



Mike Kadas
Director

Montana Department of Revenue



Steve Bullock
Governor

April 14, 2016

Robert G. Strong
Executive Director – Tax
AT&T Inc.
2700 Watt Ave., Suite 4014
Sacramento, CA 95821-6236

RE: DOR Response to AT&T Provided Cost of Capital Studies

Dear Mr. Strong:

On behalf of the Montana Department of Revenue I would like to thank you for providing AT&T's Cost of Capital Studies for our review. After reviewing the provided studies and additional industry information the department has made changes to our Capitalization Rate Study for the Telecommunications industry. These changes are summarized below:

- The department used the most up to date Value Line information to better match our calculations to the lien date.
 - This resulted in some minor changes to capital structure calculations and beta calculations and thus had an effect on yield capitalization rates.
 - The yield capitalization rate for the Telephone industry increased from 6.90% to 7.00%, the rate for Wireless was unchanged, and the rate for Cable decreased but was offset by an increase in the cost of debt.
- It was determined the cost of debt used in the yield capitalization rate for the Cable industry should be more consistent with the cost of debt used for the Telephone and Wireless industries.
 - In this case the cost of debt for Cable was matched to the cost of debt for Telephone and Wireless.
 - This caused an increase in the cost of debt from 5.0% to 6.0%

- The method the department uses to determine direct capitalization rates was modified to a determination of overall cost of capital instead of independently calculating cost of equity and cost of debt rates. This should produce a more accurate and consistent conversion of income and cash flows to market value.
 - This caused adjustments to each direct capitalization rate and is detailed in the chart below:

<i>Net Operating Profit After Tax:</i>			
Industry	Previous Cap Rate	Adjusted Cap Rate	Change
Telephone	5.30%	5.50%	0.20%
Wireless	4.70%	5.25%	0.55%
Cable	4.90%	5.15%	0.25%
<i>Gross Cash Flow:</i>			
Industry	Previous Cap Rate	Adjusted Cap Rate	Change
Telephone	14.50%	13.10%	-1.40%
Wireless	14.50%	13.90%	-0.60%
Cable	13.70%	13.30%	-0.40%

The updated Capitalization Rate Study will be posted on the department's website for your review and can be found at <https://revenue.mt.gov/home/publications>.

The Department welcomes the opportunity to discuss these changes and any other issues in more detail during the appraisal process. If you have any further questions or concerns my contact information is below.

Thanks,



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