonable rates in this proceeding.

The other difference between the Public Staff and the Company related to investment in telephone plant in service amounts to $(47,545). This difference arises from a difference in the allocation factor used to determine unregulated investment in the Company's Phone Shops. The Company used a factor of 5.0521%, while the Public Staff used 6.6788%. As discussed under the Evidence and Conclusions for Finding of Fact No. 8, the Commission rules that the Public Staff's allocation factor is appropriate for use in this proceeding.

The next difference between the parties arises from a difference in telephone plant under construction (less than one year). The Company included the full amount of telephone plant under construction at March 31, 1982, that was estimated to be completed within one year, which amounted to $7,546,187. The Applicant did not include any long-term construction work in progress (CWIP) in rate base. The Public Staff made an adjustment to eliminate all telephone plant under construction from rate base. Company witness Williamson listed some of the projects giving rise to the short-term construction work in progress. He testified that the projects are necessary in order for the Company to meet customers' service needs. He further testified that, if these costs are not included in the Company's rate base and considered in setting rates, the Company's rates could not produce the return approved by the Commission in this proceeding.

Public Staff witness Lam testified that the Company's argument that most of the construction would be completed and in service by the close of the hearing was, in effect, asking for an addition to rate base as an update to plant in service rather than as construction work in progress. She testified that to allow this additional plant in service would violate both the test year concept and the matching concept of ratemaking since the Company had presented no evidence detailing the changes in revenues, expenses, deferred income taxes, or other items which would be expected to occur as a result of the addition of new telephone plant. Public Staff witness Weiss also testified that elimination of the proposed construction work in progress from rate base would not adversely affect the Company's financial status.

Company witness Tarleton testified in rebuttal to the Public Staff position. Witness Tarleton testified that, even though the North Carolina General Statutes would permit inclusion of the full amount, the Company included only short-term CWIP in rate base, in part, due to treatment advocated by the FCC Uniform System of Accounts. Short-term CWIP does not accrue interest during construction under the Uniform System of Accounts because the FCC assumes that such investment will be included in rate base.

After examining all of the evidence on this issue, the Commission concludes that the amount of construction work in progress included by the Company in rate base in this case is appropriate. In determining the amount of construction work in progress to be included in rate base, G.S. 62-133 requires the Commission to include CWIP in rate base if the Commission determines that doing so is in the public interest and necessary to the financial stability of the utility. The treatment advocated by the Company is in the public interest because the ratepayers are paying a return only on plant which will be providing them with service in the immediate future.

In reaching this decision, the Commission also recognizes that the FCC Uniform System of Accounts, which this Commission follows and has not chosen to modify or reject, specifies that short-term CWIP shall not accrue allowance for funds during construction in anticipation of including short-term CWIP in rate base. Failure to allow the Company to include short-term CWIP in rate base would leave the Company little alternative but to begin immediately accruing AFUDC on these construction expenditures in direct contradiction of the FCC Uniform System of Accounts which the Commission has consistently followed. This would force the Company to maintain additional books, at an additional expense to the ratepayer, if it began to accrue AFUDC on this CWIP since in its settlements for interstate toll purposes with Southern Bell it must adhere to the FCC Uniform System of Accounts. Hence, the Commission concludes that it is in the public interest and necessary to the financial stability of the Applicant to include the short-term CWIP in rate base.

The next difference between the parties is a difference in the accumulated depreciation and amortization reserve and amounts to $13,156. The Public Staff made an adjustment to the Company's original filing to include the per books depreciation reserve associated with the yellow pages investment of $27,387. As discussed previously, the Commission accepts this treatment of investment related to yellow pages advertising and therefore approves this adjustment. The second adjustment to the depreciation reserve is an adjustment made by the Public Staff to remove depreciation expense related to the additional investment which the Public Staff has allocated to nonregulated sales. The amount of this adjustment is ($14,231). As discussed elsewhere herein, the Commission accepts the Public Staff's allocation factor for determining nonregulated sales and therefore determines that the appropriate amount of depreciation and amortization reserve for use in this case is $212,155,290.

In summary, the Commission concludes that the proper level of original cost investment in telephone plant in service for use in the proceeding and short-term CWIP is $426,347,717, consisting of the following:

Item	Amount
Telephone plant in service	$707,491,949
Telephone plant under construction (less than one year)	7,546,187
Plant acquisition adjustment	384,594
Less: Accumulated depreciation and amortization	212,155,290
Unamortized investment tax credit (Pre-1971)	736,472
Accumulated deferred income taxes	74,565,543
End of period customer deposits	$ 1,617,708
Net original cost of telephone plant	$426,347,717

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 5

Company witness Tarleton and Public Staff witness Lam each presented different amounts of working capital allowance as shown by the chart below:

Item	Company Witness Tarleton	Staff Witness Lam
Cash	$3,899,822	$3,899,822
Materials	7,544,502	7,544,502
Customer Funds Advanced Through Operations	(3,930,589)	(3,930,589)
Accounts Payable	(1,047,516)	(799,718)
Total	$6,466,219	$6,714,017

The only difference in the level of working capital allowance is in the amount of accounts payable that the two parties used. The Company, in determining working capital allowance, reduced its need for working capital by $247,798 for the portion of short-term telephone plant under construction that was included in accounts payable at the end of the test period. The Public Staff did not include short-term telephone plant under construction in the calculation of original cost rate base. Consequently, it did not include the accounts payable associated with short-term telephone plant under construction in the determination of working capital allowance. For reasons set forth in the Evidence and Conclusions for Finding of Fact No. 4, the Commission determines that short-term telephone plant under construction should be included in the rate base; therefore, the Commission also concludes that the associated accounts payable should be used in the determination of the appropriate level of working capital. Therefore, the Commission concludes that $6,466,219, the working capital allowance shown by the Company, is proper.

There is one other element of the rate base which warrants the Commission's attention, even though there was no disagreement between the Company and the Public Staff as to the amount which should be included in the rate base. This is the working capital allowance, or more precisely, the customer funds advanced for operations component of the working capital allowance. Witness Lam testified that the lead-lag study upon which the Company based its calculation of customer funds advanced for operations was based upon the test year of 1974 and reflected the Company's payment practices at that time. Witness Lam further testified that, even though both the Company and the Public Staff have made changes to the study to reflect known changes in payment practices, she was concerned that the total study may not accurately reflect the Company's overall payment practices. The Commission shares this concern. Since a lead-lag study provides a reasonable method for computing funds advanced for operations only so long as it reflects the Company's current payment practices, it is imperative that the study be kept up to date. Therefore, the Commission will order the Company to prepare a new lead-lag study, based upon a current test year, which reflects its current payment practices for inclusion in its next general rate case filing.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 6

The Commission, having previously concluded in Finding of Fact No. 4 that the net reasonable original cost of the Company's investment in telephone plant for use in this proceeding is $426,347,717, including $7,546,187 for

telephone plant under construction (less than one year), and in Finding of Fact No. 5 that the reasonable allowance for working capital is $6,466,219, concludes that the proper original cost rate base for use in this proceeding is $432,813,936.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 7

Evidence concerning the proper end-of-period level of operating revenues was presented through the testimony and exhibits of Company witnesses Williamson and Tarleton and Public Staff witnesses Gerringer, Willis, and Lam. The differences in the amounts proposed by the parties are shown in the chart below:

	Company	Public Staff
Local service revenue	$143,537,618	$143,558,214
Toll service revenue	96,421,098	98,089,150
Miscellaneous revenue	2,850,449	14,160,141
Uncollectibles	(1,421,602)	(294,568)
Total operating revenues	$241,387,563	$255,512,937

The only difference between the parties related to local service revenues is that Public Staff witness Lam included $20,596 in additional annual local revenue resulting from the regrouping of the Benson and Topsail Island exchanges, effective October 15, 1982, and approved by the Commission in Docket No. P-7, Sub 667-D. The Company did not disagree with this adjustment and, accordingly, the Commission concludes that the proper level of local service revenue for use in this proceeding is $143,558,214.

Witnesses for the Company and the Public Staff disagreed as to the proper level of end-of-period toll revenues for use in this proceeding. While both parties employed the same methodology for estimating the toll revenues, the disagreement centered around the appropriate intrastate toll settlement ratio to be employed in applying that methodology and whether or not, or to what extent, the impact of post-test-period pro forma adjustments should be incorporated into the calculations.

Company witness Williamson testified that the total intrastate toll revenues received by Carolina arise through settlement contracts, as is also true of other jurisdictional companies which derive their toll revenues on a cost basis. The total toll revenues received consist of a reimbursement of intrastate toll allocated expenses, including taxes, plus a return on intrastate allocated toll investments. The basis of the return is the intrastate toll settlement ratio which is calculated only after expenses are paid and is therefore dependent upon the residual revenues available in the settlement "pool" after expenses are paid. Witness Williamson testified that amounts paid out of the pool for expenses lowers the amount available for return thereby lowering the settlement ratio.

Witness Williamson stated that in Carolina's last rate case, Docket No. P-7, Sub 662, the intrastate toll revenues were overestimated by the Commission in setting rates in that proceeding. Witness Williamson asserted that overstatement resulted from employment by the Commission of a settlement ratio of 11%.

At the hearing Public Staff witness Gerringer proposed an end-of-period level of intrastate toll revenues of $100,197,897, while Company witness Tarleton proposed $96,421,098. It should be noted that the two figures do not fully reflect the toll revenue difference between the parties since the Company includes uncollectibles in the toll revenue calculation while witness Gerringer did not. Witness Gerringer included the toll revenue effect of all test period expenses, the effect of post-test-period pro forma expense adjustments and a toll settlement ratio of 11.88%. Witness Tarleton excluded the toll revenue effect of the post-test-period pro forma expenses and employed a toll settlement ratio of 11.47%.

Witness Tarleton testified that his toll revenue estimate consisted of determining the toll expense reimbursement, including taxes, to be received through settlements on an end-of-period basis and adding the return amount to be received based upon the product of the end-of-period toll settlement base and the average of the actually achieved toll settlement ratios for the eight months for which actual results have become known since the current toll rates became effective. He stated that this methodology recognizes actual levels of expenses, taxes, investments, and returns.

Witness Gerringer testified that his toll revenue estimate was produced by determining the settlement revenues to be received by Carolina for reimbursement of expenses and taxes plus a return on the end-of-period settlement base at a 11.88% settlement ratio. Witness Gerringer explained that he used the post-test-period pro forma expenses as well as the actual test year levels without adjusting his settlement ratio estimate to reflect the impact, if any, those post-period expenses would have on the settlement ratio. His estimated settlement ratio was obtained by averaging settlement ratios falling six months on each side of the end of the test period adjusted upward for the effects of the toll rate increase granted in Docket No. P-100, Sub 57, and downward due to increased settlements paid from the statewide pool to noncost settlement companies. Witness Gerringer testified that this methodology was consistent with procedures he had employed in Carolina's previous general rate case proceedings.

It is clear from analysis of the evidence presented by the parties that the difference existing in their similarly constructed estimates of the end-of-period toll revenues arises from three causes. First, the parties are in dispute as to the appropriate levels of test year expenses and investments appropriate for setting rates in this proceeding. Those differences create differing estimates of the representative level of toll revenues due to the impact of those cost elements through the settlement process. Second, the parties differ in their method of estimating the appropriate toll settlement ratio for use herein. Third, the parties differ as to whether or not the post-test-period expense pro forma adjustments proposed by the Company and considered by the Commission in setting rates herein, also should be considered as to their toll revenue effects with or without adjustment of the toll settlement ratio found appropriate.

It is not necessary to discuss here the first difference which arises from disputed rate base and test period expense levels. These issues are resolved elsewhere herein and their toll revenue effects clearly proceed from application of the toll revenue estimation methodology employed by both the Public Staff and the Company in this proceeding.

The second difference between the parties, concerning the appropriate intrastate toll settlement ratio for use herein, warrants analysis. It was shown that the settlement ratio is subject to wide monthly fluctuations and that past estimates have sometimes missed by significant margins. Accordingly, it is desirable to develop the end-of-period settlement ratio based upon the latest actually achieved data which is most nearly representative of conditions which will exist when the rates to be set herein will apply.

The toll settlement ratio estimation method employed by the Public Staff developed a ratio based upon averaging the actually achieved ratios falling six months on each side of the end-of-test-period at March 31, 1982. Since existing toll rates did not become fully effective until March 1982, however, the Public Staff's estimate required adjustment to reflect the estimated effects of current toll rates on the ratios for the earlier months considered and also for the estimated effects of settlement changes involving the noncost contract telephone companies. The final Public Staff toll settlement ratio estimate was 11.88%.

The Company's toll settlement ratio estimate as contained in its supplemental filing was based entirely upon results actually achieved since the current toll rates became effective in March 1982, and consisted of the average of data from an eight-month period ended October 30, 1983. The Company ultimately adjusted its toll settlement ratio to 11.35%, to reflect actual data for the nine-month period ended November 30, 1982, and estimated data for the month of December 1982.

The Commission is very aware of the growing competitive pressures in the Applicant's interstate and intrastate toll marketplace. In addition, the Commission is cognizant of the fact that the Applicant has generally failed to achieve its allowed toll settlement ratio in recent years, particularly after consideration of the effects of general intrastate toll increases during this same period of time. Based on the foregoing, the Commission concludes that the fair and reasonable toll settlement ratio to be used in this proceeding is 11.35%.

The third difference between the parties concerning the appropriate level of intrastate toll revenues involves whether or to what extent various post-test-period pro forma expense adjustments proposed by the Company should be considered in estimating the representative end-of-test-period toll revenues. Clearly, increasing expense levels tend to increase the expense reimbursement portion of toll settlements. Conversely, the full impact of these expenses on the Applicant's toll settlement ratio is not nearly so clear. Witness Gerringer stated that the settlement process is a dynamic one which involves many companies whose ongoing level of costs for settlement purposes is not presented into evidence in this case. Based on the foregoing and the entire evidence of record, the Commission concludes that the Public Staff's treatment of after-period adjustments in the intrastate toll calculation is inappropriate for determining the Applicant's representative level of toll revenues in this proceeding.

The Commission has given much consideration to its decision concerning the Applicant's representative level of toll revenues to be used in this proceeding. The Commission is particularly concerned that this representative level of revenue should be set at a reasonable level to reflect current

ongoing conditions in the Applicant's toll revenue market. In this proceeding, the Commission has sought to adopt the toll settlement ratio and the level of after-period expenses for toll settlements that, when considered together reflect the appropriate level of Applicant's end-of-period toll revenues. Therefore, the Commission concludes that it would not be correct to include the upward toll revenue effect of post-test-period pro forma adjustments without also recognizing the concomitant downward effect upon the toll settlement ratio. The Commission observes that witnesses for the Company accommodated this by making neither adjustment while Public Staff witness Gerringer included the effect of the expense adjustments while making no adjustment to the settlement ratio.

Hence, the Commission concludes that the Applicant's appropriate level of end-of-period intrastate toll service revenues is $95,125,295.

The difference between the parties on the representative level of miscellaneous revenues is $11,309,692. The greatest majority of this amount is due to the Public Staff's adjustment to include directory advertising yellow pages revenue. For the reasons stated in the Evidence and Conclusions for Finding of Fact No. 4, the Commission concluded that the Company's yellow pages directory advertising should be included in determining the Company's cost of service in this proceeding. For the same reasons, the Commission concludes that the revenues derived from yellow pages directory advertising sales should also be included in determining the Company's regulated revenue requirement.

The remaining difference of $68,864 in miscellaneous revenues results from the end-of-period revenue adjustment to total directory revenue which the Public Staff made using a 29-month regression. The end-of-period adjustment made by the Company using a 24-month regression related only to directory revenues applicable to the white pages. The Company agreed to the Public Staff's adjustment in its Proposed Order; therefore, the Commission concludes that the end-of-period adjustment made by the Public Staff to total directory revenue is reasonable and should be used in this case. Accordingly, the Commission concludes that the representative level of end-of-period miscellaneous revenues amounts to $14,160,141.

The Company and the Public Staff disagreed on the proper level of uncollectible revenues.

Witness Lam computed uncollectibles by applying the test year local revenue uncollectible rate of 0.190% to the Public Staff's end-of-period local revenue and by applying the test year miscellaneous revenue uncollectible rate of 0.154% to the Public Staff's end-of-period miscellaneous revenue. Witness Lam testified that, since witness Gerringer did not include an amount to cover uncollectibles in his end-of-period intrastate toll revenue calculation, it was not necessary to compute uncollectibles related to toll revenues.

The Commission concludes that witness Lam's adjustment to uncollectible revenues is proper since the Commission has employed the same methodology as to toll uncollectibles as witness Gerringer. If the Commission had included uncollectibles in the toll revenue calculation, both toll revenues and uncollectibles would have been higher by the same amount, so the net effect would be the same.

In summary, the Commission concludes that the appropriate level of operating revenues under present rates is $252,549,082, which is itemized as follows:

Item	Amount
Local service revenues	$143,558,214
Toll service revenues	95,125,295
Miscellaneous revenues	141,160,141
Uncollectible revenues	(294,568)
Total operating revenues	$252,549,082

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 8

Company witness Tarleton and Public Staff witness Lam presented testimony and exhibits showing their positions concerning the proper level of operating revenue deductions to be used by the Commission for purposes of fixing rates in this proceeding. The amounts represented below reflect the amounts by each witness:

Item	Company Witness Tarleton	Staff Witness Lam
Operating expenses	$111,733,765	$113,013,301
Depreciation	46,562,642	46,570,255
Taxes other than income	25,134,570	26,158,108
Income taxes - state and federal	18,278,680	21,315,678
Total operating revenue deduction	$201,709,657	$207,057,342

The first area of difference between the parties concerning operating revenue deductions involves operating expenses. Company witness Tarleton testified that the appropriate level of operating expenses is $111,733,765, while Public Staff witness Lam testified that the appropriate level of operating expenses is $113,013,301, a difference of $1,279,536. The $1,279,536 difference is composed of various Public Staff adjustments, as follows:

1.	Adjustment to remove the supplemental gas and diesel fuel expense adjustment made by the Company	(81,304)
2.	Adjustment to increase commercial, general office, and other operating expense for the reinstatement of expenses related to the Company's directory yellow pages operations	$2,350,846
3.	Adjustments to decrease commercial and other operating expense for Public Staff proposed higher level of nonregulated phone shop activity	(109,513)
4.	Adjustment to reduce commercial expense for cost of VIP open houses, handouts, and advertising	(40,112)
5.	Adjustment to decrease general office expense for cost of report card covers and planning calendars	(25,138)

6. Adjustment to decrease other operating expense to remove certain parent company license contract expenses	(612,343)
7. Adjustment to decrease other interest expense	(202,900)
	$1,279,536

The Commission will now discuss each of the preceding adjustments comprising the $1,279,536 difference in operating expenses.

The first difference between the parties arises from an adjustment made by the Public Staff to reverse the Company's supplemental adjustment to gas and diesel fuel expense. In its original prefiled testimony, the Company made an adjustment to reduce the per books gas and diesel expense due to a decline in the actual cost of that fuel since the end of the test period. The Company based its original adjustment on the cost that the Company was paying for fuel at April 30, 1982. In its supplemental testimony, the Company increased the level of expense based upon the level of costs incurred at December 6, 1982. The Public Staff made an adjustment to eliminate the Company's supplemental adjustment. Witness Lam stated that this adjustment should be reversed because the price of gasoline and diesel fuel had been decreasing during the period prior to the close of the hearing. Witness Lam further testified that oil industry analysts have indicated that this trend should continue into the foreseeable future. Based upon all of the evidence presented on this issue, the Commission determines that the Public Staff adjustment is appropriate.

The next difference arises from Public Staff witness Lam's reinstatement of expenses arising from the Company's yellow pages operations. As discussed under Evidence and Conclusions for Finding of Fact No. 4, the Commission agrees with the Public Staff position on this issue and therefore accepts this adjustment.

The next difference arises from the Public Staff adjustment to change the allocation factor to determine the level of nonregulated phone shop activity. Public Staff witness Toms increased the percent of phone shop and business office expenses allocated to nonutility operations from the 5.0521% used by the Company to 6.6788%. Both factors were derived from a time and motion study conducted by the Company from mid-June 1982 to mid-July 1982, subsequent to the test period, but the Company adjusted the factor derived from the study to reflect the actual level of unregulated sales activity during the test period. Witness Toms used the factor developed from the study without adjustment. Witness Toms testified that his proposed 6.6788% allocation factor was more appropriate for use in allocating net investment and operating expenses to nonregulated operations than the 5.0521% factor proposed by witness Tarleton because the 6.6788% allocation factor was the actual result of the time and motion study conducted by Carolina's Methods Group of Business Planning. As further support for his position, witness Toms observed that the average retail sales of telephones had tripled since the initial allocation factor of 2.285% was adopted by the Company and the Commission.

Witness Toms further testified that using the ratio of average test-period nonregulated sales revenue to nonregulated sales revenue realized during the time and motion study to deflate the 6.6788% allocation factor was not reasonable. He testified that, by factoring down the 6.6788% factor in this manner, the Company was in effect proposing that expenses associated with

unsuccessful efforts be included in regulated operations and passed on to ratepayers. Witness Toms testified that such treatment was not equitable, because part of the cost of doing nonregulated business is the cost of unsuccessful efforts which should be charged to nonutility operations. Additionally, witness Toms testified that the Company had improperly used a sales revenue basis to deflate the 6.6788% allocation factor, rather than an appropriate labor basis.

Witness Toms testified that his use of an allocation factor developed from a study conducted after the end of the test year was similar in nature to adjustments to wages, pensions, insurance, or any other adjustment which recognizes a known change. Further, he testified that his adjustment recognized that the Company had experienced a greater level of nonregulated activity which should be considered in this general rate case proceeding.

Based on the foregoing, and the entire evidence on this matter, the Commission concludes that Public Staff witness Tom's adjustment is appropriate.

The next difference in operating revenues arises from an adjustment of $40,112 made by Public Staff witness Lam to reduce advertising expenses. This adjustment is composed of $993, related to the cost of VIP open houses; $29,808, related to Company handouts; $4,275, related image advertising; and $5,036, related to nonregulated sales. The $993 reduction is associated with the cost of open houses which the Company held to publicize the grand opening of new phone shops. Witness Lam testified that these open houses are held to entertain influential people in the community. Witness Lam further testified that the ratepayers do not benefit from these functions and, therefore, the associated costs should not be included in the Applicant's cost of service, for determining fair and reasonable rates in this proceeding.

The Company maintains that it is beneficial to the ratepayer to disseminate widely information such as the location and office hours of phone shops, the services offered by the phone shops and other information which helps the ratepayer better use the telephone company's services. The Company maintains that an effective way to disseminate this information is to invite influential people to the phone shops and provide them with this information. After examining the evidence on this issue, the Commission determines that the Public Staff's adjustment is proper.

The $29,808 reduction in advertising expense arises from expenditures incurred for handout items that include golf tees, gas lighters, leather coasters, letter openers, mugs, desk folders, playing cards, pen and pencil sets, calendars, line lighter rulers, watchband calendars, and pencils, all of which bear the Company's name and/or logo. Public Staff witness Lam made this adjustment because she deemed the provision of handouts to be unnecessary for the provision of telephone service. After examining the evidence on this issue, the Commission determines that the Public Staff's adjustment should be accepted.

The Company took no issue with the Public Staff's adjustment to image advertising of $4,275, and the Commission therefore deems the adjustment to be appropriate. Similarly, the Company took no issue with the Public Staff's adjustment to nonregulated sales advertising and the Commission therefore deems the same to be appropriate.

The next difference between the parties concerning the appropriate level of operating expenses arises from an adjustment made by the Public Staff to remove public relations expense related to the provision of report card covers and 17-month planning calendars. Witness Lam testified that the provision of such materials is not necessary for the Company to carry on its business of providing telephone service. After examining the evidence on this issue, the Commission deems that the Public Staff adjustment should be accepted.

The next difference between the parties involves adjustments made by the Public Staff to license contract expenses. Supporting testimony for these adjustments was provided by Public Staff witness Perkerson. Witness Perkerson removed on an intrastate end-of-period basis $136,613 for an adjustment to end-of-period factors; $36,536 as an adjustment to allocation group B expenses - those of the governmental and regulatory affairs department; $274,547 as an adjustment to allocation Group M expenses - officers salaries, flight operations, and contributions; $66,443 as an adjustment to allocation Group N expenses - public relations costs; $89,820 as an adjustment to allocation Group X expenses - national advertising; and $8,384 as an adjustment to social dues and membership.

The first adjustment made by the Public Staff was to end-of-period factors. Witness Perkerson testified that nine months of test-period license contract expenses were allocated using 1981 factors and three months were allocated using 1982 factors. Witness Perkerson applied the 1982 Telco - non-Telco factor to all 1981 expenses. Next, she reduced the adjustment made by the Company for nonregulated activity by applying the same percentage used by the Company to the lower figures resulting from the use of 1982 factors. This last effect resulted from applying the 1982 factors for allocation between operating and telephone companies. The Company took no issue with this adjustment and it is therefore approved.

Witness Perkerson made an adjustment to Group B expenses and governmental and regulatory affairs department expenses, to remove those expenses from the cost of service. Witness Perkerson testified that the activity of this department is lobbying in nature and should therefore be disallowed. Based on the entire evidence of record, the Commission concludes that this adjustment is appropriate and that these expenses should be excluded from the Applicant's cost of service in this proceeding.

With respect to Group M expenses, the Public Staff's first adjustment was to remove officers salaries in the amount of $98,822. Witness Perkerson removed the jurisdictional portion of the salaries of the chairman, vice chairman, president, and two executive vice presidents of United Telecommunications, Inc. Witness Perkerson testified that these executives are only remotely involved in the managerial assistance provided to the telephone company. Witness Perkerson further concluded that the efforts of officers of UTI are stockholder oriented, and it would be unreasonable and unfair to ask the ratepayers of Carolina Telephone to share in these expenses. The Company asserted that there are benefits provided by these executives that will filter down and accrue to all entities that are a part of the United System. Witness Perkerson conceded on cross-examination that she had not analyzed the duties and responsibilities undertaken by these executives.

After examining all of the testimony on this issue, the Commission determines that the Public Staff adjustments should be rejected. The

Commission is unable to conclude that the benefits provided to the Company by these executives are less than the associated level of expenses which are included in the Applicant's cost of service.

The second adjustment to Group M expenses is an adjustment made by witness Perkerson to flight operations expense. Witness Perkerson obtained test year flight logs for the two aircraft owned by UTI. She next obtained the first-class one-way commercial fare for each of the flights shown on the flight logs. From this information, she derived a first-class commercial fare for all persons flying on the Company planes. She made an allowance for the use of rental cars at destinations where necessary and computed the excess cost of using Company planes instead of commercial flights.

The Company presented evidence showing that the Public Staff's computation of the appropriate flight expense fails to consider the cost of motel rooms, meals, and incidental expenses incurred when employees spend additional time in travel due to the scheduling of commercial flights. The Company also maintained that the savings from use of Company-owned aircraft cannot be solely measured in terms of executive salaries. As an example, the Applicant asserted that if an executive is out of touch in an airport while awaiting a flight, he is unable to perform his management functions.

After examining the evidence on this issue, the Commission determines that the adjustment made by the Public Staff to flight operations is inappropriate in that it does not consider costs related to the additional time involved in utilizing commercial air travel as opposed to Company aircraft. The Commission further concludes that after this fact is taken under consideration it is clear that the level of flight expense included by the Applicant is improper and should be reduced by $69,585 to reflect an appropriate end-of-period level of flight operation expenses for inclusion in the Applicant's cost of service in this proceeding.

With respect to the Public Staff adjustment to Group N expenses, Public Staff witness Perkerson made adjustments to remove public relations expenses relating to enhancement of corporate image. Witness Perkerson testified that this expense is unnecessary because the UTI system contains many layers of public relations costs. The Company maintains that these costs are not duplicative because the public relations effort at each level of the corporate structure are directed towards different groups of people. Based on the entire evidence of record, the Commission concludes that this adjustment is appropriate.

With respect to the Public Staff adjustment to Group X expenses for national advertising, Public Staff witness Perkerson testified that such advertising is designed to promote the corporate image. Witness Perkerson further stated that even though such advertising is intended to enhance the sale of securities, it does not deal with specific issues of stock or with ways to use the telephone more effectively or efficiently.

The Company maintains that the advertising in question appears in investor publications such as the Wall Street Journal and is intended to enhance the attractiveness of securities in the minds of investors. The Commission concludes that the Public Staff adjustment should be accepted.

The final adjustment to Group M expenses relates to the Public Staff's removal of charitable contributions from general services and licenses expenses included in the Applicant's cost of service. Similarly, the Public Staff excluded social dues and memberships from the general services and business expenses. After a review of the record on these matters, and consistent with previous Commission decisions, the Commission concludes that these items of cost should not be included in the Applicant's cost of service in this proceeding.

The next difference between the parties related to operating expenses arises from an adjustment made by the Public Staff to remove other interest expense. The interest expense which the Public Staff removed is interest on state and federal income tax liabilities. The Public Staff maintains that in the past income taxes were computed based on the revenues and expenses which were allowed in the Applicant's cost of service, thus the ratepayers have already paid into the Company the proper level of income tax expense.

The Company maintains that the interest charges in question are those inevitably incurred by any corporation as large as the Applicant, are a normal and expected cost of doing business, and, as such, should be borne by the ratepayer. The Company argues that to remove this interest as a cost-of-service item is to hold the Company to a standard of perfection which is unreasonable and unfair.

After analyzing all of the evidence presented with respect to this adjustment, the Commission rules that it should be disallowed. Whereas it is within the perogative of the Commission to disallow expense incurred as a result of management imprudence or inefficiency, there is no evidence in the record before the Commission which indicates that the isolated occurrences giving rise to the interest expense indicate any pattern of inefficiency.

As witness Lamm admitted on cross-examination, there are many gray areas in which any taxpayer and the IRS reach different conclusions as to the tax liability when audits are conducted. Often when disputes such as these at issue arise, there is no definitive tax law or regulation which is dispositive of the issue. In such instances, it is, in the long run, beneficial to the ratepayers for the Company to assert that the deduction should be taken for tax purposes. Even if, in retrospect, some of the deductions which the Company claims are disallowed, there are many other questionable items which, if not deducted, would result in the Company's paying a greater tax expense which would ultimately be borne by the ratepayer.

We further note that the Public Staff raised this identical issue in the Company's last two general rate cases, Docket No. P-7, Sub 652, and Docket No. P-7, Sub 662. In those cases, the Commission held that fairness and reasonableness required the Commission to disallow the adjustment proposed by the Public Staff.

The second area of difference in operating revenue deductions involves depreciation and amortization expense. Company witness Tarleton testified that the appropriate level of depreciation expense is $46,562,642, while Public Staff witness Lam testified that the appropriate level of depreciation expense is $46,570,255, a difference of $7,613. The difference is composed of the following two adjustments made by witness Lam:

1. Lam's adjustment to restore depreciation expense on yellow pages advertising investment	$10,027
2. Lam's adjustment to decrease depreciation expense for the Public Staff proposed higher level of nonregulated phone shop activity	(2,414)
	$ 7,613

As discussed under Evidence and Conclusions for Finding of Fact No. 4, the Commission has allowed the Public Staff adjustment to reinstate the directory yellow pages investment and expense. Therefore, the Commission also allows witness Lam's adjustment to restore the depreciation expense related to directory advertising investment.

For reasons stated earlier in Evidence and Conclusions for Finding of Fact No. 8, the Commission allowed the investment and expense adjustments related to the Public Staff proposed higher level of nonregulated phone shop activity. The Commission also allows the Public Staff adjustment to decrease depreciation expense for the same reasons.

The third component of operating revenue deductions listed above concerns the proper amount of intrastate operating taxes, other than income. Company witness Tarleton included other operating taxes of $25,134,570, while Public Staff witness Lam included other operating taxes of $26,158,108, or a difference of $1,023,538. This difference is composed of five adjustments made by witness Lam as follows:

1. Difference in gross receipts tax due to differences in revenues reflected in the Company's and the Public Staff's exhibits	$ 994,281
2. Lam's adjustment to restore payroll taxes for directory yellow pages operation	54,090
3. Difference in property tax due to difference in tax base used by the Company and the Public Staff	(5,198)
4. Lam's adjustment for change in expense percentage for payroll taxes	(10,860)
5. Lam's adjustment to remove additional payroll taxes for nonregulated phone shop sales	(8,775)
	$1,023,538

The gross receipts taxes presented by witness Lam exceed the amount presented by Company witness Tarleton because the gross revenues that witness Lam used to calculate her gross receipts taxes exceeded the gross revenues proposed by witness Tarleton. The Commission concludes that neither the level of gross receipts taxes presented by Public Staff witness Lam nor Company witness Tarleton is appropriate because the level of intrastate operating revenues found appropriate by the Commission is different from the level presented by either witness. Under Evidence and Conclusions for Finding of Fact No. 7, the Commission concluded that the appropriate level of intrastate operating revenues is $252,549,082; therefore, the Commission concludes that the appropriate level of gross receipts taxes is $15,152,945.

The Commission, as discussed elsewhere in this Order, accepts the Public Staff adjustment for yellow pages expenses and therefore also accepts the Public Staff adjustment to payroll taxes arising from the yellow pages expense adjustment.

The next difference between the parties arises from an adjustment made by the Public Staff to property tax expense. Public Staff witness Lam made an adjustment to property tax expense so that only the property tax on telephone plant in service included in the Public Staff's rate base, long- and short-term construction work in progress, and materials and supplies included in the Public Staff's rate base is included in the cost of service.

The Company did not oppose the concept behind this adjustment but pointed out on cross-examination that witness Lam had failed to include the plant acquisition adjustment in the base upon which she applied the tax rate. Witness Lam indicated that this had been an oversight on her part and that the plant acquisition adjustment should be included. Based upon the foregoing, the Commission accepts the Public Staff's method of computing property tax expense but concludes that the plant acquisition adjustment should be included in the base upon which tax rates should be applied. Also, since the Commission has accepted the Public Staff's allocation factor to determine the investment used for nonregulated sales, the Commission will exclude the investment removed by the Public Staff by applying its factor in calculating that investment for purposes of the property tax calculation.

The next difference between the parties arises from an adjustment made by the Public Staff to payroll taxes. The Public Staff recalculated the payroll tax expense percentage based upon the actual payroll taxes allocated to construction and unregulated sales through the Company's payroll procedure during the test year.

The Company took no issue with this adjustment and the Commission therefore deems it to be appropriate.

In summary, the Commission concludes that the appropriate level of operating taxes - other than income is $25,983,328, consisting of payroll taxes of $4,875,583, gross receipts taxes of $15,152,945, property taxes of $5,920,179, and other taxes of $34,621.

The next operating revenue deduction upon which the witnesses disagree involves the appropriate level of state and federal income taxes. The adjustments made by both witnesses to state and federal income taxes to reflect the income tax effects of the adjustments made to operating revenues and operating revenue deductions have been discussed previously, and they need not be discussed again relative to their income tax effects. Accordingly, since the Commission has accepted or rejected certain adjustments by each witness, it will be necessary for the Commission to recompute the appropriate level of state and federal income taxes to be used in this proceeding.

Company witness Tarleton and Public Staff witness Lam each made similar adjustments to state and federal income tax expense due to the income tax effects of disallowed depreciation, amortization of the reserve for uncollectibles, interest expense, tax credit-prior deferrals, amortization of deferred taxes, and surtax exemption, and consequently the Commission has used these adjustments in determining the Applicant's income tax expense in this proceeding.

With respect to the proper level of income tax expense to be included in the cost of service, there is one additional matter which must be addressed. This matter concerns the propriety of imputing interest to a portion of funds arising from utilization of the Job Development Investment Tax Credit (JDITC). In numerous rate proceedings before the Commission, the Public Staff has steadfastly maintained that the Revenue Act of 1971, which implemented the JDITC, permits the Commission to impute interest thereto for use in determining the test year level of federal income tax expense. Notwithstanding that the Commission had consistently found, for reasons which need not be repeated here, that the Public Staff's position in this regard was and is incorrect in its entirety. The North Carolina Court of Appeals in Utilities Commission v. Carolina Telephone, --N. C. App.-- (COA #8210UC706, filed 1 March 1983), affirmed the Commission findings in this regard, this matter having been appealed by the Public Staff. In the words of the Court:

"The issue on appeal, as stated by the Public Staff in its brief, 'is whether the Commission erred as a matter of law in concluding that Section 46(f)(2) of the Internal Revenue Code requires that all effects of JDITC should be excluded from the determination of interest expense.'

"G.S. 62-94 sets forth the standard of judicial review of orders of the Utilities Commission and includes the following:

(b) So far as necesary to the decision and where presented, the court shall decide all relevant questions of law, interpret constitutional and statutory provisions, and determine the meaning and applicability of the terms of any Commission action. The court ... may reverse or modify the decision if the substantial rights of the appellants have been prejudiced because the Commission's findings, inferences, conclusions or decisions are:

. . .
(4) Affected by other errors of law...

. . .
(e) Upon any appeal, the rates fixed or any rule, regulation, finding, determination, or order made by the Commission under the provisions of this Chapter shall be prima facie just and reasonable.

In this appeal we are called upon to interpret the applicable sections of the Internal Revenue Code to determine whether the Commission's order is affected by errors of law. We conclude that the order is not so affected.

Section 46(f)(2) of Title 26 of the Internal Revenue Code provides that JDITC will be disallowed with regard to public utility property in the following two circumstances.

(A) Cost of service reduction.--If the taxpayer's cost of service for ratemaking purposes or in its regulated books of account is reduced by more than a ratable portion of the credit

allowable by section 38 (determined without regard to this subsection), or

(B) Rate base reduction.--If the base to which the taxpayer's rate of return for ratemaking purposes is applied is reduced by reason of any portion of the credit allowable by section 38 (determined without regard to this subsection).

The term 'ratable portion' is explained in Section 46(f)(6):

For purposes of determining. . .ratable portions under paragraph (2)(A), the period of time used in computing depreciation expense for purposes of reflecting operating results in the taxpayer's regulated books of account shall be used.

The following example of 'ratable portion' appears in Section 1.46-6(g)(2) of the Treasury Regulations:

(I)f cost of service is reduced annually by an amount computed by applying a composite annual percentage rate to the amount of the credit, cost of service is reduced by a ratable portion.

The Internal Revenue Service has published the following regulations implementing Section 46(f)(2):

(2) Cost of service. (i) For purposes of this section, 'cost of service' is the amount required by a taxpayer to provide regulated goods or services. Cost of service includes operating expenses. . . maintenance expenses, depreciation expenses, tax expenses, and interest expenses. . .

(ii) In determining whether, or to what extent, a credit has been used to reduce cost of service, reference shall be made to any accounting treatment that affects cost of service. Examples of such treatment include reducing by all or a portion of the credit the amount of Federal income tax expense taken into account for ratemaking purposes and reducing the depreciable bases of property by all or a portion of the credit for ratemaking purposes.

(3) Rate base. (i) For purposes of this section, "rate base" is the monetary amount that is multiplied by a rate of return to determine the permitted return on investment.

(ii) In determining whether, or to what extent, a credit has been used to reduce rate base, reference shall be made to any accounting treatment that affects rate base. In addition, in those cases in which the rate of return is based on the taxpayers's cost of capital, reference shall be made to any accounting treatment that affects the permitted return on investment by treating the credit in any way other than as though it were capital supplied by common shareholders to which a 'cost of capital' rate is assigned that is not less than the taxpayer's overall cost of capital rate (determined without regard to the credit). What is the overall cost of capital rate depends upon the practice of the regulatory body. Thus, for example, an overall cost of capital rate may be a

> rate determined on the basis of an average, or weighted average, of the costs of capital provided by common shareholders, preferred shareholders, and creditors.

Treas. Reg. 1.46-6(b)(2)(i), (ii) and (3)(i), (ii) (1979).

Essentially, Section 46(f)(2) and the regulation provide that a utility remains eligible for the credit as long as cost of service is reduced by no more than 'a ratable portion of the credit,' and as long as no reduction is made in the rate base. The purpose of this scheme, as revealed by legislative history, is to permit the benefits of the credit to be shared by the consumers and the investors of the utility. H.R. Rep. No. 533, 92d Cong., 1st Sess., reprinted in U.S. Code Cong. & Ad. News 1825, 1839 (1971).

Pursuant to paragraph (A) of Section 46(f)(2), CT&T 'flows through' directly to its customers an annual percentage of JDITC based upon the useful life of the property producing the credit and thereby reduces its tax expense, and thus its cost of service, by a ratable portion of the credit. This treatment of JDITC by CT&T is not at issue in the present case.

Pursuant to paragraph (B) of Section 46(f)(2), CT&T makes no reduction in its rate base on account of the credit and assigns the overall cost of capital rate to the capital generated by the credit.

The Public Staff advocates an additional adjustment due to the presence of JDITC. Assuming that, in the absence of JDITC, the capital otherwise supplied by JDITC would be contributed by all capital suppliers, including debt, in the same ratios as those suppliers exist in CT&T's capital structure, the Public Staff maintains that a hypothetical interest expense attributable to that portion of JDITC which would have been provided by debt, in the absence of JDITC, should be deducted from CT&T's income tax expense for ratemaking purposes, in addition to the ratable reduction in taxes already produced by amortization of the credit. The Public Staff asserts that this adjustment to income tax expense for ratemaking purposes is in accord with Section 46(f)(2) based upon the language in Treas. Reg. Section 1.46-6(b)(3)(ii) that JDITC be 'assigned a "cost of capital" rate that is not less than the taxpayer's overall cost of capital rate (determined without regard to the credit)'. The Public Staff also maintains that its position has been upheld in three federal court decisions and is therefore the correct one. Finally, the Public Staff contends that the ratepayers are entitled to an additional benefit from the proposed imputed interest on JDITC because they are the source of the cost free capital provided by JDITC. We reject each of these arguments.

The Public Staff's interpretation of the pertinent regulation completely ignores the words which precede the phrase relied upon by the Public Staff. The regulation clearly states that, to determine whether an improper reduction in rate base has occurred, reference should be made to any accounting treatment which treats JDITC 'in any way other than as though it were capital supplied by common shareholders. . .' The phrase relied upon by the Public Staff refers

to the determination of the `overall cost of capital rate' which must be applied to JDITC under the regulation. As such, the phrase deals with the rate of return which the utility is entitled to receive on JDITC, but does not require that a utility's interest expense be calculated without regard to the credit (i.e., as though capital generated by JDITC were supplied by other sources of capital reflected in the utility's capital structure). Rather, the preceding phrase strongly indicates that in other instances, JDITC is to be treated as `capital supplied by common shareholders.' The imputation of interest to a portion of JDITC as though supplied by creditors does not treat that portion of JDITC as though supplied by common shareholders and, in addition, reduces the cost of servie by more than a `ratable portion' of JDITC. For these reasons, the adjustment proposed by the Public Staff contravenes Section 46(f)(2) and the regulation thereunder.

The cases cited by the Public Staff do not persuade us to interpret Section 46(f)(2) otherwise because each of the cases completely ignores the clear requirement in the regulation to that Section that JDITC be treated as `capital supplied by common shareholders.'

In the case of Public Service Company of New Mexico v. Federal Energy Regulatory Commission, 653 F. 2d 681 (D.C. Cir. 1981), the main issue before the court was whether capital provided by JDITC should receive the overall or common equity rate of return. The court concluded that, for purposes of determining the overall rate of return, JDITC could be treated as capital supplied by all capital suppliers in the same proportion as those suppliers existed in the capital structure of the utility, absent the credit. The court further held that excluding JDITC from the capital structure of the utility did not alter the debt/equity ratio such that the utility's interest expense deduction was increased, resulting in an additional, impermissible reduction in cost of service. No issue of imputing interest to JDITC was before the court.

That issue was before the court in New England Power Company v. Federal Energy Regulatory Commission, 668 F. 2d 1327 (D.C. Cir. 1981), <u>cert</u>. <u>denied</u>, U. S. , 102 S. Ct. 2928 (1982). However, in determining that the Federal Energy Regulatory Commission could require the utility to impute hypothetical interest to JDITC, the court relied on its earlier decision in <u>Public Service Company of New Mexico</u>, <u>supra</u>. Upon stating that, `(t)he question in this section is whether FERC may properly treat tax credit funds in relation to interest deduction in the same way it treats tax credit funds in relation to rate of return determination,' the court quoted that portion of its earlier opinion in which it had approved the Federal Energy Regulatory Commission's treatment of JDITC as capital supplied by all capital suppliers in a proportionate manner <u>for purposes of determining the overall rate of return on capital</u>. As we have previously stated, the questions of how to treat JDITC for purposes of determining interest expense for ratemaking purposes are separate issues. The court in <u>New England Power Company</u> did not treat them as such and failed to analyze in any way the tax laws or the arguments supporting the impermissible nature of the adjustment.

In Union Electric Company v. Federal Energy Regulatory Commission, 668 F. 2d 389 (8th Cir. 1981), the third case cited by the Public Staff, the court again relied upon that portion of the regulation under Section 46(f)(2) which permits a ratemaking agency to assign the "overall cost of capital rate (determined without regard to credit)" to JDITC and ignored the remainder of the regulation. Reasoning that because the regulation allows JDITC to be 'treated like other capital' in one instance, the court concluded that the regulation should be interpreted to allow such treatment on the interest deduction issue as well. In our opinion, such reasoning contravenes the clear requirement of Section 46(f)(2)(A) that only a 'ratable portion' of JDITC be flowed through to customers and of Treas. Reg. Section 1.46-6(b)(3)(ii) that JDITC be treated as 'capital supplied by common shareholders,' and we decline to follow it.

The final argument advanced by the Public Staff in support of imputing hypothetical interest to JDITC is that ratepayers are entitled to the additional benefit that would enure to them as a result of imputing interest to a portion of JDITC because they supplied the capital produced by JDITC by paying rates computed without regard to the tax credit (other than the ratable portion flowed through to them). We disagree. Without regard to the credit, a utility owes a certain amount of taxes at the end of its tax year upon which its rates are based. The credit essentially forgives or returns to the utility a portion of the taxes owed by it if certain capital assets have been purchased during the tax year. As such, the capital generated by JDITC comes from the Treasury of the United States, not the ratepayers of the qualifying utility.

Based upon the express language of Section 46(f)(2) and the regulation thereunder, as well as a consideration of the history and purpose of JDITC, that being primarily to benefit the utility so as to stimulate investment and thereby increase employment and additionally to share a ratable portion of the credit with ratepayers, we affirm the decision of the Commission to exclude all imputed interest expense related to JDITC in determining CT&T's income tax expense for ratemaking purposes."

Based upon the foregoing, including the reasoning set forth in past Commission decisions, the Commission finds and concludes that no interest expense should be imputed to funds arising from utilization of JDITC.

Therefore, the Commission concludes that the appropriate level of income tax expense to be included in the Applicant's cost of service is $22,119,471.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 9 AND 10

The Company's direct testimony on the appropriate capital structure for use in this proceeding was presented by Dr. James H. Vander Weide, Professor of Finance at the Fuqua School of Business at Duke University, and Robert E. Baker, Jr., Assistant Vice President-Rate Case Matters, United Telephone System, Inc. Dr. Robert Weiss, Economist with the Economic Research Division of the Public Staff, testified as to the appropriate capital structure recommended by the Public Staff. Additionally, the Company offered rebuttal testimony from Dr. Vander Weide and witness Baker in response to Dr. Weiss's use of the consolidated capital structure approach.

In his direct testimony, Dr. Vander Weide testified that there is no theoretical support for using any capital structure other than that of Carolina. In his opinion, the use of the consolidated capital structure approach ignores that United Telecommunications, Inc. (UTI), the owner of Carolina's common stock, has discretionary control over the finite funds invested in its subsidiaries and must place those funds in investments where it can achieve the highest returns considering commensurate levels of risk. According to Dr. Vander Weide, the consolidated method also assigns the same average cost of capital to each subsidiary regardless of risk characteristics which causes changing economic conditions in other jurisdictions to impact significantly the required rate of return on Carolina's equity.

Company witness Baker testified that Carolina is a separately constituted legal and financial entity which possesses an identifiable capital structure distinct from that of either the parent company or its affiliates. Witness Baker noted that Carolina issues its own debt and otherwise borrows funds on its own behalf to finance construction of the rate base upon which the Commission will make its findings in this docket. While witness Baker said that it may sometimes be appropriate to use the consolidated capital structure approach, he testified that this method is not appropriate for use in this proceeding since the operating subsidiaries of United have different business and financial risks. He pointed out that United's subsidiaries have different bond ratings and, in addition to operating a nonhomogeneous group of telephone companies, they are engaged in a multitude of business activities including the highly competitive packet switching network, satellite digital voice and data communications, domestic and international remote computing market, computer graphics, interconnect market, telecommunications equipment and supplies, electrical supplies, and security and alarm. Witness Baker stated that a substantial portion of United's revenues comes from its unregulated subsidiaries and that United's commitment to continued and increased diversification into unregulated business is well recognized in the investment community. In the final analysis, witness Baker suggested that the real issue is not whether the capital structure is subsidiary or consolidated but whether the Company's actual capital structure is reasonable for an operating telephone company such as Carolina. Witness Baker testified that the capital structure adopted by the Commission should be based on its own merits. He also presented evidence indicating that the existing capital structure of Carolina is reasonable and compares favorably with the capital structures of other conventionally financed telephone operating companies with whom Carolina competes for capital.

Public Staff witness Weiss recommended that the Commission use the United Telecommunications consolidated capital structure as of September 30, 1982, for determining rates in this proceeding. Dr Weiss stated that the consolidated approach should be followed in this proceeding because of the parent-subsidiary relationship between UTI and Carolina. According to Dr. Weiss, the use of the consolidated approach accomplished two desired results. First, the method accounts for all the debt and equity in the consolidated corporate structure and, second, the approach alleviates the need of determining a proper capital structure for each subsidiary. Although he indicated that it is simple to determine Carolina's actual capital structure, Dr. Weiss testified that subsidiary capital structures are artificial creations of corporate management and that a firm with both regulated and unregulated subsidiaries has a natural incentive to put as much equity as possible into its regulated subsidiaries.

In his rebuttal testimony, witness Baker testified that Dr. Weiss was incorrect in assuming that UTI has placed more equity in its regulated subsidiaries and more debt in the parent company and nonregulated subsidiaries. In responding to Dr. Weiss's recommended common equity component of 42.5%, witness Baker presented testimony showing that no conventionally financed telephone operating company in the country has an equity ratio as low as that recommmended by Dr. Weiss. Witness Baker stated that such a low equity ratio would not be reasonable or advisable particularly in an increasingly competitive marketplace which will likely require even higher equity ratios. Witness Baker reinforced his opinion by noting that Judge Greene, in his Modified Final Judgment in the AT&T Divestiture, indicated that an appropriate capital structure for the Bell operating companies would require 45% debt and 55% equity. While witness Baker does not believe that any capital structure other than Carolina's should be used, he suggested that use of the United Telephone System consolidated would be more realistic than use of the UTI consolidated since it would eliminate the diversified, nonregulated business activities of UTI from the capital structure determination. At September 30, 1982, the United Telephone System consolidated capital structure consisted of 50.88% common equity, 1.35% preferred stock, and 47.77% debt.

In his rebuttal testimony, Dr. Vander Weide stated that Dr. Weiss's reasons for using the UTI consolidated hinge on two interrelated points. The first is that the actual capital structure of Carolina is artificial and the second is that the UTI consolidated capital structure is appropriate for Carolina or any of its other telephone operating subsidiaries. Dr. Vander Weide testified that Dr. Weiss was wrong for three reasons. First, Dr. Vander Weide offered evidence tending to show that the equity ratio of Carolina is not artificially high when compared to the equity ratios of other telephone operating companies with whom Carolina must compete for capital. Second, he noted that Judge Greene, various federal agencies, and other parties involved in the AT&T Divestiture believe that the stand-alone Bell operating companies should have equity ratios of 55% with the exception of Pacific Telephone which is expected to be divested with 50% equity, still considerably higher than the 42.5% proposed by Dr. Weiss. Third, Dr. Vander Weide suggested that Dr. Weiss's assertion that electric utilities are able to finance their construction programs with more debt in their capital structure than UTI is misleading and unsupported by any evidence.

Based on the foregoing, the Commission concludes that the appropriate representative capital structure for Carolina in this proceeding is as follows:

Long-term debt	50.25%
Preferred stock	1.35%
Common Equity	48.40%
Total	100.00%

The Commission's conclusion as to capital structure is not based simply on whether the capital structure is subsidiary or consolidated since the issue cannot be so simply resolved. In the final analysis, the Commission must determine the <u>reasonable</u> <u>representative</u> capital structure for a telephone operating company such as Carolina without regard to the label one chooses for it. Since United is a highly diversified group of companies, the consolidated

capital structure advocated by the Public Staff bears no real relationship to the actual business or financial risks of Carolina, both of which have their own distinct characteristics. Additionally, to accept the consolidated approach, the Commission must assume all of United's subsidiaries have the same cost of capital notwithstanding differences in their bond ratings, capital structures, and embedded costs of debt. Though the Commission concludes that the consolidated capital structure advocated by the Public Staff is inappropriate, the Commission concludes that the parent-subsidiary relationship should be considered in determining the Applicant's representative capital structure. Consequently, the Commission concludes that the capital structure approved herein is the most appropriate, based on all evidence of record.

The Commission further finds and concludes that the cost rate for preferred stock is 11.7%, and for debt is 8.51%.

Dr. Vander Weide testified through direct and supplemental testimony that the Company should have an opportunity to achieve a rate of return on common equity of at least 17%. He determined this rate of return on the market value of Carolina Telephone's stock by utilizing the discounted cash flow (DCF) and spread test approaches. Since Carolina's stock is not publicly traded, Dr. Vander Weide performed his DCF analysis on a group of comparable companies which he used as a proxy for Carolina. He chose the comparable companies based upon four criteria: after tax interest coverage, the percent of equity in the capital structure, total capital, and predictability of the firm's operating income. In addition to these criteria, Dr. Vander Weide noted that the comparable companies have a stock quality rating of at least A- and bond rating between A and AA. He then determined the dividend yield and growth rates for each of the comparable companies. Based on his analysis for comparable companies, Dr. Vander Weide concluded through his DCF approach that the cost of equity for Carolina is 16.96%.

In order to test the reasonableness of his initial findings, Dr. Vander Weide applied the DCF approach to a group of seven telephone companies whose stock is publicly traded on the New York Stock Exchange. Dr. Vander Weide testified that while these companies are comparable to Carolina in that they face similar competitive and technological risks and share a common sensitivity to cyclical movements in the economy, they do not provide the degree of comparability as his original group of companies relative to the four key measures of business and financial risk. He determined that the average discounted cash flow rate of return for the group of seven companies was 16.46%

In his supplemental testimony, Dr. Vander Weide stated changes in economic conditions since he prepared his direct testimony in early July 1982 caused him to revise his estimates downward from those in his initial testimony. However, he also testified that the extent of his revisions was affected by recent developments within the telephone industry since July 1982, which have increased the business risk for the telephone industry as a whole and Carolina Telephone in particular. On August 24, 1982, Judge Harold Greene approved the Modified Consent Decree between AT&T and the Justice Department. Under Judge Greene's decision, AT&T and Southern Bell, as separate entities, will enjoy increased opportunities to compete with Carolina in its various markets, particularly the long-distance, terminal equipment, and other enhanced communication service markets. Additionally, the FCC's recent order on access

charges will require the telephone user to pay a fee to obtain access to the intercity long-distance network. Similar filings are expected for intrastate long-distance access. When these charges are implemented, they will fundamentally change the way in which toll rates are set and toll revenues are divided. These charges will result in higher charges for local telephone service, increase the threat of network bypass for local and intercity services, and possibly force customers to forego telephone service entirely. Dr. Vander Weide concluded that these events very clearly increase, in the minds of investors, the uncertainty surrounding Carolina Telephone's future operating income stream and returns.

Dr. Weiss testified for the Public Staff that the cost of equity the Commission should use in this case is 14.5%. Rather than attempting to determine a cost of equity for Carolina, Dr. Weiss attempted to estimate UTI's cost of equity. Dr. Weiss used essentially a three-part approach. First, he used both a DCF and risk premium approach to determine the cost of equity for the market as a whole and concluded that the cost of equity for the market is 15%. Dr. Weiss then attempted to determine whether UTI is more risky, less risky, or equally risky to the market as a whole. He used the index of Standard and Poor's 500 stocks as a surrogate for the market as a whole. In order to make this determination, he applied five different risk measures and concluded that UTI is less risky than the stocks comprising the S&P 500, and therefore, that its expected return should be lower. Finally, to determine UTI's actual cost of equity, Dr. Weiss used the DCF model and the Capital Asset Pricing Model (CAPM) and applied the DCF to a group of seven comparable telephone companies and to UTI itself. Using the DCF he found the cost of equity range for UTI to be 12.7% to 15.5% and slightly higher for the group of comparable companies. Looking at the evidence as a whole Dr. Weiss concluded that UTI's cost of equity lies in the range of 14% to 15%, and he recommended that the midpoint of this range, 14.5%, be used in setting rates for Carolina in this proceeding.

The determination of the appropriate fair rate of return for the Company is of great importance and must be made with great care because whatever return is allowed will have an immediate impact on the Company, its stockholders, and its customers. In the final analysis, the determination of a fair rate of return must be made by this Commission, using its own impartial judgment and guided by the testimony of expert witnesses and other evidence of record. Whatever return is allowed must balance the interest of the ratepayers and investors and meet the test set forth in G.S. 62-133(b)(4):

> "...to enable the public utility by sound management to produce a fair profit for its stockholders, considering changing economic conditions and other factors, as they then exist, to maintain its facilities and services in accordance with the reasonable requirements of its customers in the territory covered by its franchise, and to compete in the market for capital funds on terms which are fair to its customers and to its existing investors."

The return allowed must not burden ratepayers any more than is necessary for the utility to continue to provide adequate service. The North Carolina Supreme Court has stated that the history of G.S. 62-133(b)

> "...supports the inference that the Legislature intended for the Commission to fix rates as low as may be reasonably consistent with

> the requirements of the Due Process Clause of the Fourteenth Amendment to the Constitution of the United States..." State ex rel. Utilities Commission v. Duke Power Company, 285 N.C. 277, 206 S.E. 2d 269 (1974).

The nature of the evidence in a case such as this makes it extremely difficult to balance all of the opposing interests, since much, if not all, of the evidence is based on individual witnesses' perceptions and interpretations of trends and data from the capital markets. The Commission has considered carefully all of the relevant evidence presented in the case, with the constant reminder that whatever return is allowed will have an immediate impact on the Company, its stockholders, and its customers. The Commission must use its impartial judgment to ensure that all the parties involved are treated fairly and equitably. In coming to a final decision on this matter, the Commission is mindful of and, indeed, has given full consideration to the changes now occurring in the telecommunications industry.

Having adopted the reasonable representative capital structure above which includes a common equity ratio of 48.40% common equity, the Commission concludes that the appropriate rate of return on equity to be used in this proceeding is 15.25%. Accordingly, Carolina should be permitted to earn 11.82% on the original cost of its rate base.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 11

The Commission previously discussed its findings and conclusions concerning the fair rate of return which Carolina Telephone and Telegraph Company should be given the opportunity to earn.

The following schedules summarize the gross revenues and the rates of return which the Company should have a reasonable opportunity to achieve based upon the increases approved herein. The schedules, illustrating the Company's gross revenue requirements, incorporate the findings and the conclusions heretofore and herein made by the Commission.

SCHEDULE I
CAROLINA TELEPHONE AND TELEGRAPH COMPANY
NORTH CAROLINA INTRASTATE OPERATIONS
STATEMENT OF OPERATING INCOME
TWELVE MONTHS ENDED MARCH 31, 1982

	Present Rates	Increase Approved	After Approved Increase
Operating Revenues			
Local service	$143,558,214	$13,956,465	$157,514,679
Tol service	95,125,295		95,125,295
Miscellaneous	14,160,141		14,160,141
Uncollectibles	(294,568)	(26,517)	(321,085)
Total operating revenues	$252,549,082	$13,929,948	$266,479,030
Operating Revenue Deductions			
Operating expenses	$113,384,678	$	$113,384,678
Depreciation and amortization	46,570,255		46,570,255
Other operating taxes	25,983,328	835,797	26,819,125
Income taxes	22,119,471	6,447,560	$ 28,567,031
Total operating revenue deductions	$208,057,732	$ 7,283,357	$215,341,089
Net operating income for return	$ 44,491,350	$ 6,646,591	$ 51,137,941

SCHEDULE II
CAROLINA TELEPHONE AND TELEGRAPH COMPANY
NORTH CAROLINA RETAIL OPERATIONS
STATEMENT OF RATE BASE AND RATE OF RETURN
TWELVE MONTHS ENDED MARCH 31, 1982

	Present Rates	After Approved Rates
Investment in Telephone Plant		
Telephone plant in service	$ 707,491,949	$ 707,491,949
Construction work in progress (less than one year)	7,546,187	7,546,187
Plant acquisition adjustment	384,594	384,594
Depreciation and amortization reserve	(212,155,290)	(212,155,290)
Customer deposits	(1,617,708)	(1,617,708)
Accumulated deferred income taxes	(74,565,543)	(74,565,543)
Pre-1971 investment tax credit	(736,472)	(736,472)
Net investment in telephone plant	$ 426,347,717	$ 426,347,717
Allowance for Working Capital		
Cash	$ 3,899,822	$ 3,899,822
Materials and supplies	7,544,502	7,544,502
Accounts payable - materials and supplies	(1,047,516)	(1,047,516)
Customers' funds advanced for operations	(3,930,589)	(3,930,589)
Total working capital allowance	6,466,219	6,466,219
Original Cost Rate Base	$ 432,813,936	$ 432,813,936
Rate of return	10.28%	11.82%

SCHEDULE III
CAROLINA TELEPHONE AND TELEGRAPH COMPANY
NORTH CAROLINA INTRASTATE OPERATIONS
STATEMENT OF CAPITALIZATION AND RELATED COSTS
TWE

	Ratio %	Original Cost Rate Base	Embedded Cost %	Net Operating Income
	Present Rates - Original Cost Rate Base			
Long-term debt	50.25%	$217,489,003	8.51%	$18,508,314
Preferred stock	1.35	5,842,988	11.7	683,630
Common equity	48.40	209,481,945	12.08	25,299,406
Total	100.00%	$432,813,936		$44,491,350
	Approved Rates - Original Cost Rate Base			
Long-term debt	50.25%	$217,489,003	8.51%	$18,508,314
Preferred stock	1.35	5,842,988	11.70	683,630
Common equity	48.40	209,481,945	15.25	$31,945,997
Total	100.00%	$432,813,936		$51,137,941

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 12

Carolina witnesses Owen and Hannah and Public Staff witness Willis presented testimony of the proposed adjustments in Carolina's rates and charges.

Witnesses Owen and Hannah presented Carolina's proposals in tariff rates and regulations.

Witness Owen expressed the Company's rating principles and philosophy supporting its proposed changes. He stated the Company's objectives were to design rate structures and establish prices that are fair and reasonable, meet the public need, encourage and promote customer acceptance and usages, use its capital resources efficiently, and meet the financial needs of the Company. Witness Owen remarked that his rate development took several steps. The supplemental services and equipment were increased where practical to recover at least their cost, and, where possible in a competitive environment, to provide additional contribution toward the Company's revenue requirements. He stated that service connection charges and Extended Area Service rate components were increased to their current cost level. Based upon witness Owen's comments on his nonrecurring service charge proposals, the maximum charge for the installation of basic service at a location previously served would increase $20.20 and the minimum charge for the installation of basic service would increase $10.45 for residential customers. He proposed to increase special assembly items by 10% and foreign central office service, local private line, and miscellaneous services by 15%. He proposed to increase data service tier B rates and local obsolete service offerings by 10%. Witness Owen also proposed to increase the charge for local messages from coin telephone from 20¢ to 25¢ per call. Within the category of local exchange rates, witness Owen indicated he was proposing to apply the remainder of the companywide revenue requirement to rates for local exchange service to effect increases in residential and business individual line services which range from $2.50 to $3.20 per month and from $5.50 to $7.95 per month, respectively.

Witness Hannah filed testimony supplemental to the prefiled testimony of witness Owen. Witness Hannah gave as a reason for his filing supplemental testimony, which includes proposing a premises work charge and an outlet charge, that the existing charges do not fully recover all expenses associated with the work performed. He stated that under witness Owen's proposal the existing rate structure for premises related work spreads the costs for highly variable work functions, such as inside wiring and outlet terminations, across all customers on an average basis. According to witness Hannah, his proposal would restructure the charges associated with work functions performed on the customer's premises. Specificially, he proposed to change the structure of the present residence and business premises related charges, consisting of the inside wiring charge, the jack charge, and the equipment work charge into a premises work charge and an outlet charge. The proposed outlet charge would be comprised of the materials required in the installation of relocation of single line residence and business inside wiring and standard nonweatherproof jacks on the customer's side of the connection to the Company's access line facilities. Witness Hannah's proposal would bill premises work on 15-minute increments for the time a Company craftsman spends installing, rearranging, or reconnecting station apparatus on the customer's premises. During cross-examination, witness Hannah related that 89% of the occurrences for the equipment work function and 90% of the occurrences for the installation of a jack observed by the Company took 15 minutes of labor or less to perform.

According to witness Hannah, many customers as well as competing companies are already performing customer premises installation work. He contended that a system by which costs are recovered on an average basis is unfair to those present and potential competitors as well as to Carolina Telephone Company. It was his belief that his proposed rate structure will eliminate those inequities by charging individual customers, in 15-minute increments, for the total time expended on their premises and for each outlet installed.

Public Staff witness Willis presented testimony on four of the Company's proposals with which he did not agree.

First, on the subject of the Company's service charge proposals, he recommended that no increases be placed on the Company's present nonrecurring service charges and that the Company's tariff provision 4.2.1(j)1 which reads "Where total charges exceed $25.00, the applicant or subscriber may pay such service charges in two equal payments over the first two billing periods after such work is completed" be altered to make basic service acquisition more attainable by changing the tariff to read "Where total charges exceed $15.00, the Applicant of subscriber may pay such service charges in six equal payments over the first six billing periods after such work is completed." As support for his recommendation, witness Willis emphasized it was also important to consider upward pressures being imposed upon basic exchange rates, which are likely to cause significant increases in these rates over the next five years. He cited the recent action taken by the Federal Communications Commission to allocate nontraffic sensitive plant to the local exchange cost of service as an example. Witness Willis indicated that he was concerned that some low income customers would be priced out of the telecommunication market when confronted with both higher levels of flat monthly rates and higher service charges. He stated that a sample taken from the 1980 Census Report covering 27 counties served by Carolina indicated that only 84.7% of the households had telephone service. It was witness Willis'

opinion that the level of service charges has an influence on these statistics and should be considered in constructing the Company's overall rate structure.

Second, witness Willis disputed the Company's "time and materials" charge and recommended that the Company maintain its present tariff rates and procedures for "on premises" work. Witness Willis related that the average time necessary for an installer to perform "on premises" work with regard to equipment work, jack installation, and initial inside wiring activities is 13.4 minutes, 13.3 minutes, and 26.3 minutes, respectively. It was his view that small upward variations in these average work times would cause additional charges of 15 minutes of labor or an amount of $7.65 to be added to a customer's billing. During cross-examination, he showed that customers responsible for the cost related for 22.5 minutes and 37.5 minutes of labor would pay for 30 minutes and 45 minutes of labor which are 33.3% and 20% above cost, respectively, under the Company's time and materials proposal. Witness Willis stated in his prefiled testimony that, under the assumption that "on premises" work is highly variable, a customer would be without any definitive means of predetermining the cost of obtaining service and some low income customers would, conceivably, dismiss the hope of being connected to the network as a result of the uncertainty of knowing their total connecting charges. Witness Willis compared the Company's originally prefiled proposed charges for the equipment work charge and the jack installation charge of $6.75 and $9.25, respectively, with those charges under the supplementally filed "time and materials" proposal. According to witness Willis, in the instance where the average work times for these individual work functions exceed their average work time by two minutes or longer, the charges would increase to $15.30 and $18.40, respectively, under the "time and materials" proposal.

Third, witness Willis recommended that the Company's maintenance of service charge receive the same 1.16% increase be proposed for other service, rather than the 85% increase proposed by the Company. He described this charge as one which is applied in connection with a service difficulty or acceptance testing of a customer-provided wiring, when it is determined that the difficulty was caused by or resulted from the use of customer-provided terminal equipment, protective circuitry, or communication system connected to Company facilities. According to witness Willis, there is confusion among some customers concerning this charge, particularly among those customers who purchase their telephone instruments from Carolina. He stated that the Company's proposed minimum rate of one man-hour at $50.00 was considerably above cost and in his opinion would heighten the level of complaints if applied. Under cross-examination, witness Willis agreed that this charge should cover its cost but commented that the Company had not shown him any indication that it had included more than one man-hour of work, which, he believed, would require a loaded labor rate of $30.43 per hour. He added, however, that the nature of this kind of work appeared similar to the work necessary to perform a premises visit and an equipment work function, which on the average requires 14.88 minutes and 13.4 minutes, respectively. Witness Willis stated, however, that he believed there would be some paperwork and test desk work expense in addition to his approximation of one-half man-hour of labor but the total time expended would be less than one man-hour.

Finally, witness Willis recommended that the Company's proposal to increase the coin telephone rate 25% from $.20 per call to $.25 per call be denied. He stated that the proposed increase would increase the Company's revenues by

only 6.4% or by a dollar amount of $205,003. Witness Willis estimated a revenue requirement, after considering the contribution from intrastate and interstate toll settlements, of $.188 per local message. Therefore, it was his recommendation that the present $.20 per call for local coin telephone messages be maintained.

As for all other proposed rate changes, witness Willis recommended spreading the Public Staff's proposed revenue requirements over each of the Company's service categories uniformly with the exception of the nonrecurring service charge and coin telephone categories.

Based upon all of the evidence regarding rate design and tariff proposals, the Commission makes the following conclusions:

1. The Company's proposed tariff for "on premises" nonrecurring service connection work being charged on a "time and materials" basis is dismissed without prejudice.

2. It is in the public interest to maintain the Company's present level of nonrecurring service charges for the secondary service charges and the jack charges. All other nonrecurring service charges will be increased uniformly across-the-board.

3. The maintenance of service charge should receive the same uniform percentage increase used to establish the increased revenues for other categories of service shown in Conclusion No. 5 below.

4. The local paystation rate should remain at $.20.

5. The increases in revenue approved herein should be derived in a manner consistent with the following guidelines:

(a) All EAS components are to be increased in accordance with the Company's proposal in this regard.

(b) All other rates are to be increased uniformly across-the-board as required (and as permitted without exceeding the proposed increase in such rates) so as to produce the remaining amount of the increase in annual gross revenue approved herein.

6. The service charge billing may be spread over four equal payments if the total of service charges is over $25.

IT IS, THEREFORE, ORDERED as follows:

1. That the Applicant Carolina Telephone and Telegraph Company be, and hereby is, authorized to increase its rates and charges so as to produce additional annual gross revenues of $13,956,465.

2. That the Applicant is hereby called upon to propose specific tariffs reflecting changes in rates, charges, and regulations to recover the revenues approved herein, in accordance with the conclusions set forth above, within ten (10) days fve copies are
required) and the Public Staff (formats such as Item 30 of the minimum filing requirement, NCUC Form P-1, are suggested).

3. That the Public Staff may file written comments concerning the Company's tariffs within five (5) working days of the date on which they are filed with the Commission.

4. That the rates, charges, and regulations necessary to produce the annual gross revenues authorized herein shall become effective upon the issuance of a further order approving the tariffs filed pursuant to Paragraph No. 2 above.

5. That the Company be, and hereby is, ordered to prepare a new lead-lag study based upon a current test year, which reflects its current payment practices, for inclusion in its next general rate filing.

6. That the service charge billing may be spread over four equal payments if the total of service charges is over $25.

ISSUED BY ORDER OF THE COMMISSION.
This the 30th day of March 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sandra J. Webster, Chief Clerk

DOCKET NO. P-10, SUB 415

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Application of Central Telephone Company for Authority to Adjust Its Rates and Charges Applicable to Intrastate Telephone Service in North Carolina) ORDER GRANTING PARTIAL) INCREASE IN RATES AND) CHARGES

HEARD IN: Courtroom A, District Court Building, Hickory, North Carolina, Wednesday, April 20, 1983, at 9:00 a.m.

Courtroom, City Hall, Elkin, North Carolina, Wednesday, April 20, 1983, at 2:00 p.m.

Courtroom C, Randolph County Courthouse, Asheboro, North Carolina, Thursday, April 21, 1983, at 11:00 a.m.

North Carolina Utilities Commission Hearing Room, Dobbs Building, Raleigh, North Carolina, April 26 - 28, 1983

BEFORE: Commissioner A. Hartwell Campbell, Presiding; and Commissioners Leigh H. Hammond and John W. Winters

APPEARANCES:

For the Applicant:

James M. Kimsey, Kimsey, Smith, McMillan & Roten, Attorneys at Law, P.O. Box 150, Raleigh, North Carolina 27602

Donald W. Glaves, Ross, Hardies, O'Keefe, Babcock & Parsons, Attorneys at Law, One IBM Plaza, Chicago, Illinois 60611
For: Central Telephone Company

For the Public Staff:

Theodore C. Brown, Jr., and Paul L. Lassiter, Staff Attorneys, Public Staff - North Carolina Utilities Commission, P.O. Box 991, Raleigh, North Carolina 27602
For: The Using and Consuming Public

BY THE COMMISSION: On November 22, 1982, Central Telephone Company (Central, Company, or Applicant) filed an application with the Commission for authority to adjust its rates and charges for telephone service in North Carolina to become effective on service rendered on and after December 22, 1982. The Applicant filed testimony and exhibits along with and in support of its application.

By Order issued December 22, 1982, the Commission set the matter for investigation, declared the matter to be a general rate case, required public notice, suspended the proposed rates, and set the matter for hearing in the following locations: Courtroom A, District Court Building, 111 Main Avenue, N.E., Hickory, North Carolina, on Wednesday, April 20, 1983; Courtroom, City Hall, 116 East Market Street, Elkin, North Carolina, on Wednesday, April 20, 1983; Courtroom C, Randolph County Courthouse, 145 Worth Street, Asheboro, North Carolina, on Thursday, April 21, 1983; and Commission Hearing Room, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina, on April 26 - 28, 1983. The Order also established the test period for the proceeding as the 12-month period ended June 30, 1982.

On January 10, 1983, the Public Staff filed a Notice of Intervention on behalf of the using and consuming public..

The public hearing in Courtroom A, District Court Building, Hickory, North Carolina, on Wednesday, April 20, 1983, at 9:00 a.m., was conducted as scheduled with representatives of the Company and the Public Staff present. Four public witnesses testified: David Warren, S.A. Hartsoe, Teresa Bumgarner, and Dennis O'Connor. Public witness Dennis O'Connor testified that he had purchased a phone at Brendle's, Inc., which was not performing the automatic re-dial function properly. Additionally, witness O'Connor was having difficulty with completion of toll calls through the Centel System.

On Wednesday, April 20, 1983, at 2:00 p.m., Courtroom, City Hall, Elkin, North Carolina, a public hearing was held. Twelve members of the public presented testimony on service and the rate increase. They were: Bob Hays, a resident of Elkin; J. L. Lowe, a resident of Elkin; Russell Midkiff, a resident of Mount Airy; L. Paul Matthews, a resident of Booneville; Marvin Smith, Mayor of the Town of Booneville; Hap Martin, a resident of Booneville; Steve Edwards, a resident of North Wilkesboro; Neal Cashin, Mayor of the Town of North Wilkesboro; Lois Cooke, a resident of Elkin; David Buie, a resident of Jonesville; Ben Shelton, a resident of Elkin; and Benny Folger, a resident of Elkin, North Carolina.

On Thursday, April 21, 1983, at 11:00 a.m., in Courtroom C, Randolph County Courthouse, Asheboro, North Carolina, a public hearing was held wherein the following public witnesses gave testimony concerning service, rates, and various problems: Phyllis Illing, a resident of Asheboro; Riley Tuck, a resident of Leasburg; and Charles Franklin Williams, a resident of Mocksville.

At the hearings held in Raleigh, the Company presented the testimony and exhibits of the following witnesses: George B. Kemple, Vice President of Central Telephone Company, testified concerning the Company's operations, its expenditures required to maintain and improve service, and the quality of its service; Roy L. Puryear, General Network and Switching Manager, testified concerning the quality of service provided by the Company; John E. Puffer, General Accounting Staff Manager-Regulatory, testified about the Company's operating revenues, expenses, and rate base; Stuart M. Rutter, General Manager-Regulatory and Operational Planning, testified concerning the proposed rate structure and the apportionment of the Company's operations between interstate and intrastate jurisdictions; John R. Clark, General Capital Recovery Staff Manager, testified about Central's capital recovery requirements and request for new depreciation rates; Robert C. Stephan, General Staff Manager-Financial Planning and Analysis, testified concerning the Company's required rate of return, including capital structure and the cost of capital; and James H. Vander Weide, Professor of Finance and Associate Dean at the Fuqua School of Business of Duke University, testified concerning Central's capital structure, cost of capital, and rate of return.

The Public Staff presented the testimony and exhibits of the following witnesses: William J. Willis, Engineer in the Communications Division, testified concerning the Company's end-of-period miscellaneous revenue level and proposed rate structure; Candace A. Paton, Staff Accountant, testified concerning the Company's revenues, expenses, and rate base; Thi-Chen Hu, Engineer in the Communications Division, testified about the Company's quality of service; Hugh L. Gerringer, Engineer in the Communications Division, testified about the apportionment of the Company's operations between interstate and intrastate jurisdictions and the representative end-of-period level of intrastate toll revenues; Leslie C. Sutton, Engineer in the Communications Division, testified about the Company's proposed depreciation rates and special recovery schedules; and Robert Weiss, Economist in the Economic Research Division, testified on the Company's capital structure, cost of capital, rate of return, and the proper level of construction work in progress (CWIP) to include in rate base.

The Commission also received the testimony and exhibits of Donald R. Hoover, Director of the Commission Staff Accounting Division, who filed testimony regarding the propriety of Central's participation in the funding of the National Regulatory Research Institute.

The Company on April 28, 1983, offered rebuttal testimony and exhibits from John E. Puffer, Robert C. Stephan, and James H. Vander Weide.

Based upon the foregoing, the application, the testimony, and exhibits received into evidence at the hearing, the proposed orders submitted by counsel, and the entire record in this proceeding, the Commission now makes the following

FINDINGS OF FACT

1. The Applicant, Central Telephone Company, is a duly organized North Carolina corporation and a wholly owned subsidiary of Central Telephone Utilities, Inc. (CTU). Central is a public utility engaged in providing telecommunications service in North Carolina and as such is subject to the

jurisdiction of this Commission. Central is properly before the Commission in this proceeding, pursuant to G.S. 62-133, for a determination of the justness and reasonableness of its proposed rates and charges.

2. In its original application, Central requested rates designed to produce gross annual intrastate revenues of $74,215,960, which reflected Central's request for additional annual gross revenues of $10,594,306, based on a test year ended June 30, 1982. By its final revised application, the Company requested rates designed to produce annual gross revenues of $71,521,748, based on test year operations. The Company contended that gross revenues under present rates were $63,697,999, thereby necessitating an increase of $7,823,749. The Company proposed to achieve said increase through increases in rates for local service.

3. The test period for purposes of this proceeding is the 12 months ended June 30, 1982.

4. The overall quality of service provided by Central is adequate.

5. Excess profits of $1,177,000 earned by Centel Communications Company - Supply Division (Centel Supply), an affiliate of Central, should be deducted from Central's reasonable original cost rate base. Also, excess profits of $17,390 should be excluded from maintenance expense and $78,592 from depreciation expense.

6. Central's reasonable original cost rate base used and useful in providing service to its customers is $109,856,177. This rate base consists of telephone plant in service of $184,998,404 reduced by accumulated depreciation of $42,944,832, working capital allowance of $697,021, customer deposits of $548,574, reserve for deferred income taxes of $29,656,026, pre-1971 investment tax credit of $118,774, and excess profits on affiliated sales of $1,177,000.

7. The schedule of depreciation rates and amortization amounts as shown in Appendix A is approved.

8. Central's total end-of-period net operating revenues for the test year, under present rates and after accounting and pro forma adjustments, are $62,997,874.

9. The reasonable level of test year operating revenue deductions for Central after accounting, pro forma, end-of-period, and after-period adjustments is $51,469,113. This amount includes $13,312,295 for investment currently consumed through actual depreciation on an annual basis.

10. The capital structure for Central which is appropriate for use in this proceeding is as follows:

Item	Percent
Long-term debt	49.84%
Short-term debt	.03%
Preferred stock	1.83%
Common equity	48.30%
Total	100.00%

The proper embedded costs of long-term debt, short-term debt, and preferred stock are 9.02%, 8.88%, and 5.86%, respectively.

11. The overall rate of return to be applied to Central's original cost rate base is 12.09%. Such rate of return will allow Central the opportunity to earn 15.50% on its common equity and will enable the Company by sound management to produce a fair return for its shareholders, to maintain its facilities and service in accordance with the reasonable requirements of its customers, and to compete in the market for capital on terms which are reasonable and fair to the customers and to the investors.

12. The annual gross revenue requirement for Central is $66,391,959 which necessitates an increase in gross revenues of $3,342,059. Such revenues will allow the Company the opportunity to earn the 12.09% rate of return which the Commission has found just and reasonable. This revenue requirement is based upon the original cost of Central's property and its reasonable test year operating revenues and expenses as previously set forth in these findings of fact.

13. The rates, charges, and regulations to be filed pursuant to this Order in accordance with the guidelines contained herein, which will produce an increase in annual revenues of $3,342,059, will be just and reasonable and shall become effective upon the issuance of a further Order by this Commission.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 1 - 3

The evidence supporting these findings of fact is found in the verified application, in prior Commission Orders in this docket, and in the record as a whole. These findings are essentially procedural and jurisdictional in nature and were uncontested.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 4

The evidence for this conclusion is contained in the testimony and exhibits of Company witnesses Puryear and Kemple and Public Staff witness Hu.

Company witness Puryear referred to the service objectives set by the Commission and testified that the Company during the test year had met or exceeded each of those objectives. In addition, he pointed out that the standard of service as measured by the Commission's objectives had improved greatly since Central's last rate case. Witness Puryear also testified about how Central has upgraded its service by, among other things, the installation of additional digital electronic switching systems and remote subscriber line testing systems, and the administration of digital central offices by the Technical Assistance Center.

Witness Kemple testified as to the Company's improvements in customer service. Some of the programs to improve service and reduce costs include mechanized treatment of delinquent accounts, a mechanized service order system, centralized mail remittance for bill payments, consolidation of four small business offices, rehoming of one operator toll center, consolidation of eight plant service centers into three, customer participation programs, and internal monitoring of operating efficiency. The Company has also upgraded the Mountain View exchange to digital equipment which has eliminated the

service complaints which were noted at that exchange during the last rate proceeding. In fact, the only public witness from Mountain View, Mr. Hartsoe, stated, "The last time I attended a hearing I was complaining about the service. The service is not perfect, but it's far, far, far better than it was at that time so I am not going to complain about the service this time." Witness Kemple testified that, as a result of its efforts, Central had improved from being the telephone company with the highest complaint record with the Public Staff of the major telephone companies in the state in 1981 to the company with the lowest complaint record with the Public Staff of the major telephone companies operating in North Carolina in 1982.

Witness Hu testified that his review consisted of field inspections and tests of switching and trunking facilities; measurements of the answer time of operators, directory assistance, repair service, and business offices; and an analysis of statistics relating to the Company's service. Witness Hu stated that, based on his test results and analysis of the service data, he concluded that the overall quality of service provided by Central was adequate.

Witness Hu's testimony also included a recommendation concerning the exclusion of "planned access" and "no access" from the Company's out-of-service carried-over statistics. He stated that in the interest of consistency among companies and in order to make Central's statistics more reflective of the actual delay caused by the Company in clearing out-of-service troubles, the Company should exclude "planned access" and "no access" from the Company's statistics of out-of-service trouble reports received before 5:00 p.m. and carried over.

Based on the foregoing evidence, the Commission concludes that the overall quality of service provided by Central is adequate and the "planned access" and "no access" should be excluded from the Company's statistics of out-of-service trouble reports received before 5:00 p.m. and carried over.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 5

The evidence concerning this item is found in the testimony and exhibits of Company witness Kemple and Public Staff witness Paton. Witness Paton made adjustments to eliminate excess profits on plant purchased by the North Carolina Division of Central Telephone Company from Centel Supply as follows:

Public Staff Adjustments	Amount
Reduced rate base	$1,174,000
Reduced depreciation expense	78,459
Reduced maintenance expense	18,539

Company witness Kemple testified on the advantages to Central of making purchases from Centel Supply. Witness Kemple stated that Central enjoys the following benefits from these intercompany transactions: (1) the use of cost-free capital in the form of deferred federal income taxes which reduces the revenue required from ratepayers and which amount steadily increases as additional materials are purchased, (2) investment in materials and supplies is minimized, and (3) delivery time advantages result from volume purchasing by Centel Supply. Further, witness Kemple testified that if the Company had made purchases from another supply company it would have had to pay at least as much for the material and it would not have received the aforementioned benefits.

Witness Paton testified that since Central and Centel Supply are affiliated, it is necessary to determine whether transactions between the two were carried out in an arm's-length atmosphere. Witness Paton testified that in prior rate cases, studies have been made comparing Centel Supply's earnings to earnings of similar supply companies operating in the open market. Commission Orders in those prior rate cases ordered Centel Supply's return on equity to be limited to 15% for the years 1967 through 1976. The Commission Order in Central's last general rate case, Docket No. P-10, Sub 400, limited Centel Supply's return on equity for 1977 through 1980 to 15.8%, which was the return found fair and reasonable for Central Telephone Company in that proceeding.

In this proceeding witness Paton did not perform a comparable earnings study. Witness Paton's rate base and depreciation expense adjustments for the years 1981 and 1982 were based upon the decisions set forth in the Commission Order in Docket No. P-10, Sub 400. In order to remove excess profits existing in plant in service and depreciation expense as of June 30, 1982, witness Paton made an adjustment to reduce rate base by $1,174,000 and decreased depreciation expense by $78,459 in order to limit Centel Supply's return on equity to 15% for the years 1967 through 1976 and to 15.8% for the years 1977 through 1982.

Witness Paton also adjusted maintenance expense to exclude from the cost of service excess profits earned by Centel Supply on purchases by Central during the test year that were expensed rather than capitalized. In calculating this adjustment, witness Paton limited Centel Supply to a 14.5% return on equity which is the return on equity the Public Staff recommended for Central in this proceeding. Witness Paton testified that she used the 14.5% return because she is "trying to establish an on-going level of operating expense."

In Docket No. P-10, Sub 369, the Commission found that the transfer prices paid for telephone equipment and supplies by Central to Centel Supply for the period 1967 through 1976 had been unreasonable and excessive to the extent that they produced a return on equity to Centel Supply in excess of 15%. For the period 1977 through 1980, in Docket No. P-10, Sub 400, the Commission found that the return on equity for sales made to Central by Centel Supply should be limited to the same return on equity found fair for Central in that proceeding of 15.8%. After careful consideration of this matter, the Commission concurs with these past decisions. The Commission finds that Centel Supply still enjoys economies of operation which are the result of its close affiliation with its customers. The Commission believes it fair and reasonable to permit the supply affiliate to include in transfer prices charged to Central a reasonable level of profit. For the years 1981 and 1982, the Commission finds that the return on equity for sales made to Central by Centel Supply should be limited to the same return on equity found fair for Central in this proceeding of 15.5% (Finding of Fact No. 11).

Based upon the decisions as to the proper annual returns on equity, the Commission concludes that the Applicant's net investment in intrastate telephone plant in service should be adjusted to exclude excess profits surviving in the net plant accounts at June 30, 1982, in the amount of $1,177,000. Since the Commission finds that it is appropriate to remove excess profits from rate base, it also concludes that it is proper to exclude $78,592 of depreciation expense on that plant in service deducted from rate base. Further, the Commission concludes that it is proper to reduce

maintenance expense by $17,390 to exclude from the cost of service excess profits earned by Centel Supply on purchases by Central during the test year that were expensed rather than capitalized.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 6

The evidence for this finding is found in the testimony and exhibits of Company witnesses Puffer and Kemple and Public Staff witnesses Paton and Weiss. According to the proposed orders of the Company and the Public Staff, the appropriate amounts to be included in the intrastate original cost rate base for use in this proceeding are as follows:

Item	Company	Public Staff	Difference
Telephone plant in service	$182,412,738	$182,412,738	$ -
Reserve for depreciation	(42,944,832)	(42,944,832)	-
Net telephone plant	139,467,906	139,467,906	-
Telephone plant under construction	2,585,666	-	(2,585,666)
Working capital allowance	(697,021)	(697,021)	-
Customer deposits	(548,574)	(548,574)	-
Accounts payable - CWIP	(986,803)	-	986,803
Reserve for deferred income taxes	(28,012,641)	(29,656,026)	(1,643,385)
Pre-1971 investment tax credit	(118,774)	(118,774)	-
Excess profits on affiliated sales	-	(1,174,000)	(1,174,000)
Original cost rate base	$111,689,759	$107,273,511	$(4,416,248)

The Company and the Public Staff are in agreement on the amounts of reserve for depreciation, working capital allowance, customer deposits and pre-1971 investment tax credits. There being no evidence to the contrary, the Commission concludes that the amounts included for these items are reasonable and proper for use herein. Further, the Company and the Public Staff agree as to the proper amount of telephone plant in service, but due to the evidence presented on construction work in progress (CWIP), the Commission disagrees with the parties' position that $182,412,738 for telephone plant in service is the appropriate amount for use in this proceeding.

The first item of difference between the Company and the Public Staff is CWIP and the balance of related accounts payable. The Company included a net amount of $1,598,863 short-term CWIP (net of associated accounts payable) in rate base, while the Public Staff excluded all CWIP from rate base.

Company witness Kemple presented testimony regarding the Company's 1982 construction budget. Witness Kemple testified that the Company had actual gross expenditures of $14.4 million in 1982 for additions, replacements, and expansion of existing plant.

In his direct and rebuttal testimony, Company witness Puffer stated that the Company should be allowed to include all CWIP in its rate base and to capitalize that portion of interest during construction authorized by North Carolina Public Utilities Law in G.S. 62-133. Witness Puffer stated that the Commission, at a minimum, should include short-term CWIP in the Company's rate base as it did in the recent Carolina Telephone and Telegraph Company decision in Docket No. P-7, Sub 670, issued March 30, 1983. Under the FCC's Uniform

System of Accounts, short-term CWIP is defined as projects expected to be completed within one year. Witness Puffer testified that all of the Company's short-term CWIP as of June 30, 1982, except for discontinued projects amounting to $44,149, was in service by March 31, 1983. Excluding the discontinued projects, the intrastate amount of short-term CWIP as of June 30, 1982, included by witness Puffer was $2,585,666 and the accounts payable balance associated with CWIP was $986,803.

Further, witness Puffer testified that the inclusion of CWIP will improve the Company's cash flow and reduce its need for outside financing. In addition, he stated that the Company's rate base, depreciation expense, and revenue requirement eventually will be reduced by including CWIP and the capitalization of interest during construction. Witness Puffer stated that the inclusion of short-term CWIP in rate base would be consistent with the FCC's Uniform System of Accounts which anticipates that short-term CWIP will be included in rate base and therefore makes no provision for interest during construction on short-term projects. Witness Puffer further testified that if the inclusion of short-term CWIP in rate base and capitalization of interest during construction is not authorized the Company's shareholders will bear the financial burden of short-term CWIP.

Public Staff witness Weiss stated that G.S. 62-133(b)(1) requires that the Commission must examine the issues of public interest and financial stability in determining the proper amount of CWIP to allow in rate base. Dr. Weiss testified that the financial stability of the Company in this proceeding is not affected significantly by the inclusion or exclusion of CWIP in rate base because CWIP as a percent of rate base is only about one percent. He also noted the absence of any long lead time associated with the Company's construction expenditures and the fact that pre-tax cash interest coverage without CWIP in rate base is more than adequate at about 4.1 times.

As witness Puffer's testimony demonstrated, all of this short-term plant under construction as of the end of June 30, 1982, had been placed in service at March 31, 1983, prior to the hearing in this case. Thus, the Commission concludes that in this proceeding it is reasonable and appropriate to treat the Company's $2,585,666 investment in short-term CWIP as post-test year plant additions. Such treatment is recognized pursuant to G.S. 62-133(c) which allows for the inclusion of public utility property used and useful in providing service up to the close of the hearings. In recognizing this change in the Company's investment since the end of the test year, the Commission further finds that there is a need to impute additional net operating income on the post-test year plant additions based upon testimony during cross-examination on rebuttal, wherein witness Puffer agreed that the short-term CWIP in service was either producing additional revenues, cost efficiencies, or had the capability to render additional services. Witness Puffer further stated that he thought the major portion of this short-term CWIP was due to just plain replacement.

Based upon the evidence, the Commission concludes that the proper amount of post-test year plant additions to include in telephone plant in service is $2,585,666, which is the amount of plant additions as of June 30, 1982. Accordingly, the Commission finds that $184,998,404 is the reasonable and representative level of telephone plant in service to include in Central's rate base for the period in which rates set in this proceeding will be in effect.

Furthermore, the Commission has imputed additional net operating income on the post-test year plant additions. Based on the findings of fact and so forth reflected in this Order, the Commission finds that $162,605 is the appropriate amount of net operating income to impute on post-test year plant additions under present rates.

The next difference concerns the appropriate level of deferred income tax reserves to deduct from rate base. Deferred income taxes arise in part due to the difference in book depreciation expense and tax depreciation expense. The Company adjusted the reserve for deferred taxes to reflect the level that would have existed had end-of-period plant been in service all year and proposed depreciation rates been in effect. The Company contends that this adjustment is necessary to preserve test-period relationships.

The Public Staff disagreed with the Company's adjustment and proposed using the actual end-of-period balance in the reserve account. Witness Paton testified that the balance in the deferred tax account represents taxes which the ratepayers have already paid in based on depreciation rates set in prior rate cases. Witness Puffer agreed on cross-examination that the balance in the deferred tax account at June 30, 1982, is the amount which ratepayers have paid to the Company and which the Company has been able to retain and use for purposes other than paying taxes. Witness Paton further testified that setting new depreciation rates in this proceeding will only affect future charges to the reserve. In further support of the actual end-of-period balance, witness Paton cited Section 1.167(1)-1(h)(6) of the Federal Income Tax Regulations which states at Paragraph (6)(ii):

> ... if solely an historical period is used to determine depreciation for Federal income tax expense for ratemaking purposes, then the amount of the reserve account for the period is the amount of the reserve...at the end of the historical period.

Witness Puffer stated in rebuttal testimony that the regulation cited by witness Paton did not provide guidance in determining a minimum amount, or require that any amount of the reserve for deferred taxes be deducted from the rate base.

The fact that the regulations do not address a minimum level would seem to indicate that there would be no circumstances under which it would be appropriate to use less than the actual balance in the reserve. The Commission finds that the actual balance of $29,656,026 as of June 30, 1982, is the appropriate balance to use because it represents monies the ratepayers have already paid in to cover a normalized level of tax expense. If anything less than the actual balance were deducted from rate base, ratepayers would be forced to pay a return on money they have already provided to the Company. Furthermore, deferred taxes related to the plant balance at June 30, 1982, will not decrease until book depreciation on that plant exceeds tax depreciation.

The final difference in rate base concerns an adjustment made by witness Paton to remove from Central's rate base excess profits earned by Centel Supply, an affiliate of Central Telephone Company. The Commission has already found in Finding of Fact No. 5 that excess profits of $1,177,000 should be deducted from rate base.

In summary, the Commission concludes that the proper intrastate original cost rate base for use in this proceeding is $109,856,177, composed of the following:

Item	Amount
Telephone plant in service	$184,998,404
Reserve for depreciation	(42,944,832)
Net telephone plant	142,053,572
Working capital allowance	(697,021)
Customer deposits	(548,574)
Reserve for deferred income taxes	(29,656,026)
Pre-1971 investment tax credit	(118,774)
Excess profits on affiliated sales	(1,177,000)
Original cost rate base	$109,856,177

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 7

The evidence as to the appropriate depreciation rates and amortization amounts which should be applied to the Company's property accounts was presented by Company witness Clark and Public Staff witness Sutton. Each witness presented a depreciation and amortization study for each account and although Company witness Clark recommended depreciation rates for several accounts which were somewhat higher than those recommended by Public Staff witness Sutton, the Company stipulated that the appropriate depreciation rates and amortization amounts for the property accounts for the purpose of this proceeding should be the rates and amortization amounts recommended by Public Staff witness Sutton. Based upon the evidence and stipulations of the parties, the Commission concludes that the depreciation rates and amortization amounts shown in Appendix A of this Order are reasonable and appropriate for use in this proceeding.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 8

The evidence concerning the proper end-of-period operating revenues is found in the testimony and exhibits of Company witnesses Puffer and Rutter and Public Staff witnesses Gerringer, Willis, and Paton. The parties' positions regarding operating revenues as set forth in their proposed orders are as follows:

Item	Company	Public Staff	Difference
Local service revenue	$37,161,585	$37,161,585	$ -
Toll service revenue	24,027,703	23,090,146	(937,557)
Miscellaneous revenue	2,495,990	2,495,990	-
Uncollectible revenues	(52,026)	(52,026)	-
Total operating revenues	$63,633,252	$62,695,695	$(937,557)

Both parties agreed regarding the amounts for local service revenues, miscellaneous revenues, and uncollectible revenues. There being no evidence to the contrary, the Commission concludes that these amounts are appropriate for use in this proceeding.

The only area of disagreement concerns the proper end-of-period level of toll revenues. During the hearing, the Company agreed with Public Staff witness Gerringer's calculation of the preliminary or basic level of the end-of-test-period intrastate toll revenues of $24,245,110. There being no

disagreement between the parties as to this amount, the Commission concurs with this initial toll revenue amount.

The Public Staff Accounting Division made adjustments to this preliminary level of toll revenues to reflect its adjustments to expenses, taxes (other than income), net investment, and other items in which the intrastate toll portion enters into the calculation of the intrastate toll settlements. Similarly, the Company has made adjustments to this initial toll revenue amount. The Commission must make further adjustments to this toll revenue amount to recognize the impact of its acceptance or rejection of the various accounting adjustments. As a result of differences in opinion between the Company and the Public Staff regarding the appropriateness of these adjustments to rate base and operating expenses, there exists a difference of $937,557 in toll service revenues. In the determination of the rate base (Evidence and Conclusions for Finding of Fact No. 6) and the proper level of operating revenue deductions (Evidence and Conclusions for Finding of Fact No. 9), the Commission has approved only part of these adjustments and therefore finds that $23,392,325 is the proper amount of toll service revenues to be included in this proceeding.

In summary, the Commission concludes that the proper end-of-period level of net operating revenues for use herein is $62,997,874, composed of the following:

Item	Amount
Local service revenue	$37,161,585
Toll service revenue	23,392,325
Miscellaneous revenue	2,495,990
Uncollectible revenues	(52,026)
Total operating revenues	$62,997,874

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 9

The evidence for operating revenue deductions is found in the testimony and exhibits of Company witness Puffer, Public Staff witness Paton, and Commission Staff witness Hoover. The deductions that the Company and the Public Staff contend are proper are:

Item	Company	Public Staff	Difference
Maintenance	$11,516,741	$11,498,202	$ (18,539)
Depreciation	13,390,887	13,312,428	(78,459)
Traffic	3,263,272	3,263,272	-
Commercial	4,029,423	4,029,423	-
General office	4,828,661	4,828,661	-
Other	3,181,408	2,870,981	(310,427)
Interest on customer deposits	26,330	26,330	-
Taxes other than income	6,141,933	6,085,680	(56,253)
State income tax	853,003	763,626	(89,377)
Federal income tax	5,198,435	4,513,690	(684,745)
Total	$52,430,093	$51,192,293	$(1,237,800)

The Company and the Public Staff are in agreement on the level of traffic, commercial, general office expenses, and interest on customer deposits. Therefore, the Commission concludes that $3,263,272 is the appropriate level

of traffic expense, $4,029,423 is the appropriate level of commercial expense, $4,828,661 is the appropriate level of general office expense, and $26,330 is the appropriate level of interest on customer deposits for use in this proceeding.

The Commission has already found in Finding of Fact No. 5 that the first and second adjustments listed above resulting from the elimination of excess profits on affiliated sales between Central and Centel Supply should be an adjustment of $17,390 to maintenance expense and an adjustment of $78,592 to depreciation expense. Accordingly, the Commission finds that the appropriate levels of maintenance expense and depreciation expense for use in this proceeding are $11,499,351 and $13,312,295, respectively.

The third difference is a reduction in other operating expenses of $310,427 resulting from two adjustments as follows:

Item	Amount
Adjustment to other operating expenses for compensated absences	$(309,082)
Adjustment to other operating expenses for the funding of NRRI	(1,345)
Total other operating expense adjustments	$(310,427)

With regard to the adjustment for compensated absences, the Company proposed an adjustment to amortize over three years the June 30, 1981, balance in the liability account for compensated absences. The Company also included the adjusted test year charge to the liability account in the cost of service.

The liability account for compensated absences represents the estimated cost of vacations that are earned in one year but are to be taken and paid in the next year. Once the Company initially established the liability account, annual charges to the account were to reflect changes in levels of employees, wage rates, and vacation eligibility.

The Company contends that they have not recovered the cost of the liability established in 1981. The Public Staff's position is that there is no cost to be recovered.

Company witness Puffer testified that Financial Accounting Standards Board (FASB) Statement No. 43 requires the Company to record the liability for employee vacations earned but not yet taken. Witness Puffer stated that FASB Statement No. 71 adopted in December 1982 provides that a regulator's actions cannot eliminate a liability which was not imposed by the regulator's actions and requires regulated companies to recognize this liability in their financial statements.

In 1981 the Company recorded the cost of employee vacations which were earned prior to 1981 and paid in 1981 and the employee vacations earned in 1981 which were taken and paid in 1982. Witness Puffer testified that the vacation liability recorded in 1981 has not been recovered from ratepayers because the Commission, in the Company's last rate filing, Docket No. P-10, Sub 400, disallowed this vacation liability for rate-making purposes. According to witness Puffer, this cost was charged against the Company's retained earnings.

The Public Staff contends that the only thing the Company should be allowed to recover through rates is an annual on-going level of wage expense. Witness Paton testified that if the Company were allowed the recovery through rates of the amortization of the vacation liability as of June 30, 1981, and the annual charge to the liability, ratepayers would be forced to pay more than an annual on-going level of wages.

The Public Staff did not dispute the fact that FASB Statement No. 43 required the Company to establish the liability account for financial reporting purposes. The Public Staff did, however, argue that this does not dictate how the liability should be treated for rate-making purposes. In support of the position that only an annual on-going level of wages should be recovered through rates, witness Paton cited FASB Statement No. 71 which states in Appendix B, paragraph 48:

> For ratemaking purposes, compensation for employees' absences may be included in allowable costs when the compensation is paid.

Witness Paton testified that the Company will seldom, if ever, pay more than 52 weeks of wages to any employee in a 12-month period. According to witness Paton, the only time that this could foreseeably happen would be when an employee quit work and was paid for vacation that was earned but not yet taken.

Company witness Puffer testified during cross-examination that "it is possible for an employee to earn 53 weeks of pay in a 52-week year...when the employee's vacation eligibility changes during the following year." Under the Company's proposed treatment, this would result in 53 weeks of wages being recorded for such an employee, even though in the following year when he took his vacation he would only be paid for 52 weeks.

The Commission agrees with the Public Staff's proposed treatment of both the balance in the liability account and the annual charges to the liability account. The Commission concludes that for purposes of determining the cost of service and setting rates in this proceeding only an annual on-going level of wage expense should be included, otherwise ratepayers will be forced to pay more wage expense than the Company will actually incur. Accordingly, the Commission finds that the adjustment in the amount of $309,082 for compensated absences is inappropriate in this proceeding as wage expense has been adjusted for the effects of wage and salary increases granted at various dates during the test period based upon work force levels at December 31, 1982, and the annualization of the increases in union and nonunion wages effective August 1982 and May 1983.

The second adjustment to other operating expenses is the amount of $1,345 for the National Regulatory Research Institute (NRRI) funding expense. Commission Staff witness Hoover testified regarding the funding of the NRRI, which has been established by the National Association of Regulatory Utility Commissioners (NARUC) for the purpose of providing state utility regulatory bodies with educational programs, technical assistance, and timely, expert policy research on regulatory issues. Witness Hoover recommended that the Commission authorize Central to contribute to the funding of the NRRI's research program. The contribution amount determined by witness Hoover is $1,345 on an annual basis calculated by multiplying the contribution factor

($.00888302), as suggested by NARUC, times Central's number of main stations (151,373).

Neither the Company nor the Public Staff disagreed with witness Hoover, and at the hearing it was stipulated that the Commission would consider the Company's contribution to NRRI for inclusion in the Company's operating expenses.

Based on the evidence presented, the Commission concludes that the Company's contribution of $1,345 to fund the NRRI's research program is reasonable and appropriate and hereby allows it as part of the Company's operating expenses.

Based upon the foregoing conclusions, the Commission finds that the proper level of other operating expenses to be included in the cost of service in this proceeding is $2,872,326.

The next item of difference between the Company and the Public Staff is in the amount of $56,253 in gross receipts taxes. This difference is due solely to the parties' different levels of revenues. The Commission found in Finding of Fact No. 8 that the proper level of revenues for use in this proceeding was $62,997,874. Accordingly, the Commission finds that a reduction in the Company's gross receipts tax of $38,122 is appropriate and the appropriate level of taxes other than income is $6,103,811 for use in this proceeding.

The final area of difference in operating revenue deductions concerns the proper levels of state and federal income taxes. The difference is due to how the Job Development Investment Tax Credit (JDITC) is treated in the determination of interest expense, the adjustment reflecting the effect of the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA), and the parties' different levels of revenues and operating revenue deductions.

The Company and the Public Staff disagreed on the amount of interest expense to use in calculating income tax expense. Both parties utilized the annualized interest expense associated with the debt capital supporting their respective intrastate original cost rate bases. However, they disagreed on the proper treatment of the JDITC in computing income tax expense. In computing income tax expense, the Public Staff has taken an interest deduction for the JDITC allocated to the debt portion of the capital structure, whereas the Company has not.

Although the Public Staff has repeatedly maintained in recent rate proceedings that the Revenue Act of 1971 permits the Commission to impute interest to a portion of JDITC for purposes of calculating the test year level of federal income tax expense, the Commission has continued to reject the Public Staff's position in this regard. The Commission's treatment of JDITC was recently affirmed by the North Carolina Court of Appeals in North Carolina ex rel. Utilities Commission v. Carolina Telephone and Telegraph Company, No. 8210UC706 (N.C. Ct. App. March 1, 1983). In the words of the Court of Appeals:

> The issue on appeal, as stated by the Public Staff in its brief, "is whether the Commission erred as a matter of law in concluding that Section 46(f)(2) of the Internal Revenue Code requires that all

effects of JDITC should be excluded from the determination of interest expense."

G.S. 62-94 sets forth the standard of judicial review of orders of the Utilities Commission and includes the following:

> (b) So far as necessary to the decision and where presented, the court shall decide all relevant questions of law, interpret constitutional and statutory provisions, and determine the meaning and applicability of the terms of any Commission action. The court...may reverse or modify the decision if the substantial rights of the appellants have been prejudiced because the Commission's findings, inferences, conclusions or decisions are:
>
> . . .
>
> (4) Affected by other errors of law. . .
>
> . . .
>
> (e) Upon any appeal, the rates fixed or any rule, regulation, finding, determination, or order made by the Commission under the provisions of this Chapter shall be prima facie just and reasonable.

In this appeal the Commission is called upon to interpret the applicable sections of the Internal Revenue Code to determine whether the Commission Order is affected by errors of law. The Commission concludes that the Order is not so affected.

Section 46(f)(2) of Title 26 of the Internal Revenue Code provides that JDITC will be disallowed with regard to public utility property in the following two circumstances:

> (A) Cost of service reduction. --If the taxpayer's cost of service for ratemaking purposes or in its regulated books of account is reduced by more than a ratable portion of the credit allowable by section 38 (determined without regard to this subsection), or
>
> (B) Rate base reduction. --If the base to which the taxpayer's rate of return for ratemaking purposes is applied is reduced by reason of any portion of the credit allowable by section 38 (determined without regard to this subsection).

The term "ratable portion" is explained in Section 46(f)(6):

> For purposes of determining...ratable portions under paragraph (2)(A), the period of time used in computing depreciation expense for purposes of reflecting operating results in the taxpayer's regulated books of account shall be used.

The following example of "ratable portion" appears in Section 1.46-6(g)(2) of the Treasury Regulations:

> (I)f cost of service is reduced annually by an amount computed by applying a composite annual percentage rate to the amount of the credit, cost of service is reduced by a ratable portion.

The Internal Revenue Service has published the following regulations implementing Section 46(f)(2):

> (2) Cost of service. (i) For purposes of this section, "cost of service" is the amount required by a taxpayer to provide regulated goods or services. Cost of service includes operating expenses...maintenance expenses, depreciation expenses, tax expenses, and interest expenses....
>
> (ii) In detemining whether, or to what extent, a credit has been used to reduce cost of service, reference shall be made to any accounting treatment that affects cost of service. Examples of such treatment include reducing by all or a portion of the credit the amount of Federal income tax expense taken into account for ratemaking purposes and reducing the depreciable basis of property by all or a portion of the credit for ratemaking purposes.
>
> (3) Rate base. (i) For purposes of this section, "rate base" is the monetary amount that is multiplied by a rate of return to determine the permitted return on investment.
>
> (ii) In determining whether, or to what extent, a credit has been used to reduce rate base, reference shall be made to any accounting treatment that affects rate base. In addition, in those cases in which the rate of return is based on the taxpayer's cost of capital, reference shall be made to any accounting treatment that affects the permitted return on investment by treating the credit in any way other than as though it were capital supplied by common shareholders to which a "cost of capital" rate is assigned that is not less than the taxpayer's overall cost of capital rate (determined without regard to the credit). What is the overall cost of capital rate depends upon the practice of the regulatory body. Thus, for example, an overall cost of capital rate may be a rate determined on the basis of an average, or weighted average, of the costs of capital provided by common shareholders, preferred shareholders, and creditors.

Treas. Reg. 1.46-6(b)(2)(i), (ii), and (3)(i), (ii) (1979).

Essentially, Section 46(f)(2) and the regulation provide that a utility remains eligible for the credit as long as cost of service is reduced by no more than "a ratable portion of the credit," and as long as no reduction is made in the rate base. The purpose of this scheme, as revealed by legislative history, is to permit the benefits of the credit to be shared by the consumers and the investors of the utility. H.R. Rep. No. 533, 92d Cong., 1st Sess., _reprinted in_ U.S. Code Cong. & Ad. News 1825, 1839 (1971).

Pursuant to paragraph (A) of Section 46(f)(2), CT&T "flows through" directly to its customers an annual percentage of JDITC based upon the useful life of the property producing the credit and thereby reduces its tax expense, and thus its cost of service, by a ratable portion of the credit. This treatment of JDITC by CT&T is not at issue in the present case.

Pursuant to paragraph (B) of Section 46(f)(2), CT&T makes no reduction in its rate base on account of the credit and assigns the overall cost of capital rate to the capital generated by the credit.

The Public Staff advocates an additional adjustment due to the presence of JDITC. Assuming that, in the absence of JDITC, the capital otherwise supplied by JDITC would be contributed by all capital suppliers, including debt, in the same ratio as those suppliers exist in CT&T's capital structure, the Public Staff maintains that a hypothetical interest expense attributable to that portion of JDITC which would have been provided by debt, in the absence of JDITC, should be deducted from CT&T's income tax expense for rate-making purposes, in addition to the ratable reduction in taxes already produced by amortization of the credit. The Public Staff asserts that this adjustment to income tax expense for rate-making purposes is in accord with Section 46(f)(2) based upon the language in Treas. Reg. Section 1.46-6(b)(3)(ii) that JDITC be "assigned a `cost of capital' rate that is not less than the taxpayer's overall cost of capital rate (determined without regard to the credit)." The Public Staff also maintains that its position has been upheld in three federal court decisions and is therefore the correct one. Finally, the Public Staff contends that the ratepayers are entitled to an additional benefit from the proposed imputed interest on JDITC because they are the source of the cost-free capital provided by JDITC. We reject each of these arguments.

The Public Staff's interpretation of the pertinent regulation completely ignores the words which precede the phrase relied upon by the Public Staff. The regulation clearly states that, to determine whether an improper reduction in rate base has occurred, reference should be made to any accounting treatment which treats JDITC "in any way other than as though it were capital supplied by common shareholders...." The phrase relied upon by the Public Staff refers to the determination of the "overall cost of capital rate" which must be applied to JDITC under the regulation. As such, the phrase deals with the rate of return which the utility is entitled to receive on JDITC, but does not require that a utility's interest expense be calculated without regard to the credit (i.e., as though capital generated by JDITC were supplied by other sources of capital reflected in the utility's capital structure). Rather, the preceding phrase strongly indicates that in other instances, JDITC is to be treated as "capital supplied by common shareholders." The imputation of interest to a portion of JDITC as though supplied by creditors does not treat that portion of JDITC as though supplied by common shareholders and, in addition, reduces the cost of service by more than a "ratable portion" of JDITC. For these reasons, the adjustment proposed by the Public Staff contravenes Section 46(f)(2) and the regulation thereunder.

The cases cited by the Public Staff do not persuade us to interpret Section 46(f)(2) otherwise because each of the cases completely ignores the clear requirement in the regulation to that Section that JDITC be treated as "capital supplied by common shareholders."

In the case of Public Service Company of New Mexico v. Federal Energy Regulatory Commission, 653 F.2d 681 (D.C. Cir. 1981), the main issue before the court was whether capital provided by JDITC should receive the overall or common equity rate of return. The court concluded that, for purposes of determining the overall rate of return, JDITC could be treated as capital supplied by all capital suppliers in the same proportion as those suppliers existed in the capital structure of the utility, absent the credit. The court further held that excluding JDITC from the capital structure of the utility did not alter the debt/equity ratio such that the utility's interest expense deduction was increased, resulting in an additional, impermissible reduction in cost of service. No issue of imputing interest to JDITC was before the court.

That issue was before the court in New England Power Company v. Federal Energy Regulatory Commission, 668 F.2d 1327 (D.C. Cir. 1981), cert. denied, ____ U.S. ____, 102 S. Ct. 2928 (1982). However, in determining that the Federal Energy Regulatory Commission could require the utility to impute hypothetical interest to JDITC, the court relied on its earlier decision in Public Service Company of New Mexico, supra. Upon stating that, "(t)he question in this section is whether FERC may properly treat tax credit funds in relation to interest deduction in the same way it treats tax credit funds in relation to rate of return determination," the court quoted that portion of its earlier opinion in which it had approved the Federal Energy Regulatory Commission's treatment of JDITC as capital supplied by all capital suppliers in a proportionate manner for purposes of determining the overall rate of return on capital. As we have previously stated, the questions of how to treat JDITC for purposes of determining the overall rate of return on capital and for purposes of determining interest expense for rate-making purposes are separate issues. The court in New England Power Company did not treat them as such and failed to analyze in any way the tax laws or the arguments supporting the impermissible nature of the adjustment.

In Union Electric Company v. Federal Energy Regulatory Commission, 668 F.2d 389 (8th Cir. 1981), the third case cited by the Public Staff, the court again relied upon that portion of the regulation under Section 46(f)(2) which permits a rate-making agency to assign the "overall cost of capital rate (determined without regard to credit)" to JDITC and ignored the remainder of the regulation. Reasoning that because the regulation allows JDITC to be "treated like other capital" in one instance, the court concluded that the regulation should be interpreted to allow such treatment on the interest deduction issue as well. In our opinion, such reasoning contravenes the clear requirement of Section 46(f)(2)(A) that only a "ratable portion" of JDITC be flowed through to customers and of Treas. Reg. Section 1.46-6(b)(3)(ii) that JDITC be treated as "capital supplied by common shareholders," and the Commission declines to follow it.

The final argument advanced by the Public Staff in support of imputing hypothetical interest to JDITC is that ratepayers are entitled to the additional benefit that would enure to them as a result of imputing interest to a portion of JDITC because they

> supplied the capital produced by JDITC by paying rates computed without regard to the tax credit (other than the ratable portion flowed through to them). The Commission disagrees. Without regard to the credit, a utility owes a certain amount of taxes at the end of its tax year upon which its rates are based. The credit essentially forgives or returns to the utility a portion of the taxes owed by it if certain capital assets have been purchased during the tax year. As such, the capital generated by JDITC comes from the Treasury of the United States, not the ratepayers of the qualifying utility.
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> Based upon the express language of Section 46(f)(2) and the regulation thereunder, as well as a consideration of the history and purpose of JDITC, that being primarily to benefit the utility so as to stimulate investment and thereby increase employment and additionally to share a ratable portion of the credit with ratepayers, we affirm the decision of the Commission to exclude all imputed interest expense related to JDITC in determining CT&T's income tax expense for rate-making purposes.

Therefore, based on the Court's reasoning in the aforementioned case and the Commission's reasoning in past Commission decisions, the Commission finds and concludes that no interest expense should be imputed to JDITC.

The second difference regarding the federal and state income tax expense calculation concerns the Public Staff's exclusion of the Company's income tax adjustment for the effect of the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA).

The Company made an income tax adjustment to reflect the effect of TEFRA. TEFRA requires taxpayers either to (1) reduce the depreciable basis of fixed assets by one-half of the investment tax credit (ITC) allowable or (2) reduce the amount of the ITC otherwise allowable by 2%. In calculating the adjustment for TEFRA, the Company chose to reduce the depreciable basis of test year (July 1, 1981 through June 30, 1982) additions to plant in service. Public Staff witness Paton disagreed with the Company's adjustment because the provisions of TEFRA are applicable to asset acquisitions after December 31, 1982. During cross-examination, witness Paton was asked if she was distinguishing this adjustment from other known and measurable changes. Witness Paton testified that it was a known change with respect to the Company's filing of a tax return (for years starting after December 31, 1982), but that she did not believe it was measurable at this point.

The Commission agrees with witness Paton and concludes that her adjustment is proper. In reaching this conclusion, the Commission recognizes that this provision of the Internal Revenue Code is applicable only to assets acquired after December 31, 1982. The Commission finds that no measureable prospective tax consequence has yet occurred. Further, the Commission recognized the fact that, for rate-making purposes, income tax expense is included in the cost of service on a normalized basis. Therefore, the impact of this code provision will impact the Company's cost of service ratably over the useful lives of the assets involved rather than on a "flow-through" basis as the Company proposes in its adjustment.

Finally, the Commission is concerned over the propriety of the method chosen by the Company to implement TEFRA. Since the Company will recover its

total income tax expense from ratepayers whichever method is chosen, it is imperative that the method chosen produces the lowest revenue requirement. Ascertaining which method produces the lower revenue requirement will require an evaluation which, among other things, considers the useful life of the assets, the Company's unused investment credit carryovers, ACRS depreciation options, etc. It is quite possible that the lower credit with no rate base reduction will be the proper option to choose for the majority of the Company's assets. The Commission expects the Company to choose the option which minimizes the overall revenue requirement in the long run based on all relevant factors, variables, and parameters entering into the cost of service equation(s).

Based on the above, the Commission adopts witness Paton's adjustment reducing income tax expense by $40,629.

The third and final difference regarding federal and state income tax expenses arises because the parties used different levels of operating revenues and operating revenue deductions to which they applied the same statutory tax rates. Accordingly, as the Commission has accepted or rejected certain adjustments by each witness, it has recomputed the appropriate amount of federal and state income taxes.

Therefore, the Commission concludes and finds the proper amount of federal and state income taxes to be $5,533,644 ($794,860 + $4,738,784).

In summary, the Commission concludes that the proper level of intrastate operating revenue deductions for use in this proceeding is $51,469,113 composed of the following:

Item	Amount
Maintenance	$11,499,351
Depreciation	13,312,295
Traffic	3,263,272
Commercial	4,029,423
General office	4,828,661
Other	2,872,326
Interest on customer deposits	26,330
Taxes other than income	6,103,811
State income tax	794,860
Federal income tax	4,738,784
Total operating revenue deductions	$51,469,113

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 10 AND 11

Three witnesses testified regarding the appropriate capital structure for use in this proceeding and the fair rate of return to be allowed on the Company's investment in public utility property. The Company presented the testimony of Robert C. Stephan, Centel Corporation's General Staff Manager - Financial Planning and Analysis, and of Dr. James H. Vander Weide, Professor of Finance and Associate Dean at the Fuqua School of Business of Duke University. The Public Staff presented testimony of Dr. Robert Weiss, an economist with the Economic Research Division of the Public Staff. In addition, the Company offered rebuttal testimony of both of their witnesses on Dr. Weiss's estimate of the cost of common equity capital and his proposed capital structure.

Regarding the appropriate capital structure, Company witnesses Stephan and Vander Weide recommended that the Commission use the Company's divisional capital structure as of June 30, 1982, which consisted of 41.63% long-term debt, 1.36% short-term debt, and 57.01% common equity. Witness Stephan testified that use of the divisional capital structure was appropriate because in his opinion each of Central's four operating divisions face different business and financial risks and are financed in different ways. According to witness Stephan the use of a divisional capital structure will mean that the Company's rate of return on its investment will reflect the actual cost of debt and equity of Central's North Carolina jurisdictional operations. In addition, witness Stephan testified that use of a divisional capital structure is consistent with the determination of jurisdictional rate base, revenues, and expenses. Company witness Vander Weide also recommended the use of a divisional capital structure since he shares the view that Central and its North Carolina division face significantly different business risks due to differing economic conditions, regulatory climates, vulnerability to competition, and condition of plant and equipment experienced by each.

Witness Stephan testified that it was inappropriate to use Centel Corporation's consolidated capital structure as a proxy for the capital structure of the Company because of Centel's diverse business operations which have dissimilar risks. According to witness Stephan 39% of Centel Corporation's revenues do not come from telephone operations currently, but come from various unregulated operations. In addition, witness Stephan testified that use of Centel Corporation's consolidated capital structure is improper since individual Centel divisions generate and utilize debt and equity in a manner different than that reflected in the consolidated capital structure.

As an alternative to the Company's recommended use of the divisional capital structure, Company witness Stephan recommended use of the capital structure of all of the telephone operations in the Central Telephone System. Although the use of such a capital structure does not reflect the differences in the business risks faced by the different telephone companies in the Central Telephone System, in witness Stephan's opinion it is a more appropriate capital structure than Centel Corporation's consolidated capital structure since it reflects only Centel's regulated business operations. The alternative capital structure offered by the Company is the summation of the capital structures of Central Telephone Company consolidated, Central Telephone Company of Texas consolidated, and Central Telephone Company of Ohio.

Public Staff witness Weiss recommended the use of the capital structure of Central's combined telephone operations as of December 31, 1982, which consisted of 49,84% long-term debt, .03% short-term debt, 1.83% preferred stock, and 48.30% common equity. Witness Weiss compared the equity ratios of the large telephone holding companies as well as the telephone companies that are not holding companies to that of Central's combined telephone operations and concluded that the financing of Central's telephone operations with 48.30% common equity was reasonable and not inconsistent with the comparison companies. Dr. Weiss testified that use of a consolidated capital structure is appropriate in certain instances where the unconsolidated capital structure does not make adequate use of the leverage available and where the corporation derives a large proportion of its revenues and income from the local telephone operations. However, in Dr. Weiss' opinion the capital structure of Central's

combined telephone operations at December 31, 1982, does reflect adequate use of the leverage available to the Company. Additionally, witness Weiss testified that Central obtains a significant portion of its revenues from sources other than the local telephone operations. Thus, for the preceding reasons in this proceeding witness Weiss found it more reasonable to recommend use of the aforementioned capital structure reflecting Central's combined telephone operations rather than Central's consolidated capital structure.

Dr. Weiss testified further that use of the Company's divisional capital structure as recommended by the Company was not reasonable since said capital structure does not reflect the financial leverage available to the Company. Additionally, Dr. Weiss testified that the Company had not shown that it faced the additional risk necessary to justify the additional common equity contained in the divisional capital structure.

Company witness Stephan testifying in rebuttal to the testimony of Public Staff witness Weiss reiterated his view that the business risks faced by Central's North Carolina division were unique to it and justified the use of the divisional capital structure. Witness Stephan compared the proportion of equity in the Company's divisional capital structure to that of several publicly traded telephone operating companies and found the percentages of equity in their capital structures to be similar. Witness Stephan restated his view that in the event that the Commission found it inappropriate to use a divisional capital structure, he recommended use of the capital structure of Central Telephone System's combined telephone operations.

Dr. Vander Weide also testified in rebuttal to the testimony of Public Staff witness Weiss. It was witness Vander Weide's testimony that the substantially increased business risks faced by telephone companies today has been caused by recent actions of the Federal Communications Commission as a part of its broad policy of deregulation. As a result of these increased risks, witness Vander Weide testified that higher equity ratios than historically justified are now appropriate.

Based upon the foregoing, the Commission determines that the capital structure for Central's combined telephone operations at December 31, 1982, consisting of the following is apropriate for use in this proceeding.

Item	Percent
Long-term debt	49.84%
Short-term debt	.03
Preferred stock	1.83
Common equity	48.30
Total capitalization	100.00%

The Commission recognizes that the telephone industry, in general, and Central, in particular, stands on the threshold of a revolutionary, competitive era in providing telecommunications services. The Commission therefore deems it unwise to draw conclusions based solely upon historical equity ratios for other companies when the threat of competition did not pose the business risk that presently exists. In the Commission's opinion, Central's capital structure at December 31, 1982, properly reflects the balance of debt and equity capital necessary for the Company to adequately prepare itself for the increased business risk it is now facing and can reasonably be expected to face in the future. It is pertinent to note that

the capital structure herein approved is properly reflective of the changes which have occurred in the Company's operations, namely, the growing portion of revenues and net income derived by the consolidated entity from sources other than the local telephone operations as well as the increased business risks faced by the telecommunications industry, in general, and Central, in particular, since its last general rate proceeding. Thus, for purposes of this general rate proceeding, the Commission finds it appropriate to utilize an unconsolidated capital structure consisting of the combined capitalization of all of Centel's telephone operating companies as recommended by the Public Staff. The Commission is unpersuaded, however, that the risks facing the North Carolina division of Central Telephone Company differ significantly from that of Central's other telephone operating divisions and thus can find no merit to the proposed use of Central's North Carolina divisional capital structure in establishing the revenue requirements of the Company.

The Company and the Public Staff recommended embedded costs of debt and preferred stock consistent with the alternative capital structures proposed by each party. Company witness Stephans proposed an embedded cost of long-term debt of 8.39% and an embedded cost of short-term debt of 13.38% while Public Staff witness Weiss recommended embedded rates of 9.02%, 8.88%, and 5.86% for long-term debt, short-term debt, and preferred stock, respectively.

Consistent with the Commission's previous findings herein regarding Central's proper capital structure, the Commission finds an embedded cost of long-term debt of 9.02%, an embedded cost of short-term debt of 8.88%, and an embedded cost of preferred stock of 5.86% reasonable and appropriate for establishing the revenue requirements of the Company in this proceeding.

The final issue on which the Company and the Public Staff disagree is the appropriate rate of return on equity for Central. Using the Company's divisional capital structure, Company witness Stephan recommended to the Commission that the Company should have an opportunity to achieve a rate of return on common equity of at least 17%. Witness Stephan's determination of the cost of equity to Central was based on two methods - a risk premium analysis for the six largest independent telephone companies and a discounted cash flow (DCF) analysis for those same companies. The results from the risk premium analysis showed a cost of equity of 19% to 20% and the results from the DCF were 17% to 18%. Witness Stephan concluded that the cost of equity to the major independents is 18% to 19% and the required return to Central - North Carolina is at least 17%.

Company witness Vander Weide found the Company's overall cost of capital to be 13.44% to 14.07%, based on a cost of equity of 17.13% to 18.25% and the June 30, 1982, capital structure and embedded cost rates of Central Telephone Company - North Carolina. He stated that total risk in the telephone industry has increased dramatically since the mid-60's due to competition, technological improvements, and regulatory delay.

In his calculation of the cost of equity, witness Vander Weide used the DCF model and a spread test (risk premium analysis). Using the DCF analysis, witness Vander Weide examined a group of 10 comparable companies and a group of seven telephone companies. Based on this analysis, witness Vander Weide concluded that a rate of return on equity of 17.13% was representative of the DCF results and Central's required return. In performing the spread test, witness Vander Weide examined the results of a self-conducted study as well as

other studies of bond and stock returns. Based on the results of such studies, witness Vander Weide concluded that the risk premium of stocks over bonds was 5% to 6.5%. Adding 5% to a current bond yield of 13.25%, he determined a cost of common equity of 18.25% and concluded that the investor's required return for Central was in the range of 17.13% to 18.25%.

Dr. Weiss, testifying for the Public Staff, recommended that the Company receive an overall rate of return of 11.61%, based on a return of common equity of 14.5% and the capital structure and embedded cost rates of Centel's combined telephone operations as of December 31, 1982.

To determine the cost of equity to Centel, witness Weiss first estimated the expected return to the stock market as a whole, as represented by Standard and Poor's 500 Stock Composite. Witness Weiss then examined risk measures published by Value Line, Merrill Lynch, and Standard and Poor's and found that Centel was considered to have lower risk than the market average. Dr. Weiss found that a reasonable estimate of the expected market return was 15% and that for relatively low-risk stocks the return should be lower than the market. Based on the preceding, witness Weiss estimated the expected return for Centel to be 14.75% and the expected return of its telephone operations to be 14.5%. Witness Weiss also performed a DCF analysis which resulted in an expected return of 14.7% to 17.2% for Centel and slightly lower results for a group of seven other telephone companies.

Company witnesses Stephan and Vander Weide testified in rebuttal to the testimony presented by Public Staff witness Weiss regarding this issue. Both witness Stephan and witness Vander Weide testified that the Public Staff's recommended return was inadequate and criticized specific areas of the methodology employed by witness Weiss to derive said return.

The determination of the appropriate fair rate of return for the Company is of great importance and must be made with great care because whatever return is allowed will have an immediate impact on the Company, its stockholders, and its customers. In the final analysis, the determination of a fair rate of return must be made by this Commission, using its own impartial judgment and guided by the testimony of expert witnesses and other evidence of record. Whatever return is allowed must balance the interests of the ratepayers and investors and meet the test set forth in G.S. 62-133(b)(4): "as will enable the public utility by sound management to produce a fair profit for its stockholders, considering changing economic conditions and other factors, as they then exist, to maintain its facilities and services in accordance with the reasonable requirements of its customers in the territory covered by its franchise, and to compete in the market for capital funds on terms which are reasonable and which are fair to its customers and to its existing investors."

The return allowed must not burden ratepayers any more than is necessary for the utility to continue to provide adequate service. The North Carolina Supreme Court has stated that the history of G.S. 62-133(b):

> "supports the inference that the Legislature intended for the Commission to fix rates as low as may be reasonably consistent with the requirements of the Due Process Clause of the Fourteenth Ammendment to the Constitution of the United States...State ex rel. Utilities Commission v. Duke Power Co., 285 N.C. 277, 206 S.E. 2d 269 (1974)."

Based upon the foregoing and the entire record in this docket, the Commission finds and concludes that the fair rate of return that Central should have an opportunity to earn on the original cost of its rate base is 12.09%. Employing the capital structure of Centel's combined telephone operations and associated costs, such fair rate of return will yield a fair return on common equity of 15.5%.

In setting the approved rates of return at the foregoing levels, the Commission has considered all of the relevant testimony and the tests of a fair return set forth in G.S. 62-133(b)(4). The Commission concludes that the revenues herein allowed should enable the Company, given efficient management, to attract sufficient debt and equity capital to discharge its obligations and to achieve and maintain a high level of service to the public.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 12

The Commission has previously discussed its findings and conclusions concerning the fair rate of return which Central Telephone Company should be given the opportunity to earn.

The following schedules summarize the gross revenues and the rates of return which the Company should have a reasonable opportunity to achieve based upon the increases approved herein. Such schedules, illustrating the Company's gross revenue requirements, incorporate the findings and the conclusions heretofore and herein made by the Commission.

SCHEDULE I
CENTRAL TELEPHONE COMPANY
North Carolina Intrastate Operations
STATEMENT OF OPERATING INCOME
Twelve Months Ended June 30, 1982

Item	Present Rates	Increase Approved	Approved Rates
Operating Revenues:			
Local service revenues	$37,161,585	$3,342,059	$40,503,644
Toll service revenues	23,392,325	-	23,392,325
Miscellaneous revenues	2,495,990	-	2,495,990
Uncollectible revenues	(52,026)	(4,679)	(56,705)
Total operating revenues	62,997,874	3,337,380	66,335,254
Operating Revenue Deductions:			
Maintenance expense	11,499,351	-	11,499,351
Depreciation expense	13,312,295	-	13,312,295
Traffic expense	3,263,272	-	3,263,272
Commercial expense	4,029,423	-	4,029,423
General office salaries and expense	4,828,661	-	4,828,661
Other expenses	2,872,326	-	2,872,326
Taxes other than income taxes	6,103,811	200,243	6,304,054
Interest on customer deposits	26,330	-	26,330
State income taxes	794,860	188,228	983,088
Federal income taxes	4,738,784	1,356,498	6,095,282
Total operating revenue deductions	51,469,113	1,744,969	53,214,082
Imputed net operating income on post-test year plant additions	162,605	-	162,605
Net operating income for return	$11,691,366	$1,592,411	$13,283,777

SCHEDULE II
CENTRAL TELEPHONE COMPANY
North Carolina Intrastate Operations
STATEMENT OF RATE BASE AND RATE OF RETURN
Twelve Months Ended June 30, 1982

Item	After Approved Rates
Telephone plant in service	$184,998,404
Reserve for depreciation	(42,944,832)
Net telephone plant	142,053,572
Working capital allowance	(697,021)
Customer deposits	(548,574)
Reserve for deferred income taxes	(29,656,026)
Pre-1971 investment tax credit	(118,774)
Excess profits on affiliated sales	(1,177,000)
Original Cost Rate Base	$109,856,177
Rate of Return	
Present rates	10.64%
Approved rates	12.09%

SCHEDULE III
CENTRAL TELEPHONE COMPANY
North Carolina Intrastate Operations
STATEMENT OF CAPITALIZATION AND RELATED COSTS
Twelve Months Ended June 30, 1982

Item	Ratio %	Original Cost Rate Base	Embedded Cost %	Net Operating Income
	Present Rates - Original Cost Rate Base			
Long-term debt	49.84%	$ 54,752,319	9.02%	$ 4,938,659
Short-term debt	.03	32,957	8.88	2,927
Preferred stock	1.83	2,010,368	5.86	117,808
Common equity	48.30	53,060,533	12.50	6,631,972
Total	100.00%	$109,856,177	-	$11,691,366
	Approved Rates - Original Cost Rate Base			
Long-term debt	49.84%	$ 54,752,319	9.02%	$ 4,938,659
Short-term debt	.03	32,957	8.88	2,927
Preferred stock	1.83	2,010,368	5.86	117,808
Common equity	48.30	53,060,533	15.50	8,224,383
Total	100.00%	$109,856,177	-	$13,283,777

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 13

The evidence for this finding is found in the testimonies of Company witness Rutter and Public Staff witness Willis.

Witness Rutter stated that he pursued the following objectives, wherever possible, to structure his proposed rates and charges:

1. Produce the requested amount of annual revenue increase;
2. Distribute the requested increase among the customers equitably;
3. Relate cost to provision of service wherever possible;
4. Minimize impact on basic local exchange access rates;
5. Recognize the changing nature of the terminal equipment market brought about by changes in regulations, competition, and technology; and
6. Strike a balance of administrative ease, customer understanding, and general acceptability.

Witness Rutter remarked that he had apportioned the $10,594,306, which the Company had originally requested, throughout the Company service offerings by first reviewing vertical equipment and establishing his proposed rates by use of cost studies. He also stated that he had used a cost study to determine and propose rates for the Company's nonrecurring service charges. He proposed a new tariff to unbundle maintenance charges from single-line residence and business service to recover the direct costs of maintaining single-line instruments and associated inside wiring. An increase from $.20 to $.25 for local calls from public and semi-public paystations was proposed. In addition to the above and following his proposal to increase several miscellaneous tariff items by 21.9%, witness Rutter recommended that the residual revenue requirement to be distributed among the Company's service be placed on basic exchange and Extended Area Service (EAS) arrangements.

Under cross-examination, when asked what cost the Company had computed for local coin telephone charges, witness Rutter responded that the unsuppressed cost per call is $.2044 when using a rate of return on investment of 13.4%. It was his reasoning, however, that a coin telephone rate of $.25 per call would cause suppression in the number of units of local calls and thereby cause the cost per call to be equal to $.2271 per local call. From this assumption, witness Rutter determined that the practical rate for local coin telephone calls should be set at $.25 per local call.

The Public Staff presented specific recommendations concerning the Company's proposed rate structure through its witness William J. Willis. Witness Willis expressed his recommendations on the Company's proposed rate levels for nonrecurring service charges, standard rotary and touch call telephone set rates, mileage charges, and EAS rates. He also addressed the Company's proposals for automatic regrouping of local exchanges and the unbundling of maintenance service.

Concerning nonrecurring service charges, witness Willis indicated that the Company had updated its service connection charge cost study and proposed its rates accordingly. He emphasized that upward pressures are being extended by other jurisdictions which are likely to cause significant increases in these basic rates over the next few years, such as changes in the allocations of the Company's nontraffic sensitive plant. Witness Willis stated that it is his opinion that some low income customers will be priced out of the market when confronted with both higher levels of flat monthly rates and higher nonrecurring charges. To mitigate the difficulty some customers may have in obtaining basic service witness Willis recommended two changes in the Company's proposal. First, he recommended that the minimum connection charge for residence be increased from $24.00 to $29.10 rather than to $50.20 as proposed by the Company. Witness Willis' other recommendation would incorporate a change in the Company's tariff which would allow a customer to pay for nonrecurring connection charges over the first six billing periods

rather than over the first four. During cross-examination witness Rutter agreed that customers seeking a service connection would probably prefer to pay an additional access line rate of $.18 per month with an initial nonrecurring charge of $29.10 rather than paying the entire nonrecurring minimum cost of $50.20 proposed by the Company.

With respect to the Company's proposal of six separate charges with which to match the expenses of maintenance for inside wiring and standard stations, witness Willis expressed his difficulty with the Company's objective of having the cost of repair being paid for by the cost causer. It was his opinion that the basis for this type of tariff presumes that the majority of maintenance performed on telephone instruments and inside wiring is the result of intentional abuse or neglect by the customer. He stated that it was difficult for him to conceive that all repairs are due to deliberate action of the subscriber. It was his belief that the majority of troubles are caused by normal wear and tear and chance happenings such as damage due to lightning. He calculated the minimum charge for repair at a customer's premises to be $23.90 for inside wiring and station sets and the maximum charge for repair of a standard rotary and touch call telephone to be $29.70 and $32.60, respectively. Witness Willis recommended that the unbundling of maintenance expense be disapproved in order to safeguard those customers innocent of abusive treatment to inside wiring and standard telephone sets.

On the subject of local coin telephone call rates, witness Willis stated that it was his view that a $.20 call rate as compared to a $.25 per call rate would keep the use of coin telephone service more available to the public in general and in particular to those without telephones in their homes. It was his recommendation to maintain the present coin telephone local call rate at $.20 per call.

Witness Willis reiterated the Public Staff's long standing opposition to a tariff provision which would allow automatic regrouping of exchanges outside of rate proceedings. It was his belief and recommendation that exchanges which have grown beyond their calling scope limits should be regrouped during rate proceedings.

The Company proposed mileage charges for local private lines, off premises extensions, tie lines, and foreign central office lines to increase from $8.00 per mile to $10.60 per mile without the aid of a cost study. Witness Willis recommended $10.00 per mile which he stated was the highest rate of which he was aware that was approved for these types of circuits.

Witness Willis indicated in his prefiled testimony that the Company had proposed to increase its EAS matrix components in a disproportionate manner which ranged from a 35% increase in its lowest mileage band to a 90% increase in its highest mileage band. He also stated that the Company had not performed a cost study of its own. Witness Willis commented that he normally recommended that each element of the EAS matrix receive the same approximate percentage increase as allowed for basic local exchange. In this proceeding, however, for practical purposes, witness Willis recommended no change in the EAS rate levels due to the small increase in local exchange rates which he was recommending.

Based upon the evidence presented by Company witness Rutter and Public Staff witness Willis and the gross revenue increase determination in Finding

of Fact No. 12, the Commission makes the following conclusions to be utilized as guidelines by Central in the design of rates.

1. The schedule of nonrecurring service charges listed below are just and reasonable.

NONRECURRING SERVICE CHARGES

I. Residential Rates	
A. Service Order	
1. Primary	$25.00
2. Secondary	20.20
B. Premises visit, each	6.90
C. Central office work, each	8.90
D. Inside wiring, each	
1. Prewiring	19.45
2. Postwiring	19.45
3. Concealed wiring	40.45
E. Jacks, each	
1. Desk jack	3.95
2. Wall jack	6.45
F. Equipment work, each	7.45
II. Business Rates	
A. Service Order	
1. Primary	41.30
2. Secondary	20.20
B. Premises visit, each	6.90
C. Central office work, each	8.90
D. Inside wiring, each	
1. Prewiring	25.85
2. Postwiring	25.85
3. Concealed wiring	62.50
E. Jacks, each	
1. Desk jack	3.95
2. Wall jack	6.45
F. Equipment work, each	11.50

2. The tariff provision 4.2.1(h) shall remain at four (4) monthly payments instead of the six (6) monthly payments proposed by the Public Staff.

3. The unbundling of maintenance proposal for inside wiring and standard rotary and touch call telephone sets is dismissed without prejudice and the rates for the standard rotary and touch call telephone sets shall be set at $1.50 and $2.00 per month, respectively, which include maintenance.

4. The local paystation rate shall remain at $.20 per local call.

5. Automatic regrouping of exchanges outside of rate proceedings is in the public interest and is hereby approved. The Company is required to notify affected customers by bill insert or separate mail of the Company's intent to adjust local service rates prior to making the automatic regrouping adjustment. This notice should clearly state the reason for regrouping, the authority under which it is undertaken, and the rights of the subscribers to protest or request a hearing. The tariff provision 3.2.3(b) is reasonable and herein approved.

6. Mileage charges for the Company's local private lines, off premises extension lines, tie lines, and foreign central office lines are to be set uniformly at the rate of $10.00 per mile.

7. The EAS matrix should share in the annual revenue increase with the basic local exchange service. The EAS and basic local exchange service shall be adjusted to reflect a uniform across-the-board percentage increase as required (and as permitted without exceeding the proposed increase in such rates) so as to produce the remaining amount of the increase in annual gross revenue approved herein.

8. The additional annual revenue increase allowed of $3,342,059 should be distributed in the manner shown below:

Category of Service	Annual Revenue Increase
Basic local exchange service and EAS components	$1,263,907
Optional toll calling plans	1,771
Service charges	681,792
Special assembly items	48,151
Directory listings	68,773
Coin telephone booth	55
Telephone answering service	662
Foreign central office service	2,193
Miscellaneous service arrangement	211,036
Auxiliary equipment	601,036
Mobile telephone service	31,712
Local private line service:	
Channels and equipment	75,376
Obsolete service offering:	
Special assembly items	23,194
Telephone answering service facilities	550
Key & pushbutton telephone	163,148
Private branch exchange service	79,953
Miscellaneous service arrangement	12,869
Auxiliary equipment	61,142
Connection with facilities and/or equipment of others	3,167
Data service	8,296
Mobile set	3,276
Total	$3,342,059

IT IS, THEREFORE, ORDERED as follows:

1. That the Applicant Central Telephone Company be, and hereby is, authorized to increase its local service rates and charges so as to produce annual gross revenues of $66,391,959 from North Carolina subscribers based upon stations and operations as of June 30, 1982. Such amount represents an amount of $3,342,059 above the revenue level that would have resulted from rates currently in effect based on the test year.

2. That the Applicant is hereby called upon to propose and file with the Chief Clerk of the Commission specific tariffs reflecting changes in rates, charges, and regulations designed in a manner so as to produce a level of revenue no greater than that approved herein, in accordance with the findings, conclusions, and decretal paragraph set forth above, within ten (10) days from the date of this Order. Such filings shall include workpapers supporting such proposals. A format such as Item 30 of the minimum filing requirement N.C.U.C. Form P-1 is suggested. An original and five copies of each of the foregoing is required.

3. The Public Staff may file written comments concerning the Company's tariffs within five (5) days of the date on which they are filed with the Commission.

4. The rates, charges, and regulations necessary to produce the annual gross revenues authorized herein shall become effective upon the issuance of a further Order approving the tariffs filed pursuant to Ordering Paragraph No. 2 above.

5. That Central shall give notice of the rate increase approved herein by first-class mail to each of its North Carolina customers during the next billing cycle following the filing and acceptance of the rate schedules described in Ordering Paragraph No. 2 above. Such Notice to Customers shall be submitted to the Commission for approval prior to issuance.

ISSUED BY ORDER OF THE COMMISSION.
This the 22nd day of June 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sandra J. Webster, Chief Clerk

APPENDIX A
CENTRAL TELEPHONE COMPANY
DOCKET NO. P-10, SUB 415

Depreciation Rates

Account Number	Account Title	Approved Depreciation Rate
212	Buildings	2.3
221.1	Step by Step	15.6
221.2	Manual	5.5
221.3	Radio	6.7
221.4	Circuit Other	7.4
221.5	Crossbar	8.5
221.6	Circuit Digital	7.4
221.9	Electronic Digital	5.0
231	Station Apparatus	11.3
232.2	Station Connections Dropwire	5.0
234	Large PBX	26.7
241	Pole Lines	5.6
242.1	Aerial Cable	3.3
242.2	Underground Cable	3.3
242.3	Buried Cable	3.0
243	Aerial Wire	11.5
244	Underground Conduit	1.6
261.0	Furniture & Office Equipment-Major	4.7
264.1	Vehicles	10.0
264.2	Other Work Equipment-Major	5.5

Amortization Amounts

Account Number	Account Title	Approved Amortization Amount
221.8	Electronic Analog	$ 136,225
232.1	Station Connection-Inside Wire	1,595,925
261.1	Furniture & Office Equipment-Minor	32,049
264.3	Other Work Equipment-Minor	10,351

DOCKET NO. P-12, SUB 80

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Application by Citizens Telephone Company for Authority to Adjust Its Rates and Charges Applicable to Intrastate Telephone Service in North Carolina) ORDER GRANTING PARTIAL RATE INCREASE

HEARD IN: Transylvania County Courthouse, Brevard, North Carolina, on Tuesday, January 11, 1983

Commission Hearing Room, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina, on Tuesday, January 18, 1983, and Wednesday, January 19, 1983

BEFORE: Commissioners Edward B. Hipp, Presiding; and Commissioner Leigh H. Hammond and Commissioner A. Hartwell Campbell

APPEARANCES:

For the Applicant:

Thomas R. Eller, Jr., Attorney at Law, Post Office Drawer 27866, Raleigh, North Carolina 27611
For: Citizens Telephone Company

For the Using and Consuming Public:

Theodore C. Brown, Staff Attorney, Public Staff - North Carolina Utilities Commission, Post Office Box 991, Raleigh, North Carolina 27602
For: The Using and Consuming Public

BY THE COMMISSION: On August 25, 1982, Citizens Telephone Company (Applicant, Company, or Citizens) filed an application with the North Carolina Utilities Commission seeking authority to adjust its rates and charges for intrastate local exchange service. The application seeks the approval of rates that will produce $1,499,537 of additional annual revenues from its intrastate local exchange operations when applied to a test year consisting of the 12 months ended December 31, 1981. The Company proposed that the rates and charges be effective for service rendered on and after October 1, 1982.

By Order issued on September 24, 1982, the Commission declared the matter to be a general rate case pursuant to G.S. 62-137, suspended the proposed rates and charges for 270 days from the October 1, 1982, effective date, set hearings to begin on January 11, 1983, declared the test period to be the 12 months ended December 31, 1981, required the Company at its expense to give public notice of the proposed increase and hearings and set the time for the Public Staff and other interested parties to file interventions and/or testimonies.

The Public Staff filed Notice of Intervention in this docket on December 15, 1982. The intervention of the Public Staff has been recognized pursuant to Commission Rule R1-19(e). There were no other Notices or applications to intervene.

The Commission conducted an out-of-town hearing for the purpose of receiving testimony from the using and consuming public. The hearing was held in Brevard, North Carolina, at 7:00 p.m., in the Transylvania County Courthouse, on January 11, 1983. The following public witnesses appeared and offered testimony: Robert L. Galloway, J. W. Owen, Louise Dishman, Charles Krueck, Abe Gosen, Connie Holt, Robert Armstrong, Bill Siniard, Joseph Keller, Mike Galloway, Larry Bessette, Bill Boggs, Herbert Henson, Jr., and John R. Hudson, Jr.

The hearings were resumed in Raleigh at 10:00 a.m. on January 18, 1983, for the purpose of receiving further testimony of public witnesses and the testimony and cross-examination of the Applicant and Public Staff. Citizens offered the testimony and exhibits of the following witnesses: Charles W. Pickelsimer, Jr., Vice President and General Manager, who testified as to the

Company's financial and operating conditions, its service and construction requirements, the level of its operating expenses and capital costs required to maintain, improve and expand its service, and its proposals to distribute its revenue requirements more nearly in line with cost incurrence; David O. Albertson, Secretary-Treasurer and Controller, who testified as to the Company's property and financial records and allocations, accounting audits and results, and total cost of service and its distribution among the various subscriber classes; Judy D. Beacham, Senior Utility Analyst, Currin and Associates, Inc., who presented the results of her firm's investigation of the Company's North Carolina intrastate original cost of utility plant in service, the revenues, expenses, and return on the net original cost of the Company's property used in rendering intrastate local telephone service; and H. Randolph Currin, Jr., President of Currin and Associates, Inc., who testified on the subjects of cost of capital, fair rate of return on investment in utility property, reasonableness and standards for determining reasonableness of general officer salaries and expenses, and on the extent the proposed increase could or might result in a real price increase to subscriber classes.

The Public Staff offered the testimony and exhibits of the following witnesses: William J. Willis, Jr., Engineer - Communications Division of the Public Staff, who testified as to end-of-period revenues, miscellaneous tariff proposals, and rates; George T. Sessoms, Jr., an Economist with the Public Staff, who testified as to the appropriate capital structure, cost of equity, and cost of total capitalization; James G. Hoard, Staff Accountant - Public Staff, who testified concerning levels of operating revenues, expenses, and rate base of the Company's local exchange service operations; and Thi-Chen Hu, Engineer - Communications Division of the Public Staff, who testified concerning the adequacy and quality of the Company's intrastate service.

On Friday, January 14, 1983, Public Staff witnesses Sessoms and Hoard filed revisions in their expert testimony and exhibits which had been prefiled on December 29, 1983. Citizens objected to the timeliness of the revised testimony and filed written Motion to suppress it. The Motion of the Applicant was denied, with exceptions duly noted.

Based upon the foregoing, the testimony and exhibits admitted into the record, the arguments and briefs of counsel, the matters judicially noticed in the record, and a review and consideration of the entire record as submitted, the Commission now makes the following

FINDINGS OF FACT

1. The Applicant, Citizens Telephone Company, is a duly organized North Carolina corporation headquartered in Brevard, North Carolina. Citizens holds a franchise from this Commission to provide public utility telephone service in exchanges located in Transylvania County, North Carolina. Citizens is properly before the Commission in this proceeding, pursuant to G.S. 62-133, for a determination of the justness and reasonableness of its proposed rates and charges.

2. By its application, the Company seeks rates to produce jurisdictional gross revenues of $4,675,597, based upon a test year ended December 31, 1981. Company-contended revenues under present rates are $3,176,060, thereby necessitating an increase of $1,499,537.

3. The test period consisting of the 12-month period ended December 31, 1981, is representative and reasonable for use in this proceeding.

4. The overall quality of local exchange telephone service provided by Citizens is adequate. The service is exclusively one-party service and has been since 1971.

5. The Company's original cost rate base should include post-test year plant additions of $1,095,342, less accumulated depreciation of $66,441 and accumulated deferred income taxes of $24,715. It is also proper to impute net operating income of $54,062 on the net post-test year plant additions.

6. Citizens' reasonable original cost rate base used and useful in providing telephone service to the public within the State of North Carolina is $10,259,840. This consists of telephone plant in service of $15,530,874, investment in RTB stock of $254,809, and an allowance for working capital of $104,055, reduced by accumulated depreciation of $4,511,251, accumulated deferred income taxes of $946,316, pre-1971 investment tax credit of $20,861, and customer advances of $151,470.

7. The reasonable level of test year gross intrastate operating revenues for Citizens, under present rates and after accounting and pro forma adjustments is $3,178,216.

8. Citizens' reasonable level of jurisdictional operating revenue deductions is $2,655,554 after normalization and pro forma adjustments. This level of test year operating expenses includes $931,965 of actual investment currently consumed by previous use recovered by depreciation expense.

9. The equity ratio proposed by the Company is overstated and the total capitalization should be reduced by $950,500 which is the amount of Citizens' investment in a wholly owned cable television subsidiary which is not a public utility operation as defined by G.S. 62-3(23).

10. The Company's appropriate capital structure for use in this proceeding is as follows:

Item	Percent
Long-term debt	67.97%
Common equity	32.03%
Total	100.00%

Consistent with this capital structure, the associated cost rates are 5.57% on long-term debt and 16.00% on common equity.

11. The overall rate of return to be applied to the Company's original cost rate base is 8.91%. Said amount allows the Company the opportunity to earn a 16% return on its investment supported by common equity. Such rate of return will enable the Company, by sound management, to produce a fair return for its shareholders and to maintain its facilities and service in accordance with the reasonable requirements of its customers.

12. The annual gross revenue requirement for Citizens is $3,899,471. This is an increase of $721,255. Said revenues will allow the Company to earn the rate of return on its rate base that the Commission has found to be just and

reasonable. This revenue requirement is based upon the original cost of Citizens' property used and useful in providing service to its customers and its reasonable test year operating revenues and expenses as previously set forth in these findings.

13. The rates and charges contained in Appendix A attached hereto which will produce an increase in annual gross revenues of $721,255 are just and reasonable.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 1, 2 AND 3

The evidence supporting these Findings of Fact is contained in the Company's verified application, in prior Commission Orders in this docket of which the Commission takes judicial notice, including the Order of September 24, 1982, which set hearings and established the test period. These Findings of Fact are essentially informational, procedural and jurisdictional in nature and the matters which they involve are uncontested.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 4

The evidence for this finding comes from the testimony of the public witnesses and the Company's response thereto, and the testimony and exhibits of Company witness Pickelsimer and Public Staff witness Hu.

Company witness Pickelsimer filed a written response to each of the 14 public witnesses who testified concerning various service complaints. In witness Pickelsimer's written report, it stated that some of the complaints were justified due to the fact the Company was in a period of transition from electro-mechanical switching to all digital technology. Witness Pickelsimer also conceded that the Company has had some problems in handling out-of-service reports after working hours due to size, density, terrain, and weather conditions peculiar to the Company. Witness Pickelsimer further described the procedures used and efforts made by the Company to strengthen the handling of such reports. A number of the complaints were associated with long distance calls over which the Company did not have control. Witness Pickelsimer expressed concern that the Company's arrangement with Bell for reporting after hours trouble calls was not working as satisfactorily as previously thought and stated that the Company was considering alternatives whereby such reports would be handled locally. Witness Pickelsimer testified that for some years he had sought an improvement by Bell of the Asheville trunking for tolls and that the feasibility of several alternatives independent of Bell were being considered. Further, witness Pickelsimer pointed out that the Company had received only one written subscriber complaint in 1978, two in 1979, none in 1980, one on service in 1981, and four on service subsequent to filing the application in 1982.

Public Staff witness Hu testified that his review consisted of field inspections and tests of switching and trunking facilities; measurements of the answer time of operators, directory assistance, repair service and business offices; an analysis of statistics relating to the Company's service; and a review of complaints received by the Commission and the Public Staff from the Company's subscribers. Witness Hu testified that the Company had no held order problems and that, since the Company had rendered area-wide one-party service to all customers since 1971, no regrade problems existed. After reviewing the Company's service data and evaluating test results,

witness Hu concluded that the overall quality of service provided by the Company was adequate.

Based upon the foregoing evidence, the Commission accepts the report filed by the Company in response to the testimony of the public witnesses as satisfying the Commission's request and concludes that the overall quality of service provided by Citizen's Telephone Company is adequate.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 5

Company witnesses Beacham and Albertson and Public Staff witness Hoard presented testimony concerning post-test year plant additions. The levels that the parties' contend in their proposed orders to be proper to include as rate base and net operating income adjustments related to the plant additions are shown in the following chart:

Item	Company	Public Staff	Difference
Rate base adjustments:			
Telephone plant in service	$1,143,507	$ 915,781	$(227,726)
Accumulated depreciation	(69,748)	(49,056)	20,692
Accumulated deferred income taxes	-	(22,650)	(22,650)
Net rate base effect	$1,073,759	$ 844,075	$(229,684)
Net operating income adjustment:			
Imputed net income on post-test year plant additions	$ 54,225	$ 46,652	$ (7,573)

Company witness Beacham made an adjustment for estimated post-test year plant additions through December 31, 1982, of $1,124,325 in her pre-filed testimony. During the hearing Company witness Albertson presented evidence in Albertson Exhibit 7, that the Company's actual intrastate post-test year plant additions through January 14, 1983, were $1,143,507. Witness Beacham adjusted jurisdictional telephone plant in service pursuant to G.S. 133(c) to include plant used and useful through the close of the hearings. Thus, witness Beacham adjusted the test year plant in service account by $1,143,507, which brought the Company's plant in service amount to $15,579,039.

Public Staff witness Hoard included actual plant additions through September 30, 1982, of $915,781. Witness Hoard stated in response to cross-examination that he included post-test year plant additions through September 30, 1982, in recognition of the material changes in the Company's investment since the end of the test year. Witness Hoard stated that the September 30, 1982, investment and capitalization data were the most recent available to him and Public Staff witness Sessoms when they were assembling their exhibits. Witness Hoard further explained that, due to the materiality of the post-test year investment and capitalization changes, the plant investment and capitalization must be expressed at the same date in order to be consistent.

Based upon a review of the evidence, the Commission concludes that the proper amount of post-test year plant additions to include in telephone plant in service is $1,095,342 which is the amount of plant additions as of December 31, 1982, a date consistent with the Commission's long-term debt embedded cost rate. Accordingly, the Commission finds that $15,530,874 is the reasonable and representative level of telephone plant in service to include in Citizens'

rate base for the period in which rates set in this proceeding will be in effect.

With respect to the depreciation reserve, the $20,692 difference stems from the differing amounts of post-test year plant additions included by witnesses Beacham and Hoard. Witness Beacham computed accumulated depreciation of $69,748 related to the $1,143,507 post-test year plant additions as compared to witness Hoard's proposed amount of $49,056 related to plant additions of $915,781.

Based on the Commission's prior finding concerning telephone plant in service, the Commission finds $1,095,342 the proper amount of post-test year plant additions on which to compute the additional depreciation. The Commission also finds it more accurate to use the specific individual account depreciation rates rather than a composite depreciation rate and, therefore, concludes that the appropriate adjustment to the depreciation reserve for post-test year plant additions is $66,441.

The next item of difference concerns a $22,650 pro forma adjustment recommended by witness Hoard for additional accumulated deferred income taxes related to post-test year plant additions. Witness Hoard explained this adjustment in his prefiled direct testimony as follows:

> "Since there would have been additional excess tax over book depreciation had the plant additions been in service at December 31, 1981, I have included the related additional accumulated deferred income taxes with cost-free capital as a rate base reduction."

Company witness Beacham calculated the amount of accumulated deferred income taxes on her January 14, 1983, level of plant additions to be $25,223. However, the Company did not allow any cost-free funds to be included as a deduction from rate base and thus the $22,650 difference between the Company and the Public Staff exists.

The Commission finds that it is both consistent and proper to include additional accumulated deferred income taxes related to the post-test year plant additions since there would have been more accumulated deferred income taxes had the plant been in place at the end of the test year. Consistent with the inclusion of plant additions as of December 31, 1982, the Commission has included as a deduction from rate base $24,715 of accumulated deferred income taxes for the difference between the straight line depreciation rates used in the proceeding and liberalized depreciation methods available to Citizens for federal income tax purposes.

Witnesses Beacham and Hoard both imputed additional net operating income on the post-test year plant additions. Both parties imputed net operating income based on the ratio of net operating income to original cost rate base, exclusive of the post-test year plant additions. The $7,573 difference between the parties' imputed net operating incomes is due to the following factors:

(1) Different post-test year plant addition amounts,
(2) Different capital structures,
(3) Different embedded cost of debt percentages,
(4) Different net operating income and original cost rate base amounts before the post-test year plant additions.

The Commission has imputed net operating income of $54,062 based on the findings of fact included in this Order.

In summary, the Commission finds the following pro forma adjustments for post-test year plant additions to be appropriate for use in this proceeding:

Item	Amount
Rate base adjustments:	
Telephone plant in service	$1,095,342
Accumulated depreciation	(66,441)
Accumulated deferred income taxes	(24,715)
Net rate base effect	$1,004,186
Net operating income adjustment:	
Imputed net income on post-test year plant additions	$ 54,062

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 6

The evidence for this finding of fact is found in the testimony and exhibits of Company witnesses Albertson and Beacham and Public Staff witness Hoard. According to the proposed orders of the Company and the Public Staff the appropriate amounts to be included in the intrastate original cost rate base for use in this proceeding are as follows:

Item	Company	Public Staff	Difference
Telephone plant in service	$15,579,039	$15,351,313	$ (227,726)
Investment in RTB stock	254,809	254,809	-
Working capital allowance	106,728	102,060	(4,668)
Depreciation reserve	(4,514,558)	(4,493,866)	20,692
Accumulated deferred income taxes	-	(944,251)	(944,251)
Pre-1971 investment tax credit	-	(20,861)	(20,861)
Customer advances	-	(151,470)	(151,470)
Original cost rate base	$11,426,018	$10,097,734	$(1,328,284)

The Company and the Public Staff are in agreement as to the amount of investment in Rural Telephone Bank (RTB) stock that should be recognized in the determination of rate base. There being no evidence to the contrary, the Commission concludes that this amount is reasonable and proper for use herein.

The $227,726 difference in telephone plant in service and the $20,692 difference in depreciation reserve amounts relate entirely to the parties' respective post-test year plant additions adjustments. Based upon the Commission's previous determination of the proper levels of plant addition adjustments to be included in rate base in Evidence and Conclusions for Finding of Fact No. 5, the Commission concludes that $15,530,874 for telephone plant in service and $4,511,251 for accumulated depreciation reserve are the appropriate amounts to include in rate base in this proceeding.

The next area of difference is the appropriate working capital allowance. The working capital allowance is comprised of cash working capital, materials and supplies, and average prepayments, less average tax accruals and customer deposits. The only component that the Company and Public Staff differ on is cash working capital. This difference of $4,668 results solely from the witnesses' different levels of operating expenses exclusive of depreciation. In Evidence and Conclusions for Finding of Fact No. 8 hereinafter the Commission has concluded that the proper level of operating expenses is $1,360,092, consequently the Commission finds that the proper cash working capital amount is $113,341 and the total working capital allowance appropriate for use herein is $104,055.

The remaining differences in rate base are related to accumulated deferred income taxes, pre-1971 investment tax credits and customer advances, all of these items are cost-free funds. Company witness Beacham and Public Staff witness Hoard disagreed, both as to the amount and the rate-making treatment of cost-free funds.

The Commission will first resolve the differences between the parties as to the amount of cost-free funds. The differences in the cost-free capital amounts are reflected in the following chart:

Item	Company	Public Staff	Difference
Accumulated deferred income taxes	$ 946,824	$ 944,251	$(2,573)
Pre-1971 investment tax credit	20,861	20,861	-
Customer advances	113,448	151,470	38,022
Total cost-free capital	$1,081,133	$1,116,582	$35,449

The first item of difference in the amount of $2,573 is a result of the parties recognition of different levels of post-test year plant additions. The Company calculated accumulated deferred income taxes on post-test year plant additions to be $25,223 whereas the Public Staff amount was calculated to be $22,650.

The Commission has previously discussed additions to plant in service after the end of the test year and prior to the close of the hearings. Consistent with its findings that telephone plant additions as of December 31, 1982, should be included in rate base and the depreciation reserve be adjusted accordingly, the Commission concludes that the amount of accumulated deferred income taxes associated with the plant additions is $24,715. Therefore, the Commission concludes that the amount of accumulated deferred income taxes to be used in this case is $946,316.

There is no disagreement between the parties as to the proper level of pre-1971 investment tax credits. There being no evidence to the contrary, the Commission accepts the proper level of pre-1971 investment tax credits as $20,861.

The last area of difference concerns customer advances for construction. This difference of $38,022 for customer advances relates entirely to an advance made by Olin Corporation.

Public Staff witness Hoard explained his treatment of the Olin Corporation customer advance in his pre-filed testimony as follows:

"Since the Company has the use of these funds and the related investment is in the Company's rate base, ratepayers should not be required to pay a return on that investment."

Therefore, witness Hoard included the Olin Corporation advance as cost-free capital.

The Company stated that the Olin advance was a prepayment of rate revenues made by Olin Corporation at its own request and convenience. The Company treated this prepayment as deferred revenues and is amortizing it to local service revenues over a 10-year period. The remaining unamortized balance of these deferred revenues is $38,022. Witness Beacham credited local service revenues in the case with the appropriate amount of rate revenues based upon the 10-year amortization period. The Company argued against the Public Staff's treatment of the Olin prepayment as cost-free capital and stated that witness Hoard had mismatched rate base and revenues since he had not excluded the deferred revenues from Olin which witness Beacham had charged to local service revenues.

The Commission concurs with witness Hoard regarding the treatment of the Olin Corporation customer advance as cost-free capital, and, therefore, has reduced the Company's intrastate rate base by $151,470. The Commission finds that revenues and rate base are matched in that the proper annual level of rate revenues associated with the Olin advance have been recognized and the unamortized portion has been included in the rate base determination as cost-free capital.

The Commission will now discuss the treatment to be accorded cost-free capital in this proceeding.

Company witnesses Pickelsimer and Albertson contended that there is no such thing as "cost-free" telephone utility plant. They stated that the central switching facilities, trunks, lines, etc., comprising the Company's used and useful telephone plant cannot be segregated into two classes, one of which is cost-free and not entitled to any rate of return, the other entitled to a rate of return. The company witnesses attempted to illustrate their position by saying that all installed telephone plant is subject to the same depreciation and obsolescence, the same maintenance and repair, the same right of way maintenance, the same lightning, flooding and accidental damage, the same debt costs, taxes, and return. They further contended that, in a small company such as Citizens, where cost-free funds are almost 10% of jurisdictional rate base, the burden would be severe if these funds were eliminated from rate base. However, the Company witnesses agreed that these funds are not presently costing them anything, but said they are at most cost-free capital but not cost-free plant. The Company recognized the existence of its cost-free capital by using it as an economic factor in determining the fair rate of return and the times interest earned ratio (TIER).

Public Staff witness Hoard testified that all of the cost-free capital is directly related to the rate base investment. Accordingly, witness Hoard assigned all of the cost-free capital to the rate base investment and thus treated the cost-free capital as a deduction from rate base.

Based upon the evidence of record in this case, the Commission concludes that it is entirely equitable and proper to assign 100% of the cost-free

capital to the Company's utility operations. The Commission believes that Citizens' customers should not be required to pay a return on funds which they have contributed, when such capital has no cost to the Company. Furthermore, the Commission finds that it is improper to include cost-free capital in the capital structure as such treatment allocates a portion of these funds to the Company's investment in nonutility property. As to the Company's position of treating cost-free capital as an economic factor in determining the fair rate of return, the Commission concludes such treatment is unnecessary since the cost-free funds are directly assignable to the rate base investment. The Commission concludes that the proper rate-making treatment of cost-free capital is to directly assign it to the rate base in the form of a rate base deduction. Therefore, the Commission finds that the proper level of cost-free capital for inclusion in the determination of rate base is $1,118,647.

In summary, the Commission concludes that the proper level of the original cost rate base for use in this proceeding is $10,259,840 calculated as follows:

Item	Amount
Telephone plant in service	$15,530,874
Investment in RTB stock	254,809
Working capital allowance	104,055
Depreciation reserve	(4,511,251)
Accumulated deferred income taxes	(946,316)
Pre-1971 investment tax credit	(20,861)
Customer advances	(151,470)
Original cost rate base	$10,259,840

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 7

Company witnesses Beacham and Pickelsimer and Public Staff witnesses Hoard and Willis presented testimony and exhibits concerning the proper level of end-of-period intrastate operating revenues. According to the proposed orders filed by the parties, the appropriate level of revenues is as shown in the following chart:

Item	Company	Public Staff	Difference
Local service revenues	$1,836,108	$1,836,108	$ -
Toll service revenues	1,132,861	1,124,492	(8,369)
Miscellaneous revenues	220,305	208,240	(12,065)
Uncollectible revenues	(5,642)	(5,642)	-
Total operating revenues	$3,183,632	$3,163,198	$ (20,434)

The parties did not disagree on the proper level of end-of-period local service revenue and uncollectible revenue. Therefore, the Commission concludes without further discussion that a level of $1,836,108 for local service revenue is proper for use in this proceeding. Furthermore, the Commission finds that the use of a .29025% local service revenue uncollectible rate and a .18675% directory revenue uncollectible rate is appropriate for use herein. Based on the foregoing, the Commission finds that the reasonable level of uncollectible revenues is $5,642.

The first area of difference concerns the appropriate level of end-of-period toll service revenues. The Company's end-of-period toll service revenues of $1,132,861 was determined using an 11.5% toll settlement ratio.

Although the Public Staff did not contest witness Beacham's 11.5% toll settlement ratio, witness Hoard decreased the toll service revenue amount by $8,369 to reflect the toll revenue effect of the Public Staff's adjustments to rate base and expenses. Furthermore, since net operating income was imputed on post-test year plant additions it would have been inappropriate to present any toll service revenue effects of the post-test year plant additions adjustments. Consequently, neither witness reflected any toll service revenue effect for the plant additions.

The Commission concludes that the end-of-period level of intrastate toll revenues of $1,124,492 determined by Public Staff witness Hoard increased by the Commission's adjustments of $9,376 yields $1,133,868, the appropriate level of toll revenues for inclusion in this rate case proceeding. The Commission's adjustment of $9,376 recognizes the Commission's rate base and interest expense level and eliminates the effect of the Public Staff adjustments to salary expense and pension expense for excessive executive salaries.

Miscellaneous revenues is the remaining area of difference. The $12,065 difference is due entirely to a pole rental adjustment made by Company witness Beacham, and reversed by Public Staff witness Hoard. Witness Beacham increased pole rental revenues by $12,065 and pole rental expense by $32,077 to reflect a $10.50 per pole expected increase in the Company's joint use contract with Duke Power. Both witnesses Beacham and Pickelsimer testified that the increase in pole rentals from $2.00 to $12.50 was a fixed, known, and ascertained change at the time of the hearings.

Public Staff witness Hoard reversed witness Beacham's adjustment because a new pole attachment contract with Duke had not yet been consummated. Since no competent evidence was presented supporting an actual change in the pole rental rate, the Commission has adjusted Citizens' miscellaneous revenues to eliminate the Company's pole rental adjustment. The Commission, therefore, finds miscellaneous revenues of $208,240 appropriate for use herein.

In summary, the Commission concludes that the proper end-of-period level of gross intrastate operating revenues for use herein is $3,178,216. Net operating revenues of $3,172,574 are calculated as follows.

Item	Amount
Local service revenues	$1,836,108
Toll service revenues	1,133,868
Miscellaneous revenues	208,240
Uncollectible revenues	(5,642)
Total operating revenues	$3,172,574

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 8

The evidence for this finding of fact is found in the testimony and exhibits of Company witnesses Beacham and Currin and Public Staff witness Hoard. The parties' positions regarding operating revenue deductions as set forth in their proposed orders are given below:

Item	Company	Public Staff	Difference
Operating expenses	$1,398,881	$1,336,155	$(62,726)
Depreciation and amortization	931,966	931,965	(1)
Operating taxes - other than income	335,674	334,448	(1,226)
Other interest expense	886	886	-
State income taxes	4,165	11,471	7,306
Federal income taxes	(30,993)	21,655	52,648
Total operating revenue deductions	$2,640,579	$2,636,580	$ (3,999)

The Company and the Public Staff are in agreement on the amounts which are included in depreciation expense and other interest expense; therefore, the Commission concludes that the proper levels for depreciation and amortization expense and other interest expense are $931,965 and $886, respectively.

The Company and Public Staff disagree as to the proper level of operating expenses. The $62,726 difference is comprised of several items which are reconciled as follows:

Item	Amount
Operating expenses per Company	$1,398,881
Public Staff adjustments:	
To general office expense for excess executive salaries	(17,659)
To other operating expenses to remove the pension benefits related to the excess executive salaries	(6,278)
To other operating expenses to reverse the Company's pole rentals adjustment	(32,077)
To miscellaneous income charges to reverse the Company's charitable contribution deduction	(6,712)
Operating expenses per Public Staff	$1,336,155

The first two items of difference result from the Public Staff's reduction in the Company's top two executive salaries. Witness Hoard presented an analysis of the salaries of executives for several North Carolina based telephone companies for the years 1981 and 1980. Witness Hoard stated that his analysis showed that Citizens was the fifth largest of the eight companies in terms of main stations and that its highest paid executive was paid a salary 67% above any other executive of the companies presented. Furthermore, witness Hoard stated the analysis showed that Citizens' second highest paid executive was paid 31% more than the highest paid executive from any of the other companies.

Based upon this analysis, witness Hoard reduced general office expense by 30% of the intrastate regulated portion of the Company's highest paid executive. Witness Hoard testified that since the second highest paid executive's salary was 100% capitalized, general office expenses did not reflect an adjustment for his salary. Witness Hoard did, however, reflect a 30% salary reduction of the two top executives in adjusting other operating expenses for the related pension benefits expense.

Company witness Currin testified as to the reasonableness of Citizens' executive salaries as follows:

"The best way that I know to make a fair evaluation of the reasonableness of salary levels is to look at all of the general office salaries and expenses, and then compare those figures with other telephone companies in the State."

In order to analyze the fairness of the Company's salary payments, witness Currin chose two samples of North Carolina telephone companies to make comparisons in terms of general office salaries and expenses per subscriber and per telephone for each sample. The telephone companies used by witness Currin were segregated into the following two samples (a) all regulated REA-financed telephone utilities in North Carolina and (b) all independent telephone companies in the State. The results of witness Currin's studies showed that the general office salaries and expenses of Citizens Telephone Company were the lowest of any of the nine REA-financed telephone utilities in the State when judged by witness Currin's standards. For all six independent telephone utilities in the State, Citizens ranked as the fifth from the lowest.

The Commission concludes that Citizens Telephone Company has borne its burden of proof on this issue of reasonableness. The salaries and pension benefits of the owner-operators were allocated by witness Beacham among several companies in which they have interests (sale of terminal equipment, Sylvan Valley CATV, Valley Ford, and Utilities Holding Company). The reasonableness of these allocations was not questioned by the Public Staff. The proper issue in this case is whether these allocated jurisdictional general office salaries and wages are unreasonable for the intrastate local service customer to pay. Consistent with the prior finding on quality of service and management efficiency, the Commission observes that there is no basis for penalizing the Company's management in this case. Furthermore, upon review of Public Staff witness Hoard's salary analysis, the Commission finds such analysis questionable as it includes salary compensation for unregulated activities. Based on the foregoing, the Commission concludes that the Company's uncontradicted allocations to arrive at jurisdictional salaries and wages should be approved and that the Public Staff's adjustment for excessive executive salaries should be disallowed.

The third item was addressed in Finding of Fact No. 7 with reference to the matching adjustment to miscellaneous revenues, wherein the Commission concluded the Company's pole rental price increase adjustments should not be allowed as it is uncertain at this time what the price per pole rental rate will be in the future.

The final item of disagreement in the category of reasonable operating and maintenance expenses concerns the matter of charitable contributions to be included in the case. Company witness Beacham first excluded actual expenditures by the Company for civic club memberships and dues, Chamber of Commerce dues and contributions, country club expenses, etc. However, witness Beacham deemed contributions made by the Company to the eleemosynary institutions and funds for employee emergency relief, the Transylvania Community Hospital, Brevard College, and Brevard Music Camp as recurring and necessary contributions by Citizens to the health, safety, cultural, and economic well-being of the general body of local subscribers and included such expenses in her computations. Witness Pickelsimer stated that Citizens had always supported such institutions and believed such support to be absolutely necessary if Citizens is to be a proper corporate citizen in the territory it serves.

Public Staff witness Hoard excluded these charitable contributions in the amount of $6,712. He did so on two grounds: (1) Since Citizens' ratepayers may make their own charitable contributions, they should not be required involuntarily to make charitable contributions through the payment of telephone rates to charities selected by Citizens; and (2) the Commission has rendered numerous decisions disallowing charitable contributions as operating revenue deductions.

Based upon the evidence presented by the parties, the Commission concludes that the charitable contributions in the amount of $6,712 should not be included as an operating revenue deduction. Thus the Commission concludes that the proper level of operating expenses for use in this proceeding is $1,360,092.

The next area of difference concerns operating taxes other than income. The amount of this difference is $1,226 and is due entirely to the Public Staff's $20,434 reduction in the level of the Company's operating revenues under present rates. The Commission has concluded in Finding of Fact No. 7 that the proper level of gross operating revenues is $3,178,216 and accordingly recognizes the associated gross receipts taxes. Therefore, the Commission finds that the proper level of taxes other than income is $335,011.

The final two differences in operating revenue deductions are state and federal income taxes, these differences arise from the use of different levels of revenues and expenses by the parties. Their methodologies are the same. Furthermore, both the Company and the Public Staff have included the interest portion of the Company's post 1971 Job Development Investment Tax Credit (JDITC) as a tax deduction.

The proper level of income tax expense to be included in the cost of service in this proceeding is dependent upon the levels of rate base, revenues and expenses and the treatment of JDITC, a matter concerning the propriety of imputing interest to a portion of funds arising from utilization of the JDITC. In numerous rate proceedings before the Commission, the Public Staff has steadfastly maintained that the Revenue Act of 1971, which implemented the JDITC, permits the Commission to impute interest thereto for use in determining the test year level of federal income tax expense. The Commission has consistently found, for reasons which need not be repeated here, that the Public Staff's position in this regard was and is incorrect in its entirety. The North Carolina Court of Appeals in Utilities Commission v. Carolina Telephone, --N. C. App.-- (COA #8210UC706, filed 1 March 1983), affirmed the Commission findings in this regard, this matter having been appealed by the Public Staff. In the words of the Court:

"The issue on appeal, as stated by the Public Staff in its brief, 'is whether the Commission erred as a matter of law in concluding that Section 46(f)(2) of the Internal Revenue Code requires that all effects of JDITC should be excluded from the determination of interest expense.'

"G.S. 62-94 sets forth the standard of judicial review of orders of the Utilities Commission and includes the following:

(b) So far as necesary to the decision and where presented, the court shall decide all relevant questions of law, interpret constitutional and

> statutory provisions, and determine the meaning and applicability of the terms of any Commission action. The court ... may reverse or modify the decision if the substantial rights of the appellants have been prejudiced because the Commission's findings, inferences, conclusions or decisions are:
>
> . . .
>
> (4) Affected by other errors of law...
>
> . . .
>
> (e) Upon any appeal, the rates fixed or any rule, regulation, finding, determination, or order made by the Commission under the provisions of this Chapter shall be prima facie just and reasonable.

In this appeal we are called upon to interpret the applicable sections of the Internal Revenue Code to determine whether the Commission's order is affected by errors of law. We conclude that the order is not so affected.

Section 46(f)(2) of Title 26 of the Internal Revenue Code provides that JDITC will be disallowed with regard to public utility property in the following two circumstances.

> (A) Cost of service reduction.--If the taxpayer's cost of service for ratemaking purposes or in its regulated books of account is reduced by more than a ratable portion of the credit allowable by section 38 (determined without regard to this subsection), or
>
> (B) Rate base reduction.--If the base to which the taxpayer's rate of return for ratemaking purposes is applied is reduced by reason of any portion of the credit allowable by section 38 (determined without regard to this subsection).

The term 'ratable portion' is explained in Section 46(f)(6):

> For purposes of determining. . .ratable portions under paragraph (2)(A), the period of time used in computing depreciation expense for purposes of reflecting operating results in the taxpayer's regulated books of account shall be used.

The following example of 'ratable portion' appears in Section 1.46-6(g)(2) of the Treasury Regulations:

> (I)f cost of service is reduced annually by an amount computed by applying a composite annual percentage rate to the amount of the credit, cost of service is reduced by a ratable portion.

The Internal Revenue Service has published the following regulations implementing Section 46(f)(2):

> (2) Cost of service. (i) For purposes of this section, 'cost of service' is the amount required by a taxpayer to provide regulated goods or services. Cost of service includes operating expenses. . . maintenance expenses, depreciation expenses, tax expenses, and interest expenses. . .

(ii) In determining whether, or to what extent, a credit has been used to reduce cost of service, reference shall be made to any accounting treatment that affects cost of service. Examples of such treatment include reducing by all or a portion of the credit the amount of Federal income tax expense taken into account for ratemaking purposes and reducing the depreciable bases of property by all or a portion of the credit for ratemaking purposes.

(3) Rate base. (i) For purposes of this section, "rate base" is the monetary amount that is multiplied by a rate of return to determine the permitted return on investment.

(ii) In determining whether, or to what extent, a credit has been used to reduce rate base, reference shall be made to any accounting treatment that affects rate base. In addition, in those cases in which the rate of return is based on the taxpayers's cost of capital, reference shall be made to any accounting treatment that affects the permitted return on investment by treating the credit in any way other than as though it were capital supplied by common shareholders to which a 'cost of capital' rate is assigned that is not less than the taxpayer's overall cost of capital rate (determined without regard to the credit). What is the overall cost of capital rate depends upon the practice of the regulatory body. Thus, for example, an overall cost of capital rate may be a rate determined on the basis of an average, or weighted average, of the costs of capital provided by common shareholders, preferred shareholders, and creditors.

Treas. Reg. 1.46-6(b)(2)(i), (ii) and (3)(i), (ii) (1979).

Essentially, Section 46(f)(2) and the regulation provide that a utility remains eligible for the credit as long as cost of service is reduced by no more than 'a ratable portion of the credit,' and as long as no reduction is made in the rate base. The purpose of this scheme, as revealed by legislative history, is to permit the benefits of the credit to be shared by the consumers and the investors of the utility. H.R. Rep. No. 533, 92d Cong., 1st Sess., reprinted in U.S. Code Cong. & Ad. News 1825, 1839 (1971).

Pursuant to paragraph (A) of Section 46(f)(2), CT&T 'flows through' directly to its customers an annual percentage of JDITC based upon the useful life of the property producing the credit and thereby reduces its tax expense, and thus its cost of service, by a ratable portion of the credit. This treatment of JDITC by CT&T is not at issue in the present case.

Pursuant to paragraph (B) of Section 46(f)(2), CT&T makes no reduction in its rate base on account of the credit and assigns the overall cost of capital rate to the capital generated by the credit.

The Public Staff advocates an additional adjustment due to the presence of JDITC. Assuming that, in the absence of JDITC, the capital otherwise supplied by JDITC would be contributed by all capital suppliers, including debt, in the same ratios as those suppliers exist in CT&T's capital structure, the Public Staff maintains that a hypothetical interest expense attributable to that portion of JDITC which would have been provided by

debt, in the absence of JDITC, should be deducted from CT&T's income tax expense for ratemaking purposes, in addition to the ratable reduction in taxes already produced by amortization of the credit. The Public Staff asserts that this adjustment to income tax expense for ratemaking purposes is in accord with Section 46(f)(2) based upon the language in Treas. Reg. Section 1.46-6(b)(3)(ii) that JDITC be `assigned a "cost of capital" rate that is not less than the taxpayer's overall cost of capital rate (determined without regard to the credit)'. The Public Staff also maintains that its position has been upheld in three federal court decisions and is therefore the correct one. Finally, the Public Staff contends that the ratepayers are entitled to an additional benefit from the proposed imputed interest on JDITC because they are the source of the cost free capital provided by JDITC. We reject each of these arguments.

The Public Staff's interpretation of the pertinent regulation completely ignores the words which precede the phrase relied upon by the Public Staff. The regulation clearly states that, to determine whether an improper reduction in rate base has occurred, reference should be made to any accounting treatment which treats JDITC `in any way other than as though it were capital supplied by common shareholders. . .' The phrase relied upon by the Public Staff refers to the determination of the `overall cost of capital rate' which must be applied to JDITC under the regulation. As such, the phrase deals with the rate of return which the utility is entitled to receive on JDITC, but does not require that a utility's interest expense be calculated without regard to the credit (i.e., as though capital generated by JDITC were supplied by other sources of capital reflected in the utility's capital structure). Rather, the preceding phrase strongly indicates that in other instances, JDITC is to be treated as `capital supplied by common shareholders.' The imputation of interest to a portion of JDITC as though supplied by creditors does not treat that portion of JDITC as though supplied by common shareholders and, in addition, reduces the cost of service by more than a `ratable portion' of JDITC. For these reasons, the adjustment proposed by the Public Staff contravenes Section 46(f)(2) and the regulation thereunder.

The cases cited by the Public Staff do not persuade us to interpret Section 46(f)(2) otherwise because each of the cases completely ignores the clear requirement in the regulation to that Section that JDITC be treated as `capital supplied by common shareholders.'

In the case of Public Service Company of New Mexico v. Federal Energy Regulatory Commission, 653 F. 2d 681 (D.C. Cir. 1981), the main issue before the court was whether capital provided by JDITC should receive the overall or common equity rate of return. The court concluded that, for purposes of determining the overall rate of return, JDITC could be treated as capital supplied by all capital suppliers in the same proportion as those suppliers existed in the capital structure of the utility, absent the credit. The court further held that excluding JDITC from the capital structure of the utility did not alter the debt/equity ratio such that the utility's interest expense deduction was increased, resulting in an additional, impermissible reduction in cost of service. No issue of imputing interest to JDITC was before the court.

That issue was before the court in New England Power Company v. Federal Energy Regulatory Commission, 668 F. 2d 1327 (D.C. Cir. 1981), <u>cert.</u>

denied, U. S. , 102 S. Ct. 2928 (1982). However, in determining that the Federal Energy Regulatory Commission could require the utility to impute hypothetical interest to JDITC, the court relied on its earlier decision in Public Service Company of New Mexico, supra. Upon stating that, `(t)he question in this section is whether FERC may properly treat tax credit funds in relation to interest deduction in the same way it treats tax credit funds in relation to rate of return determination,' the court quoted that portion of its earlier opinion in which it had approved the Federal Energy Regulatory Commission's treatment of JDITC as capital supplied by all capital suppliers in a proportionate manner for purposes of determining the overall rate of return on capital. As we have previously stated, the questions of how to treat JDITC for purposes of determining interest expense for ratemaking purposes are separate issues. The court in New England Power Company did not treat them as such and failed to analyze in any way the tax laws or the arguments supporting the impermissible nature of the adjustment.

In Union Electric Company v. Federal Energy Regulatory Commission, 668 F. 2d 389 (8th Cir. 1981), the third case cited by the Public Staff, the court again relied upon that portion of the regulation under Section 46(f)(2) which permits a ratemaking agency to assign the "overall cost of capital rate (determined without regard to credit)" to JDITC and ignored the remainder of the regulation. Reasoning that because the regulation allows JDITC to be `treated like other capital' in one instance, the court concluded that the regulation should be interpreted to allow such treatment on the interest deduction issue as well. In our opinion, such reasoning contravenes the clear requirement of Section 46(f)(2)(A) that only a `ratable portion' of JDITC be flowed through to customers and of Treas. Reg. Section 1.46-6(b)(3)(ii) that JDITC be treated as `capital supplied by common shareholders,' and we decline to follow it.

The final argument advanced by the Public Staff in support of imputing hypothetical interest to JDITC is that ratepayers are entitled to the additional benefit that would enure to them as a result of imputing interest to a portion of JDITC because they supplied the capital produced by JDITC by paying rates computed without regard to the tax credit (other than the ratable portion flowed through to them). We disagree. Without regard to the credit, a utility owes a certain amount of taxes at the end of its tax year upon which its rates are based. The credit essentially forgives or returns to the utility a portion of the taxes owed by it if certain capital assets have been purchased during the tax year. As such, the capital generated by JDITC comes from the Treasury of the United States, not the ratepayers of the qualifying utility.

Based upon the express language of Section 46(f)(2) and the regulation thereunder, as well as a consideration of the history and purpose of JDITC, that being primarily to benefit the utility so as to stimulate investment and thereby increase employment and additionally to share a ratable portion of the credit with ratepayers, we affirm the decision of the Commission to exclude all imputed interest expense related to JDITC in determining CT&T's income tax expense for ratemaking purposes."

Based upon the foregoing, including the reasoning set forth in past Commission decisions, the Commission finds and concludes that no interest expense should be imputed to funds arising from utilization of JDITC.

Since the Commission has not adopted all of the components of taxable income proposed by either party, the Commission has made its own calculation of state and federal income taxes, the appropriate amounts for use in this proceeding are $10,798 and $16,802 respectively.

Based upon the foregoing findings, the Commission concludes that the appropriate level of intrastate operating revenue deductions for use in this proceeding is $2,655,554 calculated as follows:

Item	Amount
Operating expenses	$1,360,092
Depreciation and amortization	931,965
Operating taxes - other than income	335,011
Other interest expense	886
State income taxes	10,798
Federal income taxes	16,802
Total operating revenue deductions	$2,655,554

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 9

Three witnesses testified as to the appropriate amount of the total investment of the Company and the common equity component which should be recognized for rate-making purposes in this proceeding. The Company presented witnesses Beacham and Currin and the Public Staff presented witness Sessoms.

Public Staff witness Sessoms testified that the Company's total capitalization consisted of $11,956,083 and common equity comprised $3,829,363, or 32.03% of total capitalization to support utility operations as of September 30, 1982. Witness Currin testified that total capitalization of Citizens consisted of $12,906,583 and common equity comprised $4,779,863 or 37.03% of total capitalization as of the same date. The difference of $950,500 is the investment in the Sylvan Valley CATV system, a wholly-owned subsidiary of Citizens Telephone Company.

Witness Sessoms testified that the source of all debt to Citizens is the Rural Telephone Bank (RTB). Since RTB does not allow loan funds to be invested in nonutility assets, witness Sessoms concluded that the source of the $950,500 investment in the CATV system was totally supported by equity funds. Therefore, witness Sessoms recommended that the $950,500 invested in nonutility investment (CATV) be removed from common equity and the total investment of the Company for rate-making purposes.

Company witness Beacham testified that the investment in the Sylvan Valley CATV system by Citizens did not violate the loan agreement of Rural Electrification Administration (REA) and Citizens because REA allows up to 8% of total telephone plant to be in general funds which may then be applied to non-telephone plant investments. However, witness Beacham did testify that "REA does not loan funds to support the cable T.V." Further, witness Currin testified that the Company was "... not in a position to substantiate conclusively the claim we have made that REA has in fact advanced loan funds for use with the cable TV subsidiary..."

In light of all the evidence presented, the Commission finds that all investment in the wholly-owned CATV subsidiary by the Company was from common equity funds, since no REA loan funds may be invested in the CATV system and

REA is the sole source of the Company's debt. Typically, when and if a utility invests in a non-regulated subsidiary, the source of these funds is assumed to be from the parent utility's equity and debt and the proportions of which are, ideally, similar to the debt and equity ratios used to finance utility operations. However, such is not the case for the relationship between Citizens and the CATV subsidiary due to REA loan policy as previously mentioned. Therefore the Commission further finds that this investment should not be recognized in the total capitalization or common equity component of capitalization. To do so would unfairly burden the ratepayers by causing them to support a higher equity ratio than actually exists to support utility operations. The proper amount of total capitalization to be recognized is $11,956,083 and the proper amount of common equity is $3,829,363 or 32.03% for use in this proceeding.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 10 AND 11

Two witnesses testified as to the proper capital structure and cost of capital, witness Currin for the Company and witness Sessoms for the Public Staff. The witnesses' differences on capital structure are due totally to the question of the investment in Sylvan Valley CATV. The Commission has addressed this issue in Finding of Fact No. 9 and consequently concludes that the capital structure (excluding the CATV investment) as of September 30, 1982, shown below is appropriate for setting rates in this proceeding.

Item	Percent
Long-term debt	67.97%
Common equity	32.03%
Total	100.00%

Witness Currin testified that the embedded cost of debt was 5.37% as of September 30, 1982, 5.57% as of December 31, 1982, and believed it would be 6.21% at the end of 1983. Witness Currin concluded that 6.21% was the appropriate embedded cost of long-term debt for use in this proceeding. Witness Currin advocated the application of the 6.21% embedded cost rate because it would be representative of what the cost rate will be during the time the rates are in effect. Upon cross-examination, witness Currin admitted that the 6.21% cost rate was based upon the presumption that the Company will draw down on loans and payoff loans on a scheduled rate that could change.

Witness Sessoms testified that the embedded cost of long-term debt was 5.37% as of September 30, 1982, the latest date available for the known capital structure.

The Commission finds that the proper embedded cost of long-term debt is 5.57% (December 31, 1982). In so doing, the Commission cites North Carolina General Statute 62-133(c) which does allow actual changes through the close of the hearing but not anticipated changes. Therefore, the Commission does not recognize 6.21% as the proper embedded cost.

The remaining area of disagreement is the cost of common equity. Witness Currin based his recommendation of 18.0% on the results of three methods. First, he adjusted the authorized returns of larger telephone companies to reflect risk differentials. Second, he developed a risk premium and added this to the free market cost of debt to Citizens. Third, he compared the change in capital costs since the Company's last rate case and added this

change to the Company's previously allowed return on equity. The risk premiums were all derived from his judgment. Also of concern to witness Currin was the post-tax times interest earned ratio (TIER). Witness Currin testified that in his opinion a post-tax TIER of 2.5X was the minimum Citizens needed. Witness Currin's embedded cost rate of debt of 6.21% combined with a recommended return on common equity of 18.0% would produce an overall return of 9.99% on investment and a post-tax TIER of 2.37X.

Witness Sessoms based his recommendation of 15.0% as the cost of common equity on two methods. First, witness Sessoms employed the discounted cash flow (DCF) method on eight telephone companies, six of which were independent telephone companies. The cost of equity for the group using this method ranged from 13.4% to 16.5%. Second, witness Sessoms determined the overall expected return on the market, or the cost of equity in general. Witness Sessoms concluded the expected return on the market portfolio was 15.5%. Witness Sessoms then examined the risk level of the eight companies in the same general industry as Citizens and found that these firms are not as risky as the average stock; therefore, the cost of equity to these companies must be lower than the expected return on the market. Witness Sessoms then applied the capital asset pricing model (CAPM), a risk premium method, and estimated the cost of equity to the average telephone company as approximately 14.0%. Based upon the DCF results of 13.4% to 16.5% and the CAPM results of 14.0%., witness Sessoms concluded that the cost of equity to the average telephone company was 15.0%. Then witness Sessoms examined Citizens Telephone Company to determine whether Citizens is more or less risky than the average telephone company. Witness Sessoms determined that the Company's leverage was quite justified due to its association with REA. Furthermore, witness Sessoms stated that the Company's REA association and the benefits accruing to manager-owners did not qualify Citizens for any risk premium. The equity return recommendation of 15.0% was then subjected to a TIER calculation as a check on the reasonableness of the return. This resulted in a pre-tax TIER of 3.59X and a post-tax TIER of 2.32X. Witness Sessoms felt his return recommendation was quite adequate, even considering the Company's embedded cost of debt increases which witness Currin projected. Accordingly, he recommended rates be set to yield a 15.0% return on equity and an 8.45% rate of return on investment.

The Commission finds several points noteworthy in witness Currin's discussion of TIERS in general, and more specifically, in his recommended minimum post-tax TIER necessary for the Company. The Commission is usually presented with pre-tax interest coverage ratios as a measure of the ability to meet interest payments on a timely basis. Pre-tax coverge is the more relevant criteria of coverage since interest is paid before income taxes and pre-tax coverage is one criterion used by bond rating agencies. Witness Currin recommended a post-tax TIER of 2.37X as the minimum necessary for the Company. This translates to a pre-tax coverage ratio of 3.69X. However, it also must be pointed out that the 6.21% embedded cost of debt employed in witness Currin's TIER calculation is a projected cost of debt which in itself causes the present TIER to be higher than the 2.37X recommended by him. Furthermore, witness Currin testified that a post-tax TIER of 2.5-3.0 would be required for a Baa bond rating if one was at all obtainable to Citizens.

The determination of the appropriate fair rate of return for the Company is of great importance and must be made with great care because whatever return is allowed will have an immediate impact on the Company, its stockholders, and

its customers. In the final analysis, the determination of a fair rate of return must be made by this Commission, using its own impartial judgment and guided by the testimony of expert witnesses and other evidence of record. Whatever return is allowed must balance the interests of the ratepayers and investors and meet the test set forth in G.S. 62-133(b)(4):

"...to enable the public utility by sound management to produce a fair profit for its stockholders, considering changing economic conditions and other factors, as they then exist, to maintain its facilities and services in accordance with the reasonable requirements of its customers in the territory covered by its franchise, and to compete in the market for capital funds on terms which are fair to its existing investors."

The return allowed must not burden ratepayers any more than is necessary for the utility to continue to provide adequate service. The North Carolina Supreme Court has stated that the history of G.S. 62-133(b):

"...supports the inference that the Legislature intended for the Commission to fix rates as low as may be reasonably consistent with the requirements of the Due Process Clause of the Fourteenth Amendment to the Constitution of the United States..." State ex rel. Utilities Commission v. Duke Power Co., 285 N. C. 277, 206 S.E. 2d 269 (1974).

The nature of the evidence in a case such as this makes it extremely difficult to balance all of the opposing interests, since much, if not all, of the evidence is based on individual witnesses' perceptions and interpretations of trends and data from the capital markets. The Commission has considered all of the relevant evidence presented in this case, with the constant reminder that whatever return is allowed will have an immediate impact on the Company, its stockholders, and its customers. The Commission must use its own impartial judgment to ensure that all the parties involved are treated fairly and equitably.

Based upon the foregoing and the entire record in this docket, the Commission concludes that the fair rate of return that Citizens Telephone Company should have the opportunity to earn on its original cost rate base is 8.91%. Such fair rate of return will yield a fair return on common equity of approximately 16.00% and a TIER of 2.35 x (Post-tax) and 3.66 x (Pre-tax).

The Commission cannot guarantee that the Company will, in fact, achieve the level of returns herein found to be just and reasonable. Indeed, the Commission would not guarantee it if it could. Such a guarantee would remove the necessary incentives for the Company to undertake to achieve the utmost in operational and managerial efficiency. The Commission believes, and thus concludes, that the level of returns approved herein will afford the Company a reasonable opportunity to earn a reasonable return for its stockholders while providing adequate and economical service to the ratepayers. The Commission can do no more.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 12

The Commission has previously discussed its findings and conclusions regarding the fair rate of return which Citizens Telephone Company should be afforded an opportunity to earn.

The following schedules summarize the gross revenues and the rate of return which the Company should have a reasonable opportunity to achieve based upon the determinations made herein. These schedules, illustrating the Company's gross revenue requirements, incorporate the findings and conclusions heretofore and herein made by the Commission.

SCHEDULE I
CITIZENS TELEPHONE COMPANY
Intrastate Operations
STATEMENT OF OPERATING INCOME
Twelve Months Ended December 31, 1981

Item	Present Rates	Increase Approved	Approved Rates
Operating Revenues:			
Local service revenues	$1,836,108	$721,255	$2,557,363
Toll service revenues	1,133,868	-	1,133,868
Miscellaneous revenues	208,240	-	208,240
Uncollectible revenues	(5,642)	(2,093)	(7,73
Total operating revenues	3,172,574	719,162	3,891,736
Operating Revenue Deductions:			
Operating expenses	1,360,092	-	$1,360,092
Depreciation and amortization	931,965	-	931,965
Operating taxes - other than income	335,011	43,150	378,161
Other interest expense	886	-	886
State income taxes	10,798	40,561	51,359
Federal income taxes	16,802	292,307	309,109
Total operating revenue deductions	2,655,554	376,018	3,031,572
Imputed net operating income on post-test year plant additions	54,062	-	54,062
Net operating income for return	$ 571,082	$343,144	$ 914,226

SCHEDULE II
CITIZENS TELEPHONE COMPANY
Intrastate Operations
STATEMENT OF RATE BASE AND RATE OF RETURN
Twelve Months Ended December 31, 1981

Item	After Approved Rates
Investment in Telephone Plant	
Telephone plant in service	$15,530,874
Investment in RTB stock	254,809
Depreciation reserve	(4,511,251)
Accumulated deferred income taxes	(946,316)
Pre-1971 investment tax credit	(20,861)
Customer advances	(151,470)
Total investment in telephone plant	10,155,785
Allowance for Working Capital	
Cash	113,341
Materials and supplies	72,862
Average prepayments	9,382
Average tax accruals	(80,452)
Customer deposits	(11,078)
Total working capital allowance	104,055
Original Cost Rate Base	$10,259,840
Rate of return	
Present rates	5.57%
Approved rates	8.91%

SCHEDULE III
CITIZENS TELEPHONE COMPANY
Intrastate Operations
STATEMENT OF CAPITALIZATION AND RELATED COSTS
Twelve Months Ended December 31, 1981

Item	Ratio %	Original Cost Rate Base	Embedded Cost %	Net Operating Income
	Present Rates - Original Cost Rate Base			
Long-term debt	67.97	$ 6,973,613	5.57	$388,430
Common equity	32.03	3,286,227	5.56	182,652
Total	100.00	$10,259,840	-	$571,082
	Approved Rates - Original Cost Rate Base			
Long-term debt	67.97	$ 6,973,613	5.57	$388,430
Common equity	32.03	3,286,227	16.00	525,796
Total	100.00	$10,259,840	-	$914,226

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 13

The evidence presented concerning the appropriate rate design for Citizens is found in the testimonies of Company witness Pickelsimer and Public Staff witness Willis.

Company witness Pickelsimer proposed tariff changes necessary to produce the Company's proposed annual revenue requirements and to adapt certain Company offerings to a competitive environment. Witness Pickelsimer's rate proposals included proposed changes in rates affecting basic local exchange service, service connections, special assemblies, key telephone service, miscellaneous service arrangements, auxiliary equipment, connections with facilities and/or equipment of others, local private line service, and obsolete service offerings.

Public Staff witness Willis agreed with the Company's proposal to unbundle its local service rates and with all of its proposed telephone set charges. Witness Willis also agreed with all of the Company's proposed service connection charges with the exception of the proposed residential secondary service ordering charge of $9.75 which he recommended to be set identical to the Company's proposed business secondary service ordering charge of $8.90. With regard to the inside wiring work function and jack installation, witness Willis recommended that the Company be required to submit tariffs which allow its customers to install their own inside wiring. According to Willis, this provision would expand the customers' discretionary powers and allow them to avoid service ordering charges, premises visit charges, inside wiring charges, and jack charges. He stated that the Public Staff has consistently promoted this particular tariff arrangement and recommended that the Company file tariffs identical to those filed by Southern Bell Telephone Company.

It was witness Willis' recommendation that the minimum Maintenance and Service Charge be based on one-man hour of labor at $20.50 per hour rather than the Company's proposed minimum time of two man-hours at $20.50 per man hour.

The Company recommended to increase its semi-public exchange rate from the business one-party rate to two times the business one-party rate. Witness Willis recommended one and one-half times the business one-party rate which he stated should cover the cost differential between semi-public local service and the local business one-party service.

Witness Willis stated that the Company had proposed extension line and tie-line mileage charges of $1.05 per month per quarter mile or fraction thereof route measurement, but had proposed $1.30 per month per quarter mile or fraction thereof route measurement for its local private line charges. According to witness Willis, the Public Staff and companies other than Citizens have recognized the physical similarity of these services and have proposed identical rates for mileage charges applicable to each service. It was his recommendation that extension line, tie line and local private line mileage charges be set at $1.05 per month per quarter mile route measurement and that the minimum charge of $8.00 per circuit for local private lines be set at $10.00 per circuit.

Prior to cross-examination of Public Staff witness Willis, the Company's counsel stated that the testimony of witness Willis was acceptable to the Company and that the Company would comply with all of the Public Staff's rate proposals in theory. However, the annual revenue requirements recommended by the Company and the Public Staff differ thus the access line charges and those rates which are multiples of the access line charge differ under the Company and Public Staff's proposals.

Based upon the evidence presented by Company witness Pickelsimer and Public Staff witness Willis, the Commission makes the following conclusions:

Unbundling

The Commission concludes that the separation of telephone instrument charges from service charges is necessary in today's competitive environment and should be permitted.

Standard Telephone Set Charges

The Commission finds a monthly telephone set charge of $1.25 for rotary dial sets and a monthly rate of $1.90 for tone dial telephone sets to be just and reasonable.

Service Charges

The Commission concludes that the schedule of service and installation charges listed in Appendix A of this order are just and reasonable.

Customer Provided Inside Wiring

The Commission concludes that a tariff identical to the one approved for Southern Bell Telephone Company which permits subscribers to provide and own their own inside wiring and modular jacks is in the public interest and should be filed by the Company with the Commission.

Maintenance of Service Charges

The Commission concludes that one man-hour of labor of $20.50 per man hour is proper for the Company's minimum maintenance of service charge with additional repair time exceeding one man-hour being billed at the rate of $20.50 per man-hour.

Semipublic Telephone Service

The Commission concludes that a charge of 1.5 times the business one-party for semipublic telephone service is just and reasonable.

Extensions and Local Private Line Mileage Charges

The Commission concludes that a charge of $1.05 per month per quarter mile, route measurement for extension line, tie line, and local private lines, with a minimum charge of $10.00 per month for local private lines is just and reasonable.

Basic Access Line Charges and Business Multiples

The Commission finds the following basic monthly charges appropriate.

Residential	$10.20
Business	25.85
Semipublic pay stations	38.75
Key system trunks	38.75
PBX trunks	51.70

Distribution of Additional Revenue Requirements

Based upon the preceding conclusions on rate design and other findings in this Order, the Commission concludes that the additional revenue requirement of $721,255 should be distributed as shown below:

Category of Service	Annual Revenue Increase
Basic local exchange service	$530,402
Service charges	65,741
Miscellaneous recurring charges	125,112
Total	$725,255

The rates and charges found to be just and reasonable by the Commission are itemized in Appendix A attached hereto.

IT IS, THEREFORE, ORDERED as follows:

1. The Applicant, Citizens Telephone Company, be, and hereby is, allowed to increase its rates and charges so as to produce an annual level of revenue of $3,899,471 from its North Carolina subscribers based on the Company's level of test year operations. Such amount represents an increase of $721,255 above the level of revenue that would have resulted from rates currently in effect based upon the test year level of operations.

2. The Applicant is required to file modified tariff sheets incorporating the rates set forth in Appendix A.

3. The rates, charges, and regulations necessary to produce the additional annual gross revenues authorized herein shall become effective upon the day the tariff sheets are filed with the Commission.

4. The Applicant shall give public notice of the increase approved herein by first-class mail to each of its North Carolina customers during the next billing cycle following the filing of the tariff sheets described in Ordering Paragraph No. 2 above.

ISSUED BY ORDER OF THE COMMISSION.
This the 31st day of March 1983.

NORTH CAROLINA UTILITIES COMMISSION
Sharon Credle Miller, Deputy Clerk

(SEAL)

Appendix A
Docket No. P-12, Sub 80
BASIC LOCAL EXCHANGE SERVICE

RESIDENCE	Monthly Rate Per Unit
Access line charge	$10.20
Tone Dial - access charge	1.40
Set charge - rotary	1.25
Set charge - tone dial	1.90
Call fwd. sp. call (8) - call waiting	5.60
All features except 30 code	7.50
Tone dial - customer owned	1.40

TELEPHONE - RATES

BUSINESS	
Access line charge	25.85
Tone dial - access charge	1.85
Set charge - rotary	1.25
Set charge - tone dial	1.90
Call forwarding	3.00
Call waiting	5.00
3-Way calling	4.00
Semi-public paystation	38.75
Paystation inside booth	5.00
Paystation unit type booth	1.50
Paystation extension	4.30
Tone dial customer owned	1.85

BUSINESS TRUNKS	
Key system trunk	38.75
PBX trunks	51.70
PBX trunks - DID SL-1	20.50

SERVICE CHARGES

	Monthly Rate Per Unit
RESIDENCE	
Primary service order	$16.40
Secondary service order	8.90
Premise visit	7.80
Central office work	7.50
Inside wiring	6.00
Jack	4.60
Equipment work	4.35
BUSINESS	
Primary service order	25.10
Secondary service order	8.90
Premise visit	7.80
Central office work	8.20
Inside wiring	7.50
Jack	4.60
Equipment work	6.15
Rearrangement of drop	5.10
SL-1 install - move	25.65
Feature change	7.70
Feature change - Ea. additional	1.70
Install - move 6-10 button set	25.65
Feature change per station feature	1.70
Feature change - min. charge	8.55
PBX message waiting	6.85
Maintenance service charge - (minimum)	20.50 per man hour
Equipment work - key set	25.65

MISCELLANEOUS RECURRING CHARGES

	Monthly Rate Per Unit
Secretarial Ans. Unit - 20 line	$25.65
Amplifier	.60
*Answering device - memory	22.00
*Answering device - remote call	11.00
*Answering device - repeat	16.00
*Answering device - repeat & record	30.00
*Bell - chimes	1.25
*Bell - electric	2.10
*Bell - extension	.85
*Bell - gong	1.70
*Button	.45
*Buzzer	.45
Coupler - alarm	9.40
Coupler - automatic	13.60
Coupler - recorder	5.60
Cut off switch	.50
*Explosion proof bell	4.25
*Explosion proof set	8.55
*Explosion signal control (ringer)	4.70
Hands free - camp 3	9.00
Hands free - camp 3 adapter	2.25
Hands free speaker	11.00
*Headset applique	4.00
*Headset venture 1	5.55
Hold key	.70
Additional listings	.45
Non-listed number	1.00
Non-published number	1.00
Logic 1 dialer module	18.80
*Logic 1 tone dial	3.60
*Panel phone	1.25
Rotary line holding	3.50
Rotary line service	3.50
*Slenderette with light	2.40
*Slenderette w/o light	2.05
*Starlite	1.10
Toll Restrictor	11.10
*Transformer	1.75
Turn Key	1.40
*Weatherproof phone	2.60
Recorder connector equipment	3.40
Subscriber transfer	4.30
Speaker - PA	8.55
Electronic PBX rotary set charge	1.50
Electronic PBX tone dial set charge	2.15
Exclusive key	.50
PBX extensions	1.50
*Message waiting	17.00
*Message waiting signal	.85
DuPont - Tier A	3,377.61
Dupont - Tier B	2,306.90

MISCELLANEOUS RECURRING CHARGES

	Monthly Rate Per Unit
Olin - Tier A	3,202.91
Olin - Tier B	3,222.24
Set charge - tone dial (Dupont)	2.15
Set charge - tone dial (Olin)	2.15
Rotary stations - Olin or Dupont	1.50
Ring down circuit - Olin or DuPont	3.00
Ring down circuits	2.60
Pickup keys	$ .70
Tone dial intercom	12.80
Secretarial pickup of prin. line	1.35
Holding per line equipped	.95
Holding per station equipped	.70
Winking hold feature per line	.50
Manual operation & automatic restoral	.50
Automatic per line equipped	1.90
Combined line operation per system	1.70
Combined line & busy lamp operation	3.00
Flashing lamp operation	2.15
Key illumination	1.70
Dial station selector	6.85
Busy & flashing lamp control unit:	
Per line	1.70
Per station or dial intercom	.95
Selector arrangement:	
First 10 stations	18.80
Additional stations (ea.)	.85
Standard telephone only on second intercom	2.15
SL-1 desk	9.40
SL-10 button module	7.70
SL-1 20 button module	13.60
Mileage - outside extension	1.05
Mileage - private line per quarter	1.05
Mileage - private line - min.	10.00

*Obsolete offering

DOCKET NO. P-16, SUB 146

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Application of Concord Telephone Company for an Adjustment of Rates and Charges Applicable to Intrastate Telephone Service) ORDER GRANTING) PARTIAL RATE) INCREASE

HEARD IN: Commission Hearing Room 217, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina, and Courtroom No. 1, Cabarrus County Courthouse, Union Street, Concord, North Carolina

BEFORE: Commissioner Douglas P. Leary, Presiding; and Commissioners Sarah Lindsay Tate and A. Hartwell Campbell

APPEARANCES:

For the Applicant:

Robert C. Howison, Jr., and Edward S. Finley, Jr., Attorneys at Law, Hunton and Williams, P.O. Box 109, Raleigh, North Carolina 27602

John R. Boger, Jr., Attorney at Law, Williams, Boger, Davis and Tuttle, P.O. Box 810, Concord, North Carolina 28025

For the Intervenors:

Gisele L. Rankin and Thomas K. Austin, Staff Attorneys, Public Staff - North Carolina Utilities Commission, P.O. Box 991, Raleigh, North Carolina 27602
For: The Using and Consuming Public

BY THE COMMISSION: On November 19, 1982, Concord Telephone Company (Concord, Company, or Applicant) filed an application with the Commission for authority to adjust its rates and charges for telephone service in North Carolina. The proposed rates and charges were designed to produce total annual gross revenues of $19,699,006 or an increase of $2,674,613 when applied to a test period consisting of the 12 months ended March 31, 1982. The Company requested that such rates be allowed to become effective on December 19, 1982.

By Order issued on December 20, 1982, the Commission declared the application to be a general rate case pursuant to G.S. 62-137; suspended the proposed rates for a period of 270 days; set the matter for hearing; required Concord to give notice of hearing by publication and bill inserts; established the test period to be used in the proceeding; and required protest or interventions to be filed in accordance with the Commission Rules and Regulations.

The Commission conducted a hearing specifically for the purpose of receiving testimony from members of the using and consuming public with regard to Concord's proposed rate increase in Concord at 9:30 a.m., on April 6, 1983.

The hearings resumed in Raleigh on April 7, 1983. Both Concord Telephone Company and the Public Staff were present and represented by counsel.

Concord offered the direct testimony of the following witnesses: Phil A. Widenhouse, Executive Vice President, Treasurer, and Assistant Secretary; Dr. James H. Vander Weide, Professor of Finance and Associate Dean at the Fuqua School of Business of Duke University; Roy W. Long, Plant Accountant and Toll Separations Supervisor; and Jerry H. McClellan, General Plant Manager.

The Public Staff offered the testimony and exhibits of the following witnesses: Hugh L. Gerringer, Engineer - Communications Division; Thi Chen Hu, Engineer - Communications Division; William J. Willis, Jr., Engineer - Communications Division; Elizabeth C. Porter, Accountant - Accounting Division; and George T. Sessoms, Jr., Public Utility Financial Analyst - Economic Research Division.

Concord offered the rebuttal testimony and exhibits of Mr. Widenhouse and Dr. Vander Weide.

Based on the foregoing, the evidence adduced at the hearings, and the entire record in this matter, the Commission makes the following

FINDINGS OF FACT

1. Concord Telephone Company is a duly franchised public utility lawfully incorporated and licensed to do business in North Carolina, is providing telephone services in its North Carolina service area, and is lawfully before this Commission seeking an increase in its rates and charges for local exchange service.

2. By its application, Concord sought rates to produce total gross annual revenues of $19,699,006 based upon test year operations. The Company contends that gross revenues under present rates are $17,024,393, thereby necessitating an increase of $2,674,613 which the Company proposes to achieve through increases in rates for local service.

3. The test period established by the Commission and utilized by all parties in this proceeding is the 12 months ended March 31, 1982.

4. The overall quality of service provided by Concord to its customers is adequate.

5. Concord's reasonable original cost rate base used and useful in providing telephone service in North Carolina is $29,191,951. This rate base consists of telephone plant in service of $50,660,881 plus an allowance for working capital of $1,725,299, less the accumulated depreciation associated with the original cost of this plant of $18,868,597, accumulated deferred income taxes of $4,267,106, and pre-1971 unamortized investment tax credits of $58,526.

6. Concord's test year operating revenues, after appropriate adjustments, under present rates are $17,345,098.

7. Concord's test year total operating expenses, after accounting and pro forma adjustments, including taxes and interest on customer deposits, are $14,713,207, which includes the amount of $2,722,198 for actual investment currently consumed through reasonable actual depreciation.

8. The capital structure which is proper for use in this proceeding is as follows:

Long-term debt	35.12%
Preferred stock	6.29%
Common equity	58.59%
Total	100.00%

9. The proper embedded costs of Concord's long-term debt and preferred stock are 7.74% and 4.95%, respectively. The rate of return which should be applied to the original cost rate base is 12.11%. This return on Concord's rate base of 12.11% will allow the Company the opportunity to earn a return on its common equity of 15.50%, after recovery of the embedded costs of debt

and preferred stock. Such returns on rate base and on common equity will enable Concord, by sound management, to produce a fair return for its shareholders, to maintain its facilities and service in accordance with the reasonable requirements of its customers, and to compete in the market for capital funds on terms which are reasonable and fair both to the customers and to the existing investors.

10. The total annual revenue requirement for Concord is $19,259,767 which necessitates an increase of $1,896,936 in Concord's gross revenues. This revenue requirement will allow the Company the opportunity to earn the rate of return on its rate base that the Commission has found to be just and reasonable and is based upon the original cost of Concord's property used and useful in providing service to its customers and its reasonable test year operating revenues and expenses as previously set forth in these findings of fact.

11. The rates, charges, and regulations to be filed in accordance with the guidelines contained herein will be just and reasonable.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 1 - 3

The evidence supporting these findings of fact is found in the verified application, in prior Commission Orders in this docket, and in the record as a whole. These findings are essentially procedural and jurisdictional in nature and are uncontested and uncontroverted.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 4

The evidence for the finding that Concord's service is adequate is contained in the testimony and exhibits of Company witness McClellan and in the testimony and exhibits of Public Staff witness Hu.

Company witness McClellan testified that the Company utilized stringent acceptance testing of all new cable additions, subscriber loop installation, transmission facilities, and central office equipment additions, and that quality of service evaluation tests were conducted in all offices for local, EAS, and toll call completion rates and transmission quality to meet Commission objectives. Witness McClellan also testified that the companywide station trouble report index had been consistently below the Commission objective of six troubles per 100 stations and the results of answer time recorders showed that the Company was meeting the Commission objective for operator answer time for manual toll, operator identified DDD, and directory assistance calls.

During cross-examination, witness McClellan admitted that the Company was not collecting the subsequent and the repeat reports for some exchanges. Witness McClellan agreed that these reports were important quality-of-service indices and that the Company had been ordered to collect these indices by the Commission in a prior rate proceeding.

Public Staff witness Hu testified that his review of the quality of service provided by Concord consisted of field inspections and tests of switching and trunking facilities; measurements of the answer time of operators, directory assistance, repair, and business offices; and an analysis of statistics relating to the Company's service.

Based on the results of his investigation, witness Hu concluded that the overall quality of service provided by Concord was adequate. However, witness Hu pointed out that the Company was not collecting the subsequent reports and the repeat reports accurately. Witness Hu also stated that the definition of repeat reports used by the Company was different from that used by other major phone companies. In the interest of consistency among the telephone companies, it was his recommendation that the Company change its definition of the repeat reports to the definition used by the other companies; i.e., a report of another trouble within 30 days of a previous trouble report.

Based on the foregoing evidence, the Commission concludes that the overall quality of service offered by Concord is adequate. However, the Commission recognizes that the Company has not fully complied with the Commission Order in Docket No. P-16, Sub 124, regarding the collecting and accounting for the subsequent and repeat reports and concludes that the Company should endeavor to collect and account for the subsequent and the repeat reports in the appropriate manner in the future.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 5

Company witness Long and Public Staff witness Porter offered testimony regarding Concord's reasonable original cost rate base. The following chart summarizes the amounts which the Company and the Public Staff contend are the proper levels of original cost rate base to be used in this proceeding:

Item	Company	Public Staff	Difference
Telephone plant in service	$50,660,881	$50,660,881	-
Less: Accumulated depreciation	18,850,227	18,868,597	$(18,370)
Net telephone plant in service	31,810,654	31,792,284	(18,370)
Working capital			
Cash (1/12 operating expenses)	716,865	716,755	(110)
Materials and supplies	1,629,933	1,629,933	-
Average prepayments	115,009	115,009	-
Less: Average tax accruals	632,324	632,324	-
Customer deposits	104,074	104,074	-
Total working capital	1,725,409	1,725,299	(110)
Less: Accumulated deferred income taxes	4,267,106	4,267,106	-
Pre-1971 unamortized investment tax credit	58,526	58,526	-
Original cost rate base	$29,210,431	$29,191,951	$(18,480)

As shown above, the total net difference between the Company and the Public Staff is $18,480. The Company and the Public Staff agreed as to the appropriate levels of telephone plant in service, accumulated deferred income taxes, pre-1971 unamortized investment tax credit, and all components of working capital with the exception of cash (1/12 of operating expenses). As the parties are in agreement in this regard, the Commission finds these amounts to be reasonable for use in determining Concord's original cost rate base.

The first area of disagreement between the Company and the Public Staff shown above concerns the appropriate level of accumulated depreciation to be deducted from rate base. Public Staff witness Porter adjusted the depreciation reserve to correspond to the end-of-period depreciation expense

adjustment made by both the Company and the Public Staff. Witness Porter testified that had end-of-test period plant been in service the entire year, both the expense and the reserve would have been $18,370 greater. During cross-examination, Company witness Long was questioned concerning the recent North Carolina Supreme Court's decision on this issue, and in response he stated that he agreed with the dissenting justices on this issue rather than with the majority.

Based on all the evidence presented and the treatment found proper by the North Carolina Supreme Court in State ex rel. Utilities Commission v. Duke Power Company, 305 N.C.1, 287 S.E.2d 786 (1982) concerning this matter, the Commission finds it proper to adjust the depreciation reserve to correspond to the depreciation expense adjustment of $18,370.

The final item of difference deals with the proper level of cash working capital. Since this is a direct calculation based on the proper level of operating expenses and the Commission finds the appropriate level of operating expenses to be $8,601,058 hereinafter in Finding of Fact No. 7, the Commission concurs with the Public Staff's level of cash working capital of $716,755.

Based on the foregoing the Commission finds the reasonable and proper original cost rate base for Concord Telephone Company to be $29,191,951, which consists of the following:

Item	Amount
Telephone plant in service	$50,660,881
Less: Accumulated depreciation	18,868,597
Net telephone plant in service	31,792,284
Working capital	
Cash (1/12 operating expenses)	716,755
Materials and supplies	1,629,933
Average prepayments	115,009
Less: Average tax accruals	632,324
Customer deposits	104,074
Total working capital	1,725,299
Less: Accumulated deferred income taxes	4,267,106
Pre-1971 investment tax credit	58,526
Original cost rate base	$29,191,951

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 6

The evidence concerning test year operating revenues is found in the testimony and exhibits of Company witness Long and Public Staff witnesses Gerringer, Willis, and Porter. The following chart summarizes the amounts which the Company and the Public Staff contend are proper for use in this proceeding:

	Company	Public Staff	Difference
Local service revenue	$10,425,060	$10,431,138	$ 6,078
Toll service revenue	5,940,718	6,115,925	175,207
Miscellaneous revenue	855,147	855,147	-
Uncollectibles	(17,733)	(17,733)	-
Total Operating Revenues	$17,203,192	$17,384,477	$181,285

As shown in the preceding chart, the Company and the Public Staff are in agreement regarding the level of miscellaneous and uncollectible revenues. There being no controversy in this regard, the Commission without further discussion finds miscellaneous revenues of $855,147 and uncollectible revenues of $17,733 reasonable and proper.

The first item of difference shown in the chart above is a $6,078 adjustment to local service revenues proposed by the Company relating to revenues arising from the proposed increase to semi-public coin telephones. Company witness Long testified that the original testimony of the Company failed to recognize that semi-public coin telephone subscribers receive billing credits and that these billing credits will increase under the proposed rates from $48,892 to $54,970 or $6,078. The Company correspondingly proposed an adjustment to decrease local service revenues under present rates by $6,078. The Public Staff did not take exception to the proposed adjustment of the Company; however, the adjustment was treated by the Public Staff as a rate design change to the proposed rates. The Commission finds the Company's proposed adjustment appropriate in theory; however, in the Commission's opinion this adjustment does not impact the revenues of the Company under present rates but is properly treated as a rate design adjustment to the proposed rates which will be discussed further hereinafter in Evidence and Conclusions for Finding of Fact No. 10. Accordingly, the Commission finds local service revenues of $10,431,138 reasonable and proper.

The final area of disagreement involves toll service revenues. The Company proposed toll service revenues of $5,940,718 while the Public Staff proposed toll service revenues of $6,115,925. The primary differences between the proposals result from the use of alternative toll settlement ratios by the parties and the Public Staff's inclusion of the impact of the pro forma expense and rate base adjustments on toll revenues. In originally filed testimony the Company's proposed toll revenues, which did not include any uncollectible toll revenue contribution, was largely determined by the calculation method used to settle toll revenues with Southern Bell on an actual cost basis. The calculation was initially made using end-of-period levels of intrastate toll net investment settlement base and expenses and an intrastate toll settlement ratio of 11.0113%. This ratio was based on annualizing the final ratios for the months of March, April, and May of 1982, which were the most current final ratios available at the time the Company prepared its rate case and which reflected the full monthly impact of the intrastate toll rate changes that became effective mid-February of 1982.

The Company in its proposed Order recommended that toll service revenues be calculated using a revised toll settlement ratio of 11.69% which represents the average of 11 months of actual toll settlement ratios and one month estimated toll settlement ratio for the 12 months ended February 1983. The Company maintains that the use of the 11.69% toll settlement ratio appropriately reflects more current and complete information with proper recognition of seasonal fluctuations. The Company further points out that no adjustment has been made to the toll settlement ratio of 11.69% to reflect reductions in the settlement pool brought about by increased payments to the standard contract companies.

The Company's toll revenue estimate consisted of determining the toll expense reimbursement, including taxes, to be received through settlements on an end-of-period basis and adding the return amount to be received based upon

the product of the end-of-period toll settlement base and the average of the actually achieved toll settlement ratios for the 11 months for which actual results have become known since the current toll rates became effective and one month's estimated data. The Company maintains that its method properly recognizes the actual levels of expenses, taxes, investments, and returns. The Company excluded the toll revenue effects of circumstances and events which will take place beyond the end of the test period explaining that, if those were included, the actual levels of achieved toll settlement ratios employed would require adjustment.

In the original testimony presented by the Company, witness Long recommended that a further adjustment be made to the calculated end-of-period level of gross intrastate toll revenues reducing said amount by $55,477 which reflected the estimated loss in toll revenues arising from the Stanly County EAS matter in Docket No. P-55, Sub 776. Witness Long also reduced local service revenues to reflect an estimated loss of $19,094 in Extended Community Calling (ECC) revenues arising from the Stanly County EAS matter.

Company witness Widenhouse provided the basis for the Company's revenue adjustments related to the Stanly County EAS matter in his originally filed testimony. Witness Widenhouse explained that since the EAS rate increases for the Company's exchanges involved in the Stanly County EAS matter did not include the loss of toll and ECC revenues, the only method by which these revenue losses could be recovered would be by including them in this general rate case proceeding. In his summary of his direct testimony, witness Widenhouse indicated that the Stanly County EAS matter, which was on appeal with the North Carolina Court of Appeals at the time his testimony was filed, had been remanded to the Commission. Under cross-examination, he stated that to his knowledge no physical construction had occurred toward providing the EAS and assuming that the Commission amended and reissued its Order implementing the EAS, it would be at least fifteen (15) months before the service could actually be offered to the public. Company witness McClellan confirmed witness Widenhouse's testimony that the Company had done nothing toward providing EAS to the customers involved and revised witness Widenhouse's estimate of the time it would take to offer service to the public from fifteen (15) to eighteen (18) months. The toll service revenues of $5,940,718 recommended by the Company do not reflect any adjustment relating to the Stanly County EAS matter.

In his originally filed testimony and exhibits, Public Staff witness Gerringer showed a representative level of end-of-period toll revenues of $6,058,178, which did not include any uncollectible toll revenue contribution. Witness Gerringer indicated that $5,676,863 of the total amount was determined by a toll settlement calculation like that used by the Company with the only difference being that he used a toll settlement ratio of 9.61% instead of the 11.0113% used by the Company. To arrive at his total end-of-period level of $6,058,178, witness Gerringer added to his previous estimate $381,315 which was the estimated increase in toll revenues for the Company resulting from the latest toll rate changes allowed in Docket No. P-100, Sub 57, effective mid-February 1982. Witness Gerringer did not make the toll revenue adjustment, as the Company did, to reflect the estimated loss in toll revenues arising from the Stanly County EAS matter. Further, witness Gerringer recommended that the ECC revenue loss adjustment made by the Company to local service revenues be disallowed. Witness Gerringer pointed out that the final outcome of the Stanly County EAS matter was surrounded by

much uncertainty and that if it were decided that implementation of the EAS should begin immediately, it would be more than a year before the EAS could be put in service. According to witness Gerringer during the intervening time, the Company will not be experiencing any loss in its toll and ECC revenues.

Public Staff witness Porter increased the $6,058,178 amount determined by witness Gerringer by $57,747 for the toll revenue effects of her adjustments to the Company's rate base and operating expenses and for the toll revenue effects of the Company's late filed supplemental after period adjustments resulting in a final representative level of end-of-period gross intrastate toll revenues of $6,115,925.

The 9.61% settlement ratio used by witness Gerringer resulted from summing monthly achieved final settlement ratios for a 12-month period, October 1981 through September 1982, with six months falling on each side of the end of the test period (March 31, 1982) and properly adjusting the ratios for these months for two known changes: (a) a reduction to reflect the full annual impact of the revisions to the nationwide average toll schedules used by companies receiving toll settlements on a standard contract basis (to become retroactively effective October 1, 1982) and (b) a reduction to remove 7 1/2 months (mid-February through September 1982) effects of the toll rate changes that became effective mid-February 1982 resulting from the Commission's decision in Docket No. P-100, Sub 57. The latter adjustment, to remove the effects of the toll rate changes from the settlement ratio, was necessary since witness Gerringer added the annual effects of the toll rate changes as a separate specific dollar amount to the results of his calculated toll revenues.

Public Staff witness Gerringer gave the following basis for his method of developing a settlement ratio: The settlement ratio which is computed monthly by Southern Bell shows large monthly fluctuations. In addition, past estimates of the settlement ratio for both short and long periods of time have been missed in many cases by wide margins. In some cases, estimates have been too high and in other cases too low when compared to the actually achieved settlement ratios. For these reasons, he considered it reasonable to develop the end-of-period settlement ratio used in his end-of-period toll calculation based on the final monthly ratios actually achieved - not estimated - for a period of time encompassing the end of the test period. Actual toll settlements are made using the intrastate toll average net investment settlement base. Therefore, he considered it reasonable to develop a ratio based on a 12-month period with six months falling on each side of the end of the test period. A ratio developed on this basis is consistent with actual toll settlement arrangements in that the end-of-period settlement base used in the end-of-period calculation can be interpreted to represent the average or mid-point settlement base for the same 12-month period considered for developing the settlement ratio.

Public Staff witness Gerringer pointed out that the resulting 9.61% end-of-period settlement ratio did not include any impact of the toll rate changes effective mid-February 1982. If the full impact of these changes had been reflected, the resulting settlement ratio would have been 11.88%.

Having carefully considered the matter of the proper level of toll service revenues for Concord Telephone Company, the Commission concludes that there are essentially three issues in this regard that must be resolved. These

issues include the appropriate toll settlement ratio, the propriety of considering pro forma expense and settlement base adjustments in the toll revenue calculation, and finally, the proper treatment of the Stanly County EAS matter. As to the appropriate toll settlement ratio, the Commission has reviewed the toll settlement ratios proposed by the parties as well as the methodologies used by the Company and the Public Staff to arrive at such estimates. The Commission is cognizant of the fact that the toll settlement ratio for any one month or number of months is subject to wide fluctuations and that actual toll settlement ratios oftentimes differ significantly from the estimated toll settlement ratios. The Commission concludes that a toll settlement ratio of 11.41% is reasonable and appropriate for Concord. Said ratio reflects the average of the actual settlement ratio for the 12 months ended February 1983, and is fully reflective of the toll rate increase allowed in Docket No. P-100, Sub 57. Further said ratio roughly approximates the ratio proposed by the Company of 11.69% properly adjusted for the recently approved standard contract settlement schedule changes. The Commission is fully aware of the difficulties involved in estimating the appropriate toll settlement ratio and thus concludes that the 11.41% settlement ratio approved herein is reflective of the settlement ratio one can reasonably expect to occur in the future based on facts and circumstances known at this time.

With regard to the dispute regarding the propriety of considering the impact of pro forma adjustments to expenses and settlement base on toll services revenues, the Commission fully believes that such adjustments are proper. In the Commission's opinion if the pro forma expense and rate base adjustments are proper it is likewise appropriate to make the corollary adjustments to toll revenues since such factors will surely impact the toll revenues experienced by the Company on an ongoing basis in the future.

Finally, the Commission concludes that it is inappropriate to include any toll revenue loss or ECC revenue loss arising from the Stanly County EAS matter as part of this proceeding. The Company is not presently experiencing any revenue loss associated with this EAS and based on the testimony of the Company's witnesses, it would be a minimum of 15 to 18 months before the EAS could be put in service if it were decided today to go forward with establishing the service.

Therefore, the Commission concludes that the end-of-period level of gross intrastate toll revenues for Concord is $6,076,546. Such amount is determined using a 11.41% intrastate toll settlement ratio that properly reflects the increase resulting from the toll rate case proceeding in Docket No. P-100, Sub 57. Further, such amount has been properly adjusted for pro forma settlement base and expense adjustments found fair by the Commission. In summary, the Commission finds that net operating revenues of $17,345,098 are appropriate for use herein consisting of the following:

Item	Amount
Local service revenues	$10,431,138
Toll service revenues	6,076,546
Miscellaneous revenues	855,147
Uncollectibles	(17,733)
Net operating revenues	$17,345,098

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 7

The evidence concerning test year operating expenses is found in the testimony and exhibits of Company witness Long and Public Staff witness Porter. The following chart sets forth the amounts proposed by the Company and the Public Staff.

	Company	Public Staff	Difference
Maintenance	$ 4,215,978	$ 4,215,978	-
Depreciation	2,722,198	2,722,198	-
Traffic	1,548,230	1,548,230	-
Commercial	958,085	957,862	(223)
Revenue accounting	463,574	463,574	-
General office and other	485,078	485,078	-
Operating rents	65,158	65,158	-
Relief and pensions	825,014	825,014	-
Interest and customer deposits	8,481	8,481	-
Taxes other than income	1,847,284	1,858,161	10,877
Annualization adjustment	32,782	31,683	(1,099)
State income taxes	201,139	200,238	(901)
Federal income taxes	1,266,433	1,259,937	(6,496)
Total revenue deductions	$14,639,434	$14,641,592	2,158

As shown in the chart above, the Company and the Public Staff are in agreement regarding the following expense amounts; maintenance, depreciation, revenue accounting, traffic, general office and other, operating rents, relief and pensions, and interest on customer deposits. There being no dispute regarding these components of operating expense, the Commission finds the amounts listed above for each of the expense items previously referenced appropriate.

The first item of difference relates to commercial expense. The Company proposed an amount of $958,085 for Concord's commercial expense while the Public Staff proposed an amount of $957,862. The $223 difference related to an increase in expense payments to L. M. Berry which corresponds to an adjustment to increase miscellaneous revenues agreed upon by the Company and the Public Staff and previously found fair by the Commission. Although the Company and the Public Staff are in agreement as to the propriety of the adjustment, differing amounts were proposed for the adjustment. Based upon the evidence presented by the parties in this regard, the Commission finds an adjustment of $17,162 for increased commission payments to L.M. Berry reasonable and proper.

The next item of difference involves taxes other than income. The $10,877 difference between the parties' proposals relates solely to differing gross receipt tax proposals. The gross receipt tax difference results from alternative proposed net operating revenue amounts. The Commission in Evidence and Conclusions for Finding of Fact No. 6 found Concord's adjusted test period operating revenues to be $17,345,098 and correspondingly finds gross receipt taxes of $1,040,706 appropriate for use herein.

The next item of difference relates to the annualization adjustment. The Company and the Public Staff were in agreement as to the propriety of an annualization adjustment and as to the proper annualization factor of 1.12%; however, the parties disagreed as to the level of operating expenses to be

annualized. Consistent with previous findings and conclusions of the Commission in this regard, the Commission finds an annualization adjustment of $31,683 proper.

The final item of difference involves state and federal income taxes. There are several factors which provide an explanation of the difference in parties' proposals. A portion of the difference results from differing levels of operating revenues and expenses. The Commission has heretofore found the reasonable level of revenues and expenses for Concord and correspondingly finds that income tax expense should be based on operating revenues of $17,345,098 and operating revenue deduction before income taxes of $13,179,054.

The final issue to be resolved regarding income tax expense relates to the reasonable interest expense deduction. The level of interest expense is, of course, dependent upon the capital structure, embedded cost of debt, rate base, and the treatment of interest expense associated with the Job Development Investment Tax Credit (JDITC) found fair by the Commission for Concord. In Evidence and Conclusions for Findings of Fact Nos. 5, 8, and 9, the Commission has determined the appropriate treatment for each of the aforementioned items with the exception of the interest associated with allowing JDITC an overall rate of return. The remaining issue to be resolved then relates to the appropriate treatment of interest expense associated with allowing JDITC an overall rate of return. The Company holds the position that hypothetical interest expense associated with allowing JDITC an overall rate of return is not a permissible income tax deduction for purposes of calculating the Company's income tax expense. Alternatively as in numerous past rate proceedings before the Commission, the Public Staff has continued to maintain that the Revenue Act of 1971, which implemented the JDITC, permits the Commission to impute interest thereto for use in determining the test year level of federal income tax expense. Notwithstanding that, the Commission had consistently found, for reasons which need not be repeated here, that the Public Staff's position in this regard was and is incorrect in its entirety. The North Carolina Court of Appeals in Utilities Commission v. Carolina Telephone, N.C. App. (COA #8210UC706, filed March 1, 1983), affirmed the Commission findings in this regard, this matter having been appealed by the Public Staff. Therefore consistent with previous decisions made in this regard, the Commission finds the imputed interest associated with allowing JDITC an overall rate of return not to be a proper deduction for purposes of determining the income tax expense of the Company. Based on the foregoing discussion, the Commission finds Concord's reasonable state income tax to be $209,252 and federal income tax to be $1,324,901.

In summary, the Commission finds Concord's total operating revenue deductions to be $14,713,207, consisting of the following components:

Item	Amount
Maintenance	$4,215,978
Depreciation	2,722,198
Traffic	1,548,230
Commercial	957,862
Revenue accounting	463,574
General office and other	485,078
Operating rents	65,185
Relief and pension	825,014
Interest on customer deposits	8,481
Taxes other than income	1,855,798
Annualization adjustment	31,683
State income tax	209,252
Federal income tax	1,324,901
Total revenue deductions	$14,713,207

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 8 AND 9

Three witnesses testified as to the appropriate capital structure the embedded cost of debt and preferred stock and the proper return on common equity which should be recognized for rate-making purposes in this proceeding. The Company presented the testimony of Phil H. Widenhouse and Dr. J.H. Vander Weide, and the Public Staff presented the testimony of George T. Sessoms, Jr.

Company witness Vander Weide recommended use of the Company's actual capital structure as of March 31, 1982, the end of the test year consisting of 35.12% long-term debt, 6.29% preferred stock, and 58.59% common equity. Witness Vander Weide testified that the Company's proposed capital structure was properly reflective of the increased business risk facing Concord today as the result of regulatory changes and related events designed to increase competition in the telecommunications industry.

Public Staff witness Sessoms recommended that the appropriate capital structure for the Company for rate-making purposes should be set to reflect 38.83% long-term debt, 6.17% preferred stock, and 55% common equity. In his opinion, the actual equity ratio of the Company was too conservative and uneconomical for its ratepayers. Witness Sessoms based his opinion upon five considerations. First, the results of a financial analysis since the Company's last general rate case showed that the Company had been profitable enough to pay dividends, finance new investment internally, and raise the equity ratio. Second, the earned return on equity of the Company compared favorably with the earned return on equity of Value Line evaluated telephone companies, but the payout ratio was lower for Concord, during most of the years since its last rate case. Third, witness Sessoms found the Company's equity ratio to be above the mean equity ratio of 27 other telephone companies. Fourth, witness Sessoms looked at certain criteria judged to be necessary for a telephone company to receive a AAA bond-rating and found Concord's financial condition to be excellent. Fifth, witness Sessoms noted the Company has projected future increases in the equity ratio. Based upon these considerations witness Sessoms recommended 55% to be a reasonable equity ratio for Concord.

Both Company witnesses Widenhouse and Vander Weide testified in rebuttal to witness Sessoms' use of a hypothetical capital structure. Witness Widenhouse

testified on rebuttal that Public Staff witness Sessoms was in error in implying that the Company has increased its equity ratio as a result of any owner-manager relationship. Witness Widenhouse testified that he was responsible for the policy of increasing the equity ratio, and he listed the reasons for his recommendation. Witness Widenhouse testified that Concord has been able to place issues of stock at favorable prices with investors located in or near its service area who are familiar with Concord's operations. Witness Widenhouse also testified that in recent years Concord has required capital in increments so small that it would have been uneconomical to make costly bond financings. It was witness Widenhouse's testimony that Concord has attempted to better position itself for the momentous changes at work in the communications business and has also attempted to operate in a manner so as to avoid returning to the Commission for rate relief on a frequent basis. Witness Widenhouse testified further that Concord has been able to raise capital to meet customers' needs during a period when other utilities have been forced into the bond market where interest rates have reached historically high levels or into the equity market where stock prices were lower than book value.

In Company witness Widenhouse's opinion the Company's policy of increasing the equity ratio has placed Concord in an advantageous position to meet the future needs of its customers. Because of the Company's actions in this regard, witness Widenhouse stated that Concord is now in a position to plan for the expenditures of many millions of dollars required to update its central office systems to provide digital electronic technology.

Company witness Vander Weide also testified in rebuttal concerning this matter. Witness Vander Weide stated that the Public Staff's use of a hypothetical capital structure fails to recognize the increased business risks associated with telephone operating companies such as Concord. According to witness Vander Weide the regulated telephone industry is currently undergoing a period of far-reaching structural changes that will dramatically affect the way telecommunications services are delivered. Witness Vander Weide testified further that the divestiture of AT&T of its operating companies, the FCC's recent docket to implement access charges, the rapid pace of new technological achievements, the FCC's decision to detariff CPE equipment and other enhanced services, and the introduction of major competitive forces into the long distance side of the telephone business are indeed milestone events in the history of the industry. While these events are designed to increase competition in the telecommunications industry, to spur technological improvements, and to improve the allocation of resources, they have also caused increased uncertainties surrounding future telephone company earnings and dividends, and hence, have increased the business risk facing telephone operating companies. Witness Vander Weide testified that a higher equity ratio is needed by companies in the telephone industry in light of their increased business risk. He testified that Concord's common equity percentage of 58.6% is in line with the three telephone operating companies (Cincinnati Bell, Rochester Telephone, and Southern New England Telephone), followed by Value Line that are not holding companies.

Based upon the foregoing, the Commission determines that the Company's actual capital structure at March 31, 1982, consisting of the following is appropriate for use in this case.

Long-term debt	35.12%
Preferred stock	6.29
Common equity	58.59
Total	100.00%

The Commission recognizes that the telephone industry in general, and Concord Telephone Company in particular, stands upon the threshold of a revolutionary, competitive era in providing telecommunications services. The Commission deems it unwise to draw conclusions based solely upon historical equity ratios for other telephone companies during periods when the threat of competition and deregulation did not pose the business risks that presently exist. The Commission recognizes that Concord has utilized a reliable source of reasonably priced capital which has resulted in a decrease in its financial risk. The Commission concludes that Concord has been wise to utilize this source of reasonably priced capital in light of the trends that have occurred in the telecommunications industry and sees no reason to penalize Concord at this date for taking advantage of the financial opportunities available to it.

The Company and the Public Staff also disagreed on the proper embedded cost of long-term debt and preferred stock. Consistent with his recommendation on the actual capital structure, witness Vander Weide recommended the actual embedded cost of debt of 7.74% and the actual embedded cost of preferred stock of 4.95%. Public Staff witness Sessoms also recommended an embedded cost of preferred stock of 4.96% but adjusted his recommended embedded cost of long-term debt upward to 8.13% to reflect recent borrowings that would have been made had the Company employed less equity in the capital structure.

Consistent with the Commission's previous findings herein, the proper embedded cost of preferred stock is found to be 4.95% and appropriate embedded cost of debt is 7.74%.

Company witness Vander Weide and Public Staff witness Sessoms also differed in the recommended return on equity that the Company should have the opportunity to earn. Witness Vander Wiede used two methods to determine his recommended return of 16.93% - 18.25%. First, witness Vander Weide applied the discounted cash flow (DCF) model to a group of eight telephone companies traded on the New York Stock Exchange. The average cost of equity under this method for the group of 16.93% was used by witness Vander Wiede as one estimate of the cost of equity to Concord. Second, Witness Vander Weide applied a Spread Test Method in which he estimated that Concord could currently issue an A rated bond in the range of 13.0% - 13.5%. Witness Vander Weide then added a 50% risk premium which was derived from various previous studies of the historic returns on equity over bonds. On this basis witness Vander Weide estimated the cost of equity for Concord to be approximately 18.25%. Based upon the DCF and Spread Test Methods, witness Vander Weide recommended Concord's cost of common equity to be within the 16.93% - 18.25% range.

Public Staff witness Sessoms based his recommendation of 14.35% as the cost of common equity to Concord on two methods. First, witness Sessoms employed the DCF method on eight telephone companies evaluated by Value Line. The cost of equity for the group using this method ranged from 13.14% - 15.6%. Second, witness Sessoms determined the overall expected return on the market, or the cost of equity for the Standard and Poor's 500, which represented a market portfolio. Witness Sessoms concluded the expected return on the market

was 15.0%. Witness Sessoms then examined the risk level of the eight companies in the same general industry as Concord and found that by various risk measures these firms are not as risky as the average stock; therefore, the cost of equity to these companies must be lower than the expected return on the market. The Capital Asset Pricing Model (CAPM) confirmed witness Sessoms' opinion and resulted in an average cost of equity of 13.6% for the group of comparable risk companies. Based upon the DCF results of 13.14% - 15.6% and CAPM results of 13.6%, witness Sessoms recommended a cost of equity for Concord of 14.35%.

The determination of the appropriate fair rate of return for the Company is of great importance and must be made with great care because whatever return is allowed will have an immediate impact on the Company, its stockholders, and its customers. In the final analysis, the determination of a fair rate of return must be made by this Commission, using its own impartial judgment and guided by the testimony of expert witnesses and other evidence of record. Whatever return is allowed must balance the interests of the ratepayers and investors and meet the test set forth in G.S. 62-133(b)(4):

> "...to enable the public utility by sound management to produce a fair profit for its stockholders, considering changing economic conditions and other factors, as they then exist, to maintain its facilities and services in accordance with the reasonable requirements of its customers in the territory covered by its franchise, and to compete in the market for capital funds on terms which are reasonable and which are fair to its customers and to its existing investors."

The return allowed must not burden ratepayers any more than is necessary for the utility to continue to provide adequate service. The North Carolina Supreme Court has stated that the history of G.S. 62-133(b):

> "...supports the inference that the Legislature intended for the Commission to fix rates as low as may be reasonably consistent with the requirements of the Due Process Clause of the Fourteenth Amendment to the Constitution of the United States..." State ex rel. Utilities Commission v. Duke Power Co., 285 N.C. 277, 206 S.E. 2d 269 (1974).

The nature of the evidence in a case such as this makes it extremely difficult to balance all of the opposing interests, since much, if not all, of the evidence is based on individual witnesses' perceptions and interpretations of trends and data from the capital markets. The Commission has considered all of the relevant evidence presented in this case, with the constant reminder that whatever return is allowed will have an immediate impact on the Company, its stockholders, and its customers. The Commission must use its impartial judgment to ensure that all the parties involved are treated fairly and equitably.

Based upon the foregoing and the entire record in this docket, the Commission concludes that the fair rate of return that Concord Telephone Company should have the opportunity to earn on its original cost rate base is 12.11%. Such fair rate of return will yield a fair return on common equity of approximately 15.50%.

The Commission cannot guarantee that the Company will, in fact, achieve the level of returns herein found to be just and reasonable. Indeed, the

Commission would not guarantee it if it could. Such a guarantee would remove the necessary incentives for the Company to undertake to achieve the utmost in operational and managerial efficiency. The Commission believes, and thus concludes, that the level of returns approved herein will afford the Company a reasonable opportunity to earn a reasonable return for its stockholders while providing adequate and economical service to the ratepayers. The Commission can do no more.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 10

The Commission has previously discussed its findings and conclusions regarding the fair rate of return which the Concord Telephone Company should be afforded an opportunity to earn.

The following schedules summarize the gross revenues and the rates of return which the Company should have a reasonable opportunity to achieve based upon the determination made herein. Such schedules, illustrating the Company's gross revenue requirements, incorporate the findings and the conclusions heretofore and herein made by the Commission.

SCHEDULE I
CONCORD TELEPHONE COMPANY
North Carolina Intrastate Operations
STATEMENT OF OPERATING INCOME
For the Test Year Ended March 31, 1982

	Present Rates	Increase Required	Approved Increase
Operating Revenues:			
Local service	$10,431,138	$1,896,936	$12,328,074
Toll service	6,076,546	-	6,076,546
Miscellaneous	855,147	-	855,147
Uncollectibles	(17,733)	(3,225)	(20,958)
Total operating revenues	17,345,098	1,893,711	19,238,809
Operating Revenue Deductions:			
Maintenance	4,215,978	-	4,215,978
Depreciation	2,722,198	-	2,722,198
Traffic	1,548,230	-	1,548,230
Commercial	957,862	-	957,862
Revenue accounting	463,574	-	463,574
General office & other	485,078	-	485,078
Operating rents	65,158	-	65,158
Relief and pensions	825,014	-	825,014
Interest on customer deposits	8,481	-	8,481
Taxes other than income	1,855,798	113,623	1,969,421
Annualization adjustment	31,683	-	31,683
State and Federal income taxes	1,534,153	876,515	2,410,668
Total operating revenue deductions	14,713,207	990,138	15,703,345
Net operating income for return	$ 2,631,891	$ 903,573	$ 3,535,464

SCHEDULE II
CONCORD TELEPHONE COMPANY
North Carolina Intrastate Operations
STATEMENT OF RATE BASE AND RATE OF RETURN
For the Test Year Ended March 31, 1982

Item	Amount
Telephone plant in service	$50,660,881
Depreciation reserve	18,868,597
Net telephone plant	31,792,284
Working capital allowance:	
Cash (1/12 of Operating Expenses)	716,755
Materials and supplies	1,629,933
Average prepayments	115,009
Less: Average tax accruals	632,324
Customer deposits	104,074
Total working capital	1,725,299
Cost free capital:	
Accumulated deferred income tax	4,267,106
Pre-1971 unamortized ITC	58,526
Original Cost Rate Base	$29,191,951
Rates of return	
Present rates	9.02%
Approved rates	12.11%

SCHEDULE III
CONCORD TELEPHONE COMPANY
North Carolina Intrastate Operations
STATEMENT OF CAPITALIZATION AND RELATED COSTS
For the Test Year Ended March 31, 1982

	Ratio %	Original Cost Rate Base	Embedded Cost %	Net Operating Income
	Present Rates - Original Cost Rate Base			
Long-term debt	35.12%	$10,252,213	7.74%	$ 793,521
Preferred stock	6.29%	1,836,174	4.95%	90,891
Common equity	58.59%	17,103,564	10.22%	1,747,479
Total	100.00%	$29,191,951	-	$2,631,891
	Approved Rates - Original Cost Rate Base			
Long-term debt	35.12%	$10,252,213	7.74%	$ 793,521
Preferred stock	6.29%	1,836,174	4.95%	90,891
Common equity	58.59%	17,103,564	15.50%	2,651,052
Total	100.00%	$29,191,951	-	$3,535,464

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 11

The evidence for this finding is found in the testimonies of Company witness Widenhouse and Public Staff witness Willis.

Witness Widenhouse proposed the unbundling of the local service rates into an access line charge and a separate telephone set charge. According to witness Widenhouse, his proposed rates for business would remain approximately

2.6 times the residential access charge. The PBX trunk rate was proposed to stay two times the business one-party access line rate. He expressed his desire to increase the current key trunk multiple from 1.25 times the business one-party rate to 1.4 times the business one-party rate. Additionally, he proposed increases in terminal equipment, key systems, tier B rates, and mobile telephone service. His proposals included an increase in the minimum nonrecurring service connection charge from $15.00 to $22.00.

Witness Widenhouse proposed rates for a new verification and emergency intercept service. He stated that his proposed tariff followed those of this type already approved by the Commission. According to witness Widenhouse the purpose of his proposed charges was a means to hold down expenses rather than to raise revenues.

Witness Widenhouse filed revised data which shows a negative adjustment of $6,532 in the additional revenues which the Company would receive under the assumption that the Company is granted its requested access line rates. Under cross-examination, however, he recognized that his proposed adjustment would have to be revised downward in the event the Commission granted fewer additional revenue dollars than the Company requested.

Public Staff witness Willis presented specific recommendations on the Company's proposed rate structure. He expressed his recommendations on the Company's proposed rate levels for the standard rotary and touchtone telephone sets, nonrecurring service charges, operator verification and emergency interrupt service, extension, and local private line mileage charges. In addition to his recommendations for specific rates, he recommended that the Company be allowed to unbundle its basic local rates and be required to file a tariff which permits Concord's customers to install their own inside wiring.

Witness Willis recommended that the Company's proposal to establish a charge for an operator verification and emergency interrupt service be approved, but observed that the Company had not estimated its cost savings resulting from the tariff application. He performed a calculation, using Southern Bell's two-year old estimate of costs, which resulted in an adjustment of $7,904 representing the annual cost savings.

One other adjustment made by witness Willis related to the number of nonrecurring service connection charge units used by the Company. It was his belief and testimony that the Company's application of these units, which were obtained from a sample, should be adjusted to cause its calculated revenues to equal the normally expected level of revenue for the same time period. He determined that an upward adjustment of 7.54% in the Company's sampled units would cause the revenues developed from the sample to equate to the booked revenues.

During cross-examination, both witness Willis and witness Widenhouse agreed that adjustments proposed by each other were reasonable and should be considered.

Based upon the evidence presented by witness Widenhouse and witness Willis and the Commission's determination in Finding of Fact No. 10, the Commission concludes the following concerning rates and charges:

1. The unbundling of rates for station telephone sets should be accomplished by creating individual telephone set charges and access line charges and that the rates listed below for telephone instrument monthly charges are just and reasonable.

INSTRUMENT CHARGES

	Rotary	Touchcall
Standard	$ 1.20	$ 1.70
Slenderette	2.20	2.70
Styleline without light	2.20	2.70
Styleline with light	2.35	2.85
Starlite	1.70	2.20
Trendline without light	2.20	2.70
Trendline with light	2.35	2.85
Panel Phone	2.70	3.20
Ericofon	1.70	2.20
Speakerphone 881	7.95	8.45
Speakerphone 880	7.95	8.45

2. The schedule of nonrecurring service charges listed below are just and reasonable.

SERVICE CONNECTION CHARGES

I. Residential Rates	
A. Service Order	
1. Primary	$17.00
2. Secondary	8.50
B. Premises visit, each	8.00
C. Central office work, each	5.00
D. Inside wiring, each	9.00
E. Jack	4.00
F. Equipment work, each	2.50
G. Number change	14.00
H. Reconnect service	14.00
II. Business Rates	
A. Service Order	
1. Primary	21.00
2. Secondary	10.50
B. Premises visit, each	8.00
C. Central office work, each	6.00
D. Inside wiring, each	13.00
E. Jack	4.00
F. Equipment work, each	2.50
G. Number change, each	18.00
H. Reconnect charge	18.00

3. The adjustment in the proposed nonrecurring service charge revenue increase from $273,087 to $293,677 is just and reasonable.

4. A tariff identical to the one approved for Southern Bell Telephone Company, which permits subscribers to provide and own their inside wiring and modular jacks, is in the public interest and should be filed by the Company with the Commission.

5. The proposed relationship between the key trunk and business one-party line of 1.4:1 is just and reasonable.

6. The negative adjustment of $6,532 made by the Company to the proposed semi-public pay station revenue is just and reasonable, but should be set equal to the proportion which the change in the semi-public paystation guarantee found just and reasonable in this proceeding bears to the proposed increase in the guaranteed charge.

7. The Company's proposed rates for operator verification and emergency interrupt service are just and reasonable.

8. The expense adjustment of $7,904 to reflect anticipated savings afforded the Company as a result of reduced operator verification and emergency interrupt activities is a just and reasonable estimate.

9. The additional annual revenues increase found reasonable in Finding of Fact No. 10 of this Order should be distributed approximately in the manner shown below:

Category of Service	Present Annual Revenue
Basic local exchange	$1,337,987
Service charges	293,677
Special assembly item	11,735
Directory listings	6,509
Key and pushbutton telephone service	84,155
Private branch exchange service	(1,268)
Auxiliary equipment	115,171
Connection with facilities and/or equipment of others	438
Mobile telephone service	4,410
Local private line service channels and equipment	4,779
All other services	39,343
Total	$1,896,936

IT IS, THEREFORE, ORDERED as follows:

1. That the Applicant Concord Telephone Company be, and hereby is, authorized to increase its local service rates and charges so as to produce annual gross revenues of $19,259,767 from North Carolina subscribers based on test year operations. Such amount represents an amount of $1,896,936 above the revenue level that would have resulted from rates currently in effect based on the test year.

2. That the Applicant is hereby called upon to propose and file with the Chief Clerk of the Commission specific tariffs reflecting changes in rates, charges, and regulations designed in a manner so as to produce a level of revenue no greater than that approved herein, in accordance with the findings, conclusions, and decretal paragraphs set forth herein within ten (10) days

from the date of this Order. Such filing shall include the workpapers supporting such proposals. A format such as that reflected in Item 30 of N.C.U.C. Form P-1, is suggested. An original and five copies of each of the foregoing are required.

3. That the Public Staff may file written comments concerning the Company's tariffs, etc., within five (5) working days of the date such tariffs, etc., are filed with the Commission.

4. That the rates, charges, and regulations necessary to produce the annual gross revenues authorized herein shall become effective upon the issuance of a further order approving the tariffs filed pursuant to Ordering Paragraph No. 2 above.

5. That the Company shall adopt the definition of the repeat report used by the other major phone companies.

6. That the Company shall file a proposed Notice to Customers regarding this matter for Commission approval within ten (10) days from the date of this Order.

ISSUED BY ORDER OF THE COMMISSION.
This the 17th day of June 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sandra J. Webster, Chief Clerk

DOCKET NO. P-128, SUB 3

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of	
Application of Continental Telephone Company of North Carolina for an Adjustment of Its Rates and Charges Applicable to Intrastate Telephone Service	) ORDER GRANTING) PARTIAL INCREASE) IN RATES

HEARD IN: Auditorium, McDowell Senior High School, Highway 70 West, Marion, North Carolina, on Tuesday, September 27, 1983, at 2:00 p.m.

Superior Courtroom, Fifth Floor, Buncombe County Courthouse, Courthouse Plaza, Asheville, North Carolina, on Tuesday, September 27, 1983, at 7:30 p.m.

Community Service Room, Community Service Building, Scotts Creek Road, Sylva, North Carolina, on Wednesday, September 28, 1983, at 11:00 a.m.

Commission Hearing Room, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina, on Tuesday, October 4 and 5, 1983, at 9:30 a.m.

BEFORE: Commissioner A. Hartwell Campbell, Presiding; and Chairman Robert K. Koger and Commissioner Douglas P. Leary

APPEARANCES:

For the Applicant:

F. Kent Burns, Boyce, Mitchell, Burns & Smith, Attorneys at Law, Post Office Box 2479, Raleigh, North Carolina 27602

For the Public Staff:

James D. Little, Chief Counsel, and Gisele L. Rankin, Staff Attorney, Public Staff - North Carolina Utilities Commission, Post Office Box 991, Raleigh, North Carolina 27602

BY THE COMMISSION: On April 29, 1983, Continental Telephone Company of North Carolina (Continental, Company, or Applicant) filed an application with the North Carolina Utilities Commission seeking authority to adjust its rates and charges for intrastate telephone service. The requested increase in rates and charges was designed to produce approximately $5,958,502, of additional annual revenues from intrastate operations when applied to a test period consisting of the 12 months ended December 31, 1982. The Company proposed that the rates and charges become effective for service rendered on or after May 30, 1983.

By Order issued May 31, 1983, the Commission declared the matter to be a general rate case pursuant to G.S. 62-137, suspended the proposed rates and charges for 270 days from the proposed effective date, set hearings to begin on September 27, 1983, declared the test period to be the 12 months ended December 31, 1982, required the Company at its expense to give public notice of the proposed increase and hearings, and set the time for the Public Staff and other interested parties to file intervention and/or testimony.

By Order issued June 27, 1983, the Commission rescheduled the hearing location for the public in Marion, North Carolina.

The Commission conducted out-of-town hearings for the purpose of receiving testimony from the using and consuming public. The first such hearing was held in Marion, North Carolina, at 2:00 p.m., on September 27, 1983; the second in Asheville, North Carolina, at 7:30 p.m., on September 27, 1983; and the third in Sylva, North Carolina, at 11:00 a.m., on September 28, 1983.

The following public witnesses appeared and offered testimony in Marion: J. Earl Daniels, Jerry Mason, Bill Wiseman, D.H. Grayson, George Conrad, Haskell Davis, John English, Ronald Byrd, Marion Allison, Rod Birdsong, Bill Connor, Glénn Spaulding, Mike Duncan, Eloise Witte, Murrell Brooks, Alfred Shiver, and Ben Shelton.

The following public witnesses appeared and offered testimony in Asheville: C.C. Krystoset, Willie Hodge, Terri McGuire, Lisa Mazzeo, John McGuire, and Joe Tiernen.

The following public witnesses appeared and offered testimony in Sylva: C.D. Johnson, Rutledge Liles, Lewis Ledsinger, Fred Reiter, I.L. Glover, Richard L. Wall, and Arnestine Davis Parris.

The hearings resumed in Raleigh at 9:30 a.m., on October 4, 1983, for the purpose of receiving further testimony of public witnesses and the testimony and cross-examination of the Applicant and the Public Staff. Charles Wellard and William Cooper, President and Accounting Manager, respectively, of Computer Circuitry Group, appeared as public witnesses and offered testimony and exhibits concerning service at two subsidiaries located in Continental's service territory. Continental offered the testimony and exhibits of the following witnesses: John A. Feaster, President of Continental Telephone Company of North Carolina, who testified generally as to Company operations, service, and capital requirements; Donald K. Holbrook, Financial Analyst of Contel Service Corporation - Eastern Region, who testified as to the Company's accounting and financial information and revenue requirements; Paul R. Moul, Vice President, Associated Utility Services, Inc., who testified as to the appropriate capitalization and required rate of return; and James K. Nash, Senior Financial Analyst of Contel Service Corporation - Eastern Region, who testified as to the Company's rate design and tariffs.

The Public Staff offered the testimony and exhibits of the following witnesses: Leslie C. Sutton, Engineer with the Communications Division of the Public Staff, who testified as to the Company's intrastate toll revenue; Hugh Hu, Engineer with the Communications Division of the Public Staff, who testified concerning the adequacy and quality of the Company's service; Nancy B. Bright, Director of the Accounting Division of the Public Staff, who testified concerning the inclusion of construction work in progress in rate base; Julie S. Jacome, Staff Accountant with the Accounting Division of the Public Staff, who testified concerning the transactions between Continental and an affiliated company, Contel Supply and Service Corporation; Jesse Kent, Jr., Staff Accountant with the Accounting Division of the Public Staff, who testified concerning the appropriate levels of operating revenues, expenses, and rate base of the Company's intrastate operations; Dr. Robert Weiss, Director of the Economic Research Division of the Public Staff, who testified as to the appropriate capital structure, cost of equity, and rate of return for the Company; and Millard N. Carpenter, III, Engineer with the Communications Division of the Public Staff, who testified as to end-of-period local and miscellaneous revenues, the Company's proposed changes in rates and regulations, and the appropriate distribution of Continental's additional revenue requirement among the various classes of service.

Continental offered the rebuttal testimony and exhibits of John A. Feaster, Donald K. Holbrook, James K. Nash, and Clarence Prestwood, Assistant Vice President - Revenues of Contel Service Corporation.

Based on the foregoing, the testimony and exhibits admitted at the hearings, and the entire record in this docket, the Commission now makes the following

FINDINGS OF FACT

1. The Applicant, Continental Telephone Company of North Carolina, formerly Western Carolina and Westco Telephone Companies, is a duly organized North Carolina corporation and a wholly owned subsidiary of Continental Telephone Corporation. Continental is a public utility engaged in providing telephone service in western North Carolina and is subject to the jurisdiction of this Commission. Continental is properly before the Commission in this proceeding, pursuant to G.S. 62-133, for a determination of the justness and reasonableness of its proposed rates and charges.

2. By its application, the Company seeks rates to produce jurisdictional net operating revenues of $38,259,043 annually, based upon a test year ended December 31, 1982. The Company contends that net revenues under present rates are $32,316,033, thereby necessitating an increase in net local service revenue of $5,943,010.

3. The test period for purposes of this proceeding is the 12 months ended December 31, 1982.

4. The overall quality of the service provided by Continental is adequate; however, there are some problem areas which the Company should correct.

5. The reasonable level of toll revenues is $12,758,057, which has been adjusted appropriately to reflect the phasedown of existing CPE from the settlements process.

6. An adjustment for attrition is improper and should not be included in this proceeding.

7. The appropriate level of accumulated depreciation is $20,597,541.

8. No construction work in progress (CWIP) should be included in Continental's rate base in this proceeding. Inclusion of the CWIP proposed herein by the Company is neither necessary to the financial stability of Continental nor in the public interest.

9. Excess profits of $423,000 included in Continental's intrastate net investment in telephone plant in service should be excluded from the Company's rate base.

10. Continental's reasonable original cost rate base used and useful in providing telephone service within the State of North Carolina is $60,219,937. This rate base consists of telephone plant in service of $90,583,398 and an allowance for working capital of $891,517, reduced by accumulated depreciation of $20,597,541, accumulated deferred income taxes of $10,607,714, and pre-1971 investment tax credit of $49,723.

11. Continental's total end-of-period operating revenues for the test year, under present rates and after accounting and pro-forma adjustments, are $32,465,611 net of uncollectible revenues of $51,373.

12. The reasonable level of test year operating revenue deductions for Continental after end-of-period and pro forma adjustments is $26,778,356. This amount includes $7,460,959 for investment currently consumed through reasonable actual depreciation on an annual basis.

13. The capital structure appropriate for use in this proceeding is as follows:

Long-term debt	49.95
Preferred stock	2.01
Common equity	48.04
Total	100.00

14. The fair rate of return that Continental should have the opportunity to earn on its original cost rate base is 12.12%. The proper embedded costs of debt and preferred stock are 9.53% and 7.65%, respectively. The reasonable rate of return for Continental to be allowed to earn on its common equity is 15.00%. Such rate of return will allow the Company, by sound management, to maintain its facilities and service in accordance with the reasonable requirements of its customers and to compete in the market for capital on terms which are reasonable to the customers and to existing investors.

15. Based on the foregoing, Continental should increase its annual level of gross revenues under present rates by $3,385,983. This increase is required in order for Continental to have a reasonable opportunity to earn the 12.12% rate of return on its rate base which the Commission has found just and reasonable. This increased revenue requirement is based upon the original cost of the Company's property and its reasonable test period operating revenues and expenses as previously determined and set forth in these findings of fact.

16. Changes in rates, charges, and regulations in accordance with Appendix A and designed to produce an additional $3,385,983 in gross annual revenue should be made.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 1, 2, AND 3

The evidence for these findings of fact is contained in the verified application, in the Commission Order Setting Hearing, and in the testimony and exhibits of Company witnesses Feaster and Holbrook. These findings are essentially informational, procedural, and jurisdictional in nature and are uncontested.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 4

The evidence concerning the quality of service was presented by Company witness Feaster, Public Staff witness Hu, and approximately 30 public witnesses.

The major complaints of the public witnesses were about service and the requested rate increase. One customer, Charles Wellard, had previously filed a complaint with the Commission and testified with regard to ongoing service problems his companies had experienced over the years. Witness Wellard testified that the problems were so bad that he had moved his sales force to a facility outside Continental's service area, which resulted in there being 200 fewer jobs in an area of the state that could ill afford to lose them. His major complaint concerned the problems he had experienced in trying to use a computer between a facility in Taylorsville, North Carolina, and a facility in the Continental service area. As a result of these problems, two of his plants have been put up for sale.

Subsequent to the hearing, Continental filed a report agreeing that this customer had experienced some calling problems, but concluded from its

investigation that the problems were not beyond the normal network service levels on cut-offs or other experiences.

The Public Staff filed a letter, also subsequent to the hearing, recommending that because of the severity of the problems testified to by witness Wellard and because of the time and manpower constraints on the Public Staff's Communication Division, an independent engineering firm be hired by the Commission at Continental's expense to investigate witness Wellard's complaint and any other complaints the Commission wishes to include.

Based on the foregoing, the Commission reiterates its concern that a thorough investigation needs to be done with regard to the complaint of witness Wellard and a full and complete report be made available to the Commission. The Commission, therefore, concludes that an independent engineering firm should be retained at the Company's expense to investigate this problem, and any others which may be appropriate for investigation, and report the results of said investigation to the Commission. In this regard, the Commission hereby requests the Public Staff to assist the Company in the selection of an appropriate consulting engineer to conduct the investigation in question and to coordinate said investigation on behalf of the Commission. There was also testimony from public witnesses in the Marion area regarding outages of the new central office equipment. Various explanations were given by the Company including those caused by Acts of God. The Commission calls on the Public Staff to monitor the Marion situation and directs the Company to file a report in six months regarding its progress in eliminating central office outages in Marion.

Company witness Feaster testified that the Company had consistently met the standard of .1% held orders of total stations for primary service and 1% held orders of total stations for regrade applications, that the Company's average on trouble reports per 100 stations showed a reduction of over 10% from the 1981 data, that the Company's performance on trouble reports would be 14.7% better than that of 1981 if the index was based on access lines, and that the Company's performance in the area of troubles cleared within 24 hours in 1982 showed improvement over that in 1981 in each month of 1982 and met or exceeded the objective in all months except June and July. However, witness Feaster admitted, during cross-examination by the Public Staff, that the Company's performance on trouble reports cleared within 24 hours had declined in March, April, May, and June of 1983.

Public Staff witness Hu testified that the results of his investigation showed the Company had met the Commission's objectives on the intraoffice, interoffice, and direct distance dial completion tests; on EAS and DDD transmission and noise measurements; and on the answer time of operators, directory assistance, repair service and business office. Witness Hu also testified that the Company met most of the Commission's other service-related objectives. However, witness Hu stated that the exception to this was that the Franklin, Murphy, and Weaverville service centers failed to meet the Commission's object of trouble reports cleared within 24 hours, with six-month averages of 92.3%, 93.5%, and 94.5%, respectively. Witness Hu further stated that this problem should be addressed by the Company. Based on his evaluation of all the test results and service data, witness Hu concluded that the overall quality of service provided by the Company was adequate.

Based on the foregoing evidence, the Commission concludes that the overall quality of service provided by Continental is adequate. However, the Commission also recognizes the need to improve the performance of clearing troubles within 24 hours in the Franklin, Murphy, and Weaverville service centers, and therefore concludes that the Applicant should make every fair and reasonable effort to meet the service objectives in these service centers.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 5

Company witnesses Holbrook and Prestwood and Public Staff witnesses Kent and Sutton presented testimony and exhibits concerning the representative level of end-of-period intrastate toll revenues.

The Company in its proposed order submits that the appropriate end-of-period level of intrastate toll revenues to be considered in this proceeding is $12,608,480. In contrast, the Public Staff presented a level of $13,469,826. The difference of $861,346 is the result of three functions.

First, the parties disagree on the amount of intrastate toll settlement investment upon which to apply the agreed upon toll settlement ratio of 11.36%. The difference is caused by the Public Staff's utilization of specific allocation factors applicable to intrastate toll investment adjustments agreed to by the parties in the record, while the Company applied composite allocation factors to said adjustments. The Commission concludes that the Public Staff's method is more appropriate. Based on this, the Commission concludes that the Company's intrastate toll revenues, before ajustments related to expenses, fixed charges, and investment resulting from test year adjustments to these items made elsewhere herein to the Company's recommended level of said items, are $12,628,833.

Second, the $12,628,833 intrastate toll amount must be adjusted to reflect adjustments made elsewhere herein to intrastate local expenses, fixed charges, and investment. The intrastate toll portion of the Commission's adjustment to intrastate local original cost net investment, spoken to elsewhere herein, is $(235,800). The intrastate toll portion of the Commission's adjustment to intrastate local expenses, spoken to elsewhere herein, is $(183,264). Finally, the Commission's adjustment to fixed charges to be used in setting rates in this proceeding results in an increase in intrastate toll revenues of $48,288.

The final adjustment necessary to achieve the appropriate level of intrastate toll revenues to be used in setting rates in this proceeding concerns the proper reflection of the Company's toll rate increase resulting from Docket No. P-100, Sub 64. Although the Commission recognizes that in Docket No. P-100, Sub 64, it was determined that Continental would receive additional annual revenues of $910,727 as a result of the increase in intrastate toll rates granted in that proceeding, the Commission concludes that, based upon the evidence in this case and considering the uncertainties posed by deregulation and significant changes in the telecommunications industry, it is reasonable to find that the Company's level of intrastate toll revenues for purposes of this case should only be increased by $500,000 to reflect the effect of the toll rate increases recently granted in Docket No. P-100, Sub 64. Furthermore, Continental is hereby directed to establish a deferred account and to place in said deferred account any intrastate toll revenues in excess of $500,000 which the Company derives from the toll rate

increases granted in Docket No. P-100, Sub 64. As previously stated in the Commission Order entered in Docket No. P-100, Sub 64, on September 14, 1983, the appropriate rate-making treatment to be accorded to any toll revenues placed in such deferred account will be considered by the Commission in the context of a further hearing to be held within the next year. The Commission considers this procedure to be fair to both Continental and its ratepayers in view of the uncertainties which are today present in the telecommunications industry.

Based on the foregoing, the Commission concludes that the appropriate level of end-of-period intrastate toll revenues for use in setting fair and reasonable rates in this proceeding is $12,758,057.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 6

The evidence concerning an adjustment for attrition is contained in the testimony and exhibits of Company witness Holbrook and Public Staff witness Kent.

Witness Holbrook testified that the cost of new plant is far greater than the cost of existing plant and that an attrition adjustment will provide revenues more in line with plant added in the period in which the new rates will be in effect. Witness Kent testified that to allow an attrition adjustment would in effect allow earnings on a projected plant level estimated for a period past the date of the hearing in this proceeding. Witness Kent testified that the rate base presented in this proceeding includes all of the plant serving customers at the date of the hearing and that the return allowed by this Commission should be calculated on this rate base without any adjustment for attrition.

The Commission concludes that witness Kent's adjustment to eliminate the Company's attrition adjustment is reasonable and proper in this proceeding and consistent with the Commission's decision in previous rate proceedings.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 7

Evidence concerning the appropriate level of accumulated depreciation is found in the testimony and exhibits of Company witness Holbrook and Public Staff witness Kent.

Witness Holbrook testified that accumulated depreciation should not be adjusted to include the full adjustment for end-of-period depreciation expense. Witness Holbrook stated that if any adjustment was necessary, only the simple average should be used because of the fact that if the adjustment had been recorded on a monthly basis, only half of the depreciation would have been applicable on an average basis.

Witness Kent testified that the Commission does not set rates on average rate base but on the end-of-period rate base and that plant and accumulated depreciation must be included in the end-of-period. In addition, witness Kent cited State ex rel. Utilities Commission v. Duke Power Company, 305 N.C. 1, 287 S.E. 2d 786 (1982) which requires that any adjustment to depreciation expense must also be made to the reserve.

Based on all the evidence presented and the treatment mandated by the North Carolina Supreme Court in State ex rel. Utilities Commission v. Duke, supra, the Commission finds it proper to adjust accumulated depreciation by $1,961,635 to correspond to the end-of-period depreciation expense adjustment agreed to by the parties. The Commission notes that this Commission has consistently applied this adjustment in general rate case proceedings for years.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 8

The evidence for this finding of fact is found in the testimony and exhibits of Company witness Holbrook (including rebuttal testimony) and Public Staff witnesses Weiss and Bright.

In his direct testimony, Company witness Holbrook testified that inclusion of plant under construction (CWIP) is in agreement with the Commission Order of March 30, 1983, in the Carolina Telephone and Telegraph Company case. Witness Holbrook cited the Commission's recognition of the Uniform System of Accounts inclusion of short-term CWIP in rate base and preclusion of accruing allowance for funds during construction (AFUDC) on short-term CWIP. Witness Holbrook also cited the Commission's concern in the Carolina Telephone Order over record-keeping problems which would occur if the Company accrued AFUDC on short-term CWIP in lieu of including the CWIP in rate base.

Witness Holbrook also stated that, using updated separation factors, $482,345 of the intrastate CWIP at the end of the test year was in service by July 22, 1983, and $114,331 is estimated to be in service by late October 1983. Witness Holbrook did agree that $61,560 of long-term construction could justifiably be excluded from rate base. Witness Holbrook further stated that post-test year information indicates that the projects were primarily to provide better service to existing customers, not to provide for customer growth. Witness Holbrook finally stated that since the level of emloyees has not decreased, there is no indication that maintenance savings have occurred.

Public Staff witness Weiss testified that the financial stability of the Company is not affected significantly by the inclusion or exclusion of CWIP in rate base. Witness Weiss stated that CWIP was only about 1% of rate base, AFUDC is only 2% of net income, and pre-tax interest coverage without CWIP in rate base is more than adequate at about 3.7x. Witness Weiss also testified that there was no long lead time associated with construction expenditures for the Company. For these reasons, Witness Weiss concluded that allowance of CWIP in rate base is not necessary to the financial stability of the Company.

Public Staff witness Bright testified that no CWIP should be included in rate base, but rather that the Company should be allowed to accrue AFUDC on short-term CWIP. Witness Bright contended that Continental's CWIP does not meet the statutory requirements of being both necessary to the financial stability of the Company and in the public interest.

Witness Bright pointed out that the accrual of AFUDC on short-term CWIP was not a problem because the Commission can deviate and has in the past deviated from the Uniform System of Accounts for other utilities. On cross-examination and on questions from the bench, witness Bright testified that the accrual of AFUDC should be prospective and not retroactive.

The Commission must consider two issues in determing the proper treatment of short-term CWIP:

1. Should short-term CWIP be included in or excluded from rate base; and
2. If short-term CWIP is excluded from rate base, should AFUDC be allowed on capital which supported short-term CWIP during the test-year.

The Commission is restricted from including CWIP in rate base by G.S. 62-133(b)(1) unless it is determined that such inclusion is both necessary to the financial stability of the Company and in the public interest. In the Commission's opinion, the financial stability test can be met only if it is determined that the financial strength of the Company will be significantly damaged if CWIP is not included in rate base. Based on the entire evidence of record, the Commission concludes that the Company has not met the tests to include CWIP in rate base, and therefore the Commission concludes that no CWIP should be allowed in the Company's rate base in this proceeding.

The final issue to be resolved is the accrual of AFUDC on test-year CWIP. Public Staff witness Bright testified that the Company should be allowed to accrue AFUDC on CWIP since it is not included in rate base; however, on cross-examination witness Bright stated that no AFUDC on construction since the last rate case should be allowed because it would constitute retroactive ratemaking.

Based upon a careful consideration of the entire record in this proceeding, the Commission concludes that the Company should only be allowed to accrue AFUDC on short-term CWIP, if it deems such procedure necessary, on a prospective basis, thereby allowing Continental to recover its cost of capital associated with investment in short-term CWIP. In reaching this decision, the Commission concludes that limiting Continental to only prospective accrual of AFUDC on short-term CWIP is appropriate as a matter of just and reasonable regulatory policy and is fair to both the Company and its ratepayers. Thus, the Commission has not found it necessary to decide the issue of whether or not accrual of AFUDC on construction expenditures made during the test year would constitute retroactive ratemaking.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 9

Evidence concerning the exclusion of excess profits from rate base is contained in the testimony and exhibits of Public Staff witness Jacome.

In reaching a decision on this issue, the Commission must first answer two questions: (1) Is the investment in Continental's rate base for purchases from the affiliated companies reasonable, or stated another way, do excess profits exist in the rate base of Continental resulting from its purchases from its affiliated companies? (2) In the event that the cost is unreasonable or that excess profits do exist in the rate base of Continental, what adjustments are necessary to eliminate the unreasonable portion of the cost, or excess profits, from the rate base?

Witness Jacome testified that it was necessary to closely examine the transactions between Continental and its supply affiliate, (CSSC), because of the opportunity for less than arm's-length bargaining transactions.

Arm's-length bargaining is a condition existing in a competitive marketplace, where both the buyer and seller attempt to negotiate terms most favorable to its business. The close relationship existing between Continental and CSSC provides the opportunity and incentive for the affiliated companies to set transfer prices which will maximize the profits of the combined affiliated operations. Consequently, there is no guarantee that Continental is buying at the lowest reasonable cost.

Continental secured approximately 57% of its total purchases of equipment and supplies from its manufacturing and supply affiliates during the 16-year period of 1967 through 1982. As a result, the Commission finds it obligatory to closely examine the transfer prices paid. This is necessary because when a substantial portion of a utility's property is acquired by purchases from affiliated companies, it is the affiliated supplier's prices which, by and large, translate into Continental's rate base valuation. Therefore, without such determination, the situation exists where a utility's rate base may be inflated due to excessive and unreasonable transfer prices.

The fact that the prices paid by Continental for purchases from its affiliated company are not greater than those which it would have to pay if it made purchases in the open market has not been disputed herein in this proceeding. However, the validity of price comparison as proof of the reasonableness of transfer prices has been contested by Public Staff witness Jacome.

Witness Jacome testified that she performed a comparable earnings test by which she compared the rate of return on equity earned by CSSC to the return on equity earned by four wholesale distributors not affiliated with a major customer. The results of this comparable earnings test showed that similar companies operating in an open market earned returns substantially less than the 27% return on equity earned by CSSC. The ratio and percentage analysis indicate that this excessive earnings level was achieved due to inherent advantages arising when a supply company deals exclusively with affiliated companies comprising a captive and closed market. As compared to the independents, CSSC was able to make its sales with fewer operating expenses, smaller accounts receivable, and generally fewer assets. Therefore, while the Commission concedes to the Company's assertion that the transfer prices charged by CSSC are equal to or less than the prices charged by independent distributors, it is apparent to the Commission that CSSC does not incur the same level of operating costs. The Commission concludes that in a regulated environment a reasonable transfer price is one that is based on the supply affiliate's cost and fair and reasonable return on equity, and not solely on a price level charged by nonaffiliated wholesalers who deal in a competitive market.

The existence of a captive market is the primary reason that the supply affiliate of Continental is able to sell its products at prices comparable to companies competing in the open market and consistently achieve a return on equity materially greater than those achieved by the independent companies. Since the excessive profits of the supply company are the direct result of the affiliation with the telephone operating companies, the Commission finds that it is only fair that these profits be shared with those captive market telephone operating companies. The Commission concludes that the level of costs of purchases from CSSC by Continental included in the Company's rate base in this proceeding is not reasonable, and that therefore the Company's

rate base includes excess profits which should be removed in order to establish a fair and reasonable rate base level.

Witness Jacome testified that for the test year ending December 31, 1982, the earnings level from sales by CSSC to Continental should be limited to a 15% return on equity. This method of limiting CSSC's earnings would, in effect, recognize the economies inherent as a result of the existence of a captive market and has the effect of flowing these economies back to the operating telephone companies which make up that captive market.

The Commission concludes that the Applicant's net investment in utility plant in service should be adjusted to exclude "excess profits" surviving in the net plant accounts at December 31, 1982, in the amount of $423,000. This adjustment is based on the concept of limiting the earnings of the supplier affiliate to a reasonable rate of return on equity. The Commission concludes that, on transfers of equipment and supplies between the manufacturing and supply affiliates of Continental and the Applicant, a return of 15% is a reasonable rate of return on equity. Finally, the Commission notes that this adjustment is consistent with past Commission treatment of this item in numerous other telephone general rate cases.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 10

Company witness Holbrook and Public Staff witness Kent offered testimony regarding Continental's original cost rate base. The following chart summarizes the amounts which the Company and the Public Staff contend are the proper levels of original cost rate base to be used in this proceeding:

	Company	Public Staff
Telephone plant in service	$ 90,876,319	$ 90,583,398
Construction work in progress	643,667	-
Property held for future use	7,073	-
Depreciation reserve	(18,635,906)	(20,597,541)
Allowance for working capital taxes	919,903	891,543
Accumulated deferred income taxes	(10,607,714)	(10,607,714)
Pre-1971 unamortized ITC	(49,723)	(49,723)
Total original cost rate base	$ 63,153,619	$60,219,963

As shown above, the net difference between the Company and the Public Staff is $2,933,656. The Company and the Public Staff agree as to the amount of accumulated deferred income taxes and the unamortized investment tax credits prior to 1971. The Commission finds these amounts to be reasonable for use in determining original cost rate base.

The first area of disagreement is telephone plant in service. The difference here results from witness Kent's reduction of plant in service by $423,000 to account for the excess profits resulting from purchases from the affiliated supply company. This adjustment was accepted by the Commission under Evidence and Conclusions for Finding of Fact No. 9. This adjustment was partially offset by a Public Staff adjustment for a portion of the frozen customer premises equipment (CPE) in the amount of $130,079. The adjustment increasing plant for an amortized portion of frozen CPE was not contested by the Company. The Commission therefore concludes that the CPE adjustment is proper and that the appropriate level of end-of-period telephone plant in service is $90,583,398.

The next area of disagreement between the Company and the Public Staff concerns the appropriate level of CWIP to be included in rate base. As previously discussed in Evidence and Conclusions for Finding of Fact No. 8, no CWIP should be included in rate base.

The next difference concerns the treatment accorded property held for future use. Witness Kent testified that this property should not be included in rate base because it is not used and useful in providing service to the ratepayers. Witness Kent further testified that this treatment is consistent with previous treatment afforded this item by the Commission. The Commission therefore concludes that the property held for future use of $7,073 should not be included in rate base.

The difference between the Company and the Public Staff concerning the proper level of accumulated depreciation has been discussed in Evidence and Conclusions for Finding of Fact No. 7. The Commission has found it proper and reasonable to accept the Public Staff's adjustment to accumulated depreciation to correspond to the end-of-period depreciation expense adjustment.

The last difference concerns the allowance for working capital. This difference deals with the proper level of cash working capital. Since this is a direct calculation based on the proper level of operating expenses and the Commission found the appropriate level of operating expenses, excluding depreciation, to be $14,304,312 in Evidence and Conclusions for Finding of Fact No. 12, the Commission concludes that the appropriate level of cash working capital is $1,192,026. Therefore, the Commission concludes the proper allowance for working capital to be used in this proceeding is $891,517.

Based on the foregoing, the Commission concludes that the appropriate original cost rate base for use in setting rates in this proceeding is $60,219,937.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 11

The evidence concerning test year operating revenues is found in the testimony and exhibits of Company witness Holbrook and Public Staff witnesses Sutton, Carpenter, and Kent. The following chart summarizes the amounts which the Company and the Public Staff contend are proper for use in this proceeding.

	Company	Public Staff
Local service revenue	$18,780,910	$18,780,910
Toll service revenue	12,608,480	13,469,826
Miscellaneous revenue	978,017	978,017
Uncollectibles	(51,374)	(51,373)
Total operating revenues	$32,316,033	$33,177,380

The parties agree as to local service, miscellaneous, and uncollectible revenues. The Commission concludes without further discussion that the end-of-period levels of $18,780,910, $978,017, and ($51,373) for local service, miscellaneous, and uncollectible revenues, respectively, are proper for use in this proceeding.

Since the Commission previously has found the proper level of toll revenue to be $12,758,057 under Evidence and Conclusions for Finding of Fact No. 5,

the Commission concludes that the appropriate level of the Applicant's end-of-period net revenue is $32,465,611.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 12

The evidence concerning test year operating revenue deductions is found in the testimony and exhibits of Company witness Holbrook and Public Staff witness Kent. The following chart sets forth the amounts proposed by the Company and the Public Staff.

	Company	Public Staff
Maintenance	$ 7,635,099	$ 7,455,244
Depreciation and amortization	7,475,777	7,460,770
Traffic	1,076,238	1,045,102
Commercial	1,520,477	1,485,506
General office	2,091,148	2,039,034
Other operating expense	2,321,982	2,279,734
Taxes other than income	2,949,049	2,963,008
Attrition adjustment	265,556	-
State income taxes	287,770	338,523
Federal income taxes	1,612,010	1,977,769
Total operating revenue deductions	$27,235,106	$27,044,690

The differences between the Company's and the Public Staff's amounts for maintenance, traffic, commercial, general office, and other operating expenses result from witness Kent's adjustments concerning four items.

Witness Holbrook testified that certain wage adjustments taking effect beyond the end of the test period and after the close of the hearings in this matter should be allowed as a pro forma adjustment to expenses because the Company is bound by contract for some of the wage increases and will be giving the increases not bound by contract in the future. Witness Holbrook admitted on cross-examination that the Company would not be paying these increased wages until after the close of the hearing.

Witness Kent testified that adjustments to pro forma wages to the end of the test year and to the hearing date were included in his adjusted expenses. Witness Kent testified that to allow wage increases past the hearing date was not reasonable or proper and would, if allowed, cause the ratepayers to pay for an expense that is not acutal through the close of the hearing which is in contradiction to G.S. 62-133(c).

The Commission concludes that the Public Staff's position on this matter is appropriate.

Witness Holbrook included an erosion allowance in the expenses proposed by the Company and testified that such an allowance was necessary in order to guarantee that the Company will earn the rate of return authorized by the Commission in this proceeding.

In opposition, witness Kent testified that to annualize expenses to an end-of-year level is reasonable. However, the adjustment made by the Company went past the test period and past the hearing date. Witness Kent stated that it would not be proper or reasonable to allow an erosion adjustment which tends to increase expenses above and beyond the actual or pro forma

end-of-period level. Accordingly, witness Kent eliminated the protion of erosion allowance applicable to the period subsequent to the hearing date.

Based on the foregoing the Commission concludes that the erosion adjustment promulgated by the Company is inappropriate and should be disallowed.

The final two items of differences between the parties' respective levels of maintenance expense are related to the Public Staff's adjustments for excess profits, as spoken to under Evidence and Conclusions for Finding of Fact No. 9, and adjustment for CPE, as spoken to under Evidence and Conclusions for Finding of Fact No. 10. Consistent with the Commission's findings elsewhere herein, as noted, the Commission concludes that the Public Staff's adjustment to maintenance expense for these two items is appropriate.

The Public Staff adjusted depreciation expense to reflect the adjustment to CPE and excess profits, as spoken to under Evidence and Conclusions for Findings of Fact Nos. 9 and 10, respectively. Consistent with the Commission's conclusions concerning these items, the Commission concludes that the Public Staff's adjustment to depreciation expense for the two items is appropriate.

The Public Staff made adjustments to taxes other than income to reflect effects of the erosion and wage adjustments, as spoken to elsewhere herein, and to reflect a different level of operating revenues than that presented by the Company. Consistent with the decisions included herein above, the Commission concludes that the wage and erosion adjustments supported by the Public Staff, and accepted elsewhere herein, should be properly considered in determining the appropriate level of end-of-period taxes other than income in this proceeding. Further, the Commission concludes that since the level of revenue found to be appropriate under Evidence and Conclusions for Finding of Fact No. 11 is different from that of either party, then the proper level of gross receipts taxes to be included in taxes other than income, should be that based on the Commission's level of revenues.

The Commission has already addressed the issue of an attrition allowance, as proposed by the Company, under Evidence and Conclusions for Finding of Fact No. 6; therefore, the Commission concluded that no attrition allowance should be used to reduce the Applicant's net income for return in this proceeding.

The difference in the amount of taxes proposed by the Company and the Public Staff results solely from the different levels of revenues and expenses proposed by the parties.

Since the Commission adopted the revenue, expenses, and investment of neither party in its entirely, the Commission must determine the fair and reasonable level of income taxes based upon the level of expenses, revenue, and investment found to be appropriate elsewhere herein. Consequently, the Commission concludes that the appropriate level of income taxes to be included in setting rates in this proceeding is $2,080,456.

Based on all the foregoing, the Commission concludes that the proper level of end-of-period operating revenue deductions is $26,778,356, as stated below:

Item	Amount
Operating expenses	$14,304,312
Depreciation	7,460,959
Taxes other than income	2,932,629
State and federal income taxes	2,080,456
Total	$26,778,356

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 13 AND 14

On the subject of capital structure and rate of return, the Company presented the testimony of Paul R. Moul, Vice President of Associated Utility Service, a consulting firm. The Public Staff presented the testimony of Dr. Robert Weiss, Director of the Economic Research Division of the Public Staff. In addition, the Company offered rebuttal testimony from witness Moul in response to Dr. Weiss's estimate of the cost of equity capital.

There was no dispute between the parties concerning the appropriate capital structure and embedded cost rates for debt and preferred stock. Dr. Weiss recommended the use of the actual capital structure and embedded costs of Continental Telephone Company of North Carolina as of June 30, 1983. Witness Moul stated from the witness stand that he accepted the capital structure and embedded cost rates proposed by Dr. Weiss.

Based on the record in this case, the Commission concludes that the appropriate reasonable capital structure for use in setting rates for Continental is as follows:

Common equity	48.04%
Preferred equity	2.01%
Debt	49.95%
Total	100.00%

The Commission further concludes that the cost rate for preferred stock is 7.65% and for debt is 9.53%.

Mr. Moul testified that the Company should be permitted to earn an overall return of 13.01% and a return on common equity of 17.0%. As the Company's stock is not traded, he performed his analysis on Continental Telecom, Inc. (the holding company), the four largest telephone holding companies, and the three largest independent telephone companies. His conclusion was based on the discounted cash flow model (DCF), earnings/price ratios, earnings/net proceeds ratios, the capital asset pricing model, and a risk premium analysis. He stated that the earnings/price ratios and earnings/net proceeds ratios were "partial" cost rates.

Mr. Moul concluded from his analysis that the cost of equity to Continental Telecom is 16.1%, and he then added approximately one percentage point for issuing expenses to reach his final conclusion that the appropriate rate of return for Continental is 17.0%.

Dr. Weiss recommended an overall return of 12.0% and a return on common equity of 14.75%. He based his conclusion on his study of the expected return on a broadly diversified portfolio of equities, specifically the S&P 500, and then adjusted his result to reflect the lower risk of Continental.

To estimate the return on the S&P 500, Dr. Weiss used a discounted cash flow analysis and a risk premium analysis. He found the current yield on the S&P 500 to be about 4.6% and the long-term expected growth in dividends to be about 9%, for an expected return of about 13.6%. Using the risk premium methodology he found an expected market return of about 16%. He concluded that the expected return for the S&P 500 is in the range of 15% - 16%.

Dr. Weiss next compared the risk of Continental Telecom to the risk of the companies in the S&P 500 by examining risk measures published by Value Line, Standard and Poor's, and Moody's. He found Continental Telecom below average in risk by the standards of the Value Line Safety rank, S&P Stock Rating, and Beta, while it is average to above in risk in terms of Moody's Stock Grade. He noted that one would expect the risk of Continental Telecom's telephone operations to be lower than the risk of the other parts of the Company, such as Executone or Cado Systems, which are in extremely competitive fields marked by rapid technological change. Taking into account the current level of interest rates, specifically the yield of about 13 1/2% on single A utility bonds, Dr. Weiss concluded that an estimate of the cost of equity capital to Continental of 14.75% was reasonable.

As a check on his results, Dr. Weiss did a Discounted Cash Flow analysis for Continental Telecom and the other large independent telephone companies. He used current dividend yields from Value Line. For estimates of expected dividend growth rates he used a regression analysis of data from 1973 to 1983, and Value Line and Salomon Brothers forecasts. He stated that his DCF results were consistent with his cost of equity estimate of 14.75%.

In his rebuttal testimony for the Company, Mr. Moul stated his opinion that investors expect a return substantially higher than that estimated by Dr. Weiss. Specifically, he stated that there was strong evidence that investors presently expect a total market return of 18% - 22%. He based his opinion on a DCF analysis, a risk premium analysis, and a consideration of expected real growth in the economy plus expected inflation plus the current yield.

The determination of the appropriate fair rate of return for the Company is of great importance and must be made with great care because whatever return is allowed will have an immediate impact on the Company, its stockholders, and its customers. In the final analysis, the determination of a fair rate of return must be made by this Commission, using its own impartial judgment and guided by the testimony of expert witnesses and other evidence of record. Whatever return is allowed must balance the interest of the ratepayers and investors and meet the test set forth in G.S. 62-133(b)(4):

> "Fix such rate of return ... as will enable the public utility by sound management to produce a fair return for its shareholders, considering changing economic conditions and other factors, as they then exist, to maintain its facilities and services in accordance with the reasonable requirements of its customers in the territory covered by its franchise, and to compete in the market for capital funds on terms which are reasonable and which are fair to its customers and to its existing investors."

The return allowed must not burden ratepayers any more than is necessary for the utility to continue to provide adequate service. The North Carolina Supreme Court has stated that the history of G.S. 62-133(b)

> "...supports the inference that the Legislature intended for the Commission to fix rates as low as may be reasonably consistent with the requirements of the Due Process Clause of the Fourteenth Amendment to the Constitution of the United States..." State ex rel. Utilities Commission v. Duke Power Company, 285 N.C. 377, 206 S.E. 2d 269 (1974).

The nature of the evidence in a case such as this makes it extremnely difficult to balance all of the opposing interests, since much, if not all, of the evidence is based on individual witnesses' perceptions and interpretations of trends and data from the capital markets. The Commission has considered carefully all of the relevant evidence presented in the case, with the constant reminder that whatever return is allowed will have an immediate impact on the Company, its stockholders, and its customers. The Commission must use its impartial judgment to ensure that all the parties involved are treated fairly and equitably. In coming to a final decision on this matter, the Commission is mindful of and, indeed, has given full consideration to the changes now occurring in the telecommunications industry. The Commission, therefore, concludes that the appropriate rate of return on equity in this proceeding is 15.00%. Accordingly, Continental should be permitted to earn 12.12% on the original cost of its rate base.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 15

This Commission has previously discussed its findings and conclusions concerning the fair rate of return which Continental should be given the opportunity to earn.

The following schedules summarize the gross revenues and the rates of return which the Company should have a reasonable opportunity to achieve based on the increases approved herein. The schedules illustrating the Company's gross revenue requirements incorporate the findings and the conclusions heretofore and herein made by the Commission.

SCHEDULE I
CONTINENTAL TELEPHONE COMPANY OF NORTH CAROLINA
STATEMENT OF OPERATING INCOME
Twelve Months Ended December 31, 1982

	Intrastate Present Rates	Increase Approved	After Approved Increase
Operating Revenues:			
Local service revenues	$18,780,910	$3,385,983	$22,166,893
Toll service revenues	12,758,057	-	12,758,057
Miscellaneous revenues	978,017	-	978,017
Uncollectible revenues	(51,373)	(8,804)	(60,177)
Total operating revenues	$32,465,611	$3,377,179	$35,842,790
Operating Expenses:			
Operating expenses	14,304,312	-	14,304,312
Depreciation	7,460,959	-	7,460,959
Operating taxes - other than income	2,932,629	202,631	3,135,260
State & federal income taxes	2,080,456	1,563,147	3,643,603
Total operating revenue deductions	$26,778,356	$1,765,778	$28,544,134
Net operating income for report	$ 5,687,255	$1,611,401	$ 7,298,656

SCHEDULE II
CONTINENTAL TELEPHONE COMPANY OF NORTH CAROLINA
STATEMENT OF RATE BASE AND RATE OF RETURN
Twelve Months Ended December 31, 1982

	After Approved Rates
Investment in Telephone Plant:	
Telephone plant in service	$90,583,398
Accumulated depreciation	(20,597,541)
Accumulated deferred income taxes	(10,607,714)
Pre-1971 investment tax credits	(49,723)
Total investment in telephone plant	$59,328,420)
Allowance for working capital	891,517
Total rate base	$60,219,937
Rate of return:	
Approved rates	12.12%
Present rates	9.43%

SCHEDULE III
CONTINENTAL TELEPHONE COMPANY OF NORTH CAROLINA
CAPITAL STRUCTURE
December 31, 1982

Item	Ratio %	Original Cost Rate Base	Embedded Cost %	Net Operating Income
	Present Rates - Original Cost Rate Base			
Long-term debt	49.95	$30,079,858	9.53	$2,866,610
Preferred stock	2.01	1,210,421	7.65	92,597
Common equity	48.04	28,929,658	9.43	2,728,048
Total	100.00	$60,219,937		$5,687,255
	Approved Rates - Original Cost Rate Base			
Long-term debt	49.95	$30,079,858	9.53	$2,866,610
Preferred stock	2.01	1,210,421	7.65	92,597
Common equity	48.04	28,929,658	15.00	4,339,449
Total	100.00	$60,219,937		$7,298,656

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 16

Company witnesses Nash and Feaster and Public Staff witness Carpenter presented testimony concerning Continental's proposed rate structure.

Company witness Nash presented rate proposals to produce the requested amount of additional annual revenue. Witness Nash's proposals included consolidation of basic rates for the former Westco and Western Carolina service areas, reduction in the number of different zone charges from four to one with a slight increase in resulting zone charge revenue, increases in service connection charges, establishment of a late payment charge and substantial increases for numerous items of terminal equipment, including telephone sets and volume control equipment. After taking the stand, witness Nash testified that the Company had accepted Public Staff witness Carpenter's recommendations on the following issues: monthly rates for standard and dial-in-handset telephones, mileage service, and volume control equipment. Company witness Nash also agreed with certain of witness Carpenter's proposals on service connection charges: premises visit charges, inside wiring charges, jack charges, and secondary service order charges. In the area of zone charges, witness Nash acknowledged during cross-examination that subscribers who had been encouraged through past reductions in the zone A and B charges to upgrade to one-party service would, under the Company's proposal, actually see an increase in their zone charges. Company witness Feaster testified that the Company had no plans to completely eliminate zone charges but that the Company's current plans include provision of an all one-party system by the end of 1987.

Company witness Nash clarified the Company's intent to reduce the multiple applicable to nonrotary lines terminating in two- and three-line key systems from 1.75 to 1.0. Witness Nash also stated the Company's intent to regroup the Franklin exchange from Rate Group 2 to Rate Group 3. The Company also proposed tariff provisions which would allow the Company to regroup exchanges outside of a rate proceeding.

In additional testimony, witness Nash stated that the Company's estimate of late payment revenue which would result from the proposed late payment charge to be $32,276. The witness stated that the Company had no experience with the charge and therefore his calculation was based upon an estimate that 67% of those subscribers now paying late would pay on time after implementation of the charge. Witness Nash explained that the Company looked at bills between 30 and 90 days old rather than more than 25 days old as provided by Commission Rule R12-9(d). He also stated that the $32,376 estimate did not include any savings in expense resulting from avoidance of short-term interest expense. The witness acknowledged that witness Carpenter's estimate was based on actual experience of a General Telephone Company and that that experience indicated that only 12% of subscribers who had previously paid late would begin to pay on time.

Public Staff witness Carpenter presented the Public Staff's recommendations on the Company's proposed changes in rates and regulations and the distribution of Continental's additional revenue requirement among the various classes of services. He made four general recommendations on service charges and presented specific rate levels in an exhibit attached to his testimony. The general recommendations are as follows:

1. The cost levels presented by Continental should be adjusted to remove the effects of wage level adjustment which were expectd to occur beyond the time of the hearing;

2. The equipment work charges should not be increased due to questions concerning the estimated time required to perform those functions;

3. The residence service order charge and central office work charge should not be increased because those work functions are essential to the establishment of basic service and because the charges cannot be avoided by the subscriber; and

4. Other service charges should be increased or reduced to their adjusted cost levels.

Witness Carpenter stated that the Public Staff did not object to late payment charges as long as they are applied in accordance with Commission Rules. The witness pointed out that Continental had not included any effect for revenue due to the charges or due to a decrease in expense because of the effect the charge would have on prompting subscribers to pay on time. Witness Carpenter estimated that the total effect (revenue increase and expense reduction) of implementation of the charge for Continental would be $122,183. This amount was based upon calculations and estimates of the effect on General Telephone of the Southeast of implementation of the same charges in Docket No. P-19, Sub 193. Witness Carpenter stated that his estimate for Continental was calculated by determining the ratio of General's estimate of increased revenue and decreased expenses to its intrastate total adjusted operating revenue net of uncollectibles and applying that ratio to Continental's intrastate adjusted total operating revenue net of uncollectibles. The witness stated that General's method of calculation and the amount of the General's estimate was based upon experience with the charge of another General Company and was accepted by the Public Staff and the Commission in the previously cited docket. Witness Carpenter stated that his estimate of $122,183 was actually lower than the result he obtained using a slightly different method.

With regard to the Company's zone charge proposal, Public Staff witness Carpenter recommended that complete elimination of Continental's present zone charges and recovery of the $487,275 revenue shortfall through an increase in basic rates of approximately $.50 per month per residence access line and $1.25 per month per business access line. (Services with rates equal to multiples of the individual line rates would receive proportionately higher increases).

Witness Carpenter recommended no change in the rates for standard and dial-in-handset telephones and in rates for volume control equipment for subscribers with impaired hearing and speech. The witness agreed to the proposed consolidation of rates for the former Western Carolina and Westco service areas. He also recommended increases in rates for mileage services of approximately 22%.

Public Staff witness Carpenter agreed with the change in the multiple for nonrotary lines terminating in two- and three-line key systems but he did not agree that this would result in a $76,000 reduction in revenue as estimated by the Company.

Continental's proposal for automatic regrouping was opposed by witness Carpenter. He stated that the tariff unnecessarily erodes the Commission's authority in controlling basic local rates at a time when public pressures against local rate increases are rising.

Witness Carpenter's recommended distribution of the additional revenue requirement reflected his specific recommendations and recovery of the residual requirement by application of a flat percentage to other categories of service including basic service. With the exception of mileage service, none of the increases he proposed exceeded those proposed by Continental.

Based upon all of the evidence of record regarding rate design and tariff proposals, the Commission concludes that changes in rates and tariffs should be in accordance with the guidelines set forth in Appendix A. The Commission concludes that the Company must plan towards complete elimination of zones and zone charges in the near future.

IT IS, THEREFORE, ORDERED as follows:

1. That the Applicant, Continental Telephone Company of North Carolina be, and hereby is, authorized to increase its local service rates and charges by $3,385,983 above the revenue level that would have resulted from rates currently in effect based on the test year.

2. That the Applicant is hereby called upon to propose specific tariffs reflecting changes in rates, charges, and regulations to recover the revenues approved herein, in accordance with the guidelines set forth in Appendix A attached hereto, within ten (10) days from the date of this Order. These proposals and workpapers supporting such proposals shall be provided to the Commission (five copies are required) and the Public Staff (formats such as Item 30 of the minimum filing requirement, NCUC Form P-1, are suggested).

3. That the Public Staff may file written comments concerning the Company's tariffs within five (5) working days of the date on which they are filed with the Commission.

4. That the rates, charges, and regulations necessary to produce the annual gross revenues authorized herein shall become effective upon the issuance of a further Order approving the tariffs filed pursuant to paragraph 2 above.

5. That the Applicant shall file within ten (10) days from the date of this Order a proposed customer notice informing the customers of Continental Telephone Company of North Carolina of the actions taken herein.

6. That the Public Staff's Motion to Strike, filed November 8, 1983, be, and hereby is, granted. Any other motions heretofore filed in this docket and not previously ruled upon be, and are hereby, denied.

7. That Continental be, and is hereby, required to retain an independent consulting engineer to conduct a service investigation in conformity with the requirements set forth hereinabove in conjunction with the "Evidence and Conclusions for Finding of Fact No. 4." Further, that the Public Staff be, and is hereby, requested to assist the Company in the selection of an appropriate consulting engineer to conduct the investigation in question and to coordinate said investigation on behalf of the Commission.

8. That Continental be, and is hereby, required to file a report with the Public Staff and Utilities Commission in six months outlining its progress in eliminating any central office outages at the Marion exchange.

9. That Continental be, and is hereby, required to establish a deferred account and to place in said deferred account any intrastate toll revenues in excess of $500,000 which the Company derives from the toll rate increases granted in Docket No. P-100, Sub 64, pending further hearing.

ISSUED BY ORDER OF THE COMMISSION.
This the 29th day of November 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sandra J. Webster, Chief Clerk

APPENDIX A
Continental Telephone Company of North Carolina
Docket No. P-128, Sub 3
Tariff and Rate Design Guidelines

1. The schedule of nonrecurring service charges listed below is just and reasonable.

	Residence	Business
A. Service order		
1. Primary	$23.00	$23.00
2. Secondary	8.00	8.00
B. Premises visit, each	7.00	7.00
C. Central office work, each	22.00	22.00
D. Inside wiring, each	18.00	42.00
E. Equipment work, each	14.00	14.00
F. Jack, each	3.00	3.00

2. A late payment charge in accordance with Commission Rule R12-9(d) is just and reasonable. A reasonable estimate of the effect of this charge is $32,276.

3. Continental's zone charges should be reduced by 30% in each category. The revenue shortfall should be recovered by spreading the amount across all exchange access rates in accordance with the approved rate relationships.

4. No increases should be made in rates for standard and dial-in-handset telephones or in rates for volume control equipment for subscribers with impaired hearing or speech.

5. Continental's proposal to consolidate local rates for its former Western Carolina and Westco service areas is reasonable.

6. Rates for mileage services should be increased approximately 22% in accordance with the Public Staff's recommendations.

7. Continental's proposal for regrouping of exchanges outside of a rate proceeding is reasonable and is allowed under the Company's proposal.

8. The Franklin exchange should be regrouped to Rate Group 3.

9. The multiple for nonrotary lines terminating in two- and three-line key systems should be reduced to 1.0 times the individual line rate. The revenue effect of this change should be calculated based upon the actual number of rotary and nonrotary lines terminating in those systems.

10. The residual revenue requirement which remains after implementation of the above guidelines should be obtained by applying a percentage increase on all remaining categories of service with the proviso that with the exception rates for mileage services no rates should exceed those proposed by Continental.

DOCKET NO. P-118, SUB 27

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Application of Mid-Carolina Telephone Company for Authority to Adjust Its Rates and Charges for Intrastate Telephone Service in North Carolina) FINAL ORDER GRANTING PARTIAL RATE INCREASE

HEARD IN: W. Alexis Hood Meeting Room, Town Hall, 224 North Trade Street, Matthews, North Carolina, on Wednesday, November 9, 1983, at 9:00 a.m.

Gymatorium, Rural Hall Elementary School, 275 College Street, Rural Hall, North Carolina, Wednesday, November 9, 1983, at 7:30 p.m.

Courtroom, Polk County Courthouse, Main Street, Columbus, North Carolina, Thursday, November 10, 1983, at 2:00 p.m.

Commission Hearing Room, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina, Monday, November 21, and Tuesday, November 22, 1983

BEFORE: Commissioner Leigh H. Hammond, Presiding; and Chairman Robert K. Koger and Commissioner Edward B. Hipp

APPEARANCES:

For the Applicant:

F. Kent Burns, Boyce, Mitchell, Burns & Smith, Attorneys at Law, P. O. Box 2479, Raleigh, North Carolina 27602

For the Public Staff:

Theodore C. Brown, Jr., Staff Attorney, Public Staff - North Carolina Utilities Commission, P. O. Box 991, Raleigh, North Carolina 27602

G. Clark Crampton, Staff Attorney, Public Staff - North Carolina Utilities Commission, P. O. Box 991, Raleigh, North Carolina 27602

BY THE COMMISSION: On May 13, 1983, Mid-Carolina Telephone Company filed an application with the North Carolina Utilities Commission seeking authority to adjust its rates and charges for intrastate telephone service. The requested increase in rates and charges was designed to produce approximately $2,098,734 in additional annual revenues from intrastate operations when applied to a test period consisting of the 12 months ended December 31, 1982. The Company proposed that the rates and charges become effective for services rendered on and after June 13, 1983.

By Order issued on June 10, 1983, the Commission declared the matter to be a general rate case pursuant to G. S. 62-137, suspended the proposed rates and charges for 270 days from the June 13, 1983, effective date, set hearings to begin on November 9, 1983, declared the test period to be the 12 months ended December 31, 1982, required the Company at its expense to give public notice of the proposed increase and hearings, and set the time for the Public Staff and other interested parties to file intervention and/or testimonies.

By Order issued October 11, 1983, the Commission rescheduled the hearings to begin in Raleigh, North Carolina, on Monday, November 21, 1983, at 1:00 p.m.

The Commission conducted out-of-town hearings for the purpose of receiving testimony from the using and consuming public. The first such hearing was held in Matthews, North Carolina, at 9:00 a.m., on Wednesday, November 9, 1983; the second in Rural Hall, North Carolina, at 7:30 p.m., on November 9, 1983; and the third in Columbus, North Carolina, at 2:00 p.m., on November 10, 1983.

The following public witnesses appeared and offered testimony in Matthews, North Carolina: John Wimbish, Helen M. Blair, and Nancy McLendon.

The following public witnesses appeared and offered testimony in Rural Hall, North Carolina: Michael Priddy, Raeford Spainhour, Iris Fulton, Louise Spaugh, Edward Hall, Henry W. Harris, Evelyn E. Shouse, Norma Cox, and Harold Spaugh.

The following public witness appeared and offered testimony in Columbus, North Carolina: Abner O. Paulsell.

The hearings resumed in Raleigh on November 21, 1983, at 1:00 p.m. for the purpose of receiving further testimony of public witnesses and the testimony and cross-examination of the Applicant and the Public Staff. The Company offered the testimony and exhibits of the following witnesses: Archie A. Thomas, President of Mid-Carolina Telephone Company, who testified as to service and service area, extended area service (EAS), growth, and cost of service; Franklin D. Rowan, Regional Controller with ALLTEL Service Corporation, who testified as to test period data, balance sheet, per books operating statement and adjustments; L. S. Pomerantz, Vice-President - State Regulatory Matters with ALLTEL Service Corporation, who testified as to the intercompany and affiliated relationships and services performed by the service corporation of the Company; Charles E. Olson, President of Olson and Company, Inc., presented testimony and exhibits concerning the rate of return, cost of capital and general financing costs; and J. L. Shettel, Rates and Tariffs Co-Ordinator of ALLTEL Service Corporation, who testitied concerning tariffs and proposed rates and charges designed to produce the additional annual revenue increases.

The Public Staff offered the testimony and exhibits of the following witnesses: William J. Willis, Jr., Engineer, Communications Division of the Public Staff who testified as to end-of-period, local and miscellaneous revenues, and proposed changes in rates and regulations and the appropriate distribution of additional revenues required; Hugh L. Gerringer, Engineer, Communications Division of the Public Staff, who testified as to the Company's intrastate toll revenue; Leslie C. Sutton, Engineer, Communications Division of the Public Staff, who testified as to the Company's practices concerning procedures and central office equipment; Hugh Hu, Engineer, Communications Division of the Public Staff, who testified concerning the adequacy and quality of the Company's service; Karyl Lam, Staff Accountant, Accounting Division of the Public Staff, who testified concerning accounting adjustments, revenues and expenses, and rate base; and David. T. Bowerman, Financial Analyst, Economic Research Division of the Public Staff, who testified concerning the appropriate capital structure, cost of common equity, cost of capital, and rate of return.

Mid-Carolina Telephone Company offered the rebuttal testimony and exhibits of Harold W. Shaffer, regional settlements supervisor of the Southern Region for ALLTEL Service Corporation, concerning toll settlements, and Charles E. Olson of Olson and Company, Inc., concerning rate of return.

Based on the foregoing, the testimony and exhibits admitted at the hearings, and the entire record in this docket, the Commission now makes the following

FINDINGS OF FACT

1. The Applicant, Mid-Carolina Telephone Company, is a duly organized North Carolina corporation and a wholly owned subsidiary of ALLTEL Service Corporation. Mid-Carolina is a public utility engaged in providing telephone service in North Carolina and is subject to the jurisdiction of this Commission. Mid-Carolina is properly before the Commission in this proceeding, pursuant to G.S. 62-133, for a determination of the justness and reasonableness of its proposed rates and charges.

2. By its application, the Company requested rates designed to produce total annual operating revenues of $25,876,161, based upon a test year ended December 31, 1982. The Company contended that revenues under present rates are $23,777,427, thereby necessitating an increase of $2,098,734 which the Company proposes to achieve through increases in rates for local service.

3. The test period for purposes of this proceeding is the 12 months ended December 31, 1982.

4. The overall quality of the service provided by Mid-Carolina is inadequate; however, the Company has made some improvements in service since it was last granted an increase in its rates and charges on June 17, 1982, in Docket No. P-118, Sub 22.

5. Mid-Carolina's reasonable original cost rate base used and useful in providing telephone service within the State of North Carolina is $52,208,458. This rate base consists of telephone plant in service of $79,375,872, telephone plant under construction of $3,066,945, materials and supplies of $369,953, and working capital of $458,031, reduced by accumulated depreciation of $23,410,881, customer deposits of $93,347, pre-1971 investment tax credits of $74,998, and accumulated deferred income taxes of $7,483,117.

6. Mid-Carolina's total end-of-period operating revenues for the test year, under present rates and after accounting and pro forma adjustments, are $24,315,316.

7. The reasonable level of test year operating revenue deductions for Mid-Carolina after end-of-period and pro forma adjustments is $19,339,356. This amount includes $5,252,009 for investment currently consumed through reasonable actual depreciation on an annual basis.

8. The capital structure appropriate for use in this proceeding is as follows:

Item	Percent
Long-term debt	58.00%
Preferred stock	8.00%
Common equity	34.00%
Total	100.00%

9. The failure of Mid-Carolina to provide adequate telephone service is a material factor to be considered in establishing the fair rate of return. The Company's proper embedded costs of long-term debt and preferred stock are 8.95% and 7.65%, respectively. The fair rate of return which Mid-Carolina should be allowed to earn on its common equity is 15.00%. Using a weighted

average for the Company's cost of long-term debt, preferred stock, and common equity with reference to the reasonable capital structure heretofore determined yields an overall fair rate of return of 10.90% to be applied to the Company's original cost rate base.

If the service of Mid-Carolina had been adequate, a return of 11.07% on the original cost net investment and a return of 15.50% on common equity would be just and reasonable.

10. The total annual gross revenue requirement for Mid-Carolina is $25,860,676. This is an increase of $1,504,816. This increase is required in order for Mid-Carolina to have a reasonable opportunity to earn the 10.90% rate of return on its rate base which the Commission has found just and reasonable. This increased revenue requirement is based upon the original cost of the Company's property and its reasonable test period operating revenues and expenses, as previously determined and set forth in these findings of fact.

11. The rates and charges that are to be filed pursuant to this Order in accordance with the conclusions set out herein will produce an increase in annual local revenues of $1,504,816, which will be just and reasonable.

12. The appropriate length of the engineering interval for digital central offices for Mid-Carolina Telephone Company should be one year.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 1, 2, AND 3

The evidence supporting these findings of fact is contained in the verified application, the Commission's Order Setting Hearing, and the testimony and exhibits of Company witness Rowan. These findings are essentially informational, procedural, and jurisdictional in nature and were uncontested.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 4

The evidence concerning the quality of service was presented by Company witness Thomas, Public Staff witness Hu, and 13 public witnesses.

Nine customers testified at the public hearing held in Rural Hall. All but one described one or more service problems which he or she had experienced. Four customers indicated that they had problems with slow dial tone or no dial tone. One customer complained of having repeated difficulty calling and being called from Stanleyville. Two customers complained of frequent difficulty in calling the King (983) exchange. Three customers complained of problems with static on the line when it rains, although there was evidence that one had experienced no such problems since his drop had been replaced in August. At least three customers complained of frequently getting wrong numbers or a recording even though the correct working number had been dialed. Three customers complained of having experienced cut offs of their telephone conversations. Subsequent to the hearing, the Company inspected and/or tested the equipment and service of all these customers who reported service problems.

Company evidence regarding its immediate follow-up investigations of the complaints presented at the Rural Hall hearing indicated that in five of the eight cases one or more items of defective or potentially problematic

equipment had been identified and replaced. The extent to which such equipment replacement has remedied some or all of the problems of the involved customers is unknown at present.

Three witnesses who were served on the Company's Matthews exchange testified at the public hearing held there. All three complained of problems with having to redial or experiencing trouble in getting a connection completed. One of those witnesses complained of the failure of the bill to disclose connect times for long-distance calls. Company evidence, subsequently introduced, established that this information was in fact shown on bills. One of the witnesses additionally complained of problems with noise and static, cut-off calls, and frequently reaching a recording indicating that the number dialed was a nonworking number. Evidence submitted by the Company indicated that the Company had inspected or tested the equipment and service of each of these three customers after they had testified in Matthews. That evidence established that two of the three customers were found to have defective or improperly working inside equipment and that such equipment had been replaced by the Company.

Only one witness appeared and testified at the public hearing held in Columbus. His primary concern was the delay and difficulty in having his new telephone number properly listed by the Company in all information centers when he moved from Columbus to Tryon approximately six months ago. He testified that if an out-of-town caller asked information for a new number in the group of local exchanges but specified the wrong exchange that information would indicate there was no listing. He suggested that the information service should be able to give out a new listing even if the calling party mistakenly or erroneously specified that the party being called lived in a local exchange other than the one where the party in fact lived. The witness also identified two problems which he had experienced within the last year. He testified that his telephone had gone out of service on a Saturday and was not fixed until the following Monday and that he had experienced a temporary difficulty in dialing out a few days prior to the hearing.

Company Witness Thomas testified that the Company was continuously striving to provide good telephone service to all areas it served, that the Company's reported trouble index during the test year had been consistently within objectives set by this Commission and that the operator answer time, directory assistance and repair service had also remained within the objectives of this Commission. Witness Thomas further testified that community feedback indicated that subscribers were receiving good service and that the Company was responsive to customer requests for new service and for changes in their existing service. Further, witness Thomas described improvements and efforts by the Company to improve service which had been made since the last general rate case. Witness Thomas testified that in the Rural Hall/Old Town area there had been line and terminal additions, trunk replacement, addition of EAS trunks, and some new toll trunks. It was indicated by witness Thomas that extensive Automatic Line Installation Test System testing had been done in the area. Witness Thomas described generally similar improvements and testing as having been done in the Company's Columbus service area.

Upon cross-examination, witness Thomas was also asked to comment upon the possible or probable causes of the various types of problems that the public witnesses had described. Witness Thomas testified that for several types of these problems, including the cross talk and cut-off problems and the reaching

wrong numbers or recording problems, he could not speculate on causes as there were several possible causes. Witness Thomas stressed that, in order for the Company to be able to identify and remedy such problems, it was important for the customer involved to report them to the Company as soon as they occurred. It was stated by witness Thomas that the problem of static on the line when it rains may possibly be caused by the presence of a particular type of cable in the Rural Hall area local exchanges. Witness Thomas testified that the Company has begun replacing this cable and is currently scheduled to have replaced all such cable within the next four years. It was indicated by witness Thomas that the nonexistent dial tone or slow dial tone problems were possibly related to the switching equipment. In this regard witness Thomas testified that the Company was installing a new digital switch in the King exchange in January 1984 and that new digital switching equipment to handle some but not all of the Old Town exchange was scheduled to be in place by the end of 1983. Additionally, witness Thomas indicated that new digital switching equipment was currently scheduled to be installed for the Rural Hall exchange during 1986. There was also evidence that the possible cause of the slow dial tone problem and the recurrent problems in calling a particular exchange could be due to the inadequacy of lines or trunks involved and that such cause could be identified and cured by traffic studies and tests of line finder groups. Company witness Thomas also acknowledged that there were additional tests and investigations which the Company could make toward identifying and solving customer complaint problems, but which at that point the Company had not had time to carry out. Witness Thomas testified that the Company would pursue such tests and investigations.

Public Staff witness Hu testified that his review consisted of field inspections and tests of switching and trunking facilities, measurements of the answer time of operators, directory assistance, repair service and business office, and an analysis of statistics relating to the Company's service. Based on his evaluation of all the test results and service data, witness Hu concluded that the overall quality of service provided by the Company was adequate; however, there were some weak spots (summarized in Hu's Exhibit No. 13), to which the Company should give close attention and take action to correct.

During redirect, Public Staff witness Hu stated that in his opinion the Company had not done its best to address the slow-dial-tone and had-trouble-calling-King exchange problems, which were described by some public witnesses at the Rural Hall public hearing. Witness Hu stated that the Company should conduct a traffic study on line finders in the Rural Hall exchange and on trunks to the King office (983 exchange), and take corrective actions as needed.

Based upon the evidence in this proceeding, the Commission finds that the overall quality of service provided by the Company is inadequate. The Commission is concerned about the Company's failure to meet some of the Commission's established service objectives which failures were pointed out in the testimony of Public Staff witness Hu. In this regard the Commission concludes that the Company must continue and increase its efforts to improve service in the problem areas which were identified by witness Hu in his testimony and which were summarized in his Exhibit No. 13. In order for the Commission to monitor and evaluate such efforts, the Commission has determined that the Company should conduct an investigation into the causes of each of the failures to meet service objectives which were identified by witness Hu

and file its report with the Commission regarding the results of the Company's investigation of each as well as what specific corrective measures have been, or are being, taken by the Company in order to improve service in each problem area so as to meet the relevant service objective.

Further, the Commission concludes that the Company should conduct further follow-up tests and investigations of each service complaint which was addressed by each public witness (except Henry Harris who requested not to be contacted). As a part of this effort the Company shall conduct a traffic study on line finders in the Rural Hall exchange and on trunks to the King office (983 exchange) and to the Stanleyville office, and take such corrective action as may be needed to correct problems indicated. The Company shall file a report of these follow-up investigations indicating what specific tests and corrective actions, if any, have been or are being conducted with respect to each public witness's service complaint. Such report should be filed within 60 days from the date of this Order. Items that are not completed or resolved shall be filed as a follow-up each 30 days, thereafter, until completed.

The Commission further concludes that Mid-Carolina should investigate the possibility of accelerating the timetables on the replacement of the lead cable in the Rural Hall area local exchange scheduled over the next four years and the installation of the new digital switching equipment scheduled for the Rural Hall exchange during 1986. After the Company's investigation into the speeding up of these installations, the Commission requests that within a reasonable period of time the Company report to the Commission its findings and position on this matter along with appropriate explanations.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 5

The evidence concerning the proper intrastate original cost rate base is found in the testimony and exhibits of Company witness Rowan and Public Staff witness Lam. The following chart summarizes the amounts which the Company and the Public Staff contend constitute the proper intrastate original cost rate base to be used in this proceeding. The amounts shown for the Company reflect the effects of the Public Staff's adjustments which were accepted by witness Rowan during the hearing.

Item	Company	Public Staff
Telephone plant in service	$ 79,375,872	$ 79,375,872
Telephone plant under construction	3,066,945	3,066,945
Working capital	458,031	458,031
Materials and supplies	369,953	369,953
Depreciation reserve	(23,410,881)	(23,410,881)
Customer deposits	(93,347)	(93,347)
Pre-1971 investment tax credits	(74,998)	(74,998)
Accumulated deferred income taxes	(7,483,117)	(7,483,117)
Original cost rate base	$52,208,458	$52,208,458

As shown above, the Company and the Public Staff agree on the amount of each component to be included in the calculation of the original cost rate base. Therefore, the Commission concludes that the adjustments to rate base proposed by Public Staff witness Lam are proper, that the amount included for each item of rate base is reasonable, and that the proper intrastate original

cost rate base for use in this proceeding is $52,208,458, as shown in the chart above.

There are two issues which witness Lam discussed extensively in her testimony which were not contested by the Company, but which the Commission wishes to addess at this time. The first of these is witness Lam's adjustment to remove the Company's investment in unregulated operations. Witness Lam testified that during the test year the Company was involved in selling unregulated telephone equipment through its Conversation Stations, but that it made no attempt to allocate any investment to these unregulated operations, other than charging to the unregulated operations a small amount of furniture and office equipment specifically purchased for the Conversation Stations. Further, witness Lam testified that she did not believe that the Company properly allocated expenses to its unregulated operations during the test year. Several expenses were listed by witness Lam which she stated were not allocated at all and she also listed several expenses for which only very small amounts were allocated.

Witness Lam testified that, beginning in January 1983, the provision of new customer premises equipment (CPE) was completely deregulated and that, as a result, the Company is more involved in unregulated activities than ever before, but that it is making no more effort than during the test year to properly allocate investment and expenses to its unregulated operations. Witness Lam testified that it is imperative that the Company be required to set up detailed procedures for properly allocating investment and expenses to its unregulated operations so that the regulated ratepayers do not subsidize unregulated operations by paying more than their fair share of the Company's operating expenses.

The Commission shares witness Lam's concern that the regulated ratepayers should not be required to subsidize the Company's unregulated operations. Accordingly, the Commission concludes that Mid-Carolina must establish detailed procedures for properly charging investment and expenses to its unregulated operations. These procedures should specify how the amounts of all items to be charged to the unregulated operations are to be determined. Within 120 days after the effective date of this Order, the Company shall file a report with the Commission detailing all the procedures which it plans to follow in charging investment and expenses to its unregulated operations. This report should detail each item to be charged or allocated, the basis on which it is to be charged or allocated, the procedures used to determine the amount to be charged, and an explanation of why each procedure is appropriate.

The second item discussed by witness Lam which the Commission wishes to address is the Company's purchase of poles from Carolina Power & Light Company (CP&L). Witness Lam testified that during the test year Mid-Carolina, pursuant to a rental agreement, purchased 1,710 jointly used poles from CP&L. Witness Lam testified that the Company did not properly record the purchase of these poles. According to witness Lam, the Company should have debited plant in service for CP&L's original cost of the poles, credited depreciation reserve for CP&L's depreciation reserve related to the poles, and debited plant acquisition adjustment for the difference between the purchase price and CP&L's net book cost, but instead she stated that the Company actually grossed up the purchase price to what it considered the original cost of the poles and then made a corresponding adjustment to the depreciation reserve to bring the

net booked cost of the poles back down to the price actually paid. Witness Lam stated that she did not make the adjustment to properly record the purchase of the 1,710 poles because of its immaterial effect on the rate base, but she did recommend that the Company be required to properly record any future pole purchases and be allowed to request amortization and rate base treatment for any plant acquisition adjustment arising from such purchases. The Commission concurs with this recommendation. For any future purchases of poles from CP&L (or any other utility property acquired from any other utility), the Company is hereby required to record the purchase in the manner set out above, so that only the original cost of the property to the entity originally dedicating it to utility service is included in the plant accounts. The Company may apply to the Commission for permission to amortize any resulting plant acquisition adjustment to expense and may request rate base treatment for any plant acquisition adjustment in a general rate proceeding following the purchase.

There are two remaining rate base items which witness Lam adjusted that the Commission wishes to address. The first of these is the Public Staff adjustment to reclassify completed construction as plant in service. Witness Lam testified that, subsequent to her field investigation, the Company discovered that certain projects that were included in telephone plant under construction at December 31, 1982, had actually been placed in service prior to that date but had not been transferred to plant in service on the books. Witness Lam made an adjustment to transfer this completed construction to plant in service. The Commission finds that this adjustment is appropriate. However, the Commission is concerned about what appears to be a considerable delay between the time a project is completed and placed in service and the time it is transferred from the construction account to the plant in service account on the books. Such delay can lead to several problems, such as the accrual of interest during construction (IDC) on projects that are actually completed and providing service to the ratepayers and the mismatch of revenues, expenses, and plant in service in a rate case. The Company should take immediate steps to see that completed construction placed in service is promptly transferred to the appropriate plant in service account(s).

The final issue which the Commission wishes to address is witness Lam's adjustment to remove from plant in service IDC accrued on construction work in progress (CWIP) included in the rate base in the Company's last general rate case, Docket No. P-118, Sub 22. Witness Lam testified that the Company continued to accrue IDC on CWIP after it was included in the rate base in Docket No. P-118, Sub 22, in spite of G. S. 62-133(b)(4a) which specifically requires that IDC cease to accrue on CWIP included in the rate base. The Commission accepts witness Lam's adjustment to remove the IDC from plant in service. Further, the Commission requires the Company to cease to accrue IDC on the CWIP which it has included in the rate base in this proceeding, beginning on the effective date of the Order in this docket. The Company should also review its IDC procedures to ascertain that IDC is being accrued only on those projects which are eligible for it.

In closing, the Commission wishes to point out that CWIP of $3,066,945 has been allowed in the rate base as the Commission finds that such inclusion is deemed necessary to the financial stability of the Company based upon the capital structure and cost rates adopted for use in this proceeding. The Commission will continue to review each request to include CWIP in the rate base on a case-by-case basis and will make its decision based upon the facts of each case.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 6

The evidence concerning the proper end-of-period level of intrastate operating revenues was presented through the testimony and exhibits of Company witness Rowan and Public Staff witnesses Gerringer, Willis, and Lam and the rebuttal testimony and exhibits of Company witness Shaffer. The amounts proposed by the witnesses are shown in the following chart. The amounts shown for the Company have been adjusted to reflect the effects of the Public Staff's adjustments which were accepted by witness Rowan at the hearings and the amounts for the Public Staff reflect its position as set out in its Proposed Order.

Item	Company	Public Staff	Difference
Local service revenues	$16,128,910	$16,128,910	$ -
Toll service revenues	7,042,861	7,788,606	745,745
Miscellaneous revenues	766,481	766,481	-
Uncollectibles	(40,544)	(40,544)	-
Total operating revenues	$23,897,708	24,643,453	$745,745

As shown above, the Company and the Public Staff agree on the amounts of local, miscellaneous, and uncollectible revenues. Therefore, the Commission concludes that the amounts shown for these items are reasonable and require no further discussion.

The only difference between the parties is the proper level of toll revenues. Company witness Rowan calculated a representative level of gross intrastate toll revenues at December 31, 1982, of $7,075,800 in his filed direct testimony and exhibits. This amount, which did not include any uncollectible toll revenue contribution, was largely determined by the calculation method used to settle toll revenues with Southern Bell on an actual cost basis. The calculation was made using adjusted end-of-period levels of intrastate toll net investment settlement and expenses including adjustments related to the phasedown of CPE and an intrastate toll settlement ratio of 11.3785%, an average of the actual achieved ratio for the year ending December 31, 1982, of 11.2741%, and the ratio for the year ending December 31, 1983, estimated by Southern Bell to be 11.4828%.

Public Staff witness Gerringer testified that $7,068,160 is the level of toll revenue that was determined by a toll settlement calculation which did not include any uncollectible toll revenue contribution like that used by the Company with the major differences being that he used a settlement ratio of 11.36% and adjusted for the phasedown of CPE differently than the Company did. The 11.36% settlement ratio resulted from summing monthly achieved final settlement ratios for a 12-month period - July 1982 through June 1983 - with six months falling on each side of the end of the test period, December 31, 1982.

During the hearing the Company accepted the 11.36% settlement ratio used by witness Gerringer in his toll settlement calculation and the CPE phasedown adjustments reflected in his calculation. There being no evidence to the contrary, the Commission accepts that the level of toll revenue produced with an 11.36% settlement ratio in the toll settlement calculation with CPE phasedown adjustments is $7,068,160.

The $745,745 difference between the parties with respect to toll revenues results from three adjustments made by the Public Staff which are as follows:

Item	Amount
Adjustments as a result of Docket No. P-100, Sub 64:	
A. Toll rate increase from MTS, WATS, and Private Line	$571,588
B. Toll rate increase from Directory Assistance	84,686
Adjustment as a result of Public Staff's adjustment to depreciation expense and interest expense for income tax calculation	89,471
Total adjustments	$745,745

The first two adjustments deal with the Public Staff's inclusion of $656,274 ($571,588 + $84,686) of toll revenues which are the estimated increase in toll revenues for the Company resulting from the latest toll rate changes which became effective September 27, 1983.

Company witness Shaffer through rebuttal testimony presented the Company's opposition to the inclusion of the revenue impact of the intrastate toll rate case proceeding in Docket No. P-100, Sub 64. Witness Shaffer argued that the Public Staff is attempting to use an artificially high level of intrastate toll revenues in fixing local service rates. In support of his position, witness Shaffer testified that the inclusion of $571,588 by the Public Staff as additional toll revenue which Mid-Carolina should receive from the MTS, WATS, and private line increase in toll rates in Docket No. P-100, Sub 64, would mean that the entire intrastate toll pool would have to achieve a settlement ratio of 13.36% in order for Mid-Carolina to realize the amount of toll revenue attributed to it by the Public Staff. Further, witness Shaffer stated that this 13.36% ratio is an increase of two full percentage points over that actually achieved in the past and that there is no evidence that this is remotely possible much less that it is reasonably probable.

Aside from witness Shaffer's opinion as to the inaccuracy of the Public Staff's estimate based on historical "business as usual" calculations, the Company reminded the Commission of the uncertainty arising from the fact that after January 1, 1984, the present method of divisions of toll revenues will be replaced with an entirely new and yet unknown system. The Company pointed out that it would no longer have any contracts with Southern Bell or AT&T providing for a method of dividing toll revenue that will exist after January 1, 1984. The amounts of revenue, whether it will be obtained by pooling as in the past, by access charges to carriers, by end user charges, by billing and keeping toll revenues, are all unknown. Without knowing how these questions will be answered, the Company believes that neither the Company, the Public Staff, nor the Commission is in a position of being able to make any reasonable assumptions as to what will happen to the existing levels of toll revenue after January 1, 1984. The Company submitted that the only reasonable assumption that can be made is that somehow Mid-Carolina will receive the same revenues as it received in the test year.

Ordering Paragraph 9 of the Recommended Order (Docket No. P-100, Sub 64) specified that each company that had a rate case pending before the Commission's final decision in the toll rate case proceeding would consider the additional toll revenues in its rate case. This Ordering Paragraph affected the following Companies: Southern Bell, Continental of North Carolina, Mid-Carolina, and Heins. In addition, the Recommended Order (Docket

No. P-100, Sub 64) specified that, for certain companies that did not have rate cases pending, they would establish a deferred account in which the intrastate toll revenues derived from the approved toll rate increases would be placed, with the provision, among other provisions, that the deferred account revenues would be considered in any rate case filed within the next 12 months. Company witness Shaffer recommended that the Commission should in this case establish local service rates without regard to the increase in toll rates, order the Company to establish a deferred account into which any increased revenues over the level used in fixing the local rates be placed, and at the end of a year order the Company to refund any increased revenues to its customers.

Although the Commission recognizes that in Docket No. P-100, Sub 64, it was determined that Mid-Carolina would receive additional annual revenues of $656,274 as a result of the increase in intrastate toll rates granted in that proceeding, the Commission concludes that, based upon the evidence in this case and considering the uncertainties posed by deregulation and significant changes in the telecommunications industry, it is reasonable to find that the Company's level of intrastate toll revenues for purposes of this case should only be increased by 50% of the toll revenue increase granted in Docket No. P-100, Sub 64. Furthermore, Mid-Carolina is hereby directed to establish a deferred account and to place in said deferred account any intrastate toll revenues in excess of $328,137 which the Company derives from the toll rate increases granted in Docket No. P-100, Sub 64. As previously stated in the Commission Order entered in Docket No. P-100, Sub 64, on September 14, 1983, the appropriate rate-making treatment to be accorded to any toll revenues placed in such deferred account will be considered by the Commission in the context of a further hearing to be held within the next year. The Commission considers this procedure to be fair to both Mid-Carolina and its ratepayers in view of the uncertainties which are today present in the telecommunications industry.

The remaining difference of $89,471 is due to witness Lam's adjustment to increase toll revenues to reflect the impact of the difference in the levels of depreciation expense and interest expense used by witness Gerringer in the toll settlement calculation and the amounts later determined by the Public Staff to be the proper amounts. Furthermore, witness Lam made an adjustment of $25,299 to decrease the amount determined in the toll settlement calculation to reflect the Public Staff's position on rate base.

Company witness Shaffer, in his rebuttal testimony, accepted witness Lam's $25,299 reduction in toll revenues for the toll effects of her adjustments to the Company's originally proposed rate base since the Company accepted the Public Staff's position on rate base, but made no mention of the $89,471 addition to toll revenues for the toll effects of the Public Staff's depreciation and interest expense adjustments. Since witness Gerringer calculated his end-of-period toll revenues based upon the expenses and rate base originally proposed by the Company, it is necessary to reflect the toll revenue effects of any adjustments made to both rate base and expense items affecting toll.

In Evidence and Conclusions for Findings of Fact Nos. 5, 7, and 8, the Commission has adopted the Public Staff's proposed amounts for original cost rate base, operating revenue deductions other than taxes, and capital structure; therefore, the Commission finds that it is proper to add $64,172

($89,471 - $25,299) to the $7,068,160 amount of toll settlement revenues calculated by witness Gerringer to reflect the proper levels of rate base, depreciation expense, and interest expense.

Based upon the decisions herein, the Commission finds that the appropriate level of end-of-period gross intrastate toll revenues for inclusion in this proceeding is $7,460,469, consisting of revenues from: toll settlement calculation of $7,068,160, plus rate increase from Docket No. P-100, Sub 64, of $328,137, plus toll effect of depreciation expense and interest expense adjustments of $89,471, less toll effect of rate base adjustments of $25,299.

In summary, the Commission concludes that the proper end-of-period level of operating revenues for use herein is $24,315,316, made up of the following:

Item	Amount
Local service revenues	$16,128,910
Toll service revenues	7,460,469
Miscellaneous revenues	766,481
Uncollectibles	(40,544)
Total operating revenues	$24,315,316

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 7

The evidence concerning the proper end-of-period level of intrastate operating revenue deductions is found in the testimony and exhibits of Company witness Rowan and Public Staff witness Lam. The end-of-period level of operating revenue deductions proposed by each party is shown in the chart below. The amounts shown for the Company have been adjusted to reflect the effects of the Public Staff's adjustments which were accepted by witness Rowan at the hearing and the Public Staff amounts are in accordance with its Proposed Order.

Item	Company	Public Staff	Difference
Operating expenses	$10,037,395	$10,037,395	$ -
Depreciation and amortization	5,252,009	5,252,009	-
Operating taxes - other than income taxes	2,182,515	2,227,260	44,745
State income taxes	231,101	277,217	46,116
Federal income taxes	1,384,699	1,717,043	332,344
Total operating revenue deductions	$19,087,719	$19,510,924	$423,205

The Company and the Public Staff agree on the amounts of operating expenses and depreciation and amortization to be included in cperating revenue deductions. The Commission concludes, therefore, that operating expenses of $10,037,395 and depreciation and amortization of $5,252,009 are the appropriate amounts for use in this proceeding.

The first area of difference concerns operating taxes - other than income. Company witness Rowan contends that the appropriate amount of operating taxes other than income taxes for use in this proceeding is $2,182,515, while Public Staff witness Lam contends that the appropriate amount is $2,227,260. These amounts are made up of the following:

Item	Company	Public Staff	Difference
Payroll taxes	$ 194,271	$ 194,271	$ -
Property tax	553,347	553,347	-
Gross receipts tax	1,431,611	1,476,356	44,745
Other taxes	3,286	3,286	-
Total operating taxes - other than income taxes	$ 2,182,515	$ 2,227,260	$ 44,745

As can be seen from the chart above, the entire difference between the amount of operating taxes other than income taxes shown for the Company and the Public Staff is in the calculation of gross receipts tax. The $44,745 difference in gross receipts tax is the result of the $745,745 difference in the end-of-period toll revenues shown by the Company and those shown by the Public Staff. Since the Commission has previously concluded, in Finding of Fact No. 6, that the proper end-of-period level of operating revenues is $24,315,316, then the proper level of gross receipts tax is $1,456,668. This $1,456,668 amount of gross receipts tax is based upon local revenues of $16,128,910, toll revenues of $7,460,469, and directory revenues of $688,419. There being no evidence to the contrary, the Commission concludes that the amounts for payroll taxes, property tax, and other taxes as agreed to by the Company and the Public Staff are the proper amounts. Thus, the proper level of operating taxes - other than income for use in this proceeding is $2,207,572.

The remaining areas of difference are state and federal income taxes. The total difference is $378,460 and results from differences in the levels of operating revenues, and operating revenue deductions and interest expense used by the Company and the Public Staff in computing their respective levels of state and federal income taxes.

The Commission has determined and discussed the proper level of rate base, operating revenues, and operating revenue deductions in Evidence and Conclusions for Findings of Fact Nos. 5, 6, and 7 and discusses the proper capital structure and embedded cost rates in Evidence and Conclusions for Findings of Fact Nos. 8 and 9. Based upon the Commission's findings herein, the Commission concludes that the proper amount of interest expense to be used in calculating income taxes for rate-making purposes is $2,506,509 which includes a reduction for the imputed interest expense associated with the Job Development Investment Tax Credit (JDITC). Therefore, the Commission finds that the proper levels of state and federal income taxes for use in this proceeding are $258,710 and $1,583,670, respectively. The Commission wishes to acknowledge that its calculation of the level of federal income taxes reflected herein is consistent with the requirements of Internal Revenue Code Section 168(e)(3) as to normalization accounting.

In summary, the Commission concludes that the proper level of intrastate operating revenue deductions for use in this proceeding is $19,339,356, made up of the following:

Item	Amount
Operating expenses	$10,037,395
Depreciation and amortization	5,252,009
Operating taxes - other than income taxes	2,207,572
State income tax	258,710
Federal income tax	1,583,670
Total operating revenue deductions	$19,339,356

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 8 AND 9

Two witnesses presented evidence regarding the appropriate capital structure, cost of capital, and the fair rate of return. The Company offered the testimony of Dr. Olson, economist and President of Olson & Company, Inc., a utility consulting firm. The Public Staff offered the testimony of witness Bowerman, Public Utility Financial Analyst of the Public Staff's Economic Research Division. Dr. Olson also testified in rebuttal to the testimony presented by witness Bowerman.

Witness Olson testified that the consolidated capital structure of Mid-Carolina's parent company, Mid-Continent Telephone Corporation (Mid-Continent) as of December 31, 1982, adjusted for full conversion to equity of all outstanding preferred and debt securities, was appropriate for use in determining Mid-Carolina's cost of capital in this case. The capital structure ratios, as recommended by Dr. Olson, were 58.39% long-term debt, 4.71% preferred stock, and 36.90% common equity. An embedded cost of long-term debt of 9.13% and an embedded cost of preferred stock of 7.45% results from the use of this capital structure.

Witness Olson recommended that the Company should be allowed to earn an overall return in the range of 11.77% to 11.95%. The recommendation of witness Olson was based on a cost of equity of 16.5% to 17.0%. In deriving his recommendation, witness Olson used the cost of equity to Mid-Carolina's parent, Mid-Continent, as a proxy for the cost of equity to Mid-Carolina. This approach was used because, being a wholly owned subsidiary of Mid-Continent, Mid-Carolina's shares are not publicly traded and, consequently, no market information exists which could be used to determine the investor-required return for Mid-Carolina.

Witness Olson first estimated the cost of equity capital to Mid-Continent by using the Discounted Cash Flow (DCF) Model and then compared his results with an interest premium study. From his DCF study, witness Olson derived a 15.4% to 15.9% "barebones" cost of equity. He performed a similar analysis on a group of companies of comparable risk and estimated the cost of equity capital for those companies to fall between 15.2% and 15.7%.

Further, witness Olson adjusted his cost of equity range to 16.5% - 17.0% to allow for financing costs and possible market breaks. Witness Olson testified that an adjustment for financing costs was necessary in order for the Company's market to book ratio to exceed 110%. Witness Olson determined from his interest premium study that the cost of equity capital for Mid-Continent was 17%. Due to the similarities between witness Olson's DCF calculations and his interest premium study results, he determined that a 16.5% to 17.0% cost of equity capital range for Mid-Carolina was reasonable.

Witness Bowerman recommended an overall rate of return of 10.70%, based on a cost of equity of 14.40%. The capital structure he employed was the actual consolidated capital structure of Mid-Continent as of June 30, 1983. The capital structure consisted of 58% long-term debt, 8% preferred stock, and 34% common equity. Witness Bowerman did not make an adjustment for convertibles. Witness Bowerman testified that it is improper to assume full conversion for several reasons: first, he cited G. S. 62-133(c) which allows for consideration of known and actual changes but not of anticipated changes after the close of the hearing; second, the cost rates of long-term debt and preferred are not actual and are incorrect if convertibles are ignored in those cost rates; third, the Company is adequately compensated for conversion risk through its higher cost of equity than if convertibles were not present; fourth, another subsidiary of Mid-Continent, Sandhill Telephone Company, was not allowed full conversion in its last rate case (Docket No. P-53, Sub 47); and fifth, if there is substantial conversion of convertibles in the future, Mid-Carolina is free to return to this Commission and have the changes in its capital structure recognized as a known and actual change. Consistent with his use of the actual capital structure, witness Bowerman employed an embedded cost of long-term debt of 8.95% and an embedded cost of preferred stock of 7.65%.

Witness Bowerman determined the cost of equity for Mid-Continent by employing two methods, the DCF and Capital Asset Pricing Model (CAPM). His DCF results ranged from 13.60% to 14.95% for Mid-Continent and from 12.97% to 15.43% for a comparable risk group. He then estimated the expected return on the market at 15.5% and concluded that a company afforded the protection of a regulated public utility would certainly have lower risk than a comparable nonregulated entity and thus would expect a lower return. On this basis the CAPM result was 14.0%.

Based upon the results of his CAPM and the DCF methodologies, witness Bowerman concluded that the reasonable cost of equity to the Company was in the range of 14.0% to 14.50%. In order for the Company to be adequately compensated for its flotation costs, witness Bowerman made an upward adjustment of 15 basis points to the midpoint of his recommended cost of equity range. Thus, the recommended cost of equity that witness Bowerman proposed be employed for Mid-Carolina was 14.40%.

In rebuttal testimony, Company witness Olson stated his opinion that by applying witness Bowerman's overall rate of return to the book capital structure of Mid-Carolina the allowed return on equity would be insufficient. However, when witness Olson was asked under cross-examination if the book capital structure of Mid-Carolina reflected the use of double leverage, he stated that there was some but he did not know how much. Also, witness Olson stated under cross-examination that the assets of Mid-Continent are financed with 58% debt, 8% preferred stock, and 34% common equity and that the correct capital structure in determining Mid-Continent's cost of capital is its consolidated capital structure.

With respect to the issue of the appropriate capital structure for use in this proceeding, the Commission concludes that the actual consolidated capital structure at June 30, 1983, is appropriate for use in this proceeding which is as follows:

Item	Percent
Long-term debt	58.00%
Preferred stock	8.00%
Common equity	34.00%
Total	100.00%

The Commission notes that this capital structure is more current than the one advocated by witness Olson. Moreover, the Commission finds that it would be inappropriate to use a proformed capital structure which assumes the conversion to equity of all convertible securities. In the Commission's view, witness Olson's primary justification for full conversion, to wit, his opinion that there would be substantial conversions in the future, is an insufficient basis upon which to adopt his recommended full conversion approach. In this regard it is noteworthy that witness Olson admitted that the Series D no par redeemable preferred convertible issue, which he predicted holders would find advantageous to convert when the common dividend reached $1.96, was larger than all of the other five convertible issues combined. Given that the present dividend rate is only $1.80, conversion of that largest issue does not appear to be likely.

The Commission further concludes that the appropriate embedded cost rate for long-term debt is 8.95% and that the appropriate embedded cost rate for preferred stock is 7.65%.

The determination of the appropriate fair rate of return for the Company is of great importance and must be made with great care because whatever return is allowed will have an immediate impact on the Company, its stockholders, and its customers. In the final analysis, the determination of a fair rate of return must be made by this Commission, using its own impartial judgment and guided by the testimony of expert witnesses and other evidence of record. Whatever return is allowed must balance the interest of the ratepayers and investors and meet the test set forth in G. S. 62-133(b)(4):

"Fix such rate of return... as will enable the public utility by sound management to produce a fair return for its shareholders, considering changing economic conditions and other factors, as they then exist, to maintain its facilities and services in accordance with the reasonable requirements of its customers in the territory covered by its franchise, and to compete in the market for capital funds on terms which are reasonable and which are fair to its customers and to its existing investors."

The return allowed must not burden ratepayers any more than is necessary for the utility to continue to provide adequate service. The North Carolina Supreme Court has stated that the history of G. S. 62-133(b):

"...supports the inference that the Legislature intended for the Commission to fix rates as low as may be reasonable consistent with the requirements of the Due Process Clause of the Fourteenth Amendment to the Constitution of the United States..." State ex rel. Utilities Commission v. Duke Power Company, 285 N.C. 377, 206 S.E. 2d 269 (1974).

Based upon the foregoing and the entire record in this docket, the Commission finds and concludes that if Mid-Carolina's service were adequate, the fair rate of return that it should have the opportunity to earn on the original cost of its rate base is 11.07%. Such fair rate of return would yield a fair return on common equity of approximately 15.50%. However, the Commission has found that the Company's service is inadequate.

In the Company's last general rate increase occurring June 17, 1982, in Docket No. P-118, Sub 22, the Commission penalized the Company 1% on its common equity return as a result of poor service. The Commission finds that, since Mid-Carolina's last rate increase, service has improved but it is still below the level at which the Commission can find that the quality of service is adequate. Such improvement in service is due to various upgrading activities of the Company such as: line and terminal additions in the Old Town area exchanges and the Columbus area exchanges, trunk additions in the Matthews area exchanges, addition of 109 EAS trunks in the Old Town area exchanges, replacement of all of the physical trunks handling EAS and toll that were served by cable pairs with electronic or T-carrier type of facility in the Old Town area, and elimination of all the physical trunks handling EAS in the Columbus area by putting them on T-carrier type of facility. Also, the Company expects to cut over to digital switching systems in Mooresville late in 1983, in Old Town during December 1983, in King during January 1984, and in Matthews during July 1984. As a result of such service improvements, the Commission finds that the Company should only be penalized .5% in this proceeding.

The Commission cannot ignore the inadequacies of the present service provided by the Company to its ratepayers. The Commission, therefore, concludes that a fair and reasonable return on common equity for Mid-Carolina is 15.00% resulting in an overall rate of return of 10.90%. Although this overall rate of return is less than that which the Commission would have found to be reasonable if service had been adequate, the net operating income which will be produced by application of the schedule of rates necessary to produce the approved overall rate of return will be sufficient to cover all of Mid-Carolina's fixed charges and preferred dividends and provide a substantial increase in its return on common equity. Based upon the present service level, the Commission concludes that any higher rate of return on original cost net investment would be unjust and unreasonable.

The Commission cannot guarantee that the Company will, in fact, achieve the level of returns herein found to be just and reasonable. Indeed, the Commission would not guarantee it if it could. Such a guarantee would remove necessary incentives for the Company to achieve the utmost in operational and managerial efficiency. The Commission believes, and thus concludes, that the level of returns approved herein will permit the Company to improve the quality of its service and also afford it a reasonable opportunity to earn a reasonable and fair return for its stockholders.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 10

The Commission has previously discussed its findings and conclusions concerning the fair rate of return which Mid-Carolina Telephone Company should be given the opportunity to earn.

The following schedules summarize the gross revenues and the rates of return which the Company should have a reasonable opportunity to achieve, based upon the increases approved herein. The schedules, illustrating the Company's gross revenue requirements, incorporate the findings and the conclusions heretofore and herein made by the Commission.

SCHEDULE I
MID-CAROLINA TELEPHONE COMPANY
North Carolina Intrastate Operations
STATEMENT OF OPERATING INCOME
Twelve Months Ended December 31, 1982

	Present Rates	Increase Approved	After Approved Increase
Operating Revenues:			
Local service revenues	$16,128,910	$1,504,816	$17,633,726
Toll service revenues	7,460,469	-	7,460,469
Miscellaneous revenues	766,481	-	766,481
Uncollectible revenues	(40,544)	(3,611)	(44,155)
Total operating revenues	24,315,316	1,501,205	25,816,521
Operating Revenue Deductions			
Operating expenses	10,037,395		10,037,395
Depreciation and amortization	5,252,009		5,252,009
Operating taxes - other than income taxes	2,207,572	90,000	2,297,572
State income tax	258,710	84,672	343,382
Federal income tax	1,583,670	610,205	2,193,875
Total operating revenue deductions	19,339,356	784,877	20,124,233
Net operating income for return	$ 4,975,960	$ 716,328	$ 5,692,288

SCHEDULE II
MID-CAROLINA TELEPHONE COMPANY
North Carolina Intrastate Operations
STATEMENT OF RATE BASE AND RATE OF RETURN
Twelve Months Ended December 31, 1982

	Present Rates	After Approved Rates
Investment in Telephone Plant:		
Telephone plant in service	$79,375,872	$79,375,872
Telephone plant under construction	3,066,945	3,066,945
Depreciation reserve	(23,410,881)	(23,410,881)
Customer deposits	(93,347)	(93,347)
Pre-1971 investment tax credit	(74,998)	(74,998)
Accumulated deferred income taxes	(7,483,117)	(7,483,117)
Net investment in telephone plant	51,380,474	51,380,474
Allowance for Working Capital		
Cash working capital	458,031	458,031
Materials and supplies	369,953	369,953
Total allowance for working capital	827,984	827,984
Original Cost Rate Base	$52,208,458	$52,208,458
Rate of return:	9.53%	10.90%

SCHEDULE III
MID-CAROLINA TELEPHONE COMPANY
North Carolina Intrastate Operations
STATEMENT OF CAPITALIZATION AND RELATED COSTS
December 31, 1982

Item	Ratio %	Original Cost Rate Base	Embedded Cost %	Net Operating Income
	Present Rates - Original Cost Rate Base			
Long-term debt	58.00	$30,280,906	8.95	$2,710,141
Preferred stock	8.00	4,176,676	7.65	319,516
Common equity	34.00	17,750,876	10.96	1,946,303
Total	100.00	$52,208,458	-	$4,975,960
	Approved Rates - Original Cost Rate Base			
Long-term debt	58.00	$30,280,906	8.95	$2,710,141
Preferred stock	8.00	4,176,676	7.65	319,516
Common equity	34.00	17,750,876	15.00	2,662,631
Total	100.00	$52,208,458	-	$5,692,288

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 11

Company witnesses Shettel and Public Staff witness Willis presented testimony concerning Mid-Carolina's proposed rate structure.

Company witness Shettel testified that he had designed the Company's proposed rates and charges to: (1) establish prices for the Company's services which are equitable and reasonable to the customer, meet the public need, and which are consistent with the Company's policies; (2) distribute the additional required revenue among its customers equitably while attempting to minimize the impact on the basic local exchange customer; and (3) meet the financial needs of the Company by generating the required additional annual revenues.

The Company filed tariffs with its application which it asserted would produce $2,098,734 in additional annual revenue. Witness Shettel proposed increases in the Company's local exchange rates, nonrecurring service charges, maintenance of service charges, key and pushbutton telephone service rates, auxiliary equipment rates, and local obsolete service offering rates.

The Public Staff presented specific recommendations on the Company's proposed rate structure through its witness Willis. Witness Willis expressed his recommendations on the Company's proposal to change the calling scope limit between two rate groups, to alter an existing rate relationship, to increase service charge rates, to increase extension and local private line mileage charges, to increase standard telephone set charges, and to increase the maintenance of service charges.

Witness Willis agreed with the Company's proposal to redefine its calling scope boundary between rate groups 7 and 8 from 197,000 access lines to 215,000. Witness Willis commented that this proposal will permit the distinction in rates allowed by the Commission in Docket No. P-118, Sub 22, between Matthews, Hemby Bridge, Indian Trail, and Waxhaw to be maintained.

It was witness Willis' testimony that the Company's proposal to increase its key trunk multiple from 1.25:1 to 1.5:1 should be allowed with the provision that the application of its key trunk rate be redefined. It was his belief that the predominate benefit which may be included in the use of a key trunk relates to the rotary line aspect of the service. He remarked that other advantages sometimes attributed to the use of key trunks such as a greater completion rate on outgoing calls are enabled by the use of busy line light indicators. According to witness Willis the busy line light indications are paid for through charges for both multibutton instruments and key system common equipment. It was witness Willis' further recommendation that the key trunk rate be only applicable to access lines which receive rotary line service other than those which qualify for the PBX trunk rate.

Public Staff witness Willis stated that his review of the Company's proposed service charges indicated that they were generally similar to rates approved by the Commission in recent proceedings. He cited the minimum proposed cost of connection to be $29.00 and recommended that the Company's proposed rates be approved.

The Company proposed increases in key and pushbutton telephone service, auxiliary equipment, and local obsolete services of $364,197. According to witness Willis all of these proposed increases are associated with station telephone instrument charges with the majority relating to the proposed increases in the rotary and touchtone telephone units. The witness remarked that these specific proposals would raise the standard rotary and touchtone telephone monthly rates from $1.00 and $1.50 to $1.25 and $2.10 per month,

respectively. Witness Willis stated that the Company's proposal would cause its standard telephone rates to be comparable to other companies' rates and he recommended that the proposed rates be approved.

The Company proposed to increase its nonrecurring maintenance of service charge of $12.00 which applies when a test from the Company's test board identifies the subscriber's customer-provided terminal equipment as having caused the trouble and is in need of repair. The Company proposed to increase this charge to $20.00 per incident. It also proposed to increase its minimum maintenance of service charge of $24.00 for a visit of two hours or less to $40.00 and its charge of $12.00 per man hour for the time spent on the premises in excess of two hours to $20.00 per man hour.

Witness Willis recommended that the $12.00 charge which applies to trouble in the subscriber's customer-provided terminal equipment identified from the test board remain unchanged and a minimum charge of $20.00 be applied to each repair visit of one man hour or less with additional repair time exceeding one hour to be billed at a rate of $20.00 per man hour.

The Commission, having carefully considered all the evidence regarding the rate design proposals presented in this proceeding, makes the following conclusions:

A. REGROUPING OF EXCHANGES

The Commission concludes that the Company's proposal to increase the calling scope limit between rate group 7 and 8 from 197,000 to 215,000 access lines is a prudent way to maintain the rate separation allowed in Docket No. P-118, Sub 22, and should be implemented.

B. KEY TRUNK MULTIPLE CHANGE

The Commission concludes that the key trunk rate should only be applicable to access lines which receive rotary line service (other than those which qualify for the PBX trunk rate) and the multiple of 1.5:1 should exist between the key trunk and business one-party line access exchange rates.

C. SERVICE CHARGES

The Commission concludes that the service charges shown below are proper and therefore should be implemented by the Company.

SERVICE CONNECTION CHARGES

I. Residential Rates	
A. Service order	
1. Primary	$19.00
2. Secondary	10.00
B. Premises visit, each	8.00
C. Central office work, each	10.00
D. Inside wiring, each	10.00
E. Equipment work, each	5.00
F. Jack outlet	5.00
II. Business Rates	
A. Service order	
1. Primary	24.00
2. Secondary	15.00
B. Premises visit, each	8.00
C. Central office work, each	10.00
D. Inside wiring, each	15.00
E. Equipment work, each	7.00
F. Jack outlet	5.00

D. EXTENSION AND LOCAL PRIVATE LINE MILEAGE CHARGES

Having carefully considered the evidence in this proceeding concerning mileage rates, the Commission concludes that the mileage charges for both extension line mileage and local private line mileage should be set at $2.50 per quarter mile per month.

E. STANDARD TELEPHONE SET CHARGES

The Commission concludes that the standard rotary and touchtone telephone rates should be set at $1.25 and $2.10 per month, respectively.

F. MAINTENANCE OF SERVICE CHARGES

The Commission concludes that a nonrecurring charge of $12.00 for the identification of trouble caused by a subscriber's customer-provided terminal equipment and the nonrecurring charge of $20.00 to apply for each repair visit of one man hour or less to a customer's premises with additional repair time exceeding one hour to be billed at the rate of $20.00 per man hour is just and reasonable.

G. OTHER LOCAL SERVICES - RATES AND CHARGES

The Commission concludes that all rates and charges proposed by the Company other than local exchange rates not herein prescribed are reasonable and should be approved.

H. DISTRIBUTION OF ADDITIONAL REVENUE REQUIREMENT

Based upon the preceding conclusions on rate design the additional revenues approved will produce the annual revenue increases shown below:

Category of Service	Annual Revenue Increase
Basic local exchange service	$ 985,099
Service charges	154,338
Key and pushbutton telephone services	4,011
Auxiliary equipment	359,472
Local private line service	1,182
Local obsolete services	714
Total	$1,504,816

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 12

The evidence and conclusions relating to the appropriate length of the engineering interval for digital central offices is contained in the testimony of Public Staff witness Sutton.

Witness Sutton stated that during the course of his investigation he discovered that Mid-Carolina was engineering its digital central offices on the basis of a three-year engineering interval. Witness Sutton stated that the engineering interval for a digital central office should not exceed one year. According to witness Sutton, other telephone companies in North Carolina are limiting the engineering period for digital central offices to one year or less.

Witness Sutton indicated that the modularity of digital switching systems lend themselves to a shorter engineering period than was prudent for the older electro-mechanical switching systems. Further, the witness stated that it would be inappropriate for him to propose an adjustment to telephone plant in service since Mid-Carolina has not placed any of these digital central offices in service and thus the excess investment is not included in the Company's rate base. However, witness Sutton indicated that if the Company should include this excess investment in some future rate case, he would recommend an adjustment to remove it from plant in service for rate-making purposes.

Mid-Carolina did not present direct testimony addressing this subject. Nor did the Company attempt to discredit witness Sutton's testimony on the length of the engineering interval through cross-examination questions. The Company offered no rebuttal testimony in opposition to witness Sutton's recommendation of limiting the engineering interval for digital central offices to one year. Based upon these facts, the Commission concludes that the Company is unable to justify an engineering interval in excess of one year.

The Commission is acutely aware that deregulation and competition are causing escalating basic service rates. Also, the Commission is aware of its statutory obligation to require public utilities to furnish efficient service at reasonable rates. Further, allowance of telephone plant in a utility's rate base that is not used and useful in a reasonable period of time prevents the Commission from fulfillment of its statutory obligation to the ratepayers of North Carolina. Based upon the foregoing discussion, the Commission establishes the maximum engineering interval for a digital central office to be one year for Mid-Carolina.

IT IS, THEREFORE, ORDERED as follows:

1. That the Applicant, Mid-Carolina Telephone Company be, and hereby is, authorized to increase its local service rates and charges so as to produce

annual gross revenues of $25,860,676 from North Carolina subscribers based on test year operations. Such amount represents an increase of $1,504,816 above the revenue level that would have resulted from rates currently in effect based on the test year.

2. That the Applicant is hereby called upon to propose specific tariffs reflecting changes in rates, charges, and regulations to recover the revenues approved herein, in accordance with the guidelines established by this Commission in Evidence and Conclusions for Finding of Fact No. 11, within 10 days from the date of this Order. These proposals and workpapers supporting such proposals shall be provided to the Commission (five copies are required) and the Public Staff (formats such as Item 30 of the minimum filing requirement, N.C.U.C. Form P-1, are suggested). At the time of such filing, the Company shall also file with the Commission a proposed customer notice to inform the customers of Mid-Carolina Telephone Company of the actions taken herein.

3. That the Public Staff may file written comments concerning the Company's tariffs within five days of the date on which they are filed with the Commission.

4. That the rates, charges, and regulations necessary to produce the annual gross revenues authorized herein shall become effective upon the issuance of a further Order approving the tariffs and customer notice filed pursuant to ordering paragraph 2 above.

5. That the Applicant should improve the quality of service currently being provided to its subscribers and take appropriate steps to remedy the service problems described herein.

6. That the Company shall conduct investigations, including traffic studies, and take the corrective actions which are specified in the Evidence and Conclusions for Finding of Fact No. 4 of this Order and shall file its reports of those actions with the Commission within 60 days from the date of this Order.

7. That the Applicant shall file with the Clerk of the Commission within 120 days after the effective date of this Order a report detailing all the procedures which it plans to follow in charging investment and expenses to its unregulated operations. Said report should detail each item to be charged or allocated, the basis on which it is to be charged or allocated, the procedures used to determine the amount to be charged, and an explanation of why each procedure is appropriate, as detailed in the Evidence and Conclusions for Finding of Fact No. 5.

ISSUED BY ORDER OF THE COMMISSION.
This the 13th day of December 1983.

NORTH CAROLINA UTILITIES COMMISSION
Sandra J. Webster, Chief Clerk

(SEAL)

DOCKET NO. P-53, SUB 47

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Application of Sandhill Telephone Company for an Adjustment of Its Rates and Charges) RECOMMENDED ORDER) GRANTING PARTIAL) RATE INCREASE

HEARD IN: Commission Hearing Room, Dobbs Building, 430 North Salisbury Street, and in the Municipal Building in Aberdeen, North Carolina, on March 9 and 10, 1983

BEFORE: Hearing Examiner Wilson B. Partin, Jr.

APPEARANCES:

For the Company:

F. Kent Burns, Boyce, Mitchell, Burns & Smith, P. O. Box 2479, Raleigh, North Carolina 27602

For the Intervenor:

Gisele Rankin, Staff Attorney, The Public Staff, P. O. Box 991, Raleigh, North Carolina 27602
For: The Using and Consuming Public

PARTIN, HEARING EXAMINER: On November 12, 1982, Sandhill Telephone Company (Sandhill, the Company, or Applicant) filed an application with the Commission seeking to adjust and increase rates and charges for local service to its North Carolina subscribers. The proposed rates and charges were designed to produce total annual gross revenues of $1,716,703 or an increase of $456,828 when applied to a test period consisting of the 12 months ended June 30, 1982. The Company requested that such rates be allowed to become effective on December 15, 1982.

By Order issued on December 10, 1982, the Commission declared the application to be a general rate case pursuant to G. S. 62-137; suspended the proposed rates for a period of 270 days; set the matter for hearing; required Sandhill to give notice of hearing by publication and bill inserts; established the test period to be used in the proceeding; and required protests or interventions to be filed in accordance with the Commission Rules and Regulations.

The Commission conducted a hearing specifically for the purpose of receiving testimony from members of the using and consuming public with regard to Sandhill's proposed rate increase. A hearing was held in Aberdeen at 11:00 a.m., on March 9, 1983. One public witness, Linda Bowles, testified at this hearing on behalf of the Pine Hill Apartments, a Senior Citizens complex located in Aberdeen.

The Applicant went forward with its case when the hearing resumed in Raleigh at 9:30 a.m., on March 10, 1983, offering the testimony and exhibits of the following witnesses: Archie A. Thomas, President of Sandhill Telephone

Company; Franklin D. Rowan, Regional Controller - Mid-Continent Telephone Service Corporation; Lawrence S. Pomerantz, Director - Rates and Revenues for Mid-Continent Telephone Service Corporation; and John D. Russell, President of John D. Russell Associates, Inc.

The Public Staff offered the testimony and exhibits of the following witnesses: Hugh L. Gerringer, Engineer - Communications Division; Thi-Chen Hu, Engineer Communications Division; William J. Willis, Engineer - Communications Division; Julie Jacome, Accountant - Accounting Division; Leslie C. Sutton, Engineer - Communications Division; and George T. Sessoms, Jr., Public Utility Financial Analyst - Economic Research Division.

Based on the foregoing, the evidence adduced at the hearings and the entire record in this matter, the Hearing Examiner now makes the following

FINDINGS OF FACT

1. The Applicant, Sandhill Telephone Company, is a duly organized North Carolina corporation and a wholly owned subsidiary of Mid-Continent Telephone Corporation. Sandhill is a public utility engaged in providing telephone service to part of Moore County and Scotland County, and, as such, is subject to theis proceeding, pursuant to G.S. 62-133, for a determination of the justness and reasonableness of its proposed rates and charges.

2. In its original application, Sandhill requested rates designed to produce total annual revenues of $1,716,703, based on a test year ending June 30, 1982. The Company contended in its application that revenues under present rates were $1,259,875, thereby necessitating an increase of $456,828, which the Company proposes to achieve through increases in rates for local service.

3. The test period for purposes of this proceeding is the 12 months ended June 30, 1982.

4. The overall quality of service provided by Sandhill is adequate.

5. The depreciation rates as shown in Appendix A, which will result in an annual expense of $249,779, based on plant-in-service as of the end of the test period, are just and reasonable and appropriate for use in this proceeding.

6. Sandhill's reasonable original cost rate base used and useful in providing telephone service within the State of North Carolina is $3,742,490. This rate base consists of telephone plant in service of $4,835,658, average materials and supplies of $24,820, and an allowance for working capital of $21,936, reduced by accumulated depreciation of $926,364, accumulated deferred income taxes of $186,296, pre-1971 investment tax credit of $4,147, and customer deposits of $23,117.

7. Sandhill's total end-of-period operating revenues for the test year, under present rates and after accounting and pro forma adjustments, are $1,421,918.

8. The reasonable level of test year operating revenue deductions for Sandhill after end-of-period and pro forma adjustments is $1,069,223.

9. The capital structure appropriate for use in this proceeding is as follows:

Long-term debt	58.71%
Preferred stock	8.34%
Common equity	32.95%
Total	100.00%

The proper embedded costs of debt and preferred stock are 9.11% and 7.66%, respectively.

10. The overall rate of return to be applied to Sandhill's original cost rate base is 11.09%. Such rate of return will allow Sandhill the opportunity to earn a 15.50% return on its common equity and will enable the Company, by sound management, to produce a fair return for its shareholders, to maintain its facilities and service in accordance with the reasonable requirements of its customers, and to compete in the market for capital on terms which are reasonable to the customers and to existing investors.

11. The total annual revenue requirement for Sandhill is $1,554,250. This necessitates an annual gross revenue increase of $131,266. Such revenue increase will allow the Company the opportunity to earn the rate of return on its rate base which the Commission has found just and reasonable. This revenue requirement is based upon the original cost of Sandhill's property and its reasonable test year operating revenues and expenses as previously set forth in these findings of fact.

12. The rate structure proposed by Sandhill, as modified by the findings herein, is just and reasonable.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 1, 2, AND 3

The evidence for these findings of fact is contained in the verified application, the Commission's Order Setting Hearing, and in the testimony and exhibits of Company witnesses Thomas and Rowan. These findings are essentially informational, procedural, and jurisdictional in nature and were uncontested.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 4

The evidence for this conclusion is contained in the testimony of public witness Linda Bowles, the testimony of Company witness Thomas, and the testimony and exhibits of Public Staff witness Hu.

Witness Bowles testified specifically concerning the magnitude of the requested increase and the burden that such an increase would place on the elderly fixed income telephone subscribers of Sandhill Telephone Company. Witness Linda Bowles testified, however, that she had been very fortunate to have good telephone service in Aberdeen.

Company witness Thomas testified that the Company was continuously striving to provide good telephone service to all areas it served, that the Company's

reported trouble index during the test year had been consistently below the trouble index objectives set by this Commission and that the operator answer time and directory assistance and repair service had also remained within the objectives of this Commission. Witness Thomas further testified that community feedback indicated that subscribers were receiving good service and that the Company was responsive to customer requests for new service and for changes in their existing service.

Public Staff witness Hu testified that his review consisted of field inspections and tests of switching and trunking facilities, measurements of the answer time of operators, directory assistance, repair service and business office, and an analysis of statistics relating to the Company's service. Based on his evaluation of all the test results and service data, witness Hu concluded that the overall quality of service provided by the Company failed to meet the due date objective for six months out of 12 in the year 1982. Witness Hu pointed out that the Company needed to improve its performance in meeting due dates.

Based on the foregoing evidence, the Hearing Examiner concludes that the overall quality of service provided by Sandhill Telephone Company is adequate. The Hearing Examiner, however, recognizes that the Company has not consistently met the due date objective and concludes that the Company should make a greater effort to meet due dates in the future.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 5

The evidence as to the appropriateness of the depreciation rates is contained in the testimonies and exhibits of Company witnesses Russell and Rowan and Public Staff witness Sutton. The depreciation rate increases proposed by witness Russell and the extraordinary retirements proposed by witness Rowan result in annual depreciation expense of $360,643, while the depreciation rate increases proposed by witness Sutton result in annual expenses of $249,779.

There are four points of disagreement between witness Sutton and the Company's witnesses:

1. Witness Russell's use of theoretical depreciation reserves;

2. Witness Russell's proposed service life and salvage parameters for certain plant accounts;

3. Witness Rowan's proposal to recover depreciation reserve deficiencies through extraordinary retirement treatment;

4. Witness Russell's proposal to implement ELG depreciation rates for plant placed in service on or after January 1, 1983.

Concerning the use of theoretical reserve distribution, witness Russell indicated that he believed that the depreciation reserve balances were not representative of the age distribution of the assets. He felt that some reserves were understated while others were overstated. For this reason, he calculated a theoretical depreciation reserve for each plant account.

Witness Sutton objected to the use of theoretical reserves for three reasons. First, he stated that the use of a theoretical depreciation reserve could artificially overstate a company's total depreciation expense. He supported this statement by calculating that $44,801, or 58%, of the total $77,195 depreciation expense increase sought by Sandhill is attributable to witness Russell's use of theoretical reserves. Second, witness Sutton stated that both the Commission and the FCC have rejected the use of theoretical reserves in favor of reserves based upon actual debits and credits. Specifically, in response to Public Notice No. 06219 (Initiation of Proceedings to Allocate Depreciation Reserve as Required by Docket No. 20188) issued by the FCC on January 23, 1981, the Commission filed comments with the FCC that stated:

> "... we believe that the most reasonable allocation of the current book reserve is through use of actual debits and credits attributable to the various plant accounts. This method assigns the reserve to each account in essentially the same manner in which the reserve was accumulated as opposed to the theoretical reserve allocation method which allocates the reserve based on current life estimates. Since a depreciation reserve was not accumulated on the basis of current account lives, it does not seem appropriate to now allocate the reserve on that basis."

Further, in its Supplemental Opinion and Order in Docket No. 20188 adopted on October 1, 1981, the FCC stated:

> "...(we) conclude that the historical recordation of debits and credits as required in Section 31.717 (c) of the FCC Rules and Regulations, 47 CFR 31.171 (c), should be the method by which the accumulated depreciation reserve is allocated to individual plant accounts and thereafter maintained."

Witness Sutton further stated that the Commission had previously addressed this issue in the context of a general rate case and had concluded that the use of a theoretical reserve is inappropriate. Specifically, in Docket No. P-10, Sub 400 (Central Telephone Company) the Commission issued an Order on September 21, 1981, in which it stated:

> "... the Commission concludes that the debits/credits approach to assigning the depreciation reserve to a specific plant account is preferred to using some theoretical means."

Based upon the foregoing discussion, the Hearing Examiner concludes that it is inappropriate to develop depreciation rates based upon the use of theoretical reserves. Therefore, the Hearing Examiner disapproves any and all depreciation rates that incorporate theoretical reserves in their development.

The second area of disagreement concerns the remaining life depreciation rates for the Company's 17 plant accounts. For discussion purposes in this Order, the 17 plant accounts are assembled into five groups.

The first group consists of the accounts for which witness Russell and witness Sutton are in agreement as to the remaining life depreciation rates. This group contains underground cable, aerial wire, and underground conduit. Since witness Russell and witness Sutton are in agreement for these accounts

and it appears that the rates are reasonable, the Hearing Examiner concludes that the depreciation rates for these three categories are appropriate for use in this proceeding.

The second category consists of the accounts for which Company witness Russell and Public Staff witness Sutton are in agreement as to the service lives and salvage parameters but disagree as to the reserve and thus the remaining life depreciation rates. Consistent with the decision regarding the use of theoretical reserves, the Hearing Examiner rejects the depreciation rates proposed by Company witness Russell for trunk carrier equipment, step-by-step equipment, buried cable, and tools and other work equipment. Accordingly, the Hearing Examiner finds that the depreciation rates proposed by witness Sutton for these four accounts to be just and reasonable and appropriate for use in this proceeding.

The third category consists of furniture and office equipment and vehicle accounts. Witness Sutton proposed 0% depreciation rates for these two accounts since the depreciation reserve for them has already exceeded the gross investment. The depreciation reserve for furniture and office equipment is 121.7% and the depreciation reserve for vehicles is 117%. Through use of theoretical reserves, witness Russell reassigns portions of the reserve in these accounts to other accounts, thus enabling him to justify depreciation rates for these two accounts. Consistent with the rejection of the use of theoretical reserves, the Hearing Examiner finds that the 0% depreciation rates proposed by the Public Staff for these two accounts are just and reasonable and appropriate for use in this proceeding.

The fourth category consists of those accounts for which witness Russell and witness Sutton are in disagreement on the parameters to be used in calculating depreciation rates. This category includes the following accounts: buildings, subscriber carrier equipment, digital equipment, station apparatus, large PBX, pole lines, and aerial cable. Both witness Russell and witness Sutton stated that the mortality data of Sandhill Telephone Company was insufficient for the development of depreciation rates for certain accounts. In those cases where insufficient mortality data existed, witness Russell relied upon service lives and salvage parameters consistent with industry averages in developing his recommended depreciation rates, while witness Sutton based his recommended depreciation rates upon the service lives and salvage parameters that underlie depreciation rates recently prescribed by the Commission for other telephone companies operating in North Carolina. The Hearing Examiner is of the opinion that in cases where there is insufficient mortality data for the development of depreciation rates for certain accounts, it is more appropriate to develop rates for those accounts utilizing the parameters underlying depreciation rates for telephone companies operating in this state rather than parameters underlying depreciation for telephone companies operating in other jurisdictions. Accordingly, the Hearing Examiner concludes that the depreciation rates proposed by witness Sutton for buildings, subscriber carrier equipment, digital equipment, station apparatus, large PBX, pole lines, and aerial cable are just and reasonable and appropriate for use in this proceeding.

The final group of accounts for which there is disagreement concerns station connections-other and station connections-inside. Company witness Russell presented no evidence to support the service lives and salvage parameters upon which his depreciation rates were based. Public Staff witness

Sutton stated that the depreciation rates he was recommending were established by the FCC in Docket No. 79-105 and are applicable to all telephone companies. The Commission is intimately familiar with FCC Docket No. 79-105 and has concurred with that decision in all instances where represcription has been requested for the station connections accounts. Accordingly, the Hearing Examiner finds the depreciation rate recommended by the Public Staff for station connections-other and station connections-inside to be just and reasonable and appropriate for use in this proceeding.

The third area of disagreement concerns the Company's proposal to recover $109,743 in depreciation reserve deficiencies through extraordinary retirements. The reserve deficiencies result from retirements to the step-by-step and large PBX equipment accounts. According to witness Rowan, the step-by-step and large PBX equipment in question was retired prior to the end of the test period and the reserve deficiency was reflected in the Company's existing depreciation reserve. Witness Sutton stated that since the retirements occurred prior to the end of the test period, the deficiency would be included in the accumulated depreciation reserve. Further, witness Sutton pointed out that the remaining life depreciation rates reflect the accumulated reserve, and thus depreciation rates include the impact of the reserve deficiency. Moreover, he stated that allowing a remaining life depreciation rate for these two accounts <u>and</u> allowing extraordinary retirement treatment amounts to allowing double recovery of the $109,743 investment.

It is clear to the Hearing Examiner that if the remaining life depreciation rates were developed using investment and reserve levels as of June 30, 1982, and if the retirements occurred prior to that time, then the reserve deficiencies are fully reflected in the depreciation rates. Additionally, if extraordinary retirement treatment is also allowed, then double recovery of the $109,743 investment would in fact occur. Further, the Hearing Examiner is of the opinion that the appropriate way to treat this reserve deficiency is through the methodology proposed by witness Sutton. Accordingly, the Company's request for extraordinary retirement treatment is denied.

The final area of disagreement concerns the Company's proposal to implement an ELG based depreciation procedure for plant additions made after January 1, 1983. Company witness Russell indicated that an ELG procedure could provide a better matching between capital consumption and capital recovery. Further, he stated that the FCC had approved the use of ELG for telephone companies in FCC Docket No. 20188.

Witness Sutton testified that he opposed the use of ELG based depreciation rates in this proceeding because of the practical problems associated with their implementation. Implementation of the Company's ELG proposal will result in rapid and continual expansion of the number of depreciation rates. For example, whereas the Company now has 17 depreciation rates to apply to its 17 plant accounts, 10 years after the establishment of the Company's proposed ELG system, there would be 187 depreciation rates to be applied to 187 portions of the investment in the Company's 17 plant accounts for use in calculating the Company's monthly depreciation expense. Witness Sutton further testified that Sandhill currently has inadequate record-keeping procedures and proposes to implement ELG initially on a manual basis. From an administrative perspective, the complexity of accounting for such a myriad of rates would be unreasonably burdensome for the Company, the Commission, and the Public Staff.

Witness Sutton summarized his position on the Company's ELG proposal as follows:

"My review of an ELG based capital recovery system leads me to the following conclusions. First of all, it is not apparent to me that the ELG procedure proposed by Sandhill will produce sufficient benefits to justify the extensive effort required to implement it. Also, there are serious questions as to whether or not the promises of ELG theory can be realized because of the necessity for accurate life projections and extensive records. It does not seem reasonable to establish a complex procedure when the benefits of that procedure are inherently limited by the accuracy of projections and offset by burdensome data and record keeping requirements. I think material improvements in the capital recovery process can be accomplished without having to resort to ELG. The use of RL offers a means to insure full capital recovery and is more manageable than ELG. In short, ELG introduces complexity unnecessary for adequate capital recovery by Sandhill Telephone Company."

The Hearing Examiner notes that the Company's current records are inadequate for purposes of developing depreciation rates, as is illustrated by the witnesses' use of other companies' experience as a starting point in the development of such depreciation rates. Witness Russell testified that implementation of the ELG procedure to date had been minimal because of the need for improved property records and for computer technology.

With regard to the FCC preemption issue, the Hearing Examiner notes that witness Russell testified and agreed on cross-examination that the authorization of the use of the ELG procedure by the FCC was on an optional basis.

Based on the foregoing the Hearing Examiner is of the opinion that good cause exists to deny the Company's requested approval of ELG at this time. As pointed out by witness Sutton in his testimony, a decision by the Commission disallowing Sandhill's use of ELG at this time does not impact the Company's revenue requirements. Withholding approval of ELG in this proceeding will give the Company time to develop the record keeping systems and to establish the data processing facilities needed to implement this complex depreciation procedure. Furthermore, after some time of experimentation with these procedures, the Company, the Commission, and the Public Staff will be in a better position to evaluate the Company's ability to make use of such a complicated procedure. Accordingly, the Hearing Examiner disapproves any and all ELG depreciation rates proposed in this docket.

Based on the foregoing, the Hearing Examiner concludes that the reasonable level of depreciation expense appropriate for use in this proceeding is $249,779.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 6

The evidence for this finding of fact is found in the testimony and exhibits of Company witnesses Rowan and Russell and Public Staff witnesses Jacome and Sutton. The chart below summarizes the amounts proposed by the Company and the Public Staff.

	Company	Public Staff	Difference
Telephone plant in service	$ 4,835,658	$4,835,658	$ -
Materials and supplies	24,820	24,820	-
Working capital allowance	21,936	21,936	-
Accumulated depreciation	(1,037,228)	(926,364)	110,864
Accumulated deferred income taxes	(186,296)	(186,296)	-
Pre-1971 investment tax credit	(4,147)	(4,147)	-
Customer deposits	(23,117)	(23,117)	-
Original cost rate base	$ 3,631,626	$3,742,490	$110,864

As can be seen from the chart above, the Company and the Public Staff are in agreement regarding all components of rate base with the exception of accumulated depreciation. There being no evidence to the contrary the Hearing Examiner finds telephone plant in service of $4,835,658, materials and supplies of $24,820, working capital of $21,936, accumulated deferred income taxes of $186,296, pre-1971 investment tax credit of $4,147 and customer deposits of $23,117 reasonable and proper for use herein.

The Company proposed $1,037,228 to be the proper level of accumulated depreciation, while the Public Staff proposed $926,364. The $110,864 difference is a result of several factors. The first factor is the different represcribed depreciation rates proposed by Company witness Russell and Public Staff witness Sutton. The Commission has previously addressed this issue in Finding of Fact No. 5, in which the Commission found the depreciation rates proposed by Public Staff witness Sutton to be appropriate for use in this proceeding.

The second factor attributing to the differing accumulated depreciation proposals is Company witness Rowan's annualization of depreciation expense relative to plant in service at December 31, 1982. Alternatively Ms. Jacome annualized depreciation expense relative to plant in service at June 30, 1982, the end of the test period. Witness Jacome testified that since the test period in this proceeding was not changed to the 12 months ended December 31, 1982, and since the related telephone plant in service, revenues, and expenses were not updated to the December 31, 1982, level, this adjustment should not be allowed for purposes of setting rates in this proceeding. Consequently, witness Jacome applied witness Sutton's proposed depreciation rates to plant in service at the end of the test period. The Hearing Examiner finds that depreciation expense should be annualized relative to plant in service as of the end of the test period, June 30, 1982.

The third factor contributing to the $110,864 difference in accumulated depreciation is the Company's adjustment to amortize extraordinary retirements over a five-year period. Based on the decisions made in Evidence and Conclusions for Finding of Fact No. 5 regarding the appropriate treatment of extraordinary retirements, the Hearing Examiner finds it improper to increase accumulated depreciation expense to reflect amortization of extraordinary retirements in one year. Consequently, the Hearing Examiner concludes that the proper level of accumulated depreciation and amortization for use in this proceeding is $926,364.

Based on the foregoing, the Commission concludes that the proper level of the original cost rate base is $3,742,490, calculated as follows:

Telephone plant in service	$4,835,658
Material and supplies	24,820
Working capital allowance	21,936
Accumulated depreciation	(926,364)
Accumulated deferred income taxes	(186,296)
Pre-1971 investment tax credit	(4,147)
Customer deposits	(23,117)
Original cost rate base	$3,742,490

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 7

The evidence concerning the proper end-of-period level of operating revenues was presented through the testimony and exhibits of Company witness Rowan and Public Staff witnesses Gerringer, Willis, and Jacome. The amounts shown in the chart below reflect the amounts proposed by the Company and the Public Staff.

	Company	Public Staff	Difference
Local service revenue	$ 510,497	$ 510,497	$ -
Toll service revenue	847,914	840,417	(7,497)
Miscellaneous revenue	72,070	72,070	-
Uncollectibles	(5,218)	(1,066)	4,152
Total operating revenues	$1,425,263	$1,421,918	$(3,345)

As can be seen from the chart above, the Company and Public Staff are in agreement with regard to the level of local service revenues and miscellaneous revenues. There being no evidence to the contrary, the Hearing Examiner finds the appropriate level of local service revenues and miscellaneous revenues to be $510,497 and $72,070, respectively.

The Company and the Public Staff were in disagreement regarding the level of toll service revenues. Although the Company and Public Staff agreed theoretically as to the appropriate amount of toll service revenues, the difference in the amount shown in the chart above of $7,497 relates solely to the failure of the Company to incorporate a modification proposed to toll service revenues by Public Staff witness Gerringer. Witness Gerringer proposed to exclude an amount of $7,497 from toll service revenues in order to reflect the portion of such toll revenues considered to be uncollectible. The Hearing Examiner finds the decrease in toll service revenues of $7,497 recommended by the Public Staff reasonable and proper.

The final component of operating revenue on which the Company and Public Staff disagree is uncollectible revenues. The Company included uncollectible revenues of $5,218 in end-of-period operating revenues. This amount includes uncollectibles associated with local service, toll service, and miscellaneous revenues. Witness Jacome testified that since the toll revenues recommended by the Public Staff are the pro forma amounts to be collected through the Company's settlement process, net of uncollectibles, it would be inappropriate to include any uncollectibles associated with toll revenues for purposes of setting rates in this proceeding. Therefore, witness Jacome adjusted the Company's uncollectible factor to be reflective solely of local service and miscellaneous revenues.

The Hearing Examiner finds and so concludes that uncollectible revenues of $1,066 are appropriate for use herein. Such uncollectible revenues properly relate solely to local service revenues and miscellaneous revenues previously found fair by the Hearing Examiner since toll service revenues of $840,417 are expressed net of uncollectible revenues.

Based on the foregoing, the Hearing Examiner concludes that the proper end-of-period level of operating revenues for use herein is $1,421,918 and consist of the following:

Local service revenue	$ 510,497
Toll service revenue	840,417
Miscellaneous revenue	72,070
Uncollectibles	(1,066)
Total operating revenues	$1,421,918

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 8

The evidence concerning the reasonable level of test year operating revenue deductions is found in the testimony and exhibits of Company witnesses Rowan and Russell and Public Staff witnesses Jacome and Sutton. The amounts shown in the chart below reflect the amounts recommended by the Company and the Public Staff, respectively.

	Company	Public Staff	Difference
Operating expenses	$ 590,677	$ 590,677	$ -
Depreciation and amortization	360,643	249,779	(110,864)
Operating taxes - other than income	102,629	102,400	(229)
State income taxes	10,300	16,734	6,434
Federal income taxes	56,982	103,347	46,365
Total operating revenue deductions	$1,121,231	$1,062,937	$(58,294)

The Company and Public Staff are in agreement regarding the proper level of operating expenses. There being no evidence to the contrary, the Commission finds the reasonable level of operating expenses for Sandhill Telephone Company to be $590,677.

The difference between depreciation and amortization expense proposed by the Company and the Public Staff is $110,864. This difference is primarily due to the differences in the represcribed depreciation rates proposed by Company witness Russell and those proposed by Public Staff witness Sutton, and the level of plant in service upon which to apply these depreciation rates. The parties further disagreed regarding the propriety of the Company's proposed adjustment to depreciation and amortization expense to reflect one year's amortization of $109,743 in extraordinary retirements.

The Hearing Examiner addressed the aforementioned issues in Evidence and Conclusions for Findings of Fact Nos. 5 and 6. Based upon the decision therein, the Hearing Examiner finds and concludes that depreciation expense of $249,779 proposed by the Public Staff is appropriate for use herein.

The next item of difference is operating taxes - other than income. The difference of $229 in the Company and Public Staff proposals relates solely to the differing proposals regarding gross receipt taxes. The level of gross receipt taxes proposed by the parties is reflective of the alternative levels of operating revenue proposed by the Company and the Public Staff.

The Hearing Examiner in Finding of Fact No. 7 found the proper level of operating revenues to be $1,421,918, the amount recommended by the Public Staff and, correspondingly, finds gross receipt taxes recommended by the Public Staff appropriate. Based on the preceding, the Hearing Examiner finds operating taxes other than income of $102,400 reasonable and proper.

The final area of disagreement relates to the amount of state and federal income taxes proposed by the Company and Public Staff.

The amount of state income taxes and federal income taxes proposed by the Company and Public Staff differs by $6,434 and $46,365, respectively. These differences result from differing proposed levels of operating revenues and interest expense. Although the Hearing Examiner has concurred in the proposals made by the Public Staff in this regard, one further adjustment to the interest expense deduction is appropriate. In the calculation of income tax expense for utilities under its jurisdiction, the Commission has consistently in all recent general rate proceedings eliminated the interest expense tax deduction associated with allowing the Job Development Investment Tax Credit (JDITC) an overall rate of return. The Hearing Examiner concurs with the propriety of such an adjustment and therefore finds it appropriate to adjust state and federal income tax expense to exclude the interest expense deduction associated with allowing investment supported by JDITC an overall rate of return. The Hearing Examiner finds state income taxes of $17,500 and federal income taxes of $108,867 reasonable and proper for Sandhill Telephone Company.

In summary the Hearing Examiner concludes that the appropriate level of operating revenue deductions for use in this proceeding is $1,069,223 calculated as follows:

Operating expenses	$ 590,677
Depreciation	249,779
Operating taxes - other than income	102,400
State income taxes	17,500
Federal income taxes	108,867
Total operating revenue deductions	$1,069,223

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 9 AND 10

Two witnesses testified in the areas of the appropriate capital structure and the cost of capital for use in this proceeding: Company witness Pomerantz and Public Staff witness Sessoms.

Company witness Pomerantz testified that the consolidated capital structure of Mid-Continent Telephone Corporation (Mid-Continent) as of June 30, 1982, adjusted for full conversion of all outstanding preferred and debt convertibles, was appropriate for use in determining Sandhill's cost of capital in this proceeding. An embedded cost of long-term debt of 9.20% and

an embedded cost of preferred stock of 7.46% results from use of this capital structure.

In addition, witness Pomerantz estimated the cost of equity using the discounted cash flow (DCF) model and then compared his results to yields on long-term bonds as a check on the reasonableness of his results. The DCF results yielded an investor required rate of return of 15.8% to 16.3% for Mid-Continent and for a group of relatively undiversified telephone companies the results ranged from 16.1% to 16.6%. He then compared these results to the yields of A-rated and Baa-rated utility bonds in October of 14.62% and 15.12%, respectively, and concluded his results were reasonable. He adjusted his range by adding 5% to adjust for financing costs. He testified that this adjustment was necessary to guarantee net proceeds per share that are above book value. Company witness Pomerantz therefore recommended a cost of equity in the range of 16.6% to 17.2%.

Public Staff witness Sessoms proposed an overall return of 10.79%, based on a cost of equity of 14.57%. The capital structure witness Sessoms employed was the actual consolidated capital structure of Mid-Continent as of December 31, 1982. The capital structure consists of 58.71% long-term debt, 8.34% preferred stock, and 32.95% common equity. Witness Sessoms made no adjustment for convertibles and testified that it is improper to assume full conversion for several reasons. Witness Sessoms cited N.C.G.S. 62-133(c) which allows for known and actual changes but not for anticipated changes and stated that the security conversion is not a known and actual change. The cost rates proposed by the Company for long-term debt and preferred are not the actual existing rates at the time of the hearing since the convertibles were ignored in the Company's proposed cost rates. Finally, the Company is adequately compensated for conversion risk through its higher cost of equity than if convertibles were not present.

Consistent with the use of the actual capital structure, witness Sessoms employed an embedded cost of long-term debt of 9.11% and an embedded cost of preferred stock of 7.66%

Witness Sessoms determined the cost of equity for Mid-Continent by employing two methods, the DCF and the Capital Asset Pricing Model (CAPM). The DCF results ranged from 12.75% to 15.2% for Mid-Continent and 13.7% to 15.8% for a comparable risk group. Witness Sessoms then estimated the expected return on the market at 15.0% and concluded a company afforded protection by the Commission would certainly have lower risk and would expect a lower return, thus the CAPM result was 12.98%.

Based upon the results of the CAPM, the DCF, and the current level of interest rates, witness Sessoms concluded the expected return on equity to the Company was in the range of 14.25% to 14.75%. Adding a weighted average selling expense of equity of .07% derived from the Company's actual selling expense to this range and employing the midpoint, he recommended the cost of common equity to the Company is 14.57%. Witness Sessoms testified that adding 5% as the Company proposed would mean that the Company would recover selling expense prospectively for every issue of common stock since the Company began issuing stock in 1960.

The Hearing Examiner has reviewed the evidence presented by the parties. There are substantial differences on the major issues: the proper capital

structure on which to set rates and the return on equity that should be allowed.

With regard to the proper capital structure to be adopted for use in setting rates, the Hearing Examiner notes there are two reasons for the differences. The first results from the point in time each witness selected for establishing the capital structure. Company witness Pomerantz agreed on the stand that the later date used by Public Staff witness Sessoms was more representative. The second reason is the differing treatment of outstanding convertibles. The Hearing Examiner concludes that assuming the full conversion of all outstanding convertibles is improper because it is contrary to the requirements of N.C.G.S. 62-133(c). Additionally, in the Hearing Examiner's opinion the Company is adequately compensated for conversion risk through a higher cost of equity than would exist if the convertibles were not present.

Based on the foregoing, the Hearing Examiner concludes that the appropriate capital structure for Sandhill for use in this proceeding is as follows:

Long-term debt	58.71%
Preferred stock	8.34%
Common equity	32.95%
Total	100.00%

Consistent with this conclusion, the Hearing Examiner concludes the embedded cost of long-term debt is 9.11% and the embedded cost of preferred is 7.66%.

The determination of the appropriate fair rate of return for the Company is of great importance and must be made with great care because whatever return is allowed will have an immediate impact on the Company, its stockholders, and its customers. In the final analysis, the determination of a fair rate of return must be made by the Hearing Examiner, using his own impartial judgment and guided by the testimony of expert witnesses and other evidence of record. Whatever return is allowed must balance the interests of the ratepayers and investors and meet the test set forth in G.S. 62-133(b)(4):

> "... to enable the public utility by sound management to produce a fair profit for its stockholders, considering changing economic conditions and other factors, as they then exist, to maintain its facilities and services in accordance with the reasonable requirements of its customers in the territory covered by its franchise, and to compete in the market for capital funds on terms which are fair to its existing investors."

The return allowed must not burden ratepayers any more than is necessary for the utility to continue to provide adequate service. The North Carolina Supreme Court has stated that the history of G.S. 62-133(b)

> "... supports the inference that the Legislature intended for the Commission to fix rates as low as may be reasonably consistent with the requirements of the Due Process Clause of the Fourteenth Amendment to the Constitution of the United States..." State ex rel. Utilities Commission v. Duke Power Company, 285 N.C. 277, 206, S.E. 2d 269 (1974).

The nature of the evidence in a case such as this makes it extremely difficult to balance all of the opposing interests, since much, if not all, of the evidence is based on individual witnesses' perceptions and interpretations of trends and data from the capital markets. The Hearing Examiner has considered all of the relevant evidence presented in this case, with the constant reminder that whatever return is allowed will have an immediate impact on the Company, its stockholders, and its customers. Imparital judgment must be used to ensure that all the parties involved are treated fairly and equitably.

Based upon the foregoing and the entire record in this docket, the Hearing Examiner concludes that the fair rate of return that Sandhill Telephone Company should have the opportunity to earn on its original cost rate base is 11.09%. Such fair rate of return will yield a fair return on common equity of approximately 15.50%.

It cannot be guaranteed that the Company will, in fact, achieve the level herein found to be just and reasonable. Indeed, the Hearing Examiner would not guarantee it if he could. Such a guarantee would remove the necessary incentives for the Company to undertake to achieve the utmost in operational and managerial efficiency. The Hearing Examiner believes, and thus concludes, that the level of returns approved herein will afford the Company a reasonable opportunity to earn a reasonable return for its stockholders while providing adequate and economical service to the ratepayers.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 11

The Commission has previously discussed its findings and conclusions concerning the fair rate of return which Sandhill Telephone Company should be given the opportunity to earn.

The following schedules summarize the gross revenues and the rates of return which the Company should have a reasonable opportunity to achieve based upon the increases approved herein. The schedules illustrating the Company's gross revenue requirements incorporate the findings and the conclusions heretofore and herein made by the Commission.

SCHEDULE I
SANDHILL TELEPHONE COMPANY
STATEMENT OF OPERATING INCOME
For the Test Year Ended June 30, 1982

	Present Rates	Increase Approved	Approved Rates
Operating Revenues:			
Local service	$ 510,497	$131,266	$ 641,763
Toll service	840,417		840,417
Miscellaneous	72,070		72,070
Uncollectibles	(1,066)	(240)	(1,306)
Total operating revenue	1,421,918	131,026	1,552,944
Operating Revenue Deductions:			
Operating expenses	590,677	-	590,677
Depreciation and amortization	249,779	-	249,779
Operating taxes - other than income	102,400	7,862	110,262
State income taxes	17,500	7,390	24,890
Federal income taxes	108,867	53,256	162,123
Total operating revenue deductions	1,069,223	68,508	1,137,731
Net operating income for return	$ 352,695	$ 62,518	$ 415,213

SCHEDULE II
SANDHILL TELEPHONE COMPANY
STATEMENT OF RATE BASE AND RATE OF RETURN
For the Test Year Ended June 30, 1982

	Present Rates	After Approved Rates
Investment in Telephone Plant		
Telephone plant in service	$4,835,658	$4,835,658
Materials and supplies	24,820	24,820
Accumulated depreciation	(926,364)	(926,364)
Accumulated deferred income taxes	(186,296)	(186,296)
Pre-1971 investment tax credit	(4,147)	(4,147)
Customer deposits	(23,117)	(23,117)
Net investment in telephone plant	3,720,554	3,720,554
Allowance for Working Capital		
Cash	49,223	49,223
Average prepayments	117	117
Average tax accruals	(27,404)	(27,404)
Total working capital allowance	21,936	21,936
Original Cost Rate Base	$3,742,490	$3,742,490
Rate of return	9.42%	11.09%

SCHEDULE III
SANDHILL TELEPHONE COMPANY
STATEMENT OF CAPITALIZATION AND RELATED COSTS
For the Test Year Ended June 30, 1982

	Ratio %	Original Cost Rate Base	Embedded Cost %	Net Operating Income
	Present Rates - Original Cost Rate Base			
Long-term debt	58.71%	$2,197,216	9.11%	$200,166
Preferred stock	8.34	312,124	7.66	23,909
Common stock	32.95	1,233,150	10.43	128,620
Total	100.00%	$3,742,490		$352,695
	Approved Rates - Original Cost Rate Base			
Long-term debt	58.71%	$2,197,216	9.11%	$200,166
Preferred stock	8.34	312,124	7.66	23,909
Common equity	32.95	1,233,150	15.50	191,138
Total	100.00%	$3,742,490		$415,213

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 12

Company witness Thomas and Public Staff witness Willis presented testimony concerning Sandhill's proposed rate structure.

Company witness Thomas testified that the Company's proposed rates had been structured whenever possible to achieve a set of objectives. In general, it can be said that these objectives were the following: (1) the production of the amount of annual revenue requirement; (2) the equitable distribution of increased revenues among the Company's customers with an attempt to minimize the impact of basic local exchange access line rates; (3) the unbundling of exchange rates into access lines and telephone set charges and the elimination of extension service charges; (4) the striking of a balance of administrative ease, customer understanding, and general acceptability while recognizing the change in the terminal equipment market brought about by changes in regulation, competition, and technology. Witness Thomas applied his stated objectives to the majority of the Company's rate structure in distributing the Company's proposed additional revenue requirement in accordance with the Company's proposals regarding basic local exchange service, service charges, special assembly items, directory listings, coin telephone service, key and pushbutton telephone service, miscellaneous service arrangements, auxiliary equipment, local private line service, and local obsolete service offerings. Specific recommendations made by witness Thomas were the unbundling of terminal equipment from the local service rate, and the elimination of charges for extension service.

Public Staff witness Willis presented specific recommendations with respect to the Company's proposals to unbundle its local service rates, to increase its standard rotary and dial-in-hand telephone sets, and to increase its coin telephone rate. Additionally, witness Willis presented his recommendation of the distribution of the Public Staff's proposed revenue requirement among the Company's service categories.

Witness Willis testified that he recognized the necessity for unbundling telephone rates in today's environment and indicated that the Public Staff first recommended the procedures in Docket No. P-55, Sub 777, whereupon the Commission subsequently authorized Southern Bell Telephone Company to unbundle its telephone set charges by Order dated February 7, 1980. Witness Willis testified that since that date the Commission has permitted each regulated telephone company which has filed a general rate case to unbundle its telephone instrument charges. It was his recommendation that the Commission allow Sandhill to unbundle its local basic service rates in this proceeding.

Witness Willis also recommended that the Company's proposed charges of $1.00 per month for the use of a standard rotary telephone set and a charge of $2.50 per month for the dial-in-handset, which he stated were identical to Mid-Carolina Telephone Company's approved rates, be allowed.

Concerning Sandhill's proposal to raise its charge for a paystation local call from $.10 to $.20 per call, witness Willis related that the majority of telephone booths throughout the state required $.20 per call. It was his recommendation that the $.20 per call rate be approved for Sandhill Telephone Company.

The local exchange rates for the two exchanges of the Sandhill Telephone Company recommended by witness Willis have different percentage increases. According to witness Willis this is reasonable due to the effects of the unbundling of telephone sets, the proposed relationship between the two groups and the systematic rearrangement of the business access line services with respect to each other.

With the exception of witness Willis' proposed increases in the local exchange rates, the local coin telephone call rate, the standard rotary telephone set and the dial-in-handset telephone set rates, it was his recommendation that each category of service proposed to be increased receive an essentially uniform percentage increase.

Based upon the evidence presented by witnesses Thomas and Willis, the Hearing Examiner makes the following conclusions:

Unbundling

The Hearing Examiner concludes that the separation of telephone instrument charges from service charges is necessary in today's competitive environment and should be permitted.

Standard Rotary and Dial-In-Handset Telephone Rates

The Hearing Examiner finds the Company's proposed rates for standard rotary and dial-in-handset telephone set rates to be just and reasonable.

Local Coin Telephone Rate

The Hearing Examiner concludes that the charge for a local call from a Company provided paystation should increase from $.10 to $.20.

Distribution of Additional Revenue Requirements

The Hearing Examiner concludes that all additional rate schedule changes necessary to allow the Company the opportunity to recover the additional annual revenues of $131,266 authorized herein with the exception of telephone set charges and local coin telephone rates shall be on an essentially uniform

percentage increase basis. The Hearing Examiner recognizes that the local exchange rates will of necessity vary due to the effects of unbundling of telephone rates, the proposed relationship between the two rate groups and the systematic rearrangement of the business access line.

IT IS, THEREFORE, ORDERED as follows:

1. That the Applicant Sandhill Telephone Company be, and hereby is, authorized to increase its local service rates and charges so as to produce annual gross revenues of $1,554,250 from North Carolina subscribers based on test year operations. Such amount represents an increase of $131,266 above the revenue level that would have resulted from rates currently in effect based on the test year.

2. That the Applicant is hereby called upon to propose specific tariffs reflecting changes in rates, charges and regulations to recover the revenues approved herein, in accordance with the conclusions set forth above, within ten (10) days from the date of this Order. These proposals and workpapers supporting such proposals shall be provided to the Commission (five copies are required) and the Public Staff (formats such as Item 30 of the minimum filing requirement, N.C.U.C. Form P-1, are suggested).

3. That the Public Staff may file written comments concerning the Company's tariffs within five (5) working days of the date on which they are filed with the Commission.

4. That the rates, charges and regulations necessary to produce the annual gross revenues authorized herein shall become effective upon the issuance of a further order approving the tariffs filed pursuant to Paragraph No. 2 above.

5. That the Applicant shall file within ten (10) days from the date of this order a proposed customer notice informing the customers of Sandhill Telephone Company of the actions taken herein.

ISSUED BY ORDER OF THE COMMISSION.
This the 6th day of June 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sandra J. Webster, Chief Clerk

DEPRECIATION RATES

Account	Description	Investment 6-30-82	Rate	Annual Accrual	Reserve 6-30-82	Avg. Rem. Life	Future Net Salvage	Rem. Life Rate	Annual Accrual
212	Buildings	$338,384	2.5	$ 8,460	12.3	30.0	5.0	2.8	$ 9,475
	Central Office Equipment								
221.1	Trunk Carrier Equipment	124,137	5.0	6,207	-23.0	14.6	0.0	8.4	10,428
221.4	Subscriber Carrier Equipment	78,021	5.0	3,901	9.9	10.0	0.0	9.0	7,022
221.5	Step-by-Step Equipment	465,318	5.0	23,266	5.3	14.9	0.0	7.1	33,038
221.8	Digital Equipment	721,117	5.0	36,056	1.1	20.0	5.0	4.7	33,892
231	Station Apparatus	589,717	6.0	35,383	50.0	7.0	3.0	6.7	39,511
232	Station Connections Other	83,655	8.0	7,748	3.4	-	-	5.0	4,183
234	Large PBX	183,831	5.0	9,192	33.3	5.0	0.0	13.3	24,450
241	Pole Lines	69,124	4.5	3,111	56.5	14.0	-20.0	4.5	3,111
242.1	Aerial Cable	471,568	4.0	18,863	46.8	15.0	-5.0	3.9	18,391
242.2	Underground Cable	139,060	3.0	4,172	2.0	32.3	0.0	3.06	4,255
242.3	Buried Cable	1,003,271	4.0	40,131	24.4	20.8	0.0	3.6	36,118
243	Aerial Wire	28,136	5.0	1,407	5.4	9.1	-5.0	11.28	3,174
244	Underground Conduit	203,113	3.0	6,093	0.1	49.5	0.0	2.01	4,083
261	Furniture & Office Equipment	16,353	5.0	818	121.7	-	-	0.0*	-
264.1	Vehicles	81,928	20.0	16,386	117.0	-	-	0.0*	-
264.2	Tools & Other Work Equipment	32,968	10.0	3,297	53.1	6.0	0.0	7.8	2,572
	Subtotal	4,629,701	4.84	224,491	22.7			5.0	233,703
	Additional Amortization Costs:								
	Station Connections - Inside	186,483	8.0	13,863	5.0			10.0	18,648
	Tools & Other Work Equipment	(32,968)	10.0	3,297	53.1	6.0	0.0	7.8	(2,572)
	Total	4,783,216	4.95	238,354	22.1			5.2	249,779

* Rate not based on life & salvage factor

DOCKET NO. P-55, SUB 816

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of	
Application of Southern Bell Telephone and Telegraph Company for an Adjustment to Its Rates and Charges Applicable to Intrastate Telephone Service in North Carolina	) ORDER GRANTING) PARTIAL RATE) INCREASE)

HEARD IN: New Hanover County Courthouse, Third and Princess Streets, on May 16, 1983; Guilford County Courthouse, No. 2 Governmental Plaza, Greensboro, North Carolina, on May 17, 1983; County Office Building, 720 East Fourth Street, Charlotte, North Carolina, on May 18, 1983; Buncombe County Courthouse, Courthouse Plaza, Asheville, North Carolina, on May 19, 1983; and the Hearing Room of the Commission, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina, on July 6, 7, 8, 12, 13, 14, 25, 28, and 29, 1983

BEFORE: Commissioner Edward B. Hipp, Presiding; and Commissioners Douglas P. Leary and Ruth E. Cook

APPEARANCES:

For the Applicant:

R. Frost Branon, Jr., Southern Bell Telephone and Telegraph Company, P.O. Box 30188, Charlotte, North Carolina 28230
For: Southern Bell Telephone and Telegraph Company

J. B. Ray, Southern Bell Telephone and Telegraph Company, 4300 Southern Bell Center, Atlanta, Georgia 30346
For: Southern Bell Telephone and Telegraph Company

Robert C. Howison, Jr., Hunton and Williams, P.O. Box 109, Raleigh, North Carolina 27602
For: Southern Bell Telephone and Telegraph Company

For the Intervenors:

Jerry B. Fruitt, Attorney at Law, P.O. Box 2507, Raleigh, North Carolina 27602
For: North Carolina Textile Manufacturers Association

James D. Little, Antoinette R. Wike, and Thomas K. Austin, Staff Attorneys, Public Staff - North Carolina Utilities Commission, Legal Division, P.O. Box 911, Raleigh, North Carolina 27602
For: The Using and Consuming Public

Jo Anne Sanford, Robert H. Bennink, and Steve Bryant, North Carolina Department of Justice, P.O. Box 629, Raleigh, North Carolina 27602
For: The Using and Consuming Public

Terry J. R. Kolp, United States Department of Defense, USALSA - RL, 5611 Columbia Pike, Falls Church, Virginia 22041
For: The United States Department of Defense and Federal Executive Agencies as Customers in North Carolina

Charles J. Beck, Charles J. Beck, P.A., 820 Irma Avenue, Orlando, Florida 32803
For: North Carolina Alarm Association

BY THE COMMISSION: This matter is before the Commission on the application of Southern Bell Telephone and Telegraph Company (Southern Bell or the Company), filed February 8, 1983, for authority to adjust and increase its rates and charges for local and intrastate toll service in North Carolina. The Company sought to increase total intrastate revenues in the amount of $144,974,447.

On March 7, 1983, the Commission set Southern Bell's application for investigation and hearing, suspended the proposed rates, and required the Company to give notice to the public of the proceeding in this docket.

The Public Staff - North Carolina Utilities Commission filed Notice of Intervention on March 28, 1983.

The Attorney General filed Notice of Intervention on April 13, 1983.

The United States Department of Defense and all other Executive Agencies of the Federal Government filed petition for leave to intervene on March 17, 1983.

The North Carolina Textile Manufacturers Association (NCTMA) filed a petition to intevene on March 30, 1983.

The North Carolina Alarm Association filed a petition to intervene on April 15, 1983.

These petitions were allowed by Orders of the Commission issued on March 28, April 1, and April 19, 1983, respectively.

Public night hearings were scheduled and held for the specific purpose of receiving testimony from public witnesses in Wilmington on May 16, Greensboro on May 17, Charlotte on May 18, Asheville on May 19, and Raleigh on July 6, 1983. The following persons appeared and testified at these hearings:

Wilmington - Harry Dorsey, H. C. Wallace, John Fitzpatrick, Hattie M. Dixon, and Larry Wayne Bestle.

Greensboro - H. C. Settle, Larina Copeland, John Anderson, John Morton, W. E. McGehee, David Hill, Lula Chambers, Fanny Graves, H.A. Strunks, Mrs. B. C. Andrews, David Benson, Gary Liles, Larry Attaberry, Peggy Hines, Mrs. A. Walton Stokes, H. L. Simpson, Vann Massey, Wiley Hines, Jane Brenner, and C. C. Oates.

Charlotte - Monroe T. Gilmour, M.D., Brad Buie, J. W. Lee, Tere Wood, Mildred Asbury, Donna Lee, Andy Forlidas, Frederick W. Buchta, Wilson Maxwell, William Kirk, and Janelle Travis.

Asheville - Gene Pettit, Edward C. Feldon, Conley F. Boyd, Ruth Webb, John Gatling, Beverly Pahel, Wiley Brinkley, J. W. Weissenborn, E. S. Blakely, Bob Kethman, Patricia Kethman, Keith Thomson, Fred Sealey, and Scott Rogers.

Raleigh - Kirby McLennan, Arthur M. Matthews, J. W. Lee, Lula Chambers, and J. Malcolm Cates; Jeff B. Wilson, and Joseph Reinckens (daytime hearings).

The case in chief came on for hearings as scheduled on July 6, 1983. Southern Bell offered the direct testimony of the following witnesses: Jere A. Drummond, Vice President in charge of Southern Bell's operations in North Carolina; Dr. Roger A. Morin, Professor of Finance at Georgia State University, College of Business Administration; Timothy H. Weaver, formerly District Manager in the Bell System Purchased Products Division of AT&T, now employed by South Central Bell; Robert N. Dean, Assistant Vice President - Revenue Requirements Treasurer of Southern Bell; H. Gerald Prophitt, Division Staff Manager in the Revenue Requirements Department of Southern Bell; Walter S. Reid, District Staff Manager in the Comptrollers Department of Southern Bell; William E. Thornton, Manager, Corporation Analysis, in the Regulatory and Anti-Trust Matters Division of the Western Electric Company; Richard E. Stark, Director - License Contract and Regulatory Matters in the Comptrollers Department of AT&T; Stephen M. Wilson, Division Staff Manager in the Revenue Requirements Department of Southern Bell; Robert C. Hart, Jr., District Staff Manager in Service Costs for Southern Bell; and Robert L. Savage, Division Staff Manager - Rates and Service Costs for Southern Bell.

The Public Staff offered the testimony of the following witnesses: Thi-Chen Hu, Engineer - Communications Division; Leslie C. Sutton, Engineer - Communications Division; Nancy B. Bright, Director - Accounting Division; Jocelyn M. Perkerson, Accountant - Accounting Division; Curtis Toms, Jr., Supervisor - Telephone Section, Accounting Division; William J. Willis, Engineer - Communications Division; Dr. John W. Wilson, President of J. W. Wilson and Associates, Inc.

The Attorney General presented the testimony of Dr. John K. Stutz of the Energy Systems Research Group.

The North Carolina Alarm Association presented the testimony of W. Kenneth Edwards, Rate Analyst - Communications Consultants, Inc.

The North Carolina Textile Manufacturers Association offered the testimony of the following witnesses: Larry D. Brown, Manager of Corporate Telecommunications at Cone Mills Corporation; Harry M. Venable, Director of Telecommunication Services for Celanese Corporation; and Louis R. Jones, Manager of the Corporate Communications Department of Burlington Industries.

Southern Bell offered rebuttal testimony of Dr. Morin, Mr. Stark, and Mr. Drummond.

Based on the foregoing, the evidence adduced at the hearing and the entire record in this matter, the Commission makes the following

FINDINGS OF FACT

1. The Applicant, Southern Bell Telephone and Telegraph Company, is a public utility duly authorized to do business in North Carolina, is providing

telecommunications service in North Carolina and, as such, is subject to the jurisdiction of this Commission. Southern Bell is properly before the Commission in this proceeding, pursuant to G.S. 62-133, for a determination of the justness and reasonableness of its proposed rates and charges.

2. In its original application, Southern Bell requested rates designed to produce gross annual revenues of approximately $871,186,000 based upon a test year ended October 31, 1982. By its revised application, the Company requested rates designed to produce annual gross revenues of approximately $848,683,000, based on the test year level of operations. The Company contended that gross revenues under present rates are approximately $726,212,000, thereby necessitating an increase of $122,472,000 which the Company proposed to achieve through increases in rates for local service of approximately $111,769,000 and increases in rates for toll service of approximately $10,703,000.

3. The test year for purposes of this proceeding is the 12 months ended October 31, 1982.

4. The overall quality of service provided by Southern Bell is adequate.

5. No construction work in progress should be included in Southern Bell's rate base.

6. The schedule of depreciation rates and amortization amounts as shown in Appendix B is just and reasonable and should be approved.

7. Southern Bell's reasonable original cost rate base used and useful in providing service to its customers is $1,110,313,000. This rate base consists of telephone plant in service of $1,585,174,000, plus a plant acquisition adjustment of $3,213,000, the working capital allowance of $27,407,000, less the depreciation reserve of $313,182,000, customer deposits of $2,831,000, accumulated deferred income taxes of $187,948,000, and unamortized investment tax credits of $1,520,000.

8. Southern Bell's total end-of-period gross operating revenues for the test year, under present rates and after accounting, pro forma, and end-of-period adjustments, are $726,212,000.

9. The general service and license contract (GS&L) expenses included in Southern Bell's cost of service should be reduced by $3,564,000 in this proceeding.

10. The reasonable level of test year operating revenue deductions for Southern Bell after accounting, pro forma, and end-of-period adjustments is $604,881,000.

11. The Company should be allowed a rate of return on original cost rate base of 12.04% which will allow the Company a reasonable opportunity to earn a return on common equity of 14.75%. The capital structure for Southern Bell which is reasonable and proper for use in this proceeding is as follows:

Item	Ratio
Debt	45.00%
Common equity	55.00%
Total	100.00%

12. Based on the foregoing, Southern Bell Telephone and Telegraph Company should be allowed to increase local service revenues by $20,330,000. This level of increase is $16,336,000 less than would otherwise be required due to flow through of additional intrastate toll revenues arising from an increase in toll rates granted in Docket No. P-100, Sub 64. This increase is required for the Company to have a reasonable opportunity to earn the 12.04% overall rate of return which the Commission has found just and reasonable. This increased revenue requirement is based on the original cost of the Company's property and its reasonable test year operating revenues and expenses as previously determined and set forth in these findings of fact.

13. The rates, charges, and regulations to be filed pursuant to this Order in accordance with the guidelines contained herein, which will produce an annual increase in local service revenue of $20,330,000, will be just and reasonable.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NOS. 1 - 3

The evidence supporting these findings of fact is found in the verified application, in prior Commission Orders in this docket, and in the record as a whole. These findings are essentially procedural and jurisdictional in nature and are uncontested and uncontroverted.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 4

The evidence concerning the quality of service was presented by Company witness Drummond, Public Staff witness Hu, and 19 public witnesses.

There were approximatley 60 public witnesses, the majority of whom testified in opposition to the rate increase. Nineteen of the public witnesses testified about the quality of service. One testified favorably, and 18 unfavorably, on the quality of service.

Witness Drummond testified that the Company had a highly skilled, loyal, and dedicated work force - a work force that made "Bell" service a hallmark for all of industry. He also stated that he believed the Company's employees had provided the telephone consumer in North Carolina a tremendous bargain in service quality, variety, and price.

During cross-examination, witness Drummond acknowledged that the Company did not meet the Commission's objective of subsequent reports, of repeated reports, and of out-of-service reports not cleared within 24 hours for any month of 1982. However, he further testified that the Company had made substantial improvements in all three areas in the year 1983.

Witness Hu testified that, in evaluating the quality of service provided by the Company, he had reviewed and analyzed the following statistics:

Total Trouble Reports Per 100 Stations
% Subsequent Reports of Total Trouble Reports
% Repeat Reports of Total Trouble Reports
% Out-of-Service Trouble Reports Cleared Within 24 Hours
% Regular Service Orders Completed Within 5 Working Days
% Regrade Applications Held Over 14 Days
% New Service Orders Held Over 14 Days

Witness Hu stated that most of these service indices were within the Commission's objectives. The principal exception to this was that, during the three-year period 1980 through 1982, the Company consistently failed to meet the Commission's objective on the percentage of out-of-service trouble reports cleared within 24 hours. However, his further analysis of this index for the first six months of 1983 indicated that the Company had improved its performance in this area.

In summary, witness Hu concluded that the overall quality of service provided by the Company was adequate.

Based on the foregoing evidence, the Commission concludes that the overall quality of service provided by Southern Bell is adequate.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 5

Company witness Reid and Public Staff witness Bright presented evidence relating to the inclusion of construction work in progress (CWIP) in rate base.

Witness Reid stated in his direct testimony that he believed Southern Bell's short-term construction work in progress met the criteria of North Carolina General Statutes 62-133(b)(1) for inclusion in rate base. He contended that the Company must be able to include those investments in rate base in order to secure the investor return and that the financial stability of any corporation is directly related to the ability to meet its investor obligations.

Witness Bright testified that G.S. 62-133 (b)(1) requires the Commission to find and determine both that it is in the public interest and that it is necessary to the financial stability of a utility before any of that utility's investment in CWIP may be included in rate base. She also stated, based upon her examination of several generally accepted measures of financial stability as they apply to Southern Bell, that this case is a clear instance where the financial stability test has not been met. Her analysis showed that Southern Bell's pre-tax interest coverage excluding AFUDC is 4.08x, that AFUDC as a percentage of intrastate earnings is 3%, and that CWIP as a percentage of total utility investment is 1.6%, based on the Public Staff's recommended rate of return and rate base. All of these measures indicate that Southern Bell is financially stable and that the exclusion of short-term CWIP from rate base will not have any material effect on that stability.

Witness Bright explained that since the Uniform System of Accounts prescribed by this Commission for telephone utilities does not allow the capitalization of AFUDC on short-term construction work in progress, it would be appropriate for the Commission to modify the System of Accounts and allow the Company to begin capitalizing AFUDC on its short-term investment in CWIP.

Sutton stated that the depreciation rates he was recommending were established by the FCC in Docket No. 79-105 and are applicable to all telephone companies. The Commission is intimately familiar with FCC Docket No. 79-105 and has concurred with that decision in all instances where represcription has been requested for the station connections accounts. Accordingly, the Hearing Examiner finds the depreciation rate recommended by the Public Staff for station connections-other and station connections-inside to be just and reasonable and appropriate for use in this proceeding.

The third area of disagreement concerns the Company's proposal to recover $109,743 in depreciation reserve deficiencies through extraordinary retirements. The reserve deficiencies result from retirements to the step-by-step and large PBX equipment accounts. According to witness Rowan, the step-by-step and large PBX equipment in question was retired prior to the end of the test period and the reserve deficiency was reflected in the Company's existing depreciation reserve. Witness Sutton stated that since the retirements occurred prior to the end of the test period, the deficiency would be included in the accumulated depreciation reserve. Further, witness Sutton pointed out that the remaining life depreciation rates reflect the accumulated reserve, and thus depreciation rates include the impact of the reserve deficiency. Moreover, he stated that allowing a remaining life depreciation rate for these two accounts <u>and</u> allowing extraordinary retirement treatment amounts to allowing double recovery of the $109,743 investment.

It is clear to the Hearing Examiner that if the remaining life depreciation rates were developed using investment and reserve levels as of June 30, 1982, and if the retirements occurred prior to that time, then the reserve deficiencies are fully reflected in the depreciation rates. Additionally, if extraordinary retirement treatment is also allowed, then double recovery of the $109,743 investment would in fact occur. Further, the Hearing Examiner is of the opinion that the appropriate way to treat this reserve deficiency is through the methodology proposed by witness Sutton. Accordingly, the Company's request for extraordinary retirement treatment is denied.

The final area of disagreement concerns the Company's proposal to implement an ELG based depreciation procedure for plant additions made after January 1, 1983. Company witness Russell indicated that an ELG procedure could provide a better matching between capital consumption and capital recovery. Further, he stated that the FCC had approved the use of ELG for telephone companies in FCC Docket No. 20188.

Witness Sutton testified that he opposed the use of ELG based depreciation rates in this proceeding because of the practical problems associated with their implementation. Implementation of the Company's ELG proposal will result in rapid and continual expansion of the number of depreciation rates. For example, whereas the Company now has 17 depreciation rates to apply to its 17 plant accounts, 10 years after the establishment of the Company's proposed ELG system, there would be 187 depreciation rates to be applied to 187 portions of the investment in the Company's 17 plant accounts for use in calculating the Company's monthly depreciation expense. Witness Sutton further testified that Sandhill currently has inadequate record-keeping procedures and proposes to implement ELG initially on a manual basis. From an administrative perspective, the complexity of accounting for such a myriad of rates would be unreasonably burdensome for the Company, the Commission, and the Public Staff.

Although witness Sutton did not address the alleged reserve deficiency alluded to by witness Prophitt, he indicated that he considered the depreciation rates proposed by the Public Staff to be sufficient to ensure adequate capital recovery for Southern Bell. He stated that if remaining life (RL) depreciation rates were used for all accounts, as he was recommending, a reserve deficiency currently existing would be eliminated by recovering the Company's net investment over the remaining life of that plant. He indicated that, through its recent decisions (1981 for Southern Bell) to prescribe RL rates for certain accounts, the Commission is resolving the reserve deficiency.

It is apparent to the Commission that, as a result of technological changes, rising operating costs, and competition promulgated into the telecommunications industry by the FCC, there is a shortening of service lives of telephone company plant investments. Of course, this change must be reflected in the development of depreciation rates for a telephone company. However, in view of the upward pressure already exerted on basic residence service by deregulation and competition, the Commission must examine each element of a utility's operations that is further forcing basic residence service rates upward.

In this proceeding Southern Bell proposes revisions to its depreciation rates that, if allowed, will increase basic residence telephone service rates approximately $2.25 per month. To prescribe rates with so significant an impact upon basic residence service, the Commission must be convinced that the depreciation rates, and the service lives underlying those rates, are the only ones appropriate. This Commission is not so convinced, for as witness Prophitt readily admitted upon cross-examination, the process of depreciation rate development is not an exact science.

Both witness Prophitt and witness Sutton proposed decreasing the composite average service life of Southern Bell's depreciable plant investment; however, the two witnesses differed on the extent of the decrease in the composite average service life. Witness Sutton stated that his recommendation was based upon mutually agreed upon service lives by the FCC Staff and the Public Staff after independently reviewing a Southern Bell prepared depreciation study. Although the Company disagree with the service lives recommended by the Public Staff (and thus the FCC Staff), witness Prophitt did not present evidence to discredit the Public Staff's recommendation or to support the Company's proposal for any specific plant account. Witness Prophitt's arguments against the Public Staff's recommendation and for the Company's proposal can best be described as general in nature and shallow in scope. In this instance, the Company has not borne the burden of proof regarding its proposed depreciation rate parameters. Based upon the evidence presented, the Commission adopts the depreciation rate parameters proposed by the Public Staff.

The other point of disagreement between the Company and the Public Staff is the capital recovery methodology. Witness Prophitt proposed to implement an equal life group (ELG) based depreciation procedure for certain plant accounts. He indicated that an ELG procedure could provide a better matching between capital consumption and capital recovery. Further, he stated that the FCC had authorized the use of ELG for telephone companies on an optional basis in Docket No. 20188.

Witness Sutton testified that he opposed the use of ELG based depreciation rates because of the practical problems associated with their implementation and the ever-growing number of rates associated with that methodology. He indicated that implementation of an ELG based system would necessitate burdensome record keeping requirements not required for the capital recovery metholodogy he was proposing. Further, establishment of the Company's proposal will result in a rapid and continual expansion in the number of depreciation rates. For example, whereas the Company now has 28 depreciation rates to apply to its 28 plant accounts, 10 years after the establishment of the Company's proposed ELG system there would be 308 depreciation rates to be applied to 308 portions of the investment in the Company's 28 plant accounts for use in calculating the Company's monthly depreciation expense. From an administrative perspective, the complexity of accounting for such a myriad of rates would be unreasonably burdensome for the Company, the Commission, and the Public Staff.

Witness Sutton summarized his position on the Company's ELG proposal as follows:

> "My review of an ELG based capital recovery system leads me to the following conclusions. First of all, it is not apparent to me that the ELG procedure proposed by Southern Bell will produce sufficient benefits to justify the extensive effort required to implement it. Also, there are serious questions as to whether or not the promises of ELG theory can be realized because of the necessity for accurate life projections and extensive records. It does not seem reasonable to establish a complex procedure when the benefits of that procedure are inherently limited by the accuracy of projections and offset by burdensome data and record keeping requirements. I think material improvement in the capital recovery process can be accomplished without having to resort to ELG. The use of RL offers a means to insure full capital recovery and is more manageable than ELG. In short, ELG introduces complexity unnecessary for adequate capital recovery by Southern Bell." (Tr. Vol. 13, pp. 21-22).

Related to the issue of which capital recovery metholology to be authorized by the Commission is the question of whether or not this Commission has the authority to prescribe rates or methodologies it deems most appropriate. During the cross-examination of witness Sutton, counsel for Southern Bell referred to the FCC's Pre-Emption Order issued on January 6, 1983, in Docket No. 20188, in which the FCC asserted that it had authority to preempt state commissions from prescribing depreciation rates and methodologies different from those prescribed by the FCC. Witness Sutton stated that it was his understanding that this Commission has not been preempted by the FCC from prescribing depreciation rates and methodologies for intrastate rate-making purposes that differ from those prescribed by the FCC. Further, he indicated that the matter of preemption by the FCC has been appealed to the federal courts and that the courts will ultimately decide the issue.

The Commission is of the opinion that the FCC's Pre-Emption Order does not preempt this Commission from prescribing whatever depreciation rates and methodologies it determines to be appropriate for intrastate rate-making purposes. In support of its opinion, the Commission takes judicial notice of the decision of the United States District Court for the District of Maine on June 15, 1983, in Civil Action No. 83-0166-P. In that case, New England

Telephone and Telephone Company (NET) petitioned the District Court for a Temporary Restraining Order (TRO) against an Order issued by the Public Utilities Commission (PUC) of Maine. The PUC had issued an Order in a general rate case prescribing depreciation rates for intrastate rate-making purposes that differed from those previously prescribed by the FCC. In denying NET's motion for a TRO, the District Court stated that NET failed to convince the Court that: (1) plaintiff will suffer irreparable injury if the injunction is not granted; (2) such injury outweighs any harm which granting injunctive relief would inflict on the defendant; and (3) plaintiff has exhibited a likelihood of success on the merits.

As pointed out by witness Sutton during cross-examination, if this Commission adopts the position that it has been preempted, or if the courts rule that it has, then this Commission would be bound to the prescription of depreciation rates previously prescribed by the FCC. In this case that would require prescription of Southern Bell's existing depreciation rates rather than prescription of the rates proposed by Southern Bell or the Public Staff. However, as previously stated, the Commission is of the opinion that it has not been preempted by the FCC and thus has the authority to prescribe the depreciation rates and methodologies it deems appropriate for intrastate rate-making purposes.

Finally, the Commission takes judicial notice of its decision in Docket No. P-53, Sub 47 (Sandhill Telpehone Company). In that general rate case, the Commission denied the Company's request to implement an ELG based capital recovery system.

Based upon the foregoing discussion, the Commission concludes that Southern Bell's request to implement an ELG based capital recovery system should be denied and that the RL capital recovery system proposed by the Public Staff should be approved.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 7

The evidence concerning the proper intrastate original cost rate base is found in the testimony of Company witness Reid and Public Staff witness Toms. The following chart summarizes the amounts that each witness contends should be included in the intrastate original cost rate base for use in this proceeding.

(000's Omitted)

Item	Company Witness Reid	Public Staff Witness Toms	Difference
Telephone plant in service	$1,587,405	$1,585,174	$ (2,231)
Telephone plant under construction	17,731	-	(17,731)
Property held for future use	117	-	(117)
Telephone plant acquisition adjustment	3,213	3,213	-
Working capital:			
Cash	7,500	7,500	-
Materials and supplies	16,633	16,633	-
Investor funds provided for operations	12,235	12,196	(39)
Less: Accounts payable - materials & supplies	4,323	4,543	220
Accounts payable - plant in service	4,379	4,379	-
Accounts payable - plant under construction	4,747	-	(4,747)
Total original cost	1,631,385	1,615,794	(15,591)
Less: Depreciation reserve	341,261	313,182	(28,079)
Customer deposits	2,831	2,831	-
Accumulated deferred income taxes	188,586	187,948	(638)
Unamortized investment tax credit	1,569	1,520	(49)
Net original cost	1,097,138	1,110,313	13,175
Terminal equipment deregulation	(109,605)	-	109,605
Rate base	$ 987,533	$1,110,313	$122,780

As the schedule shows, the Company and the Public Staff are in agreement on the amounts of the telephone plant acquisition adjustment, the working capital components of cash, materials and supplies, accounts payable - plant in service, and the amount of customer deposits. Therefore, the Commission concludes that the amounts included for these items are reasonable and proper for use herein.

The first item of difference to be discussed by the Commission concerns terminal equipment deregulation, or the transfer of assets associated with new and embedded Customer Premises Equipment (CPE) to American Bell, Inc. (ABI). While this item is not shown as the first item of difference on the schedule above, it is being discussed first because of its relative impact on rate base.

With respect to the proposed treatment of this item, Company witness Reid made an adjustment for Computer Inquiry II through which he removed all existing terminal equipment investment and reserves to be detariffed, and related investments in buildings, furniture and office equipment, and vehicles in the amount of $109,605,000. He also removed operating revenues, expenses, and taxes related to this terminal equipment. Witness Reid testified that the purpose of his adjustment was to recognize that Southern Bell plans to

transfer this portion of its business to AT&T between August 1, 1983, and January 1, 1984, under provisions of the Modified Final Judgement (MFJ) to the 1956 Consent Decree and the FCC's Computer Inquiry II Order.

Public Staff witness Toms reversed the Company's adjustment due to uncertainty over whether the FCC would approve AT&T's plan in the Implementation Proceedings. Thus, witness Toms included embedded CPE investment, revenues, expenses, and taxes in Southern Bell's intrastate operations. Correspondingly, he removed investments in buildings and furniture plus the related reserves associated with new CPE because these items were effectively transferred from Southern Bell to ABI on January 1, 1983. In support of his position he testified in his prefiled testimony that under Computer Inquiry II the FCC ordered the detariffing of all new customer premises equipment by January 1, 1983, but postponed the detariffing of embedded CPE pending the outcome of the Implementation Proceeding in FCC Docket No. 810893. Additionally, witness Toms testified concerning additional steps taken by AT&T to enhance the chance of gaining FCC approval of its plan and all announcements or proposed orders by the FCC concerning the plan.

With respect to the additional steps taken by AT&T, witness Toms testified in his prefiled testimony that AT&T has filed additional Supplementary Comments (Docket No. 81-893, Computer Inquiry II, Procedures for Implementing and Detariffing CPE) through which AT&T asked the FCC to grant approval of its plan for detariffing and transfer of embedded CPE to ABI by January 1, 1984. He testified further that through its Supplemental Comments, AT&T had cited five proposals to facilitate detariffing and transfer of embedded CPE by the time of divestiture, and that one of the proposals was in direct response to questions that the FCC has raised about certain supporting assets. Finally, he testified that AT&T had proposed to have independent professional appraisals made of supporting assets (excluding CPE Accounts 231 and 234) to be transferred from Bell Operating Company rate bases to ABI.

In regard to announcements by the FCC concerning the current status of the Implementation Proceedings, witness Toms testified in his prefiled testimony that, while the FCC had agreed in principle with AT&T's plan, the FCC stated that further review of details was necessary and that some changes might be made before granting final approval.

During cross-examination, witness Reid was asked if the FCC had not indeed stated in its "Notice of Proposed Rulemaking" on page 41, paragraph 82, that the AT&T proposal did not address several issues which are of concern to various parties to the Implementation Proceeding and that a number of details remained to be worked out before the FCC could be assured that a plan is fashioned which promoted the FCC's goals and objections. Further, he was asked if the FCC had not stated that further adjustments and modifications of the plan as a result of the Implementation Proceeding might render the plan a suitable vehicle for carrying out the transaction. Witness Reid acknowledged both of the FCC's statements.

Witness Reid was asked if he had not made a future test year adjustment, he disagreed and testified that he was trying to recognize a change that is known from the standpoint of the FCC in that the FCC had indicated that this is the direction in which the industry is going.

During his direct testimony witness Toms stated that the FCC's "Notice of Proposed Rulemaking," filed on June 21, 1983, listed the FCC's concerns from an accounting standpoint on Pages 30, 31, 32, 33, and 34. These concerns pertained, in general, to the appropriate accounting treatment to be accorded deferred income taxes, investment tax credits, and supporting assets and related gains. Finally, he testified that the order outlines the FCC's tentative plans which indicate that the issues surrounding each of these items must be resolved before the modified plan is approved.

Based upon the evidence presented by the witnesses in this proceeding, the Commission concludes that Public Staff witness Toms' reversal of the Company's Computer Inquiry II adjustment and his inclusion of the investments in embedded CPE and related supporting assets, reserves, operating revenues, expenses, and taxes in Southern Bell's cost of service is proper. While the Commission recognizes that detariffing and transfer of embedded CPE to AT&T will happen eventually, the Commission is also cognizant of the fact that the Company's proposed adjustment is only an estimate and that its position pertaining to the transfer of embedded CPE, as compared to the FCC's position, is divergent. The Commission concludes that the Company's proposed adjustment should not be allowed for the foregoing as well as the following reasons:

1. The Company's proposed adjustment does not represent an actual change.

2. The Company's proposed adjustment does not address the concerns expressed by the FCC in its "Notice of Proposed Rulemaking," issued June 21, 1983, nor has the Company's proposed adjustment been modified to accommodate the FCC's tentative treatment of deferred income taxes, investment tax credits, the gains on supporting assets, nor transaction costs.

3. Neither the Company, the Public Staff, nor the Commission can quantify the Company's level of embedded CPE and related supporting assets, the gains from supporting assets, revenues, operating revenues, expenses, nor the taxes that will exist at January 1, 1984, the date on which AT&T has requested that these items be detariffed and transferred to ABI.

The Company's adjustment simply does not meet the requirements of G.S. 62-133 which states:

> ". . . the Commission shall consider such relevant, material and competent evidence as may be offered by any party to the proceeding tending to show <u>actual changes</u> in cost, revenue, or the costs of the utility's property used and useful, or to be used and useful within a reasonable time after the test period, in providing the service rendered to the public within this State, including construction work in progress, which is <u>based upon circumstances and events occurring up through the time the hearing is closed</u>." (emphasis added)

In regard to the second item, the Commission has taken judicial notice of the FCC's "Notice of Proposed Rulemaking," Docket No. 81-893, <u>In the Matter of Procedures for Implementing the Detariffing of Customer Premises Equipment and Enhanced Services (Second Computer Inquiry)</u>. The Commission notes the following differences with respect to deferred income taxes. The Company has proposed to reduce the transfer price of embedded CPE by the amount of deferred taxes (as determined from Item 10 of the MFR), whereas the FCC has tentatively concluded that such treatment is reasonable, with one exception.

The exception is the possibility that, at the time ABI sells this embedded equipment, it may be subject to only a capital gains tax rate, whereas these deferred taxes were accumulated at current tax rates. Further, the proposed order stated that since the ordinary tax rate is considerably higher than the capital gains tax rate, ratepayers would have paid in income taxes which may never be incurred. Consequently, the FCC's tentative plans are to pass on to the ratepayers any overpayment of taxes that might result if AT&T is granted capital gains treatment from the sale of this embedded CPE. The Commission concurs with the FCC's tentative treatment of deferred income taxes. The benefits to be derived from income taxes which resulted from the use of tax normalization for rate-making purposes should not be passed on to the purchasers at the expense of the ratepayers who originally provided them.

With respect to investment tax credits, the FCC tentatively found that the unamortized investment tax credits should be credited to the income tax expense of the carrier when the assets are removed from the regulated accounts. This Commission also concurs with the FCC's tentative treatment of this item because, unlike deferred income taxes, there are no offsetting future taxes to be paid when assets are retired from regulated service. Thus, except for recapture provisions for early retirement, the investment tax credits represent permanent tax reductions in the year they are deducted for tax purposes. A further distinction is that if these assets were sold to a third party, the unamortized investment tax credits, not subject to recapture provisions, would be credited to the income tax expense of the telephone company.

With respect to supporting assets and related gains, this Commission again concurs with the tentative treatment proposed by the FCC in its "Notice of Proposed Rulemaking." The FCC has proposed that the gains resulting from the appraisals of land be included in the "Other Operating Income" of the telephone company. This treatment will ensure that ratepayers will receive the benefit from the appreciation of the assets being transferred.

The Commission believes that a great injustice will be suffered by Southern Bell's ratepayers if the Company's pro forma adjustment for the detariffing and transfer of embedded CPE is allowed at this point in time. Since the FCC has been asked to approve the detariffing and transfer of embedded CPE at January 1, 1984, the Commission concludes that the Company's actual investment in embedded CPE, and the related operating revenues, expenses, and taxes existing at January 1, 1984, should be used to recognize the revenue requirement effect of detariffing and transferring embedded CPE to ABI. In drawing this conclusion, the Commission is mindful of the fact that neither the Company, the Public Staff, nor the Commission is in a position at this point to estimate the Company's actual expected investment in embedded CPE at January 1, 1984, because conditions are constantly changing. While the Company continues to add customers, it is also selling CPE to customers. Likewise, while the parties have requested that the FCC grant approval to detariff and transfer embedded CPE at January 1, 1984, they have not entered a contractual arrangement which sets forth the actual assets to be transferred, the amounts at which they will be transferred, nor the terms and conditions under which they will be transferred. Finally, the Commission concludes that use of the October 31, 1982, historical investment in embedded CPE, and the test period adjusted levels of embedded CPE, and related revenues, expenses, and taxes could materially misstate the revenue requirement which the ratepayers must ultimately bear. Therefore, the Commission concludes that

October 31, 1982, embedded CPE should not be used to calculate the effects of revenue requirements (Note: The proper level is discussed subsequently). This treatment will ensure that the Company's ratepayers will not be paying a return on plant that may be transferred without giving them the proper credit or reduction in rate base that they would justly deserve.

The Commission will now discuss the remaining differences in rate base beginning with the $2,231,000 reduction in telephone plant in service which results from the Public Staff adjustments that follow:

(000's Omitted)

Item	Amount
Transfer of assets associated with new CPE to ABI	$ (717)
Phase out of customer premises equipment	(1,514)
Total	$ (2,231)

The first adjustment involves an item mentioned earlier in the Commission's discussion of the Company's adjustment for Computer Inquiry II. Company witness Reid made a composite pro forma adjustment to remove all existing terminal equipment, reserves, and related assets in recognition of Southern Bell's plan to detariff and transfer embedded CPE to ABI, effective January 1, 1984. Conversely, Public Staff witness Toms reversed the Company's pro forma adjustment and made his own pro forma adjustment for reasons previously discussed and to recognize that, effective January 1, 1983, Southern Bell transferred investments in building and furniture, net of reserves and credits, to ABI in exchange for capital stock of AT&T.

The Commission has previously concluded that Public Staff witness Toms' adjustment to remove investments in buildings, furniture, the related reserves, and investment credits related to the transfer of these assets to ABI is proper. The removal of the property from the Company's books constitutes an actual change which should be recognized for rate-making purposes.

The second adjustment concerns Public Staff witness Toms' adjustment to allocate to intrastate operations, plant balances attributable to customer premises equipment on the books at December 31, 1982, through utilization of a ratio of 12/60 rather than 14/60 ratio utilized by Company witness Reid. Both witnesses made their proposed adjustments in recognition of the FCC's order in Docket No. 80-286, wherein the FCC provided for the phase-out and termination of the allocation to interstate operations of customer premises equipment in Accounts 231 and 234. Under provisions of the order, plant balances on the books at December 31, 1982, constitute a frozen base amount which will be shifted from interstate operations to intrastate operations at the rate of 1/60 per month for 60 months. Additionally, under this Order, no new investment in CPE may be apportioned to intrastate operations after December 31, 1982.

Company witness Reid testified in his prefiled testimony that he had adjusted the test period ending October 31, 1982, so that it was reflective of the separations level during the period in which the rates proposed in this proceeding would be in effect. During his cross-examination he testified that he had used a CPE ratio of 14/60 because if rates in this proceeding are set in September 1983, the midpoint of that 12-month period would be February

1984. Thus, witness Reid derived his 14/60 ratio by adding the first eight months of CPE phase-out experience to the average of the next 12-months. When he was asked under cross-examination if he had not made a future test year adjustment, witness Reid indicated that he had only adjusted the levels in the test period ending October 1982, by a factor that has changed.

Public Staff witness Toms testified in his prefiled testimony that in his opinion no more than 12/60 of the interstate base amount should be transferred to intrastate operations in this proceeding. He testified that one purpose of the phase-out of CPE from interstate to intrastate operations over five years was to lessen the burden on intrastate ratepayers that would occur if all embedded CPE were allocated to intrastate in one year. Finally, he testified that his adjustment recognized that, in the year 1983, 12-months or one year of phase-out will occur, whereas Company witness Reid's 14/60 allocation ratio would recognize in this case and in the first year more than 1/5 of the shift from interstate to intrastate operations.

During his cross-examnation, witness Toms was asked why he thought the one year adjustment through December 31, 1983, was proper as distinguished from witness Reid's adjustment. In response, witness Toms testified that Southern Bell's test period ended on October 31, 1982, and that since the test period ended prior to the beginning of phase down, his recognition of the annual effect or the effect of the first year shift was appropriate, considering that the Company requests a rate increase approximately every year. He testified further under cross-examination that he thought if he had included an amount above and beyond the effect of the first year shift, he would have prejudiced the FCC's intent. He testified that the FCC's intent was to provide a mechanism through which to move both the utility and its customers toward the competitive marketplace. Additionally, witness Toms testified that the FCC was phasing down the CPE over a five-year period, at the rate of 1/60 per month, to ensure that the ratepayers would not be unreasonably burdened with abnormally high rate increases, while also giving the Company the opportunity to sell off some of its CPE.

In response to additional questioning about CPE recovery, witness Toms acknowledged that at mid-July the Company had not received any allowance for CPE phase-out and would not receive any until an Order is issued during September. However, he explained that Company witness Reid's adjustment, as well as his adjustment, would give the Company phase out amounts at the rate of 14/60 and 12/60 per month, respectively, when in fact, 1/60, 2/60, 3/60, 4/60, and so on was actually being used. As a result, he testified that in the beginning months the Company will actually over-recover, while in later months the Company might under-recover. In further explanation, witness Toms testified that, while the FCC had frozen CPE at December 31, 1982, the FCC did not freeze the customers. Thus he contended that there is some question as to whether or not the Company will under-recover. He testified that the Company is adding customers every month, and those extra customers would pay rates to cover the frozen CPE base, and that, while it could be said that the Company might under-recover, the Company might also over-recover.

Finally on cross-examination, Public Staff witness Toms was asked if it was not true that the Staff had not recommended 12/60 for phase out of CPE in other utility cases that preceded the Bell case, whether rates in those would not go into effect before the rates in this case, and whether it would not be proper to push forward by the same number of months that the Order in this

case is subsequent to the orders in other telephone company cases in order to give the Company the benefit given other telephone companies. Witness Toms responded affirmatively to the questions pertaining to what had occurred with other telephone companies, but would not agree to the suggestion that Southern Bell's CPE adjustment should be pushed forward. He testified that what witness Reid had done was to forecast when the Company would filed for another rate increase and that the General Statutes do not permit forecasting.

Based upon the evidence presented by the witnesses, the Commission concludes that Public Staff witness Toms' adjustment to allocate the frozen CPE base from interstate to intrastate operations through the use of a ratio of 12/60 is proper. Since the Company's test period ended at October 31, 1982, or prior to the January 1, 1983, date on which the CPE phase out process began, the Company should not be allowed to pro form into the intrastate cost of service an amount that represents more than 12/60 of the CPE phase out, because the Company is adding more customers each month. Since these customers will be paying rates to cover revenue requirements associated with CPE phase out, the Company may, in fact, recover more through rates over the entire five-year phase out period than was originally established through the frozen base amount. In the Commission's opinion, this dilemma was not comtemplated by the FCC's order. Therefore, the Commission concludes that the intent of the FCC's order should be followed. By requiring that CPE be allocated from interstate to intrastate operations over a five-year period, or at the rate of 1/60 per month, the FCC has provided a transition mechanism which produces a measured even shift that balances the effect of moving both the Company and its ratepayers toward the competitive marketplace. This mechanism ensures that ratepayers will not be unreasonably burdened with abnormally high rate increases, while permitting the Company to sell off part of its CPE concurrently.

Finally, the Commission is not persuaded by Company witness Reid's argument concerning the appropriateness of his proposed CPE ratio of 14/60.

The next item of difference on the schedule above concerns telephone plant under construction. The Commission has previously concluded in Finding of Fact No. 5 that no telephone plant under construction should be included in rate base in this proceeding.

The third item of difference is property held for future use. Company witness Reid included $117,000 for this item in rate base and testified in his prefiled testimony that property held for future use was comprised of property, primarily land, not currently in service. He testified that each item of property included in this category has a definite plan for its use within two years in the provision of telephone service. Further, he testified that efficient operations planning requires the procurement of land for building sites well in advance of the commencement of building construction.

Public Staff witness Toms testified in his prefiled testimony that he had excluded property held for future use from rate base because it does not meet the criterion for being used and useful in providing telephone service to the public as prescribed by G.S. 62-133.

During his cross-examination, witness Toms was asked if it was not true that investors would receive no return on their investment until the property was placed in service or unless the property was included in rate base. In

response witness Toms testified that the General Statutes indicate that property should only be included in rate base to the extent that it is used and useful in providing telephone service. Further, with respect to investors and their return, he testified that he thought investors are sophisticated and would be knowledgeable of the fact that certain properties would not earn a return until they go into service.

On further cross-examination, witness Toms was asked if the Commission, in this case, should not recognize the statute as it is written and also recognize that the elimination of this item from rate base is detrimental to the utility's earning its authorized rate of return, and take that into account in establishing what it deems to be a fair cost of capital for the utility. In response witness Toms testified that the General Statutes guide what the Commission can and cannot do as a matter of law. He testified further as follows:

> "...in fixing of rates, this Commission shall ascertain the reasonable cost of the Public Utility's property used and useful. Now, in determining the reasonable cost, it's my contention that the Commission should exclude this property held for future use. I am proposing that the original cost rate base should be comprised of the amount set forth on witness Toms Exhibit No. 2, exclusive of property held for future use. The Commission has, in the past, excluded this item consistently."

Based upon the evidence presented by the witnesses, the Commission concludes that Public Staff witness Toms' adjustment to remove property held for future use from rate base is proper.

The fourth item of difference concerns Public Staff witness Toms' adjustment to decrease investor funds advanced for operations by $39,000 for the effect of surcharges payable by ABI. He testified that the surcharge reduction results from an installation and maintenance agreement between the Company and ABI under which the Company has agreed to provide customer premises installation and maintenance services in return for its cost of providing those services plus a surcharge for use of funds. He testified further that this surcharge reimburses the Company for advance provision of working capital and facilities usage, due to the lag periods between billings and collections for overhead and investment related costs. Finally, he testified that he had removed these surcharges from the investor funds advanced for operations component of working capital to preclude the Company from recovering this return twice.

The Company did not contest the adjustment, and the Commission concludes that witness Toms' adjustment to reduce investor funds advanced for the effect of these surcharges is proper.

The fifth item of difference concerns Public Staff witness Toms' adjustment to increase accounts payable applicable to merchandise and materials held for sale by $220,000. Witness Toms stated in his prefiled testimony that he had increased this item because the related asset (Design Line Telephone) is included in rate base. He testified further that the Company had inadvertently omitted the item. The Company did not contest the adjustment. Therefore, the Commission concludes that Public Staff witness Toms' adjustment to increase accounts payable applicable to merchandise and materials held for sale is proper.

The sixth item of difference concerns the depreciation reserve. The following chart summarizes the $28,079,000 difference between the Company and the Public Staff:

(000's Omitted)

Item	Amount
Transfer of assets associated with new CPE to ABI	$ (36)
Phase out of customer premises equipment	(388)
Represcription of depreciation rates	(27,655)
Total	$(28,079)

As the schedule shows, the first two adjustments above are directly related to issues previously decided by the Commission. Since the Commission has previously found that Public Staff witness Toms' adjustment for the transfer of assets associated with new CPE to ABI is proper, the Commission finds that his adjustment to the related depreciation reserve is also proper. Correspondingly, the Commission finds that his adjustment to the depreciation reserve applicable to the phase out of customer premises equipment is proper. The remainder of the difference is due to the use of different depreciation rates by the Company and the Public Staff. The Public Staff's proposed depreciation rates were previously found to be reasonable; thus, the Commission concludes that further discussion is not necessary.

The seventh item of difference concerns accumulated deferred income taxes. The adjustments which comprise the $638,000 difference are shown in the chart that follows:

(000's Omitted)

Item	Amount
Transfer of assets associated with new CPE to ABI	$ (91)
Phase out of customer premises equipment	(309)
Normalization of disallowed interest	(238)
Total	$(638)

With respect to the first two items, the Commission has previously agreed with Public Staff witness Toms' adjustments for the transfer of assets associated with new CPE to ABI and the phase out of customer premises equipment. Therefore, further discussions of the reasons for these adjustments are not necessary. The remaining difference results from witness Tom's adjustment to reverse the Company's adjustment for normalization of disallowed interest expense. Witness Toms testified that the disallowed interest expense represented interest expense which is being accrued by the Company due to anticipation of pending federal income tax audits but will not be deductible for tax purposes until paid. Further, he testified that this interest expense has not been included in the cost of service by the Company and, therefore, the ratepayer should not be given this tax benefit. Finally, witness Toms testified that, in computing income tax expense for rate-making purposes, normally the only interest expense used as an income tax deduction other than interest on long-term debt is interest on customer deposits. The Company did not contest this adjustment through its cross-examination of witness Toms. The Commission concludes that witness Toms' adjustment is proper and that the interest related to the underpayment of taxes should not be included in the cost of service.

The final item of difference concerns Public Staff witness Toms' adjustment to remove $49,000 of investment credits from the unamortized investment tax credit balance. This adjustment resulted from witness Toms' adjustment for the transfer of assets associated with new CPE to ABI. The Commission has previously found that his overall adjustment for the effect of the transfer was proper. The Commission therefore finds this adjustment also proper.

In summary, the Commission concludes that the proper rate base for use in this proceeding is $1,110,313,000, consisting of the following:

(000's Omitted)

Item	Amount
Telephone plant in service	$1,585,174
Telephone plant acquisition adjustment	3,213
Working capital:	
Cash	7,500
Materials and supplies	16,633
Investor funds provided for operations	12,196
Less: Accounts payable - materials and supplies	4,543
Accounts payable - plant in service	4,379
Total original cost	$1,615,794
Less: Depreciation reserve	313,182
Customer deposits	2,831
Accumulated deferred income taxes	187,948
Unamortized investment tax credit	1,520
Rate base	$1,110,313

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 8

Evidence concerning the proper end-of-period level of operating revenues was presented through the testimony and exhibits of Company witness Reid and Public Staff witness Toms. Both witnesses agree as to the proper level of operating revenues. However, Company witness Reid removed revenues associated with embedded CPE through his pro forma adjustment to net income for return for the effect of his proposed adjustment for detariffment and transfer of embedded CPE to ABI. The Commission has previously found under Evidence and Conclusions for Finding of Fact No. 7 that revenues associated with embedded CPE should be included in operating revenues. Therefore, the Commission concludes that the end-of-period level of revenues proposed by the witnesses which include revenues for embedded CPE are proper for use herein.

In summary, the Commission concludes that the appropriate level of end-of-period revenues under present rates, after giving effect to uncollectible revenues, is $721,203,000, which is itemized as follows:

(000's Omitted)

Item	Amount
Local service revenues	$441,572
Toll service revenues	231,467
Miscellaneous revenues	53,173
Uncollectible revenus	(5,009)
Total operating revenues	$721,203

Public Staff witness Perkerson and Company witness Stark, including his rebuttal testimony.

Public Staff witness Perkerson made the following adjustments to license contract, cost-sharing, and conduit expenses:

(000's Omitted)

Item	Amount
License contract business marketing expense	$ 527
License contract residence marketing expense	281
License contract business service expense	157
Cost-sharing and conduit business marketing, residence marketing, and business service expense	1,068
Holding Company expense	389
Contributions and public affairs	96
New York State and City taxes	259
National advertising and EPCOT Center expense	806
General Department overheads and rate of return on 195 Broadway and Bell Telephone Labs	682
Growth factor on license contract, cost-sharing, and conduit expenses	77
	4,342
Less Company adjustment for CPE and enhanced services	(778)
Total	$3,564

Witness Perkerson testified that she centered her investigation on license contract, cost-sharing, and conduit expenses because of the dramatic increases in these types of expenses. However, she stated that her adjustments were based on her findings during the investigation and not based on the increases themselves. She further stated, in several instances, that the license contract was a good mechanism and resulted in cost savings. She maintained, however, that this did not negate the necessity to examine these costs and that the efficiencies and cost savings of the arrangement did not impair the propriety of her adjustments. She stated that her adjustments were made to remove those expenses which she felt should not be included in the cost of service.

Witness Perkerson provided detailed testimony, both through her prefiled testimony and exhibits and through cross-examination, supporting the adjustment of $527,000 for license contract business marketing, $281,000 for license contract residence marketing, and $881,000 ($1,068,000 - $187,000 business service) for cost-sharing and conduit expenses for business and residence marketing.

Witness Perkerson testified that her basis for removal of these expenses was the transfer of this cost to American Bell, Incorporated, effective January 1, 1983. She stated that this information was provided by New York personnel during her audit and that no line item exists for the accumulation of these costs by AT&T's General Department in 1983.

The Company questioned witness Perkerson regarding the CPE related to business marketing. She stated that recognition was given to all CPE related to her adjustments by the reduction of her $778,000, the CPE amount calculated by Company witness Reid. Witness Stark did not address this adjustment in his rebuttal testimony.

As regards residence marketing, witness Perkerson was questioned by the Company regarding the requirement of the FCC's paragraph 105 for reporting costs incurred in the formation of ABI. Witness Perkerson stated that she had not dealt with the costs withheld under this requirement but only those costs that were a part of the total charge to North Carolina.

Witness Perkerson was also questioned about the transfer of a portion of the cost for residence marketing in 1982 to business service in 1983. Witness Perkerson stated she had broken out the business service on a percentage basis through a 100% review of the business service Budget Decision Packages (BDPs) and felt the percentage allowed would take into account any transfer of cost that might occur.

Company witness Stark, through his rebuttal testimony, stated that $103,000 of the license contract residence marketing reduction and $36,000 of the cost-sharing and conduit residence marketing reduction recommended by witness Perkerson was in support of the embedded CPE. Witness Perkerson repeatedly throughout her testimony and cross-examination stated that she had reduced her total adjustments by the $778,000 reduction for the CPE as determined by the Company.

Witness Stark during cross-examination of his rebuttal testimony stated that witness Perkerson had, in fact, reduced her adjustments for the CPE credit.

Based on the evidence, the Commission rejects witness Stark's contention that witness Perkerson's adjustments should be reduced and finds that her treatment of CPE in this case is appropriate. The Commission concludes, as witness Perkerson stated in her testimony, that reductions to the cost of service for license contract business marketing in an intrastate amount of $527,000 for license contract residence marketing in an intrastate amount of $281,000 and for cost-sharing and conduit business and residence marketing in an intrastate amount of $881,000 are actual known changes prior to the time of this hearing and are properly excludable from the cost of service.

The next area of difference between the Company and the Public Staff is business service.

Witness Perkerson recommended a reduction to license contract business service of $157,000 and to cost-sharing business service of $187,000 ($1,068,000 minus business and residence marketing of $881,000). She stated that her adjustment was based on a percentage calculation derived after a 100% review of the budget decision packages for business service for 1982.

She stated that in her review the assistance of Public Staff engineers and other accountants was used to determine which of the functions previously performed by business service would transfer to ABI with the transfer of business and marketing residence. The percentage derived by witness Perkerson was 67.12%.

The Company questioned witness Perkerson regarding her methodology and the items included in her calculation.

Witness Perkerson stated that the BDPs were presented to her as being highly refined documents which serve as the basis for many decisions at the General Department.

Witness Perkerson stated that her methodology was reasonable and widely used in calculations of this type. She further stated that she used BDP dollars only to calculate a relationship which she then applied to the actual dollars for business service.

Even though the Company questioned the percentage used by witness Perkerson and witness Stark stated in his rebuttal testimony that the percentage was incorrect, the Company failed to provide a better methodology or a factor which they felt was correct.

The Commission finds that the Company failed to meet the burden of proof in this area and concludes that the 67.12% calculated by witness Perkerson is reasonable and that license contract business service should be reduced in an intrastate amount of $157,000 and cost-sharing business service in an intrastate amount of $187,000.

The next adjustment made by the Public Staff was to remove expenses related to holding company operations in an intrastate amount of $389,000. The Public Staff specifically identified several categories of expense as being incurred both as a result of AT&T's ownership of the BOCs and the servicing of the BOCs by the General Department.

Witness Perkerson pointed out that if AT&T were any of the many competitive companies, it would not matter except for internal cost centers where the expenses of ownership were assigned. AT&T, however, is a regulated industry and it operates on a cost-plus basis. Profit is determined as a percent of return on investment, and all allowed expenses are added to this profit. Under these conditions profits are enhanced for AT&T by allocating out every expense it can to the regulated subsidiary.

Company witness Stark, in his rebuttal testimony, stated that AT&T is a holding company only in that it holds the capital stock of the operating telephone companies. He further stated that Congress does not apply holding company legislation to the telephone industry.

The Company further stated that in the post-divestiture period, as today, holding company costs, as described by witness Perkerson, will be allocated to all benefiting companies in the AT&T system, including prospective local companies which will be engaged in the provision of interexchange services.

Based on the evidence provided, the Commission concludes that ownership costs do exist and it is not reasonable to allow AT&T to pass all its costs of

ownership to the regulated subsidiaries. The Commission further finds that divestiture has not taken place and no issue in this proceeding can be determined as if divestiture were an actual fact.

The Commission concludes that the adjustment made by the Public Staff to remove an intrastate amount of $389,000 for holding company expenses is appropriate and is in keeping with the basic principles of proper assignment of cost for rate-making.

Witness Perkerson's next adjustment eliminated $96,000 of cost for contributions and public affairs. She testified that she had removed $47,000 of contributions because it is inappropriate to charge the consumer for the Company's charitable contributions when the customer has no choice in where he buys utility service. On cross-examination, she agreed that the contributions were not excessive and were to worthy causes; however, she contended that customers should not be forced to contribute to a charity that may not be of their choosing.

The Commission agrees that contributions should not be included in cost of service. It has been a long-standing policy of this Commission that contributions are not properly includable in cost of service.

The $49,000 balance of this adjustment related to public affairs, or lobbying, which she stated were a duplication of cost, if beneficial only to ratepayers, because as taxpayers they also support legislative bodies to represent their interest; and, if beneficial only to the Company, it should also be removed. She further stated that she did not believe that the Company would ever lobby for legislation which would benefit the ratepayer to the detriment of the Company.

On cross-examination, she agreed that the Public Affairs Department did monitor legislation, assist legislative bodies, and report information to the telephone companies; however, she contended that this lobbying was unnecessary and the ratepayers should not be burdened with the cost to support legislation which might not be in their best interest.

The Commission believes that the Public Affairs Department's primary concern is the interests of the Company and its stockholders. The Commission therefore concludes that witness Perkerson's adjustment is proper.

Witness Perkerson also removed $259,000 of taxes paid to New York City and New York State. She stated that most of the New York State's franchise tax is due to AT&T's ownership of New York Telephone, rather than the assets used to provide license contract services, since only 2.175% of New York assets are employed in providing license contract services. She testified that the gross receipts tax was not based on any income received from companies whose place of business is located outside New York State and was also properly excludable from cost of service. She also contended that 90.55% of the New York City utility tax is due to AT&T's ownership of New York Telephone.

On cross-examination, witness Perkerson was questioned concerning the fact that the New York gross receipts tax and the New York City utilities tax were based on license contract revenues and not ownership of New York Telephone. Witness Perkerson maintained her position that these taxes were primarily based on assets and activities within the State of New York.

Witness Stark, in rebuttal, stated that these two taxes were based on license contract revenues and were properly included in cost of service. Witness Stark stated that the franchise tax was based on the ratio of AT&T's New York statutory assets to AT&T's statutory assets everywhere. He stated that the purpose of this formula used for the franchise tax is similar to the apportionment of the New York State gross earnings and New York City utilities tax.

The Commission believes that an apportionment to New York State based on New York State assets to all assets everywhere indicates that the tax is applicable only to assets and activities within that state and in this case would primarily be related to the ownership and operations of New York Telephone. The Commission notes that witness Perkerson left 2.175% of this tax in Southern Bell's cost of service.

The Commision is also not persuaded by witness Stark's argument that the gross earnings and utilities tax are properly assignable to Southern Bell.

The Commission therefore concludes that witness Perkerson's adjustment of $259,000 is proper.

Witness Perkerson eliminated the total national advertising expense of $806,000 included by the Company.

Witness Perkerson stated that a review of the AT&T advertising manual shows that national advertising is designed primarily to promote the corporate image and to promote sales in the business and residence marketing area. She contended that it is unfair to require ratepayers to pay for advertising which does not reduce telephone rates and that the primary beneficiaries of the advertising she removed were the shareholders of AT&T.

On cross-examination, she was asked if advertising for recruiting women and other minorities, ethnic advertising, and informational advertising were not properly includable in cost of service. She responded that she believed that AT&T had no need for minority or ethnic advertising in that these people were walking the streets looking for jobs and that the informational advertising could best be handled at the local level.

Witness Stark, in rebuttal, stated that national advertising was properly included because ethnic advertising helps recruit minorities and informational advertising is also beneficial to ratepayers and that witness Perkerson's adjustment should be reduced by $165.000.

The Commission agrees with witness Perkerson. National advertising by AT&T is primarily image advertising promoting AT&T. The Commission therefore concludes that witness Perkerson's adjustment removing $806,000 of national advertising is proper.

Two adjustments deal with overhead expenses and the rate of return requirement on 195 Broadway and Bell Labs. Public Staff witness Perkerson made an adjustment to remove $600,000 related to overhead, $76,000 related to return on 195 Broadway, and $6,000 related to return on Bell Labs.

While the Company, through the rebuttal testimony of witness Stark, suggested that certain of these adjustments were overstated, the Commission

finds that the Company failed to meet the burden of proof in this area. The Commission realizes that a slight change in the methodology used to calculate these expenses would result in a different dollar amount, but also recognizes that none of these changes will produce a material difference in this case.

The Commission further finds that an adjustment of this nature is necessary to assure that indirect expenses, for items being removed from the cost of service in this case, are not passed to the ratepayer through rates.

Based on the evidence provided, the Commission finds that $600,000 for overhead expenses, $76,000 for return on 195 Broadway, and $6,000 for return on Bell Labs should be removed from the cost of service in this case.

The last adjustment made by the Public Staff removes the growth factor added by Southern Bell to license contract expenses. The total expenses of $4,651,000 being removed from the cost of service is therefore reduced by the $77,000 added by the Company in its growth factor calculation.

The Commission finds that this adjustment is necessary in order to assure that expenses are not overstated.

In summary, the Commission concludes that witness Perkerson's adjustments to license contract expenses are reasonable and that the Company has not borne the burden of proof that any of these amounts should be included in cost of service. The Commission therefore adopts witness Perkerson's adjustment totaling $3,564,000.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 10 -

The evidence for operating revenue deductions is found in the testimony and exhibits of Company witness Reid and Public Staff witness Toms. The amounts represented below reflect the amounts each witness contends is proper for use in this proceeding:

(000's Omitted)

Item	Company Witness Reid	Public Staff Witness Toms	Difference
Operating expenses	$371,116	$350,666	$(20,450)
Depreciation and amortization	142,417	114,862	(27,555)
Taxes other than income	71,706	70,607	(1,099)
Income taxes-state & federal	43,889	65,628	21,739
Total operating expenses	$629,128	$601,763	$(27,365)

The level of operating expenses above includes expenses associated with embedded CPE. However, Company witness Reid removed expenses associated with embedded CPE through his pro forma adjustment to net operating income for return for the effect of his proposed adjustment for detariffing and transfer of embedded CPE. The Commission has previously found, under Evidence and Conclusions for Finding of Fact No. 7, that expenses associated with embedded CPE should be included in operating expenses.

The first area of difference between the parties concerning operating revenue deductions involves operating expenses. Company witness Reid testified that the appropriate level of operating expenses is $371,116,000,

whereas Public Staff witness Toms testified that the appropriate level of operating expenses is $350,666,000, a difference of $20,450,000. This difference is comprised of various Public Staff adjustments as follows:

(000's Omitted)

Adjustment to Operating Expenses:	Amount
1. Reduction due to use of 12/60 ratio to reflect the effect of the phase out of customer premises equipment	$ (134)
2. Reduction in maintenance expense due to represcription of depreciation rates	(175)
3. Removal of refurbishing expenses	(164)
4. Removal of general service and licenses expenses	(3,564)
5. Decrease in end-of-period wages and benefits	(8,275)
6. Reversal of pro forma nonmanagement wage increase	(7,681)
7. Removal of lobbying expenses	(88)
8. Removal of charitable contributions	(369)
Total	$(20,450)

The Commission will now discuss each of the adjustments comprising the $20,450,000 difference in operating expenses.

The first difference between the witnesses of $134,000 results from Public Staff witness Toms' use of a ratio of 12/60 to recognize the shift of customer premises equipment related expenses from interstate to intrastate operations, whereas Company witness Reid utilized a ratio of 14/60. The Commission has previously concluded in Finding of Fact No. 7 that witness Toms' adjustment for the phase out of customer premises equipment was proper; therefore, this adjustment is proper.

The next difference arises due to the use of different depreciation rates by the Company and the Public Staff. The Commission has previously found in Finding of Fact No. 6 that the Public Staff's proposed depreciation rates were reasonable. Therefore, this adjustment is considered proper.

The third difference results from Public Staff witness Toms' adjustment to remove refurbishing expenses. With respect to this adjustment he testified as follows:

> "During the test year, the Company spent approximately $700,000 to refurbish phone center stores. Effective January 1, 1983, several phone center stores were transferred to American Bell, Inc. These phone center stores were estimated to have occupied 30.3% of all phone center store space. Therefore, I have removed a corresponding percentage from the cost of service. This adjustment is consistent with my previous adjustment to remove investments transferred to ABI, on January 1, 1983."

Witness Toms was not asked any questions concerning this adjustment during his cross-examination. The Commission concludes that Public Staff witness Toms' adjustment is consistent with his proposed adjustment to remove investments transferred to ABI, at January 1, 1983. Thus, the Commission, having previously found that adjustment to be proper, also finds this adjustment to be proper.

The fourth item concerns Public Staff witness Perkerson's removal of general services and licenses expenses totaling $3,564,000. With respect to this item the Commission has previously found that witness Perkerson's removal of these general service and license expenses was proper.

The fifth item concerns Public Staff witness Toms' adjustment to decrease end-of-period wages and benefits by $8,275,000. In support of his adjustment he testified as follows:

"I have adjusted the Company's salaries and wages for the effect of the drop in the number of employees from October 31, 1982 (end-of-test period) to March 31, 1983. The Company lost approximately 502 employees in North Carolina during this period. Of the 502 employees, 275 were transferred to ABI from the Commercial area during January and February of 1983. Of the 275 employees, 181 were from management positions while 94 held non-management positions. The remaining 227 employees were lost from the Maintenance, Traffic, General Office, and Commercial areas. In the Maintenance area, 80 employees were lost due to construction cutbacks, and 20 were lost due to maintenance cutbacks. In the Traffic area, 51 employees were lost due to normal attrition with no replacement. In the General Office area, 47 employees were lost due to cost cutting efforts. In regard to the Commercial category, approximately 21 employees were lost due to general force reductions.

The Company also transferred 156 headquarters employees to ABI in January and February of 1983. During the test period 16% of the salaries, wages and employees benefits of these 156 employees were allocated to North Carolina. I have removed the 16% of their salaries and benefits which the Company has included in end-of-period expenses.

Even though the Company's investment in plant continues to grow, the Company is able to operate with fewer employees. While many of these employees were lost due to cutbacks, general attrition, and transfers to ABI, a goodly number were also lost due to plant equipment efficiencies. Southern Bell's ratepayers should not be required to pay rates to cover the salaries, wages and employee benefits of employees no longer employed by the Company."

With respect to 275 employees transferred to ABI, witness Toms was asked during his cross-examination whether it would be appropriate to decrease or reduce the portion of his adjustment attributable to the 275 employees transferred to ABI in the event the Commission accepted witness Reid's adjustment regarding the transfer of embedded CPE to American Bell, and whether agnized the full
effect of the drop in employees.

In regard to this point, Company witness Reid testified on cross-examination that he had not adjusted for the salaries, wages, and employee benefits of 251 employees who had left the Company since the end of the test period. Witness Reid testified that he had not adjusted for those employee losses because, in looking back over North Carolina earnings for the period from May 1981 through December 31, 1982, he found that the Company had never earned its authorized rate of return during that period of time, even though the Company has lost 556 employees through attrition that were not replaced.

He testified further that there were many reasons which contributed to the Company's inability to earn the return authorized in its last case and that a large reason for that was due to the increases in wages and other items that were known but not actual and were not included in the Company's previous rate cases.

Although the Commission has previously dismissed Company witness Reid's adjustment for Computer Inquiry II in favor of the position taken by Public Staff witness Toms, the Commission feels that further discussion is necessary because of the position taken by witness Reid of not removing, through his adjustment for Computer Inquiry II, the effects of salaries, wages, and employee benefits attributable to an additional 251 employees who left the Company subsequent to the test year. Through his cross-examination, Company witness Reid testified that he had not recognized the effect of the employee loss because the Company had not earned the return allowed by the Commission from its last rate case due to attrition.

With respect to witness Reid's adjustment for Computer Inquiry II, the Commission concludes that the decrease in salaries, wages, and employee benefits due to the decrease in the number of employees should have been reflected in his proposed adjustment. The Commission is not persuaded by witness Reid's arguments concerning attrition. Many factors contribute to a utility's inability to achieve the return allowed by this Commission, and certainly attrition is one of them. However, there is no evidence to support witness Reid's argument for lack of achievement. An actual earnings measurement would have to take into consideration the same types of expenses, revenues, and investment that were considered by the Commission in granting a return. Further, the Commission does not guarantee a return; it only provides a utility the opportunity to earn the allowed return. In that regard, the Commission is mindful of a portion of G.S. 62-133(b)(4) which requires it to:

> "Fix such rate of return on the cost of the property ascertained pursuant to subdivision (1) as will enable the public utility by sound management to produce a fair return for its shareholders, considering changing economic conditions and other factors, as they then exist, to maintain its facilities and services in accordance with the reasonable requirements of its customers in the territory covered by its franchise, and to compete in the market for capital funds on terms which are reasonable and which are fair to its customers and to its existing investors." (Emphasis added.)

Thus, the return allowed by the Commission is not intended to insulate the utility from the effects of wage increases, inflationary pressures, or other economic effects which may evolve subsequent to the hearings on which an Order is based. If a utility finds that its authorized return has eroded, the alternative is to file for a new rate increase.

Based on the evidence presented by the witnesses, the Commission concludes that Public Staff witness Toms' adjustment to decrease end-of-period wages, salaries, and employee benefits is proper. As the evidence shows, Southern Bell lost approximately 502 employees from the end of the test period through March 31, 1983. In spite of those losses, the Company's investment in plant continues to grow and it is operating efficiently with fewer employees. Therefore, the Commission concludes that Southern Bell's ratepayers should not be required to pay rates to cover the salaries, wages, and employee benefits of employees no longer employed by the Company.

The sixth item concerns Public Staff witness Toms' reversal of the Company's $7,681,000 pro forma adjustment for a nonmanagement wage increase. Witness Toms testified in his prefiled testimony that he had removed the Company's adjustment because union negotiations had not been and were not expected to be settled by the close of the hearings in this proceeding. He testified that the adjustment was neither known, nor measurable at this point. When he was asked during his cross-examination if this Commission had, indeed, in some cases allowed for the wage increases occurring subsequent to the close of the hearings, witness Toms testified in response as follows:

> "There is a distinct difference between the wage agreement being contested here and those that were allowed by the Commission in those other cases. That distinction is that the various Boards of Directors for those utilities had decided early on the exact amount of the increase to be awarded to their employees. That is not the situation with Southern Bell. At this point in time, the increase is not quantifiable."

On redirect, witness Toms testified that if the Commission chose to allow this adjustment, it should be reduced for the effect of employees that have left the Company.

Company witness Reid testified under cross-examination that the nonmanagement wage adjustment was conservative in comparison with prior year wage increases.

Based upon the evidence presented by the witnesses, the Commission concludes that Public Staff witness Toms' adjustment to reverse the Company's pro forma nonmanagement wage adjustment is proper. In making this decision the Commission concludes that it must act pursuant to G.S. 62-133(c), which states in part that this Commission shall consider actual changes in costs based upon circumstances and events occurring up through the date of the hearings. At the close of the hearings, the amount of wage increase, if any, to be granted Southern Bell's nonmanagement employees was neither actual, nor quantifiable, because a contract simply did not exist.

The next area of difference concerns witness Toms' adjustment to remove lobbying expenses. In his prefiled testimony he testified as follows:

> "In my opinion, ratepayers should not be required to pay rates to cover expenses incurred in an effort to influence legislation or public opinion on matters that may prove beneficial to stockholders. In Southern Bell's last general rate case, Docket No. P-55, Sub 794, the Commission concurred with the Public Staff and removed these lobbying expenses from the cost of service."

The Commission has consistently excluded this item from the cost of service because it does not consider lobbying expense to be a reasonable operating expense. Therefore, the Commission concludes that Public Staff witness Toms' adjustment to exclude lobbying is proper.

The eighth and final adjustment concerns Public Staff witness Toms' adjustment to remove charitable contributions totaling $369,000 from the cost of service. Witness Toms testified in his prefiled testimony that he had

removed these contributions to preclude the ratepayers from being forced to make involuntary contributions to organizations which they may not wish to support. On cross-examination, witness Toms was asked whether he questioned the legitimacy or worthiness of the charities. He testified that he had not questioned that at all. He testified that it was not his position that the Company should not make contributions but rather, to the extent they are made, that they should be allocated below the line, or taken from shareholder profits.

With respect to charitable contributions, the Commission has consistently excluded them from the cost of service. The Commission has not been presented with any substantive evidence during this proceeding to convince it that these charitable contributions should be treated differently from the traditional treatment accorded this item. Therefore, the Commission concludes that Public Staff witness Toms' adjustment to exclude charitable contributions from the cost of service is proper.

Based upon the foregoing, the Commission concludes that the proper level of operating expenses for use in this proceeding is $350,666,000.

The second area of difference between the parties concerning operating revenue deductions involves depreciation and amortization expense. Company witness Reid testified that the appropriate level of depreciation and amortization expense was $142,417,000, whereas, Public Staff witness Toms testified that the appropriate level of depreciation and amortization expense was $114,862,000. This difference is comprised of various Public Staff adjustments as follows:

(000's Omitted)

Item	Amount
Transfer of assets associated with new CPE	$ (22)
Reduction due to use of 12/60 ratio to reflect the effect of the phase out of customer premises equipment	(207)
Represcription of depreciation rates	(27,326)
Total	$(27,555)

In regard to the first two adjustments, the Commission has previously concluded that Public Staff witness Toms' overall adjustments for these items was proper. Therefore, additional discussion is not considered necessary. The remaining adjustment for represcription of depreciation rates was also previously found to be proper; thus, additional discussion is not considered necessary.

Based upon the foregoing, the Commission concludes that the proper level of depreciation and amortization expense for use in this proceeding is $114,862,000.

The third area of difference between the witnesses concerning operating revenue deductions involves taxes other than income. Company witness Reid testified that the appropriate level of taxes other than income was $71,706,000, whereas Public Staff witness Toms testified that the appropriate level was $70,607,000. The difference of $1,099,000 results from various adjustments proposed by witness Toms, each of which has been discussed previously by the Commission. Since the Commission has adopted all of the

adjustments proposed by Public Staff witness Toms, the Commission concludes that his proposed level of taxes other than income of $70,607,000 is proper for use herein.

The final area of difference between the parties concerning operating revenue deductions involves state and federal income tax expense. The difference of $21,739,000 results from the fact that witnesses Reid and Toms each made adjustments to state and federal income taxes to reflect the income tax effect of their respective adjustments to revenue and/or expense.

One issue regarding the level of state and federal income taxes requires further discussion. This issue involves the appropriate level of interest expense to be used in the calculation of income tax expense. Company witness Reid and Public Staff witness Toms presented testimony concerning the appropriate amount of interest expense which should be deducted in arriving at taxable income for calculation of state and federal income taxes.

Company witness Reid's position is that Southern Bell's actual interest expense per books brought to an end-of-period level is the proper amount to use in the calculation of income tax expense, while Public Staff witness Toms' position is that interest expense based on the Public Staff's recommended capital structure, embedded cost of debt, and rate base including interest expense related to the Job Development Investment Tax Credit (JDITC) should be used by the Commission in calculating state and federal income tax expense.

In support of his position, Company witness Reid testified in his prefiled testimony that Southern Bell can deduct for tax purposes only that interest expense related to its own debt. He testified that Southern Bell's tax liability is not reduced because of interest expense on AT&T debt. Further, he testified that to impute additional interest expense merely understates the Company's actual tax liability and the revenues necessary to the cost of doing business.

The Commission believes and so concludes that the level of interest expense used in the calculation of income tax expense to be included in the test year cost of service should be equal to the level of interest expense included in the cost of service to the extent that such treatment does not assign, attribute, or allocate hypothetical interest expense to funds realized from utilization of the JDITC.

With respect to the JDITC, in computing income tax expense, the Public Staff has taken an interest deduction for hypothetical interest expense which it assigns to funds arising from utilization of the JDITC, whereas the Company has not.

In numerous rate proceedings before the Commission the Public Staff has steadfastly maintained that the Revenue Act of 1971, which implemented the JDITC, permits the Commission to impute interest thereto for use in determining the test year level of federal income tax expense. Notwithstanding that, the Commission had consistently found, for reasons which need not be repeated here, that the Public Staff's position in this regard was and is incorrect in its entirety. The North Carolina Court of Appeals in Utilities Commission v. Carolina Telephone, 61 N.C. App. 42 (1983), affirmed the Commission findings in this regard, this matter having been appealed by the Public Staff. In the words of the Court

"The issue on appeal, as stated by the Public Staff in its brief, 'is whether the Commission erred as a matter of law in concluding that Section 46(f)(2) of the Internal Revenue Code requires that all effects of JDITC should be excluded from the determination of interest expense.'

G.S. 62-94 sets forth the standard of judicial review of orders of the Utilities Commission and includes the following:. . .

In this appeal we are called upon to interpret the applicable sections of the Internal Revenue Code to determine whether the Commission's order is affected by errors of law. We conclude that the order is not so affected.

Section 46(f)(2) of Title 26 of the Internal Revenue Code provides that JDITC will be disallowed with regard to public utility property in the following two circumstances.

> (A) Cost of service reduction.--If the taxpayer's cost of service for ratemaking purposes or in its regulated books of account is reduced by more than a ratable portion of the credit allowable by section 38 (determined without regard to this subsection), or
>
> (B) Rate base reduction.--If the base to which the taxpayer's rate of return for ratemaking purposes is applied is reduced by reason of any portion of the credit allowable by section 38 (determined without regard to this subsection).

The term "ratable portion" is explained in Section 46(f)(2):

> For purposes of determining. . .ratable portions under paragraph (2)(A), the period of time used in computing depreciation expense for purposes of reflecting operating results in the taxpayer's regulated books of account shall be used.

The following example of "ratable portion" appears in Section 1.46-6(g)(2) of the Tresury Regulations:

> (I)f cost of service is reduced annually by an amount computed by applying a composite annual percentage rate to the amount of the credit, cost of service is reduced by a ratable portion.

The Internal Revenue Service has published the following regulations implementing Section 46(f)(2):

> (2) Cost of service. (i) For purposes of this section, "cost of service" is the amount required by a taxpayer to provide regulated goods or services. Cost of service includes operating expenses. . . maintenance expenses, depreciation expenses, tax expenses, and interest expenses. . .
>
> (ii) In determining whether, or to what extent, a credit has been used to reduce cost of service, reference shall be made to any accounting treatment that affects cost of service. Examples of such treatment include reducing by all or a portion of the credit amount of Federal income tax expense taken into account for ratemaking purposes and reducing the

depreciable bases of property by all or a portion of the credit for ratemaking purposes.

(3) Rate base. (i) For purposes of this section, "rate base" is the monetary amount that is multiplied by a rate of return to determine the permitted return on investment.

(ii) In determining whether, or to what extent, a credit has been used to reduce rate base, reference shall be made to any accounting treatment that affects rate base. In addition, in those cases in which the rate of return is based on the taxpayer's cost of capital, reference shall be made to any accounting treatment that affects the permitted return on investment by treating the credit in any way other than as though it were capital supplied by common shareholders to which a "cost of capital" rate is assigned that is not less than the taxpayer's overall cost of capital rate (determined without regard to the credit). What is the overall cost of capital rate depends upon the practice of the regulatory body. Thus, for example, an overall cost of capital rate may be a rate determined on the basis of an average, or weighted average, of the costs of capital provided by common shareholders, preferred shareholders, and creditors.

Treas. Reg. 1.46-6(2)(i), (ii) and (3)(i), (ii) (1979).

Essentially, Section 46(f)(2) and the regulation provided that a utility remains eligible for the credit as long as cost of service is reduced by no more than "a ratable portion of the credit," and as long as no reduction is made in the rate base. The purpose of this scheme, as revealed by legislative history, is to permit the benefits of the credit to be shared by the consumers and the investors of the utility. H.R. Rep. No. 533, 92d Cong., 1st Sess., reprinted in U.S. Code Cong. & Ad. News 1825, 1839 (1971).

Pursuant to paragraph (A) of Section 46(f)(2), CT&T "flows through" directly to its customers an annual percentage of JDITC based upon the useful life of the property producing the credit and thereby reduces its tax expense, and thus its cost of service, by a ratable portion of the credit. This treatment of JDITC by CT&T is not at issue in the present case.

Pursuant to paragraph (B) of Section 46(f)(2), CT&T makes no reduction in its rate base on account of the credit and assigns the overall cost of capital rate to the capital generated by the credit.

The Public Staff advocates an additional adjustment due to the presence of JDITC. Assuming that, in the absence of JDITC, the capital otherwise supplied by JDITC would be contributed by all capital suppliers, including debt, in the same ratios as those suppliers exist in CT&T's capital structure, the Public Staff maintains that a hypothetical interest expense attributable to that portion of JDITC which would have been provided by debt, in the absence of JDITC, should be deducted from CT&T's income tax expense for ratemaking purposes, in addition to the ratable reduction in taxes already produced by amortization of the credit. The Public Staff asserts that this adjustment to income tax expense for ratemaking purposes is in accord with Section 46(f)(2) based upon the language in Treas. Reg. Section 1.46-6(b)(3)(ii) that JDITC be "assigned a 'cost of capital' rate that is not less than the taxpayer's overall cost of capital rate (determined without regard to the credit)". The

Public Staff also maintains that its position has been upheld in three federal court decisions and is therefore the correct one. Finally, the Public Staff contends that the ratepayers are entitled to an additional benefit from the proposed imputed interest on JDITC because they are the source of the cost-free capital provided by JDITC. We reject each of these arguments.

The Public Staff's interpretation of the pertinent regulation completely ignores the words which precede the phrase relied upon by the Public Staff. The regulation clearly states that, to determine whether an improper reduction in rate base has occurred, reference should be made to any accounting treatment which treats JDITC "in any way other than as though it were capital supplied by common stockholders. . ." The phrase relied upon by the Public Staff refers to the determination of the "overall cost of capital rate" which must be applied to JDITC under the regulation. As such, the phrase deals with the rate of return which the utility is entitled to receive on JDITC, but does not require that a utility's interest expense be calculated without regard to the credit (i.e., as though capital generated by JDITC were supplied by other sources of capital reflected in the utility's capital structure). Rather, the preceding phrase strongly indicates that in other instances, JDITC is to be treated as "capital supplied by common shareholders." The imputation of interest to a portion of JDITC as though supplied by creditors does not treat that portion of JDITC as though supplied by common shareholders and, in addition, reduces the cost of service by more than a "ratable portion" of JDITC. For these reasons, the adjustment proposed by the Public Staff contravenes Section 46(f)(2) and the regulation thereunder.

The cases cited by the Public Staff do not persuade us to interpret Section 46(f)(2) otherwise because each of the cases completely ignores the clear requirement in the regulation to that Section that JDITC be treated as 'capital supplied by common shareholders.'

In the case of Public Service Company of New Mexico v. Federal Energy Regulatory Commission, 653 F. 2d 681 (D.C. Cir. 1981), the main issue before the court was whether capital provided by JDITC should receive the overall or common equity rate of return. The court concluded that, for purposes of determining the overall rate of return, JDITC could be treated as capital supplied by all capital suppliers in the same proportion as those suppliers existed in the capital structure of the utility, absent the credit. The court further held that excluding JDITC from the capital structure of the utility did not alter the debit/equity ratio such that the utility's interest expense deduction was increased, resulting in an additional, impermissible reduction in cost of service. No issue of imputing interest to JDITC was before the court.

That issue was before the court in New England Power Company v. Federal Energy Regulatory Commission, 668 F. 2d 1327 (D.C. Cir. 1981), cert. denied, U.S., 102 S. Ct. 2928 (1982). However, in determining that the Federal Energy Regulatory Commission could require the utility to impute hypothetical interest to JDITC, the court relied on its earlier decision in Public Service Company of New Mexico, supra. Upon stating that, "(t)he question in this section is whether FERC may properly treat tax credit funds in relation to interest deduction in the same way it treats tax credit funds in relation to rate of return determination," the court quoted that portion of its earlier opinion in which it had approved the Federal Energy Regulatory Commission's treatment of JDITC as capital supplied by all capital

suppliers in a proportionate manner for purposes of determining the overall rate of return on capital. As we have previously stated, the questions of how to treat JDITC for purposes of determining interest expense for rate making purposes are separate issues. The court in New England Power Company did not treat them as such and failed to analyze in any way the tax laws or the arguments supporting the impermissible nature of the adjustment.

In Union Electric Company v. Federal Energy Regulatory Commission, 688 F. 2d 389 (8th Cir. 1981), the third case cited by the Public Staff, the court again relied upon that portion of the regulation under Section 46(f)(2) which permits a ratemaking agency to assign the "overall cost of capital rate (determined without regard to credit)" to JDITC and ignored the remainder of the regulation. Reasoning that because the regulation allows JDITC to be "treated like other capital" in one instance, the court concluded that the regulation should be interpreted to allow such treatment on the interest deduction issue as well. In our opinion, such reasoning contravenes the clear requirement of Section 46(f)(2)(A) that only a "ratable portion" of JDITC be flowed through to customers and of Treas. Reg. Section 1.46(b)(3)(ii) that JDITC be treated as "capital supplied by common shareholders," and we decline to follow it.

The final argument advanced by the Public Staff in support of imputing hypothetical interest to JDITC is that ratepayers are entitled to the additional benefit that would enure to them as a result of imputing interest to a portion of JDITC because they supplied the capital produced by JDITC by paying rates computed without regard to the tax credit (other than the ratable portion flowed through to them). The Commission disagrees. Without regard to the credit, a utility owes a certain amount of taxes at the end of its tax year upon which its rates are based. The credit essentially forgives or returns to the utility a portion of the taxes owed by it if certain capital assets have been purchased during the tax year. As such, the capital generated by JDITC comes from the Treasury of the United States, not the ratepayers of the qualifying utility.

Based upon the express language of Section 46(f)(2) and the regulation thereunder, as well as a consideration of the history and purpose of JDITC, that being primarily to benefit the utility so as to stimulate investment and thereby increase employment and additionally to share a ratable portion of the credit with ratepayers, we affirm the decision of the Commission to exclude all imputed interest expense related to JDITC in determining CT&T's income tax expense for rate making purposes."

Based on the foregoing, including the reasoning set forth in past Commission decisions, the Commission finds and concludes that no interest expense should be imputed to funds arising from utilization of JDITC.

Since the Commission has not adopted all of the components of taxable income proposed by the Company or the Public Staff, it has calculated and concludes that the appropriate amount of state and federal income tax expense for use herein is $68,746,000.

In summary, the Commission concludes that the proper level of intrastate revenue deductions for use in this proceeding is made up of the following:

(000's Omitted)

Item	Amount
Operating expenses	$350,666
Depreciation and amortization	114,862
Taxes other than income	70,607
Income taxes - state and federal	68,746
Total	$604,881

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 11

The evidence relating to this finding of fact is found in the testimony and exhibits of Company witnesses Morin and Dean and Public Staff witness Wilson. Witnesses Dean and Dr. Wilson also testified as to the appropriate capital structure.

Witness Dean recommended the use of the Bell System consolidated capital structure in this proceeding since Southern Bell will remain an integral part of the Bell System for all of 1983. However, as an alternative, he determined Southern Bell's capital costs directly by considering its post divestiture capital structure, the embedded cost of Southern Bell debt, and the cost of Southern Bell common equity capital. Witness Dean testified that the consolidated AT&T capital structure at March 31, 1983, consisted of 41.48% long-term debt, 56.69% common equity, and 1.83% preferred equity.

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Dr. Wilson testified that the use of AT&T's consolidated capital structure would mask the wide risk and cost of capital differences between AT&T's various regulated and unregulated enterprises. He testified that it is elementary that intrastate rates in North Carolina be based on a return allowance that accurately reflects the risk associated with the provision of intrastate service in North Carolina. To fail to do so would result in local exchange service rates improperly subsidizing AT&T's and Southern Bell's competitive enterprises.

Dr. Wilson testified that the cost of capital to any company, including AT&T, depends on both its business and its financial risks. Because AT&T is increasingly being forced out of its monopoly positions in some markets and into markets which have competitive potential, investors' perceptions of AT&T have changed and require now either a higher return or a safer capital structure. While this uncertainty about AT&T's ability to compete successfully translates into an increase in risk, the increase in risk does not apply equally to the markets in which no present or potential competition exists, most notably, the local exchange service market.

In recognition of the capital cost differences among Southern Bell's service categories, Dr. Wilson divided the Company's operations into three categories, based upon degree of risk. The first category contained Southern Bell's competitive and, therefore, most risky operations, such as customer premises equipment and interstate toll and private line. The second contained Southern Bell's least risky monopoly service offerings, including local exchange. Finally, the third category, state toll and private line, was treated as an intermediate category with respect to risk.

The varying degrees of competition and risk faced by Southern Bell in each category means that the capital structures appropriate to each are different. Dr. Wilson assigned the following capital structures to each category:

Item	%Debt	%Equity
Competitive	30.00	70.00
Monoply	60.00	40.00
Remainder	39.44	60.56

Based on his analysis of the operations of Bell System operating companies, Dr. Wilson assumed that 45% of Southern Bell's operations are in the competitive category, 30% are monopoly local exchange and related services, and 25% are state toll and state private line. The resulting weights of each of these service categories, plus the determination of the jurisdictional portion of Southern Bell's competitive offerings, produce a jurisdictional capital structure of 46.23% debt and 53.77% common equity.

After considering all of the evidence of record with respect to capital structure, the Commission concludes that the appropriate capital structure for use herein is as follows:

Item	Percent
Debt	45.00
Common Equity	55.00
Total	100.00

Consistent therewith, the Commision further concludes that the appropriate debt cost is 8.73%.

The evidence concerning the cost of common equity capital is found in the testimony of Company witness Morin and Public Staff witness Wilson. Since Southern Bell has not traded common equity, but issues common equity through the parent subsidiary relationship with AT&T, both of the witnesses testified that the appropriate estimate of the cost of capital to Southern Bell begins with an analysis of the cost of common equity to AT&T.

Dr. Morin testified that Southern Bell should be allowed an equity return of 17.0%. He argued that AT&T's cost of common equity capital is directly applicable to Southern Bell, without regard for differences in risk. Dr. Morin employed four methods in estimating the costs of equity and developed his return estimates as follows:

Method	Equity Cost Ranges
Capital market trends	17.68%
Discounted cash flow	16.96%
Comparable earnings	17.80%
Risk premium	17.52%

Dr. Wilson employed the DCF methodology in determining his rate of return recommendation. He utilized recent six-month market prices for AT&T plus the current annual dividend of $5.40 to produce a dividend yield of 8.5%. Dr. Wilson then relied on a combination of historical growth rates in earnings, dividend, and book value, along with recent market estimates of AT&T growth possibilities, and concluded that a reasonable expected growth rate compatible with the dividend yield was in the range of 3% to 5%. The combination of the yield plus the growth rate expectation results in a cost of equity measure of 11% to 14% for the AT&T holding company system.

Dr. Wilson also presented data about the earnings of utilities and nonregulated companies. Electric utilities have been earning 11% to 13% on equity over the past decade. Unregulated companies, which are more risky than AT&T by any conventional measure, earned 11% on common equity in 1982.

Dr. Wilson took exception to the fundamental premise of Dr. Morin's capital market and risk premium analysis that equity is more risky than debt and therefore commands a higher return. Dr. Morin's focus on the legal implications of the senior security owner's prior claim on assets is not the only reason for risk differences between common stock and bond investments. Bond returns are fixed and cannot change as economic circumstances dictate. Not only is it true that the cost spread between debt and equity varies over time, but it is also true that debt can cost more than equity because

investors perceive that investments in common equity are less risky than investments in long-term debt.

Bonds and preferred stock require that investors commit to the receipt of fixed interest payments plus a return of the principal. If money costs and interest rates rise, the owner of this security cannot have the annual interest or dividend payments increased. At the same time, call provisions prevent the receipt of a windfall if money costs and interest rates fall. This call feature, which is disadvantageous to bond holders, was recognized by Dr. Morin on cross-examination as one justification for the higher rate that had to be offered on Southern Bell's November 5, 1981, long-term debt issue. The differentially greater yield was attributable to the call provision that would have reduced investor's ability to "lock in" the higher returns that would otherwise be forthcoming from the investment. Investors in common equity do not bear this risk because the rate of return on equity is not fixed at the time the stock is issued. Increases in allowed equity returns by state regulatory authorities to offset higher money costs provide common equity investors with a hedge not present for bondholders and holders of preferred equity.

Several deficiencies were pointed out with respect to Dr. Morin's DCF calculation. First, Dr. Morin testified that the dividend value appropriate for use in computing expected yield is between $0.39 and $0.47 in excess of the present rate. He overstated the dividend by assuming that the dividend would grow at some speculative factor that investors have already incorporated into their estimates. It was shown during cross-examination that AT&T would have to increase its dividend in excess of 14% during the remainder of 1983 for Dr. Morin's dividend estimate to be realized. Dr. Morin testified that his survey of investors demonstrates that dividend growth is only likely to be about one-half that used in his upward adjustment. If his surveyed group is to be believed, reliance on Dr. Morin's adjustment will overstate the cost of equity.

Dr. Morin's expected growth rates were based largely on historical periods terminating prior to the announced reorganization of the Bell System and prior to overall declines in virtually all money costs during the past year. For example, had he made his five-year computation of AT&T's earnings per share growth over the period 1977-1982 rather than with 1974/76 - 1979/81 data, he would have obtained a compound annual rate of 4.13% rather than 8.71%.

Second, Dr. Morin's study focused exclusively on earnings and dividends growth, to the exclusion of book value growth. This is a major deficiency because book value, especially in a regulated industry where rate base is set equal to the net book cost of utility property, is the foundation for both earnings and dividends. Unless one assumes that either the dividend payout ratio or the earnings rate will increase without limit (hardly a reasonable assumption to make), book value growth must be recognized as the foundation for earnings and dividends growth. AT&T's five-year and 10-year compound annual book value growth rates (ending in 1982) have been 3.63% and 3.87%, respectively.

Dr. Morin tried to compute a series of expected rates of return for the companies he considered of comparable risk at AT&T as a check on his DCF calculations. One of the measures he used was the standard deviation of price changes for the stocks over a historical period. The average value for Dr.

Morin's group of high quality eastern U. S. electric utilities is 35% higher than was the comparable measure for AT&T. In addition, Dr. Morin relied on the Value Line ratings for financial strength for these utilities to form his comparable risk group. Only one company, New England Electric System, had the same high financial strength rating as AT&T. All of the other companies were more risky than AT&T on this measure.

Using the same selection criteria, Dr. Morin created two other samples of comparable risk companies. The first group included 55 gas and electric companies not previously examined. Once again, none of these companies had a standard deviation as low as AT&T, and only five had financial strength ratings equal to AT&T's. The second group included industrials with similar stock and bond ratings. Again the standard deviation measures were substantially greater, on average, for this group; their beta coefficients, on average, exceeded AT&T's by 31%.

Dr. Morin testified that he increased his DCF estimates based on an annual model by 50 basis points in order to account for the fact that AT&T pays dividends quarterly. He contended that this adjustment was necessary to reflect the higher present value of these dividends to the investors. The Commission does not agree. While it is true that the investors will earn a higher rate of return than the Company because of the availability of reinvestment profits, this does not mean that the additional return should be charged to the ratepayers. If ratepayers pay the extra amount, and quarterly distributions continue, investors' returns will rise, and they will still be able to earn more than the Company does. In fact, they would get their reinvestment profits twice: once from the ratepayers, under Dr. Morin's adjustment, and again when they reinvest their quarterly dividends. It is also true that investors would require a higher rate of return if the Company changed its dividend payment policy to an annual distribution plan. This does not mean, however, that ratepayers should have to pay a higher return in their rates. The Company could continue to collect revenues monthly and, holding the dividend amounts until the end of the year, could reinvest on behalf of the investors. The only difference would be that the Company rather than the investors is reinvesting the dividends during the year.

Southern Bell offered further testimony of Dr. Morin in rebuttal to Dr. Wilson. Dr. Morin contended, among other things, that Dr. Wilson's implementation of the DCF formula was incorrect in that he had calculated AT&T's dividend yield using a past dividend. He agreed on cross-examination, however, that Dr. Wilson had, in fact, used the current $5.40 dividend rate and that $5.40 was the rate projected by Value Line through 1987. He also agreed that, while his testimony assumes that investors who purchased AT&T stock in January 1983 were expecting a dividend increase, as of the end of July no increased dividend had been declared. Moreover, he offered no opinion as to when a 1983 increase might occur.

Dr. Morin also criticized Dr. Wilson's reliance on Value Line growth forecasts for AT&T, citing several higher growth projections by security analysts. Yet, Dr. Morin himself praised Value Line's forecasting capability and stated that it is a prestigious firm with an excellent track record. Quoting ostensibly from a study by Brown and Rozeff in the March 1978 Journal of Finance, titled "The Superiority of Analyst Forecasts as Measures of Expectations: Evidence from Earnings," he extended the authors' conclusions having to do with Value Line in the forecasting area to other

analysts generally. Value Line's reputation and capability notwithstanding, Dr. Morin nevertheless excluded the Value Line forecast in arriving at his truncated mean of analysts forecasts, stating, "I believe Value Line is a little low myself."

Dr. Morin also suggested that Dr. Wilson had rejected AT&T's historical growth rates and instead favored those of partially-owned subsidiaries. This, as well as the suggestion that Dr. Wilson added AT&T's dividend yield to a non-AT&T growth rate, is a distortion of Dr. Wilson's testimony on both direct and cross-examination. It is clear from Dr. Wilson's testimony that he used both and, as shown in his exhibits, that both are consistent with the 3%-5% growth estimates used in his DCF calculation.

Dr. Morin contended further that an additional return should be allowed to cover the cost of issuing new common equity. He disagreed with Dr. Wilson's position that no such allowance was needed absent a showing that issuance costs would be incurred and that, if there were an allowance, it should match those costs Dr. Morin argued, in effect, that the allowance should be retroactive to cover issuance costs incurred in the past and that the fact that no public offerings were anticipated over the 1983-84 period was irrelevant. Dr. Morin also contended that Southern Bell's customers should pay the 5% discount market that AT&T's stockholders receive when they purchase stock through the AT&T reinvestment plan. The Commission observes that, when stockholders buy at a discount from market, this dilutes the book value of the holdings of all equity investors. Those who participate in the reinvestment plan, therefore, benefit at the expense of those who do not. Under Dr. Morin's proposal, this expense would shift to the customers, thereby relieving the stockholder who does not take advantage of the plan of the burden of subsidizing the one who does. The Commission can see no merit in requiring the customer to help pay for such stock purchases.

Dr. Morin indicated that competition is intensifying and is viewed, by some, as a threat to Southern Bell's future growth. He agreed, however, that bypass technologies such as microwave and satellite telecommunications have been in existence for quite some time. He also agreed that satellite telecommunications is used primarily for toll calls. Dr. Morin stated, on cross-examination, that he did not know if bypass was taking place with microwave or cable technologies. He agreed that Southern Bell itself had a cellular mobile franchise in North Carolina and acknowledged that he could not think of any potential supplier of local exchange service except Southern Bell and knew of no ventures being formed to bypass the local exchange network in North Carolina.

Finally, Dr. Morin accused Dr. Wilson of interchanging conceptual frameworks - cost of financing and risk to which funds are exposed - "to suit the purposes at hand," implying that he subscribed to and then rejected the double leverage approach. Dr. Wilson's testimony explained that he did not recommend the double leverage approach in this case because of the impending breakup of AT&T. Dr. Morin has apparently misread Dr. Wilson's testimony on this question.

The determination of the appropriate fair rate of return for the Company is of great importance and must be made with great care because whatever return is allowed will have an immediate impact on the Company, its stockholders, and its customers. In the final analysis the determination of a fair rate of

return must be made by this Commission, using its own impartial judgment, and guided by the testimony of expert witnesses, and other evidence of record. Whatever return is allowed must balance the interests of the ratepayers and investors, and meet the test set forth in G.S. 62-133(b)(4):

> "...(to) enable the public utility by sound management to produce a fair return for its shareholders, considering changing economic conditions and other factors, as they exist, to maintain its facilities and services in accordance with the reasonable requirements of its customers in the territory covered by its franchise, and to compete in the market for capital funds on terms which are reasonable and which are fair to its customers and to its existing investors."

The return allowed must not burden ratepayers any more than is necessary for the utility to continue to provide adequate service. The North Carolina Supreme Court has stated that the history of G.S. 62-133(b):

> "...supports the inference that the Legislature intended for the Commission to fix rates as low as may be reasonably consistent with the requirements of Due Process Clause of the Fourteenth Amendment to the Constitution of the United States..." State ex rel. Utilities Commission v. Duke Power Co., 285 N.C. 377, 206 S.E.2d 269 (1974).

The nature of the evidence in a case such as this makes it extremely difficult to balance all of the opposing interests, since much, if not all, of the evidence is based on individual witnesses' perceptions, and interpretations of trends and data from the capital markets. The Commission has considered carefully all of the relevant evidence presented, with the constant reminder that whatever return that is allowed will have an immediate impact on the Company, its stockholders, and its customers. The Commission must use its impartial judgment to ensure that all the parties involved are treated fairly and equitably. In coming to a final decision on this matter, the Commission is not unmindful of the upward pressure on capital costs generally present in the economy over recent years. The Commission is also aware of the recent downward trend in interest and other capital costs.

Based upon the foregoing and the entire record in this docket, the Commission finds and concludes that the fair rate of return that Southern Bell should have the opportunity to earn on the original cost of its rate base is 12.04%. Such fair rate of return will yield a fair return on common equity of 14.75%, after payment of interest obligations.

The Commission cannot guarantee that the Company will, in fact, achieve the level of returns herein found to be just and reasonable. Indeed, the Commission would not guarantee it if it could. Such a guarantee would remove necessary incentives for the Company to achieve the utmost in operational and managerial efficiency. The Commission believes, and thus concludes, that the level of return approved herein will afford the Company a reasonable opportunity to earn a reasonable return for its stockholders while providing adequate and economical service to ratepayers.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 12

The Commission has previously discussed its findings and conclusions concerning the fair rate of return which Southern Bell Telephone and Telegraph Company should be given the opportunity to earn.

The following schedules summarize the gross revenues and the rates of return which the Company should have a reasonable opportunity to achieve based upon the increases approved herein. The schedules, illustrating the Company's gross revenue requirements, incorporate the findings and the conclusions, heretofore and herein made by the Commission.

In determining the level of increase in local service revenues approved herein, the Commission has given effect to the additional revenues that Southern Bell is expected to realize as a result of the increase in intrastate toll rates approved in Docket No. P-100, Sub 64. The Commission fully recognizes, should the Recommended Order issued in said docket not become the final Order of the Commission, that it may become encumbent upon the Commission to modify its decision as set forth herein.

SCHEDULE I
SOUTHERN BELL TELEPHONE AND TELEGRAPH COMPANY
NORTH CAROLINA INTRASTATE OPERATIONS
DOCKET NO. P-55, SUB 816
Twelve Months Ended October 31, 1982
(000's Omitted)

Item	Present Rates	Approved Increase	After Approved Increase
Operating Revenues			
Local service	$441,572	$20,330	$461,902
Toll service	231,467	16,336	247,803
Miscellaneous	53,173	-	53,173
Uncollectibles	(5,009)	(255)	(5,264)
Total operating revenues	721,203	36,411	757,614
Operating Revenue Deductions			
Current maintenance expense	157,060	-	157,060
Depreciation and amortization	114,862	-	114,862
Traffic expense	24,232	-	24,232
Commercial expense	66,886	-	66,886
General expenses	28,599	-	28,599
Relief and pensions	45,209	-	45,209
General services and licenses	9,416	-	9,416
Other general and miscellaneous expenses	19,264	-	19,264
Operating taxes - other than income taxes	70,607	2,189	72,796
Income taxes	68,746	16,851	85,597
Total operating revenue deductions	604,881	19,040	623,921
Net operating income for return	$116,322	$17,371	$133,693

SCHEDULE II
SOUTHERN BELL TELEPHONE AND TELEGRAPH COMPANY
NORTH CAROLINA INTRASTATE OPERATIONS
DOCKET NO. P-55, SUB 816
STATEMENT OF RATE BASE AND RATE OF RETURN
Twelve Months Ended October 31, 1982
(000's Omitted)

Item	
Investment in Telephone Plant	
Telephone plant in service	$1,585,174
Telephone plant acquisition adjustment	3,213
Depreciation reserve	(313,182)
Customers' deposits	(2,831)
Accumulated deferred income taxes	(187,948)
Pre-1971 investment tax credit	(1,520)
Net investment in telephone plant	1,082,906
Allowance for Working Capital	
Cash	7,500
Materials and supplies	16,633
Investor's funds provided for operations	12,196
Accounts payable - materials and supplies	(4,543)
Accounts payable - plant in service	(4,379)
Total working capital allowance	27,407
Original Cost net Investment	$1,110,313
Rate of Return	
Present Rates	10.48%
Approved Rates	12.04%

SCHEDULE III
SOUTHERN BELL TELEPHONE AND TELEGRAPH COMPANY
NORTH CAROLINA INTRASTATE OPERATIONS
DOCKET NO. P-55, SUB 816
STATEMENT OF CAPITALIZATION AND RELATED COSTS
Twelve Months Ended October 31, 1982
(000's Omitted)

Item	Ratio (%)	Original Cost Rate Base	Embedded Cost (%)	Net Operating Income
	Under Present Rates			
Long-term debt	45	$ 499,641	8.73	43,619
Common equity	55	610,672	11.91	72,703
Total	100	$1,110,313	-	$116,322
	Under Approved Rates			
Long-term debt	45	$ 499,641	8.73	$ 43,619
Common equity	55	610,672	14.75	90,074
Total	100	$1,110,313	-	$ 133,693

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 13

Company witnesses Savage and Hart, Public Staff witness Willis, the North Carolina Alarm Association witness Edwards, Attorney General witness Stutz, and North Carolina Textile Manufacturers Association witnesses Brown, Venable, and Jones presented testimony concerning Southern Bell's proposed rate structure. In addition, there were several public witnesses who appeared and testified in opposition to specific rate proposals and increases which they believed were not in their interest.

Witness Savage described the Company's overall pricing policies in developing the rate schedules he proposed in the proceeding. In general, these policies and principles are as follows: (1) supplemental charges and equipment are priced to cover the costs and to provide a contribution toward the Company's overall revenue requirement where possible so as to keep basic rates lower than would otherwise be possible; (2) to the extent practical, those customers responsible for costs should be the source of revenues to recover those costs; (3) consideration should be given to relative costs, demand for service, equity in the distribution of charges, and the development objectives of basic service; and (4) the rate structure should achieve a balance of administrative ease and acceptability and understandability by customers.

These pricing principles, according to witness Savage, were subsequently applied to formulate rate changes for basic exchange service, charges applicable under special conditions, telephone answering service facilities, key and pushbutton telephone service, private branch exchange service, central office nontransport service offering, miscellaneous and auxiliary equipment, connecting arrangements, data service, mobile telephone service, obsolete services, and intraexchange private line services. Basic flat rate increases of $4.30 to $6.75 per month for residential individual lines, and $8.45 to $11.80 per month for individual line business rates were recommended. Additionally, the Company proposed the regrouping of 12 of its exchanges due to growth in their calling scopes. The Company filed tariffs with its application which, if adopted, would produce an increase of approximately $122 million (after June 3, 1983, revision) in annual revenue.

Witness Hart presented the result of the Company's direct cost study relating to intraexchange channel services, upon which the proposed rates were based, and described the methodology used in the study.

Witness Willis expressed his recommendations on the Company's proposed rates for directory assistance services, intraexchange channel services, rotary line service, PBX trunk service, semipublic telephone service, and its main centrex-co PBX trunk service. He also gave his recommendation on the Company's proposal to charge for the installation of inside wiring and its maintenance on a time and materials basis.

Concerning the Company's proposal to increase its directory assistance charge from $0.20 to $0.35 per request, witness Willis indicated that his recommendation to allow the Company's proposal was consistent with the Public Staff's position in Docket No. P-100, Sub 64. He stated that his calculation of an increase in revenues of $1,019,990 under this proposal excluded the repression of units which was assumed by the Company.

With respect to intraexchange channel service, witness Willis recommended an increase in revenues for these services of $5,782,453 which was the result of limiting the recurring charges to a 30% increase by category and increasing the nonrecurring charges to the level of rates proposed by the Company. According to witness Willis, his calculations for these services excluded any assumed repression in units. When asked on cross-examination what he thought would be the effect of a price increase on the number of units demanded, he answered that it would depend upon many things which may or may not happen in the future, such as changes in the levels of income, inflation, and unemployment. Additionally, he indicated that, while he did not make a formal study, he reviewed a number of USOC codes which he could identify from the last rate case prior to an increase in rates and compared them to the units shown in this case. It was his observation that there were more increases in units of service than there were decreases in units of service.

Witness Willis, during cross-examination, testified that his recommendation regarding increases in intraexchange channel services was generally consistent with the Public Staff's testimony in the toll case and was related to the revenue cost relationship shown in the Company's embedded direct analysis. He stated that the Company's embedded direct analysis indicated that the intraexchange channel service revenues needed to be increased by 61% to match its costs. He remarked that the Public Staff was recommending an increase of approximately $12.2 million for the Company's interexchange and intraexchange channel services, which would cause an average increase of approximately 36%. Witness Willis stated that the Public Staff's recommendation would not bring the Company's state private line revenues up to the aggregate revenue requirement computed in either the Company's direct current analysis or its embedded direct analysis.

Witness Willis recommended that ratios which had previously been approved by this Commission for other companies be permitted for use for the Company's rotary line, PBX, and semipublic telephone service. This would set rotary line service at 1.5 times the business one-party line rate, the PBX trunk rate at 2.0 times the business one-party line rate, and the semipublic line rate equal to the business one-party line rate. Witness Willis concurred with the Company's proposal to reduce the main centrex-co PBX trunk rate from 1.547 times the PBX trunk rate to equal the PBX trunk rate.

During cross-examination, witness Willis clarified his recommendation not to change rates relating to inside wiring for which the Company had proposed decreases of approximately $12 million. He commented that he usually agreed with reductions in rates but this particular category of service had a revenue to costs relationship of .31, according to the Company's imbedded direct analysis, which would decrease to approximately .09 if the reductions were allowed. Witness Willis further explained that these reductions would cause the exchange services for both business and residential customers to increase due to the application of residual pricing, which in return would cause residential services to subsidize business inside wiring.

When asked if he was recommending an increase in service charges, witness Willis stated that he was not, because the Commission had allowed a 77% increase in total service charges and a 98% increase in the minimum charge to establish residential service in the last rate case. Additionally, he stated that the proposed rates, if allowed, would cause an increase in service charges of over 200% over the last one and one-half years.

Concerning the Company's proposals for time and materials pricing for inside wiring and maintenance activities, witness Willis explained that the Public Staff had previously opposed similar tariff proposals in Docket Nos. P-7, Sub 670, and P-10, Sub 415. He noted that, more recently, the Public Staff opposed Southern Bell's tariff provisions for time and materials pricing in Docket No. P-100, Sub 64, which were identical in concept to the tariffs proposed in this proceeding. It was his recommendation that the Commission disallow the Company's proposals for time and materials pricing for inside wiring and maintenance in this docket.

Witness Willis' last recommendation was to reduce basic local exchange rates by $15,506,523 and to leave those rates which he did not address unchanged, which would offset the increase produced by his specific rate changes as well as effect the $8,704,080 revenue reduction in local service revenues produced by the Public Staff.

Based upon all of the evidence of record regarding rate design and tariff proposals, the Commission concludes that rates designed in accordance with the guidelines set forth in Appendix A attached hereto will be just and reasonable.

IT IS, THEREFORE, ORDERED as follows:

1. That the Applicant, Southern Bell Telephone and Telegraph Company be, and is hereby, allowed to adjust its telephone rates and charges so as to produce, based upon the adjusted test year level of operations, an increase in local service revenues of $20,330,000.

2. That the Applicant be, and is hereby, required to propose specific tariffs reflecting changes in rates, charges, and regulations to effect the increase in revenues approved herein in accordance with the guidelines set forth in Appendix A attached hereto within five working days of the date of this Order. [Five copies required]. Workpapers supporting such proposals should also be filed with the Commission. [Five copies required]. (Formats such as item 30 of the minimum filing requirement, N.C.U.C. Form P-1 are suggested). Comments to the Company's rate schedule proposals shall be filed within five working days thereafter.

3. That the rates, charges, and regulations necessary to produce the annual gross revenues authorized herein shall become effective upon the issuance of a further Order approving the tariffs filed pursuant to Ordering Paragraph 2 above.

4. That Southern Bell be, and is hereby, authorized to begin capitalizing AFUDC on short-term CWIP.

5. That Southern Bell shall give notice of the rate increase allowed herein by bill insert mailed to each of its North Carolina customers during the next billing cycle following the filing and acceptance of the rate

schedules described in Ordering Paragraph 2 above. Such Notice to Customers shall be submitted to the Commission for approval prior to issuance.

ISSUED BY ORDER OF THE COMMISSION.
This the 14th day of September 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sandra J. Webster, Chief Clerk

APPENDIX A
Southern Bell Telephone and Telegraph Company
Docket No. P-55, Sub 816
Rate Design Guidelines

1. The following schedule of price relationships for monthly rates directly related to basic access lines is just and reasonable.

Item	Relationship
Rotary Line Service	50% of 1FB or 1FR
PBX Trunks	
Flat rate	200% of 1FB
Message rate	60% of Flat Rate Trunk
Main PBX - Centrex Trunk	100% of Flat Rate Trunk
Centrex-CO Group "A" Exchange	
Access Line	11.9% of Flat Rate Trunk*
Semi - Public Telephone	100% of 1FB

1FB = Business Individual Line Flat Rate
1FR = Residence Individual Line Flat Rate

*Per Centrex Main Station

2. The Company's proposal to regroup 12 exchanges is appropriate.

3. The local directory assistance (DA) service rate shall remain at $.20 per inquiry with an allowance of five local calls per month before this charge applies. Further, the Commission approves the Company's proposal to eliminate the present allowance for one toll directory assistance inquiry and all other Company word change proposals in the DA tariff (Section A3.8).

4. The Company's proposed tariffs for charging for the installation and maintenance of inside wiring on a time and materials basis is not in the public interest and is inappropriate.

5. The following schedule of nonrecurring service charges are just and reasonable.

Service Connection Charges

	Residential Amount	Business Amount
A. Service Order		
1. Primary	$27.10	$40.50
2. Secondary	10.50	14.25
3. Record	8.25	8.65
B. Premises Visit	10.00	10.00
C. Central Office Work	15.00	21.00
D. Inside Wiring	15.00	25.50
E. Equipment Work	6.00	8.00
F. Jack Charge	6.50	6.50

6. The Company's proposed increases in monthly private line rates are excessive and may place unreasonable burdens on subscribers to these services. The Commission concludes that the revenue increase to be derived from intraexchange channel services should be $5,782,453 which is composed of the following categories of service amounts:

Telephone Answering Service	$ 124,985
Foreign Central Office Service	491,128
Miscellaneous Service Arrangements	3,185,325
Private Line Intraexchange Service	1,981,015
Total Revenue Increase	$5,782,453

Such amounts result from limiting the recurring charges to a 30% increase by category, increasing the nonrecurring charges to the level of rates proposed by the Company and using unrepressed units at the end of the test period.

7. The rate increases proposed by Southern Bell for mobile telephone service and extended community calling are just and reasonable.

8. Monthly increases in local exchange access line rates for Southern Bell's 10 different rate groups shall not be increased in excess of the amounts set forth below:

MONTHLY INCREASE IN LOCAL EXCHANGE RATES

	Residence		Business	
RATE GROUP	One Party	Two Party	One Party	Two Party
1	$.35	$.30	$.90	$ .85
2	.35	.30	.90	.80
3	.35	.30	.95	.85
4	.35	.30	.95	.85
5	.40	.35	1.00	.90
6	.40	.35	1.00	.90
7	.40	.30	1.05	.95
8	.40	.30	1.05	.95
9	.40	.30	1.10	1.00
10	.40	.30	1.10	1.00

9. All other rates proposed to be increased by the Company are to be increased uniformly across-the-board without exceeding the Company proposed increase in such rates so as to produce the remaining amount of the increase in annual gross revenues approved herein.

APPENDIX B
DEPRECIATION RATES

Acct. #	Description	Reserve %	APPROVED Avg. Serv. Life Yrs.	Avg. Rem. Life Yrs.	Future Life Salvage %	Rem. Life Rate %
217	Building	17.6	40.0	33.0	3.0	2.4
221	Central Office Equip.					
	Step by Step	25.2	8.3	4.4	-4.0	17.9
	Cross Bar	19.9	10.0	5.5	-3.0	15.2
	Circuit-Others	21.5	13.5	9.2	-1.0	8.7
	Circuit-DDS	12.5	11.4	10.6	1.0	8.2
	Radio	46.6	16.5	10.1	12.0	6.5
	Electronic	7.7	19.4	16.7	3.0	5.4
231	Station Apparatus					
	Teletypewriter	26.9	9.5	6.6	-1.0	11.2
	Telephone & Misc.	25.7	11.3	8.1	1.0	9.1
	Radio	100.0	7.2	3.5	0.0	0.0
237	Station Connection					
	Outside Wire	-	-	-	-	5.0
234	Large PBX					
	PBX Electronic	24.0	8.2	6.4	5.0	11.1
	PBX Other	39.9	6.0	3.0	-4.0	22.4
	PBX DDS	2.9	6.8	5.4	2.0	17.6
241	Pole Line	29.1	26.0	21.0	-41.0	5.3
242.1	Aerial Cable					
	Exchange	27.2	22.0	14.1	-11.0	5.9
	Toll	7.4	20.0	8.8	94.0	0.3
242.2	Underground Cable					
	Exchange	17.4	31.0	24.0	9.0	3.1
	Toll	14.1	21.0	14.2	16.0	4.9
242.3	Buried Cable					
	Exchange	18.8	25.0	19.5	-5.0	4.6
	Toll	19.2	21.0	13.6	7.0	5.5
242.4	Submarine Cable					
	Exchange & Toll	48.2	30.0	19.4	-3.0	2.9
243	Aerial Wire	1.3	8.1	5.3	-38.0	25.8
244	Underground Conduit	12.8	65.0	57.0	-5.0	1.6
261	Furniture & Office Equip.					
	Storerooms & Others	12.4	23.0	20.0	2.0	4.3
	Computers & AMA	37.0	7.1	4.5	0.0	13.9
264	Veh. & Other Work Equip.					
	Motor Vehicles	44.8	8.0	4.1	16.0	9.7
	Other Work Equipment	9.1	15.5	13.7	15.0	5.6

DOCKET NO. P-78, SUB 50

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of		
Application of Westco Telephone Company for Authority to Adjust Its Rates and Charges Applicable to Intrastate Telephone Service in North Carolina	))))	ORDER OVERRULING EXCEPTIONS AND AFFIRMING ORDER

HEARD IN: The Commission Hearing Room, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina on Monday, January 24, 1983, at 2:00 p.m.

BEFORE: Chairman Robert K. Koger, presiding, and Commissioners Sarah Lindsay Tate, John W. Winters, Edward B. Hipp, A. Hartwell Campbell and Douglas P. Leary

APPEARANCES:

For the Applicant:

F. Kent Burns, Boyce, Mitchell, Burns and Smith, Attorneys at Law, Post Office Box 2479, Raleigh, North Carolina 27602

For the Public Staff:

Theodore C. Brown, Jr., Staff Attorney, Public Staff, North Carolina Utilities Commission, Post Office Box 991, Raleigh, North Carolina 27602

BY THE COMMISSION: On November 30, 1982, the Commission issued a Panel Order in this docket entitled Order Granting Partial Rate Increase.

On December 10, 1982, Westco Telephone Company (Westco or Applicant) filed Exceptions to the Commission Order and filed a Motion requesting that the Full Commission reconsider and alter or amend its Order of November 30, 1982, entered in this docket (P-78, Sub 50).

Oral argument on exceptions was subsequently heard by the Commission on January 24, 1983, with both the Applicant and the Public Staff having been represented by counsel.

On January 27, 1983, the Public Staff filed an Answer to Motion requesting the Commission to enter an Order affirming its Order issued on November 30, 1982, and deny that portion of Westco's motion of December 10, 1982, pertaining to reconsideration.

Based upon a careful consideration of the entire record in this proceeding, including the exceptions and oral argument heard thereon, the Commission is of the opinion, finds, and concludes that all of the findings, conclusions and ordering paragraphs contained in the Order are fully supported by the record. More specifically with respect to the issue of Construction Work in Progress (CWIP), the Commission finds that the Applicant provided insufficient evidence to determine whether there has been a proper matching of revenues and expenses

for the inclusion in rate base of $301,479 of CWIP which was actually placed in service by the end of the test year and $157,713 of CWIP which was placed in service prior to the close of the hearing. Further, the Commission finds and concludes that the Order issued November 30, 1982, should be affirmed and that each of the exceptions thereto should be overruled and denied.

IT IS, THEREFORE, ORDERED as follows:

1. That each of the exceptions to the Order filed herein on December 10, 1982, by Westco, be, and each is hereby, overruled and denied.

2. That the Order in this docket dated November 30, 1982, be, and the same is hereby, affirmed.

ISSUED BY ORDER OF THE COMMISSION.
This the 1st day of March 1983.

NORTH CAROLINA UTILITIES COMMISSION
Sandra J. Webster, Chief Clerk

(SEAL)

DOCKET NO. P-58, SUB 124

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of		
Application of Western Carolina Telephone Company for Authority to Adjust Its Rates and Charges Applicable to Intrastate Telephone Service in North Carolina	)	ORDER OVERRULING EXCEPTIONS AND AFFIRMING ORDER

HEARD IN: The Commission Hearing Room, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina on Monday, January 24, 1983, at 2:00 p.m.

BEFORE: Chairman Robert K. Koger, presiding, and Commissioners Sarah Lindsay Tate, John W. Winters, Edward B. Hipp, A. Hartwell Campbell and Douglas P. Leary

APPEARANCES:

For the Applicant:

F. Kent Burns, Boyce, Mitchell, Burns and Smith, Attorneys at Law, Post Office Box 2479, Raleigh, North Carolina 27602

For the Public Staff:

Theodore C. Brown, Jr., Staff Attorney, Public Staff, North Carolina Utilities Commission, Post Office Box 991, Raleigh, North Carolina 27602

BY THE COMMISSION: On November 30, 1982, the Commission issued a Panel Order in this docket entitled Order Granting Partial Rate Increase.

On December 10, 1982, Western Carolina Telephone Company (Western Carolina or Applicant) filed Exceptions to the Commission Order and filed a Motion requesting that the Full Commission reconsider and alter or amend its Order of November 30, 1982, entered in this docket (P-58, Sub 124).

Oral argument on exceptions was subsequently heard by the Commission on January 24, 1983, with both the Applicant and the Public Staff having been represented by counsel.

On January 27, 1983, the Public Staff filed an Answer to Motion requesting the Commission to enter an Order affirming its Order issued on November 30, 1982, and deny that portion of Western Carolina's motion of December 10, 1982, pertaining to reconsideration.

Based upon a careful consideration of the entire record in this proceeding, including the exceptions and oral argument heard thereon, the Commission is of the opinion, finds, and concludes that all of the findings, conclusions and ordering paragraphs contained in the Order are fully supported by the record. More specifically with respect to the issue of Construction Work in Progress (CWIP), the Commission finds that the Applicant provided insufficient evidence to determine whether there has been a proper matching of revenues and expenses for the inclusion in rate base of $2,569,744 of CWIP which was actually placed in service by the end of the test year and $251,514 of CWIP which was placed in service prior to the close of the hearing. Further, the Commission finds and concludes that the Order issued November 30, 1982, should be affirmed and that each of the exceptions thereto should be overruled and denied.

IT IS, THEREFORE, ORDERED as follows:

1. That each of the exceptions to the Order filed herein on December 10, 1982, by Western Carolina, be, and each is hereby, overruled and denied.

2. That the Order in this docket dated November 30, 1982, be, and the same is hereby, affirmed.

ISSUED BY ORDER OF THE COMMISSION.
This the 1st day of March 1983.

NORTH CAROLINA UTILITIES COMMISSION
Sandra J. Webster, Chief Clerk

(SEAL)

DOCKET NO. P-119, SUB 9

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of Patterson Anserphone Communications Enterprises, Inc. - Joint Application for Approval of Stock Transfer and Financing Pursuant to G.S. 62-111(a) and G.S. 62-161(b) with Hilda S. Patterson, President of PACE, and Carolinas RCC, Inc.	) ORDER GRANTING APPROVAL

BY THE COMMISSION: On January 28, 1983, Patterson Anserphone Communications Enterprises, Inc. (PACE), and Hilda S. Patterson, President of PACE and its sole stockholder, and Carolinas RCC, Inc., filed with this Commission "Joint Application for Approval of Stock Transfers and Financing Pursuant to G.S. 62-111(a) and G.S. 62-161(b)." The application states that PACE and the other applicants are seeking approval of the stock transfers and financing arrangements in order that PACE will be able to offer cellular radio service to its customers. The application also seeks a ruling or declaration that "Domestic Public Cellular Service," popularly known as "cellular mobile radio service" is an enhanced two-way mobile radio common carrier service and that PACE is authorized by its present certificate to offer cellular radio service as an enhanced RCC service without necessity for amendment or modification to its present certificates.

This Order is determinative of all issues of fact and law relating to the stock transfers and financing and is determinative of the facts necessary to the declaratory ruling which is sought. The declaratory ruling is being made by separate Order in the docket, reference to which is hereby made.

The Applicants propose to reorganize and restructure PACE through transfer of its Greenville RCC certificate and assets to its wholly owned subsidiary, Coastal Carolina Communications, Inc., and by stock redemption to convey the outstanding common stock of Coastal Carolina Communications, Inc., to Hilda S. Patterson. The effect of this reorganization and restructuring is to separate those RCC operations of PACE which are not currently eligible for cellular development from those which are eligible. Hilda S. Patterson will retain legal and effective control of those certificates, facilities, and operations which are not currently eligible for cellular. In order to obtain financing for cellular development in PACE's remaining franchised areas, Hilda S. Patterson has contracted to sell and convey, and Carolinas RCC, Inc., has contracted to purchase and own, all the outstanding stock of PACE remaining after the reorganization and restructuring. This sale of stock will change the legal and effective control of PACE's North Carolina certificates and its RCC operations in the company's franchised areas of Guilford, Durham, Orange, and Wake counties. Carolinas RCC, Inc., has contracted to act as a joint venturer with PACE in applying for FCC cellular licenses and in developing cellular in PACE's franchised areas. The verified application further states that, whether or not the joint venture entity or PACE obtains cellular licenses from FCC, PACE will continue to provide and improve its existing radio common carrier service to the public in its franchised North Carolina territories, and that PACE and Carolinas RCC, Inc., are contractually and legally bound to do so.

Upon consideration of the verified application as an affidavit, the four (4) Affidavits, and some 20 exhibits filed in accordance with Rule R1-16, the Commission makes the following

FINDINGS OF FACT

1. The Applicant, PACE, is a North Carolina corporation with principal offices in Raleigh, Wake County, North Carolina. It is a duly certificated and authorized public utility engaged in providing both one-way (paging) and two-way (mobile radio) intrastate radio common carrier service to the public for compensation throughout the North Carolina counties of Durham, Orange, and Wake and contiguous areas pursuant to certificates of Public Convenience and Necessity issued by the North Carolina Utilities Commission. PACE is also certificated to provide, and provides, radio common carrier service in those areas of Guilford County and environs, having High Point as a community of interest. PACE now has approximately 468 mobile radio (two-way) and 4,346 paging (one-way) stations with 2,664 subscribers in the aforesaid certificated areas. All of said service is as contemplated and defined by G.S. 62-119; all said service is provided pursuant to tariffs and rates duly approved by this Commission, and all of said utility services are rendered under the jurisdiction and supervision of this Commission.

2. The Applicant, Hilda S. Patterson, is a citizen and resident of Raleigh, Wake County, North Carolina. She is the sole owner and stockholder of PACE, and has been since 1977. She is also president of the company and is actively engaged full time in its management and operations. The preferred and common stock owned by Mrs. Patterson is unique in that it is not traded, has no established market value, and no dividend history. She is unable individually to pay in substantial amounts of equity capital and PACE cannot raise substantial equity capital by a public offering of additional common stock. PACE cannot obtain debt capital of any consequential amount without a pledge of Mrs. Patterson's personal assets. The amounts of capital which PACE currently needs to raise to improve and enhance its service exceeds the combined credit availability of PACE and its owner.

3. The Applicant, Carolinas RCC, Inc., is a North Carolina corporation with principal offices in Greensboro, Guilford County, North Carolina. It has 100,000 shares of authorized common capital stock of which 70,000 shares have been issued and are outstanding. Providence Journal Cellular Radio, Inc., a Rhode Island corporation, owns 50% and Communications Properties, Inc., a South Carolina corporation, owns 50% of the outstanding shares of Carolinas RCC, Inc. The company was formed and capitalized by the stockholder corporations and their affiliates for the purpose of acquiring, owning, and operating existing radio common carrier systems and facilities and combining them with the advanced two-way mobile radio service known as "Cellular Mobile Radio Service" wherever possible. The balance sheet for Carolinas RCC, Inc., filed with this application reflects total assets at March 31, 1983, of $21,168,817, of which $7,515,750 (35%) is stockholder equity. In addition to the balance sheet, Providence Journal Cellular Radio, Inc., a wholly owned subsidiary of Providence Journal Company, has obtained a letter of financial support from The Chase Manhattan Bank, N.A., which assures the availability of $20,100,000 in debt funds for the licensing and development of cellular radio communications in the Greensboro/High Point/Winston-Salem metropolitan area and the Raleigh/Durham/Chapel Hill area by Carolinas RCC, Inc., and its affiliates through joint venture agreements with existing certificated RCCs in

those areas. Michael P. Metcalf, who is Publisher and President of Providence Journal Company, and William G. Chafee, Assistant Secretary-Treasurer of Providence Journal Company, are members of the Board of Directors of Carolinas RCC, Inc. A letter signed by Robert L. Wolf, Vice President-Finance, of Providence Journal Company, is an exhibit included in the affidavit of Roger H. Henry, Jr., President of Carolinas RCC, Inc. The letter states:

> "Providence Journal Company is interested in providing on a continuing basis, not only the franchise one-way and two-way radio common carrier service offered by PACE to the public in PACE's existing certificated territories in both areas through existing licensed facilities, but in obtaining additional licenses permitting the expansion of PACE's existing two-way service with modern, state of the art service more nearly meeting the needs in those areas. Subject to the satisfaction of certain conditions, Providence Journal Company is committed to providing its subsidiary, Providence Journal Cellular Radio, Inc., with sufficient capital not only to enable it to cause Carolinas RCC, Inc., in which the subsidiary will hold a 50% ownership interest, to pay all obligations due you as seller of the stock, but also to continue and expand the present one-way and two-way service. The latter improvement is commonly referred to as cellular radio service....I can assure you that both Providence Journal Cellular Radio, Inc., and Providence Journal Company have approved the action of their affiliate, Carolinas RCC, Inc., in entering into a contract..."

Providence Journal Company, both individually and through its affiliated system, is highly experienced in the communications field. Jack C. Clifford, a member of the Board of Directors of Carolinas RCC, Inc., and Vice President-Operations, Providence Journal Cellular Radio, Inc., is personally familiar, not only with radio common carrier operations and technology, but with state and federal regulatory concepts and requirements. Roger H. Henry, Jr., President of Carolinas RCC, Inc., and one of its Directors, has prior management and financial experience as President and Chief Executive Officer of a large, successful multi-unit retail organization. Cecil L. Duffie, Jr., Vice President and Secretary and a Director, has a background and experience in investment banking, financial planning, and sales management.

4. Two-way (mobile radio) common carrier sevice presently offered by PACE in its franchised territory is no longer of sufficient grade, efficiency, and speed fully to meet the increasingly complex and expanding needs of the metropolitan areas of Raleigh/Durham/Chapel Hill and Greensboro/HighPoint/ Winston-Salem. Technology is now available to enable PACE's existing two-way service to be upgraded, made more efficient, and of greater speed and accessibility. This technology is called "cellular mobile radio service."

5. Under the "cellular" technology, the number of radio base stations is expanded so that as a two-way mobile radio subscriber moves through the service area, his call is automatically and instantly handed-off from one base station to another so that a subscriber may originate and terminate calls from any point within the service area. Two (2) or more callers can share the facilities simultaneously. Central switching equipment automatically routes calls through interconnection with the landline telephone network so that mobile-to-land and land-to-mobile calls can be completed as well as mobile-to-mobile calls. Unlike the conventional two-way calling now offered

by PACE in its two (2) franchised service areas, the "cellular mobile radio" system has a built-in capacity to expand as public demand increases, with a grade of service comparable to landline telephone service.

6. The Federal Communications Commission, which allocates frequencies, grants construction permits, prescribes channel loading criteria, and grants commercial licenses for the operation and maintenance of facilities utilized in one-way and two-way mobile radio systems, has identified the Durham/Orange/ Wake County (the Research Triangle Area) and the Greensboro/High Point/ Winston-Salem (the Piedmont Triad Area) metropolitan areas as two (2) of 90 major regional markets in which cellular facilities will now be licensed. There is a single, FCC-prescribed filing date for cellular licensing applications in the Durham/Orange/Wake County area. It is March 8, 1983.

7. PACE has an obligation as a utility certificated in North Carolina to provide improved and enhanced radio common carrier service throughout its franchised and established territories in the FCC identified areas. It can do so at substantial economies and, therefore, lower subscriber prices by making joint use of existing trained personnel, existing records and billing administration, and certain existing facilities, rights-of-way, and site locations.

8. The advanced and complex central system facilities and equipment needed for cellular radio service must be available to the public from the beginning to be used on an as-needed basis; the cellular equipment needed is new and unique and, therefore, more costly than it may be after further development; the process of obtaining licenses, construction permits, additional sites, and completing construction may require years; and the period of subscriber buildup will put stress on working capital requirements. Current estimates are that up to $5 million in new capital investment will be required in the first year in the Raleigh/Durham/Chapel Hill metropolitan area alone. PACE is not able to supply such capital without joint venture assistance.

9. The Applicants, Hilda S. Patterson and Carolinas RCC, Inc., have entered a binding contract, Exhibit No. 1 to the application, subject to approval by the Commission. In simplest terms, the contract provides for the combination of PACE's existing Durham/Orange/Wake County certificates, licenses, management, employees, facilities, billing, administration, operations, and cash flow with the financial, management, capital, and capital attraction strengths and skills of the affiliated system of Providence Journal Company in a joint venture. The purpose of the joint venture is that of designing, engineering, licensing, and installing cellular mobile radio service in the Raleigh/Durham/Chapel Hill greater metropolitan area through a single utility offering an improved and expanded class of two-way service in addition to the existing two-way and one-way service provided presently by PACE. Such combination of resources presents a favorable opportunity for the avoidance of duplicate facilities and investment, for the conservative use of land and air rights, and minimum interference and impact upon the environmental and scenic advantages of the area served. In addition, the provision of said services on an integrated, single company basis will permit savings in administrative overhead and billing, records, and advertising expenses. Tariff, rate, maintenance procedures, and complaint and outage handling and reporting would be simplified. In general, the foregoing and other advantages will permit greater economies of scale which will tend to produce lower rates, both for the conventional and the enhanced radio common carrier services of PACE, than would otherwise exist.

10. Cellular mobile radio service is an enhanced, or improved two-way radio common carrier service. It is not directly competitive to PACE's existing radio common carrier service. It is not a substitute for the existing regulated radio common carrier service of PACE in its franchised territory. The existing radio common carrier rates and service of PACE will not be impaired in any material sense by the addition of cellular two-way service.

11. The reorganization and restructuring of PACE through transfer of the Greenville certificate from PACE to its wholly owned subsidiary, Coastal Carolina Communications, Inc., followed by transfer of the outstanding stock in said subsidiary to Hilda S. Patterson in exchange for the 500 shares of PACE's preferred and 158 shares of its common stock does not dissipate or dilute the financial, service, or operating abilities, nor change the effective control of either corporation. It does not adversely affect the management, employees, rates, customers, or continuity of either utility in any material respect.

12. The sale and transfer of the remaining 4,842 outstanding shares of common stock of PACE from Hilda S. Patterson to Carolinas RCC, Inc., will not in any material respect adversely affect the quality and continuity of its existing franchised radio common carrier service, rates, or tariffs. Legal title to the assets, including its certificates and licenses, will remain in PACE without modification or amendment. The utility will continue under the jurisdiction of this Commission without change. The management, operating personnel, and business offices of the company will not be substantially changed. None of PACE's existing 2,664 subscribers will be affected by the transfer. Carolinas RCC, Inc., is contractually committed not to dissolve or liquidate PACE, or to sell and convey its stock in PACE for profit, or materially change its existing management policies and business practices, or deplete its cash reserves except as may be required in the ordinary course of PACE's business as a regulated utility to render adequate, first quality radio common carrier service to the public for compensation. All said commitments of Carolinas RCC, Inc., in the interests of continuity and improvement of PACE's existing utility service in its franchised areas are applicable, whether or not PACE is ultimately licensed by FCC to construct and commercially operate cellular mobile radio facilities in its franchised North Carolina area.

13. PACE's certificated territory in Guilford County and contiguous environs substantially overlaps territory certificated to Ans-A-Phone Communications, Inc. (Greensboro), and Services Unlimited, Inc. (Winston-Salem), and vice versa. However, PACE has not established radio common carrier service in duplication of or competition with either of said utilities. Instead, it has established its service within its territory and contiguous areas having a community of interest with High Point. By contractual arrangement, each of the three (3) radio common carriers owns a 16.33 1/3 equity interest in Carolina Advanced Radio Telephone Systems of the Triad, Inc. (CARS-Triad), which was formed by them for the purpose of mutual cooperation in developing cellular mobile radio common carrier service in the Davidson/Guilford/Forsyth/Randolph/Stokes/Yadkin County area identified by FCC as a major regional market for cellular licensing purposes. This transfer will not, therefore, adversely affect the present or proposed service to the public offered by the competing RCCs in the Guilford County area or the service offered by other public utilities in PACE's certificated service area in Guilford County and contiguous environs.

14. PACE is certificated to provide, and provides, one-way and two-way intrastate radio common carrier service to the public for compensation throughout the Durham/Orange/Wake County area, and contiguous areas. Its facilities and service is established in said areas. Rates supervised and approved by the Commission are charged throughout the service area. Its service and facilities throughout the area are adequate, subject only to the need for enhancement and improvement in accordance with the needs of the area. There is no other carrier commercially licensed by FCC or certificated by this Commission to provide one-way and/or two-way radio common carrier service to the public for compensation in the Durham/Orange/Wake County franchised service area of PACE. Therefore, the proposed transaction, including the enhancement of the existing authorized service with cellular, cannot unlawfully or adversely affect the service to the public by other utilities in PACE's Durham/Orange/Wake County service area.

CONCLUSIONS

1. The North Carolina Utilities Commission has jurisdiction over the subject matter of the application pursuant to G.S. 62-111(a) and G.S. 62-161(b).

2. PACE is a radio common carrier and is certificated to provide its service, and is providing said service, to the public for compensation throughout the franchised area of Durham/Orange/Wake and contiguous environs and in the Guilford County area and contiguous environs pursuant to Chapter 62, Article 6A, of the General Statutes of North Carolina (N.C.G.S. 62-119 et seq.) The scope of service which a radio common carrier may provide in its certificated area is defined in Chapter 62 under G.S. 62-119(3) as follows:

> "The term `radio common carriers' when used in this Article includes every corporation, company, association, partnership and person and lessees, trustees, or receivers, appointed by any court whatsoever owning, operating or managing a business of providing or offering a service for hire to the public of one-way or two-way radio or radiotelephone communications whether interconnected with the land line telephone system or not and licensed by the Federal Communications Commission, but not engaged in the business of providing a public land line message telephone service or a public message telegraph service. The terms `telephone or telegraph utilities, telephone or telegraph company,' or a `person operating telegraph or telephone lines' when used in this Chapter, shall not be construed as including radio common carriers. (1969, c.766; 1973, c.1274)."

Upon the findings of fact that PACE is authorized to provide two-way radio common carrier service to the public for compensation in its certificated and established territory; that cellular mobile radio service is a two-way radio common carrier service as defined in Chapter 62, Article 6A, of the General Statutes; and that the same is not a substitute for, but is merely an improved or enhanced, two-way radio common carrier service to be rendered in conjunction with PACE's existing radio common carrier service, it is thereupon concluded as a matter of law that PACE is authorized to provide cellular service in addition to its existing radio common carrier service throughout its presently franchised and established territories without necessity for

amendment or modification of its existing certificates of public convenience and necessity. For convenience and clarity this ruling is to be made in a separate order in the docket, and predicated upon these findings, conclusions, and order.

3. Based upon the foregoing findings of fact, it is concluded that the transactions herein proposed, including without limitation the restructuring and reorganization of PACE, the sale and transfer of the remaining 4,842 outstanding shares of common stock in PACE from Mrs. Hilda S. Patterson to Carolinas RCC, Inc., and the resulting joint venture arrangements for financing the development, licensing, construction, and operation of facilities for the provision of cellular mobile radio service in conjunction with PACE's existing intrastate one-way and two-way radio common carrier service in its certificated and established North Carolina territories are:

(i) For a lawful object within the corporate purposes of Patterson Anserphone Communications, Inc., and Coastal Carolina Communications, Inc.;

(ii) Compatible with and in furtherance of the public interest;

(iii) Necessary, appropriate, and consistent with the proper performance by Patterson Anserphone Communications, Inc., and Coastal Carolina Communications, Inc., of their respective services to the public;

(iv) To strengthen rather than impair the abilities of Patterson Anserphone Communications, Inc., and Coastal Carolina Communications, Inc., to perform their respective services to the public; and

(v) Reasonable, necessary, and appropriate for the purposes for which they are made.

4. The transactions proposed and described in the contract (Exhibit No. 1) and the application, including plans by Patterson Anserphone Communications, Inc., to obtain licenses for, design, develop, construct, and operate a public intrastate cellular mobile radio system throughout its existing franchised and established areas in conjunction with its existing two-way and one-way radio common carrier operations, and to finance the same through joint venture with Carolinas RCC, Inc., and/or its corporate affiliates, or otherwise, is justified by the public convenience and necessity, and the Commission should give its written approval as provided by G.S. 62-111.

5. Pursuant to G.S. 62-111, and the facts found herein, Carolinas RCC, Inc., as the person acquiring control of Patterson Anserphone Communications, Inc., through the transfer of 4,842 shares of common capital stock to it by Hilda S. Patterson, is fit, willing and able, financially and otherwise, to perform on a continuing adequate basis all of Patterson Anserphone Communications Enterprises' present radio common carrier utility services in its franchised areas of the state, and to improve and enhance said existing two-way and one-way service in said areas by, among other improvements, providing cellular mobile radio common carrier service in conjunction with PACE's existing regulated service to the public.

6. Further pursuant to G.S. 62-111 and the applicable facts herein found, the Commission concludes that the transactions proposed, viewed as a whole:

(i) Will not adversely affect the service to the public under the franchise held by Patterson Anserphone Communications Enterprises, Inc.;

(ii) Will not unlawfully affect the service to the public by other public utilities; and

(iii) Will tend to assure that the one-way and two-way radio common carrier service, which has been continuously offered by PACE on an adequate basis throughout its franchised areas for more than 15 years, will be continued, improved, and enhanced as technology permits.

7. The proposed combination of cellular development with the existing facilities, personnel, equipment, and land rights of PACE through joint venture financing is the most economically feasible and environmentally desirable method for meeting the present and future needs and demands of the public in the Research Triangle area for fast, efficient, and flexible two-way and one-way radio common carrier service at the earliest practicable time. Economies which are achievable by the combination will tend to assure lower consumer prices, both for the present and the enhanced services.

8. It is required by G.S. 62-119(3) that before a radio common carrier may offer its services to the public for compensation, it must be "licensed by the Federal Communications Commission." The existing for-hire radio common carrier facilities of PACE are fully and regularly licensed by FCC. PACE has not heretofore been eligible to apply to FCC for the necessary licensing to permit it to construct and operate commercial cellular radio common carrier facilities. The proposed transactions will make it possible for PACE through the described joint venture financing arrangements to make application to the FCC for appropriate licenses at the earliest available date, which is March 8, 1983. Therefore, PACE will not be permitted to enhance its present two-way service by adding cellular in its certificated area until it has obtained and filed with this Commission appropriate commercial facilities licenses or permits granted by FCC.

9. The North Carolina statutes, G.S. 62-119 and 124, distinguish radio common service from the services provided by landline telephone and telegraph companies. G.S. 62-119(3) defines a radio common carrier as one "not engaged in the business of providing a public land line message telephone or a public message telegraph service." G.S. 62-124 provides:

> "The provisions of this Article relate only to 'radio common carriers' as defined herein and are distinguishable from mobile radio telephone service offered by land line telephone or telegraph utilities regulated by the Commission. (1969, c. 766.)"

Based upon the facts found and applicable law, the Commission concludes that the existing and proposed intrastate service of PACE in its franchised territories is to be distinguished from that offered by landline telephone and telegraph companies and is not in competition therewith within contemplation of North Carolina law.

IT IS, THEREFORE, ORDERED as follows:

1. That the application and contract (Exhibit No. 1) filed in this docket on January 28, 1983, be, and the same is hereby, approved.

2. That Patterson Anserphone Communications Enterprises, Inc., is hereby authorized to assign and transfer to Coastal Carolina Communications, Inc., and Coastal Carolina Communications, Inc., is authorized to own and thereafter operate under North Carolina Utilities Commission Certificate No. P-109, and all assets and facilities used in connection with rendering radio common carrier service thereunder; provided that PACE and Coastal Carolina Communications, Inc., shall within ten (10) days after completion of the transfer adjust their utility plant property records to reflect the transfer of assets at original cost, less accumulated depreciation, and shall file appropriate tariff changes for billing and reporting purposes only.

3. That upon completion of the transaction approved in Paragraph No. 2, Patterson Anserphone Communications Enterprises, Inc., is hereby authorized to transfer the entire outstanding 10,000 shares of common stock which it holds in Coastal Carolina Communications, Inc., to Hilda S. Patterson in exchange for the entire outstanding 500 shares of 8% preferred stock and 158 shares of the outstanding 5,000 shares of common stock which she now holds in PACE, provided that the books of account of PACE shall be simultaneously adjusted to reflect said stock redemption and exchange.

4. That upon completion of the transactions authorized in Paragraph Nos. 2 and 3, Hilda S. Patterson is authorized to sell, transfer, and deliver to Carolinas RCC, Inc. Carolinas RCC, Inc., is authorized to purchase, hold and own, the remaining 4,842 shares of stock outstanding in Patterson Anserphone Communications, Inc., pursuant to and in accordance with the prices, terms, and conditions set out in the approved contract executed by the parties on January 26, 1983, and make proper entries on the company's books and records to reflect the transaction.

5. That Patterson Anserphone Communications Enterprises, Inc., is authorized and directed to provide to the public in its franchised and established territories the enhanced radio common carrier service known as "Domestic Public Cellular Service," or "Cellular Mobile Radio Service," in conjunction with its present one-way and two-way service without necessity for amendment or modification to its existing certificates of public convenience and necessity, provided that, before rendering said service to the public for compensation, PACE shall first file with this Commission evidence that the Federal Communications Commission has granted, or will forthwith grant, appropriate commercial licenses and/or construction permits for the cellular facilities it proposes to use; provided further that Patterson Anserphone Communications Enterprises, Inc., shall at least 45 days prior to commencing to provide cellular service to the public for compensation, file with the Commission for approval appropriate tariffs containing service regulations, rates, and charges for the service, together with justification therefor; provided further that cellular mobile radio service shall not be offered in substitution for, or in lieu of, any radio common carrier service now offered by PACE, except upon the prior written approval of this Commission.

6. That Patterson Anserphone Communications Enterprises, Inc., and Carolinas RCC, Inc., are authorized to enter into the joint financing venture

proposed in the Applciation and to participate with other corporations in the affiliated system of Providence Journal Company as may be necessary, appropriate, and lawful to assure that PACE has sufficient investment and working capital to enable it to qualify for necessary licenses and provide the existing as well as improved and enhanced service on a continuous, adequate, and reasonable basis.

7. That Patterson Anserphone Communications Enterprises, Inc., shall file with this Commission, in duplicate, a verified report of actions taken and transactions consummated pursuant to the authority herein granted within a period of thirty (30) days following the completion of the last of the transactions authorized herein.,

ISSUED BY ORDER OF THE COMMISSION.
This the 23rd day of February 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sandra J. Webster, Chief Clerk

DOCKET NO. P-119, SUB 9

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Patterson Anserphone Communications Enterprises, Inc., and Carolinas RCC, Inc., Joint Application for Approval of Stock Transfers and Financing Pursuant to G.S. 62-111(a) and G.S. 62-161(b)) DECLARATORY ORDER

BY THE COMMISSION: On January 28, 1983, Patterson Anserphone Communications Enterprises, Inc. (PACE), and Hilda S. Patterson, President of PACE and its sole stockholder, and Carolinas RCC, Inc., filed with this Commission "Joint Application for Approval of Stock Transfers and Financing Pursuant to G.S. 62-111(a) and G.S. 62-161(b)." The application states that PACE and the other applicants are seeking approval of the stock transfer and financing arrangements in order that PACE will be able to offer cellular radio service to its customers. The application also seeks a ruling or declaration that "Domestic Public Cellular Service," popularly known as "cellular mobile radio service" is an enhanced two-way mobile radio common carrier service and that PACE is authorized by its present certificate to offer cellular radio service as an enhanced RCC service without necessity for amendment or modification to its present certificate. This Order relates to the certificate question.

PACE is a duly certificated and authorized public utility engaged in providing both one-way (paging) and two-way (mobile radio) intrastate radio common carrier service to the public for compensation in the North Carollina counties of Durham, Orange, and Wake and contiguous areas pursuant to certificates of public convenience and necessity issued by the North Carolina Utilities Commission. PACE also is certificated to provide, and provides, radio common carrier service in those areas of Guilford County having High Point as a community of interest. PACE now has approximately 468 mobile radio and 4,346 paging stations with 2,664 customers in the aforesaid certificated areas all pursuant to tariffs and rates duly approved and supervised by the North Carolina Utilities Commission.

The application describes "cellular mobile radio service" as follows:

> "Under the 'cellular' technology, the number of radio base stations is expanded so that as a two-way mobile radio subscriber moves through the service area, his call is automatically and instantly handed-off from one base station to another so that a subscriber may originate and terminate calls from any point within the service area. Two (2) or more callers can share the facilities simultaneously. Central switching equipment automatically routes calls through interconnection with the land-line telephone network so that mobile-to-land and land-to-mobile calls can be completed as well as mobile-to-mobile calls. Unlike the conventional two-way calling now offered by PACE in its two (2) franchised service areas, the "cellular mobile radio" system has a built-in capacity to expand as public demand increases, with a grade of service comparable to land-line telephone service."

The application further states that the Federal Communications Commission has identified the Durham, Orange, and Wake County service area of PACE as one of the 90 major regional markets in which cellular facilities will be licensed. PACE states that it intends to seek such a license from the FCC and it has filed the subject application with this Commission so that it can show the FCC that it is financially able to construct the facilities, and that it is already authorized by the North Carolina Utilities Commission to provide cellular service under its existing certificate.

CONCLUSIONS

The Commission concludes that PACE is a radio common carrier certified pursuant to Chapter 62, Article 6A of the General Statutes of North Carolina (N.C. G.S. 119 et seq), and as such may provide cellular mobile radio service pursuant to its existing certificate. Radio common carrier is defined in Chapter 62 under G.S. 62-119(3) as follows:

> "The term 'radio common carriers' when used in this Article includes every corporation, company, association, partnership and person and lessees, trustees, or receivers, appointed by any court whatsoever owning, operating or managing a business of providing or offering a service for hire to the public of one-way or two-way radio or radiotelephone communications whether interconnected with the land line telephone system or not and licensed by the Federal Communications Commission, but not engaged in the business of providing a public land line message telephone service or a public message telegraph service. The terms, 'telephone or telegraph utilities, telephone or telegraph company,' or a 'person operating telegraph or telephone lines' when used in this Chapter, shall not be construed as including radio common carriers(1969, c. 766; 1973, c. 1274)."

Considering that "cellular mobile radio serice" is no more than an enhanced two-way mobile radio common carrier service, and that PACE is duly certified to provide radio common carrier service throughout its service territory, PACE is thereby authorized by its exisitng certificate to provide cellular service in its presently franchised and established territories without necessity for amendment or modification of its certificate.

IT IS, THEREFORE, ORDERED as follows:

1. That PACE is authorized to provide cellular mobile radio service pursuant to its existing certificate, and

2. PACE is authorized to file for approval, pursuant to G.S. 62-134, appropriate tariffs of rates and charges for providing cellular mobile radio service.

ISSUED BY ORDER OF THE COMMISSION.
This the 23rd day of February 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sandra J. Webster, Chief Clerk

DOCKET NO. P-84, SUB 20

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of	
Two Way Radio of Carolina, Inc. - Joint Application for Approval of Stock Transfer, Financing, and Pledge of Two Way's Stock Pursuant to G.S. 62-111, G.S. 62-160, and G.S. 62-161(b) with A. L. Guin, Jr., President of Two Way, and Carolinas RCC, Inc.	ORDER GRANTING APPROVAL

BY THE COMMISSION: On May 25, 1983, Two Way Radio of Carolina, Inc. (TWR), A. L. Guin, Jr., and Linda C. Guin (Sellers), and Carolinas RCC, Inc. (CRCC), filed with this Commission "Joint Application for Approval of Stock Transfers, Financing, and Improved RCC Service for Two Way Radio of Carolina, Inc." pursuant to G.S. 62-111(a), G.S. 62-160, G.S. 62-161(b), and Commission Rule R1-16. The application states that TWR and the other applicants are seeking approval of the stock transfers, financing arrangements (including the pledge of TWR's stock after completion of the transfer), and plan of operations in order that TWR will be able to license, construct, and operate "Domestic Public Cellular Radio Service" (cellular) in conjunction with its existing authorized two-way service and wide-area, digital, alphanumeric display, data, and other forms of improved or enhanced paging service (including regional and national tie-in capabilities) in conjunction with its existing authorized one-way service, both in TWR's existing franchised and established service areas or territories in North Carolina. The application also seeks a ruling or declaration that both cellular mobile radio common carrier service and the described improved one-way (paging) services are authorized by TWR's present certificates and may be offered as enhanced radio common carrier services on an areawide, through basis in its established service areas without necessity for amendment or modification to the service or territorial scopes of TWR's present certificates.

The application further states that neither cellular nor enhanced paging service can be licensed and offered in TWR's existing franchised areas on a comprehensive, full-area coverage, and through basis without obtaining large amounts of outside capital through joint venture arrangements between TWR and CRCC as detailed in the application and seeks approval of the pledge of TWR's stock to The Bank of New York by CRCC after it is acquired.

This Order is determinative of all issues of fact and law relating to the stock transfers, financing, and pledging of TWR's stock and is determinative of the facts necessary to the declaratory rulings which are sought and are being made by separate concurrent order in the docket, reference to which is hereby made.

In substance, the Joint Applicants request that the Commission do the following:

1. Give its written approval of the sale and transfer of a minimum of 389 shares (90%) of the outstanding 432 shares of common capital stock in TWR, and therefore control of its utility stock, certificates, and operations, by the owner-operators, A. L. Guin, Jr., and Linda C. Guin to, and the purchase, ownership, and control of said stock, certificates, and operations by, CRCC, together with the joint venture financing arrangements between TWR and CRCC, all according to the prices, terms, and conditions set forth in a contract executed by the parties on January 14, 1983, and in evidence as Applicant's Exhibit No. 4.

2. Issue a declaratory ruling confirming that TWR and/or its joint venture partner, Carolina Advanced Radiophone Systems of the Carolinas, Inc. (CARS-Carolina), is authorized by TWR's existing certificates to provide enhanced two-way (cellular) service and enhanced one-way (wide-area, digital, alphanumeric display, data, and other forms of through paging service, including regional and national network tie-in capabilities) service in conjunction with TWR's existing two-way and one-way radio common carrier utility service throughout TWR's existing franchised and established service areas, or territories, without amendment or modification to said existing certificates.

3. Approve the financing arrangements made by TWR, CRCC, and their joint venture partnership, CARS-Carolina, including the pledge of TWR's stock after acquisition by CRCC to The Bank of New York as security for the advancement of approximately $5,477,333 in loan funds to CRCC in connection with the acquisition of the control of TWR's operations, the reimbursement of funds already invested by TWR in engineering, designing, and applying for FCC licenses and construction permits incident to enhanced two-way (cellular) and one-way paging improvements and coverage, and assuring the availability to TWR of sufficient working and operating capital so that its existing service and subscribers are in no way burdened or diminished by the development and extension of the enhanced services.

4. Authorize the Applicants to file, pursuant to G.S. 62-134, appropriate tariffs of rates and charges for providing the enhanced services in conjunction with existing radio common carrier service, not less than 45 days prior to offering said enhanced services to the public in all or a part of TWR's existing territory and filing with this Commission evidence that facilities for rendering the particular enhanced service for which rates are proposed have been appropriately authorized or licensed by the Federal Communications Commission (FCC) and are constructed or under construction so as to give efficient public service on an as needed basis.

The verified application and supporting affidavits further state that, whether or not TWR and CRCC through their joint venture affiliate, CARS-Carolina, obtain cellular licenses and permits from the FCC, CRCC will

cause TWR to operate its existing utility operations on a continuing, adequate basis and will forthwith cause TWR's existing one-way service to be extended, improved, and enhanced on a modern, state-of-the art, full-area coverage basis.

Upon consideration of the verified application, 17 exhibits, and three affidavits, together with records judicially noticed, upon the investigation and report of the Commission Staff, and the Public Staff having raised no objections, the Commission makes the following

FINDINGS OF FACT

1. The Applicant, Two Way Radio of Carolina, Inc., is a North Carolina corporation with principal offices in Charlotte, Mecklenburg County, North Carolina. It is a duly certificated and authorized public utility engaged in providing both one-way (paging) and two-way (mobile radio) intrastate radio common carrier service to some 4,822 stations in its franchised and established territory in Mecklenburg, Union, Stanly, Cabarrus, Gaston, Lincoln, Rowan, Iredell, Catawba, Chatham, Cleveland, Burke, Alexander, Davie, Randolph, Rutherford, Moore, Hoke, Robeson, Scotland, Richmond, Montgomery, Anson, and Lee Counties pursuant to rates and tariffs duly approved and supervised by this Commission. All of said service is as contemplated and defined by G.S. 62-119.

2. The Applicant, A. L. Guin, Jr., and wife, Linda C. Guin, are the sole owners, managers, and operators of TWR. By contract dated January 14, 1983, the Guins have agreed to sell and transfer to CRCC a minimum of 389 (90%) of the total 432 shares of capital stock in TWR issued, outstanding and owned by them. Under the terms of the contract (Exhibit No. 4) the Guins are to remain active in the management and operations of TWR, but control of its stock, certificates, and operations will be in Carolinas RCC, Inc. The common capital stock of TWR has no established dividend history or market value. For all practical purposes TWR is operated as, and has capital attraction problems normally associated with, a proprietorship. To enhance, improve, and extend its utility service in accordance with the requirements of its certificate TWR must attract very substantial amounts of construction, working, and operating capital. The amount of capital currently required to be raised for utility construction exceeds the combined credit availability of TWR and its owners. Hence, the Guins have entered this and other contracts with CRCC for joint venture financing of the market studies, engineering and design, and applications to the FCC for facility licenses and construction permits to provide both enhanced cellular (two-way) service and enhanced paging (one-way) service throughout TWR's franchised and established territory in North Carolina. Through their verified application and affidavits, Applicants contend and the Commission finds that there is no viable alternative to said contracts if TWR is to improve, enhance, and extend its existing authorized service without burdening its existing service or rates.

3. The Applicant, Carolinas RCC, Inc., is a North Carolina corporation with principal offices in Greensboro, North Carolina. It has authorized common capital stock of 1,000 shares, of which 675,000 shares are Class A Voting Common Stock with par value of $1.00 per share and 325,000 shares are Class B Voting Common Stock with preferences, limitations, and relative rights of each of the classes being set out in CRCC's Articles of Amendment, which are on file with the Commission.

The entire 1,000,000 shares of authorized stock of Carolinas RCC, Inc., has been issued and is outstanding. It is held and owned as follows:

Owner	Class A	Class B
Providence Journal Cellular Radio, Inc.	500,000	None
Communications Properties, Inc.	None	325,000
Individual Private Subscriptions	175,000	None
Total	675,000	325,000

The equity ownership of CRCC is as follows:

Providence Journal Cellular Radio, Inc.	50.0%
Communications Properties, Inc.	32.5%
Private Investors	17.5%

By virtue of an irrevocable assignment of voting rights of the 175,000 shares held by a limited number of private investors to Communications Properties, Inc., the voting control of CRCC is:

Providence Journal Cellular Radio, Inc.	50.0%
Communications Properties, Inc.	50.0%

The forecasted balance sheet as of March 31, 1983, for Carolinas RCC, Inc. (Exhibit No. 9), shows total capitalization of $21,168,817, of which $7,515,750 is stockholders' equity and $13,405,867 is debt, for an equity ratio of 35.5%.

4. The 50% stockholder in Carolinas RCC, Inc., Providence Journal Cellular Radio, Inc., is a wholly owned subsidiary of Providence Journal Company, 75 Fountain Street, Providence, Rhode Island. Providence Journal Company directly and through various subsidiaries owns, controls, and operates two television stations, three earth satellite stations (receiving only), 21 cable systems, and numerous FCC authorizations for satellite and RCC activities, in adddition to the oldest newspaper in the United States. Robert L. Wolf, Vice President-Finance, Providence Journal Company, has affirmed to this Commission in writing that the Company and its affiliate, Providence Journal Cellular Radio, Inc., have the resources and will use them in the funding of the capital needs of TWR and the other RCC utility companies in the state under contract to Carolinas RCC, Inc., in assuring the adequate continuation and improvements of existing utility services and operations, or in cellular mobile radio service if licensed and permitted by FCC, or both. Michael P. Metcalf, Publisher and President of Providence Journal Company, is a member of the Board of Directors of Carolinas RCC, Inc. Jack C. Clifford, Vice President/Operations, Providence Journal Cellular Radio, Inc., is also a member of CRCC's board. The March 31, 1983, pro forma balance sheet of Providence Journal Cellular Radio, Inc., reflects $5,075,000 of investments by the Company in the stock of Carolinas RCC, Inc.

5. The 32.5% stockholder in Carolinas RCC, Inc., Communications Properties, Inc., is a South Carolina corporation with principal offices in Greenville, South Carolina. Its 32.5% equity in the assets of Carolinas RCC, Inc., is $2,178,881, subordinated to dividends to Class A stock in the cumulative amount of $10.15 and to distributions in liquidation. Communications Properties, Inc., has affirmed its commitment to provide equity investments to Carolinas RCC, Inc., in the ratio of its ownership so that the equity ratio of CRCC will be not less than 33 1/3% at any time without regard

to the amount of debt it contracts. The equity in Communications Properties, Inc., is owned one-third each by Roger H. Henry, Jr., Cecil L. Duffie, Jr. (both residents of Greenville, South Carolina), and Neil E. Jones, Englewood, Colorado. Roger H. Henry, Jr., is President, Chief Executive Officer, and a Director of Carolinas RCC, Inc. Cecil Duffie is Vice President and Secretary and a Director. Messrs. Henry and Duffie have expertise in financial planning, sales management, and operations, cost control, and organizational techniques for private corporations.

6. Carolinas RCC, Inc., was formed and capitalized by Providence Journal Company and Communications Properties, Inc., for the purpose of acquiring, owning, and operating existing for-hire radio common carrier systems and facilities and combining them with the advanced two-way mobile radio service known as "Cellular Mobile Radio Service" wherever possible. It has entered contracts for the purchase of controlling stock interests with the owner-operators of four (4) RCCs in North Carolina. These are:

Patterson Anserphone Communications Enterprises, Inc., serving in the Durham, Orange, and Wake County area of the greater Research Triangle Area as well as in the Piedmont Triad Area surrounding High Point in Guilford County.

Services Unlimited, Inc., serving in Forsyth, Davidson, Davie, Surry, Stokes, and Yadkin Counties of the greater Piedmont Triad Area.

Ans-A-Phone Communications, Inc., serving in the Guilford, Randolph, and Rockingham County area of the greater Piedmont Triad Area.

Two Way Radio of Carolina, Inc., serving 24 counties, including Mecklenburg, Union, and Gaston County area of the greater Metrolina Area.

The FCC has given its consent to the transfer of control of the sixty-three (63) licenses and permits held by the four North Carolina RCCs which have contracted with Carolinas RCC, Inc; and, with the approval of this Commission, CRCC has completed its acquisition of control of each of the four RCCs except TWR.

7. The two-way mobile radio common carrier services presently offered by TWR in the Metrolina region of the state are no longer of sufficient grade, efficiency, and speed fully to meet the increasingly complex and expanding needs of the public. Technology is now available to enable said existing service to be upgraded, made more efficient, and of greater speed and accessibility. This technology is referred to as "cellular mobile radio service." Under the cellular technology, the number of radio base sations is expanded so that as a two-way mobile radio subscriber moves through the service area, his call is automatically and instantly handed off from one base station to another so that a subscriber may originate and terminate calls from any point within the service area. Two (2) or more callers can share the facilities simultaneously. Central switching equipment automatically routes calls through interconnection with the land line telephone network so that mobile-to-land and land-to-mobile calls can be completed as well as mobile-to-mobile calls. Unlike the conventional two-way calling now offered, the "cellular mobile radio" system has a built-in capacity to expand as public demand increases, with a grade of service comparable to land line telephone service.

8. The Federal Communications Commission, which allocates frequencies, grants construction permits, prescribes channel loading criteria, and grants commercial licenses for the operation and maintenance of facilities utilized in one-way and two-way mobile radio systems, has identified the Mecklenburg/Gaston/Union County (Metrolina) metropolitan area as one of 90 major regional markets nationwide in which cellular facilities currently will be licensed. Accordingly, the FCC has allocated two (2) 20 MHZ groups of channels for cellular purposes to said market or "Cellular Geographic Service Area" (CGSA). Initially, one license will be available to land line telephone applicants, and one will be available to radio common carriers.

9. TWR, as the franchised utility serving the Mecklenburg/Gaston/Union CGSA, recognizes its public utility duty under the laws of this state to improve and enhance its two-way mobile radio service by providing cellular mobile radio service in conjunction with existing service in its franchised and established territories. It also recognizes that neither enhanced two-way nor enhanced one-way utility service can be accomplished at the expense of existing RCC service or subscribers, this being a stockholder obligation. After preliminary studies, the owners realized that cellular development costs (consisting of market studies, engineering, design and location of facilities, and other costs incident to filing and supporting the FCC application for cellular construction licenses and permits) exceeded their capital resources as owner-operators in the CGSA area within their franchised territories. The estimated capital investment, including one year's operating costs without net income, is $9,875,000.

10. The owner-operators have caused TWR to enter a joint venture with Carolinas RCC, Inc., as provided for in the contract for sale and transfer of the stock. Further pursuant to the sales contract, a separate North Carolina cellular corporation was formed, with ownership and FCC application as follows:

MECKLENBURG/GASTON/UNION

Carolina Advanced Radiophone Systems of the Carolinas, Inc. (CARS-Carolina), owned 50% by Two Way Radio of the Carolinas, Inc., 50% by CRCC; FCC Application filed March 8, 1983.

It is estimated that it will be 12 to 18 months from the date of FCC application to date of final FCC action. Since central system facilities and equipment must be available to the public from the beginning to be used by the public on an as needed basis, the unique equipment needed must be ordered, fabricated, and supplied, and construction sites must be selected and obtained on a final basis, a period of two years or more may lapse between FCC approval of a cellular license and permits and the actual operation of the system.

11. Under the contracts, Carolinas RCC, Inc., binds itself to provide the necessary capital and operating funds, not only to continue and improve all existing utility service, but to enhance those services through provision of wide-area, digital, and other forms of paging and, particularly, the licensing, construction, maintenance, and operation of cellular mobile radio facilities in conjunction therewith, both in the same franchised territory as now exists. This is to be done both for TWR and for the joint venture, CARS-Carolina. This financial support includes reimbursement of all utility

assumption of control by Carolinas RCC, Inc., as well as direct payment after the closing, so that existing utility services, rates, and subscribers will not be required to subsidize the enhanced services, or otherwise be adversely impacted thereby.

12. TWR already holds the necessary FCC licenses and permits to construct and operate for-hire facilities incident to providing wide-area (also called areawide) paging service in its Mecklenburg/Gaston/Union County service area and such service is in process. Under the contractual arrangements, CRCC upon acquisition is to reimburse TWR for such expenditures and thereafter is to supply TWR with the necessary capital, not only to complete the offering of wide-area paging service, but also to license, install, and operate the paging services known as digital, alphanumeric display, data, and other enhanced one-way services on a full-area coverage, through basis, including regional and national tie-in capabilities, as needed by the public. As already stated with regard to cellular, the enhanced one-way services also are to be provided in conjunction with existing services in the same territory and without diminishment or substitution therefor.

13. The balance sheet for CRCC shows that it has invested $1,040,000 in obtaining cellular and paging facility licenses, permits, and certificates from the FCC and state regulatory agencies associated with the four North Carolina RCCs with which it has contracted. A substantial portion of these costs are associated with the reimbursement of ongoing expenditures of TWR and its joint venture partner, CARS-Carolina.

14. As evidence that it will be able financially to support the continuation and improvement of TWR's existing utility services as well as the licensing and offering of enhanced (cellular) two-way and enhanced (wide-area, digital, etc.) one-way service in conjunction therewith, CRCC has presented the following letters of financial facility and support:

a. The Bank of New York; $10,000,000 available for cellular development in the Mecklenburg/Gaston/Union CGSA upon FCC licensing.

b. Rhode Island Hospital Trust National Bank; in excess of $25,000,000 available to the Providence Journal Company for "general business purposes including investments such as CRCC...in addition to those that have been made available in the past for cellular radio."

15. Carolinas RCC, Inc., on May 10, 1983, closed a Revolving Credit and Term Loan Agreement in the amount of $14,000,000 with The Bank of New York. This loan agreement (Exhibit No. 12) is in addition to the letters of financial facilities and support found in Finding of Fact No. 14. The loan provides for the advancement of funds in connection with the acquisition and subsequent control and operation of the four North Carolina RCCs named therein. It is a condition of the loan agreement that, as each increment of the $14,000,000 loan is advanced, the stockholders of CRCC will invest $1.00 of equity in CRCC for each $2.00 of loan funds advanced. The terms of this agreement have been met by Providence Journal Company (through its subsidiaries) and Communications Properties, Inc., at the time CRCC acquired the stock and assumed control of the certificates and North Carolina utility operations of Patterson Anserphone Communications Enterprises, Inc. (Docket No. P-119, Sub 9), Services Unlimited, Inc. (Docket No. P-91, Sub 19), and Ans-A-Phone Communications, Inc. (Docket No. P-83, Sub 9). The amount of loan

funds to be advanced by The Bank of New York to CRCC in connection with its acquisition of the control of TWR's certificate and operations is $5,477,333, plus $1,200,000 for working capital (Exhibit No. 13). The Providence Journal Company through its duly authorized subsidiaries is committed simultaneously to invest up to $2,177,000 in equity funds in CRCC, Inc., pursuant to the loan agreement. Communications Properties, Inc., is similarly committed to invest $1,088,000 in equity funds of CRCC at the same time as said $5,477,333 in loan funds and Providence Journal's equity investment are advanced and made to CRCC in connection with its acquisition of control of the operations and certificates of TWR. The stockholders of CRCC each has given its commitment to use the total $9,942,333 thereby made available to CRCC "to sustain the existing utility operations of Two Way Radio of Carolina, Inc., whether or not cellular authority is obtained from the Federal Communications Commission" (Exhibit No. 13-A and 13-B).

16. Pursuant to the contract for which approval is sought, TWR is required to be debt free at the time Carolinas RCC assumes control of its stock. The income statements of TWR show that for the period ended November 30, 1982, the utility had an actual net operating income of $500,173.59 and that, after adjustments to operating expenses, including interest charges, for changes required by the contract, the net operating income for the same period would have been $600,499.07.

17. Upon the capital commitments of CRCC and its stockholders to TWR to supply all capital needed in connection with the acquisition of control and the continuation, improvement, enhancement, and expansion of its existing North Carolina intrastate utility service whether or not FCC cellular licenses and permits are obtained, and pursuant to the terms and conditions of CRCC's Revolving Credit and Term Loan Agreement with The Bank of New York dated May 10, 1983, the Applicant, CRCC, proposes after acquisition of a minimum of 389 shares (90%) of the outstanding capital stock of TWR, to comply with the Security Agreement (which is a part of said Revolving Credit and Term Loan Agreement) with The Bank of New York granting to the Bank a continuing security interest in said TWR stock as collateral for the entire $14,000,000 loan made to CRCC. Since TWR's stock is and will remain closely held and not traded, the creation of a first lien against a controlling interest therein is a pledge of the faith or credit of the utility for the benefit of CRCC's stockholders and affiliated agents, including CRCC as the holding company, which could decrease or increase TWR's liabilities or assets as contemplated by G.S. 62-160. The stockholder-pledgor's commitment to use up to $6,530,000 of said loan proceeds exclusively to sustain the capital attraction position of TWR and maintain, enhance, and improve its existing utility services on an as needed basis is in the interests and to the benefit of its utility purposes and its future subscribers in North Carolina.

18. The pledging of TWR's stock by CRCC to The Bank of New York has no direct, material, or adverse impact on TWR or its existing service and subscribers in that TWR has no obligation as maker, surety, guarantor, or other contractual obligation to The Bank of New York or CRCC to pay any part of the loan principal, interest, or expenses associated therewith. TWR does not incur any debt or debt charges through the pledge of 90% of its stock by CRCC after acquisition. It remains debt free. The fact that a portion of the loan funds will be used by CRCC to reimburse itself for a part of the agreed purchase price of TWR's stock at several times the book value of TWR's common equity is of no effect upon utility subscribers in that under North Carolina

equity is of no effect upon utility subscribers in that under North Carolina regulatory accounting and rate-making practices, TWR's book value of common equity is increased only by plant, or rate base, investment and not by the price paid for the utility's stock. The only resultant risks to TWR, its utility operations, and its subscribers in this state are: (a) In the event of foreclosure under the Security Agreement, the control of TWR's certificates and utility operations in this state could change to a person, or persons, not qualified in the respects required by G.S. 62-111, et seq. It is not possible to determine the utility qualifications of a mortgagee or pledgee in advance and the Commission makes no determination of the utility operating abilities of the pledgee, or its nominee(s), pursuant to G.S. 62-111 at this time; and (b) In the event CRCC should apply its loan proceeds associated with TWR either to utility or nonutility uses other than those of TWR in this state thereby impairing the faith, credit, moneys, or property of TWR needed for its North Carolina intrastate utility operations, or should apply its said loan proceeds and equity funds imprudently, excessively, or unreasonably to TWR's utility plant or rate base in this state, thereby decreasing or increasing the utility liabilities or assets of TWR in this state with resultant unjustified subscriber impacts. There is no evidence that such is likely to occur. The commitments of CRCC and of its stockholders to use up to $6,650,000 of its combined equity and Revolving Credit and Term Loan agreement proceeds to sustain the existing utility operations of TWR on an as needed basis is to the contrary. Again, this Commission's authority to audit and investigate, and to require the observance of appropriate allocations, property records systems, accounting procedures, and rate-making adjustments are safeguards reducing such risks.

19. Upon completion of its acquisition of at least 90% of the stock of TWR pursuant to the contracts and application in this docket, CRCC will control, not only TWR's certificates, licenses, and utility operations in this state, but also the operations and activities of the cellular joint venture corporation, CARS-Carolina. It is in the interests of economic feasibility, planning, and coordination that CARS-Carolina ultimately be merged with TWR, or vice versa, so that a single utility provides both TWR's existing radio common carrier service and enhanced service throughout its existing territory. The acquisition of control of said certificates, licenses, and utility operations by CRCC, followed by its causing TWR and CARS-Carolina to merge and thereafter operate as a consolidated entity does not make Carolina RCC, Inc., a certificated, operating utility in this state. Rather, its status will be that of a parent, or holding, company in relation to TWR and/or CARS-Carolina. CRCC will be subject to regulation by this Commission as provided by G.S. 62-3,53,151, et seq.

20. The proposed provision of enhanced two-way radio common carrier service in conjunction with existing services of TWR within its existing, established, and franchised territory by a single business entity having common control of the appropriate radio common carrier certificates, licenses, permits, and assets does not adversely affect the service of any other utility serving in the area and is not anti-competitive. Rather, it is in the interests, both of TWR and CRCC and is in the public interest in that it will contribute to improving, enhancing, and expanding RCC service in the area in a cost-effective, coordinated, efficient, and economically feasible manner tending to result in lower consumer prices than otherwise would exist.

CONCLUSIONS

1. The North Carolina Utilities Commission has jurisdiction over the subject matter and the utility operations involved. All parties are properly before the Commission in this proceeding.

2. Two Way Radio of Carolina, Inc., is a radio common carrier and public utility and is certificated to provide, and is providing, said service to the public for compensation throughout its established service area of Mecklenburg, Union, Stanly, Cabarrus, Gaston, Lincoln, Rowan, Iredell, Catawba, Chatham, Cleveland, Burke, Alexander, Davie, Randolph, Rutherford, Moore, Hoke, Robeson, Scotland, Richmond, Montgomery, Anson, and Lee Counties.

3. The scope of service which a radio common carrier may provide in its certificated area is defined in Chapter 62 under G.S. 62-119(3) as follows:

> The term "radio common carriers" when used in this Article includes every corporation, company, association, partnership and person and lessees, trustees, or receivers, appointed by any court whatsoever owning, operating or managing a business of providing or offering a service for hire to the public of one-way or two-way radio or radiotelephone communications whether interconnected with the land line telephone system or not and licensed by the Federal Communications Commission, but not engaged in the business of providing a public land line message telephone service or a public message telegraph service. The terms, "telephone or telegraph utilities," "telephone or telegraph company," or a "person operating telegraph or telephone lines" when used in this Chapter, shall not be construed as including radio common carriers. (1969, c. 766; 1973, c. 1274.)

Upon the foregoing findings of fact that Two Way Radio of Carolina, Inc., is authorized to provide two-way radio common carrier service to the public for compensation in its certificated and established territory, that cellular mobile radio service is a two-way radio common carrier service as defined in Chapter 62, Article 6A of the General Statutes; and that the same is not a substitute for, but is merely an improved or enhanced, two-way radio common carrier service to be rendered in conjunction with existing radio common carrier service, it is thereupon concluded as a matter of law that TWR is authorized to provide cellular service in addition to its existing certificate of public convenience and necessity. For convenience and clarity this ruling is to be made in a separate order in the docket, and predicated upon these findings, conclusions, and order.

4. Upon the findings of fact that TWR is authorized to provide one-way radio common carrier service to the public for compensation as defined in G.S. 62-119(3), _supra_, and that it is licensed and authorized by FCC to provide wide-area, digital, alphanumeric display, data, and other forms of one-way paging, on an areawide basis with tie-in to other systems, and would have done so earlier but for competitive, practical, and financial limitations which have now been eliminated, it is concluded as a matter of law that TWR is entitled and required to make full use of its licenses and certificates in satisfaction of the public need and demand for through, continuous, and enhanced one-way common carrier service to the public in North Carolina without price of service discriminations between subscribers, communities, and

localities receiving substantially the same service. Further, said enhanced, improved, and expanded one-way service should be rendered in conjunction with existing radio common carrier service, including cellular mobile radio service, due to economic feasibility considerations.

5. Based upon the foregoing findings of fact, it is concluded that the transactions proposed and supported by the application and evidence in this docket, including without limitation, the sale and transfer of at least 389 shares of the 432 outstanding shares of common stock in TWR from the present shareholders to' Carolinas RCC, Inc., the joint venture arrangements for obtaining cellular licenses and permits, the financing and extension of wide-area, digital, and other forms of paging and cellular mobile radio service in conjuncion with existing radio common carrier service and the consolidation of both existing and enhanced radio common carrier services and operations in a single, integrated service area as now established and served by TWR are:

a. For a lawful object within the corporate purposes of TWR, CARS-Carolina, and CRCC;

b. Compatible with and in furtherance of the public interest;

c. Necessary, appropriate, and consistent with the proper performance by TWR of its respective services to the public;

d. To strengthen rather than impair the abilities of TWR to perform its respective services to the public; and

e. Reasonable, necessary, and appropriate for the purposes for which made.

6. The transactions proposed and described in the contract (Exhibit No. 4) and the application, including plans by Two Way Radio of Carolina, Inc., to obtain licenses for, design, develop, construct, and operate a public intrastate cellular mobile radio system in its existing franchised and established areas in conjunction with its existing two-way and one-way radio common carrier operations, and to finance the same through joint venture with Carolinas RCC, Inc., and/or its corporate affiliates, or otherwise, is justified by the public convenience and necessity; and the Commission should give its written approval as provided by G.S. 62-111.

7. Pursuant to G.S. 62-111, and the facts found herein, Carolinas RCC, Inc., as the person acquiring control of Two Way Radio of Carolina, Inc., through the transfer of at least 389 shares of common capital stock to it by the present owners, A. L. Guin, Jr., and Linda C. Guin, is fit, willing, and able, financially and otherwise, to perform on a continuing, adequate basis all of TWR's present radio common carrier utility services in its franchised areas of the state, and to improve and enhance said existing two-way and one-way service in said areas by, among other improvements, providing cellular mobile radio common carrier service and enhanced one-way service in conjunction with TWR's existing regulated service to the public.

8. Further pursuant to G.S. 62-111 and the applicable facts herein found, the Commission concludes that the transactions proposed, viewed as a whole:

a. Will not adversely affect the service to the public under the franchise held by Two Way Radio of Carolina, Inc.;

b. Will not unlawfully affect the service to the public by other public utilities; and

c. Will tend to assure that the one-way and two-way radio common carrier service which has been continuously offered by TWR on an adequate basis throughout its franchised areas for more than 15 years will be continued, improved, and enhanced as technology permits.

9. The proposed combination of cellular two-way enhancement and paging one-way enhancement with the existing facilities, personnel, equipment, and land rights of TWR through joint venture financing is the most economically feasible and environmentally desirable method for meeting the present and future needs and demands of the public in TWR's service area for fast, efficient, and flexible two-way and one-way radio common carrier service at the earliest practicable time. Economies which are achievable by the combination will tend to assure lower consumer prices, both for the present and the enhanced services.

10. The proposal of CRCC to grant The Bank of New York a continuing security interest in all the common stock of TWR it acquires from the Guins as collateral security for its "Revolving Credit and Term Loan" dated May 10, 1983, in the amount of $14,000,000, giving consideration to the commitment of CRCC's stockholders to use up to $6,530,000 of the loan proceeds to sustain the existing utility operations of TWR on an as needed and justified basis, will not in any manner deplete, reduce, conceal, abstract, or dissipate the earnings or assets of TWR, or decrease or increase its liabilities or assets, there being no contractual obligations or promises between TWR and the lender, and no contract between TWR and CRCC which imposes obligations for the loan on TWR. Consistent with North Carolina law, no change in the control of the utility certificates, operations, services, and rates of TWR, whether by sale and transfer, foreclosure, enforcement of liens, or otherwise, shall be valid and effective, nor shall TWR assume any liability or obligation as lessor, lessee, guarantor, indorser, surety, or otherwise, with The Bank of New York or Carolinas RCC, Inc., regarding or related to said loan to CRCC or the proceeds therefrom except upon prior written application to and approval by this Commission pursuant to G.S. 62-111 and G.S. 62-161. So long as the controlling stock interest in TWR or its successor is used as collateral security for loan proceeds for the benefit of CRCC, or any of its affiliated interests, CRCC shall have used its own equity together with said loan proceeds in the ratio of not less than 35% equity and 65% loan proceeds to the extent that $9,735,000 is to be used or available for use exclusively in paying for the capital stock of TWR, making improvements to TWR plant facilities and/or providing additional working capital for TWR's utility operations. Any notes or renewal of notes made or issued by TWR or its successor for any term whatsoever during the time a controlling interest in its stock is pledged or proposed to be pledged as collateral for the benefit of any holder of its stock shall be submitted to this Commission for approval in advance.

11. Pursuant to G.S. 62-119(3) and the applicable facts herein found, the Commission concludes that the existing for-hire radio common carrier facilities of TWR are fully and regularly licensed by FCC and that FCC has

duly and regularly granted its consent to the transfer of control of each of said licenses and permits. The joint venture, Carolina Advanced Radiophone Systems of the Carolinas, Inc. (CARS-Carolina), has not yet been licensed or issued construction permits for the CGSA area which is a part of the 24-county established and franchised territory here involved, and said licenses and permits may not reasonably be expected to be issued by FCC for several months. The operation of cellular facilities and the offering of said enhanced service whether or not in conjunction and consolidation with existing RCC service in the area cannot be instituted until such time as this Commission has been advised in writing that cellular licenses and permits have been issued, or that FCC has given notice of pending issuance, and cellular facilities have been or are being constructed pursuant thereto. However, TWR is amply authorized to provide the enhanced paging service herein described and should proceed to provide this service forthwith and file its appropriate tariffs therefor pursuant to G.S. 62-134 at least 30 days in advance of providing the service(s).

12. Based upon the foregoing findings of fact and applicable law, the Commission concludes that Carolinas RCC, Inc., is not an operating, franchised utility and will not become such upon acquisition of control by stock purchase of TWR. Further, the Commission observes that: (a) Carolinas RCC, Inc., does not have utility operating income at this time and has not shown that it expects to have any such income; (b) Carolinas RCC, Inc., is relying primarily on debt attraction for its acquisition of said stock, the financing of needed construction, and the provision of working capital for itself and the RCCs it controls in the start-up periods, particularly for cellular enhancement; and (c) the debt which Carolinas RCC, Inc., has and is contracting is at a comparatively high cost in relation to the net income of the RCC over which it is acquiring control.

Upon the foregoing, the Commission hereby cautions Carolinas RCC, Inc., that the North Carolina statutes, and practice of the Commission are as follows:

a. Under G.S. 62-3, this Commission has jurisdiction over Carolinas RCC, Inc., as the parent corporation of each RCC in this state over which it acquires control "to such extent that the Commission shall find that such affiliation(s) has an effect on the rates or service of such (RCC) utility." The Commission has repeatedly exercised this jurisdiction and will not hesitate to exercise it in the event the holding company relationship of Carolinas RCC, Inc., at any time has an existing or potential adverse effect on the utility services, assets, rates, or subscribers of any of the RCCs it controls in this state.

b. Under G.S. 62-51, the Commission, its Staff, and the Public Staff are authorized to inspect the books and records of corporations affiliated with public utilities regulated by the Commission. This includes parent corporations as well as subsidiaries of parent corporations. The right to inspect applies both to books and records located in the State of North Carolina and to books and records located outside of the State of North Carolina. The authorized penalties for refusal to permit such inspections includes the jurisdiction to cancel the affiliate utility's franchise to operate as a public utility in North Carolina.

c. G.S. 62-153 provides:

> <u>Contracts of public utilities with certain companies and for services</u>. - (a) All public utilities shall file with the Commission copies of contracts with any affiliated or subsidiary holding, managing, operating, constructing, engineering, financing or purchasing company or agency, and when requested by the Commission, copies of contracts with any person selling service of any kind. The Commission may disapprove, after hearing, any such contract if it is found to be unjust or unreasonable, and made for the purpose or with the effect of concealing, transferring or dissipating the earnings of the public utility. Such contracts so disapproved by the Commission shall be void and shall not be carried out by the public utility which is a party thereto, nor shall any payments be made thereunder...
>
> (b) No public utility shall pay any fees, commissions or compensation of any description whatsoever to any affiliated or subsidiary holding, managing, operating, constructing, engineering, financing or purchasing company or agency for services rendered or to be rendered without first filing copies of all proposed agreements and contracts with the Commission and obtaining its approval...(1931, c. 455; 1933, c. 134, s. 8; c. 307, s. 17; 1941, c. 97; 1963, c. 1165, s. 1.)

This Commission as well as the North Carolina appellate courts have strictly construed the above statutes. The essence of the statutes and practice is that parent holding companies cannot use affiliate utilities in this state as a device for transmitting an unreasonable level of profits to the parent holding company from goods or services supplied the operating utility by way of an affiliate company. As a result, all contracts for goods and services, and all fees, commissions, or compensation of any description whatsoever paid by a utility regulated by this Commission to an affiliated company or its representatives must be in writing, must be not only at arm's length but just and reasonable, and must be submitted to this Commission for approval in advance of payment.

Carolinas RCC, Inc., has submitted to the Commission Staff its own feasibility studies made prior to contracting to purchase control of the RCCs involved. These feasibility studies were made both with and without cellular development. The studies would appear conservative in that a substantially higher debt cost rate than has actually been contracted for was used. Yet, both studies indicate that, with effective cost control and aggressive marketing (in both of which areas the expertise of Carolinas RCC is unquestioned) its acquisitions are feasible, with or without cellular. Therefore, the foregoing observations should not be considered as raising doubts about the financial abilities of Carolinas RCC, Inc., or its affiliated system. Rather, the observations arise from the knowledge that the Sellers, who will be continued in the active management of their respective RCCs, have little experience or knowledge with the holding company regulation in the state; and the Buyers, who will be in control of the RCC operations in the state, have no experience with our regulation of holding companies of public

utilities regulated by the Commission. We are confident that the adage of "an ounce of prevention" will hold in this case. However, as a matter of import regarding acquisitions of regulated utilities in North Carolina, the Commission does not recognize the actual price paid for a utility for rate-making purposes, but instead uses the recorded net book cost and the actual cost of facilities added thereto after date of acquisition plus a reasonable allowance for working capital to determine a reasonable rate base investment.

13. Based upon the foregoing findings of fact and conclusions of law, and upon a careful review of the entire record as a whole, it is concluded that the stock transfers, financing, and plan of operations proposed in this docket should be approved and a Declaratory Order and Order of Approval not inconsistent herewith should be issued.

IT IS, THEREFORE, ORDERED as follows:

1. That the contract (Exhibit No. 4) with its attendant financing and plan of operations as contained in the application filed in this docket on May 25, 1983, be, and the same hereby are, approved, provided that Two Way Radio of Carolina, Inc., and shall make its final report to the Commission within 30 days after the closing of the stock transaction herein approved.

2. That Two Way Radio of Carolina, Inc., is deemed authorized by its present certificate to provide enhanced one-way, or enhanced two-way, radio common carrier service, or both, as defined herein in conjunction with its existing service through its joint venturer, CARS-Carolina, without amendment or modification to its existing certificate; provided it shall file its appropriate tariffs for each said service at least 30 days in advance of offering the service in accordance with G.S. 62-134.

3. That Carolinas RCC, Inc., its stockholders, and affiliates are hereby required strictly to comply with the spirit and letter of the statutes and policies relating to the relationships and dealings of holding companies and their affiliates and agents with regulated public utility subsidiaries in North Carolina as set forth in Conclusion No. 12.

4. That Carolinas RCC, Inc., is authorized, upon completion of the acquisition of the stock in TWR as herein approved to pledge the same to The Bank of New York as collateral security upon the advancement of approximately $6,530,000 in loan proceeds to it in connection with the acquisition by CRCC of said stock in TWR, provided that the restrictions, conditions, and requirements recited in Conclusion No. 10 are incorporated herein and shall be observed.

5. That upon acquisition of control, Carolinas RCC, Inc., is authorized and directed to cause TWR or CARS-Carolina, or both, to offer to the public in TWR's established franchised North Carolina territory the enhanced two-way (cellular) and enhanced one-way (wide-area, digital, etc.) radio common carrier services as defined herein in conjunction with, and without diminution of, TWR's existing radio common carrier service in TWR's franchised and established areas, said consolidated and conjunctive services to be offered on a full-area coverage and through basis, including regional and national tie-in capabilities, and to be appropriately licensed by FCC in advance.

6. That the separate Declaratory Order issued simultaneously herewith is hereby incorporated in this Order by reference for particularity as to the findings and conclusions upon which the Declaratory Order is based.

7. That no tariff, rate, or charge currently on file with and approved by the Commission and being charged for the existing RCC service of TWR shall be increased as a result of any of the transactions and proposals approved by this Order; nor shall any such existing service be diminished or substituted for as a result of said transactions or this Order.

ISSUED BY ORDER OF THE COMMISSION.
This the 15th day of June 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sandra J. Webster, Chief Clerk

DOCKET NO. P-84, SUB 20

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Two Way Radio of Carolina, Inc., and Carolinas RCC, Inc., Joint Application for Approval of Stock Transfer, Financing, and Pledge of Two Way's Stock Pursuant to G.S. 62-111, G.S. 62-160, and G.S. 62-161(b)) DECLARATORY ORDER

BY THE COMMISSION: On May 25, 1983, Two Way Radio of Carolina, Inc. (TWR), A. L. Guin, Jr., and Linda C. Guin (Sellers), and Carolinas RCC, Inc. (CRCC), filed with this Commission "Joint Application for Approval of Stock Transfers, Financing, and Improved RCC Service for Two Way Radio of Carolina, Inc." pursuant to G.S. 62-111(a), G.S. 62-160, G.S. 62-161(b), and Commission Rule R1-16. The application states that TWR and the other applicants are seeking approval of the stock transfers, financing arrangements (including the pledge of TWR's stock after completion of the transfer), and plan of operations in order that TWR will be able to license, construct, and operate "Domestic Public Cellular Radio Service" (cellular) in conjunction with its existing authorized two-way service and wide-area, digital, alphanumeric display, data, and other forms of improved or enhanced paging service (including regional and national tie-in capabilities) in conjunction with its existing authorized one-way service, both in TWR's existing franchised and established service areas or territories in North Carolina. The application also seeks a ruling or declaration that both cellular mobile radio common carrier service and the described improved one-way (paging) services are authorized by TWR's present certificates and may be offered as enhanced radio common carrier services on an areawide, through basis in its established service areas without necessity for amendment or modification to the service or territorial scopes of TWR's present certificates.

The application further states that neither cellular nor enhanced paging service can be licensed and offered in TWR's existing franchised areas on a comprehensive, full-area coverage, and through basis without obtaining large amounts of outside capital through joint venture arrangements between TWR and CRCC as detailed in the application.

This Order relates to the certificate questions raised by the application.

TWR is a duly certificated and authorized public utility engaged in providing both one-way (paging) and two-way (mobile radio) intrastate radio common carrier service to the public for compensation in the following North Carolina counties: Mecklenburg, Union, Stanly, Cabarrus, Gaston, Lincoln, Rowan, Iredell, Catawba, Chatham, Cleveland, Burke, Alexander, Davie, Randolph, Rutherford, Moore, Hoke, Robeson, Scotland, Richmond, Montgomery, Anson, and Lee. TWR now provides central station service for approximately 4,822 stations in the aforesaid certificated areas, all pursuant to tariffs and rates duly approved and supervised by this Commission.

Under the cellular technology, the number of radio base stations is expanded so that as a two-way mobile radio subscriber moves through the service area, or areas, his call is automatically and instantly handed off from one base station to another so that a subscriber may originate and terminate calls from any point within the service area. Two (2) or more callers can share the facilities simultaneously. Central switching facilities and equipment automatically route calls through interconnection with the land line telephone network so that mobile-to-land and land-to-mobile calls can be completed as well as mobile-to-mobile calls. Unlike the conventional two-way calling now offered by TWR in its franchised service areas, the "cellular mobile radio" system has a built-in capacity to expand as public demand increases, with a grade of service comparable to land line telephone service.

The application further states that the Federal Communications Commission has identified ninety (90) markets, Cellular Geographic Service Areas (CGSA), nationwide in which the public demand and need currently will justify cellular enhancement. One currently designated service area (CGSA) in North Carolina is the area of Mecklenburg, Gaston, and Union Counties, which is already within the established, franchised territory of TWR and is already receiving TWR's existing radio common carrier service on an integrated, full-area coverage basis. Two (2) 20 MHZ groups of channels have been allocated by FCC to this CGSA area. Initially, one of the FCC licenses will be available to land line telephone applicants and one will be available to radio common carriers as selected by FCC. To attract the capital necessary to the development of market studies, engineering and design of the cellular system for the Mecklenburg/Gaston/Union County CGSA, and support of its application to FCC for licensing and construction of cellular facilities in the service area, TWR formed a joint venture partnership with CRCC called Carolina Advanced Radiophone Systems of the Carolinas, Inc. (CARS-Carolina), and on March 8, 1983, caused said joint venture to file application for cellular license and construction permits in said Mecklenburg/Gaston/Union County CGSA. If licensed by FCC, the applicants do not propose to substitute cellular service for, or in any way diminish, TWR's existing two-way and one-way radio common carrier service in its service areas; rather, the applicants propose to offer cellular service in conjunction with TWR's existing radio common carrier service in its franchised areas.

While the cellular technology is new and the required facilities and equipment is unique and costly, the technology for extending and improving paging (one-way) radio common carrier service through the offering of wide-area, digital, alphanumeric display, and various other forms of data transmission on an areawide coverage and through basis, including tie-in capabilities on a regional and national basis, has been in existence for some

time and can be provided largely through facilities already authorized and licensed with the addition of compatible computer and switching capabilities.

The Applicants contend that, given the financial ability and appropriate licensing, both cellular two-way service and improved one-way service can and should be rendered to the public in TWR's existing franchised and established North Carolina service areas in conjunction with, and as enhancements to, existing one-way and two-way service without amendment or modification to the existing certificates of TWR.

CONCLUSIONS

The Commission concludes that Two Way Radio of Carolina, Inc., is a radio common carrier service certified pursuant to Chapter 62, Article 6A, of the General Statutes of North Carolina (N.C. G.S. 62-119 et seq.), and as such may provide cellular mobile radio service pursuant to its existing certificate. Radio common carrier service is defined in Chapter 62 under G.S. 62-119(3) as follows:

> The term "radio common carriers" when used in this Article includes every corporation, company, association, partnership and person and lessees, trustees, or receivers, appointed by any court whatsoever owning, operating or managing a business of providing or offering a service for hire to the public of one-way or two-way radio or radiotelephone communications whether interconnected with the land line telephone system or not and licensed by the Federal Communications Commission, but not engaged in the business of providing a public land line message telephone service or a public message telegraph service. The terms, "telephone or telegraph utilities," "telephone or telegraph company," or a "person operating telegraph or telephone lines" when used in this Chapter, shall not be construed as including radio common carriers. (1969, c. 766; 1973, c. 1274.)

Considering that "cellular mobile radio service" is no more than an enhanced two-way mobile radio common carrier service, that "wide-area," "digital," "data," and other forms of one-way service, including "through" service with tie-in capabilities to regional and national networks, are no more than variant forms of enhanced one-way radio common carrier service, and that Two Way Radio of Carolina, Inc., is duly certified to provide radio common carrier service to the public throughout its service territory, it is thereby authorized by its existing certificates to provide cellular two-way radio common carrier service and all forms of improved and enhanced paging one-way service in its presently franchised and established territories without necessity for amendment to or modification of its certificates.

IT IS, THEREFORE, ORDERED as follows:

1. That Two Way Radio of Carolina, Inc., is authorized to provide cellular mobile radio (two-way), or all forms of paging (one-way) service, including wide-area, digital, alphanumeric display, and various forms of data transmission on a through basis with tie-in capabilities, or both, in conjunction with its existing franchised radio common carrier service pursuant to its existing certificates; and said enhanced services may be offered, either in TWR's name or in the name of its joint venture, Carolina Advanced

Radiophone Systems of the Carolinas, Inc., subject to appropriate licensing by the Federal Communications Commission.

2. That Two Way Radio of Carolina, Inc., is authorized and required to file for approval, pursuant to G.S. 62-134, appropriate tariffs of rates and charges for providing the new service(s), including cellular mobile radio service, at least thirty (30) days prior to rendering said intrastate service to the public within its franchised territory in North Carolina.

ISSUED BY ORDER OF THE COMMISSION.
This the 15th day of June 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sandra J. Webster, Chief Clerk

DOCKET NO. P-55, SUB 802

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Tariff Filing by Southern Bell Telephone and Telegraph Company to Provide Additional Options for Network Connection of Customer-Provided Communications Systems Not Subject to Part 68 of FCC's Rules and Regulations) ORDER DENYING IN PART AND APPROVING IN PART TARIFF FILING OF MAY 26, 1982

HEARD IN: Hearing Room of the North Carolina Utilities Commission, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina, on October 20, 1982

BEFORE: A. Hartwell Campbell, Presiding; and Commissioners Edward B. Hipp and John W. Winters

APPEARANCES:

For the Applicant:

R. Frost Brannon, Jr., General Attorney, Southern Bell Telephone & Telegraph Company, P.O. Box 30188, Charlotte, North Carolina 28230
For: Southern Bell Telephone & Telegraph Company

Gene Coker, General Attorney, Southern Bell Telephone and Telegraph Company, P.O. Box 30188, Charlotte, North Carolina 28230
For: Southern Bell Telephone & Telegraph Company

For the Public Staff:

Thomas K. Austin, Staff Attorney, Public Staff - North Carolina Utilities Commission, P.O. Box 991, Raleigh, North Carolina 27602
For: The Using and Consuming Public

For the Intervenors:

Dwight Allen, General Counsel, Carolina Telephone & Telegraph Company, Tarboro, North Carolina
For: Carolina Telephone & Telegraph Company

Wayne L. Goodrum, Associate General Counsel, General Telephone Company of the Southeast, 4100 Roxboro Road, P.O. Box 1412, Durham, North Carolina 27702
For: General Telephone Company of the Southeast

F. Kent Burns, Boyce, Mitchell, Burns & Smith, P.O. Box 2479, Raleigh, North Carolina
For: North State Telephone Company, Lexington Telephone Company, Concord Telephone Company, Mid-Carolina Telephone Company, and Sandhill Telephone Company

BY THE COMMISSION: On May 26, 1982, Southern Bell Telephone and Telegraph Company (Southern Bell) filed to become effective June 30, 1982, proposed tariff revisions which would provide additional options for the connection of customer-provided communications systems, such as microwave systems or cable facilities, to local, message toll, WATS, and telephone company-provided private line services. The tariff also removes certain restrictions on the use of customer-provided systems. Removal of these restrictions will enable customers to furnish their own off-premises extensions and tie lines and cross-boundary foreign exchange services.

The matter was placed on the June 28, 1982, Regular Commission Conference Agenda by the Public Staff. At the Conference, statements of position were offered by the following individuals: Millard N. Carpenter, Public Staff Engineer, Robert Friedlander and R. Frost Branon, Southern Bell, and Hubert Terry, Carolina Telephone Company.

On June 29, 1982, the Commission issued an Order suspending the tariff and requiring Southern Bell Telephone and Telegraph Company to forward the proposed tariff to all independent telephone companies in North Carolina. The independent telephone companies were allowed 30 days in which to file written comments pertaining to the proposed tariff revisions.

The following companies duly filed comments in opposition to the tariff generally proposing that the Commission reject the tariff or set the matter for hearing:

Carolina Telephone & Telegraph Company
Concord Telephone Company
North State Telephone Company
Central Telephone Company
Sandhill Telephone Company
Mid-Carolina Telephone Company
Lexington Telephone Company
General Telephone Company of the Southeast

The North Carolina Textile Manufacturers Association filed a statement of position to explain the advantages versus the disadvantages of the proposed tariff and its potential impact on business customers.

The Order scheduling hearing and requiring prefiled testimony was issued on August 24, 1982, and scheduled for hearing to commence October 20, 1982, at 10:00 a.m., in the Commission Hearing Room in Raleigh, North Carolina.

During the hearing on October 20, 1982, Southern Bell offered the testimony and exhibits of Robert A. Friedlander, District Staff Manager-Rates for Southern Bell.

The Public Staff offered the testimony of Millard N. Carpenter, Engineer in the Communications Division of the Public Staff.

Based on the foregoing, the testimony and exhibits admitted at the hearing, and the entire record in this docket, the Commission now reaches the following

FINDINGS OF FACT

1. Southern Bell is a public utility providing communications service to its customers in the area it has undertaken to serve, and is a duly created and existing corporation authorized to do business in North Carolina.

2. Southern Bell is seeking authority from this Commission to change its tariff which would permit an alternate means of connection for customer-provided communications systems.

CONCLUSIONS

1. That the tariff Item A.15.1.7A.1 proposed by the Company to be deleted be disapproved. This item deals with origination and termination requirements at the point of connection with the subscriber. It is the Commission's belief that if this aspect of the proposal is not disallowed the integrity of the franchised service boundaries as has been established over many years in this state will not be maintained.

2. That other proposed changes should be approved. Such changes provide options for the connection of customer-provided communications system not subject to Part 68 of the FCC Rules and Regulations.

3. That Southern Bell should be required to file new tariff(s) as required in order to implement the Commission's findings as set forth herein.

EVIDENCE FOR FINDINGS OF FACT NO. 1

The evidence for this finding is found in the existing tariffs, in prior Commission Orders, and in the record as a whole. This finding is essentially procedural and jurisdictional in nature and was uncontested and noncontroversial.

EVIDENCE FOR FINDING OF FACT NO. 2

Southern Bell's description of the tariff revisions in the original filing was that these tariff revisions would permit an alternate means of connection for customer-provided communications system.

Robert A. Friedlander of Southern Bell testified that systems not subject to Part 68 of the FCC Rules and Regulations are primarily private microwave systems.

Witness Friedlander explained that the present tariff provides:

> Such telecommunications service or customer-provided communications system is utilized for the origination or termination of communications at the customer's premises where the connection is made.
>
> The connection shall be through a network control signaling unit and connecting arranagement furnished by the Company.
>
> The connection shall be made through switching equipment provided either by the customer or by the Company.

> The provisions relating to minimum protection criteria set forth in the tariff shall apply to the connection of customer-provided communications systems.

Witness Friedlander testified that Southern Bell's proposed Tariff provides:

> The proposed tariff provisions would allow the connection of customer-provided communications systems to exchange, WATS or private line services without the use of a protective connecting arrangement if such connection is through registered or grandfathered terminal equipment, protective circuitry, or communications systems subject to Part 68 of the FCC's Rules and Regulations.
>
> The requirement for origination and termination at the point of connection and the requirement that the connection be made through switching equipment <u>was removed</u> when connected to exchange and WATS services.
>
> Institutional procedures were also introduced whereby the customer can certify that signal power does not exceed Part 68 limits since not all registered or grandfathered equipment or systems are designed to protect Company services against excessive voice frequency signal power that might emanate from a customer-provided communications system.

Witness Friedlander stated that the FCC has made changes in interstate tariffs and all states except North Carolina, North Dakota, South Dakota, and Iowa have adopted similar changes on an intrastate basis. This tariff simply conforms the North Carolina tariff to the manner of interconnection which has been prescribed by the FCC. Witness Friedlander testified on cross-examination that the intent of the Company is to bring intrastate service into conformance with the requirements of the FCC.

The seven private communications systems in North Carolina are Duke Power, CP&L, Blue Ridge Electric, Hanes Textile, Morgan Dye and Finishes, and Southern Railway and Family Lines.

Millard N. Carpenter of the Public Staff testified that the Company's proposal contained two major changes. Such changes were characterized as follows:

A. It provides options to the customers for the connection of customer-provided communications system not subject to Part 68 to local, message toll, WATS, and telephone company-provided private line services. The changes involving connection are as follows:

   1. In lieu of today's requirement for connection of the system through a connecting arrangement and a network control signaling unit provided by Southern Bell, the customer may, in addition, and at this option, connect this system through:

      a. A protective connecting arrangement, an item of terminal equipment, or communications system subject to Part 68 that assures that all requirements of Part 68 are met at the network interface, or

b. Through such circuitry or equipment specified in (a) above which contains all of the Part 68 protection requirements except signal power limitations, provided a properly executed affidavit certifying signal power compliance is filed.

2. In lieu of today's requirement that the connection be made through switching equipment, the customer may at his option make the connection to local exchange, WATS, and message toll service either through switching equipment or equipment that will return the Telco facilities to idle (on-hook) if the customer's system fails. The requirement that the customer's system be connected through switching equipment when the system is connected to Telco private line facilities remains unchanged.

B. A long-standing restriction on the use of customer-provided communications systems subject to Part 68 when such systems are connected to the local exchange, WATS, and MTS services has been deleted in the proposed tariff. The provision regarding the use of the service, Item A.15.1.7A.1, following, is deleted in the proposed tariff.

Witness Carpenter testified that the tariff in its present form should be disapproved. The Public Staff does not object to the changes which liberalize the means of connection to Telco facilities, Item A above.

The Public Staff does object to Item B, the deletion of the requirement for origination and termination at the point of connection. With respect to Item B under Bell's proposal, deletion of the origination and termination requirement would allow a customer to terminate an exchange access line, a WATS access line, an OPX line, or a tie line in one exchange and connect that line to this private communications system. Thus, the customer may in essence "by-pass" the local exchange access provided by the local telephone company and subscribe instead to exchange access from some other telephone company. A potential would thereby be created for the complete loss of one or more large customers by the independent telephone companies. Such loss conceivably could have a signficantly negative impact on the basic rates of the independents' remaining subscribers. A subscriber might also use this private system to avoid message toll charges and foreign exchange and interexchange private line rates and charges. Clearly, deletion of the origination and termination requirement would lead to loss of contribution from these services which would utimately require a further increase in basic rates. Therefore, the Public Staff recommends that the requirement for origination and termination, Item A.15.1.7A.1, be continued.

With regard to the Eslon Case (P-89, Sub 17), witness Carpenter testified that the Eslon property, which straddled the Pineville-Charlotte exchange boundary, was divided by a railroad spur line near the boundary. The question in that docket was whether or not Eslon could, using its own cross-boundary facilities, connect to Southern Bell on the Charlotte side of its property and extend those facilities to its business location in Pineville's service area. Witness Carpenter testified that if the Eslon property is considered two premises, the regulations proposed in this docket would be applicable. Under the proposed regulations, the tariff would allow the service which Eslon desired and which Southern Bell had furnished. If the property is considered one premises, Part 68 of the FCC's rules would apply. Under those rules Eslon

could connect using its own cable to Southern Bell's Charlotte facilities. In that docket the Commission required Southern Bell to discontinue service to Eslon.

Bob Morite, Director, of the Blue Ridge Electric Membership Corporation, testified that Blue Ridge recently installed a microwave system, primarily for data transmissions to an on-line computer. The microwave system was the least costly method of implementing Blue Ridge's load management system. Witness Morite testified that it is not his company's intention to take away toll calls of telephone companies, but rather to answer local calls in Blue Ridge's own facilities as well as to receive trouble calls at night.

Archie A. Thomas, President of Mid-Carolina Telephone Company and Sandhills Telephone Company, testified that the tariff changes would allow the customer to wire directly across all existing boundaries. Customers could furnish their own off premises extensions, tie lines, and cross boundary foreign exchange services. In addition, it would permit subscriber-owned microwave in a different exchange to be accessed. Witness Thomas testified that one might plan to provide specific service in a particular area and after having constructed the plant find, if Bell's proposal is implemented, that it would be substantially useless. The reverse is also true. Witness Thomas testified that one would never know who one's customers would be or what the requirements might be.

Witness Thomas further testified that, if investments are made that are rendered useless, the costs will have to be borne by whatever customers remain. Witness Thomas said that he understands that R.J. Reynolds Company has asked the FCC for a clarification in a letter, to determine if they could utilize CATV channels for transmitting data from one side of town to the other.

Witness Thomas stated that his major objection to Bell's proposal was the striking of the words "utilize for the origination or termination of communication at the customer premises where the connection is made" and the possible implication that it could be used on cross-boundary cases by either small individuals or large companies. Witness Thomas testified that this would open up the floodgates to let each and every person in those particular locations to get the service of his choice without regard to who has the certificate of convenience and necessity to serve that area.

Witness Thomas testified that North State Telephone Company, Concord Telephone Company, Lexington Telephone Company, and Sandhills Telephone Company concur in his testimony.

Alfred A. Banzer, Pricing and Tariffs Manager, General Telephone Company of the Southeast, testified that the main thrust of this tariff filing was to remove the protective connecting arrangement requirements and allow connection of customer-provided communications systems through registered and grandfathered equipment. The equipment could be protective circuitry, terminal equipment, or communications systems. He stated that General Telephone did not object to such modification nor to the procedures introduced whereby a customer can certify that the voice frequency signal power does not exceed Part 68 limits.

Witness Banzer testified, however, that his company's area of concern is removal of origination or termination of communications at the customer's premises where the connection is made. Witness Banzer testified that the removal of the restriction specified in Item A.15.1.7A.1 has the potential to destroy franchised boundaries as we know them today and could render useless some of the telephone equipment and facilities, thereby stranding embedded investments. This could result in inflated rates to compensate for stranded investment or, if that investment is retired early, it would have an impact on life and salvage values in depreciation studies. Further, witness Banzer stated that planning would be disrupted, long range engineering wasted, anticipated revenue would not be received, and possible construction costs already incurred to meet expected growth would be lost. Moreover, he stated that local revenue and toll revenue would be lost. The sunk investment, however, would still be in-place and the associated capital costs would still remain for the Company to recover. He also testified that General Telephone does not believe that a customer has the right to interconnect on the network side with whatever carrier he wishes in total disregard of franchised boundaries. In summary, General Telephone recommended that the Commission reject the tariff revisions as filed by Southern Bell.

IT IS, THEREFORE, ORDERED as follows:

1. That the proposal of Southern Bell to delete tariff Item A.15.1.7A.1 be, and hereby is, disapproved.

2. That the proposed changes other than the proposed change specifically disapproved in Ordering Paragraph 1 hereinabove be, and hereby are, approved.

3. That Southern Bell shall file new tariffs consistent with the Commission's findings, conclusions, and decretal paragraphs as set forth herein.

ISSUED BY ORDER OF THE COMMISSION.
This the 24th day of June 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sandra J. Webster, Chief Clerk

DOCKET NO. P-55, SUB 806

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Tariff Filing by Southern Bell Telephone and Telegraph Company to Establish Provisions for Optional Local Measured Service
) ORDER DISMISSING PROPOSED
) LOCAL MEASURED SERVICE TARIFF
) BUT ODERING EXPERIMENT ON
) SELECTED EXCHANGES

HEARD IN: Buncombe County Courthouse, Courthouse Plaza, Asheville, North Carolina, on December 1, 1982

Guilford County Courthouse, Greensboro, North Carolina, on December 1, 1982

Courthouse Annex, 700 East Trade Street, Charlotte, North Carolina, on December 2, 1982

New Hanover County Courthouse, Wilmington, North Carolina, on December 2, 1982

Hearing Room of the North Carolina Utilities Commission, Dobbs Building, 430 North Salisbury Street, Raleigh, North Carolina, on December 7, 8, and 9, 1982, and January 5 and 6, 1983

BEFORE: Edward B. Hipp, Presiding; Chairman Robert K. Koger and Commissioners Leigh H. Hammond, John W. Winters, Douglas P. Leary, Sarah Lindsay Tate, and A. Hartwell Campbell

APPEARANCES:

For the Applicant:

Robert C. Howison, Jr., Hunton and Williams, Attorneys at Law, P.O. Box 109, Raleigh, North Carolina 27602
For: Southern Bell Telephone and Telegraph Company

R. Frost Branon, Jr., General Attorney, Southern Bell Telephone and Telegraph Company, P.O. Box 30188, Charlotte, North Carolina 28207
For: Southern Bell Telephone and Telegraph Company

Gene V. Coker and J. Billie Ray, Jr., Attorneys, Southern Bell Telephone and Telegraph Company, 4300 Southern Bell Center, Atlanta, Georgia
For: Southern Bell Telephone and Telegraph Company

For the Public Staff:

Thomas K. Austin and Paul Lassiter, Staff Attorneys, Public Staff - North Carolina Utilities Commission, P.O. Box 991, Raleigh, North Carolina 27602
For: The Using and Consuming Public

For the Attorney General:

Robert H. Bennink, Jr., and Steve Bryant, Assistant Attorneys General, North Carolina Department of Justice - Attorney General, P.O. Box 629, Raleigh, North Carolina 27602
For: The Using and Consuming Public

For the Intervenors:

Jerry B. Fruitt, Eller and Fruitt, Attorneys at Law, P.O. Drawer 27866, Raleigh, North Carolina 27612
For: North Carolina Textile Manufacturers Association

Eugene Hafer, Eagles, Hafer & Hall, Attorneys at Law, P.O. Box 2211, Raleigh, North Carolina 27602
For: North Carolina Association of Realtors

Richard M. Klein, Legal Services of North Carolina, P.O. Box 6505, Raleigh, North Carolina 27628
For: Intervenors Lugenia Jackson, et al.

J. Ward Purrington, Attorney at Law, P.O. Box 20243, Raleigh, North Carolina 27619
For: North Carolina Association of Realtors

BY THE COMMISSION: On September 10, 1982, Southern Bell Telephone and Telegraph Company (Southern Bell) filed proposed tariffs with the Commission to establish rates and regulations for local measured service options for its residence and business subscribers. The proposed effective date of the tariffs was October 20, 1982.

On October 10, 1982, the Commission issued an Order setting the matter for investigation and hearing, suspending the proposed rates and requiring public notice.

Notices of Intervention were filed by the Public Staff, the Attorney General, Lugenia Jackson, et al., the North Carolina Textile Manufacturers Association, Inc., and the North Carolina Association of Realtors, Inc. The Commission issued Orders allowing these interventions.

On October 20, 1982, the Attorney General filed a motion requesting that the hearings be postponed to allow the Attorney General adequate time to investigate the filing, hire an expert witness, and prepare his case. The Attorney General's motion was supported by Lugenia Jackson, et al.

On November 2, 1982, the Commission issued an Order denying the Attorney General's motion to postpone and reschedule the hearings.

Out of town hearings were conducted by the Commission for the purpose of receiving testimony from members of the using and consuming public with regard to Southern Bell's proposed tariffs. The first and second of these hearings were held simultaneously in Asheville, North Carolina, and Greensboro, North Carolina, at 7:00 p.m., on December 1, 1982; the third and fourth of these hearings were held simultaneously in Charlotte, North Carolina, and Wilmington, North Carolina, at 7:00 p.m., on December 2, 1982; and the fifth hearing was held in Raleigh, North Carolina, beginning at 10:00 a.m., on December 7, 1982. Public witnesses at these hearings included the following persons:

Asheville - Dale Vaughn, Barbara Baskerville, Kitty Moniske, Minnie Jones, Jesse Cleman, Suzanne Daley, Linda Simmons, Sid Hodge, Thomas R. Wilson, Mrs. J. H. Priedeman, H. Edgar Pray, Eleta Jones, Juanita Jones, Pearl Nealey, Nancy Rule, Marjorie Lockwood, and Lucille Caldwell.

Greensboro - Fanny Graves, Sue Baines, Connie Burwell, Robert Anderson, Christine Keith, Lula Chambers, Byrde Chambers, Robert Jackson, Lawrence Morse, Patti Eckard, R.J. Buller, and E.L. Keith.

Charlotte - Arthur Griffin, Chet Snow, Jr., Ione E. Jones, JoAnn Morehead, and Theresa Ann Wood.

Wilmington - LaNelle Lilley, Bob Koth, Robert R. Hughes, Sr., and H.C. Wallace.

Raleigh - Ernest Messer, William H. Peace, Terry Kemp, Linda Johnston, Ben Eason, Sheila Nader, Jame Sharpe, Gary Fisher, Sandra Carson, Charles V. Petty, Don Walston, Esther Hall, Charles L. Lehning, Jr., Joseph Reinchens, Doris F. Brandburg, Wells Eddleman, Myrle Freedman, Rev. J.H. Bryan, Geoff Wycoff, John Provetero, Kay Provetero, John Healey, Dan Norman, Mary Dunn, James Grant, Ricki Grantmyre, Michael Schaul, Mark Schler, Sherwood Scott, and Virginia A. Stevens.

Southern Bell offered the testimony and exhibits of the following witnesses: Alan E. Thomas, Vice President - Responsible for the Service and Earnings of Southern Bell in North Carolina; Robert L. Savage, Division Staff Manager - Rates and Costs of Southern Bell; and W. Whitard Jordan, District Staff Manager - Rates and Costs of Southern Bell.

The Public Staff offered the testimony of Gene A. Clemmons, Director of the Communications Division of the Public Staff.

The Attorney General offered the testimony of Dr. Lee Richardson, Professor in the Department of Marketing at the University of Baltimore, and Frank David Leatherman, Telecommunications Engineer with the North Carolina Department of Administration.

The North Carolina Textile Manufacturers Association offered the testimony of Louis R. Jones, Manager of Corporate Communications - Department of Burlington Industries, Inc., and Harry M. Venable, Director of Telecommunications Services for the Celanese Corporation.

The North Carolina Association of Realtors offered the testimony of Zack Bacon, Jr., of Bacon Realty.

Based on the foregoing, the testimony and exhibits admitted at the hearing, and the entire record in this docket, the Commission now reaches the following

FINDINGS OF FACT

1. That Southern Bell is a public utility providing communications service to its customers in the area it has undertaken to serve and is a duly created and existing corporation authorized to do business in North Carolina.

2. That Southern Bell is seeking authority from this Commission to establish rates and regulations to offer optional local measured service to its residence and business subscribers in the 25 Southern Bell exchanges where the central office is equipped with an electronic switching system.

3. That Southern Bell's proposed optional Local Measured Service plan establishes the charges for local calls on the following elements. (a) A minimum fixed monthly rate which includes some usage allowance, (b) mileage distance of call from the home exchange where the call originates to the calling party where the call terminates, (c) duration of the call, and (d) time of day the call is initiated.

4. That Southern Bell's proposed LMS plan is opposed by the vast majority of public witnesses who testified at the public hearings and by the Intervenors.

5. That it would be difficult for subscribers to calculate the charges on their monthly bills.

6. That Southern Bell has failed to produce sufficient data to convince this Commission that the proposed charges are cost based.

7. That the economic circumstances prevailing in the country today as well as the evolving federal devncreases in local telephone rates.

CONCLUSIONS

1. That the presently filed optional local measured service tariff should be disapproved.

2. That the Commission recognizes the need for developing viable alternatives and options to the traditional monthly flat rate pricing structure for telephone subscribers in this state.

3. That through coordination with the Public Staff, the Attorney General, and the other Intervenors, Southern Bell should develop and conduct a year-long statistically and scientifically sound measured service experiment that will produce results sufficient to determine whether some form of optional local measured service or some other alternative service should be offered in addition to the traditional flat rate service. The study should include complete subscriber surveys or employ such scientific statistical sampling techniques as required to permit valid inferences to be made with respect to the population being sampled both before and after the completion of the experiment so as to determine on an ex ante and an ex post basis the desirability of or the demand for LMS.

4. That the experimental measured rate offerings should be instituted in the following cities: Charlotte, Raleigh, Asheville, Wilmington, Gastonia, Shelby, Cary, Apex, and Forest City.

5. That the experiment should produce information to permit a determination of the response and benefit differences among the following customer characteristics:

(1) Rural, inner-city urban, suburban subscribers
(2) Lower, middle, and upper income groups
(3) Owners of more than one home (i.e., vacation)
(4) Elderly, homebound, fixed income
(5) Industrial, college or university, resort, other (describe)

6. That Southern Bell should develop, for the experimental exchanges, at least three proposals containing only the following three elements: number of calls, duration of calls, and time of day of calls.

7. That Southern Bell should study the possible incorporation into its experiment the salient features of the measured service concept as proposed by Carolina Telephone and Telegraph Company in the letter filed with the Commission on April 14, 1983.

8. That prior to instituting the experimental Optional Local Measured Service Southern Bell should submit to the Commission for approval the proposed detailed plan which has been developed with the assistance of the Public Staff and the Attorney General.

9. That in the experimental exchanges the bills of OLMS subscribers should prominently reflect what the flat rate charges would have been.

EVIDENCE FOR FINDINGS OF FACT NOS. 1 AND 2

The evidence for these findings is found in the verified application, in prior Commission Orders, and in the record as a whole. These findings are essentially procedural and jurisdictional in nature and were uncontested and noncontroversial.

EVIDENCE FOR FINDING OF FACT NO. 3

The evidence supporting this finding is found in the verified application of Southern Bell and in the testimony given by witnesses Thomas, Savage, and Jordan. These witnesses testified that Southern Bell has proposed optional local measured service tariffs as follows: (1) a standard measured rate for residence customers; (2) a low use measured rate for residence customers; (3) a tapered measured rate for business customers; and (4) a standard measured rate for business customers.

Under Southern Bell's proposed tariffs, customers would be classified into proposed rate groups based on main stations and PBX trunks inthe local calling area as follows:

Proposed Rate Groups	Main Stations and PBX Trunks in Local Calling Area
A	1 - 22,000
B	22,001 - 60,000
C	60,001 - 150,000
D	150,001 - Up

Under Southern Bell's proposed tariffs, the local calling area for exchange and wire centers would remain unchanged but would be subdivided into tiers of exchanges for measured service calling. The distance between the customer's exchange rate center and each of the other exchange rate centers in the customer's local calling area would be determined, and the measured service calling tiers for each exchange would be established individually as follows:

Tier 1 - The home exchange plus all additional exchanges completely surrounded by the home exchange or where the rate center is located up to and including 6.0 miles from the home exchange rate center.

Tier 2 - All exchanges where the rate center is located a distance greater than 6.0 miles up to and including 22.0 miles from the home exchange rate center.

Tier 3 - All exchanges where the rate center is located a distance greater than 22.0 miles up to and including 40.0 miles from the home exchange rate center.

Under the proposals, each customer opting for measured service would be charged a basic access line charge which would include a usage allowance. These charges would be as follows:

Basic Access Lines and Usage Allowances - Residence

Measured Service Group	Standard Measured	Low Use Measured
A	$8.45 ($5.65)	$5.90 ($2.00)
B	9.05 ($5.95)	6.30 ($2.00)
C	9.65 ($6.20)	6.70 ($2.00)
D	10.25 ($6.45)	7.15 ($2.00)

( ) Allowance Included in Monthly Rate.

Basic Access Lines and Usage Allowances - Business

Measured Service Group	Standard Measured	Low Use Measured
A	$26.05 ($10.00)	$21.55 ($6.45)
B	27.25 ($10.00)	23.10 ($6.95)
C	28.40 ($10.00)	24.60 ($7.40)
D	29.65 ($10.00)	26.15 ($7.85)

( ) Allowance Included in Monthly Rate.

Basic Access Lines and Usage Allowances - Business

Measured Service Group	Standard Measured	Low Use Measured
A	$46.25 ($10.00)	$38.75 ($6.45)
B	48.73 ($10.00)	41.58 ($6.95)
C	51.08 ($10.00)	44.28 ($7.40)
D	53.57 ($10.00)	47.07 ($7.85)

( ) Allowance Included in Monthly Rate.

Each customer would be charged the applicable measured service basic access charge plus the amounts that the customer's calls exceeded the usage allowance. The usage charge would be based on the price of each completed outgoing call. This in turn would be based on the duration of the call, the distance called, and the time of day. These usage charges would be as follows:

Distance From Home Exchange (Miles)	Tier	Initial Minute	Each Additional Minute
0 - 6	1*	$ .05	$ .01
7 - 22	2	.08	.03
23 - 40	3	.12	.06

*Tier 1 always includes the home exchange.

Time of Day Discounts Applicable to Usage Charges

Time Period	Percent Discount
Evening - (5 p.m. - 11 p.m. Sunday - Friday, 12 noon - 1 p.m. Weekdays, and specified holidays)	25%
Night - (11 p.m. - 8 a.m. daily, 8 a.m. - 11 p.m. Saturday, and 8 a.m. - 5 p.m. Sunday)	50%

There would be no maximum bill under Southern Bell's proposed local measured rate tariffs. There would, however, be no service charges for a customer changing from one of the measured service options back to the flat rate within six months from the effective date of the tariffs in any wire center.

At the present time, Southern Bell can offer local measured service options in exchanges serving about 45% of its customers. However, Southern Bell is only providing enough measuring capability to service 15% to 25% of the subscribers in the exchanges where the option is offered. Consequently, Southern Bell will only have enough facilities initially available to provide the measured service option to about 10% of its customers.

EVIDENCE FOR FINDING OF FACT NO. 4

The evidence for this finding is based on the testimony given by approximately 70 public witnesses who testified at the hearings and upon the testimony given by witnesses for the Public Staff, the Attorney General, the North Carolina Association of Realtors, and for Lugenia Jackson, et al.

The Commission is impressed with the number of public witnesses who appeared at the hearings and the fact that these witnesses were almost universally opposed to local measured service. The public witnesses included customers from all walks of life: the elderly, the handicapped, low and middle income customers, governmental and social service agencies, business, industry, and volunteer organizations. Most of those testifying strongly opposed measured service and stated their preference for the existing flat rate pricing of local telephone service. Many witnesses expressed their fears that the offering by Southern Bell of optional local measured service would ultimately result in the elimination of flat rate service or cause the price of flat rate service to escalate.

The Public Staff and the Attorney General both offered testimony in support of flat rate pricing for local telephone service. These witnesses testified that Southern Bell's local measured service plan is unacceptable as a means of preserving universal service, and that the tariff to institute local measured service should be disapproved.

EVIDENCE FOR FINDING OF FACT NO. 5

This finding is based on consideration of the four elements that the Southern Bell tariff uses to determine the customers' monthly charges as specifically enumerated in Finding of Fact No. 3, <u>supra</u>. In essence, the Commission believes that customers would have difficulty in calculating the cost of single calls. Moreover, customers would experience even more difficulty in determining what total monthly local measured charges would be in advance and verifying their bill when received.

EVIDENCE FOR FINDING OF FACT NO. 6

This finding is based on Southern Bell's response to Public Staff First Data Request seeking to find "what percentage of telephone plant is sensitive to local usage." The response reveals that Exchange Use in 1981 was 12.49% of <u>total</u> Telephone Plan in Service.

The Commission is also concerned as to the accuracy of the factors chosen by Southern Bell to produce charges for local service based on cost. Southern Bell's plan includes a distance element that charges the customer 9¢, 20¢, and 36¢ for a five-minute Tier 1, Tier 2, and Tier 3 daytime call, respectively (Savage Exhibit No. 1, p. 5 of 5), while the Public Staff asserts that the actual costs of these calls to the Company are only 6.7¢, 9.1¢, and 10.1¢, respectively. In other words, the actual cost differentials between Tier 1 and Tier 3 calls is only 50%, whereas the price differential under Southern Bell's plan is 300%. Moreover, Southern Bell's plan charges substantially more for a Tier 3 call than a Tier 2 call even though there is very little cost differential between the two calls. During cross-examination, witness Jordan was asked to compute the cost of a given number of nighttime calls and to calculate how much the customer would be charged for such calls. In answer to this question, witness Jordan admitted that it would be possible under Southern Bell's proposed plan for a customer to be charged $27.75 for calls that only cost the Company $0.06.

EVIDENCE FOR FINDING OF FACT NO. 7

The evidence for this finding isbased on the testimony given by Southern Bell witness Alan E. Thomas, Public Staff witness Gene Clemmons, and Attorney General witness Dr. Lee Richardson.

Witness Alan Thomas testified that in North Carolina approximately 88% of the family units have telephones compared to the national average which is in the mid-90 range and that North Carolina has the 10th lowest per capita income level compared with the other states. Witness Thomas stated that Southern Bell has endeavored to balance the interests of the entire marketplace to promote universally available and affordable local service. The pricing system has been characterized by the subsidies to local service provided by long distance and dozens of vertical service options. Those subsidies have been eliminated. The marketplace has been decreed competitive and must now yield to competitive economies. Communications services will be driven by the individual costs of providing them. Local service cannot escape that reality. In addition to the loss of these traditional subsidies, witness Thomas mentioned additional factors which would cause the cost of service to increase: the continuing and cumulative effects of inflation, high interest rates, and the need for faster rates of capital recovery caused by the increasing pace of new technology in the telecommunications industry.

Witness Gene Clemmons, witness for the Public Staff, indicated that rates for local service will inevitably rise and some customers may be dropping off of the network now because of price.

Dr. Lee Richardson, testifying on behalf of the Attorney General, acknowledged that there exists a need to find alternatives to the present pricing structure in order to foster the concept of universal service.

The evidence here presented causes this Commission to recognize that there is a need to develop alternatives to flat rate service plans which would give customers pricing choices.

IT IS, THEREFORE, ORDERED as follows:

1. That the local measured service tariff proposed and filed herein by Southern Bell Telephone and Telegraph Company on September 10, 1982, is hereby disapproved.

2. That Southern Bell within 90 days from the issuance of this Order, through coordination with the Public Staff, the Attorney General, and other Intervenors, shall develop and file with this Commission a statistically and scientifically sound measured service experimental plan or plans. Such filing shall include a minimum of three independent alternative proposals.

3. That if within 60 days the Public Staff, the Attorney General, and other Intervenors are unable to agree with Southern Bell on a joint proposed experiment, they may each file separate proposed experimental alternative plans including variations in rates and other measurement criteria within 90 days from the issuance of this Order.

ISSUED BY ORDER OF THE COMMISSION.
This the 3rd day of June 1983.

NORTH CAROLINA UTILITIES COMMISSION
Sandra J. Webster, Chief Clerk

(SEAL)

DOCKET NO. P-19, SUB 193

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Application of General Telephone Company of the Southeast for an) Adjustment in Its Rates and Charges for Intrastate Telephone Service) ORDER in North Carolina)

BY THE PANEL: On September 6, 1983, at 2:30 p.m. attorneys representing the General Telephone Company and the Public Staff appeared before this Panel in open hearing and requested that the terms of a Consent Order attached hereto as Appendix A be allowed by this Commission.

The Panel after review of the Consent Order and deliberation on the merits concludes that the terms are just and reasonable to all parties and should be allowed.

IT IS, THEREFORE, ORDERED that the Consent Order issued in Docket No. P-19, Sub 193, is hereby allowed and the terms contained therein shall be binding upon the parties upon the issuance of this Order.

ISSUED BY ORDER OF THE PANEL.
This the 6th day of September 1983.

NORTH CAROLINA UTILITIES COMMISSION
(SEAL) Sandra J. Webster, Chief Clerk

APPENDIX A
DOCKET NO. P-19, SUB 193

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In The Matter of
Application of General Telephone Company of the Southeast for an) CONSENT Adjustment in Its Rates and Charges for Intrastate Telephone Service) ORDER in North Carolina)

BY THE COMMISSION: On February 28, 1983, General Telephone of the Southeast (General) filed its application in this docket seeking to adjust rates and charges for exchange telephone service in the State of North Carolina to produce additional annual revenues of $9,622,140. At the same time, General filed in this docket an "Application for Interim Rates to Offset Approved Depreciation Rates," (the interim request) subject to refund, in the amount of $1,337,636. The Commission on March 24, 1983, issued an Order suspending the application and the interim request for a period of 270 days from March 30, 1983. On March 30, 1983, it issued an additional Order denying the Company's interim request.

On April 27, 1983, the Commission issued its Order declaring this matter to be a general rate case under G.S. 62-137, setting the matter for investigation and hearing, establishing the test period, scheduling hearings for public witnesses and directing that public notice be given by General.

The Public Staff of the North Carolina Utilities Commission filed its Notice of Intervention in this docket on March 14, 1983. The Public Staff is duly authorized by the provisions of G.S. 62-15 to represent the using and consuming public in this case. The intervention by the Public Staff is deemed recognized pursuant to the provisions of NCUC Rule R1-19(e).

In its Order issued on April 27, 1983, the Commission ordered and directed that interventions be filed in this matter in accordance with applicable Commission Rules and "not less than 10 days prior to the hearing set for September 6, 1983." Published notice of that deadline for intervention was given as required by the Commission. No party other than the Public Staff has intervened prior to the deadline for doing so which was established and publicized as aforesaid.

As a result of negotiations between General and the Public Staff, the only two parties of record, the parties agreed, subject to approval by this Commission, to settle this case upon the following terms and conditions:

1. Effective with the date of the Commission Order approving the agreement of the parties set out herein General may implement the following changes in tariffs, rates, and charges for telephone service provided in the State of North Carolina:

A. The schedule of service connection charges as shown on Appendix A;

B. That the Company shall be authorized to implement a late payment charge pursuant to Commission Rule R12-9(d).

2. General shall be released from any and all obligations to flow thru to its North Carolina customers whatever increase, if any, in its share of toll revenues which results from the decision of this Commission, in the presently pending toll revenue case, NCUC Docket No. P-100, Sub 64.

3. This Agreement is conditioned upon and subject to the acceptance and approval of the Commission. It is expressly understood that this joint agreement resulting from GTSE's tariff filing, testimony, Public Staff audit and testimony is being proposed to settle this docket without any admission or prejudice to any positions which either the Company or the Public Staff might adopt during subsequent proceedings before this Commission, including any further proceedings in this or related cases.

4. The Company and the Public Staff adopt this joint agreement as being in the public interest, without adopting any of the compromised positions set forth herein as rate-making principles applicable to other rate proceedings or to this proceeding in the event the Agreement is not approved by the Commission.

5. It is expressly understood by the parties that this Agreement is conditional and non-severable and shall have no force or effect unless adopted in its entirety by the Commission.

6. The parties agree that the public testimony to be taken in Durham and Monroe, North Carolina, regarding service shall be considered by the Commission, and the Company will take all necessary steps to rectify any service problems or deficiencies, if any are brought forth during the hearings.

7. The parties stipulated and agreed to present to the Commission a consent order settling this case in accordance with the foregoing agreement.

THE COMMISSION, THEREFORE, CONCLUDES that pursuant to G.S. 62-69, it has the authority in the public interest to accept and approved the agreement reached by the parties for settling this case. The Commission further concludes after consideration of all of the terms and conditions of said Agreement that the same is in the public interest, should be approved and should be given effect by the entering of this consent order.

IT IS NOW, THEREFORE, ORDERED:

1. That the agreement of the parties as stated above in paragraphs 1 through 7 be, and the same is hereby, approved.

2. That General be, and hereby is, authorized to file tariffs to become effective on no less than one day's notice reflecting the charges in Appendix A attached, and the late payment charge described herein.

3. That General shall enclosed a printed notice of the late payment charge and the increased service connection charges in each subscriber's bill in accordance with Appendix B attached hereto.

4. That the public hearings now scheduled for Durham, N.C., September 6, 1983, at 7:00 p.m., and Monroe, N.C., for September 1, 1983, at 7:00 p.m. shall be held as scheduled for the specific purpose of receiving testimony from public witnesses only. All other hearings previously scheduled in this docket are hereby cancelled.

ISSUED BY ORDER OF THE COMMISSION.
This the 6th day of September 1983.

NORTH CAROLINA UTILITIES COMMISSION
Sandra J. Webster, Chief Clerk

(SEAL)

CONSENTED TO:
GENERAL TELEPHONE OF THE SOUTHEAST
By:
Dale E. Sporleder
Vice President and General Counsel

Thomas R. Parker
Attorney

PUBLIC STAFF
NORTH CAROLINA UTILITIES COMMISSION

ROBERT P. GRUBER
Executive Director
By:
Theodore C. Brown, Jr.
Staff Attorney

G. Clark Crampton
Staff Attorney

GENERAL TELEPHONE COMPANY OF THE SOUTHEAST
Docket No. P-19, Sub 193
SERVICE CONNECTION CHARGES

I. Residential Rates	
A. Service Order	
1. Primary	$20.50
2. Secondary	9.00
3. Records only	8.25
B. Premises Visit, each	11.00
C. Central Office Work, each	15.00
D. Inside Wiring, each	17.50
E. Equipment Work, each	13.00
F. Reconnection Service	22.40
G. Station Connector	6.50
H. Station Handling	4.50
II. Business Rates	
A. Service Order	
1. Primary	21.50
2. Secondary	9.50
3. Records only	8.50
B. Premises Visit, each	11.00
C. Central Office Work, each	21.00
D. Inside Wiring, each	25.50
E. Equipment Work, each	13.00
F. Reconnect Service	30.00
G. Station Connector	6.50
H. Station Handling	
Business	4.50
PBX & Centrex Stations	3.50

APPENDIX B
NOTICE

The North Carolina Utilities Commission has authorized increased charges for the installation of telephone service and equipment when such work is performed by the telephone company. The new charges can be obtained from your telephone business office. In addition, the Commission has approved a charge of 1% per month on bills not paid within 25 days from the billing date. The new installation charges and the late payment charge will be effective on and after September ___ 1983.

DOCKET NO. P-55, SUB 784

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of	
Southern Bell Telephone and Telegraph Company - Proposed Plan for the Sale of Customer Premises Equipment	) ORDER REQUIRING) SALE OF CUSTOMER) PREMISES EQUIPMENT

HEARD IN: Commission Hearing Room, 430 North Salisbury Street, Raleigh, North Carolina, on December 14, 1982

BEFORE: Chairman Robert K. Koger, Presiding; Commissioner Edward B. Hipp, Commissioner John W. Winters, Commissioner Sara Lindsay Tate, and Commissioner Douglas P. Leary

APPEARANCES:

For the Applicant:

R. Frost Branon, Jr., General Attorney, Southern Bell Telephone and Telegraph Company, Post Office Box 30188, Charlotte, North Carolina 28230

Thomas C. Cartwright, Southern Bell Telephone and Telegraph Company, 4300 Southern Bell Center, Atlanta, Georgia 30375

For the Intervenors:

Theodore C. Brown, Jr., Staff Attorney, Public Staff, North Carolina Utilities Commission, Post Office Box 991, Raleigh, North Carolina 27602

Robert H. Bennink, Jr., Assistant Attorney General, North Carolina Department of Justice, Post Office Box 629, Raleigh, North Carolina 27611

BY THE COMMISSION: On September 2, 1982, the Commission in Docket No. P-55, Sub 784, requested that Southern Bell Telephone and Telegraph Company file a plan for the sale of customer premises equipment. On September 15 and 27, 1982, Southern Bell filed a plan and minimum prices for the sale of new and embedded equipment.

The Public Staff presented the matter at the October 18, 1982, Commission Staff Conference and pointed out three specific problems relating to the Southern Belling filings.

"1. The filings do not address the sale of key systems, small PBX systems, large PBX systems, or other auxiliary terminal equipment.

2. Some of the minimum prices proposed by Southern Bell are unreasonably high and the pricing policy employed by Southern Bell is vague.

3. In light of the pending divestiture of the AT&T system, the accounting treatment proposed by Southern Bell should be modified."

Southern Bell made comments relating to the Company's proposed plan and stated its opposition to the Public Staff's suggested revisions. Moreover, Southern Bell requested to be heard further if the Commission should see fit to alter or amend or change the plan.

The Commission determined that the filing should be neither approved nor disapproved pending a further hearing and investigation into the filing. On November 2, 1982, the Commission issued an Order setting a hearing for December 14, 1982, and requiring that Southern Bell publish Notice of Hearing in newspapers in its service areas.

On November 22, 1982, Southern Bell filed the testimony of John C. Rogers, Jr., District Staff Manager of Product and Inventory Management, J. Thomas Knight, Division Staff Manager for Business Marketing Planning, W.W. Jordan, District Staff Manager of Rates and Costs, and Division Manager in the Comptrollers Department, Roderick G. Turner, Jr.

The Public Staff filed Notice of Intervention on December 2, 1982. The testimony of Communications Division Engineer, Leslie C. Sutton, and Accounting Division Assistant Director Donald E. Daniel was filed December 8, 1982.

The matter came on for hearing at the appointed time and place. Southern Bell presented the testimony and exhibits of the following witnesses: John C. Rogers, Jr., J. Thomas Knight, W.W. Jordan, and Roderick G. Turner, Jr. The Public Staff presented the testimony and exhibits of Leslie C. Sutton and Donald E. Daniel.

EVIDENCE, FINDINGS, AND CONCLUSIONS

The Commission concludes that the difference between the cost of sales positions of the Company and the Public Staff lies primarily in the Public Staff's position that the sales program would not burden the Company's operations with significant increases in personnel. Company witness Jordan testified that the Company could possibly conduct the sales program through the Company's existing force of personnel. The Commission believes that the Public Staff's position on this matter is appropriate and that this level of cost should be increased to reflect the cost of a second public notice presented as a bill insert. The cost of sales and original cost net investment for each of the six single line instruments included in the sales program is included in Appendix A.

Both the Company and the Public Staff agreed that the set fees from the sales of customer premises equipment should be booked into a subaccount of the accumulated depreciation account. The Commission agrees and adopts this accounting treatment.

An area of great concern to the Commission in this proceeding relates to the treatment to be accorded prior gains realized from the sale of CPE at the time of divestiture. The Commission wishes to make it perfectly clear that the benefit of any gain (selling price minus cost of sales and original cost net investment determined without regard to gains and losses from the sale of said equipment) realized from the sale of customer premises equipment will be used to reduce the operating company's North Carolina jurisdictional revenue requirements. The record is clear and devoid of controversy that the in-place and inventoried customer premises equipment considered in this proceeding is currently a part of Southern Bell's North Carolina jurisdictional utility rate base. The evidence is likewise clear that this North Carolina jurisdictional utility rate base is considered in determining the Company's cost of service; i.e., the revenue requirements that are supported by the Company's North Carolina jurisdictional ratepayers. Thus, equity, sound reasoning and logic require that any gain associated with the sale of said equipment should be used to reduce Southern Bell's North Carolina jurisdictional revenue requirements. Based on the foregoing and other evidence of record, the Commission concludes that any gain associated with the sale of said customer premises equipment should not be treated in any manner that would result in

lowering of the book value of the customer premises equipment to be transferred at the time of divestiture. The Commission believes that the foregoing is the fairest and most reasonable treatment that can be afforded the gains which arise from the sale of this utility's rate base. To transfer customer premises equipment at a price below book value, as defined hereinabove, would constitute confiscation of customer funds. Finally, the Commission concludes that the customer premises equipment subject to transfer at divestiture should be transferred at a price equal to the greater of that established by modified final judgment guidelines or net book cost, determined without regard to any gains realized from the prior sale of customer premises equipment. Further, the Commission concludes that the excess of the transfer price at the time of divestiture over such net book cost and the gains previously realized with respect to sale of CPE prior to the divestiture transfer should be used prospectively to reduce the operating company's revenue.

The approved selling prices for in-place and inventory single-line equipment is set forth in Appendix B. Those prices shall remain in full force and effect until further order of this Commission.

SUMMARY OF CONCLUSIONS AND FINDINGS

1. That Southern Bell should offer the following embedded terminal equipment for sale: Standard Rotary, Standard Touch-Tone*, Princess* Rotary, Princess* Touch-Tone*, Trimline* Rotary, Trimline* Touch-Tone*.

2. That Southern Bell should be authorized to sell any of its other embedded equipment.

3. That the incremental transactional expenses and net investment as presented by the Public Staff plus the costs associated with an additional public notice included as a bill insert are proper for determining the cost of sales of customer premises equipment.

4. That Customer Premises Equipment that is in-place on the date of this Order should be sold at the "in-place price."

5. That Customer Premises Equipment leased subsequent to the issuance of this Order should be sold at the "inventory price."

6. That sales prices for in-place telephone sets should not revert to the inventory price 60 days after commencement of the sales program.

7. That on April 1, 1983, Southern Bell should begin selling single-line instruments at prices set forth in Appendix B.

8. That customers should be allowed to spread payments for the equipment (Item 1 above) over a period of three months and Southern Bell should be allowed to impose a service charge of one percent (1%) per month on the unpaid balance.

9. That the following information should be included on the monthly bills of customers who are leasing Customer Premises Equipment.

1. Type or types of sets being leased;
2. Number of such sets being leased;
3. Monthly rental charge per telephone set and total monthly rental charge for all sets being leased; and
4. Approved sales price effective April 1, 1983, for each type of telephone set being leased by the customer.

10. That during the billing cycles of April and August, Southern Bell should include bill inserts clearly listing the kinds and prices of telephone sets that are for sale.

11. That the net gain from customer premises equipment sales (excess of sales price over net book value plus incremental cost of sales as determined herein) be separately identified by recording the gain in a separate subaccount of the accumulated depreciation account.

12. That the Customer Premises Equipment should be transferred from Southern Bell at divestiture at the greater of the maximum allowed by the modified final judgment or net book, with said net book calculated by excluding any gain derived from the sale of customer premises equipment.

IT IS, THEREFORE, ORDERED:

1. That Southern Bell shall begin offering single-line equipment for sale on April 1, 1983, at prices shown in Appendix B, under terms set out in Findings and Conclusions numbers 4, 5, 6 and 8.

2. Southern Bell is hereby authorized to sell any of its other embedded equipment.

3. Southern Bell shall notify its customers of the sale of equipment by means of two bill stuffers and by placing customers' present equipment charges on the bills as in Findings and Conclusions numbers 9 and 10.

4. That Southern Bell shall keep records of all sales and charges and treat gains therefrom as provided in Findings and Conclusions 11 and 12.

5. That Southern Bell shall file quarterly reports with the Chief Clerk of the Commission (16 copies required) setting forth on a monthly and cumulative basis by type of telephone the number of units sold, total revenue realized from the sale of said units, total cost of sales (as approved by the Commission and set forth in Appendix A), and total revenue in excess of cost (gain). The foregoing report shall be filed no later than one month from the last day of each quarterly reporting period. The first report shall be filed no later than August 1, 1983. This reporting requirement shall terminate upon the filing of a final report at the time of divestiture.

ISSUED BY ORDER OF THE COMMISSION.
This the 4th day of March 1983.

NORTH CAROLINA UTILITIES COMMISSION
Sharon Credle Miller, Deputy Clerk

(SEAL)

APPENDIX A
SOUTHERN BELL TELEPHONE AND TELEGRAPH COMPANY
Docket No. P-55, Sub 784
PROPOSED PLAN FOR THE SALE OF CUSTOMER PREMISES EQUIPMENT
Transaction Costs and Total Costs

	Standard Rotary	Standard Touch-Tone	Princess Rotary	Princess Touch-Tone	Trimline Rotary	Trimline Touch-tone
In-Place Sales						
Warranty expense	$ .06	$ .14	$ .09	$ .20	$ .19	$ .24
Other expense	.30	.30	.30	.30	.30	.30
Promotional expense	.44	.44	.44	.44	.44	.44
Second Bill Insert	.20	.20	.20	.20	.20	.20
Gross receipts tax	.94	2.15	1.15	2.38	1.17	2.36
Total transaction costs	1.94	3.23	2.18	3.52	2.30	3.54
Net investment	13.69	32.52	17.04	36.19	17.18	35.72
Total in-place costs	$15.63	$35.75	$19.22	$39.71	$19.48	$39.26
Inventory Sales						
Warranty expense	$ .18	$ .42	$ .27	$ .60	$ .58	$ .72
Proof of purchase stickers	.30	.30	.30	.30	.30	.30
Refurbishing cost	9.37	10.48	11.32	12.20	8.87	10.20
Promotional expense	.44	.44	.44	.44	.44	.44
Second Bill Insert	.20	.20	.20	.20	.20	.20
Supply expense	.62	1.47	.77	1.64	.78	1.62
Gross receipts tax	1.58	2.92	1.93	3.29	1.81	3.14
Total transaction costs	12.69	16.23	15.23	18.67	12.98	16.62
Net investment	13.69	32.52	17.04	36.19	17.18	35.72
Total inventory costs	$26.38	$48.75	$32.27	$54.86	$30.16	$52.34

APPENDIX B
APPROVED SELLING PRICES

Type of Telephone Set	In-Place Selling Price	Inventory Selling Price
Standard Rotary Dial	$17.40	$28.16
Standard Touch-Tone* Dial	37.56	50.57
Princess* Rotary Dial	32.25	45.29
Princess* Touch-Tone* Dial	46.39	61.54
Trimline* Rotary Dial	37.24	48.02
Trimline* Touch-Tone* Dial	46.42	59.51

*Registered Trademark or Service Mark of American Telephone & Telegraph Company

DOCKET NO. P-55, SUB 784

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Southern Bell Telephone and Telegraph Company - Proposed Plan for the Sale of Customer Premises Equipment) ORDER OF CLARIFICATION

BY THE COMMISSION: On March 4, 1983, the Commission issued an Order in this docket Requiring Sale of Customer Premises Equipment. The Order directed Southern Bell to offer for sale the following single-line equipment:

Type of Telephone Set	In-Place Selling Price	Inventory Selling Price
Standard Rotary Dial	$17.40	$28.16
Standard Touch-Tone* Dial	37.56	50.57
Princess* Rotary Dial	32.25	45.29
Princess* Touch-Tone* Dial	46.39	61.54
Trimline* Rotary Dial	37.24	48.02
Trimline* Touch-Tone* Dial	46.42	59.51

*Registered Trademark or Service Mark of American Telephone & Telegraph Company

In addition, the March 4th Order authorized Southern Bell to sell any of its other embedded equipment.

On June 28, 1983, the Public Staff filed a Motion for Clarification of the Commission's March 4 Order. The motion raised the following questions:

1. The Commission's intent in "authorizing" Southern Bell to sell any other embedded equipment.

2. The Commission's intent concerning (1) the sale of volume control equipment for use by subscribers with impaired hearing or speech, (2) single-line sets connected to two-party service, (3) single-line sets connected behind centrex systems, and (4) single-line panel telephones and complete complex key, PBX and Horizon Systems.

The Commission concluded that the Public Staff's motion for clarification required clarification and reconsideration and scheduled oral argument and hearing on August 1, 1983. The matter came on for oral argument as scheduled.

The Public Staff and Southern Bell presented oral argument. In addition, the Commission allowed North Carolina Textile Manufacturers Association to participate. Each of the parties stated their respective positions. The Public Staff stated that their motion was not for reconsideration but merely for clarification. The NCTMA urged the Commission to direct Southern Bell to sell all of its embedded equipment. Southern Bell stated that the language of the March 4 Order needs no clarification.

The Commission issued the following statements to clarify the March 4 Order.

1. Ordering paragraph number 2 authorized Southern Bell to sell any other embedded equipment meaning that Southern Bell is granted the right to sell but is allowed to use its discretionary powers in determining whether or not to sell equipment not listed in paragraph number 1 of the Order.

2. Southern Bell is directed to sell all embedded single line sets listed in paragraph number 1 of the Order including those sets connected to two-party service, behind centrex systems and single-line telephones.

3. Southern Bell is not required to sell complex key, PBX and Horizon Systems.

Southern Bell requested and was granted permission to offer for sale volume control handsets, noisy location handsets and custom telephone units effective August 31, 1983. (Appendix A)

In addition, Southern Bell filed a letter - motion to offer for sale other single-line equipment including the Touch-a-matic* Telephone, the Touch-a-matic* dialer, the Touch-a-matic* 16 Telephone, the Telehelper* Speakerphone, the AutoMatic TelePhone*, and the TeleDialer 16 adjunct dialer. (Appendix B)

The Commission is of the opinion that Southern Bell should be allowed to offer for sale the equipmet itemized in Appendix B at the associated prices.

IT IS, THEREFORE, ORDERED as follows:

1. That the March 4, 1983, Order issued in this docket is affirmed, except as clarified in preceding paragraphs of this Order.

2. That Southern Bell shall be allowed to sell equipment listed in Appendices A and B at the prices indicated therein.

ISSUED BY ORDER OF THE COMMISSION.
This the 22nd day of September 1983.

NORTH CAROLINA UTILITIES COMMISSION
Sandra J. Webster, Chief Clerk

(SEAL)

APPENDIX A
PRICE LIST

Product	Purchase Price		
	In-Place[1]	From Inventory	USOC
Volume Control Handset (Hearing)	$ 7.70	$29.25	VLN+X
Volume Control Handset (Speech)	21.20	61.15	HVS+X
Noisy Location Handset (Push to Listen)	29.00	58.00	VUX+X

Note 1: The In-Place purchase price applies only to handsets in service on or or before August 31, 1983.

Product	Selling Price	USOC
Custom Telephone Unit, without modification, Rotary, each	$22.00	CAK
Custom Telephone Unit, with Modification, Rotary, each	22.00	CAW
Custom Telephone Unit, Previous Modification, Rotary, each	22.00	CAN
Custom Telephone Unit, without Modification, Touch-Tone , each	22.00	CJK
Custom Telephone Unit, with Modification, Touch-Tone , each	22.00	CJH
Custom Telephone Unit, Previous Modification, Touch-Tone , each	22.00	CJL

Registered Trademark of American Telephone and Telegraph Company

APPENDIX B
Equipment Sold In-Place

Product	Selling Price	USOC
Touch-a-matic 12, Touch-Tone#	$ 59.95	T6D+T
Touch-a-matic 16, Rotary (including Installation Kit)	129.95	T6J++
Touch-a-matic 16, Touch-Tone# (including Installation Kit)	129.95	T6J++
Touch-a-matic S, Series Telephone	159.95	T6G++
TeleHelper* Speakerphone	69.95	SPJ++
TeleDialer 16 Adjunct Dialer	99.95	TEKWT
Automatic Telephone		
Non-Remote Operation		
Rotary Dial Set	159.95	TFA+C
Push-Button Dil Set	159.95	TFA+T
Adjunct Unit	119.95	TCC+X
Remote Operation		
Rotary Dial Set (Including Pocket Coder)	179.95	TFS+T
Push-Button Dial Set (including Pocket Coder)	179.95	TFS+T
Adjunct Unit (including Pocket Coder)	169.95	TCJ+X
Additional Pocket Coder	25.95	APC

Equipment Sold From Inventory

Product	Selling Price	USOC
Touch-a-matic 12, Touch-Tone#	$ 79.95	T6D+T
Touch-a-matic 16, Rotary (including Installation Kit)	159.95	T6J++
Touch-a-matic 16, Touch-Tone# (including Installation Kit)	159.95	T6J++
Touch-a-matic S, Series Telephone	179.95	T6G++
TeleHelper* Speakerphone	79.95	SPJ++
TeleHelper* Speakerphone Wall Kit	19.00	OSY
TeleDialer 16 Adjunct Dialer	129.95	TEKWT
Automatic Telephone		
Non-Remote Operation		
Rotary Dial Set	199.95	TFA+C
Push-Button Dil Set	199.95	TFA+T
Adjunct Unit	149.95	TCC+X
Remote Operation		
Rotary Dial Set (Including Pocket Coder)	249.95	TFS+T
Push-Button Dial Set (including Pocket Coder)	249.95	
Adjunct Unit (including Pocket Coder)	229.95	TCJ+X
Additional Pocket Coder	45.95	APC

Registered Trademark of AT&T Company
\# Registered Service Mark of AT&T Company
* Trademark of AT&T Copmpany
Trademark of American Telecommunications Corporation

DOCKET NO. P-55, SUB 792

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Investigation into the Establishment of Extended Area Service Among Certain Telephone Exchanges in Buncombe County) ORDER REQUIRING EAS POLL

HEARD IN: Superior Courtroom, 5th Floor, Courtroom 906, 9th Floor, Buncombe County Courthouse, Courthouse Plaza, Asheville, North Carolina

BEFORE: Chairman Robert K. Koger, Presiding: and Commissioners John W. Winters, A. Hartwell Campbell, Edward B. Hipp, Leigh H. Hammond, and Douglas P. Leary

APPEARANCES:

For the Respondents:

R. Frost Branon, Jr., Gene V. Coker, Southern Bell Telephone and Telegraph Company, P.O. Box 30188, Charlotte, North Carolina 28230
For: Southern Bell Telephone and Telegraph Company

F. Kent Burns, Boyce, Mitchell, Burns and Smith, P.O. Box 2479, Raleigh, North Carolina 27602
For: Continental Telephone Company of North Carolina, Inc.

Phillip J. Smith, Albert Sneed, VanWinkle, Buck, Wall, Starnes and Davis, 18 Church Street, P.O. Box 7376, Asheville, North Carolina 28807
For: Barnardsville Telephone Company

For the Public Staff:

Thomas K. Austin, Staff Attorney, Public Staff, North Carolina Utilities Commission, P.O. Box 991, Raleigh, North Carolina 27602
For: Using and Consuming Public

BY THE COMMISSION: This matter is before the Commission by the filing of a petition bearing approximately 8,600 signatures and entitled "Investigation into the Establishment of Extended Area Service Among Certain Telephone Exchanges in Buncombe County." The Public Staff placed the request on the Commission Staff Conference Agenda on May 26, 1981. The request for Extended Area Service (EAS) involves three telephone companies: Southern Bell Telephone and Telegraph Company (Southern Bell) serving the exchanges of Asheville, Arden, Black Mountain, Enka, Candler, Fairview, Leicester, and Swannanoa; Continental Telephone Company of North Carolina, Inc. (Continental), serving the Weaverville exchange; and Barnardsville Telephone Company (Barnardsville) serving the Barnardsville exchange. By Order issued on January 21, 1983, the Commission scheduled hearings and required the three companies to give public notice of these hearings to their subscribers.

On April 18 and 19, 1983, the Commission conducted a hearing in Asheville to hear testimony from the using and consuming public with regard to the requested EAS. Seventeen members of the public testified at the hearing held on April 18, 1983, and 13 members of the public testified on April 19, 1983. All but one supported the request for Extended Area Service. Additionally, on April 19, 1983, the Commission heard the testimony of Robert Friedlander for Southern Bell, Douglas Baker for Continental, Joe Hicks for Barnardsville, and Leslie Sutton for the Public Staff.

Based on the foregoing, the evidence adduced at the hearings, and the entire record in this matter, the Commission makes the following

FINDINGS OF FACT

1. Southern Bell, Continental, and Barnardsville are duly franchised public utilities lawfully incorporated and licensed to do business in North Carolina and are obligated by their franchises in the North Carolina Public Utilities Act to provide adequate, efficient, and reasonable service to all needing such service in Buncombe County, North Carolina, at just and reasonable rates.

2. Barnardsville and its subscribers shall be excluded from further consideration in this EAS proposal.

3. The basic service rates of the Asheville subscribers of Southern Bell service should not be increased as a result of the establishment of EAS.

4. The subscribers of the Arden, Black Mountain, Enka, Candler, Fairview, Leicester, Swannanoa, and Weaverville exchanges should be polled to ascertain their desire for countywide EAS.

5. The appropriate rate for polling purposes is $1.80 for residential in the Southern Bell exchanges and $4.50 for business; $0.25 for residential in the Weaverville exchange and $0.63 for business.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 1

The evidence supporting this finding of fact is found in prior Commission Orders in this docket and the record as a whole and in Chapter 62 of the General Statutes of North Carolina. This finding is essentially procedural and jurisdictional in nature and is uncontested and uncontroverted.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 2

The evidence for the finding that Barnardsville and its subscribers should be excluded from further consideration is contained in the testimony and exhibits of Barnardsville Telephone Company witness Hicks and Public Staff witness Sutton. Also, three public witnesses from Barnardsville expressed their positions concerning the exclusion of Barnardsville.

Witness Hicks stated that Barnardsville subscribers had very little interest in being included in the proposed countywide EAS system. He reminded the Commission that the Commission rejected the establishment of EAS between Barnardsville and Asheville based upon the desires of the Barnardsville subscribers as expressed in the hearing held in Barnardsville in 1980.

Witness Sutton stated that based upon meetings between representatives of the Buncombe County Telephone Committee (BCTC) and members of the Public Staff, he concluded that the Barnardsville exchange did not desire to be included in the EAS proposal. He indicated that the BCTC advised the Public Staff that there was insufficient interest in Barnardsville to recommend its inclusion in the EAS proposal. Based upon these considerations, he recommended excluding Barnardsville.

Public witness James Nash testified in opposition to the inclusion of Barnardsville in the proposed EAS arrangement. In his opinion, most of the Barnardsville subscribers do not want to be included in the EAS proposal. Also, he reminded the Commission of the resounding opposition expressed by the Barnardsville community in the prior docket which considered establishment of EAS between Barnardsville and Asheville.

Based upon the foregoing evidence, the Commission concludes that the Barnardsville exchange should be excluded from further consideration in the proposed EAS arrangement.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 3

The evidence for the finding that the basic service rates of the Asheville subscribers should not be increased is contained in the testimony and exhibits of Southern Bell witness Friedlander and of Public Staff witness Sutton.

Witness Friedlander testified that it is the position of Southern Bell that no increase should be levied upon the Asheville subscribers if the EAS proposal is implemented. He pointed out that, with the possible exception of Barnardsville, the Asheville subscribers would gain no additional local calling scope.

Witness Sutton recommended that no portion of the cost associated with implementation of the proposed EAS be assessed to the Asheville subscribers. He stated that implementation of his recommendation to exclude Barnardsville from the EAS proposal would mean that there would be no increase in Asheville's local calling area since the Asheville exchange already has EAS to all other exchanges in Buncombe County. As the Asheville subscribers will gain no additional services, witness Sutton stated that it would be inappropriate to increase Asheville's local service rates.

The Commission acknowledges the logic in the positions expressed by witness Friedlander and witness Sutton. The Commission agrees that it would be inappropriate to increase the basic service rates of the Asheville subscribers in view of the Commission's decision to exclude Barnardsville from the proposed EAS system. The Asheville subscribers will receive no additional service as a result of the establishment of EAS. Accordingly, the Commission will impose no portion of the cost associated with implementation of the EAS proposal on the Asheville subscribers.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 4

The evidence and conclusions supporting this finding of fact are found in the testimony of the 30 public witnesses and in the record as a whole.

The Commission notes that, although it had been almost two years between May 26, 1981, when this matter was first presented to this Commission and the April hearing dates of this year when the matter was heard, public interest in countywide EAS had not abated. The Commission further notes that although 30 public witnesses testified at the hearing, many more were present in the audience. Based on the evidence presented in this proceeding, the Commission concludes that a poll should be conducted of all exchanges which will experience an increase in monthly charges if the requested EAS is implemented.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 5

The evidence supporting the finding of fact that the Southern Bell subscribers should be polled at a rate of $1.80 for residential and $4.50 for business and the Continental subscribers at the rate of $0.25 for residential and $0.63 for business is found in the testimony and exhibits of Southern Bell witness Friedlander, Continental witness Baker, and Public Staff witness Sutton.

The proper rates for Continental's exchange at Weaverville as stated above is consistent with previous decisions of this Commission which have excluded the Company's purported lost toll revenues which result from EAS.

The proper rates for Southern Bell as set out above excludes loss of toll revenues. Witness Sutton pointed out that should countywide EAS be implemented, all exchanges would have virtually identical calling scopes, that at present there is only a sixty-cent differential among the Southern Bell

exchanges and that it would be equitable and reasonable to increase every subscriber's rate by the same amount and maintain only the slight differential in their rates. The Commission adopts witness Sutton's position in this matter.

IT IS, THEREFORE, ORDERED as follows:

1. That Southern Bell and Continental shall conduct an EAS poll of all affected subscribers to determine their desire and willingness to pay an increased flat monthly rate for the proposed EAS.

2. That the basic monthly rate increase to be used for polling shall be as follows:

	Residence	Business
Southern Bell		
Arden, Black Mountain, Enka-Candler, Fairview, Leicester, Swannanoa	$ 1.80	$ 4.50
Continental		
Weaverville	$ 0.25	$ 0.63

3. That within ten (10) days from the issuance of this Order, Southern Bell and Continental shall submit for approval by this Commission notices and postcard ballots which emphasize the importance of voting a yes or no on the proposed EAS. Both companies shall coordinate their efforts to determine polling dates and notify the Commission of the polling dates within ten (10) days of this Order.

4. Within two weeks from the last day on which subscribers are to return ballots, Southern Bell and Continental shall file with the Commission the results of the poll.

ISSUED BY ORDER OF THE COMMISSION.
This the 23rd day of August 1983.

NORTH CAROLINA UTILITIES COMMISSION
Sandra J. Webster, Chief Clerk

(SEAL)

Voting Yes - Hipp, Koger, Hammond
Dissenting - Leary, Campbell
Not Voting - Tate, Cook

LEARY, COMMISSIONER, DISSENTING

The majority has been persuaded to disregard two vital principles long established by this Commission when considering EAS proposals. First, the Commission completely ignores the result of toll calling studies which clearly and convincingly demonstrates an insufficient "community of interest" to warrant continuing this investigation. Second, the Commission ignores the differential (unequal) costs of providing EAS in the various Southern Bell exchanges and imposes the same incremental charge on each customer based on "equalized cost."

Over the past several years, parties have given various weight to the use of calling studies to determine a measure of community of interest in EAS considerations. Without speaking to the merits of using this measurement, this case has one of the poorest ratios of customer calls per month I have seen. In this proceeding, the results of the calling study between the Southern Bell exchanges involved in this proceeding reveal that over 88% of the involved customers made not one call to the other exchanges, and that over 93% of the customers made less than two calls between the involved exchanges.

The toll usage pattern of Weaverville subscribers conducted in March of 1983 by Continental Telephone Company of North Carolina reveals a similar lack of community of interest which can best be illustrated as follows:

Weaverville Exchange to	Percentage of Access Lines Making One or Less Calls Per Month
Arden	86.2%
Black Mountain	95.0%
Enka-Chandler	83.5%
Fairview	96.2%
Leicester	88.5%
Swannanoa	97.3%

In the past, the Public Staff and the Commission have acknowledged that a calling rate of two (2) or more calls per subscriber with 40% or more of the subscribers making at least one call during a 30-day period is considered to reflect a sufficient community of interest to justify the initiation of a formal investigation of the EAS matter. The aforementioned usage pattern illustrates such an extreme failure to meet this standard, which indicates no grounds exist to continue this investigation.

Traditionally, except for excluding loss of toll revenues, in pricing EAS this Commission has prescribed that the cost causer shall be the cost payer. Said another way, subscribers in each involved exchange are assessed a flat EAS monthly charge which is based on the cost of providing the EAS to each exchange except that loss of toll revenue is generally not considered in determining the revenue requirement. In this pricing structure, within an exchange, those subscribers making no calls are subsidizing those who would otherwise incur toll charges.

But, in this proceeding the Commission has gone even further in promoting subsidization. Through so-called "equalized rates" the cost to various exchanges is considered in total rather than separately, and the exchanges will be polled using identical increases although the costs incurred are not identical. Specifically, all the Southern Bell exchanges' cost except Asheville is grouped together to develop an "equal" cost, rather than each exchange's cost standing on its own. Thus, subscribers would be required to subsidize subscribers within their own exchange and subscribers in other exchanges. Knowing full well that the national trend toward stripping away of the conventional interstate toll subsidies which will cause local rates to escalate, it is inconceivable that this Commission would encourage local subscribers to subsidize other local subscribers through the "equalized rate" structure. It is uncontroverted that due to deregulation and the national trend of having cost causers become cost payers, customers everywhere will experience dramatic rate increases. Assuming that North Carolina households do not behave differently from national patterns identified in the Perl

Study,* a 60% increase in subscriber revenue requirements mirrored in increased flat rate subscriber charges could cause a fall-off of overall residence subscribers on the order of 4.4%. For example, residential customers in the Southern Bell exchanges that are being polled will have a substantial rate impact on their bills, assuming the $1.80 is eventually approved, when coupled with the FCC imposed access charge of $2.00 to become effective January 1, 1984. This impact by exchange is as follows: .

Exchange	Base Rate	EAS & Access Charge	% Increase
Leicester	$10.65	$3.80	35.7%
Black Mountain	$10.95	$3.80	34.7%
Enka-Chandler			
Fairview			
Swannanoa			
Arden	$11.25	$3.80	33.7%

The above increases in rates does not reflect any additional access charge that could be added by this Commission in pending intrastate toll access decisions.

For these reasons, I must dissent from the Order which uses equalized rate increases to poll subscribers on their willingness to pay for a service heretofore not used at all by an overwhelming majority of those being polled.

Douglas P. Leary, Commissioner

* "Economic and Demographic Determinants of Residential Demand for Telephone Service," Dr. Lewis J. Perl, NERA, 1978; "Use of the Perl Study In Access Charge Discussions," NERA, 1982; Report on the Study of Telephone Use, Rates and Regulations, Carruthers, et al., 1983.

COMMISSIONER CAMPBELL, DISSENTING.

As a matter of conviction on my part, as well as correcting false statements in the Order based on the vote of the majority narrow vote of three to two with two abstentions, I hereby exercise my right as a Commissioner to dissent to what I consider an ill-advised Order which may also be an illegal violation of G.S. 62-140 relating to discrimination.

This matter came before this Commission based upon a filing of approximately 8,600 signatures, but the Order fails to cite the fact that conditions have changed considerably since such filing. Both Barnardsville and Asheville have been dropped out of consideration since the filing of the petition, and such petition contains names from these exchanges. Further, the names were gathered on the assumption that the enhanced service would be on the basis of no further costs to the subscribers. Again, the hearing was not ordered or heard under any such assumption. Therefore, the significance of noting 8,600 signatures in the Order is a mistaken assumption that the same persons which signed the petition are yet in favor of such a proposal as was considered at the hearing.

While 8,600 signatures of total 71,519 main station customers represents 12% of the total, it is a misleading number for us to consider. The petition is comparable to getting a petition from school children to extend the Christmas recess for all the month of December together with a free gift from Santa.

In addressing the Order, I naturally agree with Findings of Fact #1, 2, and 3. I strongly take exception to Findings of Fact #4 and 5, and most particularly with Evidence and Conclusions #4 and 5.

The so-called Evidence and Conclusions have very little to do with the testimony of record in the Asheville hearing on August 18 and 19, 1983. At the inception of the hearing, the Chairman made an opening statement which enumerated, among other things, that the issues to be heard included the "Need for and public interest involved, and clearly stated; "whether or not any pooling arrangement resulting from equalized rate increases is legal." (Emphasis added.)

This vital consideration is not addressed by a single word of evidence or opinion in the record as to the legality of such a pooling arrangement to equalize costs irrespective and irregardless of costs. Inasmuch as Chairman Koger, in his wisdom, enunciated the legality of such an equalized pooling of costs as being a major consideration, and inasmuch as this issue was not addressed, one can only conclude that the majority ran rough-shod over this issue without any consideration. I cannot agree with this fl
The testimony of the thirty witnesses did not establish any public necessity for this service, over and above the convenience to the individuals on a personal use basis. Not one single elected representative of the affected Towns, Cities, County or State appeared to testify at the hearing. Most all of the witnesses testified to their personal needs or their savings from using toll in the affected areas. Further, no witness agreed to paying any additional funds to receive EAS. As a matter of record, one witness expressed the implied position when he says, "I ask that EAS be established for the citizens of the affected areas without increasing rates since a sizeable rate increase has already been proposed."

If need for such extended EAS service was one of a vital public interest, certainly the elected officials of this area would have been there to testify to such a need. No such evidence from these officials, elective or appointive, exists.

Perhaps the most offensive parts of this Order relate to the issue of pooling of all cost and pooling revenues from all exchanges. Evidence and Conclusions for Finding of Fact #5 is erroneous when it says:

"The evidence supporting the finding of fact that Southern Bell subscribers should be polled at a rate of $1.80 for residential and $4.50 for business and the Continental subscribers at the rate of $0.25 for residential and $0.63 for business is found in the testimony and exhibits of Southern Bell witness Friedlander, Continental Telephone Company witness Baker, and Public Staff witness Sutton." This is an absolutely false statement since both Southern Bell witness Friedlander and Continental witness Baker said exactly the opposite in their testimony. Both said that inclusion of toll-revenue losses should be added as a cost factor to be included in the total costs. Further, they said that there should be no pooling or equalizing of rates in the proposal. Such testimony was disregarded by the Commission despite the fact that it is irrefutable that toll-revenue losses will occur.

Even Public Staff witness Sutton who apparently developed the figures for a pooling of costs refused to support the concept. In the official record,

Volume II, page 129, the Attorney of the Public Staff asked his one and only witness as follows: "Mr. Sutton, there has been some discussion of pooling of rates. Is the Public Staff recommending any pooling of rates?" In response to this direct question, Mr. Sutton wisely answered, "No, sir, not at this point."

In filing a Motion for the Public Staff requesting a public hearing, filed on August 23, 1982, page 2, the Public Staff stated, "The question of pooling revenue requirements was raised in the case only because Barnardsville was included in the initial request. The pooling issue becomes moot if Barnardsville is excluded from consideration in this matter."

Despite the fact that the Public Staff witness Sutton disavowed the support of the Public Staff, and despite the fact that its own attorney filed a Motion that the pooling concept became moot with the removal of Barnardsville, we now find this questionable concept, possibly an illegal concept, that we shall submit a poll to the people adopting this pooling of costs.

Now let us look at the practical workings of this pooling concept of averaging costs. Please note the existing Southern Bell exchange rates:

	R-1 rate	B-1 rate
Arden	$11.25	$29.30
Asheville	11.25	29.30
Black Mountain	10.95	28.65
Enka-Candler	10.95	28.65
Fairview	10.95	28.65
Swannanoa	10.95	28.65
Leicester	10.65	27.85

At present there is only a $0.60 variance between the highest residential price of $11.25, and the lowest $0.65. For business rates the present variance between $29.30 and $27.85 is $1.45. Observe that Asheville is the highest of both rate classes.

Note the distortion which would exist under this Order:

	R-1 rate	B-1 rate
Arden	$13.05	$33.80
Asheville	11.25	29.30
Black Mountain	12.75	33.15
Enka-Candler	12.75	33.15
Fairview	12.75	33.15
Swannanoa	12.75	33.15
Leicester	12.45	29.30

One further matter of consideration which needs to be considered. The following chart indicates what the rates for Southern Bell Buncombe County exchanges would be for each exchange, both with and without consideration of the loss of toll revenues. This is taken from a filing made by Southern Bell dated December 17, 1982.

	Costs with Toll Losses		Costs without Toll Losses	
	R-1	B-1	R-1	B-1
Arden	$2.89	$ 7.23	$1.43	$ 3.58
Black Mountain	2.08	5.20	0.99	2.48
Enka-Candler	2.98	7.45	1.14	2.85
Fairview	2.86	7.15	1.83	4.58
Swannanoa	3.65	3.89	2.37	5.93
Leicester	8.65	21.63	6.39	15.98

These figures are consistent with the Order in that it is without consideration of Barnardsville, and without charges to Asheville.

To show the actual order which would establish EAS charges on a pooled basis, please notice the variance from cost. Using $1.80 residential and $4.50 business, please note the variance.

	R-1	B-1	(without toll revenue losses)
Arden	-.37	-.92	
Black Mountain	-1.01	-2.02	
Enka-Candler	-.66	-1.65	
Fairview	+.03	+.08	
Swannanoa	+.57	+ 1.43	
Leicester	+4.59	+11.48	

The variance ranges from -$1.01 to +$4.59 for residential service, a total range of $5.60 per month. For business it represents a range of -$2.02 to a +$11.48, a total range of $13.50 per month. This represents a subsidy from three exchanges (Arden, Black Mountain, Enka-Candler) to go to two exchanges (Swannanoa, Leicester) with one exchange being basically net (Fairview). If one could determine the number of main stations divided between residential and business, one could calculate the subsiy event, it is taking from three exchanges to subsidize the cost of two exchanges. It is my judgement that this is both an inequity, and of doubtful legality.

Whereas Asheville and Arden presently are charged $1.45 above the lowest exchange (Leicester), suddenly Asheville becomes the cheapest rate for all residential customers by as much as $1.80 per month for residential. For business the rate is $4.50 higher than for Asheville. And yet Asheville will have equal calling scope in Buncombe County with every other Southern Bell exchange. This makes for certain inequitable and discriminatory pricing. To my mind, this is an inequity and discriminatory in nature. Any subscriber in out-of-Asheville exchanges who would vote for this scheme would have every right to claim discrimination. They get only equal Buncombe County calling scope with Asheville, and in order to get this expanded calling scope, they go from below-Asheville rates to above Asheville rates. There is little wonder that the Public Staff disclaims any Public Staff support for a pooling of prices concept.

Why was Asheville deleted for consideration for the pooling costs? The answer is obvious. Asheville would be voting to increase its rates modestly by $0.11 residential and $0.28 for business, and they would vote "No" on this issue. Asheville has 40,188 main stations out of a total of 71,519 and could vote down any such proposal. This is known as a practical matter by the petitioners, the Public Staff, and the Commission.

To me, this pricing concept is illegal because of discrimination even as the Stanly County EAS was discriminatory. (The Stanly County was such that some subscribers of one particular exchange would have been charged an EAS fee while other members of the very same exchange would be given free service. The Public Staff, by Motion, withdrew the appeal of the Stanly County Case from the North Carolina Court of Appeals.) It is likely that this Order, if the pooled rates are approved by the subscribers, will also be appealed to the Courts.

In conclusion, let it be noted that this entire pooling concept is a radical departure by the Commission from its entire history of EAS proceedings. This changing in the middle of the stream on procedures is being done without benefit of a careful review or generic hearing in this matter. The Order does not even attempt to give any rationale or justification for making such a change. If this departure is allowed and implemented, one can be sure that there will be turmoil in present EAS Counties, and further demands for all-exchange County EAS petitions. This can create confusion, ill feelings, and discriminatory charges if different schedules are adopted.

Finally, on the pooling issue, please note from exhibits of Southern Bell, the highest cost for installing EAS occurs in the Leicester exchange. Yet, by the Order, Leicester exchange continues to have the lowest basic rates of any exchange. In other words, subscribers in all other exchanges are being called upon to subsidize the customers in Leicester.

For the stated reasons, I dissent from this Order. However, I want to enter into a discussion of leaving out the loss of toll revenues as an element of EAS cost determinations, and the impact of driving up all basic service costs.

PHILOSOPHICAL PROBLEMS.

Several decades ago this nation adopted a concept of Universal Service for all Citizens. The implementation of this has been accomplished by reason of large subsidies for residential customers from interstate and intrastate toll revenues. Every telephone company executive as well as every member of this Commission knows we are in the midst of a crisis of pricing as the result of the opening of competitive forces in the interstate toll area. Whereas the actual cost of providing actual basic residential service in North Carolina are paying rates far below the true cost of service, ranging on average to $10 or $11 monthly rates while costs have grown to the $20 to $30 monthly. This difference between costs and revenues has been possible because of subsidies contributed from toll and business services.

This Commission is greatly disturbed by recent developments by the F.C.C. which is starting an interstate access fee for residential customers beginning January 1, 1984 of $2.00 per month. This is to begin the painful withdrawal of toll subsidies contributing to local basic service. I concur with my fellow Commissioners in opposing this method of placing "access" charges on the residential customers on the theory that it is inequitable to customers who use little or no toll service. In any event, this Commission is being called upon to consider an additional intra-state "access" charge to be placed upon customers.

We are in a rushing crunch which is developing because of the loss of toll revenues as a subsidy. Universal Service as a concept is being gravely challenged as a withdrawal from basic rates.

Now what are we doing when we start withdrawing intra-state toll revenues? We are contributing to the very crisis which we deplore. We are playing dangerous economics when we allow intra-state tolls to be ignored, bypassed, and decreased by the rapid expansion of EAS in North Carolina. This has been a growing parasite upon toll revenues on an intra-state basis.

The encouragement of EAS with no regard to the loss of toll can be considered just as irresponsible as Members of Congress who have voted increased entitlements for political popularity without increasing the subsidies from some source. The Social Security program came near to disaster because of this irresponsibility. Somehow, we have deluded ourselves into acting as if there was such a thing as a "free lunch." Our whole economic system is endangered with this approach.

Before it is too late, we need to let telephone subscribers know the hard reality which they are facing. This Order, and similar such Orders, are drawing down the amount of intra-state tolls, while increasing "entitlements" (EAS). The time for paying the piper is rapidly approaching. This is the pricing crisis which we face.

This Order is but the latest in a long chain of Orders that is irresponsible as a pricing concept and customer signal of what is happening.

It is because of this pricing crisis that companies are rushing foward a reduction of basic service in optional local measured service.

If and when we encourage telephone customers to adopt EAS on such unsound economic principles of "pooling of charges" concepts, we are contributing to the problem. As the statement says, "We have met the enemy, and the enemy is us."

I cannot be responsible as a regulator if I vote to lead our customers down the road of a fool's paradise.

In reality I view this EAS Order as being quite comparable to levying an "access" charge upon these customers by making all customers to be assessed for the advantage of a very few.

In Conclusion, the record does not support any public necessity for this ingenious Concept of pooling expense. The toll study made in Buncombe County indicates the initial criteria for establishing EAS has not been met. In a letter to the initiators of this proceeding, Mr. Gene Clemmons, Director of Communications Staff of the Public Staff, indicated:

"A calling rate of two (2) or more calls per subscriber with 40% or more of the subscribers making at least one call during a 30-day study period is considered to reflect a sufficient community of interest to justify the initiation of a formal investigation of the EAS matter."

A toll-calling study was ordered and conducted. According to the unrefuted testimony and evidence of the record, the calling study shows that over 88% of

the Buncombe County residential subscribers did not make one call to the other exchanges. Additionally, 93% of subscribers made less than two calls between the various exchanges.

The primary question is why, oh why, did not the Commission have the courage to do what they should have done had they followed their own minimum requirements for establishing need for EAS and had dismissed this petition?

The claim that this is only the democratic process of allowing the people to vote has some appeal. But when the question put to them is discriminatory and far different from what they first requested and desired, it alleviates me from feeling any duty or necessity from having a vote taken on an entirely different proposition.

Further, if these subscribers who are being polled had some of the figures and facts contained in this dissent, it is possible that they would vote with a more informed base of data. To vote without having full disclosure of information could be an excerise of futility.

To this end, I feel the duty and necessity to dissent with this Order.

A. Hartwell Campbell, Commissioner

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Laneys Moving & Storage, Inc.	T-1955, Sub 2	7-21-83
M & S Transport, Inc.	T-578, Sub 7	7-21-83
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Carlyle Brothers Trucking	T-2097, Sub 1	7-26-83
Dalton, Cephus J.	T-2060, Sub 1	7-26-83
Dehaven's Transfer & Storage, Inc.	T-1276, Sub 4	7-26-83
Durham Transfer & Storage, Inc.	T-519, Sub 4	7-26-83
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P-100, Sub 64 - Order Overruling Exceptions and Affirming Recommended Order (Commissioner Tate Dissenting) (11-9-83)

P-100, Sub 65 - Order Denying Motion to Amend of Southern Bell Telephone and Telegraph Company and Exceptions of General Telephone Company of the Southeast (12-28-83)

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SP-3 (11-23-83))

Carolina Cogreneration Company, Inc. - (Order Granting Certificate of Public Convenience and Necessity to Construct a Steam and Electric Power Cogeneration Facility at Texasgulf Chemicals Co.)
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Radford Construction Company - (Order Authorizing Construction of Ivy River Hydroelectric Plant on the Ivy River)
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Carolina Power & Light Company - Recommended Order Denying Relief Prayer for and Dismissing Complaint of Thomas L. Smith
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Duke Power Company - Order Closing Docket in Complaint of Annie L. Colson
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Duke Power Company - Order Closing Docket on August 15, 1983, in Complaint of Henry Baker
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G-5, Sub 183 (3-16-83)

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B-411 (11-29-83)

AUTHORITY GRANTED - COMMON CARRIER

Dyer, Norman G. - Order Granting Common Carrier Operating Authority to Transport Passengers and Their Baggage from the Bus Station Located on Main Street in Roxboro to U.S. 501 and Along U.S. 501 to Durham and to the Durham Bus Station on Main Street, and Return Over the Same Route.
B-401 (5-25-83)

Joshlis Charters, Floyd David Dockery, d/b/a - Order Granting Common Carrier Authority to Transport Passengers and Their Baggage from Belmont (Highway 74 West to Intersection with Highway 221 North to its Intersection with I-40 west to Asheville, and Return)
B-405 (8-26-83)

New Hope Charter, Larry Gaddis Evangelistic Association, d/b/a - Order Granting Common Carrier Authority to Transport Passengers and Their Baggage from Gastonia Over Highways 279 and I-85 to Greensboro and Return Over the Same Route
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Convenient Tours, Patricia Ann Long, d/b/a	B-410	9-28-83
Edwards, Patricia T.	B-402	3-21-83
Great Getaway Tours, Inc.	B-407	7-29-83
Hawfields Community Travelers, Linda M. Braxton, d/b/a	B-391	2-18-83
Hepler Tours, H. M. Hepler, d/b/a	B-395	2-21-83
International Tourist Group, The, Mildred Fuller Lohr, d/b/a	B-398	4-11-83
Jaunts and Journeys, Inc.	B-409	8-18-83
Meetings, Incorporated	B-388	5-20-83
Northeastern Travel Services, Velvet Lynn Jennings and Lois L. Jennings, d/b/a	B-399	3-21-83
North State Heritage Tours, Inc.	B-400	4-5-83
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Blue Ridge Mountain Tours	EB-706	8-5-83
Smith, Jr., Robert Vernon	EB-733	5-23-83

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B-366, Sub 2 (4-29-83)

America Charters, Ltd. - Order Approving Merger of Gastonia Transit Company, Inc., into America Charters, Ltd.
B-366, Sub 3 (4-29-83)

Seashore Transportation Company - Order Approving Merger of STC Development Corporation, a Wholly Owned Subsidiary of North American Phillips Corporation, into Seashore Transportation Company
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Triad Lines, Inc. - Order Approving Change in Name from Triad Motor Lines, Inc., and Ammending Certificate No. B-359 Accordingly
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B-366, Sub 1 (4-29-83)

McBroom Coach, Inc. - Order Approving Sale and Transfer of Certificate No. B-254 from S. D. Small, d/b/a Central Buslines of North Carolina
B-392 (4-29-83)

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B-415 (11-4-83)

Dyer, Norman G. - Order Granting Temporary Authority to Transport Passengers and Their Baggage from Bus Station in Roxboro to U.S. 501 and Along U.S. 501 to Durham and the Bus Station on Main Street and Return
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Intercity Bus Lines, Inc. - Order Granting Temporary Authority to Transport Passengers and their Baggage from Winston-Salem, over U.S. Highway 311 to its junction with U.S. Highway 220
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King's Bus Service, Calvin R. King, d/b/a - Order Granting Temporary Authority to Transport Passengers and Their Baggage from Grifton to Vanceboro and Return
B-416 (11-4-83))

Mike's Travel And Adventures, Michael David Adkins, d/b/a - Order Granting Temporary Authority to Engage in the Business of a Broker Within the State
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Tel-A-Tour, Inc. - Order Granting Temporary Authority Pending Final Decision of the Commission
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Carolina Transit Lines of Charlotte, Inc. - Recommended Order Denying Exemption
B-295, Sub 5 (6-14-83)

Piedmont Coach Lines, Inc. - Order Granting Request to Discontinue Service
B-110, Sub 21 (12-21-83)

Southern Coach Company - Order Granting Request to Suspend Regular Route Bus Passenger and Express Service Between Raleigh and Wilmington, Effective May 6, 1983
B-30, Sub 53 (4-20-83)

Trailways Southestern Lines, Inc. - Recommended Order Denying Application to Discontinue Bus Runs 2101 and 2100
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Trailways Southeastern Lines, Inc. - Final Order Overruling Exceptions and Affirming Recommended Order
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O'Boyle Tank Lines, Inc. - Order Amending Application, Allowing Withdrawal of Protest and Cancelling Hearing
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Ginn, Richard Carl - Recommended Order Dismissing Application for Contract Carrier Operating Authority
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Jones, Charles Robert - Recommended Order Dismissing Application for Contract Carrier Operating Authority
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Wallace Trucking Company - Recommended Order Denying Application to Transport Group 3, Petroleum and Petroleum Products, etc., Between Trift, North Carolina, and Points in Scotland, Richmond, Moore, Hoke, and Robeson Counties
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Affordable Movers, Roger Knight and George A. Mease, d/b/a - Recommended Order Granting Amended Application for Common Carrier Certificate to Transport Group 18, Household Goods, Statewide
T-2289 (8-5-83)

B & B Movers, Richard M. Burkett, d/b/a - Order Granting Common Carrier Authority
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Bre-Dav Transportation, Inc. - Order Granting Common Carrier Authority to Transport Group 1, General Commodities with Certain Restrictions, and Group 21, Cargo Container and Packaging Equipment, Statewide
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Bunch Trucking Company, Inc. - Order Granting Common Carrier Authority to Transport Group 1, General Commodities, Except Commodities in Bulk, in Tank Vehicles, Statewide
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