

# QWEST CORP

## FORM 10-Q (Quarterly Report)

Filed 5/15/1998 For Period Ending 3/31/1998

Address	1801 CALIFORNIA ST SUITE 2950 DENVER, Colorado 80202
Telephone	303-896-3099
CIK	0000068622
Fiscal Year	12/31

---

# UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D. C. 20549

## FORM 10-Q

☒ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934

For the Quarterly Period Ended March 31, 1998

OR

☐ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

*Commission File Number 1-3040*

## U S WEST Communications, Inc.

A Colorado Corporation IRS Employer No. 84-0273800

1801 California Street, Denver, Colorado 80202

Telephone Number (303) 896-3099

THE REGISTRANT, A WHOLLY OWNED SUBSIDIARY OF U S WEST, INC., MEETS THE CONDITIONS SET FORTH IN GENERAL INSTRUCTION H(1)(a) and (b) OF FORM 10-Q AND IS THEREFORE FILING THIS FORM WITH REDUCED DISCLOSURE FORMAT PURSUANT TO GENERAL INSTRUCTION H(2).

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

---

Form 10-Q  
TABLE OF CONTENTS

Item		Page
	PART I - FINANCIAL INFORMATION	
1.	U S WEST Communications, Inc. Financial Information	
	Consolidated Statements of Income - Three Months Ended March 31, 1998 and 1997	3
	Consolidated Balance Sheets - March 31, 1998 and December 31, 1997	4
	Consolidated Statements of Cash Flows - Three Months Ended March 31, 1998 and 1997	6
	Notes to Consolidated Financial Statements	7
2.	U S WEST Communications, Inc. Management's Analysis of the Results of Operations - (Reduced disclosure format pursuant to General Instruction H(2))	9
	PART II - OTHER INFORMATION	
1.	Legal Proceedings	14
6.	Exhibits and Reports on Form 8-K	14

CONSOLIDATED STATEMENTS  
OF INCOME (Unaudited)

U S WEST COMMUNICATIONS, INC.

Dollars in Millions	Three Months Ended March 31,	
	1998	1997
Operating revenues:		
Local service	\$1,350	\$1,231
Interstate access service	698	687
Intrastate access service	206	200
Long-distance network services	201	250
Other services	214	179
Total operating revenues	2,669	2,547
Operating expenses:		
Employee-related expenses	822	806
Other operating expenses	511	450
Taxes other than income taxes	93	105
Depreciation and amortization	518	522
Total operating expenses	1,944	1,883
Operating income	725	664
Interest expense	91	96
Gain on sale of rural telephone exchanges	-	18
Other expense - net	27	22
Income before income taxes	607	564
Provision for income taxes	233	215
NET INCOME	\$374	\$349

See Notes to Consolidated Financial Statements.

CONSOLIDATED BALANCE SHEETS  
(Unaudited)

U S WEST COMMUNICATIONS, INC.

	March 31, 1998	December 31, 1997
Dollars in Millions		
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 289	\$ 26
Accounts and notes receivable - net	1,533	1,608
Inventories and supplies	144	124
Deferred tax asset	196	226
Prepaid and other	67	68
Total current assets	2,229	2,052
Gross property, plant and equipment	33,447	33,182
Accumulated depreciation	19,362	19,041
Property, plant and equipment - net	14,085	14,141
Other assets	810	815
Total assets	\$17,124	\$17,008
=====	=====	=====

See Notes to Consolidated Financial Statements.

CONSOLIDATED BALANCE SHEETS  
(Unaudited), continued

U S WEST COMMUNICATIONS, INC.

	March 31, 1998	December 31, 1997
Dollars in Millions		
LIABILITIES AND SHAREOWNER'S EQUITY		
Current liabilities:		
Short-term debt	\$ 589	\$ 497
Accounts payable	1,230	1,439
Employee compensation	247	321
Dividends payable	374	192
Advanced billings and customer deposits	306	292
Other	1,135	982
Total current liabilities	3,881	3,723
Long-term debt	4,931	5,019
Postretirement and other postemployment benefit obligations	2,352	2,365
Deferred income taxes	925	891
Deferred credits and other	635	610
Contingencies		
Shareowner's equity		
Common shares - one share without par value, owned by parent	8,017	8,017
Cumulative deficit	(3,617)	(3,617)
Total shareowner's equity	4,400	4,400
Total liabilities and shareowner's equity	\$17,124	\$17,008

See Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF  
CASH FLOWS (Unaudited)

U S WEST COMMUNICATIONS, INC.

Three Months Ended March 31,	1998	1997
	Dollars in Millions	
OPERATING ACTIVITIES		
Net income	\$374	\$ 349
Adjustments to net income:		
Depreciation and amortization	518	522
Gain on sale of rural telephone exchanges	-	(18)
Deferred income taxes and amortization of investment tax credits	62	22
Changes in operating assets and liabilities:		
Postretirement medical and life costs, net of cash fundings	(24)	(11)
Accounts receivable	76	60
Inventories, supplies and other current assets	(26)	(3)
Accounts payable and accrued liabilities	97	193
Other - net	12	(12)
Cash provided by operating activities	1,089	1,102
INVESTING ACTIVITIES		
Expenditures for property, plant and equipment	(550)	(395)
Purchase of PCS licenses	(18)	-
Proceeds from (payments on) disposals of property, plant and equipment	19	(7)
Proceeds from sale of rural telephone exchanges	-	7
Cash used for investing activities	(549)	(395)
FINANCING ACTIVITIES		
Net repayments of short-term debt	(62)	(429)
Repayments of long-term debt	(23)	(54)
Dividends paid on common stock	(192)	(307)
Equity infusions from U S WEST Communications Group	-	73
Cash used for financing activities	(277)	(717)
CASH AND CASH EQUIVALENTS		
Increase (decrease)	263	(10)
Beginning balance	26	92
Ending balance	\$289	\$ 82

See Notes to Consolidated Financial Statements.

**U S WEST COMMUNICATIONS, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**For the Three Months Ended March 31, 1998**

(Dollars in millions)

(Unaudited)

**A. Summary of Significant Accounting Policies**

**Basis of Presentation.** U S WEST Communications, Inc. (the "Company") is incorporated under the laws of the State of Colorado and is an indirect, wholly owned subsidiary of U S WEST, Inc. ("U S WEST") and a major component of U S WEST Communications Group ("Communications Group").

The Consolidated Financial Statements have been prepared by the Company, pursuant to the interim reporting rules and regulations of the Securities and Exchange Commission ("SEC"). Certain information and footnote disclosures normally accompanying financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to such SEC rules and regulations. In the opinion of the Company's management, the Consolidated Financial Statements include all adjustments, consisting of only normal recurring adjustments, necessary to present fairly the financial information set forth therein. It is suggested that these Consolidated Financial Statements be read in conjunction with the financial statements and notes thereto included in the Company's Form 10-K/A for the year ended December 31, 1997.

**B. U S WEST Separation**

On October 25, 1997, the Board of Directors of U S WEST adopted a proposal to separate U S WEST into two independent companies (the "Separation"). As a result of the Separation, the Communications Group will become an independent public company and will be renamed "U S WEST, Inc." ("New U S WEST"). In addition, Media Group's directory business known as U S WEST Dex, Inc. ("Dex") will be aligned with New U S WEST (the "Dex Alignment"). Following the Separation, U S WEST will continue as an independent public company comprised of the current businesses of Media Group other than Dex and will be renamed "MediaOne Group, Inc." ("MediaOne").

The Separation will be implemented pursuant to the terms of a separation agreement between U S WEST and New U S WEST (the "Separation Agreement"). In connection with the Dex Alignment, (i) U S WEST will distribute, as a dividend, an aggregate of \$850 in value of New U S WEST common stock to holders of Media Group common stock and (ii) \$3.9 billion of U S WEST debt, currently allocated to Media Group, will be refinanced by New U S WEST.

Further information about the Separation is contained in U S WEST's proxy statement mailed to all shareowners on April 20, 1998. U S WEST shareowners have been asked to consider and approve the Separation at its annual meeting to be held on June 4, 1998. Subject to shareowner approval, the transaction is expected to be completed by mid-June 1998.



**U S WEST COMMUNICATIONS, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
(Dollars in millions)

(Unaudited)

**C. Contingencies**

There are pending regulatory actions in local regulatory jurisdictions that call for price decreases, refunds or both.

Oregon. On May 1, 1996, the Oregon Public Utilities Commission ("OPUC") approved a stipulation terminating prematurely the Company's alternative form of regulation ("AFOR") plan, and it then undertook a review of the Company's earnings. In May 1997, the OPUC ordered the Company to reduce its annual revenues by \$97, effective May 1, 1997, and to issue a one-time refund, including interest, of approximately \$102 to reflect the revenue reduction for the period May 1, 1996 through April 30, 1997. The one-time refund is for interim rates which became subject to refund when the Company's AFOR plan was terminated on May 1, 1996.

The Company filed an appeal of the order and asked for an immediate stay of the refund with the Oregon Circuit Court which granted the Company's request for a stay, pending a full review of the OPUC's order. On February 19, 1998, the Oregon Circuit Court entered a judgment in the Company's favor on most of the appealed issues. The OPUC appealed on March 19, 1998. The potential exposure, including interest, at March 31, 1998, is not expected to exceed \$210.

Utah. In another proceeding, the Utah Supreme Court has remanded a Utah Public Service Commission ("UPSC") order to the UPSC for hearing, thereby establishing two exceptions to the rule against retroactive ratemaking: 1) unforeseen and extraordinary events, and 2) misconduct. The UPSC's initial order denied a refund request from interexchange carriers ("IXCs") and other parties related to the Tax Reform Act of 1986. The potential exposure, including interest, at March 31, 1998, is not expected to exceed \$160.

State Regulatory Accruals. The Company has accrued \$148 at March 31, 1998, which represents its estimated liability for all state regulatory proceedings, predominately the items discussed above. It is possible that the ultimate liability could exceed the recorded liability by an amount up to approximately \$220. The Company will continue to monitor and evaluate the risks associated with its local regulatory jurisdictions, and will adjust estimates as new information becomes available.

In addition to its estimated liability for state regulatory proceedings, the Company has an accrued liability of approximately \$230 at March 31, 1998 related to refunds in the state of Washington. The Company expects that the majority of these refunds will be issued to ratepayers, IXCs and independent local exchange carriers ("LECs") during the second- and third-quarters of 1998.

**Form 10-Q - Part I****Item 2. Management's Analysis of the Results of Operations**

(Dollars in millions)

Some of the information presented in or in connection with this report constitutes "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. Although the Company believes that its expectations are based on reasonable assumptions within the bounds of its knowledge of its business and operations, there can be no assurance that actual results will not differ materially from its expectations. Factors that could cause actual results to differ from expectations include: (i) greater than anticipated competition from new entrants into the local exchange, intraLATA toll and wireless markets, (ii) changes in demand for the Company's products and services, including optional custom calling features, (iii) higher than anticipated employee levels, capital expenditures, and operating expenses (such as costs associated with year 2000 remediation), (iv) the loss of significant customers, (v) pending regulatory actions in state jurisdictions, (vi) regulatory changes affecting the telecommunications industry, including changes that could have an impact on the competitive environment in the local exchange market, (vii) a change in economic conditions in the various markets served by the Company's operations that could adversely affect the level of demand for telephone, wireless, or other services offered by the Company, (viii) greater than anticipated competitive activity requiring new pricing for services, (ix) higher than anticipated start-up costs associated with new business opportunities, (x) delays in the development of anticipated technologies, or the failure of such technologies to perform according to expectations.

**Results of Operations - First Quarter 1998 Compared with First Quarter 1997**

Following are details of the Company's reported net income, normalized to exclude the effects of certain nonoperating items.

	Three Months Ended March 31,		Increase	
	1998	1997	\$	%
Reported net income	\$374	\$349	\$25	7.2
Adjustment to reported net income:				
Gain on sale of rural telephone exchanges(1)	-	(11)	11	-
Normalized income	\$374	\$338	\$36	10.7

(1) In first-quarter 1997, the Company sold certain rural telephone exchanges in Nebraska for a pretax gain of \$18 and an after-tax gain of \$11.

During 1998, the Company's normalized income increased \$36, or 10.7 percent, to \$374. The increase in normalized income is primarily due to higher demand for services partially offset by interstate access rate reductions, higher expenses related to interconnection and start-up costs associated with growth initiatives, including wireless personal communications services ("PCS").

**Form 10-Q - Part I****Item 2. Management's Analysis of the Results of Operations (Dollars in millions), continued****Operating Revenues**

	Three Months Ended March 31,		Increase (Decrease)	
	1998	1997	\$	%
Local service	\$1,350	\$1,231	\$119	9.7
Interstate access service	698	687	11	1.6
Intrastate access service	206	200	6	3.0
Long-distance network services	201	250	(49)	(19.6)
Other services	214	179	35	19.6
Total	\$2,669	\$2,547	\$122	4.8

**Local Service Revenues.** During 1998, local service revenues increased \$119, or 9.7 percent, to \$1,350, primarily as a result of access line growth and increased demand for new product and service offerings, and existing central office features. Total reported access lines increased 568,000, or 3.6 percent, during the past 12 months, of which 284,000 was attributable to second lines. Second line installations increased 25.2 percent. Access lines grew 634,000, or 4.1 percent, when adjusted for sales of approximately 66,000 rural telephone access lines during the past twelve months. Also contributing to the increase in revenues were rate increases of \$17 in various states, and interim compensation revenues from IXC's as a result of the FCC payphone orders which took effect in April 1997.

**Interstate Access Service Revenues.** Interstate access service revenues increased \$11, or 1.6 percent, to \$698 during 1998, primarily due to a change in the classification of universal service fundings which increased revenues by \$19. In 1997 these fundings were offset against interstate access service revenues through a contra-revenue account. Beginning in 1998 these fundings are recorded as access expense within other operating expense. Excluding the effects of the reclassification, interstate access revenues declined \$8, or 1.2 percent, primarily due to the effects of lower prices under the FCC's current price cap plan and the effects of 1997 true-ups to sharing-related accruals. Partially offsetting these decreases were the effects of a 6.1 percent increase in billed interstate access minutes of use and increased demand for private line services.

**Intrastate Access Service Revenues.** Intrastate access service revenues increased \$6 in 1998, or 3.0 percent, to \$206, primarily due to a 7.1 percent increase in billed intrastate minutes of use and higher demand for private line services. Partially offsetting the increase were net rate reductions of \$5 in local jurisdictions, the majority of which were in the state of Washington.

**Long Distance Network Services Revenues.** Long-distance network service revenues decreased \$49, or 19.6 percent, to \$201, primarily due to the effects of competition and rate reductions of \$14 in local jurisdictions. Also contributing to the decline were the implementation of multiple toll carrier plans ("MTCs") in various jurisdictions in 1997. The MTCs essentially allow independent telephone companies to act as toll carriers and are net income neutral with the reduction in toll revenues largely offset by increased intrastate access service revenues and lower access expense.

**Form 10-Q - Part I****Item 2. Management's Analysis of the Results of Operations (Dollars in millions), continued**

Other Services Revenues. Revenues from other services increased \$35, or 19.6 percent, to \$214, primarily as a result of greater sales of inside wire maintenance, continued market penetration in voice messaging services and increased sales of wireless communication services.

**Costs and Expenses**

	Three Months Ended March 31,		Increase (Decrease)	
	1998	1997	\$	%
Employee-related expenses	\$822	\$806	\$16	2.0
Other operating expenses	511	450	61	13.6
Taxes other than income taxes	93	105	(12)	(11.4)
Depreciation and amortization	518	522	(4)	(0.8)
Interest expense	91	96	(5)	(5.2)
Gain on sale of rural telephone exchanges	-	18	(18)	-
Other expense - net	27	22	5	22.7

**Employee-Related Expenses.** Total employee-related expenses increased \$16, or 2.0 percent, to \$822 during 1998, primarily due to higher contract labor costs and increased salaries and wages. The higher contract labor costs were predominately a result of systems development work (which includes expenses related to interconnection and year 2000 costs) and marketing and sales efforts. The increase in salaries and wages was a result of workforce increases and wage increases which were largely offset by the transfer of approximately 1,200 employees during third-quarter 1997 to an unregulated affiliate.

**Other Operating Expenses.** Other operating expenses increased \$61, or 13.6 percent, to \$511 during 1998. The increase is primarily due to increased affiliate expense as a result of the above referenced transfer of employees to an unregulated affiliate, interconnection expenses and costs associated with growth initiatives (primarily PCS). Other operating expenses also increased \$19 due to the change in the classification of the universal service funding expenses. Partially offsetting the increases were reduced access expense (primarily due to dial-around competition and the MTCPs) and a 1997 reserve adjustment associated with billing and collection activities performed for IXC's.

**Taxes Other Than Income Taxes.** Taxes other than income taxes decreased \$12, or 11.4 percent, primarily as a result of adjustments related to the 1997 property tax accrual.

**Interest Expense.** Interest expense decreased \$5, or 5.2 percent, to \$91, primarily as a result of lower average debt levels as compared to 1997. Partially offsetting the decrease was a reduction in the amount of interest capitalized resulting from a lower average balance of telecommunications plant under construction.

**Gain On Sale of Rural Telephone Exchanges.** In 1997, the Company sold certain rural telephone exchanges in Nebraska resulting in a pretax gain of \$18.

**Other Expense - Net.** Other expense increased primarily due to additional interest expense associated with the Company's state regulatory liabilities.

**Other Items**

During the first quarter of 1998, Moody's downgraded the Company's senior unsecured debt from Aa3 to A2 due to recent regulatory rulings and financial challenges associated with the Separation. See "Contingencies." The Company's debt remains under review by Moody's for possible downgrade pending clarification of New U S WEST's corporate structure and future strategic initiatives.

On May 7, 1998, Duff & Phelps reaffirmed the Company's senior unsecured debt and commercial paper ratings of AA- and D-1+, respectively.

**Contingencies**

There are pending regulatory actions in local regulatory jurisdictions that call for price decreases, refunds or both.

**Oregon.** On May 1, 1996, the OPUC approved a stipulation terminating prematurely the Company's AFOR plan, and it then undertook a review of the Company's earnings. In May 1997, the OPUC ordered the Company to reduce its annual revenues by \$97, effective May 1, 1997, and to

issue a one-time refund, including interest, of approximately \$102 to reflect the revenue reduction for the period May 1, 1996 through April 30, 1997. The one-time refund is for interim rates which became subject to refund when the Company's AFOR plan was terminated on May 1, 1996.

The Company filed an appeal of the order and asked for an immediate stay of the refund with the Oregon Circuit Court which granted the Company's request for a stay, pending a full review of the OPUC's order. On February 19, 1998, the Oregon Circuit Court entered a judgment in the Company's favor on most of the appealed issues. The OPUC appealed on March 19, 1998. The potential exposure, including interest, at March 31, 1998, is not expected to exceed \$210.

Utah. In another proceeding, the Utah Supreme Court has remanded a UPSC order to the UPSC for hearing, thereby establishing two exceptions to the rule against retroactive ratemaking: 1) unforeseen and extraordinary events, and 2) misconduct. The UPSC's initial order denied a refund request from IXC's and other parties related to the Tax Reform Act of 1986. The potential exposure, including interest, at March 31, 1998, is not expected to exceed \$160.

**Form 10-Q - Part I**

**Item 2. Management's Analysis of the Results of Operations (Dollars in millions), continued**

State Regulatory Accruals. The Company has accrued \$148 at March 31, 1998, which represents its estimated liability for all state regulatory proceedings, predominately the items discussed above. It is possible that the ultimate liability could exceed the recorded liability by an amount up to approximately \$220. The Company will continue to monitor and evaluate the risks associated with its local regulatory jurisdictions, and will adjust estimates as new information becomes available.

In addition to its estimated liability for state regulatory proceedings, the Company has an accrued liability of approximately \$230 at March 31, 1998 related to rate refunds in the state of Washington. The Company expects that the majority of these refunds will be issued to rate payers, IXC's and independent LEC's during the second- and third-quarters of 1998.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings

The Company and its subsidiaries are subject to claims and proceedings arising in the ordinary course of business. While complete assurance cannot be given as to the outcome of any contingent liabilities, in the opinion of the Company, any financial impact to which the Company and its subsidiaries are subject is not expected to be material in amount to the Company's operating results or its financial position.

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits

Exhibit No.	
12	Statement regarding computation of earnings to fixed charges ratio of U S WEST Communications, Inc.
27	Financial Data Schedule

(b) Reports on Form 8-K Filed During the First Quarter of 1998:

No reports on Form 8-K have been filed for the Company during the first quarter of 1998.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

U S WEST Communications, Inc.

May 15, 1998

/s/ Allan R. Spies  
-----  
Allan R. Spies  
Vice President and Chief  
Financial Officer



U S WEST COMMUNICATIONS, Inc.  
 RATIO OF EARNINGS TO FIXED CHARGES  
 (Dollars in Millions)

	Quarter Ended	
	3/31/98	3/31/97
-----	-----	-----
Income before income taxes	\$ 607	\$ 564
Interest expense (net of amounts capitalized)	91	96
Interest factor on rentals (1/3)	16	15
	-----	-----
Earnings	\$ 714	\$ 675
Interest expense	\$ 97	\$ 103
Interest factor on rentals (1/3)	16	15
	-----	-----
Fixed charges	\$ 113	\$ 118
Ratio of earnings to fixed charges	6.32	5.72
-----	-----	-----

**ARTICLE 5**

CIK: 0000068622

NAME: U S WEST COMMUNICATIONS, INC.

MULTIPLIER: 1,000,000

PERIOD TYPE	3 MOS
FISCAL YEAR END	DEC 31 1998
PERIOD START	JAN 01 1998
PERIOD END	MAR 31 1998
CASH	289
SECURITIES	0
RECEIVABLES	1,553
ALLOWANCES	0
INVENTORY	144
CURRENT ASSETS	2,229
PP&E	33,447
DEPRECIATION	19,362
TOTAL ASSETS	17,124
CURRENT LIABILITIES	3,881
BONDS	4,931
PREFERRED MANDATORY	0
PREFERRED	0
COMMON	8,017
OTHER SE	(3,617)
TOTAL LIABILITY AND EQUITY	17,124
SALES	2,669
TOTAL REVENUES	2,669
CGS	0
TOTAL COSTS	0
OTHER EXPENSES	1,944
LOSS PROVISION	0
INTEREST EXPENSE	91
INCOME PRETAX	607
INCOME TAX	233
INCOME CONTINUING	374
DISCONTINUED	0
EXTRAORDINARY	0
CHANGES	0
NET INCOME	374
EPS PRIMARY	0
EPS DILUTED	0

---

**End of Filing**Powered By **EDGAR**  
Online

© 2005 | EDGAR Online, Inc.