

Exhibit No.:

Issues:

Data Center, SBC Parent  
Costs, Deregulated  
Revenues/Costs, SMS/800  
Data Base

Witness:

Robert E. Schallenberg

Sponsoring Party:

MoPSC Staff

Case No.:

TC-93-224

**MISSOURI PUBLIC SERVICE COMMISSION**

**UTILITY SERVICES DIVISION**

**DIRECT TESTIMONY**

**OF**

**ROBERT E. SCHALLENGER**

**SOUTHWESTERN BELL TELEPHONE COMPANY**

**CASE NO. TC-93-224**

Jefferson City, Missouri  
February, 1993

**REVISED**

**NP**

**\*\* Denotes Proprietary Information \*\***

Exhibit No. 29  
Date 7/14/93 Case No. TC-93-224  
Reporter SAT

**DIRECT TESTIMONY**  
**OF**  
**ROBERT E. SCHALLENGER**  
**SOUTHWESTERN BELL TELEPHONE COMPANY**  
**CASE NO. TC-93-224**

Q. Please state your name and business address.

A. Robert E. Schallenberg,, P.O. Box 360, Jefferson City, Missouri 65102.

Q. By whom are you employed and in what capacity?

A. I am a Regulatory Auditor with the Missouri Public Service Commission  
(Commission).

Q. Please describe your educational background.

A. I am a 1976 graduate of the University of Missouri at Kansas City with a Bachelor of Science in Business and degree and major emphasis in Accounting. In November, 1976, I successfully completed the Uniform Certified Public Accountant (CPA) examination and subsequently received the CPA certificate. In 1989, I received my CPA license in Missouri. I began my employment with the Missouri Public Service Commission as a Public Utility Accountant in November of 1976. I remained on the Staff of the Missouri Commission until May of 1978, when I accepted the position of Senior Regulatory Auditor with the Kansas State Corporation Commission. In October of 1978, I returned to the Staff of the Missouri Commission.

**Direct Testimony of  
Robert E. Schallenberg**

1           Q.     With reference to this case, have you made an investigation or study of  
2     the books and records of Southwestern Bell Telephone Company - Missouri Division  
3     (SWBT, SWBT-MO or Company)?

4           A.     Yes, I have, with the assistance of other members of the Commission  
5     Staff (Staff).

6           Q.     Have you ever testified before this Commission?

7           A.     Yes, I have. Please refer to Schedule 1, which is attached to my direct  
8     testimony, for a list of cases in which I have previously filed testimony.

9           Q.     What is the purpose of your direct testimony in this case?

10          A.     The purpose of my direct testimony is to address five items. The first  
11     item I will address is SWBT's new Data Center facility. Second, I will address a  
12     portion of the Staff's findings and recommendations regarding Southwestern Bell  
13     Corporation's (SBC) parent company costs that are included in SWBT-MO's test year  
14     expenses. Next, I will address the Staff's treatment of deregulated revenues and costs  
15     related to SWBT-MO operations. Next, I will describe my initial finding regarding the  
16     Fully Distributed Cost (FDC) Studies that support SWBT's purchases from affiliates.  
17     Finally, I will address the Staff's adjustment to increase expenses related to the Service  
18     Management System 800 (SMS/800) data base.

19     Data Center

20          Q.     Why did you examine SWBT's new Data Center?

21          Q.     The Company identified in its response to Staff Data Request No. 148  
22     that its new Data Center was a significant new item or significant change to normal

Direct Testimony of  
Robert E. Schallenberg

operations that SWBT considers that has taken place subsequent to the Staff's test year of calendar year 1991.

Q. What is the Data Center?

A. SWBT has constructed a new computing and data processing facility in downtown St. Louis. The current SWBT-MO and Corporate data processing operations are housed in the Thomas Jefferson and International Fur Exchange Buildings located at 14 South 4th Street in downtown St. Louis.

Q. When will the 14 South 4th Street Data Center employees move into the new Data Center?

A. The move began in 1992 and will be completed in February, 1993.  
(Response to Staff Data Request No. 934)

Q. What was the cost of the Data Center?

A. The Data Center cost \$154,391,204 as of September 30, 1992. The Data Center increases SWBT-MO investment base by \$152,126,204, representing the total Data Center investment at September 30, 1992. The amount is determined from the following breakdown:

Plant in Service	\$ 154,391,204
Depreciation Reserve	(1,693,536)
Deferred Income Tax Reserve	(571,634)
	<hr/>
	\$ 152,126,034
	<hr/>

(Response to Staff Data Request No. 674)

**Direct Testimony of  
Robert E. Schallenberg**

1 SWBT-MO is assigned an allocated share of the above investment. The current  
2 January 1, 1993), compensation study, which is addressed in the direct testimony of  
3 Stephen F. Doeri, assigns 39.09% or \$59.5 million of the Data Center's rate base cost  
4 to SWBT-MO. (Response to Staff Data Request No. 702)

5 Q. Was the decision to build a new Data Center based on an economic  
6 rationale?

7 A. No. The only study performed indicated that building a new data center  
8 was uneconomic. In Case No. TC-89-14, et al., (Case No. TC-89-14), the Company  
9 indicated that this study was no longer applicable. (Rebuttal Testimony of Company  
10 witness Cynthia Browne, Case No. TC-89-14) SWBT indicated that since the time of  
11 that study, computer operations have expanded and continue to do so that SWBT was  
12 projected to outgrow its existing facility at 14 South 4th Street by 1991-1992.  
13 According to SWBT, relocation to a new facility is now the only viable alternative to  
14 maintaining effective and efficient data center operations.

15 Q. What are the problems related to the new Data Center as it relates to  
16 this case?

17 A. While the completion of the Data Center is a known event, its revenue  
18 requirement impact is not measurable at this time. The Company was unable to  
19 identify the SWBT-MO % of most of the work groups that are moving into the new  
20 Data Center. (Response to Staff Data Request No. \_\_\_\_ ) SWBT identified that the  
21 16 employees moving to the new Data Center from leased space at the 915 Olive  
22 downtown St. Louis facility presently charge approximately 12% of their time to

Direct Testimony of  
Robert E. Schallenberg

1 SWBT-MO. (Response to Staff Data Request No. \_\_\_\_ ) Even though the St. Louis  
2 based work groups will be moved into the new Data Center by March 1, 1993,  
3 additional work groups will be moving into the new Data Center in mid-1993.  
4 (Response to Staff Data Request No. \_\_\_\_ ) Given the lack of information, I have used  
5 16% as the Missouri allocator for the new Data Center in the Staff's initial filing in  
6 this complaint case. 16% represents the approximate General Headquarters prorate  
7 factor for Missouri. I will continue to examine future data and will modify this  
8 percentage as warranted by any new information received subsequent to this filing.

9 Q. Did the Staff make any adjustment to expense related to the new Data  
10 Center?

11 A. No, with the exception of depreciation and property taxes. As  
12 previously discussed, the ongoing level of Data Center expenses is not known and  
13 measurable at this time. However, it should be noted that the test year expenses  
14 include the expenses related to the 14 South 4th Street facility, as well as lease cost  
15 related to previously used leased space. Therefore, these expenses will offset to some  
16 undeterminable amount any new Data Center expenses. I will continue to examine  
17 future data related to Data Center expenses and will make an expense adjustment if  
18 warranted by new information.

19 Southwestern Bell Corporation (SBC) Parent Costs

20 Q. What was your responsibility in relation to SBC parent company costs?

21 A. Staff witness Kelly J. Riley and I examined the parent company costs  
22 charged to SWBT. I am responsible for three areas related to parent company costs

**Direct Testimony of  
Robert E. Schallenberg**

1 charged to SWBT. First, I am responsible for the overall findings made regarding  
2 parent costs charged to SWBT. Second, I was responsible for the development of an  
3 appropriate allocation for the fixed cost functions performed at SBC. Finally, I am  
4 responsible for identifying and supporting the disallowance of SBC parent costs  
5 charged to SWBT that should not be included in SWBT-MO's cost of service.

6 Q. What are SBC parent costs?

7 A. This item is addressed in the direct testimony of Staff witness Riley.  
8 SBC is the corporate parent of SWBT. SBC incurs certain costs which are shown in  
9 Mr. Riley's Schedules 2 and 3. In addition to these costs, SBC incurred the following  
10 costs which were not reflected in its cost allocation system (CAS) in 1991:

11	Entertainment	\$ 114,938
12	Miscellaneous	\$ 4,887
13	Contributions	\$1,238,314
14	Foundation Funding	\$1,400,000
15	Interest Expense	\$ 31,160

16 These costs are retained at SBC and not charged to any subsidiary. (Response to Staff  
17 Data Request No. 589)

18 SBC uses its CAS to charge directly and/or allocate a portion of its costs to its  
19 subsidiaries. Schedule 1 shows the amount of costs that SBC charged to each of its  
20 subsidiaries in 1991. This Schedule shows the amount of direct cost as well as the  
21 allocated cost for each subsidiary. Mr. Riley discusses the CAS in his direct

**Direct Testimony of  
Robert E. Schallenberg**

1 testimony. SBC does retain a portion of its costs. These costs are not charged to any  
2 subsidiary and are offset against SBC's income, which is primarily dividends received  
3 from the subsidiaries.

4 The SBC costs charged to SWBT are, in effect, an affiliated purchase by  
5 SWBT. These costs represent a significant affiliated transaction. The amount of  
6 affiliated purchases in total for SWBT-MO and the SBC cost portion of these  
7 purchases for SWBT-MO for the period 1989-1991 are as follows:

	<u>Total Affiliated Purchases</u>	<u>SBC Costs</u>	<u>% SBC Costs of Affiliated Purchases</u>
9 1989	\$56,318,137	\$22,680,202	40%
10 1990	\$54,133,894	\$18,458,037	34%
11 1991	\$54,330,457	\$16,433,502	30%

12  
13 (Response to Staff Data Request No. 222)

14 During 1989-1991, the total affiliated purchases have been relatively stable while the  
15 SBC costs charged to SWBT-MO have declined. SBC is the second largest source of  
16 affiliated purchases for SWBT-MO. Schedule 2 shows the SBC charges to SWBT-MO  
17 by account in 1991. Schedule 3 shows the relationship of the SBC cost centers to the  
18 accounts shown on Schedule 2. Bellcore is the only affiliated source that exceeds the  
19 SBC costs charged to SWBT-MO. Therefore, while the SBC costs are declining, they  
20 still represent a significant cost to SWBT-MO.

21 Q. Does a contract between SWBT and SBC exist that defines the services  
22 to be provided?



**Direct Testimony of  
Robert E. Schallenberg**

1           A.    No. The Company provided the following explanation regarding the  
2 SBC/SWBT relationship in its response to Staff Data Request No. 145:

3           The services provided to Southwestern Bell Telephone Company  
4 (SWBT) from Southwestern Bell Corporation (SBC) are not defined by  
5 a contract. These services are performed by SBC under the normal  
6 parent/subsidiary relationship.  
7

8           The SBC affiliate transactions comply with the Federal Communication  
9 Commission's (FCC) affiliate transactions rules expressed in its Report  
10 and Order in CC Docket No. 86-111 and incorporated into Parts 32 and  
11 64 of the FCC's Rules and Regulations. Pursuant to these transaction  
12 rules SWBT developed a Cost Allocation Manual (CAM), subsequently  
13 approved by the FCC, which provided a detailed list of the services  
14 received from SBC by SWBT.

15          The above response shows that the documentation of the SBC/SWBT relationship is  
16 not in a contract, but is reflected in SWBT's Cost Allocation Manual (CAM). The  
17 above response also shows that the FCC affiliate transaction rules apply to the SBC  
18 costs charged to SWBT.

19          Q.    Does SBC operate under any incentives that increase concerns that a  
20 portion of SBC costs charged to SWBT will not be necessary and reasonable?

21          A.    Yes. SBC expenses that are charged and reflected in SWBT's regulated  
22 operations increase SBC overall income and cash flow (Response to Staff Data  
23 Request No. 152). This is caused by the fact that customer rate levels will produce  
24 revenues to cover these costs, thereby eliminating the negative or downward impact  
25 of these parent costs on SBC earnings. SBC costs that are included in earnings  
26 incentive plans would also have a positive impact on SBC earnings. This incentive  
27 in itself does not prove that SBC costs charged to SWBT are unreasonable. Discussing

Direct Testimony of  
Robert E. Schallenberg

1 the existence of this incentive merely points out that SBC can produce increasing  
2 positive impacts on its earnings for every dollar of its costs that it can receive  
3 regulatory consideration by charging to SWBT.

4 Q. Does decreasing SBC charges to SWBT-MO since 1989 show that SBC  
5 is not influenced by the earnings motive to charge more costs to SWBT?

6 A. Not necessarily. The decreasing SBC charges are largely a product of  
7 SBC expansion of its non-regulated subsidiaries and its use of relative size allocators.  
8 The relative size allocators will be discussed later. SWBT's employee downsizing and  
9 the related size allocator also contributes to the decreasing trend. In light of these  
10 factors, it would be extremely difficult for SBC to justify increasing or even  
11 maintaining the same percentage of costs charged to SWBT over time. However, the  
12 earnings incentive would still encourage SBC to use approaches that minimize and/or  
13 retard the rate of declining charges to SWBT.

14 Q. Were these concerns called "cost of service manipulation" in the  
15 previous SWBT complaint case, No. TC-89-14?

16 A. Yes. In my direct testimony in that case, I stated that:

17 "Cost of service manipulation" is an action by an affiliated company or  
18 group of affiliated companies in dealing with a regulated company, or  
19 an action by a regulated company in dealing with an affiliated company  
20 or group of affiliated companies, that increases the cost of service of  
21 the regulated company in order to increase overall corporate profits. In  
22 Southwestern Bell Corporation (SBC), the regulated company is SWBT.  
23 Cost of service manipulation will occur when (1) SWBT provides a  
24 product and/or service to an unregulated affiliate and/or to a deregulated  
25 below-the-line service at less than full market value (contribution  
26 diversion), and/or (2) SWBT buys a product and/or service from an

**Direct Testimony of  
Robert E. Schallenberg**

1           unregulated affiliate and/or buys a deregulated below-the-line service  
2           which is not its best possible alternative (expense padding).

3           The SBC cost issue is an example of item number 2 cited above. The Southwestern  
4           Bell Regulatory Incentive Experiment (SBIRE) agreement used the term "earnings  
5           manipulation" for this situation. A commonly used term in regulation is "cross-  
6           subsidization". I view the three terms to be synonymous.

7           Q.     Has the Commission previously addressed the issue of SBC costs?

8           A.     Yes. In its Report and Order in Case No. TC-89-14, the Commission  
9           determined that both directly charged and allocated SBC costs are appropriate for  
10          inclusion in SWBT-MO's cost of service. Based on that decision, the Staff has  
11          included allocated SBC costs in this case. However, the Commission had noted that  
12          the Staff had conducted no study of the correctness of the allocation method or  
13          reasonableness of any of the involved charges. The scope of the examination in this  
14          audit was to determine or ensure that the allocated SBC costs met three criteria. First,  
15          the cost being allocated to SWBT-MO are for necessary functions (i.e., SWBT or  
16          SWBT-MO would incur these costs on a stand alone basis). Second the costs being  
17          allocated to SWBT-MO are not duplicative of functions performed by SWBT. Third,  
18          the allocation process is reasonable and equitable. Meeting these three criteria should  
19          ensure that SBC costs charged SWBT-MO are reasonable and necessary.

20          Q.     Do the parent costs charged to SWBT in 1991 meet the Staff's three  
21          criteria?

22          A.     No.

**Direct Testimony of  
Robert E. Schallenberg**

1           Q.     What were the specific findings that resulted from your and Mr. Riley's  
2 examination of parent costs charged to SWBT?

3           A.     The following is a list of our findings regarding parent costs charged to  
4 SWBT:

- 5           (1)    SBC's use of an investment/employee allocation factor is  
6 inequitable and unreasonable to SWBT.
- 7           (2)    SBC's investment and employee allocation factor is  
8 inappropriate for certain cost centers.
- 9           (3)    SBC's actions in items 1 and 2 have the impact of overstating  
10 its general allocator, thereby overstating the allocation of certain  
11 common costs.
- 12          (4)    SBC employees are engaging in non-SWBT activities (e.g.,  
13 Telmex) and failing to remove the associated cost from cost  
14 categories allocated to SWBT.
- 15          (5)    The costs related to certain SBC employees and activities are  
16 currently charged to cost centers which are partially allocated to  
17 SWBT. These costs relate to cost centers that are either  
18 retained by the Parent or charged below-the-line by SWBT.
- 19          (6)    SBC's definition of benefit is too broad and results in cost  
20 assignment to SWBT for activities that are either unnecessary  
21 and/or duplicative of SWBT functions.

Direct Testimony of  
Robert E. Schallenberg

(7) SBC has incurred higher than necessary expenditures by choosing an affiliate with a higher bid or not bidding out the service.

There are other concerns that exist regarding parent company costs charged to SWBT. However, these represent the only issues that the Staff is pursuing in this case. These additional concerns, if proven to be problems, will be pursued in the determination of the 1992 and/or 1993 customer credits under SBIRE.

Q. Why is SBC's use of an investment/employee allocation factor inequitable and unreasonable in relation to SWBT?

A. The investment and employee allocation factors are discussed in Mr. Riley's testimony. These allocation factors are applied to SBC's costs that do not reflect either a cost causative or cost benefit relationship. The following SBC activities are allocated to SWBT based on either the investment or employee factor:

<u>Average Investment Factor</u>		<u>Average Employee Factor</u>	
(011)	Shareowner Services	(026)	Pension Asset Administration
(012)	Annual Meetings for Shareowners	(027)	Savings Plan Administration
(014)	Compliance with Securities Law and Exchange Requirements	(028)	Employee Training and Development
(015)	Investor Relations	(029)	Compensation Planning and Administration
(016)	Earnings Requirements	(030)	Benefit Planning and Development
(017)	Interface with Securities Rating Agencies	(031)	Human Resource Planning and Staffing

**Direct Testimony of  
Robert E. Schallenberg**

- |   |                                          |                                          |
|---|------------------------------------------|------------------------------------------|
| 1 | (019) External Audit                     | (032) Employee Information               |
| 2 | (020) Corporate Economic Analysis        | (071) Corporate Services - Food Services |
| 3 | (021) Financial Research/Market Analysis | (072) Corporate Services - Automotive    |
| 4 | (061) Cash Management                    | (077) Senior Management Benefit Payments |
| 5 | (068) Financing Projects                 |                                          |

6  
7 The 1991 investment factor and employee factor for SWBT were 79.3% and 87.55%,  
8 respectively. These factors are inappropriate for certain of above cost centers. This  
9 will be further discussed later in this testimony. The investment factor is based on the  
10 ratio of dollars of equity invested in the subsidiaries with any positive retained  
11 earnings. This factor is not related to and is inappropriate for allocating the above cost  
12 centers. For example, the biggest cost center in the investment category is  
13 Shareowners Services. The following description defines the activities related to these  
14 costs:

15       01100 Shareowner Services

16               The purpose of Shareowner Services is to perform functions associated  
17 with:

- 18       -
- 19       - Issuance and transfer of stock;
- 20       - Stock certificate recordkeeping;
- 21       - Disbursement of dividends;
- 22       - Administration of shareowners plans (e.g., DRISPP);
- 23       - Issuance of shareowner newsletters, annual reports, shareowner
- 24       research, etc.;
- 25       - Special shareowner projects (e.g., stock split).

26  
27 (Source: Response to Staff Data Request No. 44)

**Direct Testimony of  
Robert E. Schallenberg**

The above description shows that these costs are caused by the number of shareowners, not the amount of dollars invested. Another example is the Annual Meeting for Shareowners. Below is the description of this cost center:

**01200 Annual Meeting for Shareowners**

This cost center includes all activities related to the annual shareowners' meeting. This includes, but is not limited to, planning and preparing for the meeting and all functions related to the hosting of the meeting. Some examples are:

- Arranging for and renting facilities;
- Providing security for the meeting.

(Source: Response to Staff Data Request No. 44)

The cost of the Annual Meeting for Shareowners is not caused by the dollars of equity invested in a company. This cost will not double if the dollars of equity double.

The use of the investment factor on these types of cost centers is not indicative of the cost causative factors related to these costs. The use of the investment factor is merely a relative size factor. This means that the costs are going to be allocated on the basis of "the bigger you are, the most cost you will be allocated". On a size basis, SWBT will receive most of the cost under this methodology. SBC finances some of its foreign expansion primarily with debt. (Response to Staff Data Request No. 693) For example, SBC financed its \$80 million purchase price of Telmex with \$400 million of debt financing. (Response to Staff Data Request No. 693) Also, SBC finances its United Kingdom Freedom Phone business with roughly \$6 million in debt and \$3 million in equity. (Response to Staff Data Request No. 755) Further, the target debt ratio (i.e., % of debt in capital structure) for SWBT is 42%, while it is

Direct Testimony of  
Robert E. Schallenberg

1       \*\*    \*\* for SBC's International Operations subsidiary (SBIH). The corresponding  
2       equity percentages are 58% for SWBT and \*\*    \*\* for SBIH. (Response to Staff  
3       Data Request No. 692) The equity investment factor leads to SWBT cross-subsidizing  
4       SBC foreign expansion in two ways. First, cost centers allocated by the equity  
5       investment factor will overallocate those cost centers to SWBT in relation to  
6       international expansion equity because \*\*

7               \*\* Second, the above overallocation will in turn overstate the general  
8       allocation factor resulting in additional cost allocation to SWBT.

9               The same problems that exist with the average equity investment factor exist  
10       with the average employee factor. Again, the average employee factor is a relative  
11       size factor and is not indicative of the cost causative factors related to the cost centers.  
12       Each SBC cost center is profiled in Schedule 4. This schedule will discuss the  
13       allocation factor used by SBC and the appropriateness of that factor. In general, the  
14       cost centers that are allocated based on investment or employee factor have costs that  
15       are fixed in nature and would be incurred by any publicly traded company.

16              Q.     Why is the use of the investment/employee size allocators inequitable  
17       to SWBT when applied to costs that are fixed in nature?

18              A.     Normally, the size allocator methodology is justified by the assertion  
19       that the telephone company (i.e., SWBT) is incurring less cost than it would if SWBT  
20       were on a stand alone basis. For example, SWBT is paying approximately 20% (100%  
21       - 79.3%) less for the annual meeting for shareowners than it would on a stand alone  
22       basis. Also, SWBT is paying approximately 13% (100% - 87.55%) less for pension



Direct Testimony of  
Robert E. Schallenberg

1 plan administration than it would on a stand alone basis. In other words, it might be  
2 claimed that SWBT is receiving a 20% and 13% discount for the costs of the annual  
3 shareowner meeting and pension plan administration, respectively.

4 The inequity in the methodology is shown when one examines these same cost  
5 centers from the perspective of SBC's other subsidiaries. For example, the 1991  
6 investment and employee factors of SBC's Mobile subsidiary is \*\* \*\* and  
7 \*\* \*\*, respectively. Therefore, Mobile is receiving an \*\* \*\* and \*\* \*\*  
8 discount for the costs of the annual shareowners meetings and pension plan  
9 administration, respectively. The cause for Mobile receiving these substantially greater  
10 discounts than SWBT is because of the use of relative size allocators for costs that are  
11 fixed in nature and applicable to any stand alone company.

12 Q. Do you have any recommendations on how to correct this inequity?

13 A. Yes. These costs should be allocated to each SBC subsidiary, based on  
14 the number of subsidiaries, or a "business unit" approach. Under this approach, each  
15 subsidiary would pay less than they would on a stand alone basis. This approach  
16 would allow each subsidiary to share equally in any benefit from centralization.  
17 Further, this approach would prevent SWBT from paying more than the other SBC  
18 subsidiaries for the same service. SBC's present methodology is akin to charging  
19 someone \$30 for a book because they are twice as big as someone else who only pays  
20 \$15 for the same book. Every subsidiary would pay an equal amount for the same  
21 service if these costs are allocated based on the number of subsidiaries.

1  
2  
3  
4  
5  
6  
7  
8  
9  
0  
1  
2  
3  
4  
5  
6  
7  
8  
9  
0  
1

3  
4  
5  
6  
7  
8  
9  
0  
1  
2  
3  
4  
5  
6  
7  
8  
9  
0  
1

7  
8  
9  
0  
1  
2  
3

- 4  
5  
6  
7  
8  
9  
0  
1

73901

- 1

Direct Testimony of  
Robert E. Schallenberg

1 The groups were developed based upon categorizing the eleven companies into the  
2 following groups of activities: 1) parent company operations (e.g., acquisition,  
3 divestment, and investment), 2) the telephone operations, 3) the national non-telephone  
4 company operations and 4) international operations.

5 Q. What SBC cost centers use an inappropriate allocation factor?

6 A. There are 20 cost centers that I feel the use of the investment or  
7 employee factor is inappropriate. The discussion of the cost center procedures is  
8 contained in the cost center profiles shown on Schedule 4.

9 Q. How does SBC overstate its general allocator?

10 A. The general allocator is derived by the ratio of direct charges and costs  
11 allocated with an investment and employee factor. SWBT's share of the SBC direct  
12 charges is approximately 30%. The SWBT's 1991 general allocator is 71.4%. SBC  
13 increases the general allocator by excluding the costs directly charged (retained) to the  
14 Parent Company. This approach understates the costs related to the Parent Company  
15 because the Parent Company does not recognize any of the general overhead costs that  
16 make these activities possible.

17 There are two other major causes that result in overstating the general allocator.  
18 The use of the relative size allocations (e.g., investment/employee factors versus a  
19 business unit approach) will cause the general allocator to be higher because the  
20 investment/employee factors are significantly higher than the business unit ratio.  
21 Second, cost centers that inappropriately use the investment/employee factor will

Direct Testimony of  
Robert E. Schallenberg

1       overstate the general factor because these dollars will increase the weight given to the  
2       investment/employee factor.

3               Q.     What is the basis for your finding that SBC employees are engaging in  
4       non-SWBT activities and failing to remove their costs from cost categories allocated  
5       to SWBT?

6               A.     The Staff received a partial listing of SBC executive meetings involving  
7       use of the Executive Dining Room that took place in 1991. (Response to Staff Data  
8       Request No. 941) These meetings were provided the period January, 1991 to July 31,  
9       1991, for the test year. An examination of these meetings showed SBC employees  
10      attending meetings regarding specific subsidiaries (e.g., Telmex) and charging their  
11      time to cost pools that allocate their time to SWBT. For example, on June 3, 1991,  
12      a meeting regarding Telmex operations took place at the Executive Dining Room on  
13      the 41st Floor of One Bell Center. (Response to Staff Data Request No. 941) The  
14      meeting was attended by the Group President-International Operations, SBC's Vice  
15      Chairman and Chief Financial Officer, and SBC's Senior Executive Vice President and  
16      General Counsel. (Response to Staff Data Request Nos. 941 and 18)

17              The following is a breakdown of what cost centers these individuals charged  
18      their time to during 1991.

<u>Job Title</u>	<u>Time Charged to Cost Center</u>
Group President	100% Subsidiary Support & Projects to Southwestern Bell-International (7515)

**Direct Testimony of  
Robert E. Schallenberg**

1       Vice President & Chief Financial     100% Office of Chairman (3600)  
2       Officer

3       Senior Executive Vice President &   100% Office of Chairman (3600)  
4       General Counsel

5  
6       (Source: Response to Staff Data Request No. 707)

7       SWBT would not receive any costs charged to Subsidiaries Support & Projects to  
8       Southwestern Bell-International (7515). However, SWBT was charged 71.4% of the  
9       costs to the Office of Chairman (3600).

10       Q.     What is the basis for your finding that SBC employees and activities are  
11       charged to cost centers that are allocated to SWBT that relate to cost centers that are  
12       either retained by the Parent Company or charged below the line at SWBT?

13       A.     SWBT does not and has indicated that they continue not to seek rate  
14       recovery of SBC costs related to Legislative Advocacy (5200) and Southwestern Bell  
15       Foundation (6200). However, a review of the Board of Directors Meetings and Board  
16       Committee Meetings Minutes indicate that activity in these areas take place at these  
17       meetings. The SBC Board and/or its Committees consider recommendations, conduct  
18       discussions, and vote on approval on matters concerning political contributions and the  
19       Foundation's strategy and budget. (Response to Staff Data Request No. 66) The  
20       expense of the SBC Board of Director Committee Meetings are charged to the Board  
21       of Directors cost center (3700) and are allocated to the SBC subsidiaries. (Response  
22       to Staff Data Request No. 799) SWBT's share of these expenses is 71.4%. The total  
23       cost of the Board of Directors Cost Center was \$2.2 million in 1991.

**Direct Testimony of  
Robert E. Schallenberg**

1           Q.     What is the basis for your finding that SBC incurs unnecessary expense  
2 levels through its affiliate purchases?

3           A.     The basis for this finding is discussed on Schedule 4 regarding cost  
4 center 1100, Shareholder Services.

5           Q.     What is your basis for the finding that SBC's definition of benefit is too  
6 broad and results in cost assignment to SWBT for activities that are either unnecessary  
7 and/or duplicative of functions already performed by SWBT?

8           A.     The Parent Company considers its management of the entire corporation  
9 and its actions to achieve conformity and standardization between its subsidiaries to  
10 be a benefit to each of the subsidiaries. I disagree with this premise. Each of the  
11 major subsidiaries has a president. This individual is responsible for establishing  
12 direction of their respective company. This is all that is needed on a stand alone basis.  
13 SBC establishes direction for the entire corporation (i.e., what is best for the whole).  
14 However, what is best for the whole corporation may not be and probably is not the  
15 best for each individual subsidiary. For example, SWBT and Mobile will have their  
16 own capital needs that are best for their respective companies. However, SBC may  
17 determine that it needs its capital elsewhere (e.g., foreign expansion) for the  
18 Corporation's long-term interest, so the SWBT and Mobile capital requests are  
19 reduced. Therefore, the Corporation's overall good was not the best result for SWBT  
20 and Mobile. I believe that SBC costs related to overall corporate management and

**Direct Testimony of  
Robert E. Schallenberg**

1 conformity between subsidiaries is duplicative and unnecessary and should be charged  
2 to the parent company.

3 Q. What SBC cost centers represent duplicative and unnecessary cost to  
4 SWBT and its ratepayers?

5 A. There are several SBC cost centers that represent duplicative and  
6 unnecessary cost to SWBT and its ratepayers. These cost centers are as follows:

7 Employee Information

8 Executive Support

9 Office of the Chairman

10 Board of Directors

11 Tax Return Preparation

12 News and Public Information

13 Trademarks, Patents & Graphic Services

14 Cash Management

15 Southwestern Bell Foundation

16 Corporate Services - Food Services

17 Corporate Services - Automotive

18 Corporate Services - Executive Air

19 Senior Management Benefits

20 Corporate Advertising

21 Marketing Support

Direct Testimony of  
Robert E. Schallenberg

SWBT has already indicated that it will not seek recovery of the costs related to the Southwestern Bell Foundation from its Missouri ratepayers (Response to Staff Data Request No. 708, Supplement 1). Therefore, these costs will not be discussed further. The Company has verbally stated that it will not seek recovery of the SBC costs related to Corporate Services - Executive Air. Likewise, this will not be discussed further. The SBC cost center for Corporate Advertising is discussed in the direct testimony of Staff witness John P. Cassidy and removed in his proposed adjustments. The remaining cost centers and the basis for disallowances are discussed in the cost center profiles shown on Schedule 4.

DEREGULATED SERVICES

Q. What adjustments in the Staff's revenue requirement calculation are related to deregulated services?

A. The following adjustments are related to deregulated services:

<u>Adjustment No.</u>	<u>Revenue/Expense Category</u>
S-1-B	Local Service Revenues
S-2-B	IntraLATA Toll Revenues
S-4-C	Other Revenues
S-5-A	Uncollectible Revenue
S-7-O	Central Office
S-8-C	Outside Plant
S-9-B	Testing
S-10-D	Terminal Equipment-Wire Service
S-11-O	Plant Administration and Support



Direct Testimony of  
Robert E. Schallenberg

1	S-12-B	Depreciation and Amortization
2	S-13-R	Marketing
3	S-15-N	Customer Services
4	S-19-P	Information Management
5	S-21-A	Procurement
6	S-22-B	Benefits
7	S-23-U	Other Expenses

8  
9 In addition, I am responsible for the removal of deregulated costs from the Staff's rate  
10 base. The above revenue/expense adjustments are to remove the revenues and  
11 expenses from SWBT-MO's cost of service related to deregulated services.

12 Q. How were these adjustments determined?

13 A. Originally, the adjustments reflected the amounts associated with  
14 deregulated services used to determine the 1991 customer credits. In May, 1992, the  
15 Company stated in response to Staff Data Request No. 30 that the Commission's  
16 surveillance report was revised. One of the revisions was described as follows:

17 Previously, non-regulated revenues and expenses were included in the  
18 intrastate jurisdictional results. Effective with the December 27, 1991  
19 report, the procedures were revised so that non-regulated revenues and  
20 expenses were excluded from intrastate results. The following non-  
21 regulated amounts were excluded in the December 27, 1991 report:

22		
23	Revenues	\$22,893,000
24	Expenses	\$25,717,000
25	Operating Taxes	\$ 1,244,000

26 (Source: Response to Staff Data Request No. 30)

27 The original adjustments were modified to agree with the above amounts.

**Direct Testimony of  
Robert E. Schallenberg**

1           Q.    Is it your intent to remove deregulated investment, revenues and  
2 expenses based upon the SWBT Cost Allocation Manual (CAM)?

3           A.    Yes. There are concerns regarding CAM modifications that result in  
4 increasing costs charged to regulated operations. The appropriateness of these shifts  
5 will be investigated in the determination of the 1992 and 1993 customer credits under  
6 SBIRE.

7  
8                   **FULLY DISTRIBUTED COST (FDC) STUDIES SUPPORTING**  
9                   **SWBT PURCHASES FROM AFFILIATES**

10          Q.    Are the FDC Studies supporting SWBT purchases from affiliates?

11          A.    The FDC Studies supporting SWBT purchases from affiliated companies  
12 is a component of the rules that govern the costing of SWBT's affiliate transactions.  
13 These rules have been discussed in the testimonies of Mr. Riley and Staff consultant  
14 Dr. Michael J. Ileo of Technical Associates, Inc. Generally, SWBT cannot record as  
15 a regulated expense more than the costs shown in the related FDC study from the  
16 affiliated company that provided the service to SWBT. The FDC study serves as a cap  
17 related to the amount of expense SWBT can recover from its ratepayers for services  
18 SWBT buys from an affiliated company. Therefore, the regulatory concern is that the  
19 FDC studies will be flawed and overstate the cost levels SWBT can record.

20          Q.    How did you become involved in the analysis of the FDC studies related  
21 to SWBT purchases from affiliates?

Direct Testimony of  
Robert E. Schallenberg

1           A.     I was asked to evaluate some of the conclusions that are reflected in the  
2 testimony of Dr. Ileo. I submitted Staff Data Request No. 928 as part of my  
3 evaluation. Staff Data Request No. 928 requested "all FDC cost studies and related  
4 data for SWBT's purchases for the period 1991 and 1992". The Company, in its  
5 response, provided several FDC studies and some FDC procedures.

6           Q.     What were your initial findings from your review of these FDC studies  
7 and procedures?

8           A.     The FDC studies and procedures had a design flaw that would overstate  
9 the cost levels determined by the FDC studies. The design flaw is related to the  
10 treatment of Return on Investment (ROI) and interest expense. The studies are taking  
11 the ROI amount and increasing it for income taxes. This increasing process is referred  
12 to as "factoring-up" or "grossing-up" for income taxes. The ROI includes both interest  
13 and return on equity. Only the equity component needs to be "grossed-up" or  
14 "factored-up" for income taxes. The reason for this is that interest is tax deductible  
15 while profits (i.e., return on equity) are not a tax deduction. Therefore, the "factor-up"  
16 or gross-up" for income taxes on the interest component of the ROI overstates income  
17 tax expense, and thereby overstates the FDC cost results.

18           There is another problem related to the ROI component. The application of the  
19 ROI to the related rate base amounts provides for recovery of both interest and return  
20 on equity. However, some of the FDC studies had reflected interest as an expense as  
21 well. Therefore, the inclusion of both ROI and interest in expenses will result in an

**Direct Testimony of  
Robert E. Schallenberg**

1       overstatement of interest cost in these FDC studies. The impact of these FDC study  
2       flaws will be examined in conjunction with the determination of the 1992 and 1993  
3       customer credits.

4           Q.     Has SWBT been notified that the "gross-up" of "factor-up" of ROI was  
5       wrong?

6           A.     Yes. This problem was brought to SWBT's attention in Case No. TC-  
7       89-14 in regard to the SWBT study presented to the FCC related to the revenue  
8       requirements for the Part 32 Uniform System of Accounts. SWBT agreed that this  
9       methodology distorted the results of that study. Likewise, the continued use of this  
10      methodology distorts the FDC studies related to SWBT's affiliated purchases.

11          Q.     What is adjustment S-19-S?

12          A.     Adjustment S-19-S is an attempt to recognize increased expenses for the  
13      Service Management System/800 (SMS/800) database at the Kansas City Data Center.  
14      These expenses are being billed to Bellcore. SWBT provides operational support and  
15      processing for the SMS/800, which is a component of the nationwide 800 service  
16      offering undertaken by the Regional Bell Operating Companies and Bellcore. This is  
17      provided under contract to Bellcore. (Response to Staff Data Request. No. 5346)  
18      Prior to July, 1992, SWBT-MO was billing approximately \$400,000 for this item.  
19      Now the billing is approximately \$1,400,000 (Response to Staff Data Request No.  
20      821). Adjustment S-19-S is based on \$12 million additional revenue less the 15%  
21      contribution built into the Bellcore bills. The Staff has not had an opportunity to audit

**Direct Testimony of  
Robert E. Schallenberg**

1 the cost data related to this project. When this audit is completed, this adjustment  
2 would be likewise modified to agree with the audit results.

3 Q. What is adjustment S-4-E?

4 A. Adjustment S-4-E is an adjustment to reflect the adjustment proposed  
5 by Dr. Ileo on Table IV-A of his testimony. The \$2.72 million is shown as the total  
6 on Table IV-A.

7 Q. Does this conclude your direct testimony?

8 A. Yes, it does.

**BEFORE THE PUBLIC SERVICE COMMISSION**  
**OF THE STATE OF MISSOURI**

The Staff of the Missouri Public Service  
Commission,

Complainant,

v.

Southwestern Bell Telephone Company,  
a Missouri Corporation,

Respondent.

Case No. TC-93-224

**AFFIDAVIT OF ROBERT E. SCHALLENBERG**

STATE OF MISSOURI


COUNTY OF COLE

ss.

Robert E. Schallenberg, of lawful age, on his oath states: that he has participated in the preparation of the foregoing Direct Testimony in question and answer form, consisting of 28 pages to be presented in the above case; that the answers in the foregoing Direct Testimony were given by him; that he has knowledge of the matters set forth in such answers; and that such matters are true and correct to the best of his knowledge and belief.

  
Robert E. Schallenberg

Subscribed and sworn to before me this 1st day of February, 1993.

  
Notary Public

My Commission Expires: \_\_\_\_\_  
JUDY FRITSCH  
NOTARY PUBLIC STATE OF MISSOURI  
COLE COUNTY  
MY COMMISSION EXP. AUG. 15, 1997

**SOUTHWESTERN BELL CORPORATION  
PARENT COMPANY COSTS  
DISTRIBUTION BY SUBSIDIARY  
IN 1991**

	<u>SUBSIDIARIES</u>	<u>SBC CHARGES</u>
1	SWBT	102,039,365
2	Yellow Pages	9,699,765
3	Mobile	16,544,815
4	Mast	2,308,618
5	Telecom	3,122,270
6	Gulf	1,488,893
7	Metromedia	7,217,404
8	Enterprises	123,772
9	International	6,816,206
10	Asset Management	1,120,692
11	SBC Retained	29,791,825
12	Other*	1,587,187
		181,860,812

\* - (Administrative Services, Audit Services, Capital Corporation Corporate Services, Gateway Insurance, Technology Resources, Washington)

**SOUTHWESTERN BELL CORPORATION**  
**(Parent Company) 1991**

**Charges to Southwestern Bell Telephone**  
**Missouri Operations**

<u>Account No.</u>	<u>Account Description</u>	
6112	Motor Vehicle Expense	\$ 117,451
6711	Executive	3,267,018
6712	Planning	1,294,306
6721	Accounting and Finance	3,670,289
6722	External Relations	2,793,817
6723	Human Resources	2,750,012
6725	Legal	188,844
6728	Other General and Administrative	487,947
7370	Special Charges	693,678
8672	Relief and Pensions	<u>1,112,443</u>
	Total SBC Charges to SWBT- MO	<u>\$16,376,610</u>

Source: Data Request No. 264



**SOUTHWESTERN BELL CORPORATION**  
**(Parent Company) Cost Centers by**  
**Southwestern Bell Telephone Account**

<u>Southwestern Bell</u> <u>Account Description/Number</u>	<u>Southwestern Bell Corporation Cost</u> <u>Centers that are charged to Account</u>
Motor Vehicle Expense (6112)	Corporate Services - Automotive (7200)
Executive (6711)	Executive Support (3500) Office of Chairman (3600) Board of Directors (3700) Corporate Services - Executive Air (7400)
Planning (6712)	Strategic Business Development (5600) New Ventures & Acquisitions (6300)
Accounting and Finance (6721)	Shareowner Services (1100) Annual Meeting for Shareowners (1200) Compliance with SEC Requirements (1400) Investor Relations (1500) Earnings Requirements (1600) Interface with Securities Rating Agencies (1700) External Audit (1900) Corporate Economic Analysis (2000) Financial Research/Market Analysis (2100) Pension Asset Management (2600) Tax Counsel, Advice, Planning & Research (3800) Tax Return Preparation (3900) Corporate Accounting Research (4000) Corporate Financial Analysis (4100) Corporate Books and Records (4200) Corporate Budgets (4300) Cash Management (6100) Financing Projects (6800) Internal Audit Services (7000)

**Southwestern Bell**  
**Account Description/Number**

**Southwestern Bell Corporation Cost**  
**Centers that are charged to Account**

**External Relations (6722)**

State Regulatory Activities (4500)  
Corporate Record Filings (4800)  
News and Public Information (5000)  
Trademarks, Patents & Graphics Services (5100)  
Public Issues Research (5200)  
Federal Regulatory (5400)  
Rate Case Activity (6700)  
Corporate Advertising (8000)  
Marketing Support (8100)

**Human Resources (6723)**

Saving Plan Management (2700)  
Employee Training & Development (2800)  
Compensation Planning & Administration (2900)  
Benefit Planning & Development (3000)  
Human Resources Planning & Staffing (3100)  
Employee Information (3200)  
Senior Management Salary & Benefit  
Administration (4600)

**Legal (6725)**

Litigation (6900)  
Legal Support (7900)

**Other General and  
Administrative (6728)**

Corporate Risk Management (4900)  
Corporate Services - Food Services (7100)  
Subsidiary Support (7500)

**Special Charges (7370)**

Legislative Advocacy (5300)  
PAC Program (5500)  
Memberships (6000)  
Southwestern Bell Foundation (6200)

**Relief and Pensions (8672)**

Senior Management Benefits Payments (7700)

**Source: Data Request No. 633**

**SBC  
COST CENTER PROFILE  
REPORT**

**00199 Controllers Support**

This cost center includes:

- . Processing of the bills, vouchers, and payroll-related documents of the Parent Company;
- . Preparation of the reports associated with the above items;
- . Maintenance of SBC's Local Area Network (LAN) and associated support functions.

This cost center does not include the preparation of vouchers or payroll input by the department incurring the voucher or payroll costs. (Data Request No. 44)

**Comments:**

This cost center contains Wages and Salaries of \$245,146. This is a Tier 1 cost center. This cost center is allocated to Tier 2 cost centers based on the percentage of wage charges to each Tier 2 cost center.

**00299 Non-Income Taxes**

**This cost center includes tax expense incurred by SBC other than income taxes.  
(Data Request No. 44)**

**Comments:**

**This is a Tier 1 cost center that is allocated to Tier 2 cost centers similar to Controllers Support (199).**

**00399 Depreciation**

**This cost center includes depreciation expense incurred by SBC.  
(Data Request No. 44)**

**Comments:**

**Same as Non-Income Taxes (0299)**

**00499 Pensions and Benefits**

**This cost center includes:**

- . **Costs associated with the various employee benefits;**
- . **Tuition reimbursement;**
- . **Personal telephone reimbursement (not including long distance or inter-LATA business calls on personal telephone bill);**
- . **Physical examination reimbursement;**
- . **Service anniversary awards and perfect attendance awards;**
- . **Pension and disability payments.**

**This includes only direct costs associated with each employee and not the costs of developing or administering the benefit and pension plans. (Data Request No. 44)**

**Comments:**

**Same as Non-Income Taxes (0299)**

**00599 Contract Administration**

This cost center consists of general corporate expenses primarily incurred through contract charges from Southwestern Bell Telephone Company. These costs include, but are not limited to:

- . Rental of floor space;
- . Telecommunications charges;
- . Treasury (cashier) services;
- . Mail operations.

(Data Request No. 44)

**Comments:**

Same as Non-Income Taxes (0299). Also contains \$40,409 of Salary and Wages.



## 01100 Shareowner Services

The purpose of Shareowner Services is to perform functions associated with:

- . Issuance and transfer of stock;
- . Stock certificate recordkeeping;
- . Disbursement of dividends;
- . Administration of shareowner plans (e.g., DRISPP);
- . Issuance of shareowner newsletters, annual reports, shareowner research, etc.;
- . Special shareowner projects (e.g., stock split).

These activities relate to the provision of an accurate accounting of transactions related to shareowners and provision of various data to shareowners regarding their investment. (Data Request No. 44)

Total 1991	SBC Costs	\$9,338,186
	Direct Charged	0
	Allocated	9,338,186
	Retained	0
	SWBT Costs	\$7,549,935
	Direct Charged	0
	Allocated	7,549,935
	Allocation Basis	Equity/Investment

### Comments:

Cost Center contains Wages and Salaries of \$477,481. Gulf Printing (an affiliated Company) was paid \$1.1 million for printing SBC's annual report to shareowner in 1991 (Data Request No. 254). The Company responses in this case would indicate that SBC did not competitively bid this printing job. The last evidence of competitive bidding was from the Company's response to Data Request No. 1477 in Case No. TC-89-14. In September, 1987, Gulf Printing was selected to print the SBC Annual Report. Gulf bid \$804,863 while two other suppliers bid \$759,280 and \$763,326. The comment section of the procurement form states: "The Annual Report is a statement about our well being. If we don't use Gulf, it will send a negative message to our shareholders concerning our printing capabilities". \$340,000 was transferred from the allocation pool to be retained by SBC based on the above situation.

**01200 Annual Meeting for Shareowners**

This cost center includes all activities related to the annual shareowners' meeting. This includes, but is not limited to, planning and preparing for the meeting and all functions related to the hosting of the meeting. Some examples are:

- . Arranging for and renting facilities;
- . Providing security for the meeting.

(Data Request No. 44)

Total 1991	SBC Costs	\$227,297
	Direct Charged	0
	Allocated	227,297
	Retained	0
	SWBT Costs	\$183,601
	Direct Charged	0
	Allocated	183,601
	Allocation Basis	Equity/Investment

**Comments:**

Cost Center contains Wages and Salaries of \$45,111. Addressed in the direct testimony.

**014\*\* Compliance with Securities Law and Exchange Requirements**

This cost center includes:

- . Preparation and filing of certain documents with federal and state regulatory bodies;
- . Legal advice and counsel on federal, state and foreign securities law;
- . Interface with the various securities exchanges;
- . Support and documentation of certain disclosure requirements in the corporation's 10-Qs, 10-K and Annual Report.

This includes both the costs of maintaining an internal staff in the corporate accounting, finance and legal areas and the engagement of external professionals. (Data Request No. 44)

Total 1991	SBC Costs	\$1,573,741
	Direct Charged	35,594
	Allocated	1,538,147
	Retained	0
	SWBT Costs	\$1,268,262
	Direct Charged	23,840
	Allocated	1,244,422
	Allocation Basis	Equity/Investment

**Comments:**

SBC issues two sets of Security Exchange Commission (SEC) required reports (e.g., 8-K, 10-Q, 10-K). One set is issued for SBC. The other set is issued for SWBT. Therefore, the SBC corporate structure requires two sets of reports when a stand alone company would need to provide only one. The requirement to comply with SEC rules and requirements is a function of being a company with publicly traded equity security and publicly issued debt. The SEC requirements and rules with related costs do not vary with the amount of equity in a company. Besides, as mentioned above, debt is a factor in the SEC rules and requirements. The cost of SEC compliance is not double for a company that has twice as much debt and equity as another firm. The cost center contains \$378,837 of wages and salaries. Of this amount \$10,834 was directly charged to SWBT and the remainder allocated to all subsidiaries including SWBT.

## 01500 Investor Relations

The purpose of the investor relations cost center is to provide an information flow from the company to various segments of the financial community. This is primarily accomplished through:

- . Daily telephone contacts with securities analysis to answer questions;
- . Regularly published newsletters to the investment community concerning activities of SBC and its subsidiaries;
- . Special direct mailings to the financial community;
- . Meetings held periodically in the financial centers of the country to present management's views to the professional investment community;
- . Meetings hosted for visiting securities analysts;
- . Visits to large institutional investors;
- . Financial community research.

(Data Request No. 44)

Total 1991	SBC Costs	\$2,314,187
	Direct Charged	0
	Allocated	2,314,187
	Retained	0
	SWBT Costs	\$1,867,491
	Direct Charged	0
	Allocated	1,867,491
	Allocation Basis	Equity/Investment

### Comments:

Cost Center contains Wages and Salaries of \$685,503. The above list of activities would be expected within a publicly traded company. The cost of these activities would not increase by an increase of equity dollars invested in the firm.

**016\*\* Earnings Requirements**

The earnings requirements cost center consists of:

- Corporate financial planning and forecasting with respect to such data as forecasted earnings or projected market share growth;
- Economic and financial research required to determine the cost of capital for the Corporation, including net income and shareowner dividend requirements.

Total 1991	SBC Costs	\$335,511
	Direct Charged	180,311
	Allocated	155,200
	Retained	0
	SWBT Costs	\$152,176
	Direct Charged	26,920
	Allocated	125,256
	Allocation Basis	Equity/Investment

**Comments**

Another cost center with costs that do not vary or increase because of variances or increases in the company's equity accounts.

**017\*\* Interface with Securities Rating Agencies**

**This cost center consists of:**

- Direct interface with rating agencies;**
- Dissemination of information about the Corporation to the rating agencies (e.g., Moody's or Standard and Poor's).**

**This cost center is very closely related to the Investor Relations and Earnings Requirements functions. However, this function is related to a specific segment of the financial community, the rating agencies.**

**(Data Request No. 44)**

<b>Total 1991</b>	<b>SBC Costs</b>	<b>\$214,398</b>
	<b>Direct Charged</b>	<b>65,000</b>
	<b>Allocated</b>	<b>149,398</b>
	<b>Retained</b>	<b>0</b>
	<b>SWBT Costs</b>	<b>\$130,839</b>
	<b>Direct Charged</b>	<b>10,000</b>
	<b>Allocated</b>	<b>120,839</b>
	<b>Allocation Basis</b>	<b>Equity/Investment</b>

**Comments**

**Costs in this cost center are related to debt rating agencies (e.g., Moody's, Standard and Poor's). An equity allocator is inappropriate because it shields SBC subsidiaries with higher debt ratios than SWBT (e.g., International) from a higher share of these costs. This places more costs on SWBT regulated operations and customers. In addition, the equity size allocator is inappropriate on these fixed cost levels.**

019\*\* External Audit

This cost center consists of:

Engagement of a public accounting firm to perform an audit of the corporation's financial statements;

Assistance to the external auditors to ensure an efficient and effective audit, which primarily consists of specific functions performed by SBC's controllers organization.

(Data Request No. 44)

Total 1991	SBC Costs	\$168,492
	Direct Charged	39,505
	Allocated	128,987
	Retained	0
	SWBT Costs	\$34,647
	Direct Charged	(69,646)
	Allocated	104,293
	Allocation Basis	Equity/Investment

Comments

Costs for external audit are not determined by the amount of equity recorded on a company's books. External audit costs are influenced by hours spent auditing various aspects of the company. While the external audit will examine the equity accounts, the external audit will also examine areas such as payroll, accounts receivable, assets, internal control, liabilities, and revenues. A possibility of these costs being duplicative and unnecessary exists since SWBT pays for its own audit costs.

## 02000 Corporate Economic Analysis

This cost center includes the analyses and forecasts of the external economic environment as it affects the Corporation and the economy of the Southwest region. These analyses include:

- . United States economic forecasts, with special emphasis on interest rates and inflation;
- . Coordination with subsidiaries to ensure consistency of regional economic forecasts with United States forecasts;
- . Analysis of current financial market conditions and the short-term impact of changes in the economy and credit markets on the interest rate outlook;
- . Analysis of subsidiary revenue and expense projections based on estimated relationships with external economic and demographic assumptions. (Data Request No. 44)

Total 1991	SBC Costs	\$134,415
	Direct Charged	0
	Allocated	334,415
	Retained	0
	SWBT Costs	\$269,571
	Direct Charged	0
	Allocated	269,571
	Allocation Basis	Equity/Investment

### Comments:

Cost Center does not have costs that are caused and/or influenced by the dollar amount of equity investment. This type of activity would be conducted in firms that do not have publicly traded stock. Cost Center also includes costs and activities that are duplicative and unnecessary to SWBT. SWBT has its own Regional Economic Group. Further, SWBT prints monthly and quarterly Economic Data. These publications are "Southwest Economic Perspectives", "Southwest Economic Forecast", "Economic Update", and "Construction in the Southwest".



021\*\* Financial Research/Market Analysis

This cost center consists of the preparation of the Corporation's basic financial policies and strategies. This include:

- . Research and evaluation of corporate finance policies/strategies;
- . Evaluation of the impact of various alternative financing strategies such as maturity schedules, short-term debt levels and equity for debt swaps.

(Data Request No. 44)

Total 1991	SBC Costs	\$103,864
	Direct Charged	0
	Allocated	103,864
	Retained	0
	SWBT Costs	\$83,742
	Direct Charged	0
	Allocated	83,742
	Allocation Basis	Equity/Investment

Comments

These costs are fixed in nature and do not vary or increase because of the amount of equity investment.

**026\*\* Pension Plan Administration**

This cost center primarily consists of:

- . Making investment decisions with respect to the pension plans;
- . Determining the asset classes in which to invest and to what degree;
- . Selecting and monitoring the investment managers;
- . Working with master trustees in performing required administration and legal work;
- . Trustees fees relating to pension plans;
- . Insurance premiums relating to pension plans;
- . Actuarial fees relating to pension plans.

These functions are performed to maintain the various pension benefit plans of the Corporation and its subsidiaries.

(Data Request No. 44)

Total 1991	SBC Costs	\$516,989
	Direct Charged	3,717
	Allocated	513,272
	Retained	0
	SWBT Costs	\$451,798
	Direct Charged	0
	Allocated	451,798
	Allocation Basis	Employee

**Comments**

These costs are fixed and do not vary or increase with corresponding changes in the number of employees.

**027\*\* Savings Plan Administration**

This cost center consists of:

- . Decisions relating to the various savings plans;
- . Selecting and monitoring savings plan investment managers;
- . Trustees fees relating to savings plans;
- . Administration and legal efforts relating to savings plans;
- . Actuarial fees relating to savings plans.

(Data Request No. 44)

Total 1991	SBC Costs	\$1,066,810
	Direct Charged	606,967
	Allocated	459,843
	SWBT Costs	\$709,064
	Direct Charged	303,745
	Allocated	405,319
	Allocation Basis	Employee

**Comments**

Same as Pension Plan Administration (026)

**028\*\* Employee Training and Development**

**This cost center consists of:**

- . Planning and developing corporate conferences, principally periodic meetings for officers;**
- . Design, development, and presentation of seminars for employees of the Corporation and its subsidiaries;**
- . Providing program management and consulting services for external education program.**

**(Data Request No. 44)**

<b>Total 1991</b>	<b>SBC Costs</b>	<b>\$4,206,956</b>
	<b>Direct Charged</b>	<b>785,539</b>
	<b>Allocated</b>	<b>3,421,417</b>
	<b>Retained</b>	<b>0</b>
	<b>SWBT Costs</b>	<b>\$3,615,202</b>
	<b>Direct Charged</b>	<b>599,082</b>
	<b>Allocated</b>	<b>3,016,120</b>
	<b>Allocation Basis</b>	<b>Employee</b>

**Comments:**

**Cost Center contains expenses related to the Leadership Forum. The costs related to Employee Training and Development are fixed and do not vary with increases or decreases in employee levels. In fact, in the case of the Leadership Forum, not all employees attended this seminar.**

**029\*\* Compensation Planning and Administration**

**This cost center includes:**

- . Formulation and distribution of corporate policies on human resources matters;
- . Assistance to the Corporate staff in human resource matters;
- . Publication of administrative guidelines relating to human resources policies and programs;
- . Guidance and assistance to subsidiaries for development of compensation programs;
- . Design and administration of compensation programs for the Corporate staff;
- . Administration of corporate job evaluation for the Corporate staff and participation on the subsidiary job evaluation committee;
- . Perform staff functions and administer centralized payroll for the Corporation;
- . Administration of the home relocation program for the Corporation and provide assistance to subsidiaries as required;
- . Provide personnel administrative support for the Corporate staff;
- . Legal counsel, advice, and research in personnel administration and various compensation matters.

**(Data Request No. 44)**

Total 1991	SBC Costs	\$2,540,626
	Direct Charged	466,191
	Allocated	2,074,435
	Retained	57,086
	SWBT Costs	\$1,829,212
	Direct Charged	264
	Allocated	1,828,948
	Allocation Basis	Employee

**Comments**

**Same as Pension Plan Administration (026)**

**030\*\* Benefit Planning and Development**

**This cost center includes:**

- **Development and implementation of the benefit plan packages for the Corporation and its subsidiaries;**
- **Formulation of corporate policies on benefit matters;**
- **Interface and coordination with subsidiary benefit groups;**
- **Counsel, advice and research in benefit planning and development;**
- **Consulting services for Corporate Health Programs;**
- **Design, development, and presentation of health programs for the Corporation and subsidiaries.**

**(Data Request No. 44)**

<b>Total 1991</b>	<b>SBC Costs</b>	<b>\$6,430,095</b>
	<b>Direct Charged</b>	<b>1,686,204</b>
	<b>Allocated</b>	<b>4,743,891</b>
	<b>Retained</b>	<b>45,845</b>
	<b>SWBT Costs</b>	<b>\$4,179,772</b>
	<b>Direct Charged</b>	<b>261</b>
	<b>Allocated</b>	<b>4,179,511</b>
	<b>Allocation Basis</b>	<b>Employee</b>

**Comments**

**Same as Pension Plan Administration (026)**

**031\*\* Human Resources Planning and Staffing**

**This cost center includes:**

- . Design and development of the corporate-wide human resources information system;
- . Development and execution of human resource planning processes and resources for use in corporate strategic planning, e.g., trend analysis, environmental scanning and force needs analysis;
- . Design and development of human resources strategies relating to the corporate business plan, management continuity, and executive succession development programs;
- . Design and development of the corporate-wide mechanized management staffing system;
- . Presentation of position papers concerning the impact of issues on corporate human resources and leading to the establishment of corporate human resource policies;
- . Design and development of management recruiting practices and policies for the Corporation and its subsidiaries;
- . Screening and hiring of general management and Leadership Development Program employees for the Corporation and its subsidiaries;
- . Consultation with subsidiaries on individual management hiring programs, e.g., recruiting, testing, interviewing, selections, etc.

**(Data Request No. 44)**

Total 1991	SBC Costs	\$3,219,881
	Direct Charged	351,793
	Allocated	2,868,088
	Retained	202,000
	SWBT Costs	\$2,674,647
	Direct Charged	146,133
	Allocated	2,528,514
	Allocation Basis	Employee

**Comments**

**Same as Pension Plan Administration (026)**

**032\*\* Employee Information**

This cost center includes:

- . Employee publications such as Enterprise Magazine;
- . Legal advice and counsel on employee information and programs (i.e., Code of Business Conduct and Employee Privacy Program);
- . Development and dissemination of information of interest to the Corporation and subsidiary employees.

(Data Request No. 44)

Total 1991	SBC Costs	\$2,315,695
	Direct Charged	0
	Allocated	2,315,695
	Retained	0
	SWBT Costs	\$2,040,533
	Direct Charged	0
	Allocated	2,040,533
	Allocation Basis	Employee

**Comments:**

Employee Information at the SBC level is unnecessary to SWBT on a stand alone basis. Under the current SBC structure, the SBC Employee Information Cost Center is duplicative of SWBT's Employee Information program. SWBT has its own Employee Information publications. These publications include "This Week", "Telephone Times", "Pioneer News", and "FYI Bulletins".



**035\*\* Executive Support**

**This cost center include:**

- . **Activities associated with executive conferences;**
- . **Administrative support provided to the SBC executives.**

**(Data Request No. 44)**

<b>Total 1991</b>	<b>SBC Costs</b>	<b>\$1,957,431</b>
	Direct Charged	6,715
	Allocated	1,950,716
	Retained	6,715
	<b>SWBT Costs</b>	<b>\$1,471,213</b>
	Direct Charged	0
	Allocated	1,471,213
	Allocation Basis	General

**Comments:**

**Same as Office of Chairman (3600)**

**036\*\* Office of the Chairman**

**This cost center includes:**

- Overall supervision of the Corporation;
- Attendance at the Board of Directors meetings and officers meetings;
- Presentations at Board meetings, Investors conferences, Shareowners meetings, etc.;
- Long-term incentive costs associated with retired executives.

**This cost center is to include all of the costs of the top four officers of Southwestern Bell Corporation (Parent).**

**(Data Request No. 44)**

<b>Total 1991</b>	<b>SBC Costs</b>	<b>\$7,717,872</b>
	Direct Charged	0
	Allocated	7,717,872
	Retained	0
	<b>SWBT Costs</b>	<b>\$5,842,131</b>
	Direct Charged	0
	Allocated	5,842,131
	Allocation Basis	General

**Comments**

**Costs in this cost center are unnecessary for SWBT on a stand alone basis. SWBT does not need two presidents or two sets of officers. SWBT's officers set direction for SWBT. SBC can impose on SWBT direction contrary to SWBT's best interest if SBC believes such direction is in SBC's overall best interest. SBC can do this because of its 100% ownership of SWBT.**

**037\*\* Board of Directors**

**This cost center includes:**

- Expenses incurred for the engagement of Directors;
- Payment of Directors fees;
- Other costs incurred for the benefit of Directors;
- Costs associated with Board of Directors meetings;
- Costs associated with the membership and participation by an SBC Senior Manager on the Board of an SBC subsidiary (to be direct charged to that subsidiary).

**(Data Request No. 44)**

<b>Total 1991</b>	<b>SBC Costs</b>	<b>\$2,226,642</b>
	Direct Charged	928
	Allocated	2,225,714
	Retained	0
	<b>SWBT Costs</b>	<b>\$1,683,445</b>
	Direct Charged	0
	Allocated	1,683,445
	Allocation Basis	General

**Comments**

**The costs are unnecessary and duplicative. SWBT has a Board of Directors and its own Board of Directors Meetings.**

**038\*\* Tax Counsel, Advice, Planning and Research**

**This cost center includes:**

- **Monitoring and interpreting current and proposed tax legislation with respect to its impact on the Corporation and its subsidiaries;**
- **Researching current legislation, internal revenue code, and various court cases;**
- **Long-range corporate tax planning, advice and counsel in connection with tax audits and disputes involving taxing authorities;**
- **Legal counsel, advice and research in tax-related areas, including issues regarding the abandonment and escheat of property.**

**(Data Request No. 44)**

<b>Total 1991</b>	<b>SBC Costs</b>	<b>\$2,957,057</b>
	<b>Direct Charged</b>	<b>508,151</b>
	<b>Allocated</b>	<b>2,448,906</b>
	<b>Retained</b>	<b>122,948</b>
	<b>SWBT Costs</b>	<b>\$2,072,844</b>
	<b>Direct Charged</b>	<b>218,113</b>
	<b>Allocated</b>	<b>1,854,731</b>
	<b>Allocation Basis</b>	<b>General</b>

**Comments**

**Same as Tax Return Preparation**

**039\*\* Tax Return Preparation**

This cost center includes:

- Preparation of the Corporation's federal, state and local income, payroll and franchise tax returns, as well as other miscellaneous forms filed with taxing authorities;
- Filing of estimated tax deposits and various payroll tax deposits;
- Advice and guidance to the Corporation's subsidiaries on tax return preparation and filings.

(Data Request No. 44)

Total 1991	SBC Costs	\$929,739
	Direct Charged	61,991
	Allocated	867,748
	Retained	37,007
	SWBT Costs	\$657,629
	Direct Charged	0
	Allocated	657,629
	Allocation Basis	General

**Comments**

Cost center has higher potential for inclusion of unnecessary and/or duplicative costs being charged to SWBT since one SBC position and related secretary charge 50% of their time to this cost center and 50% to Tax Counsel, Advice, Planning and Research (3800). This SBC position has the following titles:

- Managing Director - Taxes,
- Vice President-Taxes - Metromedia Paging,
- Vice President-Taxes - SWB Telecommunications,
- Vice President-Taxes - SWB Yellow Pages,
- Vice President-Taxes - SWB Mobile,
- Vice President-Taxes - SWBT.

SWBT employs a Director-Telephone Company Tax Operations.

(Data Request Nos. 18, 707)

040\*\* Corporate Accounting Research

This cost center includes:

- Review and investigation of accounting issues on behalf of all corporate activities;
- Responses to proposed authoritative accounting procedures on behalf of all SBC entities;
- Monitor the current events of the authoritative accounting organizations;
- Develop and propose the overall corporate accounting policies.

(Data Request No. 44)

Total 1991	SBC Costs	\$564,452
	Direct Charged	8,780
	Allocated	555,672
	Retained	0
	SWBT Costs	\$418,899
	Direct Charged	0
	Allocated	418,899
	Allocation Basis	General

Comments

Nothing to note.

**04100 Corporate Financial Analysis**

This cost center consists of the preparation of various analyses of the overall Corporation's historical and projected financial results. These analyses include:

- Evaluation of the Corporation's and its subsidiaries' financial performance;
- Determination of the impact of proposed regulation on the Corporation and its subsidiaries' financial position and objectives (e.g., proposed tax legislation).

(Data Request No. 44)

Total 1991	SBC Costs	\$885,529
	Direct Charged	0
	Allocated	885,529
	Retained	0
	SWBT Costs	\$670,710
	Direct Charged	0
	Allocated	670,710
	Allocation Basis	General

**Comments**

Nothing to note.

**042\*\* Corporate Books and Reports**

This cost center consists of:

- . Preparation of the journals, ledgers and other related accounting records of the Corporation and specific subsidiaries.
- . Design, preparation, and analysis of internal financial and administrative reports of the Parent, subsidiaries and consolidated Corporation;
- . Development and implementation of procedures and controls to accomplish the above activities.

(Data Request No. 44)

Total 1991	SBC Costs	\$1,518,064
	Direct Charged	359,171
	Allocated	1,158,893
	Retained	0
	SWBT Costs	\$868,519
	Direct Charged	0
	Allocated	868,519
	Allocation Basis	General

**Comments**

Nothing to note.



#### 04300 Corporate Budgets

This cost center includes:

- . Preparation of schedules, guidelines, and assumptions used by the Parent and subsidiaries in preparing financing and other types of forecasts;
- . Collection, analysis, and review of the Corporation's and subsidiaries' budget packages;
- . Preparation of budgets and forecasts for use in assessing current and future financial performance.

The Corporate Budgets cost center will be used by the Controllers Financial Analysis group only. Preparation of departmental budgets should be charged to each respective department's normal cost centers.

(Data Request No. 44)

Total 1991	SBC Costs	\$470,671
	Direct Charged	0
	Allocated	470,671
	Retained	0
	SWBT Costs	\$355,051
	Direct Charged	0
	Allocated	355,051
	Allocation Basis	General

#### Comments

Nothing to note.

**045\*\* State Regulatory Activities**

This cost center does not include costs associated with state rate case activities (see CCN 067\*\*). This cost center does include:

- . Developing corporate policy set before state legislators and regulatory commissions;
- . Expense for participation on various state policy counsels and boards within the telecommunications industry;
- . Parent company involvement on its own behalf with state regulators (e.g., affiliate transaction dockets, general investigation dockets, etc.).

(Data Request No. 44)

Total 1991	SBC Costs	\$2,113,492
	Direct Charged	743,703
	Allocated	1,369,789
	Retained	0
	SWBT Costs	\$1,766,502
	Direct Charged	728,861
	Allocated	1,037,641
	Allocation Basis	General

**Comments**

Nothing to note.

**046\*\* Senior Management Salary and Benefit Administration**

**This cost center includes:**

- . **Design and administration of compensation and benefit plans for the senior managers of the Corporation and its subsidiaries;**
- . **Administration of any specified program involving senior managers of the Corporation and its subsidiaries;**
- . **Trustee and actuarial fees associated with senior management benefits.**

**(Data Request No. 44)**

<b>Total 1991</b>	<b>SBC Costs</b>	<b>\$3,197,942</b>
	Direct Charged	731,291
	Allocated	2,466,651
	Retained	85,221
	<b>SWBT Costs</b>	<b>\$2,380,375</b>
	Direct Charged	516,802
	Allocated	1,863,573
	Allocation Basis	General

**Comments**

**Nothing to note.**

**048\*\* Corporate Record Filings**

**This cost center includes:**

- Maintenance of corporate records regarding required state and federal corporate filings;**
- Maintenance of corporate records regarding required contractual corporate filings.**

**(Data Request No. 44)**

<b>Total 1991</b>	<b>SBC Costs</b>	<b>\$52,997</b>
	Direct Charged	0
	Allocated	\$2,997
	Retained	0
	<b>SWBT Costs</b>	<b>\$40,091</b>
	Direct Charged	0
	Allocated	40,091
	Allocation Basis	General

**Comments**

**. Nothing to note.**

**049\*\* Corporate Risk Management**

**This cost center includes:**

- . Evaluation and acquisition of insurance and alternative methods of risk management;
- . Risk exposure identification and loss control (e.g., environmental);
- . Corporate security and claims;
- . Government industrial security clearances;
- . Procurement of all types of surety bonds (Bid, Performance, Judicial, Tax, etc.).

**(Data Request No. 44)**

Total 1991	SBC Costs	\$5,947,992
	Direct Charged	3,662,165
	Allocated	2,285,827
	Retained	36,271
	SWBT Costs	\$1,801,581
	Direct Charged	70,767
	Allocated	1,730,814
	Allocation Basis	General

**Comments**

**Nothing to note.**

**050\*\* News and Public Information**

**This cost center includes:**

- . Writing and distributing news releases;**
- . Planning and setting up news conferences and special events/projects;**
- . Researching and drafting speeches and reprints;**
- . Evaluating requests for managers to participate in public forums and conferences.**

<b>Total 1991</b>	<b>SBC Costs</b>	<b>\$1,983,989</b>
	Direct Charged	0
	Allocated	1,983,989
	Retained	0
	<b>SWBT Costs</b>	<b>\$1,503,284</b>
	Direct Charged	0
	Allocated	1,503,284
	Allocation Basis	General

**Comments**

**Costs are unnecessary and duplicative of SWBT functions. Costs are related to Parent Company activities and should be retained.**

**051\*\* Trademarks, Patents, and Graphics Services**

**This cost center includes:**

- . **Development of SBC identity/graphics guidelines;**
- . **Distribution of the guidelines to all subsidiaries;**
- . **Monitoring the use of the Southwestern Bell name and all Bell trademarks;**
- . **Legal filings to obtain and protect registered trademarks;**
- . **Legal research, advice and counsel regarding trademarks and patents.**

**(Data Request No. 44)**

<b>Total 1991</b>	<b>SBC Costs</b>	<b>\$2,032,212</b>
	Direct Charged	101,838
	Allocated	1,930,374
	Retained	25,969
	<b>SWBT Costs</b>	<b>\$1,464,976</b>
	Direct Charged	17,310
	Allocated	1,447,666
	Allocation Basis	General

**Comments**

**Cost center contains expenses related to the Company's Common Look Identity Program. The cost center represents costs related to the value of the Southwestern Bell name and logo. The chief subsidiary that has and continues to provide value and name recognition to these items is SWBT. The beneficiaries of this value are the non-telco subsidiaries. SWBT should either absorb all costs and charge franchise revenues to non-telco subsidiaries or SWBT should be charged none of these costs. I recommend the latter approach.**

**052\*\* Public Issues Research**

**This cost center includes:**

- Identifying, studying and analyzing key emerging economic, social, technological and ecological trends and issues which could have an impact on the Corporation, its subsidiaries and customers;
- Bringing changes in the external environment to the attention of senior management in all SBC entities.

**(Data Request No. 44)**

<b>Total 1991</b>	<b>SBC Costs</b>	<b>\$828,167</b>
	Direct Charged	399,097
	Allocated	429,070
	Retained	399,097
	<b>SWBT Costs</b>	<b>\$327,514</b>
	Direct Charged	0
	Allocated	327,514
	Allocation Basis	General

**Comments**

**Nothing to note.**



**053\*\* Legislative Advocacy**

The following activities are representative of the functions performed within this cost center.

- . Plan and implement the form and substance of advocacy on behalf of SBC and its subsidiaries before members of Congress, their personal staffs and Congressional committee staffs;
- . Acquire intelligence relative to the current and planned interests and the activities of Congress for their impact upon SBC and its subsidiaries;
- . Provide input, advice and guidance to officers and other personnel of SBC and its subsidiaries in developing corporate positions relative to legislative, political and other public policy matters of Congressional interest.

(Data Request No. 44)

Total 1991	SBC Costs	\$4,062,944
	Direct Charged	746,410
	Allocated	3,316,534
	Retained	707,417
	SWBT Costs	\$2,529,557
	Direct Charged	10,636
	Allocated	2,518,921
	Allocation Basis	General

**Comments**

Costs are charged below the line and not included in cost of service to ratepayers.

**054\*\* Federal Regulatory Activities**

**This cost center includes:**

- . **Monitoring the activities of the FCC for their impact upon SBC and its subsidiaries;**
- . **Providing input, advice, assistance and guidance to officers and other personnel of SBC and its subsidiaries in developing corporate positions and strategies relative to regulatory issues of interest to the FCC;**
- . **Presenting and advocating corporate positions before the FCC;**
- . **Supporting the appropriate regulatory organizations within SWBT and SBC;**
- . **Supporting all other SBC subsidiaries in their federal regulatory efforts.**

**(Data Request No. 44)**

<b>Total 1991</b>	<b>SBC Costs</b>	<b>\$4,203,477</b>
	Direct Charged	1,605,626
	Allocated	2,597,851
	Retained	51,672
	<b>SWBT Costs</b>	<b>\$3,136,990</b>
	Direct Charged	1,167,332
	Allocated	1,969,658
	Allocation Basis	General

**Comments**

**Nothing to note.**

**05500 PAC Program**

This cost center contains the costs associated with work performed on behalf of Southwestern Bell Corporation's Political Action Committee.

(Data Request No. 44)

Total 1991	SBC Costs	\$152,495
	Direct Charged	0
	Allocated	152,495
	Retained	
	SWBT Costs	\$115,359
	Direct Charged	0
	Allocated	115,359
	Allocation Basis	General

**Comments**

Same as Legislative Advocacy (5300).

**056\*\* Strategic Business Development**

This cost center includes:

- . Assistance to subsidiaries in developing and implementing business plans that expand their businesses in accordance with corporate strategic plans;
- . Identification and assessment of products, services and programs which will support subsidiary business goals;
- . Consultation with other organizations on matters affecting strategic business development;
- . Development of new business to support corporate growth and diversification;
- . Reviewing and setting policy on the overall corporate business direction;
- . Macro-based planning and direction provided by the Corporation's senior executives;
- . Research on the business climate, competitors, opportunities and threats;
- . Evaluating the above information with respect to the Corporation's long-term business philosophy.

(Data Request No. 44)

Total 1991	SBC Costs	\$14,734,463
	Direct Charged	4,790,774
	Allocated	9,943,689
	Retained	2,924,939
	SWBT Costs	\$8,201,043
	Direct Charged	662,677
	Allocated	7,538,366
	Allocation Basis	General

**Comments**

The Corporate Policy Development cost center (44) was discontinued in 1989 with the subsequent use of the Strategic Business Development cost center (56). In 1989, the Corporate Policy Development cost center had \$7.5 million of cost versus \$3 million in the Strategic Business Development cost center. Since 1989, SBC has grown its Strategic Planning and Strategic Marketing Staff from 56 in 1989 to 73 in the 1992 budget. This force growth is indicative of SBC's increased advancement/pursuit of opportunities in both the regulated and unregulated areas as well as the domestic and international fronts. In 1992, SBC budgeted \$14.2 million for Strategic Business Development. Data Request No. 706

**06000 Memberships**

This cost center includes entrance or initiation fees and annual, quarterly or monthly dues in civic, service, social, recreational or athletic clubs.

(Data Request No. 44)

Total 1991	SBC Costs	\$538,907
	Direct Charged	0
	Allocated	538,907
	Retained	60,010
	SWBT Costs	\$412,001
	Direct Charged	0
	Allocated	412,001
	Allocation Basis	General

**Comments**

Same as Legislative Advocacy (5300).

**061\*\* Cash Management**

**This cost center includes:**

- Administration of the Corporation's cash management system, including bank account maintenance and reconciliation, cash book operations and banking relations;**
- Management of the Corporation's short-term investment portfolio;**
- Preparation of the Corporation's cash flow forecasts;**
- Assessment of the earnings impact associated with alternative cash investment options.**

**(Data Request No. 44)**

<b>Total 1991</b>	<b>SBC Costs</b>	<b>\$1,185,089</b>
	Direct Charged	527,715
	Allocated	657,374
	Retained	414,754
	<b>SWBT Costs</b>	<b>\$532,285</b>
	Direct Charged	1,328
	Allocated	530,957
	Allocation Basis	Equity/Investment

**Comments**

The cost in this cost center is the responsibility of SBC (Parent). SWBT has its own cash management functions with related costs. In fact, during 1990 through 1992 to date, SWBT has not received any cash advances from SBC. (Data Request No. 114) To the extent SWBT pays dividends to the Parent Company, the cash management costs incurred in this cost center are totally related to SBC's use of its dividend income. The use of the equity investment amount allocator is not indicative of the factor that causes these costs to be incurred.

06250 Southwestern Bell Foundation

This cost center includes:

- . Development of the Corporation's contribution policy;
- . Management of the contribution requests, determination of eligibility, and authorization of payment;
- . Interface with charitable organizations and the subsidiaries on behalf of the Foundation;
- . Processing contribution payments and maintaining Foundation accounting records;
- . Managing the Foundation's assets, primarily cash and investments.

(Data Request No. 44)

Total 1991	SBC Costs	\$1,454,673
	Direct Charged	11,800
	Allocated	1,442,873
	Retained	178,378
	SWBT Costs	\$1,091,876
	Direct Charged	0
	Allocated	1,091,876
	Allocation Basis	General

Comments

Same as Legislative Advocacy (5300).

## 06350 New Ventures and Acquisitions

This cost center includes:

- Analysis and investigation of domestic and international new business ventures or potential acquisition candidates (due diligence);
- Negotiations with potential acquisition candidates, including meetings, drafting of legal documents, etc;
- Research of the legal ramifications of an acquisition or new venture (i.e., MFJ or antitrust restrictions, trade and tariff laws, customs regulations);
- Interface with subsidiaries on the assimilation of the new business.

Costs associated with these types of activities must always be retained in the Parent (charging direction code 50). The appropriate Project Identification is to be used when reporting this cost center number.

(Data Request No. 44)

Total 1991	SBC Costs	\$5,740,173
	Direct Charged	5,740,173
	Allocated	0
	Retained	5,519,039
	SWBT Costs	\$6,351
	Direct Charged	6,351
	Allocated	0
	Allocation Basis	N/A

### Comments

Normally this cost center is to have no costs charged to another SBC subsidiary other than SBC-Parent company. In 1991, SWBT was charged related to "SWBT absorbing communitel". (Data Request No. 254)



**064\*\* Group President**

This cost center includes all costs incurred within the Group President organization for the oversight of the national subsidiaries. These costs are to be direct charged only.

(Data Request No. 44)

Total 1991	SBC Costs	\$1,696,640
	Direct Charged	1,696,640
	Allocated	0
	Retained	0
	SWBT Costs	\$1,579
	Direct Charged	1,579
	Allocated	0
	Allocation Basis	N/A

**Comments**

Normally these costs are charged to SBC subsidiaries other than SWBT. However, \$1,579 was charged to SWBT in 1991.

**065\*\* Services Provided and Billed for Benefit Plans**

This cost center includes all services which are performed for and billed either to the trustee or to a subsidiary which may in turn bill to its respective trustee. Activities are performed to maintain the various pension benefits plans of the Corporation and its subsidiaries.

(Data Request No. 44)

Total 1991	SBC Costs	\$258,894
	Direct Charged	258,894
	Allocated	0
	Retained	258,894
	SWBT Costs	\$0
	Direct Charged	0
	Allocated	0
	Allocation Basis	N/A

**Comments**

No costs charged to SWBT in 1991.

**067\*\* Rate Case Activity**

This cost center includes the activities performed to support Southwestern Bell Telephone Company rate cases. This includes, but is not limited to:

- . Responses to information requests;
- . Testimony preparation;
- . Testimony and witness support;
- . Rate of return preparation and research.

This cost center on only be used to direct charge to Southwestern Bell Telephone Company's five states specifically. it is only to be used for specific rate case activity, only when SWBt is involved in such a case. All expenses must be accurately documented, including employee salary dollars charged.

(Data Request No. 44)

Total 1991	SBC Costs	\$154,786
	Direct Charged	154,786
	Allocated	0
	Retained	0
	SWBT Costs	\$154,786
	Direct Charged	154,786
	Allocated	0
	Allocation Basis	N/A

**Comments**

Nothing to note.

**068\*\* Financing Projects**

This cost center includes:

- . Activities related to the issuance, maintenance, or retirement of a specific debt issue or financing package;
- . Administrative and analytical activities associated with the above activities.

The interest cost and premium or discount amortization are not included in this category.

(Data Request No. 44)

Total 1991	SBC Costs	\$669,321
	Direct Charged	250,912
	Allocated	418,409
	Retained	2,938
	SWBT Costs	\$343,272
	Direct Charged	5,855
	Allocated	337,417
	Allocation Basis	Equity/Investment

**Comments**

Cost Center indicates activity related to debt. However, cost allocated based on equity investment. Allocation procedure would charge SWBT with high equity ratio, with cost related to debt. The allocation method eliminates possibility of an offsetting benefit to SWBT. SWBT can not even receive the benefit of a lower relative allocation of debt related costs, given SWBT higher equity ratio/lower debt ratio, to SBC operations with higher debt ratios such as SBIH.

**069\*\* Litigation (Specific Case)**

**This cost center includes:**

- Activities associated with specific legal cases;**
- Activities of the legal department and all support groups, such as external professionals or internal support of analysis or research.**

**Costs associated with federal claims must be identified with a specific Project identification.**

**(Data Request No. 44)**

<b>Total 1991</b>	<b>SBC Costs</b>	<b>\$1,728,654</b>
	Direct Charged	141,195
	Allocated	1,587,459
	Retained	9
	<b>SWBT Costs</b>	<b>\$1,197,572</b>
	Direct Charged	1,432
	Allocated	1,196,140
	Allocation Basis	General

**Comments**

**Cost center has high potential for being duplicative of SWBT activities. Data has not been received to determine whether duplication actually occurred.**

070\*\* Internal Audit Services

This cost center includes:

- Costs associated with internal audits conducted for the Corporation and its subsidiaries;
- Development issuance of corporate internal audit standards and procedures;
- Representation at the audit committee meetings of SBC's Board of Directors.

(Data Request No. 44)

Total 1991	SBC Costs	\$6,529,383
	Direct Charged	6,328,286
	Allocated	201,097
	Retained	0
	SWBT Costs	\$5,362,599
	Direct Charged	5,201,998
	Allocated	160,601
	Allocation Basis	Internal Audit

Comments

Nothing to note.

**071\*\* Corporate Services - Food Services**

**This cost center includes:**

**Activities and services related to the Executive Corporate Dining Facility.**

**(Data Request No. 44)**

<b>Total 1991</b>	<b>SBC Costs</b>	<b>\$628,634</b>
	Direct Charged	389,382
	Allocated	239,252
	Retained	0
	<b>SWBT Costs</b>	<b>\$598,075</b>
	Direct Charged	387,402
	Allocated	210,673
	Allocation Basis	Employee

**Comments**

The executive dining area is located on the 41st floor of One Bell Center (OBC). All fifth level and above managers can eat in the executive dining room. Lower level (1 through 4) managers cannot eat in the dining room unless they are with a fifth level or higher officer. Normal hours of operations were 6:30 a.m. until 1:30 p.m., Monday through Friday. It also was used occasionally for special evening functions. The corporate dining facility at OBC closed on January 1, 1993.

SBC Cost Allocation Manual states that "Most of the costs associated with these services will be directly billed to the benefitting entity." (Data Request Nos. 941 and 944)

The use of the employee allocator is inappropriate since only senior managers can use the facility. The direct allocation method is also flawed. The direct charges are actually allocated to each senior manager located in downtown St. Louis, whether they use the dining facility or not. The actual usage is maintained on an "Executive Account Log". (Data Request No. 941) These costs were disallowed since they represent unnecessary expenditures.

**072\*\* Corporate Services - Automotive**

This cost center includes:

Activities and expenses related to the Corporate Executive Ground Transportation Services.

(Data Request No. 44)

Total 1991	SBC Costs	\$892,867
	Direct Charged	330,667
	Allocated	562,200
	Retained	0
	SWBT Costs	\$810,133
	Direct Charged	314,381
	Allocated	495,752
	Allocation Basis	Employee

**Comments**

SBC's Policy on Company Automobiles for Executives states that:

An automobile will be provided to Company Executives on an unrestricted basis for use in conducting business affairs of the Company. It is also available for personal use. For tax purposes, all use will be personal. If required by Internal Revenue Service regulations, income will be imputed to the Executive; and additional withholding taxes will be credited to the Executive's payroll account.

....

**Model Selection Guidelines**

The following guidelines are for comparison purposes only and should not be interpreted as a recommendation of any particular make or model, but rather should be used as a general standard for cost and model comparison.

**Chairman**

The Chairman has flexibility to select a model and lease term consistent with the corporate image.

**Executive Policy Council (EPC)**

Members of the EPC have the flexibility to select a premium model consistent with the corporate image (excluding Lincoln, Cadillac, and Chrysler Imperial). Options will be selected at company expense subject



to the concurrence of the Senior Executive Vice President-Human Resource.

Executive in Salary Grade 31 and Above

The Executive may select a standard-equipped full-size model or substitute a mid-size model of lesser or equal value.

Executives in Salary Grades 29-30

The Executive may select a standard-equipped mid-size model.

NOTE: All vehicles should be equipped with an air bag restraint system on the driver's side and passenger's side where available.

....

Executive Automobile Administrative Guidelines include the following:

1. The operation of the vehicle will be limited to the Executive, spouse, and children when accompanied by the employee or spouse. Other SBC or subsidiary employees designated by the Executive to conduct official company business may also operate the vehicle.

....

The automobile will be provided on a closed-end agreement lease. The lease will be negotiated for a three-year term.

The following chart includes a vehicle selector list and an authorized funding level for each Executive Group. Selection will be limited to one of the vehicles on the list.

VEHICLE SELECTOR LIST

Group 1 - Chairman

Funding Level - N/A

The Chairman has flexibility to select a model and term of lease consistent with the corporate image.

Group 2 - Executive Policy Counsel

Funding Level - N/A

The Executive has flexibility to select a premium model consistent with the corporate image. Options may be selected at company expense.

Premium (4D Sedan)

Chrysler Fifth Avenue  
Buick Park Avenue  
Oldsmobile 98 Regency Elite  
Mercury Grand Marquis LS

**Group 3 - All Other Officers**

**Funding Level - \$18,700**

The Executive may select a full-size model from the following list or substitute a mid-size model.

Full-Size (4D Sedan)

Ford Crown Victoria LX  
Chevrolet Caprice Classic  
Chrysler LH Series  
Pontiac Bonneville SE

**Group 4 - Senior Managers (Below Officer Level)**

**Funding Level - \$14,800**

The Executive may select a mid-size or compact model from the following list.

Mid-Size (4D Sedan)

Buick Century LTD  
Ford Taurus GL  
Chevrolet Lumina Euro  
Oldsmobile Cutlass  
Dodge LH Series  
Mercury Sable GS  
Pontiac Grand Prix

**NOTES:**

1. Funding levels shown above reflect freight and air bags (if available) less fleet incentives. These funding levels will be reduced by any available lease company discount which may vary with each leasing company.
2. The Executive may select any of the standard-equipped models authorized within the appropriate Group. Optional equipment may be included at Company expense as long as the total price does not exceed the authorized funding level. Additional options, which increase the cost of the vehicle above the authorized funding level, will be included at personal expense.
3. The Executive will receive the benefit of rebates and other incentives whenever possible.

Options are to be selected by the Executive. Any options that will increase the cost of the vehicle above the authorized funding level will be purchased by the Executive at his/her own expense at ordering time. A "due date" for receipt of payment for such options, within 10 days, will be included on the billing transmittal letter. When payment is received, the new vehicle will be ordered.

....

### Insurance

Liability insurance will be purchased by the subsidiary to cover the Executive, spouse and children, when accompanied by the employee or spouse. This insurance covers both business and personal use. Some subsidiaries may choose to be self-insured.

### Fuel

The Company will provide one or more major credit cards to be used for the purchase of fuel. The credit card is to be used for fueling the assigned vehicle only. Current mileage should be noted on the credit card receipt.

If the Company parking space is on a motor pool lot that has a bulk fuel tank and attendant, arrangements can be made for fueling and washing.

### Maintenance

During the warranty period, all maintenance and report work will be performed by the delivering dealer or a nearby manufacturer's franchised dealer that will honor the warranty. After the warranty period, there are national accounts in Southwestern Bell Telephone (SWBT) Company's name with major suppliers that may be used. Instructions on the use of the national accounts can be obtained from the SWBT Automotive Group.

Arrangements may be made for monthly billing by the vendor or, if paid in full by the Executive, a voucher may be prepared for reimbursement.

(Data Request No. 705)

I recommended that the cost of this cost center be disallowed since purchase of automobiles for SBC executives is not a necessary expense, especially since the automobile can be used for personal use and driven by the executive's children. The employee allocator is also inappropriate for this cost center. These costs only apply to senior managers, not the entire SBC employee workforce.

074\*\* Corporate Services - Executive Air

This cost center includes:

Activities related to the provision of the Corporate Executive Air Transportation Services.

These costs are directly billed to the entity employing the company aircraft.

(Data Request No. 44)

Total 1991	SBC Costs	\$14,988,983
	Direct Charged	14,988,983
	Allocated	0
	Retained	3,949,449
	SWBT Costs	\$9,237,151
	Direct Charged	9,237,151
	Allocated	0
	Allocation Basis	N/A

Comments

SWBT-MO has indicated that they are not going to seek recovery of these costs. Adjustment is addressed in the direct testimony of John Cassidy.

**075\*\* Subsidiary Support**

**This cost center includes:**

- Work performed on special projects not includible in any other cost center,**
- Tasks performed specifically for the benefit of a subsidiary or group of subsidiaries.**

**These costs will be direct charged accordingly. Before applying this cost center to expenses, consideration must be given to other cost centers that may be more appropriate.**

**(Data Request No. 44)**

<b>Total 1991</b>	<b>SBC Costs</b>	<b>\$2,224,037</b>
	<b>Direct Charged</b>	<b>2,224,037</b>
	<b>Allocated</b>	<b>0</b>
	<b>Retained</b>	<b>60</b>
	<b>SWBT Costs</b>	<b>\$0</b>
	<b>Direct Charged</b>	<b>0</b>
	<b>Allocated</b>	<b>0</b>
	<b>Allocation Basis</b>	<b>N/A</b>

**Comments**

**Nothing to note.**

**07650 Art Program**

This cost center contains the costs associated with SBC's Art Program which is administered by the Corporate Communications Department. The costs of the actual artwork investment are not included in this cost center.

(Data Request No. 44)

Total 1991	SBC Costs	\$648,094
	Direct Charged	648,094
	Allocated	0
	Retained	648,094
	SWBT Costs	\$0
	Direct Charged	0
	Allocated	0
	Allocation Basis	N/A

**Comments**

Nothing to note.

**077\*\* Senior Management Benefit Expenses**

This cost center contains expenses for certain Senior Manager benefits, such as the Supplemental Retirement Income Plan, and is to only be used by the Controllers department.

(Data Request No. 44)

Total 1991	SBC Costs	\$15,369,802
	Direct Charged	5,954,042
	Allocated	9,415,760
	Retained	5,954,042
	SWBT Costs	\$8,295,323
	Direct Charged	0
	Allocated	8,295,323
	Allocation Basis	Employee

**Comments**

The SBC Supplemental Retirement Income Plan (SRIP) represents the only SBC Benefit Plan with expenses that are charged to this cost center. The SRIP is a benefit plan designed to provide retirement benefits in addition to those benefits provided under the management pension plan. The Company stated its objective is to reward key employees who have provided valuable services during their career with the Company. Only employees who have attained a salary grade of 29 or higher (Senior Management) are eligible for SRIP. The actual benefit for each employee is determined through a formula utilizing a service factor, salary grade, and salary with short-term award. In 1991, \$9,415,822 was charged to this cost center for the SRIP. (Data Request No. 1008)

The employee allocator is inappropriate for this cost center since a majority of SBC employees are not even eligible for these benefits. The expense are unnecessary. SRIP is designed actually to guarantee a minimum retirement benefit for SBC's senior managers. This minimum benefit is called a target percentage of final average total cash compensation. The target percentages of final average total cash compensation are chairman and chief executive officer, 75%; certain executive officers, 70%; other executive officers and other officers, 60%; and other senior managers, 50%. SRIP pays the difference, if any, between the target amount and what would be payable under the Management Pension Plan if the pension plan's payments were computed without regard to deferrals. The expenses have historically been retained by SBC and I believe such an approach is correct.

**078\*\* Benefit Payments**

This cost center includes management and nonmanagement pension plan payments which are paid by the Corporation on behalf of all subsidiaries. These expenses are to be directly charged to the appropriate subsidiaries. Pension plan payments made for Parent company employees should be charged to cost center (9400).

(Data Request No. 44)

Total 1991	SBC Costs	\$5,108,171
	Direct Charged	5,108,171
	Allocated	0
	Retained	0
	SWBT Costs	\$0
	Direct Charged	0
	Allocated	0
	Allocation Basis	N/A

**Comments**

Nothing to note.



0789\*\*

Legal Support

This cost center includes:

- . General legal advice and counsel to specific subsidiaries;
- . Assistance in preparation of legal forms;
- . Corporate governance.

(Data Request No. 44)

Total 1991	SBC Costs	\$1,682,843
	Direct Charged	1,682,843
	Allocated	0
	Retained	0
	SWBT Costs	\$443
	Direct Charged	443
	Allocated	0
	Allocation Basis	N/A

Comments

Nothing to note.

**080\*\* Corporate Advertising**

This advertising program is consumer oriented with the purpose of promoting the Southwestern Bell name and image.

This cost center includes:

- . Administration of the "corporate" advertising program;
- . Development of the overall direction of the "corporate" advertising program;
- . Engaging and working with advertising firms in developing the various advertising campaigns;
- . Campaign effectiveness research.

(Data Request No. 44)

Total 1991	SBC Costs	\$9,336,837
	Direct Charged	843,951
	Allocated	8,492,886
	Retained	1,390,667
	SWBT Costs	\$4,225,973
	Direct Charged	0
	Allocated	4,225,973
	Allocation Basis	Marketing Factor

**Comments**

Addressed in Direct Testimony of John Cassidy.

081\*\* Marketing Support

This cost center includes:

- Producing, packaging, and distributing on-going communication to key external audiences (targeted subsidiary customers, key financing and community leaders, regulators, and media);
- Expenses incurred which are associated with Update magazine.

Publications such as Update serve as information, sales and positioning tools for the Corporation and its subsidiaries.

(Data Request No. 44)

Total 1991	SBC Costs	\$14,325,957
	Direct Charged	3,628,277
	Allocated	10,697,680
	Retained	3,596,591
	SWBT Costs	\$5,421,741
	Direct Charged	178,757
	Allocated	5,242,984
	Allocation Basis	Marketing Factor

Comments

Cost center contains expenses related to 1) sponsorship of "Smithsonian World" on public television, 2) \$252,000 for SBC Colonial Golf Tournament, 3) \$795,000 for Colonial and Senior Golf Classics, 4) Ben Hogan Golf Tourney, and 5) payments to Ray Floyd, golfer. (Data Request No. 254) Costs in this cost center are unnecessary. These costs have similar characteristics with institutional advertising which is disallowed by the Missouri Public Service Commission. I recommend these costs be disallowed from SWBT-MO's cost of service.