Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of	)	
	)	
GTE Telephone Operating Companies	)	Transmittal Nos. 874, 909, 918
	)	
Revisions to Tariff F.C.C. No. 1	)	CC Docket No. 94-81

SUPPLEMENTAL DIRECT CASE OF GTE

GTE Service Corporation and its affiliated
domestic telephone operating companies

John F. Raposa, HQE03J27
GTE Service Corporation
P.O. Box 152092
Irving, TX 75015-2092
(214) 718-6969

Gail L. Polivy
1850 M Street, N.W.
Suite 1200
Washington, DC 20036
(202) 463-5214

August 28, 1995

Their Attorneys

TABLE OF CONTENTS

SUMMARY

Rates and charges applicable to the provision of video channel services in Cerritos, California, as submitted under Transmittal Nos. 874, 909, and 918, are reasonable, cost-based, and nondiscriminatory. GTECA has developed charges for the lease of capacity on the Cerritos network based on the standard methodology for establishing interstate access rates and the Commission's authorized rate of return for interstate services (11.25%). The investment transfer and pricing methodologies employed by GTECA under these Transmittals will ensure that the costs of providing the underlying video channel service will be fully recovered from the users of the network. Tariff conditions filed under these Transmittals are also nondiscriminatory since all users of the Cerritos network have been charged on a comparable basis.

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

RECEIVED
AUG 2 3 1995
FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

In the Matter of	)	
	)	
GTE Telephone Operating Companies	)	Transmittal Nos. 874, 909, 918
	)	
Revisions to Tariff F.C.C. No. 1	)	CC Docket No. 94-81

SUPPLEMENTAL DIRECT CASE OF GTE

The GTE Telephone Operating Companies, on behalf of GTE California Incorporated (GTECA) and GTE Service Corporation (Service Corp.), respectfully submit this Supplemental Direct Case in response to the Common Carrier Bureau's Supplemental Designation Order, DA 95-1769, released August, 14, 1995 (*Supplemental Designation Order*). For the reasons stated herein, the Commission should allow GTECA's video channel service tariff for Cerritos, California to remain in effect as originally filed and terminate this investigation forthwith.

I. INTRODUCTION AND BACKGROUND.

On April 22, 1994, GTECA submitted revisions to its interstate access tariff under Transmittal Nos. 873 and 874 to establish video channel service in the City of Cerritos, California. Tariff material submitted under Transmittal No. 873 established terms and conditions applicable to Apollo Cablevision, Inc. (Apollo) for its use of 39 channels of GTECA's 78 channel broadband coaxial network in Cerritos. Transmittal No. 874 provided terms and conditions for channel service applicable to Service Corp. for the remaining 39 channels. Service Corp. currently provides a pay-per-view movie service, "Center Screen", and "GTE Main Street", an enhanced interactive service, to the residents of Cerritos.

In an Order released July 14, 1994, the Bureau allowed Transmittal No. 873 to become effective, subject to an accounting order and an investigation into a number of issues raised by the filing. *In re GTE Telephone Operating Companies*, 9 FCC Rcd 3613 (1994) (*Cerritos Tariff Order*).[1] However, the Bureau rejected tariff material applicable to Service Corp. filed under Transmittal No. 874. *Id.* The United States Court of Appeals for the Ninth Circuit subsequently was granted a stay of the *Cerritos Tariff Order* to the extent that it rejected Transmittal No. 874. *GTE California Incorporated v. FCC*, No. 93-70924, Order (9th Cir., filed Sept. 7, 1994). In accordance with the Court's stay order, on September 9, 1995, GTECA reinstated the rejected tariff material originally submitted under Transmittal No. 874 in a filing made under Transmittal No. 909. The Bureau suspended this filing for one day and included Transmittal No. 909 in the pending investigation of Transmittal No. 873. *In re GTE Telephone Operating Companies,* 9 FCC Rcd 5229 (1994) (*Transmittal No. 909 Suspension Order*).

In the instant *Supplemental Designation Order*, the Bureau designates one additional issue for investigation that was not addressed in the *Cerritos Tariff Order*.

---

[1] In response to the *Cerritos Tariff Order*, GTE filed a Direct Case on August 15, 1994 in support of tariff provisions related to the provision of service to Apollo Cablevision. Apollo, the National Cable Television Association (NCTA) and the California Cable Television Association (CCTA) filed briefs on August 15, 1994. GTE filed Comments on these briefs on September 15, 1995. Apollo filed an Opposition to GTE's Direct Case, MCI filed Comments and NCTA/CCTA filed a Reply Brief on September 15, 1995. Apollo filed Reply Comments on September 30, 1995. GTE filed a Rebuttal and Reply Comments also on September 30, 1995.

Specifically, the Bureau asks whether the rates and terms proposed under Transmittal No. 909 are reasonable. In posing this question, the Bureau directs GTECA to discuss whether the computations used to develop rates under Transmittal No. 909, to the extent they are based on an 18.9% interest rate, are reasonable. GTECA is also directed to show whether there is any disparity between the rates filed under Transmittal No. 873, applicable to Apollo, and those filed under Transmittal No. 909 for Service Corp. *Supplemental Designation Order*, at ¶ 27.

II. TARIFFED CHARGES FILED UNDER TRANSMITTAL NO. 909 ARE LAWFUL AND NONDISCRIMINATORY.

The tariff charges filed under Transmittal No. 909 are reasonable, cost-based, and nondiscriminatory. *First*, the monthly rate filed under Transmittal No. 909 recovers the costs of the underlying video channel service provided to Service Corp. and was computed in accordance with Section 61.38 of the Commission's Rules, 47 C.F.R. § 61.38. *Second*, contrary to the Bureau's apparent misapprehension, rates for Service Corp. submitted under Transmittal No. 909 were not calculated using an 18.9% interest rate, but instead were derived in accordance with the standard pricing methodology and the Commission's authorized 11.25% rate of return used to establish prices for all regulated interstate services. *Third*, charges established under Transmittal No. 909 are nondiscriminatory since they are comparable to those which have been assessed to the other user of GTECA's Cerritos video network, Apollo.

In the following sections, GTE provides a detailed explanation of (1) how the charges contained in the original lease agreements were calculated, (2) the conversion of the Cerritos private lease arrangements to tariff, (3) the derivation of charges assessed to Service Corp. and (4) how the charges paid by Service Corp. relate to those paid by Apollo.

A. Development of Original Lease Charges.

In 1991, GTECA entered into private contractual arrangements with Apollo and Service Corp. for the lease of capacity on the Cerritos broadband network.[2] GTECA's original investment associated with the construction of the network, including headend and coaxial cable facilities, as well as customer premises equipment (*i.e.*, set top boxes), amounted to $12,272,887. Both customers leased 39 channels of the 78 channel network, respectively; therefore, investment related to the construction of the underlying coaxial network and headend equipment was split evenly between the two lessees for purposes of determining monthly lease obligations. In addition, investment used to calculate the original lease charges for Service Corp. contained certain equipment costs and fees which GTECA incurred at the special request of Service Corp.

After incorporating a number of minor credits and pre-payments, GTECA attributed $5,685,500 of the total investment to Apollo's use of the network and $6,284,000 was associated with investment used to provide service to Service Corp. Monthly lease charges for both Apollo and Service Corp. were computed using these investment amounts and an 18.9% cost of capital amortized over 15 years (the term of

---

2 Although video channel service has typically been provided by LECs to cable operators under tariff, the Commission conditioned GTECA's authority to operate in Cerritos on the requirement that all costs incurred in Cerritos be booked to non-regulated accounts. *In re General Telephone Company of California*, 4 FCC Rcd 5693, 5701 (¶ 61) (1989).

both Lease Agreements). The 18.9% factor represented a below-the-line (*i.e.*, nonregulated), pre-tax cost of capital which GTECA believed would ensure a reasonable after-tax return on its investment.[3] This computation resulted in a monthly charge of $95,265 for Apollo and $105,294 for Service Corp. *See* Exhibit A, "Original Contract Calculation".[4]

Beginning in May, 1991, both customers began remittance of the monthly payments to GTECA. In January, 1992, Apollo exercised a provision in its agreement that allowed for the prepayment of the remainder of its 15 year lease. This prepayment, $5,672,055.72, represented Apollo's principal balance as of January 17, 1992.[5] By paying the principal balance, Apollo avoided any future payments of the 18.9% cost of capital component inherent in the lease charge for the remainder of the 15 year lease term.

B. Conversion of Lease Agreements to Tariff.

With expiration of the Commission's "good cause" waiver on July 17, 1995, GTECA converted the Lease Agreements of Apollo and Service Corp. to a tariffed

---

3 Both customers, Apollo and Service Corp., agreed to the use of this cost of capital component in the calculation of their monthly payments by execution of the respective Lease Agreements.

4 These initial lease charges included all investment associated with transmission equipment, coaxial plant, and CPE. If CPE-related costs were excluded from the original lease calculation, the monthly payments would have amounted to $82,177 for Service Corp. and $81,764 for Apollo. *See* Exhibit A.

5 The prepayment equaled the principal balance only and did not reflect any interest charges. GTECA continues to amortize this prepaid amount on its books until the expiration of the 15 year period.

arrangement in accordance with the Act and the Commission's Rules. *See* Transmittal Nos. 873 and 874. Contemporaneously, GTECA requested permission to transfer the net book investment associated with the Cerritos coaxial network, excluding CPE, into regulated accounts.[6] *See* GTE Petition for Waiver, June 13, 1994.

Charges filed under Transmittal No. 874 for the provision of 39 channels to Service Corp., and reinstated under Transmittal No. 909, were based on the regulated net book investment value as of July 1, 1994 that GTECA proposed to transfer to regulated accounts. *See, e.g.*, Petition for Waiver; Transmittal No. 874, Description and Justification, at Exhibit A; Direct Case, August 15, 1994, at Attachment A.[7] Given that video channel service would be made available to Service Corp. under tariff, versus contract, GTECA developed charges under Transmittal Nos. 874 and 909 based upon the standard methodology for establishing interstate access rates and the Commission's authorized rate of return for LEC interstate services (11.25%), rather than the 18.9% factor employed in the private contractual agreements. Pricing in accordance with these parameters would ensure that the total regulated costs (*i.e.*,

---

6 As GTECA explained in its Direct Case, filed August 15, 1994 (at 8), only the usable portion of the circuit equipment, coaxial cable and conduit investment will be transferred above-the-line. Prior to transferring any investment to regulated accounts, GTECA will execute a write-off of impaired assets and make other accounting adjustments reflecting the assumption of ongoing maintenance responsibilities by GTECA.

7 GTECA filed terms and conditions applicable to the provision of 39 channels of the video channel service offering to Apollo under Transmittal No. 873. Because Apollo had prepaid its 15 year lease, no monthly lease charges were filed relative to the 39 channels provided to Apollo. Rather, Transmittal No. 873 reflected a "single payment" option equal to the monthly amortization of Apollo's prepayment balance as of July 1, 1994, excluding the portion of the payment representing non-regulated (CPE) investment.

transferred regulated investment plus ongoing expenses) associated with the provision of 39 channels would be fully recovered from Service Corp.

C. Calculation of Rates Under Transmittal Nos. 874 and 909.

The calculation of charges assessed to Service Corp. was illustrated in Exhibit B under Transmittal No. 874 and is also shown in Exhibit A to this Supplemental Direct Case. The total adjusted netbook value of GTECA's Cerritos video network, as of July 1, 1994, that GTECA proposes to transfer to regulated accounts is equally attributable to both Service Corp. and Apollo's use since that amount represents the headend and coaxial network facilities which are equally shared by the two customers.[8] Thus, one-half of the total net book investment value was used to calculate charges for Service Corp. *See* Exhibit A.

Monthly expenses associated with this investment amount, and used to develop the charge applicable to Service Corp., were derived in the same manner in which costs and rates are calculated for all interstate services. The development of this charge was presented in cost support data submitted under Transmittal No. 874 in compliance with Section 61.38 of the Commission's Rules.[9] These expense amounts, also shown in Exhibit A, include the following:

---

[8] The additional charges attributable to Service Corp. under the Lease Agreements related to CPE, not regulated facilities or amounts that will be written off as discussed in footnote 6.

[9] Under Transmittal No. 874, GTECA calculated a monthly cost based on the total costs of the network and divided this result by 2 to arrive at a monthly charge for Service Corp. *See* Transmittal No. 874, Exhibit B.

Depreciation- Annual depreciation expense was based on book value and standard depreciation rates for GTECA associated with buildings, circuit, and outside plant investment.

Return - As illustrated on the attached "Return and Income Tax Calculation" workpapers (*See*, Exhibit B), an "after tax" return is calculated for each year according to the revenue life for the service using 11.25% as the allowed rate of return. A simple average of the sum of each year's return was then calculated and used as the average return.

Federal and State Income Tax - Federal and State taxes were calculated in the same manner as described above for return, using the annual return and statutory income tax factors. These calculations are presented in Exhibit B.

Annual Non-Recoverable Cost - Reflects a portion of the investment and labor costs which must be recovered over the revenue life. The Non-Recoverable costs were derived by computing an annuity for the present value of capital investment plus income tax effects, based on the revenue life of the service and a discount rate equal to the authorized rate of return for local exchange carriers (11.25%). Depreciation, return, and tax expenses were then subtracted from the annuity amount to arrive at the total non-recoverable cost.

Administration - Annual general and administrative expenses based on GTE annual charge studies.

Property Tax - Property tax expense.

Maintenance - Annual estimated maintenance expense for the Cerritos coaxial network and circuit equipment.[10]

D. Comparison of Charges Assessed to Service Corp. and Apollo.

GTE proposes to transfer to regulated accounts only that investment which is fully recoverable from both Apollo's original prepayment amount and the charges assessed to Service Corp. as established under Transmittal No. 909. As Exhibit A demonstrates, a monthly payment value of $81,764 will ensure adequate recovery of

---

[10] Upon with the effective date of the Cerritos channel service tariff, GTECA assumed maintenance responsibilities for the Cerritos network.

the underlying costs of providing one-half of the network's total channels to Service Corp.

In addition, the investment transfer and pricing methodology utilized by GTECA results in charges applicable to Service Corp. that equal the monthly payment that Apollo would have paid had it not prepaid its original Lease Agreement in 1992. If CPE-related (*i.e.*, non-regulated) investment is removed from the investment amounts allocated to Apollo in the original lease calculation, the portion of Apollo's monthly charge that would have been attributable to the use of the headend and coaxial network itself would equal $81,764. *See* Exhibit A.[11] Therefore, GTECA properly priced the video channel service offering to Service Corp. in a way that avoids any disparity in charges between the two customers of the Cerritos broadband network.

III. CONCLUSION.

Charges established under Transmittal No. 909 are lawful in that they recover costs incurred by GTECA in its provision of 39 channels of the video channel service network in Cerritos to Service Corp. and are based on the Commission's 11.25% authorized rate of return for LEC interstate services. Further, Transmittal No. 909 does not discriminate against the other customer of the Cerritos video channel service network, Apollo. Charges associated with the tariffed (*i.e.*, regulated) portion of the network which are now being paid by Service Corp. to GTECA are equal to the monthly payments that Apollo previously paid and would continue to be paying had it not

---

[11] Of the original investment amount allocated to Apollo, approximately $13,500/month, or about 14.2%, was associated with subscriber set-top equipment.

exercised its prepayment option in 1992. As tariff charges filed under Transmittal No. 909 are lawful and nondiscriminatory, the Bureau should allow GTECA's video channel service tariff for Cerritos, California to remain in effect as originally filed and terminate this investigation forthwith.

Respectfully submitted,

GTE Service Corporation and its affiliated domestic telephone operating companies

John F. Raposa, HQE03J27
GTE Service Corporation
P.O. Box 152092
Irving, TX 75015-2092
(214) 718-6969

By Gail Polivy
Gail L. Polivy
1850 M Street, N.W.
Suite 1200
Washington, DC 20036
(202) 463-5214

August 28, 1995

Their Attorneys

GTE CALIFORNIA
SUPPLEMENTAL DIRECT CASE
EXHIBIT A

	ORIGINAL CONTRACT CALCULATION		
	TOTAL	SVC CORP	APOLLO
Original Investment	$11,969,500	$6,284,000	$5,685,500
Periods	180	180	180
Annual %	18.90%	18.90%	18.90%
System Price	$200,559	$105,294	$95,265
Price excluding CPE	$163,941	$82,177	$81,764

	TARIFF CALCULATION		
	% Of Adj	TOTAL	SVC CORP
Regulated Netbook		$6,853,527.00	
Adjustments		$904,543.54	
Adj Netbook		$5,948,983.46	$2,974,491.73
Depreciation	4.85%	$24,039.36	$12,019.68
Return	5.63%	$27,885.86	$13,942.93
Federal & State Income Tax	3.61%	$17,874.84	$8,937.42
Nonrecoverable	5.11%	$25,315.34	$12,657.67
Administration	9.33%	$46,269.98	$23,134.99
Property Tax	0.52%	$2,559.28	$1,279.64
Maintenance	3.95%	$19,583.34	$9,791.67
Monthly Recurring Charge	32.99%	$163,528.00	$81,764.00

EXHIBIT B

RETURN AND INCOME TAX CALCULATIONS (11.25% RATE OF RETURN)
Total System

SERVICE: CERRITOS VIDEO CHANNEL SERVICE
RATE ELEMENT: ANNUAL COSTS

STATE: CALIFORNIA

		REVENUE LIFE	AVERAGE PER YEAR
TOTAL MATERIAL	$5,948,983.46		
LESS: NET SALVAGE	$0.00		
NET MATERIAL COST	$5,948,983.46		
TOTAL ENGIN & INST	0.00		
TOTAL	$5,948,983.46	12	$495,748.62

	YR 1	YR 2	YR 3	YR 4	YR 5	YR 6
EGINNING BALANCE	$5,948,983.46	$5,453,234.84	$4,957,486.22	$4,461,737.60	$3,965,988.97	$3,470,240.35
ESS: AVE PER YEAR	495,748.62	495,748.62	495,748.62	495,748.62	495,748.62	495,748.62
NDING BALANCE	$5,453,234.84	$4,957,486.22	$4,461,737.60	$3,965,988.97	$3,470,240.35	$2,974,491.73
VERAGE BALANCE	$5,701,109.15	$5,205,360.53	$4,709,611.91	$4,213,863.28	$3,718,114.66	$3,222,366.04
RATE OF RETURN	11.25%	11.25%	11.25%	11.25%	11.25%	11.25%
ETURN	$641,374.78	$585,603.06	$529,831.34	$474,059.62	$418,287.90	$362,516.18
ETURN	$641,374.78	$585,603.06	$529,831.34	$474,059.62	$418,287.90	$362,516.18
FIT FACTOR	0.5385	0.5385	0.5385	0.5385	0.5385	0.5385
IT	$345,380.32	$315,347.25	$285,314.18	$255,281.11	$225,248.03	$195,214.96
TURN	$641,374.78	$585,603.06	$529,831.34	$474,059.62	$418,287.90	$362,516.18
SIT FACTOR	0.1025	0.1025	0.1025	0.1025	0.1025	0.1025
T	$65,740.91	$60,024.31	$54,307.71	$48,591.11	$42,874.51	$37,157.91
TAL INCOME TAXES	$411,121.23	$375,371.56	$339,621.89	$303,872.22	$268,122.54	$232,372.87

	YR 7	YR 8	YR 9	YR 10	YR 11	YR 12	PER YEAR
GINNING BALANCE	$2,974,491.73	$2,478,743.11	$1,982,994.49	$1,487,245.86	$991,497.24	$495,748.62	
SS: AVE PER YEAR	495,748.62	495,748.62	495,748.62	495,748.62	495,748.62	495,748.62	
DING BALANCE	$2,478,743.11	$1,982,994.49	$1,487,245.86	$991,497.24	$495,748.62	($0.00)	
ERAGE BALANCE	$2,726,617.42	$2,230,868.80	$1,735,120.18	$1,239,371.55	$743,622.93	$247,874.31	
RATE OF RETURN	11.25%	11.25%	11.25%	11.25%	11.25%	11.25%	
TURN	$306,744.46	$250,972.74	$195,201.02	$139,429.30	$83,657.58	$27,885.86	$334,630.32
TURN	$306,744.46	$250,972.74	$195,201.02	$139,429.30	$83,657.58	$27,885.86	
FIT FACTOR	0.5385	0.5385	0.5385	0.5385	0.5385	0.5385	
T	$165,181.89	$135,148.82	$105,115.75	$75,082.68	$45,049.61	$15,016.54	
TURN	$306,744.46	$250,972.74	$195,201.02	$139,429.30	$83,657.58	$27,885.86	
SIT FACTOR	0.1025	0.1025	0.1025	0.1025	0.1025	0.1025	
T	$31,441.31	$25,724.71	$20,008.10	$14,291.50	$8,574.90	$2,858.30	
TAL INCOME TAXES	$196,623.20	$160,873.53	$125,123.85	$89,374.18	$53,624.51	$17,874.84	$214,498.03

Certificate of Service

I, Ann D. Berkowitz, hereby certify that copies of the foregoing "Supplemental Direct Case of GTE" have been mailed by first class United States mail, postage prepaid, on the 28th day of August, 1995 to all parties on the attached list.

Ann D. Berkowitz

Daniel L. Brenner
Attorney
National Cable Television Association
1724 Massachusetts Avenue, NW
Washington, DC 20036

William Kennard
General Counsel
Federal Communications Commission
1919 M Street, NW
Room 614
Washington, DC 20554

Randy R. Klaus
Senior Staff Member
MCI Telecommunications Corporation
1801 Pennsylvania Avenue, NW
Washington, DC 20006

Geraldine Matise
Chief
Tariff Division, Common Carrier Bureau
Federal Communications Commission
1919 M Street, NW
Room 518
Washington, DC 20554

David Nall
Federal Communications Commission
Common Carrier Bureau, Tariff Division
1919 M Street, N.W.
Room 518
Washington, DC 20554

John B. Richards
Keller & Heckman
1001 G Street, N.W.
Suite 500 West
Washington, DC 20011

Jeffrey Sinsheimer
Director-Regulatory Affairs
California Cable Television Association
4341 Piedmont Avenue
Oakland, CA 94611

Edward P. Taptich
Attorney
Gardner, Carton & Douglas
1301 K Street, NW
Suite 900, East Tower
Washington, DC 20005