JOINT BOARD FOR TELEPHONE SEPARATIONS

HEARINGS

BEFORE THE

SUBCOMMITTEE ON COMMUNICATIONS AND POWER

OF THE

COMMITTEE ON INTERSTATE AND FOREIGN COMMERCE HOUSE OF REPRESENTATIVES

NINETY-FIRST CONGRESS

SECOND SESSION

ON

H.R. 12150

A BILL TO AMEND THE COMMUNICATIONS ACT OF 1934, AS AMENDED, TO ESTABLISH A FEDERAL-STATE JOINT BOARD TO PRESCRIBE UNIFORM PROCEDURES FOR DETERMINING WHAT PART OF THE PROPERTY AND EXPENSES OF COMMUNICATION COMMON CARRIERS SHALL BE CONSIDERED AS USED IN INTERSTATE OR FOREIGN COMMUNICATION TOLL SERVICE, AND WHAT PART OF SUCH PROPERTY AND EXPENSES SHALL BE CONSIDERED AS USED IN INTRASTATE AND EXCHANGE SERVICE, AND FOR OTHER PURPOSES

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JOINT BOARD FOR TELEPHONE SEPARATIONS

TUESDAY, FEBRUARY 24, 1970

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON COMMUNICATIONS AND POWER,
COMMITTEE ON INTERSTATE AND FOREIGN COMMERCE,
Washington, D.C.

The subcommittee met at 10 a.m., pursuant to notice, in room 2322, Rayburn House Office Building, Hon. Torbert H. Macdonald (chairman of the subcommittee) presiding.

Mr. MACDONALD. The subcommittee will come to order.

This morning the Subcommittee on Communications and Power begins hearings on H.R. 12150, which was introduced by our colleague, Congressman Fred Rooney of Pennsylvania.

As most of those who are present here today know, regulatory jurisdiction over the telephone industry is divided between the Federal Communications Commission and the regulatory commissions of the several States. The FCC regulates interstate and foreign telephone rates, and the State commissions regulate intrastate and local rates. These rates are determined in terms of plant and operating expenses involved in furnishing the telephone service. The combination of Federal and State regulation results in a situation of extreme complexity because most telephone plant and expenses are devoted to providing users with both interstate and intrastate telephone service. Therefore, telephone plant and expenses over the years have been allocated, or in the jargon of the industry, "separated" as between interstate and intrastate uses for purposes of ratemaking.

The bill before the subcommittee would establish a Federal-State Joint Board to prescribe uniform procedures for determining the portion of the plant and expenses of telephone companies which would be attributed to interstate and foreign operations and the portion which would be attributed to intrastate operations. Thus, the joint board would carry out certain functions now performed by the FCC.

The joint board would consist of four members of the FCC and three State regulatory commissioners nominated by the National Association of Regulatory Utility Commissioners (NARUC).

This hearing takes place shortly after a reduction of $237 million per year in interstate rates has gone into effect with respect to the Bell Telephone Systems, and at a time when over one-half billion dollars in rate increases are pending before the State regulatory commissions. The Association of State Commissioners contends that the separation procedures which have brought about this situation are inequitable.

I am informed that discussions at the staff level are currently underway between the FCC and the State commissions on the problem of telephone separations. We shall expect to be informed on the progress of these discussions in the course of these hearings.

Our purpose in these hearings will be to determine whether existing telephone separation procedures operate in the public interest and, if not, whether H.R. 12150 or some other alternative would best serve the public interest.

(The text of H.R. 12150 and departmental report thereon follows:)

[H.R. 12150, 91st Cong., 1st Sess., introduced by Mr. Rooney of Pennsylvania (by request) on June 16, 1969]

A BILL To amend the Communications Act of 1934, as amended, to establish a Federal-State Joint Board to prescribe uniform procedures for determining what part of the property and expenses of communication common carriers shall be considered as used in interstate or foreign communication toll service, and what part of such property and expenses shall be considered as used in intrastate and exchange service, and for other purposes

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as the "Federal-State Communications Joint Board Act of 1969."

SEC. 2. The Communications Act of 1934, as amended, is further amended by striking subsections (c) and (d) of section 221 and inserting in lieu thereof the following:

"(c) There is hereby established a Federal-State Joint Board (hereinafter defined) vested with sole administrative authority under this Act to adopt and amend from time to time by order uniform procedures for determining what part of the property and expenses of common carriers engaged in wire or radio communication shall be considered as used in interstate or foreign communication toll service subject to the jurisdiction of the Commission, and what part of such property and expenses shall be considered as used in intrastate, exchange or other communication service not subject to the jurisdiction of the Commission. Such uniform procedures shall be determined after opportunity for hearing, upon notice to each affected carrier, the State commission (or the Governor, if the State has no State commission) of any State in which the property of such carrier is located, and such other persons as the Federal-State Joint Board prescribe. The establishment of the Federal-State Joint Board shall not impair in any way the right of any State commission, the national organization of the State commissions, hereinafter referred to, or any other interested party to advocate its position on issues before such Board, to submit evidence and oral argument concerning same, and to seek reconsideration and judicial review of the Board's decisions.

"(d) The Federal-State Joint Board shall be composed of four Commissioners of the Commission designated by the Commission, and three commissioners of State commissions, nominated by the national organization of the State commissions, as referred to in sections 202(b) and 205(f) of the Interstate Commerce Act, as amended, and appointed by the Commission. The Commission shall designate one of the members of the Board as Chairman.

"(e) Each State commissioner member of the Federal-State Joint Board shall be selected in the following manner. The national organization of the State commissions or a committee designated by it shall nominate one, two, or three State commissioners, as requested by the Commission, and certify the name, title, and address of each nominee to the Commission within ninety days after the date this Act becomes law, or at least ninety days prior to the expiration of the term of an incumbent State commissioner, or within thirty days after a vacancy occurs in the office, as the case may be. Within thirty days after receipt of such certification, the Commission shall appoint the nominee or one of the nominees as a member of the Federal-State Joint Board. In any case where the national organization of the State commissions fails to so nominate and certify State commissioners within the prescribed time, the Commission shall appoint a State commissioner as a member of the Board to serve in lieu of the nominee it would have otherwise appointed.

"(f) Each State commissioner member of the Federal-State Joint Board shall hold office for a term of three years, except that (1) any member appointed to fill a vacancy occurring prior to the expiration of the term for which his predecessor was appointed shall be appointed for the remainder of such term, and (2) the terms of office of members first taking office after the date this Act becomes law shall expire as follows: one at the end of one year after such date, one at the end of two years after such date, and one at the end of three years after such date, as designated by the Commission at the time of appointment, and (3) the term of any member shall be extended until the date on which the successor's appointment is effective. The office of a State commissioner member of the Board shall become vacant upon the incumbent ceasing to be a State commissioner.

"(g) A State commissioner member of the Federal-State Joint Board shall, while attending meetings or hearings of such Board or otherwise engaged in the business of such Board, be entitled to receive compensation at a rate fixed by the Commission, but not exceeding $100 per diem, including traveltime, and while away from his home or regular place of business he may be allowed travel expenses, including per diem in lieu of subsistence, as authorized in section 5 of the Administrative Expenses Act of 1946 (5 U.S.C. 73b–2) for persons in the Government service employed intermittently. Payments under this section shall not render a State commissioner member of the Board an employee or official of the United States for any purpose.

"(h) The Federal-State Joint Board shall meet from time to time upon the call of the Chairman of the Board or of three members of the Board. A majority of the members of the Board shall constitute a quorum. Each member of the Board shall have one vote. All decisions of the Board shall be by majority vote. The Commission shall designate an examiner to advise with and assist the Board in the handling of any proceedings before it. The Commission shall provide the Board from among the personnel and facilities of the Commission such staff and facilities as are necessary to carry out the functions of the Board. In conducting hearings, the Board, within the scope of its authority, shall be vested with the same rights, duties, and powers as are vested in the Commission in holding a hearing. An order of the Board shall be deemed an order of the Commission for purposes of judicial review.

"(i) In making a valuation of the property of any telephone carrier, the Commission, after the adoption of the uniform procedures authorized in subsection (c) of this section, may in its discretion value only that part of the property of such carrier determined to be used in interstate or foreign communication toll service."

EXECUTIVE OFFICE OF THE PRESIDENT,
BUREAU OF THE BUDGET,
Washington, D.C., March 10, 1970.

Hon. HARLEY O. STAGGERS,
Chairman, Committee on Interstate and Foreign Commerce, House of Representatives, Rayburn House Office Building, Washington, D.C.

DEAR MR. CHAIRMAN: This is in response to your request for the views of the Bureau of the Budget on H.R. 12150, a bill, "To amend the Communications Act of 1934, as amended, to establish a Federal-State Joint Board to prescribe uniform procedures for determing what part of the property and expenses of communication common carriers shall be considered as used in interstate or foreign communication toll service, and what part of such property and expenses shall be considered as used in intrastate and exchange service, and for other purposes."

The Bureau of the Budget concurs in the views of the Federal Communications Commission which endorse the promotion of the excellent Federal-State cooperation which has resulted in improved regulatory procedures. However, for the reasons expressed by Chairman Burch in testimony before your committee last week, the Bureau does not favor enactment of H.R. 12150.

Sincerely,

WILFRED H. ROMMEL,
Assistant Director for Legislative Reference.

Mr. MACDONALD. Our first witness this morning is Mr. Francis Pearson, president of the National Association of Regulatory Utility Commissioners. To introduce him, we will hear from our distinguished colleague, not of the subcommittee but of the full committee, Mr. Brock Adams.

STATEMENT OF HON. BROCK ADAMS, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF WASHINGTON

Mr. ADAMS. Mr. Pearson, it is a great pleasure for me to welcome you here.

Mr. Chairman, I have known Mr. Pearson for many years. He has been the chairman of the Utilities Commission of the State of Washington for a number of years, and he is very experienced in these matters. We are very pleased that he is president this year of the National Association of Regulatory Utility Commissioners, and that he has brought with him a number of his colleagues for the hearings you will be holding on this bill.

Many of us who are on the full committee have other commitments this morning on the subcommittees, so if you see some of us moving in and out of the rooms, you will understand we are going to other subcommittee meetings. We are very interested in this bill, and we will be following the presentation of the matter to the full committee. We are very grateful to you, Mr. Chairman, for holding this hearing this morning so Mr. Pearson and his colleagues could present their position and offer solutions to this very perplexing question.

We are also grateful to Mr. Rooney for having shown fine leadership by introducing this bill and seeing that it was brought before the committee today.

Again, welcome, Mr. Pearson, to you and your colleagues, and thank you, Mr. Chairman, for allowing me to introduce our first witness this morning.

Mr. MACDONALD. Thank you, Mr. Adams.

We would be pleased to hear from you, Mr. Pearson.

STATEMENTS OF FRANCIS PEARSON, PRESIDENT, NATIONAL ASSOCIATION OF REGULATORY UTILITY COMMISSIONERS, AND MEMBER, UTILITIES AND TRANSPORTATION COMMISSION OF THE STATE OF WASHINGTON; GEORGE I. BLOOM, FIRST VICE PRESIDENT, NARUC, AND CHAIRMAN, PENNSYLVANIA PUBLIC UTILITY COMMISSION; FRANCIS J. RIORDAN, SECOND VICE PRESIDENT, NARUC, AND CHAIRMAN OF NEW HAMPSHIRE PUBLIC UTILITIES COMMISSION; BEN T. WIGGINS, CHAIRMAN OF THE NARUC COMMITTEE ON COMMUNICATIONS, AND VICE CHAIRMAN OF THE GEORGIA PUBLIC SERVICE COMMISSION; ARCHIE SMITH, CHAIRMAN OF THE RHODE ISLAND PUBLIC UTILITIES COMMISSION; AND WILLIAM SYMONS, PRESIDENT OF THE CALIFORNIA PUBLIC UTILITIES COMMISSION; ACCOMPANIED BY A. L. HUTCHINSON, CHAIRMAN OF THE NARUC SUBCOMMITTEE OF STAFF EXPERTS, AND EXECUTIVE DIRECTOR, KENTUCKY PUBLIC SERVICE COMMISSION; P. M. SCHUCHART, CHAIRMAN, NARUC STAFF SUBCOMMITTEE ON SEPARATIONS AND TOLL RATE DISPARITY, AND ENGINEER FOR THE PENNSYLVANIA PUBLIC UTILITY COMMISSION; AND PAUL RODGERS, GENERAL COUNSEL OF THE NARUC

Mr. PEARSON. Thank you, Mr. Chairman.

I think you might have Brock Adams around here for awhile. I attended a little function recently out in Seattle which raised a dollar or two for him.

Mr. MACDONALD. That is good news for all of us.

Mr. PEARSON. After serving for a number of years in the Washington State Senate, I resigned to become chairman of the Washington State Utilities and Transportation Commission. I was appointed once by a Democratic Governor and then by a Republican Governor and I am now serving my third term there.

I have with me at the head table, and who will make a portion of the presentation this morning, the Honorable George I. Bloom, first vice president of NARUC and chairman of the Pennsylvania Public Utility Commission. Mr. Bloom.

Secondly, Mr. Archie Smith, chairman of the Rhode Island Public Utilities Commission.

We also have the vice chairman of the Georgia Public Service Commission, Mr. Benjamin T. Wiggins who has also been chairman of the Communications Committee of the NARUC and has been working with the separations problem for many, many years.

We also have the honorable president of the California Public Utilities Commission, who is facing some big problems in the State of California, Mr. William Symons.

We also have with us Mr. A. L. Hutchinson, chairman of the NARUC Subcommittee of Staff Experts and executive director of the Kentucky Public Service Commission.

We also have Mr. P. M. Schuchart, chairman of the NARUC Staff Subcommittee on Separations and Toll Rate Disparity and engineer for the Pennsylvania Public Utility Commission.

We also have with us our general counsel, the Honorable Paul Rodgers whom you folks no doubt see from time to time.

Also present today are the following NARUC representatives:

Chairman Edward H. Boyett of the Arkansas Commerce Commission, Commissioner Robert C. Downie and Commissioner Don S. Smith of the Arkansas Public Service Commission; Commissioner John P. Vukasin, Jr., of the California Public Utilities Commission; Commissioner Harold F. Keith of the Connecticut Public Utilities Commission; Chairman George A. Avery and Commissioner William L. Porter of the District of Columbia Public Service Commission; Commissioner Walter R. McDonald of the Georgia Public Service Commission; President Ralph H. Wickberg of the Idaho Public Utilities Commission; Chairman David H. Armstrong and Telephone Engineer John Kissel of the Illinois Commerce Commission.

Chairman Dale E. Saffels and Assistant General Counsel Dan Sullivan of the Kansas State Corporation Commission; Chairman Nat B. Knight, Jr., of the Louisiana Public Service Commission; Chairman John G. Feehan of the Maine Public Utilities Commission; Chairman William O. Doub and Chief Auditor E. Edward McLean of the Maryland Public Service Commission; Commissioner Paul A. Rasmussen of the Minnesota Public Service Commission; Commissioner Norman A. Johnson, Jr., of the Mississippi Public Service Commission; Chairman William R. Clark of the Missouri Public Service Commission; Commissioner Fred N. Peterson and Commissioner Joseph J. Brown of the Nebraska State Railway Commission.

Chairman Reese H. Taylor, Jr., and Commissioner Noel A. Clark of the Nevada Public Service Commission; Chief of Telephone Bureau Thomas J. Brady of the New York Public Service Commission; Chairman Harry T. Westcott and Commissioner Marvin R. Wooten of the North Carolina Utilities Commission; President E. Bruce Hagen, Commissioner Richard Elkin and Commissioner Ben J. Wolf of the North Dakota Public Service Commission; Chairman Charles Nesbitt and Commissioner Ray C. Jones of the Oklahoma Corporation Commission; Commissioner Sam R. Haley, Oregon Public Utility Commission; Commissioner William F. O'Hara of the Pennsylvania Public Utility Commission.

Chairman Cayce L. Pentecost of the Tennessee Public Service Commission; Commissioner Jesse W. Dillon of the Virginia State Corporation Commission; Chairman Robert D. Timm of the Washington Utilities and Transportation Commission; Chairman Elizabeth V. Hallanan, Commissioner Boyce Griffith and Commissioner Robert L. Stewart of the West Virginia Public Service Commission; Chairman Arthur L. Padrutt and Chief of Rates and Research Division Orville P. Deuel of the Wisconsin Public Service Commission; Chairman Walter W. Hudson of the Wyoming Public Service Commission; and NARUC Secretary-Treasurer Everette Kreeger.

Mr. MACDONALD. Mr. Rooney.

Mr. ROONEY. Thank you, Mr. Chairman.

I would like to take this opportunity to welcome George I. Bloom to this committee meeting this morning. Mr. Bloom brought to my attention the problem between the States and the FCC and this bill was introduced at his request.

Mr. Bloom is not new to Washington. He has been here for many years. He served as an assistant to the late Senator Martin and like you, Mr. Pearson, he is respected on both sides of the aisle in Pennsylvania. We are very proud of Mr. Bloom and his dedicated service to the great Commonwealth of Pennsylvania, and I welcome you to Washington today.

Mr. PEARSON. I would like to introduce our second vice president, the Honorable Francis J. Riordan of the New Hampshire Commission, who will introduce the States that are represented here, and they have their statements which they will present for the record. I hope you realize it is hard to get people from all over the United States to come to these hearings, but I think we will show you we are serious and we have made an all-out effort in this regard.

STATEMENT OF FRANCIS J. RIORDAN

Mr. RIORDAN. Thank you. I am Francis J. Riordan, chairman of the New Hampshire Public Utilities Commission. I will attempt to make this presentation as accurately as possible, but since I left Logan Airport at 7 o'clock this morning and some of these gentlemen just came in fairly recently, I will proceed to the best of my ability to introduce them. As I do, I would ask that those desiring to make a presentation present to the reporter one copy of the statement they want to have inserted in the record and the balance they can see the clerk gets for his records.

We have with us today from the Arkansas Commerce Commission, Edward H. Boyett, Robert C. Downie and Edward W. Davis. Mr. Boyett, do you have a statement?

Mr. DOWNIE. My name is Downie and, yes, Mr. Chairman, we do have a statement by our Commission which I would like to offer in support of the bill.

Mr. MACDONALD. It will be received for the record at this time, without objection.

(The statement follows:)

STATEMENT OF THE ARKANSAS PUBLIC SERVICE COMMISSION

This commission supports Senate bill S. 1917 and hereby supports the same provisions of House bill H.R. 12150 which upon passage will give this State agency a needed voice in future negotiations on the allowable interstate telephone revenues of the A.T. & T. system.

The results of present separations procedures continue to favor that select category of telephone customers, who by reason of affluence, preference or both, continue to reap harvests of favorable rates for their out of State calling. This is at the expense of their economically overburdened neighbors, who of human necessity must limit their telephone usage to local or infrequent interexchange toll calling. This represents an inequity which if allowed to continue will eventually, if it has not already, deprive many citizens in Arkansas of any telephone service.

The local exchange rates in Arkansas have been maintained at a relatively stable level over the past three years. This can be attributed to a combination of more rapid additions of subscriber stations to existing plant, economies of new plant automation and regulatory insistence on good service prior to considering applications for rate relief. At the same time this commission is aware that with the existing inflationary pressures on the cost of service, any incident which would impose a reduction in any sector of the telephone companies' revenues, such as for interstate toll or the settlements therefrom, would undoubtedly set off a round of applications for general exchange rate and intrastate toll increases to make up for the lost revenues. Thus again this commission, with no voice in a decision to reduce interstate revenues, would be left with no jurisdictional alternative than to impose the created revenue deficiencies on those least able to bear them in their exchange and intrastate rates.

The single general rate relief application dealt with by the Arkansas Commission during the past three years was disposed of in February, 1969 when the Commission allowed only $83,000.00 of the $480,000 increase in revenues sought by the Arkansas subsidiary of the Continental Telephone Corporation. Although inadequate service by this company permitted a partial holding of the line on their local exchange rates by the Commission: such acts for subscriber protection are self limiting or temporary at best. Most assuredly, once this company has its house in order it will return for the revenues it was previously denied and also assuredly, to its original intrastate and exchange revenue deficiencies, it will have added those amounts lost in the interim to reduced interstate settlements brought about by the continuing reduction in the revenues allowed the A.T. & T. interstate operations.

Now pending is a petition by General Telephone Company of the southwest which asks this commission to allow it to increase the annual gross revenues from its Arkansas operations in the amount of $3,300,000.00. This figure represents, on an average, more than a 37% increase in the amount each telephone subscriber must pay each month for his local exchange service.

This commission takes no comfort in the relative quiet on the telephone rates front within the state over the past several years. On the contrary; the signs are ominous that both the Bell Company and the independents are lurking in the wings with rate cases partially prepared, needing only the final straw of a further reduction in their revenues from interstate calling to formally launch their demands for increases in their local exchange or intrastate toll rates, or both. This commission, reduced to the status of a mere spectator at the negotiations surrounding the application of separations procedures at the federal level and the inevitable reduction of interstate revenues which follow, can only await the falling of the other shoe.

In a predominately rural State such as Arkansas where both public authority and the telephone industry are heavily committed to the proposition that telephone service is a human necessity and therefore must be made available to all at reasonable exchange rates as soon as possible, the revenues derived from the toll and long distance sector of operations bears a special significance for all companies operating in the State. For most of the rural companies, the combined proceeds from interexchange toll and settlements for interstate calls provides the breath of life for their programs of continued expansion at reasonable rates. Even those with broader resources for earning or for attracting capital know that their dependence on such combined proceeds is growing. For all the Arkansas companies under present conditions, a loss in revenue from either intrastate or inter-

state operations will eventually have two certain results: The pricing of local exchange rates out of reach of the less affluent and the abandonment of plans to construct and extend service to all in a growing, well distributed populace.

In these times of mounting costs in every sector of the telecommunications industry there exists the phenomenon of interstate operations, which through the magic of a formula called separations procedures, seems completely immune to inflation and other cost pressures. This phenomenon manifests itself in the regular amputation by the F.C.C. of interstate revenues which, like a lizard's tail, proceeds to be regenerated only to be amputated again. But this allegory is complete only when it is realized that each new replenishment of this appendage is no more than the fruit of a hardworking circulatory and nervous system which in the telecommunications industry is embodied in the ordinary telephone subscriber and the intrastate plant he is paying for.

It is the position of the Arkansas Public Service Commission that the results of the application of the present apportionment of revenue requirements between interstate and intrastate telephone operations are inequitable and result in unreasonable discrimination against those Arkansas telephone subscribers who have little need for interstate long haul service: yet who must pay exchange and intrastate toll rates which in effect subsidize those who frequently use the interstate facilities.

LEWIS M. ROBINSON,
Chairman.
ROBERT C. DOWNIE,
Commissioner.
DON S. SMITH,
Commissioner.

Mr. RIORDAN. From the California Public Utilities Commission, Mr. William Symons, Jr., president of the commission. It is my understanding that also present is Commissioner Vukasin.

Mr. SYMONS. Mr. Vukasin is here with me and we have a statement we would like to have included in the record. We are delivering a copy to the reporter and to the clerk.

Mr. MACDONALD. Without objection, your full statement will be entered in the record at this point.

(The statement follows:)

STATEMENT BY WILLIAM SYMONS, JR., PRESIDENT OF THE CALIFORNIA PUBLIC UTILITIES COMMISSION

As the representative of the California Public Utilities Commission, the opportunity to present this statement to this Committee is greatly appreciated. The California Public Utilities Commission, in protecting the interests of the more than 20,000,000 residents of our State, is greatly concerned with the recent action of the Federal Communications Commission in requiring the American Telephone and Telegraph Company to reduce interstate message toll rates in the amount of $150 million annually effective January 1, 1970 and an additional $87 million effective February 1, 1970. Viewing the nation as a whole, it is inequitable for the FCC to reduce interstate rates $237 million at the same time that over $600 million of rate increase requests are pending in states on the same integrated network during this highly inflationary period. In the balance of this statement, the specific effects on California will be detailed.

California has the largest population in the nation and is experiencing the largest annual population growth, thereby requiring very substantial additions to communications facilities. Our State now has the largest Bell System company and the largest General Telephone System company, with a State total of over 12 million telephones.

There are present service deficiencies in California that require augmentation of the existing plant, particularly local central office equipment. The stimulated business created by the proposed lower interstate rates can only aggravate this situation. To attempt to meet these service problems and to care for California's rapid growth, our Bell System company, which constitutes about 10% of the entire Bell System, has a construction program of $561 million in 1969,

$665 million in 1970 and $710 million in 1971. These construction programs are for both interstate and intrastate operations (interstate 20% and intrastate 80%), and will require the financing of vast amounts of very expensive capital in the next few years. For example, the most recent debenture issue of $150 million on December 2, 1969 resulted in a cost of 9.21% to the company. In 1970, it is expected that $300 million in additional issues will be required by the Bell System operating company in California.

With a need for all this costly capital to finance expanding construction programs in order to meet the service requirements of our rapidly growing population, this is not the time to have an interstate rate cut, because such rate cuts can only ultimately result in further increases for intrastate ratepayers. The interstate rate reduction therefore has the ultimate effect of transferring the burden for meeting increased service demands from the relatively few interstate toll users to the millions of subscribers to local telephone service. It is our view that an appropriate means for adjusting the interstate earnings to a reasonable level is through making changes in separation procedures that will result in a more balanced load being carried by intrastate and interstate telephone users. California heartily supports the NARUC petition for separations rule-making that was filed with the FCC. This petition contains a wholly workable plan for properly reflecting the use of local central office equipment by interstate toll callers. As it would be inappropriate to have the interstate rate changes effective prior to consideration of these separation changes, a complaint was filed to suspend the tariffs pending public hearing on their reasonableness. When the California Commission appealed the $100 million decrease in 1965, the FCC successfully urged that our remedy was to file a complaint challenging the reasonableness of the rates. At that time, we argued that this was no remedy. As the FCC has refused to stay the effectiveness of the new rates and accord a public hearing thereon, we can see there is no remedy in existing law when the FCC reduces interstate toll rates outside of the procedural vehicle it has opened.

QUESTION OF DUE PROCESS

When I say "FCC reduces interstate toll rates" I use the phrase advisedly. No one is fooled by double-talk about a "voluntary reduction" by AT&T. No company will *voluntarily* throw $150 million out the window. This FCC reduction was accomplished after a series of backroom hearings in which no one but AT&T and the FCC staff was permitted to participate. A few observers from the number of those directly affected were reluctantly suffered to attend, but the "invisible shield", to use the phrase from the deodorant ad, was lowered between them and the Commission and the parties to the proceeding, and they were not permitted to speak, file statements, or in any manner record their opposition to a decrease. Even the independents, whose revenues are directly and adversely affected by the action of the FCC, were not permitted to be heard. This type of action cannot be construed as due process.

The FCC has Docket 16258 open and pending, its first full investigation of AT&T in 32 years. In 1967 the FCC found in that proceeding, which is still open, that a 7 to 7.5% range in rate of return on interstate toll was reasonable. FCC had underestimated the rise in net revenues resulting from increasing use of interstate toll service because of reductions in rates. When AT&T's rate of return exceeded the upper limit of the range, FCC had the procedural vehicle ready in its hand in which to determine, in a manner prescribed by the Federal Administrative Procedural Act, whether AT&T's rate of return was excessive and whether a rate decrease was in order, and if so, how much. But FCC ignores the laws which Congress has enacted for rate regulation. After its private hearings with AT&T it issued—not a decision or order—but a press release entitled "Public Notice," which, of course, is not appealable. The FCC Commissioners went through the sorry spectacle of voting on a press release, as they would on an order arrived at after due process, and there is even a dissenting opinion to the press release!

TOLL RATE DISPARITY

One of the big problems facing state regulatory agencies has been the disparity between state and interstate message toll telephone rates.

While today there are a few states which have message toll telephone rates for certain classifications lower than interstate and a few states have rates equal

to interstate, the vast majority of states have rates which exceed interstate for comparable distances. Rate disparities are not just an academic matter; they are a matter of dollars and cents to the telephone customer. Customers cannot understand why there is a higher rate applicable to a shorter distance on an intrastate route as compared with an interstate route.

I have had three charts prepared which illustrate the almost ridiculous rate disparity that results from the interstate message toll rates which became effective February 1, 1970. These charts compare the distance applicable to customer dialed station-to-station calls originating in San Diego, California, for a comparable state and interstate charge. Chart 1 shows that for the maximum interstate day rate of $1.35 a call may be made to anywhere in the United States, a possible maximum distance of 3,000 miles. For the same $1.35 a California intrastate call can reach up to a maximum 590 miles. Chart 2 shows that for only 70 cents an interstate call may be made to the most distant point in the United States on Saturday or Sunday. At a comparable charge of 70 cents a San Diego caller can call 275 miles. The night after 11 p.m. rate shown on Chart 3 introduces a new element of disparity—the one-minute toll call. As shown, for 35 cents an interstate call can be made to anywhere in the nation. For the same minimum charge an intrastate call of 30 miles may be made. Comparing like times of 3 minutes, for 75 cents an interstate call can be made to anywhere in the nation; an intrastate call out to 360 miles.

The problem of a rate disparity has been with us for a long time. Throughout the period of the early 1920's, state and interstate toll rates were generally at the same level of rates per mile being based upon the World War I Postmaster General schedule of rates. From about 1926 to World War II various reductions took place in the state and interstate toll rates. During post World War II years, interstate rates continued to be reduced, with two notable exceptions, whereas intrastate rates, both message toll and exchange, in these years were generally increased. Illustrative of the effects of these rate changes throughout the years is the tabulation set forth on Table 1 which shows the revisions authorized by the Federal Communications Commission since its establishment to date. Based upon straight additions of the savings to customers at the time of the rate change, the reductions for the FCC throughout these years total almost $600 million. Obviously, if the reductions were priced out at today's level of business, the total savings would be many times as great. The reductions in California intrastate toll rates during the same period have totaled only $2 million. This. of course, does not tell the full story as the rate increases are weighted heavily in the earlier years. If all the increases and decreases were priced out at today's level of business, the California intrastate toll would show a net increase.

In addition, exchange rates have been increased substantially for intrastate users. Bell rates in California were increased by $50 million in 1968 and General Telephone by $12 million in 1969. Thus it may be seen that any attempt to correct the toll rate disparity must come at the expense of increased rates for exchange users unless a more fair and equitable allocation of toll costs between state and interstate operations can be developed.

INTERSTATE CREAM SKIMMING

I'm sure that many of you wonder why anyone should object to a rate reduction. I was formerly in the cattle business, so I'll use an analogy which is familiar to me. Please envision the joint ownership of a cow—the Bell System—with the states owning 70% (intrastate) and FCC owning 30% (interstate). The only trouble is that the states have responsibility for feeding the cow, caring for the cow, and cleaning up after the cow. All the FCC does is extract the milk and skim the cream from the 30% that it owns. In this case, the FCC milked Bell for $237,000,000 and gave it to the rich.

In spite of my analogy, there is nothing facetious about the concern of the California Commission. The separations methods advocated by the NARUC in Docket 16258 were sound. FCC considered them and adopted a plan of its own, which benefited states by about only one third of the NARUC proposal. The FCC then reversed itself and came out with a new plan, which, it assured NARUC, would in a year's time work out just about the same as its original plan. FCC was wrong. It has not worked out that way—on the contrary, for 1970 the states are almost $70 million worse off.

SEPARATIONS METHODS

The allocation of telephone costs between jurisdictional operations is referred to as separations. In California, we have set toll rates on an earnings basis. California intrastate toll earnings have generally been on a close parity with interstate toll earnings. Thus, the separations methods used in determining state and interstate toll earnings are of prime importance to California.

The results of the last FCC order on telephone separations were particularly disturbing to us. While there was a transfer of costs from exchange operations to interstate toll, there was a reverse transfer from interstate toll to intrastate toll.

We agree with Chairman Burch that separations procedures are not an exact science; that arbitrary transfers of costs from intrastate to interstate jurisdictions should not be used as a device to alleviate the need for rate adjustments, and that there must be a substantial and rational basis for the proposed transfer. The changes in separations plans which have been made over the years have been the result of the most agonizing efforts of the states to get AT&T and the FCC to recognize the fact that without the local exchange facilities which stand by in readiness to serve all telephone customers 24 hours a day, every day in the year, there would be no access to the interstate toll lines. It should not be a matter of self-congratulation for FCC to claim that from time to time it has assumed a little of the burden. Neither should the statement made by Chairman Burch in his letter of November 17, 1969 to the Chairman of this Committee go unchallenged. He said, "It has been the Commission's policy objective over the years to channel the benefits of technological cost savings to the less affluent and the residential subscribers." The "less affluent and residential subscriber" uses prepaid, unmeasured exchange service; that is, he pays in advance for the service whether he uses it or not. This is the bread and butter service of the American people, the less affluent residential customers, most of whom seldom or never make an interstate telephone call.

If FCC's reductions are permitted to go into effect, the total system will need more dollars to finance growing service requirements. They can be supplied, according to FCC, by the intrastate exchange and intrastate toll user, while the interstate toll user gets a rate reduction. It is easy to understand the Bell System's desire to maintain its prepaid monthly rates as high as possible. It is easy to see why FCC wants to be able to show Congress large interstate toll rate reductions, since it is dependent on it for its budget requirements and has had difficulty in getting appropriations adequate to enable it to truly regulate the telephone industry. It is difficult to understand—indeed, incomprehensible—why FCC would reduce interstate toll rates further at a time when they are already so low that the Bell System in many parts of the country is overloaded. Inadequate consideration of stimulation in traffic and revenues at the time of the preceding "voluntary reduction" of $100 million (in 1965) was one of the factors which gave rise to the upsurge in earnings which caused the FCC to reduce the rates again, and again without adequate consideration of the effects of increased use.

PROPOSED LEGISLATION

The California Public Utilities Commission believes that H.R. 12150 in its present form would not ameliorate problems of the States with the FCC, since it provides for four FCC members on a joint board to consider separations and only three State Commissioners.

The membership on such a joint board should reflect the relative size of state (70%) and interstate jurisdictions (30%) of plant and revenues. An equitable balance would be five State Commissioners and two FCC Commissioners. The California Commission would look more favorably toward the bill if amended in this manner.

I would be more inclined to urge that Congress amend Section 221(c) of the Communications Act. It presently reads:

"(c) For the purpose of administering this Act as to carriers engaged in wire telephone communication, the Commission may classify the property of any such carrier used for wire telephone communication, and determine what property of said carrier shall be considered as used in interstate or foreign telephone toll service. Such classification shall be made after hearing, upon notice to the carrier, the State commission (or the Governor, if the State has no State commission) of any State in which the property of said carrier is located, and such other persons as the Commission may prescribe."

It would be desirable to add a policy directive along the following lines:

"It is the policy of Congress that rates for basic exchange service shall be fixed at the lowest reasonable level, and to this end the Commission is directed in determining what property of said carrier shall be considered as used in interstate or foreign telephone service, to give effect to this policy, and to give weight to the fact that exchange plant provides the continuous access vital to the functioning of the interstate toll network."

SUMMARY

The California Public Utilities Commission opposes the FCC action which required the Bell System to reduce interstate rates $150 million and an additional offset reduction of $87 million for the following reasons:

1. Appropriate separation changes should be made because of the unequal burden on interstate and intrastate telephone subscribers.
2. The interstate rate cuts at this time result in transferring the costs for growing communication needs from the relatively few interstate users to the millions of local telephone subscribers, a great number of whom are economically depressed.
3. The huge financing requirements of the California unit of the Bell System make an interstate rate reduction at this time unwise in view of the present all-time high cost of capital.
4. The rates filed with the FCC which became effective on January 1 and February 1, 1970, create intolerable disparities between California intrastate and interstate toll rates that unreasonably discriminate against the intrastate toll users and unreasonably benefit the interstate toll users. Relief from his condition can be had through withdrawal or suspension of the proposed interstate rates and implementation of appropriate separation changes as already proposed to the FCC by the NARUC.

TABLE 1.—SUMMARY OF MESSAGE TOLL RATE REDUCTIONS SINCE 1935—ESTIMATED SAVINGS TO CUSTOMERS AT TIME OF CHANGE

Year	Federal Communications Commission	California Public Utilities Commission
1935	$581,000	
1936	8,440,000	
1937	12,180,000	
1938		$516,000
1939	1,320,000	
1940	5,404,000	1,918,000
1941	13,005,000	
1942		
1943	31,842,000	375,000
1944	7,710,000	3,803,000
1945	22,220,000	
1946	19,742,000	
1947	835,000	[1] (11,250,000)
1948		1,865,000
1949		[1] (9,368,000)
1950	229,000	
1951		
1952	1,025,000	
1953	[1] (61,940,000)	
1954	$157,000	[1] ($4,916,000)
1955	102,000	
1956	477,000	
1957	42,000	
1958	[1] (2,900,000)	[1] (8,766,000)
1959	45,324,000	
1960	2,740,000	
1961	82,000	
1962		
1963	30,000,000	3,200,000
1964		10,500,000
1965	100,000,000	
1966		60,000
1967	100,000,000	2,100,000
1968	20,000,000	11,900,000
1969		
1970	237,000,000	
Total	595,617,000	1,937,000

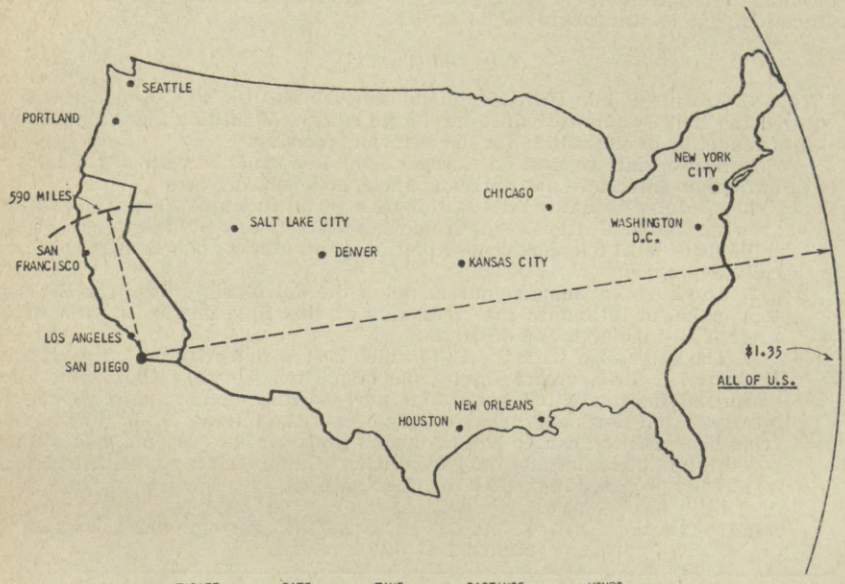
[1] Rate increase to customers.

CHART 1

STATE VS INTERSTATE CALLING DISTANCES FOR COMPARABLE CHARGE FROM SAN DIEGO, CALIFORNIA

INTERSTATE RATES EFFECTIVE FEBRUARY 1, 1970
CALIFORNIA INTRASTATE RATES EFFECTIVE DECEMBER 2, 1968

CUSTOMER DIALED STATION-TO-STATION
DAY RATE



TARIFF	RATE	TIME	DISTANCE	HOURS
INTERSTATE	$1.35	3 MINUTES	ALL OF U.S.	8 AM - 5 PM*
CALIFORNIA	1.35	3 MINUTES	590 MILES	6 AM - 6 PM*

* MONDAY THROUGH FRIDAY

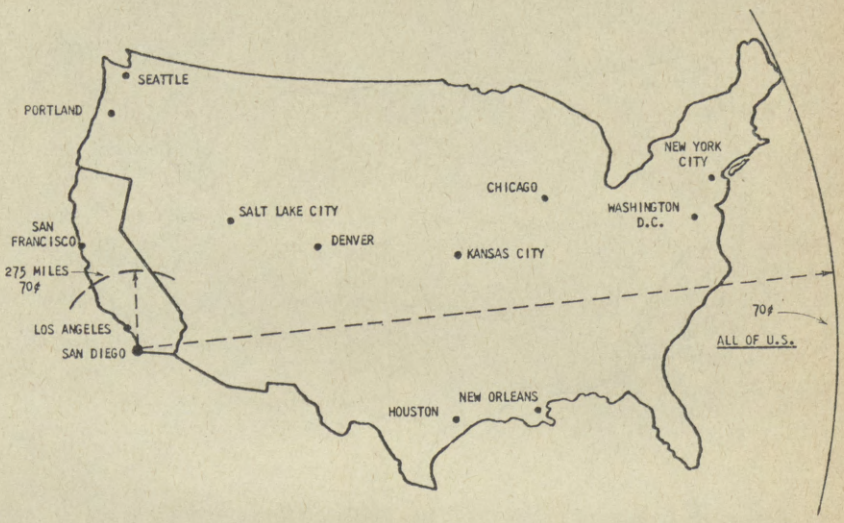
700218

CHART 2

STATE VS INTERSTATE CALLING DISTANCES FOR COMPARABLE CHARGE FROM SAN DIEGO, CALIFORNIA

INTERSTATE RATES EFFECTIVE FEBRUARY 1, 1970
CALIFORNIA INTRASTATE RATES EFFECTIVE DECEMBER 2, 1968

CUSTOMER DIALED STATION-TO-STATION
SATURDAY AND SUNDAY RATE



TARIFF	RATE	TIME	DISTANCE	HOURS
INTERSTATE	$0.70	3 MINUTES	ALL OF U.S.	8 AM - 11 PM SAT. 8 AM - 5 PM SUN.
CALIFORNIA	.70	3 MINUTES	275 MILES	6 PM - 6 AM DAILY*

* PLUS ALL DAY SATURDAY AND SUNDAY

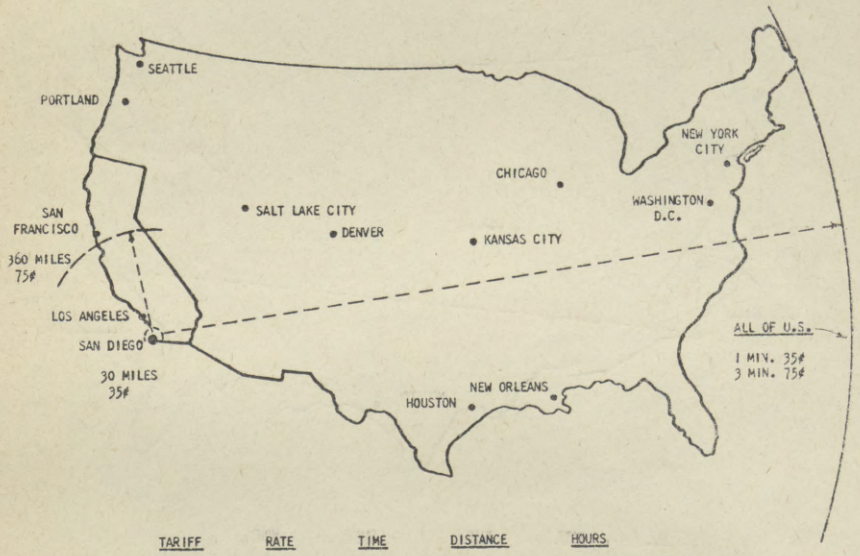
700218

CHART 3

STATE VS INTERSTATE CALLING DISTANCES FOR COMPARABLE CHARGE FROM SAN DIEGO, CALIFORNIA

INTERSTATE RATES EFFECTIVE FEBRUARY 1, 1970
CALIFORNIA INTRASTATE RATES EFFECTIVE DECEMBER 2, 1968

CUSTOMER DIALED STATION-TO-STATION
NIGHT - AFTER 11 PM - RATE



TARIFF	RATE	TIME	DISTANCE	HOURS
INTERSTATE	$0.35	1 MINUTE	ALL OF U.S.	11 PM - 8 AM
	.75	3 MINUTES	ALL OF U.S.	11 PM - 8 AM
CALIFORNIA	.35	1 TO 3 MINUTES	30 MILES	6 PM - 6 AM
	.75	1 TO 3 MINUTES	360 MILES	6 PM - 6 AM

700218

Mr. RIORDAN. From the Colorado Public Utilities Commission, Commissioner Edwin R. Lundborg.

Mr. LUNDBORG. Colorado is definitely for the bill, and I hope the Honorable Don Brotzman will support it as such.

Mr. RIORDAN. Commissioner Harold F. Keith, Connecticut Public Utilities Commission.

Mr. KEITH. Connecticut also supports the bill.

Mr. RIORDAN. From the Georgia Public Service Commission, we have Mr. Walter R. McDonald, Commissioner.

Mr. MCDONALD. Our vice chairman, Mr. Ben T. Wiggins, is also here and we, of course, are supporting the legislation, and we have a statement to submit.

(The statement follows:)

STATEMENT OF BEN T. WIGGINS, VICE CHAIRMAN, GEORGIA PUBLIC SERVICE COMMISSION

Mr. Chairman, Members of the Committee:

Your courtesy in permitting this appearance before your committee is sincerely appreciated by members of the Georgia Public Service Commission. We thank you for the opportunity to place into the record of your proceedings this prepared statement. In substance, the statement is intended to reflect the views that we have formed by experience on the urgent need for passage of HR-12150, a bill proposing the Federal-State Communications Joint Board Act of 1969.

We are hopeful that the information which we have endeavored to furnish will be helpful to this committee in its deliberations.

My name is Ben. T. Wiggins and I reside in Atlanta, Georgia and have been a member of the Georgia Public Service Commission since 1957.

The Commerce Clause of our Constitution is a common bond which has welded the United States into a great nation. At the same time, it has probably provoked as many differences of opinion between the states and the Federal Government as any other provision of that great document. The tremendous expansion in the activities of Federal Government Agencies during the past decade has increased the frequency of these controversies and the magnitude of their impact on state regulation. In the area of telecommunications, the most important area of discussion between the State and Federal Regulatory Agencies has been the separation of telephone property and expenses between State and Federal jurisdictions. Telephone companies' operations (exchange and state toll services) are regulated by the State Public Service Commissions while their interstate toll services are regulated by the Federal Communications Commission. Since every telephone, every line to your telephone central office, much of the central office switching equipment and even some of the long distance toll lines can be used in common for both intrastate and interstate service, an allocation of their costs "is essential to the appropriate recognition of the competent governmental authority in each field of regulation". (US Supreme Court (282 US 133) (1930).)

The Georgia Public Service Commission recognizes and respects the jurisdictional authority of the Federal Communications Commission over interstate long distance telephone rates, and we further feel that fair and effective regulation of telephone services can be accomplished only in an atmosphere of cooperation and trust among the various jurisdictions. The legal evidence of jurisdictional lines does not alter the fact that the State and Federal Commissions represent the same people. The person who makes the local exchange call or intrastate toll call is the same person placing the interstate toll call. Most of the plant and facilities involved in all three calls are one and the same, and are physically inseparable, and therefore are also our interest and responsibilities.

Regulations of the telecommunications industry is a complex matter involving the balancing of many factors. Most of these involve matters which are purely local or are statewide in nature and they continue to be handled with fairness and dispatch by the State Commissions. Our principal concern is service to the customer as desired and the rates which are fair to all classes of telecommunication users. The Georgia Public Service Commission believes that telecommunication regulatory problems that are of mutual concern to the respective State and Federal Regulatory Commissions can and should be resolved through joint cooperative State and Federal action. It does not appear that such cooperation is being sincerely extended to the state at present.

Over the last 20 years, many constructive changes have been made in separations procedures but these revisions have historically been the result of the cooperative efforts involving the Federal Communications Commission, the State Commissions through the NARUC and its committees, and the telecommunications industry. However, in its July 5, 1967 order in Phase 1A of Docket 16258, the Federal Communications Commission appeared to do a complete about-face and assumed the role of final, if not sole arbiter, on separations methods.

The Georgia Public Service Commission has not concluded any major Bell or Independent Telephone rate proceedings since 1962 because none was filed until the first quarter of 1969. The Commission now has pending a General Telephone Company rate increase application which totaled some $4,500,000 and a Bell rate increase application of some $29,750,000.

This Commission has representation on the important NARUC Committee on Communications, which Committee has worked untiringly for many years in the interest of all the states for the purpose of obtaining more realistic and equitable separations procedures that would result in more revenue requirements being placed on interstate facilities, thus eliminating the necessity for such large rate increases now being requested on local exchange and interstate toll service. Further, this Commission on November 26, 1969, wrote the Chairman of the Federal Communications Commission expressing our disapproval of the interstate toll rate reduction that was scheduled for January 1, 1970 (now effective) and calling attention to the adverse effect this will have on intrastate telephone service in Georgia, not only on the some million Bell subscribers, but the quarter million subscribers served by the Independent Telephone Companies in Georgia. This letter also requested reconsideration of this reduction of interstate toll rates by the Federal Communications Commission.

Attached hereto as Appendix I is a schedule showing the effect of separations changes from 1962 to the present time that have benefitted the State of Georgia. It is noted that since 1962, $5,810,760 in revenue requirements have been transferred to interstate and Georgia has passed these benefits on to its subscribers in the amount of $3,474,000. The difference is now pending in rate proceedings currently being considered by the Commission. Had the revenue requirements been larger on the interstate portion, the impact of increases on intrastate service of course would have been much less on the Georgia ratepayers.

The Georgia Public Service Commission believes that there is a real need for continued Federal Communications Commission-NARUC cooperation in separations. However, the Federal Communications Commission with regulatory jurisdiction over only 25% of telephone service cannot be permitted to make decisions for the other 75% of telephone service under state regulatory jurisdictions. Therefore, separations procedures should be defined by statute and we respectfully urge your favorable consideration of HR–12150.

Respectfully submitted.

APPENDIX I.—EFFECT OF SEPARATIONS CHANGES FROM 1962 TO PRESENT—GEORGIA

Nature of change	Month plan made effective	Estimated increase in interstate revenue requirements	Rate decreases (intrastate toll) Amount	Date
Simplification of procedures	January 1962	$940,760	$973,000	May 14, 1962
Denver plan	November 1965	[1] 1,310,000	1,323,000	April 1, 1966
Interim plan		610,000		
(FCC, July 5)	December 1967	490,000	1,178,000	Feb. 1, 1968
Subtotal		1,100,000		
FCC, January 29	January 1969	1,670,000	([2]).	
NARUC suggested changes	January 1970	790,000	([2]).	
Total		5,810,760	3,474,000	

[1] April 1966 review increased this amount by $610,000 additional.
[2] Pending.

Mr. MACDONALD. Sir, before you go much further, are you going to furnish reasonable identification to the reporter? You are going quite rapidly.

Mr. RIORDAN. I will give him this list.

From the Idaho Public Utilities Commission, Commissioner Ralph H. Wickberg.

Mr. WICKBERG. Mr. Chairman, I am in support of the bill.

Mr. RIORDAN. From the Illinois Commerce Commission, Mr. David H. Armstrong, chairman.

Mr. ARMSTRONG. I also have with me my chief engineer, John Kissel, and I would like to introduce a statement in strong support of the bill.

Mr. SPRINGER. I would just like to say, Mr. Chairman, how happy I am to have him here.

(The statement follows:)

STATEMENT OF HON. DAVID H. ARMSTRONG, CHAIRMAN, ILLINOIS COMMERCE COMMISSION

Chairman Staggers, Honorable Members of the Interstate and Foreign Commerce Committee:

I wish to express my gratitude for granting me the opportunity to appear before you and express my feeling in regard to H.R. 12150.

I am David H. Armstrong, Chairman of the Illinois Commerce Commission. The State of Illinois enacted legislation in 1871 creating our Commission and thus we are one of the oldest regulatory commissions in this nation. However, at no time in our almost 100 year history has our Commission been faced with greater problems. One of the greatest problems involves telephone service and rates.

On one hand, our state legislature and the Commission have been receiving great pressure for betterment or improvement in telephone service, especially rural service, and as a result our Commission has entered formal citation proceedings against all telephone companies in the state to show cause why more rapid improvement should not be made in telephone service.

On the other hand, during 1969, ten telephone companies out of the sixty companies under our jurisdiction filed rate cases with us requesting increased revenues totaling over 91 million dollars.

Faced with demands of telephone subscribers for improved telephone service with the increased costs attendant to such services and ten rate cases seeking rates necessary to supply the revenue requirements for the present service and the ever-increasing imbedded cost of capital improvements, we are hard pressed to answer the local telephone users in our state when they read of the toll rate reductions by AT&T totaling 150 million dollars in one month and another reduction of 87 million dollars a month later.

Of the 91 million dollars I referred to earlier, 86.5 million dollars is presently being sought in a pending rate filing by the Illinois Bell Telephone Company, a subsidiary of AT&T and a member of the Bell System. How can we explain to the citizens of our state an FCC formula or system of separations by which AT&T can reduce long line rates by 237 million dollars at the same time its Illinois affiliate urges that it requires increased revenues of 86.5 million?

I would be the first to admit that the question of separations between intrastate telephone service and interstate telephone service is a complicated matter fraught with difficulty. I do say, however, that the solution to this difficult problem should not be left to the sole and absolute control of the Federal Communications Commission. Interstate message toll rates must not be permitted to steadily decrease so as to shift the revenue requirements burden to intrastate message tolls at an unfortunately accelerating rate. The present Illinois Bell Telephone Company rate proposal in our state, if granted, will increase intrastate toll rates substantially and will affect every telephone user in our state since all the independent telephone companies apply the Bell toll rates.

I propose no simple solution to this problem other than to suggest that its magnitude and seriousness demands the most enlightened and imaginative thinking of both state and federal regulators.

It is for that reason that I now urge the adoption of H.R. 12150 which would permit the states to have minority representation on a joint board which would have the sole administrative authority to adopt and amend separations procedures. By such legislation the states could not control separations procedures but they could bring to such a board the light of their experience and intimate knowledge of the tremendous impact separation procedures have locally. Regulation in Illinois and in many states has been in operation for years longer than our counterpart on the federal level and I believe that representatives of these states can contribute much needed expertise to this difficult problem.

The vitality of local telephone service is in jeopardy and if it is to flourish it can do so only by cooperation between the states and federal government and this can be accomplished only by the actions of you, our representatives in Congress.

Thank you very much.

Mr. RIORDAN. From the Kansas State Corporation Commission, Mr. Dale E. Saffels, chairman.

Mr. SAFFELS. We have a statement to submit in support of this legislation.

Mr. RIORDAN. Do you have someone with you?

Mr. SAFFELS. Mr. Dan Sullivan, the assistant general counsel.

(The statement follows:)

STATEMENT OF THE STATE CORPORATION COMMISSION OF KANSAS

Honorable Chairman and Distinguished Members of the Committee:

The State Corporation Commission of the State of Kansas respectfully thanks this Subcommittee on Communications and Power of the United States House of Representatives for these timely hearings on this most vital matter regarding House Resolution 12150 and on the effects of telephone separations as prescribed by the Federal Communications Commission.

Time does not permit a full discussion of what we believe to be arbitrary and irresponsible decisions rendered by the Federal Communications Commission with little or no regard for the effects on each individual state. The Kansas effect, as a result of F.C.C.'s separations decision, would be to create an additional revenue requirement for Southwestern Bell Telephone Company in the amount of $190,680 which would have to be transferred to the local ratepayer of Kansas.

Southwestern Bell Telephone Company, on its Kansas jurisdictional operations for the calendar year 1968 on a net original cost rate base of $327,890,020, prior to any adjustments, earned a rate of return of 7.40%. When these earnings were adjusted for known changes, such as wage increases, ad valorem taxes, results of F.C.C.'s separations formula, Southwestern Bell Telephone Company's projected rate of return for 1969 was determined to be 6.18% rate of return. This necessitated the Commission's permitting Southwestern Bell Telephone Company to put into effect increased charges for non-recurring services which were estimated to increase revenue by $900,000 and the rate of return was estimated to be less than 7%.

The most recent decision of the Federal Communications Commission to reduce interstate telephone rates creates a disastrous shift in revenue requirements in the amount of $2,638,000, with which again the local ratepayer of necessity must be burdened.

The effects of these most unfortunate decisions by the Federal Communications Commission shift from interstate revenue requirements to local ratepayer $2,828,680 in Southwestern Bell Telephone Company alone. Our 64 independent telephone companies, as a result of the decrease in interstate toll rates, will be affected by approximately $1,200,000, making a total of approximately $4,028,680 that must be supplied by additional local rates. This would require a very substantial rate increase on monthly rates of local telephone users by the State of Kansas to pick up the loss of funds brought about by the F.C.C. alleged rate decrease.

The present separations procedure does not adequately distribute the *revenue requirements* between Federal and State. The separations procedure should be based on total plant used and useful to interstate and intrastate, respectively, which also should include the prorata share of readiness time (idle time) as well as actual use time.

We urge this Committee to suggest to the Federal Communications Commission that it is in the public interest to reconsider the reduction in interstate toll rates. Further, we urgently recommend to this Committee the passage of House Resolution 12150 establishing a Federal-State Communications Joint Board.

I wish to again thank the Committee for taking time out of their extremely busy important schedule to listen to the presentations of this very grave matter.

STATE CORPORATION COMMISSION OF KANSAS,
DALE E. SAFFELS, *Chairman.*
JULES V. DOTY, *Commissioner.*
JOHN W. CUNNINGHAM, *Commissioner.*

Mr. RIORDAN. From the Kentucky Public Service Commission, Mr. A. L. Hutchinson, executive director.

Mr. HUTCHINSON. Mr. Chairman, I believe our statement is in transit; it is in the mail.

Mr. MACDONALD. Without objection, it will be included in the record.

Mr. HUTCHINSON. We are in support of the bill.

(The statement follows:)

STATEMENT OF COMMONWEALTH OF KENTUCKY, PUBLIC SERVICE COMMISSION

On November 5, 1969, the Federal Communications Commission (FCC) released a Public Notice stating that the American Telephone and Telegraph Company was submitting to the FCC proposed rate reductions for interstate long-distance telephone calls totaling approximately $237 million per year. The Notice further stated that the reductions were being submitted in connection with the comprehensive review by the FCC of the Bell System's interstate operations and revenue requirements. The reductions are to become effective on or after January 1, 1970.

The Public Service Commission of Kentucky hereby registers its objection to the action of the Federal Communications Commission. These reductions would affect the few who place interstate long-distance telephone calls and would be to the disadvantage of the many local users who place relatively few long-distance calls.

This Commission is a member of the National Association of Regulatory Utility Commissioners (NARUC), an organization of State and Federal agencies engaged in the regulation of public utilities. Appropriate committees of this body have worked jointly with the FCC and the telephone industry in an effort to formulate fair and equitable property separations procedures. In fact, these committees were so engaged at the very time the FCC announcement was made. NARUC has urged the FCC, by modification of existing separations procedures, to increase revenue requirements applicable to interstate operations, thereby reducing that necessary to sustain intrastate telephone service.

Under these circumstances we believe that the FCC acted precipitously and unreasonably in requiring interstate rates to be reduced at a time when many state regulatory commissions are confronted with telephone rate increases. Modified allocation procedures urged by the NARUC and wholeheartedly supported by the Public Service Commission of Kentucky could have an affirmative impact on the rate increases of approximately $500 million requested by the Bell companies in some sixteen states.

Accordingly, we urge the Committee on Commerce (Committee on Interstate and Foreign Commerce) to thoroughly investigate the action of the Federal Communications Commission.

PUBLIC SERVICE COMMISSION OF KENTUCKY,
HAROLD E. KELLEY, *Chairman.*
W. HOWARD CLAY, *Commissioner.*
THOMAS D. EMBERTON, *Commissioner.*

Mr. RIORDAN. Mr. Nat B. Knight, Jr., chairman of the Louisiana Public Service Commission.

Mr. KNIGHT. Mr. Chairman, we too have a statement in support of the bill which I would like to submit for the record, and thank you for the opportunity of doing so.

(The statement follows:)

STATEMENT OF NAT B. KNIGHT, JR., CHAIRMAN, LOUISIANA PUBLIC SERVICE COMMISSION

Gentlemen:

The State of Louisiana and the Louisiana Public Service Commission are deeply concerned over the continuing inequities in separations procedures applied to telephone utilities throughout the United States, the continuation and worsening effect of which are the result of the domination of decisionmaking in this field by the Federal Communications Commission.

In this period of rising costs and other factors which inexorably force upward the cost of local telephone service, the crushing burden on the local consuming public represented by arbitrary and unfair weighting of costs against local services represents a serious threat to grass roots economy, while further favoring the already advantaged and more prospering interstate business. We in Louisiana have no confidence in the attainment of equity in this area of sad experience through the Federal Communications Commission.

Louisiana consumers are feeling the urgent demands of telephone utilities, from the smaller, such as Central Louisiana Telephone Company, Inc., which on June 24, 1969, obtained increased gross revenues of $91,000.00 annually in Louisiana Public Service Commission Docket No. 10315, to the Louisiana Bell Company, South Central Bell Telephone Company, which in Docket No. 10382 is pressing for revenue increases exceeding $24,000,000.00 annually. The utility urged that this amount be authorized at once on a interim basis, under bond, in default of which the telephone construction program in Louisiana will be severely curtailed.

On February 12, 1970, our Commission rejected this attempt to increase telephone rates substantially without full investigation and the State Court having jurisdiction took the same view by judgment on February 16, 1970.

Equitable treatment of the local telephone consumers was never more needed, nor more endangered by the Federal Communications Commission's reduction of interstate toll rates by $237,000,000.00 annually in January, with funds a very substantial part of which would in equity and by proper allocation have served to reduce intrastate financial needs, such as South Central Bell represents to exist in Louisiana.

We respectfully urge your distinguished Committee on Domestic and Foreign Commerce of the United States House of Representatives to intercede in the cause of justice and to accord to the local service operation overdue recognition of the clearly vital part it plays in the generation and conduct of interstate telephone business, and the need for its economic preservation by according no more and no less than fair play in the public interest.

Mr. RIORDAN. The Honorable John G. Feehan, chairman, Maine Public Utilities Commission.

Mr. FEEHAN. Mr. Chairman, we have a statement in strong support of the legislation and I ask that it be supported.

Mr. MACDONALD. Without objection, it will be included.

(The statement follows:)

STATEMENT OF JOHN G. FEEHAN, CHAIRMAN, MAINE PUBLIC UTILITIES COMMISSION

Mr. Chairman and members of the subcommittee, I am grateful for the opportunity to express my views on the matter in hearing this morning.

I fully concur with the position taken by the National Association of Regulatory Utility Commissioners through its President and its Communications Committee, and I would like to briefly indicate a few reasons in support of this position.

Separations, like any other allocation procedure, is not an exact science and the validity of any such procedure can be measured only by the reasonableness of the end result that it produces. Let us look at these results in the State of Maine.

Maine is a State having an area of 32,000 square miles with a population of less than a million people. These people receive service from twenty-six telephone companies having some 420 thousand telephones. From these stations this year more than 35 million toll messages will be originated—with about 72% of them being of an intrastate nature and terminating within the State over routes of 389 miles or less.

Because Maine lies at one end point of our National telephone system, calls originating near our northernmost boundary, that are directed toward the south, must traverse essentially the same cable or microwave routes regardless of their ultimate destination. This fact prompts subscribers to inquire, "Why does it cost forty-five cents to call Kittery, Maine at night when I can call California for fifty-five cents more?" Our answer, of course, must be that this comes about through separations with rates being set on the basis of cost and volumes of traffic. The subscriber's reply is, "But both calls use the same routes as far as Kittery, and are you telling me that fifty-five cents covers the cost of providing the remaining 3000 mile route from Maine to California?" Again, I must explain that through separations procedures, these costs are based on fair and objective allocations. The subscriber's final parting remark is, "Separations or not, THIS JUST ISN'T REASONABLE." To this answer I can find no meaningful reply.

The fact of the matter is that the situation is becoming progressively worse. For example, to have eliminated all disparity between intra and interstate toll schedules in Maine in 1967 would have cost $1.8 million in revenues and today the figure is in excess of $2.1 million, and I might add that during this same period, substantially all of the dollars gained through separation changes were used in reducing this disparity.

In the November 5th F.C.C. Public Notices, it is stated that growth in interstate traffic is continuing unabated and earnings of the A.T. & T. Company have consistently grown despite the increase in costs due to the inflationary spiral. The facts set forth in that release trouble me to the point of asking why, with the same phenomenal growth on the intrastate side and with the same inflationary effect, why it was necessary for the New England Telephone Company, a Bell system subsidiary, to seek relief before the Maine Commission recently? A prime answer lies with our present separations procedures and under such procedures with further interstate rate reductions, the present trend will continue.

The large number of local exchange subscribers who are essentially noninterstate toll users must have relief, and I submit the enactment of H.R. 12150 holds great promise toward that end.

Mr. RIORDAN. For the Maryland Public Service Commission, Mr. Edward McLean, chief auditor, on behalf of William O. Doub, chairman.

Mr. MCLEAN. Mr. Doub planned to be here but, unfortunately, he could not be, and I would like to submit a statement in his behalf. We are in favor of this bill.

(The statement follows:)

STATEMENT OF WILLIAM O. DOUB, CHAIRMAN, MARYLAND PUBLIC SERVICE COMMISSION

My name is William O. Doub and I am Chairman of the Maryland Public Service Commission. I speak for myself and Commissioner Edmondson and Commissioner Shoemaker and in the interest of all telephone users in the State of Maryland.

Maryland is one of the many states that was adversely affected by the separations procedures promulgated by the Federal Communications Commission on January 29, 1969, by order in Docket No. 17975. While the order of FCC did effect a shift of revenue requirements from state to interstate on a national basis in the approximate amount of 107 million dollars, many states, and Maryland was one, suffered a reversal. Of the 107 million shift to interstate 3 states received

55 million, or 51% of the benefits; 62% of the benefits was apportioned to 5 states; and over 84 million, or 78%, was apportioned to 10 states. Of the remaining 39 states, including the District of Columbia, 29 received minor amounts of benefits, while 10 states, and Maryland was one, received negative amounts. It should be apparent that an order which allots 78% of the benefits to 10 states, and penalizes 10 other states at the opposite end of the spectrum, can not be equitable. The FCC considered the national effect without proper consideration of the fact that the many states differ widely in many ways, because of relative size, location, population, degree of industrialization, and geographical peculiarities.

Since 1947, when the Separations Manual was formulated, there have been several modifications which effected relatively minor shifts of revenue requirements from state to interstate. Each came about after compelling action by the NARUC.

Over this same period there was one increase by FCC of interstate rates in 1953, followed by four successive reductions. While this spiral of increasing profits from interstate operations has continued, the states have been faced with a succession of rate cases for increases in local, or intrastate rates. In Maryland during this same period we have had 10 major rate cases resulting in revenue increases of more than $46,400,000, priced at date of inception. In 1965 we reduced rates by $2,800,000, as the result of the last modification of the manual, the Denver Plan. Those benefits were wiped out by the January 29 order.

On September 18, 1969, the president of the NARUC wrote to the FCC calling attention to the pending state rate cases and soliciting the cooperation of the FCC. On November 5, 1969, the FCC announced that it was reducing interstate rates in the amount of $237,000,000, despite the sixteen pending state rate cases aggregating more than $600,000,000 in intrastate rate increases. This is the largest interstate rate reduction in the history of the Bell System. Maryland was one of the states in which applications for rate increases had been filed and after extensive hearings authorized revenue increases of more than $22,000,000 last December.

In conclusion we would like to say that the order of the FCC can not but have the effect of causing further pressures upon the regulatory bodies of the several states for rate increases for intrastate service. It should be obvious to everyone that subscribers to local service are generally less able to pay for such service than are those using interstate, or long-distance service. Moderate rates for basic exchange service is the foundation of a reasonable tariff covering all services. Basic local exchange rates should not be forced to subsidize unrealistically low interstate rates.

Thank you for your consideration.

Mr. RIORDAN. For the Minnesota Public Service Commission, Commissioner Paul A. Rasmussen.

Mr. RASMUSSEN. We are definitely on record in support of this legislation and this bill, and we urge its adoption.

Mr. MACDONALD. Do you have a statement that will be forthcoming?

Mr. RASMUSSEN. No, we haven't.

(The following statement was subsequently received for the record:)

STATEMENT OF THE MINNESOTA PUBLIC SERVICE COMMISSION

The Minnesota Public Service Commission appeared before your Committee on February 24, 1970, in conjunction with the presentation on the part of the National Association of Regulatory Utility Commissioners (NARUC) relating to H.R. 12150. At that time Commissioner Paul A. Rasmussen, representing the Minnesota Public Service Commission and on behalf of the Commission, officially supported the position of the NARUC in urging that this Bill crystalize into law.

We wish to briefly state our reasons for our position concerning this proposed legislation:

There is a joint responsibility that currently exists on the part of the FCC and the respective State regulatory commissions to provide a satisfactory and efficient telephone service for the American people. Because of this joint re-

sponsibility, it appears to be reasonable that there should be an existing joint board to consider matters that would guarantee the equity of both the respective states' responsibility and the FCC's responsibility relating to telephony.

The proposal, as identified in H.R. 12150, provides for a joint board of 7 members, 4 representing the FCC and 3 representing the NARUC. The language of the proposed bill provides that the NARUC will recommend 3 State utility commissioners to the FCC and the FCC will officially appoint them on this joint board. From the experience we have had with the FCC, it is our judgment that this 4—3 relationship has merit. It would give the State representation on the board and they would have an opportunity, through the art of persuasion, to present their judgment and scientific analysis of any matter considered by the board to present the interest and equity of the States in any and all matters under consideration.

In establishing a joint board, the States would be given ample opportunity to present their points of view and all 7 members of the board would be in a position where they would have to justify their position as it related to any and all matters under consideration.

While the present policy of constant surveillance on the part of the FCC makes for an efficient type of regulation, it often results in a superficial analysis, and the public and the State regulatory bodies are not in a position to have sufficient facts to justify the policies and requirements resulting from constant surveillance which for the most part is a mere conversation and discussion between the members of the FCC staff and representatives of the AT&T.

While there is considerable variety of interest in the various geographical areas of the United States concerning telephony, basically and for the most part the interests of the States are decidedly identical.

It would be no problem whatsoever for the NARUC to recommend members to this joint board who would be qualified to represent the interests of all of the 50 States in connection with matters considered by such a joint board.

There are many current problems where there is a joint responsibility and it will undoubtedly take considerable experimentation, research, and analysis before they can be finalized to such a degree that the equity of both interstate and intrastate are in proper balance. We refer particularly to the current policy of the FCC in the matter of separating toll revenue and the allocation of subscriber plant and central office equipment in determining the revenue requirements of the interstate operation and the intrastate operation.

Establishing a joint board of this type would solicit cooperation between interstate and intrastate agencies, and would result in an appreciation and understanding of the joint responsibility of the FCC and the State regulatory bodies which would not be forthcoming if such a joint board did not exist. It would make for a degree of continuity that is necessary in order that the Federal and State agencies, regulating telephony, to function to a maximum degree of efficiency in the interest of the public.

Respectfully submitted.

RONALD L. ANDERSON, *Chairman.*
PAUL A. RASMUSSEN, *Commissioner.*
P. KENNETH PETERSON, *Commissioner.*

Mr. RIORDAN. The Mississippi Public Service Commission, the Honorable Norman A. Johnson, Jr., commissioner.

Mr. JOHNSON. We have a statement in support of this legislation.

Mr. MACDONALD. Without objection, it will be entered into the record at this point.

[The statement follows:]

STATEMENT OF NORMAN A. JOHNSON, JR., COMMISSIONER, MISSISSIPPI PUBLIC SERVICE COMMISSION

I am Norman A. Johnson, Jr., mailing address (Home) P.O. Box 127, Philadelphia, Mississippi. My office address is P.O. Box 1174, Jackson, Mississippi (1105 State Office Building). I am a member of the Mississippi Public Service Commission. This is my 15th year to serve on the Mississippi Public Service Commission. I have served four two-year terms as Chairman of the Mississippi Public Service Commission. I am Vice President and Chairman of the Executive

Committee of the Southeastern Association of Railroad and Utilities Commissioners. I am a member of the Executive Committee of the National Association of Regulatory Utility Commissioners and also a member of the Communications Committee of the National Association and have been a member of said committee since its inception. I would like to make the following statement on behalf of and speaking for the Mississippi Public Service Commission before the Subcommittee on Communications and Power of the House Committee on Interstate and Foreign Commerce.

Mr. Chairman, and members of the subcommittee, the Mississippi Commission fully endorses and supports passage of H.R. 12150 which would establish a seven-member Board composed of four FCC Commissioners designated by the FCC and three State Commissioners nominated by the NARUC and appointed by the FCC. The advantages of such a Board, which would have sole administrative authority in separations procedures, are:

1. It would assure uniform, consistent, equitable and reasonable telephone separations procedures applied by the State Commissions and the FCC alike; and

2. It would provide a more balanced State Commission participation, as compared to present FCC unilateral decisions, in determining future separations procedures for Bell System plant, which under current procedures runs about 75% intrastate subject to the jurisdiction of the several State Commissions.

The Mississippi Commission vigorously opposed the recent $150 million interstate rate reduction arbitrarily ordered by the FCC at a time when the overall costs of furnishing intrastate (exchange and toll) telephone services are increasing. Like many other State Commissions, we would have much preferred the development of further procedures whereby additional costs, presently allocated to intrastate, could have been transferred to the interstate operations in lieu of the rate reduction. We recognize, of course, that such procedures as may be developed in the future must be based on rational and equitable concepts that reflect actual use, or relative use, in order to meet minimum constraints of law and pass judicial review.

The procedures whereby revenues, expenses, and plant investment are separated between the instrastate and interstate jurisdictions historically have been subjected to negotiations between the State Commissions and the Federal Communications Commission, until recently. In January of 1969 separations procedures were prescribed by the FCC as a result of rule-making procedures. Throughout all of the separations changes, however, the State Commissions have had a disproportionately small influence on the determination of appropriate procedures. The proposed seven-member Board would take a giant step toward correcting this historical inequity.

Unlike several other states, the telephone companies in Mississippi have not filed major rate case proceedings within the last few years, nor are any rate cases presently pending before this Commission. However, the level of rates charged consumers within the jurisdiction of this Commission could certainly be held to a minimum if additional appropriate separations changes were made. Separations procedures that are allowed to continue without revision to reflect the changing economy, calling patterns of subscribers, relative costs and types of plant will inevitably place unjust and harmful burdens on the vast majority of intrastate telephone users.

The Mississippi Commission therefore urges favorable Congressional action on House Bill H.R. 12150 and the identical companion Senate Bill S. 1917 establishing the proposed joint Federal-State Communications Board.

PUBLIC SERVICE COMMISSION, JACKSON, MISS.

In the matter of protest against interstate telephone rate action by action of the Federal Communications Commission.

RESOLUTION

At a regular meeting duly called and attended by all members of the Mississippi Public Service Commission, on the 12th day of November, 1969, at Jackson, Mississippi, the following Resolution was unanimously adopted:

Whereas, the Federal Communications Commission exercises general regulatory jurisdiction over the rates and services of interstate telephone companies; and

Whereas, the regulatory authorities of the several states exercise general regulatory jurisdiction over the rates and services of intrastate telephone companies; and

Whereas, the Mississippi Public Service Commission exists under and by virtue of the Laws of the State of Mississippi and is the state regulatory agency having jurisdiction over intrastate rates and services of telephone companies; and

Whereas, the Mississippi Public Service Commission represents the people of Mississippi who are adversely affected by disparity between interstate and intrastate rates and charges; and

Whereas, there does exist an unjust disparity between interstate toll rates and intrastate toll rates charged by the companies which in many instances cause the intrastate toll rates to be substantially higher than the interstate toll rates over the same lines, although for a longer distance; and

Whereas, such an unjust disparity in toll rates has caused confusion and misunderstanding in the minds of the customers of such companies and has created a difficult situation for the regulatory authorities of the several states; and

Whereas, the Federal Communications Commission on November 5, 1969, announced that rates for interstate long distance calls would be reduced about $150,000,000 per year; and

Whereas, there are intrastate rate cases pending in at least sixteen states amounting to an increase of one-half billion dollars; and

Whereas, if this rate reduction by the Federal Communications Commission is allowed that it would be a serious detriment to the state and local commissions and the users of local telephone service.

NOW, THEREFORE, BE IT RESOLVED BY THE MISSISSIPPI PUBLIC SERVICE COMMISSION that it urgently requests the Federal Communications Commission to reconsider its decision to reduce interstate toll rates of the telephone company $150,000,000 and to work with the State Commissions in adopting realistic separation procedures.

BE IT FURTHER RESOLVED that Congress pass immediately the bill proposing the Federal-State Communications Joint Board Act of 1969, which has been introduced in the House as *H.R. 12150*, and in the Senate as *S. 1917*.

BE IT FURTHER RESOLVED that a copy of this Resolution be sent to Senator James O. Eastland, Senator John Stennis, Representative Thomas G. Abernathy, Representative Jamie L. Whitten, Representative William M. Colmer, Representative G. V. Montgomery, Representative Charles Griffin, Mr. Peter Flanigan, Assistant to the President of the United States, Mr. Francis Pearson, President, National Association of Regulatory Utility Commissioners, and National Association of Regulatory Utility Commissioners.

Made and entered at Jackson, Mississippi, this 12th day of November, 1969.

NORMAN A. JOHNSON, Jr., *Chairman.*
D. W. SNYDER, *Commissioner.*
W. E. "BUCKY" MOORE, *Commissioner.*

Attest:

E. W. ROBINSON, *Executive Secretary.*

Mr. RIORDAN. From the Missouri Public Service Commission, Mr. William R. Clark, chairman.

Mr. CLARK. We in Missouri have a statement in support of the bill.

Mr. MACDONALD. Without objection, it will be entered in the record at this point.

(The statement follows:)

STATEMENT OF WILLIAM R. CLARK, CHAIRMAN, MISSOURI PUBLIC SERVICE COMMISSION

Mr. Chairman, members of the Commerce Committee, I appreciate the Chairman's invitation to make a statement before this Committee in my capacity as Chairman of the Missouri Public Service Commission, and to concur in the position as stated by the Honorable Francis Pearson, President of the National Association of Regulatory Utility Commissioners. It is my opinion that the economic climate of this country requires a redefining of costs and allocation of property between interstate and intrastate operations. The Missouri Public Service Commission has disposed, within the last three years, of telephone rate cases in the aggregate amount of $31,271,713, and has pending before it for consideration rate cases in the aggregate amount of $2,231,500. Attached at the conclusion of this statement is Appendix A detailing these cases.

It would appear that policies dictate that interstate toll rates are lower than intrastate toll rates for comparable distances, partly due to differences in costs and partly due to policy of keeping exchange rates as low as possible.

Southwestern Bell Telephone Company in Missouri proved a need for a rate increase which was granted on October 14, 1969 in the amount of $30,689,409 per year. On January 1, 1970, with the approval of the Federal Communications Commission the American Telephone and Telegraph Company placed into effect an interstate toll rate reduction of $150,000,000, and again on February 1, 1970, a further reduction in interstate rates of $87,000,000. These two reductions total almost 8 times the increase granted Southwestern Bell in Missouri.

Under present economic conditions the reductions in interstate rates cannot stand with reason in light of the fact that the Bell System has applications pending in many other states for increased intrastate rates. Rates are based upon cost of rendering service plus fair rate of return on investment. Expenses and investment are separated between interstate and intrastate on the basis of separations manuals.

The only conclusion I can draw is that the many reductions over the years in interstate rates while increases have been needed in intrastate rates prove the separation procedures are biased toward the interstate jurisdiction. Over the years there has been at least 5 changes in separation procedures. See Appendix B for the various effects with regard to Missouri. The effect on the different states has varied but nationally the changes have overall transferred property and expenses from intrastate to interstate, except in 1969 with respect to the re-apportionment of the toll line plant. Had the procedures of allocation used in the Modified Phoenix Plan been retained, then the 1969 exception brought about by the Federal Communications Commission Interim Order would not have resulted in a transfer of Missouri revenue requirements to the State rate-payer of over $6 million. This certainly indicates that the allocation procedures are not satisfactory. Present conditions loudly declare that they are still unsatisfactory because they do not produce reasonable results. Separation procedures are based on various definitions of use.

Present procedures are based upon use and use studies, however, these results can and have been changed from time to time by changing the period studied of the grouping of items studied, e.g., Charleston Plan lumped several categories of plant into one. Studying the usage of the total gave a different result than studying the individual parts.

Since present separation procedures charge too much cost to intrastate operations and too little cost to interstate operations, the local user pays a higher rate for the benefit of the interstate user. As a large percentage of interstate calls are made by business which gets an income tax deduction for this expense, this situation works to the disadvantage of the residence user.

In the past when the Federal Communications Commission has decided to cut interstate toll rates rather than change separations procedures and benefit intrastate users as well as interstate users, the state commissions have had no voice in the decision. As separation procedures affect both state and federal jurisdictions the state commissions should be given a voice in such decisions.

Note also the complete disregard of "the majority rule"; that the man regulating 25% of the business should have the right to tell the man who regulates 75% of the business how he must determine the cost, revenues, and expenses applicable to his jurisdiction.

If the National Association of Regulatory Utility Commissioners' proposed legislation setting up a joint NARUC–FCC Separations Board had been in effect, the precipitous action taken by the FCC would have not occurred.

The Federal Communications Commission has further complicated the problems of intrastate regulation by its decision on August 13, 1968 in the "MCI Case" (Microwave Communications, Incorporated). This decision will permit MCI to construct a common carrier microwave radio service between Chicago, Illinois and St. Louis, Missouri, if an appeal is not filed with the courts. This system is designed to provide interoffice and interplant communications for businesses between these points.

The full impact of this decision was not realized until the flood of applications poured in on the FCC and on some state commissions. There are now at least seven additional applications pending before the FCC, and a number more anticipated, with proposals which will blanket the United States with routes and complete systems furnishing special communications services for special interests.

The decision in the "MCI Case" is diametrically opposed to sound economics and regulatory principles. It further will cost the average American ratepayer money to the immediate benefit of a favored few. I have grave and an urgent concern in this matter for Missouri will be one of the first states to feel the effects of the decision, since one of the terminal points is St. Louis.

This is a typical "cream skimming" operation for a major route has been selected, Chicago to St. Louis, with heavy traffic density characteristics and the resulting lower unit costs. The existing common carriers have been encouraged by the Federal Communications Commission, primarily for social reasons, to base their rates both for message toll and private line services on nationwide average costs. Thus, the smaller users in the outlying areas are provided the same rates as those in major populated areas. The ultimate result of the MCI decision will be to increase the rates of the small intrastate user and herein lies the problem for the intrastate regulator.

A comparable situation has arisen in the trucking industry, i.e. the long more profitable haul as opposed to the short less profitable haul. The MCI decision may portend a similar problem in the communications industry. The trucking industry no longer wants to serve the smaller towns on their regular schedules because the longer hauls are more lucrative due to lower unit costs. If the MCI's are permitted to skim off the profits on the longer more lucrative routes without regard for the short hauls and small towns, then it appears to me that the ultimate result will be similar to the trucking industry and the smaller user will suffer both rate and service wise.

The essence of the MCI decision is to authorize a specialized common carrier service requiring duplicate facilities. Such duplicate facilities are both uneconomical and unwarranted. They are uneconomical because the building of duplicate facilities will be extremely costly and these costs will be passed on to the public. They are unwarranted because existing carriers are adequately meeting the public need. These proposed systems will only offer to serve limited business customers on high density interstate routes without concern for the impact on other business and residential users, the subscribers of existing common carriers. They will risk the slowing of economies of scale, which heretofore have been shared by all users. The diversion of this interstate usage to other communication media will have the effect of placing a heavier relative burden on intrastate users. It will undermine the existing average rate structure.

The combined result of the MCI decision, if the additional applications are granted, and the lack of adequate representation of state commissions in determining separations procedures will be to affect drastically the costs and service of the small intrastate user.

The arbitrary action of the FCC in approving interstate rate reductions without properly considering a revision in separations procedures together with the further aggravating effect on future separations of the MCI decision points up the urgent need for a seven man Federal-State Communications Joint Board for determining separations procedures proposed in H.R. 12150.

I urge the passing of H.R. 12150.

APPENDIX A

TELEPHONE RATE CASES BEFORE THE MISSOURI PUBLIC SERVICE COMMISSION, DECEMBER 1966–DECEMBER 1969

CASES RESOLVED AND INCREASES APPROVED

Date approved	Case No.	Increase	Company
Dec. 29, 1967	16,184	$43,076	Modern Telephone Co.
Feb. 14, 1969	16,567	1,520	Nodaway Valley Telephone Co.
Mar. 29, 1969	16,522	16,208	Southern Telephone Co.
Sept. 18, 1969	16,662	521,500	Missouri Telephone Co.
Oct. 14, 1969	16,642	30,689,409	Southwestern Bell.
Total		31,271,713	

CASES PENDING AND INCREASES REQUESTED

Date submitted	Case No.	Request	Company
Pending Sept. 5, 1969	16,826	$150,000	Missouri Central Telephone Co.
Do	16,827	900,000	Missouri State Telephone Co.
Pending Nov. 18, 1969	16,865	1,074,000	General Telephone Co.
Pending Nov. 12, 1969	16,864	90,000	Doniphan Telephone Co.
Pending Nov. 18, 1969	16,877	10,000	Miller Telephone Co.
Pending Jan. 26, 1970	(1)	7,500	LeRu Telephone Co.
Total		2,231,500	

[1] Unassigned.

Note: Total increases approved and requested, $33,503,213.

APPENDIX B

EFFECT ON INTERSTATE REVENUE REQUIREMENT OF CHANGES IN SEPARATIONS SINCE 1947

Year	Label	Effect at time of change		Current effect, Missouri
		Bell System	Missouri	
1952	Charleston plan	$30,000,000	644,000	5,050,000
1956	Modified Phoenix	40,000	1,980	6,930
1962	"Simplifications"	46,000	1,960	3,830
1965	Denver plan	134,000	4,380	5,780
1969	Jan. 29, 1969 order [1]	110,000	250	250
1970	"NARUC proposed"	35,000	1,090	1,090
	Total	395,000,000	10,304,000	22,930,000

[1] Interim procedures were introduced in November 1967 which resulted in a transfer of Missouri revenue requirements to interstate of $940,000. The Jan. 29, 1969, FCC order revised these interim procedures. As a result, the transfer to interstate was reduced to $250,000 at the end of 1969 when Modified Phoenix is completely eliminated. The separation procedures used by S.W.B. for the rate case "test period" understated its intrastate revenue requirements by $690,000.

MISSOURI

Net book cost	1952	1969
Assigned interstate	28,500,000	223,800,000
Total [2]	210,600,000	883,000,000
Percent assigned interstate	13.5	25.3

[2] Includes all of S.W.B. investment in Missouri (intrastate plus interstate).

Mr. RIORDAN. Nebraska State Railway Commission, Commissioner Fred N. Peterson and Commissioner Joseph J. Brown.

Mr. PETERSON. We are in full support of this bill. We do not have a statement to enter in the record.

Mr. MACDONALD. Our distinguished colleague from the great State of Nebraska would like to make a comment about the gentlemen.

Mr. CUNNINGHAM. Mr. Peterson is a very able man, very conscientious. I am a member of the full committee but not this subcommittee as you well know. We are having a meeting downstairs and I will have to make that. I am in support of this legislation. I certainly hope that the committee will go into it very thoroughly, as I know it will, under your excellent chairmanship.

Mr. MACDONALD. Thank you, sir.

Mr. RIORDAN. From the Nevada Public Service Commission, Chairman Reese H. Taylor, Jr., and Commissioner Noel A. Clark.

Mr. TAYLOR. Nevada has a strong statement in support of the bill. As you indicated, Commissioner Noel Clark is here with me.

Mr. MACDONALD. Without objection, your statement will be entered in the record at this point.

(The statement follows:)

STATEMENT OF PUBLIC SERVICE COMMISSION OF NEVADA

The State of Nevada finds itself emphatically opposed to further *interstate* rate reductions prior to a thorough evaluation of the effect of additional reductions upon *intrastate* rate structures. In Nevada, our present economic growth and development has largely been confined to two urban areas—Reno and Las Vegas. These two centers have nearly 84% of Nevada's population and they are approximately 350 airline miles apart. The impact of an *interstate* rate structure that is out of balance with *intrastate* rates should be readily apparent.

Although there are no telephone rate cases currently pending before the Nevada Public Service Commission, the last rate case involving Bell of Nevada, which was heard and decided in 1968, offers a dramatic example of the wide disparity between *interstate* and *intrastate* rates which the Nevada Commission had to authorize in view of the wholly inappropriate and F.C.C.-dominated separations procedures then in effect. The Nevada Commission issued its opinion and order in that matter on August 30, 1968, allowing a 6.84% rate of return. At that time, well in advance of the F.C.C.'s determination to reduce *interstate* rates by some $237,000,000, the imbalance between *interstate* and *intrastate* revenues—made mandatory by existing settlement procedures—had already taken effect in Nevada.

Some of the matters that were of concern in the Nevada Commission's consideration of Bell of Nevada's 1968 rate case are as follows:

1. Despite continuing *interstate* toll reductions, the Applicant alleged that its rate of return had fallen to an unprecedented low of 3.44% on *intrastate* operations.

2. The Applicant was faced with a continuing obligation to satisfy the demand for telephone service required by Nevada's phenomenal growth rate.

3. The Applicant presented testimony that the use of telephone facilities had greatly expanded, but the additional usage had *not* generated additional revenue.

In arriving at its decision, the Nevada Public Service Commission made the following observations in the opinion rendered:

". . . there is also room for disagreement with respect to the division between intrastate and interstate plant, such division having been predicated by Applicant on the so-called 'separations manual' which deals with telephone plant separations on a national basis. A detailed analysis of the separations procedure applicable to Nevada might very well reflect a disproportionate share of interstate plant and expense charged against Nevada intrastate operations."

". . . we will have to rely upon existing procedures contained in the separations manual submitted by Applicant for the purpose of arriving at our ultimate decision herein."

As a result of the 1968 decision, a paradoxical situation has arisen whereby a telephone subscriber can call long distance, station-to-station for 3 minutes, from Reno to Tucson, Arizona, Denver, Colorado, Great Falls, Montana, Albuquerque, New Mexico, Portland, Oregon, Seattle or Spokane, Washington or Cheyenne, Wyoming for approximately the same amount that it costs to call station-to-station for 3 minutes from Reno to Las Vegas. A Reno subscriber placing a 3-minute person-to-person call pays approximately the same rate to talk to Chicago, Illinois, New Orleans, Louisiana, Dallas or Houston, Texas or Minneapolis, Minnesota as the rate chargeable for a 3-minute person-to-person call from Reno to Las Vegas. Even more ridiculous is the fact that within a few minutes drive of Nevada's capital city, a 3-minute person-to-person call can be placed *interstate* from a California point to Las Vegas for $1.25, whereas the same call, made *intrastate* from Carson City to Las Vegas, costs $2.75.

All of the foregoing long distance toll disparities must already be contended with by Nevada's telephone subscribers. Now comes the F.C.C.'s authorization of a $237,000,000 reduction in *interstate* tolls, and as a result, such disparities will only be magnified to an intolerable extent. Accordingly, we view the F.C.C.'s recent action as completely inexcusable in light of the fact appropriate separations allowing for further transfers of *intrastate* rate base and expense to *interstate* operations would narrow the already existing disparities and give

Nevada's *intrastate* telephone users a measure of relief to which they are clearly entitled. The Nevada Public Service Commission has therefore urged the F.C.C. to reconsider its recently announced *interstate* telephone toll reductions, and we earnestly hope more equitable separations procedures will be worked out with the states in the immediate future pursuant to the legislative proposal now before you. In this regard, the Nevada Public Service Commission unanimously supports H.R. 12150, and we urge you favorable consideration of this important piece of legislation.

REESE H. TAYLOR, Jr., *Chairman.*
NOEL A. CLARK, *Commissioner.*
EVO A. GRANATA, *Commissioner.*

Mr. RIORDAN. I appear on behalf of the New Hampshire Public Utilities Commission, and I would like to go on record as favoring the bill, and I have a statement which I will give to the reporter and to the clerk upon the completion of the reading of the roll.

(The statement follows:)

STATEMENT OF FRANCIS J. RIORDAN, CHAIRMAN, NEW HAMPSHIRE PUBLIC UTILITIES COMMISSION

The Federal Communications Commission (FCC), on November 5, 1969, released a public notice stating that it had negotiated with the Bell System telephone companies an interstate toll rate reduction totaling $237 million which we understand will be effective on or after January 1, 1970.

Under the rate base concept of rate making, practiced by the FCC and the State commissions, the Bell System, through its rates, is entitled to earn a reasonable return on its plant invested in common carrier service and to recoup its expenses reasonably incurred in furnishing such service. Since the vask bulk of Bell System plant and expenses are used in furnishing both interstate and intrastate communication service, such plant and expenses must be allocated or separated between the interstate and intrastate uses for purposes of rate-making by the respective Federal and State jurisdictions.

The FCC's present method of allocating the cost of sustaining our national telephone system is inequitable and the many states suffer from the imbalance.

It is an anomaly that the FCC should decree an interstate reduction when at the same time the affected companies (including New England Telephone in New Hampshire) have filed tariffs for greater intrastate revenue. Some of these requests are pending and some have already been granted.

In New Hampshire a $696,000 rate increase was allowed to become effective on October 19, 1969, by an increase of $426,000 in *intra*state toll rates and $270,000 in service connection charges. If New Hampshire could have had allocated to it a portion of the $237,000,000 which the FCC claims represents excess earnings of AT&TCo., then New Hampshire's $696,000 rate increase could have been minimized or completely avoided. There is an additional conflict of rate regulation by Federal and State jurisdictions which is confusing to the customer wherein day, evening, night and weekend rates do not apply for the same time periods on interstate and intrastate toll rates.

The action of the FCC in this instance of not consulting with the states or with the NARUC appears to be at odds with the concept of the new federalism attempted to be put into effect by the present administration.

We urge your favorable consideration of this Bill.

Mr. RIORDAN. The New Jersey Board of Public Utility Commissioners. Do we have someone here this morning from the State of New Jersey?

I think the chairman of the New Jersey Commission is in Florida and could not make this meeting.

From the utilities division of the New York Public Service Commission, we have Mr. Thomas J. Brady, chief of the telephone bureau.

Mr. BRADY. I have a statement on behalf of the New York Public Service Commission.

Mr. MACDONALD. Without objection, it will be put in the record at this point.

(The statement follows:)

STATEMENT OF THOMAS J. BRADY, CHIEF OF THE TELEPHONE BUREAU, NEW YORK STATE PUBLIC SERVICE COMMISSION

Mr. Chairman and members of the committee, my name is Thomas J. Brady and I am Chief of the Telephone Bureau of the New York Public Service Commission. In that capacity, I have the responsibility of supervising the Commission staff on all regulatory matters affecting the telephone and telegraph industry in New York State. I am a member of the NARUC's Staff Committee on Communications and I am a member of the Staff Subcommittee on Separations and Toll Rate Disparity.

The New York Commission wishes to go on record as supporting very strongly the enactment of HR 12150, a bill proposing the Federal-State Communications Joint Board Act of 1969. The New York Commission joins with NARUC and the other state commissions in urging enactment of this proposed legislation which would create a 7-member board composed of four FCC commissioners designated by the FCC and three state commissioners nominated by the NARUC and appointed by the FCC. This board would have sole administrative authority under the Communications Act of 1934 to adopt and amend separations procedures. An order of the Board prescribing separations procedures could be deemed an order of the FCC for purposes of judicial review.

As you gentlemen know, the New York Commission within the past week deemed itself compelled, under the law, and in application of the currently prescribed separations procedures, to authorize the filing by New York Telephone Company of increases in local exchange, intrastate toll and other intrastate charges aggregating over $136,000,000 annually. If the FCC had heeded the petitions of NARUC and a large number of other state commissions calling for amendment of the separations procedures so as to transfer substantial amounts of revenue requirements from intrastate to interstate operations, it is obvious that a significant portion of the enormous increase in New York intrastate telephone rates could have been avoided. This situation does not pertain to New York alone because clearly a situation has arisen whereby repeated rate reductions on the interstate side of the Bell System's operations are being more than offset by continuing rate increases on the intrastate side. The result, which is obvious to anyone familiar with regulation, is a mounting hardship upon the users of basic exchange service which is out of all proportion to any public benefits possibly obtained from interstate toll rate reductions.

The New York Commission believes that the state commissions who are responsible for the regulation of some three-quarters of the Bell System's operations should have a voice in determining the procedures to be followed in separating plant and expenses between interstate and intrastate jurisdictional categories. Creation of the Joint Board as contemplated by HR 12150 would provide a vehicle which would enable the state commissions, through NARUC, to have an active role in the formulation and implementation of changes and modifications of the separations procedures which have such an important effect upon the level of earnings required from intrastate operations of the operating companies and in particular, from the basic exchange service which must be supported by all of the people using telephone service and not merely by the more affluent group which can take advantage of lower interstate rates.

Although the proposed legislation would continue to give the FCC a majority voice in determinations involving separations procedures, the New York Commission believes that establishment of this Joint Board would at least give the state commission a voice in such determinations and an opportunity to place before the Board, for full consideration, all of the relevant economic and other factors which should properly be considered in any jurisdictional separation of costs and expenses.

The recent unilateral actions of the FCC in effecting substantial reductions in interstate toll rates have placed many state commissions, and New York is one of them, in the position of being forced to grant substantial increases in intrastate rates, if telephone service is to be maintained, while at the same time knowing that grave doubts exist as to whether fair and equitable distribution

of costs and expenses between interstate and intrastate operations is being realized through application of the separations manual as it now exists. Creation of the Joint Board would provide the state commissions with a forum in which such doubts might be resolved.

Accordingly, the New York Commission wishes to go on record as endorsing the opinions and suggestions made by the NARUC and respectfully urges your committee to take positive action with respect to HR 12150 to the end that such legislation be enacted at the earliest possible date.

Mr. RIORDAN. From the North Carolina Utilities Commission, Harry T. Westcott, chairman.

Mr. WESTCOTT. Mr. Chairman, I have a statement I would like to file for the record.

Mr. MACDONALD. Without objection it is so ordered.

(The statement follows:)

STATEMENT OF THE NORTH CAROLINA UTILITIES COMMISSION

To the Members of the Committee on Interstate and Foreign Commerce, U.S. House of Representatives:

On November 5, 1969, the Federal Communications Commission (FCC) issued a *Public Notice* in its FCC File 69-1210 stating that the FCC had found that American Telephone and Telegraph Company (AT&T) had $237,000,000 in excessive earnings in 1969 which by agreement between the FCC and AT&T would be reduced by giving *interstate* toll telephone customers reductions in interstate long distance telephone charges in the amount of $237,000,000.

The North Carolina Utilities Commission supports the use of excessive AT&T earnings for telephone customer benefits, but protests the use of the entire amount in the reduction of interstate toll telephone charges, without any benefits being allotted to urgently needed improvements in local telephone service and local telephone rates. The North Carolina Commission has requested the FCC to reconsider its decision announced in the *Public Notice* of November 5, 1969, and to allocate a fair share of the available $237,000,000 excessive AT&T earnings to the improvement of local service and local telephone rates.

The decision of the FCC to assign all of the excessive earnings to the reduction of interstate long distance telephone charges arises from inequitable accounting formulas utilized to separate the telephone plant utilized in long distance service from that utilized in local telephone service. The present separations formulas discriminate against local telephone service. This is evidenced by the excessive earnings of AT&T from its pro rata allocation of long distance toll charges, while the local service telephone companies are increasing local monthly telephone charges to support the local telephone plant used in making the toll calls, and local telephone service is deteriorating through lack of adequate toll revenues from the present formula to install and maintain the urgently needed local telephone plant used in the toll calls.

The long range correction of this discrimination in separations formulas can be accomplished through the enactment of S. 1917, *a Bill proposing a Federal-State Communications Joint Board*, establishing four FCC Commissioners and three State Commissioners with administrative authority to adopt and amend the separations procedures and formulas to be applied to interstate toll revenues, in allocating a fair share of the revenues from each call to the local service telephone companies originating and terminating the calls.

The separations formulas which would be corrected by S. 1917 are the formulas used in dividing interstate toll revenues between (1) *the Long Lines Division of AT&T* and (2) *the originating and terminating local telephone companies* which provide all of the basic telephone plant and local service connections utilized in long distance calls, and who service, bill and collect all of the charges for these calls. The present formulas do not give a fair share of the toll revenue to the local telephone companies providing the local plant and local service rendered on each interstate long distance call.

The present discriminatory formulas result in local telephone service subsidizing the AT&T Long Lines Division, resulting in excessive profits of the AT&T Long Lines Division, at the cost of local telephone service and local telephone rates.

LOCAL TELEPHONE SERVICE

Local telephone service is performed in North Carolina by the following local telephone companies:

	Number of telephones	Percent of total
Southern Bell Telephone & Telegraph Co	1,154,163	53.85
28 independent telephone companies	912,473	42.57
Chapel Hill (municipal)	31,721	1.48
Pineville (municipal)	1,294	.06
Telephone cooperatives	43,689	2.04
Total North Carolina telephones	2,143,340	100

North Carolina has a large rural population. Mileage or zone charges apply outside of base rate areas, and 55,030 telephone customers in North Carolina still receive 8-party and 10-party service. This service is outmoded and inadequate for today's telephone customer requirements. The North Carolina Commission is seeking every possible means to eliminate this outmoded service by upgrading it to a 4-party service, 2-party service, or 1-party service. The upgrading program is expensive, and the local telephone companies greatly need a larger share of the toll revenues to complete these service improvements. This is just and reasonable because the toll revenue is derived in part from the use of this more expensive local plant in making long distance calls.

The North Carolina Commission has under investigation complaints regarding the service of many of the telephone companies under its jurisdiction. They involve primarily lack of maintenance personnel, operating personnel, installers, repairmen and repair equipment to keep the telephone plant in good running order. This service condition stems from rising prices, restricted operating budgets, and lack of sufficient revenues from the pro rata share of interstate toll revenues on toll calls coming through the local telephone plant.

Revisions in the separations formulas for interstate toll revenue will allocate a fair share of the present excessive earnings of AT&T's Long Lines Division to the needed improvements in local telephone plant, including upgrading of outmoded multi-party service and improvement in general standards of performance through adequate maintenance budgets.

LOCAL SERVICE RATES

The local service monthly charge paid by all telephone customers establishes and supports the basic telephone plant which is used jointly for local calls and interstate long distance telephone calls. The local service monthly charges in North Carolina are already at a high level and cannot be further increased without hardship to the local service telephone subscribers. Five telephone companies under the jurisdiction of the North Carolina Commission have increased local service telephone charges in the last three years, as follows:

	Date	Applied for	Received
Concord Telephone Co	May 19, 1969	$807,329	$671,505
Lee Telephone Co	June 6, 1968	196,496	132,294
Do	July 28, 1969	239,973	142,437
General Telephone of Southeast	Dec. 19, 1968	2,319,564	1,192,836
Denton Telephone Co	July 7, 1969	29,571	29,571
E. Rowan Telephone Co	do	46,217	46,217
Total		3,639,150	2,214,860

A general reduction of AT&T long distance telephone tariffs as proposed in the FCC Public Notice of November 5, 1969, would not only reduce the earnings of AT&T's Long Lines Division, but would also reduce the pro rata share of the calling revenue due to the local service telephone companies originating and terminating the long distance telephone calls. Unless the separations formula is changed when the interstate toll reductions become effective, they will result

in loss of toll revenue to the local service telephone companies and will produce pressure on local service budgets to cut service and maintenance, or to increase local service monthly telephone charges to offset the loss of long distance telephone revenues. Either of these results, or both of them in conjunction, would be disastrous to local telephone service in North Carolina.

CONCLUSION

1. The North Carolina Commission supports the return of $237,000,000 in excess telephone profits to telephone customers, but strongly objects to the method by which it is to be returned to the relatively few interstate long distance telephone users, to the detriment of local service telephone customers.

2. The North Carolina Commission urges the Interstate Foreign Commerce Committee of the House of Representatives to exercise its oversight procedures with the FCC to revise the separations formulas so that a fair share of the $237,000,000 will go to local service telephone customers through improvement of the quality of the local service and reductions in local telephone charges.

3. The North Carolina Commission further urges the enactment of H.R. 12150 to the end that a permanent joint board may be established to insure just and reasonable separations formulas for proper allocation of interstate toll revenues to the local service telephone customers who must support the local service telephone plant utilized in long distance service.

HARRY T. WESTCOTT, *Chairman.*
JOHN W. MCDEVITT.
CLAWSON L. WILLIAMS, Jr.
MARVIN R. WOOTEN.

Mr. BROYHILL. Mr. Westcott has been commission chairman for a number of years. He is highly respected in our State and we appreciate your coming up on this occasion.

Mr. WESTCOTT. Thank you, Congressman.

Mr. RIORDAN. From the North Dakota Public Service Commission, E. Bruce Hagen, president; Richard A. Elkin, commissioner and Ben J. Wolf, commissioner. They are listed as being here but apparently they are not here yet.

From the Oklahoma Corporation Commission, Charles Nesbitt, chairman, and Ray C. Jones, commissioner. (No response.)

From the Oregon Public Utility Commission, Sam R. Haley, commissioner.

Mr. HALEY. Mr. Chairman and members of the committee, I do not wish to submit a statement later, but I do support the legislation.

Mr. RIORDAN. The Pennsylvania Public Utility Commission, Chairman George I. Bloom.

Mr. BLOOM. I will make a presentation a little later, Mr. Chairman.

Mr. RIORDAN. Rhode Island Public Utilities Commission, Chairman Archie Smith.

Mr. SMITH. I will make a statement later.

Mr. RIORDAN. South Dakota Public Utilities Commission, C. L. Doherty, commissioner.

Mr. DOHERTY. I wish to file a statement, sir. South Dakota supports this bill.

STATEMENT OF C. L. ROY DOHERTY, COMMISSIONER, SOUTH DAKOTA PUBLIC UTILITIES COMMISSION

My name is C. L. Doherty, Public Utilities Commissioner of the State of South Dakota. I was first elected to the South Dakota Public Utilities Commission in 1936—34 years ago, and I am presently serving my sixth consecutive term of office.

The South Dakota Public Utilities Commission has long recognized the fact that under current separations procedures the FCC continuously finds it neces-

sary to reduce long distance telephone rates while state commissions are continuously forced to increase local service rates. It is obvious that in order to remain in business a telephone company must collect enough revenue to cover its operating expenses. The fixing of telephone rates is not an exact science and whether the revenue comes from one type of customer or another, the telephone companies must still earn sufficient revenues to pay their operating expenses and give a reasonable rate of return to their investors.

There is no doubt that a regulatory agency would find it quite pleasant to reduce the telephone rates under its jurisdiction. However, someone must bear the responsibility of seeing that the telephone companies earn a sufficient return to attract them to continue offering good telephone service to the public.

The revenue needed to support telephone service could be paid entirely by interstate long distance users, or it could be paid entirely through local service charges. However, it seems that the best method of obtaining sufficient revenues would be to set the rates for each type of service at such a level as to make that type of service support its own operating costs. We feel that the rates charged for interstate long distance service are not adequate to cover the true costs of that service, and that this inadequacy results in the rates being paid by local users having to help support interstate long distance usage.

The average telephone user does not use interstate long distance service heavily. While basic local telephone service has come to be considered a necessity by the average person, long distance service is still a luxury used only on special occasions by the great majority of telephone users. The average consumer can derive more economic benefit from a reduction in local service rates than he can from a reduction in interstate long distance rates.

It has been said that 85% of our long distance usage comes from 15% of our telephone users. If this relationship still holds true, we are practicing discrimination in favor of the 15% of consumers who are heavy long distance users at the expense of the remaining 85% majority of consumers who use long distance service only sparingly. We feel that it is against the public interest to set telephone rates in favor of such a limited number of affluent telephone users.

The fact that interstate long distance telephone rates are decreasing at the same time local service rates are increasing should create questions about the equitableness of the present separations procedures. However, the fact that in certain cases intrastate long distance rates already exceed interstate long distance rates is indeed difficult to explain.

It seems evident that the separations procedures should be revised to reflect a more realistic amount of jointly used plant and jointly incurred expense in the cost of interstate toll service. The present separations procedures give far too much weight to the minutes of actual use. A telephone set is actually in use only a very small fraction of each 24-hour day, however, each type of service is entirely dependent upon a plant which must exist 24 hours every day. Therefore, any separation of the cost of idle time which is based on minutes of actual use is unrealistic.

In separating the cost of stand-by time we recommend a complete departure from the minutes of actual use theory. All facilities used in joint service are equally available for both toll and local use. Local plant must be available for long distance usage just as much as for local usage. If the plant were not available on a standby basis for both types of service, each type of service would have to build and maintain a separate telephone system. Therefore, division of the cost of stand-by time on a 50-50 basis is more equitable than is division on a minutes of use basis.

The South Dakota Public Utilities Commission has recently found it necessary to grant intrastate rate increases in order to assure adequate telephone service for the future. Our most recent telephone rate decision was re Northwestern Bell Telephone Company, 77 PUR 3d, 215 in which Northwestern Bell Telephone Company was granted a rate increase to provide approximately $1,213,987 additional gross revenues. The Bison State Telephone Company, a subsidiary of the Continental Telephone Corporation, has recently applied to the South Dakota Public Utilities Commission for a rate increase to provide additional gross revenues in excess of $159,000.

We are satisfied that if the separations had been made on the availability of service basis rather than the minutes of use basis, we would not have had these rate increase applications. We are further convinced that the decreases in interstate long distance rates have been a major contributing factor in the need for higher local service rates.

The South Dakota Public Utilities Commission respectfully offers the foregoing statement for insertion in the hearing records of the Subcommittee on Communications and Power of the House Committee on Interstate and Foreign Commerce.

Mr. RIORDAN. From the Tennessee Public Service Commission, Cayce L. Pentecost, chairman.

Mr. PENTECOST. We support this legislation.

Mr. RIORDAN. The Virginia State Corporation Commission, Mr. Jesse W. Dillon, commissioner.

Mr. DILLON. Virginia wholeheartedly supports this bill, and we hope we can convince Mr. Satterfield.

Mr. RIORDAN. From the Washington Utilities and Transportation Commission, Francis Pearson will have a statement to make later, and Robert D. Timm, chairman.

Mr. TIMM. The Washington Utilities and Transportation Commission would like to file a statement in support of this bill.

(The statement follows:)

STATEMENT OF ROBERT D. TIMM, CHAIRMAN, WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

Gentlemen, this Commission is deeply disturbed by the recent action taken by the Federal Communications Commission in reducing interstate toll rates on January 1 and February 1, 1970 in the aggregate amount of $237 million per year. By such action the Federal Communications Commission has completely disregarded the more realistic approach of effecting changes in separations procedures which would have equitably distributed among both intrastate and interstate telephone users the benefits to be derived from a reduction in the revenue requirements of the American Telephone and Telegraph Company.

At this time, when national efforts are directed to arresting current inflationary trends, proceedings are pending or anticipated in various states involving potential intrastate rate increases exceeding $500 million for Bell System operating companies. Pacific Northwest Bell Telephone Company was authorized a $14 million increase in annual exchange revenues in this state, effective November 3, 1969. United Telephone Company of the Northwest was granted an interim increase of $115,000 per year in September, 1969, and further increases by this company are considered likely. Hearings are now in progress involving requests from General Telephone Company of the Northwest, Inc. for increases which will approximate $3.5 million per year. This pattern is prevalent throughout many states. Any action by the Federal Communications Commission in revising separations procedures would substantially mitigate state exchange revenue requirements. A decrease by one jurisdictional segment of the total telephone network in the face of such aggravated requirements at local exchange levels demands corrective action.

Any change in separation procedure assigning additional investment and expense to interstate support would immediately be considered in rate proceedings now pending, or recently concluded, to the extent that interstate revenue requirements would be affected. Procedural changes shifting revenue requirements to interstate will benefit local exchange operations for the independent industry as well as for the Bell System.

We are grateful for your response to the National Association of Regulatory Utility Commissioners' request for a hearing on this matter and the opportunity for our Commission to express to the Committee the importance of equitable separations procedures and our support of H.R. 12150, Federal-State Communications Joint Board Act of 1969.

We are impressed that cooperation between state and Federal jurisdictions must return in this highly critical area of telephone cost separations. We are of the opinion that consideration of H.R. 12150 by this Committee may begin a return to the spirit of cooperation which has been lost.

Mr. RIORDAN. From the West Virginia Public Service Commission, we have the three commissioners and Madam Chairman, Miss

Elizabeth V. Hallanan; Mr. Boyce Griffith and Mr. Robert L. Stewart.

Miss HALLANAN. We have a statement, Mr. Chairman, we would like to submit in support of the bill and ask that it be made a part of the record.

(The statement follows:)

STATEMENT OF PUBLIC SERVICE COMMISSION OF WEST VIRGINIA

The Public Service Commission of West Verginia supports the position of the National Association of Regulatory Utility Commissioners on the desirability of readjusting costs between interstate and intrastate telephone business rather than reducing interstate toll rates and urges consideration of the proposed Federal-State Communications Joint Board Act of 1969, H.R. 12150, as a means of solving problems in this area in the future.

Illustrative of the problems created by past and present regulatory practices is the disparity between the charges for toll calls entirely within the State of West Virginia and those partly in and partly outside the State of West Virginia. For example, a person-to-person call from Charleston, West Virginia, to Huntington, West Virginia, costs $1.20, while a person-to-person call from Charleston, West Virginia, to Chesapeake, Ohio, costs $0.65. Huntington and Chesapeake are separated only by the Ohio River and persons may call from one to the other toll free. Similarly, a person-to-person call from Charleston, West Virginia, to Bluefield, West Virginia, costs $1.20, while a person-to-person call from Charleston to Bluefield, Virginia, costs $0.80. Bluefield, West Virginia, and Bluefield, Virginia, are separated only by the state line and also have free calling between them. In each of these instances, the intrastate call and the interstate call are made over exactly the same facilities with minimal additions on the interstate call. The disparity betwen station-to-station rates between these points is similar but smaller.

Since interstate calls over the same facilities cost substantially less than intrastate calls and since earnings on the interstate business have always been higher than those on the intrastate business, it is apparent that it is the *method* of arriving at the costs of jointly used facilities to be assigned to each class of business which results in the difference. The heart of that method is the assignment of costs related to jointly used facilities partly to interstate business and partly to intrastate business, a process which has been formalized in the Separations Manual.

Although we have stressed differences in toll rates for illustrative purposes, the effect of the separation process extend also, and perhaps more importantly, to exchange service. All costs not picked up by interstate or intrastate toll service must be borne by the individual subscriber.

In addition to the question of the over-all assignment of costs between interstate and intrastate service, there is the perplexing question of the effect on individual states of any one method of separations. This matter has been, and continues to be, particularly vexing to this Commission. In 1967, the Federal Communications Commission approved changes in the Separations Manual which would have resulted in savings to West Virginia of $480,000. This change was never placed in effect. On the contrary, the FCC, by order entered January 29, 1969, adopted a procedure which added $790,000 to West Virginia, instead out of the total reduction to all states of less than $100,000,000. By an additional $790,000 of expense is reflected in the Company's exhibits in the current rate case of The Chesapeake and Potomac Telephone Company in which it seeks a total increase of $11,000,000. This total shift for West Virginia of $1,270,000 is out of the total reduction to all states of less than $100,000,000. By an additional change effective January 1, 1970, the impact on West Virginia has been reduced by $430,000. We certainly could not say with any assurance what a total transfer of $237,000,000 in revenue requirements from intrastate business to interstate business would mean to West Virginia, but we feel sure that it would represent a substantial portion of the increase now being requested from us.

The interstate telephone business rides piggy-back on the intrastate systems of the separate operating companies. It is extremely doubtful that it could survive in anything like its present form without the intrastate systems. On the other hand, the intrastate systems could survive, although not so well, without the interstate business. Interstate toll business may, for a while, have been an infant requiring special care and feeding but it has now become a lusty giant which we feel should be required to bear a larger share of total system costs.

The West Virginia Commission urges this Committee and the United States Congress to give careful consideration to means of alleviating what we feel to be inequities in the assignment of costs between different services and, thus, between the ultimate consumers.

Respectfully submitted.

ELIZABETH V. HALLANAN, *Chairman.*
ROBERT L. STEWART, *Member.*
BOYCE GRIFFITH, *Member.*

Mr. RIORDAN. From the Wisconsin Public Service Commission Orville P. Deuel, director of research.

Mr. DEUEL. Mr. Chairman, our chairman, Mr. Arthur L. Padrutt is on his way but has not yet arrived, but he expects to be here later in the day.

Mr. RIORDAN. For the Wyoming Public Service Commission, Walter W. Hudson, chairman. Apparently Mr. Hudson has not arrived yet. (See statement from Wyoming, placed in the record by Congressman John S. Wold, p. 136, this hearing.)

Mr. AVERY. Mr. Chairman, I am George A. Avery, Chairman of the District of Columbia Public Service Commission which sets the rates for the people here in Washington, D.C., and we have a statement in support of the bill which I will submit for the record. With me is Commissioner William L. Porter of the District of Columbia Commission.

(The statement follows:)

STATEMENT OF GEORGE A. AVERY, CHAIRMAN, DISTRICT OF COLUMBIA PUBLIC SERVICE COMMISSION

The Public Service Commission of the District of Columbia joins with the other state commissions in protesting the action of the Federal Communications Commission in reducing interstate rates of the American Telephone and Telegraph Company at a time when subsidiaries of that same company are seeking increases in local rates. As an alternative to rate reductions, the FCC should have considered changes in separations procedures which would have shifted additional plant and expenses to the interstate category, thus relieving at least a portion of the pressure on the states for increases in local rates.

At the request of the Honorable Francis Pearson of the Washington Utilities and Transportation Commission, president of the National Association of Regulatory Utility Commissioners, we have prepared information concerning our most recent telephone rate order, the current status of telephone rate proceedings, and the estimated effect upon current separations procedures of the FCC's reduction in interstate toll rates. That information is as follows:

1. THE MOST RECENT TELEPHONE RATE ORDER OF THE D.C. PUBLIC SERVICE COMMISSION

By Order No. 4887 dated December 22, 1964, as amended by Order No. 4899 dated February 18, 1965, The Chesapeake and Potomac Telephone Company was allowed a rate of return of 6.25% and an increase in gross operating revenues of $2,346,900.

2. THE CURRENT TELEPHONE RATE PROCEEDING

On November 8, 1968, The Chesapeake and Potomac Telephone Company filed an application seeking a further increase in rates. The Company is contending that it requires an 8½% rate of return. Based upon its test year figures, such a return would require an increase in gross operating revenues of $13,282,000. The case has progressed through the presentation of testimony by the Company witnesses. There still remains the direct and cross-examination of staff and intervenor witnesses, company rebuttal, and post-hearing briefs.

3. ESTIMATED EFFECT OF THE REDUCTION IN INTERSTATE TOLL RATES ON CURRENT SEPARATIONS PROCEDURES

If the reduction in interstate rates becomes effective, past experience indicates that it will increase toll usage in relation to the local usage. At some future time, as such a pattern became apparent, a greater portion of the plant and expenses would be allocated to the interstate category. The timing and the amount of this shift in the rate base and expenses would depend upon the stimulation effect of the new toll rates. There would likely be no effect upon the issues in the rate case presently before this Commission. If, in lieu of the decrease in interstate rates, separations procedures were changed now so that a greater portion of plant and expenses fell in the interstate category, immediate effect could be given in our current proceeding to such changes.

For instance, the NARUC Communications Subcommittee is currently reviewing separations procedures applicable to local dial switching equipment. The investment in such equipment is currently separated on a dial equipment "minutes of use" theory. The most recent changes in separations, those involving subscriber station plant, changed the separation of subscriber station plant from minutes of use by adding value factors which gave greater weight to the minutes of use for interstate calling.

It is estimated that the change in the allocation of local dial switching equipment costs proposed by the NARUC Subcommittee would, on an overall basis, transfer $100,000,000 in annual revenue requirements from the states to the interstate jurisdiction.

If the separation of local dial switching equipment could be handled on a basis similar to that which is used for local subscriber station plant, it is our estimate that approximately 15% of C & P's approximately $70,000,000 investment in local dial switching equipment would be changed from the intrastate to the interstate category. Thus, about $10,000,000 of plant would be shifted. This alone would eliminate the need for intrastate revenues of between approximately $1,250,000, at the currently authorized rates, and $1,700,000, at the new rates sought by C & P.

CONCLUSION

It is clear, therefore, that we in the District of Columbia are considering whether local rates should be raised. A change in the separations procedures, such as that currently being considered by the NARUC Staff Subcommittee on Communications, would enable us to reduce by a significant amount, the amount of local revenue which The Chesapeake and Potomac Telephone Company would require. The recent reduction in interstate toll rates, while it would benefit some District customers, would not have the same benefit for all customers as would the opportunity to avoid or reduce an increase in local rates.

Mr. RIORDAN. Is there anyone else I have missed who wants to make a statement for the record?

Mr. WESTCOTT. Mr. Chairman, I would like to introduce my fellow Commissioner, Marvin R. Wooten.

Mr. RIORDAN. I have a statement from the Florida Public Service Commission.

(The statement follows:)

FLORIDA PUBLIC SERVICE COMMISSION,
Tallahassee, Fla., February 20, 1970.

Re House Hearing on H.R. 12150, a Bill Proposing the Federal-State Communications Joint Board Act of 1969.

Hon. FRANCIS PEARSON,
President, National Association of Regulatory Utility Commissioners, Washington, D.C.

SIR: The Subcommittee on Communications and Power of the House Committee on the Interstate and Foreign Commerce has scheduled a hearing beginning at 10:00 A.M., Tuesday, February 24, 1970, in Room 2322 of the Rayburn House Office Building, Washington, D.C.

It will be impossible for me or any member of this Commission to attend the hearing because of a heavy schedule of hearings and conferences. I am, therefore, taking this means to respectively advise you of the Commission's position in regard to this bill.

It is our interpretation that H.R. 12150 is identical to S. 1917 which was the subject of hearings before the Senate Committee on Commerce on December 9, 1969. This legislation proposes the creation of a seven member board composed of four FCC Commissioners designated by the FCC and three State Commissioners nominated by the NARUC and appointed by the FCC. The Board would have sole administrative authority under the Communications Act of 1934 to adopt and amend separations procedures. An order of the Board prescribing separations procedures would be deemed an order of the FCC for purposes of judicial review.

We have previously registered our support of S. 1917. The Federal Communications Commission has had a long history in telephone separations of grossly discriminating against the users of local and intrastate so as to unjustly favor the users of interstate calls. Since the overwhelming majority of calls are of a local or intrastate nature, the FCC's long-standing separations policy does not, in my opinion, benefit the interest of the general public at state level.

We believe that the Joint-Board would give the State Commissions a stronger position protecting the interest of the public at State level and are therefore in full support of the passage of H.R. 12150.

Your support will be greatly appreciated.

With kind regards, I am

Sincerely,

WILLIAM T. MAYO, *Chairman.*

Mr. RIORDAN. I also have a statement from the State of Montana which, with your permission, I would like to have inserted in the record.

Mr. MACDONALD. Without objection, it is so ordered.

(The statement follows:)

STATEMENT OF BOARD OF RAILROAD COMMISSIONERS, PUBLIC SERVICE COMMISSION OF MONTANA

GENTLEMEN: The Montana Public Service Commission wishes to express its profound and sincere desire to see the passage of H.R. 12150. This will be the culmination of a long and hard fight for equal representation for the States in the determination of the separation factors to be used in determining earnings for the AT&T Company, regulated by the FCC, and in determining the earnings of the subsidiary companies, regulated by the State Commissions.

Theoretically, there now exists a cooperative effort to do just this between the States and the FCC. However, without the required representation of the States as provided for in H.R. 12150, it just does not turn out to be much of a cooperative venture.

The most recent glaring example of that lack of cooperation by the FCC is the unilateral action taken by the FCC in ordering a reduction of $150,000,000 in interstate rates of the AT&T Company.

This, on the face of it, appears to be a great saving for all of the telephone ratepayers. But is it? The answer is a definite and resounding *No.* How many people in Montana of the lower and middle income groups make calls to New York, Rhode Island, or Florida? Very, very few indeed, and yet this is what they would have to do if they were to take advantage of this magnanimous gesture by the FCC to provide lower interstate rates for them.

The State Representatives on the Joint Board, as provided for by H.R. 12150, would have advocated an adjustment in the separations procedures so as to allocate a greater portion of the plant and related expenses to interstate operations. This would have the effect of increasing the amount of revenues needed for interstate operations and reducing the amount of revenues needed for intrastate operations. The interstate revenues could remain the same as at present, and the ever-increasing demands for intrastate rate increases by the AT&T subsidiaries would be slowed by $150,000,000. The advocating of this procedure is not without its logic. If the revenues of AT&T increase without any increase in rates, to such an extent that the FCC determines a rate reduction is necessary, it logically follows that there must be a much greater use of the plant

by the interstate callers. This is what separations is all about and why the change in allocations of plant between interstate and intrastate operations is the only sensible approach to the disposition of the surplus of revenues accrued by AT&T under FCC jurisdiction.

The rate reduction ordered by the FCC would also reduce the revenues of the independent telephone companies operating in Montana. The Montana Commission is presently faced with rate increase applications from four independent companies and the action of the FCC, if allowed to go through, would compound the problem. We have recently held an increase-in-rates hearing for the local AT&T subsidiary. Without H.R. 12150 and a reconsideration of the interstate rate reduction, another will soon be forthcoming.

At the present time you can call, more cheaply, a given number of miles interstate than you can intrastate. The action of the FCC would further increase this disparity.

The reduction of interstate rates ordered by the FCC would be of great benefit to the affluent and corporate telephone users. The only glimmer of hope on the horizon for the lower and middle income class of telephone users to lower, or even keep at the existing level, their contributions to AT&T is H.R. 12150 and a reconsideration of the recently ordered interstate rate reduction.

We, therefore, respectfully urge you to recommend passage of H.R. 12150 and to urge the FCC to reconsider its action in reducing interstate rates by the $150,000,000 so urgently needed by intrastate ratepayers to just maintain the status quo.

Respectfully submitted.

PAUL T. SMITH, *Chairman.*
LOUIS G. BOEDECKER, *Commissioner.*
ERNEST C. STEEL, *Commissioner.*

Mr. RIORDAN. That concludes my presentation, gentlemen, and thank you very much.

Mr. MACDONALD. Hasn't anyone from Massachusetts contacted you?

Mr. RIORDAN. I had trouble contacting them. One of the commissioners is sick.

Mr. MACDONALD. I had not heard from anybody.

Thank you very much.

Mr. RIORDAN. Thank you very much, Mr. Chairman, and we are sorry that all of the commissions are not represented here but, as you know, they have to travel long distances, some of them, and others will file reports for the record and we hope that Massachusetts, if they have not seen the light, will and come through; I am sure they will.

Mr. MACDONALD. You may continue with your statement, Mr. Pearson.

Mr. PEARSON. The NARUC is a quasi-governmental nonprofit organization founded in 1889. Within its membership are the governmental bodies of the 50 States and of the District of Columbia, Puerto Rico, and the Virgin Islands engaged in the regulation of carriers and utilities. We endeavor to try to do our best to see that the regulatory processes are continuously improved for the benefit of the consumer. We are making every effort to see that this is done clear along the line.

We have made every effort to work with the Federal Communications Commission. We thought that we were a few years ago but then we find ourselves in the process of increasing rates by leaps and bounds in the various States. For instance, the State of Washington, where we increased the rates by $14 million per year just 2 days before the FCC order came out cutting the interstate rates some $237 million, and I might add we allowed a 7¼ to 7½ percent rate of return on

an average of monthly earnings of original cost rate base, and the FCC is allowing something over 8 percent. On the Federal level, that is a quarter of a billion dollars to the A.T. & T. This is some of the things I hope you will take into consideration.

Mr. Chairman, you brought up the statement that we were in the process of having hearings. I received a letter from Chairman Burch of the FCC stating that their staff would meet with our staff to try to work out some mutual agreements as far as separations are concerned. So far, we have had no progress whatsoever that I can see. We are meeting now. We met yesterday, and we will continue to meet. They will make a statement, I am sure, tomorrow, that due to their rulings in 129, the first of 1969, that it will increase the rate base of the local companies some $66 or $65 million a year; with the processes that they are going through, it will be beneficial, and I will have to admit it is beneficial, but the State of Washington will receive $600,000 a year and the salary increase is much more than twice that much.

Inflation is eating up much more than that, and it is rather ridiculous for us to pay from $9 to $20 for a 7- to 7½-percent rate or return for a telephone in some retired person's home or in anyone's home when you can call clear across the Nation for 25 cents. Certainly the interstate lines are worthless unless they have the telephone on each end of the lines that are the expensive part of communications.

Enough for that now. I am going to introduce now Hon. Archie Smith, chairman of the Rhode Island Commission who will tell more of some of the problems that we are and have been facing with our problems of separations.

Mr. TIERNAN. I deem it a great honor today to introduce to the members of this committee the commissioner from Rhode Island who has been a long-time friend of mine, who served as assistant U.S. attorney in the State, worked in the legislature in drafting many of the complicated bills, had broad experience in areas of consumer protection, and has been doing an outstanding job as the new commissioner for the State of Rhode Island, and I welcome you to this subcommittee.

STATEMENT OF ARCHIE SMITH

Mr. SMITH. Thank you, Mr. Tiernan. I appreciate those remarks.

Mr. Chairman and members of the committee, in the United States today there are over 110 million telephones which average out to about 52 telephones per 100 people. Of these, 72 percent are classified as residential and the remaining 28 percent are classified as business.

These telephones comprise a nationally interconnected system which transmits approximately 150 billion calls a year.

Dominant in this national communications network is the American Telephone & Telegraph Co. and its 24 associated companies which comprise the Bell System. This system is concentrated primarily in the metropolitan areas and has over 91 million telephones, a gross plant investment of over $46 billion, and annual revenues of approximately $14.5 billion.

The remainder of the telephone service in the Nation is provided by 1,850 independent, or non-Bell companies who have 19½ million telephones, a gross plant investment of almost $12 billion and annual revenues of $2.5 billion.

Regulatory jurisdiction over the telephone industry is divided between the FCC and the State commissions.[1] The FCC regulates interstate message toll calls, commonly referred to as long distance calls.[2] The State commissioners regulate intrastate message toll calls and local exchange calls even in instances where the boundaries of the exchange area overlap State lines.[3]

Under this division of regulatory responsibility, the FCC regulates approximately 2½ billion interstate long distance toll calls a year and the State commissions regulate approximately 147 billion intrastate toll and local exchange calls a year.[4]

In terms of plant investment, the FCC exercises jurisdiction over approximately 25 percent of Bell System plant[5] while the State commissions exercise jurisdiction over the remaining 75 percent and over virtually all of the plant of the independent telephone companies.[6]

Under the rate base concept of ratemaking, practiced by the FCC and the State commissions, the Bell System, through its rates, is entitled to earn a reasonable return on its plant invested in common carrier service and to recoup its expenses reasonably incurred in furnishing such service. Since the vast bulk of Bell System plant and expenses are used in furnishing both interstate and intrastate communication service, such plant and expenses must be allocated or separated between the interstate and intrastate uses for purposes of ratemaking by the respective Federal and State jurisdictions.

The procedures employed in the division of these joint telephone costs are commonly referred to as "separations procedures." Inherently, they involve judgment factors in which there is no absolute correctness or incorrectness. We do not expect the committee to focus on the very technical details of separations procedures. However, there is involved, as hereinafter explained, a basic policy question of tremendous effect upon the American consumer which we hope the committee will consider and act upon.

It is essential to the public interest that procedures for separating such plant and expenses be fair and equitable so that no unreasonable burden will be placed on either the interstate or intrastate users of the telephone service.

Although the FCC has controlled the prescription of separations procedures since the beginning, it has never prescribed equitable ones because it has consistently refused to allocate a fair amount of the cost of providing local telephone service to the users of the interstate

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[1] Telephone companies are regulated by State commissions in every State except Texas where regulation is administered at the municipal or local level. In the District of Columbia, the Chesapeake & Potomac Telephone Co., part of the Bell System, is regulated by the District of Columbia Public Service Commission.

[2] Communications Act of 1934, as amended, sections 1 *et seq.*

[3] Id., sections 2(b) and 221(b). An example of an exchange area which overlaps State lines is the very large Washington metropolitan exchange area encompassing the District of Columbia and parts of Maryland and Virginia and calls therein are subject exclusively to State and local regulation. The dimensions of the exchange area are measured by the distance you can call without incurring a toll charge.

[4] The relationship between the national volumes of local and toll calls is revealed by a publication entitled "Statistics of Communications Common Carriers" issued by the FCC for the year ended December 31, 1967, page 21. This publication—the latest issue of its kind—reveals that during 1967 there were 141,912,636,000 "local" calls and 7,327,186,000 "toll" calls. Since all of the local calls, and that portion of the toll calls which were intrastate (estimated at two-thirds), are subject to State and local regulation, it is obvious that the telephone business in the Nation is predominantly subject to State and local jurisdiction under the Communications Act.

[5] *Re American Telephone and Telegraph Company et al.,* 70 PUR 3d 129, at p. 145, par. 21 (1967).

[6] Communications Act of 1934, as amended, section 2(b)(2).

service. Local telephone service is an integral part of the national and international toll network. It is the gateway to the toll network and without it the toll network would be worthless.

The FCC's proclivity for inequitable separations procedures which favor its narrow regulatory interests is magnified by a strong technological trend in the telephone industry which results in reduced costs for long distance service and increased costs for local service. The extensive use of microwave facilities and of coaxial cable, with its high volume circuit capacity, has dramatically reduced the cost of long distance circuits. Ten years ago coaxial cable could carry only about 500 telephone calls at a time. The newest ones can handle about 32,000 calls at a time, and it is anticipated that in the near future this capacity can be increased to 100,000 calls. During the same period, the cost of installing such cable has decreased from about $100 a mile for each channel to less than $5.

In contrast, there is no such technological breakthrough in the furnishing of local exchange service and hence the cost of providing this service steadily rises due to inflation. Although exchange plant is employed in both interstate and intrastate service, the investment in such plant is determined by the number of exchange subscribers served and not by the volume of local traffic generated. In other words, the investment in the local distribution plant connecting the subscriber to his central exchange office, as well as a significant portion of the investment in the central office, have a 1-to-1 correspondence with the number of subscribers. Accordingly, exchange plant costs vary directly with the number of subscribers, while the magnitude of the long-distance toll lines plant investment is largely determined by actual usage and hence this high use factor permits long-distance calling to achieve a high degree of economic efficiency.

The very low use of exchange plant was described by the FCC in July 1967 in the following terms:

> As a consequence of this characteristic of subscriber plant, although such plant is available for use of the subscriber twenty-four hours a day, it is in actual use, on a nation-wide average basis, only twenty-nine minutes out of the twenty-four hours. For the remainder of the time, the plant stands idle but available for the subscriber's use. In other words, actual use for all services, intrastate and interstate, accounts for only 2 percent of total time such plant is available for use. Of this 2 percent, interstate toll service makes actual use of the plant for an average of 4 percent, and exchange service for an average of 92 percent. Re *American Telephone and Telegraph Company et al.* (70 PUR 3d 129, at p. 212, par. 286).

Presently, it is estimated that the average telephone is used 1½ minutes a day for interstate toll service, 1½ minutes a day for intrastate toll service, and 27 minutes a day for local exchange service; and remains idle 23½ hours a day.

The FCC stated on page 3 of its letter to Chairman Staggers of the House Committee on Interstate and Foreign Commerce on November 17, 1969, that in 1952 less than 3 percent of subscriber line plant was assigned to interstate operations whereas today "16 percent of these costs are assigned to interstate operations even though such operations account for only about 5 percent of the actual use of their subscriber plant." By completely ignoring the 23½ hours of idle time, the FCC seeks to cast itself in a magnanimous role. In reality, the more affluent

interstate callers are paying the cost of maintaining subscriber plant, which is absolutely indispensable to long-distance service, for only about 3 hours and 50 minutes a day whereas the local and intrastate callers are paying for the remaining 20 hours and 10 minutes.

Furthermore, the FCC failed to mention that subscriber line plant only includes the telephone plant on the subscriber's premises and lines connecting the premises with the local central office. The local central office equipment, which is an integral part of both exchange and toll service, has only a 6-percent assignment to interstate operations.

Obviously, the paramount criterion employed in the separation of all telephone plant has been far too heavily based on actual time in use with far too little consideration being given to idle time which someone must pay for. Accordingly, primary criterion for the separation of telephone plant is consistent with the character of the toll business but it is inconsistent with the character of exchange business.

The basic vice in FCC policy in telephone separations is to take an overly simplistic view of our nationally integrated communications system as being divided into two parts—interstate and intrastate—and to shower the economies of long-distance circuitry upon the interstate callers instead of flowing the benefits through to the far more numerous and less affluent local callers.

Largely as a result of the FCC's longstanding unreasonable separations procedures, the consumers of America are now confronted with a ridiculous situation which would be laughable if the financial stakes were not so high. On the one hand, the FCC has recently reduced Bell System interstate message toll rates in the amount of $237 million. On the other hand, the same Bell System has instituted proceedings now pending before 13 State commissions to seek rate increases totaling $599 million as reflected by the following tabulation:

State	Amount requested (millions)	State	Amount requested (millions)
District of Columbia	$13.3	Michigan	$59.8
Florida	32.0	New York	175.0
Georgia	29.8	Ohio	93.3
Illinois	86.5	West Virginia	11.1
Indiana	5.0	Wisconsin	14.9
Kentucky	2.1		
Louisiana	24.0	Total	599.0
Massachusetts	52.2		

The following tabulation reflects the rate increases granted by 12 State commissions to Bell System companies since January 1, 1969:

State	Amount received (millions)	State	Amount received (millions)
Colorado	$5.9	Rhode Island	$5.9
Connecticut	13.2	Tennessee	2.1
Maryland	22.8	Utah	2.1
Missouri	30.7	Virginia	2.9
New Mexico	5.0	Washington	14.0
North Dakota	.5		
Oregon	1.4	Total	106.5

The preceding figures, of course, do not include the rate increases now being sought by the non-Bell telephone companies who are also adversely affected by unfair separations procedures. For example, the General Telephone & Electronics Corp., the Nation's largest non-Bell

telephone company, has stated that it will file applications with State commissions to seek in excess of $100 million in telephone rate increases by mid-1970. A G.T. & E. spokesman stated that rate increase applications will be filed "for virtually every company in our system, and some will be filing for a second increase in a very short period of time," and that the individual requests will average about 20 percent.

All non-Bell companies have lost revenue as a result of the $237 million interstate reduction since they will receive less interstate toll revenue through their settlements with the Bell System and, therefore, this loss of revenue will have to be recovered from intrastate and local users of service.

Furthermore, this growing tide of rate applications during this accelerated inflationary period clearly indicates that virtually all of the commissions of the 50 States will be pressed in the near future to increase rates for local telephone service.

The FCC in its letter to Chairman Staggers on November 17, 1969 (page 3), has sought, we believe, to exaggerate the benefit to the average telephone user of "low rates for long-distance calls made during evening and nighttime hours and throughout the weekend." The FCC says that this "has made the service economically attractive and available to the householder and members of the family who, in this age of travel and family dispersion, have become dependent upon the telephone as a principal means of communications with each other."

The FCC chooses to ignore the fact that in the vast majority of cases the person who makes an interstate toll call for a few cents less is the same person who must pay unduly high charges for exchange service and for intrastate toll calls. The result is a net loss to the average consumer.

The $150 million interstate rate reduction which the FCC negotiated with A.T. & T., which became effective January 1, 1970, accomplished the following significant changes in long-distance rate structure:

(*a*) Reduction to 90 cents for 3-minute customer-dialed coast-to-coast calls, and advancement of the time these "night rates" apply to 5 p.m. from the present 7 p.m.;

(*b*) Introduction of a 35-cent coast-to-coast rate (less for intervening points) for a 1-minute customer-dialed call between midnight and 8 a.m.;

(*c*) Lengthening of the reduced rate period by an additional hour from 7 a.m. to 8 a.m.; and

(*d*) Inauguration of a separate, discounted rate schedule for customers who dial their own calls covering distances more than 200 miles.

The Wall Street Journal, in reporting on this proposed reduction on December 3, stated that "Business customers would be among the chief beneficiaries, particularly those transmitting short bursts of data late at night." Obviously, the late-night coast-to-coast rate of 35 cents for a 1-minute call, referred to in item (*b*) above, will be of no practical benefit to the housewife or other nonbusiness user.

In contrast, the Maryland Public Service Commission has been forced to grant a rate increase to the Chesapeake & Potomac Tele-

phone Co. of Maryland, an A.T. & T. subsidiary, which will increase its annual revenues by $22.8 million. The Maryland Commission has approved a rate of return of 7.65 percent for intrastate operations whereas the FCC has indicated that a rate of return of 8.5 percent for interstate operations would not be unacceptable.[7]

It is understood that the rate schedules which had to be approved to implement the Maryland increase ranged from 80 cents to $1.25 for residential customers in the Maryland suburban portion of the Washington metropolitan area.

The Virginia State Corporation Commission has been forced to grant a rate increase to the Chesapeake & Potomac Telephone Co. of Virginia, another A.T. & T. subsidiary, which will increase its annual service charges by $2.9 million. This increase provides: for raising the charge for connecting new telephones from $12 to $15 for business and from $8 to $11 for residential subscribers; and for raising from $6 to $8 the charge for changing business and residential telephone service from one location to another.

The Chesapeake & Potomac Telephone Co. for the District of Columbia, another A.T. & T. subsidiary, is now seeking rate increases from the District of Columbia Public Service Commission which will increase its annual revenues by $13.3 million.

These kinds of cases, which involve the Washington metropolitan area, epitomize the kind of rate increases which are being sought across the Nation. Many of these increases are described in the statements of individual State commissions which have been offered by their representatives for insertion in the record at this hearing.

These kinds of increases hit the little consumer the hardest and the injurious effects are by no means offset by the kind of interstate reductions negotiated by the FCC.

This kind of rate discrimination is particularly severe on the economically underprivileged. The U.S. Department of Commerce reports that the median family income in 1964 of households with telephones is $7,281, compared with a median family income of $3,386 for families without telephones.[8]

These statistics of the Department of Commerce further reveal that there are over 7¼ million families without telephone service and that 44 percent of these families have less than $3,000 annual income, that 71.3 percent have less than $5,000 annual income, and that 82.3 percent have less than $6,000 annual income. This is particularly unfortunate since the American people have become dependent upon telephone service for police, fire, and medical protection.

Also hard hit are retired people living on fixed incomes. Their numbers are reflected by Department of Commerce figures showing that

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[7] Following the submission of the NARUC testimony to the Senate Committee on Commerce on December 9, 1969, on S. 1917, an identical bill to H.R. 12150, the FCC, with Commissioner Johnson dissenting, denied in a letter of December 10, 1969, any intention in its public notice of November 5, 1969, of indicating that a rate of return of 8.5 percent for interstate operations of the Bell System "would not be unacceptable." However, the FCC majority in the letter conceded that the public notice did "express our views that in light of current conditions of the capital market, interstate rates which would produce a rate of return which exceeds 7.5 percent—the upper limit of the range of return found to be reasonable in 1969 by our decision in docket No. 16258—*are not unreasonable.*" (Emphasis supplied.) In conjunction with this statement, we invite the committee's attention to the texts of the public notice and of Commissioner Johnson's dissenting letter in this matter.

[8] Characteristics of Households with Telephones, March, 1965, series P–20, No. 146, Dec. 27, 1965, p. 1.

there are 9.3 million households with a median income of $2,715 and a head of household, 65 years of age or older, who is not in the labor force.

The effect of inequitable separations procedures is also depicted by the following indexes which reflect that charges for local exchange service are significantly increasing while charges for long-distance calling are going in the opposite direction: [9]

	1945	1957–59	1966
Local service revenue per telephone	64	100	111
Intrastate telephone rates	68	100	99
Interstate telephone rates	96	100	94
Consumer price index	62	100	116
Wholesale price index	58	100	106

Clearly, the average user of telephone service is benefited more by fixing his flat monthly charge for service at the lowest practicable level rather than by reductions in interstate toll rates—rates which are generally paid by a more affluent class of users. The lower the flat monthly charge, the more accessible telephone service is to the economically depressed and to others who are severely disadvantaged by inflation. Furthermore, the value of telephone service increases proportionately with the number of telephone users, and the more users the lower the cost of service for each user.

These basic economic tenets are reflected in an observation made by Senator Pastore on March 5, 1969, during a hearing of the Senate Subcommittee on Communications on FCC policy matters. He stated, in reference to separations procedures, that:

> If the advantage is weighted in favor of the local caller who is least able to pay it, I think there is a definite advantage to the average American citizen and the telephone subscriber. Certainly I find no fault in that * * * I think only too long the heavy arm of the Federal Government has striven to reduce the long distance call rate which only results in an increase in the local call rate. After all, you are going to make a certain return on the capital investment, and it all depends on how you separate that capital investment and where you put your weight.
>
> Personally, I would rather see momma call up her son or daughter more cheaply than some business executive in New York calling Washington. (Hearings on Federal Communications Commission Policy Matters and Television Programing, pt. 1, Mar. 4–5, 1969, serial 91–6, p. 102, last paragraph.)

In conclusion, I wish to point out that the effectuation of the $237 million interstate rate reduction at this time aggravates the telephone service problem we now have because it stimulates interstate calling and thereby places another burden on telephone plant which is now overburdened in various parts of the Nation.

I now defer to Chairman Wiggins of the Committee on Communications to relate the significant historical aspects of Federal-State relations in telephone separations.

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[9] These index figures are derived from a presentation by Dr. Harry M. Trebing, Director, Institute of Public Utilities, Michigan State University, to the Annual Convention of the Midwest Association of Railroad and Utilities Commissioners on June 9, 1969, in Hot Springs, Ark.

STATEMENT OF BEN T. WIGGINS

Mr. WIGGINS. Mr. Chairman and gentlemen of the committee: I am Ben T. Wiggins, vice chairman of the Georgia Public Service Commission since 1957, and I have been chairman of the committee on communications of the NARUC since 1962.

I appreciate this opportunity to appear before you this morning to present our side on this pending legislation.

The earliest efforts at effective State regulation of telephone services came with the enactment in 1907 in Wisconsin, New York, and Georgia of enabling legislation creating commissions with jurisdiction over telephone service. While the Interstate Commerce Commission obtained nominal authority over interstate telephone service with passage of the Mann-Elkins Act of 1910, this area of the business remained unregulated as a practical matter until the creation of the FCC in 1934.

The history of the problem of separating plant and expenses between State and interstate services for the purposes of establishing rates is generally regarded as beginning with the Minnesota rate cases, decided by the U.S. Supreme Court in 1913 (230 U.S. 352, 435 (1913)).

In these cases the Court criticized the use of revenues as an inappropriate basis for separation of property, but accepted without criticism the employment of weighted usage as an allocation method.

The paramount issue which arose about the time of the Minnesota rate cases and continued until about 1930 was the controversy over the board-to-board versus station-to-station method of telephone separations. Under the board-to-board principle, toll service costs included only those facilities which extended from toll switchboard to toll switchboard, excluding any consideration of exchange facilities. The station-to-station principle included the costs of all facilities from the originating telephone station to the terminating telephone station. The term "station" means the telephone instrument itself.

This controversy was decided by the Supreme Court in 1930 in *Smith* v. *Illinois Bell Telephone Co.*, 282 U.S. 133, in which it adopted the station-to-station basis of telephone separations. The Court emphasized the absence of the need for "extreme nicety" in separating telephone costs with "only reasonable measures being essential." The Court further emphasized that the separation of telephone costs between the intrastate and interstate operations of the company involved "is essential to the appropriate recognition of the competent governmental authority in each field of regulation."

Following the creation of the FCC in 1934, the FCC initiated a number of interstate message toll rate reductions. As a result, intrastate toll message rates for calls of the same distance and duration as interstate calls were provided at higher charges than required by the interstate rate schedules. This problem is known as the "toll rate disparity." Accordingly, the nature of separations procedures became of major importance. A shift of telephone plant and expenses from intrastate to interstate services derived from modification of separations procedures is a means of increasing the interstate revenue requirements to alleviate the disparity in jurisdictional toll rate schedules.

The toll rate disparity problem exists in every State except Delaware and Pennsylvania which have adopted the policy of maintaining the charge for intrastate toll calls on a parity with charges for interstate toll calls. The toll rate disparity problem could be eliminated in the remaining 48 States, but this would create an even larger consumer problem because the burden removed from intrastate toll would then have to be absorbed by the users of local telephone service.

Following the 1941 interstate toll rate reduction, the NARUC urged the FCC to conduct hearings on separations procedures. Also, in 1941, a committee composed of staff members of the FCC and State commissions was assigned the task of formulating equitable and simplified separations procedures. The report of this committee was presented to a joint FCC–NARUC committee of commissioners in the early part of 1942. The State commissioners approved the report and recommended its adoption by the FCC as a procedure to be followed in the separation of telephone costs. The FCC, on June 9, 1942, instituted a formal investigation (docket No. 6328) to determine whether such procedures (incorporated in the proceeding as exhibit 2 with certain amendments) or other procedures should be adopted. Although hearings were held in the docket, no decision was ever reached therein and the docket was closed in January 1966 during consideration of the separations issues in the A.T. & T. rate proceeding (docket No. 16258).

Great pressure was exerted on State commissions for increases in telephone rates after World War II. An anomalous situation existed then, as it does today, where exchange and intrastate toll charges were being increased in the States and interstate toll rates were being reduced by the FCC.

In an effort to correct this irrational situation, a subcommittee appointed by the NARUC–FCC Staff Committee on Telephone Regulatory Problems in 1947 reviewed the procedures contained in exhibit No. 2, as amended, and recommended a number of changes in the procedures.

This report was later approved by the NARUC without the FCC taking any formal action with respect thereto. The subcommittee was then instructed to rewrite the procedures on a direct station-to-station basis, eliminating the necessity of first making a board-to-board separation. The procedures, so rewritten, were incorporated into the original separations manual which was reviewed and approved on October 22, 1947, by the NARUC Special Telephone Committee, the predecessor to the committee I now Chair. The FCC approved the manual on an interim basis.

The transfers of annual revenue requirements from States to interstate operations which were approved by the FCC at that time and subsequently are reflected in the following table:

SEPARATIONS CHANGES TRANSFERRING REVENUE REQUIREMENTS FROM STATE TO INTERSTATE OPERATIONS

[In millions of dollars]

Year	Change	Revenue requirement	
		Time of change	Current value
1947	Simplification in methods	13	80
1952	Charleston plan	30	235
1956	Modified Phoenix	40	140
1962	Simplification in methods	46	90
1965	Exchange plant plan	134	177
1969	FCC plan	108	108
1969	Mechanical changes	35	35
	Total	406	865

The FCC in its letter to Chairman Staggers of November 17, 1969 (page 2), seeks to place these figures in their most favorable light by stating that, "Since 1952 five major revisions have been adopted in the separations procedures," and that, "It is estimated that, on the basis of current operations, these revisions have relieved the intrastate operations of the Bell System of an estimated $800 million of revenue requirements annually." [10]

As indicated by the above table, the separations transfers at the time of approval totaled $393 million and their current value is now estimated at about double—$785 million. In order to place these figures in their proper perspective, it should be remembered that the period from 1952 to 1969 has produced the greatest growth in the history of the Bell System and the worst inflation in the Nation's history. During this period, the annual revenues of the Bell System have increased from a little over $4 billion to $14.1 billion.

Furthermore, the FCC in selecting the year 1952 apparently seeks to give the impression that the first major separations change in history was voluntarily arrived at by it. The background behind this change is of particular relevance to this hearing.

In 1950, the NARUC began a reexamination of separations procedures because of a rapidly growing disparity between intrastate and interstate toll rates. The NARUC proposed a change in separations procedures to alleviate the burden on the local users which was rejected by the FCC on October 18, 1950.

The FCC on January 19, 1951, directed the Bell System to show cause why its interstate rates should not be reduced and to submit a response by March 23, 1951.

Rebuffed in its efforts to obtain relief for the local users of telephone service, the NARUC brought the matter to attention of Chairman McFarland of the Subcommittee on Communications of the Senate Committee on Interstate Commerce. Chairman McFarland on January 31, 1951, sent a letter to the FCC which, after citing the toll rate disparity problem and the pending interstate toll rate proceeding, stated that:

[10] The FCC's figure of $800 million is somewhat exaggerated since the six revisions approved from 1952 to 1969, inclusive, only total $785 million, and the "five" major revisions during this period only total $750 million.

The trouble is the general public does not realize that every move that is made to reduce long distance toll rates results directly or indirectly in an eventual increase in local telephone rates and in intrastate toll rates. Put very simply and plainly, this merely shifts the cost from the big user to the little user. . . .

I had hoped that the proposal of NARUC for a tryout of its new separations formula would get a green light from the Commission (FCC). Now, I understand the Commission is going ahead with a heavy schedule to begin in April for a further reduction in long distance toll rates . . . and that the state utility commission's proposed separation formula should be formally presented at the hearing. Frankly, I do not think that is going to the state commission. . . .

I am not in a position to pass upon the question as to whether the remedy suggested by NARUC is the proper one, but I am certain that something should be done—and at once.

On February 14, 1951, the FCC decided to do "something at once" and postponed the response date in its interstate rate investigation in order to reexamine the NARUC separations proposals. As a result, FCC Chairman Walker at the 1951 NARUC Annual Convention in Charleston. S.C., proposed a plan for use on an interim basis which became known as the "Charleston Plan" as indicated in the table previously referred to. Unfortunately, congressional intervention was required to bring about the first major revision of separations procedures in history.

The FCC further states in its letter of November 17 (p. 1) that the NARUC has failed to specify inequities in separations procedures. This is untrue. The NARUC in a letter to the FCC on September 18, 1969, urged the FCC to use the interstate excess earnings of the Bell System for the benefit of local subscribers by significantly increasing the 6-percent assignment of local central office equipment to interstate operations. Moreover, the NARUC was working cooperatively with the FCC on proposed improvements in separations procedures which would have accomplished this objective at the very time the FCC announced that Bell's excess earnings would not be available to serve the larger consumer interest.

When the FCC does not like the separations modifications proposed by the NARUC, we believe it has an affirmative duty to propose modifications which it deems appropriate instead of, as it has done so many times in the past, acting in a negative, critical, and obstructive fashion.

Time does not permit me to describe all of the difficulties which the State commissions have experienced in their almost continuous battle with the FCC to achieve fair separations procedures for the average telephone consumer. However, in order to complete the account of this tortured history of separations, I respectfully request that there be inserted in the record a history of telephone separations which appeared in the appendix to an address delivered by President Pearson on June 30, 1968, to the 1968 Western Conference of Independent Telephone Associations.

Mr. MACDONALD. Without objection, the history may be inserted.

(The "History of Telephone Separations," referred to, follows:)

History of Telephone Separations

PRIOR TO COMMUNICATIONS ACT OF 1934

Between 1910 and 1934 telephone separations were generally confined to the Bell Companies and the State Commissions in connection with state rate cases. Such studies had little uniformity of method and had the disadvantage of giving different results under similar conditions in several states. The major separations controversy centered around the use of the "board-to-board" method by the Bell Companies in making separations studies.

BOARD-TO-BOARD METHOD

Under the board-to-board plan the costs of the property used at the subscriber's station and between the station and the toll switchboard, as well as the related expenses, were assigned directly to state operations. All other property costs and expenses were divided between state and interstate operations. The toll charge represented compensation for carrying a toll message from toll board to toll board. Part of the exchange charge, on the other hand, represented compensation for carrying the toll message from the subscriber's station to the toll board. Effectively, this plan permitted a state commission to set local rates which subsidized interstate operations.

STATION-TO-STATION METHOD

Most state commissions favored the "station-to-station" plan of separations. Under this plan, all property costs and expenses are divided between state and interstate operations. The toll charge represents compensation for carrying a toll message from the originating station to the terminating station. The exchange charge represents compensation for the use of exchange plant for exchange calls only.

BOARD-TO-BOARD VS STATION-TO-STATION

During the period, 1930 to 1943, separation studies submitted by the Bell Companies generally reflected an allocation of costs on both the board-to-board and station-to-station basis. However, because local and toll rates had been established on the board-to-board basis, a portion of the exchange revenues was assigned to toll in the station-to-station studies. This controversy continued unabated.

Chief among the Bell System arguments was its interpretation of Section 221(b) of the Communications Act of 1934 as prohibiting the Federal Communications Commission (FCC) from prescribing interstate toll rates on the station-to-station basis. The Bell System contended that the carrying of an interstate message between the subscriber's station and the toll board constituted part of exchange service and consequently the FCC had no authority over it and could not prescribe rates for it.

Strongly favoring the Bell System position, but for different reasons, was a minority group of state commissioners. They stated that rates had been fixed by their commissions on a board-to-board basis and that separations should be made on the same basis. These commissioners also felt that federal jurisdiction might be extended to exchange operations if rates were based on the station-to-station plan.

COMMUNICATIONS ACT OF 1934

The FCC was instituted with the enactment of the Communications Act of 1934. The business (interstate) of the Long Lines Department of the American Telephone & Telegraph Company (A.T. & T.) as well as the interstate toll business of the other Bell Companies thus came under the jurisdiction of the FCC. In one of the early proceedings before the FCC the Bell System representatives suggested that the FCC should prescribe separation procedures and although numerous discussions were held between the Commission's staff and the Bell System regarding separations matters no action was taken in the 1930's.

TOLL RATE DISPARITY PROBLEM

Prior to 1936, the intrastate toll rates of the Associated Bell Companies were largely on the same level as the interstate rates of the Long Lines Department.

During the period since its enactment the FCC negotiated several interstate toll rate reductions. With interstate toll rates going down and intrastate toll rates remaining relatively constant or increasing, the disparity between interstate and state toll rates for the same length of haul and conversation time was recognized. This situation, known as the "Toll Rate Disparity Problem" focused the spotlight on the need for better separations.

FURTHER REDUCTION OF INTERSTATE TOLL RATES

On April 1, 1941, the FCC instituted on its own motion an investigation of the joint interstate rates of A.T. & T. and its connecting carriers under Docket No. 6053. In connection with this case, the Bell System Companies filed a petition requesting the FCC to institute an investigation to determine separation methods, and, after notice and hearings, to prescribe separations methods. The FCC took no formal action on the petition, and Docket No. 6053 was terminated by a voluntary rate reduction of interstate message toll rates.

NARUC-FCC COOPERATION

With no formal action on the separations problem by the FCC and with increased toll rate disparity, The National Association of Railroad and Utilities Commissioners (NARUC) Executive Committee appointed a committee of five to confer with the FCC concerning cooperation between state and federal agencies in separations and other joint problems. A joint staff committee, consisting of staff members of the FCC and state commissions, was organized on June 11, 1941, for the purpose of developing equitable and simplified separations procedures.

The Staff Committee's report which was presented to a joint NARUC-FCC Committee of Commissioners in the early part of 1942 included both board-to-board and station-to-station methods of separations for consideration. The state commissioners approved the report and recommended its adoption by the FCC as the procedures to be followed in the separation of property costs, revenues and expenses of telephone companies subject to the FCC's jurisdiction. Instead, the FCC on June 19, 1942, instituted a formal investigation (Docket No. 6328) to determine whether such procedures or other procedures should be adopted. The Staff Committee's report with certain amendments was incorporated in these proceedings as Exhibit 2. Although brief hearings were held in 1942, no decision was reached. In fact, Docket No. 6328 remained dormant until January 1966 when it was terminated without further FCC action.

At the NARUC Convention in November 1942, a request was made of the FCC to discontinue the study of separations procedures until the end of World War II. The FCC concurred.

On January 20, 1943, the FCC agreed with the Bell System to another reduction in message toll and private line rates based upon the station-to-station separations principles.

The toll rate disparity problem was increasing by successive reductions in interstate toll rates and repeated rate increases for the intrastate services.

The procedures in Exhibit 2 (Docket No. 6328) and its amendments were used by the Bell System for separations purposes until the first edition of the Separations Manual was published in 1947. Until 1944 separations procedures had been used almost solely for the purpose of determining rates. With the introduction of the first Message Telephone Division of Revenues Contract in that year, separations were used for dividing revenues derived from interstate operations among the then 21 Associated Companies and A. T. & T. This contract replaced the commission and prorate system and parts of the June 1, 1943, Division of Revenue (DR) Contract.

Other reductions in interstate rates became effective March 1, 1944, and July 1, 1945. The 1945 reduction only affected distances of over 790 miles.

NARUC RESOLUTION

The 1946 convention passed unanimously, the following resolution as a direct result of the FCC reducing interstate rates without adopting any uniform separation procedures:

Resolved—That the Federal Communications Commission is respectfully requested to proceed under the cooperative plan before considering any further reduction in the interstate message toll telephone rate schedule, and it is further requested that ample opportunity first be given to each of the States to present testimony on the disparity existing between interstate and intrastate rates, and that in all cases a hearing be held at which the States may be heard upon the aforementioned matter prior to the issuance of a final order by the Federal Communications, and

Resolved Further—That the Special Committee on Telephone Regulatory Problems be authorized to confer with the Federal Communications Commission regarding such proposed changes in the procedure of the Federal Communications Commission in such cases and that the Federal Communications Commission be respectfully requested to proceed under Docket 6328 on a fully cooperative basis with representatives of the State Commissions to determine a proper and sound method of separation.

The toll rate disparity problem was becoming more serious and many state regulators cited this problem as evidence that separations procedures needed revision.

Early in February, 1947, the FCC advised the Special Telephone Committee of the NARUC that it was considering substantial reductions in interstate toll rates which was at a time when many Associated Bell Companies had made application to various state commissions for authority to increase exchange and state toll rates.

1947 SEPARATIONS MANUAL

Following the resolution by the 1946 NARUC Convention, a joint NARUC-FCC Staff Committee was appointed. During the year 1947, this Committee in cooperation with representatives of the telephone industry and with an NARUC consultant worked intensively on the preparation of separations methods. This work encompassed not only an appraisal of each of the procedures contained in Exhibit 2 (and its amendments) of Docket No. 6328, but also a thorough examination of separations procedures used in other industries. The Staff Committee made a number of changes in the detailed procedures contained in Exhibit 2 which both experience with the Exhibit 2 methods and results of study groups indicated were desirable for reasons of equity and simplification.

The separation procedures set forth in Exhibit 2, as amended, were rewritten as a manual on a station-to-station basis. This manual was reviewed by representatives of the FCC, NARUC and the telephone industry and on October 22, 1947, it was approved by the NARUC Special Telephone Committee.

The FCC qualified its approval of the Manual as being on an "interim basis" because it felt that the art of telephony is so subject to rapid change, separations procedures require continuous observation, study and revision. The FCC also based its qualified acceptance on the fact that no formal determination on the basis of a hearing record had been made. The FCC has accepted all subsequent revisions to the Separations Manual on an interim basis for these same reasons.

The manual entitled "Separations Manual—Standard Procedures for Separating Telephone Property. Revenues and Expenses—NARUC-FCC Special Cooperative Committee on Telephone Regulatory Problems—October 1947" was subsequently printed and distributed by the NARUC.

The initial effect of the use of the 1947 Separations Manual transferred about $6 million of plant and $12.5 million of expense from intrastate to interstate revenue requirements and apparently eliminated the need for the proposed 1947 reduction in interstate toll rates.

It was reported to the 1950 NARUC Convention that "as a result of recent state rate increases, due to increased state costs, the disparity between state and interstate toll rates has become very substantial and is increasing. Present methods employed to separate toll plant and expenses between state and interstate toll than on state toll operations notwithstanding the fact that state toll rates are now at considerably higher levels than the interstate schedule."

PHOENIX PLAN

During September 1950, at meetings of the NARUC-FCC Separations Subcommittee, the state commissions, operating through the NARUC, introduced a separations proposal (the "Phoenix Plan") relating to the allocation of Bell System toll lines investment between state and interstate toll operations. This proposal

contemplated a change in the practice of assigning Long Lines costs directly to interstate, and would have introduced a cost and use averaging concept in the treatment of Associated Company toll plant. Book cost of Long Lines plant would be computed by multiplying the number of Long Lines circuit miles in the state by the nation-wide average book cost per Long Lines message toll telephone circuit mile. The computed Long Lines plant would then be added to the Bell Company's toll plant and the sum separated to jurisdictions on a ratio of relative airline conversation-minute-miles use (MMM). The MMM factor would be determined in a similar manner. The FCC objected to the Phoenix Plan from its inception in 1950; however, by 1956 they interposed no objection to a modified version of the Phoenix Plan.

A change was made in the toll coefficients effective October 1, 1950, which had an over-all effect on the Bell System division of toll revenue settlements of assigning additional $15.5 millions gross book cost of telephone plant to interstate toll operations, and increasing interstate operating expenses by $13.2 million annually.

PRE-CHARLESTON

On January 19, 1951, the FCC issued an order under Docket No. 9889 directed to all Bell System companies instituting an investigation into the justness and reasonableness of the rates and charges for interstate and foreign communications services, and requiring those companies to show cause why the FCC should not find the existing rates and charges for interstate and foreign communications services are or will be unjust and unreasonable.

On February 8, 1951, the NARUC filed a motion requesting the FCC to enter into a joint study of the current separations procedures in conjunction and in cooperation with representatives of state regulatory commissions, limited in scope to broad issues of material effect and pending the completion of this study, the formal rate proceedings herein be continued.

On February 14, 1951, the FCC postponed the dates when the companies were to file an answer and when the hearing was to begin in order to provide to the NARUC and the FCC time in which to review jointly any proposals which might be made with respect to the revisions of the separations procedures.

CHARLESTON PLAN

During May, 1951, Bell System representatives presented to the NARUC Separations Subcommittee minor revisions to the 1947 Separations Manual which would have transferred $6.2 million of plant and an estimated $3.15 million of annual expense from state to interstate operations for the Bell System. These revised procedures and others were discussed by representatives of the NARUC and the FCC during the year.

On October 17, 1951, FCC Commissioner Paul A. Walker proposed to the NARUC Convention at Charleston, South Carolina, changes which would effect a considerable simplification in the separation of telephone exchange plant. This proposal, known as the "Charleston Plan" was accepted by the Convention, which recommended its use by all state commission and by the FCC. The objectives of the Charleston Plan were: (1) to transfer some of the exchange plant costs assignable to intrastate operations under the 1947 procedures to interstate toll operations and (2) to simplify the separations procedures related to exchange plant.

The Charleston Plan reduced the number of exchange plant categories from sixteen to three. Category A included exchange trunk outside plant, subscriber lines and station equipment. Category B was for local dial COE and Category C was for local manual switchboards.

By order dated November 21, 1951, the FCC continued the proceedings in the matter (Docket No. 9889), subject to such further orders as the FCC may issue in the light of the carriers' actual operating results for a reasonable future period. The FCC cited adjustments in interstate message toll telephone rates (interstate) to be made by the Bell System effective March 1, 1952, in order to compensate the Bell System partially for a reduction in its interstate earnings resulting from the adoption of the Charleston Plan. In the same order, the FCC also vacated its previous order to show cause since it appeared that the net effect of the cost allocation and rate changes on the level of interstate earnings would be such as to remove the immediate basis upon which the FCC had instituted the show cause aspect of the proceedings.

The 1952 NARUC Convention was told that the toll rate disparity had increased from approximately $14,000,000 in 1950 to $160,000,000 in 1951 due in part to a slight increase in the number of state toll messages but principally to increases in state toll rates.

The interstate rate revision effective March 1, 1952, reduced the disparity, estimated from 1951 toll messages, from approximately $160,000,000 to $92,000,000. This reduction was accomplished by increases in the short haul interstate rates amounting to about $22,000,000 gross revenue.

The disparity under rates in effect June 30, 1952, had increased to $104,000,000 based on 1951 messages, or to about 19% above the interstate rate. In several states revenues under the state rates are less than the revenue which would be obtained under the interstate rate. Elimination of these negative disparities would increase the total disparity to nearly $115,000,000.

It was reported to the 1952 NARUC Convention that the Charleston Plan with certain other changes, was estimated, based on June, 1951 operations, to result in a transfer of approximately $90 millions of gross plant investment and $22.5 millions of annual expenses from state to interstate categories. In November 1962, the Charleston Plan was incorporated into the 1947 Separations Manual as the 1952 Addendum.

MODIFIED PHOENIX PLAN

The state toll rate disparity was calculated on May 31, 1953, at about $121.5 million above the prevailing level of interstate rates.

During the latter part of 1953 and during 1954 the NARUC committees continued their work on proposed changes in separations procedures. Three plans were discussed with the FCC and with the telephone industry: the Phoenix Plan endorsed by the NARUC at its Phoenix Convention in 1950; the Message-Mile-Minute Plan and the Circuit Mile Plan. No real prospect existed for acceptance of any one of these plans. It developed, however, that a modification of the so-called Phoenix Plan might be acceptable. This Modified Phoenix Plan would, for cost allocation purposes, combine the book costs of Associated Company interexchange message toll lines plant in each state used to furnish toll service to subscribers therein, with the book costs of similar plant in the same state of the Long Lines Department of A.T. & T. Company. This combined total book cost would be appropriated between state and interstate operations on the basis of the relative message-mile-minutes use of such plant.

Two principal proposed modifications of the original Phoenix Plan were:

(1) That the book costs of any interexchange message toll lines plant of either Long Lines or an Associated Company, which is used to transmit interstate messages, merely transiting the state, would be excluded from the combined property to be apportioned.

(2) That the cost and usage of Long Lines Plant, which would be combined with Associated Company Plant cost and usage for the purpose of the Modified Plan, would be actual rather than estimates based upon Long Lines System averages.

At that time it was reported to the NARUC that certain conditions had to be met if it was to be accepted by the Bell System. They were:

(a) That the State Commissioners present a united front in recommending its use.

(b) That it be accepted by the FCC.

(c) That the modified method would not be placed in effect until interstate rates were adjusted to care for the increase in revenue requirements.

The NARUC convention of 1954 passed a resolution approving on an interim basis and requesting the FCC to adopt as a modification of the existing Separations Manual the so-called Modified Phoenix Plan of 1954.

Although in October 1953 the FCC was considering a major increase in interstate rates, by 1954 there was a sharp increase in interstate toll earnings making this increase unnecessary.

The FCC approved on an interim basis the Modified Phoenix Plan on January 20, 1956. The Bell System accepted and incorporated the Modified Phoenix Plan, at the request of the FCC, in its intercompany settlements effective July 1, 1956.

The revised procedures were issued as the 1956 Addendum to the Separations Manual.

Based upon June 1954 data, the Modified Phoenix Plan assigned $151,700,000 of Book Costs and $19,800,000 of expense to interstate from intrastate.

THE 1957 SEPARATIONS MANUAL

The 1956 NARUC Convention held in San Francisco, California, adopted a resolution to prepare a revision of the Separations Manual embodying all the changes which have been approved since its last revision and making such other changes required to conform the Manual with current operating conditions and regulatory requirements.

The NARUC Special Telephone Committee wrote to each State Commission, the FCC, the U.S. Independent Telephone Association (USITA), and the Bell System inviting each to suggest changes in the Manual.

A final draft of the revised Manual was submitted to the FCC for comment by the NARUC Special Telephone Committee on October 1, 1957. On October 11, 1957, the FCC stated that it had no objection to the revision and approved it on an "Interim basis." The NARUC Convention adopted the revision on October 31, 1957, and the October 1957 edition of the Separations Manual was subsequently printed by the NARUC.

The 1957 Manual incorporated the previously adopted procedures of the Charleston Plan and the Modified Phoenix Plan. The major change introduced with the provision of specific methods for the treatment of private line services. Private line services had not been identified under the procedures of the 1947 Manual because at that time they were considered to be too small a portion of the total. By 1957, however, private line services had grown to the point where they could no longer be ignored. Other changes were made to recognize technological improvements and to simplify existing procedures. These changes did not materially affect state-interstate separations results.

1959 INTERSTATE REDUCTION

On July 24, 1959, the FCC announced a $50 million reduction in interstate message toll telephone rates starting at 469 miles, to be effective the middle of September 1959. The NARUC Special Committee cooperating with the FCC in Studies of Telephone Regulatory Problems nor any other of the state members of the NARUC were made aware that such action was being considered. The president of the NARUC wrote to the chairman of the FCC on August 7, 1959, expressing his disappointment in the FCC's unilateral action. The 1959 NARUC Convention adopted a resolution instructing its committee to proceed with studies of further refinements in separations procedures.

During 1959, 1960, and 1961 the NARUC worked very hard to suggest separations changes which would be acceptable to all parties. Among the plans considered were the so-called Phoenix Plan, the Circuit Mile Plan and the Message-Mile-Minute Plan. The 1961 NARUC Convention adopted a resolution to either assign to toll or to apply to toll usage factor only to digit absorbing facilities where such facilities are not required for the rendition of local service. This proposed change was not acceptable to all parties.

1962 SEPARATIONS CHANGES

Studies of the problems of separations and toll rate disparity continued between representatives of the NARUC, FCC, USITA, and the Bell System. On February 6, 1962, the FCC announced that it had approved, on an interim basis, certain modifications of the separations procedures. These changes were proposed by A.T. & T. in conjunction with the FCC and were related to pole lines, exchange special service circuit equipment, private line telephone station equipment, repairs of cable and wire, repairs of central office equipment, maintaining transmission power and local commercial operations. The changes provided for simplification in the existing procedures which experience indicated would give results consistent with current operating conditions in the telephone industry and which would be less expensive to administer. These revisions were approved by the 1962 NARUC Convention and were issued as the 1962 Addendum to the Separations Manual.

The effect of these changes was to transfer $68.0 million book cost and $36.0 million of expense from state to interstate or approximately $46 million of gross revenue requirement to be effective April 1, 1962. By November, 1962, 37 states and the District of Columbia had ordered state toll rate reductions amounting to $40,863,000.

1963 TOLL RATE DISPARITY

The NARUC-FCC Toll Rate Subcommittee reported to the 1963 NARUC Convention the following schedule of toll rate disparity between state and interstate toll rates:

	Amount (millions)	Percent
Year:		
1951	$125	20.8
1953	110	15.3
1954	137	17.6
1958	212	19.5
1961	293	21.8
1963 (after Apr. 4, 1963)	270	17.1

The problem of toll rate disparity continued to be one of the most important and critical problems facing the various regulatory agencies. Among the factors affecting the rate disparity at the time was the introduction of the "After 9" plan of reduced interstate toll rates which was estimated to reduce gross interstate revenues $55,000,000 a year for distances above 221 miles. Partially offsetting this reduction was an increase in interstate person toll rates estimated at a gross annual amount of $25,000,000 for distances of 0 to 800 miles.

The "After 9 PM" toll rate reductions were placed in effect in interstate toll tariffs effective April 1, 1963.

During 1962, 1963 and in early 1964 a total of 38 states announced the introduction of an "After 9" rate plan in which major reductions were made in the charges for state toll calls of relatively longer distances made between the hours of 9 P.M. and 4:30 A.M.

At the time the revisions in rates were made it was estimated the "After 9" rates, absent any stimulation due to the reduced rates, would reduce charges to the public $55 million annually. The person-to-person rate increases were expected to increase charges $25 million. Thus, the net effect was estimated at an interstate reduction of $30 million. A.T. & T. Company reported that after giving consideration to the actual stimulation in traffic that did occur, a comparison of the charges at the old rates and the "After 9" rates reveals a reduction in charges of $102 million. Person-to-person rate revisions increased charges $23 million. Consequently, an annual net reduction of $79 million in charges was reported.

The report indicates that the reduced rates have caused a stimulation of approximately 16 million messages annually as well as having caused a shift in messages from the before 9 P.M. and a shift from person-to-person calls to station-to-station calls in the after 9 P.M. period. This is in addition to the normal increase in traffic that has been experienced for some time. The stimulation and shift in traffic have resulted in new peak period of usage of facilities occurring on many circuits during the hours the "After 9" rates are in effect, particularly from 9 P.M. to 10 P.M. As a result A.T. & T. Company advised it was adding approximately $100 million in additional interstate facilities to handle the increased traffic over the congested routes. However, as originally contemplated when the "After 9" rates were introduced a high per cent of the additional traffic is being handled over facilities which had previously been idle during the hours these rates apply.

THE 1963 SEPARATIONS MANUAL

The 1962 Addendum changes were incorporated into the April 1963 edition of the Separations Manual. No additional revisions were made at that time.

1964 ADDENDUM

In 1964, the increasing use of electronic computers was recognized by a change in separations procedures which was proposed by the Bell System. This change had a minor effect on the state-interstate assignment of book costs and expenses. All interested parties concurred and a 1964 Addendum to the Separation Manual was issued which covered the following matters:

1. Simplification of the procedures for separating revenue accounting expenses in recognition of the impact of the use of electronic computers for billing purposes.

2. Revenues in Account 504 from "all other local private line services" were assigned to the exchange operation to coincide with a change in the Uniform System of Accounts.

AFTER 8 P.M. PLANS

"After 8 P.M." long distance calling rates with substantially reduced charges effective after 8 P.M. on weekdays and all day on Sunday were made. These plans were coupled with decreases in evening rates as well, since rates for many calls placed between 6 P.M. and 8 P.M. on weekdays and all day Saturday were reduced. Reductions of this type were made effective in 26 states and also for interstate calls on February 1, 1965. By the end of June 1965, a total of 39 states had announced similar rate treatment. Also, a reduction of interstate station-to-station day rates was put into effect on April 1, 1965.

These reductions in toll rates could not be associated with the transfer of revenue requirements from intrastate to interstate jurisdiction arising out of separations changes on this occasion, as they were in 1962.

DENVER PLAN

The NARUC staff committees embarked on an intensive study of state-interstate separations procedures and solicited pertinent data studies and analysis from the industry. In all, 14 points were discussed and analyzed and from these analyses and studies, there evolved proposed revisions in the Separations Manual which were estimated to have the effect of transferring approximately $110 million in annual revenue requirements from state to interstate operations. Concurrently with these changes, the telephone companies revised the work time coefficients for the handling of calls by operators. The effect of this latter change was to reduce the relative work time credit for handling interstate calls and thus would tend to reduce interstate traffic expenses and the interstate assignment of switchboard investments. The shift of revenue requirements from interstate to state due to this change in coefficients approximated $35 million annually. Thus the net of all the changes contemplated at that time was to increase interstate revenue requirements by about $75 million per year and to relieve the burden on intrastate operations by an equal amount.

The proposed separation change discussed above was proposed by A.T. & T. at the meeting of the NARUC staff subcommittee of the Committee on Communications Problems on July 26–28, 1965, in Denver, Colorado. This change became known as the "Denver Plan."

The assumption of equal average length of haul on exchange plant for toll and exchange calls was basic to the Charleston Plan. It was recognized that this assumption might possibly result in some minor overstatements of property costs to interstate services as compared to a more detailed treatment. On the other hand, the assumption that in local dial switching equipment the average costs of switching toll calls and exchange calls per minute of use were the same, resulted in minor understatements of the costs assigned interstate toll as compared to a more detailed treatment.

Since 1951, there had been substantial expansions of local calling areas which had resulted in an increase in the average mileage haul over exchange circuit plant for exchange calls. Also during this period, there was a program of decentralization of toll offices in the major cities. This resulted in some shortening of the mileage in exchange plant for toll calls. These and other developments had proceeded in such a direction that it became increasingly apparent that equality of mileage haul in the exchange plant for local and toll calls could no longer be assumed to exist.

Similarly, the extension of operator dialing of toll calls and the introduction and expansion during this period of customer dialing of toll calls with their attendant technological additions to the local switching plant made the assumption of equal switching costs per minute of use for toll and exchange calls no longer valid.

Furthermore, there had been concern as to whether the existing separations procedures fully recognized the true worth of the use of the subscriber line and

station equipment plant for interstate message services. This concern stemmed from the realization that long distance business could not exist without subscriber line and station equipment plant and that the amount of such plant is a function not of volume of business, as is generally true of other telephone plant, but rather of numbers of customers.

The Denver Plan procedures for the separation of exchange plant shifted additional costs from the state to the interstate jurisdiction. The procedures provide for the following:

1. Cost of exchange trunk plant, i.e., toll connecting, local interoffice and EAS trunks, are assigned directly to state or interstate operations, if feasible. When these trunks are jointly used, their costs are apportioned on the basis of relative minutes of use.
2. Costs of local dial switching equipment are apportioned on the basis of minutes of use with the toll minutes weighted to reflect the greater average cost per toll minute to use as compared to the average cost per exchange minute of use.
3. Cost of subscriber and station equipment plant are assigned to interstate on the basis of a combined subscriber line and station equipment minutes of use-per cent interstate toll user (use-user) factor.

The Denver Plan procedures superseded the Charleston Plan procedures and to some extent constituted a return to the more detailed and precise separations procedures in use prior to 1952. In addition, for the first time the availability of subscriber line and station equipment plant for message toll use was reflected in separations procedures as embodied in the user portion of the combined use-user factor. As such, this represented a departure from the application of actual amount of time in use but the FCC and NARUC concurred that it would "provide a more reasonable and equitable allocation of costs . . ."

The Denver Plan was accepted by the September 1965 NARUC Convention on an interim basis, and by the FCC on October 27, 1965. The revised procedures were incorporated into the Separations Manual by means of the 1965 Addendum. The procedures were introduced into Division of Revenues in the Bell System effective November 1, 1965.

BELL SYSTEM INVESTIGATION

On October 27, 1965, the FCC undertook an investigation of the reasonableness of the Bell System's charges for interstate and foreign communications services under Docket No. 16258.

On December 22, 1965, the FCC issued its memorandum opinion and order dividing the investigation into two phases. Phase I and Phase II, but did not include separations in Phase I. On January 18, 1966, the NARUC filed a petition requesting that the reasonableness and propriety of the separations procedures be heard and determined in advance of any other issue in the proceeding. On April 11, 1967, by memorandum opinion and order the petition was denied, but at the same time, the FCC authorized the Telephone Committee to institute a series of conferences with the parties and the staff for a discussion of the problem and devising means of expediting consideration of the separations issue without unduly delaying the proceeding.

On April 21, 1966, the FCC requested that statements of position with regard to separation be filed by June 20, 1966. The NARUC filed a statement suggesting manual revisions with respect to:

1. Transiting Plant Apportionment
2. Three-Factor Modification
3. Holding Time Modification

Several other parties also filed statements of position requesting other modifications. To expedite resolution of this matter a series of informal conferences were scheduled to be held under the auspices of the FCC for the purpose of exploring ways to arrive at agreements which would narrow the areas of dispute and prospective formal testimony on the record regarding the separations issue.

Committee members testified at the hearings in support of NARUC's position with respect to the separations issue. In brief, this position was: (A) that the plan proposed by the Bell System with respect to procedures for separating Exchange Plant should be adopted and, (B) that the plan proposed by the Bell System with respect to Interexchange Plant including the eliminating of the Modified Phoenix Plan should be rejected. In other words, the NARUC believed that the Modified Phoenix Plan, which was adopted in 1956, should be retained.

On July 5, 1967, the FCC issued an Interim Decision and Order in which it sustained the NARUC insofar as the Modified Phoenix Plan was concerned. However, the Order did not adopt either the NARUC's recommendation or any of the other proposals advanced by the various parties for the jurisdictional separation of Exchange Plant. The NARUC's recommendation with respect to the Exchange Component would have transferred from State to Interstate approximately $251,000,000 of revenue requirements within the Bell System. Instead the FCC separations would shift from State to Interstate only $82,550,000 of revenue requirements.

After considering various petitions for reconsideration, the Commission on September 14, 1967, issued its Memorandum Opinion and Order on Reconsideration in which, insofar as jurisdictional separations are concerned, stayed the effect of its prescribed plan until December 1, 1967, (later to February 1, 1968) and reactivated the so-called Technical Experts Group to consider "improvements or refinements" which might be made in the prescribed plan.

In a letter dated December 13, 1967, to A.T. & T. Company the FCC stated that it was not prepared at this time to act on the merits of the pending petitions and during the period of the extension of the stay which the FCC recently ordered, they would interpose no objection to the implementation of the interim separations methods suggested in the petition of the Bell System respondents which entails the transfer to the interstate revenue requirements from each state, the lowest positive transfer from that state under each of three of the pending proposals.

By Memorandum Opinion and Order adopted January 24, 1968, the FCC adopted the plan set out in its July 5, 1967, Order for Purposes of determining the revenue requirements of the Bell System of its interstate operations. The Commission, however, did not prescribe its plan pursuant to the provisions of Section 221(c) and (d) of the Communications Act of 1934 as amended. Instead, the Commission indicated that it would by way of a separate rule-making proceeding prescribe separations methods pursuant to the above-mentioned Section 221(c) and (d). Notice of Proposed Rule Making was concurrently issued in Docket No. 17975 in the matter of "Prescription of procedures for separating and allocating plant investment, operating expenses, taxes and reserves between the intrastate and interstate operations of telephone companies."

The Memorandum Opinion and Order adopted by the FCC on January 24, 1968, permitted the Bell System to continue administering their internal division of interstate revenues on the basis not objected to by the letter of December 13, 1967, pending conclusion of rule-making in Docket No. 17975. The January 24, 1968, opinion and order provided that "each state agency (is) free to take such action with respect to intrastate revenue requirements in its state on the basis of whichever of these (3) plans of jurisdictional separations it deems appropriate pending conclusion of the forthcoming rule-making proceedings."

Mr. WIGGINS. I respectfully urge that the members of this committee, as Senator McFarland did in 1951, to promptly exercise their influence to see that any future excess earnings will be employed, at least in part, by the FCC to ease the burden on the backs of the local users of service who make approximately 147 billion calls a year, instead of for the benefit of the favored few who make approximately 2½ billion interstate long distance calls a year.

I now defer to Chairman Bloom of Pennsylvania, who will describe H.R. 12150 and what we perceive to be the justification for its prompt enactment.

STATEMENT OF GEORGE I. BLOOM

Mr. BLOOM. Mr. Chairman and members of the committee, I serve as chairman of the Pennsylvania Public Utility Commission, as the first vice president of NARUC, as chairman of its executive committee and chairman of the committee on legislation.

I thank each of you for the opportunity of letting me be heard.

H.R. 12150 proposes the Federal-State Communications Joint Board Act which was introduced by Mr. Rooney of Pennsylvania at the request of the NARUC. Adoption of the act would create a seven-member Board composed of four FCC Commissioners designated by the FCC and three State commissioners nominated by the NARUC and appointed by the FCC. The Board would have sole administrative authority under the Communications Act of 1934 to prescribe uniform procedures for determining what part of the property and expenses of communication common carriers shall be considered as used in interstate or foreign communication toll service, and what part of such property and expenses shall be considered as used in intrastate and exchange service.

Such uniform procedures would only be determined after opportunity for hearing and upon notice to the affected carriers and State commissions and other interested parties. The establishment of the Board will not impair in any way the right of any State commission, or any other interested party, to advocate its position on issues before the Board, to submit evidence and oral argument on them, and to seek reconsideration and judicial review of its decisions. We have no objection to the bill being clarified to specifically authorize the FCC itself to seek judicial review of Joint Board decisions.

The FCC is given latitude in the appointment of the three State commission members in that it may require the NARUC to nominate one, two, or three State commissioners for each State position on the Board, and the FCC may choose from among these nominees in making an appointment. Each of the three State commissioner members would hold office for a term of 3 years and the three terms would be staggered.

The Board would meet from time to time upon the call of the Chairman of the Board or of three members of the Board. A majority of the members of the Board would constitute a quorum. Each member of the Board would have one vote and all decisions of the Board would be by majority vote.

The FCC would designate an examiner to advise with and assist the Board in the handling of any proceedings before it. The FCC would also provide the Board from among the personnel and facilities of the FCC such staff and facilities as are necessary to carry out the functions of the Board. Accordingly, the Board would not require a separate staff and the FCC would not require any additional staff positions since it presently has a staff quite familiar with separations procedures.

Section 2(g) of H.R. 12150 provides that each State commissioner member of the Board would receive a per diem not to exceed $100 for each day engaged in the business of the Board and reimbursement for expenses incurred for travel, food, and lodging. However, if you feel this is not desirable, we would have no objection to the deletion of this provision if the committee desires, and thereby the expenses of the State commissioner members would then be borne by their respective State commissions.

While the enactment of H.R. 12150 as now proposed would require very little expenditure of Federal funds, or no expenditure if section 2(g) was deleted, it would nevertheless provide important and long-overdue protection for the American consumer.

The enactment of H.R. 12150 would provide a balanced approach in the future development of fair and equitable separations procedures which would result in relatively lower rates for the users of local telephone service.

Aside from the necessity for developing fair separations procedures, it is manifestly unfair for the FCC, which has jurisdiction over only 25 percent of Bell's property, to in effect exercise sole authority to determine how 100 percent of such property shall be separated between the Federal and State authorities for ratemaking purposes.

Not only is there a 75–25 percent on plant, but there is a 75–25 percent differential in revenues. The intrastate rates produce 75 percent of the revenues, and the interstate 25 percent of the revenues, and it therefore seems to me that the old saying is quite apropos here that the tail is wagging the dog.

We produce 75 percent of the property, 75 percent of the revenues, and yet the entire control of the separation procedure and the final decision rests with the Federal Communications Commission.

The State commissions should have at least—and I repeat at least—a minority voice in the making of such a determination, and such is the purpose of H.R. 12150.

We believe the long and difficult history of separations procedures clearly reveals the need for this legislation to benefit consumers.

Moreover, we believe time is of the essence in its enactment. The FCC in its letter of November 17, page 3, stated its intention to review Bell System interstate earnings in "the first half of 1970." Accordingly, we respectfully urge the committee to promptly seek the enactment of H.R. 12150 so that the Board may be in existence prior to the FCC again determining excess interstate earnings for the Bell System.

I now defer to President Symons of California to give the conclusion of our testimony.

STATEMENT OF WILLIAM SYMONS

Mr. SYMONS. Thank you, Mr. Bloom.

Mr. Chairman and members of the committee, I am the president of the California Utilities Commission, serving my second term there. I am also a member of the NARUC and its executive committee.

My colleagues have described in as clear and as forceful terms as possible the longstanding refusal of the FCC to allocate a fair amount of the cost of providing local telephone service to the users of the interstate service irrespective of the fact that local facilities are an integral part of the national toll network.

In the area of separations, the FCC has simply failed to discharge its responsibilities to the American people. The FCC has failed to recognize that the legal existence of jurisdictional lines does not alter the fact that the State commissions and the FCC represent the same broad consumer interest, and that their regulatory responsibilities and interests are essentially the same.

Accordingly, we stand today in the midst of another crisis in the field of telephone costing where the FCC has bestowed a $237 million benefit upon a relatively affluent class of users who make approxi-

mately 2½ billion interstate long-distance calls a year and thereby denied this long-overdue economic relief to the millions of users of local telephone service who make approximately 147 billion calls a year—uers who are threatened with rate increases totaling $599 million a year from the Bell System alone.

This $599 million that I just quoted and has been quoted earlier is a fact. In California, the Pacific Telephone Co., which is I believe the leading Bell System Company, has given us prenotice and had discussions with our staff that they will file on or before March 17 of this year a rate application in the amount of almost one-third of this $599 million.

I should also add that their current construction budget in California for this year is in excess of $740 million.

This is by far the worst disservice that the FCC has ever inflicted upon the local consumers in the long odyssey of Federal-State relations in telephone separations.

More specifically, the FCC on December 31, 1969, denied the petitions of the NARUC, New York City, and the independent telephone industry to suspend the $150 million negotiated interstate rate reduction scheduled to take effect the following day. The FCC also denied similar petitions of the NARUC and the independent telephone industry to suspend the $87 million interstate rate reduction scheduled to take effect on February 1, 1970.

As a practical matter, this money will never be recaptured for the benefit of the millions of economically overburdened local users of telephone service across the Nation. Unfortunately, the FCC has callously ignored the great concern for these local users which was expressed by the State commissions and by members of the Senate Committee on Commerce at the hearing on December 9, 1969, on S. 1917, the companion bill to H.R. 12150.

The American consumer cannot afford these losses especially in this era of intense inflation.

And so the State commissions turn again to the Congress as they did in 1951, as the last resort for acquiring and protecting economic benefits for the economically underprivileged. We strongly urge this committee to promptly seek the enactment of H.R. 12150.

We urge this committee to stand up again, as it has so many times in the past, in defense of the American consumer.

Thank you for your attention.

Mr. PEARSON. Thank you, Mr. Symons, and Mr. Chairman, we hope we have presented to you an effective presentation of our immediate problems that are taking place in your home districts.

The FCC tomorrow will tell you they are happy to meet with us. They have been happy to meet with us for the last 20 years. We think we have demonstrated the one-sided support that they are giving the entire communications problem and, while this does not come under this present legislation, I think you have probably read of the Carterfone decision that is further dilluting the income of our local companies.

You have heard of the MCI decision that is going to skim the cream for data transmission off of the long lines so there practically will be no more money left for separations, and just the other day they came

down with a decision that no independents, and the independents are the only ones that have the CATV facilities to help augment their facilities, are no longer allowed to have any CATV within their respective areas.

So we do have a lot of problems, gentlemen. We do have people here, and if you care to, we can answer your questions and we will be happy to do so.

Mr. MACDONALD. I am sure all of the members of the committee would like to ask some questions. Please don't take the questions that I might or any other committee member as indicating our position. It is just that questions do come up in our minds as we go over testimony.

My chief one, and I ask it with all due respect, and especially to our colleague, Mr. Rooney, and to you gentlemen of the association, but is there not sort of a fundamental defect in the bill itself? Judging from the language that I have heard used and read, you seem to be at a pretty strong impasse with the FCC. Some of the language on this was quite strong. You did not call them unscrupulous, but it bordered on that at times. Asking as one whose business is counting votes, what good would it be to have three men of a seven-man board which, if the lines harden—and it has been by experience they usually do—they have four votes and you have three. What have you proven?

Mr. PEARSON. Mr. Chairman, our General Counsel is here in Washington, D.C. You have his address, and this was brought up at the Communications Commission yesterday, he will be willing to discuss with you any amendment you might feel necessary, and the same thing that you bring up has come up in our States, but we felt we should not ask for four commissioners.

Maybe it would be better to have three State commissioners, three Federal Commissioners and representatives from the President's Consumer Research Division, who would sit in as a consumer member in order to break any ties or any decision there might be, but certainly we are open to make any changes you feel will assist us in trying to get a little fairer distribution of the costs of the entire communications system.

Mr. MACDONALD. As I say, I did not ask the question for any obtuse reason. I have not had the benefit of my State's utility commission's feeling about it. It was just off the top of my head, but three and three or maybe two and two neutrals on one side would be fairly quickly noticed in Washington.

My second question is what is A.T. & T.'s position or Bell's position?

Mr. PEARSON. They have informed us they are in favor of the bill and the independents have informed us they are in favor of the bill, and I am sure in later testimony, if you ask them, they will so state.

Mr. MACDONALD. We have been in a short recess and I just got back this morning. I have just a tentative witness list, but I do not see A.T. & T. listed.

Mr. PEARSON. A.T. & T. is under the regulatory authority of the Federal Communications Commission, and I don't think they are going to volunteer anything.

Mr. WIGGINS. I am sure they have some observers here, but they would not care to testify.

Mr. MACDONALD. I would just like to point out that our subcommittee is charged with the duty of going into, as you all know, a highly technical field. While, of course, we are all very interested, our technical knowledge is not perhaps so extensive that we can come down to a decision that would need the wisdom of Solomon. Certainly if the companies involved would like to testify—I suppose the independents would not mind testifying because they are pretty small in the field of long-distance calls, are they not?

Mr. PEARSON. No, they actually enter into quite a few long-distance calls.

Mr. MACDONALD. I would think the proportion would be smaller. Comparing Bell and an independent is like comparing a corner grocery store and a chain market.

Mr. PEARSON. That is true but they have a BI separation program themselves where any telephone messages that started in an independent and goes through Bell, they have a division of money. Any time the calls are cut, these separations are cut accordingly.

Mr. MACDONALD. I am only mentioning this because the message might go through you or to someone in the room who might have second thoughts, and maybe some would be willing to come forth to testify. This is not an adversary proceeding, and I think we would be interested in how they feel.

Mr. BLOOM. Chairman Macdonald, on the makeup of the committee, I think it would be better, of course, if it were equally divided. We felt, and I think counsel felt, in drawing it as he did, we would get less resistance from the Federal Communications Commission if it were drawn on the basis of 4 to 3 membership.

Take the committees of Congress. They have majority and minority members of that committee. Yet, the minority has a chance in the executive sessions to express their views, to properly argue their case in closed session, and you know the effect of it and what good comes out of it, and you know that they frequently divide in these committees in Congress as they do in the legislature where Republican members will vote with the Democratic members and Democratic members will vote with the Republican members, and the same thing could very well be true in a commission that is made up of 4 to 3.

Mr. MACDONALD. I do not want to take up the time of the other members of the committee, but the basic jurisdictional regulation that the FCC has is going across State lines; am I correct?

Mr. PEARSON. Yes, sir.

Mr. MACDONALD. I was going to ask the gentleman from New Hampshire if, say, on a call from Kittery, Maine—and I am very familiar with the area—to Portsmouth, that would be under the FCC but how about a call from Kittery to Lubec on the Canadian border? The FCC would not have anything to say about that.

Mr. RIORDAN. Technically your thought is correct. Actually, it isn't because Kittery happens to be part of a calling area even though it is part in another area. A call from Portsmouth to Kittery is a local call, but if you extended it in a little further, if you called from Kittery to Hampton Beach, that would be subject to FCC.

Mr. MACDONALD. I have a house at Cap Netick and when I get my bill it reads as though I were calling from Portsmouth.

Mr. RIORDAN. It is because the business office is out of Portsmouth for the Netick area. A call from Netick to Portsmouth is a toll call, however, and would be subject to FCC jurisdiction.

Mr. MACDONALD. So, it is not just on the basis of crossing State lines.

Mr. RIORDAN. Principally, it is, but you will have certain exceptions at times because you have some exchange areas that are on the border that will be subject to the jurisdiction.

Mr. MACDONALD. My last question: Does this reduction of rates that the FCC announced affect the carrying of TV programs? Do they just have a special rate which has nothing to do with telephones as such even though most of it comes over telephone lines? Could someone explain the connection to me between TV carrying charges and telephone carrying charges?

Mr. SYMONS. I don't think anyone is——

Mr. WIGGINS. We have no jurisdiction over TV at all. That would be on the long lines of A.T. & T. over which we have no jurisdiction.

Mr. MACDONALD. The Senator just indicated something about the CATV. I didn't get the decision.

Mr. PEARSON. The decision on the CATV is a matter that no telephone company can own any stock in a CATV station that is within its operating territory.

Mr. WIGGINS. They have to divest themselves of any.

Mr. MACDONALD. Can they give them special rates to use the telephone facilities?

Mr. WIGGINS. They have to divest themselves.

Mr. MACDONALD. Can they still sell a CATV carrier at cut rates?

Mr. PEARSON. They can allow them to use their lines and their poles. However, if they use the facilities of the telephone company, certainly we as State commissions would insist that we have some regulatory authority over them, and I am sure we would have.

Mr. BLOOM. When Bell attempted to render that service, they filed rates with our commission, filed a tariff for services to cable television companies. They did not go into effect because there were objections to it and they finally withdrew their tariff. They were going to render that service over their own property and facilities. But where they rent a space on their poles for attachment purposes, it does not come under our jurisdiction in the State of Pennsylvania.

Mr. MACDONALD. How about CATV using underground telephone ducts?

Mr. BLOOM. If they rent their facilities, they would have to file a tariff with us. If it were the facilities of and the service being rendered by the telephone company to the cable TV company so every cable TV company would have the same rate.

Mr. MACDONALD. Thank you very much, gentlemen.

Mr. Van Deerlin.

Mr. VAN DEERLIN. Thank you, Mr. Chairman.

I assume the chairman's question about Kittery, Maine, opens the door for any of us to be parochial. I would hope if you State regulators get a foot in the door here you will immediately take steps to raise the rate on that 1-minute call after midnight, coast-to-coast. When it is midnight in San Diego, it is 3 o'clock in the morning here. Some constituents take seriously the campaign literature about the Congressman serving you 'round-the-clock.

Mr. PEARSON. We will help you and let them carry their data at that time.

Mr. VAN DEERLIN. Who is the best equipped statistician among the witnesses this morning?

Mr. WIGGINS. We have some staff experts who can furnish you most of the information you might like.

Mr. VAN DEERLIN. In the total long-distance toll field, what percentage is commercial business and what percentage is household—in dollar volume?

Mr. HUTCHINSON. I believe it is about 50–50. I am talking about revenue-wise now. In other words, about 50 percent of total toll comes from the residential customers.

Mr. VAN DEERLIN. Has there been any breakdown as to income level? What noncommercial users are making these calls?

Mr. MACDONALD. Teenagers.

Mr. HUTCHINSON. You certainly put your finger on a large portion of it. I do not have a breakdown. I am certain we could get you one, though.

Mr. VAN DEERLIN. I should think there might be some studies on this, showing what people, in what income levels, are utilizing distance toll service. I assume, there would be a direct relationship between income and the proclivity for making long distance toll calls.

Mr. HUTCHINSON. Certainly at the staff level, we would be glad to attempt to supply this information.

Mr. VAN DEERLIN. Perhaps the people who would be most relieved by the type of legislation my colleague has introduced would be the people in the low-income area, because proportionally a major share of their billings would be local calls.

Mr. HUTCHINSON. That would be correct, and in light of rendering an overall telephone service, certainly the best way to get a telephone in the hands of as many people, and that telephone is something that all Americans should enjoy today, and that is to have a cheap local rate. Of course, if he has to make some toll calls, he can pay the price. To us in regulation, and I think I speak for these gentlemen here, one of the main things is to get a telephone in the hands of as many people as we can and to do that there is only one way to do it, and that is to have a cheap local exchange rate, because it is the thing that is paid month by month by month; and the toll call is one of the necessities, probably, if you wish to call it that, which has a priority to it.

Mr. VAN DEERLIN. Thank you, Mr. Chairman.

Mr. MACDONALD. Mr. Brotzman.

Mr. BROTZMAN. Thank you, Mr. Chairman.

I am trying to synthesize between your text and what I have heard now. If I understand your testimony, there are roughly 110 million telephones in this country, of which 75 percent are resident and 25 percent are business telephones. Did I understand the revenue is roughly 50–50?

Mr. HUTCHINSON. We were talking about toll revenues.

Mr. BROTZMAN. Let's take that again. What do you mean exactly by toll revenues?

Mr. HUTCHINSON. It is either a State toll call or an interstate toll call.

Mr. BROTZMAN. Fifty to fifty means what?

Mr. HUTCHINSON. Fifty percent of the total dollar volume is produced by that 75 percent of the total telephones. That, in substance, is what that means.

Mr. PEARSON. And the business toll calls I would presume are almost 100 percent deductible as far as a business expense is concerned, whereas the home phone does not have any reductions or deductions.

Mr. BROTZMAN. I think it has been established from the testimony that under the control of the Federal Communications Commission, by virtue of its jurisdiction over interstate calls, there are about two and a half billion calls made per annum; is that correct?

Mr. PEARSON. That is correct.

Mr. BROTZMAN. Conversely, under the jurisdiction of State public utility officials or otherwise, there are 147 billion telephone calls made.

Mr. PEARSON. That is correct.

Mr. BROTZMAN. I am just synthesizing here, Mr. Chairman.

The FCC under the present formula—and I don't know how this was arrived at—controls 25 percent of the Bell System which, I understand, would be the valuation of property used in calculating the rate; is that correct?

Mr. PEARSON. That is correct.

Mr. BROTZMAN. Those of you in this room plus your colleagues control 75 percent of Bell plus independent telephone companies in the land?

Mr. PEARSON. Except for interstate that certain independents may have, but that is negligible.

Mr. BROTZMAN. What I am really leading up to is the very nexus of the problem as I understand it here. I understand there has recently been a determination by the Federal Communications Commission which you people believe is unfair to the so-called intrastate telephone user; is that right?

Mr. BLOOM. That is right.

Mr. BROTZMAN. Further, there was a $237 million reduction in interstate rates; is that correct?

Mr. PEARSON. That is correct.

Mr. BROTZMAN. What caused this decision? What brought this about? Was there an application by Bell Telephone or by somebody, or was this done by the FCC's own initiative?

Mr. PEARSON. It was a negotiated arrangement made between A.T. & T. and the FCC that the States had nothing whatsoever to do with. It was negotiated and it was not in any type of formal hearing where we had an opportunity to present testimony or where we could create any objection or anything of that nature. It was simply a negotiated arrangement made between FCC and A.T. & T.

Mr. SYMONS. We were not involved.

Mr. WIGGINS. They have a surveillance procedure, and we knew they had to have a reduction and we even wrote a letter to that effect requesting that it be used for our benefit, the States' benefit, and they ignored it.

Mr. BROTZMAN. In response to your last statement, you said you knew there were going to be some reductions.

Mr. WIGGINS. Yes, sir. Our staff is constantly looking into the earnings of the Bell System.

Mr. BROTZMAN. And there would be a reduction in rates on the interstate charges.

Mr. WIGGINS. Yes, sir.

Mr. BROTZMAN. If I understand the rest of the joint testimony, at the time this was going on, there were applications pending or determinations which had already been rendered increasing toll charges for the intrastate——

Mr. WIGGINS. Intrastate exchange rates.

Mr. MACDONALD. What you are really saying is if long-distance rates are cut $237 million, then it is like a seesaw and the local rates cannot get any reduction.

Mr. WIGGINS. That is right.

Mr. MACDONALD. Would it not be fair to split the $237 million, giving half to the local and the other half to long distance? Was that ever proposed? Did anyone ever propose that to the FCC?

Mr. WIGGINS. We have proposed it.

Mr. PEARSON. We have a pending application for some $300 million in separations before the FCC that has never been set up, and we don't know if it will be set up.

Mr. MACDONALD. It seems to me that A.T. & T. could not care less. It is still $237 million, so it is just you versus the FCC. I do not see what the controversy is about—I see what it is about but I do not see the "why."

Mr. WIGGINS. Because we have to regulate telephone service just like in your own respective State and you cannot explain to a housewife when she pays that monthly bill why she has to pay a higher rate for that telephone when she sees in the paper that the FCC has just reduced the rates.

I am in politics and you are in politics, and you just don't explain that to the average person.

Mr. MACDONALD. Not if you don't understand the answer.

I yield back to Mr. Brotzman.

Mr. BROTZMAN. I will recognize the gentleman here from Pennsylvania.

Mr. BLOOM. When he said they realized there would have to be a rate reduction, what I think he had reference to was the fact that they realized that they were making more than a reasonable return on their rate base. Therefore, they either had to have a reduction in rates so that it would be a reasonable return or there had to be a shift in separations from some of the plant that was charged to State over into the interstate base which would justify that rate.

Mr. BROTZMAN. Interstate or intrastate?

Mr. BLOOM. From intrastate to interstate, which would give them a higher rate base and, therefore, could justify the revenues they had. When they did that, it would lower the rate base in the State intrastate and would not require as much revenue from the users of intrastate and local exchange service and, therefore, we would not have to raise rates. There would not be the rate cases coming in on us and eventually would lead to a reduction in rates intrastate. Does that clear it up?

Mr. BROTZMAN. That was the next question I had. What you really are seeking, assuming that H.R. 12150 is passed in some form and

what you would be seeking is what in your opinion would be a more equitable allocation of property really between interstate and intrastate which is really your rate-base structure upon which a reasonable return is reached; is that correct?

Mr. BLOOM. Yes; in general principles, that is correct.

Mr. BROTZMAN. That is all I have, Mr. Chairman.

Mr. PEARSON. Could I add for the chairman's benefit that A.T. & T. could care less. When we are talking about A.T. & T. and the Bell System, we are talking about the same individual. Of the 24 Bell Cos. they are either totally owned or almost wholly owned in all but three of them, so when you talk about A.T. & T., you are talking about the Bell System.

Mr. MACDONALD. I take it that is why they are nicknamed "Ma Bell."

Mr. PEARSON. It could be.

Mr. MACDONALD. Mr. Rooney.

Mr. ROONEY. Mr. Pearson, what has been the experience of NARUC with the FCC regarding the possibility of compromising a rate increase or decrease?

Mr. PEARSON. It actually has had its ups and downs. In my 12 years that I have been with the Commission, there were times that we have met with them and we felt we were having pretty good results and had gone ahead. Then there are other times such as the Denver plan, the FCC and A.T. & T. came up with a plan that was presented to us in Denver on separations and we took it, although we did not agree with it. We took it or they were going to cut interstate rates. So, we are strictly at the mercy of the FCC as far as our total rates problems are concerned.

They have been meeting with us for the last 20 years, way before my time, as a matter of fact, but unfortunately we have no voice in the arrangements whatsoever, and in the last cut that was made of the $237 million, as I stated, this arrangement was made between the FCC and A.T. & T. We had no opportunity to intervene or to come in as protestants, where they might proceed to a court afterwards. We had no say whatsoever. It was done and that was it.

Mr. ROONEY. In your State of Washington, are you saying if they did not cut the rates $200 million it is possible you would not have raised the rate increase in intrastate charges in Washington?

Mr. PEARSON. We would not have had to raise the $14 million. There would be $3 million less we would have had to raise. We had a $34 million disparity between intrastate and interstate. By disparity, the intrastate tolls are charged at a higher rate. There was a $4 million higher rate per mile in the States than they would have been if they had been on the same rates as the interstate rate. With this last rate cut of $237 million, the disparity has gone from $4 million to $9 million, and you try to explain to someone why they call from Seattle to Portland, which is farther, and it is a lot cheaper than when they call from Seattle to Olympia. It is virtually impossible unless you are part of the regulatory process to be able to explain this to the average layman.

Mr. ROONEY. In the last 12 years, in your service, what has been the percentage of decrease in long distance rates versus the percentage in the increase of intrastate charges? Maybe you would want to defer that question.

Mr. PEARSON. I can probably answer as well for the State of Washington as anyone. I have our chief accountant here. As I recall, there was a rate case in 1954 and then we had a toll rate case in 1957 that brought in some $2 million or so, I think, but we have also received separations in that length of time from the interstate cut in tolls. It has gained us something around $5 million per year that we have received.

Does that answer your question?

You see, by improvement in facilities that they have been able to make in their central office and with the various methods they have been using, they have been able to pick up a lot of their inflationary slack, but they cannot do it much anymore.

Mr. ROONEY. I see that Pennsylvania is not listed as one that proposed or received a rate increase, and I congratulate you.

Mr. BLOOM. We are worrying and we hope they don't come in.

Mr. ROONEY. I hope we will air this bill, Mr. Chairman, and my colleagues on the committee have seen the inequity of the consumer at the State level, and I hope that we will give this bill serious consideration in one form or another.

Mr. MACDONALD. As we always do.

Mr. Tiernan.

Mr. TIERNAN. When we use the word consumer, we use that not in the all encompassing use of the telephone services. In your statement I gather what you are talking about is the low-income consumer or that person who is most directly affected by the rates that you as an individual commissioner have to impose in the State.

Mr. SMITH. The low-income consumer is the one affected more but it affects all of the consumers, actually.

Mr. TIERNAN. Whether you increase intrastate or interstate or decrease interstate, you are affecting the consumers?

Mr. SMITH. That is right. Of course, it is extremely difficult in our State to explain why you have to pay 35 cents to call from Providence to Westerly which is less than 50 miles and you can call across the continent for 90 cents.

Mr. TIERNAN. Is it not because in your statement you point out that the technology in long-distance calling and the expense incident thereto is decreasing, whereas the increase in the State for the individual plant unit is increasing?

Mr. SMITH. That is correct, and we feel some of the charge which is allocated to the State for intrastate calls ought to be spread in the interstate calls, and the reason for that is you are paying for a telephone—the user is paying for a telephone—that is sitting on his table for 24 hours a day and this allocation is made on the basis of some 29 minutes a day.

Mr. TIERNAN. Are you familiar with Mr. Johnson's additional statement before the committee on December 9?

Mr. SMITH. Yes, I have read it.

Mr. TIERNAN. I think Mr. Bloom's explanation was very good as to what you want to do by this act. Where the FCC was to find that the rate of return on long-distance calls exceeded the amount that the Commission has established as a fair return on the investment, rather than reducing the amount of revenue, they would then transfer or allocate some of the costs of intrastate service to the interstate service system; is that correct?

Mr. SMITH. That is precisely the matter, and I say they have 23.5 hours of telephone service.

Mr. TIERNAN. But that shifting does not follow the traditional allocation of cost to service as we have known it in utilities regulations in the country.

Mr. SMITH. You have that telephone sitting on the table for 23.5 hours when it is not being used and no part of that——

Mr. TIERNAN. But the service is available.

Mr. SMITH. That is just it. The service is available 24 hours a day but the allocation is made on the basis of half an hour.

Mr. TIERNAN. Mr. Johnson says:

> The logical point of beginning is that prices ought to reflect costs and that the cost of using equipment used for multiple-purpose interstate and intrastate telephone calls can best be ascertained by usage by the subscribers. Such an approach would result in allocating about five percent of the total investment to interstate service. Interstate telephone rates would then be less than a third of what they are. Local rates would have to be raised substantially.

So what we would do by this act really would be take separations and transfer from them from intrastate to interstate service.

Mr. BLOOM. What you would do is give us an opportunity to work out a formula that would arrive at an equitable distribution between the interstate and the intrastate.

Mr. TIERNAN. That word equitable would depend on whether you are interstate or intrastate users.

Mr. BLOOM. That is why they would have to make compromises on parts of the formula which we think is not equitable when the intrastate consumes all of this idle time, and we think there ought to be an equitable formula worked out between the State regulatory bodies and the Federal Communications Commission. If we don't have an opportunity to sit down with them in their closed sessions to discuss these problems, we are out in left field without a pair of sunglasses.

Mr. TIERNAN. Let me say one of the things I certainly want to congratulate you and your association on is the fact that you are making a very strong political argument. You have made it to us because we also know that the constituents see the monthly bills and we don't see so many of the large users of the long-distance lines, and they don't vote as often, but everybody gets a phone bill.

One other thing I want to point out to you, and I think members of your association should be aware of that, the interests of the various States are quite different, so when you select a member or the three members from your group, the interest, for example, of the commissioner from Rhode Island certainly would not be the same as the commissioner from Utah or the commissioner from California would not be the same as some other State which makes or has a great use of long-distance calling.

So, these are inherent problems that you face when you say if you had four and three maybe you could get one Democrat or one Republican to go over with the commission but, on the other hand, you might find a commissioner might have to go over to your side because it would affect greatly the users of long-distance service in the State.

Mr. BLOOM. If that was the proper result and he was satisfied that ought to be done, then that is the way he should go.

Mr. PEARSON. We have representatives from 11 different States now and they have to fully agree on a proposal that goes to the executive committee and thence a proposal to the FCC. So, we do have an opportunity for the States to get together. They may not be exactly right but they are reasonably close.

Mr. MACDONALD. Thank you very much, gentlemen, for a very informative session.

We are adjourned until 10 o'clock tomorrow morning.

(The subcommittee adjourned at 12 noon, to reconvene at 10 a.m., Wednesday, February 25, 1970.)

42-223—70——6

JOINT BOARD FOR TELEPHONE SEPARATIONS

WEDNESDAY, FEBRUARY 25, 1970

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON COMMUNICATIONS AND POWER,
COMMITTEE ON INTERSTATE AND FOREIGN COMMERCE,
Washington, D.C.

The subcommittee met at 10 a.m., pursuant to notice, in room 2322, Rayburn House Office Building, Hon. Torbert H. Macdonald (chairman of the subcommittee) presiding.

Mr. MACDONALD. The hearing will come to order, please. This morning we resume our hearings on H.R. 12150 introduced by our colleague, Fred Rooney of Pennsylvania. Our first witness this morning is the distinguished Chairman of the Federal Communications Commission, Mr. Dean Burch. Again, welcome, Mr. Burch.

STATEMENT OF HON. DEAN BURCH, CHAIRMAN, FEDERAL COMMUNICATIONS COMMISSION; ACCOMPANIED BY COMMISSIONER KENNETH A. COX; H. LEROY BAKER, CHIEF, FIELD ORGANIZATION DIVISION; AND BERNARD STRASSBURG, CHIEF, COMMON CARRIER BUREAU

Mr. BURCH. Thank you, Mr. Chairman. I am accompanied this morning by Mr. Kenneth Cox, Bernard Strassburg, and Roy Baker, who is the Chief of the Field Operations Division and who is primarily concerned with the subject matter at hand, and with your indulgence, I may ask them for information.

Mr. Chairman, I welcome this opportunity to give you the Commission's views on H.R. 12150—a bill to establish a joint Federal-State board to administer the separation of telephone company costs for jurisdictional purposes. In this connection I will also discuss our recent actions concerning interstate rate reductions which, I believe, provide relevant background for a consideration of H.R. 12150.

I would like to ask the permission of the committee to insert in the record at this point a copy of our public notice by which the reduction in service was given to the public as well as a letter to Chairman Harley O. Staggers as to what we did and did not do.

Mr. MACDONALD. It was referred to yesterday and without objection it will be entered at this point.

(The documents referred to follow:)

Rates for Interstate Long Distance Calls To Be Reduced

[Public notice—Federal Communications Commission—November 5, 1969]

Reductions in rates for interstate long distance telephone calls will be submitted shortly by the Bell System telephone companies to the Federal Communications Commission. It is expected that the reduced rates will save users of telephone service about $150 million per year. In addition, AT&T has previously agreed to file reductions of about $87 million representing an offset to increases in revenues resulting from higher rates recently filed for program transmission. Telpak and teletypewriter exchange (TWX) services when the latter increases become effective. The Commission anticipates that the new rates will permit the companies to achieve earnings in a range needed to attract capital under today's conditions.

The proposed reductions are being submitted by AT&T in connection with the comprehensive review recently completed by the FCC of the Bell System's interstate operations and earnings requirements. The review was conducted as part of the Commission's continuing surveillance of the Bell System's interstate operations, and was participated in by representatives of the Commission's staff, Bell System officials, and several outside consultants who are expert in economics and finance.

The proposed rate reductions take account of the material increases in AT&T's cost of capital. At the same time, they recognize that the growth in interstate traffic is continuing unabated; that the average revenue per message has shown steady increase since the reductions required by our 1967 decision took place; and that the interstate earnings of the Company have consistently grown despite the increases in its costs due to the inflationary spiral. In 1969, interstate earnings are expected to exceed 8%. We fully expect that the growth trends in traffic, revenues, and earnings will continue. This expectation is substantiated by AT&T's own forecast of interstate operating results for 1970, which ranges under present rates, to levels above 8.5%, depending on economic conditions. Consistent with experience following prior rate reductions, we also anticipate that the interstate revenues and earnings will be stimulated to some extent by the reductions in rates the Company is now proposing. Thus, it is anticipated that the rate adjustments announced today will not, in themselves, prevent the Company from achieving earnings in the aforementioned range. The Commission will maintain a continuing surveillance and take such action as is appropriate in the light of future conditions.

The Commission initiated the current review in light of the sustained growth in the interstate earnings of the Bell System to levels well in excess of the level determined by the Commission to be adequate and reasonable in its 1967 decisions. In conducting the current review, the Commission examined the Company's present and anticipated capital needs and the levels of, and trends in, its revenues, expenses and earnings. The Commission focused on AT&T's cost, under current economic conditions, of attracting the large amounts of new capital, estimated at more than $200 million a month, required by AT&T for its ever-increasing construction program to meet new and expanding needs of the public for communication services.

The examination was made by the Commission within the framework of the principles and standards it formulated in its decisions issued in July and September 1967, following a comprehensive formal investigation and hearing into the Bell System's interstate rates (Docket 16258). In those decisions, the Commission concluded, among other things, that a return in the range of 7.0% to 7.5% was fair and reasonable at that time for purposes of effecting adjustments in AT&T's interstate rates. It also stated that it did not regard this range as establishing an absolute floor or ceiling for future earnings. Instead, it said it would, when there were departures from this range, consider the matter in light of conditions obtaining at that time.

In keeping with those principles, the Commission is of the view, in the light of current conditions, and with due regard to the proposed reductions, that interstate rates producing an earnings level which exceeds the upper limit of the 1967 range (7.5%), are not unreasonable. The Commission based this view on the changes which have taken place since 1967 in the economic, financial, and other conditions that affect AT&T's revenue requirements and its ability to attract new capital. The Commission noted particularly the sharp increase in

the interest rates on borrowed capital, the resulting increase in the Company's cost of embedded debt, the much higher rate of inflation today, and the need to raise substantial amounts of new capital under current market conditions. These factors constitute substantial changes from the conditions which prevailed at the time of the 1967 decisions and must be reflected in a current assessment of the Company's cost of capital and revenue requirements.

There are also a number of uncertainties in the current situation and in the national economic outlook. These include the persistent inflationary trend, with its effects on the cost of capital; the effectiveness of the Government's efforts and policies to curb this trend and stabilize prices; the possible effects of such efforts on the continued growth of the economy; and the duration of any period of adjustment. Another uncertainty results from the present status of the Federal corporate income tax and surcharge, as well as the potential changes resulting from the "reform provisions" of the pending tax legislation.

In view of these uncertainties, the Commission wishes to make clear that the views expressed herein relate to the current situation and cannot be binding under any future changed economic conditions.

The Commission notes that technical changes in separations methods which it recently accepted at the request of the NARUC result in a $35 million transfer of revenue requirements, to the benefit of users of local services subject to state regulatory jurisdiction.

The details of the rate changes are being worked out by the Company. The new rates will be submitted to the FCC in revised tariffs which will become effective on statutory notice.

Action by the Commission November 5, 1969. Commissioners Burch (Chairman), Bartley, Robert E. Lee, Cox and H. Rex Lee, with Commissioner Johnson dissenting and issuing a statement (attached).

Continuous Surveillance

(Separate Statement of Commissioner Nicholas Johnson)

I. INTRODUCTION

The Commission today offers for public view the results of its recent informal negotiations with the Bell System on the appropriate level of interstate rates. The effectiveness of the Commission in this area and the suitability of continuous surveillance as a regulatory technique can now be evaluated. My analysis indicates that the technique is rather ineffective and the Commission's adherence to announced principles is sharply limited when it comes into conflict with ATT. The Commission here issues a press release designed to show that significant decreases have "voluntarily" been agreed to by Bell. The implication is that some wonderful victory has been achieved for the consumer through the activities of the Commission and the benevolence of ATT. Unanswered is the question of whether *enough* has been achieved or whether the Commission's representation is a true reflection of the facts.

II. CONTINUOUS SURVEILLANCE AS A REGULATORY TECHNIQUE

"Continuous surveillance" is a regular informal review of particular regulatory issues—in this case ATT's interstate rate of return. Informal closed door negotiations were held with Bell to examine going levels of earnings with a view to possible appropriate action by the Commission or Bell. The theory is that in the context of these negotiations the Commission will be able to make an informed judgment as to what action would serve the interests of the public as consumers *and* that Bell would agree to take that action even though it is harmful to the interests of its stockholders. Initially there seems no reason that a regulated company would agree to actions inimicable to the interests of its stockholders. However, a company may in fact be willing to meet certain levels of public responsibility which are not too harmful in terms of stockholder reaction.

The Commission has certain penalties it can impose if a company is unresponsive. A company does not wish to receive the unfavorable publicity generated by public Commission criticism of a failure to respond to the interests of the consumer. (Thus, not only has the Commission negotiated with Bell on the rate reduction; the content of the FCC majority's *press release* was negotiated

with Bell officials who are clearly concerned as much with publicity as with profits.) The Commission could issue a show cause order to require a recalcitrant company to prove why its rates should not be lowered. Finally, there is the threat of a full-scale investigation with its attendant uncertainty and unfavorable publicity. The Commission is not without weapons to compel action by the regulated company—even though the continuous surveillance proceeding is not a formal hearing from which orders may be issued.

There are severe limits to the Commission's ability to function in this type of a proceeding. Virtually all of the information was selected, packaged and presented by Bell—there was no direct case from our staff or outside representatives. There was no leavening from outside consumer representatives—even though the New York City Consumers Affairs Department requested (and was denied) the opportunity to appear. The negotiating process depends on the skill and dedication of the negotiators—and a company with a single position faces a multi-member Commission with a variety of positions. There are no limits on the lobbying efforts by the company—to staff or Commissioners—since *ex parte* rules do not apply. Whatever decisions are made—whether adjustments are needed, how much, what the company agrees to and how much the Commission compromises—are not normally explained publicly in the way formal decision are. Public statements are made long after the decision in fact have been made. Appeal from decisions is difficult—there is no opportunity to seek reconsideration of a formal Commission decision or appeal it to the courts. There are no parties to appeal. Apparently all that can be done is to petition for rejection of whatever revised tariffs Bell decides to file as a result of the negotiations.

III. CONSUMER ADVOCATES

In response to some of the inherent problems with the continuous surveillance proceeding the Commission in this instance decided to denominate two staff members to ask questions of the ATT witnesses from the consumer's point of view. Operating in a capacity separated from that of the Commission's Common Carrier Bureau staff, these staff members conducted their own cross-examination of Bell's witnesses and offered some additional materials relating to their examination. The quality and completeness of the information before the Commission was improved by their performance. Bell's discomfiture was obvious. On balance, the continuous surveillance process was clearly improved by this limited use of denominated consumer representatives.

The innovation did, however, heighten the tension as to the role of the Commission's staff in rate proceedings. The Commission has traditionally viewed its staff in ratemaking proceedings as combined protector-of-the-consumer and neutral adviser-to-the-Commission. I have elsewhere argued that the combined functions necessarily affects the quality of the consumer advocacy and this was confirmed by the experiment in this proceeding. A.T. & T., 9 F. C. C. 2d 30, 122 at 141 (1967). I believe the Commission ought to use staff consumer advocates in all important ratemaking matters The Commission ought to do all it can to have forceful advocacy for alternatives presented to it—a necessary ingredient for competent choice in any decision-making process.

IV. RESULTS REACHED AND ACHIEVED

Bell argued it should be allowed to earn 8.5 to 9.0% on its total allowed rate base—and thus that the Commission should modify *de facto* its 1967 decision that the appropriate Bell rate of return was 7.0 to 7.5%. This 2% range from 7.0 to 9.0%, for interstate operations alone, could cost consumers as much as $500 million more per year depending on the level fixed by the Commission. (A change of 0.1% in Bell's rate of return has a $24 million effect on the amount of gross revenues the consumer must pay.) The majority concluded that Bell's current going rate of return is 8.25%, that 7.4% was appropriate for purposes of negotiation and a $200 million rate decrease (after adjusting for stimulation effects) was warranted. (8.25 minus 7.4 equals .85; .85 times $24 million equals $204 million). To this sum was added the $90 million in MTT rates Bell had agreed to file as a result of price increases made in non-MTT (Telpak, TWX, Program Transmission) services. The majority was seeking $290 million through negotiations conducted by the staff and the Telephone Committee.

Bell now says they have agreed to reduce rates by $240 million. The majority's compromise in negotiations will cost the consumer $50 million per year. The majority first sought $200 million in reduction plus the $85–90 million MTT reductions as offsets to the other rate increases Bell has filed. Bell as a counter offered $120 million plus the offsets. Bell also wanted a statement from the Commission that a return of 8% was justified. The majority commendably refused, although offering to say that a rate above 7.5% *is justified*, and that earnings "in the range" of 8.0 to 8.5% will result from its decision. It is, in any event, indisputably clear that the Commission today sanctions a rate of return in excess of 7½%—the maximum permitted under its own prior order! Now Bell has offered to reduce MTT rates by $240 million and the majority has accepted. The majority's compromise appears to cost the consumer $50 million per year. In fact the majority's additional compromise from what it *should have sought* from Bell may cost the consumer $250 million per year!

The majority's decision to seek only $290 million in reductions in the face of Bell's present level of earnings severely harms the consumer and is a strong critique of the continuous surveillance process. Let us assume for the moment that the majority's 7.4% floor for Bell's rate of return is correct. Would $300 million in reductions have reached this level? We can be almost certain that it would not. One need only examine the history of continuous surveillance as well as the results of the 1967 rate proceeding. Bell's interstate rate of return has never fallen below 7.5% since 1961. (1961—7.72%; 1962—7.55%; 1963—7.51%; 1964—7.99%; 1965—7.95%; 1966—8.29%; 1967—8.25%; 1968—7.60%). Although rate reductions were occasionally achieved during this period, it is not at all clear that they were enough. Bell appears to have been successful in earning extra profits through the ineffectiveness of the continuous surveillance process. These profits may have led to a significant over-evaluation of Bell's stock during this period and the subsequent readjustment.

The rate of return for 1968 is particularly significant. After a formal rate proceeding the Commission ordered Bell to file tariffs to reach an allowed rate of return of 7.0 to 7.5%. The effect of $20 million in a $120 million rate reduction order was deferred for a substantial period in 1968 out of the professed fear that earnings might fall below the 7.0% level. [A.T. & T., 12 F.C.C. 2d 167, 168 (1968)] The Commission's fears for Bell's financial health were misplaced. Not only did Bell not go below the lower end of the range, it exceeded the *higher* limit, earning 7.6%. As if this were not enough, only the Vietnam War and its attendant surtax saved the Commission from further embarrassment. Without the surtax Bell would have earned in the range of 8.2%—a full 0.7 to 1.2% above the range supposedly established by the Commission's 1967 decision. The record suggests that Commission decisions systematically err in Bell's favor on rate of return matters.

An examination of today's decision suggests some of the reasons for the FCC's errors. No estimate is made for growth in Bell's 1970 earnings, although Bell has enjoyed steady growth. No estimate is made for possible lower unit costs, although Bell proudly reports its cost-reducing achievements. No account is taken of the effects of relaxation of the income tax surcharge. If the surcharge rate is reduced to 5% on January 1, 1970, then $70 million less gross revenues will be needed to reach 7.4%. By June 30, 1970, when the remaining 5% is scheduled to be lifted, another $70 million less in gross revenues will be needed by Bell. Since the surveillance process generally takes at least a year from the time excess earnings occur, to Commission recognition, to Commission action, to tariff filing, the majority's failure to take account of the probable effects of the surcharge changes may cost the consumer $100 million in 1970. (The majority could have directed Bell to have tariff reductions in hand ready for filing when the surtax changes come. For this discussion it is recognized that Bell has effectively passed the entire surtax on to its consumers.)

The majority's willingness to settle for $240 million in reductions can also be attacked for its *de facto* modification without hearing of the Commission's 1967 order. The Commission rejected the participation of outside parties representing consumer interests but did allow attendance by representatives from NARUC (the association of state regulatory commissioners). The majority has made a decision in fact, but there is no announcement of it, no rationale offered for it, and no consideration of the rights of parties who may feel aggrieved. A leading case is often cited for the proposition that no legal redress is available for decisions reached under continuous surveillance. [*The Public Utilities Com-*

mission of the State of California v. *United States*, 356 F. 2d 236 (9th Cir. 1966)]. However, the fact that the Commission recently made an on-the-record determination, and now changes it without hearing, may present a different legal situation.

Bell argued that circumstances had changed from the 1967 environment, and that these changes warranted a change in their allowed rate of return. Its evidence focused on one basic point—the change in the interest rate for long-term debt capital. The majority agreed with Bell to the tune of $100 million per year. (The difference between a range of 7.0 to 7.5% and 7.4 to 7.9% is between $24 million and $196 million.) In 1967 the Commission reached two basic conclusions—the overall rate of return should be 7.0 to 7.5% and Bell has been severely negligent in not using more debt financing in the past, a policy that has been and continues to be costly to both consumer *and* shareholder.

The issues concerning proper capital financing of a public utility need not be as confusing as they appear. A company can raise capital by equity or by debt. Equity includes retained earnings and money gained from stock sales. Debt is capital borrowed from money-lenders at a fixed rate of interest. Other things being equal debt financing is generally less costly to the consumer while being beneficial to the stockholder. Debt costs less since the interest rate is normally lower than the required return for equity. Interest costs are a cost of doing business and as such are deducted before the payment of corporate income taxes. And for any given level of overall return the use of debt financing can often increase the pool of earnings available to equity holders.

Since the 1967 decision Bell has gone to all-debt financing and even at the present high interest rates, debt financing continues to exert a favorable leveraging effect on Bell's earnings. In fact as the staff consumer representatives pointed out in a chart submitted during cross-examination, Bell has been able to offset the effects of high interest through increased leverage.

1969 (Test Year) Allowed Rate of Return 7–7½%

31.5% Debt at 4% Interest:	
Low	1.26
High	1.26
68.5% Equity at 8.4–9.1% Return:	
Low	5.74
High	6.24
Total Allowed Rate of Return:	
Low	7.00
High	7.50

1969 Calculation Incorporating

1. Higher interest rates being paid;
2. Changed capital structure;
3. The same return on equity range as allowed in the 1967 decision.

40% Debt at 5% Interest:	
Low	2.00
High	2.00
60% Equity at 8.4–9.1% Return:	
Low	5.04
High	5.46
Total Allowed Rate of Return:	
Low	7.04
High	7.46

NOTE.—The increased interest cost for debt is counteracted by the increase in debt ratio so that if the return on equity remains the same, the allowed rate of return would remain the same.

The majority's calculation is perhaps simpler. In 1967 the Commission said the Bell System could be earning at least 9% on equity if it had achieved a debt ratio of 40% at 4% embedded interest cost, although Bell had debt ratio of about 35% at the time. (A debt ratio is the ratio of the amount of debt to the total capital of a company—a company with $100,000 total capital of which $35,000 is debt has a 35% debt ratio. "Embedded interest cost" is the average interest rate being paid on debt capital of the company.)

If Bell had a 40% debt ratio and was paying on the average of 4% in interest, a 7% overall return on capital would result in a 9% return to equity.

	Percent
40% debt times 4% interest	1.6
60% equity times 9% return	5.4
Total return	7.0

At 7.5% return Bell would be earning 9.38% on equity.

	Percent
40% debt times 4% interest	1.6
60% equity times 9.83% return	5.9
Total return	7.5

Today Bell has a 40% debt ratio but borrowing at higher interest rates has made its average interest cost for all debt capital 5%. In order to achieve a 9% return on equity, the overall rate of return must be set at 7.4%, the majority's figure.

	Percent
40% debt times 5% interest	2.0
60% equity times 9% return	5.4
Total return	7.4

The crucial question is whether the 1967 decision "guaranteed" Bell a 9% return on equity. There is a strong suggestion it did not. As noted, a 7.0 to 7.5% rate of return suggested a return on equity based on 1966 test year data of 8.4% to 9.1%. The leveraging effect of all-debt financing has retained that range of equity return even if there is no change in the allowed range of 7.0 to 7.5% on total capital. And there was no demonstration by ATT that the fundamental factors affecting the required return on equity have caused the cost of equity capital to ATT to increase.

The majority could easily have taken account both of the surtax and reduced the going rate of return to 7.0%. It could have made some estimate of the impact on rate of return in 1970 from growth and lower cost technology. It did not. Cost to the consumer: at least $200 million a year.

V. CONCLUSION

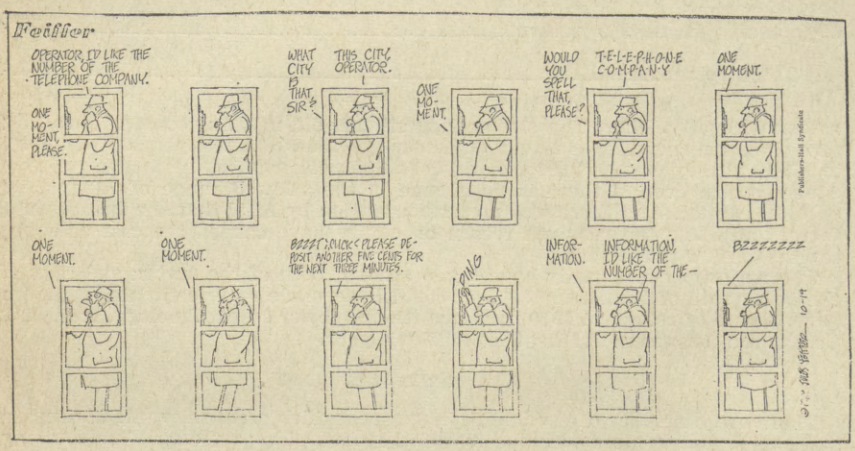
There are a number of concluding comments which seem relevant. Consumers and Bell's shareholders continue to suffer from Bell's past errors in financing. Bell abhorred debt financing in periods of low interest rates and thus finds it necessary (and cheaper) to use debt exclusively at a time of very high interest rates. But it is even more disquieting that Bell now speaks of returning to equity via convertible bonds despite the fact that debt financing continues to be less costly to the consumer and more beneficial to the stockholder than equity financing. Moreover Bell's debt ratio, although increasing, is still not within shouting distance of that employed by most other major telephone electric and gas utilities. Today consumers still must pay Bell a higher rate of return on total capital than they pay electric utilities while stockholders still get a lower return on equity from Bell than they obtain from the electrics. Moreover, these relationships are likely to prevail for some time in the future as Bell attempts to extricate itself from its past inefficient financing policies. It is of some concern that the Commission majority says nothing on this issue—as it remained silent when Bell followed costly equity financing in the past—even after it has concluded that Bell is not more risky than the electrics. If Bell elects to improve its capital structure at its leisure, must the consumer pay for today's inefficient financing as well as yesterday's?

Bell continues to refuse to use liberalized depreciation with either normalization or flow-through. The majority refuses to take action despite the fact that liberalized depreciation could in the past and would now provide substantial benefits to both consumers and stockholders. [See the discussion in Trebing (ed), Rate of Return Under Regulation, pp. 129–175 (1969)]. Bell and FCC errors on the use of liberalized depreciation are very likely of the same order of magnitude as the errors in capital financing—with the attendant adverse impact on the consumer and stockholder. The Commission implicitly allows Bell to pass the full amount of the Vietnam surtax on to consumers for the purpose of rate level

calculations. A strong case can be made that Bell should bear at least *some* of the costs of this special war-inflation tax and the Commission said in a letter to the then Consumer Affairs Assistant, Betty Furness in 1968 that it would at least consider that possibility.

Bell and the FCC use electric utilities for comparison purposes. Several comments are relevant. Implicit is the assumption that the regulation of the electrics has achieved a proper rate of return and thus the performance of the electrics is a proper benchmark. Some might disagree. Senator Lee Metcalf in his book, *Overcharge*, urges that in fact electric utilities—the FCC's comparative standard—are earning too much. [Metcalf and Reimer, *Overcharge* (1967)]. But even so the electrics, because of a higher debt ratio, require less in overall rate of return (6.7% in 1968 for the electrics to Bell's 7.6%) while returning more to equity holders (11.9% in 1968 for the electrics to Bell's 9.3%). The electrics also make substantial use of liberalized depreciation.

Bell's contempt for the consumer is clear, not only for refusing to lower exorbitant rates but also for its shocking acquiescence in the decline in the quality of telephone service its slipshod performance has permitted, as Jules Feiffer has so concisely portrayed:



It is difficult to evaluate the process of continuous surveillance as a regulatory tool. It offers some real procedural benefits. But it requires somewhat more than the Commission was able to bring to it this time.

FEDERAL COMMUNICATIONS COMMISSION,
Washington, D.C., November 17, 1969.

HON. HARLEY O. STAGGERS,
Chairman, Interstate and Foreign Commerce Committee,
House of Representatives, Washington, D.C.

DEAR MR. CHAIRMAN: The Honorable Francis Pearson, President of the National Association of Regulatory Utility Commissioners, has favored us with copies of his letter to you of November 8, 1969, objecting to the reductions proposed to be made in interstate long distance rates following the discussions we recently concluded with the Bell System concerning its level of earnings from services subject to this Commission's regulatory jurisdiction. Because of the importance of the issue raised by Mr. Pearson, we believe that you should be advised promptly of our views on the matters.

As you know, the contemplated reductions total $237 million per annum, of which $150 million is designed to reduce the Bell System's interstate earnings from its current level, which the Commission believes to be excessive. The balance of $87 million is intended to offset increases in revenues resulting from higher charges filed by the Bell System with respect to its various interstate services other than message toll.

In brief, it is Mr. Pearson's position that to effectuate reductions in interstate rates, while, in a number of states, requests are either pending or expected for increases in rates for local exchange services, is detrimental to the users of exchange service and, particularly, the economically disadvantaged, whose interest would best be served by maintaining exchange rates at the lowest possible level. He attributes this situation to alleged, but unspecified, inequities in the procedures which are applied to the separation, for rate making purposes, of the plant investment and expenses of the telephone companies between their state and interstate operations. He urges that the excess earnings from interstate services should be disposed of by revising the separation procedures so as to increase the amount of costs allocated to interstate operations and thereby reduce the amount of costs that must be recovered from rates for local telephone service.

We fully concur in Mr. Pearson's stated objective that every reasonable measure should be taken to minimize the economic burden on the users of local service. We also share his view that "it is essential to the public interest that procedures for separating . . . plant and expenses be fair and equitable so that no unreasonable burden will be placed on either the interstate or the intrastate users of telephone service."

However, the implementation of these objectives involves several important considerations. Most telephone plant in the United States is used in common for the rendition of intrastate and interstate services which are subject to different regulatory jurisdictions. Thus, fair and equitable separations procedures are essential to the proper exercise by each jurisdiction of its rate making authority. Although each has its own legal responsibilities and obligations, it has been a common objective to maintain uniformity in the separations procedures used for rate making purposes by the different jurisdictions. To this end, the establishment and maintenance of appropriate separations procedures has been the subject of continuous cooperative effort among Federal and state regulatory agencies and the telephone industry.

Separations is, of course, far from being an exact science and reasonable men will have honest differences as to the most appropriate formula for accomplishing a fair and objective cost allocation. That such differences are inherent in the nature of the subject are borne out by the record of disagreement within the regulatory community and the telephone industry regarding the merits of most proposals that, in the past, have been considered for revising the separations procedures. At the same time, there is, in our opinion, little, if any, disagreement that there are certain minimum constraints of law and reason which must govern in any formulation of jurisdictional separations if it is to pass judicial review. This means, of course, that it is not possible to make arbitrary transfers of costs from one jurisdiction to the other as a device to alleviate the need for rate adjustments. Instead there must be a substantial and rational basis for the proposed transfer.

Our activities in the field of separations have been conducted with a view to reflecting changed conditions in this dynamic industry and have in fact resulted in major reassignments of costs which have relieved the states of very substantial amounts of costs and revenue requirements applicable to local exchange service. This is borne out by the actual results which have been achieved by Federal-State cooperation in this area over the years for the benefit of the intrastate services. Since 1952 five major revisions have been adopted in the separations procedures. Each of them has resulted in net overall transfers of revenue requirements from the intrastate to the interstate operations. It is estimated that, on the basis of current operations, these revisions have relieved the intrastate operations of the Bell System of an estimated $800 million of revenue requirements annually. This sum, in turn, has been absorbed by the users of interstate services.

In order that you may appreciate the magnitude of the individual revisions, we call your attention to the fact that the most recent revision effective January 1, 1969, transferred about $95 million in annual revenue requirements from intrastate to interstate operations. The cumulative, direct effects of these revisions upon local exchange users can be illustrated by noting the following: as of 1952 less than 3% of subscriber line plant (which currently represents more than 40% of the Bell System's total investment) was assigned to interstate operations. This assignment was made by measuring the proportion of interstate use of this plant to its total use for all services. Today, through the adoption of acceptable new concepts and refinements in existing concepts of separations, more than 16% of these costs are assigned to interstate operations even though such operations account for only about 5% of the actual use of their subscriber

plant. Furthermore, as a result of the most recent revision, the proportion of subscriber line plant costs assigned to interstate will continue to increase.

The foregoing, then, is the general framework of principles and objectives which have guided our continuing cooperative efforts. In fact, as recently as October of this year, we acceded to further requests of the NARUC for certain modifications on the details of implementing the procedures which have resulted in an additional assignment of some $35 million of annual revenue requirements from the intrastate to the interstate services.

A new series of separations studies is now being undertaken by the staff experts of our Commission and the state commissions with respect to possible further revisions in the procedures. We cannot now predict the outcome of these studies, but we will certainly take the status or results of those studies into account when we will again be reviewing the level of interstate earnings within our program of continuing surveillance. In view of the growth that is anticipated in interstate revenues and earnings, it is expected that such a review will take place sometime in the first half of 1970, after the effects on earnings of any revised Federal income tax surcharge are known.

Mr. Pearson has proposed to your Committee that it schedule hearings at an early date (1) to consider H.R. 12150 which would establish a Federal-State Communication Joint Board to administer telephone separations procedures; and (2) to review the propriety of the Commission's recent action with respect to interstate rates. If your Committee should determine that such hearings will serve a useful purpose, you may be assured of a full exposition of our views on these matters and a more detailed explanation of our policies and actions than has been possible in this letter.

Before concluding, a brief comment should be made with reference to the suggestion in Mr. Pearson's letter that reductions in interstate rates favor only a limited class of affluent users. It has been the Commission's policy objective over the years to channel the benefits of technological cost savings to the less affluent and the residential subscriber. One example is the relatively low rates for long distance calls made during evening and nighttime hours and throughout the weekend. This has made the service economically attractive and available to the householder and members of his family who, in this age of travel and family dispersion, have become dependent upon the telephone as a principal means of communication with each other. It will continue to be our policy to emphasize the needs and interests of these classes of users in future rate adjustments.

A similar letter is being sent to Senator Magnuson since Mr. Pearson had also written to him concerning this matter. In addition, we are also sending a copy of this letter to Mr. Pearson so that he may be aware of our response.

Commissioner Johnson was absent.

DEAN BURCH, *Chairman.*

Mr. BROTZMAN. What is the date of that?

Mr. BURCH. The public notice is dated November 5, 1969.

The letter to Congressman Staggers dated November 17, 1969, and there is a Commission letter to Senator Magnuson dated December 10, 1969, and a letter of the same date which express the separate views of Nick Johnson concerning this matter.

Mr. BROTZMAN. Thank you.

(The letters referred to follow:)

FEDERAL COMMUNICATIONS COMMISSION,
Washington, D.C., December 10, 1969.

Hon. WARREN G. MAGNUSON,
Chairman, Committee on Commerce,
U.S. Senate,
Washington, D.C.

DEAR MR. CHAIRMAN: At the hearings of your Committee held on December 9, 1969, with respect to S. 1917, the statement was made by one or more witnesses testifying on behalf of the state commissions that this Commission, by its public notice of November 5, 1969, has indicated that it regards a rate of return of 8.5% for interstate telephone operations of the Bell System as acceptable. It was also suggested that the Bell System companies are using this alleged determination by the FCC to support their requests for higher local and intrastate rates in various states.

We believe, in fairness to all concerned, that the record in this regard should be clarified immediately since our public notice of November 5 did not purport to set forth a specific allowable rate of return. Any such specification was deemed by the Commission to be inappropriate to a negotiated rate adjustment in the context of the informal procedures of continuing surveillance.

Our public notice did, however, express our view that in light of current conditions of the capital market, interstate rates which would produce a rate of return which exceeds 7.5%—the upper limit of the range of return found to be reasonable in 1967 by our decision in Docket No. 16258—are not unreasonable. We also recognized in the public notice that there was reason to expect that, absent any further action by the Commission, the reduced rates announced by the public notice, will not, *in themselves*, prevent the company from achieving earnings in a range of 8.0% to 8.5%.

In making the latter observation, the Commission was not indicating an acceptance or approval of earnings in this range. We were simply expressing our anticipation that the growth patterns inherent in interstate business, combined with the stimulating effects of the contemplated rate reductions on interstate traffic, would continue to increase the going-level of interstate earnings. For these reasons we stressed our intention to maintain a continuing surveillance of the matter and to take appropriate action in the light of future conditions. In this connection, as the Commission advised you in its letter of November 17, 1969, and as we testified, we will again be reviewing the level of earnings in the first half of 1970 after, among other things, the effects of any revision in the Federal income tax surcharge are known.

Accordingly, any claim that the Commission specified, as acceptable, a level of earnings in the aforementioned range is a misconstruction of our November 5 public notice and misrepresents our current policies.

Because of the obvious concern of this matter to the state commissions, we are taking the liberty of sending them a copy of this letter together with a copy of our statement before the Committee.

This letter was adopted by the Commission on December 10, 1969.

Commissioner Johnson dissented and will issue a separate letter.

DEAN BURCH, *Chairman.*

FEDERAL COMMUNICATIONS COMMISSION,
Washington, D.C., December 1969.

Hon. WARREN G. MAGNUSON,
Chairman, Committee on Commerce,
U.S. Senate, Washington, D.C.

DEAR MR. CHAIRMAN: This letter is submitted as a separate statement with the Commission's letter to you of this date regarding the ATT rate of return. As indicated in the Commission letter, I dissented to its adoption.

I simply cannot agree that the Commission's action of November 5, 1969, did not constitute "acceptance or approval" of a rate of return for the Bell System in the range of 8.0 to 8.5%. The majority press release, which was drafted in consultation with Bell, states: "[I]t is anticipated that the rate adjustments announced today will not, in themselves, prevent the Company from achieving earnings in the aforementioned range." That "aforementioned range" was 8.5%. Bell's own press release stated that the rate reduction "will not by itself reduce our interstate rate of return below 8% and we concur in the Commission's view that this reduction should not preclude our achieving interstate earnings next year approaching 8.5%."

Now that the Commission has come down firmly on all sides of this issue, and "approved" virtually all rates of return from 7.0 to 8.5%, the obfuscation is admittedly thick. But I fail to see how any fair reading of these documents can lead to any other conclusion than that the Commission and Bell believe the recent rate reduction will not reduce Bell's interstate rate of return below 8.0 to 8.5%.

That conclusion will, no doubt, be pressed by Bell on state regulatory commissions that will be urged to do no less than the federal regulatory authority. In fact, I expect that other utilities will press the same argument before other regulatory agencies and that the havoc the Commission has wrought will be felt throughout our entire economy.

The Commission accepted a rate of reduction offer from Bell which Bell says will not reduce its rate of return below 8.5%. If the Commission did not "ap-

prove or accept" an 8.0 to 8.5% rate of return, it could have moved against Bell rather than accepting its offer. The majority's letter confuses and obfuscates this basic point and that is the reason for my dissent and separate statement to you.

Respectfully,

NICHOLAS JOHNSON, *Commissioner.*

Mr. BURCH. I will include treatment of the suggestion that, as an alternative to such reductions, we should have required the interstate jurisdiction to absorb a greater share of telephone company costs as a device for reducing the costs now being assigned to intrastate operations.

For reasons I will explain in my statement, we are opposed to the bill because we do not believe that it will further the objective shared by both the Federal and State regulatory jurisdictions for formulating constructive and workable separations procedures. On the contrary, it is our view that the procedures contemplated by the bill would, if imposed by enactment, represent a step backward in the type of Federal-State cooperation which has in the past brought about constructive changes in the procedures with resulting benefits for all segments of the telephone using public.

As I have recently advised the Senate Committee on Commerce and NARUC President Pearson, cooperative studies are currently in active progress looking toward possible revisions in the procedures for separating the costs of telephone service among the several jurisdictions.

I would like to offer a letter dated January 14, 1970, from Francis Pearson to Senator Magnuson and Senator Pastore, a copy of even date to me, really a cover letter to me of the same letter and my response to Mr. Pearson of January 22, 1970, and a cover letter from me to Senator Pastore explaining the letter which I think will furnish a little perspective to where we are.

Mr. MACDONALD. Without objection, it is so ordered.

(The documents referred to follow:)

FEDERAL COMMUNICATIONS COMMISSION,
Washington, D.C., January 22, 1970.

Hon. JOHN O. PASTORE,
U.S. Senate, New Senate Office Building,
Washington, D.C.

DEAR SENATOR PASTORE: There is enclosed a copy of my reply to Honorable Francis Pearson, President of the NARUC, who sent me a copy of his letter to you of January 14, concerning S. 1917 and jurisdictional telephone separations.

As you will note, our cooperative efforts with the NARUC are well underway and I am confident they will be productive if given a reasonable opportunity to succeed.

Sincerely,

DEAN BURCH, *Chairman.*

FEDERAL COMMUNICATIONS COMMISSION,
Washington, D.C., January 22, 1970.

Hon. FRANCIS PEARSON,
President, NARUC, Washington Utilities and Transportation Commission,
Olympia, Wash.

DEAR MR. PRESIDENT: Thank you for your recent letter sending me a copy of your letter to Senators Magnuson and Pastore urging action on S. 1917.

I appreciate fully the feelings expressed in your letter regarding the jurisdictional separations procedures. As I advised you and Ben Wiggins last month, we are prepared to bend every effort, in cooperation with the NARUC, to work out constructive changes in the procedures. This effort has begun in earnest.

The technical experts of your organization and our agency have already held a fruitful meeting on the subject. They are actively considering the merits of the separations revision proposed by the NARUC in its petition as well as other proposals which have now been advanced. Representatives of the telephone industry have been requested to develop data which are necessary to an evaluation of the proposals and which are expected to be available before the end of February.

I am certain that, given a reasonable opportunity to succeed, our joint efforts can be productive of results beneficial to all concerned.

May I add one brief note for information regarding the reference in your letter to the reduction of $87 million in interstate message toll rates to be effective February 1. That reduction is simply an offset to the increase in interstate revenues resulting from increases in Telpak, program transmission and other interstate rates filed by AT&T. Unlike the January 1 reduction of $150 million, the February 1 rate changes are designed to maintain, rather than reduce, the level of interstate earnings.

I look forward to my meeting with you and the other members of the NARUC Executive Committee in February.

Sincerely,

DEAN BURCH, *Chairman.*

NATIONAL ASSOCIATION OF REGULATORY UTILITY COMMISSIONERS,
Washington, D.C.

Hon. DEAN BURCH,
Chairman, Federal Communications Commission,
Washington, D.C.

DEAR CHAIRMAN BURCH: Enclosed is a copy of a letter that I have sent to both Senator Magnuson and Senator Pastore relative to S. 1917. As President of the National Association of Regulatory Utility Commissioners I feel it my obligation and duty to do everything in my power to protect the several states of our organization against what we feel have been unfair and unsound practices in separations by the FCC.

I hope you will not consider this anything personal. The battle has been going on for many, many years and unless legislation such as S. 1917 is passed, I am afraid it will continue for many more, with cooling periods when there is fairly close agreement, followed by periods of complete disagreement such as presently exists.

I hope that we will have time at the NARUC Executive Committee meeting in February, without the pressures of Congressional hearings, to exchange our ideas and become a little better acquainted with each other's thinking.

Sincerely,

FRANCIS PEARSON, *President.*

NATIONAL ASSOCIATION OF REGULATORY UTILITY COMMISSIONERS,
Washington, D.C., January 14, 1970.

Re S–1917.

Hon. WARREN G. MAGNUSON,
Chairman, Committee on Commerce, U.S. Senate,
Washington, D.C.
Hon. JOHN O. PASTORE,
Chairman, Subcommittee on Communications of the Committee on Commerce,
U.S. Senate, Washington, D.C.

DEAR CHAIRMAN MAGNUSON: As president of the National Association of Regulatory Utility Commissioners, I want to repeat my expression of deep appreciation for the courtesies extended to us during the hearing December 9, 1969 on the above bill before the Committee on Commerce.

At that time we urged upon you the necessity for prompt enactment of the bill in order to avoid the perpetuation of the highly inequitable treatment of various classes of telephone users. Forceful demonstration of this inequity was highlighted by the action of the Federal Communications Commission in approaching the problem of the high earnings of the Bell system through the simplistic procedure of reduction of interstate rates rather than through revisions in separation procedures through which all users would share on a just basis. It is not my intention now to repeat the presentation then made by the NARUC and representatives of state commissions. I do want, however,

to impress upon you recent developments which further demonstrate the urgent necessity for the prompt enactment of S–1917.

As you are no doubt aware, we have been totally unsuccessful in our efforts to convince the Federal Communications Commission that the $237 million reductions in interstate rates should be delayed pending consideration of appropriate separation changes that would provide a balanced equitable approach under the dual system of interstate and intrastate regulation. Already $150 million of interstate rate reductions have just gone into effect and the remaining $87 million of interstate rate reductions are due to go into effect February 1. We have no assurance from the FCC that it will delay even this latter portion of the reduction pending consideration of separation changes in the basic consumer interest.

As we pointed out in our presentation December 9, 1969 before your honorable committee, the NARUC has filed with the FCC a petition seeking specific changes in separation procedures. We have just been advised that the American Telephone & Telegraph Company has filed with the Commission a response to that petition which can only be construed as one of outright opposition. AT&T points out therein that the NARUC proposal would transfer substantial revenue requirements from intrastate to interstate. Parenthetically it should be noted that such a transfer was specifically what the NARUC was proposing to achieve by changes in separation methods as an alternative to the rate reductions negotiated by FCC for interstate users only, thus depriving intrastate telephone users of any of he benefits. In its instant response, AT&T takes the position that "Interstate earnings now, or expected in the foreseeable future, are not sufficient to support any substantial transfer or revenue requirements. If any separations change were adopted which had that effect, an increase in interstate rates would be necessary."

Without in any way commenting on the validity of the assertions of AT&T it should be patently obvious that under present procedures, the Federal Communications Commission is placed in a most awkward position. Certainly it would be reluctant to take a unilateral action that some contend would result in an increase in interstate rates. Yet without the enactment of S–1917 that commission would have to be cognizant of such a contention in attempting to arrive at a prescription of otherwise equitable separation procedures affecting both interstate and intrastate operations.

At the invitation of the Honorable Dean Burch, chairman of the FCC, the NARUC–FCC staff committee of technical experts is presently meeting to consider proposed separation changes and to arrive at possible recommendations relating to the same. The coordinated efforts of these experts from both the Federal and state jurisdictions provide a firm foundation upon which to extend cooperative Federal-state action to the decisional level by statutory provision for the agency contemplated by S–1917. The state jurisdictions incur substantial expenses in making its experts available in this endeavor and yet the sole decisional authority, for all practical purposes, presently rests with the FCC.

In our judgment the foregoing points up quite forcefully the absolute necessity for provision for a body composed of both the Federal and state regulators who can view the establishment of separation methods on a bilateral basis, that is, where the decisional agency is comprised of both Federal and state regulators. This is simply what S–1917 is meant to accomplish and will accomplish. While the states would still be a minority voice, at least some semblance of a balanced consumer interest approach would be injected.

Let there be no mistake that the very serious problems created by the recent negotiated settlement between AT&T and the FCC was not a one-time proposition. We have every confidence in asserting that similar situations will present themselves in the immediate future and on a continuing basis. Manifestly S–1917 requires prompt consideration and enactment. We exhort the Committee to expedite consideration of this bill immediately upon the reconvening of the Congress January 19, 1970 by reporting out the bill with a do pass.

It is respectively requested that you advise me as to problems, if any, that might militate against this requested action so that our people can supply any further information that may be deemed necessary.

Sincerely yours,

FRANCIS PEARSON, *President.*

Mr. BURCH. The technical experts of the NARUC and the FCC are actively considering the merits of a separations revision which has been proposed by the NARUC in a recently filed petition, as well as other proposals dealing with this subject which have been advanced. Progress is being made and I am certain that, given a reasonable chance these Federal-State cooperative efforts will produce results beneficial to all concerned. It is this type of cooperative procedure which has in the past produced results which we feel are noteworthy.

Over the years since 1947, when the original Separations Manual came into being through such cooperative efforts, there have been a number of substantial revisions in these procedures. The cumulative result of these various revisions has been to relieve the intrastate ratepayers of about $800 million in revenue requirements. Most of these revisions have come about through similar cooperative efforts of the NARUC and FCC. The proposed legislation with the quasi-adjudicatory procedure which it proposes would, in our opinion, hamper rather than help in the continuing efforts to improve separation methods.

At the outset, it is important to understand the purpose and significance of separations or cost allocations in telephone rate regulation by the Federal and State authorities. As you well know, a major objective of all utility rate regulation is to determine the cost of rendering service. This is especially complex where the same companies are subject to regulation by more than one jurisdiction. In exercising this dual jurisdiction there are certain legal and practical constraints that must be respected by regulatory authority—State and Federal.

Because most telephone plant is used in common to render both intrastate and interstate services which are subject, respectively, to State and Federal regulatory jurisdiction, the costs of such plant, as well as associated expenses, must be equitably apportioned between the two jurisdictions. Without such equitable apportionment, the rates for service under one jurisdiction may well result in a burden to the ratepayers of other jurisdictions. Thus, effective exercise by each jurisdiction of its ratemaking authority is dependent upon the use of separation or allocation procedures which properly reflect the costs related to the service subject to that jurisdiction.

As early as 1930 the U.S. Supreme Court, in the landmark decision of *Smith* v. *Illinois Bell Telephone Co.*, 232 U.S. 133, had occasion to rule on the necessity for an appropriate separation of commonly used telephone plant and associated expenses. The Court made it clear that a proper allocation of costs is the keystone to the sovereign exercise by the Federal Government and the States of their respective regulatory jurisdictions over interstate and intrastate rates and that each must give appropriate recognition to the different uses to which the commonly used plant is put.

In light of the *Smith* decision and other relevant Court precedents, it is clear and generally undisputed that neither the Commission nor the State regulatory authorities are free agents in fixing the method of allocating joint plant between intrastate and interstate services.

It is equally clear that the Federal Communications Commission is by no means free to arbitrarily allocate sums of money between jurisdictions solely to achieve a given purpose such as alleviating or minimizing intrastate rate increases.

I would now like to describe the background of our activity in the regulation of the Bell System's interstate rates. Our most recent activity in this respect led to our November 5 rate reduction announcement, a copy of which has been placed in the record. (See p. 80.)

You may recall that in 1965 a formal investigation was instituted into the lawfulness of the charges of the American Telephone & Telegraph Co., and the Associated Bell System Cos. for interstate and foreign communications services and other related matters. This was the first general rate investigation of this scope and type in the history of the Commission—FCC docket No. 16258.

The critical aspect of this proceeding as it pertains to the present situation involved a determination of the appropriate revenue requirements of the Bell System Cos. applicable to their interstate and foreign communications services and the basis upon which such revenue requirements are to be ascertained. This necessarily included a determination of the allowable rate base and rate of return for the Bell System's interstate operations. With respect to the specific matter of separations, the proceeding also required a determination of the appropriateness of the procedures used to allocate costs to Bell's interstate operations.

On July 5, 1967, the Commission adopted an interim decision and order which found that a range of 7 to 7½ percent was appropriate in the light of conditions existing in the test year 1966 and provided for revisions in the separations procedures.

As a result of our decision in 1967 there was a $120 million annual reduction in interstate long-distance rates. There was also a shift of revenue requirements from intrastate to interstate of approximately $85 million, as the result of the revisions in separations procedures.

It should be noted that absent the shift in revenue requirements to the interstate operations as the result of separations changes, the reductions in interstate rates would have been nearly twice what they actually were, or some $205 million. Because of various petitions for reconsideration, further changes in separations procedures were made last year through rulemaking proceedings which increased the net benefit to the States to about $135 million. This rulemaking adopted for the first time the FCC NARUC Separations Manual as a part of the Commission's rules.

Despite the rate reductions and the separations changes resulting from our decision, Bell's rate of return, which was 8.25 percent for 1967, declined only to 7.6 percent in 1968, the first full year of the reductions and separations changes; and by the first 6 months of 1969 the return had again climbed to 8.25 percent. Accordingly, in keeping with its policy of continuing surveillance, the Commission held a series of meetings with Bell System representatives between September 8, 1969, and September 19, 1969, to review this growth in interstate earnings. Representatives of the National Association of Regulatory Utility Commissioners (NARUC) and the independent telephone companies attended the meetings as observers.

In all candor, Mr. Chairman, they were observers. They did not cross-examine during these meetings.

Upon consideration of the facts adduced at the meetings, it was apparent to the Commission that although changes in the Nation's economy indicated a somewhat higher cost of capital for the Bell System than in 1966 and 1967, Bell's volume of interstate business had grown, and was growing, at a rate such as to place it in excess earnings position. This meant that the using public was paying rates at an unreasonably high level and, absent remedial action, would continue to do so.

The Commission had two alternatives. One, it could have instituted a formal investigation and, after having amassed a record, ordered such rate reductions as appeared justified. This procedure would have required the public to continue to pay the existing higher rates for approximately another 2 years while the proceedings were being conducted. Or it could enter into discussions with the Bell System and arrive at a mutually acceptable reduction in rates, thereby affording telephone users prompt benefits in the form of lower rates. For what I think are sound and readily understandable reasons, the Commission chose the latter.

With this background, I would now like to revert to the principal problem which has occasioned our appearance this morning; namely, the subject of jurisdictional separations of investment and expenses incurred in the rendition of telephone service. It has been urged that the Commission had a third alternative, that is to revise separations procedures so as to transfer portions of the Bell System's investment and expenses from its intrastate services to its interstate services, resulting in an increase in interstate revenue requirements and a lower rate of return on Bell's interstate operations. Correspondingly, it would have relieved intrastate operations on a nationwide basis of an equivalent amount of revenue requirements. However, at that time, there was before us no proposal for a revision in separations which we believed presented a sound and legally supportable basis for such action.

I would now like to review briefly the achievements of Federal-State cooperation over the years in this area. I shall also explain why reductions in interstate rates at a time when requests for rate increases are pending in various States are not necessarily, as some of the States contend, the result of deficiencies in the separations procedures.

Our cooperative activities with the State commissions have resulted in major reassignments of costs from the intrastate to the interstate jurisdiction. This has relieved the States of very substantial amounts of costs and revenue requirements applicable to local exchange service. Since 1952, five major revisions have been adopted in the separations procedures. It is estimated that, on the basis of current operations, these revisions have relieved the intrastate operations of the Bell System, and therefore the local subscriber, of an estimated $800 million of revenue requirements annually. Local rates are thus lower by $800 million a year. This sum has been absorbed by the users of interstate services who are now paying some 20 percent more for interstate services than they would have been required to pay if pre-1952 separations procedures were still in effect.

I would also like to point out that as of 1952, when separations were based on measurements of actual use, less than 3 percent of subscriber plant was assigned to interstate operations. Today, through the development of new concepts of separations, more than 16 percent of subscriber plant costs are assigned to interstate operations, even though such operations account for only about 5 percent of the actual use of the subscriber plant. Further, it should be noted that this plant amounts to over $20 billion investment or about 40 percent of the total investment of the Bell System.

It should also be noted that the intrastate operations and particularly the local exchange operations tend to benefit from interstate message toll rate reductions. Interstate rate reductions in the past have resulted in substantial stimulation of interstate toll calls. The increased interstate usage thus generated has increased the proportion of total usage accounted for by interstate calls. This in turn has increased the assignment of costs to interstate operations. This is particularly true in the case of subscriber plant where increased interstate usage does not necessitate an increase in plant investment.

As recently as October of last year, we agreed with the NARUC to certain modifications in the details of implementing the separations procedures which have resulted in an additional assignment of some $35 million of annual revenue requirements from the intrastate to the interstate services. As I noted at the outset of my statement, we are engaged in a new series of cooperative separations studies with the State commissions with respect to possible further revisions in the procedures including the plan proposed by the NARUC in its December 9 petition to the Commission. We of course will take the status or results of those studies into account in our reviews of the level of interstate earnings within our program of continuing surveillance.

I turn now to the argument of some States that the mere fact that the FCC is in a position to effectuate substantial interstate reductions at a time when even greater intrastate rate increases are sought by the same company demonstrates ipso facto that there must be fundamental deficiencies in the separations procedures. We cannot agree with this view. The critical fact is that there are inherent differences in the cost characteristics associated with the provision of the two types of service. These differences in cost characteristics are not created by the separations procedures but simply reflect differences in technological and economic factors.

In general, there have been increased economies of scale associated with circuit costs for long-distance interstate toll calls. Technological breakthroughs have dramatically reduced the necessary investment from about $200 per circuit mile some 30 years ago to about $10 per circuit mile in the most modern facilities now being installed. There have not been comparable breakthroughs in the case of local or exchange services. Thus, a major element of toll costs has been drastically decreased while no similar reductions have been realized in the cost of exchange plant.

The Commission is, of course, fully cognizant of the disparities which exist between interstate and intrastate toll rates in some States. Here again some urge that these disparities are caused by inequities in separations procedures. The fact is that these disparities result mainly from the economies of scale which occur for the most part

in longer hauls. Moreover, the relatively fixed cost of exchange facilities represents a higher proportion of the total cost of shorter distance toll calls than that involved in longer distances. Thus, the cost per mile for handling a call decreases as the distance increases. Since the average distance of intrastate toll calls is much shorter than the average distance of interstate calls, the cost factors related to distance are much more favorable for interstate calls.

It should, therefore, be clear that unit costs for furnishing interstate toll telephone service can decrease at the same time that the costs of furnishing local or intrastate services are increasing. In any system where plant is subject to different jurisdictions, separations procedures must reflect these differences.

To sum up, the purpose of separations is to ascertain as objectively and fairly as possible, but the use of sound and rational allocation procedures, the legitimate costs applicable to services subject to separate jurisdictions. It is not the purpose of cost separations to artificially or arbitrarily equalize costs of services which are inherently disparate and unequal. It is only by adhering to sound and rational cost allocation procedures that our system of regulation, which is predicated upon appropriate recognition of Federal and State authority, will have meaning.

This necessary background on separations procedures brings me to the bill before the committee today. The Commission opposes the bill essentially because it would not allow us to determine what investment and expenses are properly attributable to the public services which we are charged with the responsibility of regulating.

H.R. 12150, which is designated the "Federal-State Communications Joint Board Act of 1969" would establish a joint board composed of four FCC Commissioners and three State commissioners designated by the NARUC. This joint board would have sole administrative authority to adopt, and to amend, from time to time, procedures for determining what part of the property and expenses of communications common carriers shall be considered as used in interstate and/or foreign communications service subject to the jurisdiction of the FCC. The actions of the joint board would be final so far as the FCC's regulatory authority is concerned. The full Commission would have no authority to review or modify the action of the board. It would not be even allowed to seek judicial review of the Board's actions, even though the bill provides for such review at the behest of the States.

Fundamental to the regulation of public utilities by any regulatory authority is determination of the investment, or rate base, upon which the utility shall be allowed to earn its fair rate of return. Equally fundamental is a determination of the operating expenses the utility may recover from the ratepayer. These determinations in turn are responsible for the level of the rates paid by the public. Yet under the provisions of H.R. 12150, action by three State commissioners in conjunction with one FCC Commissioner would exclude six FCC Commissioners from any voice in the determination of questions so fundamental in carrying out the responsibilities imposed on them by Congress.

A major point advanced by NARUC, which supports this legislation, is that it is inequitable for the FCC whose regulatory authority

extends to only 25 percent of the telephone plant, to unilaterally prescribe how the total plant shall be allocated for jurisdictional purposes. Actually, current separations procedures allocate about 30 percent of the total plant to interstate. It should be noted, of course, that no other single jurisdiction is responsible for so much as 30 percent of the plant investment. More important, however, is the fact that almost every part of the total plant is used in some degree in furnishing interstate service.

NARUC seems to base its support for this legislation in part on the claim that the FCC, in adopting its order prescribing separations methods, has abandoned the long-established Federal-State cooperative approach to jurisdictional separations. We do not agree. The Commission stated in its rulemaking order of January 30, 1969, prescribing separations methods, that:

> In this connection we intend to continue our cooperation with the NARUC, as in the past, in the conduct of joint studies and reviews of jurisdictional separations matters. In fact the Commission will look to these joint studies as the prime forum for continued analysis of separation procedures and the source of proposals for their refinement, improvement or modification in light of actual experience and technological changes.

As I have already noted, since that date the Commission has approved a further transfer to interstate of $35 million in revenue requirements as a result of cooperative efforts between the States and itself. Moreover, at this time, cooperative studies are in progress involving representatives of the States and the FCC to explore the possibility of further refinements and improvements in separations methods.

We believe the record clearly shows that we have not abandoned the cooperative approach. On the contrary, the purpose of our formal prescription of uniform separations methods was to provide for an orderly and legally recognized procedure for considering proposed changes in such methods. Our codification of these methods as part of our rules provides an established procedure by which amendments can be proposed and a forum in which all interested parties can be heard. It provides a means by which the justification for changes can be be examined in the light of a public record. It also affords an opportunity for judicial review of Commission action.

On the other hand, H.R. 12150 calls for formal evidentiary hearings—a lengthier, more cumbersome process than the more flexible and speedier rulemaking procedures under section 4 of the Administrative Procedure Act.

An analysis of the provisions of H.R. 12150, in contrast with the provisions of present statutes relating to joint boards, serves to emphasize the problems we have with the proposal. The presently existing joint board procedures have long been utilized by the Interstate Commerce Commission and are also provided for in the Communications Act. Under the latter statute, the joint board has the jurisdiction and powers conferred by law upon an examiner provided for in section 11 of the Administrative Procedure Act.

Its decision is an intermediate one fully reviewable by the FCC. Thus, the FCC retained full jurisdiction and authority to determine matters fundamental to the discharge of its regulatory responsibilities. This would not be so under H.R. 12150.

We also object to the delegation to a quasi-official body—NARUC—the authority to appoint officials to whom the bill would grant so much power over the regulation of interstate commerce which clearly appears to be inappropriate and is certainly without precedent.

It should be noted that the presently effective joint board provisions are designed to give certain States directly interested in a question peculiarly affecting them a voice in the determination of that question as it affects their individual States. However, because of the interstate nature of such questions, the ultimate responsibility for their determination is left to the Federal agency. On the other hand, the matters with which H.R. 12150 is concerned affect not just a few States, but all of the States. Further, the States are affected by separations changes in different ways and their interests are often disparate. It would be difficult for the three State commissioners envisioned by H.R. 12150, with their own local concerns, to represent the divergent interests of some 50 jurisdictions.

It is for these reasons that we believe that the informal but effective cooperation which we have maintained with the States, with the full opportunity for all interested parties to participate in our rulemaking proceedings, is a far more appropriate and effective procedure for handling this complex subject of jurisdictional separations.

Accordingly it is our opinion that H.R. 12150 should not be enacted.

Thank you, Mr. Chairman.

Mr. MACDONALD. Thank you very much, Chairman Burch, for a fine statement. Actually I think this bill gives some evidence of the value of our hearings. Yesterday I thought the panel from NARUC put on a very good performance in educating us to the problems and I thought it made a very strong case. I was fairly well convinced that they had a very valid case indeed. Today you make an equally strong case for the Commission.

One of the things that struck me yesterday, which I mentioned to them, was that there is a saving to long distance line users of apparently some $237 million.

Mr. BURCH. Actually it is $150 million. The other $87 million concerned is an offset to an increase. They increased the TWX rates, program transmission rates by the amount of $87 million and then reduced so that there was just a wash as far as that was concerned.

The net was $150 million.

Mr. MACDONALD. Even if the money is less, and I am sure you are correct, the idea seems to still prevail; would you have the authority to divide the reduction between the long lines and the local consumers?

Mr. BURCH. I think it would be within our jurisdiction to allocate it provided there is some reasonable and rational reason for doing it.

We can't just say we have $150 million and we will divide it. We have to have some rationale for doing so.

Mr. MACDONALD. I thought the rationale was the profits had gotten so high.

Mr. BURCH. Interstate, but not intrastate.

Mr. MACDONALD. It is hard in my mind to separate them into two. They are one company dealing with inter- and intrastate. I suppose there their profit sheet does not differentiate, does it?

Mr. BURCH. Yes; and their books are kept differently.

Mr. MACDONALD. Do they pay stockholders differently?

Mr. BURCH. No, sir; but they maintain revenue requirements and profits and loss statements on their interstate operations as opposed to the intrastate operations.

For example, they have 50 utilities commissioners regulating their intrastate rates. Each State can regulate that. Only the FCC determines what their revenue requirements and allowable profits are for interstate operations.

I will agree with one point that NARUC makes. This is at best a rather ephemeral subject. If you look at that telephone over there, there is no way you can say we are going to take the receiver portion of it and call it interstate and take the base and say it is intrastate.

There must be some logical reason for saying 75 percent is intrastate and 25 percent is interstate, there must be some basis in fact, either the amount of use is a consideration, actually, if you consider it on that basis, we have allocated more to interstate than the percentage of use would indicate.

I have heard the argument advanced any time you pick up a telephone you have a 50–50 chance of making now an intrastate or interstate call which is true.

Mr. MACDONALD. And you have a 50–50 chance of not getting anything.

Mr. BURCH. The fact is we all know not 50 percent of the calls are interstate. I don't deny for a moment that the FCC and the NARUC should constantly be attempting to improve separations procedures.

I would like to make one pragmatic observation. Assume for the moment that we had put the entire $150 million into the States. It would probably disappear without a ripple.

If anything, it might affect your telephone bill by a nickel. So as a pragmatic observation, aside from legality or anything else, is it better to the ultimate consumer to be able to save 35 cents on a single telephone call which he might make several of during the course of a year, or is it better to save a nickel a month on your local exchange rate?

That has nothing to do with the legality of what we are saying here but it is an interesting kind of observation.

If we simply sat around at the FCC and said the Bell System is making $150 million too much money, and we are simply going to hand that over to the States, and if the Bell System wanted to they would get it handed right back by the court.

We have to have some reason other than just our sociological desire to give the local exchange service a break. We have to have a legal reason for doing it, some sort of a formula.

Mr. MACDONALD. On page 10, Chairman Burch, you point out one of the faults you found with the bill as it is now written was that judicial review could be had only at the behest of the States.

Mr. BURCH. Yes.

Mr. MACDONALD. Would it take care of some of your objections if language was put in to include getting judicial review at the behest of the FCC?

Mr. BURCH. It would take care of that objection. I think, obviously, if there is going to be a bill such as that we certainly ought to have an equal shake in it.

I would like to make one further observation about the situation in November of 1969 when we made this reduction of $150 million.

Contrary to what NARUC said, there was no way the FCC simply could have said, "Mr. Telephone Company, put that 150 million in the interstate and reduce your intrastate revenue requirements by that amount."

We had nothing pending before us that would have allowed us to do it. Second, had we ordered a hearing to determine how much we would give to the States and at the same time how much the entire State reduction would have been, I suspect it probably would have taken 2 years.

I am not saying that because we would have sat around and pondered it for that period of time but these are complex subjects. The telephone company has an almost inexhaustible supply of witnesses they can call for such a hearing, each of whom is a very persuasive man.

For however long that proceeding lasted, we would have paid the same telephone rate because no order was outstanding.

In other words, $300 million in excess profits would have accrued to the telephone company. So it seemed the better part of valor on our part to make an informal decision and reduce the rates promptly in that amount.

We did not have a vehicle at that time had we simply wanted to give that to the States. There was no hearing procedure to do so. Despite the fact that the telephone company may very well take the position sometimes that it all comes out of the same pot so it does not make a great deal of difference whether it is interstate or intrastate, nevertheless, I can assure you at the time we start a separations proceeding they will have comments and some severe comments if we decide all excess profits are to go reducing intrastate rates.

Mr. MACDONALD. Do you feel the presence of the telephone company at the hearing would be helpful?

Mr. BURCH. Yes; I do. On the Senate side, there was a feeling on the part of the Senators that it does not make any difference to the telephone company whether you take it out of one pocket or another. If you ask them it makes a great deal of difference.

Mr. MACDONALD. We would be happy to ask them. They just don't volunteer to come.

Mr. BURCH. The telephone company basically has no competition intrastate. If you want a telephone in Maryland there is only one place you are going to go and that is Chesapeake & Potomac.

On the other hand, if you are a big user of interstate telephone services, you may very well consider going to one of the other carriers, MCI or private microwave system, so they must remain competitive in the interstate field.

They have to stay competitive or their whole structure is endangered so the idea that it makes no difference if we keep raising interstate costs is not true.

It puts them at a competitive disadvantage which they cannot stand.

Mr. MACDONALD. The subject was raised yesterday by Mr. Tiernan of Rhode Island. In his judgment it would seem difficult to get a board from NARUC to pass on these things, that would not have very

divergent interests, as you put it in your testimony. His theory seemed reasonable to me when he announced it, but it immediately was knocked down by practically everyone on the panel. It was held that they have always been working in concert and they have had no internal difficulties about coming to decisions.

I thought it was a little peculiar but I just accepted their word. Has that been the experience of the Commission, too?

Mr. BURCH. Despite the very divergent backgrounds of the Commission, it is not secret that I am a conservative Republican and I believe in State's rights and I personally will bend every effort to see the States get their fair run at this thing.

Nevertheless, I am also a lawyer and I also agree that you just can't separate these things like a piece of pie. We just can't cut it up and say you get half this time and we will get the other half next time.

The regulation of interstate rates is a Federal function and I think it should be performed by a Federal agency despite the fact that I opt for the States when the situation arises.

Mr. MACDONALD. In the light of your background before coming to the Commission, I will ask you this question as a person whom I know has a practical viewpoint toward matters of this nature.

I pointed out yesterday to the members of the panel that it seemed to me when they chose up sides and four were from the FCC and three were from their group, the FCC pretty clearly seemed certain to win.

Wouldn't you give the Commissioners you appointed a sort of loyalty oath?

Mr. BURCH. I would be careful in designating Commissioners to sit on such a board.

The thing that concerns me about this is it is not without the realm of possibility for whatever reason a single FCC Commissioner out of seven could determine all of the separations procedures in the United States.

Presumably you are going to have the three State commissioners voting as a bloc. If one of the FCC Commissioners decides to vote with them he in effect controls all of the separations procedures.

Mr. MACDONALD. That brings me to the real reason for the bill. I think perhaps there could be better cooperation between the FCC and the State groups that has existed, perhaps, in the past.

They seem very, very vehement about the fact that they feel like they are passengers on a train who have nothing to say about its destination or its speed or the cost of the ticket.

Mr. BURCH. I recognize that that is their feeling. As a bit of background, I had been on the Commission 4 days when this situation arose. I was not terribly well versed in the NARUC–FCC problem. Since that time I have become familiar with Mr. Pearson and Mr. Wiggins and Mr. Bloom of Pennsylvania and I am very impressed with what they are trying to accomplish.

I think they are doing exactly what I would do if I were in their position. I also feel that with the help of NARUC and with the help of the FCC such as the Executive Committee meeting we are going to have this afternoon with NARUC and frankly I expect to

have my head taken off all afternoon because of this problem and I don't dispute their right to do it.

Nevertheless I think we can cooperate on these things and I think we can arrive at a reasonable and logical and legal answer to these things.

The point is we just cannot go on the idea we are going to achieve a social good every time the telephone company is regulated. Frankly that is Nick Johnson's point of view and his statement is he does not care about separations and that what we should worry about is social benefits that would flow from our regulations. It is a valid point of view but I am not sure the court would look at it that way because we have to base rates and revenues on costs.

That is the basic ingredient of the whole thing. I agree from the point of view of NARUC we seem to have a whip hand and maybe we did in the past, I don't know, and Commissioner Johnson may dispute this, maybe in the past we have been a little heavy handed.

I certainly don't propose to be. If you get a chance to read my letter to Mr. Pearson, Mr. Chairman, you will see it was honestly conciliatory. We could survive with the bill. I don't think the FCC would come crashing down. Neither do I think it would be a wise legislative exercise.

I don't think this is the approach because basically what this amounts to is kind of a nagging kind of a situation where you always have a hearing going on with three men in there presumably who have a point of view that would be heard.

I will say this: We have under consideration before the Commission at this time certain changes in common carrier procedures generally. I suspect if I have the opportunity to have a hearing on a rate case involving the telephone company or separations or whatever, NARUC will not be invited simply as an observer.

They will probably be given a position in this matter to so they can make somewhat of a record so it is not to the point that we destroy the whole purpose of the proceeding.

I can understand their frustration at times as being an observer and not being able to speak. That is kind of having half a loaf.

Mr. MACDONALD. Thank you very much. I want to commend you and the rest of the Commission for the speeding up of many processes at the Commission that I have noticed since you have taken over as chairman.

This is by no means to be taken as anything derogatory of the former chairman but I would like a commend you for the action that has been coming out of the Commission.

Mr. Van Deerlin.

Mr. VAN DEERLIN. Thank you, Mr. Chairman. I would like to join you in those sentiments and also in welcoming Mr. Burch back on a somewhat less volatile subject than we discussed the last time he was here.

Following up what the chairman said, I would like to compliment you specifically, Mr. Burch, on that action of a week ago in moving at long last to make more realistic the license fees that are charged broadcasters.

Clearly the Commission has been handicapped in the past by an inability of staff to keep up with the vast paperwork that exists down there.

You even had a solid, intelligent basis for proposing higher fees, based on market rate card and so forth. I think it was clearly a step in the right direction.

If you run into any flak on it I hope at least informally you will communicate with those who are sympathetic on it.

Mr. BURCH. I can assure you we will run into flak and I will be glad to communicate because we will need help on this.

Mr. VAN DEERLIN. Would you compare the situation between inter- and intrastate rates for telephones with the continuing dispute in another regulatory agency, the ICC? I refer to the fight over passenger train service versus freight trains—whether the railroad's bookkeeping correctly reflects the expenses that are necessary on each, whether there is a proper balance, and so whether the respective rate structures are justified.

Mr. BURCH. I don't know any of the factors or facts that ICC is considering. I would suspect in a broad sense it is a similar type of problem but I just don't know enough about what they have been doing on freight and passenger service to comment.

Mr. VAN DEERLIN. Those critics who see a social objective in keeping passenger service alive, especially in certain highly populated corridors of travel, have always charged that the railroads' bookkeeping is somewhat unbalanced in favor of getting rid of passenger trains and keeping freight trains.

I take it from your testimony that you think it would be much more difficult for the telephone company to make any such intentional adjustments in its bookkeeping, to reflect more heavily on intrastate than on interstate phone usage.

Mr. BURCH. I think so. I would like to respond in this way also: I think as a statement of fact that the interstate service, long distance service today does to some extent subsidize local service.

If that is a desirable social objective, so be it, it is also a fact of life right at the moment. It is a fact because of a number of reasons. One, I don't think it has been a conscious effort on anyone's part to enter into the subsidization program but I think any fair rate—any fair critic will agree interstate is paying more than its pro rata share of the load.

I would say, however, if the FCC were expected to enter into a conscious effort to subsidize local service, in effect, direct the Bell System to subsidize local service at the expense of the long distance user, I don't think that the FCC is prepared to again take a step like that because I don't think we can or should.

Mr. VAN DEERLIN. This was clearly the thrust of the testimony yesterday—that the ideal objective is a telephone in every home. It is important in police and fire protection and I suppose although it was not mentioned, job availability for hard-core unemployed—to be abe to be notified quickly when a job turns up.

Mr. BURCH. I think we have substantially reached that objective almost in terms of telephones. The figure is 90 percent of homes that have telephones.

The State of Maryland is experimenting with something which I think is a worthwhile objective. It is a limited telephone where you pay maybe a lesser fee and you are authorized maybe only 10 calls a month, but you can always spend a dime and call the fire department and you are available to receive a telephone call.

I agree with the objective. I think everybody in the United States ought to have a telephone. It is a socially degrading thing and inconvenience not to have it.

Mr. VAN DEERLIN. One of those limited phones might be the answer for parents with teenagers.

Mr. BURCH. I have never gotten over the idea that the telephone was a luxury because I was impressed by my dad that every time I made a call it cost 10 cents.

Mr. VAN DEERLIN. I assume except for Commissioner Johnson, all of the Commissioners are agreed on this.

Mr. BURCH. I think Commissioner Johnson dissents in procedures more than the actual outcome except he does make the point that probably we should be concerned with the sociological impact of our decisions more than the legal impact of our decisions.

That to me, if we were to do that, we would be legislating on a daily basis. We would be taking your role. I think if that is what we are to do, we would have to be specifically instructed.

Mr. STRASSBURG. It is a lot easier for the Commission to take those matters into account with respect to the areas subject to its jurisdiction. In other words, if the Federal Communications Commission had sole jurisdiction over all telephone service, then questions of social concern could be given greater weight than it is possible within the context of the problem we are discussing.

For example, in the interstate universe, Congress has said by policy that the Commission may or the carrier subject to the Commission's jurisdiction may establish preferential rates for educational broadcasting interconnection as part of the Public Broadcasting Act.

In other words, the Congress has said so far as interstate commerce is concerned and interstate communications, that it is proper for one interstate user to subsidize other interstate users.

It is a different story when it comes to going across the State and political delineations. There, costs are the significant factor from the standpoint of giving meaning and substance to these differences in jurisdiction.

If you don't go by your costs you have lost all markers and guidelines. That is the problem we have had with this subject.

Mr. VAN DEERLIN. Thank you, Mr. Chairman.

Mr. MACDONALD. Mr. Broyhill.

Mr. BROYHILL. Thank you, Mr. Chairman, I think Chairman Burch answered the question I was going to ask in response to your question, Mr. Chairman.

Mr. Burch, in your testimony you were saying you were ready to cooperate, but I have been impressed that the 50 State agencies at least feel the Commission is not cooperative and they are the ones who are having to do the cooperating.

So, I am glad to hear your statement expressing your own personal view that you will take steps to work more closely with them. Whether

or not this legislation is the right vehicle, I do think this subcommittee ought to keep this whole subject matter under study in terms of whether or not legislation would be necessary to work out a cooperative arrangement for arriving at these cost allocations or cost separations.

I do appreciate your statement here that you fully intend to cooperate with the State agencies.

Mr. BURCH. Congressman Broyhill, one of the concerns of NARUC and if I were in NARUC I would feel the same way: They disagreed with our decision to reduce by $150 million—that was point of dispute No. 1.

They asked us to reconsider our decision which we failed to do, so that is point of disagreement No. 2.

They asked for a stay of the imposition of our order which we did not feel would have any validity except it would deprive the interstate user of a reduction in rate, so we denied that.

So, as a practical matter if I were in NARUC, I would say we hit them one, two, three in a period of about a month and a half and I agree that does not sound very cooperative.

Mr. BROYHILL. When you made this decision of allocating costs or allocating capital investment, they had no part in it.

Mr. BURCH. That was in January of 1969 that we did that. We did not allocate any costs in this particular decision. In this case, we took the interstate base as it had been established through 1969 and calculated that on that base they were going to receive an income in excess of what we had allowed them.

Mr. BROYHILL. I appreciate your clearing up that one point.

Mr. BROTZMAN. May I get the record straighter on this point?

Originally I asked you about the notice, Mr. Chairman, and you indicated November 5. The specific date is not quite as important since I understand there was general public notice of the fact that you were going to make a determination. What was the thrust of that particular notice?

Mr. BURCH. This notice simply announced reductions in interstate long distance calls have been agreed upon by the FCC and the Bell System.

In July of that same year of 1969, we announced that we were entering into continuing surveillance studies with the telephone company. Is that term one that you are all familiar with—a continuing surveillance?

Mr. BROTZMAN. I assume you are starting to look at this particular problem, looking prospectively to a possible determination.

Mr. BURCH. It is a mutual agreement on the part of the telephone company and our part. They voluntarily do this to in effect escape a formal proceeding.

Mr. BROTZMAN. Under this surveillance procedure, would NARUC have an opportunity to come in to present its particular point of view or was it ever afforded that opportunity?

Mr. BURCH. They were observers. They did not have the opportunity to present a point of view.

Mr. BROTZMAN. The question I ask specifically is this: Is there no formal procedure to permit this or under your continuing surveil-

lance procedures could NARUC come in? I think they should have a voice in this.

Mr. BURCH. The reason they were not invited to participate in that continuing surveillance was that the only issue before the Commission at that time was whether the interstate profits were too high based on allocations that had been previously made in a proceeding at which they were parties.

Mr. BROYHILL. To what extent were they parties?

Mr. BURCH. Fully. They were parties to the proceeding.

Mr. COX. We did have three cooperating Commissioners, Congressman Broyhill, who sat with the Commission and who filed their views with us prior to our reaching our decision. But since we were, in effect, fixing separations—which we thought we had to arrive at in order to make the basic determination originally in 1967 and revised in 1969, as to the rate base we would be dealing with and the expenses which would be allocable to the interstate jurisdiction—we then made that judgment.

Actually, they participated. They were allowed to present formal——

Mr. BROYHILL. They were one party among many.

Mr. COX. They participated separately as individual Commissioners and through NARUC. There were also private users; other carriers; Western Union was a participant because it is also subject to separation procedures; the independent telephone companies participated—everyone who sought intervention in the formal rate case—was allowed to participate not only in the formal quasi-judicial proceedings, but also in informal conferences that went on as part of this proceeding.

They had every opportunity to make their case as to what they thought was the proper basis for separations. We gave them $135 million in that process. We then incorporated these separations for the first time into our rules and this means, of course, as with all of our other rules, that any party in interest may come in and petition us to modify our rules, and they in effect have now done this.

But prior to our November 5 action, there was no formally prepared petition before us asking us, in a timely way, to revise our separations in a way which could have affected what we did in November.

Mr. BROYHILL. Could we have a copy of those rules made a part of the record.

Mr. MACDONALD. I don't think they are in yet.

Mr. BURCH. We will send you a copy of the manual as well as the memorandum.

Mr. MACDONALD. I don't think we need the entire manual. I think we need just what Mr. Broyhill is requesting. I don't think we want to go through the entire manual. Let's say including the material in the record is in order, and if you could honor the request of Mr. Broyhill, we would appreciate it. Do you understand what he is after?

Mr. BAKER. Yes, sir.

Mr. MACDONALD. If you can furnish it, it will be included and made a part of the record.

Mr. BAKER. I think what would answer his question best would be the report and order where we took care of the separations problems.

Mr. MACDONALD. Furnish the necessary information. We will appreciate it.

(The report and order referred to follows:)

BEFORE THE FEDERAL COMMUNICATIONS COMMISSION, WASHINGTON, D.C.

(Docket No. 17975)

IN THE MATTER OF PRESCRIPTION OF PROCEDURES FOR SEPARATING AND ALLOCATING PLANT INVESTMENT, OPERATION EXPENSES, TAXES, AND RESERVES BETWEEN THE INTRASTATE AND INTERSTATE OPERATIONS OF TELEPHONE COMPANIES

REPORT AND ORDER

Adopted January 29, 1969; Released January 30, 1969

By the Commission: Commissioner Johnson dissenting and issuing a statement.

1. This proceeding is an outgrowth of the General Investigation (Docket No. 16258) into the lawfulness of the charges of the Bell System companies for interstate and foreign communications services and other related matters. That proceeding was instituted by our Order of October 27, 1965. As part of that proceeding we considered the propriety of the principles and procedures set forth in the NARUC-FCC Separations Manual for separating the Bell System's plant, expenses, taxes and reserves between its interstate and intrastate operations. We also considered proposals for revisions of the principles and procedures advanced by the Bell System and other parties. On July 5, 1967, the Commission issued its Interim Decision and Order in Docket No. 16258 in which it accepted and prescribed the Separations Manual's methods as appropriate with the exception of the methods applicable to the allocation of subscriber plant. At the same time the Commission rejected the various proposals for revisions to the Manual and adopted new principles and procedures for the separation of subscriber plant. A detailed discussion of the background of the jurisdictional separations problem, as well as the rationale for various methods of separations, are contained in paragraphs 240 through 322 of our July 5, 1967, Interim Decision and Order and are incorporated herein by reference.

2. In response to various Petitions for Reconsideration, the Commission, on September 14, 1967, released its Memorandum Opinion and Order on Reconsideration by which it stayed the effect of its prescribed plan and reconstituted the so-called Technical Experts Group[1] to consider "improvements or refinements" which might be made in the prescribed plan. This Technical Experts Group considered the Commission's prescribed plan, a new plan proposed by the Bell System, and various suggested modifications of the latter. The participants could not agree on the acceptability of any one plan. A report dated November 15, 1967, was filed which set out the different positions of the parties.

3. On January 24, 1968, the Commission adopted a further Memorandum Opinion and Order in Docket No. 16258 in which the separations methods prescribed by its July 5, 1967, Interim Decision were reaffirmed and made final for the purpose of determining the Bell System's interstate revenue requirements in Docket No. 16258. At the same time, the Commission noted certain questions raised in the Technical Experts Group's Report with respect to the Commission's plan. We also took cognizance of the policy of this Commission to cooperate with the telephone industry and the National Association of Regulatory Utility Commissioners (NARUC) in the development of separations methods and, in particular, the special interests of the State commissions in the matter of jurisdictional separations. In order to give full consideration to the views held by those affected by the prescription of procedures for jurisdictional separations and to evaluate any alternate plans together with the Commission's plan, the Commission adopted on the same date the Notice of Proposed Rule Making instituting this separate proceeding for the purpose of prescribing separations procedures for the future.

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[1] The Technical Experts Group was formed by direction of the Telephone Committee at a prehearing conference on July 11, 1966, in Docket No. 16258 for the purpose of endeavoring to narrow the issues and devising other means of expediting consideration of separations, pursuant to the Commission's Memorandum Opinion and Order issued April 11, 1966. It consisted of representatives of all parties who submitted separations proposals pursuant to the Telephone Committee's Order issued April 22, 1966, and members of the Commission's staff.

4. Comments of interested parties in response to the Notice of Proposed Rule Making were due on February 26, 1968, and reply comments were due on or before March 12, 1968. These dates were extended to March 12 and March 27, 1968, respectively, in our Order of February 13, 1968, in response to a request of the NARUC.

5. Timely comments have been filed by the Bell System; the Independent Telephone Group (consisting of United States Independent Telephone Association, GT&E Service Corporation, United Utilities, Inc., and the National Telephone Cooperative Association); The Western Union Telegraph Company; the National Association of Regulatory Utility Commissioners; the Networks (consisting of American Broadcasting Companies, Inc., Columbia Broadcasting System, Inc., and National Broadcasting Company, Inc.); General Services Administration for the Executive Agencies of the United States; California Public Utilities Commission; District of Columbia Public Service Commission; Iowa State Commerce Commission; Kansas State Corporation Commission; Montana Railroad Commission; New Jersey Board of Public Utilities Commissioners; North Carolina Utilities Commission; West Virginia Public Service Commission; Wisconsin Public Service Commission and Cities of Los Angeles, San Francisco and San Diego. Reply Comments have been filed by the Bell System; the Independent Telephone Group; The Western Union Telegraph Company; the Networks: California Public Utilities Commission; and District of Columbia Public Service Commission.

INTEREXCHANGE PLANT

6. Historically, two methods have been used for the separations of interexchange circuit plant to determine the allocation of the cost of this plant between state and interstate jurisdictions. The first plan was contained in the 1947 edition of the Separations Manual and remained in effect until 1956 as a method for the allocation of the interexchange circuit plant. Under the 1947 Plan the book cost of the circuits used wholly for a single service was assigned directly to that service. The book cost of circuits used jointly for both services was allocated between services on the basis of relative use measured by the conversation-minute-miles of traffic for each service using the facilities jointly.

7. In July, 1956, the Modified Phoenix Plan was introduced as the method for separations of Bell's interexchange circuit plant and is currently in use. The Modified Phoenix Plan procedures apply to the allocation of the book costs of interexchange circuit plant of the Associated Companies of the Bell System used primarily for message toll service. For purposes of the allocation, this Plan treats all Bell System toll lines pant, both Associated Company and Long Lines, which is located in a given state and which is used to serve subscribers in that state, as if such plant were jointly used to render both intrastate and interstate services. Thus, the Pan averages the lower unit costs of Long Lines plant, used only for interstate service, with the higher unit costs of Associated Company plant, used to provide both services, and thereby assigns an increased amount of costs of this plant to interstate. The Commission's July 5, 1967 decision in Docket No. 16258 concluded that the use of the Modified Phoenix Plan should continue as the procedure for the jurisdictional separations of Bell's interexchange circuit plant.

8. The Bell System, in the General Investigation, proposed changes in the procedures for jurisdictional separations of interexchange circuit plant. Thus, it proposed elimination of the Modified Phoenix Plan and a return to methods generally consistent with the procedures of the 1947 Separations Manual used prior to 1956. It also urged elimination of broad averaging of line haul and terminal costs and the adoption of a method that would determine such costs separately for each segment. Another proposed change was the designation of circuits used for one service only to include circuits handling traffic for another service so long as the use by the other service did not exceed 5% of the total usage of the circuits. These proposals were opposed by the state commissions, through the NARUC, and others. The Commission did not accept the changes proposed by the Bell System. In short, the Commission concluded that on the basis of the considerations then advanced there was not adequate justification for over-turning a separations principle of eleven years standing. With respect to elimination of broad averaging, we held that the refinement sought was not necessary for the purpose of jurisdictional separations.

9. The Bell System in this proceeding, now supported by the NARUC, has renewed its proposal for elimination of the Modified Phoenix Plan and adoption

of methods generally similar to those contained in the 1947 edition of the Separations Manual. However, the present Bell proposal retains the broad averaging features, including the use of average cost per circuit mile in each study area, as required by the current edition of the Manual. It provides for the assignment of costs of circuits used wholly in interstate or intrastate operations directly to their respective operation and the allocation of the costs of jointly used circuits among the operations on the basis of conversation-minute-miles of traffic for each operation. In this respect, Bell has modified its previously proposed method for classification of circuits where other use of a circuit did not exceed 5%. Its instant proposal provides for apportionment of the costs of any circuit whose use is not confined *entirely* to a single service.

10. Those parties seeking herein the elimination of the Modified Phoenix Plan advance the following reasons in support thereof:

(1) The methodology required by the Modified Phoenix Plan is not consistent, in principle, with the methodology now used for separating exchange plant. The latter procedures are premised on the principle that traffic sensitive plant should be apportioned on the basis of actual or relative use. Interexchange circuit plant is clearly traffic sensitive.

(2) The Modified Phoenix procedures are incompatible with current technology and foreseeable future technological advances, e.g. the use of communications satellites for domestic long haul communications.

(3) Compared to the situation existing at the time of the adoption of Modified Phoenix, short haul toll operations of the Associated companies are now benefitting cost-wise much more from technological advances and to this extent there is now less justification to equate the economic benefits of said advances through the averaging of the costs of short haul plant of the Associated companies with the costs of longer haul plant of Long Lines, which is used exclusively for interstate operations.

(4) Contrary to the original rationale for Modified Phoenix, Bell System toll lines plant is not engineered and operated as an entity to serve customers in a state, but, rather is engineered and operated to serve customers in other states as well.

(5) The plan results in an artificial overstatement in interstate book costs of about $500,000,000 currently and the amount is increasing. Moreover, the plan produces an erratic and inequitable distribution in benefits among the states (i.e., 70% of the benefits inure to 12 states which would otherwise account for only 40% of the book costs). This disproportion is also increasing with time.

11. In addition to Bell and the NARUC, the states of New Jersey and North Carolina, in their individual capacities, favor the elimination of Modified Phoenix. The elimination is opposed by the Independent Telephone Group, Western Union, GSA, and, in their individual capacities, by the states of California, Iowa, Kansas, Montana, West Virginia and Wisconsin, and by the cities of Los Angeles, San Francisco, and San Diego. Those who oppose the elimination rest their opposition principally on the argument that the toll lines plant in each state is engineered and operated as an entity and that the low cost high volume routes are dependent on the high cost low volume routes.

12. The separations procedures proposed in this proceeding by the Bell System and the NARUC are substantially changed from the procedures advocated by the Bell System in FCC Docket No. 16258. Under the previous proposal costs would be determined separately for line haul and terminal equipment. The present proposal, as already noted, contemplates continuation of the broad averaging of the line haul and terminal costs of interexchange plant in each study area. In the previous proposal, a circuit was assigned wholly to one service where other traffic on the circuit did not exceed 5% of the total usage of the circuit. This is eliminated in the present proposal. Circuits used wholly in one service are directly assigned to that service. Circuits carrying more than one service will be allocated between services on the basis of proportionate use. The previous proposal was opposed by the NARUC whereas the present proposal is supported by the NARUC and, hence, the majority of the state commissions. The previous proposal shifted $175 million in revenue requirements from interstate to intrastate. By the present proposal, this amount is reduced to $118 million.

13. We have carefully considered the arguments advanced by the parties advocating retention of the existing procedures for separating interexchange plant. In doing so, we have also reexamined, in light of current conditions, the rationale on which the adoption of these procedures was premised. We have also considered

the importance of designing cost allocation procedures so as to assign book costs to those services which are responsible for incurring them and that the principle of actual use is the best means of assigning such cost except where it can be demonstrated that adherence to actual use will not result in a fair and equitable apportionment. Upon the basis of these considerations we have concluded that reversion to the actual use principles and procedures similar to those contained in the 1947 Separations Manual applicable to interexchange circuit plant is necessary and appropriate at this time.

14. A principal argument to sustain the Modified Phoenix Plan has been that telephone plant is engineered and operated as an entity and that, therefore, the averaging of the costs of Long Lines terminating plant used exclusively in interstate service with the costs of Associated Company plant is warranted. There is no dispute that the telephone system functions as an integrated entity and that each operating component must have technical compatibility with all others. While this may be true as a generality, it tends to oversimplify the picture and to obscure the fact that substantial amounts of facilities are devoted exclusively to one or the other of the services, state or interstate. We think it is essential, in the light of present day technological considerations, that the book costs of these facilities be assigned to the service which is responsible for them.

15. Nor is there any dispute that the cost averaging of Modified Phoenix was designed to lessen the disparity between costs and revenue requirements applicable to intrastate and interstate services, respectively. However, current operating data make it apparent that the Modified Phoenix Plan is no longer producing its desired effects except in a most generalized, but unbalanced, fashion. It is further apparent that under current conditions the plan is now operating to introduce gross distortions in the relative costs of interexchange plant being assigned to state and interstate services and that such cost distortions can have undesirable economic consequences.

16. Thus, it appears that since 1956, when Modified Phoenix was adopted, Associated Company interexchange message circuit plant book costs have actually increased about 100%. However, the portion of such total book costs now being assigned to the interstate jurisdiction by virtue of the application of Modified Phoenix has increased 175%. This, in part, is the result of the more rapid growth of lower cost Long Lines plant relative to the growth of higher cost Associated Company plant. What is significant, however, is the progressive nature of the growing disproportionate assignment of Associated Company interexchange costs to interstate operations—a trend which has no relationship whatsoever to the actual use being made of Associated Company plant for state and interstate services.

17. This distortion is compounded by the disproportionate effect of the Modified Phoenix Plan among the several states. For example, 70% of the additional book costs which are assigned to the interstate service because of the procedures of the Modified Phoenix Plan are distributed among only 12 states. On the basis of actual use, or in other words, without the cost averaging introduced by the Modified Phoenix Plan, the 12 states would account for only 40% of the book costs allocated to interstate. This disproportionate distribution, which is largely attributable to the happenstance of the location and physical routing of Long Lines plant, casts serious doubt on the current validity of the Modified Phoenix procedures. It also casts doubt on their efficacy in realizing the objective of the plan to lesssen disparity between state and interstate revenue requirements.

18. Another argument advanced to support retention of Modified Phoenix has been that the cost averaging provided for therein is justified by the degree to which Long Lines route mileage represents plant jointly owned by Long Lines and the Associated Companies. To the extent that this may be a valid justification for treating all such plant as if it were used jointly for state and interstate services, it is significant that between 1954 and 1967 the proportion of Long Lines route miles which were derived from plant jointly owned with the Associated Companies decreased from 73% to 55% of total Long Lines route miles. In 1967 52% of Long Lines terminating circuit miles were, in fact, on wholly owned Long Lines routes. In any case, with respect to jointly used facilities, it appears that, in a sense, each of the services contributes to the whole and that an appropriate measure of such contribution is the relative use of such facilities in each service applied to the actual costs associated with such facilities.

19. Under all the foregoing circumstances, we conclude that the Modified Phoenix Plan is not producing fair and equitable results but rather gross distortions in cost allocation and that it is timely and necessary to revert to the actual use principles and procedures similar to those contained in he 1947 Separations Manual as the basis for assigning the costs of interexchange circuit plant. We also conclude that elimination of the Modified Phoenix Plan and reversion to actual or relative use as the basis for allocating circuit plant will establish consistency with the treatment we have prescribed for the allocation of exchange plant, namely, that such plant that is traffic sensitive should be allocated on the basis of actual or relative use. Since interexchange plant capacity is geared to traffic volume, it is traffic sensitive. Finally, we conclude that with the rapid development and advancement of new and competing technologies, it is important that the separation procedures used for determining the interstate and intrastate revenue requirements not obscure the true economic facts and advantages of each technology. The artificial assignment of costs to one service or another, as occurs under the Modified Phoenix Plan, tends to obscure the basis for objective comparison. This is of more than theoretical concern today as we expect to be confronted in the near future with the problems of making sound determinations as to where and how, if at all, the satellite facilities to provide domestic communications services would be feasible and economical, having in mind, among other things, the total costs of alternative means of supplying similar services over like distances. However, it should be noted that this discussion is related to procedures for jurisdictional separations only and should not be construed as indicating the methods we believe to be proper for the purpose of making allocations of total interstate services nor for the determination of costs for competitive services.[2]

EXCHANGE PLANT

20. As noted above, the Commission in its July 5, 1967 Interim Decision accepted and prescribed the principles and procedures of the Separations Manual (including the revisions of the Denver Plan), except those applicable to subscriber plant. With respect to this class of plant, we reached the following conclusions:

(*a*) Actual use, although a relevant factor, is not the sole factor to be considered for the allocation of subscriber plant costs. This is because subscriber plant is not traffic sensitive. The plant is installed largely for the purpose of providing subscribers with a constantly available *access* to and from the exchange and long distance telephone networks. Thus, the cost and capacity of the plant involved is not determined by the amount of its use.

(*b*) The charge per toll message, which is a characteristic feature of all toll rate schedules has in itself a deterrent effect on the actual use of subscriber plant. This is in contrast with the lack of deterrent in the exchange rate schedules which generally are based on flat or unmeasured rates.

(*c*) There is a further deterrent to use of subscriber plant in the toll rate structure which results from the fact that the charge per toll call increases with distance and conversation time. This deterrent effect of distance is enhanced in the case of interstate use of subscriber plant because on the average the interstate length of haul is greater than the average length of haul of intrastate toll calls.

(*d*) While distance gives an element of value to long distance calls and the greater cost has a restrictive effect on toll usage, procedures for the separations of costs of subscriber plant based *solely* on the concept of distance are not acceptable.

21. On the basis of the foregoing conclusions and exercising our considered judgment in light of all of the considerations then before us, we adopted a new two-part formula for the jurisdictional separations of the costs of the Bell System's subscriber plant. The formula was designed to take account of actual use of such plant for interstate services, as well as the deterrent effect on such use produced by the measured rate feature of the interstate toll schedule. The actual use is reflected in the first part of the formula which provides that a

[2] Insofar as any transfers of property between Long Lines and Associated Companies may affect the intrastate and interstate revenue requirements, the Commission has ample statutory authority to oversee this matter and to prevent possible abuses.

portion of the costs of the Bell System's subscriber plant allocated to the interstate message toll service shall be determined by applying to the study area book costs of subscriber plant the interstate SLU factors as measured by the ratio of interstate holding time minutes to total holding time minutes-of-use applicable to traffic originating and terminating in the study area. The deterrent effect is reflected in the second part of the formula which provides that an additive factor of 200% of the nationwide annual average interstate SLU factor for the total telephone industry be applied uniformly to the Bell System's subscriber plant costs in each study area. The amounts thus determined are added together to produce the total apportionment of subscriber plant costs to interstate.

22. In the instant proceeding, the Commission's July 5 plan for subscriber plant received the support of the Independent Telephone Group Western Union GSA, the states of California, Iowa, Kansas, Montana, West Virginia, and Wisconsin, and the cities of Los Angeles, San Francisco and San Diego.[3] Objections to the July 5 plan were made by NARUC, Bell, the states of New Jersey and North Carolina and the District of Columbia. The Bell System has submitted an alternative plan herein which has received the endorsement of the NARUC, and which we will discuss hereinafter.

23. The essence of the objections to the Commission's July 5 plan may be described as follows:

(*a*) The use of the same additive factor in each study area to compensate for the deterrent effect of the toll rate schedules ignores the fact that the degree of the deterrent is affected in each study area by such characteristics as its geographical location and community of interest with other parts of the nation.

(*b*) The use of a single uniform factor does not adequately reflect the increasing deterrent effect of the toll rate schedule as the calling distances increase.

(*c*) Because the plan uses a flat percentage figure, it offers no incentive for the development of additional interstate business in a given study area.

(*d*) It produces inequitable results among the states.

24. In an effort allegedly designed to meet these objections, the Bell System, supported by the NARUC, has proposed herein the adoption of a revised plan for the allocation of the cost of subscriber plant. This plan consists of a three-part formula, Part A is the same as the first part of the Commission's plan, i.e., study area interstate SLU factor times study area book costs. Part B is the same as one-half of the additive portion of the Commission's plan, i.e., 100% of the average nationwide interstate SLU factor times study area book costs. Part C of the Bell's proposal would increase the second half of the Commission's additive factor from 100% to 160% and would apply this portion of the additive factor in accordance with the following formula:

(*a*) Total industry subscriber plant book costs assigned interstate by Part B; times

(*b*) Study area interstate holding time minutes divided by total industry interstate holding time minutes; times

(*c*) Average interstate initial period station rate at study area average length of haul divided by total industry average interstate initial period station rate at nationwide average length of haul; times

(*d*) Additive factor of 160%.

25. The Bell System contends that the plan which it proposes for the separation of costs of subscriber plant retains the best features of the Commission's plan and largely alleviates the alleged deficiencies. Thus, Bell alleges it retains the Commission's plan in both Part A of its plan which reflects the actual use of subscriber plant and in Part B of its plan which uses 100% of the nationwide average interstate SLU factor. As we will set forth hereinbelow, we also accept Parts A and B of the Bell proposal. We, therefore, turn now to an analysis of the third part of Bell's plan.

26. The third part of Bell's proposal is quite complex and introduces several questionable concepts which we will discuss separately. The first concept is the use of nationwide, industrywide, average book costs. The effect of this aspect of the Bell formula is to develop an average total industry subscriber plant book cost per minute of use. This average book cost is then used to determine

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[3] Most of these parties advocated modification of the plan with respect to the District of Columbia because of its geographical situation.

the additional amount of book costs assigned to interstate operations in each study area by the third part of the formula. As is pointed out by the Independent Telephone Group and California, who object to this feature of Bell's plan, it penalizes a study area with higher than average costs and gives undue advantage to a study area with lower than average costs. Thus, it would appear that this concept is contrary to one of Bell's primary arguments in support of Part C of its plan, i.e., that it would "reflect each study area's contribution to the total interstate enterprise."

27. Secondly, it is to be noted that Bell supports items (b) and (c) of its formula on the ground that they provide an incentive to each study area to make a greater contribution to interstate business and "rewards" success by increasing the interstate share of the study area costs. Bell further argues that increased calling pursuant to such an incentive would tend to reduce unit subscriber costs for both intrastate and interstate users. The Independent Telephone Group opposes this concept, stating that the determination of a telephone company's interstate costs should be derived by separating that company's book costs and not by "rewards," "incentives" or "contributions." We agree with the Independent Telephone Group and do not believe that it is proper to base such an important aspect of separations primarily on an "incentive factor" of this type. However, we recognize that, if a proposed separations formula is otherwise fully supportable as reasonable from a cost allocation standpoint, appropriate consideration may well be given to factors which would tend to increase use or to decrease the average cost of handling calls. Unfortunately, Bell has not shown how implementation of the third part of their plan would provide such an incentive to use or which entities or users would be induced to make additional calls. Certainly there is no incentive to the interstate user since this feature of the formula by transferring costs from the intrastate to interstate jurisdiction would tend to increase total interstate costs. If the idea is to provide an incentive to the telephone companies to somehow bring about an increase in interstate calling or to increase the average length of interstate calls or length of conversation, or all three, we agree that the incentive concept would have merit. However, Bell has not shown, nor can we see, how the third component of Bell's plan would accomplish or even facilitate these objectives.

28. Aside from the foregoing, it must be borne in mind that the basic premise for an allowance in excess of actual SLU is the fact that usage of subscriber plant for interstate traffic is deterred by the combination of the unit charge and increasing initial rate as distance increases. The incentive approach which relates allocation to increased use rather than to barriers to use is diametrically opposed to the concept that there should be compensation for the existing deterrents to use and is therefore not an appropriate means for fixing additional allocation of subscriber plant.

29. The third weakness in the Bell Plan results from the arbitrary and contrived nature of the 160% factor—60% above that proposed by the Commission in its plan—which Bell would assign to the third part of its basic formula. This additional 60% appears to be premised primarily, if not solely, on the position that it would improve the results of the separations plan as among the various states. We should like to make it clear that the revisions in separations we are striving for herein are designed to remove existing inequities and to establish procedures which are reasonable and fair with respect to all jurisdictions. Since one of the basic reasons for elimination of Modified Phoenix was that it produced inequitable results and erratic distribution of interstate revenue requirements among the states, it is to be expected that the correction of this inequity would necessarily have different effects on different jurisdictions. Similarly, the application of the Denver Plan procedures resulted in an irrational distribution of benefits among the various states. Correction of both of these inequities will necessarily increase benefits to those who received too little previously and decrease benefits to those who had received too much previously. We do not believe that in correcting past inequities we should adopt a plan arbitrarily designed to maintain the *status quo* with respect to all jurisdictions and thereby give unwarranted benefits to some, if not many, jurisdictions. The elimination of one series of inequities should not be the basis for creation of a new series of inequities. For all of these reasons we cannot accept the Bell proposal.

30. Although we are unable, for the reasons outlined above, to adopt the Bell System proposal as an acceptable method for the jurisdictional apportionment of subscriber plant, we are of the opinion that our July 5 plan can improved by

certain modifications or refinements that will make its application more equitable for all study areas. Thus, we believe that there is merit to the criticism of the use of a single uniform additive for all study areas. While the additive factor was intended, properly, to compensate for the deterrent to actual use of subscriber plant inherent in the toll rate structure, we recognize that the application of the same factor in each and every study area can produce some questionable results in particular study areas. For, as pointed out by Bell, the degree of the deterrent varies from study area to study area depending upon the geographical location of the particular study area and its community of interest with the rest of the nation's telephone subscribers. In other words, subscribers situated in the central areas of the United States cannot make toll calls at the maximum rates of the interstate schedule, and such subscribers would find the toll rate schedule in this respect to be less of a deterrent to use of subscriber plant than subscribers situated on the east or west coasts. Also, subscribers in large population centers located close to each other, but separated by state boundaries, would tend to have a high calling rate between them and hence make greater toll use of the subscriber plant than subscribers located in large population centers at greater interstate distances from other population centers. These, and other considerations, necessarily affect the calling habits of toll subscribers and result in different usage patterns of exchange plant from study area to study area. Therefore, such considerations cannot adequately be reflected by a single flat nationwide additive factor designed to compensate for the deterrent effect of the interest toll rates schedule on interstate use of subscriber plant.

31. Moreover, our further analysis of the July 5 plan indicates that it warrants adjustment in another respect. As interstate rates are reduced the deterrent to use of exchange plant for interstate calling is likewise reduced. Therefore, the additive factor, which is intended to compensate for the deterrent, should also have a decreasing effect. However, as formulated by our July 5 plan, the additive factor will have the opposite effect as interstate rates are reduced and will, in itself, require an increasing allocation of subscriber plant costs to the interstate jurisdiction. In other words, with a nationwide reduction in interstate rates, there will tend to be a decrease in the deterrent effect of toll charges and an increase in the nationwide interstate SLU factor. However, under our July 5 plan, with its 200% additive factor, interstate revenues requirements would be increased by a greater allocation of plant and expenses. Thus, a factor which should have decreasing importance as deterrents are removed would have a disproportionately increasing effect. Over an extended period of time, this would defeat the spirit and intent of the additive and could unduly burden the interstate jurisdiction with excessive allocations of subscriber plant costs.

32. We believe that our concerns in the above respects, which are shared by a number of respondents in this proceeding, can be met by a modification of our July 5 formula. All respondents are in apparent agreement with our July 5 plan insofar as it provides for measuring, in each study area, actually interstate use of subscriber plant on the basis of interstate subscriber line usage (SLU). Thus, we will continue to use the study area SLU factor for the first part of our formula. As recommended by the Bell plan, we will also provide for an additive of 100% instead of 200% of nationwide interstate SLU as the second part of the formula. In doing so we give recognition to the fact that subscriber plant, wherever located, is available to interstate operations generally for the origination and termination of interstate long distance calls. It also recognizes that the single interstate toll rate schedule applies uniformly throughout the continental United States and, therefore, by virtue of this factor alone, exerts a restrictive effect on the actual use of subscriber degree of the deterrent of the toll rate schedule is not entirely the same from study area to study area because of the considerations peculiar to each study area as discussed in paragraph 30, above, we are providing, as the third part of our formula, for a second additive consisting of a modified study area SLU factor to be applied to study area book costs of subscriber plant. This modified SLU factor will consist of the study area SLU factor multiplied by the ratio of the average interstate initial period station rate at the study area average interstate length of haul to the nationwide composite total toll initial period station rate at the nationwide average length of haul for all toll traffic for the total telephone industry. The use of a modified SLU factor in this fashion will provide a reasonable measure of the deterrent effects on interstate toll use of subscriber plant in a particular study area resulting from the conditions affecting such toll usage which are peculiar

to such study area as discussed above. It will also relate compensation for the deterrent effect reasonably to the effect itself. Thus, as the relative deterrent decreases the relative compensation would tend to decrease, and when the relative deterrent effect increases so will the compensation.

33. In our best judgment and with full consideration of all the facts and arguments before us in this proceeding, we are convinced that the procedures for the jurisdictional separation of telephone plant that we are prescribing herein are fully warranted and produce fair and equitable results for all parties affected thereby.[4] We wish to stress again that there is no means of precise mathematical measurement of the amounts necessary to give effect to all of the factors under consideration in this proceeding. In the area of jurisdictional separations, it is necessary to make acceptable compromises between complex procedures which are costly to effectuate and less precise methods which are generally equitable and have the advantage of simplicity and ease of application. This is particularly appropriate since informed judgment of necessity has such a substantial impact on the overall results.

SUBSIDIARY ALLOCATION PROCEDURES

34. To effectuate our conclusions we are adopting and prescribing the principles and procedures contained in the April 1963 Separations Manual including the 1964 and 1965 Addenda thereto as modified by the revisions in those procedures adopted herein for the allocation of the costs of interexchange circuit plant and subscriber plant. A more precise description of the prescribed revisions is contained in the attached Appendix A for interexchange circuit plant and for subscriber plant. These revisions describe the procedures for the allocation of only the book costs of plant in these categories. The allocation of reserves and expenses that are directly related to such book costs shall be accomplished in a manner consistent with the procedures set forth for the allocation of book costs.

35. There are certain other traffic and commercial expenses (specified in Appendix A) which are now apportioned on the same basis as the book cost of subscriber plant. No revisions in the procedures for separating these expenses have been proposed and the revenue requirement effect of the various plans considered in this record have been calculated on the basis of continuing the apportionment of these expenses under the existing procedures. Since the Denver plan procedures will no longer be applied for the separations of subscriber plant, and in view of the relatively minor effect of these expenses on the overall amounts assigned to interstate, we do not deem it necessary to continue the calculations required to apportion these expenses by the method now being used even if they were otherwise found to be justified. Furthermore, the deterrent effect concept discussed herein as supporting the subscriber plant separations method which we are prescribing does not appear to be applicable to these expense items. In view of the nature of these expenses and after consideration of the historical treatment accorded them for separation purposes, we are of the opinion that subscriber line usage is an appropriate basis for apportioning such expenses and we are therefore prescribing such procedures as set forth in Appendix A.

PROCEDURAL QUESTIONS

36. Both California and the Independent Telephone Group have requested, in their comments, that the matter of separations be designated for an evidentiary hearing before a final determination is made herein. California is primarily concerned[5] that if it is proposed that any plan other than the original plan set forth in our Decision and Order be adopted, further evidentiary hearings should be held so that any such new plan would be subjected to cross-examination in order to afford the states concerned full due process. It is to be noted we are following the same procedures in adopting the separation plan herein as we did in adopting the plan set forth in our Interim Decision, which

[4] These procedures, and our prescription thereof, are not designed to apply to Alaska and Hawaii in view of the substantially different conditions existing in the cast of these States.

[5] California suggests the possible inaccuracy of the Bell System figures relating to results of the various separation methods. It states that no one during the course of Docket No. 16258 had access to the work papers underlying such figures. An examination of the record of that docket fails to disclose any unsatisfied request, made on the record, that the Bell System make such work papers available for inspection by California or anyone else.

California now supports as fully justified by the record in that case. In each case we arrived at a plan which reflects our informed judgment, based on all of the data before us, as to the plan which is most reasonable and feasible in the current circumstances. We specifically considered the need or requirement for cross-examination on the record before the adoption of our original plan in our Memorandum Opinion and Order on Reconsideration in Docket No. 16258 and found that it was not required (see paragraphs 47–49 of the Memorandum Opinion and Order).

37. The Independent Telephone Group is primarily concerned with the application of the Modified Phoenix Plan to the Independents. It alleges that the Independents should be in the same position as the Bell companies insofar as the application and implementation of the Modified Phoenix Plan is concerned. Since we have now provided for the elimination of that plan insofar as the Bell companies are concerned, it would appear to us that this basic argument of the Independents is no longer applicable.

38. Aside from the foregoing, it is to be noted that this entire question of separations has been considered both at great length and in great depth for a period of well over two years. All interested parties, including the Independents, participated fully in the proceedings in Docket No. 16258, in the meetings and deliberations of the Technical Experts Group, and in the filings in the instant proceeding. Thus, all parties had ample opportunity to make their views known, to propose their own separations plans, and to comment on the proposals of other parties. We stress, as has been set forth hereinabove, that the plan adopted herein is designed, insofar as exchange plant is concerned, to improve the plan we originally adopted and to satisfy legitimate criticisms which have been made with respect to that plan. Insofar as interexchange plant is concerned, we have determined, on further review and because of the fast pace and vast scope of technical change, to eliminate the Modified Phoenix Plan so that we may have available appropriate and accurate data with respect to the costs of long distance transmission facilities on the basis of which we can make informed decisions regarding the relative merits of alternative facilities which are becoming available. Under all of these circumstances we cannot find that considerations of equity require, or that any useful purpose would be served, by now setting this matter for further formal evidentiary hearing. We therefore deny the above described requests that this matter be set for further evidentiary hearing.

CONCLUSIONS

39. We are aware that a major change in jurisdictional separations of the type we are prescribing herein can have substantial effects on the various jurisdictions, particularly since intrastate telephone rates have for several years been based on revenue requirement calculations, computed in accordance with the separations procedures contained in the Modified Phoenix and Denver Plans. Immediate and full implementation of the procedures we are prescribing herein, for the separation of both subscriber plant and interexchange plant costs, could have considerable impact in a number of jurisdictions where intrastate revenue requirements would be increased. This is inevitable where corrective action is being taken to remove deep-seated inequities in the existing procedures. We believe that the appropriate method in dealing with this problem is not the selection of a factor designed solely to maintain a *status quo* as Bell has proposed by its plan. Following this course of action will simply result in creating a new series of inequities. We believe, on the other hand, that it is reasonable and appropriate to minimize the immediate impact on the revenue requirement position of individual states by phasing the implementation of our prescribed plan over a period of time. Accordingly, in our order herein we will provide for the elimination of one-half of the calculated effect of Modified Phoenix upon the effective date of this Report and Order and the elimination of the remainder over the following twelve months. The net effect of the first stage of this phased plan will be to shift revenue requirements of about ninety-four million dollars from Bell's intrastate to its interstate operations. This is about the same amount as was transferred to interstate operations under our original plan. As experience has shown, the allocation of subscriber plant to interstate will increase in sufficient amount to substantially offset the remaining effect of the elimination of Modified Phoenix by the end of 1969. Accordingly, it would

appear that as a result of such phasing of the elimination of Modified Phoenix, this plan will tend to minimize the effect of these revisions in separations procedures on intrastate revenue requirements.

40. Appendix A attached hereto is designed to serve as an Addendum to the April 1963 edition of the Separations Manual which, with the 1964 and 1965 Addenda thereto, are hereby incorporated by reference into Part 67 of our Rules and Regulations. Although Appendix A does not set forth specific language as substitute for various paragraphs of the Manual and the 1965 Addendum, we believe Appendix A with the discussion in this Report and Order adequately describes the separations procedures we are prescribing. We expect our staff to meet informally with the NARUC separations subcommittee, representatives of the industry and any other parties having an interest in this matter, for the purpose of drafting revisions to the Manual to incorporate therein the changes we are adopting in this Report and Order. Furthermore, we are well aware that because of the increasingly rapid changes in telephone technology and innovations in service offerings and rate structure, the jurisdictional separations procedure we are prescribing and incorporating in our Rules will require continuing review and possible revisions on occasions in the light of changed conditions in the industry. In this connection we intend to continue our cooperation with the NARUC, as in the past, in the conduct of joint studies and reviews of jurisdictional separations matters. In fact the Commission will look to these joint studies as the prime forum for continued analysis of separation procedures and the source of proposals for their refinement, improvement or modification in light of actual experience and technological changes. Any proposed revision in the prescribed procedures which may result from such studies or which may be advocated by any other interested party will be considered on a public record in accordance with the rule-making provisions of the Administrative Procedure Act.

Accordingly, it is ordered, That, pursuant to the provisions of Sections 4(i), 221(c) and 221(d) of the Communications Act of 1934, as amended, the NARUC–FCC Separations Manual, together with its various addenda and as modified by the procedures described in Appendix A hereto, is hereby adopted and prescribed as the procedures which shall hereafter be used in the separation of investment, operating expenses, taxes and reserves between the interstate and intrastate operations of telephone companies; and

It is further ordered, effective January 1, 1969, That Title 47 of the Code of Federal Regulations is amended by the issuance of a new Part 67 as contained in Appendix B hereto, which incorporates by reference into the Commission's Rules as Part 67 thereof, the aforesaid Separations Manual and its addenda, including the 1969 addendum as contained in Appedix A hereto; and

It is further ordered, That this proceeding is terminated.

FEDERAL COMMUNICATIONS COMMISSION [6]

BEN F. WAPLE, *Secretary.*

1969 ADDENDUM TO THE SEPARATIONS MANUAL

GENERAL

This Addendum modifies and amends the procedures covered in the April 1963 Separations Manual and the 1964 and 1965 Addenda thereto, to reflect the changes in separations set forth in the Federal Communications Commission Report and Order in Docket No. 17975, dated January 29, 1969. These changes were prescribed by the FCC for jurisdictional purposes and cover revisions in procedures for the separation of interexchange circuit plant, subscriber plant and certain traffic and commercial expenses. The modifications to the Separations Manual and Addenda are described below.

PART I INTEREXCHANGE CIRCUIT PLANT

For the purposes of jurisdictional separations the costs of interexchange circuit plant (interexchange outside plant, interexchange circuit equipment and associated land and buildings) in the area under study shall be assigned to categories and apportioned between interstate and intrastate operations as set forth below: [1]

[6] See attached dissenting statement of Commissioner Johnson.

[1] The procedures set forth herein for the separation of interexchange circuit plant shall become fully effective January 1, 1970. One-half of the effect of the Modified Phoenix Plan procedures shall be eliminated as of January 1, 1969 and one-twelfth of the remaining effect shall be eliminated each month of the year 1969.

A. Plant furnished to another company for interstate use

This category comprises that plant provided for use by another company as an integral part of its facilities. This category includes such plant as sections of whole cables, complements in a cable, and circuit equipment associated with the other Company's outside plant conductors and microwave systems. The total cost of the plant in this category is assigned directly to the interstate toll operation.

B. Broadband facilities used for private line services

This category includes the plant used for private line services employing broadband transmission (e.g., video). The cost of the plant for each broadband facility is determined separately and assigned directly to the appropriate operation (state or interstate).

C. All other interexchange facilities

This category includes the costs of all interexchange plant facilities not assigned to Categories A and B above. The facilities included in this category are used for the following classes of circuits:

1. Interstate message circuits, i.e., message circuits carrying only interstate message traffic.
2. State message circuits, i.e., message circuits carrying only state message traffic.
3. Jointly used message circuits, i.e., message switching plan circuits other than those included in 1 and 2 above.
4. Circuits used exclusively for TWX service.
5. Circuits used for interstate private line services (excluding broadband circuits).
6. Circuits for state private line services (excluding broadband circuits).

The circuit equipment in this category is first segregated between (a) basic circuit equipment, i.e., that which performs functions necessary to provide and operate channels suitable for voice transmission (telephone grade channels), and (b) special service circuit equipment, i.e., that which is peculiar to special service circuits.

The costs of outside plant, basic circuit equipment and associated land and buildings in the area under study are combined, and an average cost per interexchange telephone circuit mile is developed and applied to the interexchange telephone circuit mileage counts of each of the above six classes of circuits.

The cost assigned to interstate message circuits and interstate private line circuits is assigned directly to the interstate operation.

The cost assigned to state message circuits and state private line circuits is assigned directly to the state operation.

The cost assigned to jointly used message circuits is apportioned between state operations and interstate operations on the basis of the relative number of conversation-minute-miles applicable to such facilities.

The cost assigned to TWX interexchange intertoll circuits which, by use, are assignable to a given operation, is assigned directly to the appropriate operation. The cost of TWX intertoll trunks used jointly for state and interstate operations is apportioned between the operations on the basis of the relative number of TWX connection-minute-miles applicable to such facilities. The cost of TWX remote access line interexchange circuits is apportioned between state and interstate operations on the basis of the relative number of TWX connection-minute-miles applicable to those facilities.

The cost of special service circuit equipment is segregated among TWX service, telegraph grade private line services and other private line services. The cost assigned to TWX service is apportioned between state and interstate operations on the same basis as that used for TWX intertoll trunks. The special service circuit equipment costs assigned to telegraph grade and other private line services are allocated between state and interstate operations on the basis of analyses of the use of this equipment for state and interstate private line services.

Insofar as the above modifications affect the apportionment of related items, consistent modifications are made in the treatment of such items.

The portions of the Separations Manual and Addenda which are significantly affected as a result of the above are:

Section	Part	Paragraph
1	1	11.23, 11.231, table 1
2	3	23.221, 23.51 through 23.5233
2	4	24.02, 24.04 through 24.0441, 24.05 through 24.054.

PART II SUBSCRIBER PLANT

For the purposes of jurisdictional separations the costs of subscriber plant (subscriber line outside plant, subscriber line circuit equipment, station equipment and associated land and buildings) assigned to message telephone services shall be allocated to the interstate operations in each state or study area by the application of a factor to the study area message telephone subscriber plant book costs. This factor is comprised of the following:

(a) Interstate subscriber line usage (SLU) representing the actual interstate use of subscriber plant as measured by the ratio of interstate holding time minutes-of-use to total holding time minutes-of-use applicable to traffic originating and terminating in the study area. (This factor will be derived in each study area in accordance with present procedures) plus

(b) Nationwide annual average interstate SLU for the total industry, plus

(c) Modified study area interstate SLU, to be determined by an annual average study area interstate SLU multiplied by the ratio of (1) the average interstate initial period station rate at the study area average interstate length of haul to (2) the total industry average total toll initial period station rate at the nationwide average length of haul for all toll traffic for the total telephone industry.

Insofar as the above modifications affect the apportionment of related items, consistent modifications are made in the treatment of such items.

The portions of the Separations Manual and Addenda which are significantly affected as a result of the above are:

Section	Part	Paragraph
1	1	11.22, table 1
2	3	23.444
2	4	24.03312
2	5	25.24.

PART III TRAFFIC AND COMMERCIAL EXPENSES

Certain traffic and commercial expenses which are indirectly related to subscriber plant, and which are more fully described below, shall for the purpose of jurisdictional separations be allocated among the operations in each state or study area on the basis of the relative number of subscriber line minutes-of-use applicable to each operation in the area under study. The traffic expenses referred to above are those in (a) Customer Instruction and Miscellaneous, see Par. 44.352 of Separations Manual, (b) "All Other Expense" of Private Branch Exchange in Operators' Wages, see Par. 44.4222 of Separations Manual, and (c) the "remaining expense" of Public Telephone Expenses, see Par. 44.82 of Separations Manual. The commercial expenses referred to above are the expense of alphabetical and street address directories and traffic information records included in Directory Expenses, see Par. 45.713 of Separations Manual.

The portions of the Separations Manual and Addenda which are significantly affected as a result of the above are:

Section	Part	Paragraph
1	1	Table 2
4	4	44.352, 44.4222, 44.82
4	5	45.713.

In Chapter I of Title 47 of the Code of Federal Regulations, a new Part 67 is added to read as follows:

PART 67—JURISDICTIONAL SEPARATIONS

§ 67.1 Separations Manual: incorporation by reference

(*a*) Jurisdictional separations of telephone companies' property costs, revenues, expenses, taxes and reserves are determined under principles and procedures set forth in the Separations Manual ("Standard Procedures for Separating Telephone Property Costs, Revenues, Expenses, Taxes and Reserves"), as amended by the Federal Communications Commission, which is hereby incorporated by reference into this Part 67, pursuant to 5 U.S.C. 552(a)(1) and 1 CFR Pt. 20. The contents of the Manual, as incorporated by reference, include the April 1963 edition of the Manual, 1964, 1965 and 1969 Addenda, subsequent amendments of the Manual adopted by the Federal Communications Commission, and subsequent editions of the Manual authorized by the Federal Communications Commission. The principles and procedures set forth in the Manual are designed primarily for use in the allocation of property costs, revenues, expenses, taxes and reserves between intrastate and interstate jurisdictions.

(*b*) The Separations Manual is published by the National Association of Regulatory Utility Commissioners (formerly the National Association of Railroad and Utilities Commissioners). Copies of the current edition of the Manual, with current Addenda and Amendments, may be obtained at a cost of two dollars ($2.00) per copy, by writing to the Association, P.O. Box 684, Washington, D.C. 20044.

(*c*) Copies and current edition of the Separations Manual, with current Addenda and Amendments, are available for inspection at the following locations:

Office of the Common Carrier Bureau, Federal Communications Commission, 1919 M Street, N.W., Washington, D.C.

Field Offices of the Common Carrier Bureau, Federal Communications Commission, as listed in § 0.93 of this chapter.

Offices of the National Association of Regulatory Utility Commissioners, I.C.C. Building, 12th Street & Constitution Avenue, N.W., Washington, D.C.

(*d*) An official historic file, containing a record of all changes in the Separations Manual from 1963 forward, is maintained in the offices of the Common Carrier Bureau, Federal Communications Commission, 1919 M Street, N.W., Washington D.C., and is available for inspection at that location.

SEPARATIONS

(In the Matter of Prescription of Procedures for separating * * * plant * * * Dkt. No. 17975)

DISSENTING OPINION OF COMMISSIONER NICHOLAS JOHNSON

One of the prime responsibilities of the Federal Communications Commission is to insure that its actions serve to encourage and promote the creation of the telephone system best suited to serve all the needs of the nation. In fulfilling that responsibility the Commission must articulate the goals and purposes it seeks to serve, consider the alternatives for the achievement of those goals, and choose the most feasible alternative. I have previously indicated my concern about the lack of knowledge of the social and economic consequences of the Commission's decisions regarding telephone regulation—and even its disinclination to consider those decisions in the light of these consequences.

With regard to separations, I noted in July, 1967: "[T]he social-economic-political implications of charging costs to one telephone user rather than another are questions the Commission has been able to give less consideration than I think desirable in evaluating the alternative separations procedures available to us." *AT&T*, 9 F.C.C. 2d 30, 127 (1967). And when this rulemaking was opened I urged: "[W]e should direct the FCC staff to come forward with a well-thought out, economically rational separations analysis, not taking into account the political pressures and reactions of those whom changes would affect. Presumably there are several policy alternatives available to us—depending on the assumptions and objectives to be achieved by such a plan. Then, after the Commission had arrived at its best judgment from adequate examina-

tion of the policy matters involved, rulemaking could be proposed." *AT&T*, 11 F.C.C. 2d 493, 503 (1968). Insofar as I can discern, the past year and one half since the July 1967 decision has brought no progress in the direction I then thought to be necessary.

Jurisdictional separations is an important matter for the Commission, the Bell system, potential competitors to Bell, the states, their regulatory authorities—and the 200 million Americans who must pay the bill, and depend upon the telephone system. Separations procedures have a profound impact on dividing the costs of the Bell system, assignment of costs to users, and, ultimately, the prices users pay for the services they buy. Exchange service and long distance service may be more or less costly as a result of separations decisions—with a profound influence on the functioning of our society.

Jurisdictional separations is an inherently arbitrary undertaking: the dividing among regulatory authorities constituted along state lines of an industry that is designed as a national system, its parts interdependent and constructed to serve a whole nation. One need only look to the history of separations for illustration of the wide variation in procedures that at one time or another have constituted the conventional wisdom on this subject. The point to be drawn from this review is that justification for a particular methodology must be sought elsewhere than the pseudointellectual metaphysics of the "Charleston Plan," "Denver Plan," "Modified Phoenix," and 100% to 200% of "SLU."

Historically, the separations problem has not been addressed within the framework of public policy objectives of communications regulation, nor has it involved a thorough consideration of the consequences of alternative separations methods. Separations procedures involve arbitrary cost allocations which traditionally have been made on the basis of informal negotiations, out of the public eye, in accord with the criteria of political expediency. For Bell, separations procedures merely transfer revenues and costs from one pocket to another. If revenues appear too high in interstate services, and a rate cut seems likely, it can shift some additional costs to the interstate side of the business and make rates of return look lower. The state commissioners (many of whom must stand election) want to avoid having to raise rates to the home owners, and therefore seek to shift as much cost as possible away from their regulatory jurisdiction. The FCC wants to avoid trouble with NARUC (the association of state commissioners) and the Congress. Within this framework the Bell System has been able to exert dominant influence over the resulting separations methods because of its singular dominance in dealing with the diverse and fragmented regulatory authorities of 50 states and one federal commission. The procedures that have been undertaken and the events that have developed since the Commission's July 1967 decision, together with the new separations proposal, demonstrate a continuation of the unhappy tradition of separations "analysis." Just as in the past the separations proposal is devoid of consideration of any social or public policy objectives, and lacks a thorough analysis of the economic and social consequences of the change.

The Commission's role prior to the formal July 1967 decision and proceeding was to participate in negotiations between the parties involved—Bell, the states, and others—and then to not disapprove the separations procedures worked out by others. The procedures are embodied in a one-volume manual which consists more of exhortation than of detailed procedures. Detailed procedures are embodied in a multi-volume Bell manual prepared for its own use. Whatever one might say of the history of FCC involvement in separations, it can scarcely be accused of regulatory enthusiasm. In one instance Bell made an administrative shift in its own internal procedures which resulted in a change in separations results involving millions of dollars without changing the separations manual.[1]

I have detailed my general objections to the specific separations proposals discussed by the majority—and the concomitant adoption of the entire Separations Manual. But there are specific problems with the subscriber and interexchange plant proposals here prescribed. I do not care to elaborate on the subscriber plant formulas except to note the complete lack of rationale for the value of the ratios chosen. A substantial additional amount of cost is shifted from intrastate to interstate jurisdictions, enough to roughly balance what is to be done with interexchange plant, and to cause no embarrassment to Bell in either jurisdiction.

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[1] Gabel, Development of Separations in the Telephone Industry, p. 69–70 (1967).

For interexchange plant, the Commission action here appears to provide Bell with substantial flexibility in terms of the assignment of plant among jurisdictions and service categories (Message Toll Telephone versus private line). Further, the adopted separations procedures will be implemented by Bell via its division of revenue methodology over which the FCC cannot exercise effective control. In essence, it is adopting a separations methodology without knowing the extent to which the costs are manipulable by Bell in its implementation, or establishing effective control procedures so that the separations can be done by the Commission and not by Bell. The end result of the adoption of the proposal may be that it has moved to a point where the costs cannot be manipulated among jurisdictions by political pressures, as has been in the case in the past, but only by Bell within the adopted procedures. In either instance, public interest considerations are ignored.

The proposed change in the interexchange allocation methodology is justified by the necessity to eliminate the erratic or irrational distribution of benefits among the states. Inasmuch as the proposed plan allocates benefits among states in accordance with an arbitrary methodology dependent upon the age, density and location, of plant as well as the particular assignment for usage, it does not change the basic problem of distribution of benefits. It simply distributes them in a different arbitrary manner.

The second principal argument for changing the interexchange allocation procedures is to obtain the costs necessary for an economic comparison among the different technologies. Such an argument must be entirely fallacious. Any comparison of technologies that is undertaken after cost elements are arbitrarily allocated among jurisdictions can certainly not be very useful. And there is no indication that if and when domestic satellites become an operational part of the domestic communications system that jurisdictional separations problems of severe complexity will not be involved. The Commission's concern for Bell's ability to compete fairly is heartwarming—would that we extend it to Bell's competitors.

Finally, we are dealing with an integrated plant that can be used alternatively for a wide variety of uses. Additions to it are based upon an aggregation of interrelated factors. The particular accounting cost of a particular item of plant in a particular location need not provide any indication of the true cost of providing the service that happens to be provided over that plant at any point in time.

In summary, it is clear that the separations problem is a complex one subject to strong political forces and vested interests. Inasmuch as a state line is an artificial boundary for separating jurisdictions, the cost allocations must remain inherently arbitrary. This leaves open significant discretion in cost allocation that can be used for good or ill—that can be used to pursue the political desires of private parties and particular regulatory agencies, or that can be used to extend and broaden public interest considerations in accord with the social benefits and costs of allocating book cost to particular jurisdictions. Rather than take the broad view and use the discretion to further public interest objectives the Commission continues to prefer the more familiar, if less intelligible, path. It is content to leave primary control in the hands of the Bell System for implementation in terms of its objectives.

The net result is that the Commission's action ends up granting to Bell in 1969 what it sought unsuccessfully in 1967. Today's grant is made for reasons which clearly do not provide justification to override conclusions reached then. Moreover, the Commission opinion ignores the only substantial independent academic works in the field—both of which are strongly critical of the Commission's past failures and the specific proposals adopted here. One critic, a member of the present FCC staff, wrote two articles when he was on the staff of the Federal Power Commission in 1963.[2] The other analyst, long familiar with FCC actions in this area undertook his study as a Brookings Fellow—a study published by the Michigan State University Institute of Public Utilities.[3] He notes:

> Other criteria might involve significant redistribution of telephone costs. The telephone industry is not renowned for its risk taking. Telephone regulators are prone to follow the industry pattern. Both the industry and its regulators have been reluctant to develop comprehensive cost allocation

[2] Bushnell, "Regulatory Responsibilities in Telephone Cost Allocation," *Public Utilities Fortnightly*. Nov. 7, and Nov. 21, 1963.

[3] Gabel, Development of Separations Procedures in the Telephone Industry, p. 5, 126 (1967).

principles and aggressive pricing practices in terms of public policy objectives. Alternative separations treatment could reduce costs of local exchange service and, eventually, exchange rates, making possible a universal development of exchange services. Increased toll revenue requirements should be met not with higher rates, but by reduced unit charges.

* * * * * * *

We have concluded our chronology of telephone cost allocation methods. It should be clear that separations principles have been influenced strongly by the regulated utility, the American Telephone and Telegraph Company. It should be equally clear that the criticisms expressed herein are not primarily directed to the myths that have been generated to rationalize the "philosophy" of telephone separations. Nor is the primary question one of cost accounting method or of identifying separations principles with appropriate telephone engineering practice. Neither should separations be viewed merely as a subject of academic interest. The matter is one of sound public policy: what objectives are to be achieved and what separations methods are appropriate to achieve these objectives. Our criticism is that our public policy makers, fragmented and competitive, have been unable to arrive at a clear public direction.

It may well be that our critics are wrong—that virtue and wisdom are served by the FCC's action. But does that not impose *some* obligation upon us to explain why we think so? And for the Common Carrier Bureau to fail to even mention these major studies, much less to deal with their arguments, does strike me as unnecessarily arrogant and professionally irresponsible. I dissent.

Mr. MACDONALD. Mr. Rooney.

Mr. ROONEY. I would like to associate myself with the remarks of the distinguished chairman of this committee concerning the FCC and its present leadership. I think you are doing an outstanding job and your statement today, talking about your willingness to cooperate with the State commissioners would not necessarily necessitate the enactment of this legislation.

I hope from what you have said today you will make an extreme effort to follow through.

Yesterday, the testimony from the Commissioners representing NARUC indicated that this cooperation from the FCC is not forthcoming. I would like to say they mentioned yesterday the total of the Denver separations plan being developed between the FCC and A.T. & T. and you presented this as "take all or nothing."

Can you comment on that?

Mr. BURCH. That was long before my time.

Mr. COX. I was only forestalled from issuing a violent dissent to the Denver plan by the promise of the initiation of the formal rate proceeding which we undertook in the fall of 1965 to consider that, along with other matters, because in my judgment, the Commission had agreed to a proposal made by the telephone company which greatly benefited the States, although it did not benefit all States equally, and had thereby unfairly and unduly burdened interstate users by the shift in revenue requirements which was accomplished under that plan.

It did not seem to me that that was a rational adjustment in terms of developing technology or developing patterns of use, which I think must be the basis for action here.

We are faced with the fact that common plant is used in the conduct of a business that is regulated by different jurisdictions. We must, therefore, devise some means of separating that plant. I think it is clear that that basis must be a reasonable one. It must have

foundation. There must be some grounds for it other than the mere desire of the States to be relieved of revenue requirements.

That is a normal desire, as the chairman says. It will perhaps permit them to make rate reductions, or permit them to avoid rate increases, but we are charged with regulating that part of telephone usage which is interstate. That means that our responsibility is to the public when it is using interstate facilities.

As the chairman has pointed out, the costs of that service have been going down while the costs of building additional exchange plants and stringing additional lines in local communities have gone up. It is a question of how you are going to distribute those costs.

The Denver plan was, as I recall it, not all that unwelcome to the States. Certainly they were pleased with the ultimate outcome except, as is always the case with any separations plan, some States—because of their size, the nature of their traffic—were benefited more than others.

So some States were not as happy with the Denver plan as others. But this was certainly nothing that the FCC rammed down the States' throats.

It was a matter that in my judgment was rather hastily considered and approved by the Commission shortly after the meeting of NARUC in Denver, which is where these plans got their names.

Mr. STRASSBURG. I might add before this plan was formally adopted by the states at the annual NARUC convention in New York which took place in November of 1965, the Commission after having had more time to turn around and take a look at this plan and also after segments of the industry had more time to turn around and look at it had concerns about it, we advised the NARUC—I think Chairman Henry at that time wrote a letter to Mr. Wiggins telling him we had serious questions about this.

We went to the merits of this plan, but nevertheless we agreed to its use on an interim basis but advised the NARUC that simultaneously we were instituting a formal investigation which is the investigation that was referred to earlier, of A.T. & T. rates and earnings in order to address this issue of separations among others and to give all interested parties an opportunity to express themselves with respect to the matter of separations for the first time on a formal record.

But I think the record was clear that this was not something that was pushed by the Commission, rammed down anyone's throat by any means.

It was a matter on which we all had serious doubts. There were some substantial conceptual changes that were involved. Also you might keep in mind that at that time when this proposal was initiated truly by the company was a proposal invented by the company and it was done in response to a concern of the States that it was time to do something about separations or another change in separations because the record showed that interstate earnings were climbing at that time.

Whenever interstate earnings are climbing, that means either there is going to be a rate reduction or let's find some other rational separations method which will absorb those earnings in the form of a shift, of course, from State to interstate.

This was a plan which was devised by the company in recognition of the fact that there was a good deal of concern and eagerness on the part of the States to take some part of this red meat that was growing in the interstate jurisdiction as indicated in our report of interstate earnings.

Mr. ROONEY. You gave a supposedly pragmatic example of this $150 million decrease in rates. If it were not granted it would amount to a nickel for each telephone user throughout the country.

Mr. BURCH. I used that figure as kind of a de minimis thing. I can't stand on it.

Mr. ROONEY. The problem is the continual raising of the local rates. This is the problem. It would have been a nickel but according to Mr. Pearson yesterday, they raised rates I believe $14 million in the State of Washington.

Had that $150 million been sent back to the States, they would have had to only raise their rates $11 million.

Mr. BURCH. They would have received $3 million out of that?

Mr. ROONEY. That is what he said.

Mr. BURCH. That may well be, Congressman.

Mr. ROONEY. You talk about the cooperation with NARUC, Mr. Chairman, but why were they invited in that November or December meeting as observers, period?

Mr. BURCH. They asked to be there. First of all I was not there so I am answering this on hearsay. They had asked, I believe, to participate in the procedure.

They asked and were invited to attend as observers and as I stated, I believe to Congressman Brotzman, all the Commission had before it was the rate of return in the interstate field, not separations and not intrastate.

Had we been talking to the telephone company about separations they would have been in as parties to the action and it would have been a formal proceeding. We don't have continuous surveillance for separations where we just informally decide we are going to shift money back and forth.

That is a rulemaking proceeding and that is why this manual is available. This was adopted in January of 1969.

Mr. ROONEY. You say that interstate usage does not necessarily necessitate an increase in plant investment. I disagree with you there. If there are x thousand of numbers of interstate calls going out of a different locality because of a new industry moving in or building new houses, it is certainly going to necessitate the increase of a plant.

Mr. COX. The interstate plant goes up.

Mr. ROONEY. If I am making a call from Bethlehem, Pa., to San Francisco it is handled through the local plant.

Mr. COX. If there is a new factory built, and new residences are built to house the people who are going to work there, the local telephone plant that is built is basically to provide those people and the executives in that plant with local exchange service—with the ability to talk to other people in that community about business and personal matters.

Incidental to that, there may be an increase in interstate traffic, out of the offices of that plant and out of the homes of the workers, which will require the installation of additional interstate circuits.

The costs relative to the revenues on that interstate traffic are much lower than the costs relative to the revenues from local service. Therefore, as interstate services grow, these cost advantages seem to increase.

The advantages are greatest on those high capacity routes where the telephone company can maximize its utilization of its technology and can reduce the costs of additional circuitry the most.

As traffic is funneled through these channels, the number of calls increases, the length of calls increases, the average revenue from calls increases and we find that the telephone company, on its plant either directly installed for interstate use or assigned to it by the separations procedures, is getting too high a rate of return.

This means that those people who use interstate telephone are paying more than they need to in order to reasonably compensate the investors of the telephone company. We then reduced the rates.

We have, on five occasions since 1952, also made adjustments in separations. We are prepared to make an additional adjustment in separations if, in accordance with normal rule making proceedings, NARUC petitions us and offers us a viable, logical basis for doing this. This would be in a proceeding in which they can participate, but so will large users of interstate communications.

If we are going to say that, over the next decade, the interstate users (assuming no change in interstate volumes) are to pay $8 million more than they would otherwise pay but for the separation adjustments, then someone is bearing that cost. The large user of private interstate communications, or even of message toll service, would have a justifiable position in coming before the Commission, or going before the courts, and saying, in effect, "You are taking my property without due process. You are requiring me to pay more cost and you are making me pay for this man's service."

That is generally the sort of thing we accomplish socially through taxation, rather than through charges.

Mr. ROONEY. I have no further questions, Mr. Chairman.

Mr. MACDONALD. Mr. Brotzman.

Mr. BROTZMAN. I have just a couple of questions, Mr. Chairman.

As I reflect on this having heard the testimony yesterday and now your testimony, first of all I know it is complex because you have a jurisdictional problem basically. As I listen to the discussion here I am impressed by the fact that you might start out with a problem that is controlled by Federal jurisdiction if you are making a determination with respect to interstate rates. I can understand that it would be a Federal determination but it also affects intrastate rates because you get into the separation area and that certainly does concern and affect intrastate relationships.

In other words, on the November 5 term, NARUC and their representatives could not participate, although they came and observed, because you were determining what you believed to be strictly an interstate matter.

I think that this technically is correct but I would think you would have to admit that that particular determination does become an intrastate problem, is that not correct?

Mr. BURCH. It certainly spills over.

Mr. BROTZMAN. I guess the ultimate question is this: Is there a way to work this particular problem out under the aegis of the Commis-

sion rules? I guess you could escalate their voice to some extent by perhaps doing something under your rules of procedure.

This is what they want. They want a larger voice in making determinations. In other words, they would like to have some forum, I guess, before you transfer the $150 million which would obviously affect the interstate rates or intrastate rates depending upon where you put that $150 million or whatever the sum might be in future.

Now, are you considering a way to try to give them a larger voice in these particular matters or are you just talking about their problem?

I think this might be important to us on the committee.

Mr. BURCH. It seems to me there are two ways, one of which was attempted to be taken care of by making a rulemaking proceeding available to NARUC at their option.

Any time they want to come and petition and say we have found a new separations formula which makes sense, a new formula, they petition the Commission, we will grant a hearing, they will be parties, the telephone company would be parties, we will ultimately make the decision, grant or no grant.

The other possibility is under our act. We could convene a board which would have NARUC members, but it would be as in the case of ICC, it would simply have the dignity of an examiner's decision.

It would be an initial decision which would ultimately be reviewed and passed on by the FCC, but NARUC would sit down and participate in the original decision. I think, Congressman Brotzman, we are faced with one of those almost difficult, impasse-type situations as to who is ultimately going to make the decision.

There is again something on the face of it. It seems a little peculiar that someone who controls 30 percent of an operation by deciding whether that 30 percent ought to be 30 or 31 percent in effect decides the other 69 or 70 percent simply by that act.

I will be perfectly frank, I don't know what better way there is. I know one way and I certainly don't suggest that, and that is a U.S. telephone commission which handles State, local, the whole business.

You could do it that way and you could probably erase all of these distinctions then, you don't worry about separations.

Mr. MACDONALD. Just to keep the record straight, you are not recommending that.

Mr. BURCH. I do not recommend that at all, but in my opinion if you wanted to resolve a problem that is the way to do it but I think you are creating more problems than you are solving when you do that. I think what it boils down to is you are going to have to have some faith in the FCC or not.

If the Congress is convinced that the FCC is not going to do this job with an evenhanded administration and openminded, then probably you are going to have to change this thing by legislation.

I personally don't think that our record is that bad and neither is this a question of any self aggrandizement on the part of the FCC. This is not something we take great pleasure in. I don't think anybody is going to write me and thank me for the $150 million.

It was simply an offshoot of what we consider to be our particular job.

If we kept raising interstate rates all the time, I think we might get some letters of the other sort. In all honesty, I don't know that there is a solution.

I don't feel this bill is the solution. I think this bill logically will set up the most argumentative forum ever set up with a commitment to go in there 4 to 3 and come out with a decision.

This reminds me of the railroad retirement proceedings and——

Mr. BROTZMAN. I have never really seen this separation problem before. Does this extend to other forms of communication?

Mr. BURCH. Not in broadcast or radio because we don't regulate the rates so we don't have the problem there.

Mr. STRASSBURG. Even in telegraph we don't have it because their rates are derived predominantly from interstate service so we pretty much ignore that separations problem.

I don't think we should leave the committee with the impression that is and certainly it is not our intention that we have now put these things in the rigidity of formal proceedings here. In NARUC you want a change in rules you petition us and we hold a hearing, and so on.

We have given some order and system to what we did not have before, but the Commission has stressed time and again now, since we have gone this route it is still our intention to work in the forum that has already been established and that has been existing for some years, and informal forum where the staff experts, the guys who really do the work on both the Federal and State sides, they are the guys who sit down and generate the ideas, examine any proposals to be made and come up with the recommendations of experts, you might say, for the Commission to consider.

What I am saying is that there is a continuing apparatus for informal proceedings where we are in close contact, dealing with matters of separation with all of the State staff experts.

Mr. MACDONALD. Would you yield for an interruption?

Mr. BROTZMAN. Certainly.

Mr. MACDONALD. Mr. Strassburg, if that is the intention of the Commission I have just rechanged my mind. We won't quibble who does the most work, the Commissioners or the staff people, but I am sure the staff thinks they do and I am sure the Commissioners think they do.

In any event, the point I am making is if that working apparatus is going to be relied on just as it has been in the past then I have rechanged my mind.

I was reassured in my own mind by the chairman of the Commission's statement that he understood that in the past the thing had not really worked out as well as it perhaps could and therefore—maybe I am not paraphrasing him correctly but this is the impression I got—that there would be even more cooperation to put it that way than there has been in the past.

If there is not, then you are just going to be at loggerheads, and it does not seem to me to be a reasonable situation where the States are screaming "foul," and you people are saying "we don't want our jurisdiction infringed upon." Therefore, something new has to be done or else we are going to have this continuing quarrel between the States and the FCC.

Mr. STRASSBURG. I think Mr. Baker and I have had as much experience as anyone in this room. We know each other very well and we

have worked intimately with each other over the years. Wherever there has been something on which to get a handle, some reasonable proposal, we have never, as FCC representatives, arbitrarily turned our backs. We are constantly searching for improved methods in separation. We realize there are all sorts of separations implications for the States, and so on, but we have made an earnest effort to suggest any and all procedures, or modification of such procedures, that have been suggested so that collectively we can come to a consensus and recommend it to our superiors. This is something we can live with and would be in the best interests, and it has proven out on a number of occasions.

Mr. MACDONALD. Are those people whom we listened to yesterday not representative of the States? They are saying 180° opposite of what you say.

Mr. COX. They are saying the FCC does not lie down 100 percent of the time and agree to everything they want.

Mr. STRASSBURG. Mr. Chairman, if we had a salable, reasonable separations proposal before us, obviously the Commission would have gone with it. As the Chairman said in his statement, we had no such proposal before us then. We are working on such proposals concurrently with these hearings. We are meeting this week with the staff experts on a program of study which is well advanced. We are going places but for the first time we have a point of departure we feel is reasonable, responsible, and respectable.

Mr. MACDONALD. I am sorry for the interruption, Mr. Brotzman.

Mr. BROTZMAN. I guess those are all the questions I have.

Mr. BURCH. May I raise something right at this point, Mr. Chairman?

Mr. MACDONALD. Of course.

Mr. BURCH. When I talked to Mr. Wiggins on the telephone concurrent with the Senate hearings, I told him I was concerned with two areas. This is one of them, but I would like to point out another problem to which we are trying to address ourselves, and that is the disparity in trying to make a telephone call from San Francisco to Los Angeles, for example, for $1.75 and being able to call New York from Los Angeles for 75 cents. It seems to me there is a very difficult problem there for there is the feeling that rates should be fairly equal as far as distances are concerned. Recognizing the fact that if you call, say, from New York City, to New Jersey, you are "interstate" and a different revenue requirement applies. Nevertheless, I don't believe the average citizen is willing to sit down and examine the Federal versus the State jurisdiction.

I would like to hope that maybe out of all of this we can equalize these rates on a mileage basis. However, I do not think we could ever do it on a strict mileage basis, but it is awfully hard to explain to somebody why it costs more to call 20 miles than it costs to call 500 miles. It makes no sense to the subscribers. That is another area I talked to Mr. Wiggins and Mr. Pearson about. I don't think any of us has the answer as to how we are going to do it, but we are going to take a shot at it.

Mr. COX. On Congressman Brotzman's questions about NARUC's participation, as the chairman pointed out, they can participate not only by filing comments and reply comments in the rulemaking, but

could also participate in a joint board under our existing statutory provisions. And if in either of those proceedings they don't like the result, they can then appeal our decision to the courts and go on from there. So they are entitled to participate in the proceedings. It is true they do not participate in the final judgment.

As I understand it, when we make a judgment as to how we will separate telephone plant for interstate purposes, we don't make a judgment that is automatically binding on the States. That is a judgment binding on us. But a problem arises if the States do not go along with that judgment; the result would be sheer chaos, because if you had 51 jurisdictions separating plant on different bases, either the telephone company would be getting return from two different jurisdictions on the same plan and would be overcompensated, or it would have some plant that it was getting no compensation on from either jurisdiction and its shareholders would be undercompensated.

That is why the cooperative procedures arose in the first place, out of sheer necessity to get some order in what would otherwise have been an impossible situation; to get uniformity in the handling of these matters so that there was some fairness for all concerned.

Mr. MACDONALD. Mr. Tiernan.

Mr. TIERNAN. Thank you, Mr. Chairman.

Mr. Burch and Commissioner Cox, I am sorry I was not able to be here at the presentation of your statement. I was at an executive session of another committee meeting.

I know some of my other colleagues have expressed favorable reaction to the ways in which the Commission has been moving. I know there were lots of things on the fire when you took over as Chairman. I am glad to see you have included substantial amounts in fees in the budget and also I understand you have now issued proposed rule changes.

What I am really concerned about is whether the additional revenue that will be received from the Commission by these fees is going to be placed back with the Commission for purposes of strengthening your staff in the areas of investigation and in the area of renewal and licenses.

Mr. BURCH. No, sir; it goes directly to the Treasury.

Mr. TIERNAN. Second, you know legislation was put in before in this Congress by myself with regard to the fees. Would you have any objection to the committee having you before us to discuss some of this legislation while you have the notice of rulemaking pending?

Mr. BURCH. No objection whatsoever.

Mr. TIERNAN. On page 12 of your statement you make reference to the present law that allows you, as you say, the procedures for a Joint Board which has long been utilized. Can you tell me when the Joint Board was last utilized?

Mr. BURCH. Are you talking about the FCC?

Mr. TIERNAN. Yes, sir.

Mr. STRASSBURG. We have never used the Joint Board because we have used the informal procedure.

Mr. TIERNAN. But the law does provide for the Joint Board so you feel by cooperative proceedings you do not need to have a Joint Board?

Mr. BURCH. That is my understanding.

Also, the procedure has long been utilized by the Interstate Commerce Commission.

Mr. TIERNAN. You have the same authority under section 410. I know the ICC has used it and yet the FCC has not.

Mr. STRASSBURG. Perhaps one observation that may be relevant, Mr. Tiernan, is in the ICC you are dealing with motor carrier routes very often and you are dealing with other transportation routes whch involve just a few States. It is easy to convene a Joint Board under this pattern of a representative from each of the States involved, but here we are dealing with all jurisdictions.

Mr. TIERNAN. When you have this cooperative representation, whom do you have there? Don't you feel with a representative group more or less appointed by NARUC you have what we are talking about enacting and what you say is practiced by the legislative act?

Mr. STRASSBURG. We deal with a representative group of experts from the States who in turn report to a communications committee of the NARUC who in turn report to a larger executive committee of the NARUC and who in turn report to the annual convention of the NARUC. So, the decisions——

Mr. TIERNAN. To simplify it, are we not just saying by legislative act there shall be three committees appointed from the national group that represents all of the Commissioners in the United States and do away with all of this question about having too many States and also relieve you of the burden of maybe taking and implementing section 410 and having a Joint Board appointed? It seems to me that you would not have any objection to that.

Mr. BURCH. That has not been one of our big burdens up to now to be relieved of. But for the reasons I state in my statement, I cannot agree with your position on it.

Mr. TIERNAN. That is why I don't understand why you cite to the subcommittee that the ICC has long utilized that procedure. You had the authority to utilize it but you have never utilized it because you say you get better results from the cooperation. Whereas, on the other hand, the people who came in and represented the Commissioners yesterday testified they were not getting cooperation.

Mr. STRASSBURG. Under 410 of the act, we would have to invite——

Mr. TIERNAN. It says the Joint Board can be appointed. The Governor can appoint a Commissioner to serve.

Mr. Cox. When they make a separations change, this does not affect just the Southeast or New England it affects everyone.

Mr. TIERNAN. This legislation provides only three would be appointed to represent all of the States involved, so that would relieve you of the necessity of appointing only one from every State involved.

Mr. Cox. We think it would be difficult for NARUC to find such a Commissioner.

Mr. TIERNAN. I asked them specifically yesterday. In fact, I think I might have irritated them a little bit when I suggested they might have States that would have different interests. If they took a Commissioner from California and a Commissioner from Utah, the interests of those two Commissioners might not be the same.

Mr. Cox. Our experience has been that even when we worked out separations arrangements, starting with the staff experts and then working up through the Commissioners, at the individual State level

and the Federal level, and they went up through their committees and to the final committee in convention in which all of the Commissioners were involved, there were some disagreements. Some States were affected more than others, which is almost inevitable with a single formula, and, therefore, they argued for a different approach and they were ground out.

I think the thing basically gets back——

Mr. TIERNAN. Excuse me. May I interrupt you there. When you say it was ground out, suppose this committee made a change in the legislation saying two FCC Commissioners and two appointed from NARUC and someone appointed by the President, such as a representative of consumers. Then you would not have this loggerhead and you might take the chairman's suggestion that we set up a National Board for telephone rates?

Mr. BURCH. You would in effect have the one man deciding the entire question for the entire United States.

Mr. COX. And unless he were drawn from the ranks of former regulators, he would know virtually nothing about this—and I can assure you that separations problems have been the most complex I have faced as a Commissioner.

Mr. TIERNAN. So, as we said, the Commission by that board would have the result of an examiner and not just a simple majority overruling but a majority plus one of the FCC Commissioners overruling that determination? Would that be possible? You might want to think about that.

Let me ask you this, Mr. Chairman. On page 8 you say you are now engaged in cooperative separations studies with the States. What results can we expect from this study?

Mr. BURCH. I can't answer that.

Mr. TIERNAN. When would you have the results?

Mr. BURCH. I suppose we would have something more definitive by June.

Mr. TIERNAN. By June of this year the results would be obtained?

Mr. BURCH. These efforts have only been going on since December.

Mr. TIERNAN. Do you have a specific amount of money that would be affected by these separations?

Mr. BURCH. There is an estimate on what the States are requesting.

Mr. STRASSBURG. The States made one proposal which was covered by their petition to the FCC for a change in the rules which proposal is not really being pursued at this time, and that would amount to something like a $350 million shift in revenue requirements. It would reduce interstate earnings as if you had a rate reduction of about $350 million. But there are other alternatives that are seriously being considered, and I think they have to be considered. We don't know what the dollar effects will be. We want to decide some principles rather than looking to the end result and how do we get there. We have some general idea of what the magnitude of the dollars is, but it will depend upon the refinements yet to be made as to what the precise amounts are going to look like.

Mr. TIERNAN. Commissioner Cox, you indicated there is some questions of the constitutionality in the shifting of the cost. You say we leave the interstate rates high on that new plant Mr. Rooney suggested, a question of whether he could go into court and contest that rate on the basis he was being unduly taxed. If we spelled out in

this act a policy of Congress that in taking actions in any such proceedings which would be maybe on the question of imposing a burden on the interstate tax that was not directly related to the cost of the service rendered, that is what we would be doing in effect, and said that you should take these into account in order to promote the health and safety and the welfare and the security of the people of the United States, do you think that would meet the test of constitutionality?

Mr. Cox. If you are trying to bring this within some police power jurisdiction, I think it would depend upon the weight of your legislative record, showing in fact that the subsidization of exchange service was going to significantly promote normal police concerns.

Mr. TIERNAN. Don't you think we have a concern as Members of Congress, as individual constituents of ours who say because their level of income is less than $3,000, less than $4,000, less than $5,000 a year they are not able to obtain the telephone service in the community because the rates are so hard they can't afford it? Don't you think that is a purpose for the safety and welfare of the people?

Mr. Cox. That is the problem, and the Chairman referred a little earlier to the experimentation by the Maryland commission, which is proposing a reduced rate, limited service which would give you a telephone in the house or apartment so you could call the police or a doctor or call about a job, and you would get a reduced rate because you were going to make limited use of it. You would not use it as my teenage son does, to call his friends whenever the notion strikes him.

Mr. TIERNAN. The average plant is only used one-half hour, or is idle 23½ hours.

Mr. Cox. It is used half an hour and is idle 23½ hours.

Mr. TIERNAN. The point is the number of Americans who do not have the money to have an instrument in their homes should be of interest to the Congress and should be based on the safety and national welfare and the national security that we set as a policy that the intrastate rates should be reduced and the interstate rates would be placed as an additional burden.

Mr. Cox. I think that would be a possible approach, depending on the finding you made as to the extent of this problem and the reasonable regulation of it.

Mr. TIERNAN. Are not the Commissioners saying to us that the national rates will go down but in the States we have to increase the rates to pay for inflation, cost of plant and putting in the additional wire, and the technology has not been able to decrease the overall costs in the States?

Mr. Cox. They are faced with the problem that the consumers of interstate telephone service are pleased because costs have gone down when the prices of almost everything else are going up. But the users of local exchange service are unhappy because their local telephone service is going up just as the cost of groceries, the cost of medical care, the cost of housing is going up. The only out here is that, unlike the case when you are challenged by someone who is unhappy with inflation and the cost of living generally, there appears to be over here a source for generating revenues which can be tapped in perhaps a less painful way; that is, you simply forgo reducing the cost of a transcontinental call by 35 cents and you do give the State of Washington a net of $3 million in reduced revenue requirements.

Mr. TIERNAN. One further thing. One of the Commissioners here yesterday said he is hard put to answer the person who asks why it costs $1.50 to make a call within Rhode Island, and I received a letter from a lady who asked why she has to pay $1.50 to call within the State of Rhode Island and only 75 cents to call the west coast. The problem is when you announce these reductions in telephone rates, then the advertisers come on television and tell you that you can call California for 50 cents or 75 cents, while at the same time the people at home are hearing about a 15-percent increase in their telephone bill. They do not understand what is going on and they are getting it both ways.

Mr. MACDONALD. The figures given yesterday by the Commissioners when we were discussing the telephone instrument were 23½ hours a day idle and one-half hour of use. Where do those figures come from? Did they come from the FCC?

Mr. COX. I think they come from the telephone company, basically. This is an average. Some telephones in business offices are used much more than that.

Mr. MACDONALD. They used figures with such authority you start to believe them.

Mr. STRASSBURG. On a nationwide average, it is pretty reliable.

Mr. MACDONALD. One-half hour a day, and this includes business.

Mr. COX. They are an average, yes.

Mr. MACDONALD. This includes all telephones in the United States?

Mr. STRASSBURG. All subscriber telephones and lines, just that limited amount per day.

Mr. MACDONALD. Is anyone willing to say that under oath?

Mr. COX. We wouldn't, because we are taking it on the word of the company, but I am sure the telephone company could produce people who have a factual basis for that statement.

Mr. BURCH. If you would like some data on it, I would be happy to get it.

Mr. MACDONALD. I was just curious.

Mr. STRASSBURG. It is true to a much lesser extent with respect to long-distance lines, the circuitry itself, but there are hours of the day when thousands and thousands of circuits are lying idle and they are not recovering any costs which are operating at the same time. That is why the Commission in many of the rate reductions we have made we have always tried to steer the company toward making and inducing more use of that plant during those offpeak hours or those idle hours.

Mr. COX. It is there where you get the most extreme contrast, Congressman Tiernan.

Mr. STRASSBURG. This is where it does become attractive costwise to the people who had not been able to use it previously.

Mr. MACDONALD. If there is nothing further, thank you very much, gentlemen, and the hearings are closed.

(The following statements and letters were received for the record:)

STATEMENT OF HON. JOHN S. WOLD, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF WYOMING

Mr. Chairman, the Public Service Commission of Wyoming has asked my assistance in regard to your committee's hearings on H.R. 12150—a bill proposing the Federal-State Communications Joint Board.

I ask that the statement by the commission in support of the bill be inserted in the record of the hearing.

STATEMENT OF THE WYOMING PUBLIC SERVICE COMMISSION

H.R. 12150 will provide a necessary and properly constituted body to evaluate and act upon communications matters affecting intrastate and interstate users. The best interest of the people of Wyoming were not considered and cannot be served by the recent decision of the FCC to apply $237 million dollars in excess toll earnings of the Bell Telephone Companies only to the benefit of interstate toll users. This action disregards earlier cooperative action between the FCC and the various states' regulatory commissions which allowed benefits to be passed on to intrastate users.

This application of the excess earnings was a result of negotiations between the Federal Communications Commission and the Bell Companies to the exclusion of state regulatory bodies whose interest is vital and indispensable. This interest is illustrated by the fact that sixteen Bell System Companies have applications before state commissions requesting rate increases which total over *one-half billion* dollars.

The Wyoming Commission (and those of other states) has over the years worked diligently to eliminate a disparity in intrastate and interstate toll rates through the separations allocations and every means possible. In the past the FCC, realizing that without the intrastate systems there would be no interstate toll network, worked in cooperation with the state commissions in allowing a book shift of *intrastate* plant to interstate operations when an interstate toll rate reduction was imminent. Our state has required rate reductions each time such a shift was accomplished, with the rate reductions almost totally being applied to decrease the disparity between interstate and intrastate toll rates for the same distance called. The reductions required by the Wyoming Commission resulting from the cooperative state-FCC procedures were as follows:

May, 1962	$251,000
November, 1964	34,000
February, 1965	28,500
August, 1966	167,700
November, 1968	109,000
June, 1969	742,200
Total	1,332,400

The substantial progress made by Wyoming and other states toward reducing intrastate toll rates to the level of interstate rates will be all but lost through the agreement by the FCC to allow the Bell System Companies interstate toll reductions without any consideration to the necessary coinciding allocation of property and related expenses of the Bell System Companies to the interstate system.

The inequity arises out of the fact that the FCC determined by its own separations procedures what portion of the total toll plant of the Bell System Companies will be interstate, with the remainder being loaded on *intrastate* operations. By controlling this key aspect and crediting the interstate toll operations with virtually all the benefits of technological improvements, interstate operations have consistently shown high and improving revenues, which when applied to the FCC determined rate base support rate decreases; however, we maintain that these decreases should not be applied to interstate operations solely.

Respectfully,

WALTER W. HUDSON, *Chairman.*
PAUL T. LIAMOS, Jr., *Commissioner.*
ZAN LEWIS, *Commissioner.*

CONGRESS OF THE UNITED STATES,
HOUSE OF REPRESENTATIVES,
Washington, D.C., February 24, 1970.

Hon. TORBERT H. MACDONALD,
Chairman, Communications and Power Subcommittee, Rayburn House Office Building, Washington, D.C.

DEAR TORBERT: On behalf of the Florida Public Service Commission I would like to offer my sincere support of H.R. 12150, a bill proposing the Federal-State Communications Joint Board Act of 1969. I feel that the Joint-Board would give

the State Commissions a stronger position protecting the interest of the public at State level and I am, therefore, in full support of the passage of H.R. 12150.

With kindest regards, I am,

Sincerely,

Don

DON FUQUA, *Member of Congress.*

STATE OF SOUTH DAKOTA,
Pierre, S. Dak., March 19, 1970.

Chairman HARLEY O. STAGGERS,
House Committee on Interstate and Foreign Commerce,
Washington, D.C.

DEAR CHAIRMAN STAGGERS: I strongly urge you to support the Federal-State Communications Joint Board Act. The enactment of this legislation, by giving the State regulatory commissions a minority vote, would provide a balanced approach for future development of fair and equitable telephone separations procedures which would result in relatively lower rates for the millions of users of local telephone service across the nation.

Regulatory jurisdiction over the telephone industry is divided between the FCC and the State commissions pursuant to the Communications Act of 1934. In terms of numbers of calls, the FCC today regulates approximately 2½ billion interstate long distance toll calls a year, while the State commissions regulate approximately 147 billion intrastate toll and local exchange calls a year. In terms of plant investment, the FCC exercises jurisdiction over approximately 25 per cent of Bell System plant, while the State commissions exercise jurisdiction over the remaining 75 per cent and over virtually all of the plant of the non-Bell telephone companies.

The FCC has always controlled the prescription of separations procedures, and it has never prescribed equitable ones because it has consistently refused to allocate a fair amount of the cost providing local telephone service to the users of interstate toll service. Local telephone service is an integral and vital part of the national and international toll network. The local telephone plant is available as much for interstate long distance calls as it is for local use. Without local telephone service the toll network would be worthless.

The FCC's proclivity for inequitable separations procedures which favor its narrow regulatory interests is magnified by technological advances in the telephone industry which result in reduced costs for long distance service and increased costs for local service. Microwave transmission and coaxial cable, as a result of high volume circuit capacity, has greatly reduced the cost of long distance circuits. The volume of calls that can possibly be handled by coaxial cable has increased from 500 to 32,000 in the last ten years, and this capacity is anticipated to be increased to 100,000 calls in the near future. During the same period, the cost of installing coaxial cable has reduced from about $100 to less than $5 per channel mile. Local service has not enjoyed the benefits of technology, and the costs of providing local service are steadily rising due to inflation and the higher service standards demanded by the public.

The FCC's unreasonable telephone separations procedures have now resulted in the ridiculous situation of interstate rates decreasing at the same time interstate toll rates in the amount of $237 million, while the same Bell System interestate toll rates in the amount of $237 million, while the same Bell System has instituted proceedings now pending before 13 State commissions to seek rate increases totaling $599 million. Also, since January 1, 1969, 12 other State commissions have been forced to grant rate increases to Bell System companies totaling $106.5 million. Our own South Dakota State Public Utilities Commission was forced to grant a rate increase to the Northwestern Bell Telephone Company to provide additional gross revenues of approximately $1,213,987 effective January 1, 1969. These figures, of course, do not reflect the rate increases now being sought by the non-Bell telephone companies who are also adversely affected by unfair separations procedures. In South Dakota, numerous small independent and cooperative telephone companies have been seeking rate increases, and the pattern is expected to grow more prevalent in the next few years.

The fact that interstate long distance telephone rates are decreasing at the same time local service rates are increasing should create questions about the equitableness of the present separations procedures. However, the fact that in certain cases intrastate long distance rates already exceed interstate long distance rates is indeed difficult to explain.

The public interest cannot be properly served by fixing telephone rates that discriminate in favor of a limited number of affluent long distance users and against the more numerous and less affluent local callers. I am therefore requesting your assistance in the passage of S1917 and HB12150, duplicate bills proposing the Federal-State Communications Joint Board Act.

Sincerely yours,

FRANK L. FARRAR, *Governor.*

(The subcommittee was adjourned at 11:55 a.m., to reconvene subject to the call of the Chair.)

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