BOOK III

Show Me the Money:
RBOC Revenues, Expenses and Profits

Billions of Pennies, Nickels, Dimes, and Quarters

Chapter 14 RBOC Revenues, Expenses and Profits

Throughout the book we have claimed that the Bells have seriously overcharged customers — first, taking advantage of large holes in regulations, then as a swap promising to build the Info Bahn if regulators removed limits on our profits.

And the premise is simple. If you only add a few pennies, nickels, dimes and quarters to the price of services — since there are over 125 million Bell phone lines across America, the amount, billions of dollars, accrues very quickly.

Following the money trail requires us to give you the financial landscape of the Bells — how much money they make and how much profits they keep.

After the realization sets in, that these Bell utilities are more profitable than almost every other company in America, from the S&P 500 to the Business Week 1000, we will then show that almost all of the profits, 90+% are coming directly from telephone subscribers, not the hundreds of new businesses. (239)

For example, BellSouth, in its 1993 Annual Report shows that the company's entire profitability is not in international, wireless, or any other company initiative into new ventures, but almost all, over 95% of all PROFITS, were from the 'wireline services", i.e., the local subscriber. (240)

> "Approximately 95%, 97%, and 97% of net income for the years ended December 31, 1993, 1992, and 1991, respectively, were from wireline telecommunications services which were provided by BellSouth Telecommunications."

And we will make the case:

- that the Bell's profitability is excessive, out-performing almost all other companies in America.
- that almost all of it comes almost exclusively from the pennies, nickels, dimes and quarters on America's telephone bills.
- that all of the other businesses, are in essence funded through this excess profits.

Later, in Book IV we will travel down the Regulatory dirt road, showing that almost all of this money have been garnered because of faulty regulations and unkept promises of an Info Bahn future.

However, in order to make the case for overcharging, and the details to prove our points, we will first use Book III to discuss the basic revenues, while:

- **Book V** focuses on overcharging based on other analysts and comparing the Bells to other large market indicators

- **Book VI** takes a different approach and examines the specifics about overcharging by examining the charges on telephone bills — and how to save money.

First, the Facts:

The Bells are cash cows, short and simple. This is because of some simple business items.

- **They have a Captive Audience.** The Bells are still monopolies and have almost no competition. Customers must use their service, including all calling features, such as Touchtone service and Call Forwarding, or not have these phone services.
- **The Bells have Guaranteed Earnings** The Babies never had an unprofitable quarter or lost money from their phone services. Never. NADA. NOT ONCE.
- **The Bells Generated About $100 Billion Dollars** in revenues in 1996. Subscribers generated 80%+ of this revenues and 90%+ of all RBOC profits. The profits from the local services pays for all other business ventures, most of which have not been profitable.
- **The Bells Collectively Made $26 billion in Cash**, $14 billion in net profits in 1996.
- **In 1996, Bell Profits were about 150% Higher** than the Business Week ScoreBoard for Utilities (241), while profit margins were over 100% for the Business Week 1000. They out-perform companies as diverse as GM and Ford, or Sears & Roebuck and PepsiCo.

Road Map for this Section

So, let's follow the money. First, we're going to explore the Bells' revenues, — how much money they make each year. Then we'll ascertain how much money and profits came from telephone subscribers vs all of the other Bell ventures, clearly showing that their wealth has been created from just Plain Old Telephone services.

Some Very Basic Definitions Before We Start

This simplified model will be expanded upon during our discussions, but for the general reader, with little financial or telecom background, we hope this helps you keep track of following the money trail.

- **Revenues** are the monies a company makes when it sells a product or service. So, when you pay the phone company your monthly telephone bill, that's revenues.
- **Expenses** are all of the costs associated with the sale of a product. For example, printing the phonebill is an expense and so is keeping the staff necessary to make sure the network keeps running without problems.
- **Profits** are the money that's left over. **Net profits** are the remaining money, after everything, from taxes to dividends, has been paid.

RBOC Revenues, 1984-1996

Anyway you cut it, since 1984 the Baby Bells have grown by leaps and bounds. In 1996 they collectively made approximately $100 billion dollars, an increase of over $40 billion since the break-up — a hefty 72% increase in revenues.

And it is hard to imagine a fatter set of babies, considering that the average Bell Holding company made $14 billion dollars in 1996. The exhibit below highlights the revenues of the Bells from 1984 to 1996, showing BellSouth leading the pact with $19 billion annually, having grown 98% since 1984. (242)

EXHIBIT 33

RBOC Revenues, 1984-1996

(in the millions)

	1984	1996	Change
Ameritech	$8,378	$14,917	78%
Bell Atlantic	$8,090	$13,081	62%
BellSouth	$9,631	$19,040	98%
NYNEX	$9,573	$13,509	41%
Pacific Telesis	$7,830	$11,840	51%
SBC Communications	$7,191	$13,898	93%
US West	$7,284	$12,786	76%
Total Revenues	**$57,977**	**$99,337**	**72%**
Average Per RBOC	$8,282	$14,191	

Source: RBOC Annual Reports, 1984-1997

And the growth even between 1995 and 1996 has been huge — 1995 revenues were approximately $92.5 billion, increasing to almost $100 billion a year later — an average growth per-RBOC in one year of almost ONE billion dollars of revenue, each.

EXHIBIT 34

RBOC Revenue Growth 1995 to 1996

(in the millions)

	1995	1996	Growth
RBOC Total Revenues	$92,537	$99,337	$6,800

Sources: RBOC Annual Reports, 1995-1996

Chapter 15 The Money Details —Local Service, Toll Calls, Access Charges

When the RBOCs were created, they were each given specific local Bell telephone companies, which included the assets as well as the customers. These assets included not only the local telephone networks, but also the White and Yellow Telephone Directories businesses, as well as cellular licenses covering their entire regional fiefdom.

Baby Bell annual reports divide cash flows into five primary categories: These include (243)

- Local Service
- Toll Calls
- Access Fees
- Calling Features and Ancillary Services
- Other, including Directory, Wireless

These categories map loosely to your telephone bill charges, but they are not quite the same.

- **Local Service Revenues** are derived from a customer signing up for phone service, and it covers installation fees and deposits. It also covers the local monthly service, which connects the customer to the telephone network as well as local telephone calls.
- **Toll Calls,** (sometimes called "Intra-LATA", or "RBOC Long Distance") are calls that do not cross state or LATA boundaries. Revenues can also include corporate 800 service charges.
- **Access Fees** There are at least five different types of Access Charges. However, there are only three primary types of Access Charges that are included in a person's telephone bills. These Include:
    - **"Long Distance Access Charges"** which are fees paid by the Long Distance Company to the local telephone company for handling a local customer's long distance service. However, over 40% of the cost of every telephone long distance call made by a customer is paid back to the local company for access fees. We consider Access fees as 'pass-throughs"

i.e., the customer making the call is paying the fee, which is added to the cost of every telephone call.

- **Subscriber Line Charge** sometimes called an "FCC Line Charge" is a separate access fee charge usually costing $3.50 per month per line for residential subscribers, and $6 per line for business subscribers. This fee is directly collected and paid to the local telephone company.
- **Intra-state and Local Access Charges** Like long distance access charges, companies offering competitive Toll Call and Local competitors pay other form of access fees — Intra-state-Access Charges for Toll and Interconnection fees for Local service.

- **Calling Features and Ancillary Services** are almost everything else you as a customer pays for. This includes Touchtone Services, and basic Calling features such as Call Waiting, Call Forwarding, Caller ID, Other Services. Unlisted Numbers can also be included.
- **The "Other" Category** In RBOC Annual Reports, the Other Category is the garbage pail of line items, allowing everything and anything to be added. Ameritech's definition of this line item includes Cellular, Directory, and wire maintenance, among other services. (244)

> "Cellular, directory and other revenues include revenues derived from cellular communications, paging services, telephone directory publishing, lease financing, billing and collection services, telephone equipment sales and installation and security monitoring services....inside wire installation and maintenance and advanced data services. "

Note: Some companies include Calling Features/Voice Mail and Wire Maintenance in their "other" category in their annual reports, while some companies break out these statistics or place them in different financial "buckets", for their own reasons.

The most common list of items can or does include:

Directory	Billing and Collections
Financial Services/ Real Estate	Cellular
Equipment Leasing/Software	Foreign Investments

For example, as we have seen in the Real Estate and Overseas Investment discussions, these services can have billions of dollars tied up, sometimes making money, but many times being a loss leader. There are exceptions, however. Parts of this category, specifically services that were part of the original Bell System, such as telephone directories, are incredibly profitable. As we will discuss later, the Other category is used as a way to obfuscate the profitability of specific items, and it is a telecom shell game.

Also, some RBOCs have created separate subsidiaries, some break-out the revenues, while others still combine most information.

- **"Directory —** The publication of the Yellow and White Pages, (the original Bell Telephone books), accounts for most of the profits of this "other" revenue category. And Directory can produce very substantial revenues. BellSouth, in its 1996 year end quarterly report showed $1.7 billion in its directory Advertising and Publishing category. In their 1993 Annual Report they state: (245)

  "Ten years ago, we had no Yellow and White Pages directories outside nine-state region. Today we publish nearly 1,000 directories in 39 states and in six overseas markets."

Considering that each Bell company automatically received hundreds of directory markets, with standard profit margins of 50%, Directory has been a great source of profits.

- **Thousands of "Others" —** Over the decade the Bells have had thousands of other companies using the distinction of this category, from overseas operations, to even real estate and furniture manufacturers.

As we will see, though the Bells have ventured into hundreds of other businesses, after a decade, the local customer still supplies 80% of the revenues and approximately 90% of profits.

RBOC Revenues by Lines of Business, 1984-1996

In 1984, the Bells philosophy, as well as their earnings and expenditures were still mainly utility-customer-o-centric. The business mix consisted of the telephone companies as well as the other, primary, grandfathered-in businesses; the yellow and white pages, as well as the cellular licenses.

So, the question remains, how has the business mix of these revenues and profits changed over 12 years? Back in 1991 Ray Smith, President of Bell Atlantic, stated that by 1996 about half of the "net income" would be from Wireless, International, and business systems — net meaning profits after everything, from taxes to dividends, are paid off. (246)

> "We believe that, together, our international, wireless, and business systems lines of business will produce about 20% of our revenue stream in five years and will account for about half of our net income growth."

Unfortunately, like the Info Highway plans, the findings indicate that the profits almost all come from the basic telephone business services and over the last 12 years there has not been any major shift in the way the company makes money.

Below are the five major categories for the Bells combined revenue in 1984, compared to the current 1996 revenues. In 1984, the Bells had 44% of their revenues come from "Local Service", and almost 30% came from "Access Fees", 14% came from Toll fees. Meanwhile, only 13% accounted for other non-telephone services. This should not surprise the reader. In 1984, the Regional Bells were essentially just the telephone companies, which included the directory revenues, and the nascent cellular services. The companies had not expanded into hundreds of companies as they would do in the late 1980's. Nor was there a large number of customers for specialized. services. For example, according to Link Resources' "1985 Home Media Consumer Survey—Residential Telecommunications", based on 4,275 telephone surveyed households, only 7.7% of the population had Call Waiting, only 3.3% had Call Forwarding and only 7% even had an answering machine. (247) Therefore, the "Telecom Other" revenues most likely were included in the Local service statistics.

Exhibit 35
RBOC Business Revenue Breakout, 1984-1996
(In the Billions)

	1984	% of biz	1996	% of biz
Local Service	$25,550	44%	$40,967	41%
Network Access	$16,755	29%	$23,200	23%
Toll	$ 8,319	14%	$ 7,897	8%
Calling Features &			$ 9,361	9%
Directory & other	$ 7,372	13%	$18,985	19%
Total Revenues	$57,996	100%	$99, 919	100%

Remarkably, while revenue has increased over 70% since 1984, the bottom line is that the telephone companies, or rather, the telephone customers, still provide the overwhelming amount of revenue to the company.

Since the Regional Bells were worth almost $100 billion dollars in 1996, it is easy to calculate the amount of money and where it came from. For example, Local Service still commands over 41% of Baby Bell revenues and that equates to whopping $41 billion dollars in revenues. Similarly, Access charges is 23% of revenues, or approximately $23 billion dollars in the percentage of overall RBOC revenues — not a major change from the 29% of the business access fees accounted for in 1984.

Exhibit 35 shows that the non-bell revenues in 1996, here called "Directory & Other", as only 19% of revenues and this includes the wireless entities throughout the world, while all 'other' revenues in 1984 only accounted for 13%. (248)

Subscriber Based vs Non-Subscriber Based RBOC Revenues and Profits

Forget about real estate purchases, computer leasing, overseas operations or the billion lost from Tele-TV and Americast. When every line item in every RBOC annual report for the decade is cross-referenced, we find that approximately 80%+ of all revenues comes from the local telephone subscriber, and 90% of all profits. And this model has not changed dramatically over the last decade.

If you examine, in detail, the other Bell Holdings, which include US cellular RBOC holdings and their US directory holdings, almost all of which were grandfathered to the Bell Companies, only 6-10% of revenues is based on non-Bell products.

The trail to find this data can be daunting, since the Bells no longer have to reveal the details of most transactions. (without exact breakouts from the Bells, it is impossible to get the exact amount) However, there are other indications by the Bells themselves that the majority of money is from telephone products. For example, NYNEX's 1995 Annual Report stated that 88% of revenues were from the telephone companies. (249)

> "The Telephone Companies mainly provide two types of telecommunications services, exchange telecommunications and exchange access, in their respective territories. The Telephone Companies revenues comprise 88.1% of NYNEX's operating revenues in 1995." [emphasis added]

NYNEX used to publish a more detailed different analysis of wire (meaning local phone customer) vs. non-wire business profits in their annual reports. As demonstrated in the exhibit below, taken directly from NYNEX Annual Reports, from 1989 to 1993. Telecommunications generated an average of 85% of the revenues, compared to cellular services which generated only 3% of the revenues. However, on the profits side, telecommunications generated 103% of the profits. (250)

EXHIBIT 36

NYNEX Revenues and Profits, by Lines of Business 1989-1993

(In the millions)

	Revenues	Profits	% of Rev.	% of Total Profits
Telecom	$11,303	$2,439	85%	103%
Cellular	$ 360	$ 38	3%	2%
Publishing	$ 858	$ 67	6%	3%
Financial	$ 83	$ 51	1%	2%
Other Revs.	$ 703	$(225)	5%	-9%
Total	$13,308	$2,371	100%	100%

Source: NYNEX Annual Reports, NNI 1994

To summarize, NYNEX's telecommunications (which is mainly local telephone customers) accounted for 103% of profits over the five year period, while all other businesses combined lost 3%. (NOTE: NYNEX no longer provides this information in this format.)

BellSouth also gave information showing that the telephone company revenues, BellSouth Telecommunications, accounted for varying amounts during the 1990's, from 73%-76% of the total business. (251)

> "Approximately 73%, 74%, and 76% of BellSouth's operating revenues for the years ended December 31, 1993, 1992, and 1991, respectively, were from wireline telecommunications services which were provided by BellSouth Telecommunications."

And more recently, Bell South's 1995 Annual report stated that 71% of Revenues were from BellSouth Telecommunications. However, the fine print showed that Telecom accounted for at least 77% of the total in 1996. (252) Wireless and Directory accounted for 23% (15%+8% respectively.) This shell game did not count the profitable "Access Fees" as part of local service.

> "Approximately 71% of BellSouth's total operating revenues for each of the nine-month periods ended September 30, 1996 and 1995 were from wireline services provided by BellSouth Telecommunications. Charges for local, access and toll services for the nine-month period ended September 30, 1996 accounted for approximately 61%, 33% and 6%, respectively, of the wireline revenues discussed above. Revenues from wireless communications services and directory advertising and publishing services accounted for approximately 15% and 8%, respectively, of Total Operating Revenues for the nine months ended September 30, 1996. <u>The remainder of such revenues was derived principally from other nonregulated services provided by BellSouth Telecommunications."</u> [emphasis added]

Therefore, taking this into account, NNI estimates that BellSouth had at least 77%+ revenues from subscribers — However, BellSouth's 1993 Annual Report shows that the company's entire profitability is not in international, wireless, or any other

company initiative into new ventures, but approximately 95% of all PROFITS, were from the local subscriber. (253)

> "Approximately 95%, 97%, and 97% of its net income respectively, were from wireline telecommunications services which were provided by BellSouth Telecommunications. "

Probably the clearest example exposing which parts of the RBOC businesses are providing the revenues and profits comes from examining the US West. The company split itself into two companies, US West Communications Group, the telephone company, and US West Media Group, a media company representing all other businesses including Directory, Wireless, and Multi-media.

Exhibit 37, taken from US West 10Ks from 1995 and 1996, shows a simple model of the two companies combined. The entire company had $12.2 billion dollars, the media company consisting of only 22% of these revenues, including its directory, wireless, cable services, information services, international, etc, — telecommunications was 78%. However, in the grand scale of things, the media company only represented 3% of the total net profits (% of Net), while the phone company made $1.2 billion and accounted for 97% of the total profits. (254)

Exhibit 37
US West Communications Group and US West Media Group,
Revenues and Net Profits, 1995-1996
(in the millions)

	Revenues	% of Rev	Net	% of Net
Telephone Company	$ 9,558	78%	$1,233	97%
Media Company	$ 2,665	22%	$ 35	3%
Total	$12,222		$1,268	

The reason for this disparity is simple. The Media company is heavily involved in developing new cable and wireless services worldwide, and therefore, spends more than it makes. And it will continue to do so for years. However, many of the assets from the original Bell system, especially directory and the cellular services which are bringing in

cash, are offset by the other non- bell businesses, and these companies are not profitable, at least in the short term.

Where Has the RBOC Revenue Growth Been Over the Last 10 Years? Local Telephone Subscriber Services.

The significant growth in revenues of the Bells can only be attributed to local telephone subscriber services, specifically:

- Growth in the number of phone lines, specifically second lines.
- Growth in the number of calling features.

First, an examination of the number of Bell phonelines reveals a steady growth since 1984, with an overall increase of over 40%. In 1996, the Bells had 126 million lines, up from 89 million in 1984. (255)

Exhibit 38
RBOC Access Lines, by RBOC, 1984-1996

	1984	1996	% of Change
Ameritech	14,337	19,704	37%
Bell Atlantic	14,677	20,566	40%
BellSouth	14,000	22,135	58%
NYNEX	13,225	17,824	35%
Pacific Telesis*	11,310	16,485	46%
SBC Comm	10,650	14,955	40%
US West	10,871	15,424	42%
Change	89,070	126,446	42%

(Also, the Bell residential lines outnumber business lines, with approximately 65% of all lines dedicated to residential customers. Business customers, at least by lines, hold only approximately one-third of lines. However, Business customers are charged

more for most services, so the two groups, business and residential customers spend approximately the same.)

Over the last few years, much of the growth has not been from new business or residential customers, but in the massive increases in second lines, dedicated to the Boomer households (with kids), the Internet and fax machines.

For example, BellSouth stated that 1996 was a banner year, spurred on by the addition of new lines, especially for work-at-home, fax machines and children's numbers. (256)

> "Capping a year of record customer growth, BellSouth Corporation became the first telecommunications company to grow by more than one million access lines in a single year.
>
> "New retail distribution channels and marketing promotions of phone lines for Internet access, work-at-home, fax machines and children's numbers spurred record fourth quarter sales of 82,000 additional residential lines."

That's approximately 300,000 second lines in 1996!

As discussed in previous sections, what happens with one Bell is most assuredly happening with all other Bells. For example, Southwestern Bell's 1996 Summary stated that additional lines went up 14% in 1996 alone, almost 1/3 of all new lines added. (257)

> "Southwestern Bell added 732,000 access lines during 1996, compared with 611,000 during 1995, for a total of 15.0 million access lines at the end of the year. Additional line penetration increased to 14.5 percent, reflecting the sale of 214,000 additional lines during the year."

Meanwhile, Bell Atlantic stated that additional lines in their region grew 24 percent, accounting for 2.1 million lines. (258)

> "Total additional lines in service grew almost 24 percent during 1996, approximately 2.1 million. "

Massive Growth in Calling Features

But it has been Calling Features, products including Call Waiting, Call Forwarding, Caller ID and Voice mail that have all been big revenue winners. For example, Bell Atlantic stated that sales of 'Value-Added" products, like Caller ID have all jumped in revenues. According to Bell Atlantic (259)

- "Revenues from Home Voice Mail (formerly Answer Call) and central-office-based services such as Caller ID, Return Call and Call Waiting were up more than 23 percent compared with 1995.
- "Caller ID revenues nearly doubled as subscribers grew to about 2.3 million.
- "Revenues from Return Call, in some markets now featuring a voice-recorded readout of the calling party's number, jumped more than 40 percent, with a 50 percent increase in activations in the business markets."

BellSouth's 1996 summary states that Calling Features "surpassed $1 billion" in revenues in 1996, with over 29 million features sold. (260)

> "Sales of BellSouth's calling features and convenience services, such as Caller ID, Call Waiting and MemoryCall® service voice messaging, continued to grow rapidly. With more than 29 million features currently activated, revenues from these services surpassed $1 billion for the first time in 1996."

NOTE: BellSouth had 22 million lines and 29 million features currently activated, which means that on the average, each line had 1.3 calling features in 1996, a fact that we will address later in profitability models.

Meanwhile, Ameritech showed an almost 25% increase in calling features in 1996. (261)

> "23.5% annual growth in sales of call management services such as Caller ID, call waiting and voice messaging."

The bottom line is that the overwhelming majority of Regional Bell revenues comes directly from the telephone subscribers, not new businesses as Ray Smith had hoped in 1991.

With $100 billion dollars of revenues by the Bells, and 80% of the revenues and approximately 90-95% of the profits accruing in from the local telephone subscribers — How much profit is there?

How Much Profits Are There?

In 1996 the Bells had **$26 billion dollars in Cash,** 23% higher than in 1995. Also, there was almost **$14 billion in NET INCOME**, 74% higher than the year before! (262)

Some Very Basic Definitions:

- **Operating Revenues** are the money the company makes doing business.
- **Operating Expenses**, are the costs of doing business.
- **Cash or Operating Income**, is essentially the company's revenues, minus the working expenses.
- **Net Income** is the companies final income after paying off everything from the shareholder dividends to income taxes.

This next exhibit summarizes the **Operating Revenues**, and three other very important statistics from 1995 and 1996

EXHIBIT 39

Summary of RBOC Revenues, Expenses and Profits, 1995-1996

(in the millions)

All Seven RBOCs	1995	1996	CHANGE
Operating revenues	$92,537	$99,337	8%
Operating expenses	$71,469	$73,946	3%
Cash	$21,068	$25,973	23%
Net Income	$ 7,881	$13,700	74%
% of cash to revenues	23%	26%	

No matter how you slice it, $26 billion is a lot of cash. However, these statistics account for the entire Bell's businesses, included losses. Therefore, other more detailed statistics are needed to demonstrate the profits from subscribers' services. A clear example are Calling Features or even Touchtone service.

Profits from Calling Features

The profitability of most calling features is, for a lack of a better term, extreme. According to the New York Times (1/1/4/97) Ameritech's Caller ID and Voicemail have profit margins greater than 50%. (263)

> "Ameritech has been promoting services including Caller ID and voicemail, which can carry profit margins greater than 50%".

And some services, from Touchtone, to Unlisted Numbers are almost entirely profits. We will visit more detailed discussion of profits in the Book VI, Overcharging on Your Phonebill.

Chapter 16 Cash Cows: Comparing the Bells To Other Companies

Let's put the RBOC's massive profits in perspective by comparing the Bells profits to other free-market businesses and other Utilities.

According to SBC Communications, if an investor invested $100 dollars in SBC in 1984, their return by 1995 was $1095, almost 100% higher than the Standard & Poor 500, which represents some of America's largest companies. (264)

EXHIBIT 40

SBC Communications Cumulative Total Return, 1983-1996

YEAR	SBC	S&P 500	All Bells
83	$100.00	$100.00	$100.00
84	$128.92	$106.22	$133.92
85	$167.53	$139.83	$190.87
86	$233.47	$165.86	$250.04
87	$227.35	$174.45	$255.85
88	$284.08	$203.23	$299.34
89	$471.46	$267.43	$462.48
90	$434.31	$259.10	$449.73
91	$526.34	$337.71	$461.43
92	$630.18	$363.40	$504.60
93	$733.29	$399.86	$594.22
94	$740.54	$405.28	$569.86
95	$1085.03	$557.05	$861.61

Meanwhile, the Bells as a group made approximately 55% more than the Standard & Poor 500.

Ameritech has also had returns that far exceed the Standard and Poor 500. According to Ameritech's 1995 Annual Report, they had a 965% cumulative total return, 111% higher than the S&P 500. (265)

> "Since our stock began trading in November 1983, Ameritech investors have earned a cumulative total return of 965%-- more than double the total return of 457% for the S&P 500."

And 1996 was a banner year according to US West. US West stated in its 1996 4th Quarter Report, that including dividends, they had a "total return for the year was 61.2 percent." (266)

> "By year end, the new U S WEST stocks combined were up 53.3 percent for the year. Including dividends, total return for the year was 61.2 percent. The market value of your company increased $8.9 billion during the year."
>
> "An investment in U S WEST was up more than the average of regional "Bell company" stocks for the year, and more than the average of 500 stocks measured by the commonly used Standard & Poor's index"

Out performing the S&P 500 is just one of the indicators that the monopolies' profits are way out of line with a company who is supposed to have controlled earnings. Another simple example of the Bell's performance is to compare it to other companies, which have active competition.

The Wall Street Journal, 2/27/97, (267) ran an article discussing 8 major US companies revenues and profits. The companies are General Motors, Ford Motor, Boeing, Eastman Kodak, Sears Roebuck, JP Morgan, Caterpillar, and Kellogg. Combined, the companies had $435 billion in sales with net profits of only $16.2 billion. The RBOCs, on the other hand, had a whopping $14.3 billion in profits on only $100 billion, the RBOCs out profiting our big 8 by 275%.

EXHIBIT 41

Big 8 Company Revenues and Profits vs RBOCs, 1996

(in the billions)

	Revenues,	Profits,	% of Profits
Big Eight Total	$425	$16.2	4%
RBOCs	$100	$14.3	14%
Difference	275%		

Just to hammer in the point the Bell's profits are excessive, let's compare one other major business indicator, the Business Week ScoreBoard, which has been tracking company performance for decades. Business Week ScoreBoard not only uses standard business measurements such as "Return-on-Common Equity", "Earnings-Per-Share" and "Profit Margins", but also gives the information by industry, for Utilities or chemical companies.

Business Week Definitions: (268)

- **Return on Common Equity:** Rate of Net Income available for common stockholders (most recent 12 months) to latest available common equity, which includes common stock capital surplus and retained earnings.
- **Earnings Per Share:** For the most recent 12 months period Includes all common-stock equivalents.
- **Profit Margins:** Net income from continuing operations before extraordinary items as percent of sales

Let's start with the Bell's 1996 stats for these three indicators. Notice that the Bells averaged 28% return on equity, with Pacific Telesis topping the pack at 40%. Meanwhile the Bells averaged a 12% profit margin. (269)

EXHIBIT 42

RBOC Return on Equity, Earnings and Profit Margins, 1996

	Return-On-Equity	Earnings-per-Share	Profit Margin
Ameritech	28.8%	$3.87	14.7%
Bell Atlantic	23.9%	$3.96	10.3%
Bell South	21.6%	$2.88	12.5%
NYNEX	19.9%	$3.08	11.4%
Pacific Telesis	40.3%	$2.47	7.8%
Southwestern	30.7%	$3.46	14.4%
US West	31.8%	$2.55	12.0%
RBOC Total	28.1%	$3.18	11.9%

Source: Business Week ScoreBoard, 1996

But the kicker is in the Business Week comparisons, among other businesses as well as other Utilities. Featured in the exhibit below, the Utilities averaged only 11% return-on-equity, making the Bell's returns almost 150% higher. Meanwhile, the average for American Business profit margin is only 5.9%. The Bells, profitability was over 100% higher than the average Business Week 1000. The Bells even pay out 50% more than utilities in Earnings Per share. That's a whole lot of enchiladas. (270)

EXHIBIT 43

Comparing RBOCs 1996 Profits to Other Businesses

	ROE	Earnings Per Share	Profit Margin
RBOC Total	28.14%	$3.18	11.9%
All Industries	16.80%	$2.44	5.9%
Utilities	11.40%	$2.10	6.7%
All Industries	68%	30%	102%
Utilities	147%	51%	78%

Source: Business Week ScoreBoard, 1996

It can be argued that since the Bells are still considered utilities, and are therefore governed by the state Public Utility Commissions, the Bells return-on-equity should have stayed at 11%, instead of the current 28%.

Of course the reader should ask: "If the company has no real competition today, and its revenues are guaranteed and therefore have virtually no risk, shouldn't they be making less money than companies with serious risks?"

Before we explain just how much money the Bells have been able to pocket, and the regulation that allowed them to do it, let's look at two other important facts. There has been massive decreases in two major expenses, the number of employees and lack of new construction. Therefore, prices should have plummeted, and profits should have remained lower.

Let's examine the employee cuts and explain how construction has been stillborn, even though the promises have been sky-high.

Chapter 17 Employee Cuts and Poor Customer Services

Throughout the last decade, the Baby Bells have been aggressively been reducing staff, sometimes referring to it as "new productivity efficiencies" or at other times "getting ready for competition". Either way, staff cuts have been deep, — over 235,000 people to date, and almost all cuts have come from the local telephone company employees who work for local customers. The irony is that almost all telco filings related to the information Superhighway stated that the Info Bahn would create new jobs. (271)

Employee cuts have yielded continuing cost-of-doing-business decreases, and ever increasing profit margins. For example, NYNEX's 3rd Quarter 1996 report shows massive savings of $650 million dollars from staff layoffs and restructuring of the company. In fact, when the final restructuring is finished and 16,200 NYNEX employees have been laid-off, the company expects a whopping $1.7 billion dollars savings, annually. (272)

> "Since the inception of process re-engineering and the special pension enhancement program in 1994, approximately 11,900 employees have accepted the retirement incentives. On an annualized basis, this will equate to an average reduction in wages and benefits of approximately $650 million.
>
> "It is anticipated that the restructuring will result in reduced costs during the period of restructuring and reduced annual operating expenses of approximately $1.7 billion beginning in 1997. These savings include approximately $1.1 billion in reduced wage and benefit expenses due to lower work force levels, and approximately $600 million in non-wage savings including reduced rent expense for fewer work locations and lower purchasing costs. Partially offsetting these savings are higher costs due to inflation and growth in the business." [emphasis added]

Staff cuts have also led to serious fallout. — Customer complaints. Numerous states' Public Utility Commission have levied fines on the Bells for not being able to answer their telephones. We will return to the customer dissatisfaction shortly. But first, let's explore the cause, massive employee cuts.

Bell Employees: Walking Through the Numbers

In order to help the reader understand employee lay offs, we will walk through this section in steps.

Step One: Staff at the Baby Bells— How it Works

The Regional Bell Operating Company is a holding company which controls a number of smaller local telephone companies. For example, Ameritech owns five local state phone companies: Ohio Bell, Michigan Bell, Illinois Bell, Indiana Bell and Wisconsin Bell. Therefore, the Regional Bell, tells the local telephone companies to cut staff. Meanwhile, the parent holding company, Ameritech, added staff for it's various projects and services.

Step Two: Total Bell Employees

In 1984, the RBOCs had a total of 577,000 employees. By the end of 1996 there was 387,900 total workers, a -33% decrease. The next exhibit highlights just the RBOC staff cuts. The first exhibit shows the total Regional Bell reductions of staff, including the holding companies and its subsidiaries, from 1984 throughout 1996. (273)

EXHIBIT 44
Total RBOC Employees Cuts, 1984-1996

	# of employees	% laid off
Number of Employees in 1984	577,398	
Total RBOC, 1996	387,900	-33
Cuts from Regional Bells	190,498	

Sources, RBOCs, NY Times, 1996, Washington Post, 1995, NNI, 1992-1996

Step Three: The Lay-offs 1994-1997 Most of the staff reductions were announced in late 1993 and early 1994 and have effected the last three years. These cuts, including a whopping 21,500 at Bell South or NYNEX's 16,800, were all designed as "cost efficiencies". (274)

EXHIBIT 45
Announced RBOC Staff Reductions for 1994-1996

Ameritech	7,500
Bell Atlantic	5,600
Bell South	21,500
NYNEX	16,800
Pacific Telesis	20,500
Southwestern	1,500
US West	9,000
Total RBOC	82,400

Sources: NY Times, 96 Wash. Post, 95, NNI, 1995, Telephone cos.

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However, the overall numbers presented do not reveal the real changes that occurred over the decade. The primary change, and not for the better, has been a serious reduction of staff from the local telephone companies. While the holding companies had staff increases, the local telephone companies had massive decreases.

Step Four: Holding Company vs Local Phone Company: The next exhibit shows that the local telephone companies, specifically the staff that handles the telephone subscriber, has had much deeper cuts. The phone companies lost 235,000 while the parent company, added 45,000 staffers.

In fact, based on announced cuts, by 1997 there will be 236,000 local telephone company staff reductions. (275)

EXHIBIT 46
Summary of Data for Local Telephone Company RBOC Employees, 1984-1997

Telephone Company Staff Cuts		
Increase of Parent company	45,056	142%
Total Reductions, 1984-1996	235,550	-31%

Sources: NY Times, 96 Wash. Post, 95, NNI, 1995, Telephone cos.

Step Five: The largest cuts have been to telephone company staff that handles the local subscriber.

Since the flood, "Employees-per-line", the standard benchmark for the number of employees working for subscribers, dropped an average of 57% from 1984-1997. (276) That's half the staff required to cover more work.

EXHIBIT 47
RBOC Employees-Per-Line Cuts, 1984-1997

Employee-per-line reductions	-57%

Source: New Networks, 1995, Telephone company reports.

Step Six AT&T Break-up cut staff too: It is a little known fact that 75,000 other local telephone company staffers were cut between 1983 to 1984, during the AT&T break-up, bringing the total of cut local telephone company workers to 310,000. (277)

EXHIBIT 48
Local RBOC Phone Company Staff Cuts in 1983 to 1997

AT&T Local total From 1983 to 1984	75,000
Total RBOC Reductions, 1983-1996	310,550

Sources: AT&T & RBOC annual reports., NNI 1992-1996

Staff Cuts Lead to Customer Dissatisfaction and Fines.

One has only to go to web sites such as nynexsucks.com or USWorst.com to know that customers are having problems with their service. In fact, from the subscriber perspective, the massive staff cuts have had a detrimental impact on telephone subscribers, revealed in both the rising number of complaints as well as consumer surveys which found a growing resentment to the Bells.

For example, JD Powers Consumer Study of phone service found that for at least three RBOCs, an average of 26% of customers were not satisfied with their phone

company's services. Also, the exhibit below shows that only 75% of complaints were resolved in a timely manner, with NYNEX having only 70% of complaints actually dealt with promptly. (278)

EXHIBIT 49
Customer Complaints and RBOC Dissatisfaction, 1996

	% of dissatisfied customers	Resolved in a timely manner
Bell Atlantic	22%	71%
NYNEX	29%	70%
SBC	33%	82%
Avg.	26%	75%

Source: JD Powers and Associates

Our consumer surveys from 1993 and 1995 show a dramatic increase in Bell customer dissatisfaction. In 1995, almost 39% of the population gave the Bells a failing grade in one of seven customer service areas, more than double the number of dissatisfied customers in 1993. (279)

EXHIBIT 50
Consumer Grades for Local and Long Distance Cos., 1993-1995

1993	1995	
15%	39%	gave the local telephone company a failing grade in one of the seven customer service questions

Source: NNI Proprietary research, 1993-1995

Also, complaints are up across America. Court cases and Public Utility Commissions (PUC) actions have occurred in numerous states in the Ameritech, US West, Pacific Telesis, and NYNEX regions.

According to an LA Times article, (6/18/95) the Ohio's PUC received 10 times the number of complaints in 1994 than the previous year, while NYNEX missed 142,000 appointments in the last three months of 1994. (280)

And the problem continue. According to NYNEX's 1996 3rd quarter report, "New York Telephone will be required to issue rebates to customers of at least $102 million for not maintaining adequate service standards. (281) As a New York Post columnist, Irwin Stelzer, put it:, (2/26/97) (282)

> "**NYNEX fails to show up at about 1,000 repair appointments every business day."**

The New Jersey Ratepayer Advocate, in their review of Opportunity New Jersey and the Bell Atlantic NYNEX Merger stated that NYNEX's states, including New York, Massachusetts and Maine all had monetary penalties, while New Jersey has also had a declines in service. First about NYNEX: (283)

> "NYNEX has had an abysmal track record with regard to quality of service. In the last three years, NYNEX has been punished for its failure to meet telephone service quality standards and, consequently, subject to monetary penalties in at least three of the jurisdictions in which it operates: New York, Massachusetts and Maine. In New York alone, in November 1996, the Commission found that NYNEX's performance warranted $72.9 million in penalties, and after granting certain waivers, ordered $62.3 million in rebates. "

Bell Atlantic/New Jersey: (284)

> "BA-NJ's quality of service has also declined since the adoption of the Plan. Although the decline has been from a high level of service, any decline should however be of major concern to the Board, especially when quality of service should be increasing under the Plan, since the company is deploying cutting edge technology. For example, BA-NJ's performance in the following service categories was lower in the year ending September 1996 than in 1993, 1994, and 1995: (1) percentage of service

> order provisioning completed within 5 working days; (2) percentage of service order provisioning appointments met; and (3) percentage of directory assistance calls answered within 10 seconds. "

NNI's position on staff reductions is simple. The ratepayer is the one who is being impacted by the staff reductions because services are not getting better. In fact, in some areas, such as customer services, the reductions have meant more time on hold and more complaints to the PUCs about service.

While the Baby Bells state that productivity is really a goal, the reader should ask: In a non-competitive environment, are staff cuts productivity driven or shareholder-profits driven?

Secondly, we contend that staff reductions have decreased the ability for the remaining staff to provide adequate subscriber coverage, including their installation and implementation of ISDN. Based on the data presented, we expect the problems to get worse, not better.

Other customer service issues also should also be examined. For example, most Bell companies only offer live customer services from 9 AM to 5 PM, and few companies have hours on Sunday. In future sections we will argue that the utility has an obligation to expand its customer operations, including adequate staffing of customer services.

Finally, why haven't prices decreased dramatically if the cuts in staff have been saving so much money?

Chapter 18 New Construction by the Bells? —NOT

According to the United States Telephone Association, USTA, there's a great deal of investment in the telecommunications network — a whopping $20 billion dollars annually. (285) USTA, January 22, 1997)

> "Local telephone companies continue to invest more than $20 billion annually in maintaining and upgrading this network. All other users must pay their fair share or the problems we are facing now will indeed perpetuate." [emphasis added]

In fact, since the companies are putting up so much money, the USTA believes that the Internet users are not paying their fair share: (286)

> "Someone has to pay for that usage, the subsequent wear and tear on the network and the new equipment additions necessitated by this rapid growth.
>
> "The bottom line is that all companies, whether they provide long distance, Internet access or local telephone service, must pay for use of the world's most advanced telecommunications network."

$20 billion sounds like a great deal of money, right? (this figure represents all local companies, including the Regional Bells, as well as the independents, including GTE.)

Unfortunately, the Bells spending on new construction has been decreasing annually and the expenditures for the I-Way is simply corporate myth. In fact, the Bells spent more in the early 1980's than the have over the last decade.

Before we go into the details of why construction expenditures have been steadily decreasing over the last 13 years, (even though the companies' revenues have soared) let's first understand the basics. What are capital expenditures and construction expenditures anyway?

What are Construction Expenditures?

Construction/Capital Expenditure Definitions

Construction expenditures, sometimes called "Capital expenditures", are an assortment of costs, with the bulk of these charges applied to maintaining the current telephone networks, and the replacing of older technology with newer equipment. In terms of your telephone service, the wire that connects your home or apartment to the street's main wiring, the wiring that criss-crosses America on poles and underground conduit, as well as the big network equipment that routes calls across America, are all part of construction expenditures.

The specific items include:

- **Cabling and wiring**, including underground cable, buried cable, aerial cable poles, to deep-sea cable and submarine cable.
- **Central Office switches,** is basically an aggregator of phone calls for a specific geographic area and connects all telephone lines in a specific location.
- **Network Switches and Databases,** are other large computers attached to equipment that routes phonecalls across the neighborhood, city, state, or to long distance companies.
- **General Plant support,** which is the land, buildings, and general purpose computers.

There are two primary types of switches: analog and digital.

- **An analog switch** is based on older technology, and in most cases, it cannot deliver many of the newer enhanced calling features, such as Caller ID, etc.
- **A digital switch**, is a more enhanced model, which gives enhanced calling features, and provides "equal Access".

Some construction expenditures are used to upgrade the switch, sometimes with new software, other times replacing older analog switches with newer digital ones.

Now back to our story.

In truth, while $20 billion does sound like a lot of money, the actual spending by the Bells, as a percentage of their revenues, has been in continual decline — and worse, there is little to show that the companies ever put their money where their mouth was when it came to building the Info Bahn.

First, the $20 billion dollar figure quoted by USTA is the total including all of the independent phone companies, including GTE and Sprint. Combined with the Bells, local service providers accounted for a whopping $125 billion, the RBOCs $100 billion, and the independents $25 billion.

However, when the independent companies are removed, the Bell construction expenditures, as revealed in annual reports and filings, averaged about $16 billion from 1984-1996. (287)

Under Construction — or maybe Lack of Construction.

And the money spent on work that is "under Construction", has been virtually flat the last 13 years. Below is an aggregate of Ameritech, SBC Communications, Pacific Telesis and Bell Atlantic. With an overall 13 year average of $448 million a company. This group of Bells, which was supposed to be spending over $30 billion in new monies, had more construction occurring in 1984 and 1989 than they did in 1995 or 1996. (288)

EXHIBIT 51

RBOC, Under Construction, 1984-1996

(in the millions)

1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996
$498	$481	$444	$382	$358	$491	$480	$412	$467	$493	$429	$458	$433

The bottom line is that these companies did not spend money on the Info Bahn. In fact, they are spending about the same amount as they did 13 years ago even though revenues from local services, toll calls and access fees increased 52% from 1984-1995.

Let's put it another way. In 1984, the RBOCs' revenue was approximately $60 billion dollars and they were spending $16 billion. Today, they are bringing in $100 billion and still spending $16 billion. What this means is that their expenses for construction has decreased from 27% of revenues to only 16%, a drop of 60% relatively.

In fact, when the Consumer Price Index (CPI) is applied, the actual dollars spent on construction expenditures has gone down an astounding 74%. (289) (We bring up this index analysis because all telephone statistics presented by the FCC and the Bureau of Labor Statistics are based on the CPI, and according to these government analyses, telephone charges haven't gone up, it has simply followed the CPI's path.)

Construction Promises Unkept

In fact, the obviously massive expenditures that would be required to build the I-Way were never allocated or spent. For example, Pacific Bell specifically states in its 1993 Annual Report: (290)

> "In November 1993 Pacific Bell Announced plans to invest about $16 billion over the next seven years to upgrade its core infrastructure and to begin building an integrated telecommunications, information and entertainment network providing advanced voice, data, and video services." [emphasis added]

Unfortunately, NNI found that Pacific Telesis has not had any major increases in "Capital Expenditures", and the company spent more money on the telephone network in the mid-1980's than they do today. (291)

EXHIBIT 52
Pacific Telesis Construction & Capital Expenditures, 1984-1996
(In the Billions)

1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	95*	96'
2.1	2.3	2.2.	2.2	1.6	1.9	2.1	1.7	1.8	1.9	1.7	2.1	1.8

The only new construction seems to be promises more than anything else. According to their 1996 annual report, PacTel promised to spend $2 billion for new equipment in 1998, but even that commitment was never firm. (292)

> "In December 1994, Pacific Bell contracted for the purchase of up to $2 billion of Advanced Communications Network facilities, which will incorporate emerging technologies. Pacific Bell is committed to purchase these facilities in 1998 if they meet certain quality and performance criteria. Management now expects the actual amount of these facilities purchased in 1998 will be less than $700 million. "

More to the point, SBC, who purchased Pacific Telesis, wrote-off its Info Bahn expenses and the total was a mere $438 million for both companies. Ergo, there never was any major Info Bahn construction push. According to SBC Communications, July 1997. (293)

> "Curtailment of Video and Hybrid Fiber-Coaxial Initiatives: Discontinuance of broadband video trial in Richardson, halt construction of hybrid fiber-coaxial network in San Jose and San Diego, scale back Tele-TV, and redefine Americast joint venture $438 million."

Or take the case of Bell Atlantic, who was supposed to spend $11 billion dollars. Once again we quote the New Jersey Consumer Advocate on New Jersey Bell's failure to put its money where its promises are. (294)

> "Although Bell Atlantic-New Jersey (BA-NJ) projected that it would expend approximately $1.5 billion in network investment above "business as usual" by the end of 1999...From 1992 to 1996, BA-NJ has spent $545 million less than it forecasted in 1992...For the years 1993 through 1996, the Company's own projections stated that BA-NJ would spend $632 million above "business as usual" under Opportunity New Jersey ....However, the Ratepayer Advocate has calculated that BA-NJ has spent a total of $79 million above "business as usual" over these years."

Ameritech has also been spending less and less on new construction. (295)

> "Investment in technologies that will enable the company to provide customers with new products and services represent a high priority. Capital spending in the core landline telephone business declined by $265 million in 1993 and further declined by $100 million in 1994 as capital was deployed more cost effectively and with greater focus on the requirement of customers."
> Source: Ameritech 1994 Annual Report [emphasis added]

Is it no surprise then when the Michigan PSC's assessment of the implementation of Michigan Bell's (Ameritech) Alternate regulation, which will discussed in Book III, the Regulators and the Laws., found none of the promised spending for new construction (296)

- "Construction programs for Michigan Bell have been reduced since the enactment of the act."
- "The act has not increased the number of new services."

Massive Network Write-Offs: Depreciation = FREE CASH?

Construction expenditures are the outplays of Cash for the network and its ancillary needs, while Depreciation is method the company uses to slowly write off the costs.

And for a non-accountant, **Depreciation rates** are hard to understand, mainly because it serves as both an expense, as well as Cash the company can spend. However, billions of dollars are being overcharged using this basic accounting principle.

For example, in 1992 Consumer Federation of America (CFA) stated that the Bells were overcharging $3 billion dollars annually in just depreciation fees, up from a billion in 1986. (297)

> "In 1986 CFA estimated excessive rates resulting from accelerated depreciation of approximately $1 billion per year. Assuming that

> depreciation rates should have remained constant after divestiture, we estimate current excessive depreciation expenses of $3 billion per year. "

How Depreciation Works: A company purchases a few computers for say $10,000 in 1990 and every year the value of the computers goes down — the value is said to "depreciate". In business accounting, though a company may purchase the computers in a specific year and pay for it in that year, i.e. you purchase a computer for $10,000 dollars and you pay all of the money at the time of purchase. The company can break up the expense over a period of years, commonly known as the "life of the product". So, instead of deducting the entire amount for the computers, the company "depreciates the expense", i.e., divides the expense up over a number of years. So if the company assigns the computers' useful life as 5 years, the company deducted $2,000 for each year.

In the case of the Bells, the telephone company network and equipment each year depreciates, and the company takes a specific expense per year as the network gets older.

And there's a very lucrative catch to this entire story. According to "How to Profit from Reading Annual Reports" by Richard B. Loth, 1993 (298) depreciation deductions are really "cash" — cash the company can spend or purchase items with. It's in the formula:

Net Income and Depreciation = Cash Flow

According to author Richard Loth

> "For many financial commentors and investment information/advisory services, the sum of net income and depreciation represents *cash flow."*

And it's free cash because the expense of the item was long paid for. For example, most of the existing telephone network was paid for decades ago, and a 30 year write-off was common —i.e., the life of the network part, such as the copper wiring, was estimated to last 30 years, and therefore, the cost, which was paid for 30 years ago, was still being deducted, little by little, over three decades.

Accelerated Depreciation = More Cash Today

When you **'accelerate'** the depreciation, it means the depreciation expense that is deducted per year is increased, while the number of years is lessened.

For all those non-financial readers who may have serious cognitive problems with this rather odd phenomena of accounting — that an expense is also equal to cash, think of it is as — the faster the depreciation, the more cash there is, and you'll be fine.

And **"Accelerating Depreciation"** is the name of the game when it comes to telephone networks for it generates great amounts of, more or less, free cash. By speeding up the write off of the networks, the company not only gets a large expense that can be used to shelter profits in rate-of-return models, but also it gives the company more cash to purchase items. And, as an expense, it also lowers the amount of taxable income, and therefore, income taxes.

We are talking about a very large sum of money since the major expense of offering telephone services depends entirely on owning and maintaining a network. In 1984, the Bells had $9 billion dollars of depreciation expenses, $1.3 billion per RBOC. And since 1984, the Bells have all sped up their depreciation schedules, In 1996 the expense came to a whopping $17 billion dollars annually, $2.4 billion per RBOC — that $2.4 billion dollars per RBOC to spend above and beyond Net Income. (299)

EXHIBIT 53

RBOC Accelerated Depreciation 1984-1996

(in the millions)

	1984	1996	Change
Ameritech	$1,347	$2,400	78%
Bell Atlantic	$1,194	$2,576	116%
BellSouth	$1,755	$3,719	112%
NYNEX	$1,420	$2,601	83%
Pac Bell	$1,089	$1,870	72%
SBC	$1,141	$1,795	57%
US West	$1,106	$2,122	92%
Total Depreciation	$9,052	$17,083	89%
Per RBOC	$1,293	$2,440	

Sources: RBOC Annual Reports, 1984-1996

The I-Way Plans — Free Money on Fast Forward

While there has been a series of reasons to accelerate depreciation over the last 12 years, the largest changes have occurred with the implementation of the Alternate Regulation plans, because the excess monies were supposed to be used to build the fiber-optic highway. In fact, most states have removed controls on how much the Bells can deduct per year.

What does all this mean?

Well first, the most surprising part of this tale is that: (300)

> **"By 1992 the entire original Bell system network, including the old, copper wiring that still makes up most of the phone network infrastructure and is still the wiring in your house, was totally written off."**

Remember, the Bell system's copper wires and network switches that were already in place in 1984, were paid for during the 1960's and 1970's and 1980's.

This also means that the price of service should have plummeted, since the value of the original network, at least on paper, was literally "$0". (Of course, fully depreciated equipment can still be used and is still in service.)

But more importantly, none of these savings were being given back to the subscriber — the cash was not being used to build new networks. Think of it this way — In the construction section we showed that the construction expenses were about the same over the last 12 years. However, the deductions have gone up 90%!

An Extra $21 Billion Dollars — The "Write-OFF" Scandal

With the removal of state regulations, the Bells decided to go all out and from 1993 through 1995, they all changed their accounting to reflect what they called a "competitive marketplace". This change, known as Statement of Financial Accounting Standards 71 (FAS 71) states that rate-of-return and Utility regulations were now replaced and the company was now a 'free market" company. Ameritech 11/28/94, Investor Alert states: (301)

> "Such accounting is consistent with the regulatory actions that foster marketplace pricing of competitive service and remove regulatory caps in earnings without sharing. "

"Without sharing", means that there is no limit to the profits and Ameritech doesn't have to return anything if they make too much money. Also, there were no longer any restraints on writing off the networks.

And changing their regulations allowed the Bells to collectively write-off, in bulk, additional monies — very large Christmas presents of approximately $21 billion dollars. The exhibit below shows the massive depreciation bonus by the RBOCs as well as the year the money was garnered. Remember, though considered an expense, this is really $21 billion of extra cash the companies could spend. (302)

EXHIBIT 54
RBOC Accelerated Depreciation, FAS Bonus 1993-1995
(In the millions)

	Amount	Year
Ameritech	$3,785	1994
Bell Atlantic	$2,156	1994
BellSouth	$2,718	1995
NYNEX	$2,919	1995
Pac Bell	$3,361	1995
SBC	$2,819	1995
US West	$3,123	1993
TOTAL	$20,881	

Source: RBOC Annual Reports, 1993-1995

All of these changes were made primarily because the states all applied Alternate Regulation to build the Info Bahn. For example, Ameritech Investor Alert stated: (303)

> "Ameritech successfully achieved this form of advanced regulation in all five states in which it operates, with the adoption of the Advantage Ohio stipulation agreement on November 23, 1994. Similar plans were implemented in Michigan in 1992, and Illinois, Indiana and Wisconsin earlier in 1994."

We will return to this free cash in examining overcharging. However, all this leads us into our next question — Where were the regulators in all of this? For example, as we will see there was no competition in the Ameritech region in 1994, nor in any other region of the USA! And all the Bells used the same excuse to make the accounting changes. Our case study of Opportunity New Jersey showed Bell Atlantic had no competition, did not build the highway, and took the FAS 71 accounting change, saving about $1 billion just in that state.

How could the companies make claims that they are competitive? The Alternate Regulation plans have not fostered competition nor built the Info Bahn. So why hasn't there been a major drop in local telephone prices from the excess cash?

Let's start slowly and explore the varied, potholed landscape of regulation, trying to make sense out of words like competition, that are more defined by the eye of the beholder than by any dictionary.

"The Dark Fiber " Scandal— A Real Highway to Nowhere.

Believe it or not, though some fiber-optic wiring has been deployed, there is a very dark secret — the wiring isn't being used. Known as "Dark Fiber" or "Un-Lit Fiber", according to the FCC, of the 15 million kilometers of fiber-optic wiring in America, the majority of wiring, over 70%, is not being used. (304) It's like a highway with no on or off ramps, no traffic, just a big boondoggle.

EXHIBIT 55
FCC RBOC "Lit Fiber" vs "Dark Fiber", 1996
1995-1996 edition, in KM

Fiber Lit	4,287,303	29%
Dark	10,735,184	71%
Total Fiber	15,022,487	

Source: FCC 1995-1996

Are there at least Interactive Services going over the Lit fiber? According to the New Jersey Ratepayer Advocate, (3/21/97) (305) the fiber that was deployed is now just being used for regular voice calls, not interactive services. Also, the fiber that is being deployed has only been appearing in the affluent suburbs.

> "From our review of broadband deployment to date, it appears that broadband has not been equitably deployed to rural and urban areas of the State. The first area of the State to receive widespread deployment of broadband is in the northern New Jersey towns of Clifton and Passaic. Right now 100,000 residential customers in Clifton and Passaic are receiving voice-grade service over broadband. BA-NJ plans to provide voice-grade service over broadband technology to an additional 400,000 households in Northern New Jersey by the year 2000, though there appears

to be no intention to provide any broadband services over the high speed network."