

Confidential Release

Case Number:

93-487-TP-ALT

93-576-TP-CSS

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Direct Testimony of David Effron.

NONPUBLIC VERSION

THE OHIO BELL TELEPHONE COMPANY

**CASE NO. 93-487-TP-ALT
Direct Testimony**

**CASE NO. 93-576-TP-CSS
Supplemental Direct Testimony**

**OF
DAVID J. EFFRON**

**ON BEHALF OF THE
OFFICE OF THE CONSUMERS' COUNSEL
STATE OF OHIO**

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MAY 5, 1994

1 Q. Please state your name and business address.

2 A. My name is David J. Effron. My business address is 386 Main
3 Street, Ridgefield, Connecticut 06877.

4

5 Q. Have you previously filed testimony in OCC's complaint case,
6 Case No. 93-576-TP-CSS?

7 A. Yes. I filed testimony in Case No. 93-576-TP-CSS which
8 addressed and quantified certain rate base and operating
9 income issues. I hereby incorporate by reference that
10 testimony in its entirety into Case No. 93-487-TP-ALT.
11 References herein to my "previous," "prior," or "initial
12 direct" testimony are to my testimony filed in OCC's Complaint
13 case.

14

15 Q. Mr. Effron, is the incorporation of your prior testimony into
16 Case No. 93-487-TP-ALT the sole purpose of this supplemental
17 testimony?

18 A. No. In my initial direct testimony, I presented certain
19 adjustments to the Company's determination of rate base and
20 operating income which it presented in the standard filing
21 requirements in Case No. 93-487-TP-ALT. The purpose of this
22 supplemental testimony is to explain how the adjustments which
23 I presented in my initial direct testimony relate to the Staff
24 Report in Case No. 93-487-TP-ALT. The purpose of this
25 testimony is thus to present certain adjustments to rate base
26 and operating income as presented by Staff in the Staff

1 Report.

2

3 Q. Have you prepared schedules which summarize your proposed
4 adjustments to the Staff Report?

5 A. Yes. I have prepared Schedules DJE-1A through DJE-6A. These
6 schedules are analogous to Schedules DJE-1 through DJE-6
7 accompanying my previous testimony. However, Schedules DJE-1A
8 through DJE-6A quantify adjustments to the rate base and
9 operating income presented in the Staff Report, rather than
10 the rate base and operating income as presented by the Company
11 in the Standard Filing Requirements. These schedules, as
12 relevant, have been provided to Mr. Chan to incorporate into
13 his calculation of Ohio Bell's revenue excess.

14

15 A. DIRECTORY REVENUES

16 Q. Is any adjustment necessary to the Directory Revenue reflected
17 in the Staff Report?

18 A. No. Staff did not reflect the Company's proposed adjustment
19 to eliminate API related revenues from the test year. In
20 fact, Staff proposed an adjustment to increase the test year
21 Directory Revenue "to reflect a more compensatory rate per
22 access line." In my opinion, Staff's adjustment to reflect
23 a more compensatory rate per access line is appropriate.

24

25 Q. If you believe that Staff's adjustment to reflect a more
26 compensatory rate per access line is appropriate, why did you

1 not propose any such adjustment in your initial direct
2 testimony?

3 A. At the time that I prepared my initial direct testimony, I did
4 not have the information available to quantify such an
5 adjustment. Since that time I have obtained information which
6 clearly indicates that an adjustment to increase directory
7 revenues is proper.

8

9 Q. What information have you obtained that would indicate that
10 Staff's adjustment to reflect a more compensatory rate per
11 access line is appropriate?

12 A. This information is summarized on Schedule DJE-1A, page 2. As
13 can be seen on this schedule, the agreement between API and
14 Ohio Bell has resulted in a steadily declining percentage of
15 API net billings for directory advertising in the Ohio Bell
16 service territory being remitted to Ohio Bell. The Ohio Bell
17 compensation (sum certain) as a percentage of API net billings
18 has declined from 56.79% in 1986 to 44.44% in 1993. This
19 decline has resulted in a reduction of the contribution from
20 directory advertising to Ohio Bell's net income. This results
21 in an increase to the level of revenues that must be generated
22 by Ohio Bell's regulated services.

23 As I stated in my initial direct testimony, as a matter
24 of policy, a regulated utility company should not be able to
25 unilaterally transfer one of the most profitable segments of
26 its business to an unregulated subsidiary or affiliate,

1 thereby increasing the level of revenues that must be
2 generated by its regulated services. If the payment to Ohio
3 Bell had been maintained at a percentage of API net billings
4 equal to the percentage at the time of the transfer of Yellow
5 Pages to API, the payment would be significantly greater than
6 that actually received by OBT. Therefore, I believe that
7 Staff's adjustment to reflect a more compensatory rate per
8 access line is appropriate.

9
10 Q. Since you believe that Staff's adjustment to reflect a more
11 compensatory rate per access line is appropriate, then what
12 does your calculation on Schedule DJE-1A, page 1 represent?

13 A. My calculation on Schedule DJE-1A, page 1, represents an
14 alternative to Staff's adjustment on Schedule C-3.3 of the
15 Staff Report. There are different methods for computing an
16 adjustment to test year directory revenues to reflect a more
17 compensatory rate per access line. My adjustment on Schedule
18 DJE-1A, page 1 reflects what the adjustment to test year
19 directory revenues would be if the sum certain paid to Ohio
20 Bell for the twelve months ended September 30, 1993 was equal
21 to 55.27% of the API net billings for that period. The 55.27%
22 figure represents the sum certain as a percentage of API net
23 billings for the years 1985 - 1987, which were the first three
24 full years after the transfer of Yellow Pages to API. While
25 I do not believe that Staff's adjustment is inappropriate, I
26 believe that the alternative which appears on my Schedule DJE-

1 1A is also reasonable.

2 Because I am not proposing to substitute my adjustment on
3 Schedule DJE-1A, page 1 for that of Staff, it is not necessary
4 to incorporate this adjustment into the determination of
5 adjusted net operating income that uses the operating income
6 in the Staff Report as a starting point.

7
8 B. MANAGEMENT SEPARATION PLAN

9 Q. Is it necessary to make the adjustment which you proposed in
10 your initial direct testimony, related to the elimination of
11 the accrual for the management separation plan, to Staff's
12 determination of adjusted net operating income?

13 A. No. Schedule C-3.7 of the Staff Report reflects an adjustment
14 to eliminate "Applicant's FASB 106 Curtailment Loss
15 Amortization." This is the major component of the management
16 separation plan accrual. Therefore, the adjustment which I
17 quantified on Schedule DJE-2 of my initial direct testimony is
18 not necessary. However, if the Commission should, for any
19 reason, reject Staff's elimination of the curtailment loss,
20 then the adjustment on Schedule DJE-2 accompanying my initial
21 direct testimony would be appropriate.

22
23 C. POST-RETIREMENT BENEFITS EXPENSE OTHER THAN PENSIONS

24 Q. Is it necessary to make an adjustment to the post-retirement
25 benefits expense other than pensions ("OPEB") reflected by
26 Staff?

1 A. No. In my initial direct testimony, I quantified an
2 adjustment to the amortization of the transition obligation
3 reflected by the Company. However, Staff has eliminated the
4 amortization of the transition obligation in its entirety.
5 Therefore, no adjustment is necessary.

6 However, if the Commission should, for any reason,
7 determine that the amortization of the transition obligation
8 should be reflected in the cost of service, then I continue to
9 believe that the twenty year amortization period would be
10 appropriate, as explained in my initial direct testimony. On
11 Schedule DJE-3A, I have recalculated the adjustment necessary
12 to modify the amortization period from the 18 years reflected
13 by the Company to 20 years, as I am proposing. If the
14 Commission does determine that a 20 year amortization period
15 would be appropriate, then the adjustment reflected on my
16 Schedule DJE-3A, which is a revision to the adjustment on my
17 original Schedule DJE-3, should be used.

18

19 D. POST-EMPLOYMENT BENEFITS (SFAS 112)

20 Q. Is any adjustment to Staff's pro forma operating income
21 necessary to modify the treatment of SFAS 112 in the Staff
22 Report?

23 A. No. Staff did not reflect the SFAS 112 transitional
24 obligation in the determination of its pro forma net operating
25 income. Therefore, no adjustment is necessary to eliminate
26 or modify the treatment of the SFAS 112 transitional

1 obligation.

2

3 E. DEPRECIATION EXPENSE

4 Q. Is it necessary to make an adjustment to the depreciation
5 expense presented in the Staff Report?

6 A. Yes. Jurisdictional depreciation expense is calculated on
7 Schedule B-3.3 of the Staff Report. Page 2 of that schedule
8 indicates a reserve deficiency amortization of \$13,531,000.
9 related to Account 2211 - Analog Electronic Switching, All
10 Other. As I explained in my initial direct testimony, I do
11 not believe that any of the calculated depreciation reserve
12 deficiency in Account 2211 should be subject to special
13 amortization on a prospective basis. Therefore, on my
14 Schedule DJE-5A, I show the effect of eliminating Staff's
15 reserve deficiency amortization for Account 2211 from pro
16 forma depreciation expense. As can be seen on this schedule,
17 eliminating Staff's reserve deficiency amortization for
18 Account 2211 reduces pro forma test year depreciation expense
19 by \$13,531,000.

20

21 F. INTEREST DEDUCTION FOR INCOME TAXES

22 Q. Has Staff used the proper method to calculate the interest
23 deduction for income taxes?

24 A. Yes. Schedule C-4.1, page 1 of the Staff Report properly
25 synchronizes the interest deduction for income taxes with
26 Staff's calculation of rate base and the weighted cost of debt

1 reflected in Staff's capital structure. Therefore, no
2 adjustment is necessary to the interest deduction for income
3 taxes, given Staff's rate base and weighted cost of debt. The
4 interest deduction for income taxes reflected in the OCC's
5 determination of operating income incorporates the OCC's rate
6 base and cost of debt.

7

8 Q. Does this conclude your testimony?

9 A. Yes. However, I reserve the right to modify or amend my
10 testimony based on responses to additional discovery, changes
11 to Staff's position as presented in the Staff Report, and
12 changes to the Company's position as presented in its filings.

13

**OHIO BELL TELEPHONE COMPANY
ALTERNATIVE TO STAFF DIRECTORY REVENUE ADJUSTMENT
(\$000)**

API Net Billings - OBT Yellow Pages 12 Mos. Ended 9/93	(A)	\$191,680
Average Sum Certain Percentage of API Billings 1985-87	(B)	55.27%
Adjusted API Revenues to OBT		105,937
Test Year API Revenue to OBT, per Books	(C)	85,598
Adjustment to API Revenue		<u>\$20,339</u>

Sources:

- (A) Response to Staff Data Request 40**
- (B) Schedule DJE-1A, Page 2**
- (C) Company Exhibit 93C-3.13**

**OHIO BELL TELEPHONE COMPANY
YELLOW PAGE REVENUES
(\$000)**

YEAR	API Net Billings	OBT Sum Certain	Sum Certain Percent
1985	124,641	69,681	55.91%
1986	127,673	72,500	56.79%
1987	141,190	75,300	53.33%
1988	153,052	78,100	51.03%
1989	165,254	80,700	48.83%
1990	175,464	83,400	47.53%
1991	181,201	83,986	46.35%
1992	185,507	84,810	45.72%
1993*	177,515	78,881	44.44%
Avg. Annual Growth 1985-1993	5.66%	2.67%	
1986-1993	6.13%	2.48%	
Average 1985-1987			55.27%

* 11 Months

Source: Response to Staff Data Request 40

Schedule DJE-2A

**OHIO BELL TELEPHONE COMPANY
MANAGEMENT SEPARATION PLAN AND OUTPLACEMENT COSTS
(\$000)**

Subsumed in Staff's elimination of curtailment loss on Schedule C-3.7

Schedule DJE-3A

**OHIO BELL TELEPHONE COMPANY
ALTERNATIVE TO STAFF TREATMENT OF
TRANSITION OBLIGATION AMORTIZATION
(\$000)**

Amortization of SFAS 106 Transition Obligation	(A)	\$25,773
Company Amortization Period	(B)	<u>18</u>
Transition Obligation		463,914
Proposed Amortization Period		<u>20</u>
Annual Amortization		<u>\$23,196</u>
Adjustment to Annual Amortization		(\$2,577)
Charged to Expense	0.8825 (D)	(\$2,274)
Charged to Regulated Operations	0.9351 (C)	(\$2,127)
Jurisdictional Expense Adjustment	0.7751 (C)	<u>(\$1,648)</u>

Sources:

- (A) Response to OCC RFPD 130
- (B) Ohio Bell Exhibit 31.0, page 33
- (C) Company Workpaper WP 93C-3.7 (1-.0649)
- (D) Company Workpaper WP 93C-1.5a

Schedule DJE-4A

**OHIO BELL TELEPHONE COMPANY
SFAS 112 (POST-EMPLOYMENT BENEFITS)
(\$000)**

Amortization of SFAS 112 Transition Obligation not reflected in Staff Report.

Schedule DJE-5A

OHIO BELL TELEPHONE COMPANY
DEPRECIATION RESERVE DEFICIENCY AMORTIZATION
(\$000)

Staff Juris. Amort. of Res. Deficiency - A/C 2211	(A)	<u>(\$13,531)</u>
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Income Tax Adjustments:

Adjustment to Unallowable Depreciation	0.0603	(B)	(816)
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Adjustment to Tax SL Depreciation			<u>(\$12,715)</u>
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Adjustment to ITC Amortization	0.0475	(B)	<u>(\$604)</u>
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Sources:

(A) Staff Report, Schedule B-3.3, Page 2

(B) Company Workpaper WP 93C-2.2b

Schedule DJE-6A

**OHIO BELL TELEPHONE COMPANY
INTEREST SYNCHRONIZATION
(\$000)**

Staff's interest deduction properly synchronized.

CERTIFICATE OF SERVICE

I hereby certify that copies of the *Non-Public Version* *Direct/Supplemental Testimony of David J. Effron*, have been served by first class mail, postage prepaid, or hand-delivered to the following parties of record this 5th day of May, 1994.


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