Step 5 Determine whether the quantity of service is appropriate. Is the appropriate quantity of service obvious in terms of staffing (for example, most aspects of billing) or is it provided on a stand-by or ready-to-respond basis (for example, legal services)? If the quantity of service is obvious and it is not feasible to provide it in the wrong quantity, skip the test and enter 1 in **column 5**. If the quantity of service to be provided is determined by a third party study, enter 1 in **column 5A**. If the quantity of service to be provided is determined by an affiliate or IBT study, enter 1 in **column 5B**.

The tests below regarding costs (Steps 6 through 9) are applied on the basis that the overhead allocation methods and the accounting controls have already been verified. In this case — an audit of affiliate services wherein the provision of many services has recently been transferred from the telco, IBT — the primary alternate provider of services is most appropriately the telco itself. Prudent management practice, from the ratepayers' perspective, requires that a reasonable case be established and documented which addresses the economies to be achieved through the prospective centralization of services. Similarly, a study after the transfer must verify that the planned economies have been realized, or some tracking system must be incorporated in the ongoing management procedures to provide the verification.

Step 6 checks for a *make-or-buy study*, which compares the costs of internal provision of the service with the cost of provision by the affiliate. The first stage in testing for reasonable pricing of affiliate services is to examine documentation of the make-or-buy decision — the decision that resulted in the curtailment of services at IBT and their provision by the affiliate. Absent such documentation, the auditor follows the default procedure, which assumes IBT could have continued to provide the services. The IBT cost of providing the services is then estimated by multiplying the affiliate cost by the ratio of IBT's wage index to that of the affiliate. The lower of the two cost estimates is provisionally allowed, subject to further testing. Again, in the absence of such a study, the estimated cost of IBT provision of the service is substituted for the affiliate's item expense.

Step 6 **Make-or-Buy Decision.** Determine whether the make-or-buy decision is documented by a study. If it is not feasible to provide the service internally, and the service was historically provided to IBT by an outside party, skip the test; enter 1 in **column 6**. If the make-or-buy study was carried out by a third party study, enter 1 in **column 6A**. If the study was carried out by an affiliate or IBT, enter 1 in **column 6B**.

In Step 7, a proper market test of the cost of service is to consider the costs of *alternative providers of the service*. There should be documentation of consideration of such alternative providers. The cost estimates of the alternative providers should be based on long term contractual prospects. Short term contract costs, particularly labor rates, tend to be much higher, and do not provide a realistic alternative. This type of evidence will tend to bias the decision in favor of the affiliate and permit or encourage a cost cushion. Absent such documentation, the default provider is again IBT with its costs estimated as described in Step 6, unless the make-or-buy decision is adequately documented.

Step 7 Alternative Provider. This step checks for a study that compares the affiliate's cost of providing the service with the cost of third-party provision of the service. In almost all circumstances, this test should not be skipped, and a 0 entered in column 7. If such a study has been conducted, enter 1 in column 7A and enter the third-party cost in column 7B. If the third-party cost is lower than the affiliate's cost and the IBT cost, the third-party cost will serve as an upper limit on allowable affiliate costs, unless the cost of provision of the service by IBT is lower than that of the third party. If the IBT cost is lower than the third-party cost, then the IBT cost is the upper limit on allowable affiliate expense.

Step 8 addresses the issue of the *quality of service* of the affiliate and an alternate provider. If there is evidence that the quality of service provided by the affiliate is lower for the same or greater cost as the quality of service that would be provided by the alternate provider (third party or IBT, according to the results of Step 7), the ratio of the quality of the affiliate-provided service to the quality of the alternately provided service is computed. This ratio is applied to the affiliate cost, so that allowable affiliate cost is scaled down by the quality ratio. For example, if the affiliate provides service with 90 percent of the quality of the alternate provider, then only 90 percent of the affiliate cost will be allowed. (This test is included for completeness. It is recognized that in general there will be no clear evidence on quality of service. If there is, however, this test is appropriate.)

Step 8 Quality of Service. In cases where specific evidence allows comparison of quality of service (for example, error rates or mean times to failure), this test allows incorporation of that information. If the higher quality of service can be provided at a cost equal to or below that of the affiliate, enter the *quality measure of the affiliate* in column 8A and the comparable quality measure of the alternate provider in column 8B. The *quality ratio*, computed in column 8C, is used to scale the allowable item expense of the affiliate, as described above, resulting in the *quality adjusted value of service*, computed in column 8D.

Step 9 tests for *cost and time overruns* in providing the service. The value of project-type activities may depend on the timeliness of deliverables. If services are otherwise provided under satisfactory conditions but are substantially late, a penalty is imposed by charging a waiting penalty on the costs. This penalty is equal to the pre-tax rate of return allowed by the ICC. Similarly, cost overruns are disallowed unless there is a change in the scope of the services supplied by the affiliate that has documented approval of the responsible IBT manager. Continuing services, such as billing and accounting, are expected to pass this test routinely. This test is intended primarily for long-term projects that result in services such as deliveries of a software product or report.

Step 9 Cost and Time Overruns in Delivery of Services or Product. For elements where the test is not to be applied, enter 1 in column 9. In the case of cost overrun, enter 1 in column 9A, and enter the excess expense over planned cost in column 9B. If there is a documented change in scope of the service or product, enter 1 in column 9C. The disallowed cost, computed as the difference between planned cost and the item expense, is computed in column 9D. If there has been a time overrun in delivery of the service or product, enter 0 in column 9E, and enter the number of months late in column 9F. The allowable cost is computed by applying the discount factor to the

claimed item expense less the disallowed cost in column 9D, if any. The allowable cost is shown in column 9G.

Comparing the Cost and Value of Services

Both planning and verification of gains from provision of services by affiliates are required because there is an incentive for the unregulated parent company to charge higher prices to the regulated telco for the services it provides through unregulated affiliates, and thereby capture a higher return. That there is no incentive to do so because unregulated affiliates are jointly owned by the AOCs — as is ASI — is not a persuasive argument. The unregulated affiliates could themselves purchase services at higher than market prices from other suppliers or from the parent company to the ratepayers' disadvantage. Thus, there should be *before* and *after verification* that the new arrangements for provision of services are in the ratepayers' interest. In the absence of other market tests, the appropriate market test consists of comparing the cost of the same services provided by IBT. Step 10 compares anticipated and realized values of benefits received for completed services in terms of expense items for work profiles, projects or other items. For large projects particularly, there should be documentation of benefits expected at the time of project initiation. Absence of such documentation would lead to deficiency under the prudence criterion. Reasonable project management methods by IBT would examine benefits realized for a project and compare them with the expected benefits.

Step 10 Comparison of Expected and Realized Benefits. It is anticipated that this test will be applied to most items. To skip the test, enter 1 in column 10. If there has been a study of benefits expected to accrue to ratepayers as a result of the service, enter 1 in column 10A. If there has been a study that demonstrates the benefits realized by ratepayers from provision the service are those that were expected, enter 1 in column 10B. If either study is missing, the spreadsheet computes the allowed expense as IBT costs. Otherwise, the expense allowed by this test is the claimed expense, shown in column 10C.

Step 11 The reasonable costs of service have been determined from the cost testing conducted in Steps 6 through 9. Value of the services has been established (Steps 1-5), and comparison of expected and realized benefits carried out (Step 10). The final assessment consists of comparing the cost or value of the service or product, and taking the minimum of these as the *allowable cost for the tested expense item* which is displayed in column 11. This step is entirely computational. The consultant has completed all of the necessary work for this test in supplying the information called for in earlier steps.

Step 12 When the final allowable cost for the expense item has been determined, the *ratio of the allowable cost to the claimed expense* is computed by the spreadsheet and displayed in column 12.

Step 13 The disallowed cost is computed by the spreadsheet as the difference between the allowable cost and the claimed expense. The *disallowed cost* is displayed in column 13.

Step 14 The disallowance ratio is computed in the spreadsheet as the ratio of disallowed cost to the claimed expense for the item. The *disallowance ratio* is displayed in **column 14.**

Step 15 The weights to be applied to roll up the disallowance ratios for individual items to an overall disallowance ratio for the entire set of sampled items are computed as the ratio of the claimed expense for the item to the total expense for all items in the sample. The total of all expense items in the sample appears at the bottom of column labeled **COST OF ELEMENT AT AFFILIATE.** The *roll-up weight* for the item is displayed in **column 15.**

Step 16 The contribution of the allowed expense ratio for each claimed expense item to the total allowed expense ratio for the sample is computed by the spreadsheet as the product of the roll-up weight and the allowed expense ratio for the item. The ***contribution to the sample allowance ratio*** is displayed in **column 16.**

Sample Allowance Ratio

The ***final sample allowance ratio*** is computed by the spreadsheet as the sum of the contributions in column 16. The sample allowance ratio, so labeled, appears at the bottom of column 16.

A summary of the consultant's spreadsheet analysis is provided in *Exhibit IV-15.*

S-WS-40010	***Review actual value of services provided compared to the anticipated value of service when work was planned.***

This section was designed to specifically focus on actual versus anticipated value for work profiles that terminated during the test year. Over 90% of ASI's 1992 budget represented work that was a continuation of efforts from 1991; in particular, the scope and deliverables related to work efforts may change from one year to the next, but the primary functions were categorized by ASI management as continuations of existing 1991 projects and business management work.[242] In 1992, 12 new work profiles were created but none were terminated or merged.[243] In 1991, 134 work packages and/or product service orders were created; 28 were terminated and 9 merged. To assess whether similar decisions would have been made by ASI and/or IBT based upon actual costs or benefits (when actual costs or benefits significantly deviated from anticipated costs or benefits), the consultant first determined whether the 28 1991 terminations occurred between September 1, 1991, and August 1, 1992.[244] There were no terminations during the test year. If there had been, the consultant would have selectively reviewed test year data, to the extent possible, to assess whether similar decisions would have been made by ASI and/or IBT based upon actual costs or benefits (if actual costs or benefits significantly deviated from anticipated costs or benefits), rather than anticipated costs or benefits.

TARGET SAMPLE BY COST DETAIL, MONTH, PROFILE NUMBER AND BILL LINE
AMERITECH SERVICES, INC CHARGES TO ILLINOIS BELL

BILLING PERIOD: September, 1991 to August, 1992

PROCESS NUMBER	PROCESS NAME/DESCRIPTION	PROFILE NUMBER	PROFILE NAME/DESCRIPTION	BILL LINE	SPLIT PCT	FUNCTION CODE	MMM YY	REGULATORY STATUS	COST OF ELEMENT AT AFFILIATE (ADJUSTED FOR COST TESTING, IF APPLICABLE)
1	Establish Customer Service	010004	MIS	A7S2R0	1.0000	50GN	Aug 92	Regulated	5 243 41
1		010013	ACIS	A310000	0.0051	50J0	May 92	Shared Other	612 582 93
1		010004	ACIS Replaced Systems	L12300	1.0000	50J0	Jan 92	Shared Other	77 089 18
1		010004	ACIS Replaced Systems	L50000	1.0000	50J0	Mar 92	Shared Other	39 191 98
1		010000	CABS	A32000	0.0000	50J0	Jan 92	Shared Other	5 410 00
1		010000	ICOS Billing	AU0V00	1.0000	5000	Jun 92	Shared	1 168 559 12
2	Deliver Customer Service	000000	Telbill	A50000	1.0000	50GN	Jul 92	Regulated	378 157 61
2		000000	TIRKS	A50000	1.0000	50GN	Aug 92	Regulated	165 335 32
2		000000	Misc. & Core Support	A00000	0.0470	50J0	Feb 92	Shared Other	194 175 09
3	Assure and Maintain Customer Service	000000	Tech. Training & Development	AU0000	1.0000	50GN	Apr 92	Shared	200 345 99
3		000000	ADM Integrity (NICCDS)	A37100	0.0000	50J0	May 92	Shared Market	434 101 15
3		000000	ADM Integrity (NICCDS)	A37100	0.0000	50J0	Jun 92	Shared Market	27 789 45
3		000000	ADM Training (NICCDS) Support	AU0000	1.0000	50GN	Jan 92	Shared	20 602 72
3		000000	ADM Training (NICCDS) Support	AU0V00	1.0000	5000	Aug 92	Shared	200 002 02
3		000000	Provide Fund Use ADM Support	AU30R0	0.0000	5000	Jul 92	Shared	117 223 39
5	Manage Material Logistics	000000	Common Services	3L00	1.0000	5100	Jan 92	Shared	488 220 22
5		000000	Common Services	3L37	1.0000	5000	Feb 92	Regulated	29 185 28
5		000000	Common Services	3L03	1.0000	5100	Mar 92	Shared	512 120 73
5		000000	APVIEWS IT	A0F200	0.0000	50J0	Apr 92	Shared Other	161 600 25
6	Develop and Manage Markets, Products, and Channels	000000	Public/Business Services Prod. Mgmt.	AU3300	1.0000	501P	Jun 92	Regulated	24 237 31
6		000000	Private Line Prod. Mgmt.	AU0000	1.0000	501P	May 92	Shared	40 293 10
6		000000	Private Line Prod. Mgmt.	LU0000	1.0000	501P	Jul 92	Shared	23 831 01
6		000000	Ameritech Centers Mgmt	A10000	1.0000	37NM	Aug 92	Shared Market	19 884 57
6		000000	ASIS	A10000	0.0000	50J0	Jan 92	Shared Market	252 901 59
6		000000	IRS	AU0000	1.0000	501P	Mar 92	Regulated	5 021 72
9	Operate Data Centers and Networks (Create and Manage Information Technology Platform Re	000000	DSC- Regional Data Center Hardware/Software	D00000	1.0000	50EK	Jan 92	Shared	560 489 40
9		000000	DSC-Admin Environment	D00000	1.0000	50J0	Feb 92	Shared	840 505 43
9		000000	DSC-Sand Street Ops.	L00000	1.0000	50EK	Feb 92	Shared Other	501 101 09
9		000000	DSC-Software Support/Network (Mainf)	L00000	1.0000	50EK	Mar 92	Shared Other	80 140 25
9		000000	DSC-Admin/Resource Mgmt.	D00000	1.0000	50J0	Apr 92	Shared	200 040 91
9		000000	DSC-Admin/Resource Mgmt.	D00000	1.0000	50J0	May 92	Shared	221 107 17
9		000000	DSC-Sand Street Ops.	L00000	1.0000	50EK	May 92	Shared Other	910 202 91
9		000000	DSC-Admin Environment	D00000	1.0000	50EK	Jun 92	Shared	842 510 07
9		000000	DSC-Sand Street Ops.	L00000	1.0000	50EK	Jun 92	Shared Other	819 110 94
9		000000	DSC-Admin/Resource Mgmt.	D00000	1.0000	50EK	Jul 92	Shared	654 147 71
9		000000	DSC-Ameritech/NNI Hardware/Software	L01000	1.0000	50EK	Jul 92	Shared Other	422 487 02
9		000000	DSC-Problem Mgmt.	D00000	1.0000	50EK	Aug 92	Shared	52 023 41
9		000000	DSC-Sand Street Ops.	L00000	1.0000	50EK	Aug 92	Shared Other	159 044 11
9		100000	Video Conferencing Presence Total	AU1F00	1.0000	50GN	Jan 92	Regulated	31 389 83
10	Establish Network Infrastructure and Perform Technical	110000	Traffic & Costs	A120R0	1.0000	50J5	Aug 92	Regulated	1800 690 41
11	Support External Business Operations	140000	Property & Cost Systems	L10000	1.0000	50J0	Mar 92	Shared Other	78 784 06
14	Manage Financial Resources (SP&R/Finance)	100001	I/F Local Illinois	L53000	1.0000	50J0	May 92	Shared Other	2 890 13
15	Perform Local I/F Work/Manage Information Resources	100001	I/F Local Illinois	L07000	1.0000	50J0	Jun 92	Shared Other	5 191 28
15									

CATEGORY	WORK PROGRAM	SUB CATEGORY					
ASI MAIL MGMT SVCS/PROF SVCS	MRAS COUNCIL	PROF SVCS	A190MC	N/A	5660	Sep 91	Regulated	$68 803 37
ASI MAIL MGMT SVCS/PROF SVCS	MRAS COUNCIL	PROF SVCS	AQ10MC	N/A	561P	Oct 91	Regulated	$350 457 79
ASI MAIL MGMT SVCS/PROF SVCS	SUP SVCS COUNCIL	MAIL MGMT	IK03	N/A	5100	Oct 91	Shared	$449 501 71
ASI MAIL MGMT SVCS/PROF SVCS	MRAS COUNCIL	PROF SVCS	ASP050	N/A	501P	Nov 91	[illegible]	[illegible]
ASI MAIL MGMT SVCS/PROF SVCS	SUP SVCS COUNCIL	MAIL MGMT	IK30	N/A	5100	Nov 91	[illegible]	[illegible]
ASI MAIL MGMT SVCS/PROF SVCS	MRAS COUNCIL	PROF SVCS	ASP060	N/A	561P	Dec 91	[illegible]	[illegible]
ASI MAIL MGMT SVCS/PROF SVCS	SUP SVCS COUNCIL	MAT MGMT	IK09	N/A	022X	Dec 91	[illegible]	[illegible]

[illegible] $[illegible]

[illegible] (A) Affil [illegible] Expense Account of Receiving Function
[illegible] Salvage and/or Removal FRC of Material Returned
[illegible] allocating this line to several accounts

DISCOUNT RATE (ANN)

WAGE COMPARISON INDEX ASI AND IBI

PLE BER	1 ALLOCATE TO REGULATED BUSINESS BY PART 64 CFR YES = 1 NO = 0	2 IS THE SERVICE USEFUL? YES = 1 NO = 0	3 ARE DUPLICATE FUNCTIONS PROVIDED ELSEWHERE / NO = 1 YES = 0	TOTAL EXPENSE POTENTIALLY ALLOCABLE TO IBI (COMPUTED)	COST OF PROVIDING SERVICE AT IBI BASED ON WAGE COMPARISON INDEX (COMPUTED)	4 SKIP TEST OF NEED FOR SERVICE? YES = 1 NO = 0	4A NEEDS STUDY BY 3RD PARTY? YES = 1 NO = 0	4B NEEDS STUDY BY INTERNAL GROUP? YES = 1 NO = 0	4C IF NO STUDY ALLOWABLE SET AT IBI COST (COMPUTED)	5 SKIP TEST 5? YES = 1 NO = 0	5A QUANTITY OF SERVICE STUDY BY 3RD PARTY? YES = 1 NO = 0	5B QUANTITY OF SERVICE STUDY BY INTERNAL GROUP? YES = 1 NO = 0	5C IF NO STUDY VALUE SET AT IBI COST (COMPUTED)	6 SKIP TEST 6? YES = 1 NO = 0	6A MAKE OR BUY STUDY BY 3RD PARTY? YES = 1 NO = 0
7	1	1	1	[illegible]	[illegible]	0	0	1	[illegible]	0	0	1	[illegible]	0	1
8	1	1	1	[illegible]	[illegible]	0	0	1	[illegible]	0	0	1	[illegible]	0	0
	1	1	1	[illegible]	[illegible]	0	0	1	[illegible]	0	0	1	[illegible]	0	0
2	1	1	1	[illegible]	[illegible]	0	0	1	[illegible]	0	0	1	[illegible]	0	0
	1	1	1	[illegible]	[illegible]	0	0	1	[illegible]	0	0	1	[illegible]	1	0
1	1	1	1	[illegible]	[illegible]	0	0	1	[illegible]	0	0	1	[illegible]	1	0
2	1	1	1	[illegible]	[illegible]	0	0	1	[illegible]	0	0	1	[illegible]	1	0
5	1	1	1	[illegible]	[illegible]	0	0	1	[illegible]	0	0	1	[illegible]	1	0
1	1	1	1	[illegible]	[illegible]	0	0	1	[illegible]	0	0	1	[illegible]	1	0
7	1	1	1	[illegible]	[illegible]	0	1	1	[illegible]	0	1	1	[illegible]	0	1
1	1	1	1	[illegible]	[illegible]	0	1	1	[illegible]	0	1	1	[illegible]	0	1
7	1	1	1	[illegible]	[illegible]	0	1	1	[illegible]	0	1	1	[illegible]	0	1
	1	1	1	[illegible]	[illegible]	0	1	1	[illegible]	0	1	1	[illegible]	0	1
	1	1	1	[illegible]	[illegible]	0	1	1	[illegible]	0	1	1	[illegible]	0	1
9	1	1	1	[illegible]	[illegible]	0	1	1	[illegible]	0	1	1	[illegible]	0	1
9	1	1	1	[illegible]	[illegible]	0	1	1	[illegible]	0	1	1	[illegible]	0	1
	1	1	1	[illegible]	[illegible]	0	0	1	[illegible]	1	0	0	[illegible]	1	0
	1	1	1	[illegible]	[illegible]	0	0	1	[illegible]	1	0	0	[illegible]	1	0
1	1	1	1	[illegible]	[illegible]	0	0	1	[illegible]	1	0	0	[illegible]	1	0
1	1	1	1	[illegible]	[illegible]	0	0	1	[illegible]	1	0	0	[illegible]	1	0
1	1	1	1	[illegible]	[illegible]	0	0	1	[illegible]	0	0	0	[illegible]	1	0
1	1	1	1	[illegible]	[illegible]	0	0	1	[illegible]	0	0	0	[illegible]	1	0
1	1	1	1	[illegible]	[illegible]	0	0	1	[illegible]	1

11.25%
00.03%

E R	6B MAKE OR BUY STUDY BY INTERNAL GROUP? YES = 1 NO = 0	6C IF NO STUDY VALUE SET AT IST COST (COMPUTED)	7 SKIP TEST 7? YES = 1 NO = 0	7A COST OF UNAFFILIATED PROVIDER CONSIDERED? YES = 1 NO = 0	7B COST OF UNAFFILIATED PROVIDER ENTER COST	7C ALLOWABLE (MINIMUM OF EXPENSE, IST COST OR 3RD PARTY COST) (COMPUTED)	8 SKIP TEST 8? YES = 1 NO = 0	8A QUALITY OF AFFILIATE ENTER QUALITY INDEX	8B QUALITY OF ALTERNATE PROVIDER ENTER QUALITY INDEX	8C QUALITY RATIO: AFFILIATE DIV BY ALTERNATE PROVIDER (COMPUTED)	8D QUALITY ADJUSTED ALLOWABLE COST OF SERVICE (COMPUTED)	9 SKIP TEST 9? YES = 1 NO = 0	9A COST OVERRUN YES = 1 NO = 0	9B EXCESS EXPENSE ABOVE PLANNED COST ENTER	9C DOCUMENTED CHANGE IN SCOPE OF PROJECT? YES = 1 NO = 0
	0	$8.243	0	0		$4.743	0	1.00	1.00	1.00	$8.243	0	0		0
	0	$674.676	0	0		$674.676	0	1.00	1.00	1.00	$630.063	0	0		0
	0	$70.001	0	0		$70.001	0	1.00	1.00	1.00	$77.000	0	0		0
	0	$36.000	0	0		$30.000	0	1.00	1.00	1.00	$30.000	0	0		0
	0	$8.411	0	0		$4.000	0	1.00	1.00	1.00	$8.411	0	0		0
	0	$1,100.000	0	0		$1,000.000	0	1.00	1.00	1.00	$1,100.000	0	0		0
	0	$370.000	0	0		$300.000	0	1.00	1.00	1.00	$370.000	0	0		0
	0	$100.000	0	0		$000.000	0	1.00	1.00	1.00	$100.000	0	0		0
	0	$100.000	0	0		$000.000	0	1.00	1.00	1.00	$100.000	0	0		0
	1	$300.000	0	1		$297.000	0	1.00	1.00	1.00	$300.000	0	0		0
	1	$430.000	0	1		$000.000	0	1.00	1.00	1.00	$430.000	0	0		0
	1	$30.000	0	1		$30.000	0	1.00	1.00	1.00	$37.000	0	0		0
	1	$30.000	0	1		$30.000	0	1.00	1.00	1.00	$30.000	0	0		0
	1	$337.000	0	1		$000.000	0	1.00	1.00	1.00	$300.000	0	0		0
	1	$117.000	0	1		$000.000	0	1.00	1.00	1.00	$117.000	0	0		0
	0	$400.000	0	0		$400.000	0	1.00	1.00	1.00	$400.000	0	0		0
	0	$00.000	0	0		$00.000	0	1.00	1.00	1.00	$30.000	0	0		0
	0	$810.101	0	0		$000.000	0	1.00	1.00	1.00	$810.101	0	0		0
	0	$101.000	0	0		$000.000	0	1.00	1.00	1.00	$101.000	0	0		0
	0	$36.337	1	0		$00.000	0	1.00	1.00	1.00	$36.337	0	0		0
	0	$40.300	1	0		$00.000	0	1.00	1.00	1.00	$40.300	0	0		0
	0	$33.001	1	0		$00.000	0	1.00	1.00	1.00	$33.001	0	0		0
	0	$10.000	1	1		$07.007	0	1.00	1.00	1.00	$10.000	0	0		0
	0	$300.000	1	1		$000.700	0	1.00	1.00	1.00	$300.000	0	0		1
	0	$0.000	1	0		$0.000	0	1.00	1.00	1.00	$0.000	0	0		0
	1	$100.000	0	1		$000.300	0	1.00	1.00	1.00	$100.000	0	0		0
	1	$040.000	0	1		$007.300	0	1.00	1.00	1.00	$040.000	0	0		0
	1	$001.100	0	1		$000.700	0	1.00	1.00	1.00	$001.100	0	0		0
	1	$00.140	0	1		$00.000	0	1.00	1.00	1.00	$00.140	0	0		0
	1	$300.047	0	1		$000.300	0	1.00	1.00	1.00	$300.047	0	0		0
	1	$300.107	0	1		$000.000	0	1.00	1.00	1.00	$301.107	0	0		0
	1	$000.300	0	1		$000.000	0	1.00	1.00	1.00	$010.300	0	0		0
	1	$040.000	0	1		$000.000	0	1.00	1.00	1.00	$040.000	0	0		0
	1	$010.107	0	1		$000.300	0	1.00	1.00	1.00	$010.107	0	0		0
	1	$104.147	0	1		$000.000	0	1.00	1.00	1.00	$104.147	0	0		0
	1	$400.400	0	1		$000.700	0	1.00	1.00	1.00	$400.400	0	0		0
	1	$00.000	0	1		$07.000	0	1.00	1.00	1.00	$00.000	0	0		0
	1	$700.000	0	1		$000.000	0	1.00	1.00	1.00	$700.000	0	0		0
	0	$30.370	1	0		$00.000	0	1.00	1.00	1.00	$31.370	0	0		0
	0	($000.000)	1	0		($000.000)	0	1.00	1.00	1.00	($000.000)	0	0		0
	0	$70.704	0	0		$70.041	0	1.00	1.00	1.00	$70.704	0	0		0
	1	$2.000	0	1		$0.000	0	1.00	1.00	1.00	$2.000	0	0		0
	1	$8.101	0	1		$4.710	0	1.00	1.00	1.00	$8.101	0	0		0
		$0	0			$0	0			#DIV/0!	#DIV/0!	0			
		$0	0			$0	0			#DIV/0!	#DIV/0!	0			
		$0	0			$0	0			#DIV/0!	#DIV/0!	0			
		$0	0			$0	0			#DIV/0!	#DIV/0!	0			
		$0	0			$0	0			#DIV/0!	#DIV/0!	0			
		$0	0			$0	0			#DIV/0!	#DIV/0!	0			
		$0	0			$0	0			#DIV/0!	#DIV/0!	0			

SAMPLE NUMBER	9D DISALLOWED COST (COMPUTED)	9E RESULTS ON SCHEDULE? YES = 1 NO = 0	9F NUMBER OF MONTHS LATE ENTER MONTHS	9G VALUE ADJUSTED FOR LATE DELIVERY (COMPUTED)	10 SKIP TEST 10? YES = 1 NO = 0	10A STUDY TO DETERMINE EXPECTED VALUE? YES = 1 NO = 0	10B FOLLOW UP STUDY TO VERIFY BENEFITS? YES = 1 NO = 0	10C ADJUSTMENT: 10! COSTS IF EITHER STUDY MISSED ELSE EXPENSE ALLOWED (COMPUTED)	11 FINAL VALUE OF ITEM TO RATE PAYERS (COMPUTED)	12 RATIO OF FINAL ALLOWED VALUE TO ALLOCATED COST (COMPUTED)	13 DIS ALLOWED COST (COMPUTED)	14 DIS ALLOWANCE RATIO (COMPUTED)	15 ROLL UP WEIGHTS (PERCENT) (COMPUTED)	16 CONTRIB ROLL UP VALUE ALLOWED (COMPUTED)
37	$0	1	0	$5,343	0	1	1	$5,343	$4,703	99.83%	$481	0.17%	0.04%	0.04%
10	$0	1	0	[illegible]	0	1	1	$633,863	$674,676	99.83%	$58,000	0.17%	5.37%	0.88%
1	$0	1	0	[illegible]	0	1	1	$77,000	$90,000	99.83%	$7,000	0.17%	0.65%	0.50%
12	$0	1	0	$90,100	0	1	1	$30,100	$36,000	99.83%	$3,004	0.17%	0.33%	0.30%
2	$0	1	0	$5,400	0	1	1	$5,400	$4,000	99.83%	$400	0.17%	0.03%	0.04%
16	$0	1	0	$1,100,000	0	1	1	$1,100,000	$1,000,000	99.83%	$100,073	0.17%	0.81%	0.00%
12	$0	1	0	[illegible]	0	1	1	[illegible]	[illegible]	99.83%	$34,077	0.17%	3.21%	2.02%
10	$0	1	0	[illegible]	0	1	1	[illegible]	[illegible]	99.83%	$16,481	0.17%	1.40%	1.20%
0	$0	1	0	[illegible]	0	1	1	[illegible]	[illegible]	99.83%	$17,000	0.17%	1.65%	1.50%
17	$0	1	0	[illegible]	0	1	1	[illegible]	[illegible]	99.83%	$19,000	0.17%	1.76%	1.50%
21	$0	1	0	[illegible]	0	1	1	[illegible]	[illegible]	99.83%	$30,033	0.17%	3.00%	3.35%
27	$0	1	0	$37,700	0	1	1	$37,700	$36,000	99.83%	$3,040	0.17%	0.24%	0.21%
3	$0	1	0	$30,000	0	1	1	$30,000	$36,000	99.83%	$3,033	0.17%	0.24%	0.22%
10	$0	1	0	[illegible]	0	1	1	[illegible]	[illegible]	99.83%	$19,090	0.17%	1.77%	1.60%
33	$0	1	0	[illegible]	0	1	1	[illegible]	[illegible]	99.83%	$10,700	0.17%	1.00%	0.00%
4	$0	1	0	[illegible]	0	0	0	[illegible]	[illegible]	99.83%	$40,771	0.17%	4.16%	3.77%
6	$0	1	0	$30,100	0	0	0	$30,400	$30,400	99.83%	$3,074	0.17%	0.28%	0.23%
13	$0	1	0	$562,121	0	0	0	[illegible]	[illegible]	99.83%	$40,081	0.17%	4.38%	3.05%
16	$0	1	0	$101,000	0	0	0	[illegible]	[illegible]	99.83%	$14,037	0.17%	1.37%	1.26%
20	$0	1	0	$24,237	1	1	1	$24,237	$20,000	99.83%	$2,233	0.17%	0.21%	0.10%
22	$0	1	0	$40,000	1	1	1	$40,000	$30,000	99.83%	$3,006	0.17%	0.34%	0.31%
34	$0	1	0	$23,034	1	1	1	$23,034	$20,000	99.83%	$2,102	0.17%	0.20%	0.10%
40	$0	1	0	$10,000	1	1	1	$10,000	$17,007	99.83%	$1,700	0.17%	0.17%	0.15%
5	$0	1	0	[illegible]	1	1	1	[illegible]	[illegible]	99.83%	$23,107	0.17%	2.15%	1.65%
14	$0	1	0	$8,001	1	1	1	$8,001	$8,000	99.83%	$816	0.17%	0.08%	0.04%
9	$0	1	0	[illegible]	0	1	1	[illegible]	[illegible]	99.83%	$42,130	0.17%	4.03%	4.30%
10	$0	1	0	[illegible]	0	1	1	[illegible]	[illegible]	99.83%	$50,200	0.17%	4.40%	4.00%
11	$0	1	0	[illegible]	0	1	1	[illegible]	[illegible]	99.83%	$51,400	0.17%	4.77%	4.33%
15	$0	1	0	$80,140	0	1	1	$80,140	[illegible]	99.83%	$4,002	0.17%	0.75%	0.60%
18	$0	1	0	[illegible]	0	1	1	[illegible]	[illegible]	99.83%	$23,040	0.17%	2.21%	2.01%
23	$0	1	0	[illegible]	0	1	1	[illegible]	[illegible]	99.83%	$20,270	0.17%	1.66%	1.71%
24	$0	1	0	[illegible]	0	1	1	[illegible]	[illegible]	99.83%	$84,003	0.17%	7.70%	7.01%
29	$0	1	0	[illegible]	0	1	1	[illegible]	[illegible]	99.83%	$50,000	0.17%	4.46%	4.06%
30	$0	1	0	[illegible]	0	1	1	[illegible]	[illegible]	99.83%	$50,773	0.17%	5.26%	4.70%
35	$0	1	0	[illegible]	0	1	1	[illegible]	[illegible]	99.83%	$14,036	0.17%	1.31%	1.10%
38	$0	1	0	[illegible]	0	1	1	[illegible]	[illegible]	99.83%	$30,743	0.17%	3.50%	3.20%
41	$0	1	0	[illegible]	0	1	1	[illegible]	[illegible]	99.83%	$4,040	0.17%	0.45%	0.40%
42	$0	1	0	[illegible]	0	1	1	[illegible]	[illegible]	99.83%	$50,004	0.17%	0.45%	5.05%
7	$0	1	0	$30,370	1	1	1	$30,370	$30,400	99.83%	$3,077	0.17%	0.27%	0.24%
43	$0	1	0	[illegible]	1	0	0	[illegible]	[illegible]	100.00%	$0	0.00%	0.00%	0.00%
18	$0	1	0	$70,704	0	0	0	$71,041	$71,041	99.83%	$7,233	0.17%	0.67%	0.61%
25	$0	1	0	$3,000	0	1	1	$3,000	$3,000	99.83%	$305	0.17%	0.03%	0.03%
31	$0	1	0	$6,101	0	1	1	$6,101	$4,710	99.83%	$479	0.17%	0.04%	0.04%
[illegible]	$0			$0				$0	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!	0.19%	#DIV/0!
45	$0			$0				$0	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!	2.10%	#DIV/0!
46	$0			$0				$0	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!	3.03%	#DIV/0!
[illegible]	$0			$0				$0	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!	1.50%	#DIV/0!
[illegible]	$0			$0				$0	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!	0.22%	#DIV/0!
[illegible]	$0			$0				$0	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!	1.02%	#DIV/0!
[illegible]	$0			$0				$0	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!	0.06%	#DIV/0!
												SUM OF WTS	100.00%	

TOTAL EXPENSE ALLOWED #DIV/0!

SAMPLE ALLOWANCE RATIO #DIV/0!

ALLOWANCE RATIO: #DIV/0!
EXPENSE ALLOWED TO EXPENSE CLAIMED

EXHIBIT [illegible]

As part of value testing work performed (regarding *Value Testing S-WS-40009* work step), the consultant concluded — for the work profile/bill line combinations tested — that actual value of services provided by ASI to IBT compared favorably to the anticipated value of service when work was planned.

Cost Testing

S-WS-40011	*Determine if costs charged to IBT for ASI-provided goods/services are appropriate.*

Based upon the consultant's cost testing of the target sample of 50 items, only one exception was found. The extrapolation of this discrepancy to the entire ASI population results in no material impact. There have been no repayment contributions to IBT's regulated operations for services subsequently used by unregulated telecommunications providers,[245] nor have there been any right-to-use fees or royalties paid to IBT for I/T systems developed and charged to IBT.[246] During cost testing, no situations were noted in which repayment contributions or right-to-use fees or royalties should have resulted.

Based upon the consultant's other investigations and analyses, however, other areas were identified where inappropriate costs were charged by ASI to IBT, including:

- Excess depreciation (as discussed further in *Finding IV-7*)
- Excess wages (as discussed further in *Finding IV-8*)

S-WS-40012	*Determine the cost-competitiveness of ASI-provided services.*

The consultant's independent assessment of ASI-provided services to IBT is included in the results of the value testing spreadsheet analysis developed as part of the *Value Testing* section of this chapter. Some of the services provided by ASI are difficult to compare against external providers and some are not; both situations are addressed in this analysis.

Findings and Conclusions

The following identifies any findings and conclusions associated with work steps S-WS-40009, S-WS-40010, S-WS-40011, or S-WS-40012 included in the *Value and Cost Assessment - Transaction Testing* section of this chapter.

IV-F76 <u>Approximately $2.75 million in excess ASI depreciation is being charged to Illinois ratepayers.</u>

ASI's investment in property, plant, and equipment is recovered through monthly charges to depreciation expense, which is in turn passed through to IBT as an overhead assignment to the various work profiles.[247] For the month of July, 1992, depreciation expense recognized by ASI amounted to $5.3 million,[248] of which approximately $1.6 million (30%) was ultimately recovered from IBT.

The consultant obtained an analysis of depreciation charges for July, 1992[249] and reviewed the analysis to determine annual depreciation rates utilized by ASI. These rates were then compared with the actual depreciation rates prescribed by the Illinois Commerce Commission for IBT, and the resulting differences are noted in *Exhibit IV-16*. This exhibit shows that ASI is recognizing approximately $9 million more per year in depreciation expense than would be recognized if IBT's prescribed rates were being employed. This equates to approximately $2.75 million per year in additional depreciation charges to IBT.

In the consultant's opinion, the products and services acquired by IBT through ASI should not cost Illinois ratepayers more simply because they are provided by an affiliated entity. If these same services were in fact being produced internally by IBT, the capital assets supporting their provision would be depreciated under the ICC guidelines, resulting in less costly depreciation charges to IBT. While there is obviously justification for establishing a centralized organization (such as ASI) to serve the five AOCs, to the extent that this organization provides essentially the same services that the individual AOCs would otherwise provide themselves under full regulatory oversight, the same regulatory principles to which the AOCs are subject should pertain.

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Exhibit III-1
IV-16 Excess Depreciation

Plant	Motor Vehicles	Other Work Equipment	Buildings	Furniture	Office Equipment	General Purpose Computers	Total
Opening Balance	$10,699,309	$15,988,821	$14,998,891	$13,871,311	$2,084,272	$289,369,933	$346,958,597
Activity	$0	$13,688	$91,488	(283,880)	$365,168	$27,988,191	$28,203,235
Closing Balance	$10,699,309	$15,976,508	$15,083,378	$13,587,431	$2,449,437	$317,357,124	$345,161,829
Depreciation Expense	998,195	552,340	541,586	1,158,287	322,534	34,366,300	34,927,232
Effective Annual Rate	10.45%	3.90%	3.33%	13.83%	12.71%	20.83%	
ICC Prescribed Rate	9.40%	7.60%	2.60%	7.30%	9.30%	17.10%	
Depreciation at Prescribed Rate	928,812	1,106,139	520,087	984,728	317,960	33,594,860	34,211,987
Excess Depreciation	99,383	30	541,579	360,087	35,574	3871,030	3763,033
						Excess Depreciation Accumulated	39,161,590

IV-F87 <u>ASI's labor costs are approximately 10.1% higher than IBT's.</u>

The recent reorganization and redistribution of services from IBT to ASI is a situation that permits a special approach in evaluating alternative provision of those services. The services now provided by ASI were previously provided internally at IBT, or procured by IBT from external sources. Unless there are specific studies that show both (a) anticipated benefits and (b) realization of the benefits, there can be no basis for the transfer of function to an affiliate

Concerning the cost of those services, wages are the major component of costs for the services supplied to IBT. According to data from the Bureau of Labor Statistics, the Chicago area has the highest cost of living and the highest average wage in manufacturing among all of the metropolitan areas where the former Bell Operating Companies (BOCs), that are now Ameritech Operating Companies (AOCs), had their headquarters. The cost of living is one major component in justification of higher wage rates. The other major basis for comparison of wage rates among metropolitan areas is the average wage in manufacturing. This wage rate is taken as an indicator of general wage levels for a given metropolitan area. Consequently, IBT was already competing — to the extent that its wages are set competitively — in the most costly labor market of all the former BOCs.

The determination by Ameritech management to relocate the bulk of ASI services from the other metropolitan areas to the Chicago area (Hoffman Estates) is therefore open to question, and must be justified. To the extent that ASI employees are still living and working in the metropolitan areas that are headquarters of the other AOCs, there is no evident justification for the higher wage structure at ASI. To the extent that services, whose benefits and costs are shared by IBT, are provided outside the Chicago area, there is even greater basis to question the need for higher wage costs associated with those services.

In centralization of functions, justification is sometimes made upon the basis of "obvious" economies of scale. However, the management literature now questions whether centralization of functions inevitably yields reduced costs arising from economies of scale or "spreading the overheads." The transfer of many functions to ASI is justified on that basis by Ameritech management with little or no documentation or further evidence. While examples abound in the professional literature, two listed here accurately convey the skepticism that has emerged.

> A major outcome of varying degrees of centralization is for the organization itself. High levels of centralization mean greater coordination, but less flexibility; consistent organizationwide policies, but possibly inappropriate policies for local conditions; and the potential for rapid decision making during emergencies, but overloaded communication channels during normal operations as communications flow up and down the hierarchy.[250]

> Keeping things small by hiving off new divisions is *the* key to keeping an organization adaptive. Divisions should possess their own support staff.[251]

Especially in view of the separate regulatory and record-keeping requirements faced by the AOCs, it appears to be anything but certain that centralization of various functions (e.g., legal and many software functions) at ASI will benefit rate payers.

There are clear gains from sharing of the costs of services only if it can be shown also that the services meet the particular needs of the disperse components of the organization at least as well as the decentralized provision of the services would have done. A classic argument — and perhaps the strongest case for centralization of services — concerns the provision of software that is commonly shared by the AOCs. However, even here the case must be demonstrated by studies. In meeting the needs of AOCs under different regulatory jurisdictions, software must necessarily be more complex, which requires greater expenditure of resources in design and testing. It must be shown by studies that the savings of centralization more than offset this

added development and testing cost, and that the centrally provided software meets the needs of the AOCs, as well as would be done under decentralized provision of the software. It is also well established the more complex software is more costly to maintain, and especially to modify to meet changing and disparate needs of the disparate organizational components.

In consequence, there is no basis for the higher wages paid by ASI and passed through to IBT for the services provided. Therefore, in the absence of explicit "before and after" studies showing clear savings to IBT from the new arrangements, the higher wages should be disallowed.

A number of employees transferred from IBT positions to ASI positions during the reorganization. To measure if any excess wage payments at ASI resulted, the salaries of sampled employees as of September 30, 1992 were compared with the salaries that the employees would have received if they had remained at IBT and received standard wages for their pay grades at the time of transfer. Promotion cases were omitted from the analysis, as were workers who switched from full-time work at IBT to part-time work at ASI. The resulting wages were compared in a ratio of actual wages at ASI to alternative IBT wages that would have been received, as provided in *Exhibit IV-17*. These ratios, by employee, were almost invariably larger than one, showing that virtually every transferred employee made higher wages at ASI than at IBT. The ratios for individual employees were added up using their current wages as weights to obtain a measure of excess wage costs at ASI. This comparison was based upon a sampling of data and showed a gap of 10.1%. On average, employees who transferred to ASI received 10.1% higher wages for the same jobs that they did at IBT — in that the transfers were lateral moves, not promotions. This 10.1% results in a comparison wage index of 90.83%, or IBT's wages as a percentage of ASI's. This comparative wage index reflects the additional wage costs associated with reorganization of selected functions from IBT to affiliates, specifically ASI. This comparison wage index was then used in the value testing spreadsheet analysis as a basis for (a) general disallowances of higher wages and (b) repricing of services provided by ASI when there was inadequate documentation of benefits resulting from transfer of services.

The recommended disallowances (from the value testing spreadsheet analysis) — 9.79% — also resulted primarily from excess wages. The percentage difference between 9.79% and 9.17% (100%-90.83%=9.17%) — .62% occurs because one of the tested work profile/bill combinations (target sample 43), a negative number, was not included in the disallowed cost column. The sample dollar figure associated with the 9.79% totaled approximately $11,532,390. If these results were extrapolated to all professional services charged by ASI to IBT, the resulting figure would be approximately $19,100,000).[252] In looking at excess wage costs from a different perspective, the auditor multiplied ASI's excess wages (including payroll overheads), as determined by a review of ASI's financial statements, by 30.03%, the IBT portion for the test year would be approximately $11,500,000 in excess wages.[253]

Recommendations

The following identifies any recommendations associated with work steps S-WS-40009, S-WS-40010, S-WS-40011, or S-WS-40012 included in the *Value and Cost Assessment - Transaction Testing* section of this chapter.

84

IV-R68 Disallow approximately $2.75 million of excess ASI depreciation charged to IBT (Refer to Finding IV-F7.)

Based upon the auditor's analysis of excess depreciation, approximately $2.75 million of excess ASI depreciation charged to IBT should be considered by the ICC for possible disallowance.

IV-R79 Disallow approximately $11.5 million of ASI's fully-loaded labor costs based upon excess wage payments. (Refer to Finding IV-F8.)

Based upon both analyses of excess wages performed by the auditor, at least $11.5 million in excess ASI wages charged to IBT should be considered by the ICC for possible disallowance.

C. COST/BENEFIT ASSESSMENT

S-WS-40013 ***Determine if the level of benefit/value IBT receives from ASI-provided goods/services is commensurate with the costs billed to IBT.***

This section, as displayed in *Exhibit IV-18*, summarizes the results of the value and cost testing portions of this study.

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Exhibit IV-18
VALUE AND COST COMPARISON MATRIX

	Business Process	Value Received	Costs Appropriate	Cost/Benefit Assessment
1	Establish Customer Service	Yes	Partially	Yes
2	Deliver Customer Service	Yes	Partially	Yes
3	Assure and Maintain Customer Service	Yes	Partially	Yes
4	Create Service Inventory	*	*	*
5	Manage Material Logistics	Yes	Partially	Yes
6	Develop and Manage Markets, Products, and Channels	Yes	Partially	Yes
7	Develop and Maintain Business Processes	*	*	*
8	Deliver and Manage Business Processes	*	*	*
9	Operate Data Centers and Networks	Yes	Partially	Yes
10	Establish Network Infrastructure and Perform Technical Applications Development	Yes	Partially	Yes
11	Support External Business Operations	Yes	Partially	Yes
12	Support Internal Business Operations	*	*	*
13	Manage Human Resources	*	*	*
14	Manage Financial Resources	Yes	Partially	Yes
15	Perform Local I/T Work	Yes	Partially	Yes
16	Manage Integrated Planning	Yes	Partially	Yes

*: These processes designated with an asterisk (*) were not included in either the cost testing or value testing work due to the use of PPS sampling for selection of work profiles/bill item.

Exhibit IV-17
(***)

The first three processes are referred to as "frontline" processes by ASI and IBT management, because they have direct and immediate impact on the establishment, delivery, and continuity of information/telecommunications services for AOC customers. The next seven processes are referred to as "support" processes, as they directly contribute to the long-term viability of frontline processes, but do not have an immediate impact on customer service. The third group of processes are "administrative" processes, because they are general in nature and do not directly contribute to the delivery of products or services, but do have a direct contribution to the overall management of Amentech.[254]

Those processes designated with an asterisk (*) were not included in either the cost testing or value testing work due to the use of PPS sampling for selection of work profiles/bill lines. For those processes where work profiles/bill lines were selected, the auditor concluded that valuable services were being provided to Illinois ratepayers; however, the auditor also concluded that cost assignment and accumulation methodologies were generally appropriate, except for those items noted in this report, including:

- Inadequate justification for provision of ASI services
- Inappropriate recording of ASI charges at corporate level
- Inadequate documentation of market value for asset transfers
- Time reporting at ASI not rigorously applied
- Inadequate reviews of affiliate relationships and transactions
- Excess ASI depreciation charges to IBT
- Excess ASI wage charges to IBT
- Deficiencies in AMP activities between ASI and IBT management

D. IMPACT ASSESSMENT

S-WS-40014	*Calculate the impact of any adjustment which is warranted based upon findings of review.*

The proposed test year adjustments for ASI charges to IBT, primarily from excess wages and depreciation, total approximately $14.25 million.

Exhibit 3

MATRIX OF PART 32 ACCOUNTS AND ASSOCIATED PART 64 COST POOLS

Below is a Matrix of those Part 32 accounts and related cost pools to which ASI assigned costs in the 12 directly billed work profiles the audit team reviewed in depth. In total, there were seven Part 32 accounts with each account having between 3 to 5 cost pools.

The letters in the Ind. column may be translated as follows:

R - cost pool is directly assigned to regulated

N - cost pool is directly assigned to nonregulated

S-D cost pool is common/shared and directly attributable

S-1 cost pool is common/shared and indirectly attributable

G - cost pool is common/shared and generally allocated

Account		Cost Pool	Ind.		Apportionment Basis
6124 General Purpose Computers Expense	1	Regulated	R	–	Direct to Reg.
	2	Nonregulated	N	–	Direct to Nonreg.
	3	Other	S-I	–	Relative cost of Investment Acct. 2124
6535 Engineering Expense	1	Other: Regulated	R	–	Direct to Reg.
	2	Other: Nonregulated	N	–	Direct to Nonreg.
	3	Other: Shared	S-I	–	Engineering Wages and Salaries (in OSP investment and expense accounts)
6611 Product Mgmt.	1	General Support: Regulated	R	–	Direct to Reg.
	2	General Support: Nonregulated	N	–	Direct to Nonreg.
	3	General Support: Other	S-I	–	Marketing Allocator

6613 Product Adver-tising	1	Shared	S-I	–	Relative cost of Investment Acct. 2212.2
	2	Regulated	R	–	Direct to Reg.
	3	Nonregulated	N	–	Direct to nonreg.
6623 Customer Services	1	General Support: Regulated	R	–	Direct to Reg.
	2	General Support: Nonregulated	N	–	Direct to Nonreg.
	3	General Support: Other	G	–	General Allocator
6722 External Relations	1	Regulated	R	–	Direct to Reg.
	2	Nonregulated	N	–	Direct to Nonreg.
	3	Corp. Advertising	S-I	–	Marketing Allocator
	4	Other	G	–	General Allocator
6724 Informa-tion Mgmt.	1	Regulated	R	–	Direct to Reg.
	2	Nonregulated	N	–	Direct to Nonreg.
	3	Network	S-I	–	Network Total Costs (in OSP investment and expense accounts)
	4	Marketing	S-I	–	Marketing Allocator
	5	Corporate & Other	G	–	General Allocator

Exhibit 4

WORK PROFILE 06-0067
AMERITECH INTEGRATED MARKETPLACE SYSTEM (AIMS)

Work Profile Description

AIMS is a regionally defined, maintained, supported, and accessible marketing information system. Its purpose is to consolidate existing AOC marketing information systems into an integrated marketplace information platform. AIMS provides consistent and common information regarding Ameritech customers and all Ameritech products and services, regulated and unregulated.

Part 32 Classification

The ASI work involved system development and testing work by programmers for:
- common data warehouse
- data extracts from source systems
- maintenance and administrative modules
- access capabilities and standard reports
- integration and user acceptance testing

Three Bill Lines were established for these activities:

- Ameritech Regional (benefits all 5 AOCs)
  - .AU2Y00 — Two bill lines for internal tracking
  - . A19900 — (e.g., maintenance vs. enhancements)

- Indiana state specific work
  - .NS9900

The three Bill Lines were classified to Part 32 Account 6724, Information Management. FCC Part 32 reference in support of classification states that Account 6724 includes "costs incurred in planning, developing testing data bases and application systems for general purpose computers." These activities are classified as shared.

ASI work also involved communication from marketing regarding data needs, access requirements, and data relationships to the programmers. In addition, ASI defines and manages AIMS for marketplace analysis and decision making.

Two Bill Lines were established for these activities:
- Ameritech Regional (benefits all 5 AOCs)
  - . A199S0
- Category II employees (benefits all 5 AOCs)
  - . A199S2

Part 32 Classification (Cont.)

The two Bill Lines were classified to Part 32 Account 6611, Product Management. FCC Part 32 reference in support of classification states that Account 6611 includes "costs incurred in performing administrative activities related to marketing products and services.

Summary of AIMS Bill Lines

	← Part 32 Account →	
	Bill Line Codes	Bill Line Codes
Customer To Be Billed	Acct 6724 Information Management	Acct 6611 Product Management
Regional	AU2Y00 A19000	A19990
Regional-Category II		A19992
State Specific	NS9900	

Part 64 Classification

A Decision Hierarchy, as prescribed by the FCC, is used in determining Part 64 Cost Pool Assignment:

1. Direct Assignment: Do the activities exclusively support nonregulated products and services.

   NO. AIMS is a data base which contains information on both regulated and nonregulated products and services. The programming work is not divisible, it simultaneously supports both regulated and nonregulated products and services, and cannot be directly assigned.

Part 64 Classification (Cont.)

2. Are the activities directly attributable?

   NO. The programming and marketing efforts support a multi-informational marketing system, (i.e., customers, billing, products, etc.) for which there is no direct analysis of cost causation.

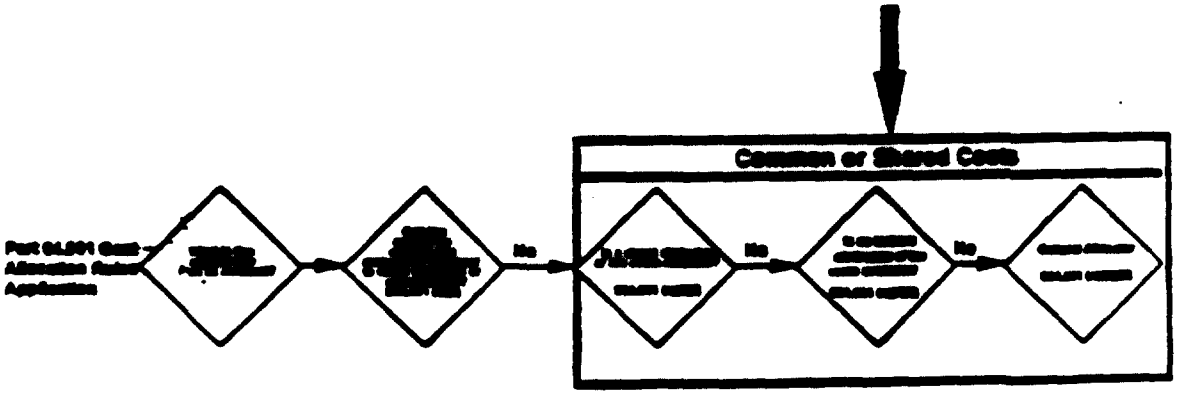
3. Are the activities indirectly attributable?

   YES. In accordance with the cost allocation standards, the Shared General Support cost pool is appropriate for the AIMS programming (Account 6724) and marketing activities (Account 6611) which allocates costs using the Marketing Allocator. (The Marketing Allocator is calculated monthly using directly assigned and attributed costs in Accounts 6611, 6612 and 6613).

4. Is the general allocator applicable?

   NO. The activities are attributable using indirect cost causation. (See #3 above).

The following chart indicates where AIMS expenses are directed in the allocation process (Shared):



Necessity of Shared Cost Pool Assignment

The AIMS system contains regulated and nonregulated marketing data. An analyst or programmer who writes or analyzes program coding is doing work which will ultimately support both regulated and nonregulated products/services necessitating a shared cost pool assignment.

There is no direct relationship between the program coding and how the marketing data will eventually be used. Therefore, an indirect cost attribution is accomplished through the Shared Marketing Allocator. The marketing allocator is calculated monthly using directly assigned and attributed costs in Accounts 6611 (Product management), 6612 (Sales) and 6613 (Product Advertising).

The above example demonstrates the billing process from classification of work, time and expense reporting and generation of service bills. In addition, the process and steps of classification and cost pool assignment were discussed. Adherence to FCC Part 32 Chart of Accounts and compliance to FCC Part 64 Cost Allocation Rules were also demonstrated.

Exhibit 5

Audit Report
on
Review of Affiliate Transactions
at
Ameritech Services, Inc.

Ameritech Response

Affidavit of Mr. Matthew Mihina, III

I, Matthew Mihina, being first duly sworn on oath, depose and state the following:

1. During the December, 1993 on-site visit by the audit team, I made the following statements to the audit team, including Mr. M. Wilson, from the Federal Communications Commission. I told the audit team that a paper which translated bill lines to Part 32 accounts and Part 64 cost pools and which ASI had provided to the audit team was not an official company record, but was an unofficial translation table an employee put together for personal use.

2. I also recall that, prior to those statements made during the December, 1993 on-site visit, I told the audit team that the sheets at issue were not official company records, but again was an unofficial translation table.

M. Mihina, III

Subscribed and sworn before me this 13th day of December, 1994.

Carol M. Fancher

OFFICIAL SEAL
CAROL M. FANCHER
NOTARY PUBLIC STATE OF ILLINOIS
MY COMMISSION EXPIRES 3/13/96