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August 24, 1994

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**FILED**

**AUG 24 1994**

RE: Case No. **MO-P-380**

MISSOURI  
PUBLIC SERVICE COMMISSION

Dear Mr. Rauch:

Enclosed for filing in the above-captioned case is an original and fourteen (14) conformed copies of **REPORT OF THE PARTIES**.

This filing has been mailed or hand-delivered this date to all counsel of record.

Thank you for your attention to this matter.

Sincerely,

*Thomas R. Schwarz, Jr.*  
Thomas R. Schwarz, Jr.  
Senior Counsel  
314-751-5239

TRS:bss  
Enclosure

cc: Counsel of Record

BEFORE THE PUBLIC SERVICE COMMISSION  
STATE OF MISSOURI

FILED

AUG 24 1994

In the matter of the investigation into )  
Southwestern Bell Telephone Company's )  
affiliate transactions. )

Case No. TO-94-184

MISSOURI  
PUBLIC SERVICE COMMISSION

REPORT OF THE PARTIES

At the June 21, 1994 prehearing in this docket, the Commission asked the parties to do the following:

A. Advise whether SWBT is complying with the FCC cost allocation rules, and whether the six questions listed in the Report and Order in Docket No. TC-93-224 have been addressed or remain to be addressed (Tr. p. 6); and

B. Advise whether either the joint audit or the audit performed for TAI which served as the basis for a report to the Kansas Corporation Commission had addressed the six questions in the TC-93-224 Report and Order or adequately addressed SWBT's compliance with the FCC rules (Tr. p. 6).

C. Report whether there is now an audit trail for affiliated transactions at Southwestern Bell Telephone Company (SWBT) which would permit the Commission to determine "whether Southwestern Bell was in compliance with whatever standard was established" (Tr. p. 7);

1. In a strict accounting sense, an audit trail consists of all accounting documents and records prepared as transactions are processed from origin to final posting. Source documents, journals, and ledgers are the main elements in the audit trail. Cross-references from the source

documents to the journals and from the journals to the ledger permit an individual transaction to be traced forward from the original transaction or backward from the final ledger entry, or either forward or backward from an intermediate accounting document. See *Auditing Concepts and Methods*. A Guide to Current Auditing Theory and Practices; D.R. Carmichael and John J. Willingham (McGraw-Hill 1987) pp. 153-156. In this case, the Staff believes the term audit trail would also include documentation that shows that all the necessary actions required to prevent inappropriate affiliate transactions have been taken.

SWBT believes adequate documentation has been provided to Staff, as further demonstrated by the results of the Kansas audit by TAI (Missouri's consultant in TC-93-224) and the joint staff audit. Further, SWBT believes the appropriateness of the affiliate transactions has been demonstrated to Staff as evidenced by compliance with the FCC affiliate rules.

The Staff believes that the Commission has not specified the standards it expects SWBT to observe when engaging in transactions with affiliated companies. Until such standards are set, the Staff believes it cannot confirm the existence or non-existence of adequate documentation. The Staff further disagrees that either the joint audit report or the CURB report in the KCC investigation demonstrates full SWBT compliance with FCC affiliate transactions standards.

2. Until this Commission adopts explicit affiliate transaction standards to prevent cross-subsidization, Staff represents that it is unable to determine whether SWBT's present accounting system captures all the necessary and relevant information to constitute an audit trail. SWBT believes the existing Commission rules adopt FCC Part 32 which is a comprehensive set of affiliate transaction rules for the prevention of cross-subsidy. SWBT further believes that the existence of a full and complete audit trail as required by FCC rule has been documented in numerous SWBT proceedings

or investigations. The existence of an audit trail has even been acknowledged by Staff's consultant (TAI) in the Kansas case.

3. In answer to the second question proposed at the prehearing conference SWBT asserts, as it did in its response to the joint audit; in Case TC-93-224; and in this docket that it is fully complying with the FCC cost allocation rules. Staff, however, does not believe that SWBT's current practices fully comply with the current FCC rules.

4. In answer to the final question posed by the Commission, SWBT avers that the joint audit and the audit by the Kansas Corporation Commission document that SWBT is complying with the FCC's affiliate transaction rules, and that they adequately address the six questions posed in the TC-93-224 Report and Order. Staff does not believe that to be the case in all instances. Staff asserts that the Kansas Corporation Commission proceeding raised an additional issue that was not considered in Missouri.

5. The Staff respectfully suggests to the Commission that the order of business in this docket should be:

- a. Adoption of a definition of an "audit trail";
- b. determination whether the FCC affiliate transaction standards are the appropriate standards for SWBT to observe in Missouri jurisdictional purposes, or if not, what those standards shall be; and
- c. determination whether the scope of this docket includes examination of the Company's deregulated cost assignment as well as its affiliated transactions costing methods.

SWBT's position is that the Commission's current rule adopts the FCC affiliate transaction guidelines as the appropriate standards to prevent cross-subsidization. SWBT is of the view that changes in the FCC's affiliate transaction rules cannot and should not be made in this docket. An NPRM is now open at the FCC which would allow Staff adequate opportunity to address the perceived need for changes to the FCC rules; and that any change in the Commission's standard for judging the reasonableness of affiliate transactions must be developed generally for all utilities, at least for all telephone utilities, and not be limited to SWBT.

Staff suggests to the Commission that the first order of business of this docket should be to determine if the FCC's affiliate transaction rules will be the appropriate standard, or, if not, whether a modified standard should apply in determining the reasonableness of transactions between affiliates, and then address the remaining questions in light of those standards.

Staff believes that the scope of this docket includes the Company's costs assignment to its deregulated operations. SWBT disagrees with Staff and asserts that the scope of this docket excludes deregulated cost assignment and addresses only its transactions with separate, affiliated companies..

6. Staff suggests that the parties file their positions relating affiliated transaction and deregulated operation standards either jointly (if they agree) or separately by October 21. The parties should likewise file their position regarding the necessary components of an audit trail and necessary steps to ensure compliance with their affiliated transaction standard.

Respectfully submitted,

SOUTHWESTERN BELL TELEPHONE COMPANY

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