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BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of General Telephone Company of California, a California corporation (U 1002 C), for authority to increase and/or restructure certain intrastate rates and charges for telephone services.	Application 87-01-002 (Filed January 5, 1987)
Investigation on the Commission's own motion into the rates, tolls, rules, charges, operations, costs separations practices, contracts, service and facilities of GENERAL TELEPHONE COMPANY OF CALIFORNIA, a California Corporation; and of all the telephone corporations listed in Appendix A, attached hereto.	I.87-02-025 (Filed February 11, 1987)

(See D.87-08-051 and D.87-12-070 for appearances.)

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SECOND INTERIM OPINION

I. Synopsis of Decision

This second interim decision provides for a revenue reduction for GTE California (General), formerly General Telephone Company of California, of $218.304 million in addition to the decrease in customer billings of $112.190 million on an annual basis ordered by Interim Decision (D.) 87-12-070 dated December 22, 1987, as revised by Advice Letter No. 5125 filed February 29, 1988, a total reduction of $330.494 million. The bases for our adopted summary of earnings leading to the $330.494 million revenue reduction are detailed in this decision.

This decision does not modify the return on equity of 12.75% which will provide a rate of return of 10.90% found reasonable in Interim D.87-12-070.

As set forth in the section on rate design, the $218.304 million incremental reduction results from a reduction of 13.45% to the present billing surcharges set forth in General's Schedule Cal. P.U.C. No. A-38 which are collected on a "bill and keep" basis not subject to intercompany settlement. The final apportionment of the rate reduction to the various customer groups and the final tariff schedules based on this record will be addressed in our next decision on this matter, together with such issues as whether General should be ordered to adjust its rates for the 1988 test year to flow through to the ratepayers approximately $27,582,755 tax savings realized on retired bonds; the present policies of General in the area of customer service, billing, and testing; GTE California's practices and policies regarding women/minority business enterprises; and the various issues raised at the public participation hearings in these proceedings.

II. Summary of Proceedings

General requests authority in this application to increase and/or restructure certain of its intrastate rates and charges. The effect of the proposed changes will be to reduce its test year revenue requirement by approximately $114 million to provide a rate of return of 11.90% on General's intrastate rate base.

To enlarge the scope of these proceedings to cover essentially all aspects of General's public utility operations, this Commission issued Order Instituting Investigation (I.) 87-02-025 into the rates, tolls, rules, charges, operations, costs, separations, practices, contracts, services, and facilities of Pacific Bell (Pacific) and all of the California telephone utilities that interconnect with General.

After due notice, 95 days of hearing have been held before Administrative Law Judges (ALJ) N. R. Johnson, K. Tomita, or M. J. Galvin in Los Angeles, San Francisco, or at the public participation hearings throughout General's service area.

The hearings on rate of return were held in San Francisco before ALJ Tomita and that phase of the matter culminated in the issuance of D.87-12-070 on December 22, 1987. Hearings on the balance of the matter were completed on January 11, 1988, and the matter was submitted on concurrent opening briefs due February 22, 1988 and concurrent closing briefs due March 7, 1988. Opening briefs were filed by General, DRA, Minority Coalition (Coalition), AT&T Communications of California (AT&T), Consumers Coalition of California (CCC), Pacific Bell (Pacific), Communications Workers of America AFL-CIO (CWA), Western Burglar & Fire Alarm Association (WBFAA), Telephone Answering Services of California (TASC), and Toward Utility Rate Normalization (TURN). Closing briefs were filed by General, DRA, AT&T, CCC, Coalition, WBFAA, and TASC.

DRA's reply brief was unavoidably filed one day late. On the basis that such late filing gave DRA an enormous advantage over other parties, General filed a motion to strike the brief. A review of the brief does not disclose any basis for such a claim. The motion is therefore denied.

Transcript Corrections

General and WBFAA filed requests for transcript corrections. DRA objected to some of the correction requests filed on May 7, 18, 19, and 27, 1987, July 9, 1987, and August 11, 1987, on the basis that the requested changes altered the substance of either the witness' testimony or counsel's questions. ALJ Johnson has reviewed those objections and has sustained a number of them. Appendix B lists those which will not be adopted. The balance of the transcript correction requests will be granted.

The Still-Pending Issue of Flow Through of Tax Savings

This issue was discussed briefly in the preceding synopsis, and involves $27,582,755 tax savings realized on retired bonds. On March 15, 1988, DRA filed a motion for an order to show cause, requesting that the Commission reopen the proceeding, or initiate a new proceeding, to explore the impacts of General's alleged failure to flow through certain tax savings. Specifically, DRA asserts that General has failed to return to its ratepayers the tax benefits it has received as a result of its decision to take advantage of a lower interest rate environment and retire certain high coupon bond issues. While the Commission has permitted amortization of the call premium, and unamortized discounts and expenses over the life of the reissued debt, DRA believes that General has been deducting these sums for tax purposes in the years in which it retired the bonds, and has failed, unlike other utilities, to flow through these tax savings to its ratepayers.

On March 25, 1988, General filed its formal opposition, arguing that the motion is an attempt to update selectively DRA's direct showing after the close of the record, and further that the motion inaccurately portrays the facts. General believes that it is ratably flowing through to its ratepayers the tax benefits in issue, albeit using a method which may differ somewhat from procedures followed by some other utilities.

On June 13, 1988, DRA filed a formal supplement to its motion recommending that General be ordered to use the "net of tax" method in connection with setting up a balancing account to capture the remaining tax benefits, i.e. the unamortized balance of the realized tax savings, during the pendency of this controversy. On June 21, 1988, General filed its formal opposition to the DRA supplement, asserting that balancing account treatment is unprecedented, unfair (since General believes it is currently flowing through these tax benefits), and violative of the retroactive ratemaking ban.

Although this issue could not be accommodated previously due to the demands of the hearing schedule, we will leave this proceeding open to consider it at this point. Thus, General and DRA will have a full opportunity to litigate the issue. However, in order to protect the ratepayer interest in the interim, we will adopt DRA's suggestion and require General to establish a balancing account into which it will book the difference between currently authorized rates and rates it would be collecting if it revised its accounting for refinancings to follow the net of tax method. The balancing account amounts will be subject to refund, in whole or in part, following hearings to determine 1) whether General ought to be ordered permanently to revise its accounting of bond refinancing premiums, and unamortized discounts and expenses and 2) what method General may use to do so. A prehearing conference will be held to set hearing dates and dates for submission of testimony in connection with this issue.

Comments on Proposed Decision

General

As provided in Section 311 of the Public Utilities Code, ALJ Johnson prepared a Proposed Decision which was filed with the Commission and served on all parties on July 8, 1988. Rules 77.1 through 77.5 of this Commission's Rules of Practice and Procedure permit parties to file comments on such a Proposed Decision within 20 days of its date of mailing July 28, 1988 and reply comments five days later.

Comments were filed by General, DRA, Pacific, and TURN and reply comments were filed by General, DRA, and AT&T-C. In addition, Independent Consulting Services (ICS) filed a motion for leave to file late-filed comments. ICS' motion is denied on the basis that it is not a party to these proceedings and therefore it has no standing to file comments to the ALJ's Proposed Decision, under Rule 77.2. However, ICS' concerns regarding the protective connecting arrangements (PCA) issue are addressed to the extent we address General's PCA-related comments.

Most of the comments reargued the parties' positions and, for that reason, are not further discussed; however, to the extent the comments point to factual, legal, or technical errors, they are addressed briefly below, and the Proposed Decision is corrected accordingly.

Comments of General

General states that the revenue requirement reduction is overstated by $35.804 million as shown in the attachment to its comments. To the extent they result in changes to the Proposed Decision, these alleged calculation errors are discussed in detail.

Item	Intrastate Amount (Thousand of Dollars)
Telephone Plant in Service	$12,300
Depreciation Reserve	(519)
Maintenance	1,937
Depreciation Expense	7,160
Subtotal	20,878
Expense Changes	10,420
Revenue Changes	4,506
Total	$35,804

The $12.3 million plant in service relates to an alleged plant deficiency of $155.424 million. However, the comments address $109.732 million with a revenue effect of $8.354 million as follows:

Item	Amount	Revenue Effect
Analog COSE	$ 1,854,000	$ 134,000
Digital COSE	26,754,000	2,052,000
Modifications	1,888,000	144,000
Capital Planning Adjust.	20,000,000	1,534,000
Transfers 100.2 to 100.1	59,236,000	4,490,000
	$109,732,000	$8,354,000

For Account 207 Analog COSE, DRA estimated $8.445 million as contrasted with General's estimate of $19.927 million. As set forth in the decision the primary difference in the estimates is the amount of growth and the inclusion by General of $4.768 million of unspecified other projects. As detailed in the decision a compromise growth of $14 million was adopted. To this was added $288,000 for equal access and USS/MSS and $4.788 million for other projects. The totals were increased to reflect TPI and apportioned between 100.1 and 100.2 to derive the 100.1 figure of $13.985 million. General alleges error stating other project costs on a 100.1 basis ($3.305 million) should be deducted from General's estimate before averaging and then added back without equal access and USS/MSS to yield a C-207 Account 100.1 amount of $15.839

million or $1.854 million greater than set forth in the decision. General's computations are based on the faulty premise that General's and DRA's estimates were averaged on a total estimate basis reflecting 1988 figures. Actually the only averaging was the growth figures before application of the TPI. The calculations as described on pages 151-153 are correct.

General alleges that the Account C-209 Digital COSE 100.1 gross additions adopted in the proposed decision are $26.754 million understated because they are based on initial NTEP cost data and do not include all of the costs that General will reasonably incur in connection with digital COSE. A review of the record lends support to General's position. However, General developed factor of actual to planning NTEP of 1.32 which appears to be excessive. DRA witness McCarthy recommended an adjustment because of an experienced 1.17 factor. Even this would appear high as it reflects initial bidding rounds. Experience gained from the bid process should decrease this ratio. Consequently, for purposes of this decision we will adopt a factor of 1.10% which will increase the C-209 Account 100.1 balance $8.348 million with an accompanying revenue requirement increase of $640,000.

General alleges that the proposed decision understates the 1988 Test Year Account 100.1 balance because it fails to reflect the appropriate level of transfers from Account 100.7 to Account 100.1. The decision has been modified to correct this error.

General questions the "Modifications Line and Trunk Testing" set forth on page 153 of the decision. Actually the decision should read Modifications of $1.888 million by General and Line and Trunk Testing of $1.833 million by DRA. General is merely rearguing its position taken in the briefs; consequently, we will give no weight to the arguments. The same holds true for the $20 million capital planning adjustment set forth in the comments.

General alleges that the computations included in the decision for maintenance, commercial, and traffic accounts are understated by $8.987 million because labor escalation factors different than the adopted factor of 1.118 were used and improper allowance was made for the adopted operator level as compared to the operator level used by DRA. After review, we believe the adopted expense level calculations are correct. Consequently General's claims are without merit.

General states that depreciation expense should be calculated as a function of adopted depreciation rates times adopted plant balances and that its analysis of the decision indicates either incorrect rates or the wrong plant balances were used in the decision. Our staff reviewed the depreciation expense calculations and found them to be correct. We will, however, increase our adopted depreciation expense to reflect our previously discussed plant balance increases.

General claims that the total of pension and benefits expense of $88.579 million was understated by $5.971 million. Our staff has reviewed the calculations and finds the pension and benefits expense was overstated by $52,000 and should total $88,527. General further states that a mathematical error of $5.5 million occurred when the Travelers and HMO medical expense amounts were added together. This is correct.

Our staff's review of the corporate oversight calculations indicated the adjustment was overstated by $2.3 million which this decision corrects.

General alleges the adopted general services and license expense is understated by $1.0 million because the estimate was developed using a 2% management labor escalation factor rather than the 4.2 % factor adopted in the decision. This is true and the account will be adjusted accordingly.

General states that although this decision does not address General's final test year rate design, one matter of considerable customer concern should be decided. This matter is the proposed relocation of the rate center for the Etiwanda Exchange to provide local calling between the Ontario and Etiwanda Exchanges. DRA concurs in this recommendation. We see no reason to delay action on this limited rate change proposal and will modify the decision to reflect the above described rate center relocation.

In its comments (Section XIII) General notes that Ordering Paragraphs 8 and 9 regarding PCA refunds in the test year billing cycle are inconsistent with D.88-03-069, which ordered General to continue its PCA refund program through August 21, 1988. We have deleted these ordering paragraphs and the associated finding and text.

General has also suggested inclusion of a table showing the adopted Results of Operations on a separated basis. DRA and AT&T-C join in this suggestion. This table has been added to the decision.

Comments by DRA

We have clarified the discussion of DRA's request for flow-through of tax savings, to underscore the fact that the request relates to the unamortized balance of the tax savings in issue.

DRA's allegation that the corporate oversight adjustment is incorrectly calculated is correct. In addition to the errors set forth in DRA's Table A, it is noted that the labor inflation factor differs from the adopted factors. We will modify the corporate oversight allocation adjustment to correct both of these error groups.

We have also eliminated some internally inconsistent language from the discussion of our adoption of DRA's transfer pricing mechanism, to clarify our intention to follow the approach adopted in D.86-01-026.

We have corrected the reference to DRA's tax witness. Also, we will include appropriate tax tables among the appendices. The decision is also modified at Section V.J. (Taxes) to clarify the procedure we adopt to reflect pre-test year impacts of interest synchronization, pursuant to D.84-04-038 in I.86-10-002.

We have corrected the allowance for the HMO cost portion of medical insurance expense in Account 672 to reflect our adopted labor force reduction rather than DRA's labor force reduction.

DRA has suggested miscellaneous grammatical corrections and a corrected estimate of weighted average plant in service; these corrections are appropriate and will be adopted.

III. Rate of Return

D.87-12-070 authorized a rate of return for General of 10.90% for the test year 1988. The capital structure and cost factors comprising this rate of return are as follows:

Item	Capital Structure	Cost Factor	Weighted Cost
Long-term debt	41.50%	9.01%	3.74%
Short-term debt	2.50	7.00	0.18
Preferred stock	2.50	6.41	0.16
Common equity	53.50	12.75	6.82
Total	100.00%		10.90%

The after-tax coverage of the above 10.90% rate of return is 2.91 times and the pre-tax coverage is approximately 3.94 times excluding short-term debt.

This decision does not modify the rate of return authorized by D.87-12-070.

IV. Affiliated Interests

A. General

GTE Corporation (GTE) is the parent company of more than 60 communications, products, research, and service subsidiaries with operations in 40 states and 19 countries abroad with 1985 combined revenues and sales of over $15.7 billion. Those GTE subsidiaries that can have an effect on General's operations and are, therefore, of particular interest to this Commission are GTE Communications Systems Corporation (CSC), GTE Service Corporation (GTESC), GTE Laboratories (GTE Labs), GTE Directories Corporation (Dir Corp), GTE Telecom Marketing Corporation (TMC), and GTE Data Services (GTEDS). In addition, General has a wholly owned subsidiary, GTEL. In keeping with this Commission's long history of reviewing transactions between a utility and its affiliates and subsidiaries to ensure that, for ratemaking purposes, the affiliates' costs allocated to the utility are just and reasonable and the affiliates' returns will not exceed that which would exist had the utility performed the service or installed the facilities itself, DRA's Affiliation Investigation Team (Team) reviewed the transactions between General and the above affiliates and/or subsidiaries.

DRA made a number of recommendations regarding 1985 and 1986 expenditures by General. In some instances, the issue involved whether allegedly extraordinary or inappropriate previous expenses should be removed from the historical date for purposes of trending past expenses to determine test year 1988 levels. In other instances, DRA considered the potential amortization of revenues anticipated in the test year from activities that generated allegedly inappropriate expenses in prior years.

B. <u>General Services and Licenses</u>

Account 674, General Services and Licenses (GS&L) expenses represent billings from General's affiliates, GTESC and GTE Labs. Account 674 is summarized in Chapter 11, General and Other Operating Expenses, of DRA's Results of Operations Report. The analysis of General's affiliated relationship with GTESC and with that portion of GTE Labs related to software, electronics, photonics, and material research was presented by Financial Examiner IV Michael Amato. That portion of Team's study relating to telecommunications system research by GTE Labs was presented by Junior Utilities Engineer Michael Vannucchi. Testimony on the 1988 test year estimate for Account 674 was presented on behalf of General by its Budget Director, L. C. Manion. Rebuttal testimony to DRA witness Amato was presented on behalf of General by Dr. A. N. Mosich, Professor of Accounting, University of Southern California.

General's estimate of 1988 test year Account 674 expenses is $55.8 million as contrasted to Team's estimate of $33.0 million, a difference of $22.8 million or 69.1%. The following tabulation details the composition of the differential and sets forth our adopted results:

	DRA	General	Difference Amount	Difference Percent	Adopted
		($ in Millions)			
Telops Hdqtrs.	$103.2	$105.4	$ 2.2	2.1%	$105.4
GTE Labs (Chap.3)	27.5	53.2	25.7	93.5	28.2
Corporate	54.4	62.3	7.9	14.5	55.6
Service Fee Credit	(23.3)	(27.4)	(4.1)	(17.6)	(23.8)
GTOC-Prorated Service Corp.	161.8	193.5	31.7	19.6	165.4
Prorate % to General	23.0%	29.6%	6.6%	28.7	29.6%
Prorate to General	$ 37.2	$ 57.3	$ 20.1	54.0	$ 49.0
Adjustments:					
Unreg. Activ.	(3.0)	(1.5)	(1.5)	(50.0)	(4.0)
International/ Corp. Comm.	(0.8)		(0.8)	(100.0)	(1.0)
Corp. Aircraft	(0.4)		(0.4)	(100.0)	(0.6)
Total Adjustments	(4.2)	(1.5)	(2.7)	(64.3)	(5.6)
Test Year GS&L Est.	$ 33.0	$ 55.8	$ 22.8	69.1%	$ 43.4

(Red Figure)

Essentially, the estimates differ because the Team considered more current information; used beneficiary analysis criteria in determining GTE Labs' expense; used a lower two-factor prorate to allocate GTESC's expenses to General; excluded a greater level of unregulated activity expenses; and disallowed certain GTESC expenses. Under a contract signed by the chairman of the board of GTESC and the president of General, GTESC agreed to provide a central organization which can render certain services to General that include:

- Advice and counsel on management and operational matters.
- The coordination of standards on equipment, materials, and supplies.

- The development of plant, engineering, and safety practices.
- The establishment and maintenance of performance measurement programs.
- The development of procedures for depreciation and separations studies.
- The development of marketing and sales programs and advice and assistance on the promotion of new services.
- The maintenance of personnel records on all key personnel, and the implementation of intercompany transfers and management development programs.
- Staff assistance on financial matters, accounting practices, budget procedures, taxes, insurance, security, safety, training, and centralized management of the pension plan.
- Staff assistance on legal matters, corporate and public affairs, and advertising.

1. GTESC's Expense Allocations

GTESC's expenses are generally allocated among four GTE groupings of companies, i.e. Telephone Operations (Telops), Diversified Products, Communication Services, and GTE Corporation, based upon a review of time spent on the various activities by GTESC-salaried employees. Expenses allocated to Telops are split between domestic General Telephone Operating Companies (GTOC) and non-GTOCs. Generally non-GTOCs are billed service fees by GTESC based on a percentage of their operating revenues. Telops' expenses, less the above service fee credits, are prorated to each domestic GTOC on the basis of the percent of each company's total operating expenses and taxes (exclusive of investment tax credit) to the total operating expenses and taxes (exclusive of investment tax credit) of all domestic GTOCs. Each month, General is billed for its prorated share of GTESC's operating expenses and, on the same bill, General's prorated share of GTE Labs' expense. For the period 1977 through 1986, the GS&L expenses billed General have increased from $6.9 million to $49.3 million.

As set forth in the previous tabulation, Team has determined that $161.8 million will be the test year level of GTESC expenses for proration to General and the other GTOCs. As indicated in the tabulation, this compares to $193.5 million estimated by General. $25.7 million of the $31.7 million difference relates to the GTE Labs' estimate; the remaining $6.0 million of the difference generally reflects Team's use of the 1987 GTESC budget as contrasted to General's use of the 1986 GTESC budget. Based on the later data set forth in the 1987 GTESC budget, which is more likely to portray actual test year conditions, we will adopt DRA's estimate of $103.2 million for Telop's headquarters, $54.4 million for corporate, and a $23.3 million service fee credit increased to $105.4 million, $55.6 million, and $23.8 million credit, respectively, to reflect our adopted management labor escalation factor.

2. <u>GTE Labs' Expenses</u>

GTE Labs' expenses are allocated to the Telephone Operating Group, the Diversified Product Group, and the GTE Communication Services Group on the basis of revenues and sales of each company to the total revenues and sales of all GTE companies. General's $53.2 million estimate depends on an allocation of GTE Labs' expense based solely on the relative revenues and sales of each client whereas Team's $27.5 million estimate allegedly considers beneficiary analysis criteria consistent with prior Commission decisions. The GTE Labs is currently conducting research in 14 strategic technical areas (STAs) encompassing telecommunications systems, electronics and photonics, computer and intelligent systems, and materials science. Team's $27.5 million estimate is essentially the summation of each STA's allowable allocated expense determined by multiplying each 1987 budgeted expense by its corresponding Telops beneficiary percentage. The Telops beneficiary percentages were essentially based on a study by

GTE Labs in December 1986, setting forth criteria of how project expenses would be allocated using a beneficiary study. Team reviewed this study and accepted as reasonable all the allocation percentages except those relating to Knowledge Based Systems, Switching Systems, and Lightwave Communication Techniques.

For Knowledge Based Systems, the principal technologies involve artificial intelligence techniques such as natural language, search, logical deduction, and problem-solving. GTE Labs has assessed the aggregated benefit to Telops at 79% including two knowledge-based system projects, which the study found to be of no benefit to GTE's manufacturing groups. However, based on an interview with Labs' subject matter expert, such research work has broad application to all GTE business units, including the GTE group companies involved in the manufacturing of communications and electrical products. Consequently, the GTE manufacturing companies should be included as beneficiaries of these projects, which would lower the aggregated benefit to 72%, which we adopt as reasonable.

The difference between GTE Labs' Telops allocation for Switching Systems of 84% as compared to Team's assessment of 79% relates to the allocation of benefit value for Burst Switching projects. GTE Lab assessed the value of the projects as being five times more valuable to Telops than to equipment manufacturers whereas Team assessed the relative value at 60% to Telops and 40% to equipment manufacturers. From the record it appears that Team's assessment is based solely on the personal judgement of the Team member. It appears that the evaluation of personnel actually involved in the work is more accurate. Consequently, we will adopt GTE Labs' allocation as reasonable, resulting in an increase to Telops of $100,000.

The difference between GTE Labs' allocation of Lightwave Communications Techniques of 66% to Telops by GTE Labs and 61% by Team relates to three optical technology projects which GTE Labs considered to be of little benefit to manufacturers. However, Team's investigation disclosed that some of the effort in these projects involved fiber-optic devices and components which Team believes to be of benefit to equipment manufacturers. We agree and will adopt the staff figures.

In accordance with the above discussion, we will adopt as reasonable a GTE Labs' expense of $27.6 million, increased to $28.2 million to reflect our adopted 4.2% management labor escalation factor, making a total to be allocated among the Telops of $165.4 million.

3. Prorate Factor

General used a 29.6% prorate factor to allocate costs to General as compared to Team's prorate factor of 23.0%. General's 29.6% prorate factor was based on the relative size criteria used by GTESC to allocate expenses among the domestic GTOCs whereas Team used a composite factor consisting of 50% relative size and 50% equal division between the seven regional clients served by GTESC consisting of California, Florida, Hawaii, the Midwest, the Southwest, and the Northwest. Team's investigation indicated that each of these regional clients has a voice on GTESC's planned work programs; that GTESC's departmental work efforts were common to all GTOCs and provided equal benefits to the GTOCs; and that certain work activities actually provided greater benefits to smaller GTOCs than large GTOCs because they would realize the greatest leverage gains in dealing with manufacturers. It, therefore, appeared to Team that there was no significant correlation between the relative size allocation method and GTESC-provided services to base the allocation only on relative size criteria. Therefore, Team is recommending that 50% of the costs be allocated on relative size and 50% on the number of subsidiaries receiving services, which results in a composite prorate factor of 23.0%.

According to the rebuttal testimony of Dr. A. N. Mosich, the costs of GTESC are allocated to service recipients on the basis of generally accepted accounting principles which provide that indirect costs shall be allocated on a reasonable basis among operating units for whose benefits the costs are incurred. This witness further testified that implementation of such a reasonable-basis principle generally results in the use of some measure of activity or size as a basis for the allocation of costs. According to the testimony, GTESC follows this principle by allocating regionally in accordance with each GTOC's operating expenses and taxes (exclusive of investment tax credit) to the total operating expenses and taxes (exclusive of investment tax credit) of all domestic telephone companies. Such a procedure, according to the record, allocates costs among the seven entities in such a way to ensure that every customer of the seven companies contributes proportionately to the recovery of the total cost of providing the service. General's rebuttal testimony appears reasonable and will be adopted resulting in a proration factor of 29.6% and an allocation to General of $49.0 million as set forth in the previous tabulation.

Team further recommends that General be directed to formally request from GTESC a cost allocation report which would determine the most appropriate beneficial or causal factors needed to fairly prorate the expenses of each GTESC's billing department. We are not persuaded that such a study is needed nor that it would be beneficial and will, therefore, not require its production.

4. <u>Ratemaking Adjustments</u>

Team recommends certain ratemaking adjustments it believes are consistent with Commission policy and decisions as follows:

1. A disallowance of $1.1 million from GTESC's Marketing and Business Planning (M&BP) Department to reflect an estimated 20% of the department's activities devoted to its unregulated customer-provided equipment (CPE) business. (Exh. 89, pp. 2-16 to 2-17.)

2. A disallowance of $1.6 million from the Business Services Department expenses of $2.0 million to reflect work activities

that are nonbeneficial to regulated telephone operations. (Exh. 89, p. 2-17.)

3. A disallowance of $0.3 million to corporate oversight activities that benefit GTEL. (Exh. 89, p. 2-18.)

4. A disallowance of $0.8 million to reflect 50% of cost of the Corporate Communications and Washington offices and the international expenses allocated to General in keeping with our past decisions providing such a disallowance because the office work provides an intermixing of benefits to shareholders and ratepayers and the international expenses provide no benefit to General's ratepayers. (D.82-04-028 and D.84-07-108.)

5. A disallowance of $0.4 million to reflect GTE-owned aircraft expenses in excess of a reasonable air travel expense allowance based on commercial air rates to allow GTE executives to conduct GTOC business. (D.91869.)

The above-listed disallowances and/or adjustments are consistent with our past decisions and stated policies and will be adopted after modification to reflect our adopted 29.6% proration factor and our adopted management labor escalation factor. The total adopted test year GS&L expenses (Account 674) are therefore $43.4 million as summarized in the previous tabulation.

C. GTE Communications System Corporation

GTE Communications Systems Corporation (CSC), formerly GTE Automatic Electric (AE), is comprised of the former GTE Network Systems, GTE Business Communication Systems, GTE Microcircuits, and certain operations of GTE Communication Products Corp. Wholly owned by GTE, CSC develops, manufactures, and markets a wide range of communications systems equipment and devices for the telecommunications market. Manufactured products include digital central office switching equipment and the GTE family of Private Automatic Branch Exchange (PABX) systems.

Team's presentation of the CSC-ratemaking adjustments was presented into evidence by Vannucchi; General's testimony was presented by Manion.

This Commission has found in General's last five rate proceedings that General and CSC (formerly AE) are in effect different departments of one business enterprise and that, as a result, the prices paid by General to CSC for equipment and supplies are unreasonable.

Both Team and General have developed rate base and expense adjustments for General's purchases from CSC based on the principles adopted in the most recent general rate decision. Both Team and General agree that telephone plant adjustment should equal a negative capitalized sales adjustment of $15,122,000 minus the associated depreciation reserve of $11,706,000 or $3,416,000 and a corresponding depreciation expense of $1,370,000. These amounts appear reasonable and will be adopted.

D. GTE Directories Corporation

GTE Directories Corporation (Dir Corp) performs the directory services for all the GTOCs as well as a number of independent and foreign telephone companies. In 1985, General accounted for approximately 18% of Dir Corp's revenues. Team testimony on Dir Corp was presented by Junior Utilities Engineer John Keen. The basic testimony was presented on behalf of General by Manion as modified by Senior Economist Lugi F. Pinna, and rebuttal testimony was presented by the Regional Vice President of Dir Corp, Ralph E. Adams.

Dir Corp is the exclusive agent to sell advertising and to compile and print the telephone directories for all exchanges of General. Dir Corp pays all expenses, except as otherwise agreed upon in the contract, incidental to the selling of advertising, compilation of directory material received from General, printing of directories, and shipping of directories to the telephone exchanges.

In return, General is responsible for and assumes all costs for the preparation and mailing of advertising billing and its collection, excluding billing for foreign (non-GTE customer) and National Yellow Page Services (NYPS). Dir Corp bills for all foreign and NYPS advertising and furnishes General with the amount of net billing from these sources (gross billing less any adjustments and uncollectibles) for use in computing the settlement payment to Dir Corp.

In calculating the settlement payment, General retains a percentage of the revenues collected for directory advertising as publishing rights, and after adjustments and uncollectibles, remits the balance to Dir Corp. This retention rate was increased to 58.5% from 57.0% on June 1, 1986. This Commission has repeatedly adjusted Dir Corp's earnings for ratemaking purposes to ensure that an affiliate is not used to realize a higher profit for providing services to the detriment of the ratepayers. General has estimated that, for the test year 1988, Dir Corp will earn in excess of General's authorized rate of return and, in keeping within the guidelines of past Commission decisions, has adjusted its commercial expenses by $6.965 million. Team believes the adjustment should be $9.159 million or $2.194 million greater than General's adjustment. Both General[1] and Team used the same Dir Corp gross directory revenues of $231,480,000 less publishing rights of $138,888,000, for a net revenue of $92,592,000. The differences between General's and Team's estimates result from: Team adjusted publishing expense from 4.4% to 3.5% of revenue to discount an unusual expense, lowering General's three-year average

1 General's witness Pinna testified that the gross directory revenue should be reduced $20 million from the $231.480 million used, and rebuttal witness Adams testified that it should be $177.3 million. However, neither figure was supported on the record; consequently, the original figure will be adopted for the 1988 test year.

expense/revenue ratio from 3.5% to 3.2%, for an after-tax difference of $409,000; Team disallowed expenses associated with Dir Corp's headquarters move to Dallas, Texas; Team used an income tax rate of 39% as compared to General's use of 34%; Team calculated Dir Corp's rate of return by dividing net income by the sum of average equity plus average long-term debt whereas General used the 1983 through 1985 average of gross income over total assets; Team used 1.56 as the net-to-gross multiplier compared to General's use of 1.54; and Team used a rate of return of 10.58%, while General used 11.90% in its adjustment. We will adopt Team's figures as reasonable except we will use the rate of return of 10.90% authorized by Interim D.87-23-070, resulting in an adjustment to expenses other than taxes for the operations of Dir Corp of $9,001,000.

Team witness Keen expressed concern that the expenses used by Team in its adjustment calculation are based on Dir Corp's unaudited allocations. Furthermore, according to this witness, a review of the allocations shows that the principle of economies of scale may be ignored as General is allocated administrative expenses on the same percentage basis as smaller operation companies doing business with Dir Corp. Rather than concentrate on verifying the expense allocation as an input to the adjustment calculation, Team believes the ratepayer would be better protected if the Commission ensured that General's retention rate for its publishing rights is fair and reasonable. To accomplish this assurance, Team recommends that General be required annually to complete a competitive analysis study of its directory services contract. Such a study, according to Team, should focus on alternatives to using Dir Corp's services and should include soliciting bids from other directory publishers. Such a requirement would serve to notice Dir Corp that it must compete for General's business or risk losing the directory services contract.

Testimony presented on behalf of General by rebuttal witness Ralph E. Adams indicated that:

1. The gross directory revenue figure should be $177,300,000 which is consistent with the downward adjustment to Directory Advertising revenue estimates supported by General witness Pinna on May 1, 1987.

2. Directory publication is a labor-intensive rather than a capital-intensive business in which skill in organizing and managing sales resources is the key element.

3. Directory listings in California are available to all directory publishers by means of Commission-approved tariffs.

4. There are no significant market entry barriers resulting in increased competition in all of the localities where General operates.

5. There are approximately 33 directory publishers publishing books in California.

6. Ninety-five percent of General's franchise areas in California are currently being overlayed by competing directories or have seen the entry of competing directories published by one or more of the 33 California publishers.

7. At this time, the principal competitors in General's operating territory are Pacific, Reuben H. Donnelley (subsidiary of Dunn and Bradstreet), Nynex (a regional Bell company), Southwestern Bell, Luskey Brothers, Arnold Publications, Ross Publishers, and others.

8. A number of intangibles come into play with respect to directory sales including strength of sales force, ability to work with telephone company personnel, degree of computerization of operations, knowledge of advertising methods, and quality orientation, especially in regard to printing.

9. Competitive bidding is not a common practice in the directory publication market.

10. Should Dir Corp not be able to retain General's directory publishing business as a result of a competitive bidding program, it would continue in the market and continue to use the GTE logo and "Walking Fingers" symbol.

11. There is already confusion in the marketplace regarding the identity of yellow pages publications.

12. It is quite possible that General will lose substantial revenue if a competitive bid approach to directories publishing is mandated.

We have long maintained that a market test is the best way to review the reasonableness of an affiliate relationship. We believe this is true not just for ratemaking purposes, but also as an ongoing management tool for utilities to use. General's rebuttal testimony reemphasizes the competitiveness of the directory market in California, lending further strength to the conclusion that a competitive market analysis is not only feasible but highly desirable.

Properly managed, an analysis of competitive alternatives ought to reduce cost. We are puzzled by General's assertions that ratepayers would face risks from such a procedure. While we recognize that the good working relationship that General has with Dir Corp is probably of some value in itself, such relationships can also be developed with unaffiliated publishers.

We will require that General perform a full competitive analysis of its options for directory publishing and submit it to CACD no later than March 31, 1989. We will not require that General seek open competitive bids for directory services at this time, although we may do so later depending on the results of this analysis. The competitive analysis should at a minimum compare the terms of General's contract with Dir Corp with the terms of similar directory contracts or arrangements maintained by other major telephone operating companies. As part of this analysis General should also identify specific operational, financial, or other criteria that would in General's mind determine whether a given directory publisher could be qualified to publish and market General's directories. To the extent that this analysis may contain proprietary information that merits confidentiality, General may seek to protect that information under our usual procedures.

General shall serve a copy of the competitive analysis on the parties to this proceeding.

E. GTE Telecom Marketing Corporation

GTE Telecom Marketing Corporation (TMC) executed a marketing agreement with AT&T Communications (AT&T) covering the period from May through December 1985. According to the record, under this agreement, TMC provided marketing service to help AT&T maintain its market share after divestiture. The marketing service was to distribute AT&T's measured toll, WATS (wide area telephone service), 800 service, private line, and foreign exchange services to business customers in the territories served by GTE's Telephone Operating Companies. TMC received $18 million under this marketing agreement. During the term of the agreement, TMC was a wholly owned subsidiary of GTE Telecom Incorporated. GTE Telecom Incorporated is a subsidiary of GTE Corporation.

DRA testimony on this transaction was presented by Financial Examiner III Francis Fok. According to his testimony, the national sales organization of TMC was deployed on a regional basis. One national director headed up the organization. Working for him were three regional sales directors, fifty-six sales executives, and three secretarial personnel. Out of the 56 sales executives, 20 were deployed in California. All of these 20 were senior employees transferred from General. Subsequent to the expiration of the agreement, all 20 of these employees were transferred back to General.

This witness further testified that California's share of the contract fee, including interest at 9% per annum, was $6,000,000, which, he believes, should be passed on to the ratepayers at a rate of $2,000,000 a year because General was the key player in running the marketing agreement and was the true provider of the marketing service, and ratepayers are entitled to compensation received through the use of utility assets.

Rebuttal testimony was presented on behalf of General by its Director of Consumer Marketing, George A. Clapsaddle. According to his testimony:

1. All General was asked to do was to provide a list of candidates and, if persons from that list were selected, to allow those selected to transfer to TMC for the duration of the contract with AT&T.

2. Levels 2 and 3 management personnel, which are only slightly above entry level management positions, were eligible for consideration.

3. General submitted a list of 20 names to TMC consisting of candidates that were selected from a variety of different departments and work groups including field sales, telemarketing, government communications, product management, network engineering, business terminal sales and service, and phone marts.

4. At the conclusion of the contract, 19 of the 20 employees working for TMC returned to General at a comparable level.

5. No personnel were added to General's payroll specifically to replace those employees who went to work for TMC.

6. General benefited from the training that AT&T provided to the employees who returned after the contract was completed because this training provided these employees a broader base of experience, including dealing with multiple companies' business practices, pricing, market segments, and tariffs for interLATA services.

We are not persuaded that General's ratepayers incurred any risk from the above-described transaction nor that they suffered any disadvantage from the temporary transfer of personnel. Furthermore, the contract terminated in December 1985, two full years prior to the commencement of the 1988 test year under consideration in this proceeding. Consequently we will not adopt DRA's recommended $2,000,000 a year revenue requirement reduction for this marketing agreement.

F. GTE Data Services

GTE Data Services (GTEDS) is a supplier of data processing and information services to GTE telephone operations and is responsible for establishing and/or operating a network of data centers to service telephone operating requirements. GTEDS also supports a Business Information System and provides Systems and Programming Services, Time Sharing Services, Computer Output

Microfiche Services, and operational support for minicomputers, leased terminals, and other data processing equipment as required.

The affiliate Team presented a "Report on the Affiliated Relationship of General Telephone Company of California With GTE Data Services". The sections on "Introduction" and "Return on Investment" were prepared by Financial Examiner III Seaneen McCarthy; the section on competitive bid analysis was prepared by Junior Utilities Engineer Michael Vannucchi; the section on rents and contracts was prepared by Associate Utilities Engineer Jerry Shiu; the section on allocation was prepared by Senior Utilities Engineer Ramesh Joshi; and the section on data processing charges was prepared by Regulatory Analyst II Mary Cooper. Testimony was presented at the hearing by witnesses McCarthy, Shiu, and Vannucchi. Mary Cooper's testimony was presented by witness McCarthy and DRA and General stipulated that witness Joshi's figures would change to reflect whatever this Commission adopts as operating expenses, obviating the necessity of his appearance as a witness.

Team's investigation of the relationship between General and GTEDS revealed that General has never performed a competitive analysis to determine the most cost-effective data processing vendor, nor did General ever consider doing its own data processing in-house. In response to questions on this alleged deficiency, General indicated that GTEDS with its technical skills and data processing knowledge, have proven to be the best available data processing provider. Team questions this statement because General has never attempted an analysis or comparison study. General did provide a comparison study performed by Price Waterhouse for GTEDS. Team questions the objectivity of the report because it was supplied to General by the vendor. Team also questions the applicability of the report to General because it does not necessarily address the specific needs and services required by General, but rather includes benchmark parameters that were calculated from six of GTEDS data processing centers. Under these circumstances, Team recommends that General should conduct a competitive analysis prior to its next rate case filing and include the study in its work papers to support continued affiliate transactions between General and GTEDS. We believe Team's recommendation has merit and the order that follows will provide for its implementation.

As part of its investigation, Team analyzed the reported return on investment (ROI) earned by GTEDS from General to determine the reliability of the data used in the calculation of the traditional Commission adjustment limiting GTEDS' earnings to a level not in excess of General's authorized return.

Team recommended no adjustment to GTEDS' ROI because the figure provided by GTEDS of 3.85% for test year 1988 is below Team's estimate of General's ROI. Team, however, questions the reliability of the data supplied because GTEDS' 3.85% ROI for General is substantially less than for other GTE subsidiaries. Such discrepancies, according to Team, support the necessity of the previously discussed competitive analysis study to be ordered by this decision.

With respect to rents and contracts, General's 1988 test year estimates of the cost of the Customer Billing Information System (CBIS) of $2,675,800 and California Billing System (CBS) of $10,253,900 (Account 996-Computer Usage) total $12,929,700 or $4,566,000 more than Team's estimate of $8,363,700. The difference is due to the inclusion by General of implemental costs of the Customer Records and Billing System (CRB) and Facilities Management System (FMS) not included by Team. The record fully supports the desirability of installing both CRB and FMS. Under these circumstances, according to the record, Team agrees that some implemental costs should be included for the test year and recommends the expense be amortized over a three-year period by excluding two-thirds of the $4,566,000 differential, or $3,044,000. Such a recommendation is proper to reflect the ratepayers test-year costs for the equipment. Consequently, we will adopt an Account 996 amount of $12,929,700 minus $3,044,000 or $9,885,700.

For General, Account 607-Operator Services, Team found General's revised estimate of $2,055,000 to be reasonable. Consequently we will adopt this figure for ratemaking purposes and reduce traffic expenses for FCC Accounts 626 and 629-635 by $1,999,000.

The Business Information Service (BIS) expenses (Account 995/31) Program Office expenses (Account 995/31), and Administrative and General Expenses (A&G) (Account 996/31) are allocated on the basis of each General Telephone Operating Company's (GTOC) operating expenses. Our adopted amount of these three allocated expenses is $2,894,000 lower than General's estimate of $36,179,000 resulting in a disallowance of this amount. The total of adjustments described above is $7,937,000 allocated $297,000 to maintenance, $1,999,000 to Traffic, $1,841,000 to Commercial, and $3,800,000 to other operating expenses.

G. GTEL

In D.84-07-108 dated July 18, 1984, this Commission ordered General to form a separate stand-alone corporate subsidiary to market, install, and maintain all unregulated customer premises equipment (CPE). In compliance with this order, General formed GTEL, headquartered in Thousand Oaks, California, which became fully operational on July 1, 1985. It currently consists of three divisions: Consumer Products and Service, Business Systems, and EFT Services. GTEL markets residential telecommunications products and services, business systems, maintenance contracts, radio-paying equipment and services, and also continues to sell General's customer-calling network services at its phone marts and through its Direct Marketing Center.

The Telecommunications Audit Branch of the Commission staff submitted into evidence Exhibit 165 entitled "Audit Report on General Telephone Company of California's Affiliate Relationship With Its Wholly Owned Subsidiary, GTEL." Chapter 1 - Purpose, Scope, and Summary of Recommendations; Chapter 2 - GTEL Corporate Structure; Chapter 3 - Unbilled Directory Services; and Chapter 4 - Unbilled Referrals were sponsored by Financial Examiner II Sophie Chia. Chapter 5 - Unbilled Corporate Oversight, Chapter 6 - Transfer Costing, Chapter 7 - Affiliate Payment, and Chapter 8 - Future Review were sponsored by Financial Examiner III Monica McCrary. Rebuttal testimony on behalf of General was presented by GTEL's Operations and Administration Director, Richard A. Murphy.

1. <u>Unbilled Directory Services</u>

According to the testimony of staff witness Chia, General has provided extensive advertising for GTEL in 77 GTE Directories in General's service areas at no cost to GTEL. In support of this position, the witness listed five examples of GTEL advertisements found in the directories as follows:

1. On page 5A, titled "Where to Reach Us," GTEL'S Direct Marketing Center's toll free number is listed under Retail Product Sales. The listing does not indicate that the 800 number is a GTEL number; thus, misleading the customers to believe they are calling the telephone company.

2. On page 6A, a two-inch advertisement appears for the GTE Phone Mart stating the address and the store hours. The advertisement caption reads "The GTE Phone Mart allows residence customers to establish new service (rent or buy selected phones), return phones or have rented GTE phones repaired."

3. The entire outside back cover advertises the GTE Phone Mart located within the specific service area of the directory. The advertisement has a map of the White and/or Yellow Pages contained in that particular directory with colored dots

signifying the location of the phone marts in that area. Next to the map are the GTE Phone Mart addresses and logo, which is printed in four different colors. The caption reads, "Where you can pick a phone and take it home."

4. Throughout the Yellow Pages are fillers urging customers to call the telephone company to get a new or an additional phone in a different style or color.

5. Full page display ads in the front introductory pages and at the back of the Yellow Pages of the directories.

According to this witness, GTEL is the main beneficiary of the above ads and should be billed its listing fees. Consequently Team recommends an adjustment of $3,708,000 for the expected revenues resulting from the GTEL listings and ads for the period 1985 through 1988 to be amortized over three years, plus interest, for an annual adjustment of $1,507,000. In addition to the above annual adjustment, Team recommends that General be required to delete GTEL's Direct Marketing Center's 800 number listed on page 5A and to change the Yellow Page fillers and the full page CPE ads in the front introductory pages and at the back of the Yellow Pages to customer service notices on regulated services.

According to the rebuttal testimony of General's witness Murphy:

1. Section 728.2[2] of the PU Code raises a very significant issue as to whether this Commission has jurisdiction over the advertisements placed in the telephone directories.

2. GTEL did not order or request any of the above types of yellow page advertising.

3. The references to the GTE Phone Marts found in the GTE Telephone Directories are in keeping with the transition latitude granted by D.84-07-108.

4. The 800 number for GTEL's Direct Marketing Center and the two-inch advertisements showing GTE Phone Mart addresses will be deleted from all future directories.

5. The yellow page fillers will be changed to ads for generic services, and

6. Hypothetical advertising revenues should not be imputed to General's regulated operations because of the reference to the Direct Marketing Center or GTE Phone Marts made in the informational section of the white pages.

General's position that PU Code Section 728.2 provides that this Commission shall have no jurisdiction or control over classified telephone directories or commercial advertising included as part of General's alphabetical telephone directories is

2 Section 728.2 states in part:
"728.2. Telephone directory advertising
"(a) Except as provided in subdivision (b), the commission shall have no jurisdiction or control over classified telephone directories or commercial advertising included as part of the corporation's alphabetical telephone directories, including the charges for and the form and content of such advertising, except that the commission shall investigate and consider revenues and expenses with regard to the acceptance and publication of such advertising for purposes of establishing rates for other services offered by telephone corporations."

obviously valid. It is equally obvious that we have jurisdiction to investigate and consider directory advertising revenues and expenses for the purpose of implementing ratemaking adjustments during rate proceedings. Team's recommendation relating to the deletion of GTEL's Direct Marketing Center's 800 number and the change in Yellow Page fillers and full page CPE ads is rendered moot in view of General's expressed intention to effect such changes in all forthcoming directories. Because of subscriber confusion during the transition period from July 1, 1985 until CPE was deregulated at the end of 1987, we do not feel that it would be proper or reasonable to impute advertising revenues in the informational section of the white pages or on the back covers of the directories. However, the yellow-page sections of the telephone directories are a different matter. It is axiomatic that the yellow pages are a form of advertising which should be paid for by the beneficiary of such advertisements. Consequently, it is only reasonable that GTEL be assessed the costs of such advertisements. We will, therefore, adopt staff's recommendation that advertising revenues be imputed for the Yellow Page fillers and provide an annual adjustment plus interest factor of $687,000.

One GTE-sponsored sales program was the "Sell One More Program" that commenced on January 1, 1986 and ended in California on December 31, 1986. Team recommends that General's revenue requirement be reduced $317,000 or $129,000 a year for three years, for expected reimbursement for GTEL's share of the expenses derived from this referral program's generated revenues of $531,533 for GTEL. Because any reimbursement for GTEL's share of expenses is speculative rather than actual and because this particular sales program will not be continued into the test year we will not make the adjustment Team recommends.

2. <u>Unbilled Referrals</u>

In her direct testimony on unbilled referrals, Team witness Chia indicated that:

1. Since the complete separation of GTEL in July 1985, the following General groups have provided referrals for CPE to GTEL: Customer Service Order Center (CSOC), Business Service Order Center (BSOC), Tele-Account Management (TAM), Sales Programs Management, and GTC Government Communications.

2. General has not charged GTEL for the costs of providing these referrals which are a valuable source of revenue for GTEL.

3. Team believes that General should be compensated for the cost of providing the referrals and for the market value of such referrals.

4. A General customer representative estimated that 8 to 10% of calls received at a CSOC involve terminal equipment inquiries that are referred to GTEL.

5. A General business representative estimated that 9% of current incoming calls involve CPE inquiries that are referred to GTEL.

6. A BSOC study conducted by General in several BSOCs in October 1986 indicated that the average percentage at total support unit hours dedicated to terminal activities in the surveyed BSOCs was 10.7%.

7. Both customer and business representatives have been following On-The-Job Instructional Bulletin for the Customer Options Program issued November 1, 1984 which instructs these representatives to refer customers to the Phone Marts or GTEL'S Direct Marketing Center for equipment.

8. In April 1987, a draft instructional bulletin entitled "Detariffing Embedded Customer Premises Equipment (CPE)" was distributed to district, phone mart, service, and regional managers, and CSOCs and BSOCs have already trained their staffs on it.

9. The draft instructional bulletin shows that referrals to GTEL will still continue.

10. TAM personnel have and continue actively making referrals to GTEL and provide customers with GTEL price quotes.

11. TAM's eight northern area management employees have made 560 referrals to GTEL during the period May 1986 to March 1987 and its southern area staff has made 1,054 referrals during the period May 1986 to May 15, 1987.

12. The Federal Communications Commission (FCC) in its BOC Capitalization Plan Order defined direct costs to include costs attributable to both successful and unsuccessful referrals.

13. Pacific was reimbursed for the cost of referrals through the transfer-pricing mechanism as required by the BOC Separation Order based on validation studies conducted at Pacific to determine the average time it took a service representative to complete a referral.

14. In the Pacific rate hearings, DRA recommended that affiliates receiving referrals from Pacific should be required to pay 13% of the sales revenues resulting from any Pacific referrals in order to approximate the market value of these referrals.

15. Since neither General nor GTEL maintained sufficient referral records, Team partly depended on information gathered from the Pacific investigation in making its recommendations for adjustments to reflect unbilled referrals.

16. Team recommends a fee of $1,906,000 be paid General for the cost of making the referral to GTEL for the period 1985 through 1987, or $775,000 a year plus $762,000 to recognize the cost of providing projected referrals to GTEL.

17. Team recommends a $2,361,000 adjustment to recognize the expected revenues for the market value of providing projected 1988 referrals to GTEL.

18. Team recommends that this Commission require General to establish referral guidelines to track all referrals and to perform a study to determine the cost plus 10% markup for each referral to GTEL and bill GTEL such costs.

Rebuttal testimony presented on behalf of General by Richard Murphy indicated that:

1. The DRA witness has incorrectly combined many types of referrals into customer premise activity referrals and has completely omitted any reference to referrals which occur daily from GTEL to General.

2. A large quantity of the referrals relate to the ongoing transfer of General's embedded base CPE to GTEL.

3. Because of severe customer confusion resulting from other entities utilizing a flash cut transfer of CPE from the regulated utility to the unregulated, separate subsidiaries, the management of General and GTEL decided against the flash cut approach and concluded that, in the best interest of the customer, as much information as necessary to resolve the customer's questions or problems should be provided at the first point of contact, be it General or GTEL.

4. Recent studies conducted during the period July 20, 1987 to August 14, 1987 indicated approximately one percent (2,572) of 216,875 calls handled at eight of General's CSOCs were related to new terminal equipment and were referred to GTEL.

5. During the period July 20, 1987 to August 14, 1987 less than one percent (311)

of 40,528 calls handled at six of General's BSOCs were related to new terminal equipment and were referred to GTEL.

6. At the time the BSOC study conducted by General in October 1986 was made, General was still responsible for the management of over 542,000 business accounts. The transfer of the embedded base would not begin until May 1987.

7. GTEL's Direct Marketing Centers (DMC) received 102,986 calls from January 1987 through June 1987 of which 47,551 calls or 46% were intended for General or others.

8. General's new On-The-Job Instructional Bulletin (OJIB) attempts to establish a framework for addressing all potential customer contact issues and is intended to assure that the customer is treated in a most business-like manner and in the most expedient way possible.

9. The OJIB shows repeated examples of situations in which General and GTEL work together to ease the customer contact whether the initial contact be with General or GTEL. Although General does provide GTEL's telephone number, it only does so after indicating that other CPE vendors are available.

DRA recommends adjustment be made to 1988 test year expenses to reflect expenses DRA believes should be assessed for the period 1985 to 1987. Because the expenses were incurred during a transition period of high customer uncertainty due to the deregulation of CPE, we will not make the adjustment DRA recommends. DRA's 1988 test year adjustments for expenses to be incurred in that year are an entirely different matter. DRA's recommended test year adjustment of $762,000 to recognize the cost of providing projected referrals to GTEL and $2,361,000 adjustment to recognize the expected revenue for the market value of providing projected 1988 referrals to GTEL for a total of $3,123,000, are fully supported by the record and will be adopted. The order that follows will also provide that General: establish referral guidelines to track successful and unsuccessful referrals to GTEL; perform a study, to be completed within six months from the effective date of the decision, to determine both the market price and the cost plus 10% markup for each referral made to GTEL; and bill GTEL the market price or the cost plus 10% markup whichever is higher for all referrals and the market value of successful referrals. We note that the Commission has previously approved the 10% markup plan for Pacific Bell in D.86-01-026.

3. Corporate Oversight

DRA witness McCrary testified that corporate oversight costs incurred by General on behalf of GTEL are not presently billed GTEL and that GTEL is a separate, unregulated subsidiary of General and should be charged for its share of costs. She further testified that in Pacific D.86-01-026 and Continental Telephone Company of California D.85-03-057, the Commission adopted a three-factor method allocating costs based on a corporate revenue, expenses, and employees, and recommends a similar procedure for General in this proceeding. Team applied the three-factor allocator to DRA's estimates of General's General Office Salaries and Expenses (excluding engineering expenses - Account 730) and to Marketing Administration Expenses, and subtracted from the resulting figure the small portion of corporate oversight that is billed resulting in a recommended adjustment of $4,900,000 for test year 1988.

In rebuttal testimony, witness Murphy testified that:

1. The three-factor method is not any more accurate than General's current corporate oversight allocation method based on employee levels.

2. Because General has more expertise in the selection of allocation methods than DRA, the present method should be continued.

3. The factor should only be applied to Account 661-Executive Salaries and Expenses. All other charges between General and GTEL should be based on General's recovery of fully allocated costs plus a return on investment.

4. It is General's policy to bill GTEL for all corporate oversight and all other services provided to GTEL by General at a fully allocated rate plus return on investment.

5. In 1986, General billed GTEL $149,183 for corporate oversight and $516,528 for various on-demand services.

6. In 1986, GTEL paid General $1,296,431 for services provided by GTE Service Corp.

DRA's recommendation that we adopt the three-factor (revenues, expenses, and employees) method of allocating unbilled corporate oversight expenses consistent with our adopted results in Pacific's and Continental's decisions is reasonable and justifiable and will be adopted. The determination of the appropriate expense amounts to which to apply such an allocation factor is more difficult. As noted by DRA witness McCrary, corporate oversight as used in D.84-07-108 describes oversight by top directors, officers, and directors of General and does not include general service functions. It is axiomatic that Account 661-Executive Department expenses, which includes salaries and expenses of corporate officers and directors, is an appropriate expense for inclusion in the total amount to which the allocation factor is to be applied.

Account 662-Accounting is comprised of pay, office, traveling, and other expenses of officers, their assistants, and office forces of the accounting department, and includes general accounting, revenue accounting, data processing, budget, and internal auditing. According to the testimony of General's witness Murphy, GTEL established a full function accounting department which provides for GTEL paying for the accounting costs incurred by

General on behalf of GTEL and to include the total cost of General's accounting department in the amount to be allocated would result in double billing through corporate oversight and on-demand services. The record is clear, however, that there are some accounting functions, such as budget consolidation, financial planning, internal audits, or accounting analyses that are performed by General on behalf of GTEL and are not included in bills for on-demand services. To reflect these costs, we will include 10% of the account total adopted for this account of $109,952,000 or $10,995,000 in the amount to be allocated.

We are persuaded that activities performed by General on behalf of GTEL which are recorded for in Account 663-Treasury and 664-Legal are generally included in billings for on-demand services and will not be included in the amount to be allocated.

Account 665-Other General Office Salaries and Expenses includes employees' salaries and expenses in human resources, public affairs, revenue requirements, miscellaneous engineering, and security of the company. DRA's position that this account amount, exclusive of miscellaneous engineering expenses, should be included in the amount to be allocated is well-taken and will be adopted. Equally acceptable to us is DRA's position that Account 643-General Marketing and Sales Administration expense is properly includable in the amount to be allocated. In accordance with the above discussion, the corporate oversight allocation adjustment, which we adopt as reasonable, is $2,271,000 computed using our adopted allocable General Office Salaries and Expenses and General Marketing and Sales Administration expenses as set forth below:

General Office Salaries and Expenses (GOSE):		
Executive		$ 1,311,000
Accounting		10,995,000
Other GOSE		72,076,000
Total		84,382,000
General Marketing and Sales Administration (GMSA)		26,045,000
Total GOSE and GMSA		110,427,000
Less: Portion of Acc. 665, Engineering Exp.		(36,681,000)
Total Allocable Expenses		73,746,000
Multiplied by 3-Factor Allocator	3.290%	
Total Allocated Corporate Oversight		2,426,240
Less: Corporate Oversight Actually Billed (excluding GTESC) Estimate: Actual 1986 Billed Amount	$ 149,183	
Multiplied by 1987 Labor Inflation Factor - 1.788%	151,850	
Multiplied by 1988 Labor Inflation Factor - 2.542%		(155,710)
Corporate Oversight Allocation Adj.		2,270,530

(Red Figure)

4. <u>Transfer Costing</u>

Team noted that General currently provides the following services to GTEL on a demand basis: legal, accounting, graphics, customer representative, security, land and building engineer, and testing. During phase two of Pacific's A.85-01-034, DRA recommended that services from Pacific to its affiliates be priced at the higher of fully loaded cost plus 10% markup or market price. DRA further recommended that Pacific conduct a market pricing study to determine market rates for the services it provides to its affiliates. Pacific concurred and is currently conducting such a study. In this matter, DRA recommends that if General plans to and/or is allowed to provide "on demand" services to GTEL, it be ordered to conduct and submit within six months of the decision a market-based pricing study to determine market rates for services it provides to its affiliates. DRA further recommends that until the study is complete, services provided by General to GTEL be priced at fully loaded cost including return on investment and a 10% markup.

General's rebuttal witness Murphy testified that the transfer pricing methodology by which General bills GTEL is based on fully allocated cost plus a return on investment and a 10% markup is therefore not appropriate. He further testified that DRA's recommended study for market rates for services would be of little value because it would continually have to be updated to reflect market conditions resulting in increased costs to General, would be a source of constant dispute between General and DRA, and would be expensive to monitor. We note that we have adopted the 10% markup previously for Pacific in D.86-01-026 and we perceive no need to depart from this plan for General. We agree with and adopt as reasonable DRA's recommendation that General conduct a market-based pricing study to determine market rates for services it provides to GTEL. The order that follows will provide for such a study to be completed within six months from the effective date of the decision and that until such a study issues, General continue to bill GTEL at its fully allocated costs including return on investment, plus a 10% markup.

5. Affiliate Payment

As was recommended by DRA in Phase 2 of the Pacific Bell rate case, Team is recommending that GTEL pay General 5% of its gross revenue to reimburse General for the value of intangible, unquantifiable benefits GTEL receives from its affiliation with General.

According to Team, the benefits GTEL receives as a result of its affiliation with General include:

1. Increased revenue stream.

2. Use of General's name, reputation, and heritage.

3. General's guarantee of GTEL'S operations.

4. Access to technical and personnel resources of General.

According to witness McCrary, GTEL is currently providing, through its Phone Mart Stores and its Direct Marketing Center, General's Custom Calling Services, increasing GTEL's business and giving the impression that General and GTEL are one and the same. Further, according to this witness, when a customer enters a General customer service center, the customer can look through a catalog of GTEL products and use the ring down line to order CPE from GTEL. This service provides GTEL with a distinct advantage over other CPE vendors and further enhances GTEL'S image as the "telephone company". Also, General's name, reputation, and heritage have value to GTEL in that GTEL's customers are familiar with and prefer to do business with the "phone company".

A prime example of GTEL'S use of its association with General can be seen in a recent brochure distributed by GTEL. The brochure, developed to define and project an image which personifies GTEL'S capabilities and differentiation within GTEL's marketplaces, uses General's affiliation to promote the GTEL name and service quality. The brochure exemplifies their experience by stating that General has been serving California for more than 55 years. The brochure states "we're the one-source solution offering both product and service...we're two separate companies, yet we share the same heritage and experience" and "we evolved specifically to combine the clout of a large company with the responsiveness of a small one."

Another benefit of GTEL's association with General is guarantee by General of GTEL's performance and obligations. Such guarantees allow GTEL to enter agreements and obligations that it may not have otherwise been able to enter and expand business operations at a pace faster than other small companies. In addition, GTEL benefits from General's telecommunications expertise, the availability of General's personnel on a loan and/or transfer basis, and its ability to draw cash from General at an attractive rate.

In his rebuttal testimony, witness Murphy testified that:

1. GTEL is closely identified with the "phone company" whether or not it chooses to promote their relationship.

2. The Phone Mart is a valuable resource for General in maintaining the revenue growth from the sale of custom calling features.

3. The additional revenue generated from the sale of custom calling services and increased traffic in the GTE Phone Marts do not support the proposed affiliate payments.

4. The one-time transaction fee paid by General to GTEL for each successful sale of custom calling service is $4.82 as compared to the average revenue generated for General per custom calling feature of $105.56 during the average life of that service.

GTEL came into being as a result of our directives. The purpose of ordering the formation of a separate and independent subsidiary was to ensure that General's unregulated CPE marketing endeavor is not subsidized by ratepayers. We addressed DRA's affiliate payment proposal in Pacific Bell's A.85-01-034. In D.87-12-067, we stated:

> "[w]e simply are not persuaded that DRA's recommendation for a 5 percent across-the-board royalty should be adopted. We do not agree that a substantial flow of intangible benefits exists which jeopardizes ratepayer interests; instead, we prefer to rely upon tangible measures to value and compensate for tangible flows of resources or other benefits from utility to affiliate which have an identifiable effect on ratepayers." (Mimeo. p. 276.)

and

> "119. The evidence did not support the allegation that there is a flow of intangibles between the regulated utility and the holding company affiliates adversely affecting ratepayers that cannot be adequately remedied via pricing mechanisms and other adopted Commission requirements." (Mimeo. p. 315.)

Similarly, in this matter, we find an affiliate payment inappropriate and will not adopt DRA's recommendation with respect to payment of the value of intangible, unquantifiable benefits GTEL receives from its affiliation with General.

6. Summary of Adjustments

The following tabulation summarizes DRA's recommended GTEL adjustments, together with our adopted results:

Item	DRA Recommended Adjustment	Adopted
Directory Advertising Adjustment[a/]	$ 1,507,000	$ 687,000
Sell One More Adjustment[a/]	129,000	0
1985 to 1987 Referral Adjustment[a/]	2,670,000	0
1988 Referral Adjustment	3,123,000	3,123,000
Corporate Oversight Adjustment	4,900,000	2,271,000 ✓
Affiliate Payment Adjustment	5,966,000	0
Total Reduction to 1988 Revenue Requirements	$18,295,000	$6,081,000 ✓

a/ Amounts equal one-year amortization plus an interest factor. Total adjustment amortized over a three-year period.

V. Results of Operations

A. General

Complete results of operations and exhibits were presented by General and DRA. Substantial differences exist in practically all categories of revenue, expense, and rate base items.

The results of operations data for General as a whole was presented by its budget director, L. G. Manion, and for the California intrastate operations by its business relations manager-intercompany revenues, Lida C. Tong. The DRA presentations were made by various subsequently identified staff members. Rebuttal testimony was presented on behalf of General as subsequently discussed.

The basic principles and procedures for separating the costs of telephone operations related to interstate and intrastate services are prescribed by Part 67 of the Federal Communications Commission (FCC) Rules and Regulations. These procedures are contained in the February 1971 NARUC (National Association of Regulatory Utility Commission)--FCC Separations Manual. The Separations Manual was amended in 1982 to provide an interim measure of controlling growth in the interstate Subscriber Plant Factor (SPF) and for removing Customer Premise Equipment (CPE) from the separations process. In April 1984, the FCC adopted an amended Separations Manual that included the use of a "frozen" SPF through 1985 and then beginning on January 1, 1986, an 8-year transition from the frozen SPF to a 25% interstate allocator. The manual was further amended in 1986 to include the permanent separations treatment of Account 645-Commercial Expenses and the direct assignment of interstate closed end Wide Area Telephone System (WATS) line costs.

In 1985, this Commission ordered that the frozen intrastate interLATA SPF factor be moved over a 6-year period to a

Subscriber Line Usage (SLU) factor and that effective January 1, 1987 all telephone utilities directly assign the intrastate interLATA closed end WATS line costs. Finally, by D.87-12-067, dated December 22, 1987, this Commission adopted the gradual transition from intraLATA SPF to SLU, and for a flash cut intraLATA direct assignment of WATS line costs so that they will coincide with the interLATA SPF to SLU transition.

B. Inflation Factors

1. General

Testimony on labor inflation factors was presented by Public Utilities Regulatory Analyst II Mark R. Loy and on nonlabor escalation rates by Research Program Specialist Thomas M. Renaghan. These factors were used by various DRA members in the preparation of their expense and rate base estimates and account for a major portion of the differentials between General's and DRA's estimates.

Rebuttal testimony to Loy's presentation was presented by General's employee relations director, Charles A. Green, and by compensation and organization planning manager, James Wainscott. Rebuttal testimony to Renaghan's testimony was presented by General's senior economist, Luigi F. Pinna.

2. Labor Inflation Factors

The labor inflation factors used by DRA reflect March 5, 1983 and March 5, 1986 wage agreements between the Communications Workers of America (CWA) and General, and include all bonus, merit, and incentive compensation awarded on a companywide basis. DRA recommends the union contract rates also be applied to management compensation levels. General is recommending increases of almost twice the union employees' agreement for management employees under its Executive Incentive Plan and Unit Incentive Plan. A quantitative comparison of these two proposals is as follows:

	Management				Nonmanagement			
	Annualized		Compounded		Annualized		Compounded	
	Staff	General	Staff	General	Staff	General	Staff	General
1985	NA	NA	1.000	1.000	NA	NA	1.000	1.000
1986	5.42%	4.5%	1.054	1.045	5.42%	8.0%	1.054	1.080
1987	1.15%	5.0%	1.066	1.097	1.15%	1.0%	1.066	1.091
1988	2.01%	5.0%	1.088	1.152	2.01%	2.0%	1.088	1.113

Weighting the above factors in accordance with the number of management and nonmanagement employees results in the following labor inflation factors for the utility as a whole:

	DRA	General	Ratios
1985	1.0000	1.0000	1.000
1986	1.0542	1.0718	0.984
1987	1.0663	1.0925	0.976
1988	1.0877	1.1226	0.969

According to the record, the DRA auditors have established the integrity and accuracy of General's 1985 standard labor rates for determining the 1985 payroll. However, according to DRA testimony, the projected 1986 and 1987 standard labor rates were not developed directly from the annual percent changes, resulting in the 1987 over 1985 inflation being overstated by 2.3%.

General's rebuttal witness Green testified that DRA's inflation factor was understated in two respects as follows:

1. DRA's labor inflation factor was based on wage levels at the top of the wage progression steps and ignored the wage progression increases of the 11% of employees who had not reached the top of the range. Factoring these progression increases into the total results in a weighted wage escalation factor of 1.1273 rather than the 1.0877 factor computed at the top of the wage progression levels.

2. Increased contributions by General for changes and increased participation in its savings and investment plans. Under these plans, General will match one-half of an employee's contributions up to a maximum company contribution of 3% of the

> employee's total annual cash compensation. According to the record, the projected increase in General's matching contribution is approximately $1.1 million or the equivalent of a 1.27% increase in compensation if the $1.1 million were distributed across the board to all hourly employees. Combining the above two factors results in a compounded labor inflation factor of 1.13 rather than the 1.0877 amount projected by DRA.

While the testimony presented by General does not appear unreasonable or illogical, it is noted that its own labor inflation factor for hourly workers is 1.113 or almost 0.02 less than the above-derived factor of 1.13. Under these circumstances, we will adopt 1.113 as reasonable for the labor inflation factor for hourly or nonmanagement employees.

According to the record, General's recommendation for management personnel increases is based on projections from five nationwide surveys. However, DRA cannot find any quantifiable link or cause-effect relationship between any of the survey's projections and General's actual proposed management pay increases and notes that, for 1986, the same surveys called for a 6% management increase as contrasted to the 4.25% General actually granted. Furthermore, DRA analyzed the recorded data from 1978 to 1985, reviewed General's Executive Incentive Plan, perused the surveys that the Hay Management Consultants conducted for the GTE Telops, and concluded that there is no quantifiable basis for making separate recommendations for nonmanagement and management employees. Witness Loy further testified that compensatory differentials between management and nonmanagement should not be authorized until a clear basis for such pay discrimination can be explained reasonably and can be verified quantitatively.

Rebuttal witnesses Green and Wainscott both addressed the compensation increases that should be permitted management personnel. These witnesses differentiated management compensation from hourly wage rates on the basis that hourly wage rates are arrived at through the process of collective bargaining with salary levels as only one of the components of the agreed upon package, whereas management compensation is determined through a survey process comparing similar jobs within General's labor markets. According to the testimony of witness Wainscott, General's management salaries have increased by 4.25% during the period July 1, 1986 to June 30, 1987, and are expected to increase by another 4.20 to 4.30% by mid-year 1988. This witness further testified that performance generated merit increases for management employees are basically determined by supply-and-demand factors within the marketplace and will rise or fall depending upon how much or how little companies must pay to attract and retain managerial talent.

We are persuaded of the validity of General's position that management and nonmanagement compensation levels be determined independently. However, the testimony presented by General does not support the 5% factor used in General's estimates. We will therefore adopt an inflation factor of 4.2% for 1987 and 4.2% for 1988. Weighting these factors in accordance with the number of management and nonmanagement employees yields the following adopted results:

	Annualized			
Year	Nonmanagement	Management	Weighted	Compounded
1985	NA	NA	NA	1.000
1986	8.0%	4.5%	7.138	1.071
1987	1.0%	4.2%	1.788	1.090
1988	2.0%	4.2%	2.542	1.118

3. Nonlabor Escalation Factors

The following tabulation compares the nonlabor escalation factors used by DRA and General:

	Percent Change		Compound	
Year	DRA	General	DRA	General
1986	2.4702%	5.50%	1.02470	1.0550
1987	2.5338	7.40	1.05067	1.1331
1988	3.7470	8.30	1.09003	1.2271

From the record, it appears that both DRA and General developed a nonlabor escalation specific to General based upon weighting specific price indices with General's actual 1985 nonlabor expenses. The nonlabor expense was divided into functional groups in accordance with the FCC System of Accounts. Each functional group was subdivided into detailed cost components. A price index was assigned to each detailed cost component within each functional group. The detailed cost components are weighted in accordance with the ratio of the cost component to the functional group cost and the functional groups are weighted as a percent of each functional group total to the total 1985 nonlabor dollars. The detailed cost element weights and the functional group weights are coupled with forecasts of the price indexes to arrive at the final nonlabor escalation rates. According to the testimony of DRA witness Renaghan, his numbers and those derived by General differ because he used a more recent forecast for the price indexes from Data Resources Institute (DRI) and the University of California at Los Angeles. We will adopt as reasonable DRA's nonlabor escalation factors based on more recent data.

C. Compensation Levels

1. General

Testimony on compensation levels of General for the test year 1988 was presented by Public Utilities Regulatory Specialist II Michael D. McNamara and on labor productivity adjustment for attrition years 1989 and 1990 by Regulatory Specialist Maurice F.

Crommie. Rebuttal testimony on behalf of General was presented by a vice president of Hay Management Consultants, Michael F. Spratt, Ph.D., by General's Compensation and Organization Planning Manager, James Wainscott, and by General's Employee Relations Director, Charles A. Green.

2. 1988 Test Year Compensation Levels

DRA witness McNamara testified that the wages paid by General exceed the average wages paid in relevant labor markets in which General competes for labor services by 7% or $63 million. This figure was revised downward to 5.04% or $47.7 million and further revised downward to 3.65% or $34.3 million. It is DRA's recommendation that this amount be disallowed for ratemaking purposes for the 1988 test year. This recommended expenditure disallowance of $34.3 million is further segregated to $26.2 million to expenses and $8.1 million to construction.

This adjustment is to be in addition to any adjustments advocated by other members of DRA. According to the record, General's employees are grouped into four categories: (a) Executive; (b) Management, Professional, and Technical (MPT); (c) Physical; and (d) Clerical.

Cash compensation levels for selected positions within each group were compared to levels for essentially the same position in the appropriate labor markets for each employee category. The results for each position were weighted by the number of employees in each position to arrive at the aggregate comparison of compensation within each category of employees at General.

According to the record, in arriving at its conclusions, DRA used both public and private survey data, established position groups by geographic areas, adjusted data for company size when selecting levels for compensation, and used independently developed and/or already-established matches of positions within surveys. A data base was assembled containing the information provided by

General linked to each of its nearly 900 positions. For each position, a record included, for example, the population in each position, the coding by functional area, the wage/salary schedule, the title, and the salary. The General data base was then divided into populations by employee group described above and tested for internal consistency, e.g. whether the distribution of compensation by position was essentially normal.

Numerous surveys were employed as follows:

1. Bureau of Labor Statistics (BLS) Area Wage Survey, Los Angeles-Long Beach Metropolitan Area, October 1986

2. BLS National Survey of Professional, Administrative, Technical, and Clerical Pay, March 1986 - Bulletin 2271

3. Hay Group, Inc. 1985 Survey of California and Nevada Nonexempt Wage and Supplemental Compensation

4. A.S. Hansen Compensation Survey 1986

5. Towers, Perrin, Foster and Crosby - TPF&C National Survey of Executive Compensation

From its review of the above surveys, DRA concluded that the MPT population is compensated at a population weighted level of 0.75% above market; that the physical population is compensated at a population weighted level of 5.19% above market; that the clerical population is compensated at a population weighted level of 4.73% above market; and that the executive population is compensated at a population weighted level of 0.87% below market levels.

General's rebuttal witness M. F. Spratt addressed the survey analysis methodology of DRA witness McNamara. According to his testimony, McNamara made an inferential leap from a sample of General's work force in comparison with the sample of the relevant marketplace to General's entire work force in comparison with the entire marketplace. Further, such inferential leaps must be made on the basis of random samples to be able to reliably estimate the sampling or standard error within desired confidence level intervals. According to this witness, since DRA's samples were not drawn on a random basis, generalizing beyond the samples is statistically inappropriate because it was done with an unknown degree of error.

With respect to nonsampling errors, Spratt testified that:

1. The method used by McNamara in selecting the survey value when more than one value was present systematically biased the data toward the most recently conducted survey;

2. Based upon the techniques employed by McNamara, the quality of the matching process, particularly for the data for professional, administrative, technical, and clerical (PATC) positions, cannot be determined;

3. There are apparent arithmetic errors in the data that have had a profound impact on the overall estimates of overpayments; and

4. The data drawn from different survey sources exhibit a high degree of dispersion.

Based on the above sampling and nonsampling errors, Spratt alleges that it is statistically and methodologically inappropriate to draw any conclusions regarding the quantitative relationships between General's total work force pay practices and its relevant marketplace.

General's rebuttal witness Wainscott testified that:

1. The surveys used by McNamara, i.e. the BLS surveys, the Hansen survey, and the Hay survey, do not accurately address the labor market from which General attracts its work force.

2. The hourly work force consists of approximately 80% of employees in positions

unique to the telecommunication industry that is highly trained.

3. The remaining 20% of the hourly work force is generally recruited from a labor market in competition with large, high-paying companies.

4. Approximately 80-85% of management employees are in telecommunication-oriented jobs and, therefore, the labor market for these employees is generally restricted to other large telecommunication companies.

5. The remaining 15-20% of the management work force represents professional and semiprofessional jobs, many of which require a unique field of specialization or level of technical depth that is not commonly found within small to medium-sized organizations.

6. There is no single labor market that accurately reflects the value of jobs within all of General's employee population segments.

7. Each year, General participates in approximately 20-25 surveys covering different markets and jobs, conducts 5-10 informal telephone surveys, and conducts one formal survey.

8. The March 1986 issue of the PATC survey indicated that relative salary levels are generally highest in mining and public utilities.

9. Only 7% of the companies included in the Hansen survey represented transportation, public utilities, and mining companies.

10. McNamara's method of aging the Hansen data resulted in understating the wages in the actual management labor market for Hansen matches by 0.85%.

11. McNamara's methods of aging the PATC and Hay Pac Bell surveys would not be used by compensation professionals.

12. National data in the PATC survey understate wages in California.

13. General conducted a survey of 25 middle management jobs which indicated that General is compensating its employees a weighted average of 1.72% below the pay levels of 19 participating large companies.

14. On a weighted basis, General's salaries are 4.82% below those of other California utilities.

15. A midpoint comparison shows General's salaries are an average of 4.77% below Pacific's.

In its brief, CWA argues that:

1. Since compensation levels were properly negotiated, McNamara's report should be disregarded:

   a. Implicit in the recommended allowance is the assertion that negotiated wage levels were excessive yet McNamara made no finding that General engaged in bad faith or imprudent bargaining with the union.

   b. It is anomalous that McNamara would find excessive the very wage rates which he conceded flowed from prudent bargaining.

2. The fact that one DRA witness (Loy) recommends adoption of the union's pay increases while another (McNamara) rejects the same suggests the wisdom of the historical posture whereby this Commission exercises self-restraint in the area of employee compensation and labor relations.

3. McNamara's conclusions are flawed due to reliance on overinclusive benchmark surveys.

   a. Hay survey covered both union-represented and unrepresented firms.

b. Surveys cannot be said to depict the labor market from which General attracts its work force because 80% of General's employees accept positions unique to the telecommunications industry.

4. To extract wages, as one isolated factor, from the collective bargaining agreement and compare it to wages in a cohort of nonunion firms fails to credit the union-represented firm with the many advantages to productivity, work force morale, and efficiency of operation which often attend the union-represented setting. Accordingly, McNamara's conclusions cannot be accepted.

It is obvious from the record that comparison of the compensation levels of General's work force is very dependent on the application of informed judgment to appropriate data and on the selection of survey data which will accurately reflect the compensation levels paid by General with the relevant job market. It is noted that DRA's findings of the alleged overcompensation of General's work force varied widely during the course of the hearings as indicated by the following tabulation:

	Exhibit 143	Exhibit 144	Exhibit 179
Management			
MPT	5.5% Above	5.5% Above	0.75% Above
Executive	0.87% Below	0.87% Below	0.87% Below
Management Total	5.4% Above	5.42% Above	0.73% Above
Nonmanagement			
Physical	8.6% Above	3.90% Above	5.19% Above
Clerical	6.4% Above	6.40% Above	4.73% Above
Nonmanagement Total	7.0% Above	5.04% Above	3.65% Above
General Total	7.0% Above	5.04% Above	3.65% Above

Such variations do little to assure us of the validity of DRA's showing. In addition, it is difficult to ignore General's evidence with respect to the weighted compensation paid by General being 4.82% below the level paid by Southern California utilities and the midpoint of General's salary ranges being on the average 4.77% below similar salary ranges of Pacific. Consequently, after careful consideration, we believe General has carried its burden of proof on this issue, and we will not adopt DRA's recommendations relating to a disallowance of alleged wage overpayments for ratemaking purposes.

3. Labor Productivity Adjustment for Attrition Years 1989 and 1990

Testimony on the labor productivity adjustment for attrition years 1989 and 1990 was presented by regulatory specialist Maurice F. Crommie. Rebuttal testimony was presented by General's rebuttal witness Charles A. Green. Based on the aggregate findings of staff witness presented in this proceeding, DRA recommends the adoption of a constant base labor productivity factor as measured by access lines per employee of 5% for each of the attrition years 1989 and 1990. The recommendation is coupled with an incentive plan allocating 50% of the actual productivity gains in excess of 5% to General's ratepayers, 25% to General's stockholders, and 25% to General's employees. In the event this Commission declines to adopt the above proposal, DRA recommends as an alternative a constant 7% labor productivity factor for the attrition years 1989 and 1990 with all productivities gains in excess of 7% going to General's stockholders.

According to the DRA witness, the labor productivity gains to be used as an input to the labor adjustment for the attrition years 1989 and 1990 is in accordance with this Commission's D.85-03-042 dated March 6, 1985, which specifies that changes in productivity should be included in the calculations of attrition year labor component. According to the record, access lines per employee (ALPE) is an indicator that is commonly used in the telecommunications industry to measure productivity. According to the record, several technological and organizational changes are suggested by both General and DRA to improve labor productivity including the implementation of a universal operator position system to combine toll, directory assistance, and intercept services in the one work station, computergraphics and automated design equipment, and organizational streamlining and other changes as described in the "Winning Connection" program and in the March 4, 1987 announcement of General's President David Anderson implementing this new strategy.

General objects to that portion of DRA's recommendation which proposes that 25% of the productivity savings in excess of 5% be allocated to employees, both hourly and management, who are identified by a committee of hourly and management employees as the persons responsible for the labor productivity gains. According to the testimony of rebuttal witness Green, the establishment of compensation plans has historically been a management prerogative. Further, according to his testimony, the DRA's plan will require this Commission to insert itself in the place of General's management in the establishment of employee compensation level. Furthermore, according to his testimony, the proposal appears to be inconsistent with the recommendation of DRA witness McNamara regarding General's compensation levels. According to his further testimony, should the Commission adopt witness McNamara's recommendations that General's current compensation levels are too high and make a ratemaking adjustment to bring them down to so-called average level, additional bonus payments would simply be converted to larger ratemaking adjustment. Therefore, according to the further testimony of witness Green, General would in effect be penalized further for paying bonuses because the bonuses only increases the alleged difference between cash compensation levels and those paid the "average" firm in the markets in which General operates.

In its brief, CWA opposes DRA's position, stating:

1. Bonuses are a form of compensation and compensation is a basic term negotiated in a collective-bargaining agreement.

2. Imposition of an incentive program would represent an unprecedented intrusion of the Commission into bargaining matters.

3. The National Labor Relations Act was intended to govern the negotiating process by which wages are set for private union-represented employees and state regulation concerning conduct that the U.S. Congress intended to be unregulated is preempted by federal labor law.

4. With the modest wage increases seen in recent years, bonuses being given to select employees are inappropriate ways to reward work with compensation.

5. The incentive plan is unworkable because: (a) it inherently contradicts the thrust of McNamara's testimony that General employees are overpaid and (b) to single out access lines per employee as the productivity measure for awarding bonuses is arbitrary and unfair.

General's and CWA's position relative to the allocation of 25% of the efficiency savings to General's work force appears to be well taken. Furthermore, we can foresee great difficulty in equitably allocating such savings to employees in a fair, equitable, and unbiased manner. Consequently we will adopt General's and CWA's position and not allocate efficiency savings to General's work force. However, the record fully supports a 5% productivity factor based on the ranges included in the testimony (4% presented by GTEC to 16% by DRA), and the testimony of DRA's witness that a 5%-7% range is a realistic assessment of productivity gains to be expected in the future. Thus, we will adopt a 5% productivity factor for computation of the attrition year labor adjustments for 1989 and 1990. Savings resulting from efficiency in excess of the 5% productivity factor will be shared equally between the ratepayers and General. Since the actual productivity savings for the attrition year will not be known until after the end of the attrition year, we will direct General to file its actual realized productivity factor with the Commission Advisory and Compliance Division (CACD) for review on or before January 31 of the following year. If the actual realized productivity factor is greater than 5%, General should file an advice letter to flow-through the ratepayers' share of savings at the time it files its productivity factor.

D. Audit Team Recommended Adjustments

1. General

The Audit Team (Team) of the DRA Telecommunications Audit Branch reviewed General's books and records covering the period from December 1, 1983 (the cutoff date of the last audit) to December 31, 1986. As the result of Team's audit of General's books and records, Team recommended a number of adjustments to recorded and/or estimated data. The DRA witnesses incorporated these recommended adjustments into their test year results of operations estimates.

2. Plant Related Items

Financial Examiner III Seaneen McCarthy recommended the following plant adjustments to recorded 1985 and 1986 data:

	1985	1986
	(Millions of Dollars)	
Olympic Plant Reclassification	$3.8	
Vacant Parcels		$ 1.8
Competitive Bid Cost Overruns		49.5

According to the testimony of this witness, General constructed $4.9 million of special utility plant to accommodate the 1984 Olympics. In accordance with D.84-07-108, General placed the Olympics plant below the line (BTL) on the basis that the Commission reasoned that the Olympics plant was not beneficial to ratepayers. At the conclusion of the Olympics, General decided to bring all Olympics plant that was either to be retired or to be reused back above the line (ATL) as plant in service. This amounted to $4.2 million of which $3.8 million was to be retired and $0.4 million was to be reused. The plant was retired over the period from March 1985 to December 1986. Each item remained in telephone plant in service until its retirement. Team recommends that, to be consistent with past decisions and our ratemaking policy, the $3.8 million in Olympics plant be retired BTL for ratemaking and accounting purposes. This position is well taken and will be adopted.

According to the testimony of witness McCarthy, included in Account 100.1-Telephone Plant In Service as of December 1986 were vacant parcels of land and unused buildings with a gross book value of $1.8 million that are not currently in use and for which General has no current usage plans. It is therefore Team's recommendation that the $1.8 million and related depreciation reserve from the buildings be reclassified from telephone plant in service to miscellaneous physical property and be excluded from rate base as not used and useful. However, a review of the record reveals that the vacant parcels of land and unused buildings consist of portions of central offices that are unoccupied as a result of General's replacement of electromechanical switches with electronic switches requiring less space. Specifically the unoccupied percentages of the buildings were 23% for La Puente, 13% for West Los Angeles, and 44% for Long Beach. The primary use of the buildings, namely the housing of central office switching gear, is unchanged as a result of the replacement of electromechanical switching gear. Consequently we find the recommended adjustment inappropriate and will not adopt it.

During an analysis of telephone plant DRA witness McCarthy noted that the actual cost of switches as set forth in work order cost detail exceeded the "not to exceed" price (NTEP) at a number of locations. According to the testimony of this witness, these overruns consist of those amounts charged to Account 209-Digital Stored Program Control Switch Equipment and were larger in the work order cost detail than in the NTEP. The total cost overrun for all projects in the competitive bid price program, rounds 1 through 4, to January 1987 was $25.1 million for installation and $24.4 million for material. It is therefore Team's recommendation that we disallow the $49.5 million of cost overruns because of General's inability to stay within the budget limit set by itself.

Rebuttal testimony on behalf of General submitted by the Director, Telecommunications Regulatory and Advisory Services of Coopers & Lybrand, C. O. Thorsen, indicated that the DRA comparison should have been based on the final rather than the original NTEP price. Such a comparison would have shown no cost overrun for materials. We are persuaded that the final NTEP and not the original NTEP should be used for comparison purposes and, consequently, will not adopt DRA's recommendation with respect to the $24.4 million material overrun. With respect to the $25.1 million labor adjustment, it is DRA's position that General's work force incurred costs of that amount greater than what would have been incurred had the CO vendor performed the installation. According to the rebuttal testimony of witness Thorsen, the vendor's labor costs were calculated by (a) for closed work orders in Rounds 1,2, and 3 the vendor's estimates of original NTEP installation costs were used as a base, (b) the labor costs estimates were adjusted for activity performed by General in advance of switch installation, for forecast changes and change orders that occur subsequent to issuance of purchase order and for General's supervision and monitoring work, and (c) calculating the cost by switch location. General's actual labor costs were based on information contained in General's work order detail. The results of this study indicated that General's actual labor cost for installation of COSE was 2.241 times that of the vendor for Rounds 1, 2, and 3. The application of this factor to Rounds 1 through 4 indicated General's costs to be $7.9 million greater than vendor's costs. Under these circumstances, we will adopt a labor overrun disallowance of $7.9 million.

3. Corporate Headquarters Move

In December 1984, General accrued $30,470,000 to various expense accounts for the cost it would be incurring relative to the move of its headquarters from Santa Monica to Thousand Oaks. This accrual represents employee household moves, employee bus transportation between Santa Monica and Thousand Oaks for one year after the move, and office moves. The cost was spread to specific expense accounts based on percentage head counts by responsibility center (RC) to total head count relocating. The counter entry to Account 174-Deferred Credits totaled $32 million, including $1,530,000 of cost related to GTEL's move to Thousand Oaks. Since these costs are of such a material and unusual nature, according to DRA witness McCarthy, it is her recommendation that, for ratemaking purposes, the accrued expense amounts of $30.47 million and deferred credit amount of $32 million be excluded from recorded data for trending purposes. This position is well taken and will be adopted by our inclusion of consideration of its impact on the trending of the capital account by the appropriate DRA witness. It should be noted, however, that such costs are an integral part of the move of headquarters from Santa Monica to Thousand Oaks and, therefore, should be considered as an offset against capital sales gains resulting from such relocation of headquarters.

In connection with the relocation of the headquarters building, numerous improvements were performed prior to moving in. The costs of these improvements totaled $1,074,000 in 1985 and $300,000 in 1986 and were booked to Account 606-Repair of Building and Grounds. According to DRA witness McCarthy, the magnitude of the work performed does not constitute recurring repairs to a building and such costs were incurred only to make the new building ready for occupancy. Since such expenses would not be incurred in the normal course of routine operations, DRA recommended elimination of the total expense of $1,374,000 from Account 606 for ratemaking purposes. We recognize the merits of DRA's ratemaking arguments, and it remains our policy not to recognize infrequent and unusual costs for ratemaking purposes. However, in this instance the costs incurred (e.g. rearrangement and relocation of air conditioning equipment, installation of room partitions, etc.) were reasonably incurred to make its new office space habitable. In the circumstances we will permit amortization of these recorded costs to Account 606 over a three-year period. We expect the Account 606 records to be maintained so that this amortization does not impact the trending of Account 606 in future years.

As a part of the purchase of land and buildings in Thousand Oaks, General acquired a parcel of land across the street from One GTE Place for the purpose of building another office--the Lakeview building. The cost of this land includes $905,782 of interest during construction (IDC). In accordance with past Commission policy, it is DRA's recommendation that the Commission not allow IDC on land for ratemaking purposes. We agree and will disallow this amount.

4. Underground Storage Tanks

During 1983, legislation was enacted requiring all owners of underground storage tanks that store hazardous substance to register with the State Water Resources Control Board by July 1, 1984 and requiring all owners to acquire a permit from the local authorizing agency. The California Underground Storage Tank Regulations, adopted 1985, cover the permitting and monitoring of underground tanks and the reporting of leaks. General incurred costs of $1,587,000 in 1985 and $1,946,000 in 1986 related to the cleanup of toxic waste, specifically the leakage of fuel from 37 storage tanks. In addition, $1,702,000 was charged to Account 171-Depreciation Reserve. According to the testimony of staff witness McCarthy, until legislation went into effect forcing General to identify or monitor its storage tanks, the company was negligent in performing its duty as owners of potentially lethal substances. General has admitted in intercompany memoranda and data responses to allowing its fuel storage tanks to deteriorate because of its own negligence. For these reasons, Team recommends disallowing all costs associated with the cleanup of toxic waste leaks which total $3,533,000 of expenses and $1,702,000 in depreciation reserve plus any future costs that General may incur in cleaning up leaks of toxic waste.

General's rebuttal testimony on this matter presented by its Research Conservation Manager Marti Schmidt indicated that:

1. GTE Telops Environmental Compliance Task Force was formed in January 1984 to study, evaluate, and recommend comprehensive programs for all hazardous material management and underground storage tanks.

2. All GTE Company subsidiaries (GTOCS) had programs already in effect, but the task force was given the responsibility to evaluate and enhance these programs.

3. The GTE Telops Environmental Compliance Task Force prepared a document entitled "Underground Storage Tanks" which was prepared in order to identify the potential problems with underground storage tanks and to assist in developing a program of preventative maintenance/action rather than reaction.

4. Two of the 37 tank leaks that had been detected as a result of General's plant leak investigation program were sudden and accidental rather than due to normal wear and tear and would presumably be covered by insurance.

5. Leaks have been attributed to corrosion of tank systems, pipes, etc., and leaks in piping caused by loose fittings. Corrosion to the tank, tank system, and pipes and the problem of loose fittings were not, according to this witness's testimony, the result of the company's negligence.

6. General has always used due care and taken appropriate action to protect against potential leaking tanks, but has been limited to the extent of technological uncertainty that has plagued tank owners nationwide.

7. General had a program of leak prevention prior to 1984 which included: (a) prior to the start of a new installation, the tank as well as the associated piping was pressure-tested with air in accordance with the Uniform Fire Code to verify its integrity; (b) in addition to inventory control by dip-sticking each tank containing diesel oil, the fuel in these tanks was filtered once a year to remove all water, sludge, and bacterial buildup; (c) soluble corrosion/breakdown inhibitors were also added to the contents of its tanks once a year to reduce internal corrosion; and (d) through the years as technology and new products became available, General developed a standard of putting a glypol lining on the interior of the tank to prevent further corrosion/breakdown of the inner tank.

8. By 1984, Federal and State laws had been enacted which require containment in new double-walled tanks (new installation) and monitoring of the tanks (both existing and new installations). The intent of the new laws are: (a) Total containment when a leak occurs and (b) monitoring for early leak detection.

9. As science and technology have improved, past acceptable means of handling storage and disposal are no longer acceptable. However, the regulations concerning contamination and cleanup are retroactive.

10. It is unreasonable to expect individuals or corporations to bear the burden of care and concern prior to the time that scientific technology is developed and technology is available which addresses the potential problems.

11. The costs of currently approved monitoring techniques are a normal cost of doing business. Underground tanks are necessary for the storing of fuels because they lessen the risk of explosion and the storage of fuels is required for General's business operations.

12. It is reasonable to believe General will experience additional leaks in the future and therefore the cleanup costs should be allowed as a normal cost of doing business.

It is obvious from the record that, in the past, General has not adequately maintained its underground storage tanks. However, as a result of the new legislation, substantial sums were recorded as expenses in the years 1985 and 1986 for cleanup and correctional measures. Nonetheless, to permit these two years' recorded expense to be used as a basis for trending future expenses would result in an abnormally high expense allowance for this item. To eliminate the amount completely would result in no allowance for future cleanup work. We are persuaded that future cleanup costs will be incurred and such costs are a normal part of doing business. Even DRA acknowledges in its Opening Brief (pp. 22-23) that there is a need for a future cleanup program and that General's expenditures for toxic cleanup should be evaluated on a case-by-case basis. Since the record supporting General's test year toxic cleanup request of $2.362 million (General's Opening Brief, p. 50) is sparse, we have no basis for finding any specific amount reasonable for the test year. General has not justified its $2.362 million request with reference to a specific cleanup program or budget. However, on a judgment basis, and in recognition that reasonable test year costs will be incurred, we will authorize $2.0 million for test year 1988.

We will direct General to include a detailed plan for investigation and program development for the test year and five years thereafter in its next test year NOI filing. In addition, we will order General to file a description of its current 1988-89 hazardous waste cleanup activities so that we may monitor continuing developments in this sensitive and important area. This report should include a site-specific accounting for cleanup funds, a detailed work plan and schedule, and a detailed budget. We will review this information consistent with the priority we have expressed regarding hazardous waste cleanup in recent decisions such as D.88-07-059.

5. GTEL Accounts Receivable

Included in Account 118-Due from Customers and Agents are accounts receivable and uncollectibles due from GTEL customers totaling a net of $1,260,000 in 1985 and $9,480,000 in 1986. These receivables represent collections for deregulated equipment rentals. All revenues collected from these receivables have been properly booked BTL by General. In order to match the receivables with the revenues collected from them, DRA recommends that Account 118 be reduced by these amounts and the dollars be transferred BTL for ratemaking and accounting purposes. This recommendation appears reasonable and will be adopted.

6. Employee Store

DRA's Financial Examiner III Francis Fok recommends a ratemaking adjustment reducing General's 1988 operating expenses by $0.6 million equal to the estimated operating loss incurred to maintain General's employee store. According to this witness's testimony, inadequate accounting for the store operation, inadequate management, lack of supporting information, and cross-subsidization of General's unregulated affiliates form the basis for the recommended disallowance. General's employee store operation operates under the policies and guidelines established by

GTE Service Corporation, which provide that all employee stores of GTE Telecoms are to be open to employees of GTE, Incorporated and its affiliates. According to the record, GTE Service Corporation negotiates purchases with eight manufacturers-suppliers and the purchase price, which includes freight costs, then becomes the selling price at the employee store. As such, there is no markup included in the price of the goods to employees. Consequently the costs to operate the store are experienced losses. Such operating cost losses are estimated to be $0.55 million a year and form the basis for the recommended disallowance of $0.6 million. Inventory from the employee stores includes all Sylvania televisions, VCRs, stereos, and other large and small appliances offered for sale to employees of General. This inventory of appliances is booked to Account 139-Other Deferred Charges. Ratepayers receive no discernible benefit from the operation of the store. Consistent with the recommendation of DRA witness Fok, DRA witness McCarthy recommends that Account 139 be reduced for ratemaking and accounting purposes by the inventory value of $253,000 for 1985 and $449,000 for 1986. These recommendations appear reasonable and will be adopted for the purposes of this proceeding.

7. Voluntary Separation Incentive Plan

DRA witness McCarthy recommends a disallowance to expenses, plant, and depreciation reserve of $7.47 million, $1.728 million, and $32,000 in 1985 and a negative $426,000, $145,000, and $1,000 in 1986, respectively, which represent costs incurred for the voluntary separation incentive plan (VSIP). The VSIP provides certain additional income to management employees who voluntarily leave the company. The offering began on November 11, 1985 and ended on January 10, 1986. In 1982, a similar plan, named a voluntary incentive separational allowance (VISA), was offered to reduce the management work force. During the rate case at that time General initiated the exclusion of expenses associated with the VISA program and in D.84-07-108 this Commission ordered General to exclude the capitalized portions of these costs. To be consistent with D.84-07-108 and General's own action in A.83-07-002 in which both the expenses and the capitalized costs associated with the VISA program were excluded for ratemaking purposes and to eliminate any significant effect of unusual nonrecurring activities on a trended test year estimates, DRA recommends the disallowance of these expenses, plant, and depreciation reserve. DRA's position is well taken and will be adopted.

8. <u>Commercial and Marketing Expenses</u>

DRA's financial examiner III Francis Fok recommends that 1986 recorded commercial and marketing expense be reduced by $16 million and Account 671-Operating Rent be reduced by $0.3 million. The ratemaking adjustments to advertising expense relate to expenditures that were unusual or of a one-time nature and those that represented institutional advertising. One-time expenditures are those which are not of an ongoing nature and therefore should be excluded from any historical base utilized to project test year estimates. Also included in the recommended adjustments are expenses of operations that will be discontinued before the test year. The institutionalized items excluded consist of National Prorates ("gee...no, GTE") of $1.1 million, "Image" which is self-explanatory of $4.9 million, "Public Information" advertising for program consisting of such events as NFL sponsorships, sports sponsorships, culture sponsorships, and academic all-America campaigns, for a total of $1.6 million and other sponsorships including "NFL Sports" and "Indy 500" totaling $2.7 million, for a total institutional advertising disallowance recommended of $10.3 million. The one-time programs that were recommended for disallowance by this witness included CPE phaseout of $0.2 million, an inside wire deregulation maintenance program of $0.4 million, together with associated expenses of $0.9 million and an equal access information program of $1.7 million, for a total of $3.2

million. The balance of the recommended adjustments include one-time expenditures for phone mart operations, which will be discontinued by 1988, consisting of operating rent of $0.3 million and marketing and sales expense of $2.5 million.

According to witness Fok, institutional advertising is defined as advertising which promotes the corporate image. It has been consistently disallowed by this Commission for ratemaking purposes. All the above-itemized recommended advertising disallowances are in keeping with past Commission decisions and policies and would be appropriate for making adjustments were they to apply to the 1988 test year. However, the proposed disallowances are to be applied to recorded 1986 data presumably with the idea of using them as the basis for projecting 1988 test year estimates of expense. Such a procedure would be appropriate if it was clear that the 1988 advertising campaigns of General would parallel the 1986 campaign. However, there is nothing in the record supporting such a position. Under these circumstances, we will not adopt DRA's recommendation relative to the disallowances of the institutional advertising expenses totaling $10.3 million.

DRA's recommended disallowances of the one-time programs, detailed above, totaling $5.7 million commercial and marketing expense and $0.3 million operating rent have merit since General has not shown that they will recur during the test year. We will adopt DRA's recommended disallowance.

9. <u>General Office and Other Operating Expenses</u>

DRA financial examiner III J. J. Simmons presented testimony recommending adjustments to the general office salaries and expense and other operating expenses as follows:

Item	Proposed by DRA 1985	Proposed by DRA 1986	Adopted 1985	Adopted 1986
	(Thousands of Dollars)			
Employee Communications	$ 551	$1,006	$ 293	$ 732
Community Relations	995	1,473	700	700
Information Communications Center	857	925	857	925
Overheads	599	470	461	588
Total Public Affairs	3,001	3,874	2,311	2,945
Lobbying	322	369	322	369
Lobbying Support and Monitoring	297	309	297	309
Telephone Assn. Membership Dues		222		222
Total	3,621	4,773	2,930	3,843

Rebuttal testimony on the adjustments for Employee Communications, Community Relations, and Information Communications Center was presented on behalf of General by its Employee Communications Manager, Don Anderson.

According to the testimony of witness Simmons, the Employee Communications disallowance consisted of $35,000 in 1985 and $457,000 in 1986 as a result of open house events and employee orientation expenses relative to moving to the new headquarters building and should be excluded for ratemaking purposes as nonrecurring and inapplicable to the test year. Further, according to this witness, the Employee Communications activities provide a dual function: partly to enhance the corporate image of the company and partly to inform. Therefore, he recommends a 50% disallowance for the remaining expenses resulting in an overall expense disallowance of $551,000 for 1985 and $1,006,000 for 1986. General's witness Anderson objected to the 50% disallowance on the basis that everything that is written and produced in the Employee Communications center is aimed at and written for the benefit of the company employees. According to this witness, the primary objective is to help create the pride and teamwork essential to building an effective, responsive and informed work force in order to assure high quality, cost-effective products and services for the ratepayers. He admits that the Employee Communications' efforts may enhance the corporate image in the eyes of the employees, but states that this is part of its purpose to make employees proud of the company for which they work. DRA's arguments with respect to the $35,000 in 1985 and the $457,000 in 1986 relative to the headquarters move being a one-time expense that will not recur in the test year have merit and will be adopted. We are somewhat less willing to adopt DRA's recommended disallowance of 50% of the remaining Employee Communications expense. It is obvious from the testimony that there is a substantial amount of corporate image enhancement inherent in these activities and in accordance with our past decisions, this should be disallowed for ratemaking purposes. Intermingled with these image enhancing activities, however, are employee communication activities which impart necessary information and which serve as an effective link between management and its employees and which are appropriate for ratemaking purposes. It is difficult to separate such intermingled activities and it is not easy to quantify the portion that should be disallowed. We will adopt a 25% disallowance for test year 1988, for a total disallowance of $293,000 for 1985 and $732,000 for 1986. We recognize that this is necessarily arbitrary and place General on notice that for the future it will have to make a more concrete showing of the benefits that such employee communications have for the ratepayer. Simple assertion of some intangible benefits will no longer suffice to keep our disallowance at the 25% level.

We place General on notice for the future it will have to make a more concrete showing of the benefits that such employee communications have for the ratepayers. Simple assertion of some intangible benefits will no longer suffice to keep our disallowance at this level.

According to witness Simmons, the stated purpose of the Community Relations section is to enhance the company's image in the community. It is primarily responsible for the allocation of $2.2 million of charitable contributions and the planning, coordination, and execution of other activities of a philanthropic nature. Consequently, according to this witness, all the expenses of the Community Relations section are primarily for the purpose of corporate image enhancement and are therefore stockholder interest expenses not properly chargeable to the ratepayer. Consequently he is recommending a total disallowance of this group's expenses for 1985 and 1986 resulting in a decrease in expenses of $995,000 in 1985 and $1,473,000 in 1986.

According to the testimony of General's rebuttal witness Anderson, Community Relations is responsible for General's consumer affairs program, the community needs assessment program, charitable contributions, and volunteer referral. The Consumer Affairs Program coordinates a representative group of 21 of General's customers who constitute a consumer advisory panel and meet monthly for the purpose of providing General's management with recommendations and suggestions regarding corporate policies and procedures. The total expenditure for the Consumer Affairs Programs for 1985 and 1986 was approximately $205,000 annually. The Community Needs Assessment Program is administered by one of the Community Relations representatives and is designed to systematically collect the opinions and concerns of cross-section of community leadership through a series of personal interviews to obtain comments on community needs and general services. The Community Relations Group is responsible for designing programs in instances where there is a broad consensus that a particular type of need that relates to telephone service is of major concern to a particular community. The total expense for this group for 1985 and 1986 was approximately $265,000. Another function of the Community Relations Group is the volunteer program which channels requests from various community groups to employees who may be interested in volunteering. According to this witness's testimony, the role of the Community Relations staff is to serve simply as a provider of that information for the various agencies. Volunteers contribute their own time and are not required to identify themselves as General employees. The cost of this function for 1985 and 1986 was approximately $180,000 annually. Another program run by the Community Relations Group is the Contributions Program. The Contributions Program is responsible for responding to all requests and, in cases where General guidelines deem it appropriate, grants are made to selected agencies from a BTL contributions account. The annual expenses of the Contributions Program are approximately $100,000. Since approximately half of the responsibility is to respond to requests that do not qualify for funds, it is General's belief that $50,000 would be an appropriate allowance for ratemaking purposes. The total of the above-discussed programs is approximately $700,000 annually which, General believes, should be allowed for Community Relations Group. It is noted that the above $700,000 is less than half of the recommended 1986 expense disallowance of DRA witness Simmons. General's position does not appear unreasonable and we will adopt the $700,000 figure for Community Relations.

According to DRA witness Simmons, the Information Communications Center (ICC) is responsible for all audio visual and television programs produced by General. In addition, the ICC is responsible for the information, distribution, network, and operations of the video conferencing center. This witness reviewed a descriptive list of all video and audio productions of the ICC during 1985 and 1986 and planned for during 1987, and determined that many of the productions fall into the category of corporate image enhancement and are therefore not allowable for ratemaking purposes. Further, according to this witness's testimony, he was unable to obtain the specific cost data for each individual production, as the company was only able to provide data on "average cost by class of production". Lacking the specific cost data and considering the dual nature of many of these audio visual productions that this section provides to the employee communications system, this witness recommends an overall disallowance of 50% for ICC's 1985 and 1986 expense. This amounts to $856,500 for 1985 and $924,500 for 1986.

According to General's witness Anderson, the ICC has the employee work force as its primary audience for its productions. Further, according to this witness, whereas employee communications specializes in written publications, the ICC specializes in video productions. The mission of ICC is to help assure that the company has informed, involved, and knowledgeable employees to provide high quality products and services to the ratepayers. Witness Anderson further testified that ICC does work, which, General would agree, is not primarily for the benefit of the company employees or ratepayers. According to his testimony, the amount of this other work totaled $130,000 for 1985 and totaled $198,000 for 1986, representing 9% for 1985 and 12.7% for 1986, which, in his opinion, should be the disallowed amount for 1985 and 1986 rather than the 50% proposed by DRA's witness Simmons. The results of DRA's review and evaluation of the descriptive list of all video and audio productions of the ICC during 1985 and 1986 and planned for during 1987 appear to us to be, if anything, on the conservative side. Consequently, we will adopt DRA witness Simmons' disallowance of 50% for ICC. Adjusting the overhead to reflect the above-adopted results yields a 1985 figure of $461,000 and a 1986 figure of $588,000, for a total public affairs expense of $2,311,000 for 1985 and $2,945,000 for 1986 which we will adopt as reasonable.

DRA's witness Simmons' recommendation that lobbying expenses of $322,000 for 1985 and $369,000 for 1986 and other governmental affairs expenses of $297,000 for 1985 and $309,000 for 1986 be disallowed adhere to our general policies and past practices and will be adopted. We will also adopt this witness's recommendation that membership dues of $222,000 for 1986 be disallowed.

10. Prudence of Relocation

DRA Financial Examiner Jean Hill presented an analysis of the prudence of General's decision to invest in a new administration building in Thousand Oaks. This analysis indicated that General's decision to relocate to Thousand Oaks is noncost-effective and that the nonquantified considerations are not sufficient to support the investment decision. DRA consequently recommends that $67 million be disallowed from General's test year 1988 rate base to be offset by the $31.5 million gain on the sale of property, testified to by DRA Auditor I Mar, for a net disallowance of $36 million. In addition to the $67 million disallowance on rate base, DRA recommends a disallowance of $21.5 million annual expense associated with employee relocation.

Rebuttal testimony to witness Hill was presented on behalf of General by its treasurer, Charles J. O'Rourke.

Prior to its relocation to the Thousand Oaks area, the General headquarters building configuration consisted of 14 separate sites of which all but one were located in the Santa Monica area. According to General's management, this fragmented building plan is operationally cost-ineffective as it requires extensive employee travel between buildings in the conduct of daily business and necessitates the duplication of common areas as well as support services such as word processing and reproduction facilities. Furthermore, due to age most of the buildings would require refurbishment with three of the major sites requiring extensive overhaul. In arriving at its decision to relocate the headquarters to the Thousand Oaks area, General assessed three alternative headquarters scenarios: stay in the existing locations and refurbish them; consolidate in Santa Monica; and consolidate in Thousand Oaks. According to the testimony of witness Hill, a major factor in the decision to relocate to Thousand Oaks was the opportunity for gaining profit on sales of existing property. In particular, General held a long-term lease on a building at 100 Wilshire with a purchase option. The exercise of this option afforded General an immediate profit. DRA is recommending that this Commission adopt rates that will reflect the most cost-effective alternative so that the ratepayers are not penalized for General's alleged imprudent management decision. Specifically, DRA is recommending that General be allowed a maximum rate base of $48.9 million for its investment in Thousand Oaks. Based on recorded capital costs of $113 million, this represents a disallowance of approximately $64.1 million. DRA's rationale for the above disallowance is based on its recommendation that the cost allowed for General's new headquarters should not exceed what the cost would have been for the most cost-effective alternative, in this case, renovation of existing quarters. According to DRA witness Hill, the present value of the present status alternative is $95.9 million, which equates to a rate base of $48.9 million and an annual expense of $4.5 million.

DRA's cost-effectiveness studies differed from General's in two key assumptions which are: (1) offsetting the Thousand Oaks' capital investment by the gain from the sales of existing properties in Santa Monica; and (2) the inclusion of the cost of 12 acres of undeveloped land in the present status alternative. According to the record, were witness Hill to accept these two assumptions then DRA would agree with General's findings that the investment in the Thousand Oaks relocation is cost-effective. General records the gain on the sale of property BTL which allocates 100% of the gain to the stockholders. Consequently, according to DRA, the gains have no impact on the ratepayers and it is inappropriate to include them in the analysis. The cost of the 12 acres of land was included in the present status alternative to make it comparable to the Thousand Oaks alternative, which included 12 acres of undeveloped land that were recorded in the miscellaneous physical property count, a BTL.

General witness O'Rourke presented rebuttal testimony which indicated that:

1. General rejected the alternative of remaining in the existing 14 Santa Monica buildings due to the inefficient building configuration and the extensive investment required to renovate four of the major buildings.

2. The after-tax present value of cash flows was the focus of General's financial recommendation to relocate the headquarters to the Thousand Oaks area.

3. General used the traditional after-tax financial model to develop the final decision criteria and the revenue model in support of an analysis.

4. General addressed the long-term cost of the decision regarding location of its headquarters facilities separately and independently of accounting and ultimate ratemaking treatment of the gain from the sale of its Santa Monica properties.

5. The accounting and ratemaking treatment of the gain of sales of properties resulting in the relocation is an independent issue separate from the financial analysis of the decision about whether or not to relocate.

6. The Uniform System of Accounts requires that the gain on sale of property by a telephone company be recorded in Account 360-Extraordinary Income (a BTL account) regardless of the future ratemaking treatment of any gain and regardless of whether the property is included or excluded from the utility's rate base.

7. The proceeds from the sale of surplus property in Santa Monica should be used to reduce the estimated cost of the relocation to Thousand Oaks.

8. The acquisition of the 85-acre site in Thousand Oaks included a 12-acre parcel that would be held for future use. In order to fairly compare the economics of the alternatives for General's management, General had to include the cost of a similar parcel in the Santa Monica alternatives.

9. General's Operations and Human Resources Departments identified several tangible benefits which were not quantified for the purpose of financial analysis but were seriously weighed by General's management in arriving at its decision.

10. The decision to relocate was based on an analysis of cash flows and not on the opportunity for capital gains in the relocation process.

We agree, in general, with the allegations set forth above, particularly with the assertion that the accounting and bookkeeping treatment of a transaction should not be a factor in economic analysis designed to test the prudence of a decision to either remain in Santa Monica or to relocate to Thousand Oaks. Consequently, in consideration of both General's and DRA's testimony and exhibits on this matter, we conclude that the relocation to Thousand Oaks was not imprudent. Therefore, we will neither adopt DRA's recommendation that $64.1 million be disallowed from General's rate base for test year 1988 nor that the maximum annual expense allowance be limited to $4.5 million.

11. <u>Gain On Sale of Property</u>

Concurrent with its 1985 corporate headquarters relocation, General sold several properties, including offices in Santa Monica at 2224 Colorado Avenue, 100 Wilshire Boulevard, and 2020 Santa Monica Boulevard. DRA's auditors ascertained that these properties had been booked in various above-the-line accounts prior to being transferred below the line in anticipation of their sale. The auditors recommend that the gain on the sale of these properties be recorded above the line, because each property was supported by ratepayers, and was in rate base, for the majority of its useful life. DRA's auditors believe that this recommendation is consistent with the ratemaking treatment adopted by the Commission for similar types of buildings and parcels in several decisions, including Pacific Bell's ongoing general rate proceeding.

For example in D.86-01-026, the Commission stated:

> "Land which has been in Account 100.1 appreciates as utilities hold it over time because all costs of ownership, including a return, are funded by ratepayers. Accordingly, when land is taken out of service or rate base any net gain should accrue above the line, and utilities, of course, have an obligation to maximize receipts from the land. Our rationale follows that of the FCC in its conclusion that any gain from parcels (including land) must accrue to ratepayers (CC Docket 81-893, Report & Order adopted November 23, 1983, pp. 97-99.)"

(D.86-01-026, mimeo. p. 83.) See also D.87-12-067 (mimeo. p. 280) issued in Phase 2 of D.85-01-034, regarding disposition of Pacific's 420 Cowper Street property formerly in rate base.

In accordance with that past decision, DRA's witness Mar recommends including these gains in miscellaneous revenues, amortized over a three-year period consistent with the approach used in D.86-01-026. According to Mar, this gain should be calculated as follows:

Property	Sale Price	Net Book Value	Selling & Other Costs*	Gain (Before Tax)
2224 Colorado	$ 8,758.8	$ 566.8	$1,079.1	$ 7,112.9
100 Wilshire	42,150.0	17,741.9	212.8	24,195.3
3630 State St.	120.0	55.2	2.4	62.4
78-202 Avenida La Fonda	109.0	7.9	9.6	91.5
				$31,462.1

* This column primarily reflects selling costs but in the case of the 2224 Colorado property includes a $1 million reserve for environmental cleanup.

When the $31,462,100 figure is amortized over a three-year period, this amounts to $10,490,000 a year.

In addition to the above four properties, the record indicates a sale of a piece of property at 2020 Santa Monica Boulevard at a gain before taxes of approximately $5,751,000, making a total gain of $37,213,000.

As more fully detailed below, General believes that DRA's recommendation should be adopted only if the expenses incurred to make that gain possible are recognized as an offset. These expenses are essentially relocation expenses, such as the cost of relocating employees, the sale of their homes, the cost of purchasing new homes, real estate commissions, taxes, and moving allowances. Also included are expenses General incurred in moving its physical property, such as office furniture from the vacated building to its new Thousand Oaks corporate offices (Ex. 287, p. 5). General argues that these incurred expenses made the gain possible, and are appropriately offset for ratemaking purposes. DRA strongly opposes this offset arguing that the gain from the sale of the Santa Monica properties belongs to the ratepayers regardless of the reason for their sale.

Rebuttal testimony by General's witness Wilson indicated that:

1. DRA included before-tax gain of $62,400 for the sale of property at 3630 State Street, Santa Barbara, and $91,500 for the sale of property at 78-202 Avenida La Fonda, La Quinta, whereas the collective after-tax gain for the sales of these properties is approximately $75,000. Because these transactions did not occur as a part of the relocation from Santa Monica to Thousand Oaks, resulting after taxes gain for these properties should not be considered in the discussion of ratemaking treatment related to the prudency of the investment in Thousand Oaks.

2. The after-tax gains for the properties sold or to be sold in connection with the relocation to Thousand Oaks are:

a.	100 Wilshire Boulevard	$15,784,700
b.	2224 Colorado Street	4,629,700
c.	2020 Santa Monica Blvd.	3,743,700
	Total	$24,122,100

3. General booked $30.5 million for the cost of relocating employees, the sale of their homes, the cost of purchasing new homes, real estate commissions, taxes, and moving allowances.

4. General spent $1.2 million to renovate the Thousand Oaks building.

5. The net effect of combining the after-tax gain of $24.1 million from the sale of the Santa Monica properties with the after-tax cost of $15.5 million for relocating the staff moving the company's physical property and renovating new headquarters buildings results in a net gain of $8.6 million.

6. If this Commission concludes that capital gain from the sale of General's property should be flowed through to the ratepayers beginning in 1988, then the relocation and renovation expenses ($15.5 million) should be netted against the net gain ($24.1 million) on the property sales and amortized over the same period, which he recommends as being 10 years rather than the 3-year period recommended by DRA witnesses.

7. The above plan was presented to representatives of Public Staff Division (now DRA) and the Commission Advisory and Compliance Division during the informal meeting on October 1, 1985 and no objections to the plan were raised at that time.

DRA's witness Seaneen McCarthy recommended the disallowance of the above $30.5 million from various expense accounts and the related $32 million from deferred credits for the accrual of moving costs to Thousand Oaks, the disallowance of $1.374 million from Account 606, representing improvements to One GTE Place, and the disallowance of $905,782 of IDC on land acquired across the street from One GTE Place for the purpose of building another office.

We will follow for General the approach we have followed for Pacific Bell, and flow the gains from these transactions to the ratepayer. However, we must consider the amount of the gain on the sale of property to be included in our adjustment and, secondly, the period of time over which such gain is to be amortized. As previously stated, according to rebuttal witness Wilson, the net effect of combining the after-tax gain of $24.1 million from the sale of the Santa Monica properties with the after-tax cost of $15.5 million for relocating the staff, moving the company's physical property, and renovating the headquarters buildings results in a net gain of $8.6 million.

On balance we believe General's offset argument is more persuasive, given the particular set of facts presented. In this situation there was not a straightforward stand-alone sale of property; rather this was a unified transaction. But for the decision to relocate to Thousand Oaks, the sales would not have occurred. Given the unified nature of the transaction General's proposed offset presents, in any event, an acceptable method of treating the nonrecurring relocation costs incurred in connection with the move to Thousand Oaks, while flowing the gain through to its ratepayers.

We do not view this result as precedent-setting for other gain on sale issues, but rather as a treatment tailored to the particular facts of General's move and employee consolidation.

Translating the net gain of $8.6 million to before-tax net gain results in a figure of $13.3 million, which we find a reasonable adjustment to reflect the relocation of the general office staff to Thousand Oaks. To this should be added the $154,000 gain before taxes for the sale of the State Street and Avenida La Fonda properties, making a total of $13,454,000. We will also adopt the staff's recommended 3-year amortization period resulting in a miscellaneous revenue for the 1988 test year of $4,485,000, for a gain on the sale of properties.

E. Revenues

1. General

Testimony on 1988 test year revenues was presented by program and project supervisor K. P. Coughlan, public utility regulatory specialists I R. R. Berry and E. S. Ting, and senior utilities engineer N. C. Low. Total operating revenues consist of subscriber station revenues including monthly service charges, service connection, semi-public telephone, total message charges, gross ZUM charges, and connecting company charges and credits; local service revenues consisting of public telephone revenues, local private lines, and other local service revenues; toll service revenues including interstate and intrastate access and intraLATA toll revenues; and miscellaneous revenues including telegraph commissions, directory revenues, rent revenues, general service and license, other miscellaneous revenues, and interstate and intrastate billing and collecting, and surcharge revenues less uncollectibles. The tabulation below sets forth the revenue estimates as estimated by DRA and General, the difference between the two in amount and percent, and our adopted revenues. The bases for our adopted revenues are set forth in the ensuing paragraphs.

Item	DRA	General	General Exceeds DRA Amount	General Exceeds DRA Percent	Adopted
		(Thousands of Dollars)			
Subscriber Station Revenues:					
Monthly Svce Chg.	$ 441,753	$ 430,926	$ (10,827)	(2.5)	$ 441,753
Service Conn.	66,336	71,436	5,100	7.7	66,336
Semi-public	7,000	7,019	19	0.3	7,000
Total Mess. Chgs.	113,400	116,131	2,731	2.4	113,400
Gross ZUM Chgs.	97,890	95,273	(2,617)	(2.7)	97,890
Conn. Co. Chgs.& Cr.	3,259	2,887	(372)	(11.4)	1,308
Subtotal	729,638	723,672	(5,966)	(0.8)	727,687
Local Service Revenues					
Public Tel. Rev.	33,260	31,798	(1,462)	(4.4)	33,260
Local PL Intrastate	3,900	5,559	1,659	42.5	3,900
Other Local Rev. (EAS)	12,430	18,439	6,009	48.3	16,310
Subtotal	49,590	55,796	6,206	1.3	53,470
Toll Service Rev.:					
IntraLATA	781,079	814,847	33,768	4.3	822,393
Intrastate Access	215,908	258,978	43,070	19.9	206,526
Interstate Access	480,425	480,425	0	0.0	480,425
Subtotal	1,477,412	1,554,251	76,839	5.2	1,509,344
Miscellaneous Rev.:					
Telegraph Comm.	19	19	0	0.0	19
Directory	231,480	198,292	(33,188)	(14.3)	205,000
Rent Revenues	1,804	1,804	0	0.0	1,804
Gen. Serv. & Lic.	1,133	1,133	0	0.0	1,133
Other Misc. Rev.	37,740	17,450	(20,290)	(53.8)	23,531
Intrastate Bill. & Coll.	26,675	20,253	(6,442)	(24.1)	26,675
Interstate Bill. & Coll.	23,819	23,819	0	0.0	23,819
Gain on Sale of Property	10,490	0	(10,490)	(100.0)	4,485
Subtotal	333,160	262,770	(70,390)	(21.1)	286,466
Surcharge Revenues	73,287	184,675	111,388	152.7	74,730
Total	2,663,087	2,781,164	118,077	4.4	2,651,697
Less: Uncoll.	18,594	24,368	5,774	31.1	21,638
Total	2,644,493	2,756,796	112,303	4.2	2,630,059
Adjustments:					
-1987 Attrition	*	(52,978)	(52,978)	(100.0)	*
-AL 5110	*	(2,944)	(2,944)	(100.0)	*
-FASB 87	*	9,113	9,113	100.0	*
-IntraLATA SPF to SLU	*	3,050	3,050	100.0	*
Total Revenues	2,644,493	2,713,037	68,544	2.6	2,630,059

(Red Figure)

*Reflected in appropriate revenue categories.

2. <u>Subscriber Station Revenues</u>

As noted from the above tabulation, subscriber station revenues consist of monthly service charges, service connection revenue, semi-public telephone revenue, total message charges, gross ZUM charges, and connecting company charges and credits. In the development of the monthly service charge revenues, both General and DRA used regression models of inward and outward movement to determine access lines for three groups: residence, business, and PBX. General utilized four independent variables consisting of local employment, short-term interest rates, several indicator variables, and the price of recurring and nonrecurring service. General then applied current rates to forecast the number of lines to derive the revenues. DRA developed historical trends of line in service and inward movement for the above three groups and developed two equations for each group. One equation was demand for customers and the other was demand for outward movement. In general, the demand for customers was based on monthly recurring and nonrecurring price and income figures and the demand for outward movement was based on building permits, the employment gain in the LA service area, density in the LA service area, and a set of seasonal indicator variables. Neither methodology appears unreasonable and it is noted from the above tabulation the difference between DRA and General estimates amounted to $10,827,000 or 2.5%. We will adopt as reasonable the DRA estimate for monthly service charge based on more recent data. General estimated 1988 service connection charges using a combination of its inward movement forecast and a single year 1984-1985 historical trend. General applied its inward forecast growth to service orders for first additional lines and a few other categories for both residence and business. General applied the historical trend 1984-85 in most other Item Of Service Codes (IOSC) categories. The staff estimated 1988 service connection revenue by starting with its 1986 to 1988 growth in inward movement estimated from its statistical models. These inward growth rates were computed to be 3.7% and 8.3% for residential and business respectively. DRA applied these growth rates directly to the IOSC first line category and for all other IOSCs categories. DRA weighted the inward growth rate by the ratio of the IOSC category specific 1985-1986 growth rate to the 1985-1986 growth rate for the first line category. DRA's estimate for service connection revenues was $66,336,000 or $5,100,000 (7.7%) less than General's estimated $71,436,000. As with the monthly service charge revenue, we will adopt DRA's estimate for service connection revenue as it is based on more recent data. The semi-public telephone revenue estimates of DRA and General differ by $19,000 or 0.3%. We will adopt DRA's estimate of $7 million for this category. General's estimate for total message charges was $116,131,000 or $2,731,000 (2.4%) more than DRA's estimate of $113,400,000. General used a revenue regression method for making its estimate based on a count of business lines (other than Centrex), the measured local service rate, and one seasonal variable. General used the forecast of business lines as a proxy for lines which fix local measured rates although in 1986 about 30% of the business lines were billed at flat rates and about 5% of the residential lines were billed at measured rates. DRA forecasted the total message charges as the product of forecasted units per line, the average revenue per unit in the last recorded year, and the forecasted number of lines for the forecast year. Starting in 1986, the total message charge revenue includes local directory assistance call revenue. DRA estimated the total message charges for test year 1988 as $97.2 million and the directory assistance revenue as $16.2 million, for a total of $113.4 million set forth above for total message charges. We will adopt DRA's estimate of $113.4 million as reasonable.

DRA's estimate for gross ZUM charges was $97,890,000 or $2,617,000 (2.7%) greater than General's estimate of $95,273,000.

General utilized a revenue regression forecast based on all in-service customer lines, ZUM rate, and a proxy variable for the recent expansion of ZUM calling area. DRA estimated the gross ZUM charges in the same manner it utilized for total message charges as described above. DRA's forecast of $97,890,000 appears reasonable and will be adopted for this proceeding.

Under a new ZUM settlement agreement between General and Pacific, which became effective on January 1, 1986, each company will "bill and keep" the revenue it receives for its originating ZUM Zones 2 and 3 traffic. Additionally this new settlement agreement requires both General and Pacific to pay each other for the termination of the other company's ZUM Zones 2 and 3 traffic. The net dollar amount of what General pays Pacific and that which Pacific pays General for the termination of ZUM Zones 2 and 3 traffic is referred to as connecting company charges and credits. DRA's estimate of General's 1988 connecting company charges and credits was $3,259,000 or $372,000 (11.4%) greater than General's estimate of $2,887,000. However, the effect of decreased access charges resulting from General's and Pacific's latest interLATA SPF to SLU AL filings, AL 5110 and AL 15325, respectively, results in General's connecting company charges and credits of $1,308,000, which we will adopt as reasonable for this proceeding.

3. Local Service Revenues

Local service revenues consist of public telephone revenue, local private line intrastate revenues, and other local service revenue. As with semi-public telephone revenues, General estimated the public telephone revenues on the basis of a revenue regression methodology and DRA estimated its public telephone revenue as a product of estimated public telephones in service times the calls per phone times the local phone call rate of 20¢ per call to derive its estimate. We will adopt DRA's estimate of $33,260,000 as reasonable.

General used a revenue regression to forecast 1988 revenues of $5.56 million for local private line revenues. The staff has analyzed the account of local private lines and noted that the number of private lines declined from 41,761 to 34,631 from the period September 1984 to September 1986 and that during the same period the revenue per line declined from $12.74 to $12.26. Applying these declining growth factors to mid-1986 data produced a forecast for the test year 1988 of 29,245 lines and a revenue of $11.20 a line, or a forecast of $3.9 million for 1988 revenues, which we will adopt as reasonable.

Other local service revenues are extended area service (EAS) and settlement revenues, which General and all independent telephone companies (ICO) who provide EAS receive from Pacific. For 1988, DRA estimates that General will receive $12,430,000 in EAS payments from Pacific as contrasted to General's estimate of $18,439,000. The EAS settlement ratio for ICOs is determined by Pacific's local exchange billings, expenses, and investments. EAS agreements allow each ICO to recover its expenses and to earn Pacific's exchange settlement rate of return on investment used to provide EAS. Pacific books the EAS payment to the ICOs as an expense while the ICOs account for such payment as revenues. Whenever a participating ICO is granted an increase or decrease in exchange rates, Pacific's EAS payment to that ICO is reduced or increased, respectively. The increase or decrease in Pacific's EAS payment to an ICO is determined by ICO's "revenue credit". Revenue credit reflects the level of EAS settlement revenues that flow from the ICO to Pacific and is a function of the ICO's exchange billings and the ratio of the total number of EAS calls to the total of all exchange calls (local plus EAS). In accordance with our adopted EAS settlement expenses, taxes, and investments, which are reflective of the exchange category, we will adopt as reasonable in this proceeding $16,310,000 for the other local service revenue.

4. Toll Service Revenues (IntraLATA)

IntraLATA toll service revenues consist of message toll and toll private line revenues. General's estimate for intrastate intraLATA toll revenues is based on moneys estimated to be received via a statewide "settlement" process administered by Pacific and participated in by all California ICOs. This settlement process allows each ICO to recover its actual expenses and to earn a return on its investment associated with the provision of intrastate intraLATA toll service. The settlement expenses and investments associated with message toll and toll private line services are allocated using a procedure known as "telephone cost separations" as contained in Part 67 of the FCC Rules and Regulations. The estimates of General's intrastate intraLATA toll service revenues are based on estimates of "industry billings" for the ICOs including Pacific and General. Additionally, the intraLATA toll service revenues for General are based on the relationship of General's settlement expenses, taxes, and plant investments to that of the industry. Based on our adopted intraLATA toll settlement expenses, taxes, and plant investments, the intraLATA toll service revenues are $822,393,000 which we will adopt as reasonable.

5. Access Revenues

Included in this category of access revenues are intrastate access revenues and interstate access revenues. Since revenues from interstate access charges do not directly affect intrastate results of operations, DRA agreed to use General's estimate of gross interstate access revenues of $504,244,000 for this results of operations analysis. This $504,244,000 figure includes $23,819,000 for interstate billing and collection services. DRA's estimate of intrastate access revenues is $242,583,000 including $26,675,000 as intrastate billing and collecting as compared to General's estimate of $279,231,000 including $20,253,000 of intrastate billing and collecting. The difference between these two estimates is $36,648,000 or 15.1%.

DRA estimated intrastate access service by dividing the service into five component parts consisting of (a) carrier common line, (b) switched access, (c) IEC (interexchange carriers) directory assistance, (d) special access, and (e) billing and collection. General's forecast of carrier common line revenue is $136,038,000 as compared to DRA's forecast of $90,981,000 which includes the effect of General's AL 5110 filing. The difference in the estimates is due to the differences in forecast of minutes of use (MOU) to be charged at the premium rate and the effect of AL 5110. General forecasts a decline in terminating out WATS conversation time from 3.119 minutes per call in 1985 to 2.927 minutes per call in 1988. DRA believes that this decline is insupportable, and we agree. Consequently, we will adopt DRA's estimate of 10,592,000 MOUs for non-premium and 2,339,613,000 MOUs for premium, as reasonable for this proceeding. We will also reflect the effect of AL 5110 and thereby adopt DRA's carrier common line revenue of $90,981,000 as reasonable for test year 1988.

General's estimate for switched access revenues is $100,679,000 as compared to DRA's estimate of $90,070,000, a difference of $10,609,000 or 11.8%. The component parts of the switched access category are intercept, line termination, local switching 1, local switching 2, common transport, and transport and RCs. The following tabulation compares General's and DRA's estimates, together with our adopted results:

Item	General	DRA	Adopted	Volumes
	(Dollars	in	Thousands)	(000 MOUs)
Intercept	$ 183	$ 183	$ 183	2,520,925
Line Termination	35,376	23,864	23,864	2,520,925
Local Switching 1	108	2,884	2,884	282,055
Local Switching 2	39,347	35,222	35,222	2,238,870
Common Transport	25,665	27,804	27,804	30,610,598/mi
Transport NRCs	0	113	113	--
Total	100,679	90,070	90,070	

As noted from the above tabulation, both DRA and General estimate the revenue for intercept at $183,000. We will adopt this figure as reasonable. The difference between General's and DRA's estimate of line termination revenues is $11,512,000 due primarily to the effect of General's AL 5110 SPF-to-SLU filing. We will adopt DRA's estimate.

According to the testimony of DRA witness Ting, General incorrectly charged the local switching rate for all premium minutes of use, whether Feature Groups A, B, C, or D were involved which is contrary to the tariffs which provide that the local switching 2 rate is applicable only to Feature Groups C and D. All Feature Group A and B usages are to be charged to local switching 1 rate whether premium or nonpremium. We will adopt as reasonable DRA's estimates of local switching 1 rate and local switching 2 rate revenues.

In the forecast of common transport revenues, General used an average transport distance from an analysis of its interstate call accounting data which presumes that average interstate and intrastate transport distances are the same. We are not persuaded this is a logical conclusion and will adopt as reasonable DRA's common transport estimate of $27,804,000. General included no revenues for transport NRCs as contrasted to DRA's relatively small estimate of $113,000. We will adopt DRA's estimate.

The total of the above component parts of switched access revenues is $90,070,000. DRA's estimate of IEC directory assistance revenues is $1,264,000 as compared to General's estimate of $1,260,000. We will adopt DRA's estimate as reasonable.

General's forecast of test year special access revenues is $21,519,000 as compared to DRA's estimate of $33,210,000, a difference of $11,691,000 or 35.2%. Special access revenues include, among other items, recurring charges for special access lines and special transport, associated nonrecurring charges, and various recurring surcharges. Approximately $9 million of the $12 million differential in estimates pertains to the treatment of WATS access lines. DRA applied a special access surcharge of $25 per line per month and other tariff surcharges to recover revenue requirements for message station equipment and inside wire whereas General did not include such surcharges in its revenue estimate. According to DRA witness Ting, D.85-06-115 changed the treatment of closed end WATS to reflect "direct assignment". For revenue purposes, the fundamental effect of such a change was to reclassify WATS access lines used in interLATA service as special access lines and to exclude closed end WATS usage from carrier common line charges.

In their briefs, both General and AT&T argue that the application of the special access surcharge of $25 per line per month is inappropriate. According to General, it does not provide any WATS lines out of its access tariff Schedule Cal. P.U.C. No. C-1 and all intrastate WATS lines are currently provided from General's local exchange tariff Schedule Cal. P.U.C. No. B3 and are not subject to the charge in its access tariffs. AT&T noted that the $25 access surcharge would only be booked as access revenue if a customer purchased an interLATA-only WATS line and there are currently no such customers. We are persuaded that General and AT&T are correct and will reduce DRA's estimate by $9 million to $24,210,000 to reflect elimination of the special access surcharge.

According to DRA witness Ting, General's original application projected a test volume of 17,404 WATS access lines whereas a more detailed response to a staff data request projected test year volumes of approximately 19,040 WATS access lines. The original projection applies an annual growth rate of less than 5% for the period from year-end 1986 to mid-year 1988 whereas the annual growth rate for the immediately preceding year was 32.2%. In view of this, DRA asserts the original forecast is unreasonable and the revised quantity should be adopted. We agree and will adopt DRA's higher estimate as reasonable for this proceeding.

Witness Ting further alleges that General used an incorrect method of pricing out General's forecasted special access volume, omitted all the forecast volumes for special access lines and special transport other than voice band in its priceout, incorrectly reflected the relationship of 4-wire voice band rates to 2-wire voice band rates, and omitted revenues from special access nonrecurring charges totaling approximately $1 million. As previously stated, we will adopt DRA's estimate of $33,210,000 decreased by $9 million to $24,210,000 for special access revenues.

Billing and collection revenues consist primarily of message recording, message processing, and billing processing and collection services for IECs. General's forecast of billing and collection revenues is $20,253,000 as contrasted to DRA's estimate of $26,675,000, a difference of $6,422,000 or 24.1%. The major difference in the two estimates derive primarily from General's forecasting a 15 to 20% drop in message recording and message processing volumes as compared to DRA's forecast of increases similar to those of AT&T's switched access volume message volumes, and timing differences in the prospective takeback of WATS billing function by AT&T-C. (General assumes takeback as of January 1, 1988 whereas DRA views takeback as highly speculative at this point.) DRA's position appears well taken and we will adopt as reasonable for this proceeding DRA's estimate of billing and collection of revenues for test year 1988 of $26,675,000.

Our adopted intrastate access revenue estimates discussed above are summarized as follows:

	($ 000)
Carrier common line	$ 90,981
Switched access	90,070
IEC directory assistance	1,264
Special access	24,210
Intrastate Billing & Collection	26,675
Intrastate Access	$233,200

Miscellaneous revenues consist of telegraph commissions, directory revenues, rent revenues, general service and license revenues, other miscellaneous revenues, intrastate billing and collecting, and interstate billing and collecting. DRA's 1988 test year estimate for miscellaneous revenues is $322,670,000 as compared to General's estimate of $262,770,000, a difference of $59,990,000 or 18.6%. In addition, DRA included in miscellaneous revenues the gain on the sale of property of $10,490,000, making a total difference in miscellaneous revenues estimate of $70,390,000 or 21.1%. As noted in the previous tabulation, both General and DRA estimated telegraph commissions to be $19,000, rent revenues to be $1,804,000, and general service and licensing revenues to be $1,133,000. We will adopt these amounts as reasonable.

In 1985, General received $176 million in Directory Advertising revenue, nearly double the $93 million received in 1981. Using a revenue regression based on the product of the number of business lines (excluding Centrex) and a price proxy for Directory Advertising, General estimated the 1988 revenue from Directory Advertising to be $231.5 million. This estimate was reduced $33,188,000 to $198,292,000 for General's comparison exhibit. According to the testimony of DRA witness Berry, a properly specified regression model is a model of the demand for directory advertising services, including such variables as a proper price index and the price of competing services, estimates of the sales volumes of General customers who use the directory advertising service, and a measure of the competitiveness of the retail market. This witness further testified that he estimated the demand for directory advertising for the periods 1975-1986 and 1983-1986 using a model including simple proxies for local sales revenues as measured by taxable sales in the six county Southern California area served by General and a measure of one aspect of market structure. The longer term model forecasted a revenue of $205 million and the shorter term model forecasted a revenue of

$222 million. We will adopt the $205 million estimate as reasonable for this proceeding.

General's estimate of Other Miscellaneous Revenues is $17,450,000 as contrasted to DRA's estimate of $37,740,000. The difference is DRA's inclusion of its proposed GTEL adjustment of $18,290,000 and its proposed GTE Telecom adjustment of $2 million with its miscellaneous revenue estimate of $17,450,000. As previously discussed, we disallowed the $2 million GTE Telecom adjustment, and allowed only $6,081,000 of the recommended GTEL adjustment of $18,290,000. Consequently we will adopt as reasonable, for miscellaneous revenues, the amount of $23,531,000 equal to the original estimate of $17,450,000 plus the allowed $6,081,000 GTEL adjustment.

As previously discussed, we are adopting a miscellaneous revenue component item of $4,485,000 a year for a three-year period, i.e. 1988, 1989, and 1990, to reflect a gain on the sale of property.

The application of the surcharge rates authorized by D.87-12-070 dated December 22, 1987 as revised by AL 5125 effective April 10, 1988 of 4.43% for intraLATA toll, 7.19% for exchange service, and a negative 2.96% for access service to our adopted billings yields a surcharge revenue of $74,730,000, which we will adopt as reasonable for this proceeding.

Uncollectible revenues include amounts of revenues which have proved impractical to collect because subscribers either cannot be located by the utility or the cost of locating such subscribers exceeded the revenues that would be recovered if they were located. General's estimate of uncollectibles for test year 1988 of $24.368 million was presented into evidence by one of its senior economists, Luigi F. Pinna, and DRA's estimate of uncollectibles of $20,502,000 was presented into evidence by one of its program and project supervisors, Kevin P. Coughlan. General's estimate was based on a rate of 1.40%; DRA's estimate was based on

working condition. Included also in upkeep is the cost for locating and clearing trouble in these facilities and the cost of power for transmitting traffic and operating supervisory signals. Moves and changes mainly consist of cost of relocating, rearranging, or replacing minor units of outside plant equipment and central office equipment. DRA's test year maintenance expense estimate is $412,062,000, which is $79,614,000 or 19.3% less than General's estimate of $491,676,000. The major reasons for the difference in the estimated amounts are the use of different methodologies, different productivity factors, different labor escalation rates, different nonlabor escalation rates, different workload volumes, and the availability to DRA of later historical data. The tabulation that follows lists by accounts DRA's and General's estimates, together with our adopted results. The bases for the adopted results are set forth in the ensuing paragraphs.

Maintenance Expenses

Acc. No.	Item	DRA	General	General Exceeds DRA Amount	General Exceeds DRA Percent	Adopted
				(Thousands of Dollars)		
602	Outside Plant	$183,427	$204,525	$21,098	11.5%	$194,484
603	Test Desk Work	48,928	57,999	9,071	18.5	53,609
604	Central Office	120,201	139,537	19,336	16.1	121,610
605	Station Equip.	17,941	11,079	(6,862)	(38.2)	18,157
606	Bldgs. & Grounds	14,554	17,402	2,848	19.6	17,012
607	Public Tel. Equip.	7,527	8,531	1,004	13.3	7,620
610	Transm. Power	18,678	19,333	655	3.5	19,333
612	Other Maint. Exp.	1,212	1,686	474	39.1	1,449
	Subtotal					433,274
	GTED	(406)		406		(297)
	Inside Wiring	a/	31,584	31,584		
	Total	412,062	491,676	79,614	19.3	432,977

(Red Figure)

a/ $12,978,000 for inside wiring included in Account 605.

a rate of 1.0%. In response to a DRA data request, General submitted a later forecast of $23.2 million which was based on a rate of 1.31%. According to the record, the uncollectible rate for the year 1984 was 2.2%, for 1985 was 1.9%, and the 11 months recorded and 1 month estimated for 1986 was 1.7%. Both General and DRA agreed that special consideration should be given to the implementation of a late payment charge (LPC) and the centralized credit check system (CCCS) in arriving at the appropriate uncollectible rate. DRA witness Coughlan contends that General's estimating model cannot accurately capture the effects of the CCCS and the LPC as these two programs only recently became effective. On this basis this witness believes the staff estimate is a reasonable expectation of what uncollectibles should be for the test year considering the downward trend of uncollectibles in General's own forecast. We agree that the CCCS and LPC programs should have the effect of reducing the rate of uncollectibles, but we believe General's estimate has understated the effect whereas DRA's estimate has overstated the effect. Consequently we will adopt as reasonable for this proceeding an uncollectible rate of 1.2%. Applying this rate to our adopted revenue figures results in an uncollectible amount of $21,638,000 which we will adopt as reasonable.

F. Maintenance Expense

Maintenance expenses are comprised of cost for labor, material, and administrative charges incurred in the repair and rearrangement of operating plant. General records maintenance expenses both in accordance with the FCC Uniform System of Accounts as adopted by this Commission and in accordance with its own accounting system where the accounts are designated with a "m" code for "moves and changes" and "r" code for "repairs". Repairs consist of charges for routine repairs and General's upkeep to outside plant facilities, inside wiring, central office equipment, and buildings and grounds, to maintain them in good physical

Senior Utilities Engineer Hassan Mirza was responsible for the testimony on outside plant maintenance expenses (Accounts 602 and 603) while Senior Utilities Engineer Melvin Hodges was responsible for the remainder of the expense accounts set forth in this section. General's Ventura County Division Manager, Jack F. Moore, presented rebuttal testimony regarding DRA witness Mirza's recommended disallowance of $1,940,000 for additional software processing costs.

Repairs of outside plant (OSP) are set forth in Account 602 and include the cost of labor and material used in the routine maintenance and upkeep and preventive maintenance of outside plant equipment. It also includes the cost of replacing minor defective OSP items. General's estimate for OSP repair is $91,511,000, which is $10,181,000 or 12.5% over DRA's estimate of $81,330,000. General's estimate for OSP repair basic labor expense is $36,925,000 as compared to DRA's estimate of $32,033,000. The main reason for the $4,892,000 differential, according to the testimony of witness Mirza, is the adjustment of the labor productivity factor for the disallowance of the noise mitigation program work force. DRA recommends that the noise mitigation program be completed, but the expenses of this program be disallowed for test year 1988 so that the ratepayers are not asked to continue to pay for poor quality work that should have been done right the first time and for the lack of overall control of the program by General.

According to the record, the noise mitigation program was fully operational in January 1987 and scheduled to be gradually reduced with about 35% of the work force left in the program by July 1989. The 1986 productivity level was slightly over 8.0 hours per outside plant trouble report. The elimination of the 211,000 hours for the noise mitigation program charged in 1986 would raise the productivity to 7.33 hours per outside plant trouble report. DRA used this productivity figure in estimating the basic labor expense for test year 1988. It is noted that the best productivity experienced by General for the period 1982 through 1986 was in the year 1983 where it was slightly under 7.8. Under these circumstances, the utilization of a 7.33 productivity labor level appears excessive. We will utilize a productivity factor of 7.8, which is the equivalent of a reduction of approximately 30% in the noise mitigation program. This translates into a reduction of approximately $1.5 million, which we will add to DRA's estimate of $32,033,000 to yield a figure of $33,533,000. We will increase this figure to $34,400,000 to reflect our previously discussed adopted labor escalation rate and find this figure to be reasonable for this proceeding.

General's estimate for OSP repair plant overhead is $17,949,000 as contrasted to DRA's estimate of $15,098,000. According to witness Mirza, the main reason for the $2,851,000 difference is staff's lower basic labor expense estimate and different methodology. Consistent with our adopted $34,400,000 basic labor expense, we will adopt plant overhead expense of $16,200,000.

General's estimate for OSP repair minor material is $9,334,000 as compared to the staff's estimate of $5,073,000. According to witness Mirza, the main reason for the $4,261,000 differential is the staff's lower basic level expense estimate and different methodology. The staff's estimate is based on the average of 1985 and 1986 historical ratios of minor material to basic labor adjusted for escalation rates. We will adopt DRA's estimate of $5,073,000 adjusted to reflect our adopted basic labor expense and our previously discussed nonlabor escalation rates or $5,450,000.

Adding the above adjustments of $2,367,000 to basic labor, $1,102,000 to overhead, and $377,000 for minor materials to the staff's estimate of $81,330,000 for repairs, we derive a figure of $85,176,000 for repairs which we will adopt as reasonable for this proceeding.

OSP moves and changes consist of the labor and material expenses of changes and rearrangements occurred while working on outside plant. It includes the moves, changes, disconnects, and reconnects associated with the drop wire, protectors, and terminals.

General's estimate for OSP moves and changes is \$113,014,000 which is \$10,917,000 or 10.7% over DRA's estimate of \$102,097,000. According to the testimony of DRA witness Mirza, the main reasons for the \$10,917,000 difference are DRA's lower basic labor expense, service order assignments, and plant overhead. General's estimate for OSP moves and changes basic labor expense is \$28,639,000 which is \$5,042,000 or 21.4% over DRA's estimate of \$23,597,000. According to the testimony of DRA witness Mirza, the basic labor expense for OSP moves and changes relates to two prime factors, namely, the outside plant construction budget and customer moves. In accordance with our previously discussed labor escalation factors and our subsequently discussed adopted gross additions, we will increase DRA's basic labor expense by \$3,152,000 to \$26,749,000. As previously discussed, the customer movement estimate set forth by DRA was adopted and we will therefore not adjust that portion of the OSP moves and changes basic labor expense.

Service order assignment costs consist of the installation activities relating to providing service to customers and it is affected by service orders relating to inter-customer movement, customer calling orders, etc. General's estimate for service order assignment is \$42,850,000, which is \$4,325,000 or 11.3% over DRA's estimate of \$38,525,000. According to the record, DRA examined the productivity measurements for service order assignment functions for the years 1981 through 1986 and noted that General had its best productivity level in 1983. The DRA witness could see no valid reason for the decrease in productivity level in the 1984 to 1985 time frame and therefore he used a 1983 productivity level for test year 1988 for nonspecial service order assignment hours. For the special service hours, DRA examined General's productivity level as measured by special service hours per serving links for the period 1984 through 1986. The productivity measurements prior to 1984 were not examined because General did not have the necessary historical data on serving links. For the periods studied, General has shown a constant improvement in productivity. In addition, it will have improvement from its switch access system (SAS), which provides remote test access to special service circuits and thereby improves the ability of the utility to perform the maintenance operation of this special service circuits. It is estimated that the test year maintenance level reduction from the SAS is 125,000 hours. For the period 1981 through 1985, the average hour per service order was .380. We will use this amount for the computation of the service order assignment expense for the nonspecial service order assignment hours. We will adopt DRA's expenses associated with the special service hour portion of the expense. Under these circumstances, we find the special order assignment expense of $42,281,000 is reasonable and will adopt it for this proceeding.

General's estimate for plant overhead is $15,142,000, which is $4,265,000 or 39.2% above DRA's estimate of $10,877,000. According to the record, the main reasons for the $4,265,000 difference are lower staff basic labor expense estimate and different methodology used. We will adopt DRA's estimate of $10,877,000 increased by $303,000 to reflect our previously discussed adopted labor and nonlabor escalation factors.

In accordance with our above discussion, our adopted Account 602-Outside Plant Maintenance expense amount is $194,484,000, consisting of $85,176,000 repair and $109,308,000 outside plant moves and changes.

General's estimate of Account 603-Test Desk Work is $57,999,000, which is $9,071,000 or 18.5% over DRA's estimate of

$48,928,000. According to the record, the main reasons for the $9,071,000 difference are labor overhead, payment for usage of rental of computer equipment, and plant overhead. General's estimate of test desk work labor overhead is $17,540,000, which is $1,842,000 or 11.7% over DRA's estimate of $15,698,000. DRA's estimate is based on the average of 1985 and 1986 historical ratios of labor overhead to basic labor expense adjusted for labor escalation factors for 1987 and 1988. We will adopt DRA's estimate adjusted for our previously discussed adopted labor escalation factors to arrive at a figure of $16,200,000 for labor overhead. General included $2,968,000 for lease payments for computer and related equipment and $1,940,000 for additional software processing costs. DRA's investigation indicated that about $1,967,000 for part of the computer equipment rental would no longer be required since the utility had purchased the equipment in 1986. According to the testimony, General was not able to show any economic benefits for the $1,940,000 additional software processing costs. According to the rebuttal testimony of General's witness Jack F. Moore, this $1,940,000 results from increased transactions in General's advance service order system (ASOS) and trouble administration system (TAS). This witness further testified that increased transactions in TAS are the result of new system release installed in 1985 in which trouble reports for all special service private lines and line circuits are now entered into TAS. Another important feature of the release is the creation of daily, weekly, and monthly output reports. General's position in regard to this $1,940,000 software cost appears reasonable and will be adopted. Consequently we will allow DRA's disallowance of $1,967,000 lease payment but not the $1,940,000 charge for additional software processing cost.

General's estimate of plant overhead is $9,832,000, which is $3,937,000 or 66.8% over DRA's estimate of $5,895,000. According to the record, DRA's estimate is based on the average of

1985 and 1986 historical ratios of plant overhead to basic labor expense adjusted for escalation rates. We will adopt DRA's methodology and apply it to our previously discussed adopted Account 603 figures to derive a plant overhead figure of $6,176,000.

In accordance with the above discussion, the total Account 603 adopted expense is $53,609,000.

General's estimate for Account 604-Central Office Equipment is $139,537,000 or $19,336,000 (16.1%) greater than DRA's estimate of $120,201,000. The account consists of the total of central office equipment moves and changes, central office equipment repairs, and repair of distributing frame work. The major difference in the estimates is due to DRA's lower estimate for the utility's Account R-20-Central Office Equipment Repairs. The main reason for DRA's lower estimate for Account R-20 is the use by DRA of a better productivity factor. DRA witness Hodges testified that the better productivity factor used by him for his estimates resulted from the continued effect of the utility's ongoing central office modernization program converting antiquated, very labor-intensive mechanical SxS central office equipment to state-of-the-art very labor-efficient electronic digital central office equipment. This witness further testified that he took into consideration the effect of two other plant operational improvement programs known as switching services work allocation procedure (SSWAP) and total network administration and control (TNAC). These programs are expected to contribute strongly to productivity improvements in General's overall switching service operation beginning in 1988. This position appears reasonable and we will adopt DRA's estimate of $120,201,000 for Account 604 increased by $1,409,000 to $121,610,000 to reflect our previously discussed adopted escalation factors.

FCC Account 605-Station Equipment includes General's Accounts M43-Station Apparatus Official Moves and Changes, R43-Station Apparatus Official Repairs, M44-Station Apparatus Repair Shops, M45-Station Apparatus Connections (IW) Moves and Changes, and R45-Station Apparatus Connections (IW) Repairs. General's estimate excluding inside wiring cost is $11,079,000, which is $6,116,000 less than DRA's estimate of $17,941,000. The major difference for the non-inside wire portion of the account is DRA's lower estimate of the utility's Account M44-Station Apparatus Repair Shops. This account is directly affected by the deregulation of terminal equipment which was to be 100% completed by January 1, 1988. As of that date, the only equipment remaining in the regulated environment will be that equipment actually used by the utility conducting the regulated operations known as company official terminal equipment. According to the testimony of DRA witness Hodges, the effect of the deregulation would be to decrease station apparatus repair shop activity by 60% in 1987 and 1988 as compared to 1986. His estimate reflects this reduction as contrasted to General's estimate which did not. We will adopt DRA's estimate of $4,963,000 for the non-inside wiring portion of this account increased by $216,000 to $5,179,000 to reflect our previously adopted escalation factors. DRA's estimate of inside wiring cost is $12,978,000 while General's is $31,584,000. We will adopt as reasonable for this proceeding DRA's estimate of $12,978,000 for inside wiring costs for a total for FCC Account 605-Station Equipment amount of $18,157,000.

While we adopt inside wire maintenance expenses and revenues in this decision, we also have OII 84 outstanding to reconcile the revenue and expense effects of inside wire maintenance detariffing as ordered by the FCC. General and other local exchange telephone companies have previously been ordered in OII 84 to track actual inside wire maintenance revenues and expenses; the expenses are contained in memorandum accounts, and rates are subject to refund to the extent necessary to make a later adjustment (if necessary) for excess revenues. Therefore, both shareholders and ratepayers are fully protected for current impacts as they may be reflected in our final reconciliation of the revenues and expenses.

In this light, it is apparent that the revenue and expense levels adopted here for inside wire maintenance are simply interim amounts subject to later retroactive refinement. However, these adopted revenue and expense levels should be identified precisely and tracked along with the actual levels so that this reconciliation can be accurate. We will direct CACD to confer with General and DRA (and any other parties who are interested) to identify for tracking purposes the exact amounts adopted in this decision for inside wire maintenance as well as the accounts in which they are found. This process should begin within 60 days of this decision.

General's estimate for FCC Account 606-Buildings and Grounds is $17,402,000 which is $2,848,000 or 19.6% greater than DRA's estimate of $14,554,000. FCC Account 606 consists of two general accounts, M12-Land and Buildings Moves and Changes and R12-Land and Buildings Repairs. According to the testimony of DRA witness Hodges, the primary difference for DRA's lower estimate for both accounts M12 and R12 is the effect of historical adjustments to these accounts as recommended by staff auditor, S. McCarthy. As previously discussed, we will amortize the corporate headquarters improvements carried in Subaccount M12 of $1,074,000 for 1985 and $300,000 for 1986 over a three-year period. The result of this three-year amortization will be to increase the M12 account by $458,000. As previously discussed, we will allow $2,000,000 for test year toxic waste cleanup. We will therefore adopt $17,012,000 for Account 606 expense, which is equal to DRA's estimate of $14,554,000 plus the above-discussed two increases totaling approximately $2,458,000

General's estimate for FCC Account 607-Public Telephone Equipment is $8,531,000 which is $1,004,000 or 13.3% higher than DRA's estimate of $7,527,000. According to the testimony of witness Hodges, the major difference in this account is due to DRA's lower estimate for the utility's Account R47-Public Telephone Equipment Repairs because of the use of a better productivity for test year 1988 than was used by General. We will adopt DRA's estimate of $7,527,000 for this account increased by $93,000 to $7,620,000 to reflect previously discussed escalation factors.

General's estimate of FCC Account 610-Maintenance of Transmission Towers is $19,333,000 which is $655,000 or 3.5% higher than DRA's estimate of $18,678,000. The difference in the estimates for this account is due to DRA's use of a lower test year estimate of kilowatt-hours of usage than used by General. We will adopt General's estimate of $19,333,000 for this account.
General's estimate for FCC Account 612-Other Maintenance Expense is $1,686,000 or $474,000 or 39.1% greater than DRA's estimate of $1,212,000. DRA used a better productivity factor than did General in the preparation of its estimates. We will adopt as reasonable for this account the amount of $1,449,000, the average of the two estimates.

G. Traffic Expenses

Traffic expenses consist primarily of the salaries, wages, and administrative costs incurred in the handling of telephone calls by switchboard operators and the costs associated with administering the use and performance of the switching network. Testimony on traffic expenses was presented on behalf of DRA by Utilities Engineer M. J. Vannucchi and rebuttal testimony was presented by the project planning manager of General's operator service staff, Thena Pettey. The tabulation below compares DRA's estimates with General's estimates, together with our adopted results. The basis for the adopted results are set forth in the ensuing paragraphs.

Traffic Expenses
(Thousands of Dollars)

Acc. No.	Item	DRA	General	Amount	Percent	Adopted
621	Genrl. Traffic Supvr.	$ 6,927	$ 7,984	$ 1,057	15.3	$ 7,047
622	Customer Instruction	622	622	0	0.0	622
624	Operator Wages	40,834	50,271	9,437	23.1	43,628
627	Oper. Employ. & Train	1,167	1,604	437	37.4	1,244
	Misc. CO Expense	13,082	14,082	1,000	7.6	13,082
	Subtotal	62,632	74,563	11,931	18.8	65,623
	GTED Adjustment	(1,999)	0	1,999	100.0	(1,999)
	Total	60,633	74,563	13,830	23.0	63,624

(Red Figure)

Testimony presented on behalf of DRA indicated that:

1. It was standard procedure for DRA to calculate General's 1988 test year estimated expense for management and nonmanagement labor. The procedure involved using 1985 as an employee salary base year and then calculating the 1988 labor using DRA's wage escalation factors.

2. DRA adjusted those areas impacted by the reductions in operator force levels by summing up all expenses in service related to the office force levels and applying the

percentage reduction of operators to achieve an appropriate expense estimate.

3. The length of time spent handling calls, commonly referred to as actual work time (AWT), is the actual seconds per call an operator spends in handling calls.

4. General provided DRA with 1988 projected AWTs for directory assistance on a sector-by-sector basis. The sectors are the five areas covered by General's automatic call distributors (ACDs).

5. The projected AWTs for the five ACDs range from a low of 23.5 seconds to a high of 25 seconds.

6. The issue of AWTs for General's directory assistance was also examined in (I&S) C.86-06-004. In Exhibit 12, sponsored in the above case, an updated version of the budget for operator services produced AWTs ranging from a low of 19.8 to a high of 21.4 seconds.

7. General attributes the reduction in AWTs to new system enhancements including standardized data base, NPA recording, and the personal response unit. DRA selected 19.8 seconds as the AWT for use in computing General's directory assistance costs.

8. In support of this selection of 19.8 seconds, DRA quoted from page 14 of General's concurrent opening brief in C.86-06-004 which stated: "In summary, General believes that the equipment it has installed to provide the proposed service will enable it to provide DA service that is superior to that currently available for Pacific Bell."

9. For the Van Nuys area in 1986, Pacific Bell, without the added feature of the personal response unit, had a recorded AWT of 18.7 seconds. General, in its best showing, had projected AWT of 19.8 seconds.

10. General has organized its toll operations into three sectors: namely, Long Beach, Santa Monica, and Ontario.

11. For the three sectors, the projected 1988 AWTs provided by General were 42.5, 41.5, and 39.5 seconds, respectively. The staff considers these figures to be high.

12. The computed AWTs for three domestic General Telephone Operating Companies (GTOCS) using Automatic Electric (AE) Traffic Service Position System (AE TSPS) range from 30.7 to 36.0 seconds considerably lower than General's projected AWTs for Long Beach, Santa Monica, and Ontario.

13. Because DRA feels that General's 1988 projected AWTs for toll represented inefficient operator operations, it adopted an AWT of 34 seconds for General's TSPS operators.

14. Included in FCC Accounts 626, 629-635 are expenses involved in contractual agreements with vendors who provide maintenance and facilities management for various traffic hardware and contract charges from Pacific for providing General with the data base for the 213/818, 714/616, and 805 NPAs. In addition, General is claiming expense for the same traffic data base provided by an outside vendor to eliminate the contract with Pacific. A review of the expenses revealed that Pacific's cost is 50% less than that of the other vendor and DRA can find no logic for General contracting a data base for double the amount of current costs. On this basis, DRA is disallowing the projected cost of a new data base. For FCC Accounts 626, 629-635, General has requested $14,082,000. DRA is recommending $13,082,000.

15. The percentage reduction in the number of operators caused by the use of shorter AWTs by DRA was the primary factor applied to General's estimates by traffic expense

account to derive DRA's projected 1988 test year results.

Testimony and/or rebuttal testimony presented on behalf of General indicated that:

1. General modified its AWT for directory assistance operators and the expense levels that flow from those average AWTs to reflect the data submitted in I&S C.86-06-004.

2. The reduction in AWTs results in reduced employee levels for 1988 of 180 hourly and seven management employees. Using a pricing methodology consistent with the submittal in C.86-06-004 results in a reduction of FCC Account 624 for operator wages from $54,722,000 to $50,548,000, a reduction in FCC Account 672-Relief and Pensions from $165,272,000 to $164,102,000, and a reduction in FCC Account 307-Operating Taxes Other Than Federal Income Taxes from $45,975,000 to $45,625,000.

3. The overall AWT that General has projected for its directory assistance service in 1988 based on the above-revised estimates is 20.4 seconds.

4. The 20.4 AWT was developed using actual AWTs for ACDs 1 through 4 and adjusting them to reflect the impact in anticipated savings resulting from the installation of personalized response system (PRN) and the NPA recordings in ACDs 1, 2, and 3.

5. The AWTs can vary between ACDs due to the mix of call types, the fact that some ACDs handle local 411 traffic only while other ACDs handle intra- and interstate "555" traffic as well as 411 calls, and the effect of employee seniority and job experience on ACD AWTs.

6. The recorded AWT for Pacific's Van Nuys sector of 18.7 seconds cannot be used to support DRA's adopted 19.8 second AWT because the Van Nuys sector of Pacific is

not representative of the entire directory assistance service provided by General.

7. Another difference between General and Pacific is General's DA operators providing service in the 818/213 and 619/714 areas have access to dual data bases which means they receive calls from and provide listings for more than one NPA or area code as contrasted to Pacific, which does not utilize dual data bases at any of its DA locations.

8. Recorded results indicate that the AWTs between toll sectors have historically been different which is the basis for General projecting discrete AWTs for each sector, namely 42.5 seconds for Long Beach, 41.5 seconds for Santa Monica, and 39.5 seconds for Ontario.

9. The factors which impact directory assistance AWTs also impact TSPS AWTs.

10. There are no other General GTOCs faced with the challenges and complexities of providing toll operator assistance that exist in California. It is therefore inappropriate to make comparisons between California and other GTOCs because of the many differences between their TSPS operations.

11. All three sectors of General's TSPS service handle calls from multiple LATAs and multiple NPAs. The LATA boundaries are not aligned with NPA boundaries which require specialized dialing instructions and explanations to customers. General's TSPS operators must determine the LATA of the calls as well as the caller and calling NPAs before appropriate dialing instructions and explanations of rates can be determined.

12. General is in the midst of equal access conversion which means that its operators must also determine when interexchange carrier service is required.

13. The above variable simply do not exist in any other GTOC where there is TSPS operators. Because of this difference in operating conditions, it is unreasonable to assume that General's AWTs should be the same as that achieved by other GTOCs.

14. The three GTOCs surveyed by DRA were General Telephone Company of the Northwest, General Telephone Company of the Southwest, and General Telephone Company of Florida. The Florida company is the most similar in size, equipment compatibility, and call volumes to General of the three GTOCs surveyed.

15. Even though the Florida company's size and more metropolitan service area make it most similar to General, all of Florida's customers call from only one NPA within the same LATA. This means that its call-handling decisions are much less complex than those faced by General's TSPS operators.

16. When a customer in Florida requires a coin refund, the TSPS operator passes the customer to a coin refund center operator whereas General's TSPS operators handle coin refund calls in their entirety.

17. Another difference is General's TSPS operators create manual tickets to record credit information and verifications/interruptions charges where in Florida these functions have been automated.

18. In the opinion of this witness, these differences invalidate DRA's utilization of the AWT of the Florida utility.

In its brief, Pacific argues that:

1. One of the most significant measures of the efficiency of DA service is the AWT reflected by the operators providing the service.

2. General's AWT has always been and remains higher than that provided by Pacific as indicated by a statewide AWT for Pacific of 19.3 seconds as compared to General's 20.4 seconds.

3. General did grossly understate its AWT in (I&S) C.86-06-004 and did not correct its inflated AWT showing in this rate proceeding until after the staff report was prepared.

4. General admits that interLATA DA service takes longer to provide than local 411 DA service.

It should be noted from the tabulation of traffic expenses that Account 624-Operator Wages accounts for approximately two-thirds of the total traffic expenses. Furthermore, it is apparent from the record that the magnitude of operator wages impacts to a large degree the other traffic expense accounts. Under these circumstances, DRA's methodology of computing traffic expenses by applying a percentage ratio based on the number of operators to General's total estimated amounts with other adjustments does not appear unreasonable. Consequently we will adopt DRA's methodology in deriving our adopted figure for traffic expenses.

We have recounted the points asserted by DRA and General in support of their respective estimates of AWT for ACD-served installations. What the above description does not convey in itself is the difficulty General's rebuttal witness had in attempting to supply relevant facts that might have cast doubt on DRA's comparative analysis. Accordingly, we will adopt DRA's AWT of 19.8 seconds.

While we are not persuaded that DRA's 34 second AWT figure is reasonable for General's three TSPSs, the times estimated by General of 42.5 seconds for Long Beach, 41.5 seconds for Santa Monica, and 39.5 seconds for Ontario impress us as being somewhat high. Consequently, to reflect the inefficiencies of manual handling we will adopt as reasonable for this proceeding AWTs of 1.5 seconds less or 41 seconds for Long Beach, 40 seconds for Santa Monica, and 38.0 seconds for Ontario. Substituting the above-adopted AWTs in DRA's computations derive a number of operators of 1,628 which we will use for our computations of the traffic expenses.

Using 1,628 operators and the DRA methodology for computing expenses result in an expense allowance for Account 621-Traffic Expenses of $7,047,000, Account 622-Customer Instruction of $622,000, Account 624-Operator Wages of $43,628,000, Account 627-Operator Employee And Training of $1,244,000, and the composite of Account 626, 629-35-Miscellaneous an amount of $13,082,000.

The above figures reflect our adopted labor escalation figures.

The total of the above figures is $65,623,000. We will decrease this by $1,999,000 to $63,624,000 to reflect our previously discussed GTED adjustment.

H. <u>Commercial Expenses</u>

Commercial expenses are comprised of salaries, wages, and administrative costs for handling customer service order contracts and the collection of billings, the preparation and distribution of telephone directories, marketing and sales functions including advertising, developing, and filing tariff schedules and other regulatory matters, and intercompany relations and settlements. DRA's presentation was made by Public Utility Regulatory Program Specialist II Marshall B. Enderby and rebuttal testimony was presented on behalf of General by its Ventura County Division Manager Jack F. Moore, by the Manager of Strategy Development of GTE Service Corporation Gabriel Sidhom, by General's Director of Access Services Lou Culkin, and its Manager of Advertising and

Promotions Michelle Shibuya. General's estimate for commercial expenses was $271,594,000 and exceeded DRA's estimate of $240,198,000 by $31,396,000 or 13.1%. The following tabulation sets forth DRA's estimates and General's estimates, together with our adopted results:

Commercial Expenses

Acct. No.	Item	DRA	General	General Exceeds Staff Amount	General Exceeds Staff Percent	Adopted
			(Thousands of Dollars)			
640	Gen'l Comm. Admin.	$ 9,498	$ 10,640	$ 1,142	12.0	$ 9,687
642	Advertising	2,520	14,795	12,275	487.1	11,415
643	Sales Expense	19,603	27,237	7,634	38.9	26,045
644	Connect. Co. Relations	2,486	2,575	89	3.6	2,529
645	Local Commercial Operations	112,785	124,551	11,766	10.4	124,000
648	Public Phone Comm.	3,605	3,605	0	0.0	3,605
649	Directory Expenses	101,348	87,560	(13,788)	(13.6)	90,760
	Inside Wire	0	4,762	4,762	0.0	0
	GTED Adj.	(2,488)	0	2,488	(100.0)	(1,841)
	Subtotal	249,357	275,725	26,368	10.6	266,200
	Directory Company	(9,159)	(4,131)	5,028	54.9	(9,001)
		240,198	271,594	31,396	13.1	257,207

(Red Figure)

General's estimate of FCC Account 640-General, Commercial, Administration was $10,640,000 and exceeded DRA's estimate of $9,498,000 by $1,142,000 or 12.0%. The difference was due to DRA's use of lower hourly labor cost ($14,980), lower management payroll and vacation accrual cost ($384,090), and a change in the cost billed to others as indicated by a General data response provided to DRA. In order to reflect test year conditions more accurately we will adopt DRA's estimate based on later data, and increase it by $189,000 to reflect our previously discussed adopted escalation factors to yield an estimate of $9,687,000.

FCC Account 642-Advertising is comprised of salaries and expenses for commercial advertising. It also covers the cost of setting up exhibits, lectures, and demonstrations for promotional purposes. DRA's estimate for this expense was $2,520,000 as contrasted to General's estimate of $14,795,000. According to the testimony, DRA elected to base an adjustment of 1988 advertising expenses on DRA's auditor adjustment for 1986. DRA's auditor adjustment disallowed $10.8 million of $13.11 million total, leaving $2.31 million as an allowable 1986 expense. Applying DRA's nonlabor escalation factors to this $2.31 million yields a 1988 estimate of $2.52 million. As previously stated, we believe that the disallowances would be reasonable had they been computed for and applied to the 1988 test year. However, such 1986 year disallowances would be appropriate for the 1988 test year only if it were shown that the advertising programs were similar for both years. The record does not indicate such similarity. Indeed, General's evidence indicated that the test year 1988 advertising programs relate much more heavily to product advertising than did the 1986 programs which appeared to be aimed at improving General's image in the community.

General's rebuttal witness Shibuya presented testimony indicating that the breakdown of the advertising budget for the test year 1988 would be $2 million for image enhancement, $1,350,000 for public service, $7,825,000 for product promotion, and $1,557,000 for national prorate, for a total of $12,732,000 exclusive of office supplies and employee expenses and compensation. In keeping with past policies as set forth by our previous decisions, we will permit the $1,350,000 public service amount and the $7,825,000 product promotion amount, together with the $2,243,000 for office supplies and employee expenses and compensation, for a total of $11,415,000, which we will adopt as reasonable for this proceeding. While adopting the majority of General's estimate for Account 642 for this proceeding we emphasize that we concur with DRA that the thrust of the Account 642 advertising expenses in 1985 and 1986 were image enhancement and would not be appropriate for recovery in rates were they to be repeated in 1988. General has represented that its 1988 programs will concentrate heavily on product advertising. We trust that General will be able to demonstrate that this has in fact occurred when General makes its next application for general rate relief.

DRA witness Enderby recommends that more attention be paid to our D.86-01-026 in Pacific's last general rate case which indicated that Pacific should perform more complete studies for rate proceedings to demonstrate that proposed expenditures are economically justified. Witness Enderby's position is well taken and this decision will provide an ordering paragraph similar to Ordering Paragraph 12 on page 215 of D.86-01-026.

FCC Account 643-Marketing and Sales Expenses includes the cost of market analysis, consumer research and promotion, and sales expenses of network services. General's estimate of Account 643-Sales Expense was $27,237,000 as compared to DRA's estimate of $19,603,000, a difference of $7,634,000 or 38.9%. The difference is primarily due to a 25% disallowance of General's estimated amount ($6,809,360) and lower hourly labor costs due to the staff's lower labor escalation factors. According to the testimony of DRA's witness Enderby:

1. After reviewing the meetings between DRA and General and related materials provided by General concerning marketing and sales expenses, DRA concluded that the information provided by General was inadequate to evaluate the expenses.

2. DRA is unaware of any explicit profitability studies of the marketing department as a stand-alone entity or of any pro forma presentation of marketing strategies and tactics for the years 1986, 1987, and 1988.

3. General did not prepare a cost benefit analysis of the marketing and advertising campaigns as required for Pacific for future rate cases by D.86-01-026.

In view of the above, DRA was inclined to disallow 50% of General's expenses for FCC Account 643 as a ratemaking adjustment in test year 1988. However, in response to a DRA data request, General indicated that currently there is a project initiated by its marketing and finance department to obtain product level contribution statements to be available in 1988 which will seek to isolate each marketing department's contribution to each product's revenue stream thereby allowing the utility to conduct the types of analyses discussed in the Pacific decision and recommended by DRA. Under these circumstances, DRA proposes to disallow 25% of FCC Account 643 in the test year 1988 with the understanding that if for the attrition year filing General comes forward with an appropriate showing that a "product level contribution" measurement system has been developed and implemented, the 25% disallowance be discontinued in 1989; if the showing is inadequate, the 25% disallowance be maintained; and if the showing is nonexistent, the disallowance be increased 50%.

Rebuttal witness Sidhon testified that:

1. The provisions of D.86-01-26 do not impose any requirement on General with respect to this proceeding as General nor any other telephone utility besides Pacific is mentioned in the decision's narrative summary, findings of fact, or ordering paragraphs regarding this issue.

2. The ordering paragraph provision will apply only when Pacific files its next general rate case for the test year 1989 and therefore Pacific was given more than two years to develop and implement the new estimating procedure mandated by the decision.

3. In its response to a DRA data request, General indicated that the marketing

> department provided a return to the company of $5.24 for each dollar-associated expense. This is projected to increase to $7.00 in 1988 and to average $7.94 for the years 1987 through 1991.

This witness further testified that an analysis provided by General clearly indicates marketing and sales activities make a positive contribution to total company revenues and that on the basis of this information supplied to DRA, Mr. Enderby's recommended 25% disallowance is inappropriate. We agree and will adopt DRA's estimate of $19,603,000 increased by the disallowance of $6,809,000 and further increased by $633,000 to reflect our previously discussed adopted labor escalation rates for a total for this account of $26,045,000.

Account 644-Connecting Company Relations covers the expenses for conducting inter-company business as it pertains to the interchange of services and includes expenses for negotiations or revisions of traffic agreements and intercompany settlements. DRA's estimate is $2,486,000 which is $89,000 or 3.5% less than General's estimate of $2,575,000. The difference is due to DRA's use of its lower labor escalation factor. We will adopt DRA's estimate increased by $43,000 to $2,529,000 to reflect our previously discussed adopted labor escalation rates.

FCC Account 645-Local Commercial Operations includes the salaries and expenses of employees involved in handling service orders and collecting revenues, other contracts, and the expenses associated with collection coin telephones. DRA's estimate of this account is $112,785,000 and is $11,766,000 or 10% less than General's estimate of $124,551,000. The differences are primarily due to DRA's use of a lower labor escalation factor and a disallowance of employee position additions requested by General in December 1986 after the submission of the NOI. According to the testimony of witness Enderby, after the submission of General's NOI, it requested expenses for an additional 40 management and 112 hourly employees for a carrier services organization (CSO) established in July 1986. According to the testimony, General also requested 53 additional management employees for "FMS/SOE" implementation in 1988. The FMS is a facilities management system that will provide mechanized facility assignment, usage forecasting, facility management, telephone number assignment, and aging and line equipment/telephone number load balancing. SOE is a service order entry system that will prompt the customer representative through the entire service order process, replacing the majority of current manual functions. This witness further testified that, according to General, 15 management employees were removed from its budget in error and 92 hourly employees were removed from its business service office centers as a data input error. According to this witness, no documentations for any of the above additions were provided by General and on this basis DRA is recommending disallowance of $9,533,470 for ratemaking purposes.

Rebuttal testimony presented by General's witness Culkin indicated that:

1. In March 1985, an interdepartmental group recommended the establishment of an organizational structure that could enable General to effectively market and provide services to the interexchange carriers (IC).

2. Approval of the recommendation resulted in the reassignment of IC-related activities and responsibilities from the Revenue Requirements Department to Special Services, the formation of the IC-OPC as the single point of contact with ICs for standard order processing, and a transfer of IC billing control functions and account management to marketing-network sales.

3. Since the ICs as a group are General's largest customers and because they have the ability to bypass General's network if their service requirements are not met, General concluded that a new department was needed to handle their accounts in an

efficient and timely manner. This led to the formation of the Access Services Department (ASD) in 1986.

4. As the result of creating the ASD in 1986, General has been able to provide strong financial support to its IC customers.

5. The need for the increase of the original hourly employee levels by 112 was determined based on order volume forecasts and labor hour coefficient for existing Universal Service Orders (USO) activities.

6. The additional 40 management employees were required when areas lacking support were identified and as new projects developed. Management judgment based on the witness's past experience in forecasting employee levels was used to derive the specific number of additional management employees.

7. The 112 hourly and 40 management employee addition to CSO is pivotal to achieve the goals of the company and the demands of the ICs. The 112 hourly and 40 management employee additions were based on a 15% growth rate ascertained by the witness after discussions with his managers and staff.

We are persuaded that the 40 management and 112 hourly employees are necessary to the efficient operation of the company and will therefore not adopt DRA's recommendation that the expenses associated with these workers be disallowed for ratemaking purposes.

Testimony presented by General's rebuttal witness Moore indicated that:

1. DRA witness Enderby's statement "General requested an additional 53 management for 'FMS/SOE' implementation in 1988" does not mean that 53 employees will be added in 1988 for implementation of the FMS/SOE system.

2. The word "implementation" is used generically to describe the efforts of several departments involved in completing the mechanization of General's service office operations. The total number of employees budgeted for this project in 1988 is 53.

3. The field implementation for FMS/SOE is scheduled to begin in 1988. The composition of the 53 management employees required for FMS/SOE for 1988, together with the benefit cost ratio for the operation, is set forth in Exhibit 16A. By disallowing the expenses associated with 53 employees, Mr. Enderby is in effect recommending that the entire FMS/SOE project be disallowed as these 53 employees represent all of the employees budgeted for FMS/SOE in 1988.

4. Termination of the FMS/SOE project would severely hamper General's continued efforts toward total service office automation.

DRA witness Enderby states: "While these functions appear to be useful, staff would like to see a complete listing and justification of all expected benefits and efficiencies from FMS/SOE. Moreover, documentation and sensitivity analysis should be provided for all benefits/costs or profitability studies performed by the utility. Staff is thus disallowing the $2,435,100 for the 53 employees." It appears that these deficiencies complained of by DRA witness Enderby were resolved in the above-quoted Exhibit 16A. Under these circumstances we will not accept DRA's recommendation that $2,435,100 for the 53 employees be disallowed for ratemaking purposes.

DRA witness testified that "according to the utility, 15 management employees were removed from their budget in error and 92 hourly employees were removed from business service office centers as a data input error. Staff would like to see a complete documentation of the errors and any justification for the employees. Staff is thus disallowing these expenses of $3,168,400." In his rebuttal testimony, General's witness Moore testified that: "Due to a data input error, these employees were inadvertently removed from the 1988 budget submitted at the time General filed its Notice of Intent (NOI) to the Commission staff on August 29, 1986. The error was discovered and corrected in the budget submitted with General's application in January 1987. As a result, these employees were labeled as 'additions' when in fact they were existing payroll employees omitted from the budget in error." We are persuaded that what occurred here was an inadvertent error of omission at the time the NOI was submitted and consequently we will not adopt DRA's recommendation for disallowance of $3,168,400.

In accordance with the above discussion, we will adopt as reasonable for Account 645-Local Commercial Operations DRA's estimate of $112,785,000 plus $9,533,470 that DRA recommends be disallowed for employee additions plus $1,682,000 to reflect our previously discussed adopted labor escalation factors, for a total of $124 million for this account.

For FCC Account 648-Public Telephone Commissions, both DRA and General estimated the expense to be $3,605,000, which we will adopt as reasonable for this proceeding.

For FCC Account 649-Directory Expenses, DRA estimated $101,348,000 as compared to General's estimate of $87,560,000, a difference of $13,788,000 or 13.6%. This expense is comprised of salaries and expenses of service department employees for developing directory production schedules and administering the compilation, warehousing, and delivery of directories and of charges by the GTE Directory Services for the production of directories and the sale of classified advertising. The latter is equal to 40% of General's total directory revenues which we have adopted as being $205 million. Forty percent of this $205 million is $82 million. DRA estimated the salaries and expenses of service department employees as being $8,759,000. To this we will add $9,000 to reflect our previously adopted labor escalation factors for a total for Account 649-Directory Expenses of $90,760,000.

We noted that General included an adjustment of $4,762,000 for inside wiring cost. The inside wiring cost was included in DRA's estimates and our previously adopted results. Therefore, we will not adopt any adjustment for this item.

As previously discussed, the GTED's adjustments adopted as reasonable for ratemaking purposes in this proceeding total $7,937,000. Such an adjustment is apportioned between maintenance expense, traffic expense, commercial expenses, and other operating expenses. The prorated share for commercial expenses of this GTED adjustment is $1,841,000 which we adopt as reasonable for this proceeding.

As set forth in the previous tabulation, DRA estimated a directory company adjustment of $9,159,000 as compared to General's estimate of $4,131,000. As previously discussed, we have adopted a figure of $9,001,000 as appropriate for this adjustment.

I. <u>General Office and Other Operating Expenses</u>

General office salaries and expenses are those operating costs incurred in performing the executive, accounting, treasury, law, personnel, public affairs, data processing, miscellaneous engineering, revenue requirements, and other general office functions. Other operating expenses are those operating costs necessary to provide overall telephone service which may not be included in the various other functional accounts. Other operating expenses include insurance, employees' fringe benefits, pensions, operating rents, and general services and licenses. It also includes the cost of director's fees, audit expenses, joint pool committee expenses, telephone expenses, new venture expense, unbillable toll expense, expenses transferred to construction, and other miscellaneous operating expenses.

Testimony was presented on behalf of DRA by Junior Utility Engineer M. J. Vannucchi (accounting and general services and licenses), Public Utility Regulatory Analyst II M. R. Loy (relief and pensions), Financial Examiner IV M. Amato (general services and licenses), and Associate Utility Engineer J. M. Shiu (balance of chapter). Rebuttal testimony was presented on behalf of General by its budget director, L. G. Manion (Vannucchi), by Dr. A. N. Mosich (Amato), of the School of Accounting, University of Southern California, by W. N. Sammis (Loy), of the firm of insurance brokers, Johnson and Higgins, and by the director of operations for GTE Investment Management Corporation, Roger S. Williams (Loy).

DRA's estimate of general operating expense was $179,385,000 as compared to General's estimate of $197,636,000, a difference of $18,251,000 or 10.2% and DRA's estimate of other operating expenses was $164,648,000 as compared to General's estimate of $235,711,000, a difference of $71,063,000 or 43.2%. The tabulation below sets forth DRA's and General's estimates, together with our adopted results. The bases for our adopted results is set forth in the ensuing paragraphs.

General Operating Expenses

Acc. No.	Item	DRA	General	General Exceeds DRA Amount	General Exceeds DRA Percent	Adopted
			(Thousands of Dollars)			
	General Office Salaries and Expenses					
661	Executive Dept.	$ 1,277	$ 1,394	$ 117	9.2%	$ 1,311
662	Accounting Dept.	103,066	109,952	6,886	6.7	109,952
663	Treasury Dept.	2,945	3,261	316	10.7	2,967
664	Law Dept.	2,411	2,627	216	9.0	2,476
665	Other Gen. Office	69,686	77,283	7,597	10.9	73,366
	Total	179,385	197,636	18,251	10.2	190,072
	Other Operating Expenses					
668	Insurance	$ 3,204	$ 3,628	$ 424	13.2%	$ 3,204
669	Accidents & Damages	1,100	1,240	140	12.7	1,100
671	Oper. Rents	14,447	15,228	781	5.4	14,447
672	Relief & Pensions	117,318	164,020	46,702	39.8	145,322
674	General Services and Licenses	33,000	55,768	22,768	69.0	43,400
675	Misc. Other	5,141	7,447	2,306	44.9	5,141
677	Exp. Chg'd. Const.	(9,562)	(20,312)	(10,250)	112.4	(17,358)
	Inside Wire	0	8,697	8,692	0.0	0
	Subtotal	164,648	235,711	71,063	43.2	195,256
	GTED Adj.	(5,235)	0	5,235	(100.0)	(3,800)
	Compensation Adj.	(26,200)	0	26,200	(100.0)	0
	Total	133,213	235,711	102,498	76.9	191,456

(Red Figure)

FCC Account 661-Executive Department includes the salaries and expenses of officers engaged in general management and administration including their assistants and office forces. DRA's estimate for this account is $1,277,000 as compared to General's estimate of $1,394,000, a difference of $117,000 or 9.2%. The reasons for the differences are DRA's lower labor inflation and

nonlabor escalation factors, the use by General of four months' actual expenses of 1986 to estimate cost billed to others for 1988 as contrasted to DRA's use of annualized eleven months' recorded cost billed to others for 1986 to derive a 1988 figure. We will adopt DRA's estimate of $1,277,000 based on later data increased by $34,000 to reflect our previously discussed adopted labor escalation figures. The Account 661 expense thus computed is $1,311,000.

FCC Account 662-Accounting Department includes the salaries and expenses of the vice president-controller, his assistants, and office force. Accounting operations include accounting, budget, information systems, and internal auditing. DRA's estimate for this account is $103,066,000 as contrasted to General's estimate of $109,952,000, a difference of $6,886,000 or 6.7%. According to the testimony of DRA's witness Vannucchi, there has been a dramatic increase in the employee levels for FCC Account 662 in spite of the trend toward a reduction in overall company employees. According to the testimony, Account 662 has grown from 338 total employees in 1978 to 605 employees in 1986. The 1988 test year estimate is 647 employees. A data request response by General indicated that the increase in employees was due to the following reasons:

1. Increases in 1982 and in 1983 were the result of reorganization between GTC and General Telephone Data Services.

2. Total company growth increased reporting requirements.

3. An increase in the construction program increased invoices, work orders, and data processing.

4. Increased reporting and record keeping necessitated by deregulation and increased regulatory involvement in the process.

5. Increased demand by both internal management as well as the external

financial community including the Commission, FCC, Securities and Exchange Commission, etc.

6. Employee level increases from 1986 to 1988 are all attributed to increased billing and record keeping associated with access charge accounting requirements.

According to the testimony of this witness, DRA's investigation of the above-listed reasonings for Account 662 increases revealed that:

1. Total company growth plateaued in 1982 with 29,253 employees and has been steadily decreasing with an estimated 23,101 employees for 1988.

2. The construction program reached a high in 1986 and with the conversion of central offices winding down, the budget for construction is consequently declining.

3. General could not supply any evidence supporting its claims of the increase in reporting and record keeping necessitated by deregulation and increased regulatory involvement for that process.

4. FCC Account 662 estimated to increase in employee count from 605 in 1986 to 647 in 1988 with the increase due to staffing requirements for access charge accounting. General provided an employee breakdown which resulted in the addition of 11 employees, 31 shy of the 1988 estimated increase.

According to the record, because of the above reasons, DRA is recommending that the employee count for FCC Account 662 remain at the 1986 level less 5% to compensate for reduction in construction programs and increased by 11 employees for the access charge accounting.

According to the rebuttal testimony of General's witness Manion, the 1987 employee level identified by Mr. Vannucchi represented the lowest employee level in 12 years of historical data provided to him by General and subsequent reorganization in 1982 shifted 34 GTEDS employees and 14 service department employees to the accounting expense account. This witness further testified that the 1986 employee level used by Vannucchi to make his calculations for the 1988 test year was an improper figure because it represented only employees on the payroll, whereas General's estimates include contract equivalent employees. Witness Manion further testified that the 1986 contract equivalent employees was 68 and that had Vannucchi used the correct 1986 employee level in his proposed adjustment the resulting 1988 employee level recommended would have been 650 employees, which is only 12 employees less than the 662 employee level included by General in the application.

We will adopt General's estimate of $109,952,000 for FCC Account 662 - Accounting Department which recognizes a total of 662 employees, including contract equivalent employees. We do this reluctantly because, like DRA, we are alarmed at the disproportionate growth in this account in view of the decline in total company numbers of employees since 1982. General's documentation for the increased accounting employees was marginal and the data it furnished DRA was apparently confusing. We would adopt DRA's estimate except for the fact that we are uncertain that it includes contract equivalent employees and we believe that the adopted amount should recognize total employees, including contract equivalent employees. We will examine this account closely in General's next proceeding to determine that General has fully justified the number of employees it is estimating and that any additional growth in this account is completely explained.

For FCC Account 663-Treasury Department, DRA's estimate for test year 1988 is $2,945,000 or $316,000 (10.7%) less than General's estimate of $3,261,000. According to the record, the reason for the difference is the use by DRA of lower labor and nonlabor escalation factors, the use by DRA of annualized 11 months recorded Cost Billed to Others as contrasted to General's four months' recorded data and the use by DRA of the average level of short-term loans in 1985 to estimate the bank activity fees for 1988 rather than the expenses of lines of credit, commercial papers, and bank service charges for the nine-month period, July 1985 to March 1986. We will adopt DRA's estimate of $2,945,000 based on more complete and later data and increase this amount by $22,000 to $2,967,000 to reflect our previously discussed adopted labor escalation factors.

Expense for FCC Account 664-Law Department was estimated by DRA to be $2,411,000 as contrasted to General's estimate of $2,627,000, a difference of $216,000 or 9.0%. The major difference between the two estimates is due to the use of lower labor escalation and nonlabor escalation factors by DRA and the elimination of two management employees from the law department. We will adopt DRA's estimate of $2,411,000 increased by $65,000 to reflect our previously discussed adopted labor escalation factors to yield a total expense for this account of $2,476,000.

FCC Account 665-Other General Office Expense includes employee salaries and expenses in human resources, public affairs, revenue requirement, miscellaneous engineering, and security of the company. DRA's estimate for this account in test year 1988 is $69,686,000 as compared to General's estimate of $77,283,000, a difference of $7,597,000 or 10.9%. According to DRA witness Shiu, the major difference between DRA's and General's estimates is due to the utilization by DRA of lower labor inflation factors, lower nonlabor escalation factors, and the use of annualized 12 months' recorded cost billed to others data for 1986 rather than 4 months' actual expenses of 1986 as used by General. The witness further testified that the DRA auditor recommended exclusion of expenses related to open house events for the new headquarters building, corporate image of the company, and political advocacy of $35,000,

$2,967,000, and $619,000, respectively, for 1985 and $457,000, $3,416,000, and $678,000, respectively, for 1986. For the test year 1988, this witness held the above disallowed expenses related to corporate image and political advocacy in conjunction with the amounts as a ratemaking adjustment for the test year 1988 in the amount of $4,094,000. As previously discussed, we have adopted a disallowance of $1,287,000 for corporate image of the company and $678,000 for political advocacy for test year 1986 and will continue these amounts as a disallowance for Account 665 for the test year 1988. We will therefore adopt DRA's estimate of $69,686,000 increased by the difference between DRA's proposed disallowance and our adopted allowance of $2,129,000 and increased further by $1,551,000 to reflect our previously discussed adopted labor escalation amounts for a total of $73,366,000.

Under general office salaries and expenses, General shows an item of expense for Uniform System of Accounts (USOA) rewrite of $42,662,000 and inside wire costs of $3,119,000. We are considering the USOA rewrite matter generically under I.87-02-023 and therefore will not adopt General's adjustment for this amount. In addition, the inside wire costs are included in DRA's estimates and therefore we will not adopt General's proposed amount.

DRA's estimate of FCC Account 668-Insurance is $3,204,000 as compared to General's estimate of $3,628,000, a difference of $424,000 or 13.2%. DRA's estimate of FCC Account 669-Accident and Damages is $1,100,000 as compared to General's estimate of $1,240,000, a difference of $140,000 or 12.7%. According to the testimony of DRA witness Shiu, the reasons for the difference are DRA's use of lower labor and nonlabor inflation factors and the use of annualized 11 months' recorded costs billed to other data of 1986 for test year 1988 rather than General's use of four months' actual expense of 1986 to estimate the cost billed to this account for 1988. We will adopt DRA's estimates for these two accounts as

reasonable for this proceeding because they are based on more complete information than General's estimates.

DRA's estimate of FCC Account 671-Operating Rents is $14,447,000 as compared to General's estimate of $15,228,000, a difference of $781,000 or 5.4%. According to the testimony of DRA's witness, the major difference is due to DRA excluding from the account the estimated costs of leases which will be terminated before December 31, 1988, whereas General prepared its estimate before the listings of leases were outdated. It is obvious that DRA's estimate excluding terminated leases is more accurate than General's estimate. Consequently, we will adopt DRA's estimate as reasonable for this proceeding.

FCC Account 672-Relief and Pensions includes expenses incurred in connection with employee pensions, group life insurance, medical and dental coverage, sickness, disability, military leave, employee savings plan, workers' compensation, and other benefits which include the administrative cost of the pension and medical plans. General's estimate for this account is $165,272,000 as contrasted to DRA's estimate of $117,317,700, a difference of $47,954,300 or 40.9%. Tabulated below are the component parts of this account as estimated by DRA and General, together with our adopted results.

Item	DRA	General	General Exceeds DRA Amount	General Exceeds DRA Percent	Adopted
		(Thousands of Dollars)			
Pensions	$ 43,873.0	$ 59,477.0	$15,604.0	35.6	$ 53,345
Group Life Insurance	2,219.5	2,929.0	709.5	32.0	2,651
Dental Insurance	4,350.8	5,629.0	1,278.2	29.4	5,126
Medical Insurance	58,552.8	89,264.0	30,711.2	52.5	74,900
Sickness Disability	13,957.2	19,454.0	5,496.8	39.4	17,294
Military Leave	8.6	16.0	7.4	86.0	13
Workers' Comp.	15,499.0	17,083.0	1,584.0	10.2	15,499
Employee Savings Plan	8,485.0	11,163.0	2,678.0	31.6	10,111
Other Benefits	6,057.0	10,529.0	4,472.0	73.8	10,529
Subtotal	153,002.9	215,544.0	62,541.1	40.9	189,468
Charged to Construction @ .233	(35,685.2)	(50,272.0)	(14,581.8)	NA	(44,146)
Total Expensed	117,317.7	165,272.0	47,954.3	40.9	145,322
Adjustment due to elimination of 202 operator service employee		1,252.0			
Net Expensed	117,317.7	164,020.0	46,702.3	39.8	145,322

(Red Figure)

Testimony on Account 672 was presented on behalf of DRA by Public Utility Regulatory Analyst II Mark R. Loy. Rebuttal testimony on the pension fund and administration expenses was presented on behalf of General by the director of operations for GTE Investment Management Corporation, Roger S. Williams, and on the subject of funding requirements for General's medical benefit plan provided through The Travelers by the vice president in the employee benefit plans department of Johnson and Higgins, William N. Sammis.

As noted from the above tabulations, General's estimate for pension expense was $59,477,000 as compared to DRA's estimate of $43,873,000, a difference of $15,604,000 or 35.6%. Both General and DRA presented testimony showing the effect of the use of

Statement of Financial Accounting Standard No. 87 (SFAS 87) in lieu of their original estimates. Testimony on the effects of SFAS 87 was presented on behalf of DRA by Financial Examiner III Tim Kenney and was rebutted by the manager of pension funding for GTE Service Corporation, Marquerita DeBonis. The tabulation below is the breakdown of the SFAS 87 pension expense estimates presented by DRA and General.

	DRA	General
	(Thousand of	Dollars)
SFAS 1987 Pension Expense	$13.3	$13.3
Additional Late Request	-	1.5
Subtotal	13.3	14.8
Less:		
Effect of 22.8% Work Force Reduction	(3.0)	-
2.01% Labor Escalation Factor	(3.0)	-
Total	7.3	14.8

(Red Figure)

DRA recognizes that this Commission has taken up SFAS 87 issues in the USOA rewrite investigation I.87-02-023, but recommends that General's pension expense be based on use of SFAS 87 because:

1. DRA and General agreed in this proceeding to use SFAS 87 in calculating General's pension expense, and both parties have done so.

2. General's pension cost will increase by $46,000,000 to $59,000,000 if SFAS 87 is not used for this proceeding.

3. General has stated it will contribute only $5.5 million to its pension fund in 1988, which would result in a windfall to the company if SFAS 87 not is used.

SFAS 87 is being separately considered by this Commission in I.87-02-023 concerning revisions to the USOA. On December 22, 1987, we issued Interim D.87-12-063 which did not address SFAS 87 but did authorize General to initiate a balancing account to record revenue requirement impacts from the adoption of Part 32 and Part 36 revisions proposed by the FCC. General believes that, for purposes of consistency in this rate case, the balancing account authorized in D.87-12-063 should be used for treatment of the SFAS 87 impacts to General's pension expense.

By D.88-03-072 in I.87-02-023, we ruled that SFAS 87 "should not be utilized for ratemaking purposes". Consequently, in this proceeding, we will not consider the testimony submitted into evidence on SFAS 87 by General and DRA.

According to the testimony of DRA witness Loy, the basic reasons for the difference in DRA's and General's expense estimates for Account 672 are:

1. The DRA employee count is 23% lower than General's accounting for more than half of the difference in the estimates.

2. DRA is recommending a different labor inflation treatment to Account 672 than General did, resulting in approximately 8.9% of the expense differential attributable to the staff's 3.2% lower labor inflation and the staff identifying different expense items than General did for labor inflation treatment.

3. The premiums and rates the staff used are based on more recent information than those used by General.

A review of the above tabulation indicates that the differential between DRA and General estimates approximates the compound effect of force reduction and lower escalation factors for pensions, group life insurance, dental insurance, sickness disability, and employee savings plans, justifying, in our mind, the utilization of these factors for determination of the reasonable costs for these component items. Although not computed in that manner, our adopted expenses reflect a force reduction of approximately 10%. Furthermore, our adopted labor escalation factors approximate 87% of the differential between the labor escalation factors used by DRA and General. Under these circumstances, we will adopt as reasonable for ratemaking purposes for those component items listed above the DRA estimate plus .607 (the compound affect of our adopted force reduction and labor escalation factors) times the difference between DRA and General estimates. Such computations result in the following adopted expenses:

Pensions	$53,345,000
Group Life Insurance	2,651,000
Dental Insurance	5,126,000
Sickness Disability	17,294,000
Employee Savings Plan	10,111,000

DRA's estimate for medical insurance is $58,552,800 as compared to General's estimate of $89,264,000, a difference of $30,711,200 or 52.5%. DRA used lower work force estimates and lower rates than General did for developing expense estimates. DRA's lower employee counts amount to a 23% reduction in the participation. The remaining differences are attributable to the development of the rate structures charged by the Travelers Company (72% of the total expenses) and the seven health maintenance organizations (28% of the total expenses). According to the testimony of DRA witness Loy, the latest rate information from the insurers' actuary indicates a dramatic increase in funding deficits beginning in 1984 and continuing through 1987, and possibly to 1988. This witness further testified that the causes of the funding shortfall are a dramatic increase in claims level as of 1985 and an unprecedented $9 million divided in 1984. As a result, according to the record, DRA found that the 29% and 22% increases were substantially greater than the expected rate increases of other Southern California utilities, i.e. Southern California Gas Company and Southern California Edison Company. Furthermore, General's HMOs experienced a rate reduction in 1987 and expect no increase in 1988 while GTE expects an increase of 10.5% for 1988. DRA believes General's 1988 customers should not be penalized for funding problems resulting from claims experience and plan administration occurring in a prior test year period (1984 and 1985). Therefore, it is DRA's recommendation that a medical escalation rate of 10% per annum, an average of GTE's 10.5% on the rates of Southern California Gas Company (6%) and Southern California Edison Company (11.2%) be used. This recommended escalation rate is 30% lower on a two-year compounded basis than General's proposal of about 25.5% per annum, resulting in DRA's estimate under The Travelers being $41,254,730 or $24,016,990 (58.2%) lower than General's estimate of $65,271,720.

Rebuttal testimony presented on behalf of General by William N. Sammis indicated that:

1. The amount of premium paid each year is the best projection of the cost of benefits to General. In the past, projections have been extremely close, considering the external factors of employment, medical costs, inflation, benefit improvements, etc. which all affect the cost of employee benefits.

2. The rate of funding increase cannot be reasonably compared between companies without knowing the underlying basis. In this respect the timing of projects is very important. For example, in 1985 and early 1986, medical cost trends of inflation and utilization of 10% were significantly below the current projections of 13.5% to 15.5% for 1988.

3. The projected overall increase of 26.03% for 1987 is a budget or funding increase intended to make up the shortfall or deficit in the 1986 budget level and cover

the expected 8.3% increase in medical cost for 1987.

4. The average cost method for estimating cost used by DRA witness Loy is often used for small employers, those with less than 100 employees, where the claim experience or utilization cannot be easily determined or predicted because of drastic changes and the impact of a single medical claim. DRA witness Loy's approach ignores actual facts and uses a method which is inappropriate for General, given its size and the available facts.

5. There is not a direct prorated reduction in medical benefits costs associated with employee force reduction.

6. The funding and administration of the benefit program is highly efficient with less than 1.25% of 1986 benefit claims applied for administration.

7. The dividend that resulted from favorable medical and dental claim experience for 1984 was $7,540,326 or 13.6% of plan contributions. The refund did not exceed the balance at the end of the year.

8. During 1984, Johnson and Higgins determined that the 1984 claim experience was developing at a lower rate than originally anticipated with the result that there would be a large surplus at the end of the year. Such a surplus could be avoided by suspension of contribution for a portion of 1984. Therefore, General, along with other GTE telephone operating companies, did not make contributions for the last two months of the 1984 plan year. Unfortunately claims increased dramatically for the months of October, November, and December 1984, resulting in the overall deficit or shortfall at year end. The suspension of contributions was recorded for accounting purposes as a dividend.

9. Medical claims totaling $39.8 million for 1984, $51.3 million for 1985, and $56.8

> million for 1986 indicated that the DRA estimate of $41.3 million for 1988 is unrealistic.

We are persuaded that DRA's estimate of $41,254,730 for The Travelers medical insurance is low and General's estimate of $65,271,720 is high. In consideration to our adoption of estimates reflecting work force reduction, we will not escalate the medical insurance costs and will adopt as reasonable for this proceeding the 1986 recorded medical insurance cost of $56.8 million.

Health maintenance organizations make up 28% of the total company medical insurance costs. General is assuming an annual increase of 5% for 1987 and 10% in 1988 for health and 4.5% for all other providers. DRA used the 1987 actual rates (a 4.4% decrease from 1986 levels) applied to its proposed labor force reduction and assumed no change for the 1988 rates. DRA's position appears reasonable, and we will adopt its recommended $16.3 million for HMO costs increased to $18.1 million to reflect our adopted labor force reduction. Adding this $18.1 million HMO cost to the $56.8 million adopted, The Travelers' cost yields a medical insurance cost of $74.9 million for test year 1988 which we will adopt as reasonable.

Both DRA and General developed their 1988 recommended expense allowances for military leave as a percentage of payroll. General used the 1985 actual percentage, but DRA used a four-year average. We will adopt DRA's estimate of $8,600 increased by $4,200 to reflect the previously discussed smaller force reduction to yield a total of $12,800 for this component item.

"Other Benefits" includes administrative costs for pension and medical plans, the nonregulated operations employees savings plan, termination costs, and the supplemental executive retirement plan. DRA's estimate for this item is $6,057,000 which is $4,472,000 or 73.8% less than General's estimate of $10,529,000. According to the record, $5,834,000 of the $6,057,000 estimate for other benefits is for administration of the pension fund, leaving

$223,000 total for the cost of the nonregulated operations employees savings plans, termination costs, and the supplemental executive retirement plan. DRA witness Loy testified that the $5,834,000 expense for the administration of the pension fund was derived by multiplying the 1985 recorded figure by the force reduction percentage and labor escalation factor. Such a procedure obviously ties the pension administration cost directly to the size of the 1988 test year labor force.

Rebuttal testimony presented on behalf of General by Roger S. Williams indicated that:

1. The primary functions associated with the administration of the pension fund are safeguarding, investing, and record-keeping of plan assets.

2. The assets are held and protected by an appointed trustee.

3. GTE within the ERISA guidelines invests the assets to maximize returns within an acceptable level of risk.

4. The expense and fees of the pension fund administration are based upon the value of the pension fund itself.

5. Approximately 85% of the annual fees are pension management fees with an additional 10% attributable to trustee funds, including the transaction charges.

6. It is the growth of the pension fund which determines the growth in administration cost, not the change in wages paid to General's hourly employees.

7. A reduction in General's work force by 23% would not act to reduce plan assets nor would such a reduction have an impact on the cost of plan administration over an extended time frame.

It appears from the record that the major portion of pension fund administrative costs are based on the level of the pension fund rather than the size of the workforce. Under these circumstances, DRA's method of estimating this expense by the application of a force reduction percentage factor appears inappropriate. Consequently, we will adopt General's figure of $10,529,000 for other items for the purposes of this proceeding.

DRA's estimate for workers' compensation is $15,499,000 or $1,584,000 or 10.2% less than General's estimate of $17,083,000. The rates of change in workers' compensation expenses for the period 1982 to 1985 decreased from 34.7% to 10.0%. DRA incorporated this decrease into its forecast by assuming that rates would increase but would do so more slowly, equal to the 1985 and 1986 experience. General, on the other hand, assumed the rates would increase at approximately the 1985 level plus payroll escalation. We are persuaded that DRA's estimate is reasonable and will adopt $15,499,000 for this component item for test year 1988.

The total of the above-discussed component items is $189,468,000. Reducing this by the 23.3% charged to construction or $44,146,000 leaves a total expense for Account 672 of $145,322,000 which we will adopt as reasonable for this proceeding.

FCC Account 674-General Services and License includes payments to GTE Service Corporation for services received under a general service contract which provides for the furnishing of advisory services on general accounting, financial, insurance and taxes, pensions and benefits, organization and personnel, legal, commercial, marketing and sales, engineering, plant, traffic, public affairs, and advertising matters. DRA's estimate for this account is $33 million or $22.8 million (69.0%) less than General's estimate of $55.8 million. As discussed under the affiliate interest portion of this decision, we have adopted a figure for this account of $43.4 million.

FCC Account 675-Other Expenses includes such items as directors' fees and expenses, the cost of publishing reports to shareholders, telephone association expenses, valuation, inventories and appraisals, audit expenses of independent auditors, rate case expenses, and other expenses of a general nature. DRA's estimate of this expense is $5,141,000 or $2,306,000 (44.9%) less than General's estimate of $7,447,000. According to the testimony of witness Shiu, the difference in the estimates is due to the use by DRA of lower labor and nonlabor escalation factors and a lower estimate of cost billed to others. Also, DRA excluded $214,000 for dues payable to the U.S. Telephone Association reflecting the traditional adjustment this Commission has adopted in prior proceedings. We will adopt as reasonable for this account DRA's recommended $5,141,000, since General has not supported its higher test year estimate.

FCC Account 677-Expenses Charged to Construction is a credit account representing the portion of operating expenses applicable to construction work. DRA's estimate of minus $9,562,000 is $10,750,000 or 112.4% less than General's estimate of minus $20,312,000. According to the testimony, the difference is due to a different estimation of labor and labor overhead charged to plant in service. Consistent with our subsequently discussed adopted plant accounts, we will adopt as reasonable for Account 677 the amount of minus $17,358,000.

DRA proposes a negative adjustment to other operating expenses of $5,235,000 for GTED and a negative $26,200,000 as a compensation adjustment. As previously discussed, we will not adopt the recommended compensation adjustment of $26,200,000. Also, as previously discussed under affiliated interest text, our GTED adjustment is $7,937,000 rather than the original amount recommended by DRA and the proration to other operating expenses is $3,800,000 which we will adopt as reasonable.

J. Taxes

Testimony was presented on taxes by DRA's Financial Examiner III Donna L. Wagoner. Rebuttal testimony on the method of computing California corporation franchise tax was presented on behalf of General by its Tax Manager, Jon F. Kieffer.

Taxes are subdivided into two major categories, income taxes and taxes other than income taxes. The Tax Reform Act of 1986 (TRA86) provides a new depreciation system, the Modified Accelerated Cost Recovery System (MACRS). MACRS and some of the more obvious provisions of TRA86, such as the change in corporate tax rate, the repeal of investment tax credit, and the repeal of deductibility of certain capitalized interest and overheads during construction, have been estimated and incorporated into the federal income tax calculations provided by DRA for this general rate case on an interim basis pending a Commission decision in OII 86-11-019 which would establish ratemaking tax expense policy for the impact of TRA86. In D.88-01-061 dated January 28, 1988 on OII 86-11-019, our investigation on the impact of TRA86, we are requiring respondents, including General, to file calculations with supporting work papers proposing a 1987 revenue requirement adjustment for TRA86 and SB572 effects in conformance with the methodology adopted in the decision. DRA recommends that the adoption of federal income tax (FIT) or California corporation franchise tax (CCFT) to be collected in 1988 rates be based upon DRA's recommendations made in this proceeding. According to DRA, the impact of TRA86 decision on General's 1988 test year will be resolved when General complies with TRA86 decision requirements. We agree. General included in its application a tax deduction for construction period interest. Treatment of the construction period interest will be resolved by General's compliance with D.88-01-061 and therefore General's tax deduction for this item will be excluded.

In D.88-01-061, we transferred review of the Privilege Year Adjustment to Pacific Gas and Electric Company A.85-12-050, Phase II, which is addressing the working cash impact of when CCFT is deductible for FIT purposes. DRA recommends that the issue of Privilege Year Adjustment be deferred until the Commission has issued its decision in A.85-12-050. We concur. DRA's FIT interest deduction was derived by applying the weighted average embedded cost of debt as supplied by DRA's rate of return witness to DRA's estimated rate base. The unamortized deferred investment tax credit (ITC) was not deducted from rate base for this calculation. This method of "interest synchronization" is permitted by Treasury Regulation Section 1.46-6. It is General's position that the propriety of using interest synchronization for ratemaking purposes is currently the subject of an investigation instituted by this Commission, I.86-10-002, to which General is a party. Consequently, General recommends that we defer any action on the use of interest synchronization pending a decision in I.86-10-002. That investigation was closed by D.88-04-008 dated April 27, 1988. Consistent with our action in D.87-12-067 in Pacific's latest rate case, we will adopt DRA's calculations of the FIT interest deduction, thereby effectively implementing the interest synchronization adjustment for General.

DRA's comments raise a technical implementation issue related to this Commission's interest synchronization (I.S.) decisions. D.88-04-038, the decision closing I.86-10-002, indicated that I.S. should be adopted in the final order in General's 1988 test year rate case, but this decision failed to address the question of how the 1987 revenue requirement data collected in I.86-10-002 for General was to be reflected in the instant record, which was already submitted at the time D.88-04-038 was issued. The Proposed Decision reflected the effects of I.S., but only for the 1988 test year.

To assess the 1987 I.S. impacts for General, it is necessary to discuss the data General provided us in I.86-10-002. In December 1986, like the other I.86-10-002 respondents, General filed an advice letter detailing the revenue requirements adjustments associated with the adoption of I.S. for ratemaking purposes. Subsequently, General transmitted updated calculations to CACD, which informed the assigned ALJ that General's 1987 I.S. adjustment was approximately $11.4 million. As previously noted, in D.88-04-038 we did not adjust General's revenue requirement to account for the advice letter data collected in the generic docket, indicating that I.S. implementation for General would occur in this proceeding. Therefore, the impacts of our I.S. investigation which predate the test year must still be recognized. Such action will place General on the same footing as the other I.86-10-002 respondents.

We will require General to file an advice letter designed to capture the pre-test year revenue requirements impacts of I.S. consistent with the Commission's prior orders in I.86-10-002. A specific ordering paragraph is added to accomplish this result.

DRA used an effective CCFT rate of 7.71% to compute General's CCFT liability at current rates whereas General used the statutory rate of 9.6%. According to DRA, the 7.71% effective rate reflects General's allocated share of GTE Corporation's total California CCFT liability based on review of the most recent historical data available covering the years 1982 to 1985. In General's 1980, 1982, and 1984 general rate cases, we adopted the effective CCFT rate in calculating General's CCFT liability but used the statutory 9.6% rate as a floor. Consistent with our past practices, we will adopt the higher of the statutory rate or the

effective tax rate, which, in this case, is the statutory tax rate of 9.3% in computing the CCFT.

Since General's unitary CCFT tax rate is established on a three-factor formula which determines the relationship of wages, revenues, and average net tangible property of all General's system telephone operations in California to wages, revenues, and average net tangible property of the total General system, an increase or decrease in revenues would impact only one of the three factors used to develop the incremental rate which, in turn, increases or decreases the average apportionment factor. Since only one of the three factors changes in computing the CCFT for reflecting an increase or decrease in rates, we have in the past used incremental tax rates for any changes in rates granted by us. Consistent with our past practices we used incremental tax rate developed for this proceeding of 1.8635% to calculate the net-to-gross multiplier. Appendix C of this decision reflects the development of our adopted CCFT and FIT.

The tabulation below sets forth taxes other than income as computed by DRA and General, together with our adopted results. The bases for the adopted results are set forth in the ensuing paragraphs.

Acc. No.	Item	DRA	General	General Exceeds DRA Amount	General Exceeds DRA Percent	Adopted
		(Thousands of Dollars)				
	Operating Taxes:					
307.1	Ad Valorem	$60,085	$ 64,997	$ 4,912	8.2%	$ 64,952
307.4	Other Taxes	941	941	0	0.0	941
	Subtotal	61,026	65,938	4,912	8.0	65,893
	Social Security Taxes:					
307.5	SUI	930	2,344	1,414	152.0	1,084
307.6	FUI	558	938	380	68.1	868
307.7	FICA	32,002	44,286	12,284	38.4	38,290
	Subtotal	33,490	47,568	14,078	42.0	40,242
Total		94,516	113,506	18,990	20.1%	106,135

The State Unemployment Insurance (SUI) tax rate used by General was 2% and by DRA was 1%. The 1% rate was most recently provided by the State of California and will be used for this proceeding.

The U.S. Department of Health and Human Services (HHS) released a base for Federal Insurance Contribution Act (FICA) tax of $45,000 for 1988. This base amount will be used for the computation of the FICA tax for this proceeding.

The most recently adopted Federal Unemployment Insurance (FUI) tax rate is 0.8%. This rate will be used for the computations in this proceeding. General's and DRA's estimates of ad valorem taxes reflect respective plant balance estimates. Consistent with our adopted plant balances we will adopt $64,952,000 as reasonable for ad valorem taxes.

K. Depreciation

DRA's testimony on depreciation expenses and depreciation reserve was presented by Senior Utilities Engineer Ramesh Joshi. General's testimony on depreciation rates was presented by its Manager of Capital Recovery and Valuation Carl R. Lanterman. General's Capital Recovery Research Manager Terence D. Robinson testified on the economic value depreciation model used in part to support the remaining lives presented by Lanterman for digital central office equipment and fiber-optic outside plant facilities.

DRA witness Joshi recommends that the Commission:

1. Authorize depreciation rates used by the staff in developing accruals for test year 1988.

2. Approve reciprocal weighting method proposed by General.

3. Defer formally recognizing life analysis techniques such as economic value depreciation (EVD) and substitution analysis to a later date.

4. Disapprove use of quantified added uncertainty (QAU) for life analysis of telephone plant.

5. Reject any amount of depreciation expense which is estimated to achieve so-called desired reserve level.

6. Separate the rate represcription process from a general rate case on the basis that the procedure adopted by Resolution RRD7 on September 13, 1977 is adequate.

General and DRA reached agreement on depreciation rates which were approved by this Commission in D.87-12-070. These rates are to be applied to our subsequently discussed adopted telephone plant in service balances (Account 100.1) to determine amounts allowed for depreciation expense and depreciation reserve. Both General and DRA agree that the reciprocal weighting method approved in D.84-07-108 should be used. This method was used to develop stipulated depreciation rates for several plant accounts and will be used in this proceeding. DRA's recommendation that we defer formerly recognized in life analysis techniques such as EVD and substitution analyses to a later date is agreeable to General and will be adopted for this proceeding. DRA's recommendation that we disapprove use of QAU for life analysis of telephone plant is not contested by General and will be adopted for this proceeding. Because General and DRA were able to reach agreement on depreciation rates for test year 1988, DRA's recommendation that we retract any amount of depreciation expense which is estimated to achieve so-called desired reserve level is rendered moot. General agrees that the rate represcription process adopted in Resolution RRD7 on September 13, 1977 is adequate and appropriate for our biannual review of depreciation. General voiced concern that DRA intended to recommend that depreciation issues be removed from consideration in rate cases. We do not believe that was DRA's

intended recommendation but, in any event, we will consider depreciation in this proceeding.

Excluding the estimated impact of issues such as USOA and SNI/RID which will be decided in other generic proceedings and including the impact of inside wire on a business-as-usual basis, DRA's depreciation expense estimate is $497,161,000 which is $42,175,000 or 8.1% less than General's estimate of $537,436,000. DRA's estimate of depreciation reserve is $2,012,217,000 which is $38,808,000 or 1.9% less than General's estimate of $2,051,025,000. Applying the agreed depreciation rates to our subsequently discussed capital plant balances in Account 100.1 yields a depreciation expense of $525,864,000 and a depreciation reserve of $2,015,626,000 (excluding Communications System Corporation adjustments) which we will adopt as reasonable for this proceeding.

L. Telephone Plant

DRA's testimony on capital additions and telephone plant in service was presented by Program and Project Supervisor Martin J. O'Donnell and Assistant Utilities Engineer Riaz Danish. Danish did the analysis and estimates of 1987 and 1988 capital additions while O'Donnell did the calculations for plant balances and telephone plant in service (TPIS). Discussion in Chapter 13 of Exhibit 85 on TPIS was limited to Account 100.1 and interest during construction (IDC) on Account 100.2 (telephone plant under construction), since DRA takes no exception to General's estimates on Account 100.3 (property held for future use). Rebuttal to Danish's testimony was presented by seven witnesses: (1) General's Network Operations Planning Manager David R. Bowman; (2) General's Network Engineering Manager Anthony G. Donato; (3) an Account Executive of GTE Communications Systems Corporation Edward J. Gronkiewicz; (4) General's Budget Manager of Operations Frederick K. Hesse; (5) General's Product Manager of Business Operations Products and Services William R. Hickam; (6) Director of Telecommunications Regulatory Advisory Services of Coopers and

Lybrand Carl O. Thorsen; and (7) General's Network Operations Planning Manager Kevin A. Young.

The tabulation below sets forth DRA's estimate of gross additions for the test year 1988, together with General's estimate and our adopted results. The basis for the adopted results is set forth in the ensuing paragraphs.

Acc. No.	Item	DRA	General	General Exceeds DRA Amount	General Exceeds DRA Percent	Adopted
		(Dollars in Thousands)				
C11	Land	$ 2,527	$ 2,527	$ 0	0.0	$ 2,527
C12	Buildings	29,491	29,491	0	0.0	29,491
C201	Electronic Toll	619	619	0	0.0	619
C203	Electro-mechanical	2,048	6,729	4,681	228.6	5,200
C205	Carrier Equip.	46,273	84,385	38,112	82.4	84,385
C206	Radio	10,576	10,576	0	0.0	10,576
C207	Analog	8,445	19,927	11,482	136.0	13,985
C209	Digital	91,748	186,014	94,266	102.7	127,498
C4XX-	Station Apparatus	16,727	16,727	0	0.0	16,727
C60	Outside Plant	139,846	322,908	183,062	130.9	305,190
C8XX	General Plant	32,032	41,507	9,475	29.6	38,740
	Transfer from Acct. 100.2	-	-	-	-	36,987
Total		380,332	721,410	341,078	89.7	671,925

General's gross addition capital budget for 1988 for Account C203-Electromechanical was $7,042,000, consisting of $996,000 lines and terminals, $1,290,000 trunking, $1,838,000 pair gain CO terminals, and $2,918,000 unidentified. According to the testimony of DRA witness Danish, the combined cost of lines and terminals of $996,000 and trunking of $1,290,000 is $2.286 million, which for the 1,610 lines and trunks to be installed in test year 1988 computes to be a cost of $1,400 per line. According to this witness, $1,400 per line is excessive. DRA's estimate for the SxS additions (Account C203) was derived by multiplying the proposed 1,610-line additions by a cost of $160 per L/T to arrive at an amount of $252,000 for SxS growth. To this, witness Danish added

$1,838,000 proposed by General for pair gain CO terminals, resulting in a final estimate for this account of $2,062,000. Danish further testified that the L/T cost of $160 per unit was based on conversations he had with Mike Burke at Continental Telephone Company (Continental) and with an employee of General's affiliate, GTE Communications Systems. Rebuttal testimony presented by General indicated that the $160 cost per L/T estimate for Continental was based on two small (100 lines) work orders in the 1986 time frame and did not include trunking equipment, control equipment, or ANI equipment. An employee of GTECS, identified as Mr. Gronkiewicz, testified that he was the employee to whom Mr. Danish had referred but that he had never provided Mr. Danish with any cost information regarding electromechanical L/T additions. He further testified that he had informed Danish that the cost per SxS L/T would be difficult to estimate.

In addition to his testimony that the use of $160 per L/T was inappropriate, rebuttal witness Gronkiewitz testified that lines, trunks, and terminals are separate pieces of equipment and that witness Danish's combination of lines and terminals and trunking for computing the cost per L/T was therefore erroneous. "Trunking" in an SxS office refers to intraoffice trunking and is the intermediate hardware required to pass the dial digits through the central office from the line finder equipment to the connector terminal equipment or the interoffice trunk network to support the call volume growth. We are persuaded that such trunking is necessary and should be computed separately for purposes of estimating gross additions.

According to this witness's rebuttal testimony, the budgeted dollars for the category entitled "Unidentified" represent General's view of the amount needed to meet unforeseen equipment needs in the 1988 test year; these dollars are particularly important with respect to General's SxS offices which have very high fills and low margins for growth. According to the record, such high fills make the company more vulnerable to unexpected increases in line growth, therefore, an amount of "unidentified" plant must be provided for so that funds will be available to meet currently unidentified needs. It is noted, however, that at no time did General provide detailed backup of the unidentified $2,918,000 amount. We believe the inclusion of an unidentified amount in a budgetary proceeding may be valid, but because such specific amount was not supported on the record, we cannot find the total amount requested, $2,918,000, to be reasonable. However, in recognization of GTE-C's need to meet presently unforeseen equipment needs, especially with SxS central offices, we will adopt as reasonable for this proceeding an amount of $1.4 million which represents approximately one-half of its request. We will also adopt the balance of General's electromechanical Account C203 budget amounts for purposes of this proceeding, making a total of $5.524 million for gross addition of capital budget for 1988 and $5,200,000 as our gross additions to Account 100.1 for 1988 for this account.

DRA's estimate for gross additions to Accounts C205-Circuit Carrier Equipment for test year 1988 was $46,273,000 as contrasted to General's estimate of $84,385,000. The difference reflects the disallowance by DRA of three items of the account detail, namely "pending plans", "special services undetailed", and "unidentified". General subsequently introduced into this proceeding Exhibit 182 which lists all of the Account C205 projects that make up its total gross addition budget in work order detail. These work orders support General's estimate of the gross additions to this account of $84,385,000 and we will adopt this figure as reasonable for this proceeding.

DRA's estimate of additions to Account 100.1 for Account C207-Analog COSE is $8,445,000 as contrasted to General's estimate of $19,927,000. According to the testimony, the main difference between DRA's and General's estimates with respect to this account relates to DRA's use of an estimated cost per L/T of $425 and the disallowance of $4.768 million for items characterized as "other projects" with no explanation or information as to what the projects are. Witness Danish stated that he developed the estimate of $425 per analog L/T addition based on information provided to him by Pacific, which estimated a cost of $425 per line trunk addition to a No. 1 AESS analog switch, and by CS, which indicated to him a cost of $300 per L/T addition for the No. 2 EAX switch. Witness Danish utilized Pacific's higher estimate of $425 per line trunk addition in calculating his estimated aggregate cost of analog line additions for the test year 1988.

Rebuttal testimony presented on behalf of General indicated that the $300 per L/T of addition to the No. 2 EAX switch was actually at the low end of the range of $300 to $1,000 per L/T addition cost figure furnished by a CS employee. Furthermore, according to the rebuttal testimony, the $425 for the L/T figure reflects capital cost for both SPC analog and SPC digital switches and reflects Pacific's cost deflated to reflect 1977 equipment dollar amounts. Therefore, this $425 is, according to General, very much understated. General's rebuttal testimony has successfully raised some questions about the validity of DRA's estimates, however, the rebuttal did little to strengthen our confidence in General's showing which was marginal. We will, therefore, adopt a compromise between the two showings of $14 million for line addition growth. To this, we will add $274,000 for equal access and $14,000 for USS/MSS included in both General's and DRA's estimates. This yields $14,288,000 which we will increase to $15,410,000 to reflect the adopted telephone plant index of 1.0785.

According to the record, witness Danish also excluded from his C207 budget estimate the $4.768 million that General included in the category "Other Projects" on the basis that General provided "no explanation or any information, today, as to what these projects involved". General subsequently provided as Exhibit 184 a document which identified all of the projects by work order number. We will add this amount to the above $15,410,000 to yield $20,178,000 for the gross additions capital budget. Translating this figure to gross additions to Account 100.1 for the test year 1988 yields a figure of $13,985,000, which we will adopt as reasonable for this proceeding.

DRA's estimate of gross additions to Account 100.1 for Account C209 digital COSE for test year 1988 is $91,748,000 as contrasted to General's estimate of $186,014,000. Tabulated below are the component items comprising General and DRA estimates, together with our adopted results. The bases for the adopted results are set forth in the ensuing paragraphs.

	DRA	General ($000)	Adopted
Digital - New	$ 51,038	$ 82,404	$ 78,037
Digital - Growth	9,065	39,923	13,823
Modifications	-	1,888	-
Line and Trunk Testing	1,833	-	1,833
Capital Planning Adj.	-	20,000	-
PPCF	-	2,530	-
Enhanced Switching	13,606	28,909	24,276
COE Tools	936	944	936
Emergency Generators	1,090	1,100	1,090
Special Projects			
USS/MSS	6,481	6,535	6,485
Unidentified	-	755	-
Analog/Misidentified	1,018	1,026	1,018
Subtotal	85,067	186,014	127,498
Times TPI	6,681	-	-
Total	91,748	186,014	127,498

General's estimate for new digital equipment of $82,404,000 is based on its budget estimates. DRA's witness testified that, in many instances, the budget amount of the COSE plant exceeded the bid amount in excess of 40%. On this basis, he believes General's figures are invalid. DRA's estimate is equal to the product of the number of L/Ts and the average weighted cost per L/T for rounds 5-8 of $177.94. On rebuttal General contended that the use of such an average cost is inappropriate because of the difference between round 5 of $155.14 and round 8 cost of $218.87. This position appears valid and we will adopt as reasonable the unit cost of $218.87 for round 8 increased by the TPI of 1.045 for 1987 and 1.0785 for 1988 to yield $246.68 per L/T. We will increase this by 10% to $271.35 to reflect the difference between the initial NTEP and the actual cost of installation. Applying this to the estimated number of new L/Ts utilized by the staff in its estimate yields a new construction figure of $78,037,000, which we will adopt as reasonable. DRA's estimate of $9,065,000 for digital growth was based on the above-discussed $177.94 per L/T per additional line. We will utilize the above-discussed $271.35 per L/T rather than the $177.94 used by DRA to arrive at our figure of $13,823,000 for growth which we will adopt as reasonable.

In rebuttal testimony, DRA witness Danish testified that prior to his cross-examination it was his understanding that the vendor does the line and trunk testing when he performs the construction of the switch. However, during cross-examination, this proved to be incorrect; so witness Danish included a line and trunk testing of $1,833,000 based on the application of the loaded labor cost to the product of 10 minutes per test time for each line and trunk and the number of trunks installed in the test years. The 10-minute figure was furnished to him by a representative of Continental Telephone Company. This amount appears reasonable and will be adopted for this proceeding.

This witness further testified that he applied the ratio of General's budgeted gross additions to Account 100.1 to derive revised figures for COE tools, enhanced switching, emergency generators, USS/MSS, analog/MISS, and the outside plant. We will adopt as reasonable for this proceeding the revised figures for COE tools, emergency generators, USS/MSS, and analog/MISS. DRA disallowed $1.888 million for an item budgeted in this account as "modifications". Rebuttal testimony presented by General indicated that every manufacturer of COSE releases an updated generic designed version for its previously purchased system, but does not project the cost for these design releases. Consequently General must estimate these costs and include them for budgeting purposes. DRA argues there is no evidence in the record that General will, in effect, purchase "modifications" from COSE manufacturers in the test year nor is there any evidence to establish the reasonableness of the amount budgeted for this amount. We agree and will disallow this item.

DRA also recommended disallowance of a $20 million capital planning adjustment on the basis General did not provide support material to justify this amount. On rebuttal General asserted that it had explained to witness Danish that the dollars budgeted under capital planning adjustment were specifically designed to meet unexpected requirements. General argues that on cross-examination Danish agreed it was appropriate for the company to have funds available to meet unexpected capital requirements. However, the only funds he recommended for unexpected projects would have to come from other identified programs in the budget which are unexpectedly canceled or which do not increase at the rate of growth the company forecasts when the budget was developed. General's rebuttal witness Bowman further testified that General has since completed a study recommending the conversions of its TSPS equipment to newer Operator Services System (OSS) equipment in 1989. According to his testimony, this replacement increases the capital budget requirement in 1988 by approximately $15 million, an amount currently not budgeted. We note that although it may be appropriate to include dollars in the 1988 construction budget for expenditures made in 1988 for this new equipment, the equipment will not be installed until 1989. Under these circumstances it will be inappropriate to allow the amount as gross additions for the test year 1988. The $20 million capital planning adjustment will be disallowed consistent with our past practices.

Another item disallowed by DRA was entitled "PPCF". According to the rebuttal testimony, this category is an indicator of the prepayment funds required for digital switch procurement. Further, according to the testimony of this witness, this capital budget amount must be included in the total budget estimate to allow General the funds to promptly pay for switches in its modernization program. DRA argues that its estimates only addressed digital COSE L/T additions for the test year and it is not important as to when payments are made to the manufacturer. DRA further argues the key variable is in what year the plant will go into service and payments made in 1988 for 1989 plant additions are probably excludable. We agree and will disallow the $2.530 million PPCF item.

The differences between General and DRA for enhanced switching reflect the recommended disallowance by DRA of $10.152 million for common channeling signaling and $5.039 million for Centrex. General's rebuttal testimony persuaded DRA that the $10.152 million for common channeling signaling was properly includable, but since the service is to be phased in in 1988 and 1989 with all the expenditures occurring in 1987 and 1988, DRA recommends that we allow 75% of the proposed expenditures in 1988 or $7.65 million. This proposal appears reasonable and we will adopt it.

DRA's recommended disallowance of $5.039 million for Centrex was based on its understanding that the NTE in competitive bid rounds six to eight included a provision for Centrex service. Further, DRA did not know when Centrex features would be available. Rebuttal testimony by General clarified that the fee which appears as part of the NTE price is only for the software capability to provide Centrex within the switch and does not cover the cost of the Centrex equipment. DRA argues, however, that the record in this proceeding is replete with facts indicating that Centrex service offerings from digital COSEs were delayed and that at the time the DRA witness was conducting his investigation there were no Centrex services being provided from a digital switch in General's service territory. Consequently, according to DRA, it was proper to disallow the cost. DRA further argues that the assumed availability date of the GTD5 switch was changed from March 1987 to June 1988, thereby pushing back the EBSS delivery capability by 1.25 years for 40% of the central offices. Because of the uncertainties of the extent of Centrex availability in General's service territory, DRA urges us to disallow the Centrex cost. We will disallow the above discussed 40% of the Centrex budget item because of the uncertainties occasioned by the delay in delivery of the switching equipment.

We will adopt as reasonable for this proceeding for enhanced switching the amount of $24.276 million in keeping with the above discussion. The total amount for Account C209 computed in accordance with the above discussion is $127,498,000, which we will adopt as reasonable for this proceeding.

General's outside plant (OSP) construction budget for 1988 is $334.730 million as compared to DRA's estimate of $137.353 million. This budget included some dollars for items outside the test year. When viewed strictly in terms of test year 1988, these amounts translate to gross additions to Account 100.1 (for Account C60) of $139,846,000 for DRA and $322,908,000 for General.

Testimony presented on behalf of DRA by witness Danish indicated that:

1. Although General's customer concentration in its service area is 277 access lines per square mile as compared to Pacific's 231 access lines per square mile, General is spending more than twice as much as Pacific for every new inward movement line.

2. General's outside plant expenditure indicates that it spends $257 per line of

inward movement as compared to Pacific's $120 per line of inward movement.

3. In 1986, General had over 1,800 people in outside plant construction while Pacific had 3,973. In view of the fact that Pacific had about four times as many customers as General, it appears that General had an excess of over 900 people in outside plant construction force (3,973 divided by 4 minus 1,800) in 1986.

4. Inasmuch as the central office modernization program is virtually over, it appears that General had shifted resources from central office construction to outside plant construction. Outside plant is budgeted for $334 million in 1988 as compared with an expenditure of $260 million in 1986 with over 80% of the budget attributed to growth.

5. General tried to justify the outside plant construction expenditure by presenting the "CAF Plan" (customer access facilities plan). Upon studying the CAF Plan, DRA determined that the maintenance savings due to the CAF Plan are minimal.

6. Using TPIS and Pacific's estimate for outside plant, DRA determined that Pacific will spend (labor and material on contract) $128 per inward line movement.

7. Using $128 per inward line movement, DRA projects for "normal growth" $112.793 million for test year 1988.

8. DRA has determined that the dollars presented by General in the CAF Plan for service and San Fernando grooming and analog subscriber-carrier removing should be accepted and therefore adopted. Adding construction cost of $15.44 million for

grooming[3] and $9.17 million for analog subscriber removal to the product of $128 and the number of inward line movement results in a total estimate for outside plant of $137.353 million.

Rebuttal testimony presented on behalf of General by Ms. Young indicated that:

1. The CAF Plan is a companywide "tops-down" description of changing technological and service environment in the CAF network that (a) quantifies the effects of introducing digital pair gain devices and fibre optics into the local loop, (b) identifies the expected change in the sophistication of service that General customers will require, and (c) identifies the need to constantly improve the quality of service provided to General customers.

2. The vast majority of General's C60 investment is required to meet new customer service requirements in General's service territory.

3. The total circuit gain is a much more meaningful driver of OSP investment than inward movement lines.

4. The major factors that contribute to General's OSP capital requirements which are budgeted to Account C60 are (a) the total circuit gain, (b) the level of plant utilization in the CAF network, (c) the level of pair gain deployment, (d) the type of OSP construction (aerial, buried, underground, conduit etc.), and (e) the condition and age of the existing plant.

5. Inward movement activity only creates additional OSP cost if the activity occurs at a new location or address not already served.

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3 Grooming is the removal of loose wires and circuit elements which for one reason or another are no longer functional.

6. A lower level of utilization means there is more existing capacity available to meet customer demands for service and only after the excess idle capacity is used would there be a requirement to add additional plant.

7. A telephone company with high utilization levels may need to invest in additional plant over and above that required for the new circuit gain in order to lower its utilization levels and to increase its plant margins.

8. In terms of average investment per pair mile, underground construction in conduit is the least costly for large cables provided vacant conduits exist; direct burial construction is the most expensive since you need to dig a trench for each cable placed; and aerial construction falls somewhere between underground construction in conduit and direct buried.

9. The APF utilization percentages for the feeder portion of the CAF network is 67.6% for Pacific and 77.5% for General.

10. Based on a 19 central office sample taken in 1987, General determined its average distribution plant utilization level is 40% as compared to Pacific's distribution plant utilization factor of 28%.

11. The $334 million additions to outside plant are required to meet the service needs of General with the majority of the investment necessary to meet the increase and demand for new service. Such an investment would not result in unneeded plant investment which will increase rate base.

We are persuaded that the level of plant utilization in the CAF network, the level of the pair gain deployment, the type of outside plant construction, and the age and condition of existing facilities are sufficiently different between General and Pacific to preclude the use of Pacific's unit costs in estimating the allowance for General's OSP construction. We are also persuaded that the key driver of the construction budget is the number of new circuits that must be physically installed to meet that growth. We note with concern, however, that the unit cost per circuit gain used in General's computations for the 1988 test year exceeds that for the 1987 estimated year by far more than the increase related to the TPI. We can discern no reason for such a substantial increase and, for computing the growth figure, we will use the 1987 unit cost increased by the TPI for that year. Computing the growth in outside plant on this basis results in $274.27 million for growth which we will accept as reasonable for this proceeding. In addition, we will adopt DRA's other estimates for the outside plant account consisting of San Fernando grooming $14.89 million, analog subscriber removal $8.84 million, and pair gain $7.19 million, for a total of $305.19 million for 1988 test year plant additions to Account C-60 of Account 100.1.

General's 1988 construction budget for general equipment Account C8XX is $48.051 million. It is DRA's understanding that $41.507 million of this amount will be expended for plant that will go into service in 1988. DRA has adopted the $41.507 million budget item and has reduced it to reflect DRA's estimated employee level for 1988 by applying the ratio of its employee estimates for 1988 to General's estimated employee 1988 level. On rebuttal General's witness Hesse indicated that such a reduction would be inappropriate because almost half of the 1987 additions and approximately one-third of the 1988 additions are for new hardware and software enhancements necessary to achieve productivity gains in the maintenance accounts and, therefore, are not directly associated with a given employee level. We will accept General's one-third of the account, or $13,836,000, as being not dependent upon the number of employees, and reduce the balance of $27,671,000 to reflect our adopted 10% force reduction to yield an adopted figure of $38,740,000. The total capital additions to Account 100.1 for test year 1988 computed as discussed above including the transfer from Account 100.2 to Account 100.1 of $36.987 million is $671,925,000, which we will adopt as reasonable for this proceeding.

Both DRA and General agree that property held for future use is equal to $79,000 and the Communications System Corporation adjustment is a negative $15,122,000. Adding these figures to the above $671,925,000 yields a total figure for telephone plant added for test year 1988 of $656,882.

M. Rate Base

Rate base consists of the sum of weighted average plant in service, property held for future use, working cash allowance, materials and supplies less the sum of depreciation reserve, and deferred taxes, and adjustments for interstate construction work in progress, commission corp. TPIS, and commission corp. depreciation reserve. The following tabulation sets forth the rate base for test year 1988 as estimated by DRA and General, together with our adopted results:

Rate Base

Item	DRA	General	General Exceeds DRA Amount	General Exceeds DRA Percent	Adopted
			(Thousands of Dollars)		
Wtd. Avg. Plant in Service	$6,320,960	$6,843,968	$523,008	8.3%	$6,675,298
Interstate Tel. Plt. Under Const.	-	48,112	48,112	0.0	-
Property Held For Future Use	79	79	-	0.0	79
Materials & Supplies	16,874	25,021	8,147	48.3	23,258
Working Cash Allow.	15,785	4,726	(11,059)	(70.1)	18,759
Less: Depr. Resv.	2,024,056	2,051,951	27,895	1.4	2,015,626
Deferred Taxes	656,125	695,140	39,015	5.9	679,418
Total Rate Base	3,673,518	4,174,815	501,297	13.6	4,022,350
Adjustments:					
L&B Transfer	(1,756)	-	1,756	(100.0)	-
Competitive Bid	(50,000)	-	50,000	(100.0)	(7,900)
Cash Compensation	(8,100)	-	8,100	(100.0)	-
Comm. Syst. TPIS	(15,122)	(15,122)	-	0.0	(15,122)
Thousand Oaks	(42,700)	-	42,000	(100.0)	-
Comm. Syst. Depr. Resv.	11,837	11,706	(131)	(1.1)	11,706
Total Adjustment	(105,840)	(3,416)	102,424	(96.8)	(11,316)
Net Adjusted Rate Base	$3,567,678	$4,171,399	$603,721	16.9	$4,011,034

(Red Figure)

DRA's estimate for materials and supplies is $16,874,000 as compared to General's estimate of $25,021,000, a difference of $8,147,000 or 48.3%. The major reason for the disparity is different estimated plant investment. Consistent with our adopted weighted average plant balance we will adopt as reasonable a material and supplies figure of $23,258,000.

Working cash allowance (WCA) is designed to compensate investors for funds provided by them which are permanently committed to the business for the purpose of paying operating expenses in advance of the receipt of offsetting revenues from the company's customers and in order to maintain minimum bank balances.

The following tabulation sets forth the component parts of the WCA as estimated by DRA and General, together with our adopted results:

Working Cash Allowance

Item	DRA	General	General Exceeds DRA Amount	General Exceeds DRA Percent	Adopted
			(Thousands of Dollars)		
Gross Working Cash Requirement:					
Misc. Spec. Deposits	$ 1,887	$ 1,918	$ 31	1.6	$ 1,887
Misc. Receivables	57,702	58,658	956	1.8	57,702
Working Funds	325	329	4	1.2	325
Other Deferred	32,512	33,596	1,084	3.3	32,512
Prepayments	16,303	16,572	269	1.7	16,303
Pay Exp. Before Revenues	-	15,055	15,055	0.0	0
Total Gross Req.	108,729	126,128	17,399	16.0	108,729
Deduction of Funds Not Supplied By Investors:					
Avg. Amt. Coll. Before Exp.	(23,652)	-	23,652	-100.0	(24,636)
Excise Taxes	692	692	0	0.0	692
City Users Tax	451	451	0	0.0	451
Employee Withhold.	11,665	11,864	199	1.7	11,665
Other Def. Credits	73,923	75,147	1,224	1.7	73,923
Rev. Settlements	(16,666)	(16,666)	0	0.0	(16,666)
Cr. from Suppliers for Cap. Mat'l.	30,379	30,379	0	0.0	30,379
Lag Pay Cap. Items	14,162	19,535	5,373	37.9	14,162
Total Deductions	90,954	121,402	30,448	33.5	89,970
Working Cash Allow.	15,785	4,726	(11,059)	(70.1)	18,759

(Red Figure)

According to the testimony of DRA witness Cooper, the reasons for the difference in the working cash component items are: (a) the use of DRA nonlabor GNP deflators and the percentage change in access lines as computed by DRA witness Berry; (b) the inclusion of other deferred charges consistent with the audit recommendation made by witness McCarthy ($253,000 for inventory from employee stores and $199,000 for trade show expense); and (c) the use of DRA witness's estimates of the capitalized portion of expenses computing the item for other funds available from lack of payment in capitalized items. We previously adopted DRA's estimates for items (a) and (b) and we will therefore adopt DRA's estimates for these items. For other funds available from lag in payment of capitalized items, we will conform our adopted result to the previously discussed adopted estimate of capital additions.

The lag days associated with the payment of expenses were calculated by General and reviewed by DRA. Most discrepancies were resolved prior to the filing of General's application with the exception of one item: the lag days associated with GTEDs payments. General's estimate was 38.37 days as contrasted to the staff's estimate of 44.275 lag days. The difference was due to General's omission of the February 1985 payment of $4,471,000 and the incorrect statement of the midpoint accrual dates for September and October 1985. We will adopt DRA's estimate of 44.275 lag days.

Both General and DRA used 34.810 days as the average lag in collecting revenues. However, DRA used 30.353 days as the average lag payment of bills before the collection of revenue, whereas General used an average lag in the payment of expenses of 32.38 days. As the result, DRA had an excess of expense lag over revenue lag of 4.457 days as compared to General's 2.43 days. We will adopt DRA's estimate of 34.810 days as the average lag in collecting revenues as reasonable for this proceeding. Our adopted average lag or payments reflects our level of adopted expenses.

N. Summary of Earnings

The following tabulation summarizes our adopted results of operation for test year 1988 for the company as a whole and its intrastate operations which is also reflected in Appendix D of this decision:

General Telephone Company of California
Summary of Earnings
1988 Test Year
($000)

Item	Total Company		Adopted	
	DRA	General	Total Company	Intrastate
Operating Revenues				
Local Service	$ 779,228	$ 835,224	$ 781,157	$ 781,157
Toll Service	781,079	825,325	822,393	822,393
Intrastate Access	215,908	201,963	206,526	206,526
Interstate Access	480,425	480,425	480,425	-
Miscellaneous	322,670	262,770	281,981	258,162
Surcharge	73,287	184,675	74,730	74,730
Gain on Sale on Prop.	10,490	0	4,485	3,639
1987 Attrition	-	(52,978)	-	-
Less: Uncollectibles	18,594	24,368	21,638	20,438
Total Operating Rev.	2,644,493	2,713,036	2,630,059	2,126,169
Operating Expenses				
Maintenance	412,062	491,676	432,977	338,060
Traffic	60,633	74,563	63,624	56,788
Commercial	240,198	275,725	257,207	212,825
Gen. Off. Sal. & Exp.	179,385	197,636	190,072	160,482
Other Oper. Exp.	133,213	235,711	191,456	156,520
Subtotal	1,025,491	1,275,311	1,135,336	924,675
Depreciation	497,161	539,288	524,494	428,000
Taxes Other than on Income	94,516	113,506	106,135	84,135
State Income Tax	71,528	59,464	68,307	57,295
Federal Income Tax	243,333	184,207	181,560	147,142
Total Operating Exp.	1,932,029	2,171,776	2,015,832	1,641,247
Net Operating Income	712,464	541,260	614,227	484,922

General Telephone Company of California (Cont'd.)
Summary of Earnings
1988 Test Year
($000)

Item	Total Company		Adopted	
	DRA	General	Total Company	Intrastate
Adjustments of Income				
CCFT	-	(2,802)	-	-
Communications System	-	865	-	-
GTE Directories	-	4,131	-	-
Total Adjust. to Income	-	2,194	-	-
Net Adjusted Income	712,464	543,454	614,277	484,922
Rate Base				
100.1 Tel. Plant in Service	6,203,282	6,843,968	6,652,276	5,266,757
100.2 Tel. Plant Under Const.	0	48,112	0	0
100.3 Prop. Held For Future Use	79	79	79	62
Materials & Supplies	16,874	25,021	23,258	17,557
Working Cash	15,785	4,726	18,759	15,278
Less: Depr. Reserve	2,012,217	2,051,951	2,003,920	1,590,739
Less: Def. Taxes	656,125	695,140	679,418	537,127
Total Rate Base	3,567,678	4,174,815	4,011,034	3,171,788
Adjustment to Rate Base				
Communications System	-	(3,416)	-	-
Net Adjusted Rate Base	3,567,678	4,171,399	4,011,034	3,171,788
Rate of Return	19.97%	13.03%	15.31%	15.29%

(Red Figure)

O. Net-to-Gross Multiplier

The net-to-gross multiplier (NTG) is 1.56267 computed as follows:

Item	Intrastate Total
	1.00000
Uncollectible rate	0.01200
Difference	0.98800
CCFT at incremental rate 0.018635	0.01841
Difference	0.96959
FIT at 34%	0.32966
Difference	0.63993
1.0000 ÷ 0.63993 =	1.56267

P. Intrastate Revenue Requirement ($000)

Rate Base	$3,171,788
Rate of Return (D.87-12-070)	0.1090
Net Revenue	345,725
Net Revenue at pres. rates	484,922
Difference	(139,197)
Revenue requirement (Diff. * NTG)	(217,520)
Interstate USF (High Cost)	(784)
D.87-12-070 Rev. Req. Add Back	(112,190)
Total Revenue Requirement	$(330,494)

VI. Total Factor Productivity

A. General

This Commission is considering the use of econometric models to measure the productivity for total utility operating expenses. Such models relate changes in a utility's level of production to changes in the level of required resources. The percentage change in the productivity index from one period to the next measures the savings due to productivity.

In presenting its case for adoption of total factor productivity (TFP), DRA chronicles the Commission's past interest in the matter:

> "In recent years the Commission has indicated an interest in developing a method of measuring productivity. The ability to quantify productivity can be used to measure the "monopoly rent" that traditional techniques of regulation cannot identify in the ratemaking process. The measure of productivity can then be used to chart the progress that a utility makes toward streamlining its operations and reducing its costs to provide a pricing structure that reflects the realities of an increasingly competitive environment. Or it may be used directly as a ratemaking tool to adjust the utility's revenue requirement.
>
> "In the last two major energy utility general rate proceedings (Pacific Gas and Electric & Southern California Edison) the utilities and the staff have produced studies of differing approaches to measuring productivity. In the Pacific Gas and Electric general rate case staff developed a Total Factor Productivity (TFP) index which attempted to measure the growth of output due to advances in technology. (D.86-12-095, mimeo page 37) Although the Commission declined in that proceeding to adopt staff's TFP methodology, it did indicate its interest in this approach:
>
> > While we are attracted to the TFP concept, we generally agree with PG&E's and Edison's criticism of staff's TFP showing. There

> are flaws in the staff analysis particularly in the use of incorrect and inconsistent data...<u>However, we find merit in adjusting total projected operating expenses to reflect potential productivity improvements in addition to the account-by-account productivity adjustments adopted in this decision. Such a broadly based productivity adjustment will provide PG&E with a necessary incentive to improve efficiency and further reduce operating expenses</u>. (D.86-12-095, mimeo page 37, emphasis added)" (DRA Opening Brief, p. 164.)

DRA's estimate of test year 1988 productivity on a companywide basis for General was presented by Public Utilities Regulatory Program Specialist Dr. Faramarz Yazdani, and indicated that:

1. For the test year 1988, the econometric model forecast productivity gains of $181,068,777.

2. Based on historical productivity trends General can reduce its cost of service by the above $181,068,777 in providing the level of service forecasted for 1988. (The $181,068,777 is not an independent productivity gain, but is structured as a validation of the plant account analysis on which DRA relies for its productivity findings. In other words, DRA does not independently recommend a productivity adjustment.)

3. The econometric cost model in his report confirms and validates the estimated operating cost adjustments made by Results of Operations (R/O) witnesses.

4. The $194 million in reduced operating expenses estimated by the R/O witnesses is based on detailed account-by-account analysis.

5. The econometric model looks at productivity from a multi-factor approach and captures productivity arising from both direct as

well as cross-relationships between the inputs which, generally speaking, may not be totally captured in the partial-factor productivity approach.

6. The great strength of the account-by-account approach lies in its detailed scrutiny of each account. The R/O witnesses utilizing this approach are also able to incorporate any new technological developments in their cost studies to arrive at forecasts of future expenses.

7. The two methods thus support the findings of each other and should be viewed as parallel and complementary studies.

8. A firm improves its productivity if the growth rate of its outputs is larger than the growth rate of its inputs.

9. DRA specifies a sufficiently general functional relationships for its cost model which is general enough so that it does not impose a priori restrictions on the true production process, but rather is flexible enough to allow the historical data itself to tell us what this relationship would be. For this reason, DRA has used the transcendental logarithmic (trans log) functional form to estimate how General's cost and labor requirements are related to those factors affecting them.

10. The only condition DRA imposes on its function is that of cost minimization. It assumes the company in any period will vary its input combination in any way which minimizes the cost of producing a given output or a given set of outputs.

On rebuttal, General's witness Dr. Mark Schankerman contended that the MFP study presented by Dr. Yazdani is fatally flawed in its empirical implication because:

1. The empirical results of the model used by DRA violate the fundamental theory for use of the short-run cost function to determine productivity.

2. The required behaviorial assumption that management optimizes its variable cost cannot be met for monthly observation periods.

3. DRA's measure of capital understates the role of capital and overstates the level of productivity gain.

4. DRA's results show productivity gain at considerable variance from what other studies have found.

5. The analysis presented by DRA does not validate the high level of productivity gains DRA claims to have identified through its plant account analysis of General's performance.

B. <u>The Duality Theorem</u>

According to Schankerman, the duality theorem says that if certain assumptions about firm behavior hold, then one can measure the rate of technical process from a short-run cost function provided that this short-run cost function has certain mathematical properties. There are three main assumptions about firm behavior which are made:

1. The firm can purchase its variable inputs (such as labor and materials) at a fixed price unit.

2. The firm is constrained to produce a certain level of output.

3. The firm uses some input which it cannot vary within the interval of observation which is the so-called fixed input.

If the above three assumptions about firm behavior hold, then the duality theorem proves mathematically that the rate of technical progress can be measured equally well by looking at a short-run cost function and it simultaneously proves that the short-run cost function which is to be used must have the following basic properties:

1. Variable costs must rise if the price of any variable input increases.

2. Variable costs must rise if the level of any output which the firm produces increases.

3. Variable costs must decline if the stock of capital available to the firm increases.

If the above three properties are not met, Schankerman maintains that it violates the fundamental duality theorem to argue that one can measure the rate of technical change from a short-run cost function which does not satisfy the required properties.

According to Schankerman, the requirement that the cost function vary negatively with the stock of capital was violated by empirical results at every point in the sample period (i.e. for every monthly observation during the period 1975 to 1986). Furthermore, the property that requires the level of variable costs increase when the level of output rises was violated for every observation in the sample period for the number of toll calls. Inasmuch as two of the three properties of the short-run cost function were violated by DRA's study, Schankerman believes the cost function is empirically invalid and cannot be used for any interpretative purposes, including the measurement of technical change. DRA admits it is true that unrestricted estimates are not consistent with economic theory, but restricted estimates that impose consistency yield virtually identical results. Such a fact, according to DRA, makes the study even more valid and the effects of technical progress more robust to alternative specifications.

General's witness Schankerman has raised fundamental questions about the theoretical underpinnings of DRA's underlying cost functions. Moreover, the record does not support DRA's claim that it is possible, in some instances, for the short run cost function to be rising in the stock of capital. (GTE-C Reply Brief p. 63.) Thus, we do not believe DRA has adequately countered the criticisms posed by General's Schankerman, and it appears from the information presently available to us, that DRA's analysis is flawed in that regard.

C. Monthly Data

DRA's TFP study is based on monthly data on all variables for the period 1975-1986, yielding a total of 144 observations. Dr. Schankerman testified that it is standard practice to apply cost function methodology to annual data rather than to some shorter interval of observation such as monthly or even quarterly data. He testified that the use of such annual data is necessary because short-run cost functions require the assumption that the firm be able to vary freely the variable inputs within the interval of observation. He further testified that any desired change in the quantities of variable inputs which firms choose to make is assumed fully implementable within the interval of observation. One of the variable inputs utilized by Dr. Yazdani was labor. It is Dr. Schankerman's position that labor computed on the number of employees is not variable within the monthly period and consequently the entire cost function model is misspecified and, in general, all the parameter estimates are incorrect and unreliable.

DRA argues that the reason virtually all productivity studies have been based on annual data is due to data constraints, not desires of researchers. In particular, the reason that most previous studies were based on annual data is that data is taken from publicly available data gathered by governmental agencies and almost all the data are collected only on an annual basis. DRA further argues that even if one uses quarterly rather than monthly data the empirical findings concerning technical progress are virtually unchanged. DRA further argues that it is worth noting its staff employed monthly data to estimate TFP for Southern California Edison Company (Edison) and that the use of such data was never an issue for that study which has been blessed by this Commission. In this respect, General points out that the Edison study was based on labor hours rather than on the number of employees and consequently Edison was able to vary freely within the monthly interval observation this variable input. It appears to us that General would be unable to vary the number of employees up and down within the monthly intervals to minimize the cost and therefore we are inclined to agree with General's position on this matter.

D. Capital Measurement

According to Schankerman's rebuttal testimony, the proper measure of the capital stock should capture variations in the utilization rates which may be substantial over time and should reflect any upgrading in the productive efficiency of the capital. Furthermore, failure of the measures of variables actually used to correspond closely to the measures we need for the analysis can cause serious problems for the empirically estimated cost function. DRA argues that at numerous times in his testimony, Dr. Schankerman acknowledges that capital measuring problems are not unique to DRA's studies but are endemic to virtually all current productivity research. Furthermore, DRA argues that Dr. Schankerman cannot state with any confidence whether failing to account for quality changes underestimates or overestimates multi-factor productivity growth. DRA further argues that it appears that the quality changes have also presumably been affecting General's output and thus it is quite possible that DRA's 16% productivity estimate understated actual productivity gains realized by General. In its reply brief, General argues that a proper measure of the stock of capital is needed in order to capture the contributions of capital equipment to the production process. Furthermore, DRA and General agree that there has been a significant technological change in the transition from electromechanical step-by-step switching equipment to computerized electronic equipment. General acknowledges that it has received the benefits of greater productive capacity by being able to absorb increased demands through acquisition of computerized switching equipment. According to General, the savings between purchases of new technology and continued purchases of old technology are realized by the ratepayer who pays only for the new and more productive equipment. These savings are thus built into the ratemaking process. According to General, DRA's concept in measuring capital stock simply by listing its annual depreciated net value adjusted only for inflation does not capture the measure of capital that will be transferred to the residual proxy for productive gain set out as "T" in DRA's equation. Furthermore, according to General, a failure to measure it in capital forces the model to place it in the gains in "T" resulting in an erroneous overstatement of productivity gains to be taken back a second time. We agree with General that an improper measure of the stock of capital can result in overstatement of the productivity gains but we also agree with DRA that failure to consider the quality changes that have been affecting General's output could result in an understatement of the productivity gain. Consequently, DRA's failure to measure the capital quality adequately would not in itself cause us to fault the results of the study.

E. Comparison of Studies

Dr. Yazdani's study indicates the empirical finding is that the average rate of technical change in general during the period 1975 to 1986 was 16% per annum. Dr. Yazdani notes, however, that one should not compare this estimate with estimates of technical change and long-run total cost inclusive of capital expenses. Since the empirical evidence on technical change from scientific studies of other firms and industries discussed during cross-examination in this matter relates to long-term cost, one must first translate Dr. Yazdani's findings into a corresponding long-run figure. Since variable costs amount to approximately one-half of total cost for General, according to Dr. Yazdani, a 16% per annum estimate for variable cost corresponds to about 8% per annum figure for a total cost. According to the rebuttal testimony of Dr. Schankerman, this calculation seems plausible on its face, but turns out to be badly incorrect in this case.

According to the rebuttal testimony of Dr. Schankerman, examples of "growth accounting" computations of TFP growth include the study of a wide range of regulated and unregulated industries by Kendrick and DRA's report for the Pacific Gas and Electric Company (PG&E) rate case. The basic findings in both studies are that the rate of growth of TFP in a wide range of industries including public utilities is on the order of 2% to 4% per annum. Such growth accounting studies are not capable of decomposing the growth in TFP into separate components due to technical change in economies of scale. Therefore, if there are any economies of scale in the industries studied, the measured TFP growth actually overstates the growth due to technical change. Further, according to Schankerman's testimony, econometric studies of technical change using cost functions and related methods covering a wide range of different regulated and unregulated industries and studies of telemetric communications all find rates of technical change in the range of 1% to 4% per annum. Because of the wide discrepancy between the above-mentioned studies and Dr. Yazdani's study, it is General's position that Dr. Yazdani's study results are invalid.

DRA argues that although an 8% annual rate of technical change is substantial, it is not unusual and notes that for the period in the 1970s multifactor productivity in Japanese manufacturing grew at the rate of 6% to 9% per year, depending on the procedure employed. DRA further argues that if industries set prices equal to marginal cost and if quality adjusted prices in the computer equipment industry drop by over 20% per year somewhere (either in the parts supply business to the computer firms or in the computer firms themselves) there must have been a great deal of technical change much greater than 8% per year. In its reply brief, General argues that it has searched the records for any discussion concerning the progress of Japanese industry or its relativity to the productivity of a regulated U.S. utility and found none. It argues further that had DRA thought this was important it had an opportunity to raise it during the hearing, which it did not do. General notes for comparison in the PG&E rate case, DRA recommended savings of 3.3% for the electric department and 2.6% for the gas department and the productivity gain recommended through total factor productivity analysis in Edison's rate case was estimated at 2.4% for the historical period studied and 3.4% for the forecasted test year. Consequently, according to General, DRA's recommendation for this case is several times greater than what DRA had included from productivity analysis of other utilities.

F. Other CPUC Matters

Since DRA has recommended that we use the TFP study only as a check against our adopted productivity factors we do not find it necessary to either adopt or reject the study. We have set forth our concerns with various elements of the study in the proceeding discussion but for purposes of this decision, we are confident that the account by account productivity adjustments we have made accurately reflect the productivity gains expected of General for test year 1988.

As we have previously stated (in D.86-12-095 for PG&E and D.87-12-066), it is difficult to apply TFP to a large public utility. DRA has made substantial refinements to its TFP approach since those decisions and we hope that it will address the concerns noted here when it next presents TFP for our consideration. We expect the utilities to regulate to address TRP seriously in future general rate case proceedings.

VII. Attrition

As discussed in the section entitled "Labor Productivity Adjustment for Attrition Years 1989 and 1990" supra, we are partially adopting DRA's proposal for an attrition formula with a base 5% factor based on the change in number of access lines for employee (ALPE). Any savings in excess of the 5% productivity level will be shared equally between the ratepayers and General.

We are aware that GTE has announced a substantial reorganization that may affect the factors we are adopting to implement productivity sharing through attrition. There is no evidence about this reorganization on the record. If General or any other party has concerns about the accuracy of productivity sharing given the reorganization, they should develop a showing describing the basis for their concerns and present it as a petition for modification of this order. We would limit such reconsideration to the attrition mechanism itself, rather than addressing the reorganization more broadly; we consider such measures as means to implement the staffing reductions that are represented in this rate reduction.

In its direct showing, General requested the option of filing for operational and financial attrition in 1989 and 1990. It recommended that the methodology ordered by this Commission and used as a basis for General's 1986 attrition award (D.85-03-042 and D.85-12-081) continue as a proved mechanism. However, that mechanism was subsequently modified by D.86-12-099 in Pacific's A.85-01-034 for a 1986 test year rate case. General therefore proposes that the attrition formula as modified by D.86-12-099 be used for attrition years 1989 and 1990. We will adopt this recommendation for this matter, subject to any changes resulting from our current investigation, I.87-11-033, which is considering the merits of continuing attrition adjustments for telephone companies generally, as part of the establishment of new regulatory framework for local exchange telephone utilities.

As noted in Interim D.87-12-070 on this matter, we indicated that events occurring in the financial market in October 1987 indicated that we should reconsider our plan of considering revision of the ROE and capital structure every three years and have General's capital structure, interest costs, ROE, and financing plans reviewed in the attrition years. The order that follows will so provide.

In addition in D.88-06-024 in A.88-05-009, we have specified that General file its application for 1989 financial attrition by July 15, 1988, which General has filed and its advice letter for 1989 operational attrition by October 1, 1988.

recommendation for this matter, subject to any changes resulting from our current investigation, I.87-11-033, which is considering the merits of continuing attrition adjustments for telephone companies generally, as part of the establishment of new regulatory framework for local exchange telephone utilities.

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In addition in D.88-06-024 in A.88-05-009, we have specified that General file its application for 1989 financial attrition by July 15, 1988, which General has filed and its advice letter for 1989 operational attrition by October 1, 1988.

Financial attrition will be heard on a consolidated record for General and Pacific, as ordered in D.88-06-024.

VIII. Rate Design

To expedite the flow through of the revenue reduction and avoid any conflict with other ongoing proceedings, we will not address the final rate design at this time.

As previously noted, the gross revenue requirement reduction adopted in this decision is $330.494 million which includes the revenue requirement reduction of $112.190 million derived from the billing surcharges/surcredits ordered in interim decision, D.87-12-070 as revised by Advice Letter No. 5125, filed February 29, 1988.

For this interim decision, we will be spreading the additional revenue requirement reduction of $218.304 million ($330.494 less $112.190) by an incremental bill and keep surcredit of 13.45% on access services, on intraLATA message toll and toll private line services and on local exchange services. (I.e., for access services negative 0.296% plus negative 13.45% equals negative 13.746%.)

The development of the incremental bill and keep surcredit and the adopted billing bases are as follows:

	Adopted Billing Base ($000)	Revenue Requirement ($000)	Incremental Surcredit
Intrastate Access	$ 233,201	$ -31,363	-13.45%
IntraLATA Toll	663,367	-89,216	-13.45%
Local Exchange	726,639	-97,725	-13.45%
Total	$1,623,207	$-218,304	-13.45%

The above incremental surcredits will be reflected in General's Schedule Cal. P.U.C. No. A-38.

General has proposed moving the rate center for its Etiwanda Exchange to provide local calling between the Ontario and Etiwanda Exchanges. This proposal is supported by DRA and the City of Rancho Cucamonga, the principal area impacted by the proposed change.

The second phase of ZUM conversion authorized by D.84-06-111 in June 1986 authorized the creation of a ZUM Zone 2 route between the Etiwanda Exchange and the Ontario Exchange. Prior to the implementation of the second phase of the ZUM conversion, this route was local (EAS). The change from free calling to ZUM Zone 2 created a number of complaints from many customers in the Etiwanda Exchange. In addition, from the time of the original plan to the implementation of the second phase, considerable change had occurred in the demographics in Etiwanda and surrounding areas resulting in the calling interest of the communities within the Etiwanda Exchange being shifted toward the City of Ontario in the Ontario Exchange.

In addition, the Etiwanda Exchange rate point is outside the Etiwanda Exchange boundary. Because of the complaints, the change in the calling interest of the communities within the Etiwanda Exchange, and the location of the Etiwanda Exchange rate point, General proposes to (1) move the rate center coordinates for General's Etiwanda Exchange so that the route between the Ontario Exchange and the Etiwanda Exchange becomes a local route; (2) establish a route between the Etiwanda Exchange and the Rialto Exchange of Pacific which with the movement of the rate center of the Etiwanda Exchange becomes nine-mile route as a ZUM Zone 2 route; and (3) revise General's billing system to reflect the route revisions needed to accomplish the first two tasks. DRA recommends that we adopt General's proposal with the following conditions: (1) we provide for an implementation interval of 90 days and

(2) Pacific and General should be ordered to provide written notice to the customers of each respective company who will be impacted by such a change and that such written notice be provided within 30 days prior to the implementation of such a change. According to the record Pacific is receptive to the proposal to move the rate center of the Etiwanda Exchange as well as the proposed revision to rate calls over the Etiwanda-Rialto route at the ZUM Zone 2 rates. In view of the concurrence of the advisability of the proposed rate changes by General, DRA, and Pacific, we will adopt DRA's recommendations. The order will provide for an implementation date of 90 days and notice by Pacific and General to customers who will be impacted by such a change within 30 days prior to the implementation of such a change.

In D.85-06-113, we modified D.85-03-056, to require that within 14 days of local exchange utilities making their advice letter filings to reduce local access charges, AT&T-C pass on to its customers through a corresponding incremental reduction in the billing surcharge any reduction in its expense stemming from reductions in local exchange utilities' access charges. We will require a slightly different treatment in this instance consistent with our action in Pacific Bell's rate design decision in A.85-01-034. Specifically, we will require AT&T-C to accumulate the reduced access expense resulting from this decision in a memorandum account, with interest, commencing on the effective date of the General tariff revision and running through December 31, 1988 at which time AT&T-C shall roll this accumulated reduced expense into its computation of the effects on access rates of the SPF to SLU phase down of the local exchange carriers which will be reflected in AT&T-C's rates.

IX. Other Issues

We are issuing this decision as an interim decision to effect the rate reductions as soon as possible. Issues we will address in the next interim decision are as follows:

1. The final apportionment of the rate reduction to the various customer groups and the final tariff schedules, based on this record.

2. Issues raised at public-participation hearings including monthly inside wiring charges, physical size of bills, quality of service, pay phone availability, and the 13-second time limit for dialing.

3. Issues raised by Consumers Coalition of California such as General's current customer practices and procedures, new testing methods for measurement of accuracy of billing, charging for one-minute calls, installation of home billing devices, and the need for conducting studies directed at identifying customer need and services.

4. The relief sought for women and minority business enterprises by Public Advocates as follows:

   a. The Commission clearly and strongly chastise General for having the worst record among major utilities.

   b. General should be required for the year 1987 and for all subsequent years to provide a detailed breakdown by both percentage and dollar amount of contracts (by sex and for each ethnic group including Filipino-American) for each of the anticipated 23 categories that it will be using.

   c. General be required to adopt Pacific's minority business task force recommendations, the results of which are producing major changes at Pacific in order to insure very substantial and very significant progress necessary to achieve its February 8, 1988 goal of 20% of contracts to W/MBEs.

   d. General be required to develop effective joint ventures as set forth in Southern California Edison's opinion in order to help achieve its goal of 20% contracts to W/MBEs.

   e. A sum equal to one-fourth of 1% of General's contract awards in 1987 ($2 million) be set aside to be used to implement relief in c. and d. above and the February 8, 1988 CPUC filing setting 20% goal within five years.

f. General specifically report on an annual basis the relationship of bonuses awarded to top executives and their W/MBE achievements under the February 8, 1988 filing.

g. All utilities be required to submit "77K" salary reports that clearly set forth actual salary with ethnic and gender identification.

5. The issue of whether or not General should be ordered to adjust its rates for the 1988 test year so as to flow through to ratepayers approximately $27,582,755 or other equivalent amount of tax savings it has realized as a result of call premium, on amortized discount, and discount related to the retirement of high interest bearing bonds.

6. Consumers Coalition of California's request for finding of eligibility for compensation.

7. Public Advocates, Inc.'s request for finding of eligibility for compensation.

X. Findings and Conclusions

Findings of Fact

1. An additional incremental revenue requirement reduction of $218.304 million for a total reduction of $330.494 million is appropriate for the test year 1988.

2. A rate of return of 10.90% for test year 1988 found reasonable in D.87-12-070 dated December 22, 1987 should remain in effect.

3. To effect the above revenue reduction, the surcredits set forth in Appendix A to this decision should be effected on a bill and keep basis.

4. A total of $165.4 million for the test year 1988 level of GTESC expenses to be prorated to General and the other GTOCs is reasonable.

5. A prorate factor of 29.6% to allocate GTESC expenses to General is reasonable.

6. DRA's 19.8 AWT figure is reasonable given its development with reference to appropriate comparisons with similar operations at other telephone companies.

7. A reasonable expense allowance for Account 674-General Services and Licenses for the test year 1988 is $43.4 million.

8. Since General has not supported its Account 675-Other Expenses estimate, DRA's figure of $5,141,000 which uses lower escalation factors, lower estimate of "cost billed to others," and excludes dues payable to the US Telephone Association, consistent with Commission policies, is reasonable, and adopted.

9. A telephone plant adjustment equal to a negative capitalized sales adjustment of $15,122,000 minus the associated depreciation reserve of $11,706,000 or $3,416,000 and a corresponding depreciation expense of $1,370,000 is a reasonable ratemaking adjustment for GTE Communications System Corporation.

10. A ratemaking adjustment to expenses other than taxes for the operations of the directory corporation of $9,001,000 is reasonable.

11. It is reasonable to require General to conduct a competitive analysis of its directory service contract consistent with the preceeding discussion.

12. General's revenue requirement should not be adjusted to reflect the earnings of GTE Telecom Marketing Corporation resulting from a marketing agreement with AT&T Communications covering the period from May to December 1985.

13. It is reasonable to require General to conduct a competitive analysis prior to its next rate filing and include the study in its work papers to support the continued affiliate transactions between General and GTEDS.

14. A GTEDS adjustment of $3,044,000 to reflect two-thirds of the 1988 implemental cost of customer records and billing system and facilities management system is reasonable.

15. A 1988 test year expense of $9,885,700 for Account 996-Computer Usage is reasonable.

16. It is reasonable to adjust General's revenue requirement for test year 1988 by $687,000 to reflect imputed Yellow Page fillers for GTEL.

17. It is reasonable to adjust General's 1988 test year revenue requirement by $762,000 to recognize the expected revenues for the cost of providing 1988 referrals to GTEL and $2,361,000 to recognize the expected revenues for the market value of providing projected 1988 referrals to GTEL.

18. It is reasonable to require General to establish referral guidelines to track successful and unsuccessful referrals to GTEL, and to perform a study to be completed within six months of the effective date of the decision, to determine the cost plus 10%

markup for each referral made to GTEL and to bill GTEL for such referrals.

19. For the test year 1988 a corporate oversight allocation adjustment of $2,271,000 for services performed for GTEL is reasonable.

20. It is reasonable to require General to conduct a market-based pricing study to determine market rates for services it provides to GTEL.

21. A compounded labor escalation factor of 1.118% is reasonable for test year 1988.

22. A compounded nonlabor escalation factor of 1.09003 is reasonable for test year 1988.

23. An adjustment for 1988 test year compensation levels in addition to various ratemaking disallowances is inapppropriate.

24. A 5% productivity factor for attrition year labor adjustment is reasonable. Savings from productivity gains in excess of 5% should be divided equally between ratepayers and General.

25. D.88-06-024 directed General to make a 1989 operational attrition filing by October 1, 1988. It also directed General to file an application, testimonies and exhibits for capital structure and cost of capital review for 1989 on or before July 15, 1988.

26. The actual productivity factor will not be known until after the end of the attrition year. Therefore, it is appropriate to implement the sharing of the productivity savings on or before January 31 of the year following the attrition year.

27. It is reasonable for General to retire $3.8 million Olympics plant below the line for ratemaking and accounting purposes.

28. It is reasonable to disallow for ratemaking purposes a labor overrun of $7.9 million for cost overruns of switching equipment.

29. It is reasonable to amortize the costs of improvements in property prior to occupancy over a three-year period.

30. Interest during construction should not be allowed on land.

31. General has failed to justify $2.362 million toxics cleanup request but the record indicates some future costs will be incurred, and as a matter of judgment we adopt $353,000 as reasonable for test year 1988.

32. General should file a report with CACD describing its current and anticipated hazardous waste cleanup activities for 1988-1989.

33. It is reasonable to disallow $0.6 million employee store losses together with inventory reduction of $253,000 for 1985 and $449,000 for 1986 for ratemaking purposes.

34. Ratemaking adjustments for institutional advertising items of National Prorates, "Image," "Public Information," "NFL Sports," and "Indy 500" totalling $10.3 million for the year 1986 are not necessarily appropriate for adjustments for test year 1988.

35. It is reasonable to disallow $5.7 million commercial and marketing expense and $0.3 million operating rent expense for test year 1988 for one-time programs.

36. It is reasonable to adjust General Office and Other Operating expenses by $1.893 million for 1985 and $2.644 million for 1986.

37. General's decision to invest in a new administration building in Thousand Oaks is not imprudent.

38. It is reasonable to include $4,485,000 a year as miscellaneous revenue representing the difference between the gain from the sale of property and the cost of relocation amortized over a three-year period; the relocation cost offset is appropriate in

this specific instance, since this was not a stand-alone sale of property, but a unified transaction.

39. The California Corporation Franchise Tax and Federal Income Tax amounts reflected in Appendix C are reasonable.

40. The adopted estimates, previously discussed, of revenues, operating expenses and rate base for test year 1988 as summarized on the tabulation in Section V.N of this decision reasonably indicate General's operations in the future.

41. The separated results of operations reflected in Appendix D is reasonable.

42. It is reasonable to require General to prepare a cost/benefit analyses of advertising campaign to justify advertising expenses for ratemaking purposes.

43. DRA's total factor productivity study raises concerns which need to be resolved before the study can be used for establishing productivity levels.

44. Labor costs computed on the number of employees is not variable within a monthly period, and consequently the entire cost function model is misspecified.

45. DRA's failure to adequately measure the capital quality would not in itself cause us to fault the results of the study.

46. The productivity gains indicated by DRA's total factor productivity study are excessively high.

47. D.85-06-113 dated June 12, 1985 directs AT&T-C to flow through any reduction in its access expense stemming from reductions in local exchange utilities' access charges to its customers.

48. It is reasonable to move the rate center, coordinate for General's Etiwanda exchange so that the route between the Ontario exchange and the Etiwanda exchange becomes a local route; establish a route between the Etiwanda exchange and the Rialto exchange with Pacific which become a nine-mile route with the movement of the rate center of the Etiwanda exchange as a ZUM 2 route; and revise

General's billing system to reflect the necessary route revisions provided we impose a 90-day implementation period and require Pacific and General to provide written notice to those customers who will be impacted by the changes within 30 days prior to the implementation of such changes.

Conclusions of Law

1. The Commission concludes that an incremental revenue reduction of $218.304 million in addition to the $112.190 million reduction ordered by D.87-12-070 for a total of $330.494 million is appropriate.

2. The revenue reductions authorized in Appendix A are just and reasonable.

2a. General should be required to conduct a competitive analysis by March 31, 1989 of its directory service contract.

3. A competitive analysis to ascertain whether GTEDS is the appropriate party to perform General's data processing and information services should be performed by General prior to its next rate case filing and the results of the analysis and supporting work papers should be included in the filing.

4. General should be required to establish referral guidelines to track successful and unsuccessful referrals to GTEL and perform a study to be completed within six months of the effective date of the decision, to determine the cost plus 10% markup for each referral made to GTEL.

5. General should be required to conduct a market-based pricing study to determine market rates for services it provides to GTEL.

6. Savings in excess of a 5% attrition year labor factor adjustment should be shared equally by ratepayers and General.

7. Since the actual productivity factor will not be known until after the end of the attrition year, General should be required to implement the productivity savings on or before January 31 of the year following the attrition year.

8. In future rate cases General should present cost/benefit analyses to justify advertising campaign expenses for ratemaking purposes.

9. DRA's total factor productivity study cannot be used for any interpretative purposes including the measurement of technical change.

10. General should make an advice letter filing on or before October 1, 1988, setting forth an appropriate operational attrition allowance for the year 1989, and has filed an application for 1989 financial attrition on July 15, 1988, in accordance with D.88-06-024.

11. General is now well into the 1988 test year and since the rate reductions are substantial, this order should be effective today.

12. The rate center coordinates for General's Etiwanda exchange should be moved so that the route between the Ontario exchange and the Etiwanda exchange becomes a local route.

13. General should establish a route between the Etiwanda exchange and the Rialto exchange with Pacific which will become a ZUM Zone 2 route.

14. General should revise its billing system to reflect the route revisions set forth in Conclusions of Law 12 and 13 and provide written notice to those customers who will be impacted by the changes within 30 days prior to the implementation of such changes.

SECOND INTERIM ORDER

IT IS ORDERED that:

1. Seven days after the effective date of this order, GTE California (General) shall file revised Schedule Cal. P.U.C. No. A-38 to reflect the revisions shown in Appendix A of this decision. Such filing shall comply with the General Order 96 series. The

effective date of the revised schedules shall be September 6, 1988. Revised schedules shall apply only to service rendered on or after the effective date.

2. In accordance with D.88-06-024, on or before October 1, 1988, General shall make an advice letter filing setting forth an appropriate operational attrition allowance for the year 1989. In accordance with that same decision General has filed its application for 1989 financial attrition on July 15, 1988. General's operational attrition advice letter filing shall provide for savings resulting from productivity in excess of 5% to be shared equally between ratepayers and stockholders. Both filings shall be served on all parties to this proceeding.

2a. Consistent with the above discussion, findings, and conclusions, General shall conduct a competitive analysis of its directory service contract and serve it on the parties to this proceeding on or before March 31, 1989.

3. General shall conduct a competitive analysis prior to its next rate filing and include the work papers with the filing to support continued affiliated transactions relating to data processing and informational service between it and GTEDS.

4. Within 60 days of the effective date of this order, General shall establish referral guidelines to track successful and unsuccessful referrals to GTEL.

5. Within 6 months of the effective date of this order, General shall submit a study of the cost plus 10% markup for each referral made to GTEL and thereafter bill GTEL the cost plus 10% markup for all referrals near the market value of successful referrals.

6. Within 6 months of the effective date of this order, General shall submit a market-based pricing study determining the market rates for service it provides to GTEL. Until further CPUC action on the matter, General shall bill GTEL at its fully

allocated cost including return on investment, plus a 10% investment.

7. In future rate proceedings, if General wants to recover advertising expense in connection with campaigns to promote usage or new services, it shall present in its direct showing a cost/benefit analysis of such campaigns over the latest available 12-month recorded period as well as its pro proma analysis of proposed future campaigns. Likewise, if General seeks to recover marketing expense (Account 643), it shall present the same types of analysis as required above for advertising expenditures.

8. Within five days from the effective date of this decision, General shall establish a balancing account into which it shall book the difference between currently authorized rates and rates it would be collecting if it revised its accounting for refinancings to follow the net of tax method. The balancing account amounts shall be subject to refund, in whole or in part, following hearings to determine (1) whether General ought to be ordered permanently to revise its accounting of bond refinancing premiums, and unamortized discounts and expenses, and (2) what method General may use to do so. A Prehearing Conference will be held to set hearing dates and dates for submission of testimony in connection with this issue.

9. Consistent with the preceeding discussion, within 90 days of the effective date of this decision General shall file with CACD a report describing its current and anticipated hazardous waste cleanup activities for 1988-1989.

10. Within 10 days after General makes its advice letter filing to reduce access charges in accordance with this decision, AT&T-C shall file an advice letter with this Commission under the terms of GO 96-A, which proposes a method for flowing through to its ratepayers the access charge reductions resulting from this decision. AT&T-C's advice letter filing shall contain a proposed effective date of no later than five working days following its

submission to the Commission or September 19, 1988, whichever is earlier. For the several rates within each class of switched service, AT&T-C shall implement a uniform percentage reduction.

11. To be effective not less than 90 days after the effective date of this order, General and Pacific are authorized to:

a. Move the rate center coordinates for the Etiwanda exchange in order that the route between the Ontario exchange and the Etiwanda exchange becomes a local route.

b. Establish the route between the Etiwanda exchange and the Rialto exchange with Pacific as a ZUM Zone 2 route.

c. Revise the billing system to reflect the tariff revisions set forth in Appendix 1-F of Exhibit 230. Both General and Pacific shall provide written notice to their customers who will be impacted by the change within 30 days prior to the implementation of the change.

12. Within 20 days of the effective date of this decision, General shall file an advice letter in conformance with GO 96-A reflecting a reduction to its revenue requirement to account for the effects of interest synchronization for 1987. This advice letter shall also reflect interest at the three-month commercial paper rate for 1987, beginning January 1, 1987 to the effective date of the tariff revision hereafter discussed. The filing shall be based on 1986 adopted attrition results of operations and the 1987 adopted financial attrition. Consistent with D.87-12-067, General shall not adjust unamortized ITC to reflect the impacts of remand. The interest synchronization effect for 1987 shall be reflected as a bill and keep surcredit based on 1987 adopted billing base, the amount to be amortized through December 31, 1988. The bill and keep surcredit shall be effective October 1, 1988, and shall apply to services rendered on and after the effective date of the tariff.

13. Within 60 days of the effective date of this decision, CACD shall confer with DRA and General to identify for tracking purposes the amounts included in this decision for detariffed inside wire maintenance as is now under consideration in OII 84. Any other party to this proceeding may participate in performing this calculation upon notice of its desire to do so to CACD. General shall continue to track actual revenues and expenses for detariffed inside wire maintenance consistent with our previous decisions in OII 84 and shall also track the adopted amounts authorized in this decision.

This order is effective today.

Dated August 24, 1988, at San Francisco, California.

STANLEY W. HULETT
President
DONALD VIAL
FREDERICK R. DUDA
G. MITCHELL WILK
JOHN B. OHANIAN
Commissioners

I CERTIFY THAT THIS DECISION WAS APPROVED BY THE ABOVE COMMISSIONERS TODAY.

Victor Weisser

Victor Weisser, Executive Director

APPENDIX A

SCHEDULE CAL. P.U.C. NO. A-38
BILLING ADJUSTMENT

The following revisions are ordered:

Rates	Monthly Percentage Increment
Adjustment Factor	(13.45%) *
Adjustment Factor	(13.45%) **
Adjustment Factor	(13.45%) ***

* The monthly percentage factor applies to all services provided under Tariff Schedule C-1, Facilities for Intrastate Access.

** The monthly percentage factor applies to all recurring and nonrecurring rates and charges for service or equipment provided under all of the Utility's Tariff Schedules except the following:

The present list of excepted services shall remain unchanged.

*** The monthly percentage factor applies to all intraLATA toll and toll private line services.

APPENDIX B
Page 1

TRANSCRIPT CORRECTION
REQUESTS DENIED

Transit Request Date	Page	Line	Change/Correction
Transcript Volume 5			
5-27-87	495	16	Change "No, they do not." to "Yes".
5-27-87	495	20	Insert "not" after "would" and change "?" to "." after "correct".
5-27-87	508	20	Insert the following sentence at the beginning of the answer: "No. The intercept operator handles a different type of call."
5-27-87	508	21	Insert "TSPS" prior to "operator".
5-7-87	569	28	Delete "the correction for".
5-7-87	570	1	Delete the line.
Transcript Volume 6			
5-7-87	585	17	Change "3" to "13".
5-7-87	585	19	Change "$957,000" to $$3.086 million".
5-7-87	586	22	Delete "estimates, our forecast" and "to".
5-7-87	586	23	Delete "estimate yields the".
5-7-87	586	27	Change "3" to "13".

APPENDIX B
Page 2

TRANSCRIPT CORRECTION
REQUESTS DENIED

Transit Request Date	Page	Line	Change/Correction
Transcript Volume 7			
5-18-87	700	1-2	Delete answer and replace with: "That would not correspond to the same definition because the 1982 volumes reflect total WATS minutes and the 1981 volumes reflect only closed-end WATS minutes."
5-18-87	701	6	Delete answer and replace with: "No. The 149 million on page 13-3.1 represents total WATS minutes and the 7 million on page 13-3.2 line 7 column B represents only closed-end WATS minutes."
5-18-87	704	14	Change "continuous " to "discontinuous".
Transcript Volume 16			
6-19-87	1949	6	Change "creates" to "relates to".
6-19-87	1958	16	Insert "at" before "whatever" and "dollar" before "figure".
Transcript Volume 48			
8-11-87	5129	6	Insert "and terminals" before "and".
Transcript Volume 50			
8-11-87	5397	1	Change "25th" to "20, 1985".

(END OF APPENDIX B)

APPENDIX C

GTC CALIFORNIA
California Corporation Franchise Tax
Test Year 1988
($000)

Operating Revenues	$2,630,059
Operating Expenses	1,135,336
Taxes On Other Than Income	106,135
Subtotal	1,241,471
Net Before Adds & Deducts	1,388,588
Net Deductions from Taxable Income	
State Tax Depreciation	425,372
Fixed Charges	140,198
Pensions & Benefit Capitalized	44,146
Use Tax Capitalized	6,929
Payroll Taxes Capitalized	14,626
Cost of Removal	22,835
Subtotal of Deductions	654,106
Net State Taxable Income	734,482
CCFT @ 9.3%	$68,307

APPENDIX C

GTC CALIFORNIA
Federal Income Tax
Test Year 1988
($000)

Operating Revenues	$2,630,059
Operating Expenses	1,135,336
Taxes On Other Than Income	106,135
State Income Tax	68,307
Subtotal	1,309,778
Net Before Adds & Deducts	1,320,281
Net Deductions from Taxable Income	
Federal Tax Depreciation	471,218
Deferred Tax Reversal	73,538
Fixed Charges	150,013
Construction Period Taxes	(3,633)
Reserve for Uncollectibles	(1,850)
Dividend Paid Credit	77
Subtotal of Deductions	689,363
Net Federal Taxable Income	630,918
FIT @ 34%	214,512
Adjustment:	
ITC Amortization	(32,952)
Net FIT	$181,560

APPENDIX D
Page 1 of 1

GTC CALIFORNIA
Adopted Separated Summary of Earnings
Test Year 1988
($000)

	Total Company	Inter-State	------ IntraState ------		------ IntraLATA ------			Exchange
			Total	Access	Total	MTT	PL	
	(a)	(b)	(c)=(a-b)	(d)	(e)=(f+g)	(f)	(g)	(h)=(c-d-e)
OPERATING REVENUES								
1 Local Revenues	781,157	0	781,157	0	0	0	0	781,157
Intrastate								
2 Access Revenues	206,526	0	206,526	206,526	0	0	0	0
3 Toll Revenues	822,393	0	822,393	0	822,393	787,312	35,081	0
4 Interstate Access Revenues	480,425	480,425	0	0	0	0	0	0
5 Miscellaneous Revenues	281,981	23,819	258,162	26,675	0	0	0	231,487
6 Surcharge Revenues	74,730	0	74,730	(6,903)	29,388	28,719	669	52,245
Gain on Sale of Properties	4,485	846	3,639	425	1,317	1,183	134	1,897
7 Other Miscellaneous	0	0	0	0	0	0	0	0
8 LESS: Uncollectibles	21,638	1,200	20,438	0	7,960	7,779	181	12,478
9 Total	2,630,059	503,890	2,126,169	226,723	845,138	809,435	35,703	1,054,308
OPERATING EXPENSES								
10 Maintenance	432,977	94,917	338,060	44,142	118,675	103,772	14,903	175,243
11 Traffic	63,624	6,836	56,788	1,952	27,141	26,979	162	27,695
12 Commercial	257,207	44,382	212,825	13,365	28,231	27,190	1,041	171,229
13 General Office Sal. & Exp.	190,072	29,590	160,482	20,732	57,884	54,564	3,320	81,866
14 Other Operating Expenses	191,456	34,936	156,520	16,830	49,566	45,463	4,103	90,124
15 Subtotal	1,135,336	210,661	924,675	97,021	281,497	257,968	23,529	546,157
16 Depreciation	524,494	96,494	428,000	56,468	147,259	129,442	17,817	224,273
17 Taxes Other than on Income	106,135	22,000	84,135	10,171	28,450	25,186	3,264	45,514
18 State Income Tax	68,307	11,012	57,295	3,900	27,024	28,070	(1,046)	26,371
19 Federal Income Tax	181,560	34,418	147,142	10,971	95,606	101,537	(5,931)	40,565
20 Total	2,015,832	374,585	1,641,247	178,531	579,836	542,203	37,633	882,880
21 Net Revenues	614,227	129,305	484,922	48,192	265,302	267,232	(1,930)	171,428
RATE BASE								
22 100.1 - Tel Plt in Serv	6,652,276	1,385,519	5,266,757	684,170	1,842,591	1,600,648	241,943	2,739,996
23 100.2 - Tel Plt under Const.	0	0	0	0	0	0	0	0
24 100.3 - Prop Held for Future Use	79	17	62	8	22	19	3	32
25 Materials & Supplies 122	23,258	5,701	17,557	2,296	6,173	5,389	784	9,088
26 Working Cash	18,759	3,481	15,278	1,603	4,651	4,262	389	9,024
27 LESS: Depreciation Reserve	2,003,920	413,181	1,590,739	208,692	545,010	466,012	78,998	837,037
28 LESS: Deferred Tax	679,418	142,291	537,127	69,586	186,677	162,530	24,147	280,864
29 Total	4,011,034	839,246	3,171,788	409,799	1,121,750	981,776	139,974	1,640,239
30 RATE OF RETURN	15.31%	15.41%	15.29%	11.76%	23.65%	27.22%	-1.38%	10.45%

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INDEX

SECOND INTERIM OPINION

I. Synopsis of Decision

This second interim decision provides for a revenue reduction for GTE California (General), formerly General Telephone Company of California, of $216.481 million in addition to the decrease in customer billings of $112.190 million on an annual basis ordered by Interim Decision (D.) 87-12-070 dated December 22, 1987, as revised by Advice Letter No. 5125 filed February 29, 1988, a total reduction of $328.671 million. The bases for our adopted summary of earnings leading to the $328.671 million revenue reduction are detailed in this decision.

This decision does not modify the return on equity of 12.75% which will provide a rate of return of 10.90% found reasonable in Interim D.87-12-070.

As set forth in the section on rate design, the $216.481 million incremental reduction results from a reduction of 13.34% to the present billing surcharges set forth in General's Schedule Cal. P.U.C. No. A-38 which are collected on a "bill and keep" basis not subject to intercompany settlement. The final apportionment of the rate reduction to the various customer groups and the final tariff schedules based on this record will be addressed in our next decision on this matter, together with such issues as whether General should be ordered to adjust its rates for the 1988 test year to flow through to the ratepayers approximately $27,582,755 tax savings realized on retired bonds; the present policies of General in the area of customer service, billing, and testing; GTE California's practices and policies regarding women/minority business enterprises; and the various issues raised at the public participation hearings in these proceedings.

SECOND INTERIM OPINION

I. Synopsis of Decision

This second interim decision provides for a revenue reduction for GTE California (General), formerly General Telephone Company of California, of $223.116 million in addition to the decrease in customer billings of $112.190 million on an annual basis ordered by Interim Decision (D.) 87-12-070 dated December 22, 1987, as revised by Advice Letter No. 5125 filed February 29, 1988, a total reduction of $335.306 million. The bases for our adopted summary of earnings leading to the $335.306 million revenue reduction are detailed in this decision.

This decision does not modify the return on equity of 12.75% which will provide a rate of return of 10.90% found reasonable in Interim D.87-12-070.

As set forth in the section on rate design, the $223.116 million incremental reduction results from a reduction of 13.75% to the present billing surcharges set forth in General's Schedule Cal. P.U.C. No. A-38 which are collected on a "bill and keep" basis not subject to intercompany settlement. The final apportionment of the rate reduction to the various customer groups and the final tariff schedules based on this record will be addressed in our next decision on this matter, together with such issues as whether General should be ordered to adjust its rates for the 1988 test year to flow through to the ratepayers approximately $27,582,755 tax savings realized on retired bonds; the present policies of General in the area of customer service, billing, and testing; GTE California's practices and policies regarding women/minority business enterprises; and the various issues raised at the public participation hearings in these proceedings.

SECOND INTERIM OPINION

I. Synopsis of Decision

This second interim decision provides for a revenue reduction for GTE California (General), formerly General Telephone Company of California, of $219.506 million in addition to the decrease in customer billings of $112.190 million on an annual basis ordered by Interim Decision (D.) 87-12-070 dated December 22, 1987, as revised by Advice Letter No. 5125 filed February 29, 1988, a total reduction of $331.696 million. The bases for our adopted summary of earnings leading to the $331.696 million revenue reduction are detailed in this decision.

This decision does not modify the return on equity of 12.75% which will provide a rate of return of 10.90% found reasonable in Interim D.87-12-070.

As set forth in the section on rate design, the $219.506 million incremental reduction results from a reduction of 13.52% to the present billing surcharges set forth in General's Schedule Cal. P.U.C. No. A-38 which are collected on a "bill and keep" basis not subject to intercompany settlement. The final apportionment of the rate reduction to the various customer groups and the final tariff schedules based on this record will be addressed in our next decision on this matter, together with such issues as whether General should be ordered to adjust its rates for the 1988 test year to flow through to the ratepayers approximately $27,582,755 tax savings realized on retired bonds; the present policies of General in the area of customer service, billing, and testing; GTE California's practices and policies regarding women/minority business enterprises; and the various issues raised at the public participation hearings in these proceedings.

motion inaccurately portrays the facts. General believes that it is ratably flowing through to its ratepayers the tax benefits in issue, albeit using a method which may differ somewhat from procedures followed by some other utilities.

On June 13, 1988, DRA filed a formal supplement to its motion recommending that General be ordered to use the "net of tax" method in connection with setting up a balancing account to capture the remaining tax benefits during the pendency of this controversy. On June 21, 1988, General filed its formal opposition to the DRA supplement, asserting that balancing account treatment is unprecedented, unfair (since General believes it is currently flowing through these tax benefits), and violative of the retroactive ratemaking ban.

Although this issue could not be accommodated previously due to the demands of the hearing schedule, we will leave this proceeding open to consider it at this point. Thus, General and DRA will have a full opportunity to litigate the issue. However, in order to protect the ratepayer interest in the interim, we will adopt DRA's suggestion and require General to establish a balancing account into which it will book the difference between currently authorized rates and rates it would be collecting if it revised its accounting for refinancings to follow the net of tax method. The balancing account amounts will be subject to refund, in whole or in part, following hearings to determine 1) whether General ought to be ordered permanently to revise its accounting of bond refinancing premiums, and unamortized discounts and expenses and 2) what method General may use to do so. A prehearing conference will be held to set hearing dates and dates for submission of testimony in connection with this issue.

III. Rate of Return

D.87-12-070 authorized a rate of return for General of 10.90% for the test year 1988. The capital structure and cost factors comprising this rate of return are as follows:

million or $1.854 million greater than set forth in the decision. General's computations are based on the faulty premise that General's and DRA's estimates were averaged on a total estimate basis reflecting 1988 figures. Actually the only averaging was the growth figures before application of the TPI. The calculations as described on pages 151-153 are correct.

General alleges that the Account C-209 Digital COSE 100.1 gross additions adopted in the proposed decision are $26.754 million understated because they are based on initial NTEP cost data and do not include all of the costs that General will reasonably incur in connection with digital COSE. A review of the record lends support to General's position. However, General developed factor of actual to planning/NTEP of 1.32 which appears to be excessive. DRA witness McCarthy recommended an adjustment because of an experienced 1.17 factor. Even this would appear high as it reflects initial bidding rounds. Experience gained from the bid process should decrease this ratio. Consequently, for purposes of this decision we will adopt a factor of 1.10% which will increase the C-209 Account 100.1 balance of $8.348 million with an accompanying revenue requirement increase of $640,000.

General questions the "Modifications Line and Trunk Testing" set forth on page 153 of the decision. Actually the decision should read Modifications of $1.888 million by General and Line and Trunk Testing of $1.833 million by DRA. General is merely rearguing its position taken in the briefs; consequently, we will give no weight to the arguments. The same holds true for the $20 million capital planning adjustment set forth in the comments.

General alleges that the computations included in the decision for maintenance, commercial, and traffic accounts are understated by $8.987 million because labor escalation factors different than the adopted factor of 1.118 were used and improper allowance was made for the adopted operator level as compared to the operator level used by DRA. After review, we believe the

DRA has suggested miscellaneous grammatical corrections and a corrected estimate of weighted average plant in service; these corrections are appropriate and will be adopted.

III. Rate of Return

D.87-12-070 authorized a rate of return for General of 10.90% for the test year 1988. The capital structure and cost factors comprising this rate of return are as follows:

	General	DRA	Difference Amount	Difference Percent	Adopted
			($ in Millions)		
Telors Hdqtrs.	$105.4	$103.2	$ 2.2	2.1%	$103.2
GTE Labs (Chap.3)	53.2	27.5	25.7	93.5	27.6
Corporate	62.3	54.4	7.9	14.5	54.4
Service Fee Credit	(27.4)	(23.3)	(4.1)	(17.6)	(23.3)
GTOC-Prorated Service Corp.	193.5	161.8	31.7	19.6	161.9
Prorate % to General	29.6%	23.0%	6.6	28.7	29.6%
Prorate to General	$ 57.3	$ 37.2	$ 20.1	54.0	$ 47.9
Adjustments:					
Unreg. Activ.	(1.5)	(3.0)	(1.5)	(50.0)	(2.3)
International/ Corp. Comm.		(0.8)	(0.8)	(100.0)	(0.6)
Corp. Aircraft		(0.4)	(0.4)	(100.0)	(0.3)
Total Adjustments	(1.5)	(4.2)	(2.7)	(64.3)	(3.2)
Test Year GS&L Est.	$ 55.8	$ 33.0	$ 22.8	69.1%	$ 44.7

(Red Figure)

Essentially, the estimates differ because the Team considered more current information; used beneficiary analysis criteria in determining GTE Labs' expense; used a lower two-factor prorate to allocate GTESC's expenses to General; excluded a greater level of unregulated activity expenses; and disallowed certain GTESC expenses. Under a contract signed by the chairman of the board of GTESC and the president of General, GTESC agreed to provide a central organization which can render certain services to General that include:

- Advice and counsel on management and operational matters.

- The coordination of standards on equipment, materials, and supplies.

same bill, General's prorated share of GTE Labs' expense. For the period 1977 through 1986, the GS&L expenses billed General have increased from $6.9 million to $49.3 million.

As set forth in the previous tabulation, Team has determined that $161.8 million will be the test year level of GTESC expenses for proration to General and the other GTOCs. As indicated in the tabulation, this compares to $193.5 million estimated by General. $25.7 million of the $31.7 million difference relates to the GTE Labs' estimate; the remaining $6.0 million of the difference generally reflects Team's use of the 1987 GTESC budget as contrasted to General's use of the 1986 GTESC budget. Based on the later data set forth in the 1987 GTESC budget, which is more likely to portray actual test year conditions, we will adopt DRA's estimate of $103.2 million for Telop's headquarters, $54.4 million for corporate, and a $23.3 million service fee credit.

2. GTE Labs' Expenses

GTE Labs' expenses are allocated to the Telephone Operating Group, the Diversified Product Group, and the GTE Communication Services Group on the basis of revenues and sales of each company to the total revenues and sales of all GTE companies. General's $53.2 million estimate depends on an allocation of GTE Labs' expense based solely on the relative revenues and sales of each client whereas Team's $27.5 million estimate allegedly considers beneficiary analysis criteria consistent with prior Commission decisions. The GTE Labs is currently conducting research in 14 strategic technical areas (STAs) encompassing telecommunications systems, electronics and photonics, computer and intelligent systems, and materials science. Team's $27.5 million estimate is essentially the summation of each STA's allowable allocated expense determined by multiplying each 1987 budgeted expense by its corresponding Telops beneficiary percentage. The Telops beneficiary percentages were essentially based on a study by

Team's investigation disclosed that some of the effort in these projects involved fiber-optic devices and components which Team believes to be of benefit to equipment manufacturers. We agree and will adopt the staff figures.

In accordance with the above discussion, we will adopt as reasonable a GTE Labs' expense of $27.6 million, making a total to be allocated among the Telops of $161.9 million.

3. <u>Prorate Factor</u>

General used a 29.6% prorate factor to allocate costs to General as compared to Team's prorate factor of 23.0%. General's 29.6% prorate factor was based on the relative size criteria used by GTESC to allocate expenses among the domestic GTOCs whereas Team used a composite factor consisting of 50% relative size and 50% equal division between the seven regional clients served by GTESC consisting of California, Florida, Hawaii, the Midwest, the Southwest, and the Northwest. Team's investigation indicated that each of these regional clients has a voice on GTESC's planned work programs; that GTESC's departmental work efforts were common to all GTOCs and provided equal benefits to the GTOCs; and that certain work activities actually provided greater benefits to smaller GTOCs than large GTOCs because they would realize the greatest leverage gains in dealing with manufacturers. It, therefore, appeared to Team that there was no significant correlation between the relative size allocation method and GTESC-provided services to base the allocation only on relative size criteria. Therefore, Team is recommending that 50% of the costs be allocated on relative size and 50% on the number of subsidiaries receiving services, which results in a composite prorate factor of 23.0%.

According to the rebuttal testimony of Dr. A. N. Mosich, the costs of GTESC are allocated to service recipients on the basis of generally accepted accounting principles which provide that indirect costs shall be allocated on a reasonable basis among operating units for whose benefits the costs are incurred. This witness further testified that implementation of such a reasonable-basis principle generally results in the use of some measure of activity or size as a basis for the allocation of costs. According to the testimony, GTESC follows this principle by allocating regionally in accordance with each GTOC's operating expenses and taxes (exclusive of investment tax credit) to the total operating expenses and taxes (exclusive of investment tax credit) of all domestic telephone companies. Such a procedure, according to the record, allocates costs among the seven entities in such a way to ensure that every customer of the seven companies contributes proportionately to the recovery of the total cost of providing the service. General's rebuttal testimony appears reasonable and will be adopted resulting in a proration factor of 29.6% and an allocation to General of $47.9 million as set forth in the previous tabulation.

Team further recommends that General be directed to formally request from GTESC a cost allocation report which would determine the most appropriate beneficial or causal factors needed to fairly prorate the expenses of each GTESC's billing department. We are not persuaded that such a study is needed nor that it would be beneficial and will, therefore, not require its production.

4. <u>Ratemaking Adjustments</u>

Team recommends certain ratemaking adjustments it believes are consistent with Commission policy and decisions as follows:

1. A disallowance of $1.1 million from GTESC's Marketing and Business Planning (M&BP) Department to reflect an estimated 20% of the department's activities devoted to its unregulated customer-provided equipment (CPE) business. (Exh. 89, pp. 2-16 to 2-17.)

2. A disallowance of $1.6 million from the Business Services Department expenses of $2.0 million to reflect work activities

that are nonbeneficial to regulated telephone operations. (Exh. 89, p. 2-17.)

3. A disallowance of $0.3 million to corporate oversight activities that benefit GTEL. (Exh. 89, p. 2-18.)

4. A disallowance of $0.8 million to reflect 50% of cost of the Corporate Communications and Washington offices and the international expenses allocated to General in keeping with our past decisions providing such a disallowance because the office work provides an intermixing of benefits to shareholders and ratepayers and the international expenses provide no benefit to General's ratepayers. (D.82-04-028 and D.84-07-108.)

5. A disallowance of $0.4 million to reflect GTE-owned aircraft expenses in excess of a reasonable air travel expense allowance based on commercial air rates to allow GTE executives to conduct GTOC business. (D.91869.)

The above-listed disallowances and/or adjustments are consistent with our past decisions and stated policies and will be adopted after modification to reflect our adopted 29.6% proration factor. The total adopted test year GS&L expenses (Account 674) are $44.7 million as summarized in the previous tabulation.

C. GTE Communications System Corporation

GTE Communications Systems Corporation (CSC), formerly GTE Automatic Electric (AE), is comprised of the former GTE Network Systems, GTE Business Communication Systems, GTE Microcircuits, and certain operations of GTE Communication Products Corp. Wholly owned by GTE, CSC develops, manufactures, and markets a wide range of communications systems equipment and devices for the telecommunications market. Manufactured products include digital central office switching equipment and the GTE family of Private Automatic Branch Exchange (PABX) systems.

9. Competitive bidding is not a common practice in the directory publication market.

10. Should Dir Corp not be able to retain General's directory publishing business as a result of a competitive bidding program, it would continue in the market and continue to use the GTE logo and "Walking Fingers" symbol.

11. There is already confusion in the marketplace regarding the identity of yellow pages publications.

12. It is quite possible that General will lose substantial revenue if a competitive bid approach to directories publishing is mandated.

It is obvious from the record that the directory publishing business in California is both lucrative and highly competitive. It appears possible, even probable, that adopting Team's recommendation with respect to mandating an annual competitive analysis of its directory services contract, including the soliciting of bids from other directory publishers, could have an adverse impact on both General's ratepayers and those that presently advertise in Dir Corp's directories. Furthermore, we are satisfied that the adjustments to General's expenses to reflect our policies regarding subsidiary and/or affiliate earnings as above-described adequately protect the ratepayers. Consequently we will not adopt Team's recommendations in this respect.

E. GTE Telecom Marketing Corporation

GTE Telecom Marketing Corporation (TMC) executed a marketing agreement with AT&T Communications (AT&T) covering the period from May through December 1985. According to the record, under this agreement, TMC provided marketing service to help AT&T maintain its market share after divestiture. The marketing service was to distribute AT&T's measured toll, WATS (wide area telephone service), 800 service, private line, and foreign exchange services calculated from six of GTEDS data processing centers. Under these circumstances, Team recommends that General should conduct a competitive analysis prior to its next rate case filing and include the study in its work papers to support continued affiliate transactions between General and GTEDS. We believe Team's recommendation has merit and the order that follows will provide for its implementation.

As part of its investigation, Team analyzed the reported return on investment (ROI) earned by GTEDS from General to determine the reliability of the data used in the calculation of the traditional Commission adjustment limiting GTEDS' earnings to a level not in excess of General's authorized return.

Team recommended no adjustment to GTEDS' ROI because the figure provided by GTEDS of 3.85% for test year 1988 is below Team's estimate of General's ROI. Team, however, questions the reliability of the data supplied because of GTEDS' 3.85% ROI for General as contrasted with 31.15% for General Telephone of Florida and 62.62% for General Telephone of the Southwest. Such discrepancies, according to Team, support the necessity of the previously discussed competitive analysis study to be ordered by this decision.

With respect to rents and contracts, General's 1988 test year estimates of the cost of the Customer Billing Information System (CBIS) of $2,675,800 and California Billing System (CBS) of $10,253,900 (Account 996-Computer Usage) total $12,929,700 or $4,566,000 more than Team's estimate of $8,363,700. The difference is due to the inclusion by General of implemental costs of the Customer Records and Billing System (CRB) and Facilities Management System (FMS) not included by Team. The record fully supports the desirability of installing both CRB and FMS. Under these circumstances, according to the record, Team agrees that some implemental costs should be included for the test year and recommends the expense be amortized over a three-year period by obviously valid. It is equally obvious that we have jurisdiction to investigate and consider directory advertising revenues and expenses for the purpose of implementing ratemaking adjustments during rate proceedings. Team's recommendation relating to the deletion of GTEL's Direct Marketing Center's 800 number and the change in Yellow Page fillers and full page CPE ads is rendered moot in view of General's expressed intention to effect such changes in all forthcoming directories. Because of subscriber confusion during the transition period from July 1, 1985 until CPE was deregulated at the end of 1987, we do not feel that it would be proper or reasonable to impute advertising revenues in the informational section of the white pages or on the back covers of the directories. However, the yellow-page sections of the telephone directories are a different matter. It is axiomatic that the yellow pages are a form of advertising which should be paid for by the beneficiary of such advertisements. Consequently, it is only reasonable that GTEDs be assessed the costs of such advertisements. We will, therefore, adopt staff's recommendation that advertising revenues be imputed for the Yellow Page fillers and provide an annual adjustment plus interest factor of $687,000.

One GTE-sponsored sales program was the "Sell One More Program" that commenced on January 1, 1986 and ended in California on December 31, 1986. Team recommends that General's revenue requirement be reduced $317,000 or $129,000 a year for three years, for expected reimbursement for GTEL's share of the expenses derived from this referral program's generated revenues of $531,533 for GTEL. Because any reimbursement for GTEL's share of expenses is speculative rather than actual and because this particular sales program will not be continued into the test year we will not make the adjustment Team recommends.

2. Unbilled Referrals

In her direct testimony on unbilled referrals, Team witness Chia indicated that:

General on behalf of GTEL and to include the total cost of General's accounting department in the amount to be allocated would result in double billing through corporate oversight and on-demand services. The record is clear, however, that there are some accounting functions, such as budget consolidation, financial planning, internal audits, or accounting analyses that are performed by General on behalf of GTEL and are not included in bills for on-demand services. To reflect these costs, we will include 10% of the account total adopted for this account of $109,952,000 or $10,995,000 in the amount to be allocated.

We are persuaded that activities performed by General on behalf of GTEL which are recorded for in Account 663-Treasury and 664-Legal are generally included in billings for on-demand services and will not be included in the amount to be allocated.

Account 665-Other General Office Salaries and Expenses includes employees' salaries and expenses in human resources, public affairs, revenue requirements, miscellaneous engineering, and security of the company. DRA's position that this account amount, exclusive of miscellaneous engineering expenses, should be included in the amount to be allocated is well-taken and will be adopted. Equally acceptable to us is DRA's position that Account 643-General Marketing and Sales Administration expense is properly includable in the amount to be allocated. In accordance with the above discussion, the corporate oversight allocation adjustment, which we adopt as reasonable, is $1,694,000 computed using our adopted allocable General Office Salaries and Expenses and General Marketing and Sales Administration expenses as set forth below:

General Office Salaries and Expenses (GOSE):		
Executive	$	$ 1,277,000
Accounting		10,995,000
Other GOSE		68,941,000
Total		81,213,000
General Marketing and Sales Administration (GMSA)		11,631,000
Total GOSE and GMSA		92,844,000
Less: Portion of Acc. 665, Engineering Exp.		(36,681,000)
Total Allocable Expenses		56,163,000
Multiplied by 3-Factor Allocator	3.290%	
Total Allocated Corporate Oversight	1,847,762	
Less: Corporate Oversight Actually Billed (excluding GTESC) Estimate: Actual 1986 Billed Amount	$ 149,183	
Multiplied by 1987 Labor Inflation Factor - 1.15%	150,899	
Multiplied by 1988 Labor Inflation Factor - 2.01%		(153,932)
Corporate Oversight Allocation Adj.		1,693,800

(Red Figure)

4. Transfer Costing

Team noted that General currently provides the following services to GTEL on a demand basis: legal, accounting, graphics, customer representative, security, land and building engineer, and testing. During phase two of Pacific's A.85-01-034, DRA recommended that services from Pacific to its affiliates be priced at the higher of fully loaded cost plus 10% markup or market price. DRA further recommended that Pacific conduct a market pricing study to determine market rates for the services it provides to its affiliates. Pacific concurred and is currently conducting such a study. In this matter, DRA recommends that if General plans to and/or is allowed to provide "on demand" services to GTEL, it be ordered to conduct and submit within six months of the decision a market-based pricing study to determine market rates for services it provides to its affiliates. DRA further recommends that until the study is complete, services provided by General to GTEL be priced at fully loaded cost including return on investment and a 10% markup.

General's rebuttal witness Murphy testified that the transfer pricing methodology by which General bills GTEL is based on fully allocated cost plus a return on investment and a 10% markup is therefore not appropriate. He further testified that DRA's recommended study for market rates for services would be of little value because it would continually have to be updated to reflect market conditions resulting in increased costs to General, would be a source of constant dispute between General and DRA, and would be expensive to monitor. We agree with General that both a return on investment and the 10% markup would be inappropriate, but we note that we have adopted the 10% markup previously for Pacific in D.86-01-026 and we perceive no need to depart from this plan for General. We agree with and adopt as reasonable DRA's recommendation that General conduct a market-based pricing study to determine market rates for services it provides to GTEL. The order that follows will provide for such a study to be completed within six months from the effective date of the decision and that until such a study issues, General continue to bill GTEL at its fully allocated costs including return on investment.

5. <u>Affiliate Payment</u>

As was recommended by DRA in Phase 2 of the Pacific Bell rate case, Team is recommending that GTEL pay General 5% of its gross revenue to reimburse General for the value of intangible,

Item	DRA Recommended Adjustment	Adopted
Directory Advertising Adjustment[a/]	$ 1,507,000	$ 687,000
Sell One More Adjustment[a/]	129,000	0
1985 to 1987 Referral Adjustment[a/]	2,670,000	0
1988 Referral Adjustment	3,123,000	3,123,000
Corporate Oversight Adjustment	4,900,000	1,694,000
Affiliate Payment Adjustment	5,966,000	0
Total Reduction to 1988 Revenue Requirements	$18,295,000	$5,504,000

a/ Amounts equal one-year amortization plus an interest factor. Total adjustment amortized over a three-year period.

2. Imposition of an incentive program would represent an unprecedented intrusion of the Commission into bargaining matters.

3. The National Labor Relations Act was intended to govern the negotiating process by which wages are set for private union-represented employees and state regulation concerning conduct that the U.S. Congress intended to be unregulated is preempted by federal labor law.

4. With the modest wage increases seen in recent years, bonuses being given to select employees are inappropriate ways to reward work with compensation.

5. The incentive plan is unworkable because: (a) it inherently contradicts the thrust of McNamara's testimony that General employees are overpaid and (b) to single out access lines per employee as the productivity measure for awarding bonuses is arbitrary and unfair.

General's and CWA's position relative to the allocation of 25% of the efficiency savings to General's work force appears to be well taken. Furthermore, we can foresee great difficulty in equitably allocating such savings to employees in a fair, equitable, and unbiased manner. Consequently we will adopt General's and CWA's position and not allocate efficiency savings to General's work force. However, the record fully supports a 5% productivity factor based on the ranges included in the testimony (4% presented by CTEC to 16% by DRA), and the testimony of DRA's witness that a 5%-7% range is a realistic assessment of productivity gains to be expected in the future. Thus, we will adopt a 5% productivity factor for computation of the attrition year labor adjustments for 1988 and 1990. Savings resulting from efficiency in excess of the 5% productivity factor will be shared equally between the ratepayers and General. Since the actual productivity savings for the attrition year will not be known until

11. The costs of currently approved monitoring techniques are a normal cost of doing business. Underground tanks are necessary for the storing of fuels because they lessen the risk of explosion and the storage of fuels is required for General's business operations.

12. It is reasonable to believe General will experience additional leaks in the future and therefore the cleanup costs should be allowed as a normal cost of doing business.

It is obvious from the record that, in the past, General has not adequately maintained its underground storage tanks. However, as a result of the new legislation, substantial sums were recorded as expenses in the years 1985 and 1986 for cleanup and correctional measures. Nonetheless, to permit these two years' recorded expense to be used as a basis for trending future expenses would result in an abnormally high expense allowance for this item. To eliminate the amount completely would result in no allowance for future cleanup work. We are persuaded that future cleanup costs will be incurred and such costs are a normal part of doing business. Even DRA acknowledges in its Opening Brief (pp. 22-23) that there is a need for a future cleanup program and that General's expenditures for toxic cleanup should be evaluated on a case-by-case basis. Since the record supporting General's test year toxic cleanup request of $2.362 million (General's Opening Brief, p. 50) is sparse, we have no basis for finding any specific amount reasonable for the test year. General has not justified its $2.362 million request with reference to a specific cleanup program or budget. However, on a judgment basis, and as an interim step in recognition that future costs will be incurred, we will authorize $353,000 for test year 1988.

If General wishes additional rate recovery for toxic cleanup programs in the immediate future (i.e., 1989 and 1990), at levels greater than normally allowed via the application of the attrition formula, we will require that it file an application seeking such relief, including as part of its showing a plan for investigation and program development for the next five years, as well as a detailed budget and project description covering 1989 and 1990 requested expenses. If General opts to forego such immediate rate recovery, we will direct it to include in its next test year NOI, as an adjunct to its test year request for toxic cleanup expenses, a plan for investigation and program development for the test year and five years thereafter.

5. GTEL Accounts Receivable

Included in Account 118-Due from Customers and Agents are accounts receivable and uncollectibles due from GTEL customers totaling a net of $1,260,000 in 1985 and $9,480,000 in 1986. These receivables represent collections for deregulated equipment rentals. All revenues collected from these receivables have been properly booked BTL by General. In order to match the receivables with the revenues collected from them, DRA recommends that Account 118 be reduced by these amounts and the dollars be transferred BTL for ratemaking and accounting purposes. This recommendation appears reasonable and will be adopted.

6. Employee Store

DRA's Financial Examiner III Francis Fok recommends a ratemaking adjustment reducing General's 1988 operating expenses by $0.6 million equal to the estimated operating loss incurred to maintain General's employee store. According to this witness's testimony, inadequate accounting for the store operation, inadequate management, lack of supporting information, and cross-subsidization of General's unregulated affiliates form the basis for the recommended disallowance. General's employee store operation operates under the policies and guidelines established by to exclude the capitalized portions of these costs. To be consistent with D.84-07-108 and General's own action in A.83-07-002 in which both the expenses and the capitalized costs associated with the VISA program were excluded for ratemaking purposes and to eliminate any significant effect of unusual nonrecurring activities on a trended test year estimates, DRA recommends the disallowance of these expenses, plant, and depreciation reserve. DRA's position is well taken and will be adopted.

8. Protective Connecting Arrangements

In D.87620, dated July 19, 1977, this Commission ordered all telephone companies in California to discontinue and refund charges for protective connecting arrangements (PCA) used with customer-provided equipment (CPE) to eligible subscribers who were subject to charges dating to February 17, 1974. General set up an initial reserve of $4.54 million and paid refunds of $2.96 million from 1979 to 1986. The remaining balance of $1.58 million plus interest of $660,000 was credited to reserve account 174-Other Deferred Credits in April 1986. DRA witness Mar recommends that consistent with D.86-05-071 dated May 28, 1986, which states in part:

> "In terminating the program, we do not intend to provide Pacific's shareholders with a windfall from unrefunded PCA charges. Accordingly, we will require Pacific to report in its next general rate case filing the outstanding balance of PCA charges which will be credited to Pacific's ratepayers.",

unclaimed PCA refunds, including interest, be charged out of reserve account 174-Other Deferred Credits and refunded to ratepayers in one test year billing cycle by appropriate adjustment to the customer billing surcharge. This position is well taken and the recommendation will be adopted.

9. Commercial and Marketing Expenses

DRA's financial examiner III Francis Fok recommends that 1986 recorded commercial and marketing expense be reduced by $16 million and Account 671-Operating Rent be reduced by $0.3 million. The ratemaking adjustments to advertising expense relate to expenditures that were unusual or of a one-time nature and those that represented institutional advertising. One-time expenditures are those which are not of an ongoing nature and therefore should be excluded from any historical base utilized to project test year estimates. Also included in the recommended adjustments are expenses of operations that will be discontinued before the test year. The institutionalized items excluded consist of National Prorates ("gee...no, GTE") of $1.1 million, "Image" which is self-explanatory of $4.9 million, "Public Information" advertising for program consisting of such events as NFL sponsorships, sports sponsorships, culture sponsorships, and academic all-America campaigns, for a total of $1.6 million and other sponsorships including "NFL Sports" and "Indy 500" totaling $2.7 million, for a total institutional advertising disallowance recommended of $10.3 million. The one-time programs that were recommended for disallowance by this witness included CPE phaseout of $0.2 million, an inside wire deregulation maintenance program of $0.4 million, together with associated expenses of $0.9 million and an equal access information program of $1.7 million, for a total of $3.2 million. The balance of the recommended adjustments include one-time expenditures for phone mart operations, which will be discontinued by 1988, consisting of operating rent of $0.3 million and marketing and sales expense of $2.5 million.

According to witness Fok, institutional advertising is defined as advertising which promotes the corporate image. It has been consistently disallowed by this Commission for ratemaking purposes. All the above-itemized recommended advertising disallowances are in keeping with past Commission decisions and policies and would be appropriate for making adjustments were they to apply to the 1988 test year. However, the proposed disallowances are to be applied to recorded 1986 data presumably with the idea of using them as the basis for projecting 1988 test year estimates of expense. Such a procedure would be appropriate if it was clear that the 1988 advertising campaigns of General would parallel the 1986 campaign. However, there is nothing in the record supporting such a position. Under these circumstances, we will not adopt DRA's recommendation relative to the disallowances of the institutional advertising expenses totaling $10.3 million.

DRA's recommended disallowances of the one-time programs, detailed above, totaling $5.7 million commercial and marketing expense and $0.3 million operating rent have merit since General has not shown that they will recur during the test year. We will adopt DRA's recommended disallowance.

10. General Office and Other Operating Expenses

DRA financial examiner III J. J. Simmons presented testimony recommending adjustments to the general office salaries and expense and other operating expenses as follows:

Item	Proposed by DRA		Adopted	
	1985	1986	1985	1986
	(Thousands of Dollars)			
Employee Communications	$ 551	$1,006	$ 164	$ 594
Community Relations	995	1,473	700	700
Information Communications Center	857	925	857	925
Overheads	599	470	429	306
Total Public Affairs	3,001	3,874	2,150	2,525
Lobbying	322.1	369.0	322.1	369.0
Lobbying Support and Monitoring	297	309	297	309
Telephone Assn. Membership Dues		222		222
Total	3,621	4,773	2,769.1	3,425

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Total	3,621	4,773	2,769	3,425

Rebuttal testimony on the adjustments for Employee Communications, Community Relations, and Information Communications Center was presented on behalf of General by its Employee Communications Manager, Don Anderson.

According to the testimony of witness Simmons, the Employee Communications disallowance consisted of $35,000 in 1985 and $457,000 in 1986 as a result of open house events and employee orientation expenses relative to moving to the new headquarters building and should be excluded for ratemaking purposes as nonrecurring and inapplicable to the test year. Further, according to this witness, the Employee Communications activities provide a dual function: partly to enhance the corporate image of the company and partly to inform. Therefore, he recommends a 50% disallowance for the remaining expenses resulting in an overall expense disallowance of $551,000 for 1985 and $1,006,000 for 1986. General's witness Anderson objected to the 50% disallowance on the

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According to witness Simmons, the stated purpose of the Community Relations section is to enhance the company's image in the community. It is primarily responsible for the allocation of $2.2 million of charitable contributions and the planning, coordination, and execution of other activities of a philanthropic nature. Consequently, according to this witness, all the expenses of the Community Relations section are primarily for the purpose of corporate image enhancement and are therefore stockholder interest expenses not properly chargeable to the ratepayer. Consequently he is recommending a total disallowance of this group's expenses for 1985 and 1986 resulting in a decrease in expenses of $995,000 in 1985 and $1,473,000 in 1986.

According to the testimony of General's rebuttal witness Anderson, Community Relations is responsible for General's consumer affairs program, the community needs assessment program, charitable contributions and volunteer referral. The Consumer Affairs Program coordinates a representative group of 21 of General's customers who constitute a consumer advisory panel and meet monthly for the purpose of providing General's management with recommendations and suggestions regarding corporate policies and procedures. The total expenditure for the Consumer Affairs Programs for 1985 and 1986 was approximately $205,000 annually. The Community Needs Assessment Program is administered by one of the Community Relations representatives and is designed to systematically collect the opinions and concerns of cross-section of community leadership through a series of personal interviews to obtain comments on community needs and general services. The Community Relations Group is responsible for designing programs in instances where there is a broad consensus that a particular type of need that relates to telephone service is of major concern to a particular community. The total expense for this group for 1985 and 1986 was approximately $265,000. Another function of the Community Relations Group is the volunteer program which channels requests from various community groups to employees who may be interested in volunteering. According to this witness's testimony, the role of the Community Relations staff is to serve simply as a provider of that information for the various agencies. Volunteers contribute their own time and are not required to identify themselves as General employees. The cost of this function for 1985 and 1986 was approximately $180,000 annually. Another program run by the Community Relations Group is the Contributions Program. The Contributions Program is responsible for responding to all requests and, in cases where General guidelines deem it appropriate, grants are made to selected agencies from a BTL contributions account. The annual expenses of the Contributions Program are approximately $100,000. Since approximately half of the responsibility is to respond to requests that do not qualify for funds, it is General's belief that $50,000 would be an appropriate allowance for ratemaking purposes. The total of the above-discussed programs is approximately $700,000 annually which, General believes, should be allowed for Community Relations Group.

It is noted that the above $700,000 is less than half of the recommended 1986 expense disallowance of DRA witness Simmons. General's position does not appear unreasonable and we will adopt the $700,000 figure for Community Relations.

According to DRA witness Simmons, the Information Communications Center (ICC) is responsible for all audio visual and television programs produced by General. In addition, the ICC is responsible for the information, distribution, network, and operations of the video conferencing center. This witness reviewed a descriptive list of all video and audio productions of the ICC during 1985 and 1986 and planned for during 1987, and determined that many of the productions fall into the category of corporate image enhancement and are therefore not allowable for ratemaking purposes. Further, according to this witness's testimony, he was unable to obtain the specific cost data for each individual production, as the company was only able to provide data on "average cost by class of production". Lacking the specific cost data and considering the dual nature of many of these audio visual productions that this section provides to the employee communications system, this witness recommends an overall disallowance of 50% for ICC's 1985 and 1986 expense. This amounts to $856,500 for 1985 and $924,500 for 1986.

According to General's witness Anderson, the ICC has the employee work force as its primary audience for its productions. Further, according to this witness, whereas employee communications specializes in written publications, the ICC specializes in video productions. The mission of ICC is to help assure that the company has informed, involved, and knowledgeable employees to provide high quality products and services to the ratepayers. Witness Anderson further testified that ICC does work, which, General would agree, is not primarily for the benefit of the company employees or ratepayers. According to his testimony, the amount of this other work totaled $130,000 for 1985 and totaled $198,000 for 1986, production, as the company was only able to provide data on "average cost by class of production". Lacking the specific cost data and considering the dual nature of many of these audio visual productions that this section provides to the employee communications system, this witness recommends an overall disallowance of 50% for ICC's 1985 and 1986 expense. This amounts to $856,500 for 1985 and $924,500 for 1986.

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DRA's witness Simmons' recommendation that lobbying expenses of $322,000 for 1985 and $369,000 for 1986 and other governmental affairs expenses of $297,000 for 1985 and $309,000 for 1986 be disallowed adhere to our general policies and past practices and will be adopted. We will also adopt this witness's recommendation that membership dues of $222,000 for 1986 be disallowed.

11. Prudence of Relocation

DRA Financial Examiner Jean Hill presented an analysis of the prudence of General's decision to invest in a new administration building in Thousand Oaks. This analysis indicated that General's decision to relocate to Thousand Oaks is noncost-effective and that the nonquantified considerations are not sufficient to support the investment decision. DRA consequently recommends that $67 million be disallowed from General's test year 1988 rate base to be offset by the above $31.5 million gain on the sale of property, testified to by DRA Auditor I Mar, for a net disallowance of $36 million. In addition to the $67 million disallowance on rate base, DRA recommends a disallowance of $21.5 million annual expense associated with employee relocation.

Rebuttal testimony to witness Hill was presented on behalf of General by its treasurer, Charles J. O'Rourke.

Prior to its relocation to the Thousand Oaks area, the General headquarters building configuration consisted of 14 separate sites of which all but one were located in the Santa Monica area. According to General's management, this fragmented building plan is operationally cost-ineffective as it requires extensive employee travel between buildings in the conduct of daily business and necessitates the duplication of common areas as well as support services such as word processing and reproduction facilities. Furthermore, due to age most of the buildings would require refurbishment with three of the major sites requiring extensive overhaul. In arriving at its decision to relocate the headquarters to the Thousand Oaks area, General assessed three alternative headquarters scenarios: stay in the existing locations and refurbish them; consolidate in Santa Monica; and consolidate in Thousand Oaks. According to the testimony of witness Hill, a major factor in the decision to relocate to Thousand Oaks was the opportunity for gaining profit on sales of existing property. In particular, General held a long-term lease on a building at 100 Wilshire with a purchase option. The exercise of this option afforded General an immediate profit. DRA is recommending that this Commission adopt rates that will reflect the most cost-effective alternative so that the ratepayers are not penalized for General's alleged imprudent management decision. Specifically, DRA is recommending that General be allowed a maximum rate base of $48.9 million for its investment in Thousand Oaks. Based on recorded capital costs of $113 million, this represents a disallowance of approximately $64.1 million. DRA's rationale for the above disallowance is based on its recommendation that the cost allowed for General's new headquarters should not exceed what the cost would have been for the most cost-effective alternative, in this case, renovation of existing quarters. According to DRA witness Hill, the present value of the present status alternative is $95.9 million, which equates to a rate base of $48.9 million and an annual expense of $4.5 million.

DRA's cost-effectiveness studies differed from General's in two key assumptions which are: (1) offsetting the Thousand Oaks' capital investment by the gain from the sales of existing properties in Santa Monica; and (2) the inclusion of the cost of 12 acres of undeveloped land in the present status alternative. According to the record, were witness Hill to accept these two assumptions then DRA would agree with General's findings that the investment in the Thousand Oaks relocation is cost-effective. General records the gain on the sale of property BTL which allocates 100% of the gain to the stockholders. Consequently, according to DRA, the gains have no impact on the ratepayers and it is inappropriate to include them in the analysis. The cost of the 12 acres of land was included in the present status alternative to make it comparable to the Thousand Oaks alternative, which included 12 acres of undeveloped land that were recorded in the miscellaneous physical property count, a BTL.

General witness O'Rourke presented rebuttal testimony which indicated that:

1. General rejected the alternative of remaining in the existing 14 Santa Monica buildings due to the inefficient building configuration and the extensive investment required to renovate four of the major buildings.

2. The after-tax present value of cash flows was the focus of General's financial recommendation to relocate the headquarters to the Thousand Oaks area.

3. General used the traditional after-tax financial model to develop the final decision criteria and the revenue model in support of an analysis.

4. General addressed the long-term cost of the decision regarding location of its headquarters facilities separately and

independently of accounting and ultimate ratemaking treatment of the gain from the sale of its Santa Monica properties.

5. The accounting and ratemaking treatment of the gain of sales of properties resulting in the relocation is an independent issue separate from the financial analysis of the decision about whether or not to relocate.

6. The Uniform System of Accounts requires that the gain on sale of property by a telephone company be recorded in Account 360-Extraordinary Income (a BTL account) regardless of the future ratemaking treatment of any gain and regardless of whether the property is included or excluded from the utility's rate base.

7. The proceeds from the sale of surplus property in Santa Monica should be used to reduce the estimated cost of the relocation to Thousand Oaks.

8. The acquisition of the 85-acre site in Thousand Oaks included a 12-acre parcel that would be held for future use. In order to fairly compare the economics of the alternatives for General's management, General had to include the cost of a similar parcel in the Santa Monica alternatives.

9. General's Operations and Human Resources Departments identified several tangible benefits which were not quantified for the purpose of financial analysis but were seriously weighed by General's management in arriving at its decision.

10. The decision to relocate was based on an analysis of cash flows and not on the opportunity for capital gains in the relocation process.

We agree, in general, with the allegations set forth above, particularly with the assertion that the accounting and bookkeeping treatment of a transaction should not be a factor in economic analysis designed to test the prudence of a decision to either remain in Santa Monica or to relocate to Thousand Oaks. Consequently, in consideration of both General's and DRA's testimony and exhibits on this matter, we conclude that the relocation to Thousand Oaks was not imprudent. Therefore, we will neither adopt DRA's recommendation that $64.1 million be disallowed from General's rate base for test year 1988 nor that the maximum annual expense allowance be limited to $4.5 million.

12. Gain On Sale of Property

Concurrent with its 1985 corporate headquarters relocation, General sold several properties, including offices in Santa Monica at 2224 Colorado Avenue, 100 Wilshire Boulevard, and 2020 Santa Monica Boulevard. DRA's auditors ascertained that these properties had been booked in various above-the-line accounts prior to being transferred below the line in anticipation of their sale. The auditors recommend that the gain on the sale of these properties be recorded above the line, because each property was supported by ratepayers, and was in rate base, for the majority of its useful life. DRA's auditors believe that this recommendation is consistent with the ratemaking treatment adopted by the Commission for similar types of buildings and parcels in several decisions, including Pacific Bell's ongoing general rate proceeding.

For example in D.86-01-026, issued at the conclusion of the first phase of A.85-01-034, the Commission stated:

> "Land which has been in Account 100.1 appreciates as utilities hold it over time because all costs of ownership, including a return, are funded by ratepayers. Accordingly, when land is taken out of service or rate base any net gain should accrue above the line, and utilities, of course, have an obligation to maximize receipts from the land. Our rationale follows that of the FCC in its conclusion that any gain from parcels (including land) must accrue to ratepayers (CC Docket 81-893, Report & Order adopted November 23, 1983, pp. 97-99.)"

the period of time over which such gain is to be amortized. As previously stated, according to rebuttal witness Wilson, the net effect of combining the after-tax gain of $24.1 million from the sale of the Santa Monica properties with the after-tax cost of $15.5 million for relocating the staff, moving the company's physical property, and renovating the headquarters buildings results in a net gain of $8.6 million.

On balance we believe General's offset argument is more persuasive, given the particular set of facts presented. In this situation there was not a straightforward stand-alone sale of property; rather this was a unified transaction. But for the decision to relocate to Thousand Oaks, the sales would not have occurred. Given the unified nature of the transaction General's proposed offset presents, in any event, an acceptable method of treating the nonrecurring relocation costs incurred in connection with the move to Thousand Oaks, while flowing the gain through to its ratepayers.

Translating the net gain of $8.6 million to before-tax net gain results in a figure of $13.3 million, which we find a reasonable adjustment to reflect the relocation of the general office staff to Thousand Oaks. To this should be added the $154,000 gain before taxes for the sale of the State Street and Avenida La Fonda properties, making a total of $13,454,000. We will also adopt the staff's recommended 3-year amortization period resulting in a miscellaneous revenue for the 1988 test year of $4,485,000, for a gain on the sale of properties.

E. Revenues

1. General

Testimony on 1988 test year revenues was presented by program and project supervisor K. P. Coughlan, public utility regulatory specialists I R. R. Berry and E. S. Ting, and senior utilities engineer N. C. Low. Total operating revenues consist of subscriber station revenues including monthly service charges, service connection; public telephone, total message charges, gross ZUM charges, and connecting company charges and credits; local service revenues consisting of public telephone revenues, local private lines, and other local service revenues; access revenues including intrastate and intrastate access and toll revenues; and miscellaneous revenues including telegraph commissions, directory revenues, rent revenues, general service and license, other miscellaneous revenues, and intrastate and intrastate billing and collecting, and surcharge revenues less uncollectibles. The tabulation below sets forth the revenue estimates as estimated by DRA and General, the difference between the two in amount and percent, and our adopted revenues. The bases for our adopted revenues are set forth in the ensuing paragraphs.

service connection, semi-public telephone, total message charges, gross ZUM charges, and connecting company charges and credits; local service revenues consisting of public telephone revenues, local private lines, and other local service revenues; toll service revenues including interstate and intrastate access and intraLATA toll revenues; and miscellaneous revenues including telegraph commissions, directory revenues, rent revenues, general service and license, other miscellaneous revenues, and interstate and intrastate billing and collecting, and surcharge revenues less uncollectibles. The tabulation below sets forth the revenue estimates as estimated by DRA and General, the difference between the two in amount and percent, and our adopted revenues. The bases for our adopted revenues are set forth in the ensuing paragraphs.

Item	DRA	General	General Exceeds Staff Amount	General Exceeds Staff Percent	Adopted
		(Thousands of Dollars)			
Subscriber Station Revenues:					
Monthly Svce Chg.	$ 441,753	$ 430,926	$ (10,827)	(2.5)	$ 441,753
Service Conn.	66,336	71,436	5,100	7.7	66,336
Semi-public	7,000	7,019	19	0.3	7,000
Total Mess. Chgs.	113,400	116,131	2,731	2.4	113,400
Gross ZUM Chgs.	97,890	95,273	(2,617)	(2.7)	97,890
Conn. Co. Chgs.& Cr.	3,259	2,887	(372)	(11.4)	(3,909)
Subtotal	729,638	723,672	(5,966)	(0.8)	722,470
Local Service Revenues					
Public Tel. Rev.	33,260	31,798	(1,462)	(4.4)	33,260
Local PL Intrastate	3,900	5,559	1,659	42.5	3,900
Other Local Rev. (EAS)	12,430	18,439	6,009	48.3	16,617
Subtotal	49,590	55,796	6,206	1.3	53,777
Toll Service Rev.:					
IntraLATA	781,079	814,847	33,768	4.3	819,735
Intrastate Access	215,908	258,978	43,070	19.9	206,526
Interstate Access	480,425	480,425	0	0.0	480,425
Subtotal	1,477,412	1,554,251	76,839	5.2	1,506,686
Miscellaneous Rev.:					
Telegraph Comm.	19	19	0	0.0	19
Directory	231,480	198,292	(33,188)	(14.3)	205,000
Rent Revenues	1,804	1,804	0	0.0	1,804
Gen. Serv. & Lic.	1,133	1,133	0	0.0	1,133
Other Misc. Rev.	37,740	17,450	(20,290)	(53.8)	22,931
Intrastate Bill. & Coll.	26,675	20,253	(6,442)	(24.1)	26,675
Interstate Bill. & Coll.	23,819	23,819	0	0.0	23,819
Gain on Sale of Property	10,490	0	(10,490)	(100.0)	4,485
Subtotal	333,160	262,770	(70,390)	(21.1)	285,866
Surcharge Revenues	73,287	184,675	111,388	152.7	74,730
Total	2,663,087	2,781,164	118,077	4.4	2,644,056
Less: Uncoll.	18,594	24,368	5,774	31.1	21,630
Total	2,644,493	2,756,796	112,303	4.2	2,621,899
Adjustments:					
-1987 Attrition	*	(52,978)	(52,978)	(100.0)	
-AL 5110	*	(2,944)	(2,944)	(100.0)	
-FASB 87	*	9,113	9,113	100.0	
-IntraLATA SPF to SLU	*	3,050	3,050	100.0	
Total Revenues	2,644,493	2,713,036	68,544	2.6	

(Red Figure)

*Reflected in appropriate revenue categories.

Item	DRA	General	General Exceeds DRA Amount	General Exceeds DRA Percent	Adopted
		(Thousands of Dollars)			
Subscriber Station Revenues:					
Monthly Svce Chg.	$ 441,753	$ 430,926	$ (10,827)	(2.5)	$ 441,753
Service Conn.	66,336	71,436	5,100	7.7	66,336
Semi-public	7,000	7,019	19	0.3	7,000
Total Mess. Chgs.	113,400	116,131	2,731	2.4	113,400
Gross ZUM Chgs.	97,890	95,273	(2,617)	(2.7)	97,890
Conn. Co. Chgs.& Cr.	3,259	2,887	(372)	(11.4)	1,308
Subtotal	729,638	723,672	(5,966)	(0.8)	727,687
Local Service Revenues					
Public Tel. Rev.	33,260	31,798	(1,462)	(4.4)	33,260
Local PL Intrastate	3,900	5,559	1,659	42.5	3,900
Other Local Rev. (EAS)	12,430	18,439	6,009	48.3	15,839
Subtotal	49,590	55,796	6,206	1.3	52,999
Toll Service Rev.:					
IntraLATA	781,079	814,847	33,768	4.3	817,213
Intrastate Access	215,908	258,978	43,070	19.9	206,526
Interstate Access	480,425	480,425	0	0.0	480,425
Subtotal	1,477,412	1,554,251	76,839	5.2	1,504,164
Miscellaneous Rev.:					
Telegraph Comm.	19	19	0	0.0	19
Directory	231,480	198,292	(33,188)	(14.3)	205,000
Rent Revenues	1,804	1,804	0	0.0	1,804
Gen. Serv. & Lic.	1,133	1,133	0	0.0	1,133
Other Misc. Rev.	37,740	17,450	(20,290)	(53.8)	23,531
Intrastate Bill. & Coll.	26,675	20,253	(6,442)	(24.1)	26,675
Interstate Bill. & Coll.	23,819	23,819	0	0.0	23,819
Gain on Sale of Property	10,490	0	(10,490)	(100.0)	4,485
Subtotal	333,160	262,770	(70,390)	(21.1)	286,466
Surcharge Revenues	73,287	184,675	111,388	152.7	74,730
Total	2,663,087	2,781,164	118,077	4.4	2,646,046
Less: Uncoll.	18,594	24,368	5,774	31.1	21,638
Total	2,644,493	2,756,796	112,303	4.2	2,624,408
Adjustments:					
-1987 Attrition	*	(52,978)	(52,978)	(100.0)	*
-AL 5110	*	(2,944)	(2,944)	(100.0)	*
-FASB 87	*	9,113	9,113	100.0	*
-IntraLATA SPF to SLU	*	3,050	3,050	100.0	*
Total Revenues	2,644,493	2,713,037	68,544	2.6	2,646,408

(Red Figure)

*Reflected in appropriate revenue categories.

Item	DRA	General	General Exceeds DRA Amount	General Exceeds DRA Percent	Adopted
		(Thousands of Dollars)			
Subscriber Station Revenues:					
Monthly Svce Chg.	$ 441,753	$ 430,926	$ (10,827)	(2.5)	$ 441,753
Service Conn.	66,336	71,436	5,100	7.7	66,336
Semi-public	7,000	7,019	19	0.3	7,000
Total Mess. Chgs.	113,400	116,131	2,731	2.4	113,400
Gross ZUM Chgs.	97,890	95,273	(2,617)	(2.7)	97,890
Conn. Co. Chgs.& Cr.	3,259	2,887	(372)	(11.4)	1,308
Subtotal	729,638	723,672	(5,966)	(0.8)	727,687
Local Service Revenues					
Public Tel. Rev.	33,260	31,798	(1,462)	(4.4)	33,260
Local PL Intrastate	3,900	5,559	1,659	42.5	3,900
Other Local Rev. (EAS)	12,430	18,439	6,009	48.3	16,287
Subtotal	49,590	55,796	6,206	1.3	53,447
Toll Service Rev.:					
IntraLATA	781,079	814,847	33,768	4.3	822,392
Intrastate Access	215,908	258,978	43,070	19.9	206,526
Interstate Access	480,425	480,425	0	0.0	480,425
Subtotal	1,477,412	1,554,251	76,839	5.2	1,509,343
Miscellaneous Rev.:					
Telegraph Comm.	19	19	0	0.0	19
Directory	231,480	198,292	(33,188)	(14.3)	205,000
Rent Revenues	1,804	1,804	0	0.0	1,804
Gen. Serv. & Lic.	1,133	1,133	0	0.0	1,133
Other Misc. Rev.	37,740	17,450	(20,290)	(53.8)	23,531
Intrastate Bill. & Coll.	26,675	20,253	(6,442)	(24.1)	26,675
Interstate Bill. & Coll.	23,819	23,819	0	0.0	23,819
Gain on Sale of Property	10,490	0	(10,490)	(100.0)	4,485
Subtotal	333,160	262,770	(70,390)	(21.1)	286,466
Surcharge Revenues	73,287	184,675	111,388	152.7	74,730
Total	2,663,087	2,781,164	118,077	4.4	2,651,673
Less: Uncoll.	18,594	24,368	5,774	31.1	21,638
Total	2,644,493	2,756,796	112,303	4.2	2,630,035
Adjustments:					
-1987 Attrition	*	(52,978)	(52,978)	(100.0)	*
-AL 5110	*	(2,944)	(2,944)	(100.0)	*
-FASB 87	*	9,113	9,113	100.0	*
-IntraLATA SPF to SLU	*	3,050	3,050	100.0	*
Total Revenues	2,644,493	2,713,037	68,544	2.6	2,630,035

(Red Figure)

*Reflected in appropriate revenue categories.

General utilized a revenue regression forecast based on all in-service customer lines, ZUM rate, and a proxy variable for the recent expansion of ZUM calling area. DRA estimated the gross ZUM charges in the same manner it utilized for total message charges as described above. DRA's forecast of $97,890,000 appears reasonable and will be adopted for this proceeding.

Under a new ZUM settlement agreement between General and Pacific, which became effective on January 1, 1986, each company will "bill and keep" the revenue it receives for its originating ZUM Zones 2 and 3 traffic. Additionally this new settlement agreement requires both General and Pacific to pay each other for the termination of the other company's ZUM Zones 2 and 3 traffic. The net dollar amount of what General pays Pacific and that which Pacific pays General for the termination of ZUM Zones 2 and 3 traffic is referred to as connecting company charges and credits. DRA's estimate of General's 1988 connecting company charges and credits was $3,259,000 or $372,000 (11.4%) greater than General's estimate of $2,887,000. However, the effect of decreased access charges resulting from General's and Pacific's latest interLATA SPF to SLU AL filings, AL 5110 and AL 15325, respectively, results in General's connecting company charges and credits of a negative $3,909,000, which we will adopt as reasonable for this proceeding.

3. Local Service Revenues

Local service revenues consist of public telephone revenue, local private line intrastate revenues, and other local service revenue. As with semi-public telephone revenues, General estimated the public telephone revenues on the basis of a revenue regression methodology and DRA estimated its public telephone revenue as a product of estimated public telephones in service times the calls per phone times the local phone call rate of 20¢ per call to derive its estimate. We will adopt DRA's estimate of $33,260,000 as reasonable.

General used a revenue regression to forecast 1988 revenues of $5.56 million for local private line revenues. The staff has analyzed the account of local private lines and noted that the number of private lines declined from 41,761 to 34,631 from the period September 1984 to September 1986 and that during the same period the revenue per line declined from $12.74 to $12.26. Applying these declining growth factors to mid-1986 data produced a forecast for the test year 1988 of 29,245 lines and a revenue of $11.20 a line, or a forecast of $3.9 million for 1988 revenues, which we will adopt as reasonable.

Other local service revenues are extended area service (EAS) and settlement revenues, which General and all independent telephone companies (ICO) who provide EAS receive from Pacific. For 1988, DRA estimates that General will receive $12,430,000 in EAS payments from Pacific as contrasted to General's estimate of $18,439,000. The EAS settlement ratio for ICOs is determined by Pacific's local exchange billings, expenses, and investments. EAS agreements allow each ICO to recover its expenses and to earn Pacific's exchange settlement rate of return on investment used to provide EAS. Pacific books the EAS payment to the ICOs as an expense while the ICOs account for such payment as revenues. Whenever a participating ICO is granted an increase or decrease in exchange rates, Pacific's EAS payment to that ICO is reduced or increased, respectively. The increase or decrease in Pacific's EAS payment to an ICO is determined by ICO's "revenue credit". Revenue credit reflects the level of EAS settlement revenues that flow from the ICO to Pacific and is a function of the ICO's exchange billings and the ratio of the total number of EAS calls to the total of all exchange calls (local plus EAS). In accordance with our adopted EAS settlement expenses, taxes, and investments, which are reflected in the exchange category, we will adopt as reasonable in this proceeding $16,617,000 for the other local service revenue.

General used a revenue regression to forecast 1988 revenues of $5.56 million for local private line revenues. The staff has analyzed the account of local private lines and noted that the number of private lines declined from 41,761 to 34,631 from the period September 1984 to September 1986 and that during the same period the revenue per line declined from $12.74 to $12.26. Applying these declining growth factors to mid-1986 data produced a forecast for the test year 1988 of 29,245 lines and a revenue of $11.20 a line, or a forecast of $3.9 million for 1988 revenues, which we will adopt as reasonable.

Other local service revenues are extended area service (EAS) and settlement revenues, which General and all independent telephone companies (ICO) who provide EAS receive from Pacific. For 1988, DRA estimates that General will receive $12,430,000 in EAS payments from Pacific as contrasted to General's estimate of $18,439,000. The EAS settlement ratio for ICOs is determined by Pacific's local exchange billings, expenses, and investments. EAS agreements allow each ICO to recover its expenses and to earn Pacific's exchange settlement rate of return on investment used to provide EAS. Pacific books the EAS payment to the ICOs as an expense while the ICOs account for such payment as revenues. Whenever a participating ICO is granted an increase or decrease in exchange rates, Pacific's EAS payment to that ICO is reduced or increased, respectively. The increase or decrease in Pacific's EAS payment to an ICO is determined by ICO's "revenue credit". Revenue credit reflects the level of EAS settlement revenues that flow from the ICO to Pacific and is a function of the ICO's exchange billings and the ratio of the total number of EAS calls to the total of all exchange calls (local plus EAS). In accordance with our adopted EAS settlement expenses, taxes, and investments, which are reflective of the exchange category, we will adopt as reasonable in this proceeding $15,839,000 for the other local service revenue.

General used a revenue regression to forecast 1988 revenues of $5.56 million for local private line revenues. The staff has analyzed the account of local private lines and noted that the number of private lines declined from 41,761 to 34,631 from the period September 1984 to September 1986 and that during the same period the revenue per line declined from $12.74 to $12.26. Applying these declining growth factors to mid-1986 data produced a forecast for the test year 1988 of 29,245 lines and a revenue of $11.20 a line, or a forecast of $3.9 million for 1988 revenues, which we will adopt as reasonable.

Other local service revenues are extended area service (EAS) and settlement revenues, which General and all independent telephone companies (ICO) who provide EAS receive from Pacific. For 1988, DRA estimates that General will receive $12,430,000 in EAS payments from Pacific as contrasted to General's estimate of $18,439,000. The EAS settlement ratio for ICOs is determined by Pacific's local exchange billings, expenses, and investments. EAS agreements allow each ICO to recover its expenses and to earn Pacific's exchange settlement rate of return on investment used to provide EAS. Pacific books the EAS payment to the ICOs as an expense while the ICOs account for such payment as revenues. Whenever a participating ICO is granted an increase or decrease in exchange rates, Pacific's EAS payment to that ICO is reduced or increased, respectively. The increase or decrease in Pacific's EAS payment to an ICO is determined by ICO's "revenue credit". Revenue credit reflects the level of EAS settlement revenues that flow from the ICO to Pacific and is a function of the ICO's exchange billings and the ratio of the total number of EAS calls to the total of all exchange calls (local plus EAS). In accordance with our adopted EAS settlement expenses, taxes, and investments, which are reflective of the exchange category, we will adopt as reasonable in this proceeding $16,287,000 for the other local service revenue.

4. Toll Service Revenues (IntraLATA)

IntraLATA toll service revenues consist of message toll and toll private line revenues. General's estimate for intrastate intraLATA toll revenues is based on moneys estimated to be received via a statewide "settlement" process administered by Pacific and participated in by all California ICOs. This settlement process allows each ICO to recover its actual expenses and to earn a return on its investment associated with the provision of intrastate intraLATA toll service. The settlement expenses and investments associated with message toll and toll private line services are allocated using a procedure known as "telephone cost separations" as contained in Part 67 of the FCC Rules and Regulations. The estimates of General's intrastate intraLATA toll service revenues are based on estimates of "industry billings" for the ICOs including Pacific and General. Additionally, the intraLATA toll service revenues are based on General's settlement expenses, taxes, and plant investments. Based on our adopted intraLATA toll settlement expenses, taxes, and plant investments, the intraLATA toll service revenues are $819,735,000 which we will adopt as reasonable.

5. Access Revenues

Included in this category of access revenues are intrastate access revenues and interstate access revenues. Since revenues from interstate access charges do not directly affect intrastate results of operations, DRA agreed to use General's estimate of gross interstate access revenues of $504,244,000 for this results of operations analysis. This $504,244,000 figure includes $23,819,000 for interstate billing and collection services. DRA's estimate of intrastate access revenues is $242,583,000 including $26,675,000 as intrastate billing and collecting as compared to General's estimate of $279,231,000 including $20,253,000 of intrastate billing and collecting. The difference between these two estimates is $36,648,000 or 15.1%.

4. Toll Service Revenues (IntraLATA)

IntraLATA toll service revenues consist of message toll and toll private line revenues. General's estimate for intrastate intraLATA toll revenues is based on moneys estimated to be received via a statewide "settlement" process administered by Pacific and participated in by all California ICOs. This settlement process allows each ICO to recover its actual expenses and to earn a return on its investment associated with the provision of intrastate intraLATA toll service. The settlement expenses and investments associated with message toll and toll private line services are allocated using a procedure known as "telephone cost separations" as contained in Part 67 of the FCC Rules and Regulations. The estimates of General's intrastate intraLATA toll service revenues are based on estimates of "industry billings" for the ICOs including Pacific and General. Additionally, the intraLATA toll service revenues for General are based on the relationship of General's settlement expenses, taxes, and plant investments to that of the industry. Based on our adopted intraLATA toll settlement expenses, taxes, and plant investments, the intraLATA toll service revenues are $817,213,000 which we will adopt as reasonable. ✓

5. Access Revenues

Included in this category of access revenues are intrastate access revenues and interstate access revenues. Since revenues from interstate access charges do not directly affect intrastate results of operations, DRA agreed to use General's estimate of gross interstate access revenues of $504,244,000 for this results of operations analysis. This $504,244,000 figure includes $23,819,000 for interstate billing and collection services. DRA's estimate of intrastate access revenues is $242,583,000 including $26,675,000 as intrastate billing and collecting as compared to General's estimate of $279,231,000 including $20,253,000 of intrastate billing and collecting. The difference between these two estimates is $36,648,000 or 15.1%.

4. Toll Service Revenues (IntraLATA)

IntraLATA toll service revenues consist of message toll and toll private line revenues. General's estimate for intrastate intraLATA toll revenues is based on moneys estimated to be received via a statewide "settlement" process administered by Pacific and participated in by all California ICOs. This settlement process allows each ICO to recover its actual expenses and to earn a return on its investment associated with the provision of intrastate intraLATA toll service. The settlement expenses and investments associated with message toll and toll private line services are allocated using a procedure known as "telephone cost separations" as contained in Part 67 of the FCC Rules and Regulations. The estimates of General's intrastate intraLATA toll service revenues are based on estimates of "industry billings" for the ICOs including Pacific and General. Additionally, the intraLATA toll service revenues for General are based on the relationship of General's settlement expenses, taxes, and plant investments to that of the industry. Based on our adopted intraLATA toll settlement expenses, taxes, and plant investments, the intraLATA toll service revenues are $822,392,000 which we will adopt as reasonable.

5. Access Revenues

Included in this category of access revenues are intrastate access revenues and interstate access revenues. Since revenues from interstate access charges do not directly affect intrastate results of operations, DRA agreed to use General's estimate of gross interstate access revenues of $504,244,000 for this results of operations analysis. This $504,244,000 figure includes $23,819,000 for interstate billing and collection services. DRA's estimate of intrastate access revenues is $242,583,000 including $26,675,000 as intrastate billing and collecting as compared to General's estimate of $279,231,000 including $20,253,000 of intrastate billing and collecting. The difference between these two estimates is $36,648,000 or 15.1%.

$222 million. We will adopt the $205 million estimate as reasonable for this proceeding.

General's estimate of Other Miscellaneous Revenues is $17,450,000 as contrasted to DRA's estimate of $37,740,000. The difference is DRA's inclusion of its proposed GTEL adjustment of $18,290,000 and its proposed GTE Telecom adjustment of $2 million with its miscellaneous revenue estimate of $17,450,000. As previously discussed, we disallowed the $2 million GTE Telecom adjustment, and allowed only $5,481,000 of the recommended GTEL adjustment of $18,290,000. Consequently we will adopt as reasonable, for miscellaneous revenues, the amount of $22,931,000 equal to the original estimate of $17,450,000 plus the allowed $5,481,000 GTEL adjustment.

As previously discussed, we are adopting a miscellaneous revenue component item of $4,485,000 a year for a three-year period, i.e. 1988, 1989, and 1990, to reflect a gain on the sale of property.

The application of the surcharge rates authorized by D.87-12-070 dated December 22, 1987 as revised by AL 5125 effective 4-10-88 of 4.43% for intraLATA toll, 7.19% for exchange service, and a negative 2.96% for access service to our adopted billings yields a surcharge revenue of $74,730,000, which we will adopt as reasonable for this proceeding.

Uncollectible revenues include amounts of revenues which have proved impractical to collect because subscribers either cannot be located by the utility or the cost of locating such subscribers exceeded the revenues that would be recovered if they were located. General's estimate of uncollectibles for test year 1988 of $24.368 million was presented into evidence by one of its senior economists, Luigi F. Pinna, and DRA's estimate of uncollectibles of $20,502,000 was presented into evidence by one of its program and project supervisors, Kevin P. Coughlan. General's estimate was based on a rate of 1.40%; DRA's estimate was based on a rate of 1.0%. In response to a DRA data request, General submitted a later forecast of $23.2 million which was based on a rate of 1.31%. According to the record, the uncollectible rate for the year 1984 was 2.2%, for 1985 was 1.9%, and the 11 months recorded and 1 month estimated for 1986 was 1.7%. Both General and DRA agreed that special consideration should be given to the implementation of a late payment charge (LPC) and the centralized credit check system (CCCS) in arriving at the appropriate uncollectible rate. DRA witness Coughlan contends that General's estimating model cannot accurately capture the effects of the CCCS and the LPC as these two programs only recently became effective. On this basis this witness believes the staff estimate is a reasonable expectation of what uncollectibles should be for the test year considering the downward trend of uncollectibles in General's own forecast. We agree that the CCCS and LPC programs should have the effect of reducing the rate of uncollectibles, but we believe General's estimate has understated the effect whereas DRA's estimate has overstated the effect. Consequently we will adopt as reasonable for this proceeding an uncollectible rate of 1.2%. Applying this rate to our adopted revenue figures results in an uncollectible amount of $21,630,000 which we will adopt as reasonable.

F. <u>Maintenance Expense</u>

Maintenance expenses are comprised of cost for labor, material, and administrative charges incurred in the repair and rearrangement of operating plant. General records maintenance expenses both in accordance with the FCC Uniform System of Accounts as adopted by this Commission and in accordance with its own accounting system where the accounts are designated with a "m" code for "moves and changes" and "r" code for "repairs". Repairs consist of charges for routine repairs and General's upkeep to outside plant facilities, inside wiring, central office equipment, and buildings and grounds, to maintain them in good physical

working condition. Included also in upkeep is the cost for locating and clearing trouble in these facilities and the cost of power for transmitting traffic and operating supervisory signals. Moves and changes mainly consist of cost of relocating, rearranging, or replacing minor units of outside plant equipment and central office equipment. DRA's test year maintenance expense estimate is $412,062,000, which is $79,614,000 or 19.3% less than General's estimate of $491,676,000. The major reasons for the difference in the estimated amounts are the use of different methodologies, different productivity factors, different labor escalation rates, different nonlabor escalation rates, different workload volumes, and the availability to DRA of later historical data. The tabulation that follows lists by accounts DRA's and General's estimates, together with our adopted results. The bases for the adopted results are set forth in the ensuing paragraphs.

Maintenance Expenses

Acc. No.	Item	DRA	General	General Exceeds DRA Amount	General Exceeds DRA Percent	Adopted
				(Thousands of Dollars)		
602	Outside Plant	$183,427	$204,525	$21,098	11.5%	$194,384
603	Test Desk Work	48,928	57,999	9,071	18.5	53,609
604	Central Office	120,201	139,537	19,336	16.1	121,610
605	Station Equip.	17,941	11,079	(6,862)	(38.2)	18,157
606	Bldgs. & Grounds	14,554	17,402	2,848	19.6	15,365
607	Public Tel. Equip.	7,527	8,531	1,004	13.3	7,620
610	Transm. Power	18,678	19,333	655	3.5	19,333
612	Other Maint. Exp.	1,212	1,686	474	39.1	1,449
	Subtotal					431,527
	GTED	(406)		406		(297)
	Inside Wiring	a/	31,584	31,584		
	Total	412,062	491,676	79,614	19.3	431,230

(Red Figure)

a/ $12,978,000 for inside wiring included in Account 605.

working condition. Included also in upkeep is the cost for locating and clearing trouble in these facilities and the cost of power for transmitting traffic and operating supervisory signals. Moves and changes mainly consist of cost of relocating, rearranging, or replacing minor units of outside plant equipment and central office equipment. DRA's test year maintenance expense estimate is $412,062,000, which is $79,614,000 or 19.3% less than General's estimate of $491,676,000. The major reasons for the difference in the estimated amounts are the use of different methodologies, different productivity factors, different labor escalation rates, different nonlabor escalation rates, different workload volumes, and the availability to DRA of later historical data. The tabulation that follows lists by accounts DRA's and General's estimates, together with our adopted results. The bases for the adopted results are set forth in the ensuing paragraphs.

Maintenance Expenses

Acc. No.	Item	DRA	General	General Exceeds DRA Amount	General Exceeds DRA Percent	Adopted
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603	Test Desk Work	48,928	57,999	9,071	18.5	53,609
604	Central Office	120,201	139,537	19,336	16.1	121,610
605	Station Equip.	17,941	11,079	(6,862)	(38.2)	18,157
606	Bldgs. & Grounds	14,554	17,402	2,848	19.6	15,365
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612	Other Maint. Exp.	1,212	1,686	474	39.1	1,449
	Subtotal					431,627
	GTED	(406)		406		(297)
	Inside Wiring	a/	31,584	31,584		
	Total	412,062	491,676	79,614	19.3	431,330

(Red Figure)

a/ $12,978,000 for inside wiring included in Account 605.

experienced by General for the period 1982 through 1986 was in the year 1983 where it was slightly under 7.8. Under these circumstances, the utilization of a 7.33 productivity labor level appears excessive. We will utilize a productivity factor of 7.8, which is the equivalent of a reduction of approximately 30% in the noise mitigation program. This translates into a reduction of approximately $1.5 million, which we will add to DRA's estimate of $32,033,000 to yield a figure of $33,533,000. We will increase this figure to $34,400,000 to reflect our previously discussed adopted labor escalation rate and find this figure to be reasonable for this proceeding.

General's estimate for OSP repair plant overhead is $17,949,000 as contrasted to DRA's estimate of $15,098,000. According to witness Mirza, the main reason for the $2,851,000 difference is staff's lower basic labor expense estimate and different methodology. Consistent with our adopted $34,400,000 basic labor expense, we will adopt plant overhead expense of $16,200,000.

General's estimate for OSP repair minor material is $9,334,000 as compared to the staff's estimate of $5,073,000. According to witness Mirza, the main reason for the $4,261,000 differential is the staff's lower basic level expense estimate and different methodology. The staff's estimate is based on the average of 1985 and 1986 historical ratios of minor material to basic labor adjusted for escalation rates. We will adopt DRA's estimate of $5,073,000 adjusted to reflect our adopted basic labor expense and our previously discussed nonlabor escalation rates or $5,450,000.

Adding the above adjustments of $2,367,000 to basic labor, $1,102,000 to overhead, and $377,000 for minor materials to the staff's estimate of $81,330,000 for repairs, we derive a figure of $85,076,000 for repairs which we will adopt as reasonable for this proceeding.

productivity level for test year 1988 for nonspecial service order assignment hours. For the special service hours, DRA examined General's productivity level as measured by special service hours per serving links for the period 1984 through 1986. The productivity measurements prior to 1984 were not examined because General did not have the necessary historical data on serving links. For the periods studied, General has shown a constant improvement in productivity. In addition, it will have improvement from its switch access system (SAS), which provides remote test access to special service circuits and thereby improves the ability of the utility to perform the maintenance operation of this special service circuits. It is estimated that the test year maintenance level reduction from the SAS is 125,000 hours. For the period 1981 through 1985, the average hour per service order was .380. We will use this amount for the computation of the service order assignment expense for the nonspecial service order assignment hours. We will adopt DRA's expenses associated with the special service hour portion of the expense. Under these circumstances, we find the special order assignment expense of $42,281,000 is reasonable and will adopt it for this proceeding.

General's estimate for plant overhead is $15,142,000, which is $4,265,000 or 39.2% above DRA's estimate of $10,877,000. According to the record, the main reasons for the $4,265,000 difference are lower staff basic labor expense estimate and different methodology used. We will adopt DRA's estimate of $10,877,000 increased by $303,000 to reflect our previously discussed adopted labor and nonlabor escalation factors.

In accordance with our above discussion, our adopted Account 602-Outside Plant Maintenance expense amount is $194,384,000, consisting of $85,076,000 repair and $109,308,000 outside plant moves and changes.

General's estimate of Account 603-Test Desk Work is $57,999,000, which is $9,071,000 or 18.5% over DRA's estimate of

FCC Account 605-Station Equipment includes General's Accounts M43-Station Apparatus Official Moves and Changes, R43-Station Apparatus Official Repairs, M44-Station Apparatus Repair Shops, M45-Station Apparatus Connections (IW) Moves and Changes, and R45-Station Apparatus Connections (IW) Repairs. General's estimate excluding inside wiring cost is $11,079,000, which is $6,116,000 less than DRA's estimate of $17,941,000. The major difference for the non-inside wire portion of the account is DRA's lower estimate of the utility's Account M44-Station Apparatus Repair Shops. This account is directly affected by the deregulation of terminal equipment which was to be 100% completed by January 1, 1988. As of that date, the only equipment remaining in the regulated environment will be that equipment actually used by the utility conducting the regulated operations known as company official terminal equipment. According to the testimony of DRA witness Hodges, the effect of the deregulation would be to decrease station apparatus repair shop activity by 60% in 1987 and 1988 as compared to 1986. His estimate reflects this reduction as contrasted to General's estimate which did not. We will adopt DRA's estimate of $4,963,000 for the non-inside wiring portion of this account increased by $216,000 to $5,179,000 to reflect our previously adopted escalation factors. DRA's estimate of inside wiring cost is $12,978,000 while General's is $31,584,000. We will adopt as reasonable for this proceeding DRA's estimate of $12,978,000 for inside wiring costs for a total for FCC Account 605-Station Equipment amount of $18,157,000.

General's estimate for FCC Account 606-Buildings and Grounds is $17,402,000 which is $2,848,000 or 19.6% greater than DRA's estimate of $14,554,000. FCC Account 606 consists of two general accounts, M12-Land and Buildings Moves and Changes and R12-Land and Buildings Repairs. According to the testimony of DRA witness Hodges, the primary difference for DRA's lower estimate for both accounts M12 and R12 is the effect of historical adjustments to these accounts as recommended by staff auditor, S. McCarthy. As previously discussed, we will amortize the corporate headquarters improvements carried in Subaccount M12 of $1,074,000 for 1985 and $300,000 for 1986 over a three-year period. The result of this three-year amortization will be to increase the M12 account by $458,000. As previously discussed, we will allow $353,000 for test year toxic waste cleanup. We will therefore adopt $15,248,000 for Account 606 expense, which is equal to DRA's estimate of $14,554,000 plus the above-discussed two increases totaling approximately $811,000.

General's estimate for FCC Account 607-Public Telephone Equipment is $8,531,000 which is $1,004,000 or 13.3% higher than DRA's estimate of $7,527,000. According to the testimony of witness Hodges, the major difference in this account is due to DRA's lower estimate for the utility's Account R47-Public Telephone Equipment Repairs because of the use of a better productivity for test year 1988 than was used by General. We will adopt DRA's estimate of $7,527,000 for this account increased by $93,000 to $7,620,000 to reflect previously discussed escalation factors.

General's estimate of FCC Account 610-Maintenance of Transmission Towers is $19,333,000 which is $655,000 or 3.5% higher than DRA's estimate of $18,678,000. The difference in the estimates for this account is due to DRA's use of a lower test year estimate of kilowatt-hours of usage than used by General. We will adopt General's estimate of $19,333,000 for this account. General's estimate for FCC Account 612-Other Maintenance Expense is $1,686,000 or $474,000 or 39.1% greater than DRA's estimate of $1,212,000. DRA used a better productivity factor than did General in the preparation of its estimates. We will adopt as reasonable for this account the amount of $1,449,000, the average of the two estimates.

to these accounts as recommended by staff auditor, S. McCarthy. As previously discussed, we will amortize the corporate headquarters improvements carried in Subaccount M12 of $1,074,000 for 1985 and $300,000 for 1986 over a three-year period. The result of this three-year amortization will be to increase the M12 account by $458,000. As previously discussed, we will allow $353,000 for test year toxic waste cleanup. We will therefore adopt $15,365,000 for Account 606 expense, which is equal to DRA's estimate of $14,554,000 plus the above-discussed two increases totaling approximately $811,000.

General's estimate for FCC Account 607-Public Telephone Equipment is $8,531,000 which is $1,004,000 or 13.3% higher than DRA's estimate of $7,527,000. According to the testimony of witness Hodges, the major difference in this account is due to DRA's lower estimate for the utility's Account R47-Public Telephone Equipment Repairs because of the use of a better productivity for test year 1988 than was used by General. We will adopt DRA's estimate of $7,527,000 for this account increased by $93,000 to $7,620,000 to reflect previously discussed escalation factors.

General's estimate of FCC Account 610-Maintenance of Transmission Towers is $19,333,000 which is $655,000 or 3.5% higher than DRA's estimate of $18,678,000. The difference in the estimates for this account is due to DRA's use of a lower test year estimate of kilowatt-hours of usage than used by General. We will adopt General's estimate of $19,333,000 for this account. General's estimate for FCC Account 612-Other Maintenance Expense is $1,686,000 or $474,000 or 39.1% greater than DRA's estimate of $1,212,000. DRA used a better productivity factor than did General in the preparation of its estimates. We will adopt as reasonable for this account the amount of $1,449,000, the average of the two estimates.

G. Traffic Expenses

Traffic expenses consist primarily of the salaries, wages, and administrative costs incurred in the handling of telephone calls by switchboard operators and the costs associated with administering the use and performance of the switching network. Testimony on traffic expenses was presented on behalf of DRA by Utilities Engineer M. J. Vannucchi and rebuttal testimony was presented by the project planning manager of General's operator service staff, Thena Pettey. The tabulation below compares DRA's estimates with General's estimates, together with our adopted results. The basis for the adopted results are set forth in the ensuing paragraphs.

Traffic Expenses
(Thousands of Dollars)

Acc. No.	Item	DRA	General	Amount	Percent	Adopted
621	Genrl. Traffic Supvr.	$ 6,927	$ 7,984	$ 1,057	15.3	$ 7,191
622	Customer Instruction	622	622	0	0.0	622
624	Operator Wages	40,834	50,271	9,437	23.1	44,518
627	Oper. Employ. & Train	1,167	1,604	437	37.4	1,269
	Misc. CO Expense	13,082	14,082	1,000	7.6	13,082
	Subtotal	62,632	74,563	11,931	18.8	66,682
	GTED Adjustment	(1,999)	0	1,999	100.0	(1,999)
	Total	60,633	74,563	13,830	23.0	64,683

(Red Figure)

Testimony presented on behalf of DRA indicated that:

1. It was standard procedure for DRA to calculate General's 1988 test year estimated expense for management and nonmanagement labor. The procedure involved using 1985 as an employee salary base year and then calculating the 1988 labor using DRA's wage escalation factors.

2. DRA adjusted those areas impacted by the reductions in operator force levels by summing up all expenses in service related to the office force levels and applying the

2. General's AWT has always been and remains higher than that provided by Pacific as indicated by a statewide AWT for Pacific of 19.3 seconds as compared to General's 20.4 seconds.

3. General did grossly understate its AWT in (I&S) C.86-06-004 and did not correct its inflated AWT showing in this rate proceeding until after the staff report was prepared.

4. General admits that interLATA DA service takes longer to provide than local 411 DA service.

It should be noted from the tabulation of traffic expenses that Account 624-Operator Wages accounts for approximately two-thirds of the total traffic expenses. Furthermore, it is apparent from the record that the magnitude of operator wages impacts to a large degree the other traffic expense accounts. Under these circumstances, DRA's methodology of computing traffic expenses by applying a percentage ratio based on the number of operators to General's total estimated amounts with other adjustments does not appear unreasonable. Consequently we will adopt DRA's methodology in deriving our adopted figure for traffic expenses.

We are not persuaded that DRA's AWT of 19.8 seconds for the ACDs is more reasonable than General's estimated revised AWT of 20.4 seconds. The 20.4 figure appears reasonable given the comparisons between General's and Pacific's operations which demonstrate that General's operators receive and provide listings for more than one area code. In addition the 20.4 AWT was developed using actual AWTS adjusted to reflect anticipated savings. The 20.4 figure will be adopted as reasonable for the test year.

While we are not persuaded that DRA's 34 second AWT figure is reasonable for General's three TSPSs, the times estimated by General of 42.5 seconds for Long Beach, 41.5 seconds for Santa Monica, and 39.5 seconds for Ontario impress us as being somewhat high. Consequently, to reflect the inefficiencies of manual handling we will adopt as reasonable for this proceeding AWTs of 1.5 seconds less or 41 seconds for Long Beach, 40 seconds for Santa Monica, and 38.0 seconds for Ontario. Substituting the above-adopted AWTs in DRA's computations derive a number of operators of 1,662 which we will use for our computations of the traffic expenses.

Using 1,662 operators and the DRA methodology for computing expenses result in an expense allowance for Account 621-Traffic Expenses of $7,191,000, Account 622-Customer Instruction of $622,000, Account 624-Operator Wages of $44,518,000, Account 627-Operator Employee And Training of $1,269,000, and the composite of Account 626, 629-35-Miscellaneous an amount of $13,082,000.

The above figures reflect our adopted labor escalation figures.

The total of the above figures is $66,682,000. We will decrease this by $1,999,000 to $64,683,000 to reflect our previously discussed GTED adjustment.

H. Commercial Expenses

Commercial expenses are comprised of salaries, wages, and administrative costs for handling customer service order contracts and the collection of billings, the preparation and distribution of telephone directories, marketing and sales functions including advertising, developing, and filing tariff schedules and other regulatory matters, and intercompany relations and settlements. DRA's presentation was made by Public Utility Regulatory Program Specialist II Marshall B. Enderby and rebuttal testimony was presented on behalf of General by its Ventura County Division Manager Jack F. Moore, by the Manager of Strategy Development of GTE Service Corporation Gabriel Sidhom, by General's Director of Access Services Lou Culkin, and its Manager of Advertising and

General Operating Expenses

Acc. No.	Item	DRA	General	General Exceeds DRA Amount	General Exceeds DRA Percent	Adopted
				(Thousands of Dollars)		
	General Office Salaries and Expenses					
661	Executive Dept.	$ 1,277	$ 1,394	$ 117	9.2%	$ 1,311
662	Accounting Dept.	103,066	109,952	6,886	6.7	109,952
663	Treasury Dept.	2,945	3,261	316	10.7	2,967
664	Law Dept.	2,411	2,627	216	9.0	2,476
665	Other Gen. Office	69,686	77,283	7,597	10.9	72,076
	Total	179,385	197,636	18,251	10.2	188,782
	Other Operating Expenses					
668	Insurance	$ 3,204	$ 3,628	$ 424	13.2%	$ 3,204
669	Accidents & Damages	1,100	1,240	140	12.7	1,100
671	Oper. Rents	14,447	15,228	781	5.4	14,447
672	Relief & Pensions	117,318	164,020	46,702	39.8	148,199
674	General Services and Licenses	33,000	55,768	22,768	69.0	44,700
675	Misc. Other	5,141	7,447	2,306	44.9	5,141
677	Exp. Chg'd. Const.	(9,562)	(20,312)	(10,250)	112.4	(17,358)
	Inside Wire	0	8,697	8,692	0.0	0
	Subtotal	164,648	235,711	71,063	43.2	199,433
	GTED Adj.	(5,235)	0	5,235	(100.0)	(3,800)
	Compensation Adj.	(26,200)	0	26,200	(100.0)	0
	Total	133,213	235,711	102,498	76.9	195,633

(Red Figure)

FCC Account 661-Executive Department includes the salaries and expenses of officers engaged in general management and administration including their assistants and office forces. DRA's estimate for this account is $1,277,000 as compared to General's estimate of $1,394,000, a difference of $117,000 or 9.2%. The reasons for the differences are DRA's lower labor inflation and

General Operating Expenses

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	Total	179,385	197,636	18,251	10.2	188,782
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669	Accidents & Damages	1,100	1,240	140	12.7	1,100
671	Oper. Rents	14,447	15,228	781	5.4	14,447 ✓
672	Relief & Pensions	117,318	164,020	46,702	39.8	143,941 ✓
674	General Services and Licenses	33,000	55,768	22,768	69.0	43,400 ✓
675	Misc. Other	5,141	7,447	2,306	44.9	5,141
677	Exp. Chg'd. Const.	(9,562)	(20,312)	(10,250)	112.4	(17,358)
	Inside Wire	0	8,697	8,692	0.0	0
	Subtotal	164,648	235,711	71,063	43.2	193,875 ✓
	GTED Adj.	(5,235)	0	5,235	(100.0)	(3,800)
	Compensation Adj.	(26,200)	0	26,200	(100.0)	0
	Total	133,213	235,711	102,498	76.9	190,075 ✓

(Red Figure)

FCC Account 661-Executive Department includes the salaries and expenses of officers engaged in general management and administration including their assistants and office forces. DRA's estimate for this account is $1,277,000 as compared to General's estimate of $1,394,000, a difference of $117,000 or 9.2%. The reasons for the differences are DRA's lower labor inflation and

General Operating Expenses

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			(Thousands of Dollars)			
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662	Accounting Dept.	103,066	109,952	6,886	6.7	109,952
663	Treasury Dept.	2,945	3,261	316	10.7	2,967
664	Law Dept.	2,411	2,627	216	9.0	2,476
665	Other Gen. Office	69,686	77,283	7,597	10.9	72,141
	Total	179,385	197,636	18,251	10.2	188,847
	Other Operating Expenses					
668	Insurance	$ 3,204	$ 3,628	$ 424	13.2%	$ 3,204
669	Accidents & Damages	1,100	1,240	140	12.7	1,100
671	Oper. Rents	14,447	15,228	781	5.4	14,447
672	Relief & Pensions	117,318	164,020	46,702	39.8	145,322
674	General Services and Licenses	33,000	55,768	22,768	69.0	43,400
675	Misc. Other	5,141	7,447	2,306	44.9	5,141
677	Exp. Chg'd. Const.	(9,562)	(20,312)	(10,250)	112.4	(17,358)
	Inside Wire	0	8,697	8,692	0.0	0
	Subtotal	164,648	235,711	71,063	43.2	195,256
	GTED Adj.	(5,235)	0	5,235	(100.0)	(3,800)
	Compensation Adj.	(26,200)	0	26,200	(100.0)	0
	Total	133,213	235,711	102,498	76.9	191,456

(Red Figure)

FCC Account 661-Executive Department includes the salaries and expenses of officers engaged in general management and administration including their assistants and office forces. DRA's estimate for this account is $1,277,000 as compared to General's estimate of $1,394,000, a difference of $117,000 or 9.2%. The reasons for the differences are DRA's lower labor inflation and

nonlabor escalation factors, the use by General of four months' actual expenses of 1986 to estimate cost billed to others for 1988 as contrasted to DRA's use of annualized eleven months' recorded cost billed to others for 1986 to derive a 1988 figure. We will adopt DRA's estimate of $1,277,000 based on later data increased by $34,000 to reflect our previously discussed adopted labor escalation figures. The Account 661 expense thus computed is $1,311,000.

FCC Account 662-Accounting Department includes the salaries and expenses of the vice president-controller, his assistants, and office force. Accounting operations include accounting, budget, information systems, and internal auditing. DRA's estimate for this account is $103,066,000 as contrasted to General's estimate of $109,952,000, a difference of $6,886,000 or 6.7%. According to the testimony of DRA's witness Vannucchi, there has been a dramatic increase in the employee levels for FCC Account 662 in spite of the trend toward a reduction in overall company employees. According to the testimony, Account 662 has grown from 338 total employees in 1978 to 605 employees in 1986. The 1988 test year estimate is 647 employees. A data request response by General indicated that the increase in employees was due to the following reasons:

1. Increases in 1982 and in 1983 were the result of reorganization between GTC and General Telephone Data Services.

2. Total company growth increased reporting requirements.

3. An increase in the construction program increased invoices, work orders, and data processing.

4. Increased reporting and record keeping necessitated by deregulation and increased regulatory involvement in the process.

5. Increased demand by both internal management as well as the external

$2,967,000, and $619,000, respectively, for 1985 and $457,000, $3,416,000, and $6,780,000, respectively, for 1986. For the test year 1988, this witness held the above disallowed expenses related to corporate image and political advocacy in conjunction with the amounts as a ratemaking adjustment for the test year 1988 in the amount of $4,094,000. As previously discussed, we have adopted a disallowance of $2,537,000 for corporate image of the company and $678,000 for political advocacy for test year 1986 and will continue these amounts as a disallowance for Account 665 for the test year 1988. We will therefore adopt DRA's estimate of $69,686,000 increased by the difference between DRA's proposed disallowance and our adopted allowance of $867,000 and increased further by $1,523,000 to reflect our previously discussed adopted labor escalation amounts for a total of $72,076,000.

Under general office salaries and expenses, General shows an item of expense for Uniform System of Accounts (USOA) rewrite of $42,662,000 and inside wire costs of $3,119,000. We are considering the USOA rewrite matter generically under I.87-02-023 and therefore will not adopt General's adjustment for this amount. In addition, the inside wire costs are included in DRA's estimates and therefore we will not adopt General's proposed amount.

DRA's estimate of FCC Account 668-Insurance is $3,204,000 as compared to General's estimate of $3,628,000, a difference of $424,000 or 13.2%. DRA's estimate of FCC Account 669-Accident and Damages is $1,100,000 as compared to General's estimate of $1,240,000, a difference of $140,000 or 12.7%. According to the testimony of DRA witness Shiu, the reasons for the difference are DRA's use of lower labor and nonlabor inflation factors and the use of annualized 11 months' recorded costs billed to other data of 1986 for test year 1988 rather than General's use of four months' actual expense of 1986 to estimate the cost billed to this account for 1988. We will adopt DRA's estimates for these two accounts as

$2,967,000, and $619,000, respectively, for 1985 and $457,000, $3,416,000, and $678,000, respectively, for 1986. For the test year 1988, this witness held the above disallowed expenses related to corporate image and political advocacy in conjunction with the amounts as a ratemaking adjustment for the test year 1988 in the amount of $4,094,000. As previously discussed, we have adopted a disallowance of $2,488,000 for corporate image of the company and $678,000 for political advocacy for test year 1986 and will continue these amounts as a disallowance for Account 665 for the test year 1988. We will therefore adopt DRA's estimate of $69,686,000 increased by the difference between DRA's proposed disallowance and our adopted allowance of $930,000 and increased further by $1,525,000 to reflect our previously discussed adopted labor escalation amounts for a total of $72,141,000.

Under general office salaries and expenses, General shows an item of expense for Uniform System of Accounts (USOA) rewrite of $42,662,000 and inside wire costs of $3,119,000. We are considering the USOA rewrite matter generically under I.87-02-023 and therefore will not adopt General's adjustment for this amount. In addition, the inside wire costs are included in DRA's estimates and therefore we will not adopt General's proposed amount.

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Item	DRA	General	General Exceeds DRA Amount	General Exceeds DRA Percent	Adopted
			(Thousands of Dollars)		
Pensions	$ 43,873.0	$ 59,477.0	$15,604.0	35.6	$ 53,366
Group Life Insurance	2,219.5	2,929.0	709.5	32.0	2,651
Dental Insurance	4,350.8	5,629.0	1,278.2	29.4	5,157
Medical Insurance	58,552.8	89,264.0	30,711.2	52.5	78,600
Sickness Disability	13,957.2	19,454.0	5,496.8	39.4	17,294
Military Leave	8.6	16.0	7.4	86.0	12
Workers' Comp.	15,499.0	17,083.0	1,584.0	10.2	15,499
Employee Savings Plan	8,485.0	11,163.0	2,678.0	31.6	10,111
Other Benefits	6,057.0	10,529.0	4,472.0	73.8	10,529
Subtotal	153,002.9	215,544.0	62,541.1	40.9	193,219
Charged to Construction @ .233	(35,685.2)	(50,272.0)	(14,581.8)	NA	(45,020)
Total Expensed	117,317.7	165,272.0	47,954.3	40.9	148,199
Adjustment due to elimination of 202 operator service employee		1,252.0			
Net Expensed	117,317.7	164,020.0	46,702.3	39.8	148,199

(Red Figure)

Testimony on Account 672 was presented on behalf of DRA by Public Utility Regulatory Analyst II Mark R. Loy. Rebuttal testimony on the pension fund and administration expenses was presented on behalf of General by the director of operations for GTE Investment Management Corporation, Roger S. Williams, and on the subject of funding requirements for General's medical benefit plan provided through The Travelers by the vice president in the employee benefit plans department of Johnson and Higgins, William N. Sammis.

As noted from the above tabulations, General's estimate for pension expense was $59,477,000 as compared to DRA's estimate of $43,873,000, a difference of $15,604,000 or 35.6%. Both General and DRA presented testimony showing the effect of the use of

Item	DRA	General	General Exceeds DRA Amount	General Exceeds DRA Percent	Adopted
			(Thousands of Dollars)		
Pensions	$ 43,873.0	$ 59,477.0	$15,604.0	35.6	$ 53,345
Group Life Insurance	2,219.5	2,929.0	709.5	32.0	2,651
Dental Insurance	4,350.8	5,629.0	1,278.2	29.4	5,126
Medical Insurance	58,552.8	89,264.0	30,711.2	52.5	73,100
Sickness Disability	13,957.2	19,454.0	5,496.8	39.4	17,294
Military Leave	8.6	16.0	7.4	86.0	13
Workers' Comp.	15,499.0	17,083.0	1,584.0	10.2	15,499
Employee Savings Plan	8,485.0	11,163.0	2,678.0	31.6	10,111
Other Benefits	6,057.0	10,529.0	4,472.0	73.8	10,529
Subtotal	153,002.9	215,544.0	62,541.1	40.9	187,668
Charged to Construction @ .233	(35,685.2)	(50,272.0)	(14,581.8)	NA	(43,727)
Total Expensed	117,317.7	165,272.0	47,954.3	40.9	143,941
Adjustment due to elimination of 202 operator service employee		1,252.0			
Net Expensed	117,317.7	164,020.0	46,702.3	39.8	143,941

(Red Figure)

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As noted from the above tabulations, General's estimate for pension expense was $59,477,000 as compared to DRA's estimate of $43,873,000, a difference of $15,604,000 or 35.6%. Both General and DRA presented testimony showing the effect of the use of

reasonable costs for these component items. Although not computed in that manner, our adopted expenses seem to reflect a force reduction of approximately 10%. Furthermore, our adopted labor escalation factors approximate 87% of the differential between the labor escalation factors used by DRA and General. Under these circumstances, we will adopt as reasonable for ratemaking purposes for those component items listed above the DRA estimate plus .607 (the compound affect of our adopted force reduction and labor escalation factors) times the difference between DRA and General estimates. Such computations result in the following adopted expenses:

Pensions	$53,366,000
Group Life Insurance	2,651,000
Dental Insurance	5,157,000
Sickness Disability	17,294,000
Employee Savings Plan	10,111,000

DRA's estimate for medical insurance is $58,552,800 as compared to General's estimate of $89,264,000, a difference of $30,711,200 or 52.5%. DRA used lower work force estimates and lower rates than General did for developing expense estimates. DRA's lower employee counts amount to a 23% reduction in the participation. The remaining differences are attributable to the development of the rate structures charged by the Travelers Company (72% of the total expenses) and the seven health maintenance organizations (28% of the total expenses). According to the testimony of DRA witness Loy, the latest rate information from the insurers' actuary indicates a dramatic increase in funding deficits beginning in 1984 and continuing through 1987, and possibly to 1988. This witness further testified that the causes of the funding shortfall are a dramatic increase in claims level as of 1985 and an unprecedented $9 million divided in 1984. As a result, according to the record, DRA found that the 29% and 22% increases

> million for 1986 indicated that the DRA estimate of $41.3 million for 1988 is unrealistic.

We are persuaded that DRA's estimate of $41,254,730 for The Travelers medical insurance is low and General's estimate of $65,271,720 is high. In consideration to our adoption of estimates reflecting work force reduction, we will not escalate the medical insurance costs and will adopt as reasonable for this proceeding the 1986 recorded medical insurance cost of $56.8 million.

Health maintenance organizations make up 28% of the total company medical insurance costs. General is assuming an annual increase of 5% for 1987 and 10% in 1988 for health and 4.5% for all other providers. DRA used the 1987 actual rates (a 4.4% decrease from 1986 levels) and assumed no change for the 1988 rates. DRA's position appears reasonable and we will adopt its recommended $16.3 million for HMO costs. Adding this $16.3 million HMO cost to the $56.8 million adopted, The Travelers' cost yields a medical insurance cost of $78.6 million for test year 1988 which we will adopt as reasonable.

Both DRA and General developed their 1988 recommended expense allowances for military leave as a percentage of payroll. General used the 1985 actual percentage, but DRA used a four-year average. We will adopt DRA's estimate of $8,600 increased by $4,200 to reflect the previously discussed smaller force reduction to yield a total of $12,800 for this component item.

"Other Benefits" includes administrative costs for pension and medical plans, the nonregulated operations employees savings plan, termination costs, and the supplemental executive retirement plan. DRA's estimate for this item is $6,057,000 which is $4,472,000 or 73.8% less than General's estimate of $10,529,000. According to the record, $5,834,000 of the $6,057,000 estimate for other benefits is for administration of the pension fund, leaving $223,000 total for the cost of the nonregulated operations

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Both DRA and General developed their 1988 recommended expense allowances for military leave as a percentage of payroll. General used the 1985 actual percentage, but DRA used a four-year average. We will adopt DRA's estimate of $8,600 increased by $4,200 to reflect the previously discussed smaller force reduction to yield a total of $12,800 for this component item.

"Other Benefits" includes administrative costs for pension and medical plans, the nonregulated operations employees savings plan, termination costs, and the supplemental executive retirement plan. DRA's estimate for this item is $6,057,000 which is $4,472,000 or 73.8% less than General's estimate of $10,529,000. According to the record, $5,834,000 of the $6,057,000 estimate for other benefits is for administration of the pension fund, leaving $223,000 total for the cost of the nonregulated operations employees savings plans, termination costs, and the supplemental executive retirement plan. We will adopt this $223,000 estimate for other than administration and pension fund and address the pension fund directly. DRA witness Loy testified that the $5,834,000 expense for the administration of the pension fund was derived by multiplying the 1985 recorded figure by the force reduction percentage and labor escalation factor. Such a procedure obviously ties the pension administration cost directly to the size of the 1988 test year labor force.

Rebuttal testimony presented on behalf of General by Roger S. Williams indicated that:

1. The primary functions associated with the administration of the pension fund are safeguarding, investing, and record-keeping of plan assets.

2. The assets are held and protected by an appointed trustee.

3. GTE within the ERISA guidelines invests the assets to maximize returns within an acceptable level of risk.

4. The expense and fees of the pension fund administration are based upon the value of the pension fund itself.

5. Approximately 85% of the annual fees are pension management fees with an additional 10% attributable to trustee funds, including the transaction charges.

6. It is the growth of the pension fund which determines the growth in administration cost, not the change in wages paid to General's hourly employees.

7. A reduction in General's work force by 23% would not act to reduce plan assets nor would such a reduction have an impact on the cost of plan administration over an extended time frame.

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5. Approximately 85% of the annual fees are pension management fees with an additional 10% attributable to trustee funds, including the transaction charges.

6. It is the growth of the pension fund which determines the growth in administration cost, not the change in wages paid to General's hourly employees.

7. A reduction in General's work force by 23% would not act to reduce plan assets nor would such a reduction have an impact on the cost of plan administration over an extended time frame.

It appears from the record that the major portion of pension fund administrative costs are based on the level of the pension fund rather than the size of the workforce. Under these circumstances, DRA's method of estimating this expense by the application of a force reduction percentage factor appears inappropriate. Consequently, we will adopt General's figure of $10,529,000 for other items for the purposes of this proceeding.

DRA's estimate for workers' compensation is $15,499,000 or $1,584,000 or 10.2% less than General's estimate of $17,083,000. The rates of change in workers' compensation expenses for the period 1982 to 1985 decreased from 34.7% to 10.0%. DRA incorporated this decrease into its forecast by assuming that rates would increase but would do so more slowly, equal to the 1985 and 1986 experience. General, on the other hand, assumed the rates would increase at approximately the 1985 level plus payroll escalation. We are persuaded that DRA's estimate is reasonable and will adopt $15,499,000 for this component item for test year 1988.

The total of the above-discussed component items is $193,219,000. Reducing this by the 23.3% charged to construction or $45,020,000 leaves a total expense for Account 672 of $148,199,000 which we will adopt as reasonable for this proceeding.

FCC Account 674-General Services and License includes payments to GTE Service Corporation for services received under a general service contract which provides for the furnishing of advisory services on general accounting, financial, insurance and taxes, pensions and benefits, organization and personnel, legal, commercial, marketing and sales, engineering, plant, traffic, public affairs, and advertising matters. DRA's estimate for this account is $33 million or $22.8 million (69.0%) less than General's estimate of $55.8 million. As discussed under the affiliate interest portion of this decision, we have adopted a figure for this account of $44.7 million.

It appears from the record that the major portion of pension fund administrative costs are based on the level of the pension fund rather than the size of the workforce. Under these circumstances, DRA's method of estimating this expense by the application of a force reduction percentage factor appears inappropriate. Consequently, we will adopt General's figure of $10,529,000 for other items for the purposes of this proceeding.

DRA's estimate for workers' compensation is $15,499,000 or $1,584,000 or 10.2% less than General's estimate of $17,083,000. The rates of change in workers' compensation expenses for the period 1982 to 1985 decreased from 34.7% to 10.0%. DRA incorporated this decrease into its forecast by assuming that rates would increase but would do so more slowly, equal to the 1985 and 1986 experience. General, on the other hand, assumed the rates would increase at approximately the 1985 level plus payroll escalation. We are persuaded that DRA's estimate is reasonable and will adopt $15,499,000 for this component item for test year 1988.

The total of the above-discussed component items is $187,668,000. Reducing this by the 23.3% charged to construction or $43,727,000 leaves a total expense for Account 672 of $143,941,000 which we will adopt as reasonable for this proceeding.

FCC Account 674-General Services and License includes payments to GTE Service Corporation for services received under a general service contract which provides for the furnishing of advisory services on general accounting, financial, insurance and taxes, pensions and benefits, organization and personnel, legal, commercial, marketing and sales, engineering, plant, traffic, public affairs, and advertising matters. DRA's estimate for this account is $33 million or $22.8 million (69.0%) less than General's estimate of $55.8 million. As discussed under the affiliate interest portion of this decision, we have adopted a figure for this account of $43.4 million.

J. Taxes

Testimony was presented on taxes by DRA's Financial Examiner III Donna L. White. Rebuttal testimony on the method of computing California corporation franchise tax was presented on behalf of General by its Tax Manager, Jon F. Kieffer.

Taxes are subdivided into two major categories, income taxes and taxes other than income taxes. The Tax Reform Act of 1986 (TRA86) provides a new depreciation system, the Modified Accelerated Cost Recovery System (MACRS). MACRS and some of the more obvious provisions of TRA86, such as the change in corporate tax rate, the repeal of investment tax credit, and the repeal of deductibility of certain capitalized interest and overheads during construction, have been estimated and incorporated into the federal income tax calculations provided by DRA for this general rate case on an interim basis pending a Commission decision in OII 86-11-019 which would establish ratemaking tax expense policy for the impact of TRA86. In D.88-01-061 dated January 28, 1988 on OII 86-11-019, our investigation on the impact of TRA86, we are requiring respondents, including General, to file calculations with supporting work papers proposing a 1987 revenue requirement adjustment for TRA86 and SB572 effects in conformance with the methodology adopted in the decision. DRA recommends that the adoption of federal income tax (FIT) or California corporation franchise tax (CCFT) to be collected in 1988 rates be based upon DRA's recommendations made in this proceeding. According to DRA, the impact of TRA86 decision on General's 1988 test year will be resolved when General complies with TRA86 decision requirements. We agree. General included in its application a tax deduction for construction period interest. Treatment of the construction period interest will be resolved by General's compliance with D.88-01-061 and therefore General's tax deduction for this item will be excluded.

In D.88-01-061, we transferred review of the Privilege Year Adjustment to Pacific Gas and Electric Company A.85-12-050, Phase II, which is addressing the working cash impact of when CCFT is deductible for FIT purposes. DRA recommends that the issue of Privilege Year Adjustment be deferred until the Commission has issued its decision in A.85-12-050. We concur. DRA's FIT interest deduction was derived by applying the weighted average embedded cost of debt as supplied by DRA's rate of return witness to DRA's estimated rate base. The unamortized deferred investment tax credit (ITC) was not deducted from rate base for this calculation. This method of "interest synchronization" is permitted by Treasury Regulation Section 1.46-6. It is General's position that the propriety of using interest synchronization for ratemaking purposes is currently the subject of an investigation instituted by this Commission, I.86-10-002, to which General is a party. Consequently, General recommends that we defer any action on the use of interest synchronization pending a decision in I.86-10-002. That investigation was closed by D.88-04-008 dated April 27, 1988. Consistent with our action in D.87-12-067 in Pacific's latest rate case, we will adopt DRA's calculations of the FIT interest deduction, thereby effectively implementing the interest synchronization adjustment for General.

DRA used an effective CCFT rate of 7.71% to compute General's CCFT liability at current rates whereas General used the statutory rate of 9.6%. According to DRA, the 7.71% effective rate reflects General's allocated share of GTE Corporation's total California CCFT liability based on review of the most recent historical data available covering the years 1982 to 1985. In General's 1980, 1982, and 1984 general rate cases, we adopted the effective CCFT rate in calculating General's CCFT liability but used the statutory 9.6% rate as a floor. Consistent with our past practices, we will adopt the higher of the statutory rate or the

effective tax rate, which, in this case, is the statutory tax rate of 9.3% in computing the CCFT.

Since General's unitary CCFT tax rate is established on a three-factor formula which determines the relationship of wages, revenues, and average net tangible property of all General's system telephone operations in California to wages, revenues, and average net tangible property of the total General system, an increase or decrease in revenues would impact only one of the three factors used to develop the incremental rate which, in turn, increases or decreases the average apportionment factor. Since only one of the three factors changes in computing the CCFT for reflecting an increase or decrease in rates, we have in the past used incremental tax rates for any changes in rates granted by us. Consistent with our past practices we used incremental tax rate developed for this proceeding of 1.8635% to calculate the net-to-gross multiplier.

The tabulation below sets forth taxes other than income as computed by DRA and General, together with our adopted results. The bases for the adopted results are set forth in the ensuing paragraphs.

Acc. No.	Item	DRA	General	General Exceeds DRA Amount	General Exceeds DRA Percent	Adopted
				(Thousands of Dollars)		
	Operating Taxes:					
307.1	Ad Valorem	$60,085	$ 64,997	$ 4,912	8.2%	$ 64,334
307.4	Other Taxes	941	941	0	0.0	941
	Subtotal	61,026	65,938	4,912	8.0	65,275
	Social Security Taxes:					
307.5	SUI	930	2,344	1,414	152.0	1,084
307.6	FUI	558	938	380	68.1	868
307.7	FICA	32,002	44,286	12,284	38.4	38,290
	Subtotal	33,490	47,568	14,078	42.0	40,242
Total		94,516	113,506	18,990	20.1%	105,517

effective tax rate, which, in this case, is the statutory tax rate of 9.3% in computing the CCFT.

Since General's unitary CCFT tax rate is established on a three-factor formula which determines the relationship of wages, revenues, and average net tangible property of all General's system telephone operations in California to wages, revenues, and average net tangible property of the total General system, an increase or decrease in revenues would impact only one of the three factors used to develop the incremental rate which, in turn, increases or decreases the average apportionment factor. Since only one of the three factors changes in computing the CCFT for reflecting an increase or decrease in rates, we have in the past used incremental tax rates for any changes in rates granted by us. Consistent with our past practices we used incremental tax rate developed for this proceeding of 1.8635% to calculate the net-to-gross multiplier. Appendix C of this decision reflects the development of our adopted CCFT and FIT.

The tabulation below sets forth taxes other than income as computed by DRA and General, together with our adopted results. The bases for the adopted results are set forth in the ensuing paragraphs.

Acc. No.	Item	DRA	General	General Exceeds DRA Amount	General Exceeds DRA Percent	Adopted
			(Thousands of Dollars)			
	Operating Taxes:					
307.1	Ad Valorem	$60,085	$ 64,997	$ 4,912	8.2%	$ 64,373
307.4	Other Taxes	941	941	0	0.0	941
	Subtotal	61,026	65,938	4,912	8.0	65,314
	Social Security Taxes:					
307.5	SUI	930	2,344	1,414	152.0	1,084
307.6	FUI	558	938	380	68.1	868
307.7	FICA	32,002	44,286	12,284	38.4	38,290
	Subtotal	33,490	47,568	14,078	42.0	40,242
Total		94,516	113,506	18,990	20.1%	105,556

The State Unemployment Insurance (SUI) tax rate used by General was 2% and by DRA was 1%. The 1% rate was most recently provided by the State of California and will be used for this proceeding.

The U.S. Department of Health and Human Services (HHS) released a base for Federal Insurance Contribution Act (FICA) tax of $45,000 for 1988. This base amount will be used for the computation of the FICA tax for this proceeding.

The most recently adopted Federal Unemployment Insurance (FUI) tax rate is 0.8%. This rate will be used for the computations in this proceeding. General's and DRA's estimates of ad valorem taxes reflect respective plant balance estimates. Consistent with our adopted plant balances we will adopt $64,334,000 as reasonable for ad valorem taxes.

K. Depreciation

DRA's testimony on depreciation expenses and depreciation reserve was presented by Senior Utilities Engineer Ramesh Joshi. General's testimony on depreciation rates was presented by its Manager of Capital Recovery and Valuation Carl R. Lanterman. General's Capital Recovery Research Manager Terence D. Robinson testified on the economic value depreciation model used in part to support the remaining lives presented by Lanterman for digital central office equipment and fiber-optic outside plant facilities.

DRA witness Joshi recommends that the Commission:

1. Authorize depreciation rates used by the staff in developing accruals for test year 1988.

2. Approve reciprocal weighting method proposed by General.

3. Defer formally recognizing life analysis techniques such as economic value depreciation (EVD) and substitution analysis to a later date.

intended recommendation but, in any event, we will consider depreciation in this proceeding.

Excluding the estimated impact of issues such as USOA and SNI/RID which will be decided in other generic proceedings and including the impact of inside wire on a business-as-usual basis, DRA's depreciation expense estimate is $497,161,000 which is $42,175,000 or 8.1% less than General's estimate of $537,436,000. DRA's estimate of depreciation reserve is $2,012,217,000 which is $38,808,000 or 1.9% less than General's estimate of $2,051,025,000. Applying the agreed depreciation rates to our subsequently discussed capital plant balances in Account 100.1 yields a depreciation expense of $519,494,000 and a depreciation reserve of $2,013,126,000 which we will adopt as reasonable for this proceeding.

L. Telephone Plant

DRA's testimony on capital additions and telephone plant in service was presented by Program and Project Supervisor Martin J. O'Donnell and Assistant Utilities Engineer Riaz Danish. Danish did the analysis and estimates of 1987 and 1988 capital additions while O'Donnell did the calculations for plant balances and telephone plant in service (TPIS). Discussion in Chapter 13 of Exhibit 85 on TPIS was limited to Account 100.1 and interest during construction (IDC) on Account 100.2 (telephone plant under construction), since DRA takes no exception to General's estimates on Account 100.3 (property held for future use). Rebuttal to Danish's testimony was presented by seven witnesses: (1) General's Network Operations Planning Manager David R. Bowman; (2) General's Network Engineering Manager Anthony G. Donato; (3) an Account Executive of GTE Communications Systems Corporation Edward J. Gronkiewicz; (4) General's Budget Manager of Operations Frederick K. Hesse; (5) General's Product Manager of Business Operations Products and Services William R. Hickam; (6) Director of Telecommunications Regulatory Advisory Services of Coopers and

intended recommendation but, in any event, we will consider depreciation in this proceeding.

Excluding the estimated impact of issues such as USOA and SNI/RID which will be decided in other generic proceedings and including the impact of inside wire on a business-as-usual basis, DRA's depreciation expense estimate is $497,161,000 which is $42,175,000 or 8.1% less than General's estimate of $537,436,000. DRA's estimate of depreciation reserve is $2,012,217,000 which is $38,808,000 or 1.9% less than General's estimate of $2,051,025,000. Applying the agreed depreciation rates to our subsequently discussed capital plant balances in Account 100.1 yields a depreciation expense of $521,177,000 and a depreciation reserve of $2,013,282,000 (excluding Communications System Corporation adjustments) which we will adopt as reasonable for this proceeding.

L. <u>Telephone Plant</u>

DRA's testimony on capital additions and telephone plant in service was presented by Program and Project Supervisor Martin J. O'Donnell and Assistant Utilities Engineer Riaz Danish. Danish did the analysis and estimates of 1987 and 1988 capital additions while O'Donnell did the calculations for plant balances and telephone plant in service (TPIS). Discussion in Chapter 13 of Exhibit 85 on TPIS was limited to Account 100.1 and interest during construction (IDC) on Account 100.2 (telephone plant under construction), since DRA takes no exception to General's estimates on Account 100.3 (property held for future use). Rebuttal to Danish's testimony was presented by seven witnesses: (1) General's Network Operations Planning Manager David R. Bowman; (2) General's Network Engineering Manager Anthony G. Donato; (3) an Account Executive of GTE Communications Systems Corporation Edward J. Gronkiewicz; (4) General's Budget Manager of Operations Frederick K. Hesse; (5) General's Product Manager of Business Operations Products and Services William R. Hickam; (6) Director of Telecommunications Regulatory Advisory Services of Coopers and

Lybrand Carl O. Thorsen; and (7) General's Network Operations Planning Manager Kevin A. Young.

The tabulation below sets forth DRA's estimate of gross additions for the test year 1988, together with General's estimate and our adopted results. The basis for the adopted results is set forth in the ensuing paragraphs.

Acc. No.	Item	DRA	General	General Exceeds DRA Amount	General Exceeds DRA Percent	Adopted
		(Dollars in Thousands)				
C11	Land	$ 2,527	$ 2,527	$ 0	0.0	$ 2,527
C12	Buildings	29,491	29,491	0	0.0	29,491
C201	Electronic Toll	619	619	0	0.0	619
C203	Electro-mechanical	2,048	6,729	4,681	228.6	5,200
C205	Carrier Equip.	46,273	84,385	38,112	82.4	84,385
C206	Radio	10,576	10,576	0	0.0	10,576
C207	Analog	8,445	19,927	11,482	136.0	13,985
C209	Digital	91,748	186,014	94,266	102.7	119,150
C4XX-	Station Apparatus	16,727	16,727	0	0.0	16,727
C60	Outside Plant	139,846	322,908	183,062	130.9	305,190
CBXX	General Plant	32,032	41,507	9,475	29.6	38,740
Total		380,332	721,410	341,078	89.7	626,590

General's gross addition capital budget for 1988 for Account C203-Electromechanical was $7,042,000, consisting of $996,000 lines and terminals, $1,290,000 trunking, $1,838,000 pair gain CO terminals, and $2,918,000 unidentified. According to the testimony of DRA witness Danish, the combined cost of lines and terminals of $996,000 and trunking of $1,290,000 is $2.286 million, which for the 1,610 lines and trunks to be installed in test year 1988 computes to be a cost of $1,400 per line. According to this witness, $1,400 per line is excessive. DRA's estimate for the SxS additions (Account C203) was derived by multiplying the proposed 1,610-line additions by a cost of $160 per L/T to arrive at an amount of $252,000 for SxS growth. To this, witness Danish added

Lybrand Carl O. Thorsen; and (7) General's Network Operations Planning Manager Kevin A. Young.

The tabulation below sets forth DRA's estimate of gross additions for the test year 1988, together with General's estimate and our adopted results. The basis for the adopted results is set forth in the ensuing paragraphs.

Acc. No.	Item	DRA	General	General Exceeds DRA Amount	General Exceeds DRA Percent	Adopted
		(Dollars in Thousands)				
C11	Land	$ 2,527	$ 2,527	$ 0	0.0	$ 2,527
C12	Buildings	29,491	29,491	0	0.0	29,491
C201	Electronic Toll	619	619	0	0.0	619
C203	Electro-mechanical	2,048	6,729	4,681	228.6	5,200
C205	Carrier Equip.	46,273	84,385	38,112	82.4	84,385
C206	Radio	10,576	10,576	0	0.0	10,576
C207	Analog	8,445	19,927	11,482	136.0	13,985
C209	Digital	91,748	186,014	94,266	102.7	127,498
C4XX-	Station Apparatus	16,727	16,727	0	0.0	16,727
C60	Outside Plant	139,846	322,908	183,062	130.9	305,190
CBXX	General Plant	32,032	41,507	9,475	29.6	38,740
Total		380,332	721,410	341,078	89.7	634,938

General's gross addition capital budget for 1988 for Account C203-Electromechanical was $7,042,000, consisting of $996,000 lines and terminals, $1,290,000 trunking, $1,838,000 pair gain CO terminals, and $2,918,000 unidentified. According to the testimony of DRA witness Danish, the combined cost of lines and terminals of $996,000 and trunking of $1,290,000 is $2.286 million, which for the 1,610 lines and trunks to be installed in test year 1988 computes to be a cost of $1,400 per line. According to this witness, $1,400 per line is excessive. DRA's estimate for the SxS additions (Account C203) was derived by multiplying the proposed 1,610-line additions by a cost of $160 per L/T to arrive at an amount of $252,000 for SxS growth. To this, witness Danish added

these projects involved". General subsequently provided as Exhibit 184 a document which identified all of the projects by work order number. We will add this amount to the above $15,410,000 to yield $20,178,000 for the gross additions capital budget. Translating this figure to gross additions to Account 100.1 for the test year 1988 yields a figure of $13,985,000, which we will adopt as reasonable for this proceeding.

DRA's estimate of gross additions to 100.1 for Account C209 digital COSE for test year 1988 is $91,748,000 as contrasted to General's estimate of $186,014,000. Tabulated below are the component items comprising General and DRA estimates, together with our adopted results. The bases for the adopted results are set forth in the ensuing paragraphs.

	General	DRA	Adopted
Digital - New	$ 82,404	$51,038	$ 70,945
Digital - Growth	39,923	9,065	12,567
Modifications Line and Truck Testing	1,888	1,833	1,833
Capital Planning Adj.	20,000	-	-
PPCF	2,530	-	-
Enhanced Switching	28,909	13,606	24,276
COE Tools	944	936	936
Emergency Generators	1,100	1,090	1,090
Special Projects			
USS/MSS	6,535	6,481	6,485
Unidentified	755	-	-
Analog/Misidentified	1,026	1,018	1,018
Subtotal	186,014	85,067	119,150
Times TPI	-	6,681	
Total	186,014	91,748	

General's estimate for new digital equipment of $82,404,000 is based on its budget estimates. DRA's witness testified that, in many instances, the budget amount of the COSE plant exceeded the bid amount in excess of 40%. On this basis, he believes General's figures are invalid. DRA's estimate is equal to the product of the number of L/Ts and the average weighted cost per

L/T for rounds 5-8 of $177.94. On rebuttal General contended that the use of such an average cost is inappropriate because of the difference between round 5 of $155.14 and round 8 cost of $218.87. This position appears valid and we will adopt as reasonable the unit cost of $218.87 for round 8 increased by the TPI of 1.045 for 1987 and 1.0785 for 1988 to yield $246.68 per L/T. Applying this to the estimated number of new L/Ts utilized by the staff in its estimate yields a new construction figure of $70,945,000, which we will adopt as reasonable. DRA's estimate of $9,065,000 for digital growth was based on the above-discussed $177.94 per L/T per additional line. We will utilize the above-discussed $246.68 per L/T rather than the $177.94 used by DRA to arrive at our figure of $12,567,000 for growth which we will adopt as reasonable.

In rebuttal testimony, DRA witness Danish testified that prior to his cross-examination it was his understanding that the vendor does the line and trunk testing when he performs the construction of the switch. However, during cross-examination, this proved to be incorrect; so witness Danish included a line and trunk testing of $1,833,000 based on the application of the loaded labor cost to the product of 10 minutes per test time for each line and trunk and the number of trunks installed in the test years. The 10-minute figure was furnished to him by a representative of Continental Telephone Company. This amount appears reasonable and will be adopted for this proceeding.

This witness further testified that he applied the ratio of General's budgeted gross additions to Account 100.1 to derive revised figures for COE tools, enhanced switching, emergency generators, USS/MSS, analog/MISS, and the outside plant. We will adopt as reasonable for this proceeding the revised figures for COE tools, emergency generators, USS/MSS, and analog/MISS. DRA disallowed $1.888 million for an item budgeted in this account as "modifications". Rebuttal testimony presented by General indicated that every manufacturer of COSE releases an updated generic designed version for its previously purchased system, but does not project the cost for these design releases. Consequently General must estimate these costs and include them for budgeting purposes. DRA argues there is no evidence in the record that General will, in effect, purchase "modifications" from COSE manufacturers in the test year nor is there any evidence to establish the reasonableness of the amount budgeted for this amount. We agree and will disallow this item.

DRA also recommended disallowance of a $20 million capital planning adjustment on the basis General did not provide support material to justify this amount. On rebuttal General asserted that it had explained to witness Danish that the dollars budgeted under capital planning adjustment were specifically designed to meet unexpected requirements. General argues that on cross-examination Danish agreed it was appropriate for the company to have funds available to meet unexpected capital requirements. However, the only funds he recommended for unexpected projects would have to come from other identified programs in the budget which are unexpectedly canceled or which do not increase at the rate of growth the company forecasts when the budget was developed. General's rebuttal witness Bowman further testified that General has since completed a study recommending the conversions of its TSPS equipment to newer Operator Services System (OSS) equipment in 1989. According to his testimony, this replacement increases the capital budget requirement in 1988 by approximately $15 million, an amount currently not budgeted. We note that although it may be appropriate to include dollars in the 1988 construction budget for expenditures made in 1988 for this new equipment, the equipment will not be installed until 1989. Under these circumstances it will be inappropriate to allow the amount as gross additions for the test year 1988. The $20 million capital planning adjustment will be disallowed consistent with our past practices.

Another item disallowed by DRA was entitled "PPCF". According to the rebuttal testimony, this category is an indicator of the prepayment funds required for digital switch procurement. Further, according to the testimony of this witness, this capital budget amount must be included in the total budget estimate to allow General the funds to promptly pay for switches in its modernization program. DRA argues that its estimates only addressed digital COSE L/T additions for the test year and it is not important as to when payments are made to the manufacturer. DRA further argues the key variable is in what year the plant will go into service and payments made in 1988 for 1989 plant additions are probably excludable. We agree and will disallow the $2.530 million PPCF item.

The differences between General and DRA for enhanced switching reflect the recommended disallowance by DRA of $10.152 million for common channeling signaling and $5.039 million for Centrex. General's rebuttal testimony persuaded DRA that the $10.152 million for common channeling signaling was properly includable, but since the service is to be phased in in 1988 and 1989 with all the expenditures occurring in 1987 and 1988, DRA recommends that we allow 75% of the proposed expenditures in 1988 or $7.65 million. This proposal appears reasonable and we will adopt it.

DRA's recommended disallowance of $5.039 million for Centrex was based on its understanding that the NTE in competitive bid rounds six to eight included a provision for Centrex service. Further, DRA did not know when Centrex features would be available. Rebuttal testimony by General clarified that the fee which appears as part of the NTE price is only for the software capability to provide Centrex within the switch and does not cover the cost of the Centrex equipment. DRA argues, however, that the record in this proceeding is replete with facts indicating that Centrex service offerings from digital COSEs were delayed and that at the time the DRA witness was conducting his investigation there were no Centrex services being provided from a digital switch in General's service territory. Consequently, according to DRA, it was proper to disallow the cost. DRA further argues that the assumed availability date of the GTD5 switch was changed from March 1987 to June 1988, thereby pushing back the EBSS delivery capability by 1.25 years for 40% of the central offices. Because of the uncertainties of the extent of Centrex availability in General's service territory, DRA urges us to disallow the Centrex cost. We will disallow the above discussed 40% of the Centrex budget item because of the uncertainties occasioned by the delay in delivery of the switching equipment.

We will adopt as reasonable for this proceeding for enhanced switching the amount of $24.276 million in keeping with the above discussion. The total amount for Account C209 computed in accordance with the above discussion is $119,150,000, which we will adopt as reasonable for this proceeding.

General's outside plant (OSP) construction budget for 1988 is $334.730 million as compared to DRA's estimate of $137.353 million. This budget included some dollars for items outside the test year. When viewed strictly in terms of test year 1988, these amounts translate to gross additions to Account 100.1 (for Account C60) of $139,846,000 for DRA and $322,908,000 for General.

Testimony presented on behalf of DRA by witness Danish indicated that:

1. Although General's customer concentration in its service area is 277 access lines per square mile as compared to Pacific's 231 access lines per square mile, General is spending more than twice as much as Pacific for every new inward movement line.

2. General's outside plant expenditure indicates that it spends $257 per line of inward movement as compared to Pacific's $120 per line of inward movement.

3. In 1986, General had over 1,800 people in outside plant construction while Pacific had 3,973. In view of the fact that Pacific had about four times as many customers as General, it appears that General had an excess of over 900 people in outside plant construction force (3,973 divided by 4 minus 1,800) in 1986.

4. Inasmuch as the central office modernization program is virtually over, it appears that General had shifted resources from central office construction to outside plant construction. Outside plant is budgeted for $334 million in 1988 as compared with an expenditure of $260 million in 1986 with over 80% of the budget attributed to growth.

5. General tried to justify the outside plant construction expenditure by presenting the "CAF Plan" (customer access facilities plan). Upon studying the CAF Plan, DRA determined that the maintenance savings due to the CAF Plan are minimal.

6. Using TPIS and Pacific's estimate for outside plant, DRA determined that Pacific will spend (labor and material on contract) $128 per inward line movement.

7. Using $128 per inward line movement, DRA projects for "normal growth" $112.793 million for test year 1988.

8. DRA has determined that the dollars presented by General in the CAF Plan for service and San Fernando grooming and analog subscriber-carrier removing should be accepted and therefore adopted. Adding construction cost of $15.44 million for grooming[3] and $9.17 million for analog subscriber removal to the product of $128 and the number of inward line movement

3 Grooming is the removal of loose wires and circuit elements which for one reason or another are no longer functional.

results in a total estimate for outside plant of $137.353 million.

Rebuttal testimony presented on behalf of General by Ms. Young indicated that:

1. The CAF Plan is a companywide "tops-down" description of changing technological and service environment in the CAF network that (a) quantifies the effects of introducing digital pair gain devices and fibre optics into the local loop, (b) identifies the expected change in the sophistication of service that General customers will require, and (c) identifies the need to constantly improve the quality of service provided to General customers.

2. The vast majority of General's C60 investment is required to meet new customer service requirements in General's service territory.

3. The total circuit gain is a much more meaningful driver of OSP investment than inward movement lines.

4. The major factors that contribute to General's OSP capital requirements which are budgeted to Account C60 are (a) the total circuit gain, (b) the level of plant utilization in the CAF network, (c) the level of pair gain deployment, (d) the type of OSP construction (aerial, buried, underground, conduit etc.), and (e) the condition and age of the existing plant.

5. Inward movement activity only creates additional OSP cost if the activity occurs at a new location or address not already served.

6. A lower level of utilization means there is more existing capacity available to meet customer demands for service and only after the excess idle capacity is used would there be a requirement to add additional plant.

7. A telephone company with high utilization levels may need to invest in additional plant over and above that required for the new circuit gain in order to lower its utilization levels and to increase its plant margins.

8. In terms of average investment per pair mile, underground construction in conduit is the least costly for large cables provided vacant conduits exist; direct burial construction is the most expensive since you need to dig a trench for each cable placed; and aerial construction falls somewhere between underground construction in conduit and direct buried.

9. The APF utilization percentages for the feeder portion of the CAF network is 67.6% for Pacific and 77.5% for General.

10. Based on a 19 central office sample taken in 1987, General determined its average distribution plant utilization level is 40% as compared to Pacific's distribution plant utilization factor of 28%.

11. The $334 million additions to outside plant are required to meet the service needs of General with the majority of the investment necessary to meet the increase and demand for new service. Such an investment would not result in unneeded plant investment which will increase rate base.

We are persuaded that the level of plant utilization in the CAF network, the level of the pair gain deployment, the type of outside plant construction, and the age and condition of existing facilities are sufficiently different between General and Pacific to preclude the use of Pacific's unit costs in estimating the allowance for General's OSP construction. We are also persuaded that the key driver of the construction budget is the number of new circuits that must be physically installed to meet that growth. We note with concern, however, that the unit cost per circuit gain used in General's computations for the 1988 test year exceeds that for the 1987 estimated year by far more than the increase related to the TPI. We can discern no reason for such a substantial increase and, for computing the growth figure, we will use the 1987 unit cost increased by the TPI for that year. Computing the growth in outside plant on this basis results in $274.27 million for growth which we will accept as reasonable for this proceeding. In addition, we will adopt DRA's other estimates for the outside plant account consisting of San Fernando grooming $14.89 million, analog subscriber removal $8.84 million, and pair gain $7.19 million, for a total of $305.19 million for 1988 test year plant additions to Account C-60 of Account 100.1.

General's 1988 construction budget for general equipment Account CAXX is $48.051 million. It is DRA's understanding that $41.507 million of this amount will be expended for plant that will go into service in 1988. DRA has adopted the $41.507 million budget item and has reduced it to reflect DRA's estimated employee level for 1988 by applying the ratio of its employee estimates for 1988 to General's estimated employee 1988 level. On rebuttal General's witness Hesse indicated that such a reduction would be inappropriate because almost half of the 1987 additions and approximately one-third of the 1988 additions are for new hardware and software enhancements necessary to achieve productivity gains in the maintenance accounts and, therefore, are not directly associated with a given employee level. We will accept General's one-third of the account, or $13,836,000, as being not dependent upon the number of employees, and reduce the balance of $27,671,000 to reflect our adopted 10% force reduction to yield an adopted figure of $38,740,000. The total capital additions to Account 100.1 for test year 1988 computed as discussed above is $626,590,000, which we will adopt as reasonable for this proceeding.

Both DRA and General agree that property held for future use is equal to $79,000 and the Communications System Corporation circuits that must be physically installed to meet that growth. We note with concern, however, that the unit cost per circuit gain used in General's computations for the 1988 test year exceeds that for the 1987 estimated year by far more than the increase related to the TPI. We can discern no reason for such a substantial increase and, for computing the growth figure, we will use the 1987 unit cost increased by the TPI for that year. Computing the growth in outside plant on this basis results in $274.27 million for growth which we will accept as reasonable for this proceeding. In addition, we will adopt DRA's other estimates for the outside plant account consisting of San Fernando grooming $14.89 million, analog subscriber removal $8.84 million, and pair gain $7.19 million, for a total of $305.19 million for 1988 test year plant additions to Account C-60 of Account 100.1.

General's 1988 construction budget for general equipment Account CBXX is $48.051 million. It is DRA's understanding that $41.507 million of this amount will be expended for plant that will go into service in 1988. DRA has adopted the $41.507 million budget item and has reduced it to reflect DRA's estimated employee level for 1988 by applying the ratio of its employee estimates for 1988 to General's estimated employee 1988 level. On rebuttal General's witness Hesse indicated that such a reduction would be inappropriate because almost half of the 1987 additions and approximately one-third of the 1988 additions are for new hardware and software enhancements necessary to achieve productivity gains in the maintenance accounts and, therefore, are not directly associated with a given employee level. We will accept General's one-third of the account, or $13,836,000, as being not dependent upon the number of employees, and reduce the balance of $27,671,000 to reflect our adopted 10% force reduction to yield an adopted figure of $38,740,000. The total capital additions to Account 100.1 for test year 1988 computed as discussed above is $634,938,000, which we will adopt as reasonable for this proceeding.

adjustment is a negative $15,122,000. Adding these figures to the above $626,590,000 yields a total figure for telephone plant added for test year 1988 of $611,547,000.

M. Rate Base

Rate base consists of the sum of weighted average plant in service, property held for future use, working cash allowance, materials and supplies less the sum of depreciation reserve, and deferred taxes, and adjustments for interstate construction work in progress, commission corp. TPIS, and commission corp. depreciation reserve. The following tabulation sets forth the rate base for test year 1988 as estimated by DRA and General, together with our adopted results:

Rate Base

Item	DRA	General	General Exceeds DRA Amount	General Exceeds DRA Percent	Adopted
			(Thousands of Dollars)		
Wtd. Avg. Plant in Service	$6,271,872	$6,811,173	$539,301	8.6%	$6,611,888
Interstate Tel. Plt. Under Const.	-	48,112	48,112	0.0	-
Property Held For Future Use	79	79	0	0.0	79
Materials & Supplies	16,874	25,021	8,147	48.3	21,688
Working Cash Allow.	15,785	4,726	(11,059)	(70.1)	18,293
Less: Depr. Resv.	2,024,056	2,051,025	26,969	1.3	2,013,126
Deferred Taxes	656,125	694,503	38,378	5.8	672,958
USOA TPIS	0	(21,331)	(21,331)	0.0	0
USOA Depr. Reserve	0	(926)	(926)	0.0	0
USOA Acc. Deferred Tax	0	(637)	(637)	0.0	0
Adjustments:					
Comm. Bid	(7,900)	0			(7,900)
Comm. Corp. TPIS	(68,589)	(15,122)	53,467	(78.0)	(15,122)
Comm. Corp. Depr. Reserve	11,839	11,706	(133)	(1.1)	11,706
Total Adjustments	(56,750)	(3,416)	53,334		11,316
Total	3,567,680	4,117,273	549,593	15.4	3,954,548

(Red Figure)

Both DRA and General agree that property held for future use is equal to $79,000 and the Communications System Corporation adjustment is a negative $15,122,000. Adding these figures to the above $634,938,000 yields a total figure for telephone plant added for test year 1988 of $619,895,000.

M. Rate Base

Rate base consists of the sum of weighted average plant in service, property held for future use, working cash allowance, materials and supplies less the sum of depreciation reserve, and deferred taxes, and adjustments for interstate construction work in progress, commission corp. TPIS, and commission corp. depreciation reserve. The following tabulation sets forth the rate base for test year 1988 as estimated by DRA and General, together with our adopted results:

Rate Base

Item	DRA	General	General Exceeds DRA Amount	General Exceeds DRA Percent	Adopted
			(Thousands of Dollars)		
Wtd. Avg. Plant in Service	$6,320,960	$6,843,968	$523,008	8.3%	$6,616,063
Interstate Tel. Plt. Under Const.	-	48,112	48,112	0.0	-
Property Held For Future Use	79	79	-	0.0	79
Materials & Supplies	16,874	25,021	8,147	48.3	21,977
Working Cash Allow.	15,785	4,726	(11,059)	(70.1)	18,428
Less: Depr. Resv.	2,024,056	2,051,951	27,895	1.4	2,013,282
Deferred Taxes	656,125	695,140	39,015	5.9	673,362
Total Rate Base	3,673,518	4,174,815	501,297	13.6	3,969,903
Adjustments:					
L&B Transfer	(1,756)	-	1,756	(100.0)	-
Competitive Bid	(50,000)	-	50,000	(100.0)	(7,900)
Cash Compensation	(8,100)	-	8,100	(100.0)	-
Comm. Syst. TPIS	(15,122)	(15,122)	-	0.0	(15,122)
Thousand Oaks	(42,700)	-	42,000	(100.0)	-
Comm. Syst. Depr. Resv.	11,837	11,706	(131)	(1.1)	11,706
Total Adjustment	(105,840)	(3,416)	102,424	(96.8)	(11,316)
Net Adjusted Rate Base	$3,567,678	$4,171,399	$603,721	16.9	$3,958,587

( ) (Red Figure)

Both DRA and General agree that property held for future use is equal to $79,000 and the Communications System Corporation adjustment is a negative $15,122,000. Adding these figures to the above $671,925,000 yields a total figure for telephone plant added for test year 1988 of $656,882.

M. Rate Base

Rate base consists of the sum of weighted average plant in service, property held for future use, working cash allowance, materials and supplies less the sum of depreciation reserve, and deferred taxes, and adjustments for interstate construction work in progress, commission corp. TPIS, and commission corp. depreciation reserve. The following tabulation sets forth the rate base for test year 1988 as estimated by DRA and General, together with our adopted results:

Rate Base

Item	DRA	General	General Exceeds DRA Amount	General Exceeds DRA Percent	Adopted
			(Thousands of Dollars)		
Wtd. Avg. Plant in Service	$6,320,960	$6,843,968	$523,008	8.3%	$6,675,298
Interstate Tel. Plt. Under Const.	-	48,112	48,112	0.0	-
Property Held For Future Use	79	79	-	0.0	79
Materials & Supplies	16,874	25,021	8,147	48.3	23,258
Working Cash Allow.	15,785	4,726	(11,059)	(70.1)	18,788
Less: Depr. Resv.	2,024,056	2,051,951	27,895	1.4	2,015,626
Deferred Taxes	656,125	695,140	39,015	5.9	679,418
Total Rate Base	3,673,518	4,174,815	501,297	13.6	4,022,379
Adjustments:					
L&B Transfer	(1,756)	-	1,756	(100.0)	-
Competitive Bid	(50,000)	-	50,000	(100.0)	(7,900)
Cash Compensation	(8,100)	-	8,100	(100.0)	-
Comm. Syst. TPIS	(15,122)	(15,122)	-	0.0	(15,122)
Thousand Oaks	(42,700)	-	42,000	(100.0)	-
Comm. Syst. Depr. Resv.	11,837	11,706	(131)	(1.1)	11,706
Total Adjustment	(105,840)	(3,416)	102,424	(96.8)	(11,316)
Net Adjusted Rate Base	$3,567,678	$4,171,399	$603,721	16.9	$4,011,063

(Red Figure)

DRA's estimate for materials and supplies is $16,874,000 as compared to General's estimate of $25,021,000, a difference of $8,147,000 or 48.3%. The major reason for the disparity is different estimated plant investment. Consistent with our adopted weighted average plant balance we will adopt as reasonable a material and supplies figure of $21,688,000.

Working cash allowance (WCA) is designed to compensate investors for funds provided by them which are permanently committed to the business for the purpose of paying operating expenses in advance of the receipt of offsetting revenues from the company's customers and in order to maintain minimum bank balances.

The following tabulation sets forth the component parts of the WCA as estimated by DRA and General, together with our adopted results:

DRA's estimate for materials and supplies is $16,874,000 as compared to General's estimate of $25,021,000, a difference of $8,147,000 or 48.3%. The major reason for the disparity is different estimated plant investment. Consistent with our adopted weighted average plant balance we will adopt as reasonable a material and supplies figure of $21,977,000.

Working cash allowance (WCA) is designed to compensate investors for funds provided by them which are permanently committed to the business for the purpose of paying operating expenses in advance of the receipt of offsetting revenues from the company's customers and in order to maintain minimum bank balances.

The following tabulation sets forth the component parts of the WCA as estimated by DRA and General, together with our adopted results:

Working Cash Allowance

Item	DRA	General	General Exceeds DRA Amount	General Exceeds DRA Percent	Adopted
			(Thousands of Dollars)		
Gross Working Cash Requirement:					
Misc. Spec. Deposits	$ 1,887	$ 1,918	$ 31	1.6	$ 1,887
Misc. Receivables	57,702	58,658	956	1.8	57,702
Working Funds	325	329	4	1.2	325
Other Deferred	32,512	33,596	1,084	3.3	32,512
Prepayments	16,303	16,572	269	1.7	16,303
Pay Exp. Before Revenues	-	15,055	15,055	0.0	0
Total Gross Req.	108,729	126,128	17,399	16.0	108,729
Deduction of Funds Not Supplied By Investors:					
Avg. Amt. Coll. Before Exp.	(23,652)	-	23,652	-100.0	(24,170)
Excise Taxes	692	692	0	0.0	692
City Users Tax	451	451	0	0.0	451
Employee Withhold.	11,665	11,864	199	1.7	11,665
Other Def. Credits	73,923	75,147	1,224	1.7	73,923
Rev. Settlements	(16,666)	(16,666)	0	0.0	(16,666)
Cr. from Suppliers for Cap. Mat'l.	30,379	30,379	0	0.0	30,379
Lag Pay Cap. Items	14,162	19,535	5,373	37.9	14,162
Total Deductions	90,954	121,402	30,448	33.5	90,436
Working Cash Allow.	15,785	4,726	(11,059)	(70.1)	18,293

(Red Figure)

Working Cash Allowance

Item	DRA	General	General Exceeds DRA Amount	General Exceeds DRA Percent	Adopted
			(Thousands of Dollars)		
Gross Working Cash Requirement:					
Misc. Spec. Deposits	$ 1,887	$ 1,918	$ 31	1.6	$ 1,887
Misc. Receivables	57,702	58,658	956	1.8	57,702
Working Funds	325	329	4	1.2	325
Other Deferred	32,512	33,596	1,084	3.3	32,512
Prepayments	16,303	16,572	269	1.7	16,303
Pay Exp. Before Revenues	-	15,055	15,055	0.0	0
Total Gross Req.	108,729	126,128	17,399	16.0	108,729
Deduction of Funds Not Supplied By Investors:					
Avg. Amt. Coll. Before Exp.	(23,652)	-	23,652	-100.0	(24,305)
Excise Taxes	692	692	0	0.0	692
City Users Tax	451	451	0	0.0	451
Employee Withhold.	11,665	11,864	199	1.7	11,665
Other Def. Credits	73,923	75,147	1,224	1.7	73,923
Rev. Settlements	(16,666)	(16,666)	0	0.0	(16,666)
Cr. from Suppliers for Cap. Mat'l.	30,379	30,379	0	0.0	30,379
Lag Pay Cap. Items	14,162	19,535	5,373	37.9	14,162
Total Deductions	90,954	121,402	30,448	33.5	90,301
Working Cash Allow.	15,785	4,726	(11,059)	(70.1)	18,428

(Red Figure)

Working Cash Allowance

Item	DRA	General	General Exceeds DRA Amount	General Exceeds DRA Percent	Adopted
		(Thousands of Dollars)			
Gross Working Cash Requirement:					
Misc. Spec. Deposits	$ 1,887	$ 1,918	$ 31	1.6	$ 1,887
Misc. Receivables	57,702	58,658	956	1.8	57,702
Working Funds	325	329	4	1.2	325
Other Deferred	32,512	33,596	1,084	3.3	32,512
Prepayments	16,303	16,572	269	1.7	16,303
Pay Exp. Before Revenues	-	15,055	15,055	0.0	0
Total Gross Req.	108,729	126,128	17,399	16.0	108,729
Deduction of Funds Not Supplied By Investors:					
Avg. Amt. Coll. Before Exp.	(23,652)	-	23,652	-100.0	(24,665)
Excise Taxes	692	692	0	0.0	692
City Users Tax	451	451	0	0.0	451
Employee Withhold.	11,665	11,864	199	1.7	11,665
Other Def. Credits	73,923	75,147	1,224	1.7	73,923
Rev. Settlements	(16,666)	(16,666)	0	0.0	(16,666)
Cr. from Suppliers for Cap. Mat'l.	30,379	30,379	0	0.0	30,379
Lag Pay Cap. Items	14,162	19,535	5,373	37.9	14,162
Total Deductions	90,954	121,402	30,448	33.5	89,941
Working Cash Allow.	17,785	4,726	(11,059)	(70.1)	18,788

(Red Figure)

N. Summary of Earnings

The following tabulation summarizes our adopted results of operation for test year 1988 for the company as a whole and its intrastate operations which is also reflected in Appendix D of this decision:

General Telephone Company of California
Summary of Earnings
1988 Test Year
($000)

Item	Total Company DRA	Total Company General	Adopted Total Company	Adopted Intrastate
Operating Revenues				
Local Service	$ 779,228	$ 835,224	$ 780,686	$ 780,686
Toll Service	781,079	825,325	817,213	817,213
Intrastate Access	215,908	201,963	206,526	206,526
Interstate Access	480,425	480,425	480,425	-
Miscellaneous	322,670	262,770	281,981	258,162
Surcharge	73,287	184,675	74,730	74,730
Gain on Sale on Prop.	10,490	0	4,485	3,639
1987 Attrition	-	(52,978)	-	-
Less: Uncollectibles	18,594	24,368	21,638	20,438
Total Operating Rev.	2,644,493	2,713,036	2,624,408	2,120,518
Operating Expenses				
Maintenance	412,062	491,676	431,330	336,774
Traffic	60,633	74,563	64,683	57,733
Commercial	240,198	275,725	257,207	212,825
Gen. Off. Sal. & Exp.	179,385	197,636	188,782	159,448
Other Oper. Exp.	133,213	235,711	190,075	155,413
Subtotal	1,025,491	1,275,311	1,132,077	922,193
Depreciation	497,161	539,288	519,807	424,084
Taxes Other than on Income	94,516	113,506	105,556	83,679
State Income Tax	71,528	59,464	68,662	57,495
Federal Income Tax	243,333	184,207	184,735	149,655
Total Operating Exp.	1,932,029	2,171,776	2,010,837	1,637,106
Net Operating Income	712,464	541,260	613,571	483,412

N. Summary of Earnings

The following tabulation summarizes our adopted results of operation for test year 1988 for the company as a whole and its intrastate operations:

General Telephone Company of California
Summary of Earnings
1988 Test Year
($000)

Item	Total Company DRA	Total Company General	Adopted Total Company	Adopted Intrastate
Operating Revenues				
Local Service	$ 779,228	$ 835,224	$ 776,247	$ 776,247
Toll Service	781,079	825,325	819,735	819,735
Intrastate Access	215,908	201,963	206,526	206,526
Interstate Access	480,425	480,425	480,425	-
Miscellaneous	322,670	262,770	281,381	257,562
Surcharge	73,287	184,675	74,730	74,730
Gain on Sale on Prop.	10,490	0	4,485	3,639
1987 Attrition	-	(52,978)	-	-
Less: Uncollectibles	18,594	24,368	21,630	20,430
Total Operating Rev.	2,644,493	2,713,036	2,621,899	2,118,009
Operating Expenses				
Maintenance	412,062	491,676	431,230	336,696
Traffic	60,633	74,563	64,683	57,733
Commercial	240,198	275,725	257,207	212,825
Gen. Off. Sal. & Exp.	179,385	197,636	188,782	159,448
Other Oper. Exp.	133,213	235,711	195,633	159,961
Subtotal	1,025,491	1,275,311	1,137,535	926,663
Depreciation	497,161	539,288	519,494	423,804
Taxes Other than on Income	94,516	113,506	105,517	83,649
State Income Tax	71,528	59,464	68,323	57,162
Federal Income Tax	243,333	184,207	182,710	147,932
Total Operating Exp.	1,932,029	2,171,776	2,015,066	1,639,210
Net Operating Income	712,464	541,260	608,320	478,799

N. Summary of Earnings

The following tabulation summarizes our adopted results of operation for test year 1988 for the company as a whole and its intrastate operations which is also reflected in Appendix D of this decision:

General Telephone Company of California
Summary of Earnings
1988 Test Year
($000)

Item	Total Company		Adopted	
	DRA	General	Total Company	Intrastate
Operating Revenues				
Local Service	$ 779,228	$ 835,224	$ 781,134	$ 781,134
Toll Service	781,079	825,325	822,392	822,392
Intrastate Access	215,908	201,963	206,526	206,526
Interstate Access	480,425	480,425	480,425	-
Miscellaneous	322,670	262,770	281,981	258,162
Surcharge	73,287	184,675	74,730	74,730
Gain on Sale on Prop.	10,490	0	4,485	3,639
1987 Attrition	-	(52,978)	-	-
Less: Uncollectibles	18,594	24,368	21,638	20,438
Total Operating Rev.	2,644,493	2,713,036	2,630,035	2,126,145
Operating Expenses				
Maintenance	412,062	491,676	431,330	336,774
Traffic	60,633	74,563	64,683	57,733
Commercial	240,198	275,725	257,207	212,825
Gen. Off. Sal. & Exp.	179,385	197,636	188,847	159,500
Other Oper. Exp.	133,213	235,711	191,456	156,520
Subtotal	1,025,491	1,275,311	1,133,523	923,352
Depreciation	497,161	539,288	524,494	428,000
Taxes Other than on Income	94,516	113,506	106,135	84,135
State Income Tax	71,528	59,464	68,473	57,423
Federal Income Tax	243,333	184,207	182,112	147,541
Total Operating Exp.	1,932,029	2,171,776	2,014,737	1,640,451
Net Operating Income	712,464	541,260	615,298	485,694

General Telephone Company of California (Cont'd.)
Summary of Earnings
1988 Test Year
$000)

Item	Total Company DRA	Total Company General	Adopted Total Company	Adopted Intrastate
Adjustments of Income				
CCFT	-	(2,802)	-	-
Communications System	-	865	-	-
GTE Directories	-	4,131	-	-
Total Adjust. to Income	-	2,194	-	-
Net Adjusted Income	712,464	543,454	608,320	478,799
Rate Base				
100.1 Tel. Plant in Service	6,203,282	6,843,968	6,588,866	5,215,201
100.2 Tel. Plant Under Const.	0	48,112	0	0
100.3 Prop. Held For Future Use	79	79	79	62
Materials & Supplies	16,874	25,021	21,688	16,372
Working Cash	15,785	4,726	18,293	14,902
Less: Depr. Reserve	2,012,217	2,051,951	2,001,420	1,588,200
Less: Def. Taxes	656,125	695,140	672,958	532,020
Total Rate Base	3,567,678	4,174,815	3,954,548	3,126,317
Adjustment to Rate Base				
Communications System	-	(3,416)	-	-
Net Adjusted Rate Base	3,567,678	4,171,399	3,954,548	3,126,317
Rate of Return	19.97%	13.03%	15.38%	15.32%

(Red Figure)

General Telephone Company of California (Cont'd.)
Summary of Earnings
1988 Test Year
($000)

Item	Total Company DRA	Total Company General	Adopted Total Company	Adopted Intrastate
Adjustments of Income				
CCFT	-	(2,802)	-	-
Communications System	-	865	-	-
GTE Directories	-	4,131	-	-
Total Adjust. to Income	-	2,194	-	-
Net Adjusted Income	712,464	543,454	613,571	483,412
Rate Base				
100.1 Tel. Plant in Service	6,203,282	6,843,968	6,593,041	5,218,789
100.2 Tel. Plant Under Const.	0	48,112	0	0
100.3 Prop. Held For Future Use	79	79	79	62
Materials & Supplies	16,874	25,021	21,977	16,590
Working Cash	15,785	4,726	18,428	15,011
Less: Depr. Reserve	2,012,217	2,051,951	2,001,576	1,588,427
Less: Def. Taxes	656,125	695,140	673,362	532,340
Total Rate Base	3,567,678	4,174,815	3,958,587	3,129,685
Adjustment to Rate Base				
Communications System	-	(3,416)	-	-
Net Adjusted Rate Base	3,567,678	4,171,399	3,958,587	3,129,685
Rate of Return	19.97%	13.03%	15.50%	15.45%

(Red Figure)

General Telephone Company of California (Cont'd.)
Summary of Earnings
1988 Test Year
($000)

Item	Total Company DRA	Total Company General	Adopted Total Company	Adopted Intrastate
Adjustments of Income				
CCFT	-	(2,802)	-	-
Communications System	-	865	-	-
GTE Directories	-	4,131	-	-
Total Adjust. to Income	-	2,194	-	-
Net Adjusted Income	712,464	543,454	615,298	485,694
Rate Base				
100.1 Tel. Plant in Service	6,203,282	6,843,968	6,652,276	5,266,757
100.2 Tel. Plant Under Const.	0	48,112	0	0
100.3 Prop. Held For Future Use	79	79	79	62
Materials & Supplies	16,874	25,021	23,258	17,557
Working Cash	15,785	4,726	18,788	15,305
Less: Depr. Reserve	2,012,217	2,051,951	2,003,920	1,590,739
Less: Def. Taxes	656,125	695,140	679,418	537,127
Total Rate Base	3,567,678	4,174,815	4,011,063	3,171,815
Adjustment to Rate Base				
Communications System	-	(3,416)	-	-
Net Adjusted Rate Base	3,567,678	4,171,399	4,011,063	3,171,815
Rate of Return	19.97%	13.03%	15.34%	15.31%

(Red Figure)

O. Net-to-Gross Multiplier

The net-to-gross multiplier (NTG) is 1.56267 computed as follows:

Item	Intrastate Total
	1.00000
Uncollectible rate	0.01200
Difference	0.98800
CCFT at incremental rate 0.018635	0.01841
Difference	0.96959
FIT at 34%	0.32966
Difference	0.63993
1.0000 ÷ 0.63993 =	1.56267

P. Intrastate Revenue Requirement

	(000 Dollars)
Rate Base	$3,126,317
Rate of Return (D.87-12-070)	0.1090
Net Revenue	340,769
Net Revenue at pres. rates	478,799
Difference	(138,030)
Revenue requirement (Diff. NTG)	(215,697)
Interstate USF (High Cost)	(784)
D.87-12-070 Rev. Req. Add Back	(112,190)
Total Revenue Requirement	$(328,671)

O. Net-to-Gross Multiplier

The net-to-gross multiplier (NTG) is 1.56267 computed as follows:

Item	Intrastate Total
	1.00000
Uncollectible rate	0.01200
Difference	0.98800
CCFT at incremental rate 0.018635	0.01841
Difference	0.96959
FIT at 34%	0.32966
Difference	0.63993
1.0000 ÷ 0.63993 =	1.56267

P. Intrastate Revenue Requirement

	(000 Dollars)
Rate Base	$3,129,685
Rate of Return (D.87-12-070)	0.1090
Net Revenue	341,136
Net Revenue at pres. rates	483,412
Difference	(142,276)
Revenue requirement (Diff. NTG)	(222,332)
Interstate USF (High Cost)	(784)
D.87-12-070 Rev. Req. Add Back	(112,190)
Total Revenue Requirement	$(335,306)

O. Net-to-Gross Multiplier

The net-to-gross multiplier (NTG) is 1.56267 computed as follows:

Item	Intrastate Total
	1.00000
Uncollectible rate	0.01200
Difference	0.98800
CCFT at incremental rate 0.018635	0.01841
Difference	0.96959
FIT at 34%	0.32966
Difference	0.63993
1.0000 ÷ 0.63993 =	1.56267

P. Intrastate Revenue Requirement ($000)

Rate Base	$3,171,815
Rate of Return (D.87-12-070)	0.1090
Net Revenue	345,728
Net Revenue at pres. rates	485,694
Difference	(139,966)
Revenue requirement (Diff. x NTG)	(218,722)
Interstate USF (High Cost)	(784)
D.87-12-070 Rev. Req. Add Back	(112,190)
Total Revenue Requirement	$(331,696)

VII. Attrition

As discussed in the section entitled "Labor Productivity Adjustment for Attrition Years 1989 and 1990" supra, we are partially adopting DRA's proposal for an attrition formula with a base 5% factor based on the change in number of access lines for employee (ALPE). Any savings in excess of the 5% productivity level will be shared equally between the ratepayers and General.

In its direct showing, General requested the option of filing for operational and financial attrition in 1989 and 1990. It recommended that the methodology ordered by this Commission and used as a basis for General's 1986 attrition award (D.85-03-042 and D.85-12-081) continue as a proved mechanism. However, that mechanism was subsequently modified by D.86-12-099 in Pacific's A.85-01-034 for a 1986 test year rate case. General therefore proposes that the attrition formula as modified by D.86-12-099 be used for attrition years 1989 and 1990. We will adopt this recommendation for this matter, subject to any changes resulting from our current investigation, I.87-11-033, which is considering the merits of continuing attrition adjustments for telephone companies generally, as part of the establishment of new regulatory framework for local exchange telephone utilities.

As noted in Interim D.87-12-070 on this matter, we indicated that events occurring in the financial market in October 1987 indicated that we should reconsider our plan of considering revision of the ROE and capital structure every three years and have General's capital structure, interest costs, ROE, and financing plans reviewed in the attrition years. The order that follows will so provide.

In addition in D.88-06-024 in A.88-05-009, we have specified that General file its application for 1989 financial attrition by July 15, 1988, and its advice letter for 1989 operational attrition by October 1, 1988. Financial attrition will

VII. Attrition

As discussed in the section entitled "Labor Productivity Adjustment for Attrition Years 1989 and 1990" supra, we are partially adopting DRA's proposal for an attrition formula with a base 5% factor based on the change in number of access lines for employee (ALPE). Any savings in excess of the 5% productivity level will be shared equally between the ratepayers and General.

In its direct showing, General requested the option of filing for operational and financial attrition in 1989 and 1990. It recommended that the methodology ordered by this Commission and used as a basis for General's 1986 attrition award (D.85-03-042 and D.85-12-081) continue as a proved mechanism. However, that mechanism was subsequently modified by D.86-12-099 in Pacific's A.85-01-034 for a 1986 test year rate case. General therefore proposes that the attrition formula as modified by D.86-12-099 be used for attrition years 1989 and 1990. We will adopt this recommendation for this matter, subject to any changes resulting from our current investigation, I.87-11-033, which is considering the merits of continuing attrition adjustments for telephone companies generally, as part of the establishment of new regulatory framework for local exchange telephone utilities.

As noted in Interim D.87-12-070 on this matter, we indicated that events occurring in the financial market in October 1987 indicated that we should reconsider our plan of considering revision of the ROE and capital structure every three years and have General's capital structure, interest costs, ROE, and financing plans reviewed in the attrition years. The order that follows will so provide.

In addition in D.88-06-024 in A.88-05-009, we have specified that General file its application for 1989 financial attrition by July 15, 1988, which General has filed and its advice letter for 1989 operational attrition by October 1, 1988.

be heard on a consolidated record for General and Pacific, as ordered in D.88-06-024.

VIII. Rate Design

To expedite the flow through of the revenue reduction and avoid any conflict with other ongoing proceedings, we will not address the final rate design at this time.

As previously noted, the gross revenue requirement reduction adopted in this decision is $328.671 million which includes the revenue requirement reduction of $112.190 million derived from the billing surcharges/surcredits ordered in interim decision, D.87-12-070 as revised by Advice Letter No. 5125, filed February 29, 1988.

For this interim decision, we will be spreading the additional revenue requirement reduction of $216.481 million ($328.671 less $112.190) by an incremental bill and keep surcredit of 13.34% on access services, on intraLATA message toll and toll private line services and on local exchange services. (I.e., for access services negative 0.296% plus (negative 13.34%) equals negative 13.636%.)

The development of the incremental bill and keep surcredit and the adopted billing bases are as follows:

	Adopted Billing Base	Revenue Requirement ($000)	Incremental Surcredit
Intrastate Access	$ 233,201	$ -31,101	-13.34%
IntraLATA Toll	663,367	-88,471	-13.34%
Local Exchange	726,639	-96,909	-13.34%
Total	$1,623,207	$-216,481	-13.34%

Financial attrition will be heard on a consolidated record for General and Pacific, as ordered in D.88-06-024.

VIII. Rate Design

To expedite the flow through of the revenue reduction and avoid any conflict with other ongoing proceedings, we will not address the final rate design at this time.

As previously noted, the gross revenue requirement reduction adopted in this decision is $335.306 million which includes the revenue requirement reduction of $112.190 million derived from the billing surcharges/surcredits ordered in interim decision, D.87-12-070 as revised by Advice Letter No. 5125, filed February 29, 1988.

For this interim decision, we will be spreading the additional revenue requirement reduction of $223.116 million ($335.306 less $112.190) by an incremental bill and keep surcredit of 13.34% on access services, on intraLATA message toll and toll private line services and on local exchange services. (i.e., for access services negative 0.296% plus negative 13.75% equals negative 14.046%.)

The development of the incremental bill and keep surcredit and the adopted billing bases are as follows:

	Adopted Billing Base ($000)	Revenue Requirement ($000)	Incremental Surcredit
Intrastate Access	$ 233,201	$ -32,055	-13.75%
IntraLATA Toll	663,367	-91,182	-13.75%
Local Exchange	726,639	-99,879	-13.75%
Total	$1,623,207	$-223,116	-13.75%

Financial attrition will be heard on a consolidated record for General and Pacific, as ordered in D.88-06-024.

VIII. Rate Design

To expedite the flow through of the revenue reduction and avoid any conflict with other ongoing proceedings, we will not address the final rate design at this time.

As previously noted, the gross revenue requirement reduction adopted in this decision is $331.696 million which includes the revenue requirement reduction of $112.190 million derived from the billing surcharges/surcredits ordered in interim decision, D.87-12-070 as revised by Advice Letter No. 5125, filed February 29, 1988.

For this interim decision, we will be spreading the additional revenue requirement reduction of $219.506 million ($331.696 less $112.190) by an incremental bill and keep surcredit of 13.52% on access services, on intraLATA message toll and toll private line services and on local exchange services. (i.e., for access services negative 0.296% plus negative 13.52% equals negative 13.816%.)

The development of the incremental bill and keep surcredit and the adopted billing bases are as follows:

	Adopted Billing Base ($000)	Revenue Requirement ($000)	Incremental Surcredit
Intrastate Access	$ 233,201	$ -31,536	-13.52%
IntraLATA Toll	663,367	-89,707	-13.52%
Local Exchange	726,639	-98,263	-13.52%
Total	$1,623,207	$-219,506	-13.52%

The above incremental surcredits will be reflected in General's Schedule Cal. P.U.C. No. A-38.

In D.85-06-113, we modified D.85-03-056, to require that within 14 days of local exchange utilities making their advice letter filings to reduce local access charges, AT&T-C pass on to its customers through a corresponding incremental reduction in the billing surcharge any reduction in its expense stemming from reductions in local exchange utilities' access charges. We will require a slightly different treatment in this instance consistent with our action in Pacific Bell's rate design decision in A.85-01-034. Specifically, we will require AT&T-C to accumulate the reduced access expense resulting from this decision in a memorandum account, with interest, commencing on the effective date of the General tariff revision and running through December 31, 1988 at which time AT&T-C shall roll this accumulated reduced expense into its computation of the effects on access rates of the SPF to SLU phase down of the local exchange carriers which will be reflected in AT&T-C's rates.

IX. Other Issues

We are issuing this decision as an interim decision to effect the rate reductions as soon as possible. Issues we will address in the next interim decision are as follows:

1. The final apportionment of the rate reduction to the various customer groups and the final tariff schedules, based on this record.

2. Issues raised at public-participation hearings including monthly inside wiring charges, physical size of bills, quality of service, pay phone availability, and the 13-second time limit for dialing.

X. Findings and Conclusions

Findings of Fact

1. An additional incremental revenue requirement reduction of $216.481 million for a total reduction of $328.671 million is appropriate for the test year 1988.

2. A rate of return of 10.90% for test year 1988 found reasonable in D.87-12-070 dated December 22, 1987 should remain in effect.

3. To effect the above revenue reduction, the surcredits set forth in Appendix A to this decision should be effected on a bill and keep basis.

4. A total of $161.9 million for the test year 1988 level of GTESC expenses to be prorated to General and the other GTOCs is reasonable.

5. A prorate factor of 29.6% to allocate GTESC expenses to General is reasonable.

6. General's 20.4 AWT figure is reasonable given its development with reference to actual AWTS data, and given the characteristics of General's operations, as previously discussed.

7. A reasonable expense allowance for Account 674-General Services and Licenses for the test year 1988 is $44.7 million.

8. Since General has not supported its Account 675-Other Expenses estimate, DRA's figure of $5,141,000 which uses lower escalation factors, lower estimate of "cost billed to others," and excludes dues payable to the US Telephone Association, consistent with Commission policies, is reasonable, and adopted.

9. A telephone plant adjustment equal to a negative capitalized sales adjustment of $15,122,000 minus the associated depreciation reserve of $11,706,000 or $3,416,000 and a corresponding depreciation expense of $1,370,000 is a reasonable ratemaking adjustment for GTE Communications System Corporation.

X. Findings and Conclusions

Findings of Fact

1. An additional incremental revenue requirement reduction of $223.116 million for a total reduction of $335.306 million is appropriate for the test year 1988. ✓✓

2. A rate of return of 10.90% for test year 1988 found reasonable in D.87-12-070 dated December 22, 1987 should remain in effect.

3. To effect the above revenue reduction, the surcredits set forth in Appendix A to this decision should be effected on a bill and keep basis.

4. A total of $165.4 million for the test year 1988 level of GTESC expenses to be prorated to General and the other GTOCs is reasonable. ✓

5. A prorate factor of 29.6% to allocate GTESC expenses to General is reasonable.

6. General's 20.4 AWT figure is reasonable given its development with reference to actual AWTS data, and given the characteristics of General's operations, as previously discussed.

7. A reasonable expense allowance for Account 674-General Services and Licenses for the test year 1988 is $43.4 million. ✓

8. Since General has not supported its Account 675-Other Expenses estimate, DRA's figure of $5,141,000 which uses lower escalation factors, lower estimate of "cost billed to others," and excludes dues payable to the US Telephone Association, consistent with Commission policies, is reasonable, and adopted.

9. A telephone plant adjustment equal to a negative capitalized sales adjustment of $15,122,000 minus the associated depreciation reserve of $11,706,000 or $3,416,000 and a corresponding depreciation expense of $1,370,000 is a reasonable ratemaking adjustment for GTE Communications System Corporation.

X. Findings and Conclusions

Findings of Fact

1. An additional incremental revenue requirement reduction of $219.506 million for a total reduction of $331.696 million is appropriate for the test year 1988.

2. A rate of return of 10.90% for test year 1988 found reasonable in D.87-12-070 dated December 22, 1987 should remain in effect.

3. To effect the above revenue reduction, the surcredits set forth in Appendix A to this decision should be effected on a bill and keep basis.

4. A total of $165.4 million for the test year 1988 level of GTESC expenses to be prorated to General and the other GTOCs is reasonable.

5. A prorate factor of 29.6% to allocate GTESC expenses to General is reasonable.

6. General's 20.4 AWT figure is reasonable given its development with reference to actual AWTS data, and given the characteristics of General's operations, as previously discussed.

7. A reasonable expense allowance for Account 674-General Services and Licenses for the test year 1988 is $43.4 million.

8. Since General has not supported its Account 675-Other Expenses estimate, DRA's figure of $5,141,000 which uses lower escalation factors, lower estimate of "cost billed to others," and excludes dues payable to the US Telephone Association, consistent with Commission policies, is reasonable, and adopted.

9. A telephone plant adjustment equal to a negative capitalized sales adjustment of $15,122,000 minus the associated depreciation reserve of $11,706,000 or $3,416,000 and a corresponding depreciation expense of $1,370,000 is a reasonable ratemaking adjustment for GTE Communications System Corporation.

10. A ratemaking adjustment to expenses other than taxes for the operations of the directory corporation of $9,001,000 is reasonable.

11. It is reasonable not to adopt Team's recommendation with respect to mandating that General undertake an annual competitive analysis of its directory service contract including the soliciting of bids from other directory publishers.

12. General's revenue requirement should not be adjusted to reflect the earnings of GTE Telecom Marketing Corporation resulting from a marketing agreement with AT&T Communications covering the period from May to December 1985.

13. It is reasonable to require General to conduct a competitive analysis prior to its next rate filing and include the study in its work papers to support the continued affiliate transactions between General and GTEDS.

14. A GTEDS adjustment of $3,044,000 to reflect two-thirds of the 1988 implemental cost of customer records and billing system and facilities management system is reasonable.

15. A 1988 test year expense of $9,885,700 for Account 996-Computer Usage is reasonable.

16. It is reasonable to adjust General's revenue requirement for test year 1988 by $687,000 to reflect imputed Yellow Page fillers for GTEL.

17. It is reasonable to adjust General's 1988 test year revenue requirement by $762,000 to recognize the expected revenues for the cost of providing 1988 referrals to GTEL and $2,367,000 to recognize the expected revenues for the market value of providing projected 1988 referrals to GTEL.

18. It is reasonable to require General to establish referral guidelines to track successful and unsuccessful referrals to GTEL, and to perform a study to be completed within six months of the effective date of the decision, to determine the cost plus 10%

10. A ratemaking adjustment to expenses other than taxes for the operations of the directory corporation of $9,001,000 is reasonable.

11. It is reasonable not to adopt Team's recommendation with respect to mandating that General undertake an annual competitive analysis of its directory service contract including the soliciting of bids from other directory publishers.

12. General's revenue requirement should not be adjusted to reflect the earnings of GTE Telecom Marketing Corporation resulting from a marketing agreement with AT&T Communications covering the period from May to December 1985.

13. It is reasonable to require General to conduct a competitive analysis prior to its next rate filing and include the study in its work papers to support the continued affiliate transactions between General and GTEDS.

14. A GTEDS adjustment of $3,044,000 to reflect two-thirds of the 1988 implemental cost of customer records and billing system and facilities management system is reasonable.

15. A 1988 test year expense of $9,885,700 for Account 996-Computer Usage is reasonable.

16. It is reasonable to adjust General's revenue requirement for test year 1988 by $687,000 to reflect imputed Yellow Page fillers for GTEL.

17. It is reasonable to adjust General's 1988 test year revenue requirement by $762,000 to recognize the expected revenues for the cost of providing 1988 referrals to GTEL and $2,361,000 to recognize the expected revenues for the market value of providing projected 1988 referrals to GTEL.

18. It is reasonable to require General to establish referral guidelines to track successful and unsuccessful referrals to GTEL, and to perform a study to be completed within six months of the effective date of the decision, to determine the cost plus 10%

markup for each referral made to GTEL and to bill GTEL for such referrals.

19. For the test year 1988 a corporate oversight allocation adjustment of $1,694,000 for services performed for GTEL is reasonable.

20. It is reasonable to require General to conduct a market-based pricing study to determine market rates for services it provides to GTEL.

21. A compounded labor escalation factor of 1.118% is reasonable for test year 1988.

22. A compounded nonlabor escalation factor of 1.09003 is reasonable for test year 1988.

23. An adjustment for 1988 test year compensation levels in addition to various ratemaking disallowances is inappppropriate.

24. A 5% productivity factor for attrition year labor adjustment is reasonable. Savings from productivity gains in excess of 5% should be divided equally between ratepayers and General.

25. D.88-06-024 directed General to make a 1989 operational attrition filing by October 1, 1988. It also directed General to file an application, testimonies and exhibits for capital structure and cost of capital review for 1989 on or before July 15, 1988.

26. The actual productivity factor will not be known until after the end of the attrition year. Therefore, it is appropriate to implement the sharing of the productivity savings on or before January 31 of the year following the attrition year.

27. It is reasonable for General to retire $3.8 million Olympics plant below the line for ratemaking and accounting purposes.

28. It is reasonable to disallow for ratemaking purposes a labor overrun of $7.9 million for cost overruns of switching equipment.

29. It is reasonable to amortize the costs of improvements in property prior to occupancy over a three-year period.

30. Interest during construction should not be allowed on land.

31. General has failed to justify $2.362 million toxics cleanup request but the record indicates some future costs will be incurred, and as a matter of judgment we adopt $353,000 as reasonable for test year 1988.

32. Given the scanty record, and the 1988 test year allowance, it is appropriate to allow General to file an application seeking recovery of 1989 and 1990 toxics cleanup amounts, contingent on its submission of a plan for investigation and program development, consistent with the preceding text.

33. It is reasonable to disallow $0.6 million employee store losses together with inventory reduction of $253,000 for 1985 and $449,000 for 1986 for ratemaking purposes.

34. It is reasonable to refund unclaimed PCA refunds, including interest, to ratepayers in one test year billing cycle.

35. Ratemaking adjustments for institutional advertising items of National Prorates, "Image," "Public Information," "NFL Sports," and "Indy 500" totalling $10.3 million for the year 1986 are not necessarily appropriate for adjustments for test year 1988.

36. It is reasonable to disallow $5.7 million commercial and marketing expense and $0.3 million operating rent expense for test year 1988 for one-time programs.

37. It is reasonable to adjust General Office and Other Operating expenses by $2.7691 million for 1985 and $3.425 million for 1986.

38. General's decision to invest in a new administration building in Thousand Oaks is not imprudent.

39. It is reasonable to include $4,485,000 a year as miscellaneous revenue representing the difference between the gain from the sale of property and the cost of relocation amortized over

29. It is reasonable to amortize the costs of improvements in property prior to occupancy over a three-year period.

30. Interest during construction should not be allowed on land.

31. General has failed to justify $2.362 million toxics cleanup request but the record indicates some future costs will be incurred, and as a matter of judgment we adopt $353,000 as reasonable for test year 1988.

32. Given the scanty record, and the 1988 test year allowance, it is appropriate to allow General to file an application seeking recovery of 1989 and 1990 toxics cleanup amounts, contingent on its submission of a plan for investigation and program development, consistent with the preceding text.

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36. It is reasonable to adjust General Office and Other Operating expenses by $2.7691 million for 1985 and $3.425 million for 1986.

37. General's decision to invest in a new administration building in Thousand Oaks is not imprudent.

38. It is reasonable to include $4,485,000 a year as miscellaneous revenue representing the difference between the gain from the sale of property and the cost of relocation amortized over a three-year period; the relocation cost offset is appropriate in

29. It is reasonable to amortize the costs of improvements in property prior to occupancy over a three-year period.

30. Interest during construction should not be allowed on land.

31. General has failed to justify $2.362 million toxics cleanup request but the record indicates some future costs will be incurred, and as a matter of judgment we adopt $353,000 as reasonable for test year 1988.

32. Given the scanty record, and the 1988 test year allowance, it is appropriate to allow General to file an application seeking recovery of 1989 and 1990 toxics cleanup amounts, contingent on its submission of a plan for investigation and program development, consistent with the preceding text.

33. It is reasonable to disallow $0.6 million employee store losses together with inventory reduction of $253,000 for 1985 and $449,000 for 1986 for ratemaking purposes.

34. Ratemaking adjustments for institutional advertising items of National Prorates, "Image," "Public Information," "NFL Sports," and "Indy 500" totalling $10.3 million for the year 1986 are not necessarily appropriate for adjustments for test year 1988.

35. It is reasonable to disallow $5.7 million commercial and marketing expense and $0.3 million operating rent expense for test year 1988 for one-time programs.

36. It is reasonable to adjust General Office and Other Operating expenses by $2.930 million for 1985 and $3.843 million for 1986.

37. General's decision to invest in a new administration building in Thousand Oaks is not imprudent.

38. It is reasonable to include $4,485,000 a year as miscellaneous revenue representing the difference between the gain from the sale of property and the cost of relocation amortized over a three-year period; the relocation cost offset is appropriate in

a three-year period; the relocation cost offset is appropriate in this specific instance, since this was not a stand-alone sale of property, but a unified transaction.

40. The adopted estimates, previously discussed, of revenues, operating expenses and rate base for test year 1988 as summarized on the tabulation in Section V.N of this decision reasonably indicate General's operations in the future.

41. It is reasonable to require General to prepare a cost/benefit analyses of advertising campaign to justify advertising expenses for ratemaking purposes.

42. DRA's total factor productivity study raises concerns which need to be resolved before the study can be used for establishing productivity levels.

43. Labor costs computed on the number of employees is not variable within a monthly period, and consequently the entire cost function model is misspecified.

44. DRA's failure to adequately measure the capital quality would not in itself cause us to fault the results of the study.

45. The productivity gains indicated by DRA's total factor productivity study are excessively high.

46. D.85-06-113 dated June 12, 1985 directs AT&T-C to flow through any reduction in its access expense stemming from reductions in local exchange utilities' access charges to its customers.

<u>Conclusions of Law</u>

1. The Commission concludes that an incremental revenue reduction of $216.481 million in addition to the $112.190 million reduction ordered by D.87-12-070 for a total of $328.671 million is appropriate.

2. The revenue reductions authorized in Appendix A are just and reasonable.

3. A competitive analysis to ascertain whether GTEDS is the appropriate party to perform General's data processing and

information services should be performed by General prior to its next rate case filing and the results of the analysis and supporting work papers should be included in the filing.

4. General should be required to establish referral guidelines to track successful and unsuccessful referrals to GTEL and perform a study to be completed within six months of the effective date of the decision, to determine the cost plus 10% markup for each referral made to GTEL.

5. General should be required to conduct a market-based pricing study to determine market rates for services it provides to GTEL.

6. Savings in excess of a 5% attrition year labor factor adjustment should be shared equally by ratepayers and General.

7. Since the actual productivity factor will not be known until after the end of the attrition year, General should be required to implement the productivity savings on or before January 31 of the year following the attrition year.

8. In future rate cases General should present cost/benefit analyses to justify advertising campaign expenses for ratemaking purposes.

9. DRA's total factor productivity study cannot be used for any interpretative purposes including the measurement of technical change.

10. General should make an advice letter filing on or before October 1, 1988, setting forth an appropriate operational attrition allowance for the year 1989, and should file an application for 1989 financial attrition on July 15, 1988, in accordance with D.88-06-024.

11. General is now well into the 1988 test year and since the rate reductions are substantial, this order should be effective today.

General's billing system to reflect the necessary route revisions provided we impose a 90-day implementation period and require Pacific and General to provide written notice to those customers who will be impacted by the changes within 30 days prior to the implementation of such changes.

<u>Conclusions of Law</u>

1. The Commission concludes that an incremental revenue reduction of $223.116 million in addition to the $112.190 million reduction ordered by D.87-12-070 for a total of $335.306 million is appropriate.

2. The revenue reductions authorized in Appendix A are just and reasonable.

3. A competitive analysis to ascertain whether GTEDS is the appropriate party to perform General's data processing and information services should be performed by General prior to its next rate case filing and the results of the analysis and supporting work papers should be included in the filing.

4. General should be required to establish referral guidelines to track successful and unsuccessful referrals to GTEL and perform a study to be completed within six months of the effective date of the decision, to determine the cost plus 10% markup for each referral made to GTEL.

5. General should be required to conduct a market-based pricing study to determine market rates for services it provides to GTEL.

6. Savings in excess of a 5% attrition year labor factor adjustment should be shared equally by ratepayers and General.

7. Since the actual productivity factor will not be known until after the end of the attrition year, General should be required to implement the productivity savings on or before January 31 of the year following the attrition year.

General's billing system to reflect the necessary route revisions provided we impose a 90-day implementation period and require Pacific and General to provide written notice to those customers who will be impacted by the changes within 30 days prior to the implementation of such changes.

Conclusions of Law

1. The Commission concludes that an incremental revenue reduction of $219.506 million in addition to the $112.190 million reduction ordered by D.87-12-070 for a total of $331.696 million is appropriate.

2. The revenue reductions authorized in Appendix A are just and reasonable.

3. A competitive analysis to ascertain whether GTEDS is the appropriate party to perform General's data processing and information services should be performed by General prior to its next rate case filing and the results of the analysis and supporting work papers should be included in the filing.

4. General should be required to establish referral guidelines to track successful and unsuccessful referrals to GTEL and perform a study to be completed within six months of the effective date of the decision, to determine the cost plus 10% markup for each referral made to GTEL.

5. General should be required to conduct a market-based pricing study to determine market rates for services it provides to GTEL.

6. Savings in excess of a 5% attrition year labor factor adjustment should be shared equally by ratepayers and General.

7. Since the actual productivity factor will not be known until after the end of the attrition year, General should be required to implement the productivity savings on or before January 31 of the year following the attrition year.

SECOND INTERIM ORDER

IT IS ORDERED that:

1. Five days after the effective date of this order, GTE California (General) shall file revised Schedule Cal. P.U.C. No. A-38 to reflect the revisions shown in Appendix A of this decision. Such filing shall comply with the General Order 96 series. The effective date of the revised schedules shall be 5 days after the date of filing. Revised schedules shall apply only to service rendered on or after the effective date.

2. In accordance with D.88-06-024, on or before October 1, 1988, General shall make an advice letter filing setting forth an appropriate operational attrition allowance for the year 1989. In accordance with that same decision General shall file its application for 1989 financial attrition on July 15, 1988. General's operational attrition advice letter filing shall provide for savings resulting from productivity in excess of 5% to be shared equally between ratepayers and stockholders. Both filings shall be served on all parties to this proceeding.

3. General shall conduct a competitive analysis prior to its next rate filing and include the work papers with the filing to support continued affiliated transactions relating to data processing and informational service between it and GTEDS.

4. Within 60 days of the effective date of this order, General shall establish referral guidelines to track successful and unsuccessful referrals to GTEL.

5. Within 6 months of the effective date of this order, General shall submit a study of the cost plus 10% markup for each referral made to GTEL and thereafter bill GTEL the cost plus 10% markup for all referrals near the market value of successful referrals.

6. Within 6 months of the effective date of this order, General shall submit a market-based pricing study determining the

market rates for service it provides to GTEL. Until further CPUC action on the matter, General shall bill GTEL at its fully allocated cost including return on investment.

7. In future rate proceedings, if General wants to recover advertising expense in connection with campaigns to promote usage or new services, it shall present in its direct showing a cost/benefit analysis of such campaigns over the latest available 12-month recorded period as well as its pro proma analysis of proposed future campaigns. Likewise, if General seeks to recover marketing expense (Account 643), it shall present the same types of analysis as required above for advertising expenditures.

8. Five days after the effective date of this order, General shall make an advice letter filing to revise Schedule Cal. P.U.C. No. A-38 to reflect revisions to customer billing surcharge refunding the remaining Protective Connecting Arrangement unclaimed refunds of $1.58 million plus interest of $660,000 to ratepayers in one test year 1988 billing cycle. Such filing shall comply with the General Order series. The effective date of the revised schedules shall be 5 days after the date of filing. Revised schedules shall apply only to service rendered on or after the effective date.

9. General shall refund the remaining PCA unclaimed refunds of $1.58 million plus interest of $660,000 to ratepayers in one test year 1988 billing cycle.

10. Within five days from the effective date of this decision, General shall establish a balancing account into which it shall book the difference between currently authorized rates and rates it would be collecting if it revised its accounting for refinancings to follow the net of tax method. The balancing account amounts shall be subject to refund, in whole or in part, following hearings to determine (1) whether General ought to be ordered permanently to revise its accounting of bond refinancing premiums, and unamortized discounts and expenses, and (2) what

method General may use to do so. A Prehearing Conference will be held to set hearing dates and dates for submission of testimony in connection with this issue.

11. If General wishes to seek recovery for additional toxic waste cleanup expenses, in accordance with the preceding discussion in this decision, it shall include in any such request a plan for investigation and program development over a five-year time horizon, as well as a detailed budget and project description relative to the expenses for which it seeks rate recovery.

12. Within 14 days after General makes its advice letter filing to reduce access charges in accordance with this decision, AT&T-C shall file an advice letter with this Commission under the terms of GO 96-A, which proposes accumulating the reduced access charge expense resulting from this decision in a memorandum account, with interest, commencing on the effective date of the General tariff revision and running through December 31, 1988 at which time AT&T-C shall roll this accumulated reduced expense into its computation of the effects on access rates of the SPF to SLU phase down of the local exchange carriers which will be reflected in AT&T-C's rates.

This order is effective today.

Dated ____________________, at San Francisco, California.

cost/benefit analysis of such campaigns over the latest available 12-month recorded period as well as its pro proma analysis of proposed future campaigns. Likewise, if General seeks to recover marketing expense (Account 643), it shall present the same types of analysis as required above for advertising expenditures.

8. Within five days from the effective date of this decision, General shall establish a balancing account into which it shall book the difference between currently authorized rates and rates it would be collecting if it revised its accounting for refinancings to follow the net of tax method. The balancing account amounts shall be subject to refund, in whole or in part, following hearings to determine (1) whether General ought to be ordered permanently to revise its accounting of bond refinancing premiums, and unamortized discounts and expenses, and (2) what method General may use to do so. A Prehearing Conference will be held to set hearing dates and dates for submission of testimony in connection with this issue.

9. If General wishes to seek recovery for additional toxic waste cleanup expenses, in accordance with the preceding discussion in this decision, it shall include in any such request a plan for investigation and program development over a five-year time horizon, as well as a detailed budget and project description relative to the expenses for which it seeks rate recovery.

10. Within 14 days after General makes its advice letter filing to reduce access charges in accordance with this decision, AT&T-C shall file an advice letter with this Commission under the terms of GO 96-A, which proposes accumulating the reduced access charge expense resulting from this decision in a memorandum account, with interest, commencing on the effective date of the General tariff revision and running through December 31, 1988 at which time AT&T-C shall roll this accumulated reduced expense into its computation of the effects on access rates of the SPF to SLU

phase down of the local exchange carriers which will be reflected in AT&T-C's rates.

11. To be effective not less than 90 days after the effective date of this order, General and Pacific are authorized to:

a. Move the rate center coordinates for the Etiwanda exchange in order that the route between the Ontario exchange and the Etiwanda exchange becomes a local route.

b. Establish the route between the Etiwanda exchange and the Rialto exchange with Pacific as a ZUM Zone 2 route.

c. Revise the billing system to reflect the tariff revisions set forth in Appendix 1-F of Exhibit 230. Both General and Pacific shall provide written notice to their customers who will be impacted by the change within 30 days prior to the implementation of the change.

12. Within 20 days of the effective date of this decision, General shall file an advice letter in conformance with GO 96-A reflecting a reduction to its revenue requirement to account for the effects of interest synchronization for 1987. This advice letter shall also reflect interest at the three-month commercial paper rate for 1987, beginning January 1, 1987 to the effective date of the tariff revision hereafter discussed. The filing shall be based on 1986 adopted attrition results of operations and the 1987 adopted financial attrition. Consistent with D.87-12-067, General shall not adjust unamortized ITC to reflect the impacts of remand. The interest synchronization effect for 1987 shall be reflected as a bill and keep surcredit based on 1987 adopted billing base, the amount to be amortized through December 31, 1988. The bill and keep surcredit shall be effective October 1, 1988, and shall apply to services rendered on and after the effective date of the tariff.

remand. The interest synchronization effect for 1987 shall be reflected as a bill and keep surcredit based on 1987 adopted billing base, the amount to be amortized through December 31, 1988. The bill and keep surcredit shall be effective October 1, 1988, and shall apply to services rendered on and after the effective date of the tariff.

This order is effective today.

Dated ___________________, at San Francisco, California.

APPENDIX A
Sheet 1 of 1

SCHEDULE CAL. P.U.C. NO. A-38
BILLING ADJUSTMENT

The following revisions are ordered:

Rates	Monthly Percentage Increment
Adjustment Factor	(13.75%) *
Adjustment Factor	(13.75%) **
Adjustment Factor	(13.75%) ***

* The monthly percentage factor applies to all services provided under Tariff Schedule C-1, Facilities for Intrastate Access.

** The monthly percentage factor applies to all recurring and nonrecurring rates and charges for service or equipment provided under all of the Utility's Tariff Schedules except the following:

The present list of excepted services shall remain unchanged.

*** The monthly percentage factor applies to all intraLATA toll and toll private line services.

GTC CALIFORNIA
California Corporation Franchise Tax
Test Year 1988
($000)

Operating Revenues	$2,624,408
Operating Expenses	1,132,077
Taxes On Other Than Income	105,556
Subtotal	1,237,633
Net Before Adds & Deducts	1,386,775
Net Deductions from Taxable Income	
State Tax Depreciation	421,580
Fixed Charges	138,777
Pensions & Benefit Capitalized	43,727
Use Tax Capitalized	6,929
Payroll Taxes Capitalized	14,626
Cost of Removal	22,835
Subtotal of Deductions	648,474
Net State Taxable Income	738,301
CCFT @ 9.3%	$68,662

APPENDIX C

GTC CALIFORNIA
Federal Income Tax
Test Year 1988
($000)

Operating Revenues	$2,624,408
Operating Expenses	1,132,077
Taxes On Other Than Income	105,556
State Income Tax	68,662
Subtotal	1,306,295
Net Before Adds & Deducts	1,318,113
Net Deductions from Taxable Income	
Federal Tax Depreciation	467,017
Deferred Tax Reversal	73,538
Fixed Charges	148,051
Construction Period Taxes	(3,633)
Reserve for Uncollectibles	(1,850)
Dividend Paid Credit	77
Subtotal of Deductions	683,200
Net Federal Taxable Income	634,913
FIT @ 34%	215,871
Adjustment:	
ITC Amortization	(31,136)
Net FIT	$184,735

APPENDIX D

GTC CALIFORNIA
Adopted Separated Summary of Earnings
Test Year 1988
($000)

		Total Company	Inter-State	IntraState Total	IntraState Access	IntraState IntraLATA Total	IntraState IntraLATA MTT	IntraState IntraLATA PL	IntraState Exchange
		(a)	(b)	(c)=(a-b)	(d)	(e)=(f+g)	(f)	(g)	(h)=(c-d-e)
	OPERATING REVENUES								
1	Local Revenues	780,686	0	780,686	0	0	0	0	780,686
	Intrastate								
2	Access Revenues	206,526	0	206,526	206,526	0	0	0	0
3	Toll Revenues	817,213	0	817,213	0	817,213	782,231	34,982	0
4	Interstate Access Revenues	480,425	480,425	0	0	0	0	0	0
5	Miscellaneous Revenues	281,981	23,819	258,162	26,675	0	0	0	231,487
6	Surcharge Revenues	74,730	0	74,730	(6,903)	29,388	28,719	669	52,245
	Gain on Sale of Properties	4,485	846	3,639	425	1,317	1,183	134	1,897
7	Other Miscellaneous	0	0	0	0	0	0	0	0
8	LESS: Uncollectibles	21,638	1,200	20,438	0	7,960	7,779	181	12,478
9	Total	2,624,408	503,890	2,120,518	226,723	839,958	804,354	35,604	1,053,837
	OPERATINS EXPENSES								
10	Maintenance	431,330	94,556	336,774	43,974	118,224	103,377	14,847	174,576
	Traffic	64,683	6,950	57,733	1,985	27,594	27,429	165	28,154
	Commercial	257,207	44,382	212,825	13,365	28,231	27,190	1,041	171,229
13	General Office Sal. & Exp.	188,782	29,334	159,448	20,621	57,552	54,260	3,292	81,275
14	Other Operating Expenses	190,075	34,662	155,413	16,712	49,209	45,137	4,072	89,492
15	Subtotal	1,132,077	209,884	922,193	96,657	280,810	257,393	23,417	544,726
16	Depreciation	519,807	95,723	424,084	55,952	145,900	128,245	17,655	222,232
17	Taxes Other than on Income	105,556	21,877	83,679	10,111	28,291	25,048	3,243	45,277
18	State Income Tax	68,662	11,167	57,495	3,979	26,814	27,842	(1,028)	26,702
19	Federal Income Tax	184,735	35,080	149,655	11,310	94,801	100,655	(5,854)	43,544
20	Total	2,010,837	373,731	1,637,106	178,009	576,616	539,183	37,433	882,481
21	Net Revenues	613,571	130,159	483,412	48,714	263,342	265,171	(1,829)	171,356
	RATE BASE								
22	100.1 - Tel Plt in Serv	6,593,041	1,374,252	5,218,789	677,937	1,825,603	1,585,884	239,719	2,715,249
23	100.2 - Tel Plt under Const.	0	0	0	0	0	0	0	0
24	100.3 - Prop Held for Future Use	79	17	62	8	22	19	3	32
25	Materials & Supplies 122	21,977	5,387	16,590	2,169	5,833	5,092	741	8,588
26	Working Cash	18,428	3,417	15,011	1,573	4,571	4,190	381	8,867
27	LESS: Depreciation Reserve	2,001,576	413,149	1,588,427	208,392	544,137	465,254	78,883	835,898
28	LESS: Deferred Tax	673,362	141,022	532,340	68,966	185,013	161,082	23,931	278,361
	Total	3,958,587	828,902	3,129,685	404,329	1,106,879	968,849	138,030	1,618,477
30	RATE OF RETURN	15.50%	15.70%	15.45%	12.05%	23.79%	27.37%	-1.33%	10.59%

APPENDIX A
Sheet 1 of 1

SCHEDULE CAL. P.U.C. NO. A-38
BILLING ADJUSTMENT

The following revisions are ordered:

Rates	Monthly Percentage Increment
Adjustment Factor	(13.34%) *
Adjustment Factor	(13.34%) **
Adjustment Factor	(13.34%) ***

* The monthly percentage factor applies to all services provided under Tariff Schedule C-1, Facilities for Intrastate Access.

** The monthly percentage factor applies to all recurring and nonrecurring rates and charges for service or equipment provided under all of the Utility's Tariff Schedules except the following:

The present list of excepted services shall remain unchanged.

*** The monthly percentage factor applies to all intraLATA toll and toll private line services.

(END OF APPENDIX A)

APPENDIX A
Sheet 1 of 1

SCHEDULE CAL. P.U.C. NO. A-38
BILLING ADJUSTMENT

The following revisions are ordered:

Rates	Monthly Percentage Increment
Adjustment Factor	(13.52%) *
Adjustment Factor	(13.52%) **
Adjustment Factor	(13.52%) ***

* The monthly percentage factor applies to all services provided under Tariff Schedule C-1, Facilities for Intrastate Access.

** The monthly percentage factor applies to all recurring and nonrecurring rates and charges for service or equipment provided under all of the Utility's Tariff Schedules except the following:

The present list of excepted services shall remain unchanged.

*** The monthly percentage factor applies to all intraLATA toll and toll private line services.

GTC CALIFORNIA
California Corporation Franchise Tax
Test Year 1988
($000)

Operating Revenues	$2,630,035
Operating Expenses	1,133,523
Taxes On Other Than Income	106,135
Subtotal	1,239,658
Net Before Adds & Deducts	1,390,377
Net Deductions from Taxable Income	
State Tax Depreciation	425,372
Fixed Charges	140,199
Pensions & Benefit Capitalized	44,146
Use Tax Capitalized	6,929
Payroll Taxes Capitalized	14,626
Cost of Removal	22,835
Subtotal of Deductions	654,107
Net State Taxable Income	736,270
CCFT @ 9.3%	$68,473

GTC CALIFORNIA
Federal Income Tax
Test Year 1988
($000)

Operating Revenues	$2,630,035
Operating Expenses	1,133,523
Taxes On Other Than Income	106,135
State Income Tax	68,473
Subtotal	1,308,131
Net Before Adds & Deducts	1,321,904
Net Deductions from Taxable Income	
Federal Tax Depreciation	471,218
Deferred Tax Reversal	73,538
Fixed Charges	150,014
Construction Period Taxes	(3,633)
Reserve for Uncollectibles	(1,850)
Dividend Paid Credit	77
Subtotal of Deductions	689,364
Net Federal Taxable Income	632,540
FIT @ 34%	215,064
Adjustment:	
ITC Amortization	(32,952)
Net FIT	$182,112

GTC CALIFORNIA
Adopted Separated Summary of Earnings
Test Year 1988
($000)

		Total Company	Inter-State	IntraState					
				Total	Access	IntraLATA			Exchange
						Total	MTT	PL	
		(a)	(b)	(c)=(a-b)	(d)	(e)=(f+g)	(f)	(g)	(h)=(c-d-e)
	OPERATING REVENUES								
1	Local Revenues	781,134	0	781,134	0	0	0	0	781,134
	Intrastate								
2	Access Revenues	206,526	0	206,526	206,526	0	0	0	0
3	Toll Revenues	822,392	0	822,392	0	822,392	787,351	35,041	0
4	Interstate Access Revenues	480,425	480,425	0	0	0	0	0	0
5	Miscellaneous Revenues	281,981	23,819	258,162	26,675	0	0	0	231,487
6	Surcharge Revenues	74,730	0	74,730	(6,903)	29,388	28,719	669	52,245
	Gain on Sale of Properties	4,485	846	3,639	425	1,317	1,183	134	1,397
7	Other Miscellaneous	0	0	0	0	0	0	0	0
8	LESS: Uncollectibles	21,638	1,200	20,438	0	7,960	7,779	181	12,478
9	Total	2,630,035	503,890	2,126,145	226,723	845,137	809,474	35,663	1,054,285
	OPERATING EXPENSES								
10	Maintenance	431,330	94,556	336,774	43,974	118,224	103,377	14,847	174,576
11	Traffic	64,683	6,950	57,733	1,985	27,594	27,429	165	28,154
12	Commercial	257,207	44,382	212,825	13,365	28,231	27,190	1,041	171,229
13	General Office Sal. & Exp.	188,847	29,347	159,500	20,627	57,570	54,276	3,294	81,303
14	Other Operating Expenses	191,456	34,936	156,520	16,830	49,566	45,463	4,103	90,124
15	Subtotal	1,133,523	210,171	923,352	96,781	281,185	257,735	23,450	545,386
16	Depreciation	524,494	96,494	428,000	56,468	147,259	129,442	17,817	224,273
17	Taxes Other than on Income	106,135	22,000	84,135	10,171	28,450	25,186	3,264	45,514
18	State Income Tax	68,473	11,050	57,423	3,919	27,046	28,091	(1,045)	26,455
19	Federal Income Tax	182,112	34,571	147,541	11,046	95,703	101,622	(5,919)	40,792
20	Total	2,014,737	374,286	1,640,451	178,365	579,645	542,076	37,569	882,421
21	Net Revenues	615,298	129,604	485,694	48,358	265,492	267,398	(1,906)	171,864
	RATE BASE								
22	100.1 - Tel Plt in Serv	6,652,276	1,385,519	5,266,757	684,170	1,842,591	1,600,648	241,943	2,739,996
23	100.2 - Tel Plt under Const.	0	0	0	0	0	0	0	0
24	100.3 - Prop Held for Future Use	79	17	62	8	22	19	3	32
25	Materials & Supplies 122	23,258	5,701	17,557	2,296	6,173	5,389	784	9,088
26	Working Cash	18,788	3,483	15,305	1,604	4,661	4,272	389	9,040
27	LESS: Depreciation Reserve	2,003,920	413,181	1,590,739	208,692	545,010	466,012	78,998	837,037
28	LESS: Deferred Tax	679,418	142,291	537,127	69,586	186,677	162,530	24,147	280,864
29	Total	4,011,063	839,248	3,171,815	409,800	1,121,760	981,786	139,974	1,640,255
30	RATE OF RETURN	15.34%	15.44%	15.31%	11.80%	23.67%	27.24%	-1.36%	10.48%