

States Treasury and undertake other remedial actions.²¹ Similar findings as to excessive nonregulated affiliate earnings were made in an earlier audit of transactions between BellSouth Corporation's operating companies and a nonregulated subsidiary.²²

A month after the GTOC Consent Decree was entered, the Commission released a federal-state joint audit examining transactions between Southwestern Bell Telephone Company (SWBT) and various of its affiliates, including its parent, Southwestern Bell Corporation (SBC). The audit report found a lack of supporting documentation for time charged by SBC employees for work done for SWBT, use of an improper marketing allocator and improper use of the general allocator. The report also found that certain services provided by SBC to SWBT were improperly charged at a prevailing company rate that did not reflect actual costs. The Commission accordingly issued an Order to Show Cause why SWBT should not be found to have violated the affiliate transaction and cost allocation rules and appropriate enforcement action taken.²³

²¹ Consent Decree Order, The GTE Telephone Operating Companies, AAD 94-35, FCC 94-15 (released April 8, 1994).

²² BellSouth Affiliate Transaction Audit: Summary of Audit Findings (undated). See BellSouth Corporation, et al., AAD 93-127, FCC 93-487 (released Oct. 29, 1993).

²³ Southwestern Bell Telephone Co., AAD 95-32, FCC 95-31 (released March 3, 1995) (SWB Audit).

Subsequently, the Commission entered into a Consent Decree settling issues arising out of a joint federal-state audit of the transactions between the Ameritech Operating Companies (AOCs) and their affiliate, Ameritech Services, Inc. (ASI). The Joint Audit Report concluded that ASI failed to provide adequate documentation to support the assignment of many costs to the AOCs and other affiliates. The Report also alleged that certain misclassifications of costs by ASI resulted in overallocation of costs to regulated ratepayers. Under the Consent Decree, ASI agreed to make certain changes in its accounting practices and payments to the United States Treasury and to the states of Ohio and Wisconsin.^{24/}

Furthermore, the cost allocation and other accounting rules are only as good as the Commission's willingness and ability to enforce them with sufficient penalties to inhibit future misallocations. That final link in the chain may be the weakest of all. Most recently, the Commission released a summary of its audit of the BOCs' accounting for lobbying costs, which found \$116.5 million in misclassified lobbying costs during the period from 1988 through 1991.^{25/} Moreover, the inflated access rates resulting from such misallocations were carried over into the LECs' access rates under price cap regulation. In spite of these

^{24/} Consent Decree Order, Ameritech, AAD 95-75, FCC 95-223 (released June 23, 1995) (Ameritech Consent Order).

^{25/} Commission Releases Summary of Lobbying Costs Audit Findings, Report No. CC 95-65 (released Oct. 26, 1995).

egregious violations, the Commission failed to take any remedial action for the past ratepayer injuries resulting from these misallocations.²⁵ Its failure to take such remedial action confirms the inadequacy of the entire cost accounting regulation and audit function, since the LECs apparently have a "free shot" at any accounting violation they may wish to commit, knowing that the worst that can happen is that someday, if they are caught, they might have to correct such practices only on a going-forward basis.

The cost misallocations, excessive costs and cross-subsidies uncovered by these audits, and the Commission's limp response thereto, thus demonstrate the ineffectiveness of the cost allocation regulations in preventing LEC cross-subsidies between regulated and unregulated services. Since LEC monopoly and regulated competitive services are more similar to one another than LEC regulated and unregulated services, allocations of costs between monopoly and competitive regulated services are even more difficult to audit. Thus, the cost allocation rules, having failed at their primary mission, certainly cannot be relied upon to prevent cross-subsidies between LEC monopoly and regulated competitive services.

Moreover, price cap regulation has not dampened the incentive to misallocate costs, as shown by the continuation of

²⁵ See id.

CERTIFICATE OF SERVICE

I, Sylvia Chukuwocha, do hereby certify that copies of the foregoing "OPPOSITION OF MCI TELECOMMUNICATIONS CORPORATION" were sent via first class, mail, postage paid to the following on the 8th day of September, 1997.

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