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July 31, 2008

***Via E-mail and USPS***

filed electronically in docket office on 08/05/08

Chairman Tre Hargett
c/o Ms. Sharla Dillon
Tennessee Regulatory Authority
460 James Robertson Parkway
Nashville, Tennessee 37243

**Re: Docket No. 08-00039**
**In Re: Petition of Tennessee American Water Company to Change and Increase Certain Rates**

Dear Chairman Hargett:

Enclosed please find an original and five (5) copies of the following document which has been filed electronically and served today on behalf of the City of Chattanooga:

City of Chattanooga's Responses to Tennessee American Water Company's Second Discovery Requests

I would appreciate you stamping the extra copy of this document as "filed," and returning it to me in the enclosed, self-addressed and stamped envelope.

With best regards, I am

Sincerely yours,

Frederick L. Hitchcock

FLH:kwr
Enclosures
cc: Ryan L. McGehee, Esq. (w/encl)
Timothy C. Phillips, Esq. (w/encl)
David C. Higney, Esq. (w/encl)
R. Dale Grimes, Esq. (w/encl)
Ross Ian Booher, Esq. (w/encl)
J. Davidson French, Esq. (w/encl)
Adam Futrell, Esq. (w/encl)
Erin Everitt, Esq. (w/encl)
Henry M. Walker, Esq. (w/encl)
Michael A. McMahan, Esq. (w/encl)

**IN THE TENNESSEE REGULATORY AUTHORITY**
**AT NASHVILLE, TENNESSEE**

| | | |
|---|---|---|
| **IN RE:** | ) | |
| | ) | **DOCKET NO. 08-00039** |
| **PETITION OF TENNESSEE AMERICAN** | ) | |
| **WATER COMPANY TO CHANGE AND** | ) | |
| **INCREASE CERTAIN RATES AND** | ) | |
| **CHARGES SO AS TO PERMIT IT TO** | ) | |
| **EARN A FAIR AND ADEQUATE RATE** | ) | |
| **OF RETURN ON ITS PROPERTY USED** | ) | |
| **AND USEFUL IN FURNISHING WATER** | ) | |
| **SERVICE TO ITS CUSTOMERS** | ) | |

---

**CITY OF CHATTANOOGA'S RESPONSES**
**TO TENNESSEE AMERICAN WATER COMPANY'S**
**SECOND DISCOVERY REQUESTS**

---

The City of Chattanooga ("City") responds to Tennessee American Water Company's ("TAWC") second discovery requests as follows:

## GENERAL OBJECTIONS

1. City objects to all requests that seek information by the attorney-client privilege, the work product doctrine, and/or any other applicable privilege or restriction on disclosure.

2. City objects to the definitions and instructions accompanying requests to the extent definitions and instructions contradict, are inconsistent with, or impose any obligations beyond those required by the Tennessee Rules of Civil Procedure or the rules, regulations, and orders of the Tennessee Regulatory Authority.

3. City objects to the definitions of the words "document" or "documents" or "documentation" that accompany the requests, because such definitions are overbroad and unduly burdensome.

4. City is providing its objections herein without waiver of, or prejudice to, its right at any later time to raise objections to: (a) the competence, relevance, materiality, privilege, or

admissibility of the response, or the subject matter thereof; and (b) the use of any response or subject matter thereof, in any subsequent proceedings.

5. City objects to each request to the extent that it is unreasonably cumulative or duplicative or seeks information obtainable from some other source that is more convenient, less burdensome, or less expensive.

6. City objects to each request to the extent it is premature such that it seeks information concerning matters about which discovery is ongoing and/or seeks information to be provided by expert witnesses.

7. City's specific objections to each request shall be in addition to the General Objections set forth in this section. These General Objections form a part of each discovery response, and they are set forth here to avoid the duplication and repetition of restating them for each discovery response. The absence of a reference to a General Objection in response to a particular request does not constitute a waiver of any General Objection in response to that discovery request. All responses are made subject to and without waiver of City's general and specific objections.

**DISCOVERY REQUEST NO. 1.:**

For each docket number listed on Appendix B to the testimony of Michael Majoros, please provide a thorough description of each topic addressed by Mr. Majoros in each docket (e.g. cost of service, depreciation rates, management fees, management audit, revenues, O&M expenses, etc.).

**RESPONSE:** Mr. Majoros is preparing and will provide a CD-Rom containing copies of testimony presented by Mr. Majoros during the past four (4) years. The staff person responsible

for this is out of the country and will not return until next week. The CD-Rom should be available on or about August 5, 2008.

**DISCOVERY REQUEST NO. 2.:**

Please provide a detailed listing in the tabular format below for each docket or case in which Mr. Majoros has testified specifically to the prudence or imprudence of management fees charged by the Service Company of an investor-owned, multi-jurisdictional utility.

| State of Jurisdiction | Docket(case)# | Name of Parent Co. | Name of Subsidiary | Summary Of MJM position | Was MJM position upheld by Commission |
|---|---|---|---|---|---|
| | | | | | |
| | | | | | |

**RESPONSE:** The requested information may be found in the material being provided in response to Request No. 1.

**DISCOVERY REQUEST NO. 3.:**

Please provide all information reviewed by Mr. Majoros (or analysis performed by Mr. Majoros) prior to the filing of his pre-filed testimony in this docket supporting or underlying his assertion that TAWC was charged $1.3 million in management fees in 1996, $3.9 million in Docket No. 06-00290, and that the current case reflects a 10% increase in management fees charged to TAWC.

**RESPONSE:** Sources are identified in Mr. Majoros' pre-filed testimony.

**DISCOVERY REQUEST NO. 4.:**

Please provide all information reviewed by Mr. Majoros (or analysis preformed by Mr. Majoros) prior to the filing of his pre-filed testimony in this docket that addresses how organization changes at AWW, AWWSC, or TAWC have impacted or caused the changes in

management fees for 1996 through 2007, including but not limited to: the creation of the national customer service facility, the creation of the centralized shared service transactional accounting facility, the creation of the centralized national procurement group, or any other organization change that has occurred at AWW, AWWSC, or TAWC.

**RESPONSE:** The referenced information was not relevant to the subject of Mr. Majoros' testimony. Accordingly, it was not necessary to review such information.

**DISCOVERY REQUEST NO. 5.:**

Please provide all information reviewed by Mr. Majoros (or analysis performed by Mr. Majoros) prior to the filing of his pre-filed testimony in this docket that addresses the impact that changes in ERISA pension expense and OPEB expenses have had on the change in management fees charged to TAWC from 1996 to 2007.

**RESPONSE**: The referenced information was not relevant to the subject of Mr. Majoros' testimony. Accordingly, it was not necessary to review such information.

**DISCOVERY REQUEST NO. 6.:**

Please provide a comprehensive list of sources and individuals that Mr. Majoros consulted with in developing his testimony in this proceeding.

**RESPONSE:** Sources are identified in Mr. Majoros' testimony. Mr. Majoros consulted with counsel for the City.

**DISCOVERY REQUEST NO. 7.:**

Please provide a list of all formal training Mr. Majoros has received in the interpretation or implementation of Sarbanes-Oxley legislation.

**RESPONSE:** None.

**DISCOVERY REQUEST NO. 8.:**

Please provide a detailed listing in the tabular format below of each docket or case in which Mr. Majoros has testified as an expert on the adoption, implementation, or interpretation of Sarbanes-Oxley legislation or law.

| State of Jurisdiction | Docket(case)# | Name of Parent Co. | Name of Subsidiary | Summary Of MJM position |
|---|---|---|---|---|
| | | | | |
| | | | | |

**RESPONSE:** None.

**DISCOVERY REQUEST NO. 9.:**

Please provide a copy of every management audit conducted or performed by either Mr. Stoffel or Mr. Majoros, and the state, docket number, year, company name and parent company name for every case in which a management audit was conducted or performed by either Mr. Stoffel or Mr. Majoros was filed.

**RESPONSE:** Attached as Exhibit COC-DR2-09 is an audit Mr. Majoros conducted on behalf of the Georgia Public Service Commission.

**DISCOVERY REQUEST NO. 10.:**

On page 2 of his testimony, Mr. Stoffel states "I have researched and developed training that stresses benchmarking as a key component to successful management." Please produce all documents reflecting any such research and development, including any final training product or course materials produced in whole or part by Mr. Stoffel.

**RESPONSE:** The City objects to this request because production of the information sought is unduly burdensome, and the information sought is neither relevant nor calculated to lead to the discovery of relevant information.

**DISCOVERY REQUEST NO. 11.:**

On page 5 of Mr. Stoffel's pre-filed testimony in this docket, he refers to the 2005 AWWA "Benchmarking Performance Indicators for Water and Wastewater Utilities," and states that this report relies on 2003-2004 data. Please identify and produce a copy of the most current available version of the AWWA "Benchmarking Performance Indicators for Water and Wastewater Utilities."

**RESPONSE:** The City objects to the request because it is unduly burdensome. The AWWA document sought is publicly available through AWWA and can be obtained readily from that source at TAWC's expense.

**DISCOVERY REQUEST NO. 12.:**

Please explain how AWWA collected the data on which its "Benchmarking Performance Indicators for Water and Wastewater Utilities" report is based and whether the "Benchmarking Performance Indicators for Water and Wastewater Utilities" report differentiates between investor owned, multi-state utilities with service company structures and publicly owned or municipal utilities.

**RESPONSE:** According to the AWWA report referenced in the Request, the data were generated from survey responses provided by each participating utilities. Information concerning the participating utilities is contained in Chapter 4 of the "Benchmarking Performance Indicators for Water and Wastewater Utilities: Survey Data and Analyses Report" appended to Mr. Stoffel's pre-filed testimony in this Docket.

**DISCOVERY REQUEST NO. 13.:**

Please provide a list of the companies in the 61 company peer group referenced on page 7 of Mr. Stoffel's testimony and indicate whether each company is (i) municipally owned, (ii) a

co-op, (iii) a public service district or public water utility district, (iv) an investor-owned, (v) an investor-owned, multi-state utility that is provided services by a centralized service company organization, or (vi) other (and if other, please describe its ownership type or structure).

**RESPONSE:** The City objects to this Request because it neither seeks relevant information nor is it reasonably calculated to lead to the discovery of relevant information. Without waiving this objection, see response to Request No. 12.

**DISCOVERY REQUEST NO. 14.:**

Please provide all information (other than that provided in appendices to the testimony of Glynn Stoffel) reviewed by Mr. Stoffel or any analysis performed by Mr. Stoffel prior to the filing of Mr. Stoffel's pre-filed testimony in this docket that addresses or compares the type and level of services provided by the 61 utilities referenced on page 7 of his testimony to those services provided by the utilities referenced in the Booz Allen Hamilton peer group contained on Exhibit 9-1, page 8 of the Booz Allen Hamilton report filed in this docket.

**RESPONSE:** As noted in his testimony, in general, Mr. Stoffel compared information contained in Mr. Van den Berg's report and that contained in the AWWA report "Benchmarking Performance Indicators for Water and Wastewater Utilities" appended to Mr. Stoffel's pre-filed testimony in this Docket.

**DISCOVERY REQUEST NO. 15.:**

For each company included in the 61 company peer group referenced on page 7 of Mr. Stoffel's testimony in this docket, please provide a comprehensive list of the costs (by NARUC account number) used to determine the $38.20 benchmark referenced on page 7, line 6 of the testimony.

**RESPONSE:** See "Benchmarking Performance Indicators for Water and Wastewater Utilities: Survey Data and Analyses Report", including pp. 107-109 thereof, appended to Mr. Stoffel's pre-filed testimony in this Docket.

**DISCOVERY REQUEST NO. 16.:**

For the companies that appear in the 61 company peer group referenced on page 7 of Mr. Stoffel's testimony in this docket that have "service companies," describe in detail the type, nature, number and scope of the services provided by the service companies.

**RESPONSE:** The City objects to this Request because it neither seeks relevant information nor is it reasonably calculated to lead to the discovery of relevant information. Without waiving this objection, see response to Request No. 12.

**DISCOVERY REQUEST NO. 17.:**

Please provide all information reviewed by Mr. Stoffel or any analysis performed by Mr. Stoffel prior to the filing of Mr. Stoffel's pre-filed testimony in this docket that attempts to determine the differences among the 61 company peer group referenced on page 7 of his testimony and the utility peer group used in the Booz Allen Hamilton report including, but not limited to: the number of and types of services included in Mr. Stoffel's peer group compared to the Booz Allen Hamilton peer group, taxes for investor-owned versus non-taxable public or municipal systems, the size of the systems, the sophistication of the billing and accounting systems, the differences in regulation (Commission or TRA rules and regulations) between the systems or the absence of regulation in some cases, whether the systems have surface or ground water source water, etc.

**RESPONSE:** See response to Request No. 12.

**DISCOVERY REQUEST NO. 18.:**

Please identify each of the entities among Mr. Stoffel's 61 company peer group that is subject to the Sarbanes-Oxley Act or presently engaged in the process of Sarbanes-Oxley implementation.

**RESPONSE:** See response to Request No. 12.

**DISCOVERY REQUEST NO. 19.:**

Please provide a detailed listing in the tabular format below of each case or docket in which Mr. Stoffel has testified as an expert on the management fees charged by the Service Company of an investor owned, multi-jurisdictional utility.

| State of Jurisdiction | Docket(case)# | Name of Parent Co. | Name of Subsidiary | Summary Of GS position | Was GS position upheld by Commission |
|---|---|---|---|---|---|
| | | | | | |
| | | | | | |

**RESPONSE:** Mr. Stoffel has not previously presented testimony on the subject specified in the Request.

**DISCOVERY REQUEST NO. 20.:**

Please provide a comprehensive list of sources and individuals that Mr. Stoffel consulted with in developing his testimony in this proceeding.

**RESPONSE:** Sources are identified in Mr. Stoffel's testimony. Mr. Stoffel consulted with counsel for the City.

**DISCOVERY REQUEST NO. 21.:**

Has Mr. Majoros ever participated in or reviewed a management audit he considers to be in compliance with Sarbanes Oxley requirements? If so, please produce a copy of any such management audits.

**RESPONSE:** No.

**DISCOVERY REQUEST NO. 22.:**

Please provide any studies, reports, correspondence, City Council minutes, committee minutes, ordinances, resolutions, or other documents of any kind created from January 1, 2006 to the present and reflecting discussions with or requests to TAWC related to planning, proposing, or making capital improvements for reasons including, but not limited to: fire protection, downtown revitalization, service problems, economic development, or transportation improvements.

**RESPONSE:** The City objects to this request because collection and production of the information sought would be unduly burdensome and because the request seeks information that is neither relevant to this proceeding nor calculated to lead to the discovery of relevant information. Without waiving the objection, City agrees to make potentially responsive documents available for inspection and copying at TAWC's expense at a mutually agreeable time. With respect to fire protection, TAWC files will contain all City fire service requests, and such records are already in the possession of TAWC. Adjustments in TAWC facilities involving City projects since January 1, 2006, are summarized in the attached Exhibit COC-DR2-22.

**DISCOVERY REQUEST NO. 23.:**

Produce all documents, studies, proposals, or other communications in which the City or any of its departments, offices, agencies, officials, agents or any other of its representatives of

any kind communicated with any representative of Volkswagen Group of America, Volkswagen AG, or any Volkswagen affiliate concerning water use or wastewater requirements for the planned Volkswagen manufacturing facility in the Chattanooga area.

**RESPONSE:** The planned Volkswagen of America, Inc. manufacturing facility is not located within TAWC's service area. The City objects to this Request because the information sought is irrelevant to this proceeding, the Request is not reasonably calculated to lead to the discovery of relevant information, and the Request is obviously made for improper purposes. Without waiving this or its other objections, the City has attached as collective Exhibit COC-DR2-23 documents concerning wastewater treatment that it understands were provided to representatives of Volkswagen of America, Inc.

**DISCOVERY REQUEST NO. 24.:**

Please produce a copy of the management audit conducted by the Kentucky Public Service Commission, referenced on page 11, lines 15-17 of Mr. Majoros' testimony.

**RESPONSE:** Mr. Majoros does not have a copy of the referenced audit, as he was not the lead. He completed the work under subcontract to another firm.

**DISCOVERY REQUEST NO. 25.:**

On page 2 of Mr. Stoffel's testimony, he states "In my role with Snavely King, one of my duties is to benchmark the data obtained from various utilities to determine what level of best practices and potential efficiency they are attaining both internally and when compared to other utilities." Please produce any document containing any portion of any such benchmarking activities, including the workpapers, underlying data, and results of those benchmarking activities.

**RESPONSE:** The City objects to this request because collection and production of the information sought would be unduly burdensome and because the request seeks information that is neither relevant to this proceeding nor calculated to lead to the discovery of relevant information. Without waiving the objection, Mr. Stoffel has undertaken this work in connection with support provided to Mr. Majoros.

City reserves the right to supplement its responses.

Respectfully submitted,

By: _____

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*Attorneys for the City of Chattanooga*

CITY OF CHATTANOOGA, TENNESSEE
RANDALL L. NELSON, CITY ATTORNEY

By: _____

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Telephone: (423) 757-5338

*Attorneys for the City of Chattanooga*

## CERTIFICATE OF SERVICE

This is to certify that the undersigned has this day served a true and correct copy of the foregoing pleading by electronic mail and by depositing same in the United States mail, postage prepaid, and addressed to the following:

Ryan L. McGehee, Esq.
Office of the Attorney General
Consumer Advocate and Protection Division
P.O. Box 20207
Nashville, TN 37202-0207
ryan.mcgehee@state.tn.us

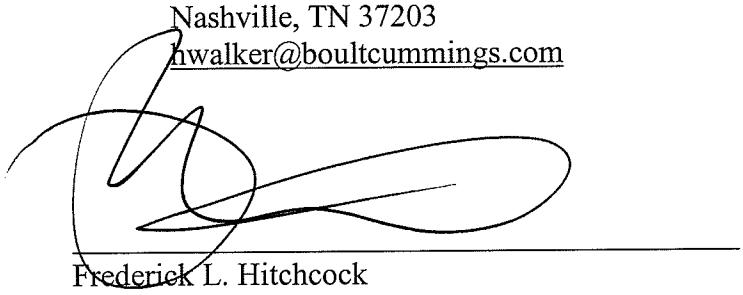
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This the 31st day of July, 2008.



Frederick L. Hitchcock

IN THE TENNESSEE REGULATORY AUTHORITY
AT NASHVILLE, TENNESSEE

| | | |
|---|---|---|
| **IN RE:** | ) | |
| | ) | **DOCKET NO. 08-00039** |
| **PETITION OF TENNESSEE** | ) | |
| **AMERICAN WATER COMPANY TO** | ) | |
| **CHANGE AND INCREASE CERTAIN** | ) | |
| **RATES AND CHARGES SO AS TO** | ) | |
| **PERMIT IT TO EARN A FAIR AND** | ) | |
| **ADEQUATE RATE OF RETURN ON** | ) | |
| **ITS PROPERTY USED AND USEFUL IN** | ) | |
| **FURNISHING WATER SERVICE TO** | ) | |
| **ITS CUSTOMERS** | ) | |

## AFFIDAVIT

Washington, )
District of Columbia )

I, Michael J. Majoros, do hereby certify that the foregoing responses to Petitioner Tennessee American Water Company's Second Discovery Requests Nos. 1-9, 21, and 24 were prepared by me or under my supervision and are true and accurate to the best of my knowledge and information.

Dated this 30th day of July, 2008.

(signature)

Michael J. Majoros, Jr.
(printed name)

Sworn to and subscribed before me this 30th day of July, 2008.

Notary Public

My Commission Expires:
March 14, 2011

IN THE TENNESSEE REGULATORY AUTHORITY
AT NASHVILLE, TENNESSEE

| | | |
|---|---|---|
| **IN RE:** | ) | |
| | ) | **DOCKET NO. 08-00039** |
| **PETITION OF TENNESSEE AMERICAN WATER COMPANY TO CHANGE AND INCREASE CERTAIN RATES AND CHARGES SO AS TO PERMIT IT TO EARN A FAIR AND ADEQUATE RATE OF RETURN ON ITS PROPERTY USED AND USEFUL IN FURNISHING WATER SERVICE TO ITS CUSTOMERS** | ) | |

## AFFIDAVIT

Washington, )
District of Columbia )

I, Glynn L. Stoffel, do hereby certify that the foregoing responses to Petitioner Tennessee American Water Company's Second Discovery Requests Nos. 9-20 and 25 were prepared by me or under my supervision and are true and accurate to the best of my knowledge and information.

Dated this 30th day of July, 2008.

(signature)

Glynn L. Stoffel
(printed name)

Sworn to and subscribed before me
this 30th day of July, 2008.

Notary Public

My Commission Expires:
March 14, 2011

# EXHIBIT COC-DR2-09

COMMISSIONERS:
ROBERT B. (BOBBY) BAKER, CHAIRMAN
MAC BARBER
BOB DURDEN
ROBERT C. (BOBBY) PAFFORD
ROBERT A. (BOBBY) ROWAN

WILLIAM J. DOVER
EXECUTIVE DIRECTOR
TERRI M. LYNDALL
EXECUTIVE SECRETARY

Georgia Public Service Commission
244 WASHINGTON STREET, S.W.
ATLANTA, GEORGIA 30334-5701
(404) 656-4501 OR 1 (800) 282-5813

September 1, 1994

Robert B. Baker, Chairman
Georgia Public Service Commission
244 Washington Street, S.W.
Atlanta, GA 30334-5701

Honorable Chairman and Commissioners:

In July 1992, the Commission directed the Staff to conduct an audit of Southern Bell Telephone and Telegraph Company's cost allocations and affiliated transactions. The Commission wanted a review of the relationship between the Company's regulated telephone operations and both its nonregulated activities and the nonregulated operations of its affiliates in order to learn whether Southern Bell's regulated customers are protected from cross-subsidy.

The audit identified a number of specific cross-subsidies and cost shifts and makes recommendations relating thereto. In general the auditors conclude that the best protection for regulated customers and the Company's competitors is continued audits as long as the Commission has regulatory oversight of the Company's costs. This leads to a second general finding. The elimination of the cross-subsidies and cost shifts identified in this report appear to have taken on considerable urgency in light of Southern Bell's

efforts to advance legislative and regulatory plans that would declare all existing rates just and reasonable and apparently eliminate regulatory oversight of costs.

The draft findings were sent to the Company for its review and comment. The written responses are attached. Southern Bell is disappointed with the individual audit findings for several reasons and apparently disagrees with every finding and recommendation. Southern Bell's disappointment also stems in part from its opinion that the outside consultants were not objective. The Company ultimately concludes that "no further action is required by the Commission."

We appreciate the courtesy and cooperation of Southern Bell's staff. The auditors in charge of this project were Don Craig of the Commission Staff and Michael J. Majoros, Jr. of the economic consulting firm of Snavely, King & Associates, Inc. who were assisted by Mr. James W. Currin and Mr. Richard B. Lee also of Snavely, King & Associates, Inc.

B.B. Knowles
Director of Utilities

Audit Report on
Southern Bell Telephone and Telegraph Company
Cost Allocations and Affiliate Transactions

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III. FINDINGS AND RECOMMENDATIONS . . . . . III - 1

Tax Allocation

1. The special tax benefits of the Company's Leveraged Employee Stock Ownership Plan should flow to regulated operations. . . . . III - 1

2. The Company has achieved a significant cross-subsidy from its regulated operations and BAPCO to its nonregulated operations as a result of its filing of consolidated tax returns. The cumulative tax savings should be deducted from the Company's rate base. . . III - 6

3. Income tax expense charged to regulated operations should not be used to subsidize the losses of nonregulated products and services offered by Southern Bell Georgia. III - 18

4. The Commission should instruct the Company to match benefits to related costs. . . . . III - 24

5. Accumulated deferred taxes and unamortized investment tax credits which represent taxes charged to regulated operations should not be transferred to nonregulated operations. Case-by-case burden of proof concerning any IRC violation belongs with the Company. . . III - 26

6. The Commission should be cognizant that the Company derives benefits through deferred tax activity in rate case years and non-rate case years. . . . . III - 31

7. Georgia PSC auditors should be provided access to all income tax returns and related workpapers. . . . . III - 34

MemoryCall®

8. The Company should be reprimanded for adding MemoryCall® losses to the Surveillance Report without notifying the Commission and the Company's failure to file tariffs and supporting cost of service studies. . . . . III - 39

9. Southern Bell's construction program should be regularly audited. . . . . III - 44

10. Right-To-Use fees should be directly assigned whenever possible. . . . . III - 48

Purchasing, Warehousing and Transfers

11. The Commission should investigate the implications of a 1990 switch price restructure and increase its audit scrutiny of BellSouth to ensure that basic business and residential ratepayers are protected against cross-subsidies. . . . . III - 52

12. The inclusion of BellSouth Services' net income and equity in the Surveillance Report provided a subsidy for it's nonregulated CPE products and masked the over-earnings on sales to the regulated operations. . . . III - 61

13. The calculation and booking process used to record transfers of equipment between regulated companies should be mechanized to prevent errors. . . . . III - 69

Cost Allocation

14. Recent legislative and regulatory initiatives increase the urgency of eliminating subsidies found in this audit. . . . . III - 72

15. The Company's regulated vs. nonregulated cost allocation process should be subjected to continued and increased audit scrutiny. III - 79

16. The auditors recommend the use of positive time reporting for BellSouth's and Southern Bell's legal departments. . . . . III - 82

Affiliate Transactions

17. Chaining calculations relating to affiliated transactions should recognize operations, such as BAPCO, which are treated as regulated at the intrastate level. . . . . III - 92

18. Sunlink's Corporate cost allocation process provides an opportunity for the regulated telephone operations to subsidize BellSouth's nonregulated commercial ventures. If Southern Bell is unwilling to calculate the portion of Sunlink's lease price increases which flow into regulation, the total amount of the leases should be disallowed. . . . . III - 96

19. Commercial space which is leased from a nonregulated affiliate for regulated operations should be evaluated to determine if the lease space is actually being utilized. . . . . III - 101

20. Commission should perform regular future audits focussed on real estate and lease transactions which involve affiliates in any way. An intrastate adjustment of $321,609 should be made to the Surveillance Report to compensate regulated customers for excessive Chastain Center lease expenses. . III - 104

21. The interest received by Southern Bell from advances to affiliates should be offset against book interest in the interest synchronization adjustment. . . . . III - 112

22. The Company achieved a cross-subsidy relating to the Rose CXC PBX. The Commission should increase its audit scrutiny of the Company's CPE-related transactions. . . . . III - 116

23. Accounting and information management costs should be directly assigned whenever possible. . . . . III - 119

24. BSC international calls should be directly assigned to nonregulated in most cases. . . III - 123

25. A portion of BSC unattributable costs should be retained by BSC. . . . . III - 126

26. The transactions between BAPCO and SGI should be specifically covered by Rule 32.27(d) for the purposes of the Georgia Surveillance Report. Substantial third party sales should be interpreted to mean that 75 percent or more of the sales are to non-affiliated companies. . . . . III - 129

27. BellSouth Enterprise's retention of expenses associated with its foreign subsidiaries should be referred to the Internal Revenue Service International Examination Branch and the Georgia Department of Revenue Income Tax Division for further investigation with regard to its tax deductions. . . . . III - 133

IV. APPENDICES

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BSS CPE Analysis. . . . . Appendix G - 1

Affiliate Transaction - BSC Allocator. . Appendix H - 1

V. COMPANY RESPONSE

# I. SUMMARY

The primary objective of this audit was to review the relationship between the Company's regulated telephone operations and both its nonregulated activities and the nonregulated operations of its affiliates in order to learn whether Southern Bell's regulated customers are protected from cross-subsidy. Regardless of whether a practice was sanctioned by any particular rule, standard, or procedure, if the practice resulted in a cross-subsidy the auditors were obligated to identify it as such. For example, the Company achieves a significant cross-subsidy in the income tax area which is not precluded by any particular rule.

This audit required the recognition of numerous regulatory and policy issues in addition to accounting matters. It required analyses of the applicable regulatory policies developed in Commission Dockets 3905-U, 3987-U and 4000-U and FCC Docket 86-111 that deal with cost allocation standards, affiliate transactions and related accounting. The audit also required analyses of the purposes and effects of Southern Bell's actions, plus the reasoning that was used to apply the underlying policies in light of those purposes and effects. From the auditors' perspective, these requirements and reasoning were applied within constraints imposed by proprietary agreements and the inability to examine certain material.

As summarized below the auditors identified a number of specific cross-subsidies and cost shifts. The elimination of these

cross-subsidies and cost shifts appears to have taken on considerable urgency in light of Southern Bell's efforts to advance legislative and regulatory plans that would declare all existing rates just and reasonable and apparently eliminate any regulatory oversight of costs.

This report is divided into five parts. This Summary is Part I; Part II relates to the history of Commission activity in the area of cost allocations and affiliate transactions. Part III contains detailed discussion of the auditors' twenty-seven findings categorized into five issue areas -- tax allocation, MemoryCall[R], purchasing, cost allocations and affiliate transactions.

Tax Allocation

Finding Nos. 1 through 7 and 27 deal with the Company's allocation of tax benefits. The auditors found that many of these benefits result in cross-subsidies from regulated operations to nonregulated services and from Southern Bell to BellSouth affiliates. The auditors offer recommendations that will provide a fair and equitable sharing of these tax benefits.

MemoryCall[R]

Finding Nos. 8 through 10 deal with the Company's provision of MemoryCall[R] service. During the course of the audit it became clear that the Company's construction program should be regularly audited for proper assignment between regulated and nonregulated

activities and that Right-to-Use fees should be directly assigned whenever possible.

In June, 1991 the Company began to add MemoryCall[R] costs to regulated operations in the Georgia Surveillance Report. It did not identify these costs in the Surveillance Report and it provided no official notification, tariffs or cost support. The auditors recommend the Company be reprimanded for these failures.

Purchasing, Warehousing and Transfers

Finding Nos. 11 through 13 address purchasing, warehousing and transfers. Two primary issues emerged: (1) cost shifts from competitive to noncompetitive services and (2) a cross-subsidy of nonregulated customer premises equipment ("CPE") by regulated operations. The cost shifts from competitive to noncompetitive services are related to a 1990 switch price restructure negotiated between Southern Bell and AT&T which appears to have inflated noncompetitive service costs and reduced competitive service costs. The auditors recommend that the Commission investigate the implications and effects of this price restructure.

The cross-subsidy of nonregulated CPE by regulated operations resulted from the inclusion of unprofitable CPE in BellSouth Services's ("BSS") operations and the consequent inclusion of those results in regulated operations in the Company's Surveillance Report. The auditors recommend a rate base deduction. The Company should also be reprimanded for its failure to inform the Commission

that the BSS add-back included unprofitable, obsolete, nonregulated business CPE.

Cost Allocation

Finding Nos. 15 and 16 deal with cost allocations between regulated and nonregulated services. The auditors found the Company generally to be in compliance with Part 64 of the FCC rules. However, assuming continued regulatory oversight of the Company's costs, audit scrutiny of these cost allocations will become more critical as the Company's nonregulated operations increase. The auditors recommend the use of positive time reporting for BellSouth's and Southern Bell's Legal Departments to ensure that each individual is held more directly accountable for how his or her time is charged.

Affiliate Transactions

Finding Nos. 17 to 27 identify several issues and cross-subsidies in connection with affiliate transaction rules and cost allocation standards. The auditors recommend increased scrutiny of affiliated lease transactions (Finding Nos. 17 to 20). The auditors also recommend an adjustment to the Surveillance Report interest synchronization adjustment to reflect interest received from advances to affiliates (Finding No. 21). Finding No. 22 recommends that the Commission increase its audit scrutiny of the Company's CPE-related transactions, and is particularly relevant in light of Finding Nos. 3 and 12. Finding Nos. 23 to 26 recommend

specific cost allocation procedures. Of particular significance is the recommendation to define "substantial third party sales" as meaning that 75 percent or more of the sales are to non-affiliated companies.

Finding No. 27 deals with affiliated transactions between nonregulated domestic and foreign affiliates. It recommends referral of this finding to the IRS International Examination Branch and the Georgia Department of Revenue Income Tax Division for further investigation.

Finally, Finding No. 14 explains why Southern Bell's recent legislative and regulatory initiatives increase the urgency of eliminating subsidies found in this audit.

## II. INTRODUCTION

### BACKGROUND

Snavely, King & Associates,Inc. ("SKA") was retained by the Georgia Public Service Commission ("GPSC"), to perform an audit of the cost allocations and affiliate transactions of the Southern Bell Telephone and Telegraph Company ("Southern Bell", "SB" or "the Company") from 1988 to 1991. The SK&A auditors worked under the direction of Don Craig, Audit Manager of the GPSC.

This audit represents one element in a series of initiatives taken by the Commission to ensure the appropriateness of intrastate revenue requirements as they could be affected by regulated versus non-regulated cost allocations and affiliate transactions. Concurrent with the Commission's December, 1990 adoption of an experimental incentive regulation plan ("IRP") for the Company, the Commission initiated an effort to design a mechanism that will safeguard ratepayers against problems of improper charging of expenses and cross-subsidization. This effort resulted in the development of an extensive record in Docket 3897-U on the subject of cross-subsidy and cost allocations. The Commission has specifically addressed one of the Company's enhanced services, MemoryCall$^{R}$, in Docket 4000-U, and it has addressed Open Network Architecture in Docket 4018-U.

On premise review of Company records and operations was conducted by the auditors between July 1992 and April 1994. Field review was supplemented by nearly 300 formal audit requests and numerous informal telephone discussions. Audit results were

discussed with Company representatives throughout the audit, and written preliminary audit findings were provided to the Company between February and May 1994. The Company provided the auditors with written responses, and clarifying discussions were held prior to the finalization of all findings. Draft copies of the findings in this report were provided to the Company in August 1994. The Company's written Responses on these drafts comprise Part V of this report.

## SCOPE AND OBJECTIVES OF AUDIT

The GPSC defined the scope and objectives of this audit in its Request for Proposals ("RFP") dated May 19, 1992, as follows:

> The scope of this audit will be limited to a review and evaluation of Southern Bell's compliance with this COMMISSION's rule 515-3-1-.10[1] as it pertains to the allocation of costs between its regulated services and non-regulated activities and to recording transactions with its non-regulated affiliates on the Company's regulated books of account for the years 1988, 1989, 1990, and 1991. Specifically, Sections 32.27[2] and 64.901[3] of the Federal Communications COMMISSION's rules.
>
> Objectives
>
> (1) to have a review of the relationship between the Company's regulated telephone operations and its non-regulated activities and the non-regulated operations of its affiliates;

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[1]This rule requires telephone companies to follow FCC rules governing cost allocations and affiliate transactions.

[2]FCC affiliate transaction rules.

[3]FCC cost allocation rules.

(2) to learn whether as a result of these relationships Southern Bell's regulated customers are protected from cross-subsidy, the regulated operations are receiving adequate support and the level of charges from the affiliates are reasonable taking into account the appropriateness of the methods of allocation;

(3) to learn whether or not opportunities exist in these organizational and operating relationships for realizing reductions in operating expense or for increasing operating revenue;

(4) to get quantification of the achievable savings associated with reduced operating expenses or increased revenues and any possible adverse effects associated with these savings;

(5) to receive recommendations for instituting the changes necessary to achieve those savings or improvement;

(6) to have a special review within the scope of the affiliate transaction rules of the purchasing, supply and warehousing function provided by non-regulated affiliates to the regulated operations in Georgia, including a review of the independent auditor's workpapers in regard to the attest audit of the BellSouth cost allocation manual for the years 1988, 1989, 1990 and 1991;

(7) to learn whether or not inflated costs were recorded in Georgia's regulated books for the purchasing, supply and warehousing functions provided by non-regulated affiliates;

(8) to receive a report of all instances of non-compliance with this COMMISSION's rules concerning transactions with affiliates (FCC-Section 32.27), allocation of costs between regulated services and non-regulated activities (FCC - Section 64.901) and all indications or instances of illegal acts that could result in criminal prosecutions (these may be reported separately).

The Federal Communications Commission ("FCC") requires major local exchange carriers to file and maintain a Cost Allocation Manual ("CAM") providing descriptive information regarding their allocation of costs between regulated and nonregulated activities.[4] The FCC also requires each carrier filing a CAM to have an independent auditor verify each year that its regulated reports are fairly presented in accordance with the CAM and other FCC regulations.[5]

During the period of the audit, Southern Bell was subject to the CAM filed by its parent, the BellSouth Corporation ("BSC"). The auditors were given access to the CAM workpapers and reports of BSC's independent auditor, Coopers & Lybrand ("C&L"), at the outset of their work. The auditors also reviewed related internal audits performed by Company personnel.

The auditors review of C&L's workpapers and internal audits provided them with a basis for focusing their efforts in an efficient manner. The auditors were thus able to avoid redundant review of areas routinely audited, and concentrate on aspects of the Company's operations which receive less critical attention.

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[4]Code of Federal Regulations, Title 47, §64.903.

[5]Id., §64.904.

SOUTHERN BELL BACKGROUND

During the audit period, Southern Bell was a regulated carrier providing a variety of local exchange and interexchange services to more than 8.5 million customers in areas of Florida, Georgia, North Carolina and South Carolina. Southern Bell's parent, BSC, was also the parent corporation of the South Central Bell Telephone Company ("SCB"), another regulated carrier, and various nonregulated subsidiaries engaged in business other than the provision of regulated local exchange service.

During the audit period, SB and SCB jointly owned BellSouth Services ("BSS"), which provided services on a centralized basis. Effective January 1, 1992, SB, SCB and BSS were merged into a new regulated carrier, BellSouth Telecommunications ("BST"). Detailed organization charts covering the audit period from the BSC Cost Allocation Manual ("CAM") appear in Appendix B.

1. The special tax benefits of the Company's Leveraged Employee Stock Ownership Plan should flow to regulated operations.

Summary

BellSouth Corporation is obtaining a subsidy by allocating leveraged employee stock ownership plan ("LESOP") costs to regulated operations while retaining the related tax advantages at the Corporate level. Although BellSouth Corporation allocates a majority of LESOP costs to its regulated subsidiaries, it retains all of the special tax advantages associated with LESOP Trust stock dividends at the nonregulated corporate level. This is a mismatch of costs and benefits. The Georgia intrastate portion of these tax benefits for the 1990 - 1994 period is estimated to be $6.1 million. The Georgia Surveillance report should be adjusted to flow LESOP tax benefits to regulated operations.

Criteria

The audit objective in this area was to determine if the nonregulated corporate parent, BSC, is obtaining a subsidy by allocating LESOP costs to regulated operations while retaining associated tax advantages at the corporate level. This evaluation included an analysis of the basic LESOP Trust's stock purchases, the economic assumptions used by the Company to evaluate the initial LESOP plan, subsequent stock performance, interest on LESOP notes, tax savings associated with LESOP stock dividends and the additional allocation of cost associated with the plan to Georgia.

Condition

In 1990 the Company implemented a leveraged employee stock ownership plan (LESOP). The plan revolves around a trust. The trust borrowed $850 million and purchased an equivalent amount of BSC common stock to be used in the future as an employee savings plan benefit. As employees place money into a savings plan, the trust provides matching contributions at specified percentages in the form of BSC stock. The LESOP plan was approved and implemented under the assumption that the growth in stock price and dividends associated with the purchased shares would reduce BellSouth's overall cost of providing benefits to its employees.[6]

The interest and principal on the loan taken to purchase BSC stock is charged to the operating companies as a "Benefit expense" and recorded above-the-line as operating expense. Any market loss on the value of the original stock purchases is also charged to the operating companies and their regulated customers as an operating

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[6]Thus far this has not been the case. The plan will cost Georgia's regulated customers about $24.4 million ($18.3 million intrastate) in increased benefit expense above what would have been charged had the plan not been implemented for the 1990-1994 period. The plan's economic evaluation anticipated that BellSouth's stock prices would increase at a rate of 6.5 percent per year. One of the Company's LESOP Plan assumptions was that the 1991 stock price would be $59.50. This assumption leads to a forecasted stock price of $63.37 and $67.52 for 1992 and 1993 respectively at the 6.5 percent assumed growth rate. The actual 1991 average stock price was only $49.80, while the 1992 average stock price was $53.70. BellSouth's 1993 end-of-year stock price was approximately $58.00 per share, which is about 20 percent less than what was anticipated in the plan's economic evaluation.

The anticipated increase in BellSouth's stock price was intended to off-set the interest expense resulting from the $850 million loan. In reality, stock prices fell rather than increased. Consequently, the LESOP increased employee benefit expenses rather than reducing them.

expense. Finally, any other increased costs are charged to the regulated operating companies as benefit expenses. Dividends received by the trust on the BSC common stock are netted against the benefit expenses charged to the operating companies.[7] BSC receives a special tax deduction for the dividends it pays to the trust.

The audit determined that BSC is retaining, at the corporate level, the special tax deductions associated with dividends on the stock purchased by the LESOP trust, while allocating trust expenses to Georgia's customers as part of BSC's allocation of employee benefit expense.

Although the LESOP was designed to provide benefits for 13 years, the Company only provided LESOP estimates of cost, dividends and tax information through 1994. This became the basis for a five year audit evaluation. (See Appendix C).

Effect

The tax savings associated with Georgia's portion of the dividend deduction being retained at BellSouth for the 1990-1994 period is $8.1 million dollars ($6.1 million intrastate).

Cause

Retaining LESOP dividend tax savings at BSC, while allocating LESOP expenses to the individual companies, was a corporate

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[7]The annual interest alone is approximately $30 million more than the dividends received by the trust.

decision.

Recommendation

The auditors recommend that the tax savings associated with LESOP stock dividends be included as an adjustment to Georgia's Net Operating Income ("NOI") as reported on the Georgia Surveillance Report. A one time NOI adjustment of $6.1 million should be included in Georgia's Surveillance Report to reflect Georgia's intrastate portion of the 1990-1994 tax savings. Also, an ongoing NOI adjustment of at least $1.2 million should be made each year. An alternative to an annual $1.2 million adjustment would be to require the Company to incorporate an adjustment comparable to the appropriate LESOP dividend tax deduction in future Georgia regulated tax calculations.

This audit recommendation is based on the premise that if regulated customers are required to provide revenue to cover all of the cost for their portion of the LESOP Plan, then those same customers should share in any off-setting tax benefits available because of the plan. It is important to note that the auditors are not proposing to exclude any LESOP expenses from the ratemaking process, but that we strongly recommend that all tax savings associated with the plan be used to reduce the expense of the plan whenever possible. The Company's position is that it should retain the tax advantage of the plan because BSC "signed" for the LESOP Loan from Morgan Stanley, although the local Operating Telephone Company ("OTC") must assume the risks and costs associated with the

loan and value of the stock purchased. The OTC is obligated to compensate BellSouth for all employee benefit expense assigned (including interest on the loan and loss in stock value). Southern Bell's management does not have the option of not paying BSC for any expense assigned, as BSC is the "owner" of Southern Bell and South Central Bell, and dictates policy. The Company's position relating to the loan liability and retention of the tax savings has no merit.

Finally, the Company claims that GAAP requires that the nonregulated parent retain the tax benefit. GAAP does not control ratemaking and should not be used as a justification for mismatching costs and benefits between nonregulated and regulated operations.

2. The Company has achieved a significant cross-subsidy from its regulated operations and BAPCO to its nonregulated operations as a result of its filing of consolidated tax returns. The cumulative tax savings should be deducted from the Company's rate base.

Summary

Southern Bell is a signatory to an agreement under which it charges income taxes to its regulated operations at a rate that exceeds the actual tax rate of the consolidated group of which it is a member. Resulting excess taxes are transferred through the corporate parent to unprofitable affiliates which are also members of the consolidated group. These transfers, which are actual cash payments from the regulated operations to the nonregulated operations, help finance the losses of BSC's nonregulated operations. If nonregulated operations eventually become profitable, future taxes will be paid out of future revenues without any recognition of the fact that regulated operations helped finance early losses. If nonregulated operations remain unprofitable, regulated operations will continue to finance their losses until the unprofitable operations are discontinued. In either case, there is a significant cross-subsidy from regulated operations to nonregulated operations. The auditors recommend that Georgia's share of the cumulative tax savings resulting from the filing of consolidated tax returns back through 1984 be deducted from Southern Bell - Georgia's rate base.

Criteria

One of the objectives of this audit was to learn whether, as a result of the relationship between the Company's regulated telephone operations and the nonregulated operations of its affiliates, Southern Bell's regulated customers are protected from cross-subsidy. The Commission has defined cross-subsidy as any action undertaken by SBT which results in an understatement of intrastate regulated revenues or an overstatement of intrastate regulated expenses or investment for SBT.[8]

Condition

The auditors identified a tax deduction associated with the Company's leveraged employee stock ownership plan ("LESOP") being taken by BSC which was not being shared with regulated subsidiaries such as Southern Bell. The regulated operations in Georgia received no benefit from this tax deduction even though they absorbed the cost of the LESOP.[9] The auditors also identified a situation in which the company obtained an interest income benefit which was taken below-the-line even though a portion of the related cost was recorded above-the-line as an accumulated deferred tax debit. Consequently, the auditors determined that it would be appropriate to compare and attempt to reconcile the parent company's Federal income tax return to the Georgia Federal income

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[8]Docket No. 3987-U.

[9]The LESOP is the subject of Finding No. 1.

tax return.[10]

During the course of the attempted reconciliation the auditors were informed that profitable subsidiaries such as Southern Bell pay their tax liabilities to BSC, but BSC does not pay all of these funds to the Federal government. A portion of the funds collected from the profitable subsidiaries is distributed to unprofitable subsidiaries.

BSC files a consolidated Federal tax return. Its eligible subsidiaries include Southern Bell, South Central Bell, BSS, BAPCO and other nonregulated and international subsidiaries. These companies signed an agreement titled "Consolidated Federal Income Tax Allocation Policy ("CFITAP") under which each company computes its annual Federal income tax expense on a "stand-alone" basis as if it were not a member of an affiliated group filing a consolidated tax return. BSC collects the stand-alone taxes from its profitable subsidiaries and transfers a portion of the funds to its unprofitable subsidiaries as described above. The taxes distributed to the unprofitable subsidiaries are not, and never will be, payable to the government. BSC's first consolidated Federal tax return was its 1984 return.

In the context of this finding, it is important to understand the relationship of Southern Bell to BAPCO since BAPCOs tax expense has an impact on Southern Bell of Georgia's intrastate regulated net income.

BAPCO is a nonregulated affiliate treated as regulated in

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[10]This reconciliation is the subject of Finding No. 3.

Georgia. Under the terms of an agreement between Southern Bell and BAPCO, Southern Bell receives a significant portion of BAPCO's revenues. The agreement provides for a 45.26 percent revenue sharing factor (publishing fee) from BAPCO to Southern Bell. These revenues are included in Southern Bell - Georgia's regulated earnings. The Georgia PSC requires additional imputations that result in a BAPCO publishing fee of 50 percent (instead of 45.26 percent) and an imputation of 50 percent of BAPCO's income over a 10.15 percent Return on Investment.

These additional imputations are done monthly and adjustments are made to the Georgia Surveillance Report. The imputation of 50 percent of BAPCO income over 10.15 percent is measured after taxes. Consequently, BAPCO's income tax expense is treated as regulated cost and has an impact on Georgia's regulated net income. The higher BAPCOs income tax expense, the lower Southern Bell - Georgia's regulated net income. Since BAPCO is a signatory to the CFITAP, it's income taxes are also computed on a stand-alone basis and therefore subject to transfer to unprofitable operations.

The audit period tax liability summary below is based on individual annual summaries provided by the Company.

BellSouth Corporation and Subsidiaries
Tax Liability Summary
1988 to 1991[11]
($000,000)

| | Description | Amount |
|---|---|---|
| 1. | Tax Liability of Bell South Services | $ 48[12] |
| 2. | Tax Liability of South Central Bell | 1,315 |
| 3. | Tax Liability of Southern Bell | 1,650 |
| 4. | Tax Liability of Other Profitable Operations[13] | 350[14] |
| 5. | Tax Liability of Nonregulated Loss Operations | (280)[15] |
| 6. | Total | $3,083 |
| 7. | Taxes Collected by BSC (L1 to L4) | 3,363 |
| 8. | Tax Distributions to Loss Operations | (280)[16] |
| 9. | Tax Liability to Government | $3,083 |

This tax liability summary demonstrates that $280 million of taxes were collected from profitable operations and distributed to unprofitable affiliates during the 1988 to 1991 audit period. The revenue requirement effect of the $280 million tax distribution is $424 million at a 34 percent tax rate ($280/.66 = $424). The auditors estimate that $44.7 million of the $280 million distribution is attributable to Southern Bell - Georgia. This would equate to a $67.7 million revenue requirement at a 34 percent

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[11]Item No. MJM-29, Supplement.

[12]Company treats BellSouth Services as regulated, for the purpose of this summary.

[13]Includes BAPCO and other nonregulated operations.

[14]By subtraction based on the $280 on line 5.

[15]Summary level number based on February 10, 1994 interview with Company personnel. Proprietary figures were shown to auditors and then withdrawn.

[16]Summary level number based on February 10, 1994 interview with Company personnel. Proprietary figures were shown to auditors and then withdrawn.

tax rate.

The Company asserts that the $44.7 million amount attributed to Georgia is "grossly overestimated since it was based on total nonregulated losses for the entire period 1988 to 1991". The tax liability summary above indicates that the positive tax liabilities of the Other Profitable Operations (line 4) exceed the negative tax liabilities of the Nonregulated Loss Operations (line 5). However, the Other Profitable Operations figure includes BAPCO, whose earnings are treated as regulated in Georgia. The auditors requested, but were denied, access to the BAPCO tax liability numbers and thus are unable to determine the portion of the $350 million tax liability of Other Income Operations which is attributable to BAPCO.

The table below shows the annual net tax liabilities of BSC's nonregulated operations for the 1988 to 1991 audit period. As explained above these amounts include BAPCO results even though BAPCO is treated as regulated in Georgia.

Annual Net Tax Liability
of Other Profitable Operations
and Nonregulated Loss Operations
1988 - 1991
($000,000)

| Year | Amount |
|---|---|
| 1988 | ($17.6) |
| 1989 | 35.3 |
| 1990 | 12.7 |
| 1991 | 40.2 |

The first year (1988), shows a negative amount, which means that, even with the inclusion of BAPCO in nonregulated operations, losses exceeded profits. The auditors were informed that in 1991

the Cellular operation became profitable, but that does not account for the significant turnaround in 1989. Since the auditors were denied access to financial information concerning any nonregulated affiliate, they can only speculate as to the cause of the 1989 turnaround.

The 1989 turnaround appears to have resulted from the Company's reintegration of Advanced Systems Inc.'s CPE line of business back into Southern Bell as a nonregulated line of business. CPE, as explained in Finding Nos. 3 and 12, was an unprofitable operation. Hence, the reintegration of the CPE business into the regulated companies would have increased the collective net profit of the nonregulated affiliates. It also appears that a majority, if not all, of the nonregulated profits in the years 1990 and before (i.e. back to 1984) were provided by BAPCO. Thus, for the period 1984 to 1990 BSC's regulated operations and BAPCO financed the losses of all of BSC's nonregulated affiliates (including the Cellular operation) through the transfer of tax funds collected under the terms of the CFITAP.

The estimates discussed in the finding have been made at a summary level because the information provided by the Company was at a summary level. No specific tax information relating to any of BSC's nonregulated subsidiaries, including BAPCO, was provided. The summary information upon which these estimates were based was only shown to the auditors one time. It was not, like certain other proprietary information, retained in a room available for additional review, although the Company has offered to make it

available for further review upon request. BSC would not release proprietary information to the possession of BellSouth Telecommunications even under the terms of a proprietary agreement.

Effect

The stand-alone tax calculations and the Company's CFITAP resulted in a significant cross-subsidy from profitable regulated operations and BAPCO to unprofitable nonregulated operations. Beginning in 1984, funds provided by regulated operations were transferred to nonregulated operations. Consequently, the initial losses of all nonregulated subsidiaries, whether they subsequently became profitable or not, were subsidized by regulated operations.

The amount of the subsidy prior to the audit period was not available to the auditors. During the 1988 to 1991 audit period the subsidy was $280 million at the BSC level and $44.7 at the SB-Ga. level.[17] The equivalent revenue requirement effects at a 34 percent tax rate are $424 million and $67.7 million respectively. The subsidy extending back to 1984 is undoubtedly much larger.

Although the Company does not dispute the fact that tax funds were and continue to be transferred from profitable to unprofitable subsidiaries, it disagrees conceptually that the stand-alone tax calculations and CFITAP resulted in a subsidy from regulated to nonregulated operations.

The Company believes that if any recognition is given by the

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[17]

| | |
|---|---|
| $280.0 | 100% BSC |
| 154.0 | 55% SBT |
| 44.7 | 29% SBT - Ga. |

regulated operations to the transfer of tax funds to nonregulated operations this would produce a subsidy to the regulated operations from the nonregulated operations. The auditors disagree. This is a matter of substance over form. The substance of the transaction is that the cash flows from regulated operations to nonregulated operations.

The table below provides an example of the cross-subsidy from regulated to nonregulated resulting from the use of the stand-alone tax calculation combined with consolidated tax returns under the terms of BSC's CFITAP. It is based on an example provided by the Company and utilizes a 35 percent tax rate.

Example of Subsidy
Resulting From Stand-Alone Tax Calculations
and Consolidated Tax Returns

| | Year 1 Stand-Alone | | |
|---|---|---|---|
| | Regulated | Nonregulated | Consolidated |
| Taxable Income | $ 35,000 | $(10,000) | $ 25,000 |
| Tax Liability at 35% | 12,250 | 0 | 8,750 |
| Cash Transferred to Nonregulated[18] | ( 3,500) | 3,500 | - |
| Tax Paid to Government | $( 8,750) | 0 | $( 8,750) |

| | Year 2 Stand-Alone | | |
|---|---|---|---|
| | Regulated | Nonregulated | Consolidated |
| Taxable Income | $ 35,000 | $ 10,000 | $ 45,000 |
| Tax Liability at 35% | 12,250 | 3,500 | 15,750 |
| Cash Transferred to Nonregulated | 0 | 0 | 0 |
| Tax Paid to Government | $(12,250) | $( 3,500) | $(15,750) |

[18]Subsidy

The cross-subsidy occurs in the first year when the nonregulated subsidiary loses $10,000. Cash of $3,500 is transferred from the regulated operations to the nonregulated operations thus subsidizing the loss. In the second year, when the nonregulated operation becomes profitable, it pays taxes out of its own income to the government.

Under the terms of the CFITAP combined with stand-alone tax calculations, the regulated operations subsidize a portion of the initial losses by being charged with overstated taxes and then distributing the excess amount to the unprofitable affiliates. The subsidy is permanent since any future tax expenses will be paid out of the affiliate's future earnings if it becomes profitable. However, if the nonregulated affiliate becomes profitable, none of the nonregulated profits are assigned to the regulated operations. Regulated operations will have financed early losses and born a portion of the risk associated with the success of the operation without any share of the profitable outcome. If, on the other hand, the unprofitable subsidiary never becomes profitable, the regulated operations merely continue to finance losses until the unprofitable subsidiary is discontinued. In either case there is a cross-subsidy.

Cause

This cross-subsidy resulted from the Company's decision to adopt a CFITAP requiring stand-alone tax calculations and the distribution of the excess taxes from profitable subsidiaries to

unprofitable subsidiaries. As indicated above, this began in 1984. The FCC's Part 32 was initially implemented in 1988. Rule 32.27(e) requires the use of stand-alone tax calculations for carriers who are parties to consolidated tax returns. Therefore, the Company's decision and subsequent strict adherence to FCC Rule 32.27(e) cause the cross-subsidy described in this finding.

Recommendation

The auditors recommend that Southern Bell - Georgia's share of the cumulative net tax savings resulting from BSCs filing of a consolidated tax return be used as a rate base reduction in the Surveillance Report. This calculation should be based on all years from 1984 to date. This will recognize the nonregulated losses which have been subsidized by regulated operations.

As indicated in the finding, amounts prior to the audit period were not made available to the auditors. The Company should be instructed to provide these amounts. The amount for the audit period is $44.7 million. The additional amounts for the four years prior to the audit period and two years subsequent to the audit period will result in a rate base reduction significantly greater than $44.7 million.

On a going-forward basis, the Commission has two available options. First, to recognize the tax losses in the calculation of the Surveillance Report tax expense calculation. Alternatively, the Commission could merely continue accumulating the net tax savings as a rate base reduction. The auditors recommend the

latter approach on a going-forward basis.

The recommended approach was initially proposed by the Internal Revenue Service in proposed regulations relating to sections 1.167(1) - 1(a)(7) and 1.268(i)-1 regarding the treatment of consolidated tax savings by public utilities. These proposed regulations were subsequently withdrawn. Nevertheless, it was the IRS's position that such an adjustment would not violate the normalization rules of the Internal Revenue Code, whereas, an adjustment to the tax expense to account for consolidated tax savings would have violated normalization rules. Since these proposed regulations have been withdrawn, the Commission is free to make any adjustment it deems appropriate relating to consolidated tax savings. The auditors believe that the rate base reduction of the cumulative tax savings is the most theoretically correct with respect to past subsidies. A continuation of this approach on a going forward basis would result in a single approach being used for Surveillance Report purposes.

3. Income tax expense charged to regulated operations should not be used to subsidize the losses of nonregulated products and services offered by Southern Bell Georgia.

Summary

During the 1988 to 1991 audit period, Southern Bell - Georgia subsidized $19.5 million of losses incurred by its nonregulated lines of business by increasing the taxes charged to its regulated business. The auditors recommend that on a going forward basis, the adjustments to total company and regulated tax expense relating to nonregulated lines of business be limited to subtracting taxes resulting from taxable income - not losses - of nonregulated lines of business. The auditors recommend that the $19.5 million subsidy during the audit period be set up as an accumulated deferred debit, with the corresponding credit to nonregulated taxes. The accumulated deferred tax amount should be deducted from rate base and amortized back into regulated income over a four-year period.

Criteria

Telecommunications companies in Georgia may not use current revenues earned or expenses incurred in conjunction with services subject to regulation to subsidize services which are not regulated or tariffed.[19] One of the objectives of this audit was to learn whether Southern Bell's regulated customers are protected from cross-subsidy. The Commission has defined cross-subsidy as any action undertaken by SBT which results in an understatement of

[19]O.C.G.A. Section 46-2-23(g).

intrastate regulated revenues or an overstatement of intrastate regulated expenses or investment for SBT.[20]

Condition

Southern Bell - Georgia provides both regulated and nonregulated products and services. Our review of the Company's income tax calculation indicates that the Company calculates its Federal tax expense at the total Company - Georgia level including its regulated and nonregulated business, and then makes various adjustments to arrive at the Federal income tax included in the Surveillance Report. When a nonregulated line of business (LOB) is profitable, the total Company - Georgia tax expense includes a positive amount for the income taxes resulting from the profits of the nonregulated LOB. One of the Company's adjustments to arrive at the Surveillance Report tax expense is to subtract the nonregulated income taxes from the total Company tax expense. This is an appropriate adjustment since it represents actual tax expense incurred by the nonregulated LOB which should not be charged to the regulated operations.[21]

When the nonregulated LOB loses money, a negative tax expense amount is included in the total Company tax expense. Consequently, the Company's adjustment discussed above results in an addition to the total Company tax expense when the nonregulated lines of

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[20]Docket No. 3987-U.

[21]Other aspects of the tax calculation for Georgia's regulated operations are addressed elsewhere.

business lose money.[22] The increased amount is charged to the regulated operation's tax expense. However, the funds derived from this increased charge to regulated operations are never paid to the government as taxes, but merely serve to offset the losses of the nonregulated LOB.

The table below provides two examples demonstrating the Company's tax adjustments for its nonregulated operations. Both examples assume that the regulated operations have taxable income of $15,000, and that the Federal Income Tax rate is 35 percent. The first column assumes that the nonregulated LOB had taxable income of $300. The second column assumes that the nonregulated LOB incurred a loss of $3,700.[23]

Example of Company's Income Tax Calculation for Nonregulated Business

| Description (A) | Nonregulated Income (B) | Nonregulated Loss (C) |
|---|---|---|
| 1. Regulated Net Income | $15,000 | $15,000 |
| 2. Nonregulated Net Income (Loss) | 300 | ( 3,700) |
| 3. Total Net Income (L1 + L2) | $15,300 | $11,300 |
| 4. Tax Rate | 35% | 35% |
| 5. Total Company Tax Payable to Government (L3 x L4) | $ 5,355 | $ 3,955 |
| 6. Company Adjustment for Nonregulated (L2 x L4) | 105 | ( 1,295) |
| 7. Total Taxes Charged to Regulated (L5 - L6) | $ 5,250 | $ 5,250 |

[22]Mathematically the subtraction of a negative amount results in an addition. This was confirmed by the auditors' review of the Company's calculation of its 1991 Georgia FIT expense. The review indicates the Company added $6,362,148 of taxes associated with nonregulated losses to arrive at the Surveillance Report income tax expense charged to Georgia ratepayers.

[23]These examples are drawn from an example provided by the Company.

Column (C) of the example demonstrates that when the nonregulated LOB incurs a loss, the regulated operations absorb a tax expense which is greater than the amount for which the Company is liable to the Federal government. This is a permanent difference for which the Company will never be liable. The Company is able to use current expenses incurred in conjunction with services subject to regulation to subsidize services which are not regulated or tariffed, since the money retained from the higher tax expense charged to regulated operations serves to offset or subsidize the losses of the nonregulated LOB.

Effect

The Company's nonregulated lines of business lost money each year of the audit period. These losses were caused primarily by the losses of its Customer Premises Equipment (CPE) LOB. The amounts shown below were added back to regulated tax expense as a result of the nonregulated losses.

| Year | Tax Effects of Nonregulated Losses Added To Regulated Fit Expense |
|---|---|
| 1988 | $ 632,363 |
| 1989 | 5,712,729 |
| 1990 | 6,769,635 |
| 1991 | 6,362,148 |
| Total | $19,476,875 |

The amounts charged to regulated income tax expense were increased by the $19.5 million shown above as a result of nonregulated losses even though the $19.5 million was not and will not be paid to the Federal government. Consequently, the $19.5 million charged to regulated tax expense reduced the regulated returns each year and also reduced (subsidized) the net after-tax losses of the nonregulated lines of business.

Cause

The Company believes that its adjustments result in an "equitable apportionment" between regulated and nonregulated income tax expense. It is the Company's position that when a nonregulated LOB loses money, any tax treatment other than that which it uses will result in a subsidy from nonregulated operations to regulated operations. This logic, with which the auditors disagree, is the root cause of the condition and effect discussed above.

Recommendation

Income taxes charged to regulated operations should not be used to subsidize the losses of nonregulated products and services offered by Southern Bell - Georgia. In order to stop the subsidy on a going-forward basis, the adjustments to total company and regulated tax expense should be limited to subtracting taxes resulting solely from the taxable income - not losses - of nonregulated lines of business. Regarding the past subsidies, the auditors recommend that the $19.5 million which the Company debited

to the tax expense of its regulated operations over the four-year audit period be set up as an accumulated deferred tax amount with a corresponding debit to account 7220 - Operating FIT - Current Nonregulated. The accumulated deferred taxes should be deducted from rate base and amortized over a four-year period as equal annual reductions to regulated tax expense.

The Company believes that this adjustment would constitute an unlawful taking of Southern Bell's property in contravention of the 14th Amendment to the United States Constitution as well as analogous provisions of the Georgia Constitution. The Company also believes the recommended adjustment would contravene federal decisions on Hope and Bluefield, as well as case authority in Georgia.

There may or may not be merit to the Company's legal allegations. The auditors disagree, from a technical standpoint, that the recommended adjustment would constitute a "taking" of Southern Bell's property since the auditors believe the tax expense amounts in question were improperly charged to regulated operations. The auditors further believe that to continue this practice will continue an improper cross-subsidy.

4. The Commission should instruct the Company to match benefits to related costs.

Summary

It is axiomatic that costs and benefits should be matched. This finding identifies interest income (a benefit) received in 1991 by the Company relating to an amount included above-the-line in regulated rate base (a cost) for eight years. The Company's literal interpretation of the Part 32 USOA resulted in the entire benefit being recorded below-the-line, i.e. the benefit was not matched to the cost. The auditors recommend that the Commission instruct the Company to match specific benefits to related costs.

Criteria

Benefits should be matched to related costs.

Condition

In January, 1991 Southern Bell - Georgia received $2.7 million in interest income from the IRS relating to a 1983 payment to the IRS. The 1983 payment was comprised of tax and interest associated with a 1978 disputed issue. The tax component of the 1983 payment resulted in a $.8 million accumulated deferred tax debit which increased regulated rate base without any corresponding reduction to regulated tax expense. The interest portion of the 1983 payment was charged to nonregulated operations "below-the-line".

The interest income received in 1991 and recorded below-the-line related to both the interest expense and taxes paid in 1983.

Therefore, a portion of the interest income related directly to the $.8 million amount which was included in Southern Bell - Georgia's rate base, above-the-line, for approximately 8 years.

Effect

Southern Bell - Georgia's nonregulated below-the-line operations derived a benefit at the expense of its regulated above-the-line operations. Although the regulated operations bore the carrying costs of a $.8 million rate base amount for 8 years, none of the resulting benefits were matched to these costs.

Cause

Part 32 definitions place "interest income" below-the-line. In these circumstances, strict adherence to Part 32 enabled the company to derive a nonregulated benefit at the expense of regulated operations.

Recommendation

The Commission should instruct the Company to match benefits to related costs.

5. Accumulated deferred taxes and unamortized investment tax credits which represent taxes charged to regulated operations should not be transferred to nonregulated operations. Case-by-case burden of proof concerning any IRC violation belongs with the Company.

Summary

Accumulated deferred income taxes ("ADITs") and unamortized investment tax credits ("ITCs") generated under regulation represent charges to tax expense for taxes that were not actually paid. In general, it is assumed that these tax amounts will eventually be used to reduce future tax expenses. If ADITs and unamortized ITCs are generated under regulation and then transferred to a nonregulated affiliate, the transfer results in a subsidy to the Company's shareholders. This finding identifies certain ADITs and unamortized ITCs transferred from Southern Bell - Georgia to nonregulated operations. These transfers may have resulted in such subsidies. Consequently, the auditors recommend that ADITs and unamortized ITCs generated under regulated operations not be transferred to nonregulated operations. Should the Company claim that such transfers are required to avoid IRS violations, the auditors recommend that the burden of proof be placed on the Company on a case-by-case basis.

Criteria

One of the objectives of this audit was to learn whether, as a result of the relationship between the Company's regulated telephone operations and its nonregulated activities and the

nonregulated operations of its affiliates, Southern Bell's regulated customers are protected from cross-subsidy.

Condition

During the course of the 1988 to 1991 audit period the Company made several asset transfers to and from affiliated companies. The accumulated deferred income taxes and unamortized investment tax credits associated with these assets were "transferred" along with the related assets. Certain of the ADITs and unamortized ITCs that were transferred represent tax expenses charged to regulated operations which were not actually paid. The quid-pro-quo is that these amounts would be used to reduce future regulated taxes. Once the ADITs and unamortized ITCs were transferred out of regulation, the Company was relieved of the necessity to reduce future regulated tax expense under the terms of the quid-pro-quo.

The table below summarizes the specific transfers of which the auditors are aware:

Transfers of ADIT and
Unamortized ITCs From
Regulated Operations to
Nonregulated Operations

| Year | Description | Amount |
|---|---|---|
| 1985 | Southern Bell - Ga. to ASI | ? [24] |
| 1987 | Southern Bell - Ga. to BSS | approx. $250,000 |
| 1989 | Southern Bell to BSS | $ 74,926 |
| 1991 | Southern Bell - Ga. to BCI | $213,333 |

[24]Amount not provided to auditors.

The 1985 transfer was from Southern Bell - Georgia to Advanced Systems, Inc. ("ASI"). Advanced Systems, Inc. was a subsidiary created to handle the Company's CPE business. Prior to the creation of a separate entity in 1985, the CPE assets attributable to Southern Bell - Georgia's ASI line of business were segregated from the company's regulated operations in Southern Bell's books of account on a below-the-line basis. In 1989, the CPE line of business was reintegrated into Southern Bell - Georgia as a nonregulated line of business and that such reintegration was the primary cause of the cross-subsidy discussed in Finding No. 12.

The 1987 and 1989 transfers were to BellSouth Services. As described in Finding No. 12, the Company began to add back BellSouth Services net income and equity to Georgia's earnings and rate base respectively. The Company contends that because the unamortized ITCs transferred to BSS continued to be amortized on BSS's books, Georgia's regulated customers received all the asset related tax benefits to which they are appropriately entitled.

In general, the auditors would agree with respect to the add-back of the 1989 amount. As explained in Finding No. 12, the BSS add-back appears to have resulted in a subsidy to the Company's nonregulated CPE line of business. While the add-back should have protected regulated customers, the CPE cross-subsidy convolutes the issue. The first year of the add-back was 1989. The regulated customers were not protected in 1987 or 1988 regarding the 1987 transfer.

Finally, the Company contends that the assets which were

transferred in 1991 to BCI had been assigned or apportioned to nonregulated on Southern Bell's books. The auditors examined the actual journal voucher associated with this entry. The ADITs in question were included in the following function codes ("FCs") while on Southern Bell's books: 5D85 and 5D8B. Both of these FCs are common and are allocated between regulated and nonregulated lines-of-business on the regulated company's books via the cost allocation manual.

Effect

The transfers above may or may not have resulted in subsidies to the Company's shareholders. The auditors believe the practice of transferring ADITs and unamortized ITCs generated and charged to regulated operations to nonregulated operations will result in subsidies to the Company's shareholders.

Cause

The Company cites to Part 32.27 of the USOA and certain IRS private letter rulings as the cause of these transfers. The auditors have found no specific Part 32 requirement to transfer ADITs and unamortized ITCs along with the related assets. Furthermore, the Company in fact retained the ADITs on the Southern Bell - Ga. books associated with the transfer of an airplane to BSS. The auditors are, however, cognizant of certain IRS private letter rulings which indicate that retention of unamortized ITCs attributable to assets no longer in rate base would violate

normalization requirements.

Recommendation

ADITs and unamortized ITCs which represent taxes charged to regulated operations should not be transferred to nonregulated operations. Such transfers result in a subsidy to the Company's shareholders. The Commission should require the Company to prove, on a case-by-case basis, that it will be in violation of the Internal Revenue Code before any ADITs or unamortized ITCs generated under regulation are transferred to nonregulated operations.

6. The Commission should be cognizant that the Company derives benefits through deferred tax activity in rate case years and non-rate case years.

Summary

The calculations and rules surrounding deferred tax calculations enable the Company to derive benefits in rate case years and non-rate case years. This finding demonstrates that the Company derived a cash benefit from deferred taxes in the Rule Nisi case, and reduced earnings and increased rate base through deferred taxes in non-rate case years. The auditors recommend that the Commission be cognizant of Company's ability to derive these benefits at the expense of its regulated customers in the tax area.

Criteria

Accumulated deferred income taxes ("ADIT") are deducted from the Company's regulated rate base because they represent cost-free capital derived from regulated customers through the regulatory process.

Condition

In general, deferred taxes have the following impacts:

a) A debit (increase) to deferred tax expense and a credit to accumulated deferred income taxes results in higher expense with a corresponding reduction to the rate base.

b) A credit (decrease) to deferred tax expense and a debit to accumulated deferred income taxes results in lower expense with a corresponding increase to rate base.

The Company derives a cash benefit when deferred tax debits

are included in allowable expenses in a rate case because the expense is noncash. These expenses are charged to customers in the form of higher rates and yet there is no corresponding cash outlay on the part of the Company. Furthermore, in a rate case the benefit to the Company of the increased cash flow normally exceeds the value of the corresponding rate base deduction. In non-rate case years it is in the Company's best interest to build rate base.

While reviewing the Company's tax return calculations, the auditors noted an anomalous situation concerning Southern Bell - Georgia's deferred tax expenses. The table below shows the Company's deferred tax expenses for each audit year. The only rate case during the audit period was the Rule NISI case which was based on a 1989 test year. The only year the Company recorded a deferred tax debit was 1989, i.e. the Rule NISI test year. The Company's deferred tax expense was negative for all other years. Thus, the Company derived the cash flow benefit in the Rule NISI case and then built rate base in all other non-rate case years.

Summary of Deferred Tax Expense
1988 to 1991
($000,000)

| Year | Southern Bell Total Company | Georgia |
|---|---|---|
| 1988 | $( 5) | $(17) |
| 1989 | 53 | 34 |
| 1990 | ( 85) | (17) |
| 1991 | (135) | (13) |

The deferred taxes were negative in the non-rate case years because the Company recorded expenses in those years which were not deductible for tax purposes: vacation pay accruals, for example.

Vacation pay accruals are also non-cash expenses. Therefore, in the non-rate case years, the Company recorded non-cash expenses which reduced net income on a net basis after the deferred tax credit, and at the same time increased its rate base through a deferred tax entry.

Effect

The Company derived a net cash benefit in the Rule NISI case, and then decreased net earnings while increasing rate base in the non-rate case years.

Recommendation

The auditors concur that this Finding does not identify any violation of GAAP, Part 32 or IRC provisions. Nevertheless, the auditors recommend that the Commission be cognizant of the Company's ability to derive benefits at the expense of its regulated customers through deferred tax activity in rate case years and non-rate case years.

## 7. Georgia PSC auditors should be provided access to all income tax returns and related workpapers.

### Summary

The auditors have identified various tax-related findings, several of which identify cross-subsidies. However, the auditors were unable to reconcile Southern Bell - Georgia's 1991 tax calculation to BellSouth Telecommunications' tax return because the Company denied them access to records relating to any nonregulated operations other than those specifically provided by Southern Bell - Georgia. The customers of the Company's regulated services are not protected from cross-subsidy as long as access to such tax information is denied. The Commission should direct the Company to provide Georgia PSC auditors with unrestricted access to all tax returns and related workpapers.

### Criteria

Telecommunications companies in Georgia may not use current revenues earned or expenses incurred in conjunction with services subject to regulation to subsidize services which are not regulated or tariffed.[25] One of the objectives of this audit was to learn whether, as a result of the relationship between the Company's regulated telephone operations and its nonregulated activities and the nonregulated operations of its affiliates, Southern Bell's regulated customers are protected against cross-subsidy. The

[25]O.C.G.A. Section 46-2-23(g).

Commission has defined cross-subsidy as any action undertaken by SBT which results in an understatement of intrastate regulated revenues or an overstatement of intrastate regulated expenses or investment for SBT.[26]

Condition

The auditors identified a tax deduction being taken on the BSC Federal tax return which was associated with costs being incurred by the regulated operations. The tax benefit of this deduction was not being flowed down to the regulated operations. This situation, as discussed in Finding No. 1, resulted in a cross-subsidy from the regulated operating company to the nonregulated parent.

Given this cross-subsidy, the auditors considered it appropriate to review the parent company return and reconcile it to the Southern Bell - Georgia tax calculation. The auditors were denied access to any consolidating workpapers underlying the parent company's return and any subsidiary's tax return other than Southern Bell's and BellSouth Services'.

In response to audit request MJM-33 the Company offered certain consolidated tax information with the proviso that all BellSouth Enterprises information would be redacted from the workpapers. In essence, no workpapers underlying BellSouth Corporation's consolidated tax returns were shown to the auditors.

The auditors informed the Company that they intended to report their inability to reconcile these tax returns due to the denial of

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[26]Docket No. 3987-U.

access to the requested records. On November 19, 1993, the auditors were offered a list of the various affiliate tax returns. The Company was asked if the auditors could select affiliates from the list on a test basis and review those tax returns. The Company would not allow this approach.

Next, the auditors asked if they could select affiliates from the Cost Allocation Manual and review those returns. Again, the answer was no. The auditors determined that an unauditable list was worthless.

Audit request MJM-89 requested typical spreadsheet summaries of tax payments, taxable income and allocation of consolidated returns, tax credits and separate tax calculations, and summaries of tax and allocation entries resulting in final tax liabilities. The Company would not provide the information for any companies other than Southern Bell, South Central Bell, BellSouth Services and BellSouth Consolidated.

In a January 13, 1994 letter relating to audit request MJM-90 the Company offered to "provide the total bottom-line amount remitted by BellSouth Corporation on its consolidated tax return as well as a list of all entities that were party to the return". However, in a February 10, 1994 meeting, the auditors were informed that the subject list would not be provided.

Finally, the auditors were also denied access to nonregulated tax information relating to any other Southern Bell state. The table below summarizes the attempted reconciliation.

Attempted Reconciliation
of Tax Returns 1991
($000,000)

| | Description | Amount | Able to Test |
|---|---|---|---|
| 1. | SB - Ga. Fed. Tax Return Liability | $111.5 | Yes |
| 2. | Other Southern Bell States | 315.1 | No |
| 3. | Total Southern Bell | 426.6 | Reviewed return |
| 4. | Other Affiliates | xxxx | No |
| 5. | BellSouth Corporation | $xxxx | Reviewed return |

Effect

Anything other than an unqualified "yes" under the "Able to Test" column above results in an inability to perform the attempted reconciliation. Thus, the auditors were unable to perform the attempted reconciliation as a result of being denied access to certain documents. With the inclusion of this specific finding, the auditors have identified seven tax-related findings. Several of these involve cross-subsidies. Therefore, it is the auditors opinion that, unless the Georgia PSC auditors are provided access to all income tax returns and related workpapers associated with the consolidated return of which Southern Bell - Georgia is a member, Georgia's regulated customers are not protected against cross-subsidy.

Cause

Company denial of access to tax returns and workpapers relating to nonregulated operations.

Recommendation

The Company should be instructed to provide Georgia PSC auditors with unrestricted access to all tax returns and related workpapers.

8. The Company should be reprimanded for adding MemoryCall[R] losses to the Surveillance Report without notifying the Commission and the Company's failure to file tariffs and supporting cost of service studies.

Summary

Inclusion in the Surveillance Report of MemoryCall[R] results beginning in June 1991 was not reported to the Commission. Full reporting of such results and filing of a tariff and cost of service study, including all workpapers in support thereof demonstrating that the price of MemoryCall[R] is just and reasonable, would have permitted a current appraisal of Southern Bell's progress in the transition to a competitive environment and be consistent with goals established by the Commission. The record relating to MemoryCall[R] is somewhat convoluted. It appears Southern Bell determined, on an informal basis, how it intended to interpret and implement the various provisions of the Order in Docket No. 4000-U.

At a minimum, the auditors believe that SBT should have notified the Commission and filed tariffs when it began to add MemoryCall[R] operating losses to regulated operations. This would have permitted a prompt and fair evaluation of the trial offering of MemoryCall[R].

Absent such a process, Southern Bell had the opportunity to interpret and implement the broad principles of the Order in such a manner as to disadvantage its competitors or otherwise act in a manner contrary to the public interest. The Company should be

reprimanded for its failure to notify the Commission, and its failure to file a tariff and supporting cost of service study.

Criteria

The following quotations are excerpted from the May 21, 1991 Order of the Commission in Docket No. 4000-U.

> Nothing in this record disproves the possibility that MemoryCall[R] is cross-subsidized and/or predatorily priced. Rather, the record suggests the opposite possibility, namely that MemoryCall[R] is priced below cost.[27]
>
> Whatever the reasons, the actual cost analysis filed by SBT at the close of the Docket is insufficient to allow the record in this case to reflect a detailed, reasoned analysis of the true cost to SBT of providing MemoryCall[R].[28]
>
> ACTION TAKEN TO PREVENT AND/OR DETER MONOPOLY ABUSE
>
> As explained in the Order, the Commission desires to promote the development of an efficient, competitive ES market, including specifically the VMS market. SBTs presence therein will assist that development, so long as SBT is practically prevented from using its monopoly position to unfairly promote and provide its enhanced services over its competitor's similar services.[29]
>
> Ordered further, that SBT shall file a complete cost of service study, including all workpapers in support thereof, demonstrating that the price of MemoryCall[R] is just and reasonable.

Condition

In Docket No. 3896-U, the Company was instructed to file tariffs and cost support relating to its MemoryCall[R] service.

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[27]Order of the Commission, Docket No. 4000-U, May 21, 1991, p. 41.

[28]Id., p. 42.

[29]Id., p. 47.

Certain cost data was filed on the last day of the hearings in Docket No. 4000-U. The Company informed the auditors that it has not filed tariffs because the 3896-U Orders were stayed and the Order in Docket No. 4000-U did not specify tariffs.

According to line-of-business income statements, MemoryCall[R] has lost money each year since its inception. Appendix D to this report is a copy of the Company-developed 1991 line-of-business income statement for MemoryCall[R] with all numbers deleted. The Company contends that it is inappropriate to rely on this statement to determine the profitability of MemoryCall[R].

In June 1991 the Company began to add MemoryCall[R] losses to the regulated results of operations included in the Georgia Surveillance Report. The Surveillance Report made no mention of the add-back of the losses, and it is impossible to determine by examining the Surveillance Report that such an add-back was occurring. The Company did not identify specific MemoryCall[R] information because it was proprietary.

The only indication, prior to this audit, that MemoryCall[R] was included in the Surveillance Report was through cross-examination of a Company witness in Docket No. 3987-U on February 19, 1992, i.e. nine months after the Company began to be add back losses to the Surveillance Report. The colloquies below represent the Company's advisement to the Commission.

By Commissioner Rowan: The Commission ---- this might not have been adjudicated all the way, but there's an assumption I believe on the Commissioners part that MemoryCall[R] was a regulated entity.

The Witness: A. Yes.[30]

* * * *

By Mr. Adelman: Q. So at that point, was it the Company's position that MemoryCall[R] was regulated?

The Witness: A. I don't think it was the Company's position. It to me is a legal argument of whether it was regulated or non-regulated, and we appealed to the FCC to try to resolve that issue. But from the standpoint of the earnings report, since the Georgia Commission had ruled and that was the rule of the day, then the non-regulated -- previously non-regulated investment expenses for MemoryCall[R] were included in the intrastate results starting in June of 1991.

Mr. Adelman: Q. So it was in -- they were included 100 percent intrastate?

A. Yes, they were. That was the interpretation of the Commission's June Order as relayed to me.

Mr. Adelman: No further questions, Mr. Chairman.[31]

The auditors do not agree that these colloquies represent official notification. Were it not for the questions, the Commission would not have been notified. Nevertheless, the Commission was notified.

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[30]Docket No. 3987-U, February 19, 1992, at 1062.

[31]Id., p. 1093 to 1094.

Effect

MemoryCall[R] losses have been absorbed by other regulated operations since June, 1991. In 1991 the add-back reduced the Georgia ROE from 12.03 percent to 11.85 percent. The Company's add-back of MemoryCall[R] losses to regulated operations without specific direct disclosure to this Commission hindered the Commission's evaluation of the trial offering of MemoryCall[R].

Cause

Company's interpretation of the Commission's Order in Docket No. 4000-U.

Recommendation

The auditors recommend that the Commission reprimand the Company by whatever means are available for adding MemoryCall[R] losses to regulated profits on the Surveillance Report without any notification to the Commission and without the filing of any tariffs and cost studies.

## 9. Southern Bell's construction program should be regularly audited.

### Summary

The auditors' review of MemoryCall[R] construction program estimates revealed several errors. Incorrect coding on the two MemoryCall[R] estimates processed by SB in 1990 caused the capital costs involved to be initially assigned to regulated instead of nonregulated. Additional incorrect coding on one of these estimates caused 30 percent of the Right-To-Use ("RTU") software costs involved to be charged to capital, instead of expense. The December 1991 ARMIS Joint Cost Report failed to reflect as nonregulated plant-in-service over $250,000 of MemoryCall[R] investment placed in 1990 and 1991. Although internal controls eventually detected and corrected the coding errors and the ARMIS issue was a timing difference, the RTU problem was not corrected until uncovered by this audit. The auditors recommend that internal and external audits of SB's construction program be scheduled on a regular basis to help ensure proper cost assignment.

### Criteria

The initial assignment of investment is critical to the maintenance of an accurate separation of regulated and nonregulated costs. Absent special scrutiny, input errors may escape detection because of the magnitude of investment data processed each month and the complexity of related accounting systems.

Condition/Effect

The controversial nature of SB's MemoryCall[R] service led the auditors to carefully review the four MemoryCall[R] estimates processed in 1990 and 1991.[32] It was found that the input code on estimates M1290 and M1418 was 615A0 instead of 615X1. This coding error led to the initial assignment of related capital costs to regulated, instead of nonregulated. Fortunately, this discrepancy was detected as part of SB's monthly review of Cost Separations System ("CSS") activity, and corrected in December 1990.

The audit further revealed that 30 percent of the RTU software costs on estimate M1418 was charged to capital (Account 2212,377C), instead of expense (Account 6212,377M). An adjustment was made in May, 1993, to correct this error.

The auditors also attempted to track the MemoryCall[R] investment placed in service in 1990 and 1991 to the December 31, 1991 ARMIS Joint Cost Report (FCC Report 43-03). The ARMIS Report was found to include $3,881,807 of directly charged MemoryCall[R] Digital Electronic Switching (Account 2212) investment.[33] The four estimates completed by the end of 1991 contained $4,169,151 of Account 2212 investment. As of January 1, 1993 it was found that $4,139,474 of MemoryCall[R] related Account 2212 investment placed in 1990 and 1991 remained in service.[34] The difference between the

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[32]Estimates M1290, M1418, M1765 and M1842.

[33]The ARMIS Report reconciles to the CCS/PPS Part X Summary for the month of December, 1991. Direct charges to Memory Call are found to be $3,881,806.62 on page 30 of the CCS/PPS Part X Summary.

[34]ICS/DCPR run dated January 2, 1993, pages 10756 to 10761.

estimate total and the 1993 plant-in-service total ($29,677) is not considered significant by the auditors since some plant placed in 1990 and 1991 may have been retired by 1993. However, the difference between these totals and the 1991 ARMIS Report amount is significant because it indicates an understatement of MemoryCall[R] investment of at least $257,667, or 6.2 percent, as of the end of 1991. To the extent that this discrepancy was a result of the one month lag between the Company's Detailed Continuing Property Record ("DCPR") and CCS, it was corrected in January 1992. In any case, it is likely that complete reconciliation was effected in June 1992 in connection with the Company's annual true-up of central office equipment.

Cause

The cause of the input errors described above could not be specifically determined, but may be related to the fact that these were the first four MemoryCall[R] estimates to be processed by the Company.

Recommendations

In light of these findings, the auditors believe that special scrutiny should be afforded construction program activities related to nonregulated services. Since such activity makes up only a small portion of the total construction program, the unique coding required for nonregulated treatment can sometimes be overlooked. To provide a safety net to supplement SB efforts to maintain

accuracy in this highly sensitive area, the auditors recommend that both internal and external audits focus on this aspect of SB's construction program on a regular basis.

10. Right-To-Use fees should be directly assigned whenever possible.

Summary

During the audit period, MemoryCall[R] RTU fees were not directly charged to nonregulated, but were instead allocated on the basis of investment in the digital switching account. Although the CAM approved by the FCC in 1989 included a direct charge cost pool, this pool was not used for RTU fees prior to 1993. In 1993, the Company revised its systems and documentation to allow the direct charging of RTU fees. If a cost pool is listed in the Company's CAM, the FCC, the Commission and other interested parties have a right to assume the cost pool is used when appropriate.

Criteria

Part 64 of the FCC's rules states:

> Costs shall be directly assigned to either regulated or nonregulated activities whenever possible.[35]

In conformance with this rule, MemoryCall[R] RTU fees, booked to Digital Electronic Switching Expense (Account 6212) should be directly assigned to nonregulated.

Condition

During its review of the four MemoryCall[R] estimates processed in 1990-1991, the auditors found that RTU fees were not being directly assigned to nonregulated. The Company confirmed that

[35]Code of Federal Regulations, Title 47, §64.901 (b)(2).

these expenses were being allocated based on the investment in Digital Electronic switching (Account 2212, 377C).

Further review revealed that the Company had established a "Direct Regulated/Nonregulated" cost pool in its CAM on June 30, 1989.[36] In early 1989, the FCC staff was working informally with telephone company personnel to guide them in the improvement of their CAMs. Although the Company contends that the FCC did not order it to establish a direct charge cost pool in Account 6212, this account was one of 14 which received new "Direct Regulated/Nonregulated" cost pools in the Company's June, 1989, CAM revision.

The Company did not, however, immediately revise its procedures to allow this cost pool to be used for the charging of RTU fees. From June 1989 through September 1991 this pool was used for the direct charging of Equal Access/Network Reconfiguration expenses to regulated. Effective October 1, 1991, the Company's CCS/PPS User Guide was changed to state that the "Direct Regulated/Nonregulated" cost pool (CP 01) was "not used".[37] The Company finally revised its systems and procedures to allow the direct charge cost pool to be used for RTU fees in 1993.

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[36]See Appendix E, Table 7-4.

[37]See Appendix E, pp. 9.12.4 and 9.12.8. Note also that CP 99 as described on p. 9.12.1 contains investment leased to others and is assigned to regulated.

Effect

Since the great majority of digital switching investment is classified as regulated, the allocation of Memory call RTU fees resulted in the overstatement of regulatory expense and the understatement of nonregulated expense. In estimate M1418, $95,000 of RTU fees were so allocated instead of directly charged in 1990. The net effect of all RTU fee transactions during the audit period could not be determined, however, since direct charges to regulated might also have been made if the Company used CP 01.

Perhaps of greater significance than the amounts involved, however, is the fact that the Company listed in its CAM a direct charge cost pool which could not actually be used for RTU fees for over three years, and could not be used at all for over one year. If a cost pool is listed in a company's CAM, the FCC, the Commission and other interested parties have a right to assume that the cost pool is used when appropriate.

Cause

The auditors were unable to determine why the "Direct Regulated/Nonregulated" cost pool was not used for RTU fees until 1993. The Company contends that its activation in 1993 was not related to the auditors' review of construction program activity.

Recommendation

The auditors recommend that the Company ensure that its personnel are trained to directly assign RTU fees whenever

possible. The auditors also recommend that the Company not list any cost pool in its CAM which can not be used, unless this condition is fully disclosed in the CAM and the CCS/PPS User Guide.

11. The Commission should investigate the implications of a 1990 switch price restructure and increase its audit scrutiny of BellSouth to ensure that basic business and residential ratepayers are protected against cross-subsidies.

Summary

A 1990 switch price restructure negotiated between BellSouth and AT&T[38] appears to have increased the costs assignable to noncompetitive services, e.g. POTS, call waiting, call forwarding, speed calling, etc., while reducing the costs assignable to competitive services, e.g. ESSX. The price restructure will have a direct impact on any current or future service cost studies reflecting switches purchased after the price restructure. Since the price restructure immediately preceded a major switch purchase, negotiated by BellSouth Services, a subsidiary of Southern Bell, the impact of these shifts are being incurred in addition to the fact that overall rate base and investment related costs are increasing.

AT&T's price restructure resulted in more of the total cost than would have been incurred prior to the restructure being absorbed by noncompetitive basic local exchange service and by noncompetitive discretionary services normally purchased by POTS customers. This was offset by lower incremental costs of competitive services (ESSX) after the restructure. The AT&T price restructure positioned Bellsouth to subsidize future competitive services at the expense of increased costs to noncompetitive

[38]See Appendix F.

services.

The Commission should investigate whether BellSouth has taken an unfair competitive advantage of its monopoly position in favor of its ESSX service and all other competitive services at the expense of its monopoly customers. This investigation must also determine how the price restructure impacts current and future cost studies. The Commission should also increase its audit scrutiny of this Company to ensure that basic business and residential ratepayers are protected against cross-subsidies of any kind.

Criteria

Telecommunications companies in Georgia may not use current revenues earned or expenses incurred in conjunction with services subject to regulation to subsidize services which are not regulated or tariffed.[39] One of the objectives of this audit was to learn whether Southern Bell's regulated customers are protected from cross-subsidy. The Commission has defined cross-subsidy as any action undertaken by SBT which results in an understatement of intrastate regulated revenues or an overstatement of intrastate regulated expenses or investment for SBT.[40]

Condition

In 1990 AT&T restructured its switch and software prices. It appears that even after certain discounts were applied, the

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[39]O.C.G.A Section 46-2-23(g).

[40]Docket No. 3987-U.

restructure created two basic cost shifts: (a) from direct expense (software) to capital cost (hardware and capitalized software), and (b) an inter-service shift from the competitive ESSX service to non-competitive residence and business service.

The first shift was accomplished by AT&T's regrouping of its software features to accommodate BellSouth's concerns regarding its most competitive lines of business. This shift decreased the price for the expensed (noncapitalized) software required to provide ESSX service with a partially offsetting increase to the price of the noncapitalized BRCS Universal software required to provide enhanced services such as call waiting, call forwarding, speed calling, etc. to monopoly residence and business customers.[41] The price decrease for ESSX software was so substantial that the overall total net price for feature (noncapitalized) software decreased.

AT&T's second shift increased hardware (capital) prices to recoup the overall reduction in software (expense) prices resulting from the decreased price for ESSX software. Specifically, AT&T increased the price for line cards so that the overall switch price remained revenue neutral. Line cards are required to provide dial tone and therefore are a fundamental component of the cost of monopoly service. Southern Bell properly notes that the price of line card units ("LCUs") decreased. LCUs are also a component of the cost of dial tone. Nevertheless, the line card price increase

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[41]Prior to the price restructure BRCS I supported basic business and residence lines. Subsequent to the restructure, BRCS Universal contained four new services, i.e cancel call waiting, call hold, automatic callback calling, distinctive ringing.

overwhelmed the LCU decrease.

BellSouth denies that there was a shift from expense to capital. AT&T, on the other hand, indicates that the expense-to-capital shift was the intent as well as result of the price restructure. AT&T contends that the restructure was "revenue neutral" to AT&T (i.e., total bottom-line switch and software revenue remained the same.)

BellSouth also maintains that the overall result of the price restructure and the subsequent negotiations was a net reduction in the per-line price of hardware and software. This net reduction appears to have resulted from increased discounts to BellSouth rather than from the price restructure. The restructured prices which are the subject of this finding were separate and apart from the additional discounts negotiated by the Company after the prices were restructured. Importantly, the Company acknowledges that even after discounts, the price of line cards increased.

The auditors note that Southern Bell "retained an unaffiliated third-party consulting/accounting firm to investigate this matter and to provide an unbiased expert opinion". According to the Company, that firm's conclusions apparently found "no merit in any of the auditors' allegations".

The auditors requested a copy of the third-party consulting/accounting firm's report in order to consider it in the development of our final opinion. The report in question is titled Bellsouth Telecommunications AT&T 5ESS Switch Procurement (1989-1991). It was prepared by Deloitte & Touche and transmitted to the

Company on March 9, 1994. The auditors have reviewed the Deloitte & Touche report and identified apparent technical flaws and inconsistencies.[42] The Company's representatives have been notified of these flaws and inconsistencies. The auditors have been informed that Deloitte & Touche stands behind its report. In general, the auditors believe that when the flaws are corrected, the Deloitte & Touche report corroborates the auditors' findings in this area.

Effect

AT&T's price restructure is significant for many reasons. Immediately following the restructure, BellSouth made a commitment to purchase 86 new AT&T switches. Approximately 30 of the new switches were to replace existing switches in the Atlanta metropolitan area. AT&T's invoices reflecting the restructured prices determine BellSouth's accounting for the switch purchases. Therefore, the consequences of the price restructure are being incurred as the switches are placed in service and are reflected in any service cost study performed or to be performed subsequent to the price restructure.

The restructured prices resulted in cost shifts with

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[42]For example, Appendix 4 of the report compares AT&T list prices as of 1989 with restructured 1991 prices. The 1989 prices, however, exclude BRCS II which comprises a majority of BRCS-ESSX at the restructured price. Another example is that the report appears to assume that BRCS 3 essentially became BRCS Extended ESSX (Centrex). This assumption is incorrect. The overwhelming majority of BRCS ESSX is from BRCS II prior to the restructure. The exclusion of BRCS II from any comparison of list prices pre and post restructure is inappropriate and misleading.

regulatory implications for BellSouth. The auditors determined this based on a review of (1) all relevant correspondence between the parties and internally within BellSouth dating from August 1989 to January 1991, (2) an April, 1990 AT&T presentation to BellSouth, (3) interviews with AT&T Network Systems and with a BellSouth officer and other BellSouth SMEs, and (4) discovery responses and price lists attached to contract 6700-B.[43] The auditors attempted to obtain from the Company, "surrogate cost studies" before and after the price restructure. However no such studies were available.

Since BRCS Universal software is purchased for all access lines, the average cost and incremental cost of a basic line increased as a result of this shift. The remaining portion of the ESSX software reduction was shifted to the cost of monopoly service by a direct increase to the cost of line cards. Line cards are required to provide dial tone and therefore are a fundamental component of the cost of monopoly service. Again, the average and incremental cost of a basic line increased. The incremental cost of BRCSs ESSX services declined significantly.

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[43]The auditors attempted to review the contract PR-2774-B which first effected the price restructure. They were provided with a copy of contract PR-6700-B which went into effect January 1, 1992. All prices, with the exception of one, from AT&Ts April, 1990 presentation of the price restructure, were traced into contract PR-6700-B. The per line price for BRCS Universal was higher in contract PR-6700-B than as shown in AT&Ts presentation. The Company explained that the restructured price for this one item increased by 25 percent in the one year between contract PR-2774-B and PR-6700-B. Consequently, the original increase to the cost of basic residential and business service, increased yet further within one year.

BellSouth took advantage of the fact that its accounting is based on AT&T's invoices. BellSouth forced down AT&T's bid price for ESSX service without regard to AT&T's cost and did not object to the offsetting increases to AT&T's prices for hardware and software assignable to monopoly service.

AT&T's price restructure shifted cost from BellSouth's ESSX service category to its monopoly residence and business categories. This enabled BellSouth to increase the profit margins of its competitive service by shifting cost to its monopoly service. The increased profit margins could be used to reduce prices or alternatively to avoid price increases. The restructure also shifted cost from expense (ESSX software) to capital (rate base). These shifts are reflected in an increase to BellSouth's overall rate base resulting from the major switch purchase it made from AT&T. The shifts will also be reflected in any current or future cost studies which include switch and software costs at the restructured prices.

Under these circumstances AT&T's price restructure would result in more cost being absorbed by noncompetitive basic local exchange service and noncompetitive, discretionary services normally purchased by POTS customers, e.g. speed calling, call waiting, call forwarding, etc., offset with lower incremental costs for the competitive operations than would have been incurred prior to the restructure. The AT&T price restructure positioned Bellsouth to subsidize future competitive services at the expense of increased costs to noncompetitive services. At the same time

total rate base was increasing due to BellSouth's major switch purchase from AT&T.

Cause

The AT&T price restructure was a national price restructure. Specifically, as it related to BellSouth, it appears that BellSouth used its purchasing power to achieve lower software costs assignable to its competitive customers because its Line of Business organization determined that those costs were too high for competitively marketing services in BellSouth. AT&T responded with lower directly assignable ESSX software costs and higher directly assignable non-competitive feature software and line card costs.

The correspondence and other documents reviewed by the auditors relating to this finding are attached as Appendix F. Certain significant documents are still in the Company's hands due to the proprietary agreement.

Recommendation

BellSouth used its purchasing power to obtain restructured prices which shifted BellSouth costs from competitive services to non-competitive monopoly services. BellSouth used the market power it possesses as a result of its virtual monopoly position in the local exchange market to achieve these results.

The Commission should investigate whether BellSouth has taken an unfair competitive advantage of its monopoly position in favor of its ESSX service and all other competitive services at the

expense of its monopoly customers. This investigation must also determine how the price restructure impacts current and future cost studies. The Commission should also increase its audit scrutiny of this Company to ensure that basic business and residential ratepayers are protected against cross-subsidies of any kind.

12. The inclusion of BellSouth Services' net income and equity in the Surveillance Report provided a subsidy for it's nonregulated CPE products and masked the over-earnings on sales to the regulated operations.

Summary

BellSouth Services, Inc. ("BSS") was a nonregulated subsidiary that provided supplies and equipment to the BellSouth companies. As proposed by the Company, BSS's equity and net income were treated as regulated, i.e. above-the-line rate base and net income adjustments in the Rule NISI case. The Commission was not aware, however, that these BSS adjustments contained millions of dollars of obsolete nonregulated customer premises equipment ("CPE").[44] Since BSS's return on its CPE investment was significantly less than Southern Bell's allowed rate of return this resulted in a cross-subsidy to BSS's CPE operations.[45] The Commission was also not aware that the Company increased the add-back to its regulated rate base merely by relieving BSS of its liability for advances from other affiliates.

As a result of the inclusion of BSS's CPE investment and earnings in the Surveillance Report adjustments, the regulated telephone customers in Georgia were not protected from the

[44]The CPE was comprised of PBXs and Key Systems normally used by businesses. The inventory was continually written-down due to the tremendous technological advances in Customer Premises Equipment during this period, and subsequent changes in customer needs and preferences. The inventory write-downs were charged directly to nonregulated accounts on Southern Bell's books. Therefore, they did not reduce BSS's earnings. However, neither did they reduce the equity add-back to Southern Bell's rate base.

[45]See Appendix G.

excessive earnings BSS experienced on overpriced sales of other equipment to the regulated companies during the 1989 to 1991 time frame. Southern Bell's rate base is presently overstated as a result of purchasing overpriced products from BSS.

The auditors recommend a permanent $19.152 million reduction to Southern Bell's rate base to eliminate the effect of the overpriced products included therein. The $19.152 million amount is actually the cumulative CPE-related equity included as an add-back to Georgia's intrastate rate base by way of the BSS adjustments in the Surveillance Reports. Although the $19.152 million represents the cumulative equity add-back, the auditors are recommending its use as a surrogate for the overpriced products included in the Company's rate base. The auditors also recommend that the Company be strongly reprimanded for its failure to inform the Commission that the BSS add-back included its unprofitable, obsolete, nonregulated business CPE line of business and for increasing the rate base add-back by relieving BSS of its liabilities to other affiliates.

Criteria

Georgia telecommunications companies may not use current revenues earned or expenses incurred in conjunction with services subject to regulation to subsidize services which are not regulated or tariffed.[46] One of the objectives of this audit was to determine if the Company's regulated customers are protected for

[46]O.C.G.A. Section 46-2-23(g).

cross-subsidy relating to the Company's nonregulated affiliates. The Commission has defined cross-subsidy as any action undertaken by SBT which results in an understatement of intrastate regulated revenues or an overstatement of intrastate regulated expenses or investment for SBT.[47]

The objective of this audit activity was to determine if BSS's equity, which was included in Georgia's rate base calculations, included Customer Premise (CPE- PBX and Key System) investment and if the return on that equity investment was being subsidized by over-charging for the equipment being sold to the telephone companies for regulated services.

Condition

BellSouth Services, Inc. ("BSS") was established as a nonregulated subsidiary to perform centralized purchasing functions and in turn sell supplies and equipment to the BellSouth companies. BSS was owned equally (50-50) by Southern Bell ("SB") and South Central Bell ("SCB"), i.e. BellSouth's two regulated entities. A majority of BSS's sales were to SB and SCB.

In the Rule NISI case (Docket No. 3905-U) SB proposed to treat BSS's net income and equity as ratemaking adjustments.[48] In other

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[47]Docket No. 3987-U.

[48]This adjustment excluded a BSS subsidiary called BellSouth Products ("BSP").

words BSS was treated as if it was regulated.[49] The BSS adjustments were represented to the Commission as a method of protecting Georgia's regulated customers from excessive charges for purchases from BSS. However, the Company did not inform the Commission that it had transferred a substantial amount of obsolete business-CPE inventory into BSS and that those operations would be reflected in the add-back.

Prior to 1989, BSS's sales and operations primarily related to equipment and services typically used by SB's and SCB's regulated telephone operations. In 1989 two major CPE transfers were made to BSS.[50] One of these CPE transfers consisted of $15 million in "Residence CPE" equipment. This investment was segregated into a separate subsidiary ("BSP") of BSS. The BSP earnings, losses and equity are adjusted out of the BSS add-back in Georgia's Surveillance Report.

Of greater importance was the second CPE transfer to BSS. This transfer directly impacted the BSS rate base and net income adjustments in Georgia's Surveillance Reports. This transfer, from BellSouth Advanced Systems, Inc. ("ASI"), consisted of nonregulated business CPE. These business CPE assets and liabilities were not put into a separate subsidiary company within BSS as was done with the residential CPE. The business CPE assets and liabilities were

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[49]The auditors were informed that the BSS equity and net income was treated above-the-line in all BellSouth states.

[50]CPE was preemptively deregulated by the FCC in its 1980 Computer II decision, 77 FCC 2d 384.

combined with the existing regulated type equipment, masking the fact that nonregulated CPE investment was being included in the regulated rate base as part of the Rule NISI equity adjustment.

The business CPE inventory was apparently written-down immediately prior to being transferred into BSS and then further written-down several times due to tremendous technological advances in CPE during the audit period, and subsequent changes in customer's needs and preferences. Business CPE was an unprofitable line of business and never should have been added back to regulated operations. In the auditors' opinion, the Company cross-subsidized CPE through the BSS add-back and the internal tax subsidy described in Finding No. 3.

The business CPE transfer from ASI to BSS was comprised of the following: assets - [redacted] million, liabilities - [redacted] million, equity - $55.9 million.[51] In March and April 1989, there were two additional equity infusions to BSS totaling $50 million. These increased the equity amounts that were added to Georgia's rate base. Questions by the auditors concerning the additional $50 million did not produce any journal entries which specifically identify BSS's accounting for these equity infusions.

The Company maintains that the equity infusions were used to reduce BSS's "Advances from Affiliates". Whether the $50 million was used to reduce the $39.8 million CPE liabilities or other

[51]It is the Company's position that this $55.9 million of equity represented $32.6 million of inventory and $23.3 million of cash and cash equivalents, and therefore only CPE assets were $32.6 million. The Company maintains that the $23.3 million was utilized by all BSS operations. Figures redacted at Company request.

Advances from Affiliates, the result was a significant increase to Georgia's regulated rate base. The significance of this should be noted. BSS's advances from affiliates were directly added to the regulated rate base via Surveillance report adjustments.

In 1992, a majority of the BSS operations were reintegrated into the regulated operations of BST. At the same time, the CPE line of business was transferred to another nonregulated affiliate called BellSouth Communications Systems, Inc. ("BCS"). When the CPE assets were transferred from BSS to BCS, the transfer did not include the liabilities that originally had been transferred from ASI.

In July 1990, as a result of a FCC audit, BellSouth made a $5.6 million interstate refund for 1989 overcharges. From the documents reviewed, it appears that the FCC's staff was not aware that BSS's operations included the mixing of CPE assets with regulated type investment sales, when they agreed to the refund amount. Also the impact of CPE equipment was not considered in their evaluation of 1990 and 1991 BSS's charges and rate-of-return evaluations. Furthermore, the FCC did not allow the BSS add-back the Companies used for their intrastate regulated operations. None of the 1990 refund was funnelled to intrastate operations.

The auditors' evaluated BSS's net income earnings for the 1989 - 1991[52] period by product group (regulated and nonregulated business CPE) and the equity included in the rate base for each.

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[52]1989 to 1991 was considered to be relevant since it reflects the period that the CPE operation was included in BSS.

The combined earnings for both product groups was 18.3 percent in 1989. This was significantly greater than Georgia's allowed rate of return. The three year combined average return on equity was 13.6 percent. This 13.6 percent return on total BSS equity was a combination of a 18.0 percent return on regulated equity and a 4.3 percent return on business CPE equity.[53] The auditors have concluded that the combining of the CPE equity and net income into the regulated operations Surveillance Reports adjustments resulted in a cross-subsidy for BellSouth's CPE operations (Appendix G).

Even without considering the $50 million equity infusion, the combined amount of CPE equity, included in Georgia's Intrastate Rate Base for the 1989, 1990 and 1991 Surveillance Reports was $19.152 million.

Effect

The auditors have concluded that the combining of the CPE equity and net income into the regulated Surveillance Report's adjustments resulted in a cross-subsidy of BellSouth's CPE operations. The "form" was that the regulated ratepayers would be protected from the actions of the nonregulated companies, when in reality the "substance" is that they were actually harmed.

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[53]The Company was asked to provide calculations such as these but declined. It maintains that "Any calculation by the auditors that purports to show that BSS earned a different return on its investment in CPE as opposed to the other services it provided is simply incorrect." The auditors disagree, but have supplied their calculation to the Company for any corrections. None have been provided.

Cause

Regulated and nonregulated investments were commingled at BSS and included as a BSS's equity and net income (less BSP) Surveillance Report adjustments. These adjustments were proposed by the Company and represented as a method of protecting Georgia customers from paying too much for BellSouth affiliate purchases. In reality, the inclusion of the unprofitable CPE operations in BSS masked significant overcharges for equipment purchases that were charged to regulated ratepayers and included in the current regulated rate base as telephone plant in service. This overcharging resulted in cross-subsidy for the BSS CPE operations. When the Company proposed including BSS's equity and net income as Surveillance Report adjustments, it failed to mention to the Georgia Commission that the adjustments included millions of dollars of obsolete nonregulated CPE investment.

Recommendation

The auditors recommend a permanent $19.152 million Surveillance Report rate base reduction to eliminate the effect of the overpriced products included therein. The auditors also recommend that the Company be strongly reprimanded for its failure to inform the Commission that the BSS add-back proposed by the Company included unprofitable, obsolete, nonregulated business CPE and also for increasing the rate base add-back by relieving BSS of its liabilities to other affiliates.

13. The calculation and booking process used to record transfers of equipment between regulated companies should be mechanized to prevent errors.

Summary

The objective of the audit review of this function was to verify that assets (predominately central office Plug-In equipment) are being properly accounted for in transfers between state jurisdictions. The audit verified that Southern Bell's investment accounting process for the equipment transfers and inventory controls are proper and that the depreciation reserve calculation process which is used by the Company follows the affiliated transaction rules. The only negative item noted during the evaluation was that the net book salvage calculation process used by the Company is a manual operation, utilizing interstate reserve factors which may be as much as 18 months old. The manual process is labor intensive and could potentially result in errors, even though none were detected in the data reviewed. The auditors recommend that the calculation and booking process be mechanized to reduce manual effort and time delays. Southern Bell indicates that the calculation and booking process is tentatively scheduled to be mechanized by February 1995. Since the Company has plans for a system which will address the audit's concerns, no further action is required in this area.

Criteria

The audit determined that junking, scrap, salvage sales and

transfers are tracked individually within the warehouse and accounted for using a shipping invoice procedure. The audit verified that appropriate forms are being produced within the warehouse locations, so that the individual units of equipment and the associated investment can be tracked. Once the net book values are calculated, the salvage entries are then mechanically processed from that data so that appropriate salvage credits are received by each state for transfers. One objective of this review was to verify that the assets (predominately central office Plug-In equipment) being accounted for in transfers between regulated state jurisdictions is transferred (sold) at its net book value, per the FCC Part 32 rules for affiliate transactions. The data analyzed in the audit indicates that Southern Bell is correctly following the rules governing the transfer of regulated assets from one jurisdiction to another by using a manual process to calculate the net book values and resulting investment transfer amounts.

Condition/Effect

A review of the mechanized entries from the PICS/DCPR system indicates that as units are transferred from one jurisdiction to another, a retirement is processed in the state from which it is being transferred. A salvage entry is also processed, which is based on a calculated net book value using depreciation reserve tables that are provided by the Company's depreciation organization. These reserve tables are produced in about July using the previous end-of-year data. At times, therefore, the

reserve calculation for the transfer may be using a reserve distribution that existed one and one-half years before. It was also noted that the reserve ratio table used to calculate the net book for transfer is on an interstate reserve basis, rather than on an intrastate depreciation reserve basis.

Recommendation

No errors were noted in the data reviewed, but the auditors recommend that the process for calculating the depreciation reserve and net book values be mechanized to prevent errors, reduce labor expense and expedite journal processing. Since the Company indicates that such a mechanized system is scheduled to be implemented by February 1995, no further action is required in this area.

14. Recent legislative and regulatory initiatives increase the urgency of eliminating subsidies found in this audit.

Summary

In its 1994 session the Georgia State Legislature considered, but did not adopt, legislation (Senate Bill 566) which would have significantly changed the regulatory framework for Southern Bell.[54] The legislation would have eliminated monitoring or regulation of Southern Bell's rate base and rate of return. In lieu of such regulation, the rates for all services would be deemed just and reasonable at the date the Company files its notice of intent to adopt alternative regulation. S.B. 566 would have provided the Company the unrestricted ability to set the prices for its enhanced, competitive and new services. At the same time it would be assured of indexed price increases from its monopoly POTS service. There would be no further surveillance reporting or any other type of earnings scrutiny.[55]

If there is an imminent likelihood that the existing rates will be deemed just and reasonable, then the Commission must accelerate its efforts to ensure that there are no unreasonable subsidies embedded in these rates. This finding notes the consequent urgency to implement action to resolve the issues raised

[54]In June 1994 the Company filed a similar proposal entitled Georgians FIRST, with the Commission. Georgians FIRST apparently contains certain slight modifications to Senate Bill 566. The auditors will focus on Senate Bill 566 for the purposes of this finding since it was the first effort.

[55]S.B. 566, section 46-5-165(c).

in numerous other findings regarding cross-subsidies and cost shifts.

Criteria

Telecommunications companies in Georgia may not use current revenues earned or expenses incurred in conjunction with services subject to regulation to subsidize services which are not regulated or tariffed.[56] One of the objectives of this audit was to learn whether Southern Bell's customers are protected from cross-subsidy. The Commission has defined cross-subsidy as any action undertaken by SBT which results in an understatement of intrastate regulated revenues or an overstatement of intrastate regulated expenses or investment for SBT.[57]

Condition

In early 1994 SB proposed and lobbied for legislation titled "The Telecommunications Competition, Consumer Protection, and Economic Development Act of 1994" (S.B. 566). Although the legislation was ultimately withdrawn, it reflects the Company's goals and intentions. S.B. 566 would have accepted all existing service rates as just and reasonable. Services would have been divided into three categories: basic local exchange service, interconnection or access services, and "all other" services.

"Basic local exchange service is the flat rated, voice service

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[56]O.C.G.A. Section 46-2-23(g).

[57]Docket No. 3987-U.

within a local calling area (plain old telephone service -- "POTS") provided to residents and single line [businesses]."[58] Prices for basic local exchange service would be capped at their current level for three years and then allowed to increase by the cumulative change in inflation. Increases within the inflation limit would not be reviewable by the Commission. Government mandated changes such as separations changes would be automatically flowed into basic local exchange service rates.

Intrastate interconnection or access service rates would be set at a maximum defined by the interstate rate level and capped.

The prices for "all other services" would be set by the Company. Although there was a provision to require toll service rates to include the incremental cost of toll plus the foregone contribution from access, toll rates could have been set at even lower prices.

S.B. 566 would have eliminated rate base rate of return regulation and removed the Company's depreciation rates from the jurisdiction of the Commission.

The Company stressed to the auditors that S.B 566 was not a "deregulation bill" rather it was a "price regulation proposal".

The following quotations are taken directly from S.B. 566:

> "Deregulate" means to remove a service from the jurisdiction of and oversight or regulation by the Georgia Public Service Commission or the provisions of this article. [46-5-162(5)].

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[58]Summary of "The Telecommunications Competition, Consumer Protection, and Economic Development Act of 1994", SB, February 4, 1994, p. 4.

"New service" means a function, feature, capability or combination of such which has not previously been offered. [46-5-162(13)].

The earnings of the telecommunications company eliciting alternative regulation under this article shall not be subject to rate of return or rate base monitoring or regulation. [46-5-165(c)].

Any telecommunications company electing alternative regulation under this article shall not be required to seek regulatory approval of its depreciation rates or schedules. [46-5-165(d)].

The telecommunications company electing alternative regulation under this article may determine its rates, terms, and conditions for telecommunications services not defined as basic local exchange services and interconnection services. Such services may be provided by the telecommunications company through tariff, contract, or commercially reasonable means. The rates, terms, and conditions may include flexible pricing options, including but not limited to deaveraged variable rates and volume discounts. [46-5-169].

Any service not regulated by the commission as of the date of the filing of the notice of the intent to elect the alternative regulation described in this article shall continue to be unregulated and not subject to the jurisdiction of the commission. [46-5-170(a)].

A telecommunications company may, at any time, request that the provision of services other than basic local exchange services be deregulated. The commission shall order deregulation upon a showing that functionally equivalent or substitute services are available at competitive rates, terms, and conditions. [46-5-170(b)].

The telecommunications company electing alternative regulation under this article may request that any form of regulation of basic local exchange services be terminated and that such services be provided on a deregulated basis. The commission shall order such deregulation in any geographic area where 30 percent of the residential households or single-line businesses have a functionally equivalent or substitute service available at competitive rates, terms, and conditions for basic local exchange services. [46-5-170(c)].

Senate Bill 566 was not enacted, but on June 22, 1994, Southern Bell filed its "Georgians FIRST" proposal with the Commission to succeed the incentive plan approved by the Commission three years earlier on Docket 3905-U and due to expire on June 30, 1994. That plan resembles S.B. 566 in most respects except that the freeze on basic services would last for five years, and there is no cap on interconnection service rates. It contains the identical provision that on the effective date of the plan, all existing rates, terms and conditions for the services in Southern Bell's existing tariffs and contracts would be deemed just and reasonable.

Effect

During the course of the audit the auditors noted several specifically identifiable and assignable costs associated with existing services (e.g. ESSX, ONA, ISDN, etc.) which are currently regulated but would have been placed in the "all other services" category under S.B. 566. The auditors also noted costs associated with new and future services (e.g., Video-On-Demand and other broadband services) that were charged to regulated operations. Although these costs were properly treated as regulated under the terms of the Company's existing CAM, under S.B. 566 they would either be nonregulated or directly assignable to the "all other services" category whose prices would be set solely by the

company.[59]

This finding is significant. Under the terms of S.B. 566, the Company would have the unrestricted ability to set the prices for its enhanced, competitive, and new services. At the same time it would be assured of indexed price increases from its monopoly POTS service. Under S.B. 566, all existing rates would be deemed just and reasonable upon the date the Company files its notice of intent to adopt alternative regulation. There would be no further surveillance reporting or any other type of earnings scrutiny.[60]

Cause

An embedded base of captive customers for a service which has become a basic necessity, combined with the service and revenue potential produced by advanced technology and potential competition for existing and future services, provides an incentive to absorb the costs related to competitive and future services with revenues derived from captive customers.

Recommendation

S.B. 566 demonstrates the Company's desire to change the existing regulatory environment to a more permissive environment. The auditors recommend that the Commission accelerate its

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[59]S.B. 566, sections 46-5-169 and 46-5-170(a). On August 14, 1992 the FCC released Order FCC 92-327 in CC Docket No. 87-266 which authorizes telephone company provision of Video Dialtone as an interstate service (para. 72). It would appear, therefore, that Video Dialtone costs should be assigned to interstate.

[60]S.B. 566, section 46-5-165(c).

examination of the other findings of this audit and treat their resolution with considerable urgency. Otherwise, the opportunity to eliminate subsidies now embedded in the Company's rates may be lost owing to changes in the framework under which the Commission regulates Southern Bell.

15. The Company's regulated vs. nonregulated cost allocation process should be subjected to continued and increased audit scrutiny.

Summary

A review of the cost allocation assignment process for the audit period 1988 through 1991 verified that the costs associated with the nonregulated CDAR and Public Telephone Voice Message ("PTVM") Services in Georgia were assigned to the nonregulated service category, while the nonregulated revenue was assigned to regulated services.[61] Southern Bell - Georgia's customers were not harmed by the cost and revenue assignment process for these services, but to a limited extent actually benefitted from the assignment of some minor nonregulated revenue to regulated operations. No additional action is required at this time for these services. However, continued and increased audit scrutiny of the regulated vs. nonregulated cost allocation process will become much more critical as the Company's nonregulated operations increase. As the number of nonregulated services increase there are greater possibilities of revenue to cost mismatches and there is a greater need to insure that the costs of the remaining regulated services are accurate based upon usage or whatever other measurement tools are used.

[61]PTVM was never offered in Georgia but a small amount of overheads was mechanically assigned to nonregulated for PTVM prior to October, 1993. This provided a small benefit to regulated operations.

Criteria/Condition

The objective of this audit activity was to verify that the costs associated with the provision of non-regulated services are being assigned to the nonregulated segment of the business. To accomplish this verification, the cost and revenue data information contained on the Company's NONREG Product Income Statement (Report 1648) was evaluated by product and compared with the assignment in the CAM data for Georgia which assigns expenses, revenue and investment by cost pools.

Effect

A review of the cost allocation assignment process verified that the cost associated with nonregulated services were being assigned to the nonregulated category, while the nonregulated revenue was being assigned to regulated services. The effect of the cost and revenue assignment process for these services is that Southern Bell of Georgia's customers are not being harmed, but to a minor extent actually benefit from the assignment of some minor nonregulated revenue to regulated operations.

Cause

The Company representatives interviewed indicated that the revenue associated with CDAR for the audit period was at such a low level that the benefits to the Company did not justify the additional cost required to separate the revenue into the nonregulated category.

Recommendation

No additional action is required at this time for these services. Continued and increased audit scrutiny of the Company's regulated vs. nonregulated cost allocation process is warranted, however, as nonregulated operations and services increase.

16. The auditors recommend the use of positive time reporting for BellSouth's and Southern Bell's legal departments.

Summary

The objective of this audit activity was to verify that BellSouth's and Southern Bell's Legal Department expenses are being properly assigned to regulated and nonregulated services. The auditors determined that no internal or external audit was performed for any Legal Department employee during the audit period. The availability of such an audit may have resolved some of the uncertainty in verifying past work activities of the Legal Departments.

The allocation of Legal Department employee time and related expense is based on exception time reporting and the pre-assignment of job function codes ("JFCs"). These procedures result in an inability to verify the propriety of the allocation of Legal Department costs.

The inability to verify conclusively whether there has been a correct allocation of Legal Department employee time to nonregulated activities was demonstrated by the auditors' review of the 1991 time allocation of two of the Company's attorneys. One of the attorney's formal filing activity related almost exclusively to nonregulated services such as Cellular, Personal Communication Services and Radio Experimental Applications, yet only 12 percent of his time was assigned to the nonregulated cost category. The auditors acknowledge that this attorney could have worked on other functions, but with exception time reporting there is no record of

those activities.

After the fact, it is virtually impossible to verify if the personnel in the legal department have accurately reported their time relating to nonregulated activities, because, unless exception time has been reported, the Company does not have any detailed records of what functions were being performed at any given time.

The auditors recommend that BellSouth's and Southern Bell's Legal Departments be required to change to positive time reporting. The auditors also recommend that the cost pools to which Legal Department time is assignable include nonregulated, interstate and intrastate by state jurisdiction, or seek modification of the Part 69 rules.

Criteria

One of the objectives of this audit was to learn whether Southern Bell's regulated customers are protected from cross-subsidy. The Georgia PSC has defined cross-subsidy as any action undertaken by SBT which results in an understatement of intrastate regulated revenues or an overstatement of intrastate regulated expenses or investment for SBT.

Condition

Below is a listing of the sources of the $4,458,694 legal expense (Account 6725) reported on Georgia's 43-03, 1991 ARMIS Report:

| | | |
|---|---|---|
| Georgia Legal Dept. | $ 1,284,027 | 28.8% |
| Southern Bell Legal | 1,587,591 | 35.6% |
| BellSouth Headquarters | 1,587,006 | 35.6% |
| | $ 4,458,694 | 100.0% |

A review of the formal Docket information provided by the Company was conducted and compared to the eventual assignment of BellSouth Headquarters' legal expense. A major portion of the activities reviewed involved FCC filings and dockets which do not relate to the provision of intrastate customer service. BellSouth's legal expense is first allocated to Southern Bell and then apportioned to Georgia operations.

The allocation of BellSouth and Southern Bell Legal Department employee time and related expense is based on exception time reporting and the pre-assignment of job function codes. During the audit period, the Legal Department had 22 six digit JFCs, ten of which were assigned to nonregulated activities. The JFC Mini File directs the predominance of cost assignment and the use of exception reporting generally applies only to special activities. A work function profile is established for each individual and only when the individual reports exception time is a record produced indicating specific work activities. If no exception time is reported, then the individual's time is allocated based on the preassigned profile.

The auditors requested copies of all external and internal audits which included the Legal Department, so that the results could be analyzed. Initially the Company provided a copy of an November 15, 1991 audit report for the Part 64 - Job Function Code

audit prepared by the internal auditors. Investigation revealed that no personnel in the Legal Department were actually evaluated. The Company's responses to numerous other audit data requests indicate that the Company's internal auditors have not conducted a formal audit of the Southern Bell's Legal Departments since at least 1988. The Company indicates that its internal review procedures for evaluating JFC assignments is the direct responsibility of it's "segment accounting coordinators" who do not issue any formal reports summarizing their findings.

The assignment of an employee's JFCs generally takes place only when an employee changes jobs or when there is a general reorganization. The Company's response to data request JWC-58 (Supplement) indicates that a questionnaire is sent quarterly to a random sample of employees, but the data responses indicate that the Legal Departments have not received such a questionnaire. The Company's responses to JWC-46, JWC-57 & JWC-58 indicate that no formal report summarizing the results of these surveys has been issued.

The auditors had several meetings with Company personnel seeking alternative sources for information which could be verified for the audit period. These meetings identified the JFC Quality Task Force which had been recently established as a possible source for auditible information relating to the Legal Department. The Company's subsequent response to data requests indicated that the Task Force's first review of the Legal Department occurred on June 15, 1992. The Company response to the auditors' information

request stated that a formal report was not issued by the task force and that "The JFC Quality Task Force Team was formed primarily to reduce the number of JFCs and to simplify the associated assignment and administrative process." The Company also stated that the material associated with the Task Force's work effort is "clearly outside the 1988 - 1991 audit period" but that the simplification process reduced the number of job function codes by 45 percent.

The Company's responses to the auditors' data requests and interviews relating to the Legal Department's reported time, indicates that there is no documentation for the audit period which would provide verification that the actual time reported corresponds to the exception time reporting rules. The departmental budget process tracks expenses by general functions (e.g. training, personnel, travel expenses, relocation expenses), but it does not attempt to track expenses by services or activity for potential regulatory assignment.

For example, if an employee's Mini File indicates 12 percent of his time is assigned to nonregulated function codes, then that is the time that would be assigned unless the employee maintained separate personal records of what his actual assignments were. These personal records would need to identify each assignment, whether the assignment was regulated or nonregulated, the hours spent, and the cumulative nonregulated hours versus total hours. With this type of personal record, the employee might be able to estimate the portion of his time that is exception time. However

it is unlikely that anyone would maintain such records unless they were required to do so.

The Legal Department's work functions are not repetitive in nature, as are those of the Company's plant departments. If the work functions were repetitive and consistent, a survey could provide a verifiable indication as to whether the department's time is being properly assigned. But this is not the case where an individual may work on one activity one day and never address the issue again.

In response to data requests, the Company provided the auditors with a list of 1991 Company formal legal filings. The list identified which of its attorneys was responsible for each filing. The Company also provided information relating to each of those attorneys' time allocation between regulated and nonregulated cost pools. The auditors selected information on attorneys Helen Shockey and R. Frost Branon for evaluation. Ms. Shockey and Mr. Branon were BellSouth attorneys.

The data provided by the Company indicated that 100 percent of Ms. Shockey's but only 88 percent of Mr. Branon's 1991 time was assigned to regulated activities. The auditors' review of the filings list indicates that all of Ms. Shockey's activities seem to pertain to regulated activities. Therefore, the 100 percent assignment of her time appears to be correct. The auditors' review of Mr. Branon's time and filing data does not result in the same conclusion. Below is a complete list of filings for which Mr. Branon was responsible:

| FILING DATE | DOCKET # | DOCKET DESCRIPTION/SUBJECT |
|---|---|---|
| 1-15-91 | 90-314 | Personal Communications Services |
| 3-11-91 | RM-7618 | PCS - Data (Apple Corp. PFRM Comments) |
| 4-12-91 | 89-554 | ITU WARC Frequency Allocations |
| 5-20-91 | 91-33 | Cellular Resale Policies |
| 5-20-91 | 91-34 | Cellular Bundling |
| 7-24-91 | 90-314 | Personal Communication Services Field Trials Results |
| 8-15-91 | | Radio Experimental Application |

The Company's explanation of Mr. Branon's charges to regulation indicates that since the PCS FCC Docket was in the early stages of inquiry and development, and it was uncertain whether it would be considered a regulated or nonregulated business, it was appropriate to charge PCS cost to regulation. The Company also indicated that since the original FCC Cellular ruling was built around a telco bundling decision it was necessary to review and compare the bundling applications to determine if such a decision applied to Cellular. Therefore, once again the cost was assigned to the regulatory cost pool, rather than nonregulated services.

The Company explained that in 1991, BellSouth followed and/or intervened in twenty-seven cases arising from proceedings at the FCC and from the MFJ, and that nearly two-thirds of these cases were related to telephone company matters. Mr. Branon was apparently responsible for BellSouth's efforts in those cases as well as the cases he handled in the regulatory area. In other words, at least one third of the other cases did not relate to telephone company matters and the other two-thirds did not relate to regulatory matters. Nevertheless, only 12 percent of Mr.

Branon's time was charged to nonregulated. Conversely, 88 percent of Mr. Branon's time was charged to regulated, even though a majority of his work appears to have related to nonregulated matters.

The problem is that with exception time reporting, it is virtually impossible to verify after the fact whether the personnel in Southern Bell's legal department have accurately reported their exception time relating to nonregulated activities. Unless exception time has been reported, the Company does not have detailed records of what functions were being performed at any given time.

The problem for Georgia and Southern Bell is not simply the assignment of cost between regulated and nonregulated activities. There is a more critical issue involving BellSouth Headquarters' Legal Department. BellSouth Headquarters' Legal Department is involved in the establishment and operation of numerous nonregulated companies and other nonregulated business activities. In general, the assignment of its legal expense is based on a fully distributed cost concept for allocation. Under this process, BellSouth's legal cost is allocated to its subsidiaries based on either their legal expenses or type of work performed. Since the telephone operations have more attorneys than any of the other BellSouth enterprise companies, a majority of the legal expense is allocated to telephone operations where the general allocator is used.

The allocated expense is further reallocated to each state

jurisdiction by Southern Bell and South Central Bell. Ultimately after all of the allocations have been completed, the majority of the expense is assigned to intrastate regulation. The use of general allocators for cost assignment invariably results in a major portion of the legal expense being assigned to intrastate, when in fact the activities which caused the expense to occur are primarily either nonregulated services or interstate filings and has little or nothing to do with intrastate regulation or services. Therefore, the cost allocation problems associated with legal expense stem not only from the use of exception time reporting, but also from a lack of cost pools sufficient to assure that costs are driven to the appropriate categories.

Effect

Inability to determine if Legal Department time is appropriately charged.

Cause

Exception time reporting.

Recommendation

The auditors recommend that the Company eliminate the use of exception time reporting and require positive time reporting for all employees in the BellSouth and Southern Bell Legal Departments. This will assure that each individual is held more directly accountable for how his or her time is charged, as the individual's

time report would require their signature. Positive time reporting may reduce any predisposition of the Company to automatically charge regulated services for its legal costs. The need for this change will become more critical as the Company moves into additional nonregulated areas of service.

17. Chaining calculations relating to affiliated transactions should recognize operations, such as BAPCO, which are treated as regulated at the intrastate level.

Summary

BellSouth Enterprises, Inc. ("BSE") leased space in a building located at 1100 Peachtree Street from Sunlink (an affiliate) at a price per square foot which is significantly greater ($393,349 annually) than the amount being paid by other non-affiliated tenants in the building.[62] A portion of this excess flowed directly into regulated operations. A greater portion flowed indirectly into Georgia's regulated intrastate operations since BAPCO's net income is treated as regulated for Surveillance Report purposes.[63]

Southern Bell should be required to calculate all affiliate costs "chaining" into intrastate regulation, and not restrict its chaining calculation to the FCC's interstate definition of what is regulated and nonregulated. This calculation should recognize that BAPCO is treated as a regulated entity. The auditors also recommend that the Commission continue to impose strict monitoring of all affiliated leases in which any portion of the lease cost is included in intrastate revenue requirements, expenses or earnings.

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[62]$393,349 annually on a going-forward basis.

[63]The annual amount flowing to Georgia is estimated to be approximately $12,000. No adjustment is proposed for this minor amount.

Criteria

The auditors analyzed the lease information contained in the Coopers & Lybrand's ("C&L") 1991 Part 64 audit workpapers as well as the Company's affiliate billings to evaluate the impact on Southern Bell's net income adjustments. BSE's intercompany billing practices were analyzed to determine if BSE's 2.1 percent management fee billing method protects the regulated customers from the excessive rent paid by BSE for the 1100 Peachtree property. Since the accounting structures of BSE's foreign and start-up companies are not comparable to those of BSE's established U.S. companies, a review of C&L's Part 64 evaluation was conducted to determine the potential impact of the excessive lease's cost on Georgia's BAPCO net income adjustment.

Condition

BSE's lease for 1100 Peachtree is a "market priced" lease. The data included in the C&L's 1991 Part 64 audit workpapers (Binder 37) relating to the lease indicates that BSE's lease payments are $636,469 per year greater than a comparable Kilpatrick & Cody lease in the same building. The Company has subsequently furnished the auditors with information which indicates that the 1991 lease data included in C&L's workpapers was not complete, and that lease concessions were made to BSE in 1992 and 1993, that reduced the excessive amount per year from $636,469 to $393,349. Since these concessions took place outside the specified (1988 - 1991) audit period, the revised lease documents or C&L's 1992 and 1993 work

papers have not been reviewed by the auditors.

As part of its 1991 Part 64 Attestation audit, C&L performed a chaining evaluation which determined that 2.4 percent of the excess lease expense would flow to regulation. However, since C&L's chaining calculation was based on the FCC's definition of regulated and nonregulated, it did not recognize that more that 2.4 percent would flow into Georgia's regulated operations due to its treatment of BAPCO's net income.

Effect

BSE incurred an excessive lease payment. The annual amount of the excessive lease payment to Sunlink was $393,349. This payment is not significant from an interstate perspective, because all of BSE's Companies were nonregulated from the FCC's perspective, with only a small portion of those costs chaining into interstate regulated operations. A greater portion of the excess flowed into the regulated operations in Georgia since BAPCO is treated as regulated in Georgia.

Cause

C&L's chaining impact evaluation was based on the FCC's definition of regulated and nonregulated companies. This evaluation did not recognize that BAPCO is treated as a regulated company in Georgia.

Recommendation

The auditors recommend that for intrastate reporting purposes, Southern Bell should be required to calculate all affiliate BellSouth Corporation costs "chaining" into intrastate regulation as defined by Georgia's Surveillance Report, and not just the FCC's definition of what is regulated and nonregulated. The auditors also recommend that the Commission reaffirm its need to have access to the BellSouth's nonregulated affiliates' books and records to ensure that any costs flowing into regulation are not excessive or that a cross-subsidy is not taking place.

18. Sunlink's Corporate cost allocation process provides an opportunity for the regulated telephone operations to subsidize BellSouth's nonregulated commercial ventures. If Southern Bell is unwilling to calculate the portion of Sunlink's lease price increases which flow into regulation, the total amount of the leases should be disallowed.

Summary

Sunlink, Inc. is a nonregulated affiliate which owns real estate and leases it to its customers which include regulated affiliates. Southern and South Central Bell lease, from Sunlink, warehouses located in Birmingham, AL, Jacksonville, FL and St. Augustine, FL. The warehouses are used for regulated operations. During the 1987-88 time period, the auditors noted that there were significant increases in the lease prices per square foot at the Birmingham and Jacksonville locations.

If there is no viable market for a service or product provided by a nonregulated affiliate, Part 64 rules require prices to be based on the calculated fully distributed cost ("FDC"). The lease prices for the warehouses are based on FDC. Overhead operating cost assignments and expense allocations within Sunlink, to a specific FDC lease location, are not "arms length" transactions. These allocations can be controlled by Sunlink, whose books and records are excluded from regulatory review. Therefore, even the application of FDC pricing for some buildings provides an opportunity to cross-subsidize the nonregulated commercial activities of BellSouth's leasing company.

Because of the unwillingness of the Company to provide specific details on Sunlink's cost allocation process, or

sufficient data to justify the increases in warehouse lease prices, the auditors recommend that the cumulative increased lease amounts be disallowed as charges to regulated operations.

Criteria

Telephone companies in Georgia may not use current revenues earned or expenses incurred in conjunction with services subject to regulation to subsidize services which are not regulated or tariffed.[64] One of the objectives of this audit was to determine whether the regulated telephone operations are protected from any cross-subsidy to BellSouth's nonregulated affiliates through the cost allocation process.

Condition

The Coopers & Lybrand's ("C&L") 1991 Part 64 audit workpapers provided the auditors with information that within the 1987-1988 time period there was a significant increase in the lease price per sq. foot at warehouse locations leased from Sunlink. The 1991 Part 64 audit workpapers contained a simple series of numbers and totals comparing a present worth calculation of the lease price by year to an FDC amount. The notes in the workpapers indicate that the lease price present worth amount for Jacksonville was slightly higher than the FDC, while for other locations the present worth amounts were less than FDC. The C&L representative present during the initial review of the C&L workpapers indicated that the increase in

[64]O.C.G.A Section 46-2-23(g).

lease price per square foot resulted from changes in Sunlink's mechanized cost allocation system. Several months later, Southern Bell's response to the auditors's data request stated that the year over year lease price per sq. foot increase was because of additions to the warehouse buildings and parking lots. The new lease prices for the properties indicates that the change in lease prices applied not only to new additions, but to areas that had been previously leased. The auditors requested information pertaining to the allocation of FDC for the leases and data on the allocation process used to assign cost within Sunlink. Details relating to Sunlink's mechanized cost allocation system were not made available to the auditors. Neither Company nor C&L representatives provided any specific details relating to the basis for the fully distributed cost amount used in the new leases or any information relating to the allocation of cost within Sunlink.

The Company now contends that sufficient information is available in C&L's files to verify that lease prices are equal to or less than FDC cost. Without specific data on Sunlink's cost allocation process, it is impossible to independently determine whether the cost allocation to each location is appropriate. Although the data may be in C&L's files it was not included in the 1991 Part 69 audit workpapers, nor has any C&L representative referenced the existence of such records during numerous interviews on this subject.

Effect

Without access to sufficiently detailed information, relating to the cost allocation within Sunlink there is no way to determine if BellSouth is using its regulated telephone operations to provide a subsidy to its nonregulated commercial leasing operations. Virtually all of Sunlink's corporate overhead costs could be assigned to the properties that are priced at FDC. This would provide a subsidy to BellSouth's commercial leasing operations.

Cause

The Company continues to maintain that virtually all of the cost and lease data involving Sunlink properties and its internal cost allocation process is "proprietary" even though all of the property's lease costs are assigned to regulated telephone operations.

Recommendation

Because of the unwillingness of the Company to provide specific details on Sunlink's cost allocation process, or other data which would justify the increases in warehouse lease prices, the auditors recommend that the cumulative increases to the lease amounts be disallowed. The auditors also recommend that the Commission require the Company to provide specific detailed calculations as to the amount of these increases flowing to Georgia's regulated intrastate operations. If the Company is unwilling to calculate the portion chaining into Georgia's

operations, the total amount of these leases should be disallowed as charges to regulated operations. Because the Company has refused to provide Sunlink's cost allocation information to the auditors, the Commission should require the Company to provide this information directly to the Commission.

19. Commercial space which is leased from a nonregulated affiliate for regulated operations should be evaluated to determine if the lease space is actually being utilized.

Summary

During the audit, two field trips were made to 3700 Colonnade in Birmingham, Alabama. The 3700 building is one of three buildings being leased from Sunlink (an affiliated company) at that location. During these visits, the auditors noted that a significant amount of floor space at the 3700 Colonnade location was unoccupied. The auditors recognize that there could be many reasons for this vacancy: reorganizations; reduction in work force; or simply that more space was leased than is required for the operations located in Birmingham.[65] If excessive space is being leased by a regulated company from Sunlink, then Sunlink would be receiving a subsidy from regulated operations. The auditors recommend that the Commission perform regular future audits focussed on all real estate and lease transactions which involve affiliates in any way.

Criteria

Georgia telecommunications companies may not use current revenues earned or expenses incurred in conjunction with services subject to regulation to subsidize services which are not regulated

[65]The vacancy in question was due to reorganization.

or tariffed.[66] One of the objectives of this audit was to determine if the Company's regulated customers are protected for cross-subsidy relating to the Company's nonregulated affiliates. The Commission has defined cross-subsidy as any action undertaken by SBT which results in an understatement of intrastate regulated revenues or an overstatement of intrastate regulated expenses or investment for SBT.[67]

Condition

The lease price for these three buildings at the Colonnade location is based on a fully distributed cost ("FDC") methodology. The costs of these leases flow directly into the regulated operations. It was noted that significant amounts of floor space at the 3700 Colonnade location was unoccupied, but this observation spanned a limited time when BellSouth was involved in massive reorganization.

Effect

Regulated operations may be paying BellSouth's nonregulated operations for floor space which is not required. Most companies with unused lease space attempt to sub-lease the space in an effort to reduce their cost of operations. In this case, there is a reduced incentive to take such action since the expense incurred by the regulated operations is passed on through to ratepayers. If

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[66]O.C.G.A Section 46-2-23(g).

[67]Docket No. 3987-U.

the regulated operations attempted to sub-lease or renegotiate the leases, then Sunlink's business would be impacted. The leasing of excessive space by the regulated operations could be significantly underwriting Sunlink's operating cost.

Cause

There could be many reasons for this condition: reorganizations; reduction in work force; or simply more space was leased than is required for the operations located in Birmingham. The auditors understand that the vacant space at Colonnade resulted from a reorganization.

Recommendation

The auditors recommend that the Commission perform regular future audits focused on all real estate and lease transactions which involve affiliates in any way.

20. Commission should perform regular future audits focussed on real estate and lease transactions which involve affiliates in any way. An intrastate adjustment of $321,609 should be made to the Surveillance Report to compensate regulated customers for excessive Chastain Center lease expenses.

Summary

In March 1989 Southern Bell ("SB") moved its Engineering, Business and Forecast operations from Whitlock to the Chastain Center, which was owned by Sunlink (a nonregulated affiliate). In March 1990, SB also moved its Outside Plant Control Center ("OPCC") operations from Whitlock to the Chastain Center. These moves and the resulting affiliate leases were negotiated by BellSouth Services, a subsidiary of Southern Bell. The lease at Whitlock did not expire until October 1991 and was renewable at a lower price than the Chastain Center lease price. The Whitlock lease price was $5.11 per sq. ft., while the Chastain Center lease price was $7.00 for the first two years, with an escalator provision which would increase the square foot lease price to $16.50 over a 15 year period. In addition to the higher lease price at Chastain Center, Southern Bell also incurred a $400,000 penalty because it relocated from Whitlock before the end of its existing lease.

BellSouth's corporate structure tends to create a predisposition by telephone company managers in favor of nonregulated affiliates' profits and against general trade competition. In this case, leasing from Sunlink rather than the existing nonaffiliated landlord produced additional profits to the vertically integrated entity.

The combination of vertical integration and rate of return regulation also tends to generate decisions by operating companies to enter into transactions with nonregulated affiliates that may not be economically justified. The decision in question resulted in a higher cost than would have resulted had the Company maintained its operations at Whitlock and used excess Southern Bell owned space wherever possible. BellSouth's profits were maximized since, even under modified rate of return regulation, Southern Bell's operations tend to remove the negative impact of uneconomical additional expense. The extra cost is simply absorbed as a regulated expense, allowing extra profits to flow up to the corporate parent rather than to non-BellSouth companies or regulated telephone customers.

The auditors recommend that the Commission strongly discourage leases by regulated operations from a nonregulated affiliate company, unless it can be clearly demonstrated that such leases result in reduced cost to the regulated utility and are not anticompetitive in nature. The Commission should perform regular future audits focussed on real estate and lease transactions which involve affiliates in any way. The auditors also recommend that there be a positive adjustment of $428,812 ($321,609 intrastate) to the Company's net income as reported on Southern Bell's Surveillance Report. This adjustment would compensate regulated customers for the excessive expense being assigned to regulation.

Criteria

The auditors analyzed the economic evaluation used by the Company to support the initial decision to relocate operations from Whitlock to the Chastain Center. The Chastain Center leases and current intercompany billing were also analyzed. This analysis focused on whether BellSouth used its corporate structure to benefit its nonregulated companies at the expense of its regulated customers. The auditors' analysis also focused on whether BellSouth used its corporate structure, relating to this lease, in an anticompetitive manner.

Condition

In March 1989 Southern Bell moved its Engineering, Business and Forecast operations from Whitlock to the Chastain Center, which was owned by Sunlink (a nonregulated affiliate). In March 1990, SB also moved its Outside Plant Control Center ("OPCC") operations from Whitlock to the Chastain Center. The lease at Whitlock did not expire until October 1991 and was renewable at a lower price than the Chastain Center lease price. The Whitlock lease price was $5.11 per sq. ft., while the Chastain Center lease price was $7.00 for the first two years, with an escalator provision which would increase the square foot lease price to $16.50 over a 15 year period. In addition to the increased lease price at Chastain Center, Southern Bell also incurred a $400,000 penalty for relocating from Whitlock before the end of its existing lease.

The "initial economic analysis" used to support the Whitlock

relocation was a present worth study that contained numerous discrepancies and omissions. Some of these are as follows:

(1) The common area cost estimate for the Chastain Center was estimated to be $.65 per sq. ft. per year over the lease life. This estimate was significantly understated. For example, in 1991 the common area maintenance cost at the Chastain Center was actually $1.05 per sq. ft. This equates to $18,340 per year more than the cost used in the initial analysis. Assuming no increase from the 1991 level difference, this correction would add $107,849 to the present value assumption for the Chastain Center.

(2) The Company's initial economic analysis assumed that the OPCC, which was located at Whitlock, would relocate to another Southern Bell owned location and, therefore, it was not included in its Chastain present value comparisons. In fact, in 1990 an additional 10,779 sq. ft. of space was leased for OPCC at Chastain Center for a 7 1/2 year $380,283 present value.

(3) Part of the justification for the move from Whitlock was a forecast of additional space needs. The Executive Summary relating to the relocation indicates that there was at least 8,518 sq. ft. of Southern Bell owned space available in addition to the 46,716 sq. ft. at Whitlock.

(4) The analysis also did not include an additional 2,617 sq. ft. for a heating, ventilation and air conditioning ("HVAC") system with a 7 1/2 year $39,701 present value lease cost and a one time $195,000[68] charge to Southern Bell.

(5) In addition to the omissions from the Chastain Center analysis, there was an inclusion of $700,000 in the economic analysis for renovation of Whitlock at Southern Bell's expense, rather than the landlord's. The auditors continued to include this $700,000 in Whitlock's cost comparison, even though this item appears somewhat questionable.

Below is a comparison of the two lease alternatives, including the items which were omitted from the original Company analysis, assuming a 7 1/2 year lease period:

[68]The auditors reduced this amount to $140,000 to reflect future energy savings.

| | Whitlock | Chastain Center |
|---|---|---|
| Company's PV Cost Analysis | $2,633,199 | $2,806,461 |
| Items Not Included: | | |
| (1) Additional Common Area | | 107,849 |
| (2) OPCC Space[69] | | 0 |
| (3) HVAC Space | | 39,701 |
| (4) Early Termination of Lease | | (32,000) |
| (5) One Time Charge | | 140,000 |
| Revised PV Cost Analysis | $2,633,199 | $3,062,011 |
| Increased Present Value Cost | | $ 428,812 |
| Intrastate Present Value Cost | | $ 321,609 |

The Company cites several intangibles as justification for incurring the increased cost associated with its decision to lease facilities from a nonregulated affiliate. One intangible, which is not cited, is the disruption and expense that occurred with the relocation of the workforce from Whitlock.

Effect

The leasing of Chastain Center effectively shifted the cost of nonrevenue producing building space from a nonregulated affiliate to regulated telephone operations. The owners of Whitlock and the other potential lease locations were competitors of BellSouth's real estate leasing company during a period of a depressed real estate market. This transfer decision is an example of how regulated operations can be used by BellSouth to assure the success

[69]The Company leased OPCC space at Chastain Center at a present value cost of $380,283 rather than occupying Company owned space at zero incremental cost as proposed in the initial Whitlock relocation evaluation.

of its nonregulated companies at a significant cost to the regulated operations. It should again be noted that BellSouth had almost two years remaining on the Whitlock lease for which it paid despite its relocation of telephone operations to an nonregulated affiliate's building.

Cause

BellSouth's corporate structure tends to create a predisposition by telephone company managers in favor of nonregulated affiliates' profits and against general trade competition. In this case, leasing from Sunlink rather than the existing nonaffiliated landlord produced additional profits to the vertically integrated entity.

The combination of vertical integration and rate of return regulation also tends to generate decisions by operating companies to enter into transactions with nonregulated affiliates that may not be economically justified. The decision in question resulted in a higher cost than would have resulted had the Company maintained its operations at Whitlock and used excess Southern Bell owned space wherever possible. BellSouth's profits were maximized since, even under modified rate of return regulation, Southern Bell's operations tend to remove the negative impact of uneconomical additional expense. The extra cost is simply absorbed as a regulated expense, allowing extra profits to flow up to the corporate parent rather than to non-BellSouth companies or regulated telephone customers.

Recommendation

The auditors recommend that the Commission take action which would strongly discourage leases by regulated operations from BellSouth's nonregulated affiliate companies unless the Company can clearly demonstrate that such leases result in reduced cost to the regulated utility and are not anticompetitive in nature. On a going-forward basis, the Commission should require:

(1) Regular future audits focussed on real estate and lease transactions which involve affiliates in any way.

(2) A positive adjustment of $428,812 ($321,609 intrastate) to the Company's net income as reported on Southern Bell's Surveillance Report. This adjustment would compensate regulated customers for the excessive expense assigned to regulation.

21. The interest received by Southern Bell from advances to affiliates should be offset against book interest in the interest synchronization adjustment.

Summary

Southern Bell's accounting for advances to affiliates had a negative impact on the Georgia Surveillance Report's interest synchronization adjustment. During the audit period, Southern Bell loaned substantial amounts of capital in the form of advances to BellSouth Services and received interest on those loans. BellSouth Services' interest payment reduced its net income and consequently reduced the BSS add-back adjustment on Georgia's Surveillance Report. Southern Bell treated its interest expense and interest income (i.e. the interest received from BSS) below-the-line as non-operating revenue. If the advances had not been made to the nonregulated affiliates, Southern Bell debt could have been substantially lower. A lower debt would have impacted the interest synchronization adjustment. The interest paid on those advances (1988 - 1991) totaled $8,523,109, of which Georgia's portion was $2,510,551. The auditors recommend that an adjustment be included in the Surveillance Report's NOI of $947,382 to reflect the four year audit period impact of these advances as well as a change in the Interest Synchronization calculation to reflect the interest on future advances to affiliates.

Criteria

The audit evaluated the components of the Surveillance Report

which impact the Interest Synchronization Adjustment and investigated Southern Bell Advances to Bell South Services and Bell South Products, Inc. The accounting treatment for the interest payments was verified to determine the impact on the regulatory monitoring process.

Condition

During the audit period (1988 - 1991), Southern Bell made numerous "Advances" to BellSouth Services. The interest paid on those Advances totaled $8,523,109 with Georgia's portion being $2,510,551. The interest paid by BellSouth Services reduced its Net Income included in Georgia's Surveillance Report as an NOI BSS Adjustment. The interest received by Georgia from BSS was accounted for as a non-operating revenue and not included in its Net Operating Income, which is used for evaluating Southern Bell of Georgia's Rate of Return.

Southern Bell of Georgia's 1991 book interest expense was $82,161,201. If Southern Bell had not made any advances to BSS then its short-term debt could have been lower, along with its interest expense. Effectively, Southern Bell and South Central Bell were "middle-men" for BSS financing.

Southern Bell of Georgia includes a Pro Forma NOI Interest Synchronization Adjustment as part of its Surveillance Report. In establishing the Rules for Surveillance Reporting, the Commission mandated an allowable "Capital Structure". The established procedures include a provision which allows an NOI interest

adjustment which is the Federal and State tax impact on the difference between the allowed Capital Structure and the actual interest paid on debt by the Company. In 1991 the allowed capital structure interest was $78.1 M while the actual Company interest recorded was $82.2 M. This difference resulted in a Pro Forma adjustment which reduced the Net Operating Income that was used in the Rate of Return evaluation by $1,542,346.

Effect

Southern Bell - Georgia received a cross-subsidy. The interest synchronization adjustment resulted in an increase to Georgia's 1991 revenue requirement as a result of the very high level of book interest expense. Obviously a portion of Southern Bell - Georgia's book interest expense is attributable to funds it borrowed and in turn advanced to BSS. Consequently, the Company was able to achieve a cross-subsidy through the interest synchronization adjustment.

Cause

Southern Bell's accounting for the interest on advances was correct, but without an adjustment in the Interest Synchronization Adjustment calculation, similar to the one for customer's deposits, the resulting negative NOI adjustment is overstated.

Recommendation

The auditors recommend that the Interest Synchronization

calculation process included in the Surveillance Report be modified so that any future interest received from an affiliate will be reflected as if it is a reduction to Southern Bell's debt interest. Also, the auditors recommend a one time NOI adjustment of $947,382 to reflect the four year impact of the Affiliate advances.

22. The Company achieved a cross-subsidy relating to the Rose CXC PBX. The Commission should increase its audit scrutiny of the Company's CPE-related transactions.

Summary

A Private Branch Exchange ("PBX") was transferred from BellSouth Services ("BSS") to Southern Bell - Georgia's regulated books. Although the PBX was dedicated to the use of the BSS Corporate Communications Group, BSS did not pay Southern Bell for its use. Nor could the Company document the initial transfer from BSS to Southern Bell. This transaction resulted in a cross-subsidy from regulated operations to nonregulated operations. The auditors recommend increased audit scrutiny of all of the Company's CPE-related transactions.

Criteria

Telephone companies in Georgia may not use current revenues earned or expenses incurred in conjunction with services subject to regulation to subsidize services which are not regulated or tariffed.[70] One of the objectives of this audit was to learn whether, as a result of the relationship between the Company's regulated telephone operations and the nonregulated operations of its affiliates, Southern Bell's regulated customers are protected from cross-subsidy.

[70]O.C.G.A. Section 46-2-23(g).

Condition

The auditors selected a judgmental sample of forty-four construction estimates closed in 1991. Of these forty-four estimates, only two related to customer premises equipment on Southern Bell - Georgia's books. Estimate No. T9546 was for the retirement of the Rose CXC PBX. Although this PBX was originally purchased by Bellsouth Services ("BSS"), it was recorded on Southern Bell - Georgia's books. The Company could not explain or document the transaction in which the PBX was transferred to Southern Bell from BSS. The audit sample was too small to determine whether this was an isolated incident.

The equipment cost ($88,755) was included as Southern Bell - Georgia Office Equipment (Account 2123), which is a directly assigned regulated investment account. Although the PBX exclusively served BSS' Corporate Communications Group, there was no lease agreement or other arrangement compensating Southern Bell for the use of the PBX. In 1991, the PBX was retired because BSS desired ESSX service, for which it paid the tariffed rates.

Effect

The Company's inability to explain or provide documentation relating to the transfer of this asset from BSS to Southern Bell indicates a lack of internal control. Furthermore, at the time this took place, BSS was an nonregulated affiliate receiving service from Southern Bell at no charge. The asset was in Southern Bell's rate base, depreciation was being charged to regulated

operations, and any early retirement losses were absorbed into regulated operations.

Cause

Unknown.

Recommendation

This finding may or may not represent an isolated incident. However, it is in the CPE area in which the auditors have identified other cross-subsidies.[71] As a result of these findings, the auditors recommend increased audit scrutiny of all Company CPE-related transactions.

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[71]See Finding Nos. 3 and 12.

## 23. Accounting and information management costs should be directly assigned whenever possible.

### Summary

The auditors' review of billing by affiliates to SB in 1991 revealed three nonregulated projects which were allocated instead of directly assigned to nonregulated. One of the projects was related to accounting, and the other two were related to information management work. The latter projects could not be directly assigned because the Company has not established a direct charge cost pool for information management expense. The auditors recommend that the Company establish a "Direct Regulated/Nonregulated" cost pool for information management, and directly assign accounting and information projects whenever possible.

### Criteria

Part 64 of the FCC's rules states:

> Costs shall be directly assigned to either regulated or nonregulated activities whenever possible.[72]

In conformance with this rule, accounting and information projects should be directly assigned whenever possible.

### Condition

The auditors examined the cost pool assignment of successive

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[72]Code of Federal Regulations, Title 47, §64.901 (b)(2).

samples of projects billed to SB by affiliates through the Incoming Billing Interface Tracking System ("IBITS"). The official description of related IBITS Authority codes was reviewed and interviews were conducted as necessary to determine the appropriateness of cost pool assignments.

Although most assignments appeared to be appropriate, three projects were found that should have been directly assigned to nonregulated, but were instead allocated between regulated and nonregulated. In all three cases, the official description of the project was marked nonregulated, and the work involved was, indeed, solely related to nonregulated operations. These projects and their 1991 billing to Georgia were as follows:

ACT3111 - Invoicing, Voucher Preparation for CPE ($14,035)

ACT2079 - Enhanced Voice ($3,955)

ACT2405 - Billing of Unregulated Pulselink ($884)

Effect

Because these projects were allocated, instead of directly assigned, most of the costs charged to them were assigned to regulated.

Cause

The first project (ACT3111) involved the invoicing and voucher preparation for non-stock service order related purchases of customer premises equipment ("CPE"). This project was properly classified to Accounting and Finance expense (Account 6721), but

not to the "Direct Regulated/Nonregulated" cost pool. The reason this project was allocated instead of directly assigned to nonregulated could not be specifically determined. The fact that most accounting work relates to both regulated and nonregulated services may have been a factor, although for this project direct assignment was clearly appropriate.

The other two projects (ACT2079 and ACT2405) were properly charged to information management expense (Account 6724). Since this account does not have a "Direct Regulated/Nonregulated" cost pool, the costs involved were allocated. The Company contends that this is appropriate since information management work relates to data base and application systems for general purpose computers. Since such computers run programs related to both regulated and nonregulated operations, the company contends that all information management costs should be allocated.

The Company's argument is relevant to General Purpose Computer Expense (Account 6124), which includes the cost of maintaining general purpose computers and their operating systems. The auditors do not challenge the lack of a direct charge cost pool in that account, since Account 6124 costs are computer asset related, and not associated with data base and applications systems.

These Company arguments are not relevant to information management costs, however. If a project is solely related to either regulated or nonregulated services, it must be directly assigned, whether it involves a computer program run on a general purpose computer or not. Recognizing this, the FCC has approved

Account 6724 direct charge cost pools for the other six Bell Regional Holding Companies.[73]

Recommendation

The auditors recommend, therefore, that the Company establish a "Direct Regulated/Nonregulated" cost pool for account 6724, and directly assign accounting and information management costs whenever possible.

[73]NYNEX has "Attributed Regulated" and "Attributed Nonregulated" cost pools in Account 6724. NYNEX states the "Projects that directly identify regulated or nonregulated investment, expense or revenue are placed in the regulated or nonregulated pool." NYNEX CAM, 12/31/93, p. VI-47.

## 24. BSC international calls should be directly assigned to nonregulated in most cases.

### Summary

BSC procedures result in the cost of international telephone calls placed by the staff of BSC becoming part of departmental overhead and allocated based upon the individual department's established allocators. Because most such calls relate to BellSouth nonregulated ventures, the auditors recommend that the cost of BSC international telephone calls be directly assigned to nonregulated unless a definite regulated cause can be identified.

### Criteria

Part 64 of the FCC's rules states:

> Costs shall be directly assigned to either regulated or nonregulated activities whenever possible.[74]

Since international telephone calls are readily identifiable and relatively expensive, they should be directly assigned whenever possible in conformance with this rule.

### Condition

The auditors found that international telephone calls made by the staff of BSC are not segregated from domestic long distance calls. All long distance costs are charged to Occupancy Expense - Utilities (Account 744.2) and treated as departmental overhead.

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[74]Code of Federal Regulations, Title 47, § 64.901(b)(2).

The cost of international long distance calls is, therefore, allocated to regulated and nonregulated according to established departmental allocators.

Effect

Since the Company does not segregate the costs of international calls, the auditors were not able to quantify the effect of the current allocation system. Because the cost of individual international calls is much greater than that of domestic calls, however, it is likely that treating them as an overhead is effectively resulting in a cross-subsidy of nonregulated by regulated.

The nature of this cross-subsidy can best be illustrated by an example. Suppose a BSC task requires a hundred calls each to employees working on regulated work domestically and nonregulated work overseas. Assuming the time required to make these calls is equally divided, most overheads, such as floor space, can be equitably allocated according to the time spent by the BSC staff on regulated and nonregulated calls. Because the cost of international calls is much greater than that of domestic calls, however, such a simple allocation of long distance expense will result in regulated being charged too much and nonregulated too little. This effect can be eliminated by the direct assignment of international telephone calls.

Cause

It is likely that Company procedures have always treated telephone calls of all sorts as overheads, and allocated their cost accordingly. The rapid increase in BellSouth involvement in nonregulated overseas ventures since divesture, however, has made such accounting inappropriate.

Recommendation

The auditors recommend, therefore, that the Company revise its procedures to directly assign international telephone calls to nonregulated unless a definite regulated cause can be identified. International calls can be readily identified and assigned automatically. Exception reporting can be authorized in those relatively few cases when an international call is required in support of regulated operations.

25. A portion of BSC unattributable costs should be retained by BSC.

Summary

All BSC "unattributable" expenses are billed to subsidiary entities as corporate services. The auditors recommend that an equitable portion of these costs be retained by BSC and not billed to subsidiaries.

Criteria

Part 32 of the FCC's rules states:

> When a carrier provides substantially all of a service to or receives substantially all of a service from an affiliate which are not also provided to unaffiliated persons or entities, the services shall be recorded at cost which shall be determined in a manner that complies with the standards and procedures of the apportionment of joint and common costs between the regulated and nonregulated operations of the carrier entity.[75]

Part 64 of the FCC's rules states:

> When neither direct nor indirect measures of cost allocation can be found, the cost category shall be allocated based upon a general allocator computed by using the ratio of all expenses directly assigned or attributed to regulated and nonregulated activities.[76]

Taken together, these rules require that the "unattributable" costs of BSC be allocated based upon a general allocator computed by using the ratio of all expense directly assigned or attributed to

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[75]Code of Federal Regulations, Title 47, § 32.27(d).

[76]Code of Federal Regulations, Title 47, § 64.901(b)(iii).

regulated and nonregulated activities.

Condition

The auditors found that the company's procedures for complying with these rules involve the calculation of a monthly "General Allocator" which is than applied to all BSC unattributable costs. Examination of the allocator calculation revealed that costs retained by BSC are not included in the development of entity factors. The absence of retained costs in the development of entity factors results in all "unattributable costs" being billed to entities, and none being retained by BSC.

Effect

Since BSC retained costs are nonregulated, the effect of the Company's procedures is an understatement of nonregulated expense and an overstatement of regulated expense. The auditors estimate that, if retained costs had been included as an element in the development of the 1991 General Allocator, over $225,000 of unattributable costs would have been retained by BSC. This would have reduced BSC's billing to SB by over $25,000.[77]

Cause

The auditors were not able to determine why the General

[77]See Appendix H. BSC retained costs are currently at a lower level than in 1991. General Allocator procedures should recognize the existence of retained costs regardless of their level in any particular year.

Allocator calculation excluded retained costs, although the relatively small impact of retained costs on overall allocations may well have been a factor.

Recommendation

In any case, the auditors recommend that the BSC General Allocator calculation be revised to include retained costs. This change will better conform the Company's procedure to the FCC's rules without adding any significant administrative burden. This simple revision will, however, ensure that an equitable portion of "unattributable costs" are retained by BSC and not billed to the regulated entities.

26. The transactions between BAPCO and SGI should be specifically covered by Rule 32.27(d) for the purposes of the Georgia Surveillance Report. Substantial third party sales should be interpreted to mean that 75 percent or more of the sales are to non-affiliated companies.

Summary

Had BAPCO's transactions with it's affiliate Stevens Graphics, Inc. ("SGI") been specifically subject to the FCC's cost allocation rules, and if a clear-cut definition of "substantial" existed, Southern Bell of Georgia's regulated earnings would have been greater during the audit period. Thus, SGI obtained a subsidy. The auditors recommend that the transactions between BAPCO and SGI be specifically covered, and that substantial be interpreted to mean 75 percent or more of the sales are to third parties.

Criteria

The FCC's interpretation of Part 32.27 of its Joint Cost Order rules requires the use of fully distributed costs ("FDC") to limit the price of nonregulated affiliates' products that pass into regulated operations unless the level of unaffiliated business of the nonregulated affiliate meets certain tests. In order for affiliated transactions to be exempt from FDC, all three of the following tests must be met.

Are there:

1. substantial third party sales,
2. of the same or similar product or service,
3. at the same or lower price?

Condition

SGI is an affiliated company that, among other things, prints Southern Bell's white and yellow page directories. SGI charges BellSouth Advertising and Publishing Co. ("BAPCO") for directory printing at a negotiated price. The Georgia Surveillance Report includes an imputation of 50 percent of BAPCO's earnings above a stipulated 10.15 percent return on investment ("ROI"). Thus the cost of directory publishing has a direct impact on intrastate earnings in Georgia. If SGI had used fully distributed costs to set its prices in 1992, BAPCO's Georgia earnings would have been approximately $_____ higher based on an estimate provided by the Company.[78]

BAPCO has taken the position that "the negotiated pricing methodology has been accepted by the FCC and included in the BellSouth Cost Allocation Manual, and thus does not subject BAPCO's affiliated transactions to the pricing hierarchy as set forth in Part 32.27." BAPCO also states that "although the level of non-affiliated business necessary to establish a substantial outside market under the FCC's definition is subject to interpretation, Stevens Graphics believes that [its] market pricing is supportable by the level of non-affiliated business in 1992."

The Company could only provide the auditors with "off the top of the head" estimates of the relative levels of SGI's directory printing business with affiliated versus non-affiliated companies. Based on these estimates, it appears that in 1992 BAPCO represented

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[78]Amount is proprietary.

at least 78 percent of SGI's directory printing business. In other words, the non-affiliated directory sales were apparently 22 percent of SGI's directory printing business. This does not appear to be substantial.

Effect

Had BAPCO's transactions with SGI been specifically identified as being covered by Rule 32.27(d), Southern Bell's Georgia intrastate earnings would have been $_____ higher in 1991. This equates to a $_____ understatement of intrastate earnings. This understatement constitutes a cross-subsidy. Since the Company was unable to provide any estimates for the other audit years, the auditors assumed the results were the same in all four audit years. We estimate the amount for all four audit years, therefore, as $____ (____x 4).[79]

Cause

BAPCOs transactions with SGI are not specifically identified as being covered by Rule 32.27(d) and there is no clear cut definition of "substantial" in the interpretation and application of the tests applicable to third-party markets.

Recommendation

On a going-forward basis the Commission should require that, for the purposes of the Georgia Surveillance Report, FCC Rule

[79]Amounts are proprietary.

32.27(d) shall apply to the transactions between BAPCO and Stevens Graphics, Inc., and the concept of substantial third-party sales should be interpreted to mean that 75 percent or more of sales are to non-affiliated companies.

The Company has termed the 75 percent threshold recommended by the auditors "ludicrous, unreasonable, overly burdensome, unnecessary and unwarranted".[80] The FCC, however, has also proposed the establishment of a 75 percent threshold. The FCC states:

> We tentatively conclude that any nonregulated affiliate that sells less than 75 percent of its output to nonaffiliates has too large a volume of affiliate transactions to be deemed to have a predominant purpose of serving non-affiliates.[81]

That consideration aside, the purpose of the cost allocation manual, and the Part 32 affiliated transaction rules, is to protect regulated customers from cross-subsidies. This is consistent with Georgia Statute 46-2-23(g). The intent of the 75 percent threshold recommendation is to provide such protection.

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[80]Company response to Preliminary Finding No. 32.

[81]Amendment to Parts 32 and 64 of the Commission's Rules to account for transactions between Carriers and their Nonregulated Affiliates, CC Docket No. 93-251, Notice of Proposed Rulemaking, FCC 93-453, released October 20, 1993, para. 22.

27. BellSouth Enterprise's retention of expenses associated with its foreign subsidiaries should be referred to the Internal Revenue Service International Examination Branch and the Georgia Department of Revenue Income Tax Division for further investigation with regard to its tax deductions.

Summary

A review of the intercompany billing by BellSouth Enterprises, Inc. for projects and management fees to its foreign subsidiaries indicates that significant expense incurred for foreign companies is not billed to them. The auditors are concerned that BSE's action may have some negative federal and state tax consequences. The auditors are concerned that BellSouth may be overstating the expense associated with its domestic operations and understating the expense associated with its foreign operations.

From the data reviewed for the audit period, it is estimated that as much as $50 million in expense for these foreign subsidiary companies may have been incurred by BSE Headquarters, but not billed. The exact amount can not be determined by the auditors, as BellSouth and BSE have repeatedly denied them access to its 1988 through 1991 Federal Tax returns for the BSE companies. The non-billing of foreign company expense does not have a direct impact on Georgia's regulated telephone expense allocations, but there may indeed be an impact on BellSouth's Georgia tax obligation. The auditors recommend that the Commission refer this issue to the Internal Revenue Service International Examination Branch and the Georgia Department of Revenue Income Tax Division for follow-up review.

Criteria

Article I, Scope of Services, dated July 8, 1992 defined the Scope and Objectives of the Audit. Section eight (8) states the following:

> "to receive a report of all instances of non-compliance with this COMMISSION'S rules concerning transactions with affiliates (FCC-Section 32.27), allocation of cost between regulated services and non-regulated activities or **instances of illegal acts that could result in criminal prosecutions (these may be reported separately)."**

Condition

During the audit period significant expenses were incurred at BSE Headquarters for specific projects and other services provided to BSE's foreign subsidiaries that were not billed to them. Binder 34 of Coopers & Lybrand's work papers for its 1991 Part 64 audit indicates that BSE, for the most part, does not bill its foreign subsidiaries for specific project costs or BSE management fees. It does bill its U.S. companies a 2.1 percent management fee to cover the cost of such items as Human Resource, Marketing, Legal Counsel, Financial Management, etc. expense. Two of the BSE foreign subsidiaries which were not billed during 1991 were BellSouth Australia and INVERSORA.

Binder 34 of C&L's Part 64 Audit work papers provides some information as to the amount of expense not billed to the foreign companies. From the data reviewed during the audit, for the 1988-1991 period the amount of expense not billed could exceed $50 million. For example, for only three of the foreign companies during the last half of 1991 alone, the expense retained by BSE

totaled $3.6 million. The specific financial information pertaining to any single BSE company is considered proprietary by BellSouth.

By not billing the foreign companies for the expense incurred, and keeping that expense on BSE's books, the expense would not be identified as being associated with its foreign operations. The Company has stated that the estimated $50 million expense is "stewardship expense" and is allowed to be retained. The auditors believe that the legality of retaining these expenses as "stewardship expenses" is a matter which can only be determined by the appropriate federal and state taxing authorities.

Effect

The effect may be an underpayment of U.S and Georgia taxes as the foreign company related expenses are being retained as deductions on U.S. tax returns, while the revenue of the foreign operations is not subject to U.S taxes.

Cause

Unknown

Recommendation

The auditors recommend that the Commission refer this issue to the Internal Revenue Service International Examination Branch and the Georgia Department of Revenue Income Tax Division for further investigation.

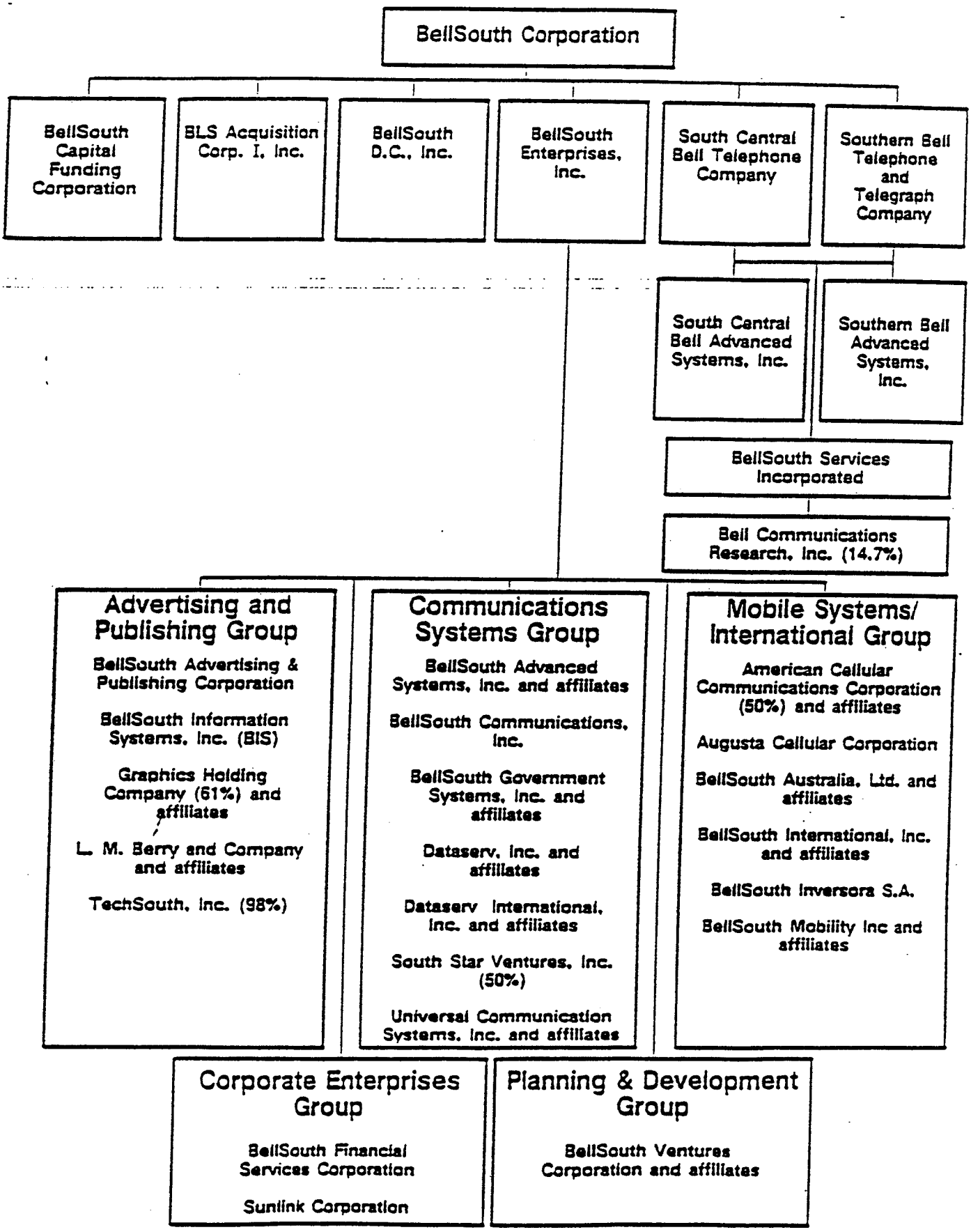
## List of Acronyms

| Acronym | Meaning |
|---|---|
| ADIT | Accumulated Deferred Income Taxes |
| AIC | Average Inward Cost |
| AT&T | AT&T Corporation |
| BAPCO | BellSouth Advertising and Publishing Corporation |
| Bellcore | Bell Communications Research |
| BRCS | Business Residential Calling Services |
| BSC | BellSouth Corporation |
| BSE | BellSouth Enterprises, Inc. |
| BSI | BellSouth International, Inc. |
| BSS | BellSouth Services, Inc. |
| BST | BellSouth Telecommunications, Inc. |
| CAM | Cost Allocation Manual |
| CAPRI | Computer Assisted Purchasing, Receiving, and Invoicing |
| CDAR | Customer Dialed Account Recording |
| CFITAP | Consolidated Federal Income Tax Allocation Policy |
| COE | Central Office Equipment |
| CPE | Customer Premises Equipment |
| CRIS | Customer Record Information System |
| CSS | Cost Separation System |
| CUCRIT | Capital Utilization Criteria |
| C&L | Coopers & Lybrand |
| DCPR | Detailed Continuing Property Record |
| DRMA | Detailed Regulatory Monthly Allocation |
| ESOP | Employee Stock Ownership Plan |

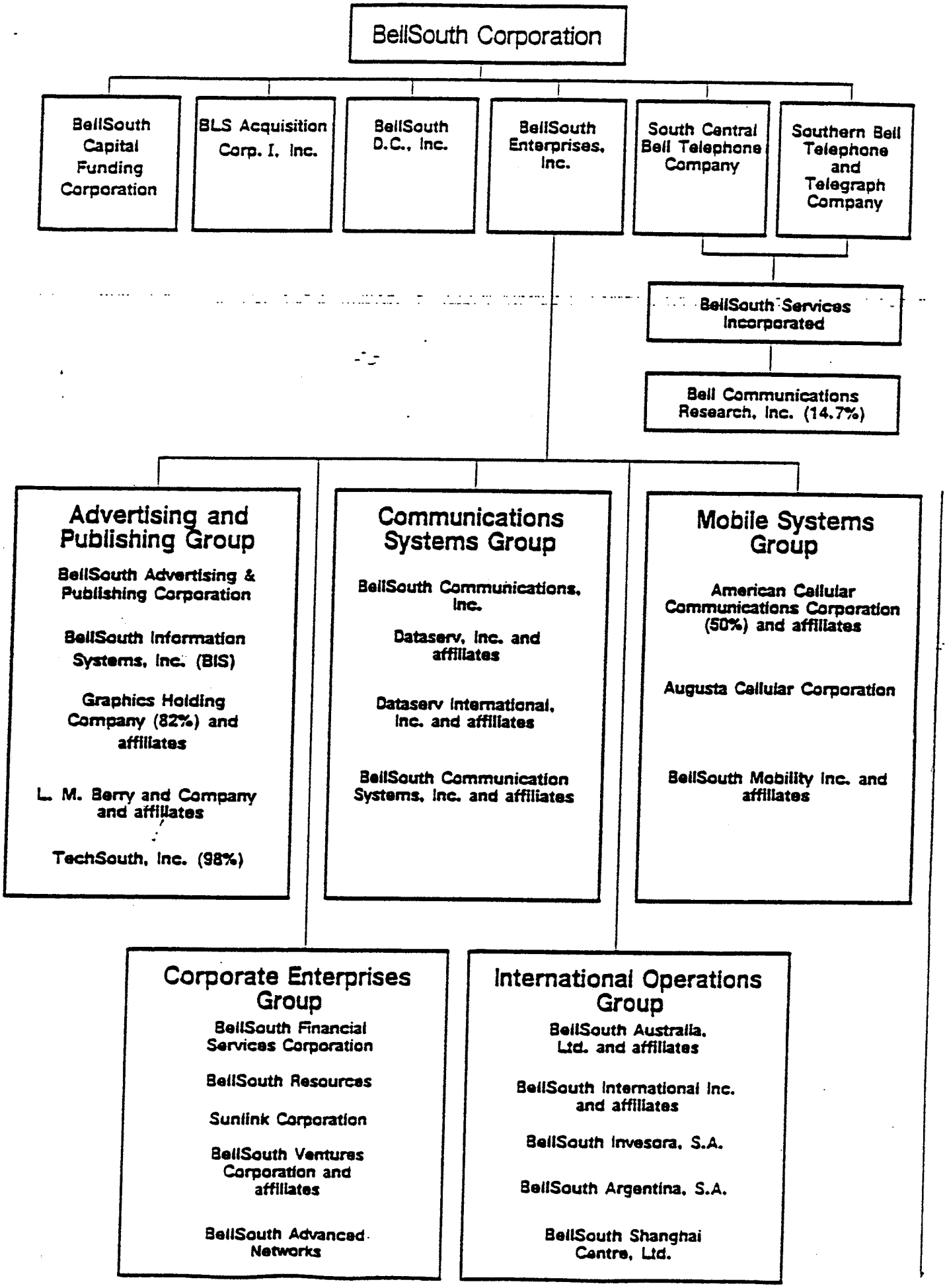
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|---|---|
| ESP | Enhanced Service Provider |
| FCC | Federal Communications Commission |
| FDC | Fully Distributed Costs |
| GA | Georgia |
| GAAP | Generally Accepted Accounting Principles |
| GPSC | Georgia Public Service Commission |
| HQ | Headquarters |
| HVAC | Heating Ventilation Air Conditioning |
| IBITS | Incoming Billing Interface Tracking System |
| IRC | Internal Revenue Code |
| IRP | Incentive Regulation Plan |
| IRS | Internal Revenue Service |
| ISDN | Integrated Services Digital Network |
| ITC | Investment Tax Credit |
| JCO | Joint Cost Order |
| JFC | Job Function Code |
| LESOP | Leveraged ESOP |
| LOB | Line of Business |
| MFJ | Modified Final Judgement |
| NOI | Net Operating Income |
| ONA | Open Network Architecture |
| OPCC | Outside Plant Control Center |
| OTC | Operating Telephone Company |
| PBX | Private Branch Exchange |
| PCS | Personal Communications Service |
| PICS | Plug-in Control System |

| | |
|---|---|
| POTS | Plain Old Telephone Service |
| PSC | Public Service Commission |
| PTVM | Public Telephone Voice Messaging |
| RFP | Request for Proposals |
| RTU | Right-to-Use |
| R&D | Research and Development |
| SB | Southern Bell Telephone and Telegraph Company |
| SCB | South Central Bell |
| SFAS | Statement of Financial Accounting Standards |
| SGI | Stevens Graphics, Inc. |
| SKA | Snavely, King & Associates |
| TPIS | Telephone Plant In Service |
| TPUC | Telephone Plant Under Construction |
| USOA | Uniform System of Accounts |

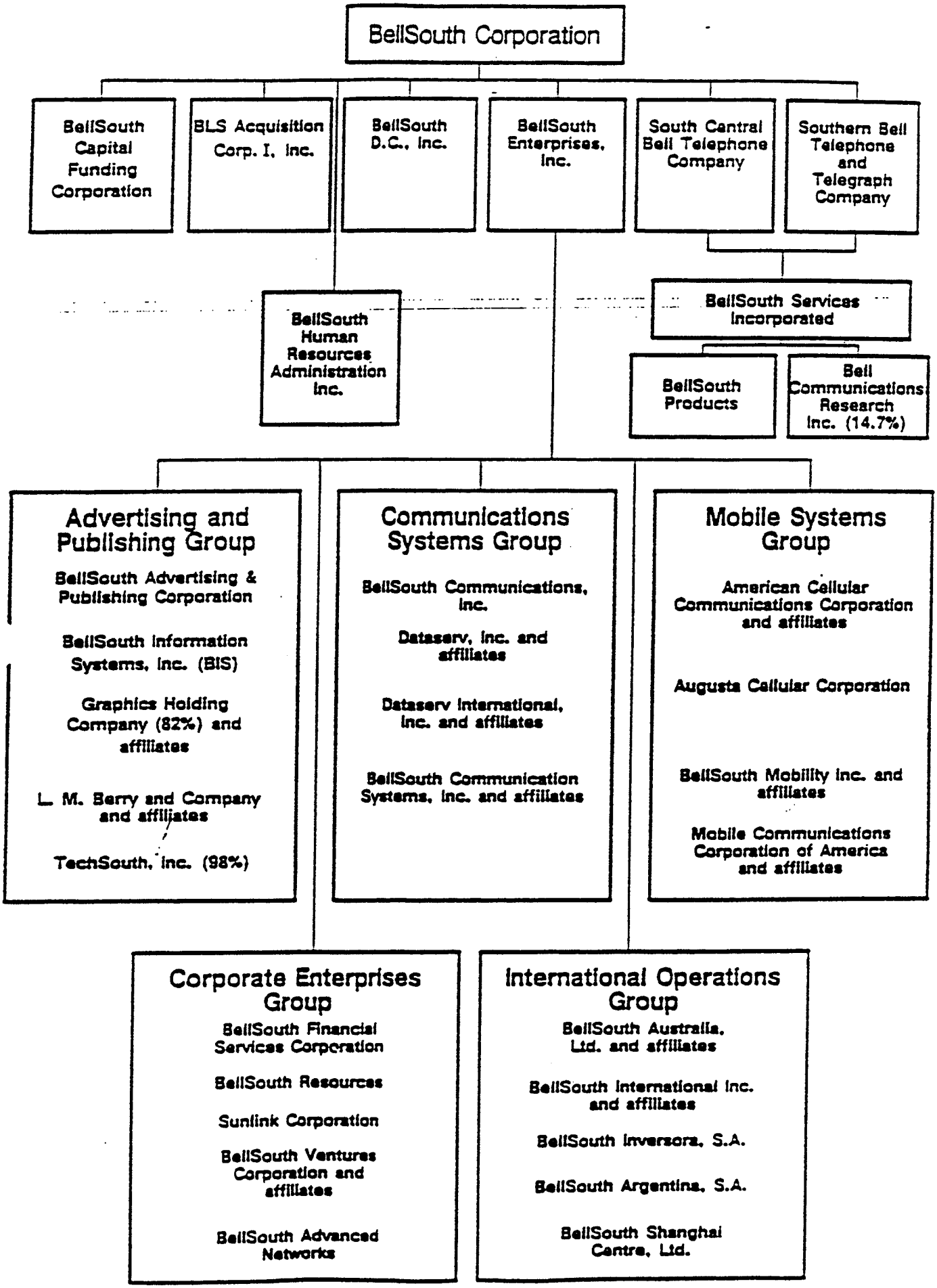
# BellSouth Corporate Structure



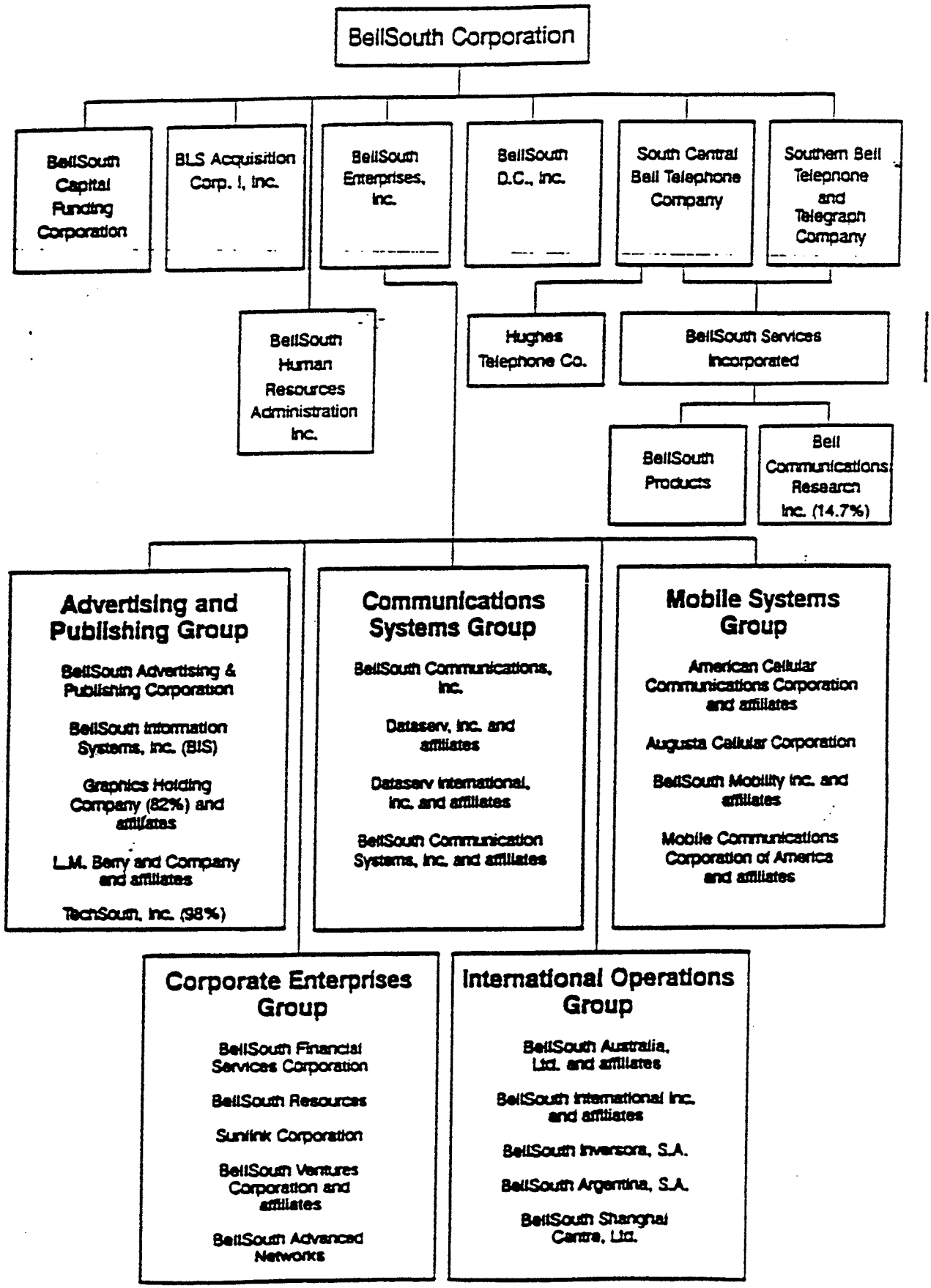
# Structure


BellSouth Corporation
BellSouth Capital Funding Corporation
BLS Acquisition Corp. I, Inc.
BellSouth D.C., Inc.
BellSouth Enterprises, Inc.
South Central Bell Telephone Company
Southern Bell Telephone and Telegraph Company
BellSouth Services Incorporated
Bell Communications Research, Inc. (14.7%)
Advertising and Publishing Group
BellSouth Advertising & Publishing Corporation
BellSouth Information Systems, Inc. (BIS)
Graphics Holding Company (82%) and affiliates
L. M. Berry and Company and affiliates
TechSouth, Inc. (98%)
Communications Systems Group
BellSouth Communications, Inc.
Dataserv, Inc. and affiliates
Dataserv International, Inc. and affiliates
BellSouth Communication Systems, Inc. and affiliates
Mobile Systems Group
American Cellular Communications Corporation (50%) and affiliates
Augusta Cellular Corporation
BellSouth Mobility Inc. and affiliates
Corporate Enterprises Group
BellSouth Financial Services Corporation
BellSouth Resources
Sunlink Corporation
BellSouth Ventures Corporation and affiliates
BellSouth Advanced Networks
International Operations Group
BellSouth Australia, Ltd. and affiliates
BellSouth International Inc. and affiliates
BellSouth Invesora, S.A.
BellSouth Argentina, S.A.
BellSouth Shanghai Centre, Ltd.

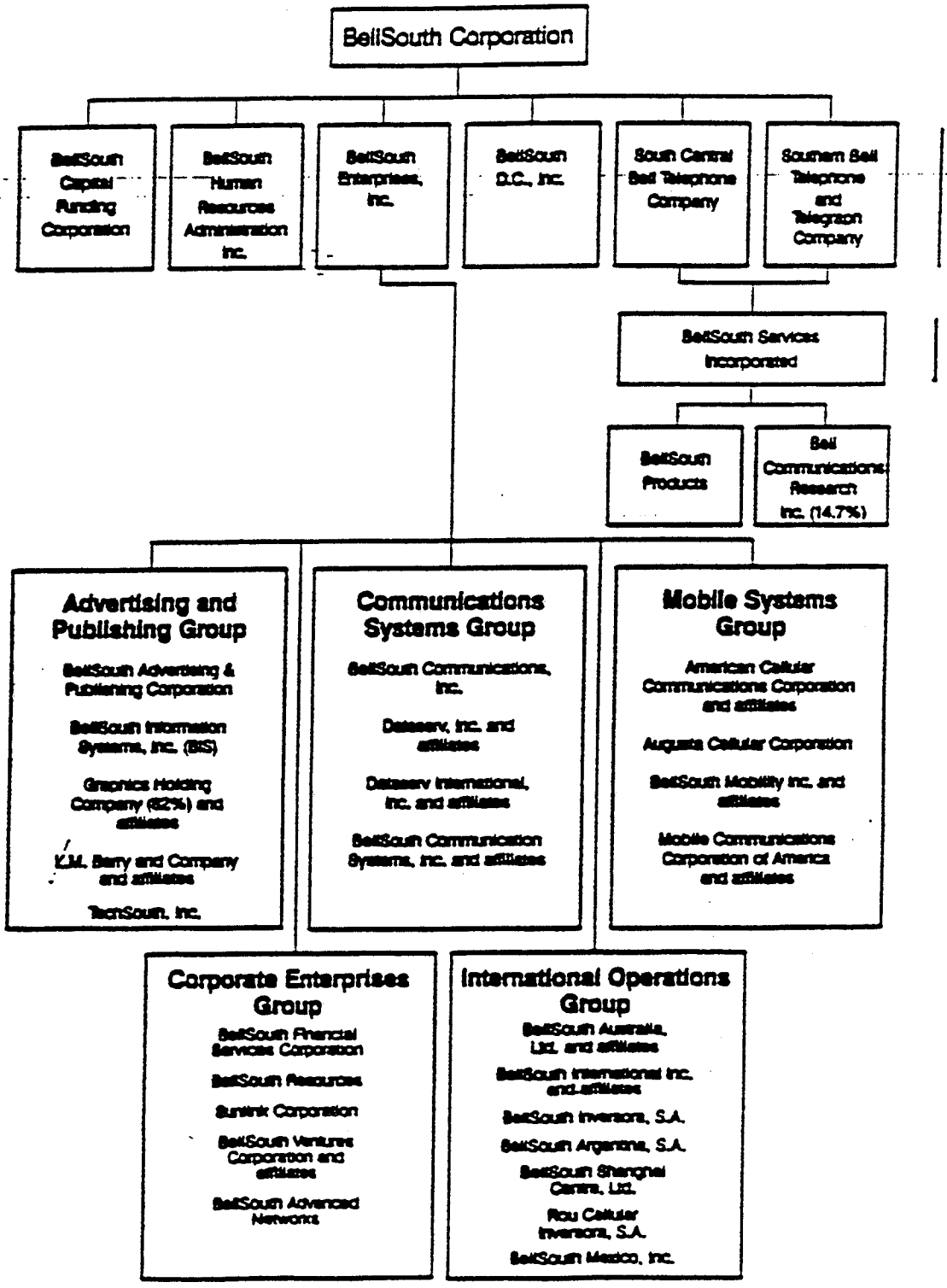
# BellSouth Corporate Structure



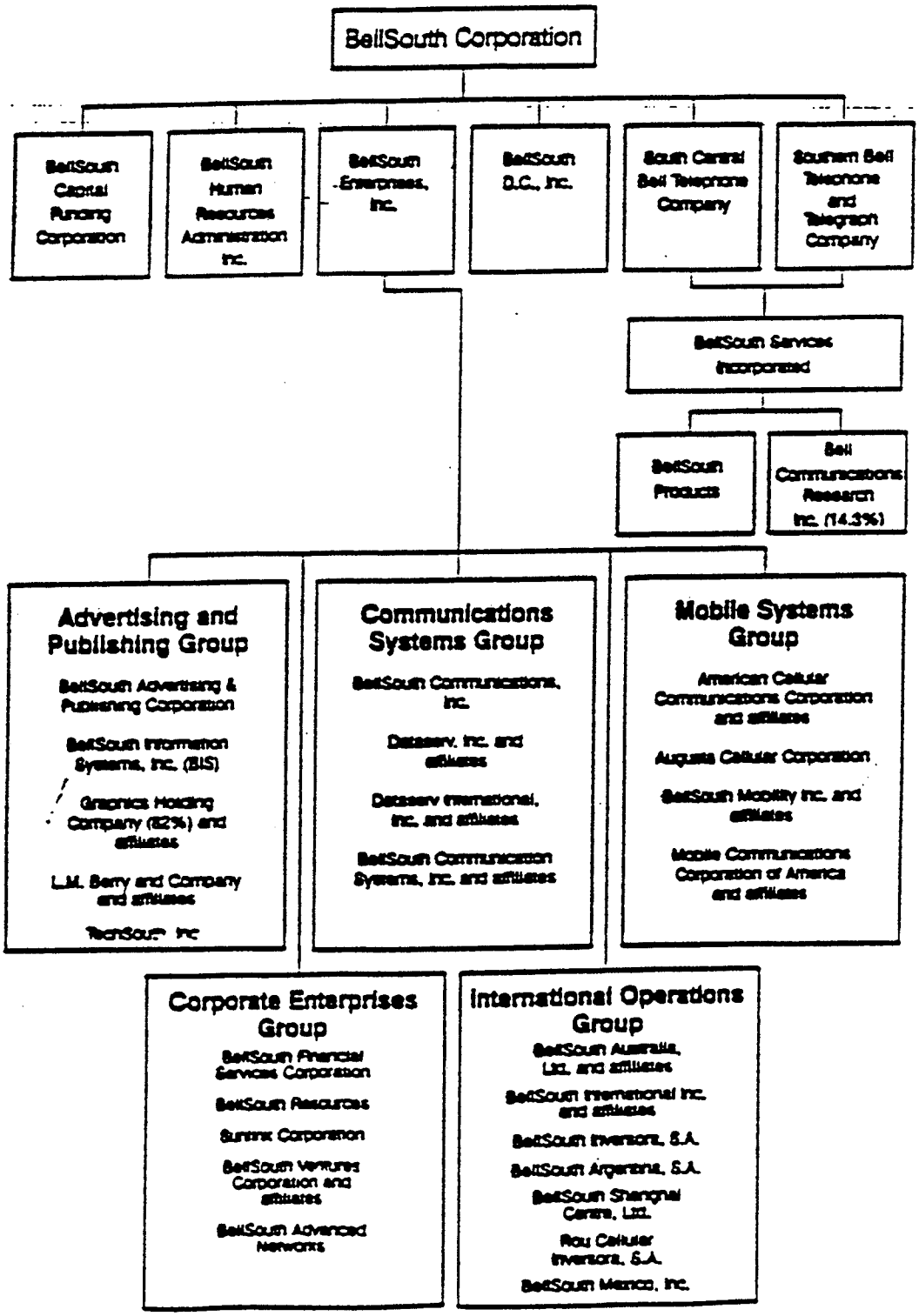
# BellSouth Corporate Structure



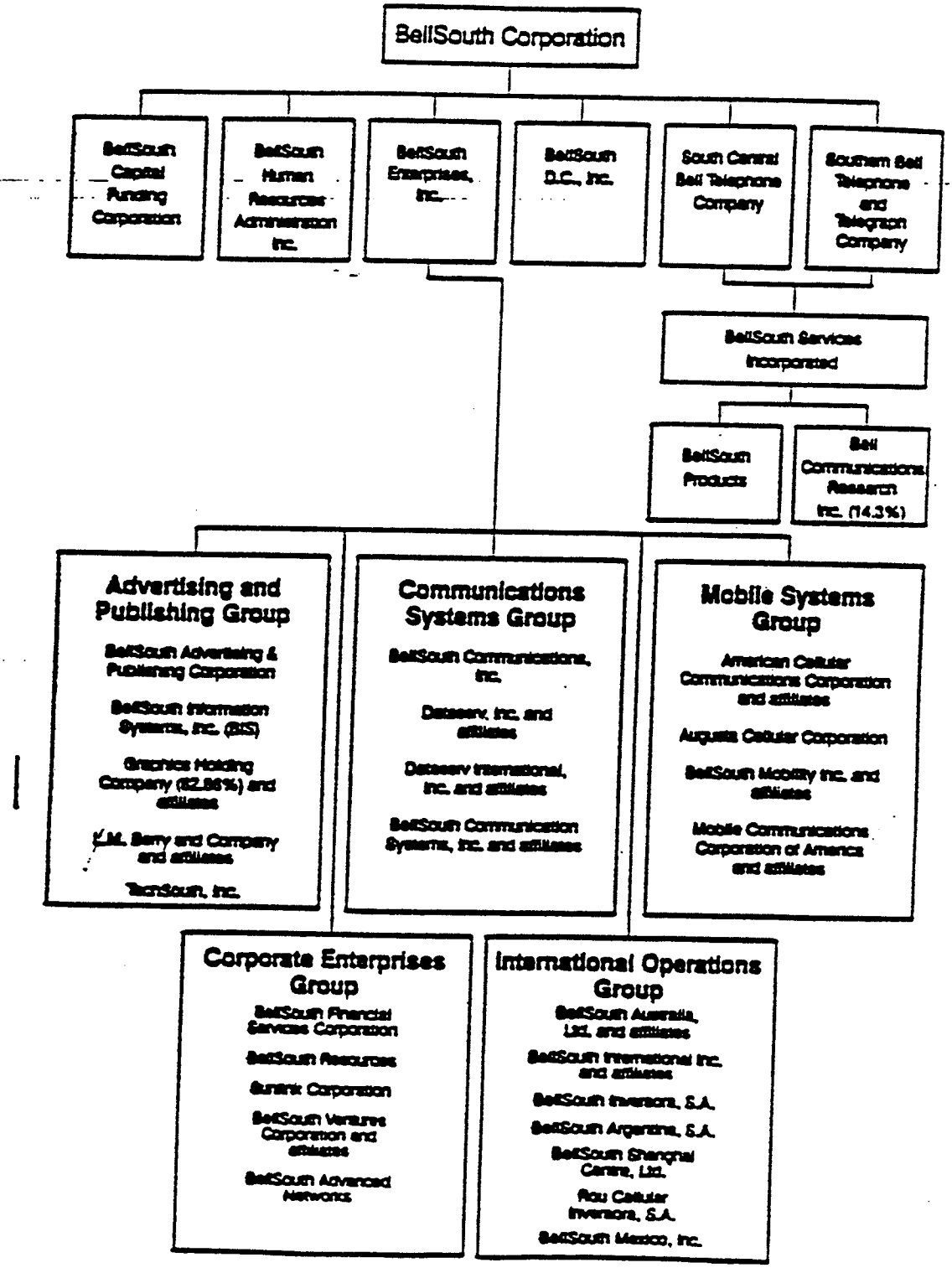
# BellSouth Corporate Structure



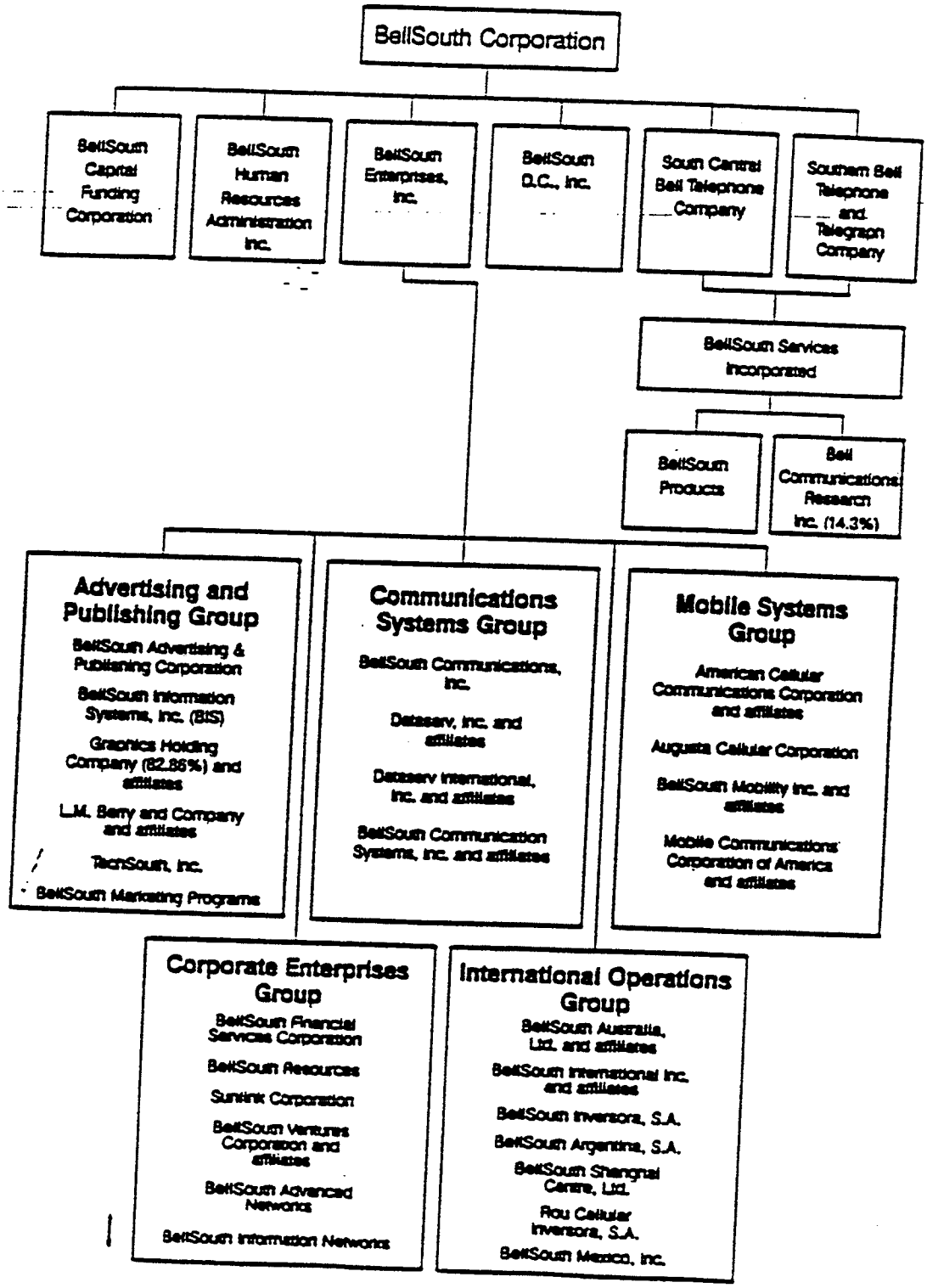
# BellSouth Corporate Structure



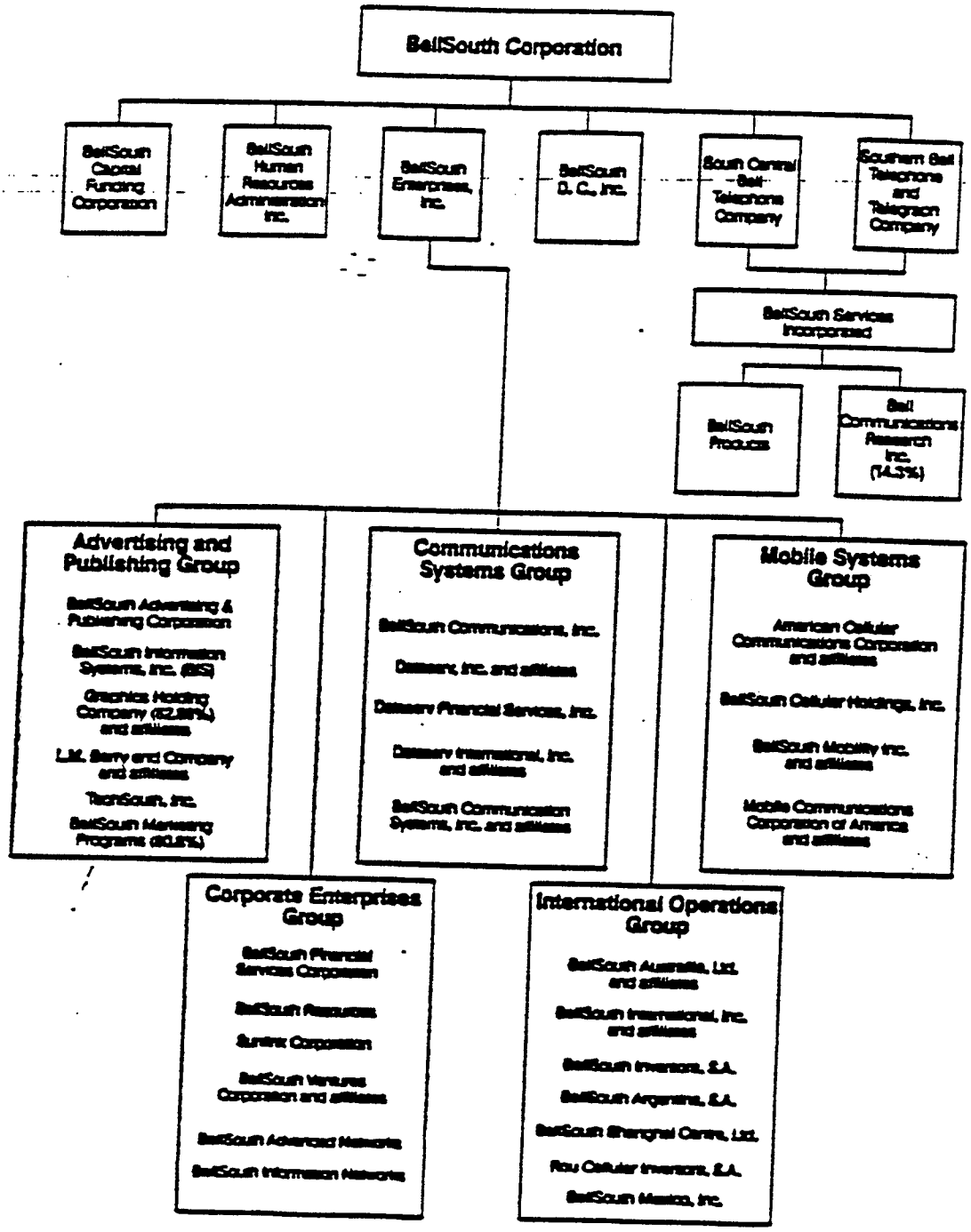
# BellSouth Corporate Structure



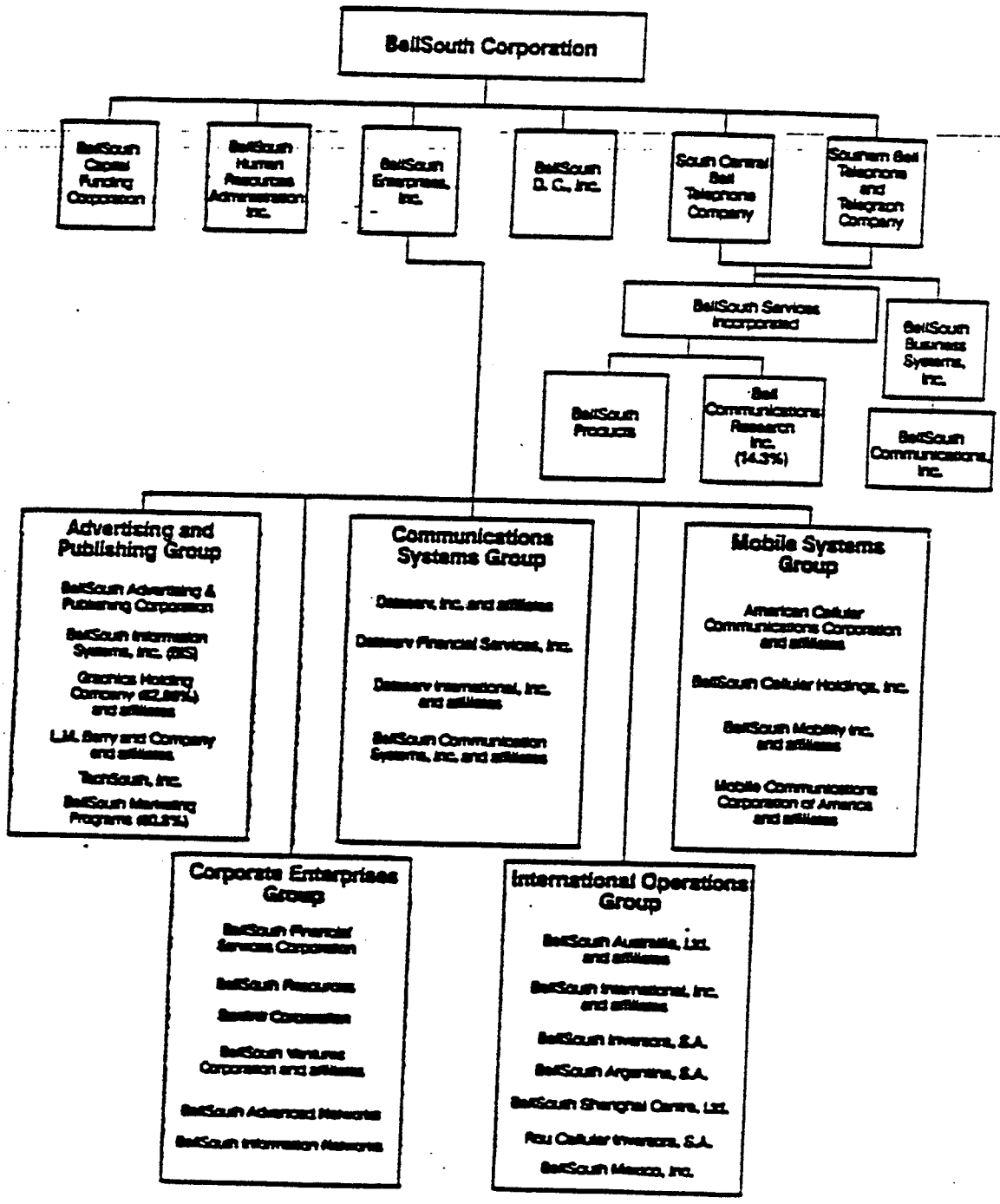
# BellSouth Corporate Structure



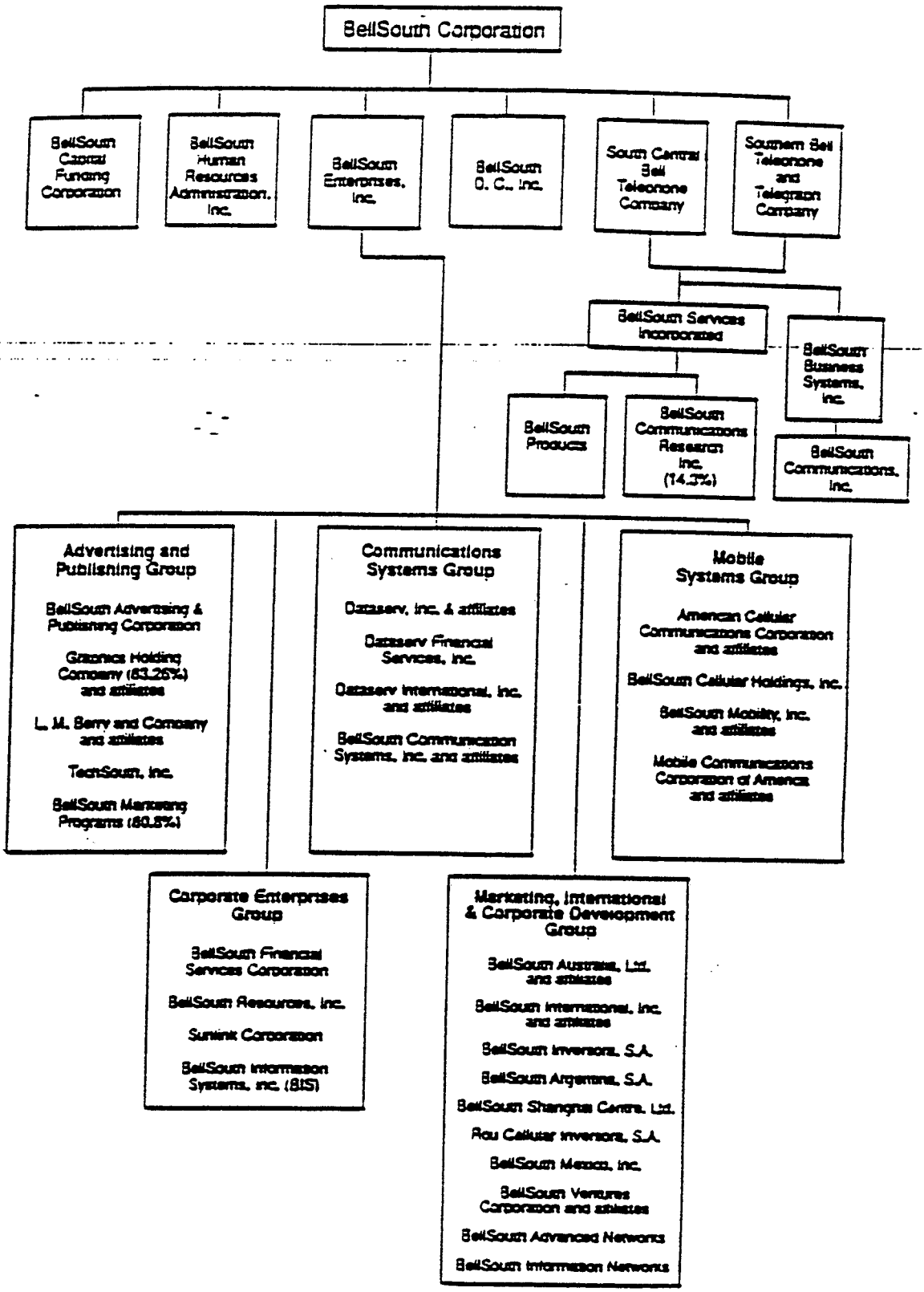
## BellSouth Corporate Structure



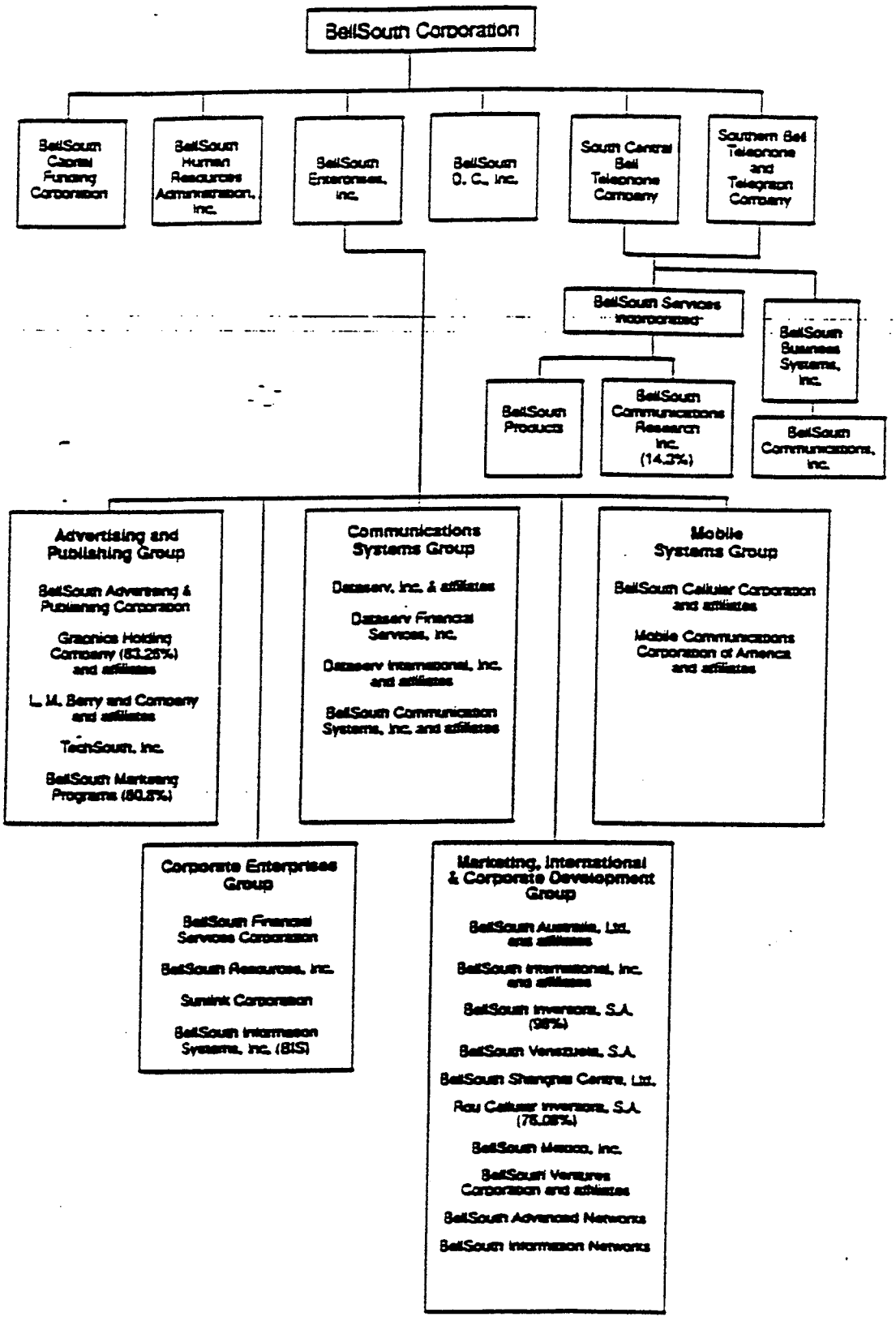
## BellSouth Corporate Structure



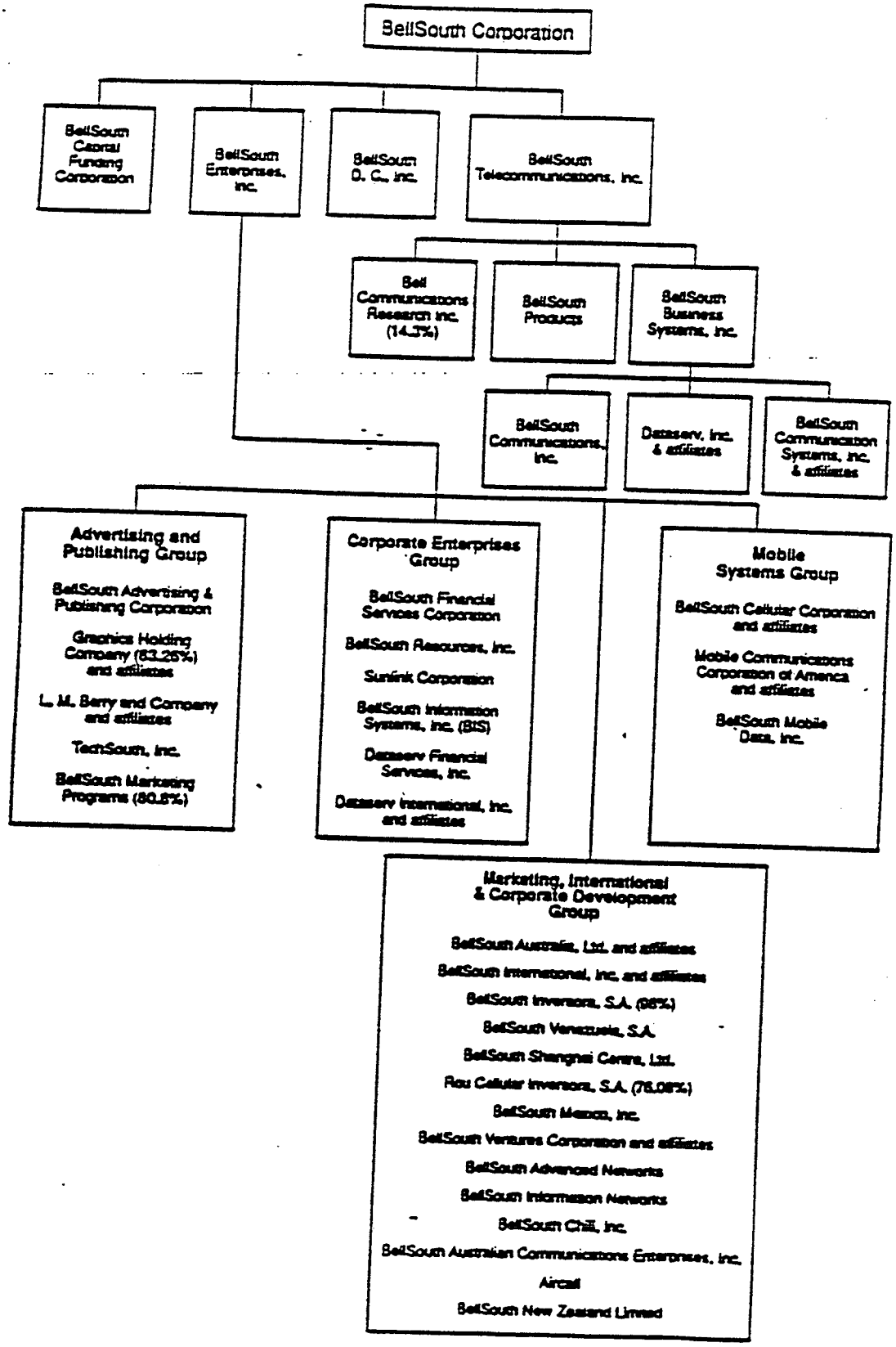
# BellSouth Corporate Structure



# BellSouth Corporate Structure



# BellSouth Corporate Structure



AFFILIATE TRANSACTION AUDIT OF SB OF GEORGIA

LEVERAGE STOCK OWNERSHIP PLAN (ESOP)

The tax benefits associated with the dividends for stock held by the LESOP Trust are being retained at BellSouth Corporation, while Georgia's telephone customers incur the following increased costs charged as benefit expense:

(1) Interest cost for the ESOP loan;

(2) Additional matching fund requirements for savings plans' participants;

(3) Risk associated with change in stock value for shares held by the Trust.

Southern Bell of Georgia's telephone customers increased benefit cost, associated with having the Leveraged ESOP plan, is estimated to be $24.4 million ($18.3 million intrastate) for the 1990 through 1994 period. Georgia's portion of the tax benefits, being retained at the BellSouth Corporate level for the same period, is estimated to be $8.1 million ($6.1 million intrastate).

## ANALYSIS OF LESOP DATA RESPONSES

**(JWC-14)** "The tax benefits associated with the dividends on Bellsouth Corporation stock held by the Trust and used to service debt is retained by Bellsouth Corporation."

BELLSOUTH CORPORATION ($ M)

| | DIVIDENDS ON STOCK IN TRUST **(114)** | TAX REDUCTION ON DIVIDENDS PAID TO TRUST **(JWC-6)** | INTEREST ON ESOP NOTES **(JWC-4, 62)** |
|---|---|---|---|
| 1990 | $ 23.1 | $ 7.9 | $ 60.5 |
| 1991 | $ 43.5 | $ 14.8 | $ 74.8 |
| 1992 | $ 43.7 | $ 14.8 | $ 72.4 |
| 1993 | | $ 14.8 | $ 69.5 |
| 1994 | | $ 14.8 | $ 66.2 |
| | | $ 67.3 | $343.4 |

GEORGIA ALLOCATION FACTOR (CALCULATED PAGE 2) .120839743

**GEORGIA'S PORTION OF TAX SAV. = $ 8.1 MILLION**
INTRASTATE FACTOR = 75%
**INTRASTATE PORTION OF TAX SAVINGS = $ 6.1 MILLION**

DEVELOPMENT OF GEORGIA ALLOCATION FACTOR:
**(JWC-30 DATA):**

| | | | GEORGIA |
|---|---|---|---|
| 1. | SHARES ALLOCATED - GEORGIA | | $3,203,464 |
| 2. | SHARES ALLOCATED -SB HQ. | 788,708 | |
| 3. | GA. PRORATE FACT FROM SB | .2899 | |
| 4. | SB ALLOCATION TO GA. | 228,646 | 228,646 |
| 5. | TOTAL ALLOCATED TO GA. | | 3,432,110 |
| 6. | TOTAL BELLSOUTH CORP. | | 28, 402,166 |
| 7. | ALLOCATION FACTOR TO GEORGIA (7=5/6) | | 0.120839743 |

ESTIMATED INCREASED BENEFIT COST ASSIGNED TO GEORGIA DUE TO LEVERAGED EMPLOYEE STOCK OWNERSHIP PLAN (LESOP):

| | | 1990 ($M) | 1991 ($M) | 1992 ($M) | TOTAL 90-92 ($M) |
|---|---|---|---|---|---|
| 8. | INTEREST EXPENSE **(JWC-4)** | 60.5 | 74.8 | 72.4 | 207.7 |
| 9. | DIVIDENDS TO TRUST **(114)** | 23.1 | 43.5 | 43.7 | 110.3 |
| 10. | STOCK LOSS (SHARES ALL.) **(JWC-64)** | .4 | 2.9 | 4.0 | 7.3 |
| 11. | TOTAL BS INCREASED COST (11=8-9+10) | 37.8 | 34.2 | 32.7 | 104.7 |
| 12. | EST. ALLOCATION TO GA. | .1208 | .1208 | .1208 | .1208 |
| 13. | EST. GA INCREASED BENEFIT EXPENSE ALLOCATION | 4.5 | 4.1 | 4.0 | 12.6 |
| 14. | INCREASED MATCHING EXPENSE TO GA FOR ESOP **(JWC-63)** | 1.2 | 1.3 | 1.3 | 3.8 |
| 15. | INCREASED BENEFIT COST TO GA FOR ESPO (15=13+14) | 5.7 | 5.4 | 5.3 | 15.4 |
| 16. | ESTIMATED 93 & 94 INCREASED GA COSTS (BASED ON 90-92 DATA, INCREASES IN STOCK PRICE & DECREASING LOAN INTEREST **(JWC-4)** ) | | | | 9.0 |
| 17. | INCREASE IN 90-94 EXPENSE DUE TO LESOP (17=15+16) = | | | | $24.4M |
| 18. | INTRASTATE FACTOR = | | | | 75% |
| 19. | INCREASED GEORGIA INTRASTATE EXPENSE 90-94 (19=17*18)= | | | | $18.3M |

ADDITIONAL DATA FROM RESPONSES:

A. ESOP loan amount **(JWC-1)** $850,000,000

B. Start date July 1, 1990; End July 1, 2003 **(JWC-2)**

C. Loan source **(JWC-3)** Morgan Stanley

D. All shares of stock were purchased on the open market. **(JWC-7)**

E. Number of shares purchased and average price. **(JWC-8&32)**

| | NUMBER OF SHARES PURCHASED | AVERAGE PURCHASE PRICE | ESTIMATED PURCHASE COST TO TRUST |
|---|---|---|---|
| MANAGEMENT SAV. PLAN | 10,356,020 | $53.11 | $550,000,000 |
| SAV. SECURITY PLAN | 5,533,342 | $54.22 | $300,000,000 |
| | 15,889,362 | | $850,000,000 |

F. The administration cost associated with the Leveraged ESOP is not separated from other administrative cost associated with the existing employee savings plans, therefore none of the ESOP's administration cost is included in the Audit's estimated additional Georgia intrastate expense due to the LESOP. **(JWC-11)**

G. The estimated tax savings associated with the dividends identified in JWC-6 assumes a tax rate of 33.6 percent for 1993 and 1994. **(JWC-29)** The current federal corporate tax rate is 35 percent, therefore the tax savings will be slightly higher than the amount calculated.

CSS... FORM NUMBER: HP2700
CSS/PPS MODULE NAME: AB01R111
CSS/PPS REPORT NAME: NONREG PRODUCT INCOME STATEMENT BY PRODUCT
56 START-UP COSTS

BELLSOUTH CORPORATION
GEORGIA

RETENTION: PERMANENT
REPORT DATE AND TIME: 01/24/92 1648
CURRENT MONTH/YEAR OF BUSINESS: 12/1991

| | | TOTAL PRODUCT GROUP | | IUO START-UP COST | | CPE START-UP COST | | MEMORYCALL SERVICE | |
|---|---|---|---|---|---|---|---|---|---|
| | | CURR MO | Y-T-D | CURR MO | Y-T-D | CURR MO | Y-T-D | CURR MO | Y-T-D |
| 1 | LOCAL SERVICE REVENUE | | | | | | | | |
| 2 | NETWORK ACCESS REVENUE-INTERSTATE | | | | | | | | |
| 3 | NETWORK ACCESS REVENUE-INTRASTATE | | | | | | | | |
| 4 | LONG DISTANCE REVENUE | | | | | | | | |
| 5 | MISCELLANEOUS REVENUE | | | | | | | | |
| 6 | LESS - UNCOLLECTIBLE REVENUE | | | | | | | | |
| 7 | TOTAL OPERATING REVENUES | | | | | | | | |
| | - PERCENTAGE | | | | | | | | |
| 8 | NETWORK SUPPORT EXPENSE | | | | | | | | |
| 9 | GENERAL SUPPORT EXPENSE | | | | | | | | |
| 10 | CENTRAL OFFICE SWITCHING EXPENSE | | | | | | | | |
| 11 | OPERATOR SYSTEMS EXPENSE | | | | | | | | |
| 12 | CENTRAL OFFICE TRANSMISSION EXPENSE | | | | | | | | |
| 13 | INFORMATION ORIGINATION/TERM. EXPENSE | | | | | | | | |
| 14 | CABLE AND WIRE FACILITIES EXPENSE | | | | | | | | |
| 15 | OTHER PROPERTY & NETWORK OPRNS EXPENSE | | | | | | | | |
| 16 | CUSTOMER ASSISTANCE EXPENSE | | | | | | | | |
| 17 | COST OF SERVICES | | | | | | | | |
| | - PERCENTAGE | | | | | | | | |
| 18 | DEPRECIATION AND AMORTIZATION EXPENSE | | | | | | | | |
| 19 | MARKETING EXPENSE | | | | | | | | |
| 20 | CORPORATE EXPENSE | | | | | | | | |
| 21 | SELLING, GENERAL & ADMINISTRATIVE | | | | | | | | |
| | - PERCENTAGE | | | | | | | | |
| 22 | TAXES OTHER THAN INCOME | | | | | | | | |
| 23 | OTHER EXPENSES | | | | | | | | |
| 24 | TOTAL OPERATING EXPENSES | | | | | | | | |
| | - PERCENTAGE | | | | | | | | |
| 25 | NET OPERATING REVENUE | | | | | | | | |
| | - PERCENTAGE | | | | | | | | |
| 26 | NON-OPERATING INCOME AND EXPENSES (NET) | | | | | | | | |
| 27 | ALLOWANCE FOR FUNDS USED DURING CONST. | | | | | | | | |
| 28 | INC BEFORE INTEREST AND INCOME TAXES | | | | | | | | |
| | - PERCENTAGE | | | | | | | | |
| 29 | INTEREST AND RELATED ITEMS | | | | | | | | |
| 30 | INCOME BEFORE INCOME TAXES | | | | | | | | |
| | - PERCENTAGE | | | | | | | | |
| 31 | FEDERAL INCOME TAXES | | | | | | | | |
| 32 | STATE AND LOCAL INCOME TAXES | | | | | | | | |
| 33 | TOTAL INCOME TAXES | | | | | | | | |
| | - PERCENTAGE | | | | | | | | |
| 34 | EXTRAORDINARY ITEMS (INCOME) EXPENSE | | | | | | | | |
| 35 | INCOME TAXES ON EXTRAORDINARY ITEMS | | | | | | | | |
| 36 | NET INCOME | | | | | | | | |
| | - PERCENTAGE | | | | | | | | |

CSS/PPS FORM NUMBER: MP2700
CSS/PPS MODULE NAME: AB01R11H
CSS/PPS REPORT NAME: NONREG PRODUCT INCOME STATEMENT BY PRODUCT
56 START-UP COSTS

BELLSOUTH CORPORATION
GEORGIA

RETENTION: . PERMANENT PAGE: 18
REPORT DATE AND TIME: 01/24/92 1648
CURRENT MONTH/YEAR OF BUSINESS: 12/1991

| | | TOTAL PRODUCT GROUP | | TVG START-UP COST | | CPE START-UP COST | | MEMORYCALL SERVICE | |
|---|---|---|---|---|---|---|---|---|---|
| | | CURR MO AVG | Y-T-D AVG | CURR MO AVG | Y-T-D AVG | CURR MO AVG | Y-T-D AVG | CURR MO AVG | Y-T-D AVG |
| 37 | TOTAL TELEPHONE PLANT IN SERVICE | | | | | | | | |
| 38 | PROPERTY HELD FOR FUTURE USE | | | | | | | | |
| 39 | TELECOMM. PLANT UNDER CONSTRUCTION | | | | | | | | |
| 40 | TELECOMMUNICATIONS PLANT ADJS. | | | | | | | | |
| 41 | NONOPERATING PLANT | | | | | | | | |
| 42 | GOODWILL | | | | | | | | |
| 43 | INVENTORIES | | | | | | | | |
| | LESS | | | | | | | | |
| 44 | DEPRECIATION & AMORTIZATION | | | | | | | | |
| 45 | DEFERRED INCOME TAXES | | | | | | | | |
| 46 | NET INVESTMENT | | | | | | | | |
| | - PERCENTAGE | | | | | | | | |
| 47 | ANNUALIZED RATE OF RETURN | | | | | | | | |
| 48 | LAND | | | | | | | | |
| 49 | VEHICLE, AIRCRAFT, AND OTHER WORK EQUIP. | | | | | | | | |
| 50 | BUILDINGS | | | | | | | | |
| 51 | FURN., OFFICE EQUIP., GEN'L PURP. COMPUT. | | | | | | | | |
| 52 | CENTRAL OFFICE ASSETS | | | | | | | | |
| 53 | OPERATOR SYSTEMS | | | | | | | | |
| 54 | DIAL | | | | | | | | |
| 55 | LOOP | | | | | | | | |
| 56 | INTEROFFICE | | | | | | | | |
| 57 | INFORMATION ORIG./TERMINATION | | | | | | | | |
| 58 | CABLE AND WIRE FACILITIES | | | | | | | | |
| 59 | LOOP | | | | | | | | |
| 60 | INTEROFFICE | | | | | | | | |
| 61 | CAPITAL LEASES AND LEASEHOLD IMPRVMTS. | | | | | | | | |
| 62 | INTANGIBLES | | | | | | | | |
| 63 | TOT TELEPHONE PLANT IN SERVICE (LINE 37) | | | | | | | | |
| | TARIFFED SERVICES PROVIDED TO NONREGULATED ACTIVITIES: | | | | | | | | |
| 64 | LOCAL SERVICE REVENUE (LINE 1) | | | | | | | | |
| 65 | LONG DISTANCE REVENUE (LINE 4) | | | | | | | | |
| 66 | MISCELLANEOUS REVENUE (LINE 5) | | | | | | | | |
| 67 | CORPORATE COMM EXPENSE | | | | | | | | |
| 68 | CORPORATE COMM INVESTMENT | | | | | | | | |

BELLSOUTH
COST APPORTIONMENT TABLES
TABLE SEVEN

| USOA PART 32 ACCT. | COST POOLS | BASIS FOR APPORTIONMENT TO COST POOLS | BASIS FOR APPORTIONMENT TO REGULATED/NONREGULATED | COST DEFINITION | COMMENTS |
|---|---|---|---|---|---|
| 6211 Analog Electronic Expense (Con't) | Common Use Equipment - Repair and Maintenance | Ratio of common use analog switching investment to total analog switching investment | Ratio of basic calls and of enhanced calls to total calls | Indirectly Attributable | |
| | Dedicated Use Equipment - Repair and Maintenance | Ratio of dedicated use analog switching investment to total analog switching investment | Ratio of dedicated regulated and of dedicated nonregulated analog switching investment to total dedicated analog switching investment | Indirectly Attributable | Ratios for apportionment to regulated/nonregulated are based on actual assignments of investment in dedicated use equipment to regulated and nonregulated activities. |
| 6212 Digital Electronic Expense | Direct Regulated/Nonregulated | Identified from field reporting or function codes | Directly assigned to regulated/nonregulated | Directly Assignable | This cost pool includes EA/NR. |
| | Packet Switching Common - Repair Maintenance | Ratio of common packet switching investment to total digital switch investment | Ratio of regulated and of nonregulated packets switched to total packets switched | Indirectly Attributable | |
| | Other Common Use Equipment - Repair and Maintenance | Ratio of common digital switching investment, excluding packet switching to total digital switch investment | Ratio of basic calls and of enhanced calls to total calls | Indirectly Attributable | |
| | Dedicated Use Equipment - Repair and Maintenance | Ratio of dedicated use digital switch investment to total digital switch investment | Ratio of dedicated regulated and of dedicated nonregulated investment to total dedicated digital switching investment | Indirectly Attributable | Ratios for apportionment to regulated/nonregulated are based on actual assignments of investment in dedicated use equipment to regulated and nonregulated activities. |

INDEX

1. GENERAL
2. ACCOUNT 6211 - ANALOG ELECTRONIC SWITCHING EXPENSE
3. ACCOUNT 6212 - DIGITAL ELECTRONIC SWITCHING EXPENSE
4. ACCOUNT 6215 - ELECTROMECHANICAL SWITCHING EXPENSE
5. ACCOUNT 6220 - OPERATOR SYSTEMS EXPENSE
6. ACCOUNT 6231 - RADIO SYSTEMS EXPENSE
7. ACCOUNT 6232 - CIRCUIT EQUIPMENT EXPENSE

GENERAL

1.01 The following accounts are the Central Office Equipment Expense accounts.

1.02 Dollars used in the processing of these accounts are extracted from FP through the CISSP interface file. The amounts associated with investment leased to others is retrieved from Table TMANAMT and assigned to CP99 as regulated. The CISSP balance is reduced by the amount of the CP99 assignment prior to other cost pool assignments.

1.03 Direct assignments for these accounts are made from Table TACCOUNT.

ACCOUNT 6211 - ANALOG ELECTRONIC SWITCHING EXPENSE

2.01 Account 6211 contains the expenses associated with analog electronic switching systems. It contains the cost of routine inspection and maintenance of analog electronic central office equipment, repairs of analog electronic central office equipment in the course of clearing trouble, and other maintenance of such equipment not chargeable to other accounts.

2.02 In addition to those listed in the General paragraph, the following inputs are used:

MTAS
CPAM
Table TDACAT
Table TUSOCSC

2.03 Account 6211 is divided into three cost pools as described in the following paragraphs.

2.03.1 CP01, Direct Regulated/Nonregulated, is not used.

2.03.2 CP02, Dedicated Use Equipment, is identified based on a ratio of dedicated analog switching investment to total analog switching investment. This ratio is determined by dividing the CPAM amount in Account 2211, CP04 SP02 through SP06, by the CPAM amount in Account 2211, CP01, CP02, and CP04, SP02 through SP06. CP02 contains the expense associated with analog electronic switching equipment which is identified as dedicated use for specific regulated/nonregulated activity.

1. SP01, Dedicated Repair Trouble Tickets Expense, is identified based on the total trouble ticket associated expense amount. This amount is determined by accumulating the trouble ticket report hours from MTAS and dividing the total by SRC 6211.1000 (77R) labor and engineering hours from CISSP to develop a trouble ticket ratio. A ratio of 1.0 will be used if the computed ratio is greater than 1.0. The CISSP amount to 77R is multiplied by the trouble ticket ratio to determine the trouble ticket associated amount. This amount is multiplied by the dedicated use ratio and the result is assigned to SP01.

2. SP02, Dedicated Use Maintenance Software Expense, is identified based on the maintenance software expense amount, which is determined by accumulating the CISSP amounts to SRC 6211.1000 (77M) with a JFCI of 4390. The maintenance software expense amount is multiplied by the dedicated use ratio and the result is assigned to SP02.

3. SP03, Dedicated Use Maintenance Service Order Expense, is identified based on the maintenance service order expense amount. This amount is determined by accumulating the CISSP amounts to SRC 6211.1000 (77M) with JFCI not equal to 4390 and an authorization that does not match one of the following formats:

| | |
|---|---|
| EA####&& | EA####Y& |
| &J###### | JJ###### |
| &J@@#### | JJ@@#### |
| &KC@#### | KKC@#### |
| &H@@#@## (SBT only) | &RECORDS |

&####### (SCB only)

where & = space
# = numeric
@ = alphanumeric
A = alphabetic

This amount is multiplied by the dedicated use ratio and the result is assigned to SP03.

4. SP04, Dedicated Use Repair and Maintenance Expense, is identified based on the 77M and 77R amounts that have not been assigned. These amounts are multiplied by the dedicated use ratio and the result is assigned to SP04.

2.03.3 CP03, Common Use Equipment - Repair and Maintenance, is identified based on the amounts assigned to CP02. It contains the expense associated with analog electronic switching equipment which is identified as joint use for both regulated and nonregulated activity.

1. SP01, Common Use Repair Trouble Ticket Expense, is identified based on the total trouble ticket associated dollars. The amount assigned to CP02 SP01 is subtracted from the total trouble ticket associated amount to determine the SP01 amount.

2. SP02, Common Use Maintenance Software Expense, is identified based on the maintenance software expense amount. The amount assigned to CP02 SP02 is subtracted from the maintenance software expense to determine the SP02 amount.

3. SP03, Common Maintenance Service Order Expense, is identified based on the maintenance service order expense amount. The amount assigned to CP02 SP03 is subtracted from the maintenance service order expense amount to determine the SP03 amount.

4. SP04, Common Use Repair and Maintenance Expense, contains the balance of the account.

2.04 Each cost pool of Account 6211 is assigned to regulated/nonregulated as described in the following paragraphs.

2.04.1 CP01 is not used.

2.04.2 Subpools of CP02 are assigned as described in the following paragraphs.

1. SP01 is assigned based on a ratio of MTAS nonregulated USOC quantity to total USOC quantity. The ratio is determined by extracting records from MTAS and comparing them against Table TUSOCSC to determine the nonregulated USOCs. The ratio is applied to the SP01 amount to allocate the nonregulated amount.

2. SP02 is assigned to regulated.

3. SP03 is assigned to regulated.

4. SP04 is assigned based on ratios of dedicated VMS and dedicated PTVM nonregulated investment to total dedicated investment. The dedicated VMS and PTVM amounts are obtained from SP04. The total dedicated investment equals the amount in Account 2211, CP04 SP02 through SP06. The dedicated VMS ratio is multiplied by the SP04 amount and the result is assigned to Product 107. The dedicated Public Coin ratio is multiplied by the SP04 amount and the result is assigned to Product 161. The balance of the subpool is assigned to regulated.

2.04.3 CP03 is assigned based on a Table TDACAT ratio representing nonregulated call volume to total call volume. The ratio is applied to the amount in the subpool and the result is assigned to Product 160. The balance of the cost pool is assigned to regulated.

ACCOUNT 6212 - DIGITAL ELECTRONIC SWITCHING EXPENSE

3.01 Account 6212 contains the cost of routine inspection and maintenance of digital electronic central office equipment and repairs of central office equipment in the course of clearing trouble.

3.02 In addition to those listed in the General paragraph, the following inputs are used:

MTAS
CPAM
Table TUSOCSC
Table TDACAT

3.03 Account 6212 is divided into five cost pools as described in the following paragraphs.

3.03.1 CP01, Direct Regulated/Nonregulated, is not used.

9.12.4

OCT 1 1991

3.03.2 CP02, Dedicated Use Equipment, is identified based on a ratio of dedicated switching investment to total digital switching investment. This ratio is determined by dividing the CPAM amount assigned to Account 2212, CP04 SP02 through SP11, by the CPAM amount assigned to Account 2212. CP02 contains the expense associated with digital electronic switching equipment which is identified as dedicated use for specific regulated and nonregulated activity.

1. SP01, Dedicated Repair Trouble Tickets Expense, is identified based on a trouble ticket report hours ratio. The ratio is determined by summing the trouble ticket report hours from MTAS, and dividing the amount by the total labor and engineering hours from CISSP in SRC 6212.1000 (377R). A ratio of 1.0 will be used if the computed ratio is greater than 1.0. The ratio is multiplied by the 377R amount to determine total trouble ticket associated dollars. The trouble ticket dollars are multiplied by the dedicated use ratio to determine the SP01 amount.

2. SP02, Dedicated Use Maintenance Software Expense, is identified based on SRC 6212.1000 (377M) with JFC Indicator of 4390. The result is the total maintenance software expense amount and is multiplied by the dedicated use ratio to determine the SP02 amount.

3. SP03, Dedicated Use Maintenance Service Order Expense, is identified based on the dedicated use ratio. All amounts to 377M not assigned to SP02 are accumulated if the authorization does not meet the following criteria:

| | |
|---|---|
| EA#####&& | EA####Y& |
| &J######& | JJ######& |
| &J@@#### | JJ@@#### |
| &KC@#### | KKC@#### |
| &H@@#@## (SBT only) | &RECORDS |
| &######## (SCB only) | |

where & = space
# = numeric
@ = alphanumeric
A = alphabetic

This amount is the maintenance service order expense amount. The dedicated use ratio is

applied to this amount to determine the SP03 amount.

4. SP04, Dedicated Use Repair and Maintenance Expense, is identified based on the dedicated use ratio. The 377M and 377R unassigned amount is the repair and maintenance expense. This amount is multiplied by the dedicated use ratio to determine the SP04 amount.

3.03.3 CP03, Packet Switching Common - Repair and Maintenance, is identified based on a ratio of packet switch investment to total digital switching investment. The amount assigned to Account 2212, CP03, is divided by the total investment in Account 2212 to develop the ratio. It contains the expense associated with digital electronic switching equipment which is identified as processor elements associated with asynchronous packet switching.

1. SP01, Common Use Packet Switching Trouble Ticket Repair Expense, is identified based on the total trouble ticket associated amount. The packet switch ratio is multiplied by the total trouble ticket dollars to determine the SP01 amount.

2. SP02, Common Use Packet Switching Maintenance Software Expense, is identified based on the maintenance software expense. The maintenance software expense is multiplied by the packet switch ratio to determine the SP02 amount.

3. SP03, Common Packet Switching Maintenance Service Order Expense, is identified based on the maintenance service order expense. The maintenance service order expense is multiplied by the packet switch ratio to determine the SP03 amount.

4. SP04, Packet Switching Common Repair and Maintenance Expense, is identified based on the repair and maintenance expense. The repair and maintenance expense is multiplied by the packet switch ratio to determine the SP04 amount.

3.03.4 CP04, Other Common Use Equipment - Repair and Maintenance, is identified based on the amounts assigned to CP02, CP03, and CP05. It contains the expense associated with digital electronic switching equipment which is identified as common use for both regulated and nonregulated activities.

1. SP01, Common Use Other Trouble Ticket Repair Expense, is identified based on the total trouble ticket associated dollars. The amount assigned to SP01 of CP02, CP03, and CP05 is subtracted from the total trouble ticket associated amount to determine the SP01 amount.

2. SP02, Common Use Other Maintenance Software Expense, is identified based on the maintenance software expense. The amount assigned to SP02 of CP02, CP03, and CP05 is subtracted from the total maintenance software expense amount to determine the SP02 amount.

3. SP03, Common Use Other Maintenance Service Order Expense, is identified based on the maintenance service order expense. The amount assigned to SP03 of CP02, CP03, and CP05 is subtracted from the maintenance service order expense amount to determine the SP03 amount.

4. SP04, Common Use Other Repair and Maintenance Expense, contains the balance of the account.

3.03.5 CP05, VMS Common Use Maintenance Software Expense, is identified based on a VMS common ratio. The amount assigned to Account 2212, CP06 is divided by the total investment in Account 2212 to develop the ratio. This subpool contains the expense associated with maintaining the Information Storage, Forward, and Retrieval investment.

1. SP01, VMS Common Trouble Ticket Repair Expense, is identified based on the total trouble ticket associated amount. The VMS common ratio is multiplied by the total trouble ticket dollars to determine the SP01 amount.

2. SP02, VMS Common Use Maintenance Software Expense, is identified based on the maintenance software expense. The maintenance software expense is multiplied by the VMS common ratio to determine the SP02 amount.

3. SP03, VMS Common Use Maintenance Service Order Expense, is identified based on the maintenance service order expense. The maintenance service order expense is multiplied by the VMS common ratio to determine the SP03 amount.

4. SP04, VMS Common Repair and Maintenance Expense, is identified based on the repair and maintenance expense. The repair and maintenance expense is multiplied by the VMS common ratio to determine the SP04 amount.

3.04 Each cost pool of Account 6212 is assigned to regulated/nonregulated as described in the following paragraphs.

3.04.1 CP01 is not used.

3.04.2 Subpools of CP02 are assigned as described in the following paragraphs.

1. SP01 is assigned based on a ratio of nonregulated USOC quantity to total USOC quantity. The ratio is determined by extracting records from MTAS and comparing them against Table TUSOCSC to determine the nonregulated USOCs. The amount assigned to SP01 is multiplied by the ratio and the result is assigned to nonregulated. The balance of the subpool is assigned to regulated.

2. SP02 is assigned to regulated.

3. SP03 is assigned to regulated.

4. SP04 is assigned based on ratios of dedicated CSL, VMS, PTVM, and TUG nonregulated investment to total dedicated investment. The VMS amount is obtained from Account 2212, CP04 SP06, the PTVM amount from SP07, the TUG amount from SP08, and the CSL amount from SP11. The total dedicated investment equals the amount in Account 2212, CP04 SP02 through SP11. The CPAM amount in Account 6212, CP02 SP04, is multiplied by each of these ratios and the result assigned to Products 168 (CSL), 107 (VMS), 161 (PTVM), and 108 (TUG). The balance of the subpool is assigned to regulated.

3.04.3 CP03 is assigned based on a ratio of the number of enhanced packets switched to total packets switched of all asynchronous ports from Table TDACAT. The ratio is applied to the CP03 amount and the result assigned to Product 102. The balance of the subpool is assigned to regulated.

3.04.4 CP04 SP02 and SP04 are assigned based on a ratio of nonregulated call volume to total call volume from Table TDACAT. The ratio is applied to SP02 and SP04

amounts and the result assigned to Product 150. The balance of the cost pool is assigned to regulated.

3.04.5 CP05 is assigned based on a ratio of the amount of nonregulated connect time to total connect time from Table TDACAT. The ratio is applied to the CP05 amount and the result assigned to Product 107. The balance of the cost pool is assigned to regulated.

ACCOUNT 6215 - ELECTROMECHANICAL SWITCHING EXPENSE

4.01 Account 6215 contains the cost associated with step-by-step central office equipment and crossbar switching systems. It contains the cost of routine inspection and maintenance of this equipment and repairs made in the course of clearing trouble. It also contains the expenses associated with other electromechanical switching systems not properly chargeable as step-by-step or crossbar.

4.02 No additional inputs are used in this account.

4.03 CP01, Electromechanical Expense, equals the entire account.

4.04 The entire account is assigned to regulated.

ACCOUNT 6220 - OPERATOR SYSTEMS EXPENSE

5.01 Account 6220 contains the expenses of routine inspection and maintenance of operator systems equipment, maintenance of operator systems equipment in the course of clearing trouble, and other maintenance of such equipment.

5.02 No additional inputs are used in this account.

5.03 CP01, Operator Systems Expense, equals the entire account.

5.04 The entire account is assigned to regulated.

ACCOUNT 6231 - RADIO SYSTEMS EXPENSE

6.01 Account 6231 contains the cost of routine inspection and maintenance of radio equipment and maintenance of radio equipment in the course of clearing trouble.

APPENDIX F
Re: Finding No. 11

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MEMO TO FILE

Prepared by: M. Majoros
Date: 9/3/93
Re: AT&T Price Restructure

During our meeting yesterday concerning MJM-10, i.e. generic upgrades, D. Craig discovered a copy of what appears to be a slide presentation given to BellSouth by AT&T concerning a price restructure which took place in April 1990. The presentation appeared to demonstrate that AT&Ts price restructure was basically retaining total cost but shifting cost from expense to capital, i.e. from software to hardware. The presentation cited to BellSouth concerns such as:

BellSouth Issues

- Expense budget tightly constrained.
- Profit regulation based on capital investment.
- FCC tightened accounting rules 1/1/88 to require expensing of all RTU fees.
- 5ESS allocates too much of its cost to BellSouths marketing most competitive customers.

REQUEST: Provide all correspondence associated with the AT&T price restructure for the 5ESS$^{R}$ and software.

RESPONSE: Attachment 1 is all the correspondence that could be found in the Company's files which was associated with the AT&T 5ESS$^{R}$ price restructure.

INFORMATION PROVIDED BY: Frances Dennis
Operations Manager
675 West Peachtree St.
Atlanta, GA 30375



BellSouth Services

Mr. F. S. Topor
Vice President - Network Systems Sales
AT&T Network Systems
475 South Street
Morristown, New Jersey 07962-1976

Item 118
Attachment 1
Page 1 of 10

Dear Mr. Topor:

5ESS growth costs have been a major topic of discussion between BellSouth and the AT&T Southern Region for some time. Your current pricing strategy appears to be to offer a very competitive price for a new switch but results in pricing as much as 36% above new costs for additions.

Of equal importance is our concern with AT&T's feature software pricing policy. We believe that your pricing for feature software is unacceptably high. This conclusion is based on the following observations:

1) Features on the 5ESS have been found to cost frequently up to two to three times as much as similar features on the 1AESS.

2) Features on the 5ESS nearly always cost more than similar features on other vendors' switches.

3) Feature software pricing is often higher than our Lines of Business organization finds acceptable for competitively marketing services in BellSouth.

One key element appears to be per Switching Module pricing of software. This policy tends to drive not only software, but overall growth costs as well, above reasonable levels. Although our current contract with AT&T provides for capping of some software at 35 Switching Modules, we feel that this does not even begin to address the issue. We believe that all software in the 5ESS should be capped at 10 Switching Modules.

We ask your assistance in addressing these issues. AT&T has a very good product in the 5ESS. We don't want to see economics hinder our ability to continue deployment of the 5ESS.

Sincerely,

Executive Vice President-
Marketing, Network
and Planning

Vice President-
Procurement, Property and
Services Management



A BELLSOUTH Company

CONCURRENCE BEFORE SIGNATURE

NOVEMBER 1989 LETTER ON 5ESS GROWTH COSTS AND SOFTWARE PRICING POLICIES.

TO: Mr. F. S. Topor
Vice President
AT&T Network Systems

FROM: Mr. J. A. Drummond
Executive Vice President
BellSouth Services

Operations Manager-
COE Products and Services

Operations Manager-
Procurement

Director-
Equipment Engineering Support
11/7/89

Assistant Vice President-
Procurement, Product Planning
and Contracting

Assistant Vice President-
Network Provisioning

Vice President-
Procurement, Property and
Services Management

Vice President-
Network Strategic Planning

AT&T Network Systems

F. S. Tapor
Vice President
Network Systems Sales

Western Electric® products
475 South Street
Morristown, NJ 07960
201 631-6200

February 8, 1990

MR. C. S. BOREN
Vice President - Procurement,
Property and Services Management
BellSouth Services
4515-675 West Peachtree Street, N.E.
Atlanta, Georgia 30375

Dear Mr. Boren:

We wish to apologize for the delay in answering your November letter concerning 5ESS(R) Switch prices, but we wanted to have a positive reply to your concerns and it has taken since then to convert your comments and suggestions into an action plan.

1989 proved to be a productive year for enhancing the BellSouth/AT&T Network Systems relationship. We both now have a better understanding of each others needs and desires in the area of switching products. On January 1, our two companies implemented a new contract for the purchase of the 5ESS Switch. In that contract AT&T responded to BellSouth's well documented concerns about the 5ESS Switch's competitive position on first costs mainly focusing on the forthcoming 1AESS(tm) Switch replacements. Our two staffs are currently working to expand that contract for 1990 to include an increased commitment in exchange for certain considerations desired by BellSouth.

Our Switching Product Management has listened to the many concerns BellSouth has expressed about 5ESS Switch growth prices and software price concepts and we would like to offer a new 5ESS price structure as a part of our 1991 Commitment Contract. Assuming that the level of business in 1991 is similar to our previous levels of business, we expect to provide BellSouth with the new 5ESS price structure for orders received after July 1, 1990 and shipping in 1991, with additional changes scheduled in the 5E7 generic program time frame.

Some major aspects of this restructure which we feel will address your concern about 5ESS Switch growth cost are:

1. We have accepted BellSouth's suggestion and we will have a cap for base generic software at 10 Switch Modules.

2. BRCS will be repackaged into groups of features more in line with BellSouth's needs with very attractive pricing.

3. We will begin to move from per Switch Module pricing to per Line or per Switch for new software features beginning in the 1992 time frame (5E7). Overall, software prices for a typical new office or switch module growth will decrease.

4. Our BellSouth list hardware prices will be realigned to better match growth patterns (i.e., the Switch Module prices will decrease and the analog Line Unit and cards will increase.) The total hardware prices for a typical fully equipped Switch Module will increase but the software will decrease.

5. The mix between capital and expense dollar prices for a 5ESS Switch will change with expense decreasing and capital increasing, but the average bottom line switch system price will remain consistent with the previous 5ESS price plan.

Some details about this restructure have not been completed at this time, but Al Basey and I are willing to discuss these changes with you when we meet on February 15 and 16, 1990, to present the CO 2000 Story. Also, Joe Mauriello will be requesting a meeting with BellSouth Purchasing in March to present the complete price restructure plan. I know you will find it very satisfactory.

We have also made excellent progress this year in the area of 5ESS features. BellSouth's creation of one unified list of desired features has helped us greatly in clearly focusing on BellSouth's most important software needs. We completely understand your concerns about the effect that the price of our features have in regard to your ability to generate tariffs that are within the range of your customers willingness to pay. We have suggested that an indication in some manner of the customers willingness to pay or a target software cost element input to the tariff would be a valuable addition to the BellSouth feature priority list. Also, we continue to be interested in working with you to evaluate and implement a way to take advantage of revenue sharing.

The comparison of the 5ESS feature software prices to the 1AESS Switch and to other vendor's prices is most difficult to reconcile. We attempt to price 5ESS features based on their development costs and their value added. Other vendors may have an entirely different philosophy.

The pricing of 1AESS features was set many years ago under a different price policy which has set precedents that are difficult to change at this stage of the 1AESS switch life cycle. The difference in 1AESS and 5ESS switch technology and life cycle stage also affect software pricing.

We have been addressing this concern and you may have noticed recently that new features developed in both 1AESS and 5ESS are priced more consistently and we frequently offer a buy out price that covers both 1AESS and 5ESS.

We consider the 5ESS Switch to be a premier product designed for the 90's that will carry our customers well into the 21st century with SONET, Broadband and Photonic capabilities. Our switch has significant added value not found in any competitive product and we believe that the slightly higher price is a fair return for the increased benefits available to BellSouth by its implementation into your network.

Let me assure you again that Joe Mauriello and his staff have made me and the entire Switching Product Management Organization very aware of the concerns voiced in your recent letter as well as your previous letters on the availability and costs of 5ESS special features. AT&T Network Systems wants to be BellSouth's major switch vendor and we will remain price competitive considering our added value. We are confident that our differences can be resolved to our mutual satisfaction. I look forward to personally discussing this issue with you when we meet on February 15 and 16.

Sincerely,

Letter to:
C. S. Boren - BellSouth Services, Atlanta
J. A. Drummond - BellSouth Services, Atlanta

AT&T
Network Systems

J. M. Mauriello
Regional Vice President
(Southern)

6701 Roswell Road, N E
Atlanta, GA 30328
404 573-7000

June 12, 1990

JUN 1990
REC...
OF...
G. G...

MR. C. S. BOREN, Vice President
Information Resources & Technology Planning
BellSouth Services
4515 Southern Bell Center
675 W. Peachtree St., NE
Atlanta, GA 30375

Re: Announcement of 5ESS(R) Switch Price Restructure Plan

Dear Mr. Boren:

AT&T Network Systems - Switching Division is pleased to announce a change in the Pricing Structure for the 5ESS Switch. In recent meetings with your staff and other BellSouth organizations, we have provided indepth information on this restructure, and we have shown how the Price Restructure Plan will enhance your ability to model, price, and order new growth 5ESS Switch purchases. These meetings were planned in advance of this formal announcement to promote better communication and understanding.

The Price Restructure Plan incorporates several changes designed to address concerns expressed by your purchasing and network planning organizations in the areas of budgeting, long term planning, and new service introduction. The result will be to improve the 5ESS Switch purchase process and ultimately improve your product and service offering profit margins.

Based on input from your purchasing and network planning organizations, the price restructure plan includes four elements:

Changes in the Hardware and Software Price Balance. The Price Restructure Plan changes the amount of dollars spent on hardware components versus software RTU fees, allowing greater latitude with capital and expense budgets. This change will more closely align with your construction budget, and is aimed at providing more flexible spending.

Per Office Pricing for the 5ESS Switch Base Software Fee. The Base Software fee will no longer be priced on a per-switching module basis. One base software fee will be charged per central office. This per office fee is based on an office sized at ten Switching Modules. Offices with less than ten SMs will be charged proportion-



Western Electric® products

ately less for the base fee, and additional (above 10 SMs) Switching Modules added to the switch subsequent to initial purchase will not be charged any additional base software fee. This change is aimed at reducing your growth expenses, and making it easier to plan for providing new services in the network.

Realignment of 5ESS Switch ERCS Offerings. The robust set of 5ESS Switch ERCS Offerings are now realigned into three packages to improve ordering procedures and enhance marketability. The new packages are called Universal ERCS, ERCS Centrex (ESSX) and ERCS Extended Centrex (ESSX). The contents of each package were determined based on customer ordering patterns, and are designed to provide you the best choice for an individual 5ESS Switch. In addition, the Price Restructure Plan includes a new reduced price for the ERCS Centrex (ESSX) package. Finally, pricing for the three ERCS packages will now be on a per line basis, providing maximum flexibility to introduce new services.

Discount Structure Simplified. Realigning the hardware and software price mix, and repackaging the ERCS Offerings results in the need for fewer price adjustments to determine the bottom-line price for a 5ESS Switch. These changes will simplify switch modeling, and will make your purchase procedures easier.

Our goal is to incorporate your budget and planning issues into the standard price models, and move the 5ESS Switch plan into alignment with your current and future switch purchase plans. The Price Restructure Plan is not a general price increase, and bottom-line prices will generally remain the same.

The Price Restructure Plan takes effect in two steps, on January 1, 1990, and with the introduction of the 5E7 Generic (4Q91). All current contracts remain intact and will not be affected by the new plan.

As we begin discussions about the 1991-1992 contract, the 5ESS Switch Price Restructure is timely and provides a responsive cornerstone for BellSouth's needs.

Sincerely,

Copy to:
J. A. Drummond - BellSouth Services, Atlanta
W. M. Ferguson - South Central Bell, Birmingham
G. Giovanni - BellSouth Services, Atlanta
R. K. Snelling - BellSouth Services, Atlanta

RECEIVED

July 20, 1990

MEMORANDUM

TO: W. D. Sweet, Operations Manager - Product Manager and Contracting (BSS)

FROM: H. H. Puckhaber, Operations Manager - Network Program Planning (SBT)

RE: 1991 AT&T 5ESS Digital Switch Contract

The Southern Bell area planners have discovered some disturbing information from the new edition of 5EDOPS, the AT&T Ordering and Pricing system. Essentially, it appears that hardware pricing, thus capital associated expenditures, have increased dramatically. Since 5EDOPS is a national tool, BellSouth discounts are not included. Our prices, therefore, might not be subject to the apparent adverse increases when we agree to the 1991 contract.

Our concern is that AT&T may be reacting inappropriately to the concerns expressed concerning software pricing, and that their pricing may be shifting money from software to hardware. While we are attempting to have software priced more economically, it must not be done by increasing hardware costs.

As soon as you have a specific information on the new 1991 discount structure, we would appreciate your analysis of the apparent increases in 5EDOPS.

Questions may be referred to Ken Parker at 529-0522.

cc: S. A. Mulcahy, E. W. Stevens, W. N. Ware, Area Planners

August 23, 1990

To: E. M. Zier
Operations Manager
COE Products and Services

From: W. D. Sweet
Operations Manager
Procurement, Product Planning and Contracting

Subject: 5ESS™ Contract

We are in complete agreement with your memo of August 7, and are very aware of the problems associated with the absence of an arrangement for 1991 business, not only with AT&T but NTI and Stromberg Carlson as well.

As stated in your memo, Procurement did not receive AT&T's complete proposal until July 18, 1990. We have already negotiated improvements to the original proposal, however, should we accept their proposal as it stands today BellSouth would experience a price increase, additional commitment requirements, and new restrictions in our business arrangements with AT&T.

It is our understanding AT&T is providing Firm Price Quotes on initial jobs and growth jobs of 3 switch modules or greater during this period. The remainder of the jobs must be estimated as stated in your memo.

I do not understand Mr. Hester's closing statement. The current agreement covers 1989 and 1990. There was no period of time this year when we were without a contract.

Please be assured we will finalize the best obtainable agreement at the earliest possible date with AT&T.

If there are any questions please contact me or Steve Manion at 420-2140 or 420-2389, respectively.

W. D. Sweet

8



BellSouth Services

January 4, 1991



Mr. R. C. Harper
Contract Negotiations Manager
AT&T Network Systems
6701 Roswell Road, N. E.
Atlanta, GA 30328

Dear Bob:

In response to your verbal request, BellSouth anticipates accepting AT&T's revised 5ESS(R) Switch Contract Proposal for 1991, dated October 30, 1990. Our intent is to accept the proposal, at commitment level 3, along with the subsequent modifications that have been agreed to, such as the 14.5% growth discount, the digital line adjustment, 1A processor trade-in, etc. Our acceptance is contingent upon satisfactory resolution of, but not limited to, the following issues:

1. Continuation of 5EDOPS at no charge.
2. Plug-in repair costs.
3. Modification of features included in the Core Package Software

We appreciate AT&T's diligence in working towards completion of the final 1991 Agreement. Please contact me on 420-6052, if you should have any questions or comments.

Sincerely,

Veronne H. Williams
Senior Contract Manager

Copy to: W. D. Sweet
S. F. Manion
M. E. Ward



A BELLSOUTH Company

REQUEST: Why did BellSouth request AT&T address the following issues:

1. 5ESS growth costs, and
2. AT&T's pricing of feature software.

RESPONSE: 1. Growth costs refer to dollars spent adding lines, trunks, software upgrades, and new software features to 5ESS$^{R}$ digital switches embedded in our network.

Competition between Switch Suppliers for the initial switch replacement provides the necessary cost containment on the "initial first cost". Once the switch is in the network, growth requirements can only be provided by the original equipment manufacturer and no competition exists.

Although the switch selection decision is based on overall "life cycle cost" BellSouth continuously strives to reduce the growth costs associated with switching equipment.

2. As stated above, BellSouth was striving to reduce growth costs. Software RTU Fees are a major part of growth costs. AT&T's method of pricing (per switch module) for many features in the 5ESS$^{R}$ resulted in higher RTU fees than similar features deployed in other technologies in the network.

INFORMATION PROVIDED BY: Frances Dennis
Operations Manager
675 West Peachtree St.
Atlanta, GA 30375

REQUEST: If AT&T had responded favorably to all of BellSouth's concerns, please explain the effects and implications on Southern Bell's ratepayers and unregulated services.

RESPONSE: Even though this is a hypothetical question, the Company will attempt to answer it in order to be responsive. The Company was requesting these pricing changes in order to control growth costs and help maintain stable rates. Any price changes in switch investment or related software would be reflected in future cost studies. However, changes in any single cost component would not necessarily materially impact the price of individual services.

INFORMATION PROVIDED BY: Frances Dennis
Operations Manager
675 West Peachtree St.
Atlanta, GA 30375

REQUEST: What did AT&T ultimately do to meet BellSouth's request?

1. Explain the method AT&T used to resolve the points at issue.

2. Explain and demonstrate the effects and implications of this resolution on Southern Bell's ratepayers and unregulated services using an actual example.

RESPONSE: 1. Although BellSouth cannot answer for AT&T, the Company will attempt to summarize the process which occurred. As part of the typical procurement process, BellSouth's November 1989 letter on 5ESS$^{R}$ growth costs was the beginning of a series of negotiations between the Company and AT&T.

AT&T's 5ESS$^{R}$ price restructure was implemented nationwide and was not unique to BellSouth. Furthermore, AT&T's price restructure only impacted a small subset of list prices. The negotiations referred to above were BellSouth's efforts to obtain the best contract on 5ESS$^{R}$ hardware and software. This included an attempt to maximize discounts off AT&T's list prices based upon BellSouth's business volume.

The culmination of this negotiation process was an increased discount off list price for BellSouth.

2. The AT&T 5ESS$^{R}$ Price Restructure only affected the LIST PRICE of a small subset of items normally ordered on growth jobs. However, as discussed in # 1 above, the resulting negotiations did result in an increased discount off list price for BellSouth.

It is not practical to provide an actual representative example since each individual growth job has unique software/hardware requirements. However, in an attempt to be responsive, see the response to Item 118C for additional discussion.

INFORMATION PROVIDED BY: Frances Dennis
Operations Manager
675 West Peachtree St.
Atlanta, GA 30375

REQUEST: Provide a complete explanation of 5E7 and a list of offices where it is installed.

RESPONSE: Software Release 5E7 is a designation used by AT&T to identify a particular generic upgrade. Release 5E6 would indicate the previous upgrade and Release 5E8 would be the designation for the next upgrade. AT&T traditionally rolls out one upgrade per year. An analogy for a software release upgrade in a central office would be LOTUS 123 or WORDPERFECT upgrades in a Personal Computer. Each upgrade provides new or improved features and functionality in addition to corrections identified in the previous release.

Georgia has thirty three (33) 5ESS$^{R}$ Host/Standalone Central Offices in the network. Only four offices are on release 5E7. They are as follows: Chamblee Main, Columbus NW, Dunwoody, and Toco Hills.

INFORMATION PROVIDED BY: Frances Dennis
Operations Manager
675 West Peachtree St.
Atlanta, GA 30375

REQUEST: A February 8, 1990 letter to Mr. C. S. Boren, V.P.-Procurement, Property and Services BSS from J. S. Topor V.P. AT&T Network Systems Sales mentions the concept of "revenue sharing."

1. Please explain the concept of revenue sharing as used in this letter.

2. Explain BellSouth's response to AT&T's proposal to implement revenue sharing.

RESPONSE: 1. Although BellSouth cannot answer for AT&T, the Company will attempt to answer the question in order to be responsive. Based upon the Company's interpretation of AT&T's intent, we believe this AT&T proposal was referring to some kind of deferred payment schedule for 5ESS® software Right To Use fees based upon BellSouth's market penetration.

BellSouth did not pursue any type of revenue sharing with AT&T. It is BellSouth's policy to pay for Right To Use fees prior to deployment of any features in the network.

2. BellSouth did not pursue revenue sharing with AT&T. Revenue sharing was not implemented in our contract agreement with AT&T for switching equipment.

INFORMATION PROVIDED BY: Frances Dennis
Operations Manager
675 West Peachtree St.
Atlanta, GA 30375

REQUEST: Regarding 2/8/90 letter to Mr. C. S. Boren from Topor.

1. Please explain the following statement "In that contract AT&T responded to BellSouth's well documented concerns about the 5ESS Switches competitive position on first costs, mainly focusing on the forthcoming 1AESS (tm) Switch replacement."?

2. Please identify the "certain considerations" discussed in the last sentence of the second paragraph on page 1.

3. Please explain the following statement 2. BRCS will be repackaged into groups of features more in line with BellSouth's needs with very attractive pricing.

4. Please provide a copy and explanation of BellSouth's "unified list of desired features" (page 2).

5. Please explain the following statement:

> We completely understand your concerns about the effect that the price of our features have in regard to our ability to generate tariffs that are within the range of your customers willingness to pay.

6. Please provide all "previous letters on the availability and costs of 5ESS special features" discussed on page 3.

RESPONSE: 1. Although BellSouth can not answer for AT&T, the Company will attempt to answer the question in order to be responsive. Based upon the Company's interpretation of AT&T's intent, we believe that AT&T was referring to BellSouth's concerns about the competitiveness of the initial cost of the 5ESS$^{R}$ switch as it replaced the 1ESS switch.

2. Although BellSouth can not answer for AT&T, the Company will attempt to answer the question in order to be responsive. Based upon the Company's interpretation of AT&T's statement, we believe it refers to additional discounts requested by BellSouth (considerations) in return for an increased commitment of business to AT&T.

3. At this time, Business Residential Custom Services (BRCS) was offered only in packages (groupings of individual features). AT&T's statement refers to the regrouping of these packages into smaller packages and in some cases individual feature offerings. This allowed BellSouth to purchase smaller packages more in line with its needs.

4. Although BellSouth can not answer for AT&T, the Company will attempt to answer the question in order to be responsive. Based upon the Company's interpretation of AT&T's reference, Attachment 2 will show a "unified list of desired features". This information will be made available for review at a mutually agreeable time and place. The list is a comprehensive feature priority list for the 5ESS$^{R}$ and 1AESS switches. These lists were developed to help communicate our feature development requirements and priorities to major vendors such as AT&T.

5. Although BellSouth can not answer for AT&T, the Company will attempt to answer the question in order to be responsive. Based upon the Company's interpretation of AT&T's statement, we believe AT&T was stating that they understood that the cost to deploy some features in the 5ESS$^{R}$ could cause our tariffs to be higher than our customer's willingness to pay.

6. BellSouth Procurement is unaware of "previous letters" from Mr. Boren to AT&T addressing availability and costs of 5ESS$^{R}$ special features. BellSouth's concerns with respect to high growth costs including software features has been expressed to AT&T in many different forums (eg., meetings, contract negotiations, etc.).

INFORMATION PROVIDED BY: Frances Dennis
Operations Manager
675 West Peachtree St.
Atlanta, GA 30375

118 G4
Attachment 2
P1 of 12



BellSouth Services

D. W. Jones
Assistant Vice President
Network Planning

675 West Peachtree Street, N.E.
Atlanta, Georgia 30375
404 529-0815

August 24, 1989

Mr. J. R. Griser
Sales Director - Switching
AT&T Network Systems
300 Chase Park South
Birmingham, Alabama 35244

Dear Mr. Griser:

Development of timely, cost effective software for our network switches is of prime importance to BellSouth. At divestiture, BellSouth formed an interdepartmental intercompany Switch Feature Evaluation Committee (SFEC) whose only purpose was to establish priorities for vendor software development. Until now, the SFEC only set priorities for miscellaneous central office features and for features requiring relatively small development effort. Priorities for features requiring large development efforts such as Integrated Services Digital Network (ISDN), Common Channel Signaling (CCS7), and Custom Local Area Signaling Service (CLASS) were set by individual project teams. These feature priorities were conveyed to AT&T separately in meetings and various correspondence.

In our regularly scheduled November 1988 meeting between the BellSouth SFEC and AT&T Network Systems, the need for a single priority feature list was recognized. Following that meeting, the SFEC began the process of reevaluating nearly 1200 feature requests including a host of ISDN, CCS7, and CLASS features. Those features that were determined to be of high interest to BellSouth were further evaluated and priorities established for each feature consistent with our corporation's marketing and network strategies.

Attached, you will find the BellSouth feature priority lists for the 5ESS and 1AESS switches. These lists indicate the rank for each feature, the Bellcore TA-TSY-000185 reference where available,

feature title, BellSouth contact, Bellcore reference documents where available and the desired general availability date. Descriptions for the attached features may be found in the associated technical requirements documents. For features without current requirements, a brief description of the feature may be found in TA-TSY-000185. Descriptions for features not yet in TA-TSY-000185 will be provided to you as they become available.

It is important to note that our interest in many of these features is predicated upon availability by the date indicated. In some cases, later availability may decrease our interest. In determining our interest and priorities in these features, no consideration was given to the cost of development. Feature prices out of line with our customer's willingness to pay may decrease our interest in these features as well. A date of 01/01/99 is shown for any feature where a desired general availability date was not available.

For these reasons, it is important that an ongoing dialogue be established between our subject matter experts. It is our intention to revise and reissue this list semiannually in April and October with follow-up meetings in May and November. Ad hoc meetings, conference calls, etc., between our subject matter experts will take place throughout the year to review requirements, proposed availability dates, planning prices, etc., and to determine the final disposition of each feature. It is expected that some features will be removed from the lists because of lower interest due to cost, newer evolving technologies and missed market windows. Conversely, new features will be added to the lists as new market opportunities arise and new technologies become reality.

Presentation of these lists do not represent any commitment by BellSouth or any of it's subsidiaries to purchase any product whether or not it provides any of the capabilities or features presented on the lists. Commitments to purchase any of these features must be secured through the BellSouth Services purchasing and contracting organization.

Within the next few days, a representative of our SFEC will be contacting your representatives to make meeting arrangements to allow our SFEC to formally present the list and establish a framework for future dialogue.

I believe that these new priority feature lists and the process we have implemented within BellSouth to develop them, will help us to better communicate our feature development requirements to AT&T Network Systems. If you have any questions please call me on 404-529-0815. If your associates should have any questions about the list they may call Jim Bridges at 205-977-7177 or the BellSouth contact if the question pertains to a specific item on the list.

Yours truly,

D. W. Jones
Assistant Vice President - Network Planning

REQUEST: Regarding letter to Mr. F. S. Topor from C. S. Boren.

1. Why no date?

2. Why no signature of Executive Vice President - Marketing, Network and Planning?

3. Provide copy of actual signed letter sent to Topor.

4. Provide documentation from lines of Business organizations which underlie item 3 in letter.

RESPONSE: 1. It appears that the date was inadvertently omitted from the letter. Typically, executive letters are not dated until after the letter has circulated among the levels of management for concurrence and been signed by the executive(s). In this case, the date was inadvertently omitted after the letter was signed. However, the concurrence sheet (see Attachment 1) indicates the letter was sent in November, 1989.

2. The correspondence which had been provided earlier to members of the audit team was actually a copy of the letter before it was signed by the Executive Vice President-Market, Network, and Planning.

This particular copy was obtained from the Procurement organizations' files. The Procurement file copy only had their Vice President's signature and did not include the Executive Vice President's signature from the other involved departments.

3. See Attachment 1 for a copy of the actual signed letter.

4. This was a broad and ambiguous question. However based upon our interpretation of the question, selected representatives from the lines-of-business organization (including those most likely to have responsive documentation) searched their files and found no responsive documentation.

INFORMATION PROVIDED BY: Frances Dennis
Operations Manager
675 West Peachtree St.
Atlanta, GA 30375

# INITIAL SWITCH COMPARISON
# 1989 VS 1991

| | 1989 SWITCH | 1991 SWITCH |
|---|---|---|
| ANALOG LINES | [redacted] | [redacted] |
| DIGITAL LINES | | |
| ISDN LINES | | |
| TOTAL LINES | | |
| TRUNKS | [redacted] | [redacted] |
| ANALOG LINE UNITS | [redacted] | [redacted] |
| DIGITAL LINE UNITS | | |
| SWITCH MODULES | | |
| SOFTWARE RELEASE | 5E5 | 5E6 |
| MAJOR SW FEATURES | CENTREX<br>CCS7 | CENTREX<br>CCS7<br>ISDN<br>TOUCHSTAR<br>RINGMASTER |
| LIST PRICE HARDWARE | [redacted] | [redacted] SEE NOTE 1 |
| LIST PRICE SOFTWARE | | |
| LIST PRICE MATERIAL | | |
| NET PRICE HARDWARE | [redacted] | [redacted] |
| NET PRICE SOFTWARE | | |
| NET PRICE MATERIAL | | |
| % EFFECTIVE DISCOUNT | [redacted] | [redacted] |
| COST PER LINE | [redacted] | [redacted] |

NOTE 1 : THIS COLUMN EXCLUDES ISDN HARDWARE AND ISDN, TOUCHSTAR, AND RINGMASTER RTU FEES

PRIVATE/PROPRIETARY/LOCK
CONTAINS PRIVATE AND/OR PROPRIETARY INFORMATION.
MAY NOT BE USED OR DISCLOSED OUTSIDE THE BELLSOUTH
COMPANIES EXCEPT PURSUANT TO A WRITTEN AGREEMENT.
MUST BE STORED IN LOCKED FILES WHEN NOT IN USE.

Don Craig

(Unidentified Speaker): December 13, 1993. Interview with Sid Boren, with Don Craig, Mike Majoris, Michele Young, Steve Manion. Regarding BellSouth's negotiations with switch vendors during the 1989-90 time frame.

Michael Majoros

(Unidentified Speaker): I'd just like to say that the purpose of this interview is to help us understand some information and correspondence that we've received regarding the 1991 AT&T price restructure and I'm just gonna go straight to the questions.

Q: In your capacity, I believe you were the Vice President of Procurement of BSS back in that time period

A: Yes, that's correct.

Q: And how would constrained expense budgets impact BellSouth's negotiations with switch vendors?

A: Constrained expense budgets? I ...

Q: Yes Sir. Or would constrained expense budgets impact BellSouth's negotiations with switch vendors.

A: Well, the reason I had asked for clarification I guess is the term constrained expense budgets is one that I'm not familiar with the terminology of the company that you're referring to. In an attempt to have a lower expense budget we have a budgeting process, we don't call it a constrained expense budget, but, most of the switch purchases... switch purchases drive both expense and capital, so what you try to do is look at the total cost of the machine which involves both expense and capital. Try to move to product life cycle type cost rather than trying to analyze whether it's expense or capital.

But the motivation for the purchaser is to always try to get the lowest price if that's what you mean.

Q: Alright, so would constrained, uh, tight expense budgets have an impact on your decisions, on your negotiations with the switch vendor within the context of the total life cycle approach?

A: Well, only... I mean its... the negotiation process with any of our vendors is an attempt by us to make the cost of the product that we buy as low as possible. And I've been in the company for 25 years and every year we have a budget, an expense budget and a capital budget and I guess maybe I'm not understanding the nature of your question or something, but obviously we try to get as good a price as we can. There was no single event... I don't... maybe I'm not understanding the question properly.

Q: Alright. Uhm, let's move on to the next one then. Would rate of return regulation have an impact on your negotiations with switch vendors?

A: Well, no, I mean again, the rate of return regulation is a way that, I'm just thinking out loud, it's the method that all regulation ultimately is based on. We've got a variety of plans around the company in the states that we're in, but in one way or another they're all tied to a rate base rate of return calculation. But in terms of how that's related to the negotiation of a switch, again it gets back to an attempt to get the lowest possible cost for the switch and that's related

to, I guess in a way, the rate base rate of return regulation because expense is certainly a, and capital, are both products of that, but again, the question is puzzling.

Q: Alright, I'll try to move along here as quickly as possible.

A: I'm trying to be responsive, I think maybe we have a slight different terminology or something because it's really, I don't feel like I'm answering your questions properly, and yet, anyway, let's continue.

Q: How would, and these are hypotheticals, I'm just, how would tightened accounting rules requiring the expensing of all RTU fees impact BellSouth's negotiations with switch vendors.

A: Well, the connection wouldn't be direct, I guess, and I don't understand again the connection. In the negotiating process for purchasing products the things you've mentioned are not directly related. In the negotiation for the purchase of a product, you've got competitive situations, you've got history that you can look back on, you've got a bid process, you've got business cases that you prepare and all of that but none of them are related to your line of question directly that I'm familiar with.

Q: Okay. Would tariff concerns impact your negotiation with vendors and specifically, one group of tariff customers versus another or one type of tariff versus another.

A: I'm not sure I know what you mean by tariff considerations but in the negotiating process we never got involved in the tariffing process.

Q: Okay.... I'm cognizant that we only have an hour and that's why I'm trying to do this as quickly as possible. Could you explain to us what the background was, and I take it you were the chief negotiator, what the background was prior to the restructure and what things were going on in and outside the company which would have precipitated the need for the price restructure that AT&T did.

A: Well, a couple of things. Chief negotiator has different connotations so let me respond to that first. My organization was responsible for the procurement process. I didn't do any negotiating myself. But my organization was responsible for it so maybe that's a technicality but again I don't know the context of your question so that, maybe clarify that first. The price restructure, maybe we better, I don't really relate to exactly that event, maybe you need to brief me or they can exactly what you're referring to.

Q: Uhh, What I'm referring to is basically these, we have these, some of this correspondence between you and Mr. Topor and it resulted in a price restructuring, then I guess ultimately a purchase of switches.

A: When you say restructure, what does that mean to you. I mean, I want to make sure of our... I don't know the term restructure, what definition of that?

Q: Uhm, Well, I will say that to me what I see in these documents is it means that what AT&T said it was going to be is a shift in price from expense to capital.

A: I don't, I don't, I don't understand that kind of distinction I guess is why I wanted you to define the term price restructure because in our discussions with the vendor community including AT&T our motivation is always to reduce the price, consistent with what their competition is doing, what our markets are doing, and the term restructure or shift from expense to capital is not an event that is meaningful in my world.

Q: Do you try to fit the negotiations or your vendor requests for quotes to your expected budget for expense or capital?

A: Not, not, ... The way we go about it not like that. Now that may be an end result, but that's not the process we go through. The process we go through is we have in our engineering organization continuing studies about replacement and growth needs, which you're very familiar with, then we have in the procurement organization ongoing discussions with the vendor community with regard to the price performance curves in the industry. So we try to group switches, we try to make vendors compete with each other, we try to package purchases, we disaggregate sometimes purchases. We try to do everything we could, in those times, and I'm sure they continue to, to get the price performance for the product as low as we possibly can. Then that becomes a more or less fixed amount. Then you have your studies over here that show the breaking point for when you can replace or add based on that particular price. But as far as starting it out the way

you're describing, we don't; and it's not associated in the way your question set it up. I mean, it's just not the way to do it. So whether it's expense or capital is a byproduct, not a negotiating point, I guess, is the answer.

Q: One of the things that was evident from these documents, what Steve and (_____?_____) were talking about is one of your goals apparently was to reduce, having AT&T to reduce it's software and growth costs...

A: Yes.

Q: ... above all else.

A: Not only AT&T but other vendors as well. We felt like we were becoming a product of the Gillette razor syndrome, give us the razor for nothing then sell us all the blades you can at exorbitant prices. So, we... In the world of technology that we live in, the software pricing becomes very very important because that's the platform that most of our products and services are ultimately based on, so I was very concerned, still am as a matter of fact, about right to use fees and recurring software costs. It's a really, we have to be real careful that we don't mortgage our future by locking into exponentially increasing software costs, because they should be decreasing as the software research and development is written off.

Q: Are you familiar with this August 24 letter to Mr. Grieser and, you didn't sign this, it's signed by E. W. James.

A: Jones.

Q: Jones, pardon me.

A: I would have to read it, I haven't seen it.

Q: He makes a reference here. And this is about the first, he says that, and here we're talking about software cost, and in determining our, and this is that unified list of priorities, he says, in determining our interest in priorities in these feature no consideration was given to the cost of development. Does that mean that, uh, what does that mean, do you know?

A: I don't know. I mean, I'm sure it would become evident in the context of the whole letter but I don't know, I haven't seen the letter until you just read it to me.

Q: You haven't seen this letter?

A: Well I mean I may have but I don't remember it. When was it written?

Q: It was in 89, August 1989.

A: I haven't seen it, if I saw it it was in 89 and I don't remember anything I saw in 1989.

(Laughter)

Q: Here's a letter from, I might as well ...

A: Don has since retired even. A good friend of mine.

Q: Let's get rid of these - dispose of these letters. This is a letter to Mr. Topor from you.

A: Uh-hmm

Q: And item number 1 states that features in the 5E have been found to be, cost frequently up to [redacted] times as much similar features on the 1A. Does that mean that you're unable

to prove in economically a 5E based upon those feature prices?.

A: It could be. You know, the replacement costs or addition costs would be based on the total cost which would include the features I'm sure, but it would be a total economic analysis not just based on feature costs.

Q: Now item #3 says that feature software pricing is often higher than our lines of business organization finds acceptable for competitively marketing services in BellSouth. We had asked for documents supporting that statement from the, from that organization, and we're told that no documents were available. Do you, is this, was this all verbally done, this infor...

A: I don't, I don't, I, no, I mean it would have been I'm sure a combination of discussions, impressions, conclusions that we all have made. The statement, I'm not, I don't remember exactly y'know the time I wrote the letter but it is a problem in our industry to, this is kind of a funny industry in a way, but, if you're going to market a feature like one of the vertical features that we sell like three way calling or something like that, then when you get to the point that you do the cost studies to determine what the pricing has to be for the purpose of filing the tariff, then, all of the cost information is loaded into that and if three way calling has, if the customer has other alternatives to that, then market research would show where his decision price point would be, and there you would then say, well, unless we can come to

market with that priced in this particular range, the product's not going to be successful. So, conceptually, I understand what we were referring to, but I don't have any piece of paper with that analysis on it today. But it sure is true.

Q: Here's one of the letters from back to you from Mr. Topor and this paragraph talks about BellSouth's well documented concerns about the 5ESS switch's competitive position on first costs, and also at the end of this letter it talks about your previous letters on the availability and cost of five ESS special features. And, one of our concerns here, sir, is that we feel that we, y'know, there seem to be some documents that we're not getting in this area, and I'm wondering if you are aware of any other documents that we have not received in this area.

A: Well, I'm not, but the only two documents I'm familiar with are the two you've shown me. I haven't, I can't personally testify one way or another to what documents were available. I don't know what you're looking for, so...

Q: We would have been looking for documents concerning the well documented concerns and then the previous letters mentioned on page 3 of this letter.

A: I don't know. I know that we've, that I've been concerned about that very subject from time to time, but I don't have any documents in my file one way or the other. I figure y'all did a search, didn't you. (Young: Um-hmm.)

Q: This letter from Mr. Topor to you on page 2. It says the mix between capital and expense prices for five ESS switch will change with expense decreasing and capital increasing, but the average bottom line switch price will remain consistent with the previous five ESS price plan. He also, down here, said he completely understands your concerns about the effect that the price of our features have in regard to your ability to generate tariffs that are within the range of your customers willingness to pay.

A: Yeah, that's the thing I went through a minute ago.

Q: And they were, so that was indeed a concern in your negotiations with, um?

A: It was a concern in the letter that I wrote just like I said it. If you look at the way we offer products, we buy a switch and then we have generic upgrades with new software packages that we pay certain amounts of money for, and then we take a feature and when we do a cost study on that particular feature, which picks up a part of the generic and part of the switch capital cost and then it gets an approved methodology that we have with our regulators and then that gives you underlying cost of the product which we then come up with a price and file a tariff. Now, I've always, and still am, concerned that in a world that has many many CPE type applications that we have switch based solutions that are competitively priced, but our, my concern was not whether it shifts things from expense to capital or capital to expense,

because my concern was that we decrease the cost to the switch, making our products more competitive because they would have a lower underlying cost and therefore would be able to put to the market with a lower price. But, uh, I mean, that was the intent, and I've had many discussions with these fellows about that, a very reasonable concern for a company like ours to have.

Q: Do you think it's possible that AT&T could as a result of this, this plan or price restructuring, how ever you'd define this, be pricing it's software below cost, below it's development cost.

A: Looking at what it's done, I would doubt that very seriously. But I don't know personally but I wouldn't think so.

Q: The concern would be ...

A: The history, the history of computers and stuff is in the other direction. Price the hardware real low so you can get the hardware in to the customer and then after the customer buys the hardware he's sort of wedded to purchasing the software so the motivation is the other way around. For any hardware or software manufacturers. This company, in his letter here, our desire was to get the total product life cycle cost to a minimum, which was expense and capital over a period of time, and we did indeed do that. If you look at the price we're paying per line today compared to what we were paying in 1989, 88, 87 there've been orders of magnitude reductions based on this kind of negotiating, where we do with

all vendors one against the other to try to get them to move their prices down. These guys lost alot of market share during that period of time. When the 5E first came out it was not competitive, price-wise, and they had to bring the prices down rather dramatically over time so we were, and I am, very proud of these kinds of negotiations because our company and the people that buy our service have benefitted from them.

Q: Struck a lot of these questions. (Laughter) And as a result of this, we, the company signed a switch purchase agreement for the Atlanta area and Mr. Manion told me this morning that that was a part of a much larger deal, AT&T got probably the most out of the deal, but the other two switch vendors got pieces of that.

A: It was a pretty remarkable negotiation. The main beneficiary was us.

Q: Do you, would you know what in general swung the deal most heavily in favor of AT&T?

A: They were very aggressive in their pricing because we had introduced the concept of the third vendor. That was our strategy all along was to use the third vendor to try to drive the prices down. We knew somebody would blink and these guys blinked pretty substantially. We had a pretty much of a duopoly before that. In a duopoly, if you're the purchaser, you can use a third person or third company in this case coming into the negotiation advantageously, and we did pretty

successful. That did not happen all over the country. We were able to get some pretty aggressive prices.

Q: The bottom line is they came in at a lower price for the majority of the switches.

A: I don't remem...

Q: Lower total cost, I'm just trying to...

A: Yeah, I don't remember the details of who got exactly what percentage, but I do recall that they aggressively priced and one of their competitors, if I remember right, did not at that time, wasn't that right. One of their competitors lost market share in this negotiation. We picked up a little bit with the third guy and the majority went to these fellows because they responded so aggressively. Is my memory ...? (Manion: Yes.)

Q: Was this... This wasn't exactly one sided all in your favor, all in Bellsouth's favor; what did AT&T receive, other than a substantial piece of business

A: Kept their factories running.

Q: Continuation of them actually being in the business?

A: Yeh. The problem these guys have and the reason a purchaser can take advantage of it is they have to level load the factory and they got to have a pretty consistent volume, and if you can, or if you're good enough or lucky enough or whatever, sometimes you can get a very aggressive behavior on price because they see their factories not being loaded to full capacity and BellSouth is a big account for any of these vendors, and they can't, if we can position it right, they

can't walk away from our situation because we're so big. One of the benefits of volume purchasing. AT&T and BellSouth have had a good relationship over the 10 years or so we've been doing this. Sometimes a contentious relationship based on price or from time to time performance; their quality has not always been what it should. But, over the years they've been an exceptionally good vendor for us. Their machine is of high quality, their pricing has been pretty aggressive, and I would imagine their market share here is probably what is it? Do you know?

(Manion): In this RQ or in BellSouth's total?

(Boren): No in total, what would you guess? percent?

(Manion): [redacted] of our lines.

A: (Boren): Yeah, and so we have a good healthy relationship with them which they would not want to see go away. It's too big. Because of that, when we write a letter the way I did, complaining basically about their pricing, it gets their attention. They worry about it because we're so big. Now we don't do it lightly, because if you're a good purchaser, you don't just without reason flail about. You sit down and plan your strategy and try to execute it. That's what we did on this case. It was very successful for us, this particular negotiation.

Q: Uh, this same letter, lemme, refers to the concept of revenue sharing somewhere along the line. Here we go. Also we

continue to be interested in working with you to evaluate and implement a way to take advantage of revenue sharing. Now we had an explanation here of what that might mean in response to our data request 118F and it is that we believe that in this AT&T proposal is referring to some kind of deferred payment schedule for 5ESS software right to use fees based upon BellSouth's market penetration. Is that what you think they meant?

A: I don't know specifically, but they're not in the letter. There's been a couple of concepts advanced by different vendors about return of revenue sharing, and generally it's different ways that purchasers and sellers have of sharing the risk in the market, particularly if it's a new market. We've had discussions over the years with AT&T and others about a way to do that. We've never successfully worked anything out because it's complex and gets into, well you're an accountant supreme, so you understand the difficulties when you get into something like that. But basically all it means in country boy language is we agree on a price, take it to market and if it's successful, then we have some kind of a risk sharing with the vendor. It can work in some cases, but we never have been able to work it out.

Q: Well, what I was, see what, the way I interpreted this explanation was that it was referring to some kind of an arrangement where the cost would be matched to revenues in those new markets.

A: What kind of revenues? I don't know how that would work.

Q: Is it BellSouth's policy to pay for right to use fees prior to deployment of any features in the network?

A: Yeah, I think the right to use fees are generally based on a total package of feature functionality not just on a specific product. A generic in one of these switches is a very large piece of software. When you have a generic update it usually sweeps under it lots and lots of things, some as simple as some mistake that's been found in the software. So we buy software in different ways, but I don't know of a revenue sharing situation. Do we, did we have one during that period?

(Manion): No, The only thing I can even think that comes close to it is some software features are priced on per line basis, for, if we only need 100 lines, we only have to buy 100 lines of it and if it's a successful feature and we get a heavy penetration then all of a sudden we need 10,000 lines of it, we have to buy more lines, so as we increase our penetration in the feature they would also get some revenue when we buy on a per line basis, and that would be a risk sharing. Instead of having to purchase the right to use for the whole switch at one time, not knowing if we can sell that particular feature or not, we can deploy it with a minimum number of lines, see how it goes, and if we're able to sell it, we buy more lines and (__?__) more lines and they would get the right to use fees everytime we buy more lines. That's

the only thing I can think of that would even be close to revenue sharing.

(Boren): And that's not classical revenue sharing, at least in the way I think of it. We've, I've always hoped we could find situations where we could, where we could have some kind of risk sharing, but we haven't been able to come up with a formula yet.

Q: Mr. Boren, the reason we're here is because somehow we laid our hands on this document which is this AT&T presentation which was sort of in the middle of all this correspondence and I guess at the beginning was the negotiations, at the end was the switch deal, and this presentation has these words on pages 3 and 4 and it calls them BellSouth issues and it talks about - it says you're going to do, or AT&T was going to do what it said it was going to do in all these letters, that is shift expense, shift from expense to capital. And our concern is that it seems like whether or not total cost went down, there is some shift that had regulatory implications here for pricing purposes, and, in fact, this talks about rate base profit regulation on capital investment and the FCC tightening accounting rules to require expensing of (_____?_____), so here we are with this, and Steve Manion has steadfastly reported that they didn't do what they said they were going to do so all of this is a non-issue. I'm asking you is this, were there, are their statements accurate? Were these BellSouth issues back in those negotiations?

A: Not to my knowledge. If I look at the piece of paper, expense budgets are tightly constrained. In my 25 years of experience, every year the expense budget is tightly constrained. That's in any business has all the time a tight expense budget. Profit regulation based on capital investment. That's rate base rate of return regulation in a different sort of slant on it than I would put on it, and of course the accounting change we're all familiar with, so the statements on the face of them are true. If the implication that, and I haven't seen the rest of the document, but if the implication is that there was some strategy with AT&T for a particular purchasing strategy related to that, it's not true.

Q: Well, it would be these, plus this one here, "the five ESS allocates too much of its cost to BellSouth marketing's most competitive services ESSX," and that's where I, that's my concern. I think that they said these are your issues and you're telling me they're not your issues.

A: Well, not in any sort of way that is a conspiracy to make things shift from one account to another. That's not true. As I know you are more aware than I, because of your profession, this, if you look inside AT&T or any other company, the pricing strategy is something they have to worry about. Far removed from me as a purchaser. Now if they've looked at me and deduced that these are my concerns, I can't refute that, and if that's what they think, then that's what they think. All I can report to you is what our own strategy

is, which we talked about previously to some extent and can do to more extent. But as far as any thought on my part of an expense or capital shift for some competitive reason, that just wasn't the case.

Q: You think the results of this restructure is that now less cost is being allocated to those customers than would have been otherwise?

A: I don't know. I really don't. The product of this negotiation was an overall reduction in prices, both expense and capital. Now when you go through that calculation and reflect what these prices are, I don't have a sense for how that come out, because that was never, that was not a factor in what we did. So, y'all may have gone through the calculation and know what the answer is, but I have not.

(Manion): You talking about, you mean, the kind of stuff I showed you with the growth costs?

Q: Well, what I'm asking here now is if I, is that, is as a result of this price restructure that less cost is being allocated to those customers than would have been under previous price structure. I don't we've addressed that.

A: (Manion): Well, BRCSII, which is the package in the 5E switch that has most of the ESSX features. One of the things they offered there is it went from a line to a line, which lowered software costs. And we showed you that in a...

Q: So that's the answer, is yes?

A: (Manion): That for BRCSII package, which is our ESSX software right to use fee, there was a significant reduction in price. (Boren): And my discussion is at a level above that, where what I was seeing was a total reduction in cost of the purchase. I didn't get into which package was up and which package was down. There was an overall reduction in the per line cost of software and hardware, and when you put them together an overall reduction in the total price of the switch. That's what I saw and what I reacted to.

(Manion): I mean if you flip back into the pages of that it shows you where the BRCS is now a line and it used to be a line (_____?_____) in that presentation AT&T (_____?_____). It's in the back pages.

Q: Well, so these were, I guess, I don't have too many more questions, they either were or were not BellSouth issues. AT&T had said they were BellSouth issues. Seems to me, I will just ask you, did you achieve some regulatory goal other than an overall reduction in the cost when this deal was struck.

A: Not to my knowledge. The regulatory goal, as you put it, just simply in the years that I did this job, was not my concern. I don't know how to put it any plainer than that. I didn't think about, I didn't write about it, I didn't talk about it. It just wasn't a factor. It, my, this job is a businessman's job, not related to the regulatory situation. It's just a businessman's job. We had a market, product and a purchasing opportunity. Now, I don't know the regulatory impacts

discretely by product of the negotiations we did because it wasn't a, it wasn't involved in anyway. So I didn't know it before and I didn't know it after. What I was after was the businessman's approach, because if you can make the price of the products of what you're buying to provide the products that we sell go down, everybody benefits, and that was the motivation. Maybe I should have been more sophisticated and had some way to slice that in a different way, but it just wasn't true.

Q: I guess where I'm getting to beyond, y'know sort of beyond that, is that y'know Steve has told us, I think, that we don't know where these words came from and we're trying to find out...

A: If you're talking about these three words here, these three bullets? Those words we read?

Q: Those bullets and this bullet.

A: Which one?

Q: Where we are. This one, and the three above it. Whether AT&T, y'know, if we go ask them, why did you write those and just call them BellSouth issues, whether it's BellSouth's position that they don't know where those words came from and AT&T was not accurate and shouldn't have written those words is what, you know?

A: The fact is, let's just take them one at a time. Any year that I've been involved, that first bullet is true. Any year.

This year. As it was true whenever this took place. The second bullet, as long as I've been in this industry that has been true, because we've always been under one form or another rate base rate return regulation, where if you are in rate base rate of return regulation, your profits are related to your capital investment or at least as much of it as goes in the rate base. The third bullet is just a fact. The FCC did indeed change their accounting rules with regard to right to use. So there's nothing magic about where those came from. Other than the third bullet, they are exactly true today. So, nothing very remarkable about those three statements is the point I'm making. And this, we were saying, as I'm sure I was saying or my folks were saying, that the five ESS were simply not being competitive against its competition. Now, if inside AT&T, they want to conclude that the reason the price is being perceived as noncompetitive is because they have decided to make their allocation a certain way, that's an internal AT&T issue. I can't, I mean, it's not my issue one way or the other. That's a conclusion that they made for themselves, I guess. So when you say, don't know where the statements came from, there's nothing remarkable about the statements. There's nothing mysterious or remarkable, to me anyway. Maybe you're seeing something there that I...

[end of side one of tape]

... they put in on. I'm just trying to tell you they're just truisms. They're not...

Q: Stating the obvious?

A: Yeah, they're just staying the obvious. And on this, if they decided, I mean it's like, it's like any vendor that had a product comprised on two pieces. If they want to say, gosh, the customer is complaining about this piece being too high, I think, and therefore, let's lower this one a little bit and raise this one a little bit, and that's internal to them, and what I'm looking at is adding the two together to get them to come down, I can't, I mean, that just the way things worked out.

Q: What is the effect of the BRCS feature dropping from to What's the effect of that?

A: (Manion): Uh, associated with the price of the switch?

Q: Marketing the features, whatever? What's the impact on your customers?

A: (Manion): Well, I'd just have to, I mean, I can't answer that. From a procurement standpoint, the effect would be, depending on the amount of penetration of that feature in a particular switch, would be how much we would save, or whatever, for every line of Centrex or BRCS that we deployed where we used to pay a line for it, we pay Some switches have zero ESSX in it, other ones have 10,000 lines. So, you know, that effect. As far as the marketings

aspects, I would assume our marketing folks might be able to sell it a little better. I don't know.

(Boren): I think the answer intuitively is that the price of this package would go down in the market place making it more competitive. Now, precisely how much it went down, you know, you could go talk to the pricing folks that do the costing studies and see how much that change in that software package rolls out into the decreased cost of the product in the market place. We don't have that information, but it's certainly available. It wouldn't be a one for one because it's a very complex product, I would imagine, and has lots of loaded cost into it.

(Manion): (____?____) I think that's the key, as I think was pointed out earlier, a portion of the processor, the computer, and all the hardware in the switch is also rolled into the cost of delivering that feature, and it's not just purely that software.

(Boren): But it would, I mean, assuming accounting systems work, and I've sometimes wondered, but assuming they work, if you get a product associated with a specific software package and that software package is reduced in cost, you ought to be able to reflect that in the reduced cost of the product, and therefore reduced price, therefore you'll be more competitive. The only point we're trying to make is that since the pricing of a particular product that comes out of a switch is not just an assignment of the software that provides that, but also an

assignment of other cost in the switch allocated to that product, it wouldn't be a one for one reduction. Because any given product coming out of the switch that supports all products takes a percentage of the total cost of switch, as well as the specific incremental cost associated with the product.

Q: That's correct. And, you know, obviously, one of our concerns is that, uh, that pot is bigger than it ordinarily would have been and then, y'know, the incremental cost is, of that is smaller than it would have been, were it not...

A: With all due respect, I understand your concern. I'm just telling you it ain't true, in as specific a way as I know how. I don't know how to be any more specific than I've been. But I certainly understand your line of questioning. I've been in this business for a long time.

Q: I can tell. (Laughter) Well, I can't think of any more questions that I have, sir. Don? I want to say I appreciate your time.

A: Oh, you're more than welcomed. I'm sorry that it has to be on such a subject that seems to be contentious, because it really was a fine piece of work that my organization did at the time this was done, and it appears that in studying it we've picked up an angle of question that makes you think there was some underlying reason that wasn't appropriate, and to my knowledge, that was not the case. It was a fine piece of work and all of the folks that pay our rates benefitted, and the

commission benefited, and it was a good thing to do. So, I sure respect the fact that you have to chase every lead that you think is appropriate and we were glad to cooperate with you.

Q: Thank you.

A: Good luck to you.

[end of tape]

BELLSOUTH
TELECOMMUNICATIONS

36M66 Southern Bell Center
675 West Peachtree Street, NE
Atlanta, Georgia 30375

January 21, 1994

Mr. Don Craig
Room 267
Georgia Public Service Commission
244 Washington St., S.E.
Atlanta, Georgia 30334-5701

Don:

As requested, SBT's response to the twenty-fourth audit data request is attached. Upon your request, we have sent an identical package to Snavely & King, care of Mike Majoros. Some responsive but proprietary information related to this request-set is ready for your review during your next visit.

As you are aware, the format of this set of data requests differs significantly from that of previous sets. Rather than being propounded in the form of questions, the requests more closely resemble random statements or thoughts from which it is sometimes difficult to discern the precise issue to be addressed. Moreover, to the extent some of these requests appear similar to requests for admission, we note that you did not characterize them as such and we did not treat them as such. Nonetheless, we have diligently tried to respond to the "requests" as we understand then and will be happy to provide clarification during your impending visit.

When reviewing our responses, please keep in mind the clarification we agreed to by telephone concerning the interpretation of "competitive" and "basic" in the context of switch lines. As you recall, "competitive" and "basic" were to be construed as "ESSX[R]" and "business and residence" respectively.

Please also note that to the extent Requests or Responses would reflect quantifiable data about our relationship with vendors (i.e., prices, units), we have redacted that information from the enclosed materials. As always, unredacted copies of these materials will be available for your on-site review. Also, please refrain from including such data in future requests or other documents. We consider this data to be proprietary and governed by the terms of the agreement we have for handling such information. We will, of course, be happy to work with you to respond to any request you might have that by its terms would otherwise disclose proprietary information.

[R]ESSX is a registered trademark of BellSouth

I'm happy to report that Mark Stephen will be assisting you at Southern Bell Center throughout your visit. (Mark acted in a similar capacity at Perimeter during the fall of 1992.) When you arrive at the building on Monday, please call my number to arrange for building access. If I am away from my desk or on the telephone, please dial "0" and ask for Mark.

We look forward to seeing you, Mike and Jim next Monday.

Please call me with any questions or concerns.

Michele Young
Docket Manager
529-8512

cc w/atts: Mike Majoros

cc w.o./atts: Kirven Gilbert
Dave Williams

REQUEST: 5ESS Price Restructure Effects

"Competitive" feature costs were reduced on per line basis.

"Basic" Residence and Business features were regrouped. Average cost per line increased.

RESPONSE: One of the results of AT&T's 5ESS[R] "price restructure" was that the 5E BRCS Feature Packages were also restructured.

"Universal" BRCS replaced BRCS I at restructure. This new Universal BRCS Feature Package contains six additional features that were not included in BRCS I. This change makes it impossible to make a meaningful comparison between the BRCS I and Universal BRCS feature packages' pre- and post-restructure. Moreover, AT&T introduced a per-line RTU fee structure for the Universal BRCS feature package, while the previous, more limited BRCS I feature package had to be licensed only on a full switch module (SM) basis. Since each 5ESS SM can support anywhere from 0 to over 2,000 lines, any simple comparison between the per line RTU fee structure of the enhanced Universal BRCS feature package with the per switch module RTU fee structure for the more limited set of BRCS I features would be invalid.

The restructure also affected the RTU structure of ESSX related features. The majority of the features from the BRCS II feature package were combined with another set of ESSX related features (BRCS III), that previously, had been licensed separately. This combined feature package was denominated BRCS Centrex. Again, however, Centrex differs from previous BRCS packages of ESSX features, simple comparisons of pre- and post-restructure RTU fees for the different packages are not meaningful.

The Company has previously provided detailed examples and explanations of both initial and growth switch projects using actual firm price quotes (FPQ). The actual contracts and price lists, both before and after restructure, were also provided. These documents and explanations all showed that another result of AT&T's restructure was an overall reduction in the price per line. Therefore, BellSouth cannot agree that the average price of any line increased as a result of this restructure.

[R]5ESS is a trademark of AT&T

INFORMATION PROVIDED BY: Steve Manion
Project Manager
675 West Peachtree St.
Atlanta, GA 30375

REQUEST: Initiation of Price Restructure

BellSouth initiated the Price Restructure described in Michael Ward's April 3, 1990 AT&T Switch Price restructure, and ~~maintained~~ MAN. TESTED in Contract No. PR-6700-B.

See August 24, 1989 letter from D. W. Jones (BSS) to J. R. Criser (AT&T).

See November, 1989 letter from C. S. Boren (BSS) to F. S. Topor.

RESPONSE: (It is important to note in response to this, and several subsequent questions, that "price restructure" was actually effected in Contract PR-2774-B, Amendment 3. This amendment went into effect on 1/1/91. Contract PR-6700-B replaced PR-2774-B and became effective on 1/1/92.)

As previously stated in the Company's response to item 118 D, AT&T's price restructure was implemented nationwide and was in no way unique to BellSouth. The letters listed in the request, respectively, conveyed to AT&T a feature priority list for 5ESS® and 1AESS switches and the Company's concern that AT&T's pricing strategy and policies caused its growth and software prices to be too high. However, it is highly unlikely that the concerns expressed by one customer, albeit a major one, would cause an overall nationwide change in AT&T's switch pricing. Rather, the restructure was initiated by AT&T to address its own perceptions of the marketplace.

®5ESS is a registered trademark of AT&T

INFORMATION PROVIDED BY: Steve Manion
Project Manager
675 West Peachtree St.
Atlanta, GA 30375

REQUEST: Effect of Contract PR-6700-B

Rate Base Increased.

Average cost of basic residence line increased.

Average cost of basic business line increased.

Average cost of ESSX[R] line decreased.

Other?

RESPONSE: (As noted in the response to item #122, the actual agreement that implemented "price restructure" was Contract PR-2774-B, Amendment 3, effective 1/1/91.) The changes introduced by this agreement did not necessarily result in an increase in the Company's revenue requirements. Generally, net investment will increase when a significantly depreciated switch is replaced by a new switch. However, this may not impact revenue requirements or overall costs since newer technology usually has less associated maintenance expense and offers significantly more revenue potential.

Furthermore, deployment of a new switch is based upon a number of factors including access line growth, maintenance considerations, regulatory requirements, and customer needs. Any initial or growth switch procurement is carefully reviewed by the Company and an economic evaluation is performed for each purchase decision. The auditors have had numerous interviews with the Company's SMEs regarding switch procurement and implementation. In addition, literally hundreds of telephone equipment orders, and other voluminous documentation, have been provided to demonstrate this process.

[R]ESSX is a registered trademark of BellSouth Telecommunications

Finally, as has been addressed in other responses to this data request set and in numerous interviews with Company personnel and documentated information previously supplied to the auditors, the Company does not agree with the second, third and fourth statement in this request. The Company has repeatedly demonstrated that "price restructure" resulted in an overall reduction in line costs.

INFORMATION PROVIDED BY: Frances E. Dennis
Operations Manager
675 W. Peachtree Street
Atlanta, GA 30375

REQUEST: Definition of Price Restructure

BellSouth definition of price restructure as reflected in Michael Ward's April 3, 1990 presentation, all-related correspondence, and Contract No. PR-6700-B?

RESPONSE: BellSouth presented its interpretation of AT&T's nationwide price restructure to the auditors on November 16, 1993. Proprietary information showing representative price changes was also provided. This documentation, as well as other responsive materials identified above, continues to be available for review on Company premises upon reasonable notice.

(Please note that AT&T's price restructure was introduced in Contract PR-2774-B, Amendment 3, effective 1/1/91, not Contract PR-6700-B, as stated in this request.)

INFORMATION PROVIDED BY: Steve Manion
Project Manager
675 W. Peachtree St.
Atlanta, GA 30375

REQUEST: Effect of Price Restructure

Canceled order with Northern Telecom for purchase of switch of Chamblee.

Signed contract with AT&T with purchase of switches, of these are in the Atlanta metro area.

Other?

RESPONSE: As has been explained previously, neither the cancelled order for the Northern Telecom switch nor the contract with AT&T for multiple switches was an effect of the price restructure. The price restructure was merely an amendment to an existing contract with AT&T (PR-2774-B) that modified the price list for orders, mainly for growth and upgrades, placed against that contract. The Company has a similar contract with Northern Telecom to govern orders placed against it. The Northern Telecom order for the Chamblee office was issued against that contract, but later delayed due to lower than forecasted line growth. The Chamblee office was subsequently included in a list of offices identified for switch replacements in a longer time frame, i.e., 1991 to 1996. This list was included in a request for quotation (RFQ) sent to switch vendors, including both AT&T and Northern Telecom. As a result of this RFQ process, AT&T was awarded switch orders for a number of offices, including Chamblee, and Northern Telecom was awarded others. Each RFQ response contained its own pricing structure and was specific to central office locations. The RFQ responses were not dependent on pricing in the existing contract price lists. Thus, the RFQ price on which AT&T was awarded the Chamblee office and other locations were not the effect of price restructure. The only relationship between the RFQ responses and the existing contracts was that switch procurement under the RFQ responses were to be governed by the general terms and conditions (i.e., boilerplate) of the existing contracts and were to be counted toward any dollar volume commitment of switching products contained in the respective contracts.

INFORMATION PROVIDED BY: Steve Manion
Project Manager
675 W. Peachtree St.
Atlanta, GA 30375

REQUEST: Revenue/Risk Sharing

Explanation of Revenue/Risk sharing resulting from restructured per line pricing?

RESPONSE: As the Company stated in its response to Item 118 F and as has been explained in interviews with Company personnel, the Company did not pursue any type of revenue sharing with AT&T, and neither revenue nor risk sharing resulted from AT&T's restructured switch pricing.

INFORMATION PROVIDED BY: Steve Manion
Project Manager
675 W. Peachtree St.
Atlanta, GA 30375

REQUEST: Contract PR-6700-B Prices

Prices in contract are the same as those shown in April 3, 1990 Michael Ward presentation, except universal BRCS. Actual universal BRCS price per contract is //line rather than /line shown in Ward presentation.

RESPONSE: As stated in prior responses, AT&T's "Price Restructure" was implemented and became incorporated into PR-2774-B, Amendment 3. PR-2774-B, Amendment 3 went into effect on 1/1/91. The Price Factor Table for this Contract Amendment reflects a /line RTU fee for Universal BRCS, which is consistent with the Ward presentation.

Subsequently, AT&T initiated price revisions for 5ESS® equipment which were permitted under the contract. These price changes went into effect on 1/1/92 concurrent with execution of Contract PR-6700-B. One of the price changes was an increase in the Universal BRCS per-line RTU fee from to .

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INFORMATION PROVIDED BY: Steve Manion
Project Manager
675 W. Peachtree St.
Atlanta, GA 30375

REQUEST: April 3, 1990 Michael Ward AT&T Presentation

- Basic savings shown in presentation are overstated due to use of /line universal BRCS charge rather than /line BRCS universal charge per Contract PR-6700-B.

- Cost shift from ESSX to universal per April 3, 1990 presentation is ~~overstated~~ understated due to use of /line BRCS universal charge rather than /line charge per Contract PR-6700-B.

- Presentation reflects BellSouth issues.

RESPONSE: As explained in the response to Item 128, was the correct rate for Universal BRCS per-line RTU fee. (Contract PR-2774-B, Amendment 3, not Contract PR-6700-B implemented "restructure.") Therefore, the amount stated in this presentation is accurate.

The Company cannot address materials prepared by AT&T other than to suggest that the AT&T presentation reflects AT&T's characterization of various items as "BellSouth issues." As the Company has explained in previous interviews, the presentation is not an accurate protrayal of matters of unique concern or relevance to the Company.

INFORMATION PROVIDED BY: Steve Manion
Project Manager
675 W. Peachtree St.
Atlanta, GA 30375

REQUEST: Price Restructure Expense vs. Capital

- AT&T believes that its price restructure changed the mix between capital and expense dollar prices for a 5ESS[R] switch with expense decreasing and capital increasing, but the average bottom line switch system price remained consistent with the previous 5ESS price plan.

  See February 8, 1990 Topor letter to Boren; April 3, 1990 Michael Ward Presentation; June 12, 1990 Mauriello letter to Boren; and July 20, 1990 Puckhaber memo to Sweet.

- BellSouth official position is that the price restructure did not result in a shift of expense to capital.

RESPONSE: Regarding the first request-point, BellSouth cannot speak for AT&T. However, in an effort to be responsive, the Company respectfully submits that it has repeatedly addressed the auditors' concerns in this regard.

The Company has previously provided its general position on this request in its responses to Items 118 A; B; C; D; F; and G. The Company also has facilitated numerous meetings between the Auditors and Company SMEs where this topic, and its underlying documentation, were reviewed in detail. The Company provided and explained actual Firm Price Quotes for both initial and growth switch projects. This effort affirmed that there was no shift from expense to capital as a result of AT&T's "price restructure". (The documentation cited in the second request-point was initially supplied in response to item 118. It was also discussed in Auditor-Company meetings.)

Throughout all of this activity, the Company has demonstrated that AT&T's price restructure did not result in a shift of expense to capital.

[R]5ESS is a registered trademark of AT&T

INFORMATION PROVIDED BY: Steve Manion
Project Manager
675 W. Peachtree St.
Atlanta, GA 30375

REQUEST: Effect of Price Restructure

- BellSouth expressed concern about new service introduction.

- Pricing for the three BRCS packages will now be on a per line basis, providing maximum flexibility to introduce new services.

RESPONSE: While this request is extremely vague and ambiguous, the Company will attempt to respond to the greatest degree possible.

With respect to the first request-point, the Company is not able to discern the precise issue to be addressed. Clearly, BST, like any company, will have "concerns" associated with new service introduction or availability. One such concern is that vendors' prices for underlying components may be too high. The Company acknowledges that it expressed this concern to AT&T. Beyond this, we cannot determine whether a question is being asked to which we can respond with specificity.

Before addressing the second request-point, it is important to note that per line pricing has always been available in BRCS Feature Packages, with the exception of BRCS I. As reported in the response to Item 121, BRCS I was replaced by "Universal" BRCS in the 5ESS® coincident with AT&T's "restructure". "Universal" BRCS includes per line pricing instead of the per Service Module (SM) pricing associated with its predecessor. Per line pricing, combined with additional feature-functionality, differentiated "Universal" BRCS from BRCS I. The addition of these attributes enabled the Company both to provide features for customers to whom the features otherwise would have been available only from switches equipped with BRCS II packages and to do so by paying an RTU fee for the Universal BRCS package on a per line basis rather than having to pay an RTU fee for a full switching module. Thus, the Company was afforded greater flexibility in equipping its switches to bring new services to its customers.

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INFORMATION PROVIDED BY: Steve Manion
Project Manager
675 West Peachtree St.
Atlanta, GA 30375

REQUEST: Price Restructure

Average ESSX cost went down. Did or will this provide a benefit to ESPs and other users of our services, including SBT as an ESP (provider of MemoryCall[R])? If not, were there other aspects of price restructure and Contract PR-6700-B that provides these benefits.

RESPONSE: As has been previously explained, the current BRCS Centrex package that facilitates availability of features specific to ESSX[R] service contains a different mix of features than its predecessors and is priced at a lower per line RTU fee. BST's customers, however, who want to buy features associated with their ESSX service, continue to buy those features essentially at the same tariffed rate as before, regardless of whether the feature is now enabled via the previously described "Universal" BRCS package or the current BRCS Centrex (ESSX) package. Thus, there was no immediate rate benefit to ESPs (including SBT's MemoryCall service) or other ESSX customers. As explained previously, however, BST's customers, and in particular its non-ESSX customers, do benefit from the regrouping of a greater number of non ESSX-specific features in the Universal BRCS package and the availability of this package with a per line price structure, compared to the more limited set of BRCS I features that were only available to BST on a per switch module price structure. (See response to Item 132 for more information.)

[R]ESSX and MemoryCall are registered trademarks of BellSouth

INFORMATION PROVIDED BY: Michele Young
Staff Manager
36M66 675 W. Peachtree St.
Atlanta, GA 30325

REQUEST: Chamblee - Price Restructure

Only AT&T and NTI were studied as replacements for the Chamblee 1AESS. AT&T beat NTI substantially on both first cost and growth. How did NTI get any of the approximately (total switch purchase orders?

RESPONSE: Each vendor that responded to the Request For Quotation (RFQ) was allowed to provide its best price quote on any individual office listed. Vendors were not required to provide the same level of discounts for all offices upon which they submitted bids. Therefore, each office was analyzed and awards were made based on each office's individual characteristics. As a result of these analyses, AT&T was selected for some offices; Northern Telecom for other individual offices.

INFORMATION PROVIDED BY: Justin Pratt
Staff Manager
203-100 Perimeter Ctr. Pl.
Atlanta, GA. 30328

REQUEST: Contract PR-6700-B

- How are first engineering costs treated and billed?
- Is PR-6700-B still in effect? Agreement was between BSS and AT&T. BSS no longer exists. Who are parties to new agreement?

RESPONSE: Engineering costs are listed in the Price Factor Table of the Contract. Engineering costs are divided into two categories - 1st and additional. If a switch unit is ordered in multiples (a quantity greater than one), the engineering cost in the "1st" column is applied for the first unit; the engineering costs in the "additional" column applies to every unit after the first. If only one unit is ordered, the engineering cost in the 1st column applies.

Contract PR-6700-B is still in effect. On January 1, 1992, BellSouth Services, Inc., Southern Bell Telephone and Telegraph Company, and South Central Bell Telephone Company were merged and became a single legal entity named "BellSouth Telecommunications, Inc." (BST). While the trade names "Southern Bell" and "South Central Bell" will remain in use, all of BellSouth Services rights and obligations were vested in BST by operation of law, and BST is now the party to that contract with AT&T

INFORMATION PROVIDED BY: Steve Manion
Project Manager
675 W. Peachtree St.
Atlanta, GA 30375

**MEMORANDUM**

**TO:** Mr. Joseph Mauriello

**DATE:** January 26, 1994

**FROM:** Don Craig

**RE:** AT&T Presentation to BellSouth and December 21, 1993 Interview.

I understand that you have received from BellSouth the missing pages from AT&T's April 1990 presentation. That presentation formed the basis for our December 21, 1993 interview with you.

Attached to this memorandum is December 21, 1993 memorandum summarizing Mr. Majoros' and my notes taken during that interview. Please review these and send me your comments and any clarifications or corrections that should be made. I will attach your comments to the December 21, 1993 memorandum in our workpapers.

We would like to have another discussion with you after you have had a chance to review the pages missing from the April 1990 presentation. I will call you to set-up a time for this discussion.

Thank you.

cc: T. Hobbs

**MEMORANDUM**

**TO:** File

**DATE:** December 22, 1993

**FROM:** Michael J. Majoros, Jr. and Don Craig

**RE:** A December 21, 1993 Interview of Mr. Joseph Mauriello by Don Craig and Michael Majoros.

The interview was held in the offices of AT&T. It was attended by Mr. Gene Coker, Mr. Joseph Mauriello and Mr. Don Craig. Michael Majoros participated in the interview via telephone. Mr. Mauriello was informed of the purpose of the interview which is summarized in a Seven Point document handed to him by Don Craig. In summary, the purpose of the interview was as follows:

1) Obtain information regarding the goal and result of the AT&T 5 ESS price restructure.
2) Determine whether it was BellSouth's intent to gain some regulatory advantage by causing a shift of cost from expense to capital resulting in a ratebase buildup.
3) Determine whether price restructure resulted in a cross-subsidy among certain customer classes of Southern Bell.
4) That is, did AT&T regroup and reprice those features generally selected by basic residential and business customers and those features needed to provide ESSX service?

5) Did this regrouping and repricing result in the average cost per line increasing for basic residential and basic business customers, while the average per line cost for the competitive ESSX customers decrease?

6) Was there an overall decrease in initial and growth software cost?

7) Did AT&T remain whole by increasing the costs for material capitalized?

Below is a summary of the questions that were asked of Mr. Mauriello and his responses thereto.

Q1. Did, as a result of the AT&T price restructure, total hardware prices increase (for a typical fully equipped switch module) while software prices decreased? If yes, what? where? demonstrated in the April 1990 presentation and what equipment prices went up?

A1. Mr. Mauriello responded yes. Mr. Mauriello stated that this was a national price roll-out and that it had nothing to do specifically with the Southern Regional operations. Mr. Mauriello indicated that a national price roll-out was necessary to change the way AT&T was doing business, but that no pressure from any single customer was exerted upon AT&T, however pressure from all customers was exerted. Mr. Mauriello discussed the fact that prior to this price restructure, there were two separate business units within AT&T, one for the 1A ESS switch and another business unit for the 5 ESS switch. He indicated that they were going about

their business separately and pricing things in inconsistent ways. The market place impact needed to be addressed.

Q2. Did the price restructure result in a change in the mix of capital and expense dollar prices for a 5 ESS switch with expense decreasing and capital increasing, but the average bottom line switch system price remain consistent with the previous price plan?

A2. Mr. Mauriello stated yes. There was a change in the mix, but the total price did not go up or down. (He emphasized that was the intent and that was the result of the price restructure in response to Question 10.) Mr. Mauriello indicated that this was a revenue neutral price restructure. Mr. Mauriello was asked the meanings of the words "capital" and "expense" from his viewpoint. He stated that capital was equivalent to hardware in the 5 ESS switch and that expense was equivalent to software or generic upgrades for the 5 ESS switch. Finally, Mr. Mauriello indicated that what AT&T was after was to be paid for its switch no matter how the payment is split between capital or expense.

Q3. Is it AT&T's policy to price 5 ESS features based upon their development cost and value added?

A3. Mr. Mauriello stated yes. He indicated that AT&T would not price any features below cost because he believes that is illegal.

Q4. How could it be that the restructured prices were based upon cost after the restructure if they were based upon cost prior to the restructure and the restructure was in fact revenue neutral?

A4. Mr. Mauriello indicated that AT&T always covered its costs. He stated that prior to the restructure, AT&T managed its business on a product management group basis. For switching, there were two independent development groups: hardware and software. Each group had unique profit margins. Now the development groups are unified as business units: switching (hardware and software), transmission, cable, etc.

We returned to this issue later in the interview. Mr. Majoros' notes indicated that Mr. Mauriello made the following statements in this conversation. He will make a lot of money from residential...??? (It is not clear whether Mr. Mauriello was referring to AT&T or BellSouth.) Give the total package up front...??? Don't price to match the revenue potential of market...??? Will sell for same price throughout territory - sell generics at set price to customers to use however he wants...??? ISDN is equivalent to a growth job.

Q5. Why was this done and how does it relate to cost?

A5. Mr. Mauriello brought up the concept of basic research cost. He indicated that basic research cost allocations may have had something to do with the restructure, but that was only speculation on his part.

Q6. Could you explain the concept of Revenue Sharing as used in Mr. Topor's February 8, 1990 letter?

A6. Mr. Mauriello responded again, that this price restructure was a national offering and that AT&T had discussed revenue sharing with all of its customers. It was the desire of

AT&T to workout financial arrangements to protect its own revenue streams over a longer period. Mr. Mauriello stated that revenue sharing is a marketing package that was never accepted by any of its customers. The concept was for AT&T to become a partner in the revenue streams provided by its equipment. Essentially, AT&T offered its hardware and software free, with the proviso that it share in the revenues resulting from that equipment and software. Mr. Mauriello indicated that risk sharing was a large part of this offering, but he reiterated that nobody accepted it.

Q7. The last paragraph of Topor's February 8, 1990 letter refers to Joe Mauriello and discusses Mr. Boren's recent letters and previous letters on the availability and cost of 5 ESS special features. Are you familiar with any letters prior to November 1989 from Mr. Boren to AT&T concerning the availability of five ESS special features or with any other correspondence?

A7. Mr. Mauriello was not familiar with any previous letters. Mr. Mauriello stated in this response that the price restructure had to occur, not only because of BellSouth but because of the confusion in the previous pricing plan.

* * * * *

We next moved on to the April 1990 AT&T presentation which Mr. Majoros and Mr. Craig had seen in the offices of BellSouth. Mr. Craig did not have a copy of that document because it was deemed proprietary by BellSouth, however, Mr. Mauriello was requested to obtain a copy for the purposes of this interview.

Q8. Were the bullets identified as "BellSouth Issues" in the April 1990 AT&T presentation first raised by BellSouth or AT&T?

A8. Mr. Mauriello indicated that typically AT&T is presumptuous and creates issues. He stated that AT&T created the issues indicated as BellSouth issues in the presentation. He stated that it was a marketing ploy.

Q9. Specifically, why is too much cost going to ESSX customers?

A9. Mr. Mauriello stated that this assumption was based upon feedback from end-users (Customers of LEC's???) The end-users could not buy the telephone companies' services (Centrex). Mr. Mauriello stated that BellSouth never said anything to him about profit regulation or FCC expensing rules. We confirmed with Mr. Mauriello that the correspondence relating to this issue started with BellSouth.

Q10. The issues were important to BellSouth as a regulated company, how did AT&T restructure its prices to accommodate these concerns.

A10. Mr. Mauriello responded as follows:

1) The intent and result of the restructure was as explained in Item no. 5 of Mr. Topor's February 8, 1990 letter.

2) The intent was to realign cost to what that they were worth.

3) It was not the intent to do market based pricing. Also Mr. Mauriello indicated that Mr. Ward left the company as a disgruntled employee and went to a competitor.

Q11. How did AT&T make up the difference resulting from the price restructure?

A11. Mr. Mauriello answered there was no net difference.

S/B Page 11 XDT 1/18/94

Q12. Page 23 of the presentation that Don Craig and Mike Majoros saw at BellSouth contained an example which indicated that the price restructure resulted in an increase in the average cost of a BRCS1 Universal line and a decrease in the average cost of an ESSX line, however overall cost went down. Is this a fair representation of the price restructure?

A12. Mr. Mauriello stated that he did not have these examples in his copy of the presentation, therefore he could not respond to the examples. Mr. Mauriello stated that Universal BRCS is residential. He also indicated in the restructure the original four packages were combined. Mr. Mauriello stated that he would not be able to justify shifting cost between services. Mr. Mauriello asked us for copies of the examples from the presentation we had seen in the offices of BellSouth. Mr. Craig indicated that he would provide or attempt to have BellSouth provide those copies.

* * * * *

The next document we discussed with Mr. Mauriello was his June 12, 1990 letter to Mr. C.S. Boren.

Q13. Does your letter fairly represent the price restructure?

A13. Mr. Mauriello responded yes.

Q14. Are the restructured prices applicable to all customers or just BellSouth?

A14. Mr. Mauriello responded yes. Restructured prices are applicable to all customers.

Q15. Please explain the reference to the Realignment of 5 ESS switch BRCS offerings in your letter.

A15. Mr. Mauriello explained the four BRCS packages prior to the restructure and the three BRCS packages subsequent to the restructure. Original: Four BRCS offerings: I, II, III and IV. New: UNIVERSAL: All of BRCS I and some of BRCS II. CENTREX (ESSX): Balance of BRCS II. Mr. Mauriello stated that the customer ordering patterns referred to in his letter were equivalent to national patterns. AT&T apparently has a national database and tracks every office for hardware and software for each office and customer ordering patterns.

Q16. Is the price restructure reflected in Contract No. PR6700B?

A16. Mr. Mauriello was not certain but believes it to be true.

Q17. Is there anything else we should know or understand about the price restructure?

A17. Mr. Mauriello wanted to make it clear that the major emphasis was to make it simpler, not just here in the South but all over. He believes that AT&T answered a lot of BellSouth's concerns, but not all of them.

Gene V. Coker
General Attorney

Room 4044
1200 Peachtree Street, N.E.
Atlanta, Georgia 30309
404 810-8700

March 10, 1994

Mr. Don Craig
Georgia Public Service Commission
244 Washington Street
Atlanta, Georgia 30334

Dear Don:

Attached is a revised version of your notes regarding the December 21, 1993, interview with Joe Mauriello. Mr. Mauriello has incorporated his comments in this revision.

I am still trying to establish a mutually satisfactory time for Mr. Mauriello to answer your follow up questions. It may be easier for you to contact him direct at 573-7000. I will also continue to try to set something up with Mr. Mauriello.

Please let me know if I can be of further assistance.

Sincerely,

Attachment

cc: Joseph Mauriello
Dennis Pines

5) Did this regrouping and repricing result in the average cost per line increasing for basic residential and basic business customers, while the average per line cost for the competitive ESSX customers decrease?

6) Was there an overall decrease in initial and growth software cost?

7) Did AT&T remain whole by increasing the costs for material capitalized?

Below is a summary of the questions that were asked of Mr. Mauriello and his responses thereto.

Q1. Did, as a result of the AT&T price restructure, total hardware prices increase (for a typical fully equipped switch module) while software prices decreased? If yes, what? where? demonstrated in the April 1990 presentation and what equipment prices went up?

A1. Mr. Mauriello responded yes. Mr. Mauriello stated that this was a national price roll-out and that it had nothing to do specifically with BellSouth. Mr. Mauriello indicated that a national price roll-out was necessary to change the way AT&T was doing business, but that no pressure from any single customer was exerted upon AT&T. Mr. Mauriello discussed the fact that prior to this price restructure, there were two separate product units with the AT&T switching business, one for the 1AESS switch and another unit for the 5ESS switch. He indicated that they were going

about their business separately and pricing similar products differently. The market place impact needed to be addressed.

Q2. Did the price restructure result in a change in the mix of capital and expense dollar prices for a 5ESS switch with expense decreasing and capital increasing, but the average bottom line switch system price remain consistent with the previous price plan?

A2. Mr. Mauriello stated yes. There was a change in the mix, but the total price did not go up or down. (He emphasized that was the intent and that was the result of the price restructure in response to Question 10.) Mr. Mauriello indicated that this was a revenue neutral price restructure. Mr. Mauriello was asked the meanings of the words "capital" and "expense" from his viewpoint. He stated that capital was equivalent to hardware and operating software in the 5ESS switch and that expense was equivalent to all other software for the 5ESS switch. Finally, Mr. Mauriello indicated that what AT&T was after was to be paid for its switch no matter how the payment is split between capital or expense.

Q3. Is it AT&T's policy to price 5ESS features based upon their development cost and value added?

A3. Mr. Mauriello stated yes. He indicated that AT&T would not price any features below cost because he believes that is illegal.

Q4. How could it be that the restructured prices were

based upon cost after the restructure if they were based upon cost prior to the restructure and the restructure was in fact revenue neutral?

A4. Mr. Mauriello indicated that AT&T always covered its costs in aggregate. He stated that prior to the re-structure, AT&T managed its business on a product management group basis. For switching, there were two independent development groups: hardware and software. Each group had unique cost structure and the development groups are unified as business units.

Q5. Why was this done and how does it relate to cost?

A5. The restructure was an attempt to more closely align 5ESS switch pricing with the marketplace, as well as simplifying the price plan for our customers.

Q6. Could you explain the concept of Revenue Sharing as used in Mr. Topor's February 8, 1990 letter?

A6. Mr. Mauriello responded again, that this price restructure was a national offering and that AT&T had discussed revenue sharing with all of its customers. It was the desire of AT&T to workout financial arrangements

to protect its own revenue streams over a longer period. Mr. Mauriello stated that revenue sharing is a marketing concept that was never accepted by any of his customers. The concept was for AT&T to become a partner in the revenue streams provided by its equipment. Essentially, AT&T offered its hardware and software at minimal initial price with the provision that it share in the revenues resulting from that equipment and software. Mr. Mauriello indicated that risk sharing was a large part of this offering, but he reiterated that none accepted it.

Q7. The last paragraph of Topor's February 8, 1990 letter refers to Joe Mauriello and discusses Mr. Boren's recent letters and previous letters on the availability and cost of 5ESS special features. Are you familiar with any letters prior to November, 1989 from Mr. Boren to AT&T concerning the availability of 5ESS special features or with any other correspondence?

A7. Mr. Mauriello was not familiar with any previous letters. Mr. Mauriello stated in this response that the price restructure had to occur, not only because of AT&T's need to address the marketplace, but because of the confusion in the previous pricing plan.

* * * * * * *

We next moved on to the April, 1990 AT&T presentation which Mr. Mjoros and Mr. Craig had seen in the offices of BellSouth. Mr. Craig did not have a copy of that document because it was

deemed proprietary by BellSouth;; however, Mr Mauriello was requested to obtain a copy for the purposes of this interview.

Q8. Were the bullets identified as "BellSouth Issues" in the April, 1990 AT&T presentation first raised by BellSouth or AT&T?

A8. Mr. Mauriello indicated that typically AT&T attempts to identify customers concerns and needs as a normal course of business. He stated that it was typical marketing activity.

Q9. Specifically, why is too much cost going to ESSX customers?

A9. ESSX pricing is a function of BellSouth, not AT&T. AT&T sells its products to its customers, not end users.

Q10. The issues were important to BellSouth as a regulated company, how did AT&T restructure its prices to accommodate these concerns?

A10. Mr. Mauriello responded as follows:

1) The intent was to realign the offerings to what customers were purchasing & wanted.
2) It was our intent to do market based pricing, basing price on cost and value to the customer. Also Mr. Mauriello indicated that Mr. Ward left the company and went to a competitor.

Q11. How did AT&T make up the difference resulting from the price restructure?

A11. Mr. Mauriello answered there was no net difference

Q12. Page 23 of the presentation that Don Craig and Mike Mojors saw at BellSouth contained an example which indicated that the price restructure resulted in an increase in the average cost of a BRCS1 Universal line and a decrease in the average cost of an ESSX line, however, overall cost went down. Is this a fair representation of the price restructure?

A12. Mr. Mauriello stated that he did not have these examples in his copy of the presentation, therefore, he could not respond to the examples. Mr. Mauriello stated that Universal BRCS is intended to serve residential customers. He also indicated in the restructure the original four packages were combined. Mr. Mauriello asked us for copies of the examples from the presentation we had seen in the offices of BellSouth. Mr. Craig indicated that he would provide or attempt to have BellSouth provide these copies.

* * * *

The next document we discussed with Mr. Mauriello was his June 12, 1990 letter to Mr. C. S. Boren.

Q13. Does your letter fairly represent the price restructure?

A13. Mr. Mauriello responded yes

Q14. Are the restructured prices applicable to all customers or just BellSouth?

A14. Mr. Mauriello responded yes. Restructured prices applicable to all customers.

Q15. Please explain the reference to the Realignment of 5ESS switch BRCS offerings in your letter.

A15. Mr. Mauriello explained the four BRCS packages prior to the restructure and the three BRCS packages subsequent to the restructure. Original: Four BRCS offerings: I, II, III and IV. New: UNIVERSAL: All of BRCS I and some of BRCS II. CENTREX (ESSX): Balance of BRCS II and part of BRCS II: The Balance of BRCS III and BRCS IV. Mr. Mauriello stated that the customer ordering patterns referred to in his letter were equivalent to national patterns. AT&T apparently has a national database and tracks every office for hardware and software for each office and customer ordering patterns.

Q16. Is the price restructure reflected in Contract No. PR6700B?

A16. Mr. Mauriello was not certain, but believes it to be true.

Q17. Is there anything else we should know or understand about the price restructure?

A17. Mr. Mauriello wanted to make it clear that the

major emphasis was to make 5ESS pricing simpler, not just here in the South, but all over. It was also our intent to more closely align pricing with the marketplace to address the needs of all of our customers.

COMMISSIONERS:

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# Georgia Public Service Commission

244 WASHINGTON STREET, SW
ATLANTA, GEORGIA 30334-5701

(404)656-4501 OR 1(800)282-5813

February 21, 1994

Mr. Gene Coker
AT&T
1200 Peachtree Street
Room 4044
Atlanta, GA 30309

Gene,

Thanks for your phone call today. Enclosed are ten additional questions for Mr. Mauriello. These questions relate to the 40 page AT&T presentation reviewed by us at Southern Bell. Hopefully a copy of the same presentation is in Mr. Mauriello's hands.

I understand your secretary will transmit the questions to Mr. Mauriello this week and you will call me on Friday.

Sincerely,

Don Craig

DC/jmh
Enclosures
cc: T. Hobbs w/enclosures

## Additional Questions for Mr. Mauriello

See Page 7, Question 12 of the Majoros and Craig file memorandum regarding the December 21, 1993 interview with Mr. Joseph Mauriello. Mr. Mauriello was unable to answer certain questions because his copy of AT&T's April 1990 presentation does not have certain pages.

Michele Young (Southern Bell Telephone) sent a copy of the AT&T presentation in its entirety to AT&T Attorney Gene Coker. The copy sent was the work copy being used by Mr. Craig and Mr. Majoros in their review of this area. It contained several handwritten notes of either Majoros or Craig and each page was numbered in the lower right hand corner. There were 40 pages in total.

1. Page 11 of AT&T's presentation is titled "Price Restructure - BRCS Savings." It contains an example which demonstrates that the Price Restructure resulted in an increase in the average cost of a BRCS I - Universal Line. This is shown by comparing the amount under "Current Pricing - BRCS I - $[redacted] to "Restructure -BRCS Universal - $[redacted] The increase is $[redacted]

2. BRCS I and BRCS Universal are equivalent to Residential - therefore the example demonstrates an increase to residential software?

3. Page 11 of AT&T example also shows a decrease to ESSX or CENTREX Software. This is demonstrated by comparing the "current pricing cost for BRCS II and BRCS III" which total $[redacted] ($[redacted] and $[redacted] to the "Restructured Price for BRCS ESSX" of $[redacted] The ESSX decrease is $[redacted]

4. Finally Page 11 shows that while overall BRCS cost went down from $[redacted] to $[redacted] the cost for residential went up by $[redacted] Was this the intent and result of the price restructure?

5. Turn to Page 33 of AT&T's presentation - titled "Price Restructure Study - GDX LU Price Comparison." Does this demonstrate that the price of a Line Card went up?

6. Turn to Page 34, titled GDX Line Unit. Does this demonstrate that the price of a LU frame went down but the price of a Line Card went up?

7. Are Line Units and Line Cards considered to be non traffic sensitive costs?

8. Turn to Page 35 of AT&T's presentation titled "Hardware and Software prices." Is the first benefit of the price restructure that it "Reduces impact of traffic sensitivity on growth plan"?

9. Does that mean that the price restructure shifted traffic sensitive growth costs to non traffic sensitive costs?

10. Turn to Page 39 of AT&T's presentation - titled "RTU Comparison." It shows software costs dropping from $[redacted] to $[redacted] to $[redacted] for 5E7. If the price restructure was revenue neutral, were these decreases picked up by non tariff sensitive costs e.g. Line Units and Line Cards?

BELLSOUTH TELECOMMUNICATIONS

38M66 Southern Bell Center
675 West Peachtree Street, NE
Atlanta, Georgia 30375

April 22, 1994

Mike Majoros
Vice President
Snavely & King
1220 L. St. N.W.
Washington, D.C. 20005

VIA FACSIMILE

Re: SBT's Response to the 25th Data Request-Set

Dear Mike:

At Don Craig's request, attached are the Company's non-proprietary responses to items #136 and 137. (As you will recall, our initial responses, including the attachments, are considered proprietary and were hand-delivered for your review during your last visit to Company premises.)

All audit-related proprietary information will be available for review in room 531 at SBC until April 30. After this date, proprietary responses, including those related to items 136 and 137, can be made available for your review at a mutually agreeable time and place.

As always, thank you for your cooperation.

Michele

Michele Young
404-529-8512



04-22-94 03:34 PM P03/06

BELLSOUTH TELECOMMUNICATIONS

38M66 Southern Bell Center
675 West Peachtree Street, NE
Atlanta, Georgia 30375

April 22, 1994

Don Craig
Audit Manager
Georgia Public Service Commission
244 Washington St. SW
Atlanta, GA 30334

VIA FACSIMILE

Re: SBT's Response to the 25th Data Request-Set

Dear Mike:

At your request, attached are Southern Bell's non-proprietary responses to items #136 and 137. (As you will recall, our initial responses, including the attachments, are considered proprietary and were hand-delivered for your review during your last visit to Company premises.)

All audit-related proprietary information will be available for review in room 531 at SBC until April 30. After this date, proprietary responses, including those related to items 136 and 137, can be made available for your review at a mutually agreeable time and place.

As always, thank you for your cooperation.

Michele

Michele Young
404-529-8512



04-22-94 03:34 PM P02/06

Southern Bell Telephone & Telegraph Co.
Georgia PSC Audit Request
Item No. 136
25th Data Request (SUPPLEMENT)
April 22, 1994
Page 1 of 1

REQUEST: The subject of this request is the 1991 AT&T price restructure.

a) What impact did the price restructure have upon line card prices?

RESPONSE: The Company's response to this item is considered proprietary but will be made available for review, at a mutually agreeable time and place, pursuant to the terms and conditions of the audit protective agreement between and among the parties.

This information constitutes financial data that reflects vendor-specific pricing negotiated by Southern Bell. Public disclosure of this information would impair Southern Bell's ability to contract for goods and/or services on favorable terms. In addition, AT&T may independently assert that public disclosure of this information could impair the ability of AT&T, which is not a party to this audit nor its protective agreement, to fairly compete in the marketplace for goods and services it provides to other potential purchasers.

INFORMATION PROVIDED BY: Steve Manion
Project Manager
675 W. Peachtree St., N.E.
Atlanta, GA 30375



04-22-94 03:34 PM P04/06

Southern Bell Telephone & Telegraph Co.
Georgia PSC Audit Request
Item No. 137
25th Data Request (SUPPLEMENT)
Page 1 of 2

REQUEST: The subject of this data request is the cost of line cards as they relate to the cost of a basic residence and basic business telephone lines.

a) Please confirm that the Company has prepared, from time to time, surrogate cost studies to estimate the cost of a basic residence and basic business line.

b) Please confirm that the cost studies discussed in a) above, reflect the Company's assumption that there are three cost causative factors which drive the cost of a basic business and residence line: 1) local loop, 2) switch usage, and 3) non-traffic sensitive cost.

c) Please provide a copy of at least one surrogate cost study prepared by the Company which clearly shows the three cost causers discussed in b) above. Also, please indicate who requested the initial study.

d) Regarding the surrogate cost study requested in c) above, please explain and demonstrate precisely how the 1991 AT&T price restructure would have impacted the cost study.

RESPONSE: The information being requested is proprietary. However, it will be made available for review, on Company premises at a mutually agreeable time and place.

This information constitutes financial data that reflects vendor-specific pricing negotiated by Southern Bell. Public disclosure of this information could impair Southern Bell's ability to contract for goods and/or services on favorable terms. In addition, AT&T may independently assert that public disclosure of this information could also affect the ability of AT&T to compete in the marketplace for the sale of its goods and services to other potential purchasers.



04-22-94 03:34 PM P05/06

Further, this information reflects measures of Southern Bell's costs of providing certain competitive or potentially competitive services. If disclosed publicly, such information could provide a competitive advantage to Southern Bell's competitors and, consequently, impair Southern Bell's ability to market its goods and services.

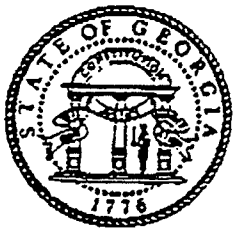
INFORMATION PROVIDED BY: Steve Manion
Project Manager
675 W. Peachtree St., N.E.
Atlanta, GA 30375



04-22-94 03:34 PM P06/06

COMMISSIONERS:

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# Georgia Public Service Commission

244 WASHINGTON STREET, SW
ATLANTA, GEORGIA 30334-5701

(404)656-4501 OR 1(800)282-5813

TRANSMITTAL NO. 32

May 17, 1994
DATE

5-19-94

Mr. Thomas L. Hamby
Assistant Vice President
Southern Bell
125 Perimeter Center West, Suite 397
Atlanta, Georgia 30346

J. Mauriello:
For your comment No. 24 (2 pages) is attached.
Don Craig
656-4549

Dear Mr. Hamby:

Enclosed are Audit Finding Worksheets for audit finding(s) Number 7-1 thru 7-4, 20, 21-1 thru 21-5, 22, 23, 24, 26, 27, 29, 32, 33, 34, and 36. The worksheets include the findings, causes of the problem and the auditor's recommendation for corrective action. Space is provided for auditee comments. Write in this area or on attached pages, the auditee's reaction to the findings, causes and recommended corrective action. Please have each person responding to the finding(s) sign the form or page(s) containing their statement.

I would appreciate a response to the findings no later than four weeks from the date of this transmittal. Please provide two complete sets to me in Room 267 at the above address.

After a review of the auditees responses, a final opinion regarding the audit findings will be formed.

Please sign and date the attached acknowledgement statement and return to me.

If you have any questions about this transmittal, contact me at 656-4549.

Yours very truly,

Don Craig

Don Craig
Audit Manager

ATTACHMENT(S)
DC:DP

AT&T
Network Systems

Dennis S. Pines
Senior Attorney

Western Electric® products
2600 Warrenville Road
Lisle, IL 60532-1084
708 224-2690
FAX 708 224-4477

June 14, 1994

Mr. Don Craig
Audit Manager
Georgia Public Service Commission
244 Washington Street, S.W.
Atlanta, GA 30334-5701

Re: Transmittal No. 32

Dear Mr. Craig:

AT&T is in receipt of your Audit Finding Worksheet No. 24, which suggests that AT&T's 1990 restructure of its hardware and software prices for AT&T's 5ESS® Switch System was specifically directed to concerns expressed by BellSouth Telecommunications Corporation. This is directly contrary to the information provided to you by AT&T's Switching Systems Business Unit.

Frankly, we are offended by the inference that BellSouth and AT&T were in collusion to restructure 5ESS Switch System prices to disadvantage consumers.

I am including an Affidavit from Richard F. Neri, Manager, Bids and Pricing, which states that the 1990 price restructure was national in scope and not directed to any single customer, including BellSouth Telecommunications Corporation. The same information was communicated to you repeatedly on at least three separate occasions which included several hours of interviews with representatives of AT&T Network Systems.

We believe that your Audit Finding No. 24 needs to be modified to eliminate the unsupported suggestion that the 1990 price restructure was "specifically directed to concerns expressed to AT&T Network Systems by BellSouth Services Property and Services Management" or any inferences that BellSouth and AT&T were in collusion to restructure prices to disadvantage consumers. The attached Affidavit establishes that any conclusions to the contrary based upon your interpretation of the correspondence and April 1990 presentation between BellSouth and AT&T are unfounded.

Recycled Paper

Finally, any suggestion that AT&T implemented the 1990 price restructure for BellSouth is simply contrary to the established fact that the 1990 price restructure was implemented on a nationwide basis.

Very truly yours,

Dennis S. Pines

Enc.

cc: (w/enc.)
Chairman Robert Baker, Jr.
Commrs. Mac Barber
Bob Durden
Robert Pafford
Robert Rowan

# AFFIDAVIT

State of Illinois:

County of DuPage:

I, Richard F. Neri, first being duly cautioned and sworn, make this Affidavit from my own personal knowledge:

1. I was the Manager, Bids and Pricing for AT&T's 5ESS® Switch systems from 1988 through 1991 and in such capacity was responsible for implementing pricing decisions and pricing policy for the 5ESS Switch System.

2. The 1990 restructure of hardware and software prices for the 5ESS Switch System was implemented in response to competitive pressures in the market for switching systems and changing market conditions.

3. AT&T conducted market research and analysis to determine whether its pricing of hardware and software for the 5ESS Switch System needed to be modified. After analyzing this market research information, AT&T determined that it should restructure its hardware and software prices for the 5ESS Switch System.

4. The 1990 price restructure was implemented on a nationwide basis, equally affecting all of AT&T's 5ESS Switch System customers and was not implemented in response to any request by a single customer, including BellSouth Telecommunications Corporation.

FURTHER AFFIANT SAYETH NAUGHT:

Richard F. Neri

State of Illinois:

County of DuPage:

Signed and sworn to before me on June 8, 1994 by Richard F. Neri.

OFFICIAL SEAL
JOYCE A ST JOHN
NOTARY PUBLIC STATE OF ILLINOIS
MY COMMISSION EXP. MAR 23,1998

Joyce A. St. John
Notary Public

ANALYSIS OF BSSI CPE EQUITY & NOI
ASSIGNED TO GEORGIA
($000)

| | 1988 | 1989 | 1990 | 1991 | TOTAL 1989-1991 |
|---|---|---|---|---|---|
| A. TOTAL BSSI EQUITY (END OF YEAR, INC. BSP) (JWC-56) | 93,845 | 199,464 | 179,421 | 198,365 | 577,250 |
| EQUITY: | | | | | |
| B. BSSI EQUITY (AVERAGE EXCLUDING BSP) (JWC-56) | 93,845 | 195,945 | 192,109 | 183,572 | 571,626 |
| C. RATE BASE ADJUSTMENT TO GEORGIA (SURVEILLANCE REPORT) | | 19,328 | 20,531 | 20,090 | 59,949 |
| D. % EQUITY TO GEORGIA (D=C/B) | | 9.86% | 10.69% | 10.94% | 10.49% |
| NET OPERATING INCOME (NOI) | | | | | |
| E. TOTAL BSSI NOI (EXCLUDING BSP & REFUND) (P.3) | | 32,528 | 21,547 | 20,240 | 74,315 |
| F. NOI ADJUSTMENT TO GEORGIA (SURVEILLANCE REPORT) | | 3,530 | 2,302 | 2,341 | 8,173 |
| G. % NOI TO GEORGIA (G=F/E) | | 10.85% | 10.68% | 11.57% | 11.00% |

| | 1989 | 1990 | 1991 | |
|---|---|---|---|---|
| EQUITY INCLUDED IN GEORGIA'S SURVEILLANCE REPORT'S RATE BASE ADJUSTMENT | | | | |
| H. BSSI RATE BASE ADJUSTMENT TO SURVEILLANCE REPORT (Line C) | 19,328 | 20,531 | 20,090 | 59,949 |
| I. CPE EQUITY INCLUDED IN RATE BASE ADJUSTMENT (PAGE 4,G * D) | 5,731 | 6,545 | 6,875 | 19,152 |
| NOI INCLUDED IN GEORGIA'S SURVEILLANCE REPORT'S ADJUSTMENT | | | | |
| J. BSSI NOI (EXCLUDING BSP & REFUND) ADJUSTMENT IN SURVEILLANCE REPORT | 3,530 | 2,302 | 2,341 | 8,173 |
| K. CPE PORTION OF NOI ADJUSTMENT (P4.H * G) | 479 | 199 | 151 | 828 |
| RETURN ON EQUITY | | | | |
| L. TOTAL GEORGIA BSSI ADJUSTED RETURN ON EQUITY (J/H) | 18.3% | 11.2% | 11.7% | 13.6% |
| M. CPE GEORGIA BSSI RETURN ON EQUITY (K/I) | 8.3% | 3.0% | 2.2% | 4.3% |
| N. RETURN EXCLUDING CPE ((J-K)/(H-I)) | 22.4% | 15.0% | 16.6% | 18.0% |

NOTE: THE GEORGIA RETURN ON EQUITY (ROE) RATIOS ON THIS PAGE ARE DIFFERENT THAN THE TOTAL BSSI ROE RATIOS ON PAGE 4 DUE TO THE REQUIREMENT TO ESTIMATE THE PORTION OF THE CPE OPERATIONS THAT WERE ALLOCATED TO GEORGIA. ALTHOUGH THE RATIOS ARE SLIGHTLY DIFFERENT, THE CONCLUSIONS ARE THE SAME. THE CPE OPERATION EARNED SIGNIFICANTLY LESS THAN NON-CPE OPERATIONS.

BELLSOUTH SERVICES - DATA BY PRODUCT GROUP
($000)

| | 1988 | 1989 | 1990 | 1991 |
|---|---|---|---|---|
| A. TOTAL BSSI EQUITY (END OF YEAR) (JWC-56) | 93,845 | 199,464 | 179,421 | 198,365 |
| B. TOTAL BSSI INVENTORY (END OF YEAR) (JWC-56) | 116,440 | 128,430 | 89,704 | 71,475 |
| GENERAL STOCK (EXCLUDING CPE & BSP) | | | | |
| C. AVERAGE MONTHLY INVENTORY (JWC-82) | 100,607 | 91,637 | 78,565 | 59,305 |
| D. MATERIAL COST OF GOODS SOLD (JWC-75) | | 391,028 | 376,844 | 223,596 |
| BSSI EUCE OTHER STOCK (PBX, KEY CPE, DOES NOT INCLUDE BSP) | | | | |
| E. AVERAGE MONTHLY INVENTORY (JWC-82) | | 32,559 | 29,142 | 12,217 |
| F. MATERIAL COST OF GOODS SOLD (JWC-75) | | [redacted] | [redacted] | [redacted] |

BELLSOUTH SERVICES

| | |
|---|---|
| G. TOTAL BSSI EQUITY AS OF 12-31-88 | 93,845 |
| CPE TRANSFERS TO BSS FROM ADVANCED SYSTEMS | |
| H. EQUITY 1-1-89 JWC-65) | 55,900 |
| I. LIABILITIES 1-1-89 (JWC-87) | [redacted] |
| TOTAL ASSETS TRANSFERED | |
| BSSI EQUITY INFUSIONS | |
| J. MARCH 1989 (JWC-65) | 30,000 |
| K. APRIL 1989 (JWC-65) | 20,000 |
| | 50,000 |
| TOTAL EQUITY TRANSFERRED TO BCS 1-1-92 | |
| L. "STRONG" RECOMMENDATION LETTER (JWC-68) | 62,600 |

Figures redacted at Company request.

BSSI NET INCOME ANALYSIS
($000)

| | 1989 | 1990 | 1991 * |
|---|---|---|---|
| A. TOTAL BSSI NET INCOME (JWC-56) | 32,502 | 366 | 18,945 |
| B. LESS BSP NET INCOME & INTERSTATE REFUND (SURVEILLANCE REPORT) | (26) | (21,181) | (1,295) |
| C. BSSI NET INCOME FOR SURVEILLANCE REPORTS (C=A-B) EXCLUDING BSP & $5.5M REFUND IN 1990 | 32,528 | 21,547 | 20,240 |
| GENERAL STOCK (EXCLUDING CPE & BSP) | | | |
| D. CONTRIBUTION REALIZED AFTER EXPENSES (JWC-75) ASSIGNED BY COMPANY FOR MATERIAL SOLD | 34,331 | 12,782 | 9,375 |
| E. EFFECTIVE TAX RATE (JWC-81 BSS NOI CALCULATIONS) | 33.9% | 33.5% | 33.4% |
| F. EFFECTIVE CONTRIBUTION TO NOI (F=D*(1-E)) | 22,693 | 8,500 | 6,244 |
| BSSI EUCE OTHER STOCK (PBX, KEY CPE, DOES NOT INCLUDE BSP) | | | |
| G. CONTRIBUTION REALIZED AFTER EXPENSES (JWC-75) ASSIGNED BY COMPANY FOR MATERIAL SOLD | [redacted] | [redacted] | [redacted] |
| H. EFFECTIVE TAX RATE (JWC-81 BSS NOI CALCULATIONS) | 33.9% | 33.5% | 33.4% |
| I. EFFECTIVE CONTRIBUTION TO NOI (I=G*(1-H)) | [redacted] | [redacted] | [redacted] |
| J. NOI CONTRIBUTION FROM SERVICES (P=I-L-O) | 5,426 | 11,184 | 12,692 |

Figures redacted at Company request.

BSSI RATE OF RETURN ON EQUITY ANALYSIS
TOTAL BSSI
($000)

| | EOY 1988 | EOY 1988 PLUS TRANSFER & 1/2 INFUSION | EOY 1989 | EOY 1990 | EOY 1991 |
|---|---|---|---|---|---|
| A. TOTAL BSSI EQUITY (END OF YEAR) (JWC-56) | 93,845 | 174,745 1/ | 199,464 | 179,421 | 198,365 |
| B. AVERAGE EQUITY ((BOY+EOY)/2) | | | 187,105 | 189,443 | 188,893 |

| BSSI EUCE OTHER STOCK (PBX, KEY CPE, DOES NOT INCLUDE BSP) | 1989 AVERAGE CPE EQUITY | 1990 AVERAGE CPE EQUITY | 1991 AVERAGE CPE EQUITY |
|---|---|---|---|
| C. INITIAL CPE EQUITY TRANSFER (JWC-56) | 55,900 | 55,900 | 55,900 |
| D. ESTIMATED CPE LIABILITY CONVERSION TO EQUITY | [redacted] | [redacted] | [redacted] |
| E. PREVIOUS NOI CONVERSION TO EQUITY | | | |
| F. ONE HALF NOI CONTRIBUTION (P.3I) | | | |
| G. AVERAGE CPE EQUITY (G=C+D+E+F) | | | 62,825 2/ |
| H. CPE NOI CONTRIBUTION (P.3I) | [redacted] | [redacted] | [redacted] |
| I. CPE RETURN ON EQUITY IN RATE BASE (I=H/G) | 7.6% | 3.0% | 2.1% |

| GENERAL STOCK AND SERVICES(EXCLUDING CPE & BSP) | 1989 | 1990 | 1991 |
|---|---|---|---|
| J. AVERAGE NON-CPE EQUITY (J=B-G) | 129,000 | 128,202 | 126,068 |
| K. NON-CPE NOI CONTRIBUTION (K=P.2, L+P) | 28,118 | 19,684 | 18,935 |
| L. NON-CPE RETURN ON EQUITY | 21.8% | 15.4% | 15.0% |

1/ 1/1/89 CPE transfer and 1/2 of the March and April equity infusion.
2/ This is corroborated by the amount of equity transferred to BCS on 1/1/92. See JWC-68 Company's "strong" recommendation letter.

Figures redacted at Company request.

Affiliate Transactions - BSC Allocator
Preliminary Finding No. 17

| | | |
|---|---|---|
| 1. | Total Retained Costs/Year (RBL 62B, Column F, Lines 7, 10 and 12) | $125,443,146 |
| 2. | Total Retained Costs/Month (Line 1 ÷ 12) | 10,453,596 |

3. November 1991 Allocation per RBL-57 ($000):

| | As Performed | With Retained |
|---|---|---|
| A. UNHQ | $109,558 | $101,416 * |
| B. SBTT | 458,107 | 458,107 |
| C. SCBT | 323,541 | 323,541 |
| D. BSBS | 18,863 | 18,863 |
| E. RETAINED | - | 10,454 |
| F. TOTAL | $910,069 | $912,381 |

| | | | |
|---|---|---|---|
| 4. | Percent SBT (Line B ÷ Line F) | 50.34% | 50.21% |
| | Percent Retained (Line E ÷ Line F) | 0.00 | 1.15% |
| 5. | Total Allocated in 1991 (RBL-62B, Col.B, Line 8) | | $19,662,336 |
| 6. | Amount which should have been retained (Line 4 x Line 5) | | $ 226,117 |
| 7. | Reduction in SBT percent (Line 4 difference) | | .13% |
| 8. | Reduction in SBT allocation (Line 5 x Line 7) | | $ 25,561 |
| 9. | Reduction in GA Allocation (Line 8 x .29) | | $ 7,413 |
| 10. | Reduction in Intrastate GA Allocation (Line 9 x .75) | | $ 5,560 |

* Reduced by amount transferred to BSC from BSE.

**BELLSOUTH**
**TELECOMMUNICATIONS**

**Thomas L. Hamby**
Assistant Vice President
Regulatory

Suite 397
125 Perimeter Center West
Atlanta, Georgia 30346
404 391-2450

August 23, 1994

Mr. Don Craig
Audit Manager
Georgia Public Service Commission
244 Washington Street, S.W.
Atlanta, Georgia 30334-5701

RE: Southern Bell's Responses to the Final Report of Audit Findings to be presented to the Commission

Dear Mr. Craig:

As agreed, we have attached Southern Bell's responses to the above referenced findings which were essentially transmitted to us on August 15, 1994. We are still receiving revisions to these findings as this transmittal package is being prepared. In addition, no summary of the Audit's findings has been received at this time.

Our assumption is that the final findings, as written, will be included in the report that will be filed with the Commission. The findings that were provided, however, are still stamped as DRAFT. If and to the extent the findings are amended, supplemented or edited, the Company reserves the right to conform its response. The Company's ultimate response to the audit also depends somewhat on the use which is made of the audit or further action by the Commission in reliance on the audit or any finding. The Company reserves the right to supplement or amend its responses in the event of such action.

The Company was still receiving revisions to the findings as late as 12:00 noon on the day the responses were to be transmitted. The Company has made a good faith effort to reflect these changes in its responses. However, the Company feels that it is unfair and unreasonable to receive these changes at such a late date. Furthermore, the Company's time to analyze and respond to the audit findings was unreasonably compressed. The Company considers it unfair and unreasonable that it was only provided approximately two weeks to review the audit findings.

In addition, certain of the draft Audit findings contain information which the Company considers, and has identified as, proprietary. As you are aware, access to proprietary information throughout the audit has been provided to you and

the Snavely & King auditors subject to the terms and conditions of the protective agreement. We will respond to findings and preliminary reports which contain proprietary material so long as such information will not subsequently be made public, published or shared outside the scope of the protective agreement.

Furthermore, if any page numbers in the auditors' report have been changed prior to the Company's last draft copy, please note that the Company often refers to specific pages in the report and those numbers would need to be changed accordingly.

We appreciate the opportunity to address the audit findings prior to issuance of the final report.

Please feel free to contact me with any questions concerning this matter. A copy of Southern Bell's responses has been sent to Snavely and King on this date by overnight mail.

Sincerely,

Assistant Vice President

Attachment

Copy to: Snavely, King & Associates, Inc.

## SUMMARY

Beginning in October, 1992, Southern Bell has cooperated with the Commission Staff and its outside consultants in an audit, supposedly related to affiliated transactions. The Company has expended countless employee-hours in assimilating documents and copies of documents for the auditors' review, providing interviews and explanations of the Company's policies, procedures and systems, and otherwise assisting the auditors. Most recently Company representatives have worked closely with the auditors to refine and correct preliminary findings. Through this process, a number of the more obvious and gratuitous miscalculations, misunderstandings, and erroneous conclusions have been eliminated. Some remain. As the close of the process draws near[1], the Company's overall assessment and reaction to the audit findings can be summed up in with three basic points:

First, the Company is pleased with the inescapable conclusion that it strictly adheres to and applies the rules and regulations of this Commission. In other words, after nearly two years of intense scrutiny by

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[1]To date, Southern Bell has not been provided with a copy of the final report as it is to be presented to the Commission. The findings provided are still in draft form. However, the Company is advised that the findings will not be changed after the Company's final review. If and to the extent that any finding is amended, supplemented or edited, the Company reserves the right to conform its response. The Company's ultimate response to the audit also depends somewhat on the use which is made of the audit or further action by the Commission in reliance on the audit or any finding. The Company reserves the right to supplement or amend its responses in the event of such action.

It should also be noted that as late as 12:00 noon on the day the Company's responses were to be transmitted to the auditors, the auditors were still making changes to their findings. The Company made a good faith effort to reflect these changes in it's responses to the findings.

Staff and consultant auditors involving the review of thousands of pages of documentation, and countless hours of on-site discussions with a large number of Company employees, the auditors identified only 27 scant areas[2] falling into only 5 major categories even worth addressing in the Report. There is a vastly larger number of processes, accounting practices, and types of transactions which received a clean bill of health.[3] This was expected by the Company and should be good news to the Commission.

At the same time -- and this is the second point -- the Company is disappointed in the audit. The Company cooperated from day one, and has taken every reasonable step to help the auditors understand its practices and procedures. Despite these efforts, the auditors have persisted with a

---

[2]This is not to say that the Company accepts or agrees with the substance of these 27 findings. They are, in fact, seriously flawed. As will be discussed in more detail later in the summary, roughly 20% acknowledge the Company is strictly adhering to this Commission's rules or other mandates; another 20% acknowledge that no error was detected or simply recommend further expensive, time consuming audits anyway, and at least one identifies transactions that actually benefitted Georgia ratepayers. See eg. Finding No. 15, Report at III, p. 84.

[3]In fact, several finding note the proprietary of some of these processes. For example, Finding No. 13 states "[t]he audit verified that Southern Bell's investment accounting process for the equipment transfers [between jurisdictions] and inventory controls are proper and that the depreciation reserve calculation process which is used by the Company follows the affiliated transaction rules." Report at III, p. 72. See also, Finding No. 9, Report at III, p. 48. "It likely that complete reconciliation was effected...in connection with the Company's annual true-up of central office equipment."

number of findings which can only be characterized as remarkable, particularly in light of the ultimate audit objective as stated in the report. While possibly repetitious, that objective bears repeating here. It reads:

> (8) to receive a report of all instances of non-compliance with this COMMISSION's rules concerning transactions with affiliates (FCC - Section 32.27), allocation of costs between regulated services and non-regulated activities (FCC - Section 64.901) and all indications or instances of illegal acts that could result in criminal prosecutions (these may be reported separately).

Report at II, p. 4.

What is astonishing is not the objective. It is plainly stated and makes sense. The astonishing part is that in several findings the auditors recommended "penalizing" the Company in some form or another for strict adherence to the Commission's rules.

Finding No. 2, Tax Allocation is an example. "Rule 32.27(e) requires the use of stand-alone accounting tax calculations for carriers who are parties to consolidated tax returns." Report at III, p. 17. As is correctly pointed out in footnote 1 to the Report, Commission Rule 515-3-1 "requires telephone companies to follow FCC rules governing cost allocations and affiliate transactions." Report at II, p. 3, footnote 1. Even so, the auditors reject the Company's application of stand-alone accounting. Findings No. 3 and 4 are similarly flawed.

Similarly, with regard to Finding No. 1, which discusses the Company's Leveraged Employee Stock Ownership Plan, the auditors do not dispute the Company's claim that its treatment of the dividend deduction for tax purposes is dictated by Generally Accepted Accounting Principles ("GAAP"). Report at III, p. 6. The auditors simply reject GAAP. In Finding No. 5, which attacks the Company's method of accounting for accumulated deferred taxes and unamortized investment tax credits, the auditors acknowledge that there are private letter rulings supporting that methodology.[4] In Finding No. 8, which criticizes the Company's treatment of MemoryCall[R] as regulated for intrastate reporting purposes, the auditors challenge the view that MemoryCall[R] is regulated in Georgia. Perhaps if the auditors had been here a year earlier they would have a clearer understanding. Even so, they provide a quote to an open hearing before this Commission in which the Company witness stated in response to a question from Commissioner Rowan and follow-up questions from the Assistant Attorney General:

> It to me is a legal argument of whether it was regulated or non-regulated, and we appealed to the FCC to try to resolve that issue. But from the standpoint of the earnings report, since the Georgia Commission had ruled and that was the rule of the day, then the non-regulated -- previously non-regulated investment expenses for MemoryCall[R] were included in the intrastate results starting in June of 1991.

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[4]Private letter rulings are not binding authority except for the party seeking the ruling. However, one can scarcely imagine the Internal Revenue Service imposing a diametrically opposed application of the tax code on another party.

Report at III, p. 44.

In roughly 20% of the findings, the auditors acknowledge the authority cited by the Company, but recommend some penalty anyway. In several of these cases, the auditors are urging the Commission to act in flagrant and arbitrary disregard for and in violation of its own rules. Assuming such action would be legally sustainable, which it would not, it would create a policy of absolute uncertainty among regulated utilities which ultimately would work to the detriment of ratepayers.

The third category can only be characterized as disappointment and frustration at the lack of objectivity displayed by the outside consultants. In Finding No. 11, the auditors suggest that somehow Southern Bell prevailed upon AT&T to restructure to shift cost from expense to capital based on the incredible premise, the auditors argued that Southern Bell was able to charge lower rates for its competitive services at the expense of basic ratepayers. This finding is nothing short of absurd. That is what the Company has explained repeatedly and that is what AT&T has explained. On June 14, 1994, AT&T provided to each Commissioner the affidavit of Richard F. Neri. Mr. Neri explained that AT&T's decision to restructure its hardware and software prices was the result of "market research and analysis." Moreover Mr. Neri pointed out that the "1990 price restructure was implemented nationwide, equably effecting all of AT&T's 5ESS[R] Switched System customers. It was not implemented in response to any

[R]5ESS is a registered trademark of AT&T

request by a single customer, including BellSouth Telecommunications Corporation." Key representatives of Southern Bell have explained repeatedly, and in many forms, that the auditors findings are unfounded. Southern Bell employed Deloitte & Touche to conduct an independent analysis of the impact of the price restructuring. This major accounting firm concluded that the auditors findings were totally erroneous. The auditors simply shrug off the overwhelming weight of this evidence and persist on the basis of copies of several slides from an AT&T marketing presentation designed to pique the Company's interest in additional switch purchases. The company believes that this reflects a blatant lack of objectivity.

In Finding No. 14, without any reference or citation to the basis for the statement, the auditors contend that the Company's primary motive for supporting such regulatory reform was to enhance its opportunity to cross-subsidize regulated services and to shift costs from competitive to non-competitive services. Senate Bill 566 did not pass. One wonders why the auditors make this finding at all. Whatever the auditors motives, political commentary and speculation on the Company's or anyone's motives in the legislative process are far removed from the scope of any credible audit. The finding might be appropriate on the editorial pages of a newspaper, but has no place in a formal audit.

In the final analysis, the Company is disappointed with what the audit contains, but at the same time it is pleased with what the audit did not say. There are far more practices, procedures, and transactions that were scrutinized and given a clean bill of health than were the subject of finding in this audit. When the absurd, the speculative, those findings noting compliance with the Commission's rules or other mandates, and those reflecting extreme subjectivity are eliminated, the result is a complementary picture of Southern Bell which indicates no further action is required by the Commission.[5]

[5]Contrary to the auditors' assertion in Finding No. 14 in which the auditors imply a sense of urgency for resolving the audit issues, for the various reasons pointed out in the Company's responses, the findings are seriously flawed and no further action is required.

FINDING/RECOMMENDATION:

The special tax benefits of the Company's Leveraged Employee Stock Ownership Plan should flow to regulated operations.

COMPANY RESPONSE:

The Company does NOT agree that the Commission should adjust Georgia's earnings to include an allocated share of the BellSouth tax savings associated with the dividend payments. The auditors have used a seriously flawed analysis, ignored factual data provided by the Company, and are not cognizant of more recent developments all of which would lead to a different conclusion than that recommended by the auditors.

First, the dividend payments, which result in the tax savings, are made by BellSouth Corporation, on BellSouth Corporation common stock, from equity earnings. The financial accounting employed for the ESOP tax benefit is required by GAAP. For federal tax purposes, BSC is the only entity legally entitled to the tax benefit. The tax savings do not result from expenses charged to subsidiaries, and therefore, they are not allocated to the subsidiaries.

Second, the fundamental concept of any LESOP is based upon growth in stock price and dividends which, accordingly, reduce the cost of the LESOP versus a non-leveraged. This would result in lower expenses for the Company and ratepayers over the LIFE of the plan. However, the audit has focused on a relatively short period of time (1990-1992), while the BellSouth plan covers a 13 year period. The analysis and subsequent decision to adopt the LESOP occurred during 1989 and early 1990, a period of good national economic conditions. Subsequent to the adoption of the plan, the national economy took an unforeseen severe downturn, which adversely affected financial markets, generally, and BellSouth's stock price specifically. The auditors' recommendation ignores factual data which clearly demonstrates that BellSouth's common stock has regained and sustained significant market value well above the earlier period and well in excess of the Trustee's cost per share. In fact, in 1994 the existence of the ESOP has resulted in LOWER costs to Georgia ratepayers. Based on current projections, the stock losses incurred during the recessionary period will be recovered over a very short period of time.

Third, the analysis is defective and, thus inappropriate, as regards several key points based upon a review of the backup workpapers which were provided.

CALCULATION OF 1993-1994 INCREASED COSTS

The calculation of the increased cost for the period of 1993-1994 incorrectly assumes the EXACT same set of circumstances that existed during

COMPANY RESPONSE (Cont'd.):

1990-1992. In fact, actual data for all of 1993 and through August of 1994 is contrary to the auditors' assumptions.

Assumed Stock Loss[1]

The analysis of the assumed stock loss is inappropriate. The stock loss calculation used PROJECTED data for 1993-1994 based on results during 1990-1992. In 1993, BellSouth's stock price rose from $51.75 to $58.00 (10.8%), which was well above the Trustee's cost per share. Using actual 1993 stock prices, there was a $3.3 million gain which would offset the earlier expense increase. Furthermore, if the BellSouth stock increases only 6% in 1994, there would be an additional ESOP gain of $7.1 million. As of 7/31/94, the BSC common stock had sustained an average daily closing share price in 1994 of $60 or more per share with highs approaching $63 per share. (Many independent market analysts continue to place a "buy" recommendation on BSC stock, reflecting continued appreciation of the stock.) The combined gain would more than offset the stock loss of $7.3M shown on Appendix D, page 3, line 10. The auditors' assumption of a continuing stock loss is without foundation.

Interest Expense[1]

The narrow time period (1990-1992) in the audit analysis assumes that interest expense and the shares allocated accrual methodology will yield the same results over the remaining life of the leveraged features. This is contrary to the actual operation of the plan. For example, the auditors have assumed interest expense in the years of 1993 and 1994 remain, on average the same as in the past (Appendix D, page 3, line 8). Since the ESOP debt is an amortizing security, interest expense is high in the early years and declines in the later years as the outstanding principle is reduced. The actual average interest expense for 1993-1994 is less than the average interest expense during 1990-1992. (For example, interest expense was $74.8 million in 1991 and $67.9 million in 1993.) The auditors' assumption that interest expense will remain essentially unchanged is contrary to the actual debt obligation.

[1]The audit report in Appendix D, Page 3, line 16 notes that the auditors, after numerous discussion with the Company, have considered increases in stock price and decreases in loan interest in their calculations. However, the actual impact of these items is significantly higher than what the auditors have included in their calculations, and it would continue to increase in future years.

COMPANY RESPONSE (Cont'd.):

RISK ASSUMPTION

In the reports' Recommendation, the statement is made, "...the local telephone company ("OTC") must assume the risks and costs associated with the [ESOP] loan and value of the stock purchased." This is an incorrect understanding of the ESOP obligation. As set forth in the debt offering for the ESOP, there is no obligation ascribed to Southern Bell or any other subsidiary of BSC. BSC is ultimately and solely the guarantor of the debt obligation.

ADMINISTRATION COSTS

The report makes reference to the administration costs of the LESOP (Appendix D, page 4, Note f) based on information originally provided the Company in prior years. Subsequent to that response the LESOP and BSC modified the treatment of such administrative costs. Effective January 1, 1993, certain administrative costs incurred by BSC were recovered from the trust. In turn, the Trustee began to recover administrative costs of the ESOP from individual plan participants (e.g. employees) using a schedule of annual and transaction fees, as more fully described in the 1993 SEC Form 10-K for the ESOP plans. Consequently, BSC has materially reduced the costs it has incurred in the operations of the plan and those passed down to subsidiaries.

CONCLUSION

In conclusion, the Company disagrees with the audit's finding of the existence of a cross-subsidy, or the need for either a one-time or continuing NOI adjustment to the Georgia Surveillance Report. The tax accounting related to the dividends arises solely because BSC, not SB, common stock is used to provide the matching obligation and because BSC, not SB, dividends are used to service the debt obligation, which is the actual legal obligation of BSC, not SB. (BSC, not SB, advanced the funds to make the first debt service payment to the ESOP. BSC will not recover those funds from the participating subsidiaries until the end of the 13 year leverage period.) As demonstrated in the information provided to the auditors, each participating company bears the direct expenses of the employee benefit plans and shares in the attendant cost reductions. Thus, no cross subsidy exists. Furthermore, the Company disagrees with the assertion that the tax benefit should be assigned to Southern Bell because such assignment would be contrary to GAAP and the current tax code.

COMPANY RESPONSE (Cont'd.):

CONCLUSION

Finally, in proposing the NOI adjustments to Georgia Surveillance Report, the auditors have employed a seriously flawed methodology which results in a distorted projection. Any LESOP is designed and intended to reduce costs over the life of the plan. The wide-spread adoption of the LESOP is a testament to its financial attractiveness. A complete analysis of BSC LESOP's performance to date demonstrates that it is currently doing so. The auditors have used selected, non-representative data upon which it has based the proposed NOI adjustments. Accordingly, the NOI adjustments as proposed are inappropriate.

FINDING/RECOMMENDATION:

The Company has achieved a significant cross-subsidy from its regulated operations and BAPCO to its nonregulated operations as a result of its filing of consolidated tax returns. The cumulative tax savings should be deducted from the Company's rate base.

COMPANY RESPONSE:

The Company thinks this finding is remarkable since the objective of the audit was to find "all instances of non-compliance with the Commission's rules concerning transactions with affiliates (FCC-Section 32.27)" and yet the auditors state that the cause of this Finding is the Company's "strict adherence to FCC Rule 32.27(e)."

Tax expense for Southern Bell is appropriately determined on a stand-alone basis, which as the auditors state is in compliance with Part 32. Moreover, this finding incorrectly asserts that the "stand-alone tax expense calculations enables a cross-subsidy from profitable regulated operations to unprofitable nonregulated operations." In fact, the converse is actually true. If the regulated entity's tax liability has been correctly calculated, and that fact has not been challenged, then to reduce the regulated liability by losses generated by nonregulated operations results in a subsidy to the regulated operations.

The Company believes that any consolidated tax adjustment is inherently unfair and inappropriate since the tax benefits derived from filing a consolidated return are a result of shareholders' investments in unregulated enterprises which are not supported nor insured by the ratepayers. The Commission would be instituting a change in policy for all regulated utilities and not just BellSouth because the adjustment recommended by the auditors would impact all regulated entities that file consolidated returns. In addition, an adjustment to rate base of any past consolidated return benefits would constitute inappropriate ratemaking.

A basic principle of regulation is the separation of regulated utility operations from nonregulated operations. This principle is achieved related to income taxes when the stand-alone concept is applied to the calculation of current income taxes. Under this concept, the tax law is applied on an entity by entity basis. The result is that the current expense for the regulated utility reflects the impact of the activities of the regulated utility and only those activities. In other words, if BellSouth had chosen not to invest in any unregulated operations after divestiture, Southern Bell (and Southern Bell-Georgia) would have recorded

COMPANY RESPONSE (Cont'd.):

the same tax expense for the years 1988 through 1991 as were actually recorded. Even though some unregulated operations may have initial losses, the assertion by the auditors that "the regulated operations subsidize a portion of the initial losses by being charged with overstated taxes" is incorrect. The stand-alone concept results in each company recording its true separate company tax liability. The FCC recognizes the fairness of this concept by requiring stand-alone tax expense calculations under Rule 32.27(e). The Georgia PSC has adopted Part 32.

The auditors also assert that the regulated utility will not share in any of the profits once an unprofitable unregulated company becomes profitable. The Company believes that the principle of regulation should be upheld maintaining the separation of the regulated utility operations from the unregulated operations. Under the Company's current procedures, the regulated operations do not share in either the losses or the gains from the nonregulated operations.

Furthermore, the auditors are incorrect that any benefit from filing a consolidated tax return is permanent. Although such filing allows the group to use a group member's loss in the current year, that member company would have been able to use that loss itself when it became profitable. The auditor's "Example" illustrating a supposed subsidy is flawed in that it fails to reflect the fact that the consolidated return prevented the nonregulated entity from using its own loss in Year 1 to reduce its income tax liability from $3,500 to $0 in Year 2.

In addition to the basic inequity of their position, the impact of $44.7 million which the auditors estimate to be the benefits of consolidation attributed to Georgia are grossly overstated. Profitable unregulated operations have provided substantially all the tax payments necessary to appropriately compensate the unprofitable unregulated operations for the benefits of their tax attributes contributed to the consolidated group. As a result, there is no consolidated benefit to be attributed to Georgia.

It should be clear that the adjustment is simply incorrect, but the Company would note that if the Commission were to make the recommended adjustment, this would constitute an unlawful taking of Southern Bell's property in contravention of the 14th Amendment to the United States Constitution as well as analogous provisions of the Georgia Constitution. In addition, under the federal decisions in Hope and Bluefield, as well as the case authority in Georgia, Southern Bell is entitled to an opportunity to earn a reasonable return on its investments dedicated to the provision of

COMPANY RESPONSE (Cont'd.):

regulated services in this state. Artificially reducing Southern Bell's tax expenses generated by its regulated operations, by considering matters outside the jurisdiction of this Commission, would violate these legal requirements.

Georgia's rates were set based on consistent estimates in accordance with clearly accepted methods of determining tax expense (in terms of tax law, FCC, and Georgia PSC requirements). Any attempt to engage in retroactive ratemaking back to 1984 would be inappropriate and unlawful.

In conclusion, the tax expense as reported on the Georgia surveillance report is the true tax expense incurred by Southern Bell-Georgia; therefore, the Commission should not make any adjustments to Georgia's earnings or rate base.

FINDING/RECOMMENDATION:

Income tax expense charged to regulated operations should not be used to subsidize the losses of nonregulated products and services offered by Southern Bell Georgia.

COMPANY RESPONSE:

The tax calculation for Georgia's regulated operations has been made correctly and the auditors do not challenge that calculation. In addition, the auditors do not challenge the calculation for the unregulated operations when the operations generate income. As is typical of this audit, however, the finding asserts that the properly calculated regulated obligation should be offset by losses associated with Southern Bell's unregulated operations. This is another example of the auditors recommending an inconsistent policy with regard to recording tax expense. The auditors only objective appears to be the assignment of all costs to the unregulated operations and all benefits to the regulated operations regardless of which operation generates the benefits.

While the finding asserts that this adjustment should be done in order to avoid subsidizing unregulated operations, the converse is true. If the regulated operation's tax liability has been correctly calculated, then requiring that the properly calculated regulated tax obligation be reduced by losses in the unregulated area, actually results in a subsidy to the regulated operations. Stated more simply, if the regulated operations of Southern Bell generated $1,000 in tax liability, but ratepayers were only required to pay $800 because of losses in the unregulated area, then it is the regulated operations that are receiving a subsidy.

The Company disagrees with this finding and does believe that if the Commission were to make the recommended adjustment, this would constitute an unlawful taking of Southern Bell's property in contravention of the 14th amendment to the United States Constitution as well as analogous provisions of the Georgia Constitution. In addition, under the federal decisions in Hope and Bluefield, as well as the case authority of Georgia, Southern Bell is entitled to an opportunity to earn a reasonable return on its investment dedicated to the provision of regulated services in this state. Artificially reducing Southern Bell's tax expenses generated by its regulated operations, by considering matters outside the jurisdiction of this Commission, would violate these legal requirements.

FINDING/RECOMMENDATION:

The Commission should instruct the Company to match benefits to related costs.

COMPANY RESPONSE:

As was the case in the second finding, the Company thinks this finding is remarkable since the objective of the audit was to find "all instances of non-compliance with the Commission's rules concerning transactions with affiliates (FCC-Section 32.27)" and yet the auditors state that the cause of this finding is the Company's "strict adherence to Part 32."

The auditors have used a "snapshot" approach to make a recommendation contrary to the Commission's rules, while ignoring similar issues that have a different impact. Following the auditor's recommendation would result in a violation of Part 32 and also would result in a policy change affecting all regulated utilities, not just BellSouth.

In 1978, Southern Bell did not recognize a customer's deposit as income for book or tax purposes because this money was eventually returned to the customer. The IRS disagreed with this treatment for tax purposes and argued that customer deposits should be recognized as income when the customer paid it to Southern Bell. In 1983, Southern Bell paid the tax and interest calculated back to 1978. As a result, deferred tax expense was credited and deferred tax liability was debited. The interest expense was excluded from regulation.

In 1990, the IRS conceded this issue to Southern Bell and as a result, in 1991, refunded the taxes (which had been paid in 1983) and paid Southern Bell interest calculated from 1978 to 1991 (which was partially a reimbursement for the interest expense paid in 1983). Southern Bell recorded the interest received from the IRS and excluded it from regulation, in accordance with Part 32, and reversed the debit to the deferred tax liability.

If Southern Bell had not prevailed in this argument with the IRS, the debit to the deferred tax liability would have remained on the books (continuing today at a potentially even higher balance). This outcome would also mean that Southern Bell should have had a debit to the deferred tax liability beginning in 1978 (i.e., under the auditor's reasoning, Southern Bell's rate base would have been UNDERstated from 1978 to 1983). In addition, Southern Bell still would have incurred the interest expense paid in 1983 and excluded it from regulation.

COMPANY RESPONSE (Cont'd.):

Southern Bell does not win every disagreement with the IRS. When Southern Bell does not prevail, audit settlements with the IRS have the result of understating rate base, for a period of time. Therefore, the auditors have singled out this one situation and asked the Commission to make an adjustment to the Company's records without giving similar weight to the situations where Southern Bell's rate base is understated and where Southern Bell is required to exclude interest expense from regulation.

The Company feels that the current treatment of excluding interest income and interest expense from regulation, is in accordance with Part 32, and is fair and appropriate. Therefore, the Company recommends that the Commission make no adjustment to its treatment of interest income. However, if the Commission decides to implement the recommendation of this finding, the Commission would have to apply the same treatment to interest expense which would result in higher expense to the ratepayer.

FINDING/RECOMMENDATION:

Accumulated deferred taxes and unamortized investment tax credits which represent taxes charged to regulated operations should not be transferred to nonregulated operations. Case-by-case burden of proof concerning any IRC violation belongs with the Company.

COMPANY RESPONSE:

The auditors acknowledge in the audit finding that they are aware of previous IRS private letter rulings in which the Government has concluded it is a normalization violation if a public utility flows through unamortized Investment Tax Credits (ITC) to its ratepayers in conjunction with assets which are no longer in the Company's rate base. Nevertheless, in their recommendation the auditors insist that the Company should not transfer unamortized ITCs to nonregulated operations. This issue is not a choice or a decision which is made by the Company. The IRS position applies to all public utility property which is subject to the IRC's normalization provisions, not just that of BST.

Prior to the creation of a separate entity in 1985, the CPE assets attributable to Southern Bell - Georgia's ASI line of business were already segregated from the Company's regulated operations in Southern Bell's books of account and booked on a below-the-line basis. Similarly, the assets which were transferred in 1991 to BellSouth Communications, Inc., had been assigned or apportioned to nonregulated on Southern Bell's books. Thus Southern Bell - Georgia's regulated customers were not charged the tax expense associated with the unamortized ITC on these assets; and accordingly, were not rightfully entitled to the related benefit. The audit report states that the auditors examined the actual journal entry associated with the BCI transfer and noted that the taxes were appropriately allocated to nonregulated. As a result, the Company is unclear what concerns the auditors had with this transaction.

Regarding the 1987 and 1989 asset transfers to BellSouth Services (BSS), the Company continued to amortize the ITC relating to these assets on BSS' books of account. In 1989, the ratepayers began receiving the related tax benefits through BellSouth's policy of dividending BSS' earnings back to Southern Bell. This dividending was obviously a benefit to the ratepayer.

Lastly, the auditor notes that Southern Bell - Georgia retained the accumulated deferred income taxes associated with the 1989 transfer of an airplane to BSS. It should be understood that this transaction was an intercompany sale accounted for in accordance with Internal Revenue Code sections 1501 and 1502, and not an asset transfer.

FINDING/RECOMMENDATION:

The Commission should be cognizant that the Company derives benefits through deferred tax activity in rate case years and non-rate case years.

COMPANY RESPONSE:

The Company thinks this finding is remarkable since the objective of the audit was to find "all instances of non-compliance with the Commission's rules concerning transactions with affiliates (FCC-Section 32.27)" and yet the auditors state this finding "does not identify any violation of GAAP, Part 32, or IRC provisions." The Company records its book transactions, including deferred income tax expense, in accordance with Generally Accepted Accounting Principles (GAAP) and files its tax return in accordance with the Internal Revenue Code (IRC). As a result, this issue is not a choice or decision which is made by the Company. Any change to the treatment of deferred taxes would involve a change in policy which would impact all regulated utilities, not just BellSouth. Therefore, the Company feels this finding has no merit.

Southern Bell Telephone & Telegraph Co.
Georgia PSC Staff Audit
Response to Findings
Item No. 7
September 1, 1994
Item No. 1 of 1

FINDING/RECOMMENDATION:

Georgia PSC auditors should be provided access to all income tax returns and related workpapers.

COMPANY RESPONSE:

This finding is based on the same misunderstanding of the Company consolidated tax return as is evidenced in finding No. 2. As stated in the response to that item, the Company is in full compliance with all the FCC's rules, Part 32 and the Internal Revenue Code. Georgia's tax liability is calculated on a stand-alone basis and the tax liabilities of the nonregulated affiliates are not relevant to that calculation.

In addition, this finding is totally without merit since the Company has: (1) provided a detailed reconciliation of the Southern Bell (SB) income tax return liability to the Georgia intrastate tax expense and (2) also has reconciled the SB tax return to the BellSouth Corporate (BSC) tax return. Over the course of the audit, Company personnel from the Tax and Comptrollers organizations have spent approximately 10 employee days with the auditors answering tax-related questions and providing reconciliations. Additional discussions with Company personnel occurred during follow-up sessions.

For reconciliation purposes, financial information for the SB nonregulated entities and other states was provided. Two detailed reconciliation packages dated September 15 and September 20, 1993, were developed and submitted to the auditors. These packages (over 30 pages) provided a detailed reconciliation of the 1991 SB tax return liability to the intrastate tax expense per the December 1991 surveillance report. Also, the packages included a detailed comparison (for both SB and Georgia) of the 1991 federal income tax expense to the 1991 tax return as filed.

Furthermore, a reconciliation of the SB tax return to the BSC tax return was provided during discussions with the auditors in September, 1993. Access to the individual returns of the nonregulated affiliates was not necessary as discussed above, since Georgia's federal income tax expense is based solely upon Georgia's state specific income.

This finding is wholly without merit. The recommendation that access to all tax returns and workpapers be provided is completely unnecessary for the reasons discussed above. Ample data was provided for the auditors to ascertain the complete compliance and appropriateness of all relevant tax calculations.

FINDING/RECOMMENDATION:

The Company should be chastised for adding MemoryCall[R] losses to the Surveillance Report without notifying the Commission and the Company's failure to file tariffs and supporting cost of service studies.

COMPANY RESPONSE:

The Company is in full compliance with all Commission orders regarding MemoryCall[R]. Details concerning the report's specific findings are provided below.

FILING OF TARIFF

Southern Bell has not been ordered by the Commission to file a tariff covering the provision of MemoryCall[R]. As this finding was originally cast, the auditors concluded that Southern Bell had failed to file a tariff in disregard of Commission orders in Docket No. 3896-U. The Company pointed out to the auditors that those orders (Docket No. 3896-U, March 5, 1991; April 2, 1991) were stayed by the Fulton County Superior Court on April 5, 1991. Southern Bell Tel. & Tel. Co. v. Georgia Public Service Comm'n, et al., Civil Action File No. D-86218.[1]

The auditors have now shifted their analysis to Docket No. 4000-U (the correct docket), but continue to strain to reach the conclusion that the Company should have filed a tariff. The auditors state, "[i]t appears Southern Bell determined, on an informal basis, how it intended to interrupt and implement the various provisions of the order in Docket No. 4000-U." Report at III, p. 41. In fact, Southern Bell petitioned the F.C.C. to preempt the Commission's "freeze" on the provisions of MemoryCall[R], which the F.C.C. did. The F.C.C.'s preemption was upheld by the Eleventh Circuit Court of Appeal on September 22, 1993. However, one might construe the F.C.C.'s preemption order and subsequent court appeals, these actions were not informal. During the course of the litigation, and until this day, the Commission has abstained from further action regarding MemoryCall[R] and has never ordered the Company to file a tariff.

[R]MemoryCall is a Registered Trademark of BellSouth Telecommunications

[1]NOTE: The Fulton County Superior Court action was eventually dismissed without prejudice because the orders referred to had been superseded by later orders of the Commission. Southern Bell Tel. & Tel. Co. v. Georgia Public Service Comm'n, et al., Dismissal of Petition for Review without Prejudice, Civil Action File No. D-86218, September 2, 1992.

COMPANY RESPONSE (Cont'd.):

The auditors have overlooked or ignored other important developments in Docket No. 4000-U since the May 21, 1991 order.[2] On July 26, 1991, the Georgia Association of Telemessaging Services ("GATS") filed a petition asking the Commission to clarify its earlier order. In pertinent part, GATS asked the Commission to clarify the Commission's intentions regarding tariffing of MemoryCall[R]. GATS urged the Commission to avoid any interpretation of the May 21 order that would involve a tariff to diminish the likelihood that the F.C.C. would preempt regulation of MemoryCall[R]. The issue of whether the Commission should ultimately require tariff filings was squarely raised before the Commission.

Provision of MemoryCall[R] has received intense scrutiny by the Commission and other parties to Docket No. 4000-U. During the course of the audit, the Company has made every effort to explain the record in the various MemoryCall[R] proceedings. In fact, in their report, the auditors include a portion of the transcript of a hearing before this Commission. The pertinent portion of the quote bears repeating here. In an open hearing, before all the Commissioners, the Staff, the CUC and other parties, the Company's witness stated:

> But from the standpoint of the earnings report, since the Georgia Commission had ruled and that was the rule of the day, then the non-regulated -- previously non-regulated investment expenses for MemoryCall[R] were included in the intrastate results starting in June of 1991.

[2]NOTE: The auditors have likewise overlooked a protracted dispute which resulted in litigation regarding the Commission's and its Staff's ability to enter into a protective agreement. The detailed cost information sought by the Commission in its Order is confidential trade secret information entitled to protection under Georgia law. The Company and Staff eventually worked out an arrangement through which Staff reviewed the cost data. It was not filed because the Commission took that no mechanism exists which would have afforded the information protection while in the possession of the Commission. More recently, the Commission has initiated a rule-making, in response to an order of Fulton County Superior Court, to create such a mechanism. In any event, the Staff has had access to and has reviewed the cost data.

[R]MemoryCall is a Registered Trademark of BellSouth Telecommunications

COMPANY RESPONSE (Cont'd.):

This statement was made before the Commission on February 19, 1992. If there was doubt before this point, which the Company would dispute, there was certainly no doubt after this point regarding the treatment of MemoryCall[R].[3]

Finally, two facts are noticeably absent from the finding which make it impossible to respond fully. First, there is no reference to the factual basis upon which the auditors conclude that the Commission is unaware that MemoryCall[R] is being treated as regulated for intrastate reporting purposes. In fact, the contrary appears to be the case. Second, the auditors failed to point to any rule or regulation of this Commission which would require the Company to notify the Commission that it is complying with the Commission's orders. The simple fact is that on May 21, 1991, the Commission entered an order stating its clear intention that MemoryCall[R] be regulated. The Commission went in to an elaborate discussion regarding its jurisdiction in the order. Immediately following the effective date of the Order, Southern Bell took an appeal from one portion of the order and implemented that portion which was final and from which no appeal was taken. No further action was contemplated, ordered or necessary.

MemoryCall[R] OPERATIONS

The basic assertion that MemoryCall[R] is losing money is predicated on a fully distributed cost methodology which drives significantly more costs to unregulated operations than is appropriate. Similarly, it is not possible to determine the "profitability" of a product based on its allocated and fully distributed cost, as was the case here.

Also, virtually all new products and services introduced in any business involve "up front" investment commitments and "start up" costs which begin before the product or service is offered for sale. It is not practical or feasible to expect that such costs can be fully recovered by sales revenues in the initial years. Typically, such costs are recovered over a number of

[R]MemoryCall is a Registered Trademark of BellSouth Telecommunications

[3]NOTE: Contrary to the auditors' report, this not the only reference in a record acknowledging that MemoryCall[R] was being treated as regulated for intrastate reporting purposes. There are others. However, this one was so obvious and so unambiguous that no others had been provided.

COMPANY RESPONSE (Cont'd.):

years. In other words, the cash flow in the early years of most products and services is negative due to this mismatch of costs and revenues. As additional units are sold over time, a crossover is realized and a net profit or contribution is generated over the life cycle of the product or service. This is especially the case with MemoryCall[R] since it is a capital intensive service.

The conditions also totally overlook the contribution from the tariffed service charges which MemoryCall[R] pays the regulated operations similar to any other Enhanced Service Provider. Also, the results do not include complementing network services (CNSs) such as "call forwarding busy line/don't answer" and Message Waiting Indicator (MWI) which are frequently used in conjunction with MemoryCall[R] mailboxes.

Beyond this, the Company would note that it was temporarily forced out of selling MemoryCall[R] for approximately 8 months by the Commission and precluded from providing the service in portions of Georgia other than the Atlanta area for over two years. Consequently, even if there were any merit in the auditors comments regarding "profit", MemoryCall[R] is still a new product whose marketing has been limited over the past few years, which clearly would affect its profitability. Furthermore, investment costs and other ongoing expenses for the service continued because the MemoryCall[R] network structure remained in place in anticipation of customer demand.

CONCLUSION

Southern Bell is in full and complete compliance with all rules, regulations and orders of this Commission regarding MemoryCall[R]. Furthermore, the assertion that MemoryCall[R] is losing money is inappropriately predicated on a fully distributed cost methodology, overlooks tariffed service charges and complementing network services and ignores the "start up" nature of MemoryCall[R].

[R]MemoryCall is Registered Trademark of BellSouth Telecommunications

FINDING/RECOMMENDATION:

Southern Bell's construction program should be regularly audited.

COMPANY RESPONSE:

The auditors focused a great deal of attention on the MemoryCall[R] construction program. This inordinate scrutiny revealed only (1) a misclassification which existing controls identified and corrected on a real-time basis, (2) a minor misclassification of $28,500 and (3) a one month timing difference associated with an input file in the Company's Cost Separation System (CSS). The above issues are all minor in nature, and do not require that the Company's "construction program ... be regularly audited".

With regard to the first issue, in November 1990, the Company did erroneously assign some MemoryCall[R] investment as regulated investment. However as noted in the report, this discrepancy was detected as part of the Company's normal review of the monthly CSS cost allocation activity in December 1990. An adjustment was made in December 1990 to move the investment from regulated to dedicated nonregulated. Therefore, there was NO cost allocation impact and the MemoryCall[R] investment was correctly reflected both in CSS and on the Georgia Surveillance Report.

Regarding the second issue, MemoryCall[R] right-to-use fees of $28,500 in estimate M-1418 were originally booked incorrectly to capital instead of expense. However as noted in the report, an adjustment was made in May, 1993 to move the right-to-use fees from capital (Account 2212, 377C) to expense (Account 6212, 377M).

In regard to the last issue, the report notes that this simply was a timing difference due to a one month lag between the Company's Detailed Continuing Property Record (DCPR) and its Cost Separation System (CSS). The DCPR file is an input for identifying investment for CSS. Each month's DCPR file is processed by CSS the following month. Furthermore, each year the investment in CSS is synchronized with the DCPR investment after completion of an annual true-up of central office equipment. This ensures that all regulated and nonregulated investment is appropriately reflected in CSS.

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[R]MemoryCall is a Registered Trademark of BellSouth Corp.

FINDING/RECOMMENDATION:

Right-To-Use fees should be directly assigned whenever possible.

COMPANY RESPONSE:

In January 1993, the Company independently developed the methodology and system changes which were necessary to revise the Cost Separation System (CSS) allocation process to directly assign software right-to-use fees to regulated or nonregulated whenever possible. This allows MemoryCall[R] software right-to-use fees to be directly assigned to nonregulated.

Prior to January 1993, a methodology did not exist for the Company to directly assign right-to-use fees between regulated and nonregulated operations. Prior to 1993, all software right-to-use fees in Account 6212 were considered common and were allocated based upon the related central office investment. The vast majority of right-to-use fees are entirely regulated but these too were included in the apportionment process.

Furthermore, the Company did consistently use the Cost Allocation Manual's (CAM) Account 6212 direct cost pool during the entire period of 1989-1993. This direct pool was initially established and used for Equal Access/Network Reconfiguration investment in June 1989. The pool was also subsequently used for leased to others investment (e.g., Shared Network Facilities Agreement) until January 1993. As stated above, methodology was developed and implemented in January 1993 to directly assign right-to-use fees.

[R]MemoryCall is a Registered Trademark of BellSouth Corp.

FINDING/RECOMMENDATION:

The Commission should investigate the implications of a 1990 switch price restructure and increase its audit scrutiny of BellSouth to ensure that basic business and residential ratepayers are protected against cross-subsidies.

COMPANY RESPONSE:

Apparently, the auditors have concluded that the expense decrease negotiated by the Company with AT&T was offset by increased capital expenditures. In addition, the auditors have reached the conclusion that AT&T's price restructure resulted in a shift from competitive services to noncompetitive services. These allegations are unfounded and in fact, the subject price restructure and associated contractual arrangements resulted in reductions in overall switch expenditures which is what the Company intended to achieve from the outset.

The auditors have repeatedly been provided proof refuting all of their allegations. Numerous meetings between the auditors and Company SMEs (including an Officer) were facilitated to address the auditors' "issues". Actual Firm Price Quotes, for both initial and growth switch projects (pre and post restructure) were also provided and explained in excruciating detail. These quotes, actual contracts, price lists, surrogate cost studies and other documentation have repeatedly demonstrated beyond a reasonable doubt that price restructure and associated contractual arrangements have resulted in an overall switch cost reduction, thereby benefiting the ratepayers of Georgia. Further, these efforts have also proved that AT&T's price restructure did **not** result in a shift of expense to capital.

First, contrary to the Auditors' inferences, AT&T's price restructure had no relationship to Southern Bell's 1990 switch award. Rather, each approved switch vendor was invited to reply to a Request for Quotation (RFQ) and both AT&T and Northern Telecom were awarded switches based on responses to this RFQ. Therefore any insinuation that the central offices awarded to AT&T were due to price restructure is unfounded.

Second, the insinuation that Southern Bell was involved in a deliberate shift of central office costs from expense to capital is unfounded. The analog line card was the **only** hardware (capital) item that increased in list price as a result of price restructure. As the auditors correctly noted, the line unit (a capital item) decreased in price. It should also be noted that the switch module (also a capital item) decreased in price. As previously stated, comparisons of pre and post price restructure jobs

COMPANY RESPONSE (Cont'd.):

(initial and growth) clearly indicate that there was no shift from expense to capital, and in fact there was an overall reduction in both capital and expense costs.

Third, in regards to the auditors contention that there has been a shift from competitive (i.e., ESSX$^{R}$) to noncompetitive residential and basic business services, the Company has repeatedly explained the following points:

A. 70% of Georgia lines-in-service during the audit period were analog. Every analog line, whether it be a residence, basic business or an ESSX$^{R}$ line, must have access to a line unit. Since analog line cards are used with all classes of service (basic business, residence or ESSX$^{R}$) any price increase associated with line cards would not benefit or act to the detriment of any particular customer group. In addition, contrary to the auditors' findings in footnote #38, the Company has provided the auditors evidence that the price of capitalized operating system software did not change as a result of the price restructure.

B. The auditors were correct that BRCS I supported basic business and residence lines prior to Universal BRCS. Universal BRCS contains six additional features that were never included in BRCS I. Since each of these additional features (i.e.- cancel call waiting, call hold, automatic callback calling, call forwarding-busy line, call forwarding-don't answer-all calls, and distinctive ringing) has value and revenue potential, it is not feasible to make a simple comparison between the BRCS I and Universal BRCS feature packages. The only possible inference that can be derived is that Universal BRCS became more feature rich, and thereby potentially more valuable, at the expense of BRCS ESSX$^{R}$. (The six additional features contained in Universal BRCS were removed from the BRCS ESSX$^{R}$ feature package).

C. Basic business and residence customers actually benefited from the regrouping of a greater number of non ESSX$^{R}$-specific features which became available coincident with this restructure. These features allow SBT to market contribution-rich services to these customers which help offset the cost of basic service. It is also important to note that there has been no increase in basic business or residence service rates as a result of this restructure.

Fourth, as the auditors' have independently corroborated with AT&T, price restructure was implemented nationwide and was in no way unique to BellSouth. Obviously, the concerns expressed by one customer, albeit a

COMPANY RESPONSE (Cont'd.):

major one, would not cause an overall nationwide change in AT&T's switch pricing. Therefore, the allegation that the restructure was specifically directed to concerns expressed to AT&T Network Systems by BellSouth is clearly unfounded.

AT&T is outraged by this allegation and sent an unsolicited letter to the PSC audit manager with a copy to all the Commissioners. An affidavit was attached to the letter signed by an AT&T employee involved in the restructure testifying in no uncertain terms that the restructure was a result of market research conducted by AT&T.

Fifth, these allegations were sufficiently important, and objectionable, to Southern Bell that the Company retained an unaffiliated third-party Consulting/Accounting firm to investigate this matter in detail and to provide an unbiased expert opinion. This firm's conclusions agree with the Company's position in this regard and find no merits in any of the auditors' allegations.

As a final note, even in the face of extensive analyses provided by the Company to the auditors, AT&T's independent challenge to the auditors' conclusions, and the analyses of a major accounting firm's independent review, the auditors continued down the wrong track. This displays most poignantly the auditors' lack of objectivity.

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[R]5ESS is a registered trademark of AT&T
[R]ESSX is a registered trademark of AT&T

FINDING/RECOMMENDATION:

The inclusion of BellSouth Services' net income and equity in the Surveillance Report provided a subsidy for its nonregulated CPE products and masked the over-earnings on sales to the regulated operations.

COMPANY RESPONSE:

This finding indicates a failure on the part of the auditors to understand the relationships between SB and BSS and between SB and its customers. It also fails to recognize that moving the BSS dividend and investment above the line is a further protection to the ratepayer.

The auditors' confusion about the relationship between BSS and SB and the relationship between SB and its customers has led the auditors to make a number of erroneous conclusions. The auditors' statement that "Business CPE was an unprofitable line of business and never should have been added back to regulated operations" is based on confusing the two relationships. CPE was a nonregulated line of business at SB and was always treated as nonregulated on SB books. BSS was not in the CPE business and had no losses related to CPE.[1]

The Company will address these issues by discussing the following points:

1. BSS/SB Relationships and SB/SB Customer Relationship,
2. BSS' billing methodology,
3. CPE Operations,
4. BSS Equity,
5. Handling of BSS Income and Investment for Ratemaking.

[1]BSS did have a nonregulated subsidiary, BellSouth Products, (BSP) which marketed certain CPE products. However, as noted in the auditor's report, BSP results were not included in the BSS dividend and investment which were included in intrastate results.

COMPANY RESPONSE (Cont'd.):

**BSS/SB RELATIONSHIP AND SB/SB CUSTOMER RELATIONSHIP**

The auditor has confused the relationship between BSS and SB with the relationship between SB and its customers. A description of the two relationships is provided below:

BSS/SB Relationship

BSS provided many centralized services to SB. As one of its services, BSS maintained inventory for SB. Whether this inventory was used by SB for regulated operations or nonregulated operations was completely irrelevant to BSS. BSS charged SB for the cost of purchasing inventory, expenses related to handling the inventory, and a cost of capital. (For further details see section on BSS' billing methodology below.) The provision of inventory to SB was NOT an unprofitable business for BSS. This is true whether BSS was providing SB with CPE inventory or non-CPE related inventory.

SB/SB Customer Relationship

SB, in turn, used the inventory it purchased from BSS in both its regulated and nonregulated operations. If it was used for regulated customers, it was booked to regulated operations. If it was used for CPE customers, it was booked to nonregulated operations. Revenues from regulated customers were booked to regulated operations and revenues from CPE customers were booked to nonregulated operations on SB's books. Any losses from CPE were booked entirely to nonregulated operations on SB books. CPE losses remained in nonregulated operations on SB books and were NEVER "added back to regulated operations."

**BSS' BILLING METHODOLOGY**

As discussed above, BSS was, in essence, a cost center, which provided goods and services to its clients, primarily SB and SCB. For services and goods that it provided the telcos, BSS determined their costs on a fully distributed basis, added the allowable rate of return, and charged the telcos the resulting figure. For instance, if SB needed CPE for a customer, BSS determined the cost of the CPE and then added to that cost the expenses associated with handling the CPE, including a predetermined cost of capital. If BSS provided SB with a service, instead of CPE, it followed the same path. It determined the cost of the service, added any other expenses incurred, including a cost of capital, and billed SB. It was irrelevant whether CPE was involved or any other service, BSS determined the cost, added a cost of capital, and billed the result to SB.

COMPANY RESPONSE (Cont'd.):

The cost-of-capital methodology was specifically designed to ensure that cross-subsidization did NOT occur. Earnings requirements for BSS were determined based on the overall allowable rate of return. This earning requirement was assigned to pools of operating units with similar asset usage in proportion to the assets in the pool. A cost of capital loading was then calculated for each pool to achieve the overall allowable rate of return. By using this methodology, the cost of capital for each type of asset took into account different usage and turnover rates.

If it were CPE that was being billed to SB, SB would record the charge as an unregulated expense, and if it resold the CPE to a customer, would record the revenue from the sale as unregulated revenues. If it were a regulated service, SB paid for the service out of regulated funds. In either event, the charges to SB from BSS were based on the same overall rate of return. Any calculation by the auditors that purport to show that BSS earned a different return on its investment in CPE as opposed to the other services it provided, is simply incorrect. Such a conclusion is at odds with both the theory and the facts which underlie BSS's billings.

Obviously no subsidy occurred, because the price SB paid BSS for CPE and the revenues received from the end user were all treated as unregulated services. The ratepayers were not affected because every service and product were marked up to achieve its share of the earnings requirements.

**CPE OPERATIONS**

The audit report is incorrect in its allegation that any CPE losses or inventory write-downs impacted the regulated ratepayer. All CPE losses were booked entirely to nonregulated by Southern Bell. The Company's accounting for the CPE inventory write-downs was also appropriate and it ensured that the regulated ratepayer was not adversely impacted. Any CPE inventory write-downs were subsequently billed to Southern Bell and South Central Bell and booked as a revenue deduct to CPE nonregulated revenues (Account 5280). This accounting only impacted nonregulated operations.

**BSS EQUITY**

As stated above, earnings requirements for BSS were determined based on the overall allowable rate of return. The auditor's report is flawed in its attempt to assign equity to business segments. The Company could not and did not assign equity investment to its business segments.

COMPANY RESPONSE (Cont'd.):

With the reintegration of ASI, $55.9 million of equity was infused into BSS. This equity consisted of approximately $32.6 million of inventory and $23.3 million of cash equivalents and other assets. The inventory was used to fulfill SB and SCB's needs, which were either regulated or nonregulated depending upon the ultimate usage. The inventory may have been used by SB to provide CPE to external customers or to provide equipment for telco internal needs. The $23.3 million of cash equivalents and other assets were utilized by all BSS operations, consisting of providing services and products to the telcos. These assets reduced the need for additional funding from other sources.

The auditor's use of $55.9 million as CPE equity is erroneous. As discussed above, the absolute maximum amount of assets deployed for CPE was the $32.6 million in inventory. If the auditor had recognized this in his calculation, his return for CPE would have been significantly higher and his return for regulated would have been significantly lower. This was discussed with the auditors on numerous occasions. This further shows the erroneous nature of the auditor's assumptions and conclusions.

Furthermore, the audit report is incorrect in its allegation that "the Company increased the add-back to its regulated rate base merely by relieving BSS of its liability for advances from other affiliates." In 1989, BSS did receive equity infusions of $20 million and $30 million from SB and SCB. However these equity infusions were not related to CPE but were necessary to reduce the level of advances from the telephone companies. At times these advances reached a threshold where management deemed it appropriate to reduce them with equity infusions. These equity infusions (and all BSS equity) were utilized by all BSS operations, which consisted of providing general services and products to its clients. These assets reduced the need for additional funding from other sources to support BSS' normal operations. The needs for continuous funds was evidenced by prior and subsequent telco funding to BSS for ongoing operations.

## HANDLING OF BSS INCOME AND INVESTMENT FOR RATEMAKING

As an additional protection for the ratepayer, all earnings by BSS were returned to SB and SCB in the form of dividends. For intrastate ratemaking purposes, the telephone companies included both their investment in and dividends from BSS in above-the-line accounts, thereby further ensuring

COMPANY RESPONSE (Cont'd.):

that profits from BSS operations were returned to intrastate ratepayers. Therefore, intrastate ratepayers were not overcharged by BSS. Furthermore, as stated in the auditor's report the treatment of the investment in BSS and its net income were specifically considered in Southern Bell's Rule Nisi (Docket 3905-U) proceeding and this treatment was allowed. Specifically, a BSS dividend of $3,530,021 and BSS investment of $19,328,907 were used in the Rule Nisi rate setting. This resulted in an 18.3% rate of return and a reduction in revenue requirements for SB-Georgia.

The audit report is correct that the refund for BSS alleged overearnings in connection with the FCC audit was booked to interstate operations only. However, that accounting was entirely appropriate since any alleged over earnings were already in intrastate operations through the BSS dividend. In addition, it should be noted that Southern Bell and South Central Bell also voluntarily reduced their plant accounts by $3.9 million. Approximately 75 percent of that reduction did get assigned to intrastate operations.

**CONCLUSION**

The auditors have misunderstood the role of BSS and its billing methodologies. BSS applied a cost of capital to all products and services and this methodology was specifically designed to ensure that cross-subsidization did not occur. Earnings requirements (not equity) were assigned to pools with similar asset usage. This prevented BSS from subsidizing CPE and over earning on regulated operations. Furthermore, the inclusion of the BSS dividend and investment in intrastate results was an added protection to the ratepayer.

FINDING/RECOMMENDATION:

The calculation and booking process used to record transfers of equipment between regulated companies should be mechanized to prevent errors.

COMPANY RESPONSE:

The report correctly concludes that Southern Bell is "...correctly following the rules governing the transfer of regulated assets from one jurisdiction to another..." and it states that "no errors were noted in the data reviewed..." The concern expressed is that the process of recording the transfers is not mechanized and it should be in order to prevent errors and expedite the journal processing. As stated in the report, SB is planning to mechanize this process. Current plans are for system testing in the fourth quarter of 1994 with implementation by second quarter 1995. This should alleviate any concerns raised by this finding.

FINDING/RECOMMENDATION:

Recent legislative and regulatory initiatives increase the urgency of eliminating subsidies found in this audit.

COMPANY RESPONSE:

SENATE BILL 566

The comments, observations and conclusions made by the auditors with respect to Senate Bill 566 (S.B. 566) are completely misleading and reflect a total lack of objectivity on the part of the outside consultants. Political commentary and speculation on the Company's or anyone's motives in the legislative process are far removed from the scope of this or any credible audit. This finding might be appropriate on the editorial pages of a newspaper but has no place in a formal audit.

First, Southern Bell did not propose S.B. 566. Southern Bell has no seat in either Chamber of the General Assembly. Instead, the bill was co-sponsored and introduced by four highly regarded, well-respected members of the State Senate. As stated in the preamble to the bill actually introduced, S.B. 566 was designed to recognize and prepare the State of Georgia for monumental changes taking place in the telecommunications industry. The bill sought to secure the benefits of these changes for the citizens of this state. Without a doubt, Southern Bell strongly supported the measure.

The auditors contend that the Company's primary motive for supporting such regulatory reform was to enhance its opportunity and incentive to cross-subsidize between regulated and deregulated services and to shift cost from competitive to non-competitive services. They further assert that under such legislation, the Company would have the "unrestricted ability" to set prices, without regard to cost for competitive services.

There were absolutely no provisions in S.B. 566 that would have permitted the Company to perpetrate such abuse. This legislation did not propose to deregulate any services. The Commission was given the authority to deregulate services. It has that authority today. See O.C.G.A. 46-2-23(b)(1). Tariff filing for regulated services would have continued.

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Note: Contrary to the Report, the bill was not withdrawn. It was not voted out of committee. However, both Chambers passed resolutions establishing study committees to examine issues related to telecommunications and local competition.

COMPANY RESPONSE (Cont'd.):

Price levels for all non-basic services would have continued to exceed long run incremental costs. The Commission would have maintained full regulatory oversight over all regulated services to assure that consumer and competitive safeguards are adhered to.

In fact, under this legislation the prices for basic services would have been capped at existing levels for three years, after which they could only have been raised, if at all, by the rate of inflation. In other words, the opportunity to shift costs to the "captive customers" would have been virtually eliminated, rather than enhanced. It is misleading to refer to these as indexed price increases. To suggest that costs, and thus prices, can be shifted from competitive to non-competitive, optional services is purely speculative and completely unrealistic in either the current environment or in the environment envisioned under S.B. 566. Eventually, competition would drive the price for all services. In their analysis, the auditors do not even mention the fact that Southern Bell, or any other LEC, would have to, in effect, surrender its local franchise in order to obtain the regulatory flexibility which they describe in subjective and misleading terms.

The auditors' assertions, on the surface, would indicate that they have a fundamental misunderstanding about S.B. 566 and also do not fully understand the current regulatory oversight process utilized by the Commission in tariff filings. However, a considerable amount of time and effort was expended in order to educate them in that regard. Regardless, it is not an auditor's role to argue policy. An auditor tests whether policy, as reflected in current rules and procedures, is being followed. Political posturing and prognostication have no place in "audits."

FINDING/RECOMMENDATION:

The Company's regulated vs. nonregulated cost allocation process should be subjected to continued and increased audit scrutiny.

COMPANY RESPONSE:

As stated by the auditors in the report, these transactions had no adverse impact on Southern Bell's regulated activities in Georgia.

Public Telephone Voice Messaging Service (PTVM) was never offered to the public in Georgia. As stated in the auditor's report, the assignment of overhead costs to nonregulated PTVM operations by the Company's Cost Separation System (CSS) benefited the Georgia ratepayer.

The revenues associated with Customer Dialed Account Recording (CDAR) have been assigned to regulated. The revenues were assigned to regulated operations because the costs associated with modifying the Company's billing system (Customer Record Information System - CRIS) were significant when compared to the product's small revenues, particularly since CDAR service represents an older declining technology that will eventually be eliminated. However as stated in the report, the expenses were properly assigned to nonregulated operations, and ratepayers again benefited from this transaction.

FINDING/RECOMMENDATION:

The auditors recommend the use of positive time reporting for BellSouth's and Southern Bell's legal departments.

COMPANY RESPONSE:

This finding is incorrect in its assertion that current time reporting procedures and controls are inadequate, particularly in the legal area. The recommended use of positive time reporting for legal would be a costly, work intensive effort. The Company and the entire industry are currently attempting to make time reporting procedures more cost effective (e.g., statistical sampling time reporting for certain network employees). The recommendation for additional positive time reporting would be moving in the opposite direction.

The Company's response is provided below in the following areas; BST Time Reporting and cost allocation, Job Function Code audits, and the BSC allocation of legal costs.

BST TIME REPORTING AND COST ALLOCATION

The time of each employee is assigned to a Job Function Code (JFC) as determined by an analysis of that employee's work. Once the assignment is made, it is updated periodically or when the employee's work content changes. The employee uses "exception time reporting" when the employee does something totally outside the scope of his or her normal duties, i.e., does work that would not normally fall within one of the JFCs used by that employee.

The assignment of the employee's time to the various JFCs could be audited by anyone who chooses to do so. In conducting such an audit, the auditor could determine whether the employee's time was properly apportioned. Daily time records are not necessary to achieve this same result.

During 1988-1991, departmental JFC representatives were responsible for training employees in the use of JFCs and for coordinating appropriate JFC changes. In October 1993, the responsibility for performing accounting data reviews was centralized in the Comptroller's Time Reporting Administration and Compliance group.

This group now performs semiannual JFC reviews utilizing statistical sampling. Adjustments and changes are made if appropriate. Also, effective in the fourth quarter of 1993, a monthly report of non-monetary payroll changes (e.g., employee moves, changes, etc.) is being generated and sent

COMPANY RESPONSE (Cont'd.):

to segment accounting coordinators. These segment accounting coordinators are responsible for reviewing their employees' JFCs and initiating any changes that may need to be made. This provides an effective control to ensure that JFCs are updated when employees' responsibilities change.

Furthermore, the auditor's recommendation "that the cost pools to which Legal Department time is assignable include nonregulated, interstate and intrastate"... is not appropriate. First, the Company's Cost Allocation Manual (CAM) includes a direct regulated/nonregulated cost pool in Account 6725 (legal expense) and that cost pool is used. Secondly, interstate and intrastate allocation is handled via the Part 36 Separations rules and not by CAM cost pools.

The above described procedures and controls regarding Job Function Codes and exception time reporting are more than adequate to ensure that BST's legal costs are appropriately allocated to regulated and nonregulated activities. Additional burdensome positive time reporting by BST legal is not necessary since their efforts are generally associated with activities within BST and they do not provide legal services for nonregulated subsidiaries.

JOB FUNCTION CODE AUDIT

The statement that there were no audits of the Legal Department is misleading. As noted in the auditor's report, there was a JFC audit in 1991 and members of the Legal Department were included as part of the universe that was sampled. All SB employees were included in the audit sample, and the sample was selected so that it would be statistically valid at the 95% confidence level for the universe of all employees.

BSC ALLOCATION OF LEGAL COSTS

The auditors state that 88 percent of a certain BSC attorney's (R. Frost Branon) time was assigned to regulated. Actually only about 63 percent of his time was charged to intrastate regulated operations. Approximately 88 percent of Branon's time was billed to telephone operations. Of this amount billed to the telcos, approximately 95 percent would have been assigned to regulated operations within the telco, and approximately 75 percent of that amount would have been charged to intrastate operations.

COMPANY RESPONSE (Cont'd):

Furthermore, in request JWC-49, the auditors asked for a list of all of BellSouth's legal filings in 1991, which was provided together with the name of the attorney that worked on the filing during that period. The auditors did not sufficiently review the underlying work to determine whether it involved regulated or unregulated activities. In addition, the auditors did not ask whether Mr. Branon worked on other matters during the relevant period. Consequently, the auditors did not ask for sufficient information to reach their conclusion.

In reviewing the limited historical information requested, the auditors failed to consider or inquire concerning changes in the time reporting procedures which have taken place since 1991. Upon consolidation of the BellSouth and BellSouth Enterprises Headquarters organizations, the combined Legal Department implemented procedures for regular periodic time and expense reporting. These procedures were implemented because of the increased BellSouth Legal Department work for unregulated entities which occurred following combination of the two organizations. Prior to that time, most legal work for BellSouth Enterprises companies was performed by the BSE Legal Department, rather than at BSC. Accordingly, this finding is unnecessary and without merit as to both its factual basis and conclusions.[1]

The auditors could have sufficiently explored the allocation of Mr. Branon's time to determine whether the Company had properly allocated it. They did not, and as a result, this finding is without support.

[1]As explained in a previous section, these procedures are not required for the BST legal department due to the nature of their work.

FINDING/RECOMMENDATION:

Chaining calculations relating to affiliated transactions should recognize operations, such as BAPCO, which are treated as regulated at the intrastate level.

COMPANY RESPONSE:

This finding includes several inaccurate statements and conclusions which are explained below.

BSE did not incur an excessive lease payment. The difference in the two leases is explained by various benefits received by BSE such as private lobby area, first choice of floor space, floor location, etc. which are not quantifiable for purposes of the financial comparison performed. Although these differences are important, BSE nevertheless adjusted the potential chained overage each year to avoid even any possibility of regulatory noncompliance.

Further, this finding, even as asserted, no longer has any basis because BSE ceased leasing space in the 1100 building in 1994.

This finding is also in error because it draws incorrect distinctions concerning BAPCO. Neither BAPCO nor its earnings are deemed regulated by the FCC. Further, BAPCO is in an intensely competitive business and "treating it as regulated" for this purpose is beyond the Commission's jurisdiction. The C&L audit and potential chaining calculation were thus validly performed.

In addition, BSE's management fee to BAPCO was calculated as a percentage of BAPCO's expenses so BSE's incurred lease costs did not affect BSE charges to BAPCO or reduce BAPCO's net income in any way.

Further, in various analyses related to management fees, BSE has demonstrated that overall costs of BSE incurred on behalf of subsidiaries greatly exceeded charges to its subsidiaries. BAPCO is included in each of these analyses. Even if "excess" lease costs alleged by the audit team were deducted from fully distributed costs or overhead rates in these analyses, allocations computed in compliance with the JCO would still greatly exceed actual charges billed to all subsidiaries, particularly BAPCO. The Georgia audit team has had the opportunity to review these analyses in the C&L workpapers and yet failed to recognize or acknowledge this fact.

COMPANY RESPONSE (Cont'd.):

The audit team's recommendation that the Commission have access to the books and records of the unregulated affiliates is wholly without merit; these documents are not in the possession, custody or control of the regulated entity. The C&L workpapers contain sufficient information for a full and complete audit and support the responses above.

Based on the above, the audit team's recommendation that the Commission impose strict monitoring of BSC's affiliate leases demonstrates an astonishing lack of understanding of the stringent rules with which BSC is already in compliance. The FCC has already imposed "strict rules governing...allocations of expenses" in order to avoid cross-subsidization; therefore, the recommendation for more restriction is inappropriate and without basis. The requirements proposed would be both burdensome and unnecessary.

FINDING/RECOMMENDATION:

Sunlink's Corporate cost allocation process provides an opportunity for the regulated telephone operations to subsidize BellSouth's nonregulated commercial ventures. If Southern Bell is unwilling to calculate the portion of Sunlink's lease price increases which flow into regulation, the total amount of the leases should be disallowed.

COMPANY RESPONSE:

This finding is incorrect and reflects a lack of understanding of the information provided and reviewed and the allocation procedures therein described. This finding includes many incorrect statements, the most significant of which are corrected in this response.

- The finding ignores obviously material facts in stating "During the 1987-88 time period, the auditors noted that there were significant increases in the lease prices per square foot at the Birmingham and Jacksonville locations."

  As was documented to the auditors, these rate increases were not the result of any changes in accounting techniques or mechanization of the cost allocation system. While it is true that mechanization of the cost allocation system represented a change for Sunlink in 1991, it neither caused a substantial increase in cost allocations used for comparison purposes only nor did it effect lease rate charges which were established through contract negotiations several years prior to 1991.

  Contract negotiations and lease agreements between Sunlink and BST management are typical of arms-length transactions in the industry whereby rates are established based on the real estate market at the time of negotiations. Amenities, concessions, condition, and value of the property are all considered in these transactions and factored into the negotiated rate. New leases for the Jacksonville and Birmingham warehouses were negotiated in 1987 and 1988 respectively. It is reasonable that rates for the entire space leased changed from previous leases which were at or near their expiration for several reasons. First, real estate market rates would have obviously changed between 1984 and 1987, even absent the inflationary real estate market. Also, additional space, improvements, and amenities, which increased the value of the space overall, were added to each of the warehouses based on the requirements of BST as follows:

COMPANY RESPONSE (Cont'd.):

(Birmingham): A warehouse addition and improvements were made to the interior of the administrative facility by Sunlink. The addition consisted of 120,000 square feet of warehouse space plus loading dock and additional paved area. The additions required by BST increased the original cost- per-square-foot of the building by 36%.

(Jacksonville) Prior to July, 1987, 188,274 square feet of space were leased and were billed at approximately $2.00 per square foot. An addition of 97,978 square feet of office and warehouse space was made bringing the total leased space to 286,252 square feet. The additions increased the original cost-per-square-foot of the building by 30%.

These additions and cost-per-square-foot data can be observed easily through review of the C&L workpapers. Also, numerous publications exist to support market rental rates in these areas as well as inflationary trends in the economy. The remaining major incorrect statements are corrected below:

- Contrary to this finding, complete information necessary to evaluate FDC and overhead calculations was provided on numerous occasions. The C&L workpapers contain the complete FDC analysis with all components included. C&L also retains relevant lease documentation in their files. They compute FDC per square foot for the warehouses which was compared to actual lease rates to show that FDC exceeded lease rates in every case through 1991. Abundant evidence to support the pricing of warehouse rentals charged to BST was clearly provided and corporate overhead charges were supported.

- The finding irresponsibly asserts that Sunlink selectively applies FDC pricing. The facts simply do not support such an assertion. In each case, an FDC comparison is made to document that lease rates were below FDC. Using FCC rules, the only option for evaluating pricing of the warehouse transactions with BST has been FDC since Sunlink provides no warehouse leasing to any other customer and thus has no basis for market rate comparisons for this type of property. Since an FDC comparison is typically a more conservative means of evaluating lease rates than market rate comparisons, such a comparison documents the prudency of these leases. The allegation that FDC pricing naturally causes cross-subsidization of properties priced at market is illogical and totally without merit.

- Sunlink's project-based accounting system ensures that every activity or project including the leasing of each property owned by Sunlink (regardless of pricing methodology) receives its appropriate share (i.e.,

COMPANY RESPONSE (Cont'd.):

JCO compliant allocation) of overheads and other corporate costs. This system has been designed in strict compliance with JCO fully distributed costing rules and is used in the evaluation of affiliate leasing transactions.

Clearly, the audit team had available to it sufficient evidence to support Sunlink's JCO compliance and relevant cost data when reviewing the C&L workpapers. In addition, the increase in lease prices per square foot had been specifically explained in response to JWC-16 as well as above. Therefore, the recommendation to exclude lease costs from the rate base, calculate chaining to Georgia, or disallow all costs is contrary to the documented facts and clearly without merit.

FINDING/RECOMMENDATION:

Commercial space which is leased from a nonregulated affiliate for regulated operations should be evaluated to determine if the lease space is actually being utilized.

COMPANY RESPONSE:

As stated in the auditor's report, the vacancy observed at 3700 Colonnade related to reorganizations and expiring leases. The audit team requested no information on this matter during the course of discovery and its finding therefore includes inaccurate and misleading conclusions. This situation was the result of carefully planned and prudent business decisions and the correct statement of facts is detailed below.

The lease for the building located at 3700 Colonnade was executed in June of 1989 for a 10-year primary term. Upon lease approval, the building was at full occupancy. During the last 5 years, the company has undergone considerable restructuring. The most notable effect in Birmingham was the consolidation of Comptrollers during 1992 and 1993. Much of the occupied space in 3700 Colonnade consisted of Comptroller functions which were consolidated to other locations during the second and third quarters of 1993. The vacant space in 3700 Colonnade was held in reserve in anticipation of relocating other functional groups from expiring and less desirable leases in the Birmingham area. This relocation was complete in October and November of 1993. The building has been at or near 100% occupancy levels since that time.

Clearly this finding was based on a lack of understanding of the facts and is wholly without merit. Any additional future requirements would be unnecessary, unduly burdensome and inappropriate.

FINDING/RECOMMENDATION:

Commission should perform regular future audits focused on real estate and lease transactions which involve affiliates in any way. An intrastate adjustment of $321,609 should be made to the Surveillance Report to compensate regulated customers for excessive Chastain Center lease expenses.

COMPANY RESPONSE:

The Company will address the two significant parts to this finding.

1. The analysis of the initial relocation of Engineering, Business, and Forecasting operations and the Outside Plant Control Center (OPCC) from the Whitlock Building to Chastain Center.

2. An analysis of costs and other considerations related to the Whitlock Building.

INITIAL RELOCATION

Commission approval is not needed before the Company leases space from nonregulated affiliates. All real estate decisions are made based upon careful analysis and in-depth economic studies.

The Company decision to move from the Whitlock Building was economically justified based upon two detailed economic analyses. One study was done and provided to the auditors concerning the proposed move of the Engineering, Business, and Forecasting Operations. A second study (also provided to the auditors) was performed concerning the relocation of the OPCC. Both studies were comprehensive and included all relevant information such as present value of the rents, renovations, lease penalties, and utilities.

The first study focused on the Engineering, Business, and Forecasting Operations and it shows that the Company did definitely search and identify alternatives to moving to Chastain. The other alternatives included moving to Whitewater Business Park, moving to Park Square, or remaining at Whitlock. Whitewater was several hundred thousand dollars higher than any of the other alternatives. Park Square was less expensive, but it was not pursued because of concerns that the building might not ever be built and concerns that the actual costs might exceed the estimated costs. (As information, the building has yet to be built). The option of remaining at Whitlock was carefully reviewed, but the Company decided against this alternative based on the economic analysis in conjunction with other considerations (discussed in "Other Considerations for Whitlock" on page 3).

COMPANY RESPONSE (Cont'd.):

The second study analyzed the proposed move of the OPCC. This study considered the alternatives of remaining at Whitlock, moving to Chastain, or moving to another location. When all relevant factors were considered, the study showed that the Company would save $107,018 by moving to Chastain. See "Analysis of Costs" Item (5) for more information.

ANALYSIS OF COSTS

The allegations regarding the $428,812 overcharging of expense are erroneous because the auditors failed to consider all the facts. The Company's decision to move to Chastain was economically justified based upon two detailed economic analyses. At the very most, the additional cost of moving was $321,794 or $241,346 on an intrastate basis. This amount was considered along with the noneconomic factors described under "Other Considerations for Whitlock" in making the decision to move. A summary of the correct costs and a discussion of each of the items is provided below:

| | Whitlock | Chastain |
|---|---|---|
| Engineering Move<br>Company's PV Analysis | $2,633,199 | $2,806,461 |
| Items Not Included: | | |
| (1) Common Area | | 107,849 |
| (2) HVAC Space | | 39,701 |
| (3) Rental Savings | | (32,000) |
| (4) One Time Charges | | 140,000 |
| OPCC Move<br>(5) Company's PV Analysis | 357,163 | 250,145 |
| Total | $2,990,362 | $3,312,156 |

(1). Common Area Maintenance (CAM) - As stated in the audit report, the CAM costs at Chastain were approximately $1.05 per square foot in 1991. It is probable that the CAM costs at Whitlock would also have been higher than in the study since both buildings are in the same geographic location. In order to be conservative, however, the Company will not dispute this amount.

COMPANY RESPONSE (Cont'd.):

(2). Heating Ventilation Air Conditioning (HVAC) Space -

The increase in costs due to the HVAC was for two mechanical rooms for the Heating Ventilation Air Conditioning (HVAC) system. Furthermore, relocation of the HVAC system inside the building was expected to yield cost reductions and maintenance advantages over roof mounted units. However, the Company will be conservative and not dispute the amount.

(3). Rental Savings

As noted by the auditors, the Company was able to negotiate two month's rental reduction of $32,000 with the owners of the Whitlock Building.

(4). One Time Charge of $140,000

The $140,000 was for technological and architectural changes to the original plans which were likely to have occurred under any of the alternatives. However the Company will be conservative and not dispute the $140,000.

(5). Outside Plant Control Center (OPCC) -

The Company actually saved $107,018 by moving to Chastain. This was based upon a separate economic analysis that was performed regarding the move of the OPCC. The OPCC was not included in the original analysis because the decision to move the OPCC to Chastain had not been made.

The Company's original plans were to move the OPCC from Whitlock to available central office space. However, space requirements for the OPCC increased subsequent to that decision, making it impossible for this function to fit into the available central office space.

OTHER CONSIDERATIONS FOR WHITLOCK

Furthermore, the auditors failed to consider some very important issues associated with the Whitlock Building. These considerations more than offset the relatively small additional costs to move to Chastain. These items are described below:

COMPANY RESPONSE (Cont'd.):

1. There was no expansion room available at Whitlock. As a matter of fact, with implementation of the following year's plans (1989), the Whitlock Building would have been 100% occupied and the Company was going to have to lease an additional 2,471 square feet elsewhere.

2. The owners of the Whitlock Building were unwilling to commit to a lease term longer than 7 1/2 years. The forecasted need for space was for 15+ years.

3. The building was in a deteriorated condition and the present owner was unwilling to spend significant funds for repairs. For example, there were some structural problems with the building and the front entrance and steps were settling. On the other hand, Chastain was a new building.

4. The building had poor heating and cooling.

5. The building was in a very congested area, with poor ingress and egress.

## CONCLUSION

Even being extremely conservative, the auditor's alleged additional expenses for the move to Chastain were overstated by at least 25%. Furthermore, the auditors failed to note some very important other issues such as the Company's search for other alternatives, the building condition, and poor response from the landlord.

FINDING/RECOMMENDATION:

The interest received by Southern Bell from advances to affiliates should be offset against book interest in the interest synchronization adjustment.

COMPANY RESPONSE:

The audit report is erroneous in its conclusion that the Company received a cross-subsidy from the interest synchronization adjustment.

Southern Bell made advances to BSS and BSS paid interest to Southern Bell. The audit report notes that "Southern Bell's accounting for the interest on advances was correct." However, the report is incorrect when it concludes that "if the advances had not been made to the nonregulated affiliates, Southern Bell debt could have been substantially lower." This is based upon the erroneous conclusion that the Company had to borrow incremental funds to loan to BSS, resulting in increased Georgia revenue requirements. If SB did not have BSS as a centralized provider of various services, SB would have had to either provide the services internally or use outside suppliers. In either case, SB would have needed to fund the same operations BSS provides. The existence of BSS did not increase the amount of debt SB needed to do business.

The staff's witness in the 1989-90 Rule Nisi hearings (Docket 3905-U) claimed that SB's debt ratio should be higher. It is surprising that the audit team is now recommending a decreased debt ratio for SB.

Even if the Company accepted the fact that eliminating the BSS advances would reduce SB debt, which it does not, this change would not have as much of an impact on the interest synchronization adjustment as the auditors contend. The Company provided information to the auditors to correct their calculations, but it was not used by the auditors.

FINDING/RECOMMENDATION:

The Company achieved a cross-subsidy relating to the Rose CXC PBX. The Commission should increase its audit scrutiny of the Company's CPE-related transactions.

COMPANY RESPONSE:

It is misleading to state that "this transaction resulted in a cross-subsidy from regulated operations to nonregulated operations." In this finding, the auditors have discovered one billing error and nothing else.

This was an isolated incident of a small magnitude. This finding reflects the only instance of not billing an affiliate for asset usage that the auditors found over a discovery period of almost 2 years.

During the audit period, telecommunications equipment used by BSS generally remained on the books of the telco, and the investment was identified for billing to BSS. In this case, the investment for the Rose PBX was in a Southern Bell owned building, and it was not properly identified for billing. However, it should be noted that if asset usage for the Rose PBX had been properly billed to BSS, approximately 55% of the costs would have been return billed to SB.

The report is incorrect in the statement that the Rose PBX "is in the CPE area in which the auditors have identified other cross-subsidies." The Rose PBX was used internally for corporate communications equipment and was entirely unrelated to the BSS CPE inventory which was held for resale.

FINDING/RECOMMENDATION:

Accounting and Information Management costs should be directly assigned whenever possible.

COMPANY RESPONSE:

The Company is in full compliance with the FCC's cost allocation rules in Part 64. The costs associated with the three authority codes in the Incoming Billing Interface Tracking System (IBITS) were corporate expenses related to centralized accounting and information management functions which were common and not directly assignable to either regulated or nonregulated. In addition, all information management expenses (Account 6724) are associated with general purpose computers and cannot be directly assigned based upon the definition of direct assignment.

In the CAM Uniformity Order (AAD 92-42, released July 1, 1993), the FCC clarified the definition of direct assignment as "costs incurred in providing either regulated service exclusively or nonregulated service exclusively". Furthermore, the FCC said "direct assignment of an asset can only occur when an entire asset is used exclusively for regulated activities or when an entire asset is used exclusively for nonregulated activities".

The three accounting and information management projects which were billed to SB from BSS did not meet the criteria for direct assignment. These functions were centralized to provide for multiple departments and business functions. Therefore these expenses cannot be directly assigned to a single business function or line of business. The expenses associated with all three of these projects were directed to the appropriate cost pool based upon the function performed and apportioned to regulated and nonregulated in a cost causative manner based upon the FCC's cost allocation principles.

The inappropriateness of a direct cost pool for BST is relevant to both Account 6124 (General Purpose Computer expense) and Account 6724 (Information Management expense). Part 32 defines information management expenses in Account 6724 as costs "incurred in planning, developing, testing, implementing and maintaining data bases and application systems for general purpose computers." SB's general purpose computers literally perform hundreds of various functions and are not used exclusively for regulated or nonregulated activities. A direct cost pool is not appropriate due to the large volumes of applications and the impracticability of trying to directly assign each of these projects.

COMPANY RESPONSE (Cont'd.):

In summary, information management costs cannot be directly assigned but are appropriately apportioned to regulated and nonregulated in a cost causative manner as per the FCC approved Cost Allocation Manual (CAM).

FINDING/RECOMMENDATION:

BSC International calls should be directly assigned to nonregulated in most cases.

COMPANY RESPONSE:

Again, the auditors simply have missed the essence of the cost allocation process. International calls placed by employees of the international operations of BSC are directly billed to the nonregulated side of the business. When international calls are placed by the staff at BSC, the expenses of the calls follow the expense allocations of the department or group making the calls. That is, long distance charges on BSC's bill become part of departmental overheads and are allocated based upon the individual department's established allocators [as per FCC 64.901 (b)(3)(ii) above] with respect to regulated and nonregulated entities. As a result, international long distance calls have been allocated appropriately to the unregulated functions and in complete compliance with FCC rules.

COMPANY RESPONSE (Cont'd.):

However, as stated above, since BSC's expenses have been appropriately allocated in accordance with FCC rules 32.37 and 64.901, all of these amounts become irrelevant.

FINDING/RECOMMENDATION:

The transactions between BAPCO and SGI should be specifically covered by Rule 32.27(d) for the purposes of the Georgia Surveillance Report. Substantial third party sales should be interpreted to mean that 75 percent or more of the sales are to non-affiliated companies.

COMPANY RESPONSE:

This finding is incorrect and reflects a lack of understanding of the information provided, discussed and reviewed. The finding is based on statements taken out of context in documents relating to other jurisdictions. As noted, there are no existing cost allocation rules from the FCC or in Georgia that apply to transactions between BAPCO and Stevens (SGI). Because the FCC has accepted the negotiated pricing methodology embodied in the publishing fee contract between BAPCO and BST, transactions related to this contractual arrangement between BAPCO and other affiliates are not subject to the pricing hierarchy described in Part 32 of the JCO rules.

However, as also stated, SGI "believes that this [its] market pricing is supportable by the level of non-affiliate business in 1992." The relationship between BAPCO and SGI predated SGI's acquisition by BellSouth. Today's contract reflects, in the aggregate, the same prices as those charged prior to this acquisition. These prices were comparable when set to those charged by SGI to non-affiliate customers. It is therefore clear that these transactions meet any reasonable standard of prudency.

No compelling reason to utilize the proposed methodology has been put forth by the auditors and no benefit would be realized by so doing. Further, their calculations lack factual support and grossly overstate the amount of alleged cross-subsidy under this improper standard. It is totally illogical to assume, without any information on growth trends or prior year's volumes, that an amount estimated for 1992 would apply equally to four previous years.

Furthermore, the recommendation that the concept of substantial third party sales, even though not relevant to anything discussed in this finding, be interpreted to mean that 75% or more of the sales are to non-affiliates is ludicrous. As BellSouth explained in its Comments filed in FCC Docket No. 93-251, for an affiliate (or any other company) to successfully market as

# EXHIBIT COC-DR2-22

**EXHIBIT COC-DR2-22**

**Project from January 1, 2006 to Present Concerning TAWC**

| Contract No. | Description | TAWC Extent of Work | City Request/Responsibility |
|---|---|---|---|
| R-07-005 | Warner Park Ballfields | Installed new service meter | City purchased new meter |
| T-06-002 | 25th Street and 26th Street Two-way Conversion | Relocated Fire Hydrant | City improved intersection radius requested relocation of FH |
| E-06-009 | Manufacturers Road Streetscaping (Renaissance Park Entrance West to Hwy 27 Ramps) | Provide future services to customers (2) and Fire hydrant relocation | City improved roadway and requested utilites extend new services to future parcels |
| W-05-007-202 | Warner Park/Engel Stadium Combined Sewer Parallel Interceptor | TAWC agreed to $16,000 cost to field redesign to stay further away from their 30" main | City already redesigned once to avoid existing facilities, in the field TAWC requested a second redesign, TAWC agreed to pay cost of revised structures and boring length. |
| E-05-011 | 18th Street - Adams to Jefferson | Installed new water main in new roadway | City built new residential roadway |
| E-05-024 | Gunbarrel Road @ Standifer Gap Road Intersection Improvements | Relocation of existing service line | City built new roudabout intersection, required service relocation |
| E-03-037 | Hope VI - All Other Work (Public Works) | Reduced work to adding new valves and repacking existing valves, and relocated one fire hydrant | City redesigned new sanitary sewer to eliminate relocation of water main |
| E-03-029 | Market Street at Cherokee Blvd | Raised one valve | City built new concrete intersection |
| E-03-011 | Igou Gap Rd. (Gunbarrel Rd to Gray Rd.) | Lowered existing water main at Clearview for cutting hill to proposed grade | City widened and improved exisiting roadway required relocation of a portion of existing water main |
| S-06-011 | 601 North Moore Rd Stormwater Project | Lowered existing water main on Colonial Dr. because of conflict with storm drain. | City installed new storm system, required relocation of a portion of existing water main |

# EXHIBIT COC-DR2-23

# SECTION A. GENERAL CONDITIONS AND DEFINITIONS

## 1. SEVERABILITY

The provisions of this permit are severable and if any provision of this permit or the application of any provision of this permit to any circumstance is held invalid, the application of such provision to other circumstances and the remainder of this permit shall not be affected thereby.

## 2. DUTY TO COMPLY

The permittee must comply with all conditions of this permit. Failure to comply with the requirements of this permit may be grounds for administrative action or enforcement proceedings including civil or criminal penalties, injunctive relief and summary abatements.

## 3. DUTY TO MITIGATE

The permittee shall take all reasonable steps to minimize or correct any adverse impact to the public treatment plant or the environment resulting from non-compliance with this permit, including such accelerated or additional monitoring as necessary to determine the nature and impact of the non-complying discharge.

## 4. PERMIT MODIFICATION

This permit may be modified for good causes including, but not limited to, the following:

(a) To incorporate any new or revised Federal, State or local pre-treatment standards or requirements.

(b) Material or substantial alterations or additions to the discharger's operation processes, or discharge volume or character which were not considered in drafting the effective permit.

(c) A change in any condition in either the industrial user or the POTW that requires either a temporary or permanent reduction or elimination of the authorized discharge.

(d) Information indicating that the permitted discharge poses a threat to the Control Authority's collection and treatment systems, POTW personnel or the receiving waters.

(e) Violation of any terms or conditions of the permit.

(f) Misrepresentation or failure to disclose fully all relevant facts in the permit application or in any required reporting.

(g) Revision of or a grant of variance from such categorical standards pursuant to 40 CFR 403.13.

(h) To correct typographical or other errors in the permit.

(i) To reflect transfer of the facility ownership and/or operation to the new owner/operator.

(j) Upon request of the permittee, provided such request does not create a violation of any applicable requirements, standards, laws, or rules and regulations.

The filing of a request by the permittee of a permit modification, revocation and reissuance, or termination, or a notification of planned changes or anticipated noncompliance, does not stay any permit condition.

## 5. PERMIT TERMINATION

This permit may be terminated for the following reasons:

(a) Falsifying self-monitoring reports.

(b) Tampering with monitoring equipment.

(c) Refusing to allow timely access to the facility premises and records.

(d) Failure to meet effluent limitations.

(e) Failure to pay fines.

(f) Failure to pay sewer charges.

(g) Failure to meet compliance schedules.

## 6. PERMIT APPEALS

The permittee may petition to appeal the terms of this permit within thirty (30) days of the notice.

This petition must be in writing; failure to submit a petition for review shall be deemed to be a waiver of the appeal. In its petition, the permittee must indicate the permit provisions objected to, the reasons for this objection, and the alternative condition, if any, it seeks to be placed in the permit.

The effectiveness of this permit shall not be stayed pending a reconsideration by the Board. If after considering the petition and any arguments put forth by the Director, the Board determines that reconsideration is proper, it shall remand the permit back to the Director for reissuance. Those permit provisions being re-considered by the Director shall be stayed pending reissuance.

A Board of Directors' decision not to reconsider a final permit shall be considered final administrative action for purposes of judicial review. The permittee seeking judicial review of the Board's final action must do so by filing a complaint with the Chancery Court for Hamilton County within sixty (60) days pursuant to the common law writ of certiorari.

## 7. PROPERTY RIGHTS

The issuance of this permit does not convey any property rights of any sort, or any exclusive privileges, nor does it authorize any injury to private property or any invasion of personal rights nor any violation of federal, state or local laws or regulations.

## 8. LIMITATION ON PERMIT TRANSFER

Permits may be reassigned or transferred to a new owner and/or operator with prior approval of the Director:

(a) The permittee must give at least thirty (30) days advance notice to the Director.

(b) The notice must include a written certification by the new owner which:

(i) States that the new owner has no immediate intent to change the facility's operations and processes.

(ii) Identifies the specific date on which the transfer is to occur.

(iii) Acknowledges full responsibility for complying with the existing permit.

(c) A copy of the existing control mechanism (wastewater discharge permit) shall be provided to the new owner and/or operator.

## 9. DUTY TO REAPPLY

If the permittee wishes to continue an activity regulated by this permit after the expiration date of this permit, the permittee must submit an application for a new permit within the period of time not more than ninety (90) days and not less than thirty (30) days before the expiration date of this permit.

## 10. CONTINUATION OF EXPIRED PERMITS

An expired permit will continue to be effective and enforceable until the permit is reissued if:

(a) The permittee has submitted a complete permit application at least thirty (30) days and not more than ninety (90) days prior to the expiration date of the user's existing permit.

(b) The failure to reissue the permit, prior to expiration of the previous permit is not due to any act or failure to act on the part of the permittee.

## 11. DILUTION

The permittee shall not increase the use of potable or process water or in any way attempt to dilute an effluent as a partial or complete substitute for adequate treatment to achieve compliance with the limitations contained in this permit.

## 12. DEFINITIONS

(a) **Daily Maximum** - The maximum allowable discharge of pollutant during a calendar day. Where daily maximum limitations are expressed in units of mass, the daily discharge is the total mass discharged over the course of the day. Where daily maximum limitations are expressed in terms of a concentration, the daily discharge is the arithmetic average measurement of the pollutant concentration derived from all measurements taken that day.

(b) **Composite Sample** - A sample that is collected over time, formed either by continuous sampling or by mixing discrete samples. The sample may be composited either as a time composite sample: composed of discrete sample aliquots collected in one (1) container at constant time intervals providing representative samples irrespective of stream flow; or as a flow proportional composite sample: collected either as a constant sample volume at time intervals proportional to stream flow, or collected by increasing the volume of each aliquot as the flow increases while maintaining a constant time interval between the aliquots.

(c) **Grab Sample** - An individual sample collected in less than fifteen (15) minutes without regard for flow or time.

(d) **Instantaneous Maximum Concentration** - The maximum concentration allowed in any single grab sample.

(e) **Cooling Water** -

(1) **Uncontaminated** - Water used for cooling purposes only which has no direct contact with any raw material, intermediate, or final product and which does not contain a level of contaminants detectable higher than that of the intake water.

(2) **Contaminated** - Water used for cooling purposes only which may become contaminated either through the use of water treatment chemicals used for corrosion inhibitors or biocides, or by direct contact with process materials and/or wastewater.

(f) **Monthly Average** - The arithmetic mean of the values for effluent samples collected during a calendar month or specified thirty (30) day period (as opposed to a rolling thirty (30) day window).

(g) **Weekly Average** - The arithmetic mean of the values for effluent samples collected over a period of seven (7) consecutive days.

(h) **Bi-Weekly** - Once every other week.

(i) **Bi-Monthly** - Once every other month.

(j) **Upset** - Means an exceptional incident in which there is unintentional and temporary noncompliance with technology-based permit effluent limitations because of factors beyond the reasonable control of the permittee, excluding such factors as operational error, improperly designed or inadequate treatment facilities, or improper operation and maintenance or lack thereof.

(k) **Bypass** - Means the intentional diversion of wastes from any portion of a treatment facility.

## 13. GENERAL PROHIBITIVE STANDARDS

**Prohibited Pollutants** - No person shall introduce into the publicly owned treatment works any pollutant(s) which cause pass through or interference. Additionally, the following specific prohibitions apply:

(a) Pollutants which create a fire or explosion hazard in the POTW, including, but not limited to, wastestreams with a closed cup flashpoint of less than one hundred forty (140°) degrees Fahrenheit (sixty (60°) degrees Centigrade), using the test methods specified in 40 CFR 261.21 and pollutants which cause an exceedance of 10% of the lower explosive limit (LEL) at any point within the POTW;

(b) Pollutants which cause corrosive structural damage to the POTW, but in no case discharges with a pH lower than 5.0 or higher than 10.5.

(c) Solid or viscous pollutants in amounts which cause obstruction to the flow of the sewers, or other interference with the operation of or which cause injury to the POTW; including waxy or other materials which tend to coat and clog a sewer line or other appurtenances thereto;

(d) Any pollutant, including oxygen demanding pollutants (BOD, etc.) released in a discharge (slug) of such volume or strength as to cause interference in the POTW or individual unit operations or cause adverse effects on its workers or the environment.

(e) Heat in amounts which will inhibit biological activity in the POTW resulting in interference, but in no case heat in such quantities that the temperature at the treatment works influent exceed 40° Centigrade (104° Fahrenheit). Unless a higher temperature is allowed in the user's wastewater discharge permit, no user shall discharge into any sewer line or other appurtenance of the POTW wastewater with a temperature exceeding 63.5° Centigrade (150° Fahrenheit).

(f) Pollutants which result in the presence of toxic gases, vapors, or fumes within the POTW in a quantity that may cause acute worker health and safety problems.

(g) Any trucked or hauled pollutants, except at discharge points designated by the POTW.

(h) Any hospital waste, pathological waste, surgical operating room waste or delivery room waste.

(i) **Oil & Grease Discharge Control** - Disposal of "oil" by discharge to the sewer system is not permitted. Oils include automotive lubricating oils, transmission and brake fluid, other industrial oils, vegetable oils used in a restaurant or food processing facility.

Dischargers of oil and grease waste shall be required to provide an equivalent of primary treatment based on gravity separation of visible and floating oil, and grease and oil, and grease sludge, from wastewater discharges. Such pretreatment processes shall be subject to the good management practices as required by Section 31-52 (f) of the City Code and approval by the Director. Discharges shall also be subject to monitoring, entry, inspection, reporting and other requirements as determined by the Director at his discretion.

(j) **Limitation on Radioactive Waste** - No person shall discharge or permit to be discharged any radioactive waste into a community sewer except:

(1) When the person is authorized to use radioactive materials by the Tennessee Department of Health and Environment or the Nuclear Regulatory Commission;

(2) When the waste is discharged in strict conformity with applicable laws and regulations of the aforementioned agencies, or any other agency having jurisdiction; and

(3) When a copy of permits received from said regulatory agencies have been filed with the Director.

## 14. COMPLIANCE WITH APPLICABLE PRETREATMENT STANDARDS AND REQUIREMENTS

Compliance with this permit does not relieve the permittee from its obligations regarding compliance with any and all applicable local, state and federal pretreatment standards and requirements including any such standards or requirements that may become effective during the term of this permit.

## SECTION B. OPERATION AND MAINTENANCE OF POLLUTION CONTROLS

### 1. PROPER OPERATION AND MAINTENANCE

The permittee shall at all times properly operate and maintain all facilities and systems of treatment and control (and related appurtenances) which are installed or used by the permittee to achieve compliance with the conditions of this permit. Proper operation and maintenance includes, but is not limited to: effective performance, adequate funding, adequate operator staffing and training, and adequate laboratory and process controls, including appropriate quality assurance procedures. This provision requires the operation of backup or auxiliary facilities or similar systems only when necessary to achieve compliance with the conditions of the permit.

### 2. DUTY TO HALT OR REDUCE ACTIVITY

Upon reduction of efficiency of operation, or loss or failure of all or part of the treatment facility, the permittee shall to the extent necessary to maintain compliance with its permit, control its production or discharges (or both) until operation of the treatment facility is restored or an alternative method of treatment is provided. This requirement applies, for example, when the primary source of power of the treatment facility fails or is reduced. It shall not be a defense for a permittee in an enforcement action that it would have been necessary to halt or reduce the permitted activity in order to maintain compliance with the conditions of this permit.

### 3. BYPASS OF TREATMENT FACILITIES

(a) Bypass is prohibited unless it is unavoidable to prevent loss of life, personal injury or severe property damage or no feasible alternatives exist.

(b) The permittee may allow bypass to occur which does not cause effluent limitations to be exceeded, but only if it is also for essential maintenance to assure efficient operation.

(c) **Notification of Bypass:**

(1) **Anticipated Bypass** - If the permittee knows in advance of the need for a bypass, it shall submit prior written notice, at least ten (10) days before the date of the bypass, to the Pretreatment Supervisor.

(2) **Unanticipated Bypass** - The permittee shall immediately notify the Pretreatment Supervisor and submit a written notice to the POTW within five (5) days. This report shall specify:

(i) A description of the bypass, and its cause, including its duration;

(ii) Whether the bypass has been corrected; and

(iii) The steps being taken or to be taken to reduce, eliminate and prevent a reoccurrence of the bypass.

## 4. REMOVED SUBSTANCES

Solids, sludges, filter backwash or other pollutants removed in the course of treatment or control of wastewater shall be disposed of in accordance with Section 405 of the Clean Water Act and Subtitles C and D of the Resource Conservation and Recovery Act.

## SECTION C. MONITORING AND RECORDS

### 1. REPRESENTATIVE SAMPLING

Samples and measurements taken as required herein shall be representative of the volume and nature of the monitored discharge. All samples shall be taken at the monitoring points specified in this permit and unless otherwise specified before the effluent joins or is diluted by any other waste stream, body of water or substance. All equipment used for sampling and analysis must be routinely calibrated, inspected and maintained to ensure their accuracy. Monitoring points shall not be changed without notification to and the approval of the Pretreatment Supervisor.

### 2. FLOW MEASUREMENTS

If flow measurement is required by this permit, the appropriate flow measurement devices and methods consistent with approved scientific practices shall be selected and used to ensure the accuracy and reliability of measurements of the volume of monitored discharges. The devices shall be installed, calibrated, and maintained to ensure that the accuracy of the measurements are consistent with the accepted capability of that type of device. Devices selected shall be capable of measuring flows with a maximum deviation of less than 10 percent from true discharge rates throughout the range of expected discharge volumes.

### 3. ANALYTICAL METHODS TO DEMONSTRATE CONTINUED COMPLIANCE

All sampling and analysis required by this permit shall be performed in accordance with the techniques prescribed in 40 CFR Part 136 and amendments thereto, otherwise approved by EPA, or as specified in this permit.

### 4. ADDITIONAL MONITORING BY THE PERMITTEE

If the permittee monitors any pollutant more frequently than required by this permit, using test procedures identified in Section C.3, the results of this monitoring shall be included in the permittee's self-monitoring reports.

## 5. INSPECTION AND ENTRY

The permittee shall allow the Director or an authorized representative, upon the presentation of credentials and/or other documents as may be required by law, to:

(a) Enter upon the permittee's premises where a regulated facility or activity is located or conducted, or where records must be kept under the conditions of this permit;

(b) Have access to and copy, at reasonable times, any records that must be kept under the conditions of this permit;

(c) Inspect at reasonable times any facilities, equipment (including monitoring and control equipment), practices, or operations regulated or required under this permit;

(d) Sample or monitor, for the purposes of assuring permit compliance, any substances or parameters at any location; and

(e) Inspect any production, manufacturing, fabricating, or storage area where pollutants, regulated under the permit, could originate, be stored, or be discharged to the sewer system.

## 6. RETENTION OF RECORDS

(a) The permittee shall retain records of all monitoring information, including all calibration and maintenance records and all original strip chart recordings for continuous monitoring instrumentation, copies of all reports required by this permit, and records of all data used to complete the application for this permit, for a period of at least three (3) years from the date of the sample, measurement, report or application.

This period may be extended by request of the Director at any time.

(b) All records that pertain to matters that are the subject of special orders or any other enforcement or litigation activities brought by the Director shall be retained and preserved by the permittee until all enforcement activities have concluded and all periods of limitation with respect to any and all appeals have expired.

## 7. RECORDS CONTENTS

Records of sampling and analyses shall include:

(a) The date, exact place, time, and methods of sampling or measurements, and sample preservation techniques or procedures;

(b) Who performed the sampling or measurements;

(c) The date(s) analyses were performed;

(d) Who performed the analyses;

(e) The analytical techniques or methods used; and

(f) The results of such analyses.

## 8. FALSIFYING INFORMATION

Knowingly making any false statement on any report or other document required by this permit or knowingly rendering any monitoring device or method inaccurate, is a crime and may result in the imposition of criminal sanctions and/or civil penalties.

## SECTION D. ADDITIONAL REPORTING REQUIREMENTS

### 1. PLANNED CHANGES

The permittee shall give notice to the Director ninety (90) days prior to any facility expansion, production increase, or process modifications which results in new or substantially increased discharges or a change in the nature of the discharge.

### 2. ANTICIPATED NONCOMPLIANCE

The permittee shall give advance notice to the Director of any planned changes in the permitted facility or activity which may result in noncompliance with permit requirements.

### 3. AUTOMATIC RESAMPLING

If the results of the permittees' wastewater analysis indicates a violation has occurred, the permittee must notify the Director within twenty-four (24) hours of becoming aware of the violation and repeat the sampling and pollutant analysis and submit, in writing, the results of this repeat analysis within thirty (30) days after becoming aware of the violation.

### 4. DUTY TO PROVIDE INFORMATION

The permittee shall furnish to the Director within five (5) days, any information which the Director may request to determine whether cause exists for modifying, revoking and reissuing, or terminating this permit, or to determine compliance with this permit. The permittee shall also, upon request, furnish to the Director within five (5) days, copies of any records required to be kept by this permit. Self-monitoring reports must be made on the standard forms authorized by the Director.

### 5. SIGNATORY REQUIREMENTS

All applications, reports, or information submitted to the Director must contain the following certification statement and be signed as required in Sections (a), (b), (c) or (d) below:

"I certify under penalty of law that this document and all attachments were prepared under my direction or supervision in accordance with a system designed to assure that qualified personnel properly gather and evaluate the information submitted. Based on my inquiry of the person or persons who manage the system, or those persons directly responsible for gathering the information, the information submitted is, to the best of my knowledge and belief, true, accurate, and complete. I am aware that there are significant penalties for submitting false information, including the possibility of fine and imprisonment for knowing violations."

(a) By a responsible corporate officer if the Industrial User submitting the reports is a corporation. For the purpose of this paragraph, a responsible corporate officer means:

(i) a President, Secretary, Treasurer, or Vice-President of the corporation in charge of a principal business function, or any other person who performs similar policy or decision making functions for the corporation, or;

(ii) the Manager of one or more manufacturing, production or operating facilities, provided the Manager is authorized to make management decisions which govern the operation of the regulated facility including having the explicit or implicit duty of making major capital investment recommendations, and initiate and direct other comprehensive measures to assure long-term environmental compliance with environmental laws and regulations; can ensure that the necessary systems are established or actions taken to gather complete and accurate information for control mechanism requirements; and where authority to sign documents has been assigned or deligated to the Manager in accordance with corporate procedures.

(b) By a general partner or proprietor if the Industrial User submitting the reports is a partnership or sole proprietorship respectively.

(c) The principal executive officer or director having the responsibility for the overall operation of the discharging facility if the Industrial User submitting the reports is a federal, state or local governmental entity or their agents.

(d) By a duly authorized representative of the individual designated in paragraph (a), (b), or (c) of this section if:

(i) the authorization is made in writing by the individual described in paragraph (a), (b), or (c);

(ii) the authorization specifies either an individual or a position having responsibility for the overall operation of the facility from which the industrial discharge originates, such as, the position of Plant Manager, Operator of a well, or a well Field Superintendent, or a position of equivalent responsibility, or having overall responsibility for environmental matters for the company; and

(iii) the written authorization is submitted to the City.

(e) If an authorization under paragraph (d) of this Section is no longer accurate because a different individual or position has responsibility for the overall operation of the facility, or overall responsibility for the environmental matters for the company, a new authorization satisfying the requirements of paragraph (d) of this section must be submitted to the City prior to or together with any reports to be signed by an authorized representative.

## 6. OPERATING UPSETS

Any permittee that experiences an upset in operations that places the permittee in a temporary state of noncompliance with the provisions of either this permit or with Chapter 31 of City Code shall inform the Director within twenty-four (24) hours of becoming aware of the upset at 423-757-5026.

A written follow-up report of the upset shall be filed by the permittee with the Director within five (5) days. The report shall specify:

(a) Description of the upset, the cause(s) thereof and the upset's impact on the permittee's compliance status;

(b) Duration of noncompliance, including exact dates and times of noncompliance, and if not corrected, the anticipated time the noncompliance is expected to continue; and

(c) All steps taken or to be taken to reduce, eliminate and prevent recurrence of such an upset.

The report must also demonstrate that the treatment facility was being operated in a prudent and workmanlike manner.

A documented and verified operating upset shall be an affirmative defense to any enforcement action brought against the permittee for violations attributable to the upset event.

## 7. ANNUAL PUBLICATION

The Director shall provide at least annual publication in a newspaper(s) of general circulation that provides meaningful public notice within the jurisdiction(s) served by the POTW of industrial users which at any time during the previous twelve (12) months, were in significant noncompliance with applicable pretreatment requirements. Accordingly, the permittee is apprised that noncompliance with this permit may lead to an enforcement action and may result in publication of its name in an appropriate newspaper(s) in accordance with this Section.

## 8. CIVIL AND CRIMINAL LIABILITY

Nothing in this permit shall be construed to relieve the permittee from civil and/or criminal penalties for noncompliance under Section 31-61 of the City Code or state or federal laws or regulations.

## 9. AFFIRMATIVE DEFENSES

A user shall have an affirmative defense in any action brought against it alleging a violation of the general prohibitions established in Section A, paragraph 13 of this document and the specific prohibitions in paragraphs c, d and e of this document where the user can demonstrate that:

(a) It did not know or have reason to know that its discharge, alone or in conjunction with a discharge or discharges from other sources, would cause pass through or interference; and

(b) (1) A local limit designed to prevent pass through and/or interference, as the case may be, was developed pursuant to Code Section 31-51 (i) and (j) for each pollutant interference, and the user was in compliance with each such local limit directly prior to and during the pass through or interference; or

(2) If a local limit designed to prevent pass through and/or interference, as the case may be, has not been developed for the pollutant(s) that caused the pass through or interference, and the user's discharge directly prior to and during the pass through or interference did not change substantially in nature of constituents from the user's prior discharge activity when the POTW was regularly in compliance with the POTW's NPDES permit requirements and, in the case of interference, applicable requirements for sewage sludge use or disposal.

## 10. PENALTIES FOR VIOLATION OF PERMIT CONDITIONS

Section 31-61 of the City Code provides that any person who violates a permit condition is subject to a civil penalty of up to $10,000.00 per day of such violation. The permittee may also be subject to sanctions under state and/or federal law.

## 11. RECOVERY OF COSTS INCURRED

In addition to civil and criminal liability, the permittee violating any of the provisions of this permit or Chapter 31 of the City Code or causing damage to or otherwise inhibiting the City of Chattanooga wastewater disposal system shall be liable to the City for any expense, loss, or damage caused by such violation or discharge. The Director shall bill the permittee for the costs incurred by the City for any cleaning, repair, or replacement work caused by the violation or discharge. Refusal to pay the assessed costs shall constitute a separate violation of Section 31-61 of the Code.

## 12. SLUG CONTROL PROGRAM

(1) The permittee shall provide protection from slug discharges of restricted materials or other substances regulated by the City Code. A "slug" shall be defined as any pollutants, including oxygen demanding pollutants (BOD) (COD, NHS, etc.) released in a discharge of such volume or strength as to cause interference in the POTW or individual unit operations or cause adverse effects upon its workers or the environment.

(2) In the case of a slug discharge, it is the responsibility of the permittee to immediately by telephone (423) 757-5026 (24 Hr. number) or in person, notify the POTW of the incident. The notification shall include location of discharge, type of waste, concentration and volume and corrective action. Within five (5) days following a slug discharge, the permittee shall submit a detailed written report describing the cause of the discharge and the measures being taken by the permittee to prevent similar future occurrences. Such notification shall not relieve the permittee of any expense, loss, damage, or other liability which may be incurred as a result of damage to the sewerage system, fish kills, or any other damage to property, nor shall notification relieve the permittee of the fines, civil penalties, or other liability which may be imposed by the City Code or other applicable law.

(3) A notice shall be permanently posted on the permittee's premises advising employees whom to call in the event of a slug discharge. The permittee shall ensure that all employees who may cause, or allow such slug discharge to occur, are advised of the emergency notification procedure.

## 13. NOTIFICATION OF THE DISCHARGE OF HAZARDOUS WASTE

(1) The Industrial User shall notify the POTW, the EPA Regional Waste Management Division Director, and State hazardous waste authorities in writing of any discharge into the POTW of a substance, which, if otherwise disposed of, would be a hazardous waste under 40 CFR Part 261. Such notification must include the name of the hazardous waste as set forth in 40 CFR Part 261, the EPA hazardous waste number, and the type of discharge (continuous, batch, or other). If the Industrial User discharges more than 100 kilograms of such waste per calendar month to the POTW, the notification shall also contain the following information to the extent such information is known and readily available to the Industrial User: An identification of the hazardous constituents contained in the wastes, an estimation of the mass and concentration of such constituents in the wastestream discharged during that calendar month, and an estimation of the mass of constituents in the wastestream expected to be discharged during the following twelve (12)

months. All notifications must take place within 180 days of the effective date of this rule. Industrial Users who commence discharging after the effective date of this rule shall provide the notification no later than 180 days after the discharge of the listed or characteristic hazardous waste. Any notification under this paragraph need be submitted only once for each hazardous waste discharged. However, notifications of changed discharges must be submitted under 40 CFR 403.12 (j). The notification requirement in this section does not apply to pollutants already reported under the self-monitoring requirements of this permit.

(2) Dischargers are exempt from the requirements of this paragraph during a calendar month in which they discharge no more than fifteen kilograms of hazardous wastes, unless the wastes are acute hazardous wastes as specified in 40 CFR 261.30 (d) and 261.33 (e). Discharge of more than fifteen kilograms of non-acute hazardous wastes in a calendar month, or of any quantity of acute hazardous wastes as specified in 40 CFR 261.30 (d) and 261.33 (e), requires a one-time notification.

Subsequent months during which the Industrial User discharges more than such quantities of any hazardous waste do not require additional notification.

(3) In the case of new regulations under Section 3001 of RCRA identifying additional characteristics of hazardous waste or listing any additional substance as a hazardous waste, the Industrial User must notify the POTW, the EPA Regional Waste Management Waste Division Director, and State hazardous waste authorities of the discharge of such substance within ninety (90) days of the effective date of such regulations.

(4) In the case of any notification made under paragraph (p) of this section, the Industrial User shall certify that it has a program in place to reduce the volume and toxicity of hazardous wastes generated to the degree it has determined to be economically practical.

## 14. REPORT SUBMISSION

Industrial self-monitoring compliance reports and pH self-monitoring compliance reports shall be submitted within fifteen (15) days of the end of each calendar quarter. Surcharge self-monitoring compliance reports shall be submitted within thirty (30) days of the end of each calendar six (6) month period (or otherwise as noted) in the permit to:

**Pretreatment Program Supervisor**
**Moccasin Bend Treatment Plant**
**455 Moccasin Bend Road**
**Chattanooga, TN 37405**

## 15. OTHER INFORMATION

If the permittee becomes aware that he failed to submit any relevant facts in a permit application, or submitted incorrect information in a permit application or in any report to the Director, then he shall promptly submit such facts or information.

## 16. UPSET PROVISION

(1) **Definition** - For the purpose of this section, "Upset" means an exceptional incident in which there is unintentional and temporary noncompliance with Pretreatment Standards because of factors beyond the reasonable control of the permittee. An Upset does not include noncompliance to the extent caused by operational error, improperly designed treatment facilities, inadequate treatment facilities, lack of preventive maintenance, or careless or improper operation.

(2) **Effect of an Upset** - An upset shall constitute an affirmative defense to an action brought for noncompliance with categorical Pretreatment Standards if the requirements of paragraph (3) are met.

(3) **Conditions Necessary for a Demonstration of Upset** - If the permittee wishes to establish the affirmative defense of Upset, then he shall demonstrate, through properly signed, contemporaneous operating logs, or other relevant evidence that:

(a) An Upset occurred and permittee can identify the specific cause(s) of the Upset:

(b) The facility was at the time being operated in a prudent and workmanlike manner and in compliance with applicable operation and maintenance procedures;

(c) The permittee has submitted the following information to the Chattanooga ISS within twenty-four (24) hours of becoming aware of the Upset (if this information is provided orally, a written submission must be provided within five (5) days):

(i) A description of the Indirect Discharge and cause of noncompliance;

(ii) The period of noncompliance, including exact dates and times or, if not corrected, the anticipated time the noncompliance is expected to continue:

(iii) Steps being taken and/or planned to reduce, eliminate and prevent recurrence of the noncompliance.

(4) **Burden of Proof** - In any enforcement proceeding, the permittee seeking to establish the occurrence of an Upset shall have the burden of proof. The permittee will have the opportunity for a judicial determination on any claim of Upset only in an enforcement action brought for noncompliance with Pretreatment Standards.

(5) **User Responsibility in Case of Upset** - The permittee shall control production of all discharges to the extent necessary to maintain compliance with Pretreatment Standards upon reduction, loss, or failure of its treatment facilty until the facility is restored or an alternative method of treatment is provided. This requirement applies in the situation where, among other things, the primary source of power of the treatment facility is reduced, lost or fails.

## 17. ANNUAL PERMIT FEE

All significant Industrial Users shall be charged an annual permit fee of $500.00. This permit shall become valid only after payment of the annual fee. The fee shall be due for payment on or before March 31 of each year.

## 18. HAULED WASTE

No trucked or hauled wastewater from this facility may be discharged to the Chattanooga regional sewer system except at discharge points designated by the Director. As provided under Section 31-51 (h) of the City Code, the Director has authorized that this permit may be substituted for the "holding tank discharge permit" required by the section provided that: the wastewater or sludges are derived from the same processes covered by this permit; that a licensed hauler be used; that all fees are paid; and that all federal manifest requirements and reg- regulations under RCRA have been satisfied.

Chapter 31

# SEWERS, MAINS AND DRAINAGE[1]


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[1] **Charter references**--Sewage system, § 15.19 et seq.; removal, relocation and installation of utilities in connection with public improvements § 15.44 et seq.; sewer connections by city, § 15.61 et seq.

**Cross references**--Garbage and refuse, Ch. 18; health and sanitation, Ch. 20; plumbing, Ch. 27.

**State law reference**--Authority to require connections, T.C.A., § 7-35-201(1).

# ARTICLE I. IN GENERAL

## Sec. 31-1. General provisions.

(a) The purpose of this article is to establish uniform requirements for the disposal of wastewater and to regulate wastewater discharged into the City of Chattanooga's (hereinafter "city") sewer system. This article establishes conditions for connection to the sanitary sewer system and requires a permit. Certain acts which may be detrimental to the sewer system are prohibited, and the article provides measures for enforcement of its provisions and abatement of violations thereof.

(b) The superintendent (hereinafter "superintendent") shall exercise administrative management, control and jurisdiction over sanitary and storm sewers, sewage treatment and disposal facilities, mains and drainage, including their location, design, construction, operation, maintenance, repair and rehabilitation.

(c) The Wastewater Regulations and Appeals Board (hereinafter "board"), established pursuant to Section 31-57, shall hold hearings upon appeals from orders or actions of the superintendent as may be provided under any provision of this chapter.
(Ord. No. 9409, § 1, 6-5-90)

## Sec. 31-2. Connection with city sanitary sewer required.

(a) *Sewer connection required.* Every building having plumbing fixtures installed and intended for human habitation, occupancy, or use on premises abutting a street, alley, or easement in which segment there is a sanitary sewer which is within one hundred (100') feet of the property line of the parcel containing the building shall be considered as being served by the city's sanitary sewer system.

All new buildings hereafter constructed which may be served by the city's sewer system shall not be occupied until the connection has been made. The owner or occupant of each lot or parcel of land which is now served or which may hereafter be served by the city's sewer system shall cease to use any other method for the disposal of sewage except as approved for direct discharge by the Tennessee Department of Health and Environment or by discharge to a properly functioning and approved septic tank. Septic tanks shall not be used where sewers are available. The superintendent shall make any decision as to the availability of sewers. Notwithstanding the above exceptions, all premises served by the city sanitary sewer are subject to sewer user charges as described in article II of this chapter.

(b) *Unconnected sewer service lines a nuisance where connection is available*. Except for discharge to a properly functioning septic tank system approved by the Chattanooga-Hamilton County Health Department or discharges permitted by a national discharge elimination system permit (hereinafter "NPDES") issued by the State of Tennessee Department of Health and Environment, the discharge of sewage into places other than the city's sewer system is declared a nuisance. All permanently moored boats, floating houses or floating restaurants which are not intended to be used as a means of transportation, are likewise required to discharge sanitary sewage into the city sewer system. If the owner of any property which requires a sewer connection fails or refuses to connect to the city's system, a notice shall be given to the Public Officer of the Department of Neighborhood Services for such action as may be proper under chapter 21 of this code. The superintendent may take such other action to abate the nuisance as may be warranted under the circumstances. (Ord. No. 11345, §12, 11-12-02)

(c) *Insufficient capacity, connection moratorium*. In those parts of the city sewer system where there is no additional capacity, and a sewer moratorium has been established pursuant to orders of the Tennessee Department of Health and Environment, no new or additional sewer connections shall be permitted. Permits issued prior to the date of the moratorium may be completed. No new plumbing permits shall be issued for new buildings in a moratorium area after the effective date of the moratorium. A moratorium shall continue in effect until the capacity restriction has been corrected.
(Ord. No. 9409, § 1, 6-5-90; Ord No. 11345, §12, 11-12-02)

**Sec. 31-3. Adequate and minimum fixtures, water heaters.**

(a) *Minimum number of fixtures*. A dwelling shall have at least one commode, one bathtub or shower, one lavatory, one kitchen-type sink, and an adequate source of hot water for each family unit to meet minimum basic requirements for health, sanitation and personal hygiene. All other buildings, structures, or premises intended for human occupancy or use shall be provided with adequate sanitary facilities as may be required by any other law or regulation, but not less than one commode and one hand-washing lavatory.

(b) *Adequate water for disposal of waste required*. It shall be unlawful for any person in possession of premises into which a pipe or other connection with the city sanitary sewers and drains have been laid to permit the same to remain without adequate fixtures attached to allow a sufficient quantity of water to be so applied as properly to carry off all waste matter and keep the same unobstructed.

(c) *Water heaters*. Water heating facilities shall be accessible for emergency maintenance without entering any individual apartment or living unit, except that water heaters may be located within an apartment or living unit when supplying hot water to that unit only. (Ord. No. 9409, § 1, 6-5-90)

**Sec. 31-4. Installation, maintenance, repair of sewer service lines; charge; exception.**

(a) *Definition*. A "standard sanitary sewer service line" is a four inch (4") or six inch (6") pipe extending from the sewer main or trunk location in a street, alley, or easement to the property served by the main or trunk.

(b) *Installation of sewer service lines*. Four-inch building sewers shall be laid on a grade of at least one percent (1.0%). Larger building sewers shall be laid on a grade that will produce a velocity when flowing full of at least two feet (2') per second. Slope and alignment of all building sewers shall be neat and regular.

Building sewers shall be constructed only of: (1) cast-iron soil pipe using rubber compression joints of approved type; (2) polyvinylchloride pipe with rubber compression joints; (3) ABS composite sewer pipe with solvent-welded or rubber compression joints of approved type; or (4) such other materials of equal or superior quality as may be approved by the superintendent. Under no circumstances will cement mortar joints be acceptable. Each connection to the sewer system must be made at a wye, or service line stubbed out, or in the absence of any other provision, by means of a saddle of a type approved by the city, attached to the sewer. No connection may be made by breaking into an existing sewer and inserting the service line.

The building sewer may be brought into the building below the basement floor when gravity flow from the building to the sewer is at a grade of one percent (1.0%) or more if possible. In cases where basement or floor levels are lower than the ground elevation at the point of connection to the sewer, adequate precautions through the installation of check valves or other backflow prevention devices, to protect against flooding shall be provided by the owner. In all buildings in which any building drain is too low to permit gravity flow to the sewer, wastes carried by such building drain shall be lifted by an approved means and discharged into the city sewer.

(c) *Standard Sewer Stubouts*. Hereafter, as a part of sanitary sewer projects in the city, the city shall install, or cause to be installed, standard sanitary sewer service lines from mains or trunks located in a street, alley, or easement to the property line of each lot or residence on the street being sewered. In the case of sewers being constructed in undeveloped

subdivisions located within a designated sewer project, the standard sanitary sewer service lines may be constructed to each lot as shown on the plat of the subdivision by the developer as filed in the Register's Office of Hamilton County, Tennessee. Sewer service lines may not be constructed by the city in a street where the property is unsubdivided and undeveloped. A fee shall be charged upon connection to the sewer line as provided in article II.

(d) *Fee*. There is hereby levied and imposed a sewer service line charge of eight hundred dollars ($800) for every sanitary sewer service line installed hereafter where a lateral sewer connection has been provided for use by the applicant. The service line charge shall be paid by property owners at the time that application is made to the city for permission to tie on to the sanitary sewer service line. The collection of such payments shall be the responsibility of the inspection division of the department of public works, streets and airports. In lieu of the payment of eight hundred dollars ($800) at the time of application, the property owners may execute an authorization to have the sum of twenty dollars ($20) per month added to the statement for sewer charges for a period of sixty (60) months. If a sixty (60) months' payment is authorized and the property is sold, the property owner shall either pay the balance remaining or have the new property owner execute authorization to continue the twenty dollars ($20) per month payments for the balance of the sixty (60) months. This eight hundred dollars ($800) charge shall be in addition to any required fee for a plumbing permit, street cuts, or other fees; provided that, such sewer service line charge shall not apply if the lateral sewer connection was constructed by and the cost of same borne by the developer of a subdivision incident to the construction of a collector sewer system for the subdivision or there has been no lateral sewer connection provided; and the applicant shall be required to show that he is entitled to this exception.

(e) *Title and maintenance*. When a property owner ties on to a sanitary sewer service line installed pursuant to paragraph (c) of this section, and pays the sewer service line charge levied in paragraph (d) of this section, the city, by appropriate instrument, shall convey and release to the property owner all its right, title and interest in the sanitary sewer service line so installed by the city. Thereafter, all repairs and maintenance of the sanitary sewer service line shall be the responsibility of the property owner or user of the sewer; provided, for all sanitary sewer service lines hereafter installed by developers in subdivisions and not by the city, for which no sewer service line charge is charged to the property owner, all repairs and maintenance of such sanitary sewer service lines shall be the responsibility of either the property owner, user of the sewer, or the developer, as the owner, user and developer shall agree by separate contract between themselves.

(f) *Location of sewer stubout*. The plumbing contractor is responsible for locating the sewer stubout. City personnel will provide whatever information is available for this

purpose. If no "wye" or "tee" exists within three (3) feet of either side of the location shown in the city's records then a tap will be provided by the city when the sewer main is uncovered. If a manhole needed for locating a service line has been lost, then the city shall be responsible for locating the manhole.

(g) *Taps on city sewers*. All taps directly made unto the city's sewer lines shall be made by city sewer maintenance personnel. The request for the tap shall be made by the plumbing inspector. The plumbing contractor shall excavate to the city's sewer and expose the pipe in preparation for the tap. Only one service line shall be allowed to be installed in a trench. New taps shall be made using a "wye" type connection.

(h) *Manhole required*. A new manhole will be required whenever a sewer service line larger than six inches (6") is needed to tie unto the city's sewer. The plumbing contractor shall excavate to the city's sewer and sufficiently expose the pipe for installation of a manhole. The city's sewer maintenance personnel shall install the manhole after a request is made by the plumbing inspector. The cost of the manhole, including labor and materials, shall be charged to the owner after construction is completed.

(i) *Maintenance of sewer service lines*. All repairs and maintenance of the sanitary sewer service line to include correction of excessive inflow or infiltration shall be the responsibility of the property owner or user of the sewer. The city shall be responsible for the maintenance of collector lines and interceptor lines only up to the point where the owner's sewer service line connects to the city's lines.

(j) *Exceptions for state highways and railroads*. When the installation of sanitary sewer service lines is required for sewers constructed in highways or streets owned by the State of Tennessee for which boring rather than open cutting is required by regulation of the State of Tennessee, installation shall be at the expense of the property owner, and the provisions of paragraph (c) shall not be applicable. Whenever a sanitary sewer service line must be installed under a railroad track or railroad right-of-way, the provisions of paragraph (c) shall not be applicable, and the property owner shall construct and maintain the sanitary sewer service line at his own expense. Installation of sanitary sewer service lines in state highways or streets must additionally be approved by the State Department of Transportation, and in railroad rights-of-way by the railroad.
(Ord. No. 9409, § 1, 6-5-90; Ord. No. 11175, § 32, 9-11-01)

**Sec. 31-5. Service lines to enter sanitary sewers at junction; exception.**

No service lines shall enter a sanitary sewer at any point except where a junction has been made and left therefor, unless by special permission of the superintendent, which authority he may delegate to the chief plumbing inspector. In all cases where such permission is given, the work shall be done under the inspection of the chief plumbing inspector and at the risk and expense of the party making the connection.
(Ord. No. 9409, § 1, 1-6-92)

**Sec. 31-6. Permit required to make connection.**

(a) Before the owner of any property within or beyond the corporate limits of the city connects such property to the city sewer, he or his agent shall make application to the building official for, and have issued to him, a permit so to do. Such work shall only be performed by a licensed master plumber who must sign the permit. The permit application shall be a form prescribed by the chief plumbing inspector. All connections shall be inspected and approved by a city inspector before being used.

(b) Connections made without an approved application may be cut off by order of the superintendent or chief plumbing inspector. Such unapproved connection may be allowed to remain active if inspected and accepted, however, the owner shall be required to pay a fee in lieu of a permit application fee that is double the regular permit fee then in effect.

(c) No permit for a connection which may be used for discharge of industrial process wastes or other non-domestic wastes regulated by article III of this chapter shall be issued except upon separate application to the superintendent and approval of the discharge under the provisions of article III.
(Ord. No. 9409, § 1, 6-5-90)

**Sec. 31-7. Reserved.**

**Sec. 31-8. Sewer construction; acceptance of work.**

All sewer construction involving interceptor sewer lines, pump stations, metering stations and appurtenances which shall become a part of the city's sewer system shall not be constructed without the plans therefore having first been approved and the construction inspected and approved by the superintendent. Any construction work where city sewers are opened, uncovered, or undercut shall have been previously approved by the superintendent or the city engineer.
(Ord. No. 9409, § 1, 6-5-90)

## Sec. 31-9. Right to enter, inspect connection.

The superintendent, the building inspector or other designated employees of the city shall have free and unobstructed access to any part of the premises where house drains or other drains connected with or draining into the city sewers are laid, for the purpose of examining the construction, condition and method of use of the same, upon cause or reasonable suspicion that there may be inadequate facilities, the facilities present may not be properly functioning, there is an improper discharge, or upon a periodic systematic inspection of a particular drainage basin or other large segment of the system through those facilities at any time of the day between the hours of 7:00 a.m. and 6:00 p.m. or any other time in the event of an emergency. If such entry is refused, the sewer service may be disconnected upon reasonable notice and an opportunity for a hearing. The service may be suspended immediately in the event of an emergency if there is reasonable cause to suspect that the discharge will endanger the public health or the environment, shall have the potential to interrupt the treatment process, or shall damage the city's lines or facilities, and a hearing shall thereafter be afforded the user as soon as possible.
(Ord. No. 9409, § 1, 6-5-90)

## Sec. 31-10. Demolished buildings.

When a building is demolished, it shall be the responsibility of the owner to have the sewer service line plugged securely so that extraneous water will not enter the sewer. The owner of the premises or his agent shall notify the building inspector of such a plug, and allow same to be inspected prior to covering of any work. If such line is to be reused, it must first undergo inspection by the building inspector and be in conformity with then-existing standards.
(Ord. No. 9409, § 1, 6-5-90)

## Sec. 31-11. Limitations on point of discharge; temporary facilities.

No person shall discharge any substance directly into a manhole or other opening in a city sanitary sewer other than through an approved building sewer, unless he shall have been issued a temporary permit by the superintendent. A temporary permit may be issued in the discretion of the superintendent to provide for discharges from portable sanitary facilities for festivals or public shows or for other reasonable purposes. The superintendent shall incorporate in such a temporary permit such conditions as he deems reasonably necessary to insure compliance with the provisions of this chapter. The user shall be required to pay reasonable charges and fees for the permit and service in an amount not less than the charges and fees for normal discharges. Any discharge other than through an approved building sewer or upon a permit issued by the superintendent shall be unlawful.
(Ord. No. 9409, § 1, 6-5-90)

## Sec. 31-12. Vehicle wash racks.

All filling stations, garages, self-service automobile washers and other public wash racks where automobiles or other vehicles are washed shall install catch basins in conformity with the plumbing code upon a permit obtained from the building official. In the event any existing premises shall not have a catch basin and the sewer line servicing the facility shall stop up due to grit or slime in the sewer lines, then the owner or operator of such premises shall be required to modify their facilities to construct a catch basin as a condition of continuing to use the system. If such users are industrial users as defined in article III of this chapter, they are required to obtain a permit as specified therein.
(Ord. No. 9409, § 1, 6-5-90)

## Sec. 31-13. Grease traps, grit traps, oil traps and lint traps.

Restaurants, laundries, wash racks, vehicle service stations, private multi-user systems, engine or machinery repair shops and other facilities that produce grease, grit, oil, lint or other materials which accumulate and cause or threaten to cause stoppages or impair the efficiency of the city's sewers or threaten the safety of its employees, shall install and maintain a grease trap, grit trap, lint trap, oil interceptor, or other appropriate device of standard design and construction to prevent excess discharges of such materials. The design and construction of any such device shall be subject to prior approval of the superintendent, and constructed in accord with applicable building codes.
(Ord. No. 9409, § 1, 6-5-90)

## Sec. 31-14. Multi-user private sewer systems.

Excluding industrial waste facilities issued a permit pursuant to article III, the owner or operator of a private sewer system such as but not limited to multi-tenant buildings, building complexes, or shopping malls shall be responsible for the quality of wastewater discharged at the point of connection to the city's sanitary sewer system, and shall be responsible for any violations of the provisions of this chapter including liability for the damage or injury caused to the city's system as a result of any discharge through the private system. (Ord. No. 9409, § 1, 6-5-90)

## Sec. 31-15. Prohibitions on storm drainage, ground water, unpolluted water, and contaminated storm water.

(a) No storm water, ground water, rain water, street drainage, rooftop drainage, basement drainage, subsurface drainage, foundation drainage, yard drainage, cooling water,

process water drainage, or other unpolluted water shall be discharged to the city's sanitary sewer system unless no other reasonable alternative is available, and then no such water shall be discharged to the city's sanitary sewer system except upon permission by the superintendent upon such reasonable conditions as he may prescribe and upon payment of a sewer service charge based upon the quantity of water discharged as measured by a flow meter or a reasonable estimate accepted by the superintendent. All users shall be required to maintain their private sewer lines so as to prevent infiltration of ground or storm water as a condition of use of the system and shall immediately repair or replace any leaking or damaged lines.
(Ord. No. 12023, § 4, 10-2-07)

(b) The city will accept the discharge of contaminated storm water if the following criteria are met: 1) all known and available technology will not prevent contamination or treat contaminated water to meet state standards for discharge to receiving waters or will cause unreasonable financial burden; 2) the contaminated storm water meets the city's discharge limits and all state and federal pretreatment requirements; and 3) volume of the discharge will not exceed the hydraulic loading in the collection system or the treatment plant.
(Ord. No. 9409, § 1, 6-5-90; Ord. No. 12023, § 4, 10-2-07)

**Sec. 31-16. Limitations on the use of garbage grinders.**

No waste from garbage grinders shall be discharged into the city's sewers except for private garbage grinders used in an individual residence or upon permit issued by the superintendent for preparation of food consumed on premises, and then only where applicable fees therefor are paid. Installation of any garbage grinder equipped with a three-fourths horsepower (or greater) motor shall require a permit. The superintendent may issue a permit when there is inadequate space on the user's premises to properly store food preparation waste between regularly scheduled garbage pickup by city crews or a private collection service with equal or greater frequency of collection. Provided, further, that such grinders shall shred the waste sufficiently that it can be carried freely under normal flow conditions prevailing in the city's sewer lines. It shall be unlawful for any person to use a garbage grinder connected to the sewer system for the purpose of grinding and discharging plastic, paper products, inert materials or anything other than the waste products from normal food preparation and consumption.
(Ord. No. 9409, § 1, 6-5-90)

**Sec. 31-17. Hospital or pathological waste.**

It shall be unlawful for any person to dispose of pathological waste, surgical operating room waste or delivery room waste by discharging same to the city's sewer system.
(Ord. No. 9409, § 1, 6-5-90)

## Sec. 31-18. Obstruction of or damage to sewer lines.

It shall be unlawful for any person to deposit or cause to be deposited any waste of any character whatsoever which may obstruct or damage storm or sanitary sewer lines or which may inhibit, disrupt, or damage either system, including the sewer treatment process and operations. This prohibition shall include any and all substances, whether liquid, solid, gaseous or radioactive and whether associated with human habitation, of human or animal origin, or from any producing, manufacturing or processing. It shall be unlawful to block or obstruct any catch basin, sewer line, or other appurtenance, or to break, injure or remove any portion from any part of a sewer, drain or catch basin including plates covering manholes.
(Ord. No. 9409, § 1, 6-5-90)

## Sec. 31-19. Assessment of damages to users.

When the discharge of waste or any other act or omission causes an obstruction, damage, or any other impairment to the city's facilities, causing an expense or damages of whatever character or nature to the city, the superintendent shall assess the expenses and damages incurred by the city to clear the obstruction, repair damage to the facility, and otherwise rectify any impairment, and bill the person responsible for the damage for reimbursement of all expenses and damages suffered by the city. If the person responsible refuses to pay, then the superintendent shall forward a copy of the statement and documentation of all expenses to the city attorney who shall be authorized to take such legal action as shall be appropriate.
(Ord. No. 9409, § 1, 6-5-90)

## Sec. 31-20. Violations, discontinuance of water service.

(a) *Penalties for violations of article*. Anyone violating a provision of this article shall be guilty of a misdemeanor, and upon conviction, is punishable as provided in section 1-8 of this code.

(b) *Violations deemed separate offenses*. Separate violations shall constitute separate offenses and, upon conviction, each day of violation shall constitute a separate offense.

(c) *Other remedies*. In addition to other remedies provided herein, the superintendent may issue a show cause notice to any user who appears to be violating any provisions of this article or chapter to show cause why sewer service should not be discontinued. The notice shall include the nature of the violation with sufficient specificity as to the character of the violation, and the date(s) on which such violation(s) occurred to enable the user to prepare a defense. Such notice shall be mailed to the user by certified mail, return receipt requested, or shall be personally delivered to the user at least twenty (20) days prior to the proposed action except in

the event of an emergency. At the show cause hearing, the user may present any defense he may have to such charges, either in person or through submission of written or documentary proof. Following such hearing or opportunity for a hearing, the superintendent may in his discretion order the termination of sewer service if satisfied from all the proof available that the violation was willful and the termination is necessary to abate the offending condition, or to prevent future violations. The superintendent may terminate service for a period not to exceed one (1) year for a willful violation and may terminate service indefinitely to abate offending conditions or prevent future violations, subject to the correction of such conditions or violations by the user.

(d) *Emergency termination of service*. If in the opinion of the superintendent it appears that such violation presents or may present an emergency situation endangering the public health, the environment, sewer system personnel, or the operation of the system, he may take immediate action to abate the condition and terminate service. In the event such emergency action adversely affects the user, the superintendent shall provide the user an opportunity for a hearing as soon as practicable thereafter to consider restoration of service upon abatement of the condition or other reasonable conditions. Following the hearing, the superintendent may take any such action authorized by paragraph (c) should the proof warrant such action.

(e) *Water service*. Any violation of provisions of article I, II or III which is not corrected or abated following a notice and opportunity for a hearing shall be grounds for the termination of water service and/or plugging the sewer line.
(Ord. No. 9409, § 1, 6-5-90)

**Secs. 31-21 -- 31-30. Reserved.**

## ARTICLE II. SEWER SERVICE CHARGES[2]

### Sec. 31-31. Levied.

For the purpose of paying the interest on and principal of revenue bonds issued by the city for the payment of the cost and expenses appurtenant, incident or necessary thereto for the construction and acquisition of additions, extensions and improvements to the sewer system,

[2] **Cross reference**--Businesses, trades and occupations generally, Ch. 11.

consisting of sanitary sewers, intercepting and outfall sewers, pumping facilities, treatment and disposal plants and other facilities for the collection, treatment and disposal of sewage and industrial waste and the operation and maintenance of the sewers and sewerage system and sewage disposal facilities of the city, there hereby is imposed sewer service charges upon the owner or occupant of all property now served or which may hereafter be served by the city's sewer system at the rates set forth in this article.
(Code 1986, § 31-31)

### Sec. 31-32. Abutting property owners, to pay charges.

The owner or occupant of each lot or parcel of land which abuts upon a street or other public way containing a sanitary sewer upon which lot or parcel a building has been or may hereafter be constructed for residential, commercial or industrial use shall pay the sewer service charges as provided in this article. The superintendent or his designee shall make the determination whether or not a lot or parcel abuts upon a segment of street, alley, easement or other public way in which there is a sewer for the purposes of levying services charges; provided that he or she may waive the collection of such charges where the connection is infeasible based upon engineering or hydraulic principles, the connection would not comport with applicable plumbing or building codes, or the connection would not comport with other applicable codes, laws or regulations.
(Code 1986, § 31-32; Ord. No. 9384, § 1, 5-29-90)

### Sec. 31-33. Contracts for disposal of sewage authorized; charges.

The superintendent may, subject to approval by the city council, enter into contracts with any municipality, county, incorporated district or person for the treatment and disposal of sewage collected and pumped or delivered to some part of the sewage collected and pumped or delivered to some part of the sewer system; provided, however, that the charges to be paid for the treatment and disposal of such sewage shall not be less than an amount which is fair and equitable, taking into account the cost to the city of such treatment and disposal and the cost of the sewage disposal system. All revenues received pursuant to such contract shall be deemed to be revenues of the sewer system, and shall be applied and accounted for in the same manner as other revenues derived from the operation of such system.
(Code 1986, § 31-33; Ord. No. 9384, § 2, 5-29-90)

### Sec. 31-34. Charge to be based on water consumption.

The sewer service charges imposed by this article shall be based upon the water consumption of the owner or occupant of the properties served, as measured by the meters of the

water company or meters installed by the owner or occupant of property, as provided in this article.
(Code 1986, § 31-34; Ord. No. 9384, § 12, 5-29-90)

**Sec. 31-35. Billing procedure.**

(a) The sewer service charges shall become effective on water company services rendered at the rates hereinafter imposed and shall be billed by the water company at the same time it bills the owner or occupant for water service charges, and shall be due and payable at the same time as are the water service charges.

(b) Sewer service charges shall be billed by the water company as a separate designated item on its water bills.
(Code 1986, § 31-35; Ord. No. 9384, § 12, 5-29-90)

**Sec. 31-36. Schedule.**[3]

(a) Enumeration of charges; quantity of water used. Sewer service charges shall be based upon the quantity of water used as shown by water meter readings and shall be the dollar amount derived by applying the total charge in dollars per one thousand (1,000) gallons for the quantities of water shown in the following table:

| User Class (gallons) | Fiscal Year 2007/2008 - 1 Total Charges ($/1,000 gallons) | Fiscal Year 2007/2008 - 2 Total Charges ($/1,000 gallons) |
|---|---|---|
| First 100,000 | $ 4.69 | $ 4.83 |
| Next 650,000 | 3.48 | 3.58 |
| Next 1,250,000 | 2.82 | 2.90 |
| Next 30,000,000 | 2.16 | 2.25 |
| Over 32,000,000 | 2.05 | 2.15 |

[3] **Editor's note:** Ordinance No. 11221, Section 7, adopted December 18, 2001, provided that the operative date for changes in rates shall be July 1, 2001, and the operative date for residential users billed through the water suppliers shall be November 1, 2001.

In addition, the total charges derived from the above chart for residential users will be multiplied by ninety (90) percent to compensate for water use not going to the sewer such as lawn and garden watering. Any residential location where a separate water meter has been installed for the purpose of lawn and garden watering shall not be entitled to have the multiplier applied to any water consumed through the primary water meter. Each residence or apartment unit shall have a maximum monthly sewer service charge for a volume of no more than 12, 000 gallons water used; unless the minimum charge due to water meter size exceeds the 12,000 gallon limit then the monthly sewer service charge shall be at least the minimum for that particular size water meter.
[Ord. No. 12023, § 5, 10-2-07]

(b) Regional service charge rates (wheelage and treatment). The regional sewer service use charge (wheelage and treatment) shall be collected from regional users of the system including Collegedale, Tennessee; Hamilton County, Tennessee; Walker County, Georgia; Catoosa County, Georgia; Lookout Mountain, Georgia; Dade County, Georgia; Rossville, Georgia; Ringgold, Georgia and Fort Oglethorpe, Georgia: and shall be determined either under the "billable flow" methods based on the quantity of water used as shown by applicable water company meter readings or the "total flow" method based upon flow meter measured flow according to the applicable contract with the regional user pursuant to subparagraphs (c) and (d).
[Ord. No. 12023, § 6, 10-2-07]

(c) Billable flow. The amount due from the regional user shall be the dollar amount derived by applying the total charge shown in the table below per one thousand (1,000) gallons of water sold.

| | Regional Operation & Maintenance Charge ($/1,000 gallons) | Regional Debt Charge ($/1,000 gallons) | Regional Total Charge (Wheelage and Treatment) ($/1,000 gallons) |
|---|---|---|---|
| Wheelage and Treatment | $ 1.3138 | $ 0.6813 | $ 1.9951 |

If regional customers are billed directly through the water company, the rate to be charged shall be two dollarsand four cents ($2.04) per one thousand (1,000) gallons.
(Ord. No. 11728, § 16, 8-16-05; Ord. No. 12023, § 7, 10-2-07)

(d) Total flow. The amount due from the regional user shall be the dollar amount derived by applying the total charge shown in the table below applied to the quantity of water measured by a flow meter installed and maintained at or near the point of connection between the system of the regional user and the Chattanooga system. In the event of any malfunction of said meters, flow shall be estimated, interpolated and/or projected in the most equitable manner possible. Such estimates, along with available readings for periods where there was no malfunction, shall be the basis for billing.

| | Operation & Maintenance Charge ($/1,000 gallons) | Regional Debt Charge ($/1,000 gallons) | (Wheelage and Treatment) ($/1,000 gallons) |
|---|---|---|---|
| Wheelage and Treatment | $ 0.7190 | $ 0.3579 | $ 1.0769 |

(Ord. No. 11728, § 17, 8-16-05; Ord. No. 12023, § 8, 10-2-07)
(Code 1986, § 31-36; Ord. No. 9187, §§ 1-3, 7-5-89; Ord. No. 9384, §§ 3-5, 5-29-90; Ord. No. 9631, §§ 1-3, 10-22-91; Ord. No. 9761, §§ 1-3, 7-28-92; Ord. No. 9963, §§ 1-3, 10-19-93; Ord. No. 10094, §§ 1-3, 8-30-94; Ord. No. 10285, §§ 1-3, 9-12-95; Ord. No. 10495, §§ 1-3, 11-12-96; Ord. No. 10632, §§ 1-3, 10-28-97; Ord. No. 10769, §§ 1-3, 10-6-98; Ord. No. 10935, §§ 1-3, 11-16-99; Ord. No. 11070, §§ 1-3, 9-19-00; Ord. No. 11221, §§ 1-3, 12-18-01; Ord. No. 11344, §§1, 3, 5, 11-05-02; Ord. No. 11473, §2, 10-21-03; Ord. No. 11581, §§17-18, 07-06-04; Ord. No. 11728, §§ 16-17, 8-16-05; Ord. No. 12023, §§ 6-8, 10-2-07)

**Sec. 31-37. Minimum service charges.**

Minimum sewer service charges based upon water meter connection size shall be as follows:

Monthly Minimum Sewer Service Charges

| Meter Size (inches) | Fiscal Year 2007/2008-1 Charge per Month | Fiscal Year 2007-2008-2 Charge per Month |
|---|---|---|

| | | |
|---|---|---|
| 5/8 | $ 9.70 | $ 9.98 |
| 3/4 | 34.60 | 35.60 |
| 1 | 60.45 | 62.21 |
| 1-1/2 | 135.29 | 139.23 |
| 2 | 239.54 | 246.52 |
| 3 | 561.51 | 577.86 |
| 4 | 1,037.68 | 1,067.90 |
| 6 | 2,471.59 | 2,543.57 |
| 8 | 4,371.79 | 4,499.12 |

The minimum sewer service change for residential users with various meter size shall be multiplied by ninety (90) percent to compensate for water use not going to the sewer such as lawn and garden watering. Any residential location where a separate water meter has been installed for the purpose of lawn and garden watering shall not be entitled to have the multiplier applied to any water consumed through the primary water meter.
(Code 1986, § 31-37; Ord. No. 9187, § 4, 7-5-89; Ord. No. 9384, § 6, 5-29-90; Ord. No. 9631, § 4, 10-22-91; Ord. No. 9761, § 4, 7-28-92; Ord. No. 9963, § 4, 10-19-93; Ord. No. 10094, § 4, 8-30-94; Ord. No. 10935, § 4, 11-16-99; Ord. No. 11344, §2, 11-05-02; Ord. No. 12023, § 9, 10-2-07)

## Sec. 31-38. Designation of water accounts to be charged.

The superintendent shall designate and report to the water company the water service accounts which shall be billed for sewer service charges, and shall furnish the water company serving the user with the rates as they may be changed from time to time to be charged for sewer services. This designation and report shall include all properties for which sewer service has been provided by the city. In event of the extension of the city's sewer system to any property now served by sewers, the superintendent shall immediately notify the water company serving the user of the additional accounts to be billed for sewer service.
(Code 1986, § 31-38; Ord. No. 9384, § 7, 5-29-90)

## Sec. 31-39. Charges where water usage not metered.

(a) *Generally*. The owners or occupants of property obtaining water from a source or sources other than through a meter of the city water company which is discharged into the city's sewers shall install, without cost to the city, a meter to measure the quantity of water received from such source, and shall pay the same rates as provided in sections 31-36 and 31-37 of this Code. No meter shall be installed or used for such purpose without the approval of the city engineer. If the owner of such property fails to install an approved meter or meters, the city

engineer shall make an estimate of the quantity of such water used by such property owner and discharged into the city's sewers from the property, and the owner or occupant of the property shall be liable to the city for the sewer service charges due, which may be collected by suit in any court of competent jurisdiction.

(b) *Multi-unit complexes*. To provide more equality between single-family and multi-unit dwellings (with just one (1) or less number of water meters than the total number dwelling units in complex), sewer service charges to multi-unit apartment complexes served by master meters or any combination of meters totaling less than the number of units served shall be charged by the following formula:

$U_{ADJ} \times S_C \times O_C$

Where:

$U_{ADJ}$ = $U_{TOT} / O_C$

$U_{TOT}$ = Total usage of individual meter or master meter

$O_C$ = The number of units served by the referenced meter times a ninety (90) percent occupancy rate

$S_C$ = The service charge as detailed in sections 31-36(a) and 31-37

(Code 1986, § 31-39)

**Sec. 31-40. Consumers not to be charged sewer user charges for water used for industrial, commercial purposes not discharged into city sewers.**

(a) *Secondary metering.* Whenever a property upon which a sewer user charge is imposed under this article uses water for an industrial or commercial purpose, which water so used is not discharged into the sewerage system of the city, the quantity of water so used and not discharged into the city's sewers shall be excluded in determining the sewer user charge of the owner or occupant; provided that, the quantity of water so used and not discharged into the city sewers is measured by a device or meter (called a secondary meter) approved by the superintendent and installed by the owner or occupant without cost to the city. The sewer user charge based upon the consumption of water to be paid by the owner or occupant of such property shall be computed at the rates provided in this article less the quantity not discharged into the city's sewers. The city reserves the right to require calibration of secondary meters when appropriate. A secondary meter shall meet the following requirements:

(1) Meters should read in hundred (100) cubic feet.

(2) Meters must be located either in an outdoor meter box or vault, or inside the customer's building or structure in a clean, dry, safe place not subject to wide temperature variations so that the meter can be easily examined, read or removed.

(3) The customer shall, at its expense, provide suitable pipe connections and shut-off valves, one each at the inlet and outlet sides of the meter.

(4) The meter box or vault may be constructed to protect the meter from freezing and damage by vehicular traffic, and its location and design shall prevent, as far as possible, the inflow of surface water.

(5) Any changes in location of secondary meters, malfunctions, replacements or any other changes in the approved secondary meter installation must be reported to the superintendent in writing. Also a copy must be forwarded to the water company containing all pertinent information regarding that particular meter.

(6) No retroactive credits will be issued, if the holder of the secondary meter permit fails to comply with the rules and regulations in force at any particular time.

(7) If any water exempted from the sewer service charge is returned to the sewer system at any time or point, a metering device shall be installed. Any flow registered through such a meter shall be charged for sewer service.

(8) Any secondary meter must be easily accessible by the water company. If this is not possible, remote read meters shall be installed and be protected from any magnetic interference. It is the responsibility of the permit holder to assure the accuracy of the remote read to the installed meter.

(9) All meters must be calibrated and certified for accuracy once every eighteen (18) months. The certification of the inspection or a copy thereof has to be forwarded to the Moccasin Bend Treatment Plant.

(b) *Other sewer user charge credits.* User charge credits may also be given by the superintendent for the following purposes:

(1) Hidden or underground leaks except for accounts identified as residential; (Ord. No. 12023, § 10, 10-2-07)

(2) Catastrophic leaks where the water does not enter the sewer line except for accounts identified as residential; (Ord. No. 12023, § 10, 10-2-07)

(3) Where secondary meters are installed for swimming pools, lawn or garden watering, sprinkling systems, and other processes where water is used but not returned to the sewer;

(4) Filling a swimming pool will be allowed one credit per year for the initial fill if the water is not returned to the sewer at the end of the swimming season.

No sewer user may receive a credit for an amount which would reduce the resultant sewer bill below the minimum charge required by Section 32-31 of this article. To be considered for credit, leaks must be reported to the water company, and corrected by the owner or occupant without cost to the city. The sewer user charge based upon the consumption of water to be paid by the owner or occupant of such property shall be computed at the rates provided in this article less the quantity not discharged into the city's sewers.
(Code 1986, § 31-40; Ord. No. 9384, § 8, 5-29-90; Ord. No. 12023, § 10, 10-2-07)

## Sec. 31-41. Industrial user sewer surcharge.[4]

(a) *Levy.* There shall be and is hereby levied upon industrial users which discharge wastewater in concentrations in excess of "normal wastewater" a surcharge as set forth in this section.

(b) *Charge formula.* The industrial user surcharge is based upon the increased operation and maintenance cost and other increased expenses incurred in the handling of such wastewater as determined by the following formula:

$$Cs = [(Bc \times B) + (Sc \times S) + (Pc \times P)] Vu \times 8.34$$

[4] **Editor's note:** Ordinance No. 11221, Section 7, adopted December 18, 2001, provided that the operative date for changes in rates shall be July 1, 2001, and the operative date for residential users billed through the water suppliers shall be November 1, 2001.

Cs = Surcharge for wastewaters exceeding the strength of "normal wastewater" expressed in dollars per billing period.

Bc = Operation and maintenance (O & M) cost for treatment of a unit of $BOD_5$ expressed in dollars per pound.

B = Concentration of $BOD_5$ from a user above the base level of 300 mg/l expressed in mg/l.

Sc = Operation and maintenance (O & M) cost for treatment of a unit of total suspended solids expressed in dollars per pound.

S = Concentration of total suspended solids from a user above the base level of 400 mg/l, expressed in mg/l.

Pc = Operation and maintenance (O & M) cost for treatment of a unit of any pollutant which the city is committed to treat by virtue of its NPDES permit or other regulatory requirement expressed in dollars per pound.

P = Concentration of any pollutant from a user above the base level. Base levels for pollutants subject to surcharge as may be hereafter established by the city expressed in mg/l.

Vu = Volume contribution of a user per billing period. Expressed in million gallons.

8.34 = Conversion factor to make units cancel. Expressed as (pounds/million gallons)/mg/l.

(c) Rates. Based upon the current cost of treating wastewater containing constituents with concentrations in excess of “normal wastewater,” numerical rates are hereby established for Bc and Sc as follows:

Bc = $0.094 per pound of BOD for concentrations in excess of three hundred (300) milligrams per liter.

Sc = $0.067 per pound of total suspended solids for concentrations in excess of four hundred (400) milligrams per liter.

(Ord. No. 11728, § 18, 8-16-05; Ord. No. 12023, § 11, 10-2-07)

(d) *Billing*. The superintendent shall notify and in conjunction with a normal bill charge each industrial user within sixty (60) days following the semi-annual periods ending on December thirty-first and June thirtieth, and such surcharges shall be payable no later than April first and October first respectively. The superintendent, at his discretion, may enter into an agreement with the industrial user to bill and collect such fees on a monthly basis. Each user shall be notified at least annually in conjunction with a regular bill of the rate and that portion of the user charges which are attributable to wastewater treatment services.

(e) *Data concerning concentration.* The concentrations of any pollutant of an industrial user and the volume contribution of that user shall be calculated from discharge monitoring reports which shall be submitted by the industrial user following the semi-annual periods ending on December thirty-first and June thirtieth by January thirty-first and July thirtieth respectively and being subject to verification by inspection and monitoring undertaken by the superintendent pursuant to division 9 of this article, from records maintained by the industrial user pursuant to division 8 of this article, and from reliable information obtained from any other source.

(f) *User charge and surcharge studies.* The superintendent shall, based upon a documented study, recommend to the mayor and city council no less frequently than biennially an equitable rate structure for purposes of establishing a basic user charge computed on the basis of "normal wastewater" and a surcharge for industrial users which discharge effluent in concentrations in excess of "normal wastewater". The superintendent shall consider in his report the amount of revenue needed for the purposes specified in section 31-31, consistent with 40 CFR part 35 and all other applicable federal and state laws and regulations. Such recommendation shall be based upon the premises that each user or user class pays his proportionate share of the operation and maintenance including replacement costs of the treatment works, based upon the user's proportionate contribution to the total wastewater loading from all users or user classes. The superintendent shall also recommend as warranted that surcharges be placed upon specific wastewater constituents, including a surcharge for all users which discharge any toxic pollutant which causes an increase in the cost of managing the effluent or the sludge of the city's treatment works, so as to recover such increased costs. In making his recommendation relative to changes in user charges or surcharges, the superintendent may recommend that any excess revenues or any deficiency in revenues collected from a class of users in the preceding period be applied to the operation and maintenance cost attributed to that class for the next period and that the rate for that class of users be adjusted accordingly.

(g) *Appeal.* An industrial user may contest the accuracy of a user sewer surcharge bill by paying such bill under protest and within thirty (30) days following the date of the bill

lodging with the superintendent a notice of appeal to the wastewater regulation board. No particular form of notice of appeal is required, but it shall set forth with particularity the nature of any errors allegedly committed in the computation of such bill. Unless the superintendent shall agree to correct any error or enter into a reasonable compromise concerning same, he shall notify the board at its next regularly scheduled meeting of the pendency of an appeal. The board shall, upon notice to the industrial users, schedule a hearing to receive evidence relating to the matter, and shall render such determinations and issue such orders as the law and facts of the case may require.
(Code 1986, § 31-136; Ord. No. 9187, § 5, 7-5-89; Ord. No. 9384, § 9, 5-29-90; Ord. No. 9631, § 5, 10-22-91; Ord. No. 9654, § 108, 1-6-92; Ord. No. 9761, § 5, 7-28-92; Ord. No. 9963, § 5, 10-19-93; Ord. No. 10094, § 5, 8-30-94; Ord. No. 10285, § 4, 9-12-95; Ord. No. 10495, § 4, 11-12-96; Ord. No. 10632, § 4, 10-28-97; Ord. No. 10769, § 4, 10-6-98; Ord. No. 10935, § 5, 11-16-99; Ord. No. 11070, § 4, 9-19-00; Ord. No. 11221, § 4, 12-18-01; Ord. No. 11344, §5, 11-05-02; (Ord. No. 11473, §3, 10-21-03; Ord. No. 11581, §19, 07-06-04)

## Sec. 31-42. Appeals.

A user may contest a credit or billing determination by the superintendent by paying said bill under protest and within thirty (30) days following the due date of said bill lodging with the superintendent a notice of appeal with the Wastewater Regulations and Appeals Board. The appeal shall follow the procedures in Section 31-295.
(Ord. No. 9384, § 10, 5-29-90)

## Sec. 31-43. Miscellaneous fees.[5]

(a) *Applicability.* There shall be and is hereby levied miscellaneous fees to be collected by the superintendent for various purposes relating to this chapter as set forth in this section.

(b) *Fees for garbage grinders.* Any user of a garbage grinder, except users in a premise used exclusively for an individual residence, shall be charged at a rate of one hundred forty six dollars ($146.00) per month. The superintendent shall bill users on a bi-monthly basis and the bills shall be due and payable within thirty (30) days following the last day of the billing period.

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[5] **Editor's note:** Ordinance No. 11221, Section 7, adopted December 18, 2001, provided that the operative date for changes in rates shall be July 1, 2001, and the operative date for residential users billed through the water suppliers shall be November 1, 2001.

(Ord. No. 11728, § 23, 8-16-05; Ord. No. 12023, § 12, 10-2-07)

(c) *Monitoring Requested by User.* The superintendent shall charge and collect from any user requesting the collection of effluent samples and the analysis of same a sum of money sufficient to pay for the personnel, equipment, and materials needed to collect and analyze same. He shall publish no less frequently than yearly a schedule of such fees, and shall charge all persons uniformly according to said schedule of charges. No such monitoring requested by user shall be performed unless the user shall agree in advance to payment of charges according to said schedule. The superintendent shall bill for such monitoring reports within one (1) week following the completion thereof, said bills to be payable within thirty (30) days following the date of the bill. The superintendent shall not perform for a user routine self-monitoring required under the provisions of an industrial discharge permit.

(d) *Permit Fee.* All significant industrial users as defined in article III of this chapter shall be charged an annual permit fee of five hundred dollars ($500.00) per year. The superintendent shall bill significant industrial users annually and the bills shall be due and payable within thirty (30) days.

(e) *Truck discharge operation fee.* The superintendent shall charge and collect the sum of forty dollars ($40.00) per truck per year for a truck discharge operation permit as authorized pursuant to division 6 of this article. The holders of such permits shall also be charged a fee set forth in paragraphs (d) and (e) of this section. Such additional fees shall be collected by the superintendent at the time of the discharge or, in his discretion, he may enter into an agreement with the holder of such a permit to bill and collect the fees on a monthly basis.

(f) *Fees for septic tank discharge*. All persons discharging concentrated, domestic septic tank sewage waste from a truck under the provisions of Article III of this Chapter shall be charged at the rate of fifty three dollars ($53.00) per one thousand (1,000) gallons of such waste. The minimum charge for septic tank discharges shall be one half (1/2) of the rate for one thousand (1,000) gallons of the rate in effect at the time of such discharge. All persons discharging grease trap or grease interceptor waste or loads where septic tank waste has been mixed or blended with grease trap or grease interceptor waste shall be charged at the rate two (2) times the rate for septic tank wastes.

(Ord. No. 11728, § 23, 8-16-05; Ord. No. 12023, § 12, 10-2-07)

(g) *Fees holding tank wastes*. All persons discharging any holding tank waste authorized pursuant to division 6 of this article shall be charged at the rate of four dollars and sixty-nine cents ($4.69) per one thousand (1,000) gallons of such discharge, plus any surcharge rate authorized by Article III of this chapter for concentrations of pollutants in excess of normal

waste water without regard to the definition of the industrial user or other limitations set forth in such section. The superintendent may also require a chemical analysis of such waste and charge therefore. The fee for fiscal year 2007/2008 – 2 shall be four dollars and eighty-three cents ($4.83). The minimum charge for holding tank wastes shall be the fee for one thousand (1,000) gallons of said discharge of the rate in effect at the time of such discharge.

(Ord. No. 12023, § 12, 10-2-07)

(Ord. No. 9384, § 11, 5-29-90; Ord. No. 9631, §§ 6-8, 10-22-91; Ord. No. 9761, §§ 6-7, 7-28-92; Ord. No. 9963, §§ 6-7, 10-19-93; Ord. No. 10094, §§6-8, 8-30-94; Ord. No. 10632, §§ 5-6, 10-28-97; Ord. No. 10769, §§ 5-6, 10-6-98; Ord. No. 10935, §§ 6-7, 11-16-99; Ord. No. 11070, §§ 5-6, 9-19-00; Ord. No. 11221, §§ 5-6, 12-18-01; Ord. No. 11344, §§6-8, 11-05-02; Ord. No. 11728, §§ 16-18 and 23, 8-16-05, Ord. No. 12023, § 12, 10-2-07)

**Secs. 31-44 -- 31-49. Reserved.**

## ARTICLE III. INDUSTRIAL WASTE

### DIVISION 1. GENERALLY

**Sec. 31-50. General provisions.**

(a) *Purpose and policy.* The purpose of this article is to set uniform requirements for users of the city's wastewater collection system and treatment works to enable the city to comply with the provisions of the Clean Water Act and other applicable federal and state law and regulations, and to provide for the public health and welfare by regulating the quality of wastewater discharged into the city's wastewater collection system and treatment works. This article provides a means for determining wastewater volumes, constituents and characteristics, the setting of charges and fees, and the issuance of permits to certain users. This article establishes effluent limitations and other discharge criteria and provides that certain users shall pretreat waste to prevent the introduction of pollutants into the publicly owned treatment works (hereinafter referred to as POTW) which will interfere with the operation of the POTW, may cause environmental damage, interfere with the use or disposal of sewage sludge; and to prevent the introduction of pollutants into the POTW which will pass through the treatment works into the receiving waters or the atmosphere, or otherwise be incompatible with the treatment works; and to improve the opportunities to recycle and reclaim wastewaters and the sludges resulting

from wastewater treatment. This article provides measures for the enforcement of its provisions and abatement of violations thereof. This ordinance establishes a "Wastewater Regulations and Appeals Board" and establishes its duties and establishes the duties of the superintendent to insure that the provisions of this ordinance are administered fairly and equitably to all users.

(b) *Definitions.* For purposes of this article the following phrases and words shall have the meaning assigned below, except in those instances where the content clearly indicates a different meaning:

(1) **Act or "the Act" or the "CWA".** The Federal Water Pollution Control Act, also known as the Clean Water Act, as amended, 33 U.S.C. 1251, et seq.

(2) **"Approved POTW Pretreatment Program" or "Program" or "POTW Pretreatment Program".** This means a program administered by a POTW that meets the criteria established in 40 CFR (§ 403.8 and 403.9) and which has been approved by a regional administrator or state director in accordance with § 403.11 of Chapter 40 of the Code of Federal Regulations.

(3) **Building Sewer.** A sewer conveying wastewater from the premises of a user to a community sanitary sewer.

(4) **Board.** Wastewater Regulations and Appeals Board.

(5) **Categorical Standards.** National Pretreatment Standards, established by EPA for specific industrial user SIC (Standard Industrial classification) code categories.

(6) **Centralized Waste Treatment Facility or "CWT".** The term "CWT" means a commercial centralized waste treatment facility (other than a landfill or an incinerator) which treats or stores aqueous wastes generated by facilities not located on the site of the CWT and which disposes of these wastes by introducing them to the POTW.

(7) **City.** The City of Chattanooga, Tennessee, a municipal corporation.

(8) **Combined sewer.** A sewer which has been designed to carry both sanitary sewage and storm water runoff.

(9) **Community sewer.** Any sewer containing wastewater from more than one premise.

(10) **Conventional pollutant.** Biochemical oxygen demand, total suspended solids, pH, fecal coliform bacteria, and oil and grease.

(11) **Direct Discharge.** The discharge of treated or untreated wastewater directly to the waters of the State of Tennessee.

(12) **Discharge Monitoring Report.** A report submitted by an industrial user to the superintendent pursuant to this article containing information relating to the nature and concentration of pollutants and flow characteristics of a discharge from the industrial user to the POTW, using standard methods approved by the superintendent.

(13) **Environmental Protection Agency or "EPA".** The Environmental Protection Agency, an agency of the United States, or where appropriate the term may also be used as a designation for the administrator or other duly authorized official of said agency.

(14) **Grab Sample.** A sample which is taken from a waste stream on a one-time basis with no regard to the flow in the waste stream and without consideration of time.

(15) **Holding tank waste.** Any waste from holding tanks such as vessels, chemical toilets, campers, trailers, septic tanks, and vacuum-pump tank trucks. This specifically includes wastewaters from industrial users, which wastewaters are conveyed to the POTW by any means other than by a standard connection to a sanitary or combined sewer.

(16) **Indirect Discharge.** The discharge or the introduction of pollutants from any source regulated under section 307(b), (c), or (d) of the Act, (33 U.S.C. 1317), into the POTW (including holding tank waste discharged into the system) for treatment before direct discharge to the waters of the state.

(17) **Industrial User.** A source of indirect discharge which does not constitute a "discharge of pollutants" under regulations issued pursuant to section 402 of the Act. For the purposes of this article, an industrial user is a source of non-domestic wastes from industrial processes.

(18) **Interceptor Sewer System or "ISS".** Any portion of or all of the City of Chattanooga's wastewater collection system, treatment works, pump stations, and other appurtenances.

(19) **Interference.** The term "interference" means a discharge which, alone or in conjunction with a discharge or discharges from other sources, both:

(i) inhibits or disrupts the POTW, its treatment processes or operations, or its sludge processes, use or disposal; and

(ii) therefore is a cause of a violation of any requirement of the POTW's NPDES permit (including an increase in the magnitude or duration of a violation) or of the prevention of sewage sludge use or disposal in compliance with the following statutory provisions and regulations or permits issued thereunder (or more stringent State or local regulations), Section 405 of the Clean Water Act, the Solid Waste Disposal Act (SWDA) (including Title II, more commonly referred to as the Resource Conservation and Recovery Act (RCRA), and including State regulations contained in any State sludge management plan prepared pursuant to Subtitle D of the SWDA), the Clean Air Act, the Toxic Substances Control Act, and the Marine Protection, Research and Sanctuaries Act.

(20) **Mass emission rate.** The weight of material discharged to the community sewer system during a given time interval. Unless otherwise specified, the mass emission rate shall mean pounds per day of the particular constituent or combination of constituents.

(21) **Maximum concentration.** The maximum amount of a specified pollutant in a volume of water or wastewater.

(22) **National Pretreatment Standard.** Any regulations containing pollutant discharge limits promulgated by the EPA in accordance with section 307(b) and (c) of the Act (33 U.S.C. 1347) which applies to industrial users. These terms also include prohibited discharges promulgated in 40 CFR 403.5, and local limits adopted as part of the City's Approved Pretreatment Program.

(23) **New Source.**

(i) The term "new source" means any building, structure, facility or installation from which there is or may be a discharge of pollutants, the construction of which commenced after the publication of proposed pretreatment standards under Section 307(c) of the Act which will be applicable to such source if such standards are thereafter promulgated in accordance with that Section, provided that:

A) The building, structure, facility or installation is constructed at a site at which no other source is located; or

B) The building, structure, facility or installation totally replaces the process or production equipment that causes the discharge of pollutants at an existing source; or

C) The production or wastewater generated processes of the building, structure, facility or installation are substantially independent of an existing source at the same site. In determining whether these are substantially independent, factors such as the extent to which the new facility is integrated with the existing plant, and the extent to which the new facility is engaged in the same general type of activity as the existing source should be considered.

(ii) Construction on a site at which an existing source is located results in a modification rather than a new source if the construction does not create a new building, structure, facility or installation meeting the criteria of paragraphs (i)(B) or (C) of this subsection but otherwise alters, replaces, or adds to existing process or production equipment.

(iii) Construction of a new source as defined under this paragraph has commenced if the owner or operator has:

A) Begun, or caused to begin as part of a continuous onsite construction program:

1) Any placement, assembly, or installation of facilities or equipment; or

2) Significant site preparation work including clearing, excavation, or removal of existing buildings, structures,

or facilities which is necessary for the placement, assembly or installation of new source facilities or equipment; or

B) Entered into a binding contractual obligation for the purchase of facilities or equipment which are intended to be used in its operation within a reasonable time. Options to purchase or contracts which can be terminated or modified without substantial loss, and contracts for feasibility, engineering, and design studies do not constitute a contractual obligation under this paragraph.

(24) **National Pollutant Discharge Elimination System or NPDES permit.** A permit issued pursuant to Section 402 of the Act (33 U.S.C. 1342).

(25) **Normal Wastewater.** Effluent which contains constituents and characteristics similar to effluent from a domestic premise and specifically for the purposes of this article does not contain biochemical oxygen demand (BOD), or total suspended solids (TSS) in concentrations in excess of the following:

BOD -- 300 milligrams per liter
TSS -- 400 milligrams per liter

(26) **Pass Through.** The term "pass through" means a discharge which exits the POTW into waters of the United States in quantities or concentrations which, alone or in conjunction with a discharge or discharges from other sources, is a cause of a violation of any requirement of the POTW's NPDES permit (including an increase in the magnitude or duration of a violation). In the case of POTW receiving discharges from CWTs as defined above, pass through also means the failure of the CWT and the POTW to reduce pollutant discharges from the POTW to the degree which would be required under section 301(b)(2) of the CWA if the CWT discharged directly to surface waters.

(27) **Person.** Any individual, partnership, co-partnership, firm, company, corporation, association, joint stock company, trust, estate, governmental entity or any other legal entity, or their legal representatives, agents or assigns. The masculine gender shall include the feminine, the singular shall include the plural where indicated by the context.

(28) **Pollution.** The man-made or man-induced alteration of the chemical, physical, biological, and radiological integrity of water.

(29) **Premises.** A parcel of real estate or portion thereof including any improvements thereon which is determined by the superintendent to be a single user for purposes of receiving, using, and paying for services.

(30) **Pretreatment.** The term "pretreatment" means the reduction of the amount of pollutants, the elimination of pollutants, or the alteration of the nature of pollutant properties in wastewater prior to or in lieu of discharging or otherwise introducing such pollutants into a POTW. The reduction or alteration may be obtained by physical, chemical or biological processes, process changes or by other means, except as prohibited by 40 CFR § 403.6(d). Appropriate pretreatment technology includes control equipment, such as equalization tanks or facilities, for protection against surges or slug loadings that might interfere with or otherwise be incompatible with the POTW. However, where wastewater from a regulated process is mixed in an equalization facility with unregulated wastewater or with wastewater from another regulated process, the effluent from the equalization facility must meet an adjusted pretreatment limit calculated in accordance with 40 CFR § 403.6(e).

(31) **Pretreatment Requirements.** Any substantive or procedural requirement related to pretreatment, other than a national pretreatment standard imposed on an industrial user.

(32) **Publicly owned treatment works or POTW.** A treatment works as defined by section 212 of the Act, (33 U.S.C. 1292). This definition includes any sewers that convey wastewater to such a treatment works, and any devices and systems used in the storage, treatment, recycling and reclamation of municipal sewage or liquid industrial waste but does not include pipes, sewers or other conveyances not connected to a facility providing treatment.

The term in some contexts also means the City of Chattanooga, a municipality, as defined in Section 502(4) of the Act, (33 U.S.C. 1362) which has jurisdiction over the indirect discharges and the discharges from such a treatment works.

(33) **Reclaimed water.** Water which, as a result of treatment of waste, is suitable for direct beneficial uses or a controlled use that would not occur otherwise.

(34) **Significant Industrial User.** This term shall mean:

i) All dischargers subject to categorical pretreatment standards under 40 CFR 403.6 and 40 CFR Chapter 1, subchapter N; or

ii) All noncategorical dischargers that contribute more than 10,371 pounds per day of BOD, or more than 10,656 pounds per day of total suspended solids, or more than 700 pounds per day of ammonia nitrogen, or more than 25,000 gallons per day of process wastewater to the POTW; or

iii) All noncategorical dischargers that, in the opinion of the superintendent, have a reasonable potential to adversely affect the POTW's operation. This shall include but shall not be limited to all centralized waste treatment discharges, all tank and drum cleaning facilities, and all paint manufacturing facilities; or

iv) All noncategorical discharges that contain more than 100 pounds per day of combined BOD and total suspended solids load above that level found in "normal wastewater", or that contain more than 1000 pounds in a month of combined BOD and total suspended solids load above that level found in normal wastewater.

(35) **Standard industrial classification.** A classification pursuant to the Standard Industrial Classification Manual issued by the Executive Office of the President, Office of Management and Budget, 1972.

(36) **Superintendent.** The person designated by the city to supervise the operation of the publicly owned treatment works and the interceptor sewer system and who is charged with certain duties and responsibilities by this article, or his duly authorized representative, or in his absence or inability to act the person then in actual charge of said system.

(37) **Toxic pollutant.** Any pollutant or combination of pollutants listed as toxic in 40 CFR Part 401 promulgated by the Administrator of the Environmental Protection Agency under the provisions of 33 U.S.C. 1317.

(38) **Treatment works.** Any devices and systems used in the storage, treatment, recycling and reclamation of domestic sewage or industrial wastes of a liquid nature including interceptor sewers, outfall sewers, sewage collection systems,

pumping, power, and other equipment and appurtenances; extensions, improvements, remodeling, additions and alterations thereof; elements essential to provide a reliable recycled supply such as standby treatment units and clear well facilities; and any works, including land that will be an integral part of the treatment process or is used for ultimate disposal of residues resulting from such treatment; and including combined storm water and sanitary sewer systems.

(39) **Twenty-four hour, flow proportional composite sample.** A sample consisting of several effluent portions collected during a twenty-four (24) hour period in which the portions of sample are proportionate to the flow and combined to form a representative sample.

(40) **Unpolluted water.** Water to which no constituent has been added, either intentionally or accidentally, which would render such water unacceptable to the State of Tennessee or the Environmental Protection Agency having jurisdiction thereof for disposal to storm or natural drainage, or directly to surface waters.

(41) **User.** Any person, firm, corporation or governmental entity that discharges, causes or permits the discharge of wastewater into a community sewer.

(42) **Waste.** Includes sewage and any and all other waste substances, liquid, solid, gaseous or radioactive, associated with human habitation, or of human or animal origin, or from any producing, manufacturing or processing operation of whatever nature, including such waste placed within containers of whatever nature prior to, and for purposes of, disposal.

(43) **Wastewater.** Waste and water, whether treated or untreated, discharged into or permitted to enter a community sewer.

(44) **Wastewater constituents and characteristics.** The individual chemical,, physical, bacteriological and radiological parameters, including toxicity, volume and flow rate and such other parameters that serve to define, classify or measure the contents, quality, quantity and strength of wastewater.

(45) **Waters of the State of Tennessee.** Any water, surface or underground, within the boundaries of the state.

(c) The following abbreviations shall have the following meanings:

(1) BAT - Best Available Technology.

(2) BPT - Best Practical Technology.

(3) BPJ - Best Professional Judgment.

a) BOD - Biochemical oxygen demand.

b) $BOD_5$ - Biochemical oxygen demand (5 day).

(4) CFR - Code of Federal Regulations.

(5) CWA - Clean Water Act.

(6) CWT - Centralized Waste Treatment Facility.

(7) EPA - Environmental Protection Agency.

(8) GMP - Good Management Practices.

(9) ISS - Interceptor Sewer System.

(10) 1 - Liter.

(11) MBAS - Methylene-blue-active substances.
(12) mg - Milligrams.

(13) mg/l - Milligrams per liter.

(14) NPDES - National Pollutant Discharge Elimination System.

(15) POTW - Publicly owned treatment works.

(16) RCRA - Resource Conservation and Recovery Act.

(17) SIC - Standard Industrial Classification.

(18) SWDA - Solid Waste Disposal Act, 42 U.S.C. 6901, et seq.

(19) TSS - Total Suspended Non-filterable Solids.

(20) USC - United States Code.

(Ord. No. 9409, § 2, 6-5-90)

## DIVISION 2. PRETREATMENT STANDARDS

### Sec. 31-51. Prohibitions and limitations on discharge into the publicly owned treatment works.

(a) *Purpose and policy.* This section establishes limitations and prohibitions on the quantity and quality of wastewater which may be lawfully discharged into the publicly owned treatment works. Pretreatment of some wastewater discharges will be required to achieve the goals established by this article and the Clean Water Act. The specific limitations set forth in Paragraph (i) hereof, and other prohibitions and limitations of this article, are subject to change as necessary to enable the city to provide efficient wastewater treatment, to protect the public health and the environment, and to enable the city to meet requirements contained in its NPDES permit. The superintendent shall review said limitations from time to time to insure that they are sufficient to protect the operation of the treatment works, the health and safety of ISS personnel, to enable the treatment works to comply with its NPDES permit, to provide for a cost effective means of operating the treatment works, and to protect the public health and the environment. The superintendent shall recommend changes or modifications as necessary.

(b) *Prohibited pollutants.* No person shall introduce into the publicly owned treatment works any pollutant(s) which cause pass through or interference. Additionally, the following specific prohibitions apply:

(1) Pollutants which create a fire or explosion hazard in the POTW,, including, but not limited to, pollutants with a closed cup flashpoint of less than 140 degrees Fahrenheit (sixty degrees Centigrade), as determined by a Pensky-Martens Closed Cup Tester, using the test method specified in the American Society for Testing and Materials (ASTM) standard D-93-79 or D-93-80k or a Setaflash Closed Cup Tester, using the test method specified in ASTM Standard D-3278-78 and pollutants which cause an exceedance of 10% of the lower explosive limit (LEL) at any point within the POTW;

(2) Pollutants which cause corrosive structural damage to the POTW, but in no case discharges with a pH lower than 5.0 or higher than 10.5;

(3) Solid or viscous pollutants in amounts which cause obstruction to the flow of the sewers, or other interference with the operation of or which cause injury to the POTW; including waxy or other materials which tend to coat and clog a sewer line or other appurtenances thereto;

(4) Any pollutant, including oxygen demanding pollutants (BOD, etc.), released in a discharge (slug) of such volume or strength as to cause interference in the POTW or individual unit operations or cause adverse effects on its workers or the environment;

(5) Heat in amounts which will inhibit biological activity in the POTW resulting in interference, but in no case heat in such quantities that the temperature at the treatment works influent exceed 40E Centigrade (104E Fahrenheit). Unless a higher temperature is allowed in the user's wastewater discharge permit, no user shall discharge into any sewer line or other appurtenance of the POTW wastewater with a temperature exceeding 63.50E Centigrade (150E Fahrenheit).

(6) Pollutants which result in the presence of toxic gases, vapors, or fumes within the POTW in a quantity that may cause acute worker's health and safety problems.

(7) Any trucked or hauled pollutants, except at discharge points designated by the POTW.

(c) *Affirmative Defenses.* A user shall have an affirmative defense in any action brought against it alleging a violation of the general prohibitions established in paragraph (b) of this section and the specific prohibitions in paragraphs (b)(3), (4) and (5) of this section where the user can demonstrate that:

(1) It did not know or have reason to know that its discharge, alone or in conjunction with a discharge or discharges from other sources, would cause pass through or interference; and

(2) (A) A local limit designed to prevent pass through and/or interference, as the case may be, was developed pursuant to section 31-51(i) and (j) for each pollutant in the user's discharge that caused pass through or interference, and the user was in compliance with each such local limit directly prior to and during the pass through or interference; or

(B) If a local limit designed to prevent pass through and/or interference, as the case may be, has not been developed for the pollutant(s) that caused

the pass through or interference, and the user's discharge directly prior to and during the pass through or interference did not change substantially in nature of constituents from the user's prior discharge activity when the POTW was regularly in compliance with the POTW's NPDES permit requirements and, in the case of interference, applicable requirements for sewage sludge use or disposal.

(d) *Wastewater Constituent Evaluation.* The wastewater of every industrial user shall be evaluated using the following criteria:

(1) Wastewater containing any element or compound which is not adequately removed by the treatment works which is known to be an environmental hazard;

(2) Wastewater causing a pass through, discoloration, foam, floating oil or grease, or any other condition in the quality of the city's treatment works' effluent such that receiving water quality requirements established by law cannot be met;

(3) Wastewater causing conditions at or near the city's treatment works which violate any statute, any rule, or regulation, of any public agency of this state or the United States;

(4) Wastewater containing any element or compound known to act as a lacrimator, known to cause nausea, or known to cause odors constituting a public nuisance;

(5) Wastewater causing interference with the effluent or any other product of the treatment process, residues, sludges, or scums causing them to be unsuitable for reclamation, reuse, causing interference with the reclamation process, or causing them to be unsuitable for disposal;

(6) Wastewater discharged at a point in the collection system that is upstream of any overflow, bypass, or combined sewer overflow and which may thereby cause special environmental problems or specific discharge limitations;

(7) Wastewater having constituents and concentrations in excess of those listed in section 31-51(i), or cause a violation of the limits in section 31-51(j).

(8) The capacity of existing sewer lines to carry the anticipated wastewater flow, particularly with respect to any problems, overflows, or overloads caused by heavy rain infiltration.

(9) The toxicity of each wastewater shall be evaluated by an appropriate biomonitoring technique to determine if a specific discharge may significantly affect the overall toxic level of the POTW influent.

The superintendent or the Board, as applicable, shall establish reasonable limitations or prohibitions or monitoring requirements in addition to the limits established pursuant to section 31-51(e) and (i) in the wastewater discharge permit of any industrial user that discharges wastewater violating any of the above criteria or that has processes that generate wastewater that could violate any of the above criteria prior to pretreatment as shall be reasonably necessary to achieve the purpose and policy of this article.

(e) *National Pretreatment Standards.* Certain industrial users are now or hereafter shall become subject to National Pretreatment Standards promulgated by the Environmental Protection Agency specifying quantities or concentrations of pollutants or pollutant properties which may be discharged into the POTW. All industrial users subject to a National Pretreatment Standard shall comply with all requirements of such standard, and shall also comply with any additional or more stringent limitations contained in this article. Compliance with National Pretreatment Standards for existing sources subject to such standards or for existing sources which hereafter become subject to such standards shall be within three (3) years following promulgation of the standards unless a shorter compliance time is specified in the standard. Compliance with National Pretreatment Standards for new sources shall be required upon promulgation of the standard. New sources shall install and have in operating condition, and shall "start-up" all pollution control equipment required to meet applicable pretreatment standards before beginning to discharge. Within the shortest feasible time (not to exceed 90 days), new sources must meet all applicable pretreatment standards. Except where expressly authorized by an applicable National Pretreatment Standard, no industrial user shall increase the use of process water or in any way attempt to dilute a discharge as a partial or complete substitution for adequate treatment to achieve compliance with such standard.

(f) *Limitation on Radioactive Waste.* No person shall discharge or permit to be discharged any radioactive waste into a community sewer except:

(1) When the person is authorized to use radioactive materials by the Tennessee Department of Health and Environment or the Nuclear Regulatory Commission;

(2) When the waste is discharged in strict conformity with applicable laws and regulations of the aforementioned agencies, or any other agency having jurisdiction; and

(3) When a copy of permits received from said regulatory agencies have been filed with the superintendent.

(g) *Septic Tank Pumping, Hauling, and Discharge.* No person owning vacuum or "cess pool" pump trucks or other liquid waste transport trucks shall discharge directly or indirectly such sewage into the POTW, unless such person shall first have applied for and received a truck discharge operation permit from the superintendent for each vehicle used in this manner. All applicants for a truck discharge operation permit shall complete such forms as required by the superintendent, pay appropriate fees, and agree in writing to abide by the provisions of this chapter and any special conditions or regulations established by the superintendent.

(1) The owners of such vehicles shall affix and display the permit number in four inch (4") block figures on the side of each vehicle used for such purposes.

(2) Such permit shall be valid for a period of one (1) year from date of issuance; provided, that such permit shall be subject to suspension or revocation by the superintendent for violation of any provisions of this code, regulations as established by the superintendent, or any other applicable law or regulations. A revocation or suspension of such a permit shall be for a period of time not to exceed five (5) years. Such revocation or suspension shall bind the permittee, any member of the immediate family of the permittee, or any person who has purchased the business or a substantial amount of the assets of the permittee who paid less than fair market value for such business or assets. Users found operating in violation of a permit issued under this subsection and whose permit is therefore revoked by the superintendent, shall be notified by certified mailing or notice shall personally be delivered to the user.

(3) Truck discharge operation permits are not automatically renewed. Application for renewal must be made to the superintendent.

(4) Such permits shall be limited to the discharge of domestic sewage waste containing no industrial waste. All other hauled wastes shall be governed by paragraph (h) of this section. Any user transporting, collecting, or discharging non-domestic industrial process wastewaters, or a mixture of such wastewaters with domestic wastewater shall obtain a holding tank discharge permit in accordance with paragraph (h).

(5) The superintendent shall designate the locations and times where such trucks may be discharged, and may refuse to accept any truckload of waste in his absolute discretion where it appears that the waste could interfere with the effective operation of the treatment works or any sewer line or appurtenance thereto, or where it appears that a truckload of waste contains industrial process waste or a mixture of domestic sewage and industrial process waste.

(6) The superintendent shall have authority to investigate the source of any hauled waste and to require testing of the waste at the expense of the discharger prior to discharge.

(h) *Other Holding Tank Waste.* No user shall discharge any other holding tank wastes including hauled industrial waste into the POTW unless he shall have applied for and have been issued a 'holding tank discharge permit' by the superintendent. Unless otherwise allowed under the terms and conditions of the permit, a separate permit must be secured for each separate discharge. All applicants for a holding tank discharge permit shall complete such forms as required by the superintendent, pay appropriate fees, and agree in writing to abide by the provisions of this chapter and any special conditions or regulations established by the superintendent. All such dischargers and transporters must show that they have complied with federal manifests and other regulations under RCRA. The permit shall state the specific location of the discharge, the time of day the discharge is to occur, the volume of the discharge, the source and character of such waste, and shall limit the wastewater constituents and characteristics of the discharge. Such user shall pay any applicable charges or fees therefor, and shall comply with the conditions of the permit issued by the superintendent; provided, however, the superintendent may waive in his discretion the completion of an application and for the payment of fees for the requirement for discharge of domestic waste from a recreational vehicle holding tank.

(i) *Limitations on Wastewater Strength (Local Limits).* No user shall discharge wastewater with pollutant concentrations in excess of the concentration set forth in the table below unless: (1) an exception has been granted the user under the provisions of section 31-52; or (2) the wastewater discharge permit of the user provides as a special permit condition a higher interim concentration level in conjunction with a requirement that the user construct a pretreatment facility or institute changes in operation and maintenance procedures to reduce the concentration of pollutants to levels not exceeding the standards set forth in the table within a fixed period of time.

| | *Maximum Concentration mg/l (24 Hour Flow* | *Maximum Instantaneous* |
|---|---|---|

| *Pollutant* | *Proportional Composite Sample)* | *Concentration mg/l (Grab Sample)* |
|---|---|---|
| Cadmium (Cd) | 1.0 | 2.0 |
| Chromium (Cr) | 5.0 | 10.0 |
| Copper (Cu) | 5.0 | 10.0 |
| Cyanide (CN) | 2.0 | 4.0 |
| Lead (Pb) | 1.5 | 3.0 |
| Mercury (Hg) | 0.1 | 0.2 |
| Nickel (Ni) | 5.0 | 10.0 |
| Silver (Ag - free ionic) | 1.0 | 2.0 |
| Zinc (Zn) | 5.0 | 10.0 |
| pH | | 5-10.5 Standard units |

NOTE: All measurements for the above-listed pollutants are in the total form except for silver.

(j) *Criteria to Protect the Treatment Plant Influent.* The superintendent shall monitor the treatment works influent for each pollutant in the following table. Industrial users shall be subject to the reporting and monitoring requirements set forth in section 31-53 and section 31-54 as to these pollutants. In the event that the influent at the treatment works reaches or exceeds the levels established by said table, the superintendent shall initiate technical studies to determine the cause of the influent violation, and shall recommend such remedial measures as are necessary, including but not limited to recommending the establishment of new or revised pretreatment levels for these pollutants. The superintendent shall also recommend changes to any of these criteria in the event the POTW effluent standards are changed, there are changes in any applicable law or regulation affecting same, or when changes are needed for more effective operation of the POTW.

| *Pollutant* | *Monthly Average Maximum Concentration (mg/l)* |
|---|---|
| Copper (Cu) | 0.40 |
| Chromium (Cr) | 0.47 |
| Nickel (Ni) | 0.35 |
| Cadmium (Cd) | 0.01 |
| Lead (Pb) | 0.10 |
| Mercury (Hg) | 0.015 |
| Silver (Ag-free ionic) | 0.036 |

| | | |
|---|---|---|
| Zinc (Zn) | | 0.80 |
| Cyanide (CN) | | 0.05 |
| Toluene | | 0.115 |
| Benzene | | 0.015 |
| 1,1,1-Trichloroethane | | 0.167 |
| Ethylbenzene | | 0.031 |
| Carbon tetrachloride | | 0.015 |
| Chloroform | | 0.193 |
| Tetrachloroethylene | | 0.278 |
| Trichloroethylene | | 0.077 |
| 1,2 Transdichloroethylene | | 0.150 |
| Methylene chloride | | 0.111 |
| Phenols | | 0.555 |
| Naphthalene | | 0.011 |
| Bis (2-ethyl hexyl) phthalate \ | | |
| Butyl benzyl phthalate \ | | |
| Di-n-butyl phthalate / | = | 0.064 |
| Diethyl phthalate / | | |
| Chromium - Hexavalent (Cr+6) | | 0.02 |
| Iron (Fe) | | 6.7 |
| Manganese (Mn) | | 0.33 |
| Total Kjeldahl Nitrogen (TKN) | | 30.0 |
| Oil & Grease | | * |
| MBAS | | * |
| Total Dissolved Solids | | 2,500 |
| BOD | | 207,420 lb/day |
| Suspended Solids | | 213,137 lb/day |
| Ammonia Nitrogen | | 14,000 lb/day |
| Ph | | 6-9 standard units |
| Lower Explosion Limit | | 10% |

NOTE: All measurements for these pollutants are for the total form except as noted.

*No limit established for plant protection, however monitoring will be required to provide numerical correlation with NPDES conditions.

(k) *Pretreatment Requirements.* Industrial users of the POTW shall design, construct, operate, and maintain wastewater pretreatment facilities whenever necessary to reduce or modify the user's wastewater composition to achieve compliance with the limitations in wastewater strength set forth in paragraph (i) of this section, to meet applicable National Pretreatment Standards, to prevent slug discharge or to meet any other wastewater condition or limitation contained in the industrial user's wastewater discharge permit.

(l) *Plans and Specifications.* Plans and specifications for such wastewater pretreatment facilities shall be prepared, signed, dated, and sealed by a registered engineer, and shall be submitted to the superintendent for review in accordance with accepted engineering practices. The superintendent shall review said plans within 45 days and shall recommend to the industrial user any appropriate changes. Prior to beginning construction of said pretreatment facility, the user shall submit a set of construction plans and specifications to be maintained by the superintendent. Prior to beginning construction the industrial user shall also secure such building, plumbing, or other permits that may be required by other parts of this code. The industrial user shall construct said pretreatment facility within the time provided in the industrial user's wastewater discharge permit. Following completion of construction the industrial user shall provide the superintendent with "as built" drawings to be maintained by the superintendent.

(m) *Prevention of Accident Discharges.* All users shall provide such facilities and institute such procedures as are reasonably necessary to prevent or minimize the potential for accidental discharge into the POTW of waste regulated by this article from liquid or raw material storage areas, from truck and rail car loading and unloading areas, from inplant transfer or processing and materials handling areas, and from diked areas or holding ponds of any waste regulated by this article. The wastewater discharge permit of any industrial user who has a history of significant leaks, spills or other accidental discharge of waste regulated by this article shall be subject on a case-by-case basis to a special permit condition or requirement for the construction of facilities or establishment of procedures which will prevent or minimize the potential for such accidental discharge. Plans,, specifications, and operating procedures for such special permit conditions shall be developed by the user and submitted to the superintendent for review under the provisions of paragraph (k) and (1) of this section.

(n) *Oil & Grease Discharge Control Program.* Disposal of "oil" by discharge to the sewer system is not permitted. oils include automotive lubricating oils, transmission and brake fluid, other industrial oils, and vegetable oils used in a restaurant or food processing facility.

The superintendent shall contact all city discharge permit holders, restaurants, auto shops, septic tank pumpers, commercial food processors, oil tank firms and transporters, and

others as appropriate, as often as needed by letter to advise them of requirements for oil and grease discharge control. These dischargers will also be informed of approved alternate oil and grease disposal options available in the Chattanooga vicinity. The above dischargers of oil and grease waste shall be required to provide an equivalent of primary treatment based on gravity separation of visible, and floating oil and grease and oil and grease sludge from wastewater discharges. Such pretreatment processes shall be subject to the good management practices as required by section 31-52 and approval by the superintendent. Discharges shall also be subject to monitoring, entry, inspection, reporting and other requirements as determined by the superintendent at his discretion. These dischargers may be required by the superintendent to apply for industrial waste discharge permits if he determines that they are a source of prohibited pollutants, toxic pollutants in toxic amounts, or are otherwise controlled by federal or state regulations. All dischargers of oil and grease as listed above are subject to all enforcement and penalty provisions of this article.

(o) *Slug Control Program.*

(1) Each user shall provide protection from slug discharges of restricted materials or other substances regulated by this article. A "slug" shall be defined as any pollutants, including oxygen demanding pollutants (BOD) (COD, NH3 etc.) released in a discharge of such volume or strength as to cause interference in the POTW or individual unit operations or cause adverse effects upon its workers or the environment. No user who commences discharge to the sewerage system after July 1, 1990 shall be permitted to introduce pollutants into the system until the need for slug discharge control plans or procedures has been evaluated by the superintendent.

(2) Certain users will be required to prepare Slug Discharge Prevention and Contingency Plans (SDPC) showing facilities and operating procedures to provide this protection. These plans shall be submitted to the superintendent for review and approval. All existing users required to have SDPC Plans shall submit such a plan within three months after notification from the superintendent and complete implementation within six months. Review and approval of such plans and operating procedures shall not relieve the user from the responsibility to modify the user's facility as necessary to meet the requirements of this article.

(3) In the case of a slug discharge, it is the responsibility of the user to immediately by telephone or in person notify the POTW of the incident. The notification shall

include location of discharge, type of waste, concentration and volume, and corrective action.

Within five (5) days following a slug discharge, the user shall submit a detailed written report describing the cause of the discharge and the measures being taken by the user to prevent similar future occurrences. Such notification shall not relieve the user of any expense, loss, damage, or other liability which may be incurred as a result of damage to the sewerage system, fish kills, or any other damage to person or property, nor shall notification relieve the user of any fines, civil penalties, or other liability which may be imposed by the article or other applicable law.

(4) A notice shall be permanently posted on the user's premises advising employees whom to call in the event of a slug discharge. The user shall ensure that all employees who may cause, or allow such slug discharge to occur, are advised of the emergency notification procedure.

(p) *Centralized Waste Treatment Facilities.* The superintendent shall establish effluent limits for centralized waste treatment facilities to insure that the level of pollution discharged from the CWT through the POTW to the environment will not exceed the level that would be allowed if the CWT discharged directly to surface waters under section 301(b)(2) of the Act (33 U.S.C. § 1311). Additionally, centralized waste treatment facilities shall maintain records and submit reports as directed by the superintendent regarding the SIC codes of their customers, and the frequency, characteristics, and volume of wastes from the various categories. (Ord. No. 9409, § 2, 6-5-90)

**Sec. 31-52. Exception to wastewater strength standard.**

(a) *Applicability.* This section provides a method for industrial users subject to the limitation on wastewater strength pollutants listed in section 31-51(i) to apply for and receive a temporary exception to the discharge level for one or more pollutants or parameters.

(b) *Time of Application.* Applicants for a temporary exception shall apply for same at the time they are required to apply for a wastewater discharge permit or renewal thereof. Provided, however, that the superintendent shall allow applications at any time unless the applicant shall have submitted the same or substantially similar application within the preceding year and the same shall have been denied by the board.

(c) *Written Applications.* All applications for an exception shall be in writing, and shall contain sufficient information for evaluation of each of the factors to be considered by the superintendent pursuant to paragraph (d) hereof.

(d) *Review by Superintendent.* All applications for an exception shall be reviewed by the superintendent. If the application does not contain sufficient information for complete evaluation, the superintendent shall notify the applicant of the deficiencies and request additional information. The applicant shall have thirty (30) days following notification by the superintendent to correct such deficiencies. This thirty (30) day period may be extended by the superintendent upon application and for just cause shown. Upon receipt of a complete application the superintendent shall evaluate same within thirty (30) days and shall approve or deny the application based upon the following factors:

(1) The superintendent shall consider whether or not the applicant is subject to a national pretreatment standard containing discharge limitations more stringent than those in section 31-51 and grant an exception only if such exception may be granted within limitations of applicable federal regulations;

(2) The superintendent shall consider whether or not the exception would apply to discharge of a substance classified as a toxic substance under regulations promulgated by the Environmental Protection Agency under the provisions of section 307(a) of the Act (33 U.S.C. 1317), or similar state regulation, and then grant an exception only if such exception may be granted with the limitations of applicable federal or state regulations;

(3) The superintendent shall consider whether or not the granting of an exception would create conditions or be a hazard to city personnel that would reduce the effectiveness of the treatment works taking into consideration the concentration of said pollutant in the treatment works' influent and the design capability of the treatment works;

(4) The superintendent shall consider whether or not the granting of an exception might cause the treatment works to violate the limitations in its NPDES permit;

(5) The superintendent shall consider whether or not the granting of an exception would cause elements or compounds to be present in the sludge of the treatment works which would prevent sludge use or disposal by the city or which would cause the city to violate any regulation promulgated by EPA under the provisions of section 405 of the Act (33 U.S.C. 1345) or similar state regulatory measure;

(6) The superintendent may consider the cost of pretreatment or other types of control techniques which would be necessary for the user to achieve effluent reduction, but prohibitive cost alone shall not be the basis for granting an exception;

(7) The superintendent may consider the age of equipment and industrial facilities involved to the extent that such factors affect the quality or quantity of wastewater discharge;

(8) The superintendent may consider the process employed by the user and process changes available which would affect the quality or quantity of wastewater discharge;

(9) The superintendent may consider the engineering aspects of various types of pretreatment or other control techniques available to the user to improve the quality or quantity of wastewater discharge;

(10) The superintendent may consider an application for exception based upon the fact that water conservation measures instituted by the user or proposed by the user result in a higher concentration of particular pollutants in the wastewater discharge of the user without increasing the amount of mass of pollutants discharged. To be eligible for an exception under this subparagraph, the applicant must show that except for water conservation measures, the applicant's discharge has been or would be in compliance with the limitations on wastewater strength set forth in section 31-51. Provided however, no such exception shall be granted if the increased concentration of pollutants in the applicant's wastewater would have significant adverse impact upon the operation of the POTW.

(e) *Review by Wastewater Regulations and Appeals Board.* The board shall review any appeal from a denial by the superintendent of an application for an exception and shall take into account the same factors considered by the superintendent. At such hearing, the applicant and the superintendent shall have the right to present relevant proof by oral or documentary evidence. The procedure set forth in section 31-295 hereof shall be applicable to such a hearing. The applicant shall bear the burden of proof in such hearing.

(f) *Good Management Practices Required.* The superintendent or the board shall not grant an exception unless the applicant shall demonstrate to the board that he is utilizing "good management practices" (GMP) to prevent or reduce his contribution of pollutants to the POTW.

GMP's include but are not limited to preventative operating and maintenance procedures, schedule of activities, process changes, prohibiting activities, and other management practices to reduce the quality or quantity of effluent discharged and to control plant site runoff, spillage, leaks, and drainage from raw material storage.
(Ord. No. 9409, § 2, 6-5-90)

## DIVISION 3. PERMITS AND ADMINISTRATION

### Sec. 31-53. Wastewater discharge permit; discharge reports; and administration.

(a) *Applicability.* The provisions of this section are applicable to all industrial users of the POTW. The City of Chattanooga has an "Approved POTW Pretreatment Program" as that term is defined in 40 CFR Section 403.3(d), and any permits issued hereunder to industrial users who are subject to or who become subject to a "National Categorical Pretreatment Standard" as that term is defined in 40 CFR 403.3(j) shall be conditioned upon the industrial user also complying with all applicable substantive and procedural requirements promulgated by the Environmental Protection Agency or the State of Tennessee in regard to such "Categorical Standards" unless an exception for the city's program or for specific industrial categories has been authorized.

(b) *Application and Permit Requirements for Industrial Users.* All significant industrial users of the POTW prior to discharging non-domestic waste into the POTW shall apply for and obtain a wastewater discharge permit in the manner hereinafter set forth. Prior to discharge of non-domestic wastewater into the POTW, an industrial user shall request the superintendent to determine if the proposed discharge is significant as defined in section 31-50(b). If the discharge is determined not to be significant, then the superintendent may still establish appropriate discharge conditions for the user. Any noncategorical industrial user designated as significant may petition the superintendent to be deleted from the list of significant industrial users on the grounds that it has no potential for adversely affecting the POTW's operation or violating any pretreatment standard or requirement. All significant industrial users shall obtain an industrial wastewater discharge permit and shall complete such forms as required by the superintendent, pay appropriate fees, and agree to abide by the provisions of this article and any specific conditions or regulations established by the superintendent. All original applications shall be accompanied by a report containing the information specified in subparagraph (c) hereof. All original applications shall also include a site plan, floor plan, mechanical and plumbing plans with sufficient detail to show all sewers and appurtenances in

the user's premises by size, location, and elevation; and the industrial user shall submit to the superintendent revised plans whenever alterations or additions to the user's premises affect said plans.

(c) *Report Requirement.* The report required by paragraph (b) above or other provisions of this article for all significant industrial users shall contain in units and terms appropriate for evaluation the information listed in subparagraphs (1) through (5) below. Industrial users subject to national pretreatment standards shall submit to the superintendent a report which contains the information listed in subparagraphs (1) through (6) below within one hundred and eighty days (180) after the promulgation by the Environmental Protection Agency of a National Pretreatment Standard under Section 307(b) or (c) (33 U.S.C. 1317 (b) or (c)) of the Act. This report is called the "Baseline Monitoring Report" or BMR. Industrial users who are unable to achieve a discharge limit set forth in section 31-51 hereof without improved operation and maintenance procedures or pretreatment shall submit a report which contains the information listed in subparagraph (1) through (7) of this paragraph.

As specified hereinabove, the report shall contain all or applicable portions of the following:

(1) the name and address of the industrial user;

(2) the location of such industrial user;

(3) the nature, average rate of production and standard industrial classification of the operation(s) carried out by such industrial user;

(4) the average and maximum flow of the discharge from such industrial user to the POTW, in gallons per day;

(5) the nature and concentration of pollutants in the discharge from each regulated process from such industrial user and identification of any applicable pretreatment standards and requirements. The concentration shall be reported as a maximum or average level as provided for in the applicable pretreatment standard and as determined by standard methods approved by the superintendent. If an equivalent concentration limit has been calculated in accordance with any pretreatment standard, this adjusted concentration limit shall also be submitted to the superintendent for approval. Whenever pH information is required in the initial report or in regular periodic self-monitoring reports, it shall be collected in the form of a chart from a continuous pH recorder;

(6) a statement, reviewed by an authorized representative of the industrial user (as defined in paragraph (h)(11) below) and certified by a professional engineer indicating whether pretreatment standards are being met on a consistent basis and, if not, whether additional operation and maintenance procedures or additional pretreatment is required for the industrial user to meet the pretreatment standards and requirements; and

(7) if additional pretreatment or operation and maintenance procedure will be required to meet the pretreatment standards, then the report shall contain the shortest schedule by which the industrial user will provide such additional pretreatment. The completion date in this schedule shall not be later than the compliance date established for the applicable pretreatment standard.

For purposes of this paragraph when the context so indicates the phrase "pretreatment standard" shall include either a national pretreatment standard or a pretreatment standard imposed as a result of the industrial user's discharging any incompatible pollutant regulated by section 31-51 hereof. For purposes of this paragraph the term "pollutant" shall include any pollutant identified in a national pretreatment standard or any incompatible pollutant identified in section 31-51 hereof.

(d) *Incomplete Applications.* The superintendent will act only on applications that are accompanied by a report which contains all the information required in paragraph (c) above. Industrial users who have filed incomplete applications will be notified by the superintendent that the application is deficient and the nature of such deficiency and will be given thirty (30) days to correct the deficiency. If the deficiency is not corrected within thirty (30) days or with such extended period as allowed by the superintendent, the superintendent shall deny the application and notify the applicant in writing of such action.

(e) *Evaluation of Application Permit Conditions.* Upon receipt of complete applications, the superintendent shall review and evaluate the applications and shall propose such special permit conditions as he deems advisable. All wastewater discharge permits shall be expressly subject to all the provisions of this article and all other applicable ordinances, laws, and regulations. The superintendent may also propose that the wastewater discharge permit be subject to one or more special conditions in regard to any of the following:

(1) Pretreatment requirements;

(2) The average and maximum wastewater constituents and characteristics;

(3) Limits on rate and time of discharge of requirements for flow regulations and equalization;

(4) Requirements for installation of inspection and sampling facilities;

(5) Specifications for monitoring programs which may include sampling, number, types and standards for tests and reporting schedule;

(6) Requirements for submission of technical reports or discharge reports;

(7) Requirements for maintaining records relating to wastewater discharge;

(8) Mean and maximum mass emission rates, or other appropriate limits when toxic pollutants (as set forth in section 31-51) are proposed or present in the industrial user's wastewater discharge;

(9) Other conditions as deemed appropriate by the superintendent to insure compliance with this article or other applicable ordinance, law or regulation;

(10) A reasonable compliance schedule, as determined by the superintendent up to one year in duration, or such earlier date as may be required by other applicable law or regulation, whichever is sooner, to ensure the industrial user's compliance with pretreatment requirements or improved methods or operation and maintenance;

(11) Requirements for the installation of facilities to prevent and control accidental discharge or "spills" at the user's premises; and

(12) The unit charge or schedule of charges and fees for the wastewater to be discharged to a community sewer.

(f) *Applicant to be Notified of Proposed Permit Conditions; Right to Object.*

(1) Upon completion of his evaluation, the superintendent shall notify the applicant of any special permit conditions which he proposed be included in the wastewater discharge permit;

(2) The applicant shall have forty-five (45) days from and after the date of the superintendent's recommendations for special permit conditions to review same and file written objections with the superintendent in regard to any special permit conditions recommended by the superintendent. The superintendent may, but shall not be required, to schedule a meeting with applicant's authorized representative within fifteen (15) days following receipt of the applicant's objections, and attempt to resolve disputed issues concerning special permit conditions;

(3) If applicant files no objection to special permit conditions proposed by the superintendent, or a subsequent agreement is reached concerning same, the superintendent shall issue a wastewater discharge permit to applicant with such special conditions incorporated therein. otherwise, the superintendent shall submit the disputed matters to the board for resolution as hereinafter provided.

(g) *Board to Establish Permit Conditions; Hearing.*

(1) In the event the superintendent cannot issue a wastewater discharge permit pursuant to paragraph (f) above, the superintendent shall submit to the board his proposed permit conditions and the applicant's written objections thereto at the next regularly scheduled meeting of the board or a specially called meeting;

(2) The board shall schedule a hearing within ninety (90) days following the meeting referred to hereinabove unless such time be extended for just cause shown to resolve any disputed matters relevant to such permit;

(3) The superintendent shall notify the applicant of the date, time, place, and purpose of the hearing scheduled by the board. The applicant and the superintendent shall have the right to participate in such hearing and present any relevant evidence to the board concerning proposed special permit conditions or other matters being considered by the board;

(4) Following such hearing or such additional hearings as shall be deemed necessary and advisable by the board, the board shall establish such special permit conditions as it deems advisable to insure the applicant's compliance with this article or other applicable law or regulation and direct the superintendent to issue a wastewater discharge permit to the applicant accordingly.

(h) *Compliance Schedule and Reporting Requirements.* The following conditions shall apply to the schedules and reports required by paragraphs (c), (e), or (g) of this section:

(1) Schedule components. The schedule shall contain increments of progress in the form of dates for the commencement and completion of major events leading to the construction and operation of additional pretreatment requirements for the industrial user to meet the applicable pretreatment standards (e.g. hiring an engineer, completing the engineering report, completing final plans, executing contracts for major components, commencing construction, completing construction, etc.)

(2) Schedule intervals. No increment referred to in subparagraph (h)(1) shall exceed nine (9) months.

(3) Progress reports. No later than fourteen (14) days following each date in the schedule and the final date for compliance, the industrial user shall submit a progress report to the superintendent including, as a minimum, whether or not it complied with the increment of progress to be met on such date and, if not, the date on which it expects to comply with this increment of progress, the reason for the delay, and steps being taken by the industrial user to return the construction to the schedule established. In no event shall more than nine (9) months elapse between such progress reports to the superintendent.

(4) 90 Day report, new source compliance. Within ninety (90) days following the date for final compliance with applicable pretreatment standards or, in the case of a new source, following commencement of the introduction of wastewater into the POTW, any industrial user subject to pretreatment standards and requirements shall submit to the superintendent a report containing the information described in section 31-53(c)(4)-(6).

(5) Semiannual Reports.

(i) All significant industrial users shall submit to the superintendent during the months of June and December, unless required more frequently in the pretreatment standard or by the superintendent, a report indicating the nature and concentration, of pollutants in the effluent which are limited by their permit. In addition, this report shall include a record of average and maximum daily flows. At the discretion of the superintendent, and in consideration of such factors as local high or low flow rates, holidays,

budget cycles, etc., the superintendent may agree to alter the months during which the above reports are to be submitted.

(ii) The superintendent, as applicable, may impose mass limitations on industrial users which are using dilution to meet applicable pretreatment standards or requirements or in other cases where the imposition of mass limitations are appropriate. In such cases, the report required by subparagraph (i) of this paragraph shall indicate the mass of pollutants regulated by pretreatment standards in the effluent of the industrial user.

(6) Slug Reporting. The industrial user shall notify the POTW immediately by telephone of any slug loading, as defined by section 31-51 (b)(4), by the industrial user.

(7) The reports required in this section shall contain the results of sampling and analysis of the discharge, including the flow and the nature and concentration, or production rates and mass limits where requested by the superintendent, as applicable, of pollutants contained therein which are limited by the applicable pretreatment standards or industrial permit. For industrial users subject to equivalent mass or concentration limits established by the superintendent as alternative standards, the report required by paragraph (h)(5) shall contain a reasonable measure of the user's long term production rate. For all other industrial users subject to categorical pretreatment standards expressed only in terms of allowable pollutant discharge per unit of production (or other measure of operation), the report required by paragraph (h)(5) shall include the user's actual average production rate for the reporting period. The frequency of monitoring shall be prescribed in the applicable treatment standard. All analyses shall be performed in accordance with procedures established by the Environmental Protection Agency under the provisions of section 304(h) of the Act (33 U.S.C. 1314 (h)) and contained in 40 C.F.R. Part 136 and amendments thereto or with any other test procedures approved by the Environmental Protection Agency or the superintendent. Sampling shall be performed in accordance with the techniques approved by the Environmental Protection Agency, or the superintendent.

(8) Notification of the discharge of hazardous wastes.

(i) The industrial user shall notify, as soon as practicable, the POTW, the EPA Regional Waste Management Division Director, and State

hazardous waste authorities of any discharge into the POTW of a substance which is a listed or characteristic waste under section 3001 of RCRA (42 USCA §6921). Such notification must include a description of any such wastes discharged, specifying the volume and concentration of such wastes and the type of discharge (continuous, batch, or other), identifying the hazardous constituents contained in the listed wastes, and estimating the volume of hazardous wastes expected to be discharged during the following twelve months. The notification must take place within 180 days after notification by the superintendent. This requirement shall not apply to pollutants already reported under the self-monitoring requirements of section 31-53.

(ii) Dischargers are exempt from the requirements of this paragraph during a calendar month in which they generate no more than 100 kilograms of hazardous wastes, unless the wastes are acute hazardous wastes as specified in 40 CFR 261.5(e), (f), (g), and (j). Generation of more than one hundred kilograms of hazardous wastes in any given month requires a one-time notification. Subsequent months during which the industrial user generates more than one hundred kilograms of hazardous waste do not require additional notification, except for the acute hazardous wastes specified in 40 261.5(e), (f), (g), and (j).

(iii) In the case of new regulations under section 3001 of RCRA (42 USCA 56921) identifying additional characteristics of hazardous waste or listing any additional substance as a hazardous waste, the industrial user must notify the POTW of the discharge of such substance within 90 days of the effective date of such regulations, except for the exemption in paragraph (ii) of this section.

(iv) In the case of any notification made under this paragraph, the industrial user shall certify that it has a program in place to reduce the volume and toxicity of wastes generated to the degree it has determined to be economically practicable and that it has selected the method of treatment, storage, or disposal currently available which minimizes the present and future threat to human health and the environment.

(9) Notification of Changed Discharge. All industrial users shall promptly notify the POTW in advance of any substantial change in the volume or character of pollutants in their discharge, including the listed or characteristic hazardous

wastes for which the industrial user has submitted initial notification under paragraph (8) above.

(10) Provisions Governing Fraud and False Statements. The reports required to be submitted under this section shall be subject to the provisions of 18 U.S.C. §1001 relating to fraud and false statements and the provisions of sections 309(c)(4) and (6) of the Act (33 USCA §1311), as amended, governing false statements, representation or certifications in reports required under the Act.

(11) Signatory requirements for industrial user reports. The reports required by this section shall include a certification statement as follows:

> I certify under penalty of law that this document and all attachments were prepared under my direction or supervision in accordance with a system designed to assure that qualified personnel properly gather and evaluate the information submitted. Based on my inquiry of the person or persons who manage the system, or those persons directly responsible for gathering the information, the information submitted is, to the best of my knowledge and belief, true, accurate, and complete. I am aware that there are significant penalties for submitting false information, including the possibility of fine and imprisonment for knowing violations.

The reports shall be signed as follows:

(A) By a responsible corporate officer, if the industrial user submitting the reports required by this section is a corporation. For the purpose of this paragraph, a responsible corporate officer means (i) a president, secretary, treasurer, or vice-president of the corporation in charge of a principal business function, or any other person who performs similar policy- or decision-making functions for the corporation, or (ii) the manager of one or more manufacturing, production, or operation facilities employing more than 250 persons or having gross annual sales or expenditures exceeding $25 million (in second-quarter 1980 dollars), if authority to sign documents has been assigned or delegated to the manager in accordance with corporate procedures.

(B) By a general partner or proprietor if the industrial user submitting the reports required by this section is a partnership or sole proprietorship respectively.

(C) By a duly authorized representative of the individual designated in subparagraph (A) of this section if:

i) The authorization is made in writing by the individual described in subparagraph (A);

ii) The authorization specifies either an individual or a position having responsibility for the overall operation of the facility from which the industrial discharge originates, such as the position of plant manager, operator of a well, or well field superintendent, or a position of equivalent responsibility, or having overall responsibility for environmental matters for the company; and

iii) The written authorization is submitted to the superintendent.

(D) If an authorization under subparagraph (C) of this section is no longer accurate because a different individual or position has responsibility for the overall operation of the facility, or overall responsibility for environmental matters for the company, a new authorization satisfying the requirements of subparagraph (C) of this section must be submitted to the superintendent prior to or together with any reports to be signed by an authorized representative.

(12) If sampling performed by an industrial user indicates a violation, the user shall notify the superintendent within 24 hours of becoming aware of the violation. The user shall also repeat the sampling and analysis and submit the results of the repeat analysis to the superintendent within 30 days after becoming aware of the violation, except the industrial user is not required to resample if:

(A) The city performs sampling at the industrial user at a frequency of at least once per month, or

(B) The city performs sampling at the user between the time when the user performs its initial sampling and the time when the user receives the results of this sampling.

(13) If an industrial user subject to the reporting requirement in paragraph (e) of this section monitors any pollutant more frequently than required by the superintendent, using approved procedures prescribed in this section, the results of this monitoring shall be included in the report.

(i) *Bypass.*

(1) Definitions.

(i) "Bypass" means the intentional division of wastestreams from any portion of an industrial user's treatment facility.

(ii) "Severe property damage" means substantial physical damage to property, damage to the treatment facilities which causes them to become inoperable, or substantial and permanent loss of natural resources which can reasonably be expected to occur in the absence of a bypass. Severe property damage does not mean economic loss caused by delays in production.

(2) Bypass not violating applicable Pretreatment Standards or Requirements. An industrial user may allow any bypass to occur which does not cause pretreatment standards or requirements to be violated, but only if it also is for essential maintenance to assure efficient operation. These bypasses are not subject to the provision of paragraphs (3) and (4) of this section.

(3) Notice.

(i) If an industrial user knows in advance of the need for a bypass, if shall submit prior notice to the superintendent, if possible at least ten days before the date of the bypass.

(ii) An industrial user shall submit oral notice of an unanticipated bypass that exceeds applicable pretreatment standards to the superintendent within 24 hours from the time the industrial user becomes aware of the bypass. A written submission shall also be provided within 5 days of the time the industrial user becomes aware of the bypass. The written submission shall contain a description of the bypass and its cause; the duration of the bypass, including exact dates and times, and, if the bypass has not been

corrected, the anticipated time it is expected to continue; and steps taken or planned to reduce, eliminate, and prevent reoccurrence of the bypass. The superintendent may waive the written report on a case-by-case basis if the oral report has been received within 24 hours.

(4) Prohibition of Bypass.

(i) Except as allowed in (2) above, bypass is prohibited, and the superintendent may take enforcement action against an industrial user for a bypass, unless:

a) Bypass was unavoidable to prevent loss of life, personal injury, or severe property damage;

b) There were no feasible alternatives to the bypass, such as the use of auxiliary treatment facilities, retention of untreated wastes, or maintenance during normal periods of equipment downtime. This condition is not satisfied if adequate back-up equipment should have been installed in the exercise of reasonable engineering judgment to prevent a bypass which occurred during normal periods of equipment downtime or preventative maintenance; and

c) The industrial user submitted notices as required under subparagraph (3) of this section.

(ii) The superintendent may approve an anticipated bypass, after considering its adverse effect, if the superintendent determines that it will meet the three conditions listed in subparagraph (4)(i) of this section.

(j) *Maintenance of Records.* Any industrial user subject to the reporting requirements established in this section shall maintain records of all information resulting from any monitoring activities required by this section. Such records shall include for all samples:

(1) The date, exact place, method, and time of sampling and the names of the persons taking the samples;

(2) The dates analyses were performed:

(3) Who performed the analyses;

(4) The analytical techniques/methods; and

(5) The results of such analyses.

(k) *Retention Period.* Any industrial user subject to the reporting requirement established in this section shall be required to retain for a minimum of three (3) years any records of monitoring activities and results (whether or not such monitoring activities are required by this section) and shall make such records available for inspection and copying by the superintendent, Director of the Division of Water Pollution Control Tennessee Department of Health and Environment, or the Environmental Protection Agency. This period of retention shall be extended during the course of any unresolved litigation regarding the industrial user or when requested by the superintendent, the Director, or the Environmental Protection Agency.

(l) *Duration of Permit.* All existing permits for significant industrial users shall be reviewed and reissued with revisions as necessary to comply with new regulatory measures of this article on or before June 30, 1991.

Wastewater discharge permits shall be issued for a period of three (3) years. Provided that permits issued prior to June 30, 1991, may be issued for a period between two (2) and three (3) years for the administrative convenience of the superintendent so as to stagger the renewal dates of the permits. Provided further that permits issued to industrial users granted an exception pursuant to section 31-52 shall be issued for a period of one (1) year. Notwithstanding the foregoing, industrial users becoming subject to a national pretreatment standard shall apply for new permits on the effective date of such national pretreatment standards. The superintendent shall notify in writing any industrial user whom he has cause to believe is subject to a national pretreatment standard of the promulgation of such federal regulations, but any failure of the superintendent in this regard shall not relieve the industrial user of the duty of complying with such national pretreatment standards. An industrial user must apply in writing for a renewal permit within the period of time not more than ninety (90) days and not less than thirty (30) days prior to expiration of the current permit. Provided further that limitations or conditions of a permit are subject to modification or change as such changes may become necessary due to changes in applicable water quality standards, changes in the city's NPDES permit, changes in section 31-51(i), changes in other applicable law or regulation, or for other just cause, industrial users shall be notified of any proposed changes in their permit by the superintendent at least thirty (30) days prior to the effective date of the change. Any change or new condition in a permit shall include a provision for a reasonable time schedule for compliance. The industrial

user may appeal the decision of the superintendent in regard to any changed permit conditions as otherwise provided in this article.

(m) *Transfer of a Permit.* Wastewater discharge permits are issued to a specific industrial user for a specific operation. A wastewater discharge permit shall not be reassigned or transferred or sold to a new owner, new user, or for different premises, or a new or changed operation, unless approved by the superintendent.

(n) *Revocation of Permit.* Any permit issued under the provisions of this article is subject to be modified, suspended, or revoked in whole or in part during its term for cause including but not limited to, the following:

(1) Violation of any terms or conditions of the wastewater discharge permit or other applicable law or regulation;

(2) Obtaining of a permit by misrepresentation or failure to disclose fully all relevant facts; or

(3) A change in any condition that requires either a temporary or permanent reduction or elimination of the permitted discharge.

(4) Refusal of reasonable access to the user's premise for the purpose of inspection or monitoring.

(Ord. No. 9409, § 2, 6-5-90)

**Sec. 31-54. Inspections, monitoring, entry, and confidentiality.**

(a) Whenever required to carry out the objective of this article, including but not limited to (1) developing or assisting in the development of any effluent limitation, or other limitation, prohibition, or effluent standard, pretreatment standard, standard of performance, or permit condition under this article; (2) determining whether any person is in violation of any such effluent limitation, or other limitation, prohibition or effluent standard, pretreatment standard, standard of performance, or permit condition; (3) any requirement established under this section;

(1) The superintendent shall require any industrial user to (a) establish and maintain such record, (b) make such reports, (c) install, use, and maintain such monitoring equipment or methods, including where appropriate, biological monitoring methods, (d) sample such effluents in accordance with such methods, at such

locations, at such intervals, and in such manner as the superintendent shall prescribe, and (e) provide such other information as he may reasonably require; and

(2) The superintendent or his authorized representative, upon presentation of his credentials -

A) shall have a right of entry to, upon, or through any user's premises in which an effluent source is located or in which any records required to be maintained under this subsection are located, and

B) may at reasonable times have access to and copy any records, inspect any monitoring equipment or method required under clause (a)(1), and sample any effluents which the owner or operator of such source is required to sample under such clause.

(b) Any records, reports, or information obtained under this section (1) shall, in the case of effluent data, be related to any applicable effluent limitations, toxic, pretreatment, or permit condition, and (2) shall be available to the public to the extent provided by 40 CFR Part 2.302 except that upon a showing satisfactory to the superintendent by any person that records, reports, or information, or particular part thereof (other than effluent data), to which the superintendent has access under this section, if made public would divulge methods or processes entitled to protection as trade secrets of such person, the superintendent shall consider such record, report, or information, or particular portion thereof confidential in accordance with the purposes of this article, except that such record, report or information may be disclosed to officers, employee, or authorized representatives of the State of Tennessee or the United States concerning with carrying out the provisions of the Clean Water Act or when relevant in any proceeding under this article or other applicable laws.

(c) Specific requirements under the provisions of paragraph (a)(1) of this section shall be established by the superintendent, or the board as applicable, for each industrial user and such requirements shall be included as a condition of the industrial user's wastewater discharge permit. The nature of degree of any requirement under this provision shall depend upon the nature of the user's discharge, the impact of the discharge on the POTW, the volume of water discharged, and the technical feasibility of an economic reasonableness of any such requirement imposed.

(d) The industrial user shall be required to design any necessary facility, and to submit according to the permit compliance schedule, an engineering report, including detailed

design plans and operating procedures to the superintendent for review in accordance with accepted engineering practices. The superintendent shall review said plans and other documents within 45 days and shall recommend to the industrial user any change he deems appropriate.

(e) Upon approval of plans and other documents as specified in paragraph (d), the industrial user shall secure such building, electrical, plumbing or other permits as may be required by this code and proceed to construct any necessary facility and establish such operating procedures as are required within the time provided in the industrial user's wastewater discharge permit.

(f) All significant industrial users shall install a monitoring station of a standard design or designed in a manner satisfactory to the superintendent by June 30, 1991.

(g) In the event any industrial user denies the superintendent or his authorized representative the right of entry, to or upon the user's premises, for purposes of inspection, sampling effluents, inspecting and copying records, or verifying that a user is not discharging industrial wastes and is not subject to section 31-51, or performing such other duties as shall be imposed upon him by this article, the superintendent shall seek a warrant or use such other legal procedures as shall be advisable and reasonably necessary to discharge his duties under this section.

(h) Any industrial user failing or refusing to discharge any duty imposed upon him under the provisions of this section, or who denies the superintendent or his authorized representative the right to enter upon the industrial user's premises for purposes of inspection, sampling effluents, inspecting and copying records, or such other duties as may be imposed upon him by this section, shall be deemed to have violated the conditions of his wastewater discharge permit and such permit shall be subject to modification, suspension, or revocation under the procedures established in this article. A user who does not have an industrial waste discharge permit and denies the superintendent or his authorized representative the right to inspect as described in section 31-9 or 31-54(g) is subject to having the sewer service in question terminated by the superintendent.
(Ord. No. 9409, § 2, 6-5-90)

## Sec. 31-55. Dangerous discharge notification requirements.

(a) *Telephone Notification.* Any person or user causing or suffering any discharge whether accidental or not, which presents or may present an imminent or substantial endangerment to the health and welfare of persons, to the environment, or which is likely to cause interference with the POTW, shall notify the superintendent immediately by telephone. In

the absence of the superintendent, notification shall be given to the city employee then in charge of the treatment works.

(b) *Written Report.* Within five (5) days following such occurrence, the user shall provide the superintendent with a detailed written report describing the cause of the dangerous discharge and measures to be taken by the user to prevent similar future occurrences. Such notification shall not relieve the user of any expense, loss, damage, or other liability which may be incurred as a result of damage to the POTW, fish kills, or any other damage to person or property; nor shall such notification relieve the user of any fines, civil penalties, or other liability which may be imposed by this article or other applicable law.

(c) *Notice to Employees.* A notice shall be permanently posted on the user's bulletin board or other prominent place advising employers whom to call in the event of a dangerous discharge. Employers shall insure that all employees who may cause or suffer such a dangerous discharge to occur are advised of the emergency notification procedure.
(Ord. No. 9409, § 2, 6-5-90)

**Sec. 31-56. Reserved.**

## DIVISION 4. WASTEWATER REGULATIONS BOARD

**Sec. 31-57. Wastewater Regulations and Appeals Board.**

(a) *Established.* There is hereby established a Board of seven (7) members to be known as the "Wastewater Regulations and Appeals Board."

(b) *Composition; Terms; Filling Vacancies.* The seven (7) members of this board shall be appointed by the mayor, subject to the approval of the city council. The mayor shall appoint one (1) member each with the following qualifications: one (1) environmental engineer or environmental scientist, one (1) attorney, one (1) person employed or retired from an industrial or commercial establishment regulated by this article, and one (1) person that is experienced in the science or practice of finance. One (1) member shall be nominated by a regional user located in the State of Georgia and one (1) member nominated by a regional user in the State of Tennessee, but subject to approval by the mayor and confirmation by the city council of Chattanooga. The remaining member shall not have any qualification other than being an adult citizen of the area served by the regional system. The five (5) members of the board appointed before this reconstitution of the board shall continue to serve until their terms expire. The new members of the board and all future members of the board shall be appointed for terms

of four (4) years. All members shall serve until their successor is appointed and all members shall serve at the pleasure of the mayor and the city council. In the event of a vacancy, the mayor shall appoint a member to fill the unexpired term subject to approval by the city council. The board shall organize and select its own chairman, vice chairman, and secretary who shall serve in said offices for terms of one (1) year. The members shall serve without compensation, but shall receive their actual expenses incurred in attending meetings of the board and the performance of any duties as members of the board.

(c) *General Duties of the Board.* In addition to any other duty or responsibility otherwise conferred upon the board by this chapter, the board shall have the duty and power as follows:

(1) To recommend from time to time to the city council that it amend or modify the provisions of this chapter;

(2) To grant exceptions pursuant to the provisions of section 31-52 hereof, and to determine such issues of law and fact as are necessary to perform this duty;

(3) To hold hearings upon appeals from orders or actions of the superintendent as may be provided under any provision of this chapter;

(4) To hold hearings relating to the suspension, revocation, or modification of a wastewater discharge permit and issue appropriate orders relating thereto;

(5) To hold such other hearings as may be required in the administration of this chapter and to make such determinations and issue such orders as may be necessary to effectuate the purposes of this article;

(6) To request assistance from any officer, agent, or employee of the city or the Chattanooga-Hamilton County Regional Planning Commission and to obtain such information or other assistance as the board might need;

(7) The board acting through its chairman shall have the power to issue subpoenas requiring attendance and testimony of witnesses and the production of documentary evidence relevant to any matter properly heard by the board;

(8) The chairman, vice chairman or chairman pro tem shall be authorized to administer oaths to those persons giving testimony before the board;

(9) The board shall hold regular annual meetings and such special meetings as the board may find necessary;

(d) *Quorum.* Five (5) members of the board shall constitute a quorum, but a lesser number may adjourn a meeting from day to day. Any substantive action of the board shall require four (4) votes, but a majority of the quorum may decide any procedural matter.
(Ord. No. 9409, § 2, 6-5-90)

## DIVISION 5. SUPERINTENDENT

### Sec. 31-58. Superintendent.

(a) *Superintendent and Staff.* The superintendent and his staff shall be responsible for the administration of all sections of this chapter. Administratively, he shall be appointed by the mayor.

(b) *Authority of Superintendent.* The superintendent shall have the authority to enforce all sections of this chapter. He shall be responsible and have the authority to maintain and operate the various treatment works, sewer lines, pump stations, and other appurtenances. He shall be responsible for the preparation of operating budgets subject to the normal budgetary processes of the City.

(c) *Records.* The superintendent shall keep in this office or at an appropriate storage facility all applications required under this chapter, a complete record thereof, including a record of all wastewater discharge permits. He shall also maintain the minutes and other records of the Wastewater Regulations and Appeals Board.

(d) *Superintendent to Assist Board.* The superintendent shall attend all meetings of the Wastewater Regulations and Appeals Board, or whenever it is necessary for him to be absent he shall send a designated representative, and shall make such reports to and assist said board in the administration of this article.

(e) *Notice of National Pretreatment Standard.* The superintendent shall notify industrial users identified in 40 CFR 403.8(f)(2) of any applicable pretreatment standards or other applicable requirements promulgated by the Environmental Protection Agency under the provisions of section 204(b) of the Act (33 U.S.C. 1284), section 405 of the Act (33 U.S.C. 1345), or under the provisions of sections 3001 (42 U.S.C. 6921), 3004 (42 U.S.C. 6924) or 4004 (42 U.S.C. 6944) of the Solid Waste Disposal Act. Failure of the superintendent to so notify

industrial users shall not relieve said users from the responsibility of complying with said requirements.

(f) *Public Participation Notice.* The superintendent shall comply with the public participation requirements of 40 CFR Part 25 in the enforcement of National Pretreatment Standards. The superintendent shall at least annually provide public notification, in the largest daily newspaper published in Chattanooga, of a significant industrial user which, during the previous 12 months, were significantly violating applicable Pretreatment Standards or other Pretreatment Requirements. For the purposes of this provision, a significant industrial user is in significant violation if its violations meet one or more of the following criteria:

(1) Chronic violations of wastewater discharge limits, defined here as those in which sixty-six percent (66%) or more of all of the measurements taken during a six-month period exceed (by any magnitude) the daily maximum limit or the average limit for the same pollutant parameter;

(2) Technical review criteria (TRC) violations, defined here as those in which thirty-three percent (33%) or more of all of the measurements taken during a six-month period equal or exceed the product of the daily average maximum limit or the average limit times the applicable TRC [TRC=1.2 for toxic pollutants except pH];

(3) Any other violation of a pretreatment effluent limit (daily maximum or longer-term average) that the superintendent believes has caused, alone or in combination with other discharges, interference or pass through (including endangering the health of POTW personnel or the general public);

(4) Any discharge of a pollutant that has caused imminent endangerment to human health, welfare or to the environment and has resulted in the POTW's exercise of its emergency authority to halt or prevent such a discharge;

(5) Violation, by ninety (90) days or more after the schedule date, of a compliance schedule milestone contained in a permit or enforcement order, for starting construction, completing construction, or attaining final compliance;

(6) Failure to provide required reports such as baseline monitoring reports, 90-day compliance reports, periodic self-monitoring reports, and reports on compliance with compliance schedules within thirty (30) days of the due date;

(7) Failure to accurately report noncompliance; or

(8) Any other violation or group of violations which the superintendent considers to be significant.

(g) *Regulations and Standards Authorized.* The superintendent may promulgate rules, regulations and design criteria not inconsistent with this chapter and have them printed for distribution. These rules may include requirements for performing wastewater characterizations, analysis and other measurements by standard methods approved by the superintendent. Such rules and regulations shall be ratified and adopted by the city council.

(h) *Certification of Wastewater Laboratories.* On and after July 1, 1991, all wastewater monitoring and preparation of reports required in sections 31-53 or 31-54 shall be done by laboratories approved and certified by the superintendent. Laboratories aspiring to be approved for purposes of submitting such monitoring reports shall submit to an inspection by the superintendent or his representative, and to annual reinspections thereafter. Such laboratories shall for a period of one (1) year maintain records of all monitoring activities for users of the city's sewer system containing the information specified in section 31-53. Such laboratories shall agree with and shall utilize the analytical test procedures described in section 31-53 and shall implement and maintain a reasonable quality control-quality assurance program. As a further condition of certification, such laboratories shall agree to and shall participate in a program of blind cross-check analyses with the city's laboratory at no cost to the City of Chattanooga.

(i) *Sewer Credits.* Approves secondary meters and determines other kinds of sewer user charge credits.

(j) *Approves New Construction.* Gives approval in acceptance of newly constructed sanitary sewer lines, pump stations and other appurtenances.
(Ord. No. 9409, § 2, 6-5-90)

## DIVISION 6. PRETREATMENT ENFORCEMENT

### Sec. 31-59. Pretreatment enforcement; procedure; complaints; orders.

(a) *Complaints and Orders.*

(1) Whenever the superintendent has reason to believe that a violation of any provision of the pretreatment program of the city or orders of the Wastewater

Regulations and Appeals Board issued pursuant thereto has occurred, is occurring, or is about to occur, the superintendent may cause a written complaint to be served upon the alleged violator or violators.

(2) The complaint shall specify the provision or provisions of the pretreatment program or order alleged to be violated or about to be violated, the facts alleged to constitute a violation thereof, may order that necessary corrective action be taken within a reasonable time to be prescribed in such order, and shall inform the violators of the opportunity for a hearing before the Wastewater Regulations and Appeals Board.

(3) Any such order shall become final and not subject to review unless the person or persons named therein request by written petition a hearing before the local hearing authority as provided in section 31-60, no later than thirty (30) days after the date such order is served; provided, however, that the Wastewater Regulations and Appeals Board may review such final order on the same grounds upon which a court of the state may review default judgments.

(b) *Emergency Suspensions.*

(1) Whenever the superintendent finds that an emergency exists imperatively requiring immediate action to protect the public health, safety or welfare, the health of animals, fish or aquatic life, a public water supply, or the facilities of the publicly owned treatment works of the pretreatment agency, the superintendent may, without prior notice, issue an order reciting the existence of such an emergency and requiring that such action be taken as the superintendent deems necessary to meet the emergency.

(2) If the violator fails to respond or is unable to respond to the superintendent's order, the superintendent may take such emergency action as he deems necessary, or contract with a qualified person or persons to carry out the emergency measures. The superintendent may assess the person or persons responsible for the emergency condition for actual costs incurred by the superintendent in meeting the emergency.

(c) *Service.* Except as otherwise expressly provided, any notice, complaint, order or other instrument issued by or under authority of this chapter may be served on any person affected thereby personally, by the superintendent or any person designated by him, or such

service may be made in accordance with Tennessee statutes authorizing service of process in civil actions. Proof of service shall be filed in the office of the superintendent.
(Ord. No. 9409, § 2, 6-5-90)

**Sec. 31-60. Pretreatment enforcement; hearings.**

(a) Any hearing or rehearing brought before the Wastewater Regulations and Appeals Board shall be conducted in accordance with the following:

(1) Upon receipt of a written petition from the alleged violator pursuant to this section, the superintendent shall give the petitioner thirty (30) days' written notice of the time and place of the hearing, but in no case shall such hearing be held more than sixty (60) days from the receipt of the written petition, unless the superintendent and the petitioner agree to a postponement;

(2) The hearing herein provided may be conducted by the Wastewater Regulations and Appeals Board at a regular or special meeting. A quorum of the Wastewater Regulations and Appeals Board must be present at the regular or special meeting in order to conduct the hearing herein provided;

(3) A verbatim record of the proceedings of such hearings shall be taken and filed with the Wastewater Regulations and Appeals Board, together with the findings of fact and conclusions of law made pursuant to subdivision (6) of this section. The transcript so recorded shall be made available to the petitioner or any party to a hearing upon payment of a charge set by the superintendent to cover the costs of preparation;

(4) In connection with the hearing, the chairman shall issue subpoenas in response to any reasonable request by any party to the hearing requiring the attendance and testimony of witnesses and the production of evidence relevant to any matter involved in the hearing. In case of contumacy or refusal to obey a notice of hearing or subpoena issued under this section, the chancery court of Hamilton County shall have jurisdiction upon the application of the Wastewater Regulations and Appeals Board or the superintendent to issue an order requiring such person to appear and testify or produce evidence as the case may require and any failure to obey such order of the court may be punished by such court as contempt thereof;

(5) Any member of the Wastewater Regulations and Appeals Board may administer oaths and examine witnesses;

(6) On the basis of the evidence produced at the hearing, the Wastewater Regulations and Appeals Board shall make findings of fact and conclusions of law and enter such decisions and orders as in its opinion will best further the purposes of the pretreatment program and shall give written notice of such decisions and orders to the alleged violator. The order issued under this subsection shall be issued no later than thirty (30) days following the close of the hearing by the person or persons designated by the chairman;

(7) The decision of the Wastewater Regulations and Appeals Board shall become final and binding on all parties unless appealed to the courts as provided in subsection (b); and

(8) Any person to whom an emergency order is directed pursuant to section 31-59 shall comply therewith immediately but on petition to the Wastewater Regulations and Appeals Board shall be afforded a hearing as soon as possible, but in no case shall such hearing be held later than three (3) days from the receipt of such petition by the Wastewater Regulations and Appeals Board.

(b) An appeal may be taken from any final order or other final determination of the superintendent or the City of Chattanooga by any party, including the Wastewater Regulations and Appeals Board, who is or may be adversely affected thereby, to the chancery court pursuant to the common law writ of certiorari set out in T.C.A. §27-8-101, within sixty (60) days from the date such order or determination is made.
(Ord. No. 9409, § 2, 6-5-90)

**Sec. 31-61. Pretreatment enforcement; violations; civil penalty.**

(a) (1) Any person including, but not limited to industrial users, who does any of the following acts or omissions shall be subject to a civil penalty of up to ten thousand dollars ($10,000) per day for each day during which the act or omission continues or occurs:

(i) Violates an effluent standard or limitation imposed by a pretreatment program;

(ii) Violates the terms or conditions of a permit issued pursuant to a pretreatment program;

(iii) Fails to complete a filing requirement of a pretreatment program;

(iv) Fails to allow or perform an entry, inspection, monitoring or reporting requirement of a pretreatment program;

(v) Fails to pay user or cost recovery charges imposed by a pretreatment program; or

(vi) Violates a final determination or order of the Wastewater Regulations and Appeals Board.

(2) Any civil penalty shall be assessed in the following manner:

(i) The superintendent may issue an assessment against any person or industrial user responsible for the violation;

(ii) Any person or industrial user against whom an assessment has been issued may secure a review of such assessment by filing with the superintendent a written petition setting forth the grounds and reasons for his objections and asking for a hearing in the matter involved before the Wastewater Regulations and Appeals Board and if a petition for review of the assessment is not filed within thirty (30) days after the date the assessment is served, the violator shall be deemed to have consented to the assessment and it shall become final;

(iii) Whenever any assessment has become final because of a person's failure to appeal the superintendent's assessment, the superintendent may apply to the appropriate court for a judgment and seek execution of such judgment and the court, in such proceedings, shall treat a failure to appeal such assessment as a confession of judgment in the amount of the assessment;

(iv) In assessing the civil penalty the superintendent may consider the following factors:

a) Whether the civil penalty imposed will be a substantial economic deterrent to the illegal activity;

b) Damages to the city, including compensation for the damage or destruction of the facilities of the publicly owned treatment works, and also including any penalties, costs and attorneys' fees incurred by the city as the result of the illegal activity, as well as the expenses involved in enforcing this section and the costs involved in rectifying any damages;

c) Cause of the discharge or violation;

d) The severity of the discharge and its effect upon the facilities of the publicly owned treatment works and upon the quality and quantity of the receiving waters;

e) Effectiveness of action taken by the violator to cease the violation;

f) The technical and economic reasonableness of reducing or eliminating the discharge; and

g) The economic benefit gained by the violator.

(v) The superintendent may institute proceedings for assessment in the chancery court of the county in which all or part of the pollution or violation occurred, in the name of the City of Chattanooga.

(3) The Wastewater Regulations and Appeals Board may establish by regulation a schedule of the amount of civil penalty which can be assessed by the superintendent for certain specific violations or categories of violations.

(b) Any civil penalty assessed to a violator pursuant to this section may be in addition to any civil penalty assessed by the Commissioner of Health and Environment for violations of T.C.A. §69-3-115(a)(1)(F). Provided, however, the sum of penalties imposed by this section and

by §69-3-115(a) shall not exceed ten thousand dollars ($10,000) per day for each day during which the act or omission continues or occurs.
(Ord. No. 9409, § 2, 6-5-90)

**Sec. 31-62. Pretreatment enforcement; assessment for noncompliance with program permits or orders.**

(a) The superintendent may assess the liability of any polluter or violator for damages to the pretreatment agency resulting from any person's or industrial user's pollution or violation, failure, or neglect in complying with any permits or orders issued pursuant to the provisions of the pretreatment program, T.C.A. §§ 69-3-123, 69-3-124, or 69-3-125, or Sections 31-59, 31-60, or 31-61.

(b) If an appeal from such assessment is not made to the Wastewater Regulations and Appeals Board by the polluter or violator within thirty (30) days of notification of such assessment, he shall be deemed to have consented to such assessment and it shall become final.

(c) Damages may include any expenses incurred in investigating and enforcing the pretreatment program or T.C.A. §§ 69-3-123 - 69-3-129, or Sections 31-61 - 31-65, in removing, correcting, and terminating any pollution, and also compensation for any actual damages caused by the pollution or violation.

(d) Whenever any assessment has become final because of a person's failure to appeal within the time provided, the superintendent may apply to the appropriate court for a judgment, and seek execution on such judgment. The court, in such proceedings, shall treat the failure to appeal such assessment as a confession of judgment in the amount of the assessment.
(Ord. No. 9409, § 2, 6-5-90)

**Sec. 31-63. Pretreatment enforcement; judicial proceedings and relief.**

The superintendent may initiate proceedings in the chancery court of the county in which the activities occurred against any person or industrial user who is alleged to have violated or is about to violate the pretreatment program, T.C.A. §§ 69-3-123 - 69-3-129, Sections 31-61 - 31-65, or orders of the Wastewater Regulations and Appeals Board or the superintendent. In such action, the superintendent may seek, and the court may grant, injunctive relief and any other relief available in law or equity.
(Ord. No. 9409, § 2, 6-5-90)

**Sec. 31-64. Administrative enforcement remedies.**

(a) *Notification of Violation.* Whenever the superintendent finds that any industrial user has violated or is violating this article, or a wastewater permit or order issued hereunder, the superintendent or his agent may serve upon said user written notice of the violation. Within 10 days of the receipt date of this notice, an explanation of the violation and a plan for the satisfactory correction and prevention thereof, to include specific required actions, shall be submitted to the superintendent. Submission of this plan in no way relieves the user of liability for any violations occurring before or after receipt of the notice of violation.

(b) *Consent Orders.* The superintendent is hereby empowered to enter into consent orders, assurances of voluntary compliance, or other similar documents establishing an agreement with the industrial user responsible for the noncompliance. Such orders will include specific action to be taken by the industrial user to correct the noncompliance within a time period also specified by the order. Consent orders shall have the same force and effect as administrative orders issued pursuant to paragraph (d) below.

(c) *Show Cause Hearing.* The superintendent may order any industrial user which causes or contributes to violation of this article or wastewater permit or order issued hereunder, to show cause why a proposed enforcement action should not be taken. Notice shall be served on the user specifying the time and place for the meeting, the proposed enforcement action and the reasons for such action, and a request that the user show cause why this proposed enforcement action should not be taken. The notice of the meeting shall be served personally or by registered or certified mail (return receipt requested) at least 10 days prior to the hearing. Such notice may be served on any principal executive, general partner or corporate officer. Whether or not a duly notified industrial user appears as noticed, immediate enforcement action may be pursued.

(d) *Compliance Order.* When the superintendent finds that an industrial user has violated or continues to violate this article or a permit or order issued thereunder, he may issue an order to the industrial user responsible for the discharge directing that, following a specified time period, sewer service shall be discontinued unless adequate treatment facilities, devices, or other related appurtenances have been installed and are properly operated. orders may also contain such other requirements as might be reasonably necessary and appropriate to address the noncompliance, including the installation of pretreatment technology, additional self-monitoring, and management practices.

(e) *Cease and Desist Orders.* When the superintendent finds that an industrial user has violated or continues to violate this ordinance or any permit or order issued hereunder, the

superintendent may issue an order to cease and desist all such violations and direct those persons in noncompliance to:

(1) Comply forthwith; or

(2) Take such appropriate remedial or preventive action as may be needed to properly address a continuing or threatened violation, including halting operations and terminating the discharge.

(Ord. No. 9409, § 2, 6-5-90)

**Sec. 31-65. Disposition of damage payments and penalties; special fund.**

All damages and/or penalties assessed and collected under the provisions of sections 31-59 through 31-64 shall be placed in a special fund by the city and allocated and appropriated to the sewer system for the administration of its pretreatment program.
(Ord. No. 9409, § 2, 6-5-90)

**Secs. 31-66 -- 31-240. Reserved.**

## ARTICLE IV. DISPOSAL OF EXCRETA

**Sec. 31-241. Definitions.**

For the purposes of this article, the following words and phrases shall have the meanings respectively ascribed to them by this section:

*Cesspool.* An underground cavity without watertight walls, in which human excreta is placed.

*Human excreta.* The bowel and kidney discharges of human beings.

*Sanitary water closet.* Any flush-type toilet which is properly connected to a city sewer or to a septic tank of approved construction.

*Septic tank.* An underground cavity with watertight walls into which the effluent of a sanitary water closet flows, and from which the effluent does not come to the surface of the ground.
(Code 1986, § 31-241)

**Sec. 31-242. Disposal prohibited except in water closets.**

It shall be unlawful for any person to dispose of any human excreta in the city except in a sanitary water closet.
(Code 1986, § 31-242)

**Sec. 31-243. Where water closet required.**

Every residence and building in the city in which human beings reside, are employed or congregated shall have, for the disposal of human excreta, a sanitary water closet.
(Code 1986, § 31-243)

**Sec. 31-244. Liability of property owner.**

It shall be unlawful for any person owning, leasing or renting property in the city to permit the disposal of human excreta on any property owned, leased or rented by such person or his agent, except in a sanitary water closet.
(Code 1986, § 31-244)

**Sec. 31-245. Connection with septic tank required.**

Any building in the city in which toilet facilities are required, which is not located within an area required for connection with a sewer, as provided in section 31-1 of this Code, shall have such toilet facilities connected with a septic tank.
(Code 1986, § 31-245)

**Sec. 31-246. Permit and inspection fees required for septic tank installations.**

No septic tank shall be constructed in the city without a permit having first been obtained from the county health department. An inspection fee of fifteen dollars ($15.00) shall be charged for each septic tank permit issued and for which a receipt shall be given. No permit shall be issued before payment is received therefor. The funds received from the collection of such fees shall be used by the department for the enforcement of the provisions of this article.
(Code 1986, § 31-246)

**Sec. 31-247. Privies declared a nuisance; abatement.**

All privies in the city are declared to be a nuisance, dangerous to the public health, and shall be condemned and abated as provided in article II of chapter 20 of this Code.
(Code 1986, § 31-247)

**Sec. 31-248. Cesspools prohibited.**

No cesspools shall be built or maintained in the city.
(Code 1986, § 31-248)

**Sex. 31-249 -- 31-265. Reserved.**

## ARTICLE V. WATER AND GAS MAINS[6]

**Sec. 31-266. Location; notice of required improvements; variances.**

(a) All water companies shall lay their water mains on streets running east and west in the city on the south side of the center of the street, and on streets running north and south in the city on the west side of the center of the street.

(b) All gas companies shall lay their gas mains on streets running east and west in the city on the north side of the center of the street, and on all streets running north and south in the city on the east side of the center of the street.

(c) When any street is widened, reconstructed, repaved, or otherwise improved, the city engineer may designate the part of the street in which utility facilities shall be placed. The city engineer shall give the utility companies and abutting landowners notice of the improvements and require the utility companies and the abutting landowners to provide for service connections from the mains in the street to the abutting owners' property line.

(d) Nothing in this section shall be deemed to prohibit the Tennessee-American Water Company from installing a water main on the east side of Amnicola Highway from a point beginning at Citico Creek and extending northwardly and eastwardly to its intersection with Riverside Drive in the City of Chattanooga.

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[6] **Cross reference**--Plumbing generally, Ch. 27.

(e) Nothing in this section shall be deemed to prohibit the Chattanooga Gas Company from installing a four (4) inch gas main on the west side of Dorris Street, beginning at Hooker Road and extending a distance of three hundred fifty (350) feet northward along Dorris Street.
(Code 1986, § 31-266)

**Sec. 31-267. Depth.**

All water or gas companies shall lay their mains not less than three (3) feet in depth below the established curb grade.
(Code 1986, § 31-267)

**Sec. 31-268. Location of pipes laid parallel to mains.**

All water mains or gas companies laying pipes alongside of or parallel to water or gas mains previously laid shall lay such pipes on the outside of such mains, between the mains and the center of the street and not less than three (3) feet from such mains.
(Code 1986, § 31-268)

**Sec. 31-269. Service connections.**

All water and gas companies or persons doing the work shall make service pipe connections on the sides of mains and conduct the same to the inside of the curbstone at a depth not less than three (3) feet below the curb grade.
(Code 1986, § 31-269)

**Secs. 31-270 -- 31-285. Reserved.**

## ARTICLE VI. SEWER AGREEMENTS WITH CHATTANOOGA AREA REGIONAL COUNCIL MEMBERS

**Sec. 31-286. Agreements for wheelage and treatment of wastewater discharges authorized.**

The mayor of the city is hereby authorized to execute a contract with individual members of the Chattanooga Area Regional Council of Governments for sewer charges for wheelage and

treatment of wastewater discharged into the city's interceptor sewer system and to execute any and all documents in connection therewith.
(Code 1986, § 31-286)

**Sec. 31-287. Sewer charges for wheelage and treatment of wastewater discharges established.**

For the purpose of providing wheelage and treatment of wastewater discharged into the city's interceptor sewer system by a member of the Chattanooga Area Regional Council of Governments, sewer charges are hereby established which shall be designated "Sewer Charges for Wheelage and Treatment of Wastewater Discharged into the Chattanooga Interceptor Sewer System."
(Code 1986, § 31-287)

**Sec. 31-288. Areas where rates applicable.**

The rates established for sewer charges for wheelage and treatment shall apply only to a municipality or other eligible local governmental unit which has constructed and shall operate and maintain its own complete sewerage collection system including necessary lift stations, trunk and outfall sewers to the point of connection with one (1) or more available city interceptors, outfall or trunk sewers which have ample capacity to handle the expected flows to be discharged into the city's system, and sewage flow meter at each such connection, provided such municipal or other sewerage system has been constructed in accordance with policies and standards of design and construction required by the city.
(Code 1986, § 31-288)

**Sec. 31-289. Methods of calculating sewer charges.**

The sewer charge for wheelage and treatment may be based upon either a "billable blow" method which is based upon the gross quantity of water sold as determined by water company meter readings or a "total flow" method as based upon flow meter readings as either method may be required or allowed according to the applicable contract with the user or applicable law or regulations.
(Code 1986, § 31-289)

**Sec. 31-290. Estimated charges; increased charges.**

In the event a water meter or flow meter is inoperative or is malfunctioning, the engineering management consultant shall estimate, interpolate and/or project in the most equitable manner possible quantities of flow for such connection. Such projection along with

available readings shall be used by the engineering consultant in calculating monthly charges and shall be for certifying such estimates for billing purposes. sewer service charges for residents of the city be the same percentage of increase may be applied to the above rate.
(Code 1986, § 31-290)

**Sec. 31-291. Connection to interceptor sewer system; agreements authorized.**

The mayor is authorized to execute on behalf of the city an agreement with any member of the Chattanooga Area Regional Council of Governments for such member to connect to the city's interceptor sewer system provided the aforementioned provisions are contained in such agreement.
(Code 1986, § 31-291)

**Secs. 31-292 -- 31-294. Reserved.**

## ARTICLE VII. OTHER ENFORCEMENT AND APPEAL PROCEDURES

**Sec. 31-295. Applicability; procedure.**

(a) The Wastewater Regulations and Appeals Board shall schedule adjudicatory hearings to resolve disputed questions of law and fact whenever provided by a provision of this chapter or whenever a due process hearing is constitutionally required, excluding pretreatment enforcement provided for by Sections 31-59 to 31-65.

(b) Any person aggrieved by any order or determination of the superintendent where an appeal is not otherwise provided by this chapter may appeal said order or determination to be reviewed by the board under the provisions of this section. A written notice of appeal shall be filed with the superintendent and with the chairman, and said notice shall set forth with particularity the action or inaction of the superintendent complained of and the relief being sought by the person filing said appeal. A special meeting of the board may be called by the chairman upon the filing of such appeal, and the board may in its discretion suspend the operation of the order or determination of the superintendent appealed from until such time as the board has acted upon the appeal.

(c) The chairman may issue subpoenas requiring the attendance of witnesses or the production of evidence, or both. Upon endorsement by the chairman, they may be served in accordance with Tennessee statutes authorizing service of subpoenas.

(d) The party at such hearing bearing the affirmative burden of proof shall first call witnesses, to be followed by witnesses called by other party. Rebuttal witnesses shall be called in the same order. The chairman shall rule on any evidentiary questions arising during such hearing, and shall make such other rulings as shall be necessary or advisable to facilitate an orderly hearing subject to approval of the board. The board, the superintendent, or his representative, and all parties shall have the right to examine any witness. The board shall not be bound by or limited to rules of evidence applicable to legal proceedings.

(e) The vice-chairman or the chairman pro tem shall possess all the authority delegated to the chairman by this section when acting in his absence or in his stead.

(f) Any person aggrieved by any final order of determination of the board hereunder shall have judicial review by common law writ of certiorari.
(Ord. No. 9409, § 3, 6-5-90)

**Sec. 31-296. Injunctive relief.**

Upon approval of the mayor, the superintendent shall in the name of the city file in circuit or chancery court of the county, or such other courts as may have jurisdiction, a suit seeking the issuance of an injunction, damages or other appropriate relief to enforce the provisions of this chapter or other applicable law or regulation. Suit may be brought to recover any and all damages suffered by the city as a result of any action or inaction of any user or other person who causes or suffers damage to occur to the POTW or for any other expense, loss or damage of any kind or nature suffered by the city.
(Ord. No. 9409, § 3, 6-5-90)

**Secs. 31-297 -- 31-300. Reserved.**

## ARTICLE VIII. STORM WATER MANAGEMENT

### DIVISION 1. GENERALLY

**Sec. 31-301. Purpose.**

(a) It is the purpose of this article to protect, maintain, and enhance the environment of the City of Chattanooga and the short-term and long-term public health, safety, and general welfare of the citizens of Chattanooga by controlling discharges of pollutants to the Chattanooga Storm Water System and to maintain and improve the quality of the community waters into

which the storm water outfalls flow, including without limitation, the lakes, rivers, streams, ponds, wetlands, sinkholes, and groundwater of Chattanooga.

(b) It is further the purpose of this article to enable Chattanooga to comply with the National Pollution Discharge Elimination System permit (NPDES) and applicable regulations (40 CFR §122.26) for storm water discharges.
(Ord. No. 9942, § 1, 8-31-93)

**Sec. 31-302. Definitions.**

For the purpose of this article the following terms, phrases and words and their derivatives, shall have the meaning given herein:

"Accidental Discharge" means a discharge prohibited by this article into the "Community Waters" or to the "Waters of the State" which occurs by chance and without planning or consideration prior to occurrence.

"Best Management Practices" or "BMPs" means schedules of activities, prohibitions of practices, maintenance procedures, and other management practices to prevent or reduce the pollution of stormwater runoff. BMPs also include treatment requirements, operating procedures, and practices to control site runoff, spillage or leaks, sludge or waste disposal, or drainage from raw material storage.

"Clean Water Act" means the Federal Water Pollution Control Act, as amended, codified at 33 U.S.C. §1251 et. seq.

"Commercial" means property devoted in whole or in part to the commerce, that is, the exchange and buying and selling of commodities or services. The term shall include, by way of example but not of limitation, the following businesses: amusement establishments, animal clinics or hospitals, automobile service stations, new or used automobile dealerships, automobile car washes, automobile and vehicular repair shops, banking establishments, beauty and barber shops, bowling alleys, bus terminals and repair shops, camera shops, dental offices or clinics, day care centers, department stores, drug stores, funeral homes, furniture stores, gift shops, grocery stores, hardware stores, hotels, jewelry stores, laboratories, laundries and dry cleaning establishments, liquor stores, medical offices and clinics, motels, movie theaters, office buildings, paint stores or shops, parking lots, produce markets, professional offices, radio stations, repair establishments, retail stores, restaurants and similar establishments serving

prepared food and beverages, rooming houses, shopping centers, stationary stores, television stations and production facilities, and theaters.

"Community Waters" means any and all rivers, streams, creeks, branches, lakes, reservoirs, ponds, drainage systems, springs, wetlands, wells and other bodies of surface or subsurface water, natural or artificial, lying within or forming a part of the boundaries of the City of Chattanooga the waters into which the Chattanooga Storm Water System outfalls flow.

"Erosion and sediment control plan" means a written plan, including drawings or other graphic representations, for the control of soil erosion and sedimentation resulting from a land disturbing activity.

"Impervious" means not allowing the passage of water through the surface of the ground or ground covering or a substantial reduction in the capacity for water to pass through the surface of the ground or ground covering.

"Industrial" means a business engaged in industrial production or service, that is a business characterized by manufacturing or productive enterprise or a related service business. This term shall include, by way of example but not of limitation, the following: apparel and fabric finishers, blast furnace, blueprint and related shops, boiler works, cold storage plants, contractors plants and storage facilities, foundries, furniture and household good manufacturing, forge plants, foundries, greenhouses, junk yards, manufacturing plants, metal fabricating shops, ore reduction facilities, planing mills, rock crushers, rolling mills, saw mills, smelting operations, stockyards, stone mills or quarries, textile production, utility transmission or storage facilities, warehousing, and wholesaling facilities.

"Institutional" means an established organization, especially of a public or eleemosynary character. This term shall include, by way of example but not of limitation, the following: churches, community buildings, colleges, day care facilities, dormitories, drug or alcohol rehabilitation facilities, fire halls, fraternal organizations, golf courses and driving ranges, government buildings, hospitals, libraries, kindergartens or preschools, nursing homes, mortuaries, schools, social agencies, synagogues, parks and playgrounds.

"Manager" means the person designated by the city to supervise the operation of the storm water management system and who is charged with certain duties and responsibilities by this article, or his duly authorized representative.

"Multi-family Residential" means an apartment building or other residential structure built for three or more family units, mobile home parks with three or more units or lots under common ownership, and condominiums of three or more units.

"National Pollution Discharge Elimination System" or "NPDES" permit means a permit issued pursuant to Section 402 of the Act (33 U.S.C. §1342).

"Notice of Intent" (NOI) means a written notice by a discharger to the Commissioner of the Tennessee Department of Environment and Conservation, or his designee, that the person wishes his discharge to be authorized under a general permit authorized by state law or regulation, particularly Rule 1200-4-10-.04 or Rule 1200-4-10-.05, Rules and Regulations of the State of Tennessee.

"Person" means any individual, partnership, copartnership, firm, company, corporation, association, joint stock company, trust, estate, governmental entity or any other legal entity, or their legal representatives, agents or assigns. The masculine gender shall include the feminine, the singular shall include the plural where indicated by the context.

"Pollution Prevention Plans" means a written site specific plan to eliminate or reduce and control the pollution of storm water through designed facilities, sedimentation ponds, natural or constructed wetlands, and best management practices.

"Significant spills" includes, but is not limited to releases of oil or hazardous substances in excess of reportable quantities under section 311 of the Clean Water Act (see 40 CFR 110.10 and CFR 117.21) or section 102 of CERCLA (see 40 CFR 302.4)

"Storm Water" means storm water runoff, snow melt runoff, and surface runoff and drainage.

"Storm Water Management" means the collection, conveyance, storage, treatment and disposal of storm water runoff in a manner to meet the objectives of this article and its terms, including, but not limited to measures that control the increased volume and rate of storm water runoff and water quality impacts caused by manmade changes to the land.

"Storm Water Management Plan" or "SWMP" means the set of drawings and other documents that comprise all of the information and specifications for the programs, drainage systems, structures, BMPs, concepts, and techniques for the control of storm water and which is incorporated as part of the NPDES permit for Chattanooga and as part of this article.

"Toxic Pollutant" means any pollutant or combination of pollutants listed as toxic in 40 CFR Part 401 promulgated by the Administrator of the Environmental Protection Agency under the provisions of 33 U.S.C. §1317.

"Variance" means the modification of the minimum storm water management requirements contained in this article and the Storm Water Management Plan for specific circumstances where strict adherence of the requirements would result in unnecessary hardship and not fulfill the intent of this article.

"Water Quality" means those characteristics of storm water runoff that relate to the physical, chemical, biological, or radiological integrity of water.

"Water Quantity" means those characteristics of storm water runoff that relate to the rate and volume of the storm water runoff.

"Waters of the State of Tennessee" or "Waters of the State" means any water, surface or underground, within the boundaries of the state, which the Department of Environment and Conservation exercises primary control over with respect to storm water permits.
(Ord. No. 9942, § 1, 8-31-93)

**Sec. 31-303. Same - Abbreviations.**

"BMP" means Best Management Practices.

"CFR" means Code of Federal Regulations.

"NOI" means Notice of Intent.

"NPDES" means National Pollutant Discharge Elimination System.

"T.C.A." means Tennessee Code Annotated.

"U.S.C." means United States Code.
(Ord. No. 9942, § 1, 8-31-93)

**Secs. 31-304 -- 31-309. Reserved.**

## DIVISION 2. APPLICATIONS AND PERMITS FOR INDUSTRIAL, COMMERCIAL, INSTITUTIONAL

AND CERTAIN RESIDENTIAL FACILITIES

**Sec. 31-310. Existing facilities required to obtain permit.**

(a) Any existing Industrial, Commercial, Institutional, and multi-family or group residential facilities having an impervious surface greater than three thousand four hundred (3,400) square feet which discharges storm water into community waters and which does not have current NPDES permits issued by the Tennessee Department of Environment and Conservation authorizing a discharge storm water into the waters of the state will be required to develop Pollution Prevention Plans, and apply for a Chattanooga Storm Water Discharge Permit on or before the dates set forth in the following schedule:

(1) Service stations and convenience stores by May 1, 1994;

(2) Vehicular repair and vehicular parts repair shops by May 1, 1994;

(3) Industrial, warehousing, and manufacturing facilities by May 1, 1995;

(4) Commercial uses and institutional uses with six (6) or more parking places north of the Tennessee River by May 1, 1996;

(5) Commercial uses and institutional uses with six (6) or more parking places south of the Tennessee River by May 1, 1997;

(6) Apartments and other multi-family or group residential uses with six (6) or more parking places by May 1, 1998.

(b) These plans will be submitted to the Manager of the Storm Water Management Section for approval or denial. Upon approval, a permit will be issued within six (6) months of the submittal date, which will incorporate any approved Pollution Prevention Plans into the permit. The permit may require the facility to implement structural and non-structural Best Management Practices (BMP) to reduce pollution discharge. If the application is disapproved, the Manager shall notify the applicant of deficiencies and allow ninety (90) days for the application to be revised and re-submitted. If the noted deficiencies are not corrected within ninety (90) days, and the application re-submitted for approval or if after being submitted is disapproved, any discharge of storm water after that date into waters of the community shall be unlawful. Once issued, a permit shall be valid for five (5) years, unless sooner revoked for violations of permit conditions, changes in applicable law, or other good cause.

(c) The application for a Chattanooga Storm Water Discharge Permit for an existing facility shall comply with the following:

(1) A site map of facility showing buildings, parking, drives, materials loading and access areas, type of each impervious surface, ditches, pipes, catch basins, drainage basin limits, area of facility, acreage of off-site water draining onto facility, discharge points to "Waters of the State" or "Community Waters" with name of the water or drainage basin. This map will be a minimum of scale of 1"=100'.

(2) Description of facility, nature of work performed and type of facility.

(3) A narrative description of significant materials (as defined at 40 CFR §122.26, November 16, 1990) that are currently or in the past have been treated, stored or disposed outside; method of on site storage or disposal; materials management practices used to minimize contact of these material with storm water runoff for the past three years and presently; materials loading and access area; the location and a description of existing structural and non-structural control measures to reduce pollutants in storm water runoff; and a description of any treatment the storm water receives;

(4) Cleanup schedule for debris, material storage areas, garbage storage or disposal areas, or other areas that have the potential to pollute stormwater.

(5) Description of plan of instruction to employees of all level in ways to prevent pollution. The plan shall identify periodic dates for such training.

(6) Name of contact person for permit compliance, including job title, address, and phone number.

(7) Maintenance schedule of sweeping or vacuuming of facility to prevent washout of a build-up of emissions laden with hydrocarbons, oxides, salts, metals, worn pavement particulates, hydrocarbons for leaks and spills, trash, debris, garbage, metals, tire particles, brake lining particles and various chemicals from the wear, deterioration, and deposition from vehicles.

(8) Description of other ways the facility plans to implement programs to reduce the discharge of pollutants through stormwater flow. For each area of the facility that generates storm water discharges associated with an activity with a

reasonable potential for containing significant amounts of pollutants, a prediction of the direction of flow, and an estimate of the types of pollutants which are likely to be present in storm water discharges associated with industrial activity.

(9) Each application shall include plans showing the construction of an appropriately sized grit sediment basin and oil skimmer structure for discharge outfalls into "Community Waters" in accordance with detail drawings of these structures are shown in the Stormwater Management Section Best Management Practices Manual. Provided that this requirement may be waived in the discretion of the Manager if similar facilities are available or soon will be available in public rights-of-way or when programs implemented at the facility substantially eliminate grit and oil discharges.

(10) Each application shall include a record of available sampling data describing pollutants in storm water discharges.

(11) Each application shall include a preventive maintenance program that includes regular inspection and maintenance of storm water management devices (e.g. cleaning grit chambers, catch basins) as well as inspecting and testing plant equipment and systems to uncover conditions that could cause breakdowns or failures resulting in discharges of pollutants to surface waters.

(12) Each application shall designate a person to keep record of incidents such as significant spills of toxic pollutants or other discharges which materially affect the storm water, along with other information describing the quality and quantity of storm water discharges. Inspections and maintenance activities shall be documented and recorded.

(Ord. No. 9942, § 1, 8-31-93; Ord. No. 10111, § 2, 9-20-94)

**Sec. 31-311. New facility permits.**

(a) All new "industrial", "commercial", "institutional", and "multi-family residential" facilities, and all new residential subdivisions of ten (10) or more lots shall obtain a Chattanooga Storm Water Discharge Permit prior to construction of the facility. This permit shall be required in addition to any permits required by the State of Tennessee for storm water discharges associated with industrial activity or for storm water discharges associated with construction activity.

(b) The minimum standards for issuance of a new facility permit shall be a pollution prevention plan, and either an approved NPDES permit from the Tennessee Department of Environment and Conservation for storm water discharges associated with construction activity or a land disturbing activity plan. The application for a new facility permit shall include:

(1) If the facilities is to be covered under the Tennessee Department of Environment and Conservation General NPDES Permit for Storm Water Discharges Associated with Industrial Activity, a General NPDES Permit for Storm Water Discharges Associated with Construction Activity, or an individual NPDES permit, the owner or developer shall timely obtain such permits or file the Notice of Intent (NOI) and shall submit copies to the Manager.

(2) The application for a new facility permit shall demonstrate how the owner or developer will insure that post-development off-site discharge rates shall not exceed the pre-development discharge rates.

(3) Unless otherwise specified, off-site discharges for the existing and developed conditions shall be computed using the twenty-five (25) year return frequency, and Soil Conservation Service (SCS Type II) design. The design shall also show an evaluation of the result of the one hundred (100) year return frequency storm.

(4) To reduce the "first flush" pollutant load, facilities shall be designed to capture the design storm in a detention or retention pond and achieve a ninety-six (96) hours drawdown time of the first three quarters(3/4) of an inch of the runoff. A grit trap and oil separator shall be installed upstream of any detention or retention pond.

(5) Detention or retention ponds shall have at least one (1) foot of freeboard above the design storm, provide a paved emergency overflow, and the maximum level in the pond to be one (1) foot below any finished floor level of the facility. Ponds shall also have permanent vehicle access for maintenance purposes. A plan for the routine maintenance of the ponds will be incorporated in the Pollution Prevention Plan.

(6) Constructed wetlands may be used to deal with the "first flush" pollutant load instead of the ninety-six (96) hours drawdown. Grit trap and oil separators are to be installed upstream of the wetland to prevent contamination.

(7) A Pollution Prevention Plan shall be prepared for the facility. This plan shall demonstrate how the facility will collect, control, and treat stormwater so as to

control the quantity and quality of stormwater leaving the site. The plan shall include as necessary structural controls and non-structural Best Management Practices (BMP) adequate to prevent the violation of any water quality standard, and shall meet the provisions of Sections 301 and 402 of the Federal Water Pollution Control Act (BCT and BAT treatment requirements).

(8) All developments installing new detention facilities, retrofitting existing detention facilities or other stormwater management facilities shall be required to execute an Inspection and Maintenance Agreement for Private Stormwater Management Facilities designating the party or parties responsible for maintenance and granting the City the right to inspect said facilities. In cases where the responsible party or parties do not perform required maintenance after being given appropriate notice in writing, the Agreement shall grant authority to the City to perform such maintenance as may be required and bill the responsible party in an amount equal to double the City's cost of maintenance and enforcement.
(Ord. No. 11883, § 1, 9-5-06)

(c) The Pollution Prevention Plan must be approved by the Manager prior to the issuance of a Certificate of Occupancy by the Building Official.
(Ord. No. 9942, § 1, 8-31-93; Ord. No. 10111, § 3, 9-20-9; Ord. No. 11883, § 1, 9-5-06)

**Sec. 31-312. Permit application fees.**

(a) Each application for the issuance of a New Facility Permit under this article shall be accompanied by a minimum non-refundable fee of one hundred dollars ($100.00) plus such additional fees for land disturbing activity or industrial activity as may be required below.

(b) Each application for the issuance of a land disturbing permit under this article shall be accompanied by a nonrefundable permit fee thirty dollars ($30.00) per acre developed or a minimum fee of one hundred dollars ($100.00).

(c) Each application for an existing facility permit required by Section 31-310 shall be accompanied by a fee of one hundred dollars ($100.00).
(Ord. No. 9942, § 1, 8-31-93)

**Secs. 31-313 -- 31-319. Reserved.**

## DIVISION 3. LAND DISTURBING ACTIVITY AND EROSION AND SEDIMENTATION CONTROL

### Sec. 31-320. Land disturbing activity.

All land disturbing activities shall be in compliance with and permitted under this division of this article. If five acres or more are disturbed, an application shall be applied for under the "State of Tennessee's General NPDES Permit for Storm Water Discharges Associated with Construction Activity." If a Tennessee General NPDES Permit is applied for, a copy of the Notice of Intent (NOI) shall be sent to the Manager of the Storm Water Management Section. To seek coverage under the Tennessee Department of Environment and Conservation General Permit the NOI shall be submitted to the following address:

Storm Water Coordinator
Division of Water Pollution Control
150 Ninth Ave. North, 4th floor
Tennessee Dept. of Environment
and Conservation
Nashville, TN 37243-1534

(Ord. No. 9942, § 1, 8-31-93)

### Sec. 31-321. Land disturbing activity regulated.

(a) It shall be unlawful for any person to conduct or permit to be conducted any land disturbing activity upon land owned or controlled by them without a permit issued under this article or, if five acres or more are disturbed, a General Permit for Storm Water Discharges Associated with Construction Activity from the Tennessee Department of Environment and Conservation with a copy provided to the Manager. For purposes of this article the phrase land disturbing activity is defined as follows:

*Land disturbing activity*. Any land change which may result in soil erosion from water and wind and the movement of sediments into community waters or onto lands and roadways within the community, including, but not limited to, clearing, dredging, grading, excavating, transporting and filling of land, except that the term shall not include the following:

(1) "Surface mining" as the same is defined in Tennessee Code Annotated Section 59-8-202;

(2) Such minor land disturbing activities as home gardens and individual home landscaping, home repairs, home maintenance work, and other related activities which result in minor soil erosion;

(3) The construction of single-family residences when built separately on lots within subdivisions which have been approved and recorded in the office of the Hamilton County Register, and when applicable for subdivisions of ten or more lots have been issued a permit under this article; provided that excavation is limited to trenches for the foundation, basements, service and sewer connections, and minor grading for driveways, yard areas and sidewalks;

(4) Individual service and sewer connections for single- or two-family residences;

(5) Agricultural practices involving the establishment, cultivation or harvesting of products of the field or orchard, preparing and planting of pasture land, farm ponds, dairy operations, and livestock and poultry management practices, and the construction of farm buildings; (Ord. No. 11470, §1, 10-14-03)

(6) Any project carried out under the technical supervision of the Soil Conservation Service of the United States Department of Agriculture;

(7) Construction, installation or maintenance of electrical, telephone and cable television lines and poles;

(8) Installation, maintenance and repair of any underground public utility lines when such activity occurs on an existing hard-surface road, street or sidewalk, provided the activity is confined to the area of the road, street or sidewalk which is hard-surfaced and a street, curb, gutter or sidewalk permit has been obtained;

(9) Construction, repair or rebuilding of tracks or other related facilities of a railroad company;

These activities may be undertaken without a permit; however, the persons conducting these excluded activities shall remain responsible for otherwise conducting those activities in accordance with the provisions of this article and other applicable law including responsibility for controlling sedimentation and runoff.

(b) *Best Management Practices for Land Disturbing Activities*. The minimum standards for controlling erosion and sedimentation from land disturbing activities shall be set forth in the "Best Management Practices Manual," as adopted and amended from time to time by resolution approved by the City Council. The "General Criteria" handbook adopted by reference by Ordinance No. 8959, adopted June 21, 1988, shall be renamed "Best Management Practices Manual, and a copy of same shall be maintained on file in the offices of the Manager, the City Engineer, and the City Finance Officer.
(Ord. No. 9942, § 1, 8-31-93; Ord. No. 11470, §1. 10-14-03; Ord. No. 11639, § 2, 11-09-04)

**Sec. 31-322. Land disturbing permit required.**

No land disturbing activity, whether temporary or permanent, shall be conducted within the City of Chattanooga until either a land disturbing permit shall have been issued by the Manager allowing such activity pursuant to the provisions of this article or pursuant to a General NPDES Permit for Storm Water Discharges Associated with Construction Activity issued by the Department of Environment and Conservation. Such permit shall be available for inspection by the Manager or Manager's representative on the job site at all times during which land disturbing activities are in progress. Such permit shall be required in addition to any building permit or other permit required upon the site.
(Ord. No. 9942, § 1, 8-31-93)

**Sec. 31-323. Data required in land disturbing permit application.**

(a) Any application for the issuance of a land disturbing permit under this article shall include the following:

(1) Name of applicant;

(2) Business or residence address of applicant;

(3) Name and address of owner of subject property;

(4) Address and legal description of subject property;

(5) Name and address of the contractor and any subcontractor(s) who shall perform the land disturbing activity and who shall implement the erosion and sediment control plan;

(6) A statement setting forth the nature, extent and purpose of the land disturbing activity including the size of the area for which the permit shall be applicable and a schedule for the starting and completion dates of the land disturbing activity.

(b) Each application for a land disturbing permit shall be accompanied by a map or plat of the premises showing the present contour lines and the proposed contour lines resulting from the land disturbing activity in relation to all parts of the premises and the properties immediately adjacent thereto and in relation to all abutting street grades and elevations; such map or plat shall show all existing drainage facilities and the proposed permanent disposition of surface waters upon completion of the land disturbing activity.

(c) Each application for a land disturbing permit shall be accompanied by an erosion and sediment control plan which shall accurately describe the potential for soil erosion and sedimentation problems resulting from the land disturbing activity and shall explain and illustrate the measures which are to be taken to control these problems. The length and complexity of the plan is to be commensurate with the size of the project, severity of the site condition, and potential for off-site damage; the plan shall contain a description of the existing site conditions, a description of adjacent topographical features, a description of soil types and characteristics in the area, potential problems of soil erosion and sedimentation, stabilization specifications, storm water management considerations, a time schedule for completion of the land disturbing activity and for maintenance after completion of the project, clearing and grading limits, and all other information needed to accurately depict solutions to potential soil erosion and sedimentation problems. Any erosion and sediment control plan shall meet the Best Management Practices Manual and shall be approved by the Manager prior to the issuance of the land disturbing permit. The land disturbing permit shall be issued promptly upon approval of the plan.

(d) At any time the Manager determines that an erosion and sediment control plan does not comply with the provisions of this article, he shall notify the applicant in writing of all deficiencies within said plan.
(Ord. No. 9942, § 1, 8-31-93)

**Sec. 31-324. General requirements.**

No land disturbing activity shall be conducted within the city except in such manner that:

(a) Stripping of vegetation, regrading and other development activities shall be conducted so as to minimize erosion. Clearing and grubbing must be held to the minimum necessary for grading and equipment operation. Pre-construction vegetative ground cover shall

not be destroyed, removed or disturbed more than twenty (20) calendar days prior to grading or earth moving. Construction must be sequenced to minimize the exposure time of cleared surface area.

(b) Property owners shall be responsible upon completion of land disturbing activities to leave slopes so that they will not erode. Such methods could include revegetation, mulching, rip-rapping, or gunniting. Regardless of the method used, the objective will be to leave the site as erosion-free and maintenance-free as practicable.

(c) Whenever feasible, natural vegetation shall be retained, protected and supplemented.

(d) Permanent or temporary soil stabilization must be applied to disturbed areas to the extent feasible within seven days on areas that will remained unfinished for more than thirty (30) calendar days. Permanent soil stabilization with perennial vegetation shall be applied as soon as practicable after final grading is reached on any portion of the site. Soil stabilization refers to measures which protect soil from the erosive forces of wind, raindrop impact and flowing water, and includes the growing of grass, sod, application of straw, mulch, fabric mats, and the early application of gravel base on areas to be paved.

(e) A permanent vegetative cover shall be established on disturbed areas not otherwise permanently stabilized.

(f) To the extent necessary, sediment in runoff water must be trapped by the use of debris basins, sediment basins, silt traps or similar measures until the disturbed area is stabilized.

(g) Neighboring persons and property shall be protected from damage or loss resulting from excessive storm water runoff, soil erosion or deposition upon private property or public streets of water transported silt and debris. Adjacent property owners shall be protected from land devaluation due to exposed bare banks.

(h) Erosion and sediment control measures must be in place and functional before earth moving operations begin, and must be constructed and maintained throughout the construction period. Temporary measures may be removed at the beginning of the work day, but must be replaced at the end of the work day.

(i) Structural controls shall be designed and maintained as required to prevent pollution. All surface water flowing toward the construction area shall to the extent practicable be diverted by using berms, channels, or sediment traps as necessary. Erosion and sediment

control measures shall be designed according to the size and slope of disturbed or drainage areas, to detain runoff and trap sediment. Discharges from sediment basins and traps must be through a pipe or lined channel so that the discharge does not cause erosion. Muddy water to be pumped from excavation and work areas must be held in settling basins or treated by filtration prior to its discharge into surface waters where practicable. Waters must be discharged through a pipe or lined channel so that the discharge does not cause erosion and sedimentation.

(j) All control measures shall be checked, and repaired as necessary, weekly in dry periods and within 24 hours after any rainfall of 0.5 inches with a 24 hour period. During prolonged rainfall, daily checking and repairing is necessary. The permittee shall maintain record of such checks and repairs.

(k) A specific individual shall be designated to be responsible for erosion and sediment controls on each site.

(l) There shall be no distinctly visible floating scum, oil or other matter contained in the storm water discharge. The storm water discharge must not cause an objectionable color contrast in the receiving water. The storm water discharge must result in no materials in concentrations sufficient to be hazardous or otherwise detrimental to humans, livestock, wildlife, plant life, or fish and aquatic life in the receiving stream.

(m) When the land disturbing activity is finished and stable perennial vegetation has been established on all remaining exposed soil, the developer shall notify the Manager of these facts and request termination of the permit issued under this section. The Manager shall then inspect the site within twenty (20) days after receipt of such notice, and when advisable may require additional measures to stabilize the soil and prevent erosion. If such requirements are given by letter, the owner or developer shall continue to be covered by this provisions of this section, until a request for termination of the permit has been accepted by the Manager.
(Ord. No. 9942, § 1, 8-31-93)

## Sec. 31-325. Landfilling requirements in certain residential areas.

(a) It shall be unlawful for any person to fill any unimproved land in any property which is within one hundred (100) feet of any R-1 Residential Zone, RT-1 Residential Townhouse Zone, RZ-1 Zero Lot Line Residential Zone, R-T/Z Residential Townhouse/Zero Lot Line Zone or R-2 Residential Zone or which is itself zoned in one of these categories without first obtaining a land disturbing activity permit, which shall be subject to the following additional restrictions:

(1) Fill material must be comprised only of suitable dirt, bricks, concrete without exposed rebars, stones or other similar inert materials;

(2) Maximum height of fill shall be two (2) feet above adjacent roads or two (2) feet above the one hundred (100) year flood elevation, whichever is higher;

(3) Fill must not interfere with the free drainage of adjoining properties;

(4) Except where existing stormwater conveyances are adequate for any increase in drainage, appropriately sized on-site retention facilities shall be provided;

(5) Filling of the property must be completed, including capping the fill with stable perennial vegetation, within one (1) year of permit issue date, at which time the permit shall become null and void; and

(6) A second land disturbing activity permit may be issued only in conjunction with building on the property but only after ninety (90) days from the termination or completion of the preceding land disturbing permit on the same property.

(b) Each application for permit, with the required fee therefor, shall be filed with the Stormwater Manager and in addition to the requirements of Section 31-321, shall contain the following information:

(1) Written approval of the request for a permit from the owner of the property;

(2) The character and description of the fill materials to be deposited;

(3) The rate at which the fill materials are expected to be deposited on a weekly or monthly basis;

(4) Equipment to be used; and

(5) The date upon which the applicant desires the permit to be issued.

(c) The Stormwater Manager may impose conditions upon the issuance of a permit which are reasonably calculated to eliminate excessive noise, scattering of dust or dirt, scattering of materials, to prevent nuisances and to prevent obstruction of public streets or interference with traffic.

(d) An additional twenty-five dollar ($25.00) fee shall be charged for any application for a permit to fill property.

(e) Where any filling work for which a permit is required is started prior to obtaining said permit, the fee herein specified shall be doubled but the payment of such double fee shall not relieve any person from fully complying with the requirements of this Code in the execution of the work nor from any other penalties prescribed herein.

(f) Any person filling property at the time of the enactment of this provision shall obtain a permit within sixty (60) days and shall to the extent practical comply with all provisions in this section.
(Ord. No. 10708, § 1, 6-2-98)

**Sec. 31-325.1. Timber Removal Requirements - Applicability.**

These Timber Removal Requirements apply to the removal of timber from a site which:

(a) will not be developed within the subsequent three (3) years after such timber removal; and

(b) is one (1) acre in size or larger and five thousand (5,000) square feet or more of the tree canopy is going to be harvested, cut, or removed within a 1 (one) year period; or

(c) is having timber harvested, cut, or removed for the purpose of conducting Forestry Land Management Practices.

These Timber Removal requirements are not to be construed as eliminating other permit requirements in this Chapter for land which is to be developed within three (3) years following such timber removal.

**Sec. 31-325.2. Timber Removal Requirements - Exemptions.**

(a) Special exceptions may be granted if undue hardship can be proven.

(b) Such application for exception shall be made to the Municipal Forester and shall show:

(1) the special conditions peculiar to the property that would cause the undue

hardship;

(2) how enforcement of these rules will deprive the landowner of rights commonly enjoyed by others in similar areas;

(3) that the granting of the modification will not confer on the landowner a special privilege that would be denied to other applicants;

(4) that the modification request is not based on conditions or circumstances that are the result of actions by the applicant;

(5) that the request does not arise from a condition relating to land or building use, either permitted or legally nonconforming, on a neighboring property; and

(6) that the granting of a modification will not adversely affect water quality.

**Sec. 31-325.3 Removal - Definitions.**

*DBH (Diameter at Breast Height)* – shall mean the total cross sectional diameter in inches of a tree measured at a height of four and one-half (4 1/2) feet above ground level.

*Forestry Land Management Practices* - shall mean the practice of controlling forest establishment, composition and growth, as set forth by the Tennessee Department of Agriculture's Division of Forestry's, "Forestry Best Management Practices".

*Municipal Forester* - means an employee of the City of Chattanooga who manages the City's Urban Forestry Program.

*Re-Vegetation Management Plan* - shall mean a site plan drawn to scale that shows in graphic and text form all the necessary re-planting and / or re-growth requirements.

*Slash* - shall mean unutilized wood debris.

*Steep Slope* - shall mean any parcel or group of contiguous parcels with 1 acre or more of a minimum 30% slope.

*Timber* - means a tree of a size greater than a four-inch (4") diameter at a height of five

(5) feet from ground level.

*Tree Canopy* - shall mean the effective radial circumference area of a mature tree's vegetative cover, including all branches and leaves. The canopy can be conveyed in values of percentage area of total land space being assessed or by numerical measurement.

*Timber Removal* - means the cutting of timber and / or removal of forest products including logs, pulpwood, or chips.

*Tree Protection Area (TPA)* - shall mean the area set aside for the express purpose of removing no trees.

*Tree Removal Area* - shall mean the location indicated on a site plan and physically marked on the ground designating an area set aside for the express purpose of removing trees.

*Watercourse* - shall mean any natural or artificial stream, river, creek, ditch, channel, canal, conduit, culvert, drain, waterway, gully, ravine, or wash in which water flows in a definite direction or course, either continuously or intermittently, and has a definite channel, bed, and banks and includes any area adjacent thereto subject to inundation by reason of overflow or floodwater.

**Sec. 31-325.4. Permit**.

(a) For applicable sites pursuant to Section 31-325.1, a Timber Removal Permit is required prior to any timber removal.

(b) The Timber Removal Permit is effective for 180 days for the cutting, removal or harvesting of timber and the permit is effective for an additional for 12 months for the exclusive purpose of re-vegetation. If the timber removal activity is not completed during the 180 days, a new Timber Removal Permit must be applied for. One permit extension of up to ninety (90) days may be granted at the discretion of the Municipal Forester.

(c) Each application for the issuance of a timber removal permit under this article shall be accompanied by a non-refundable permit fee of thirty dollars ($30.00) per acre affected or a minimum fee of fifty dollars ($50.00).

(d) The Timber Removal Permit Application will include information which includes, but is not limited to:

(1) Applicant’s name, address and contact information.

(2) Names and addresses of the owner of the subject parcel and the contractor/ subcontractors who shall perform the timber removal activity.

(3) Address and location of subject parcel.

(4) A statement setting forth the nature, extent and purpose of the timber removal activity, including the size of the area for which the permit shall be applicable and a schedule for the starting and completion of the timber removal activity.

(5) Type of removal method to be used (i.e. clear-cut, shelterwood, selective cut)

(6) The proposed method of disposal of all slash/ unutilized wood debris, which will provide for either chipping or burning (provided such burning is approved by the Air Pollution Control Board).

(7) Ingress and egress locations.

(8) Additional information as may be required by the Inspection Department or the Municipal Forester.

(e) The Re-vegetation Management Plan, as defined in Sec. 31-325.5, must be submitted and approved before a Timber Removal Permit and a Timber Removal Notice Sign is issued.

(f) A Timber Removal Notice Sign must be posted 21 days prior to tree removal activity.

(g) No development that would require approval, such as the issuance of a land disturbance permit, a building permit, or re-zoning of the subject parcel shall be permitted for a period of three (3) years following the issuance of a Timber Removal Permit. The three year period shall begin to run at the time the permitted timber removal is completed.

(h) All required permits must be in place before harvesting or tree removal begins.

**Sec. 31-325.5**. **Re-Vegetation Plan.**

(a) The Re-Vegetation Management Plan shall identify and demonstrate the following:

(1) The location of the mandated undisturbed buffer around the perimeter and any other tree protection areas, including types of existing vegetation and trees.
(2) Location of tree removal areas.

(3) Location of re-vegetation areas and types of trees/ vegetation to be planted. Re-vegetation with trees is to have a density of 8' x 10' for pine and a density of 10' x 10' for white pine, other softwoods and all hardwoods.

(4) The method to be used to regenerate the timber removal area.

(5) That a fifty-foot undisturbed buffer shall be provided and maintained along the entire perimeter of the property, including road frontages, during and after the timber removal activities, except for authorized access crossings.

Notwithstanding the other provisions of this section, no property owner shall be required to preserve an undisturbed buffer that covers more than thirty (30) percent of the total land area of the property. In any such case, an alternative buffer width shall be provided, as determined by the municipal forester.

(6) Contours of the land in 10 foot increments.

(7) Location of watercourses.

(8) Additional information as may be required by the Inspection Department or the Municipal Forester.

(b) Required re-vegetation of the permitted site must be completed within 12 (twelve) months of the timber removal.

**Sec. 31-325.6. Provisions.**

(a) The Forestry Best Management Practices as established by the Tennessee Division of Forestry must be utilized.

(b) The use of a Master Logger is strongly encouraged.

(c) At completion of the required re-vegetation, a final inspection must be requested.

**Sec. 31-325.7. Bond.**

No person shall be issued a permit for or engage in timber removal as set out in this chapter without first posting a surety bond not to exceed $100 per acre of land to be cut/ cleared.

Upon the satisfactory final inspection at the completion of the required re-vegetation, the amount of surety posted shall be returned/released.

**Sec. 31-325.8. Violations.**

If the Municipal Forester or the Inspection Department determines that violations of these requirements have occurred, the Timber Removal Permit may be revoked and/ or citations issued as otherwise authorized by City Code. Each day a violation continues is a separate violation.

**Sec. 31-325.9. Conflict.**

Where the standards and management requirements of this ordinance are in conflict with other City, State or Federal laws, regulations, and policies regarding streams, steep slopes, erodible soils, wetlands, floodplains, timber removal, or other environmental protective measures, the more restrictive shall apply.

## DIVISION 4. GENERAL REQUIREMENTS APPLICABLE TO ALL PERMITS ISSUED UNDER THIS ARTICLE

**Sec. 31-326. Maintenance and submittal of records.**

Appropriate proof and records of compliance with the provisions of the Chattanooga Storm Water Discharge Permit or Land Disturbing Permit will be maintained in the office of the designated contact person and be made available for review at any time by the Manager. A copy of the records of compliance will be sent yearly on the anniversary date of the permit to the Manager.
(Ord. No. 9942, § 1, 8-31-93)

## Sec. 31-327. Transfer of permit.

A Chattanooga Storm Water Discharge Permit or Land Disturbing Permit may be transferred only upon the filing of an amendment to the permit application or an amended or restated application containing all changes from the original application providing there are no changes in the operation of the facility which may affect the quantity or quality of the storm water runoff. If there are to be any changes in the operation of he facility which may effect the quantity or quality of storm water runoff, then the new owner or operator shall re-apply for a Chattanooga Storm Water Discharge Permit or Land Disturbing Permit prior to the beginning of operation of the facility. The filing of an amended or restated application shall be treated as an interim permit allowing the continued operation of the facility pending review of the application by the Manager, which shall remain in force until the application shall be approved or denied by the Manager.
(Ord. No. 9942, § 1, 8-31-93)

## Sec. 31-328. Signatory requirements.

(a) All applications and reports required by this article to be submitted to the Manager shall be signed as follows:

(1) Corporation: a president, secretary, treasurer, or vice-president of the corporation in charge of a principal business function, or any other person who performs similar policy-or decision-making functions for the corporation.

(2) Partnership or sole proprietorship: by a general partner or the proprietor.

(3) Municipality, State, Federal, or other public facility: by either a principal executive officer or the chief executive officer of the agency, or a senior executive officer having responsibility for the overall operations of a principal geographic unit of the agency.

(b) Any person signing any document above shall make the following certification: "I certify under the penalty of law that I have personally examined and am familiar with the information submitted in the attached document; and based on my inquiry of those individuals immediately responsible for obtaining the information. I believe the submitted information is true, accurate, and complete. I am aware that there are significant penalties for submitting false information, including the possibility of fine and civil penalty."
(Ord. No. 9942, § 1, 8-31-93)

**Sec. 31-329. Reserved.**

## DIVISION 5. MONITORING AND INSPECTION

**Sec. 31-330. Monitoring.**

The Manager shall periodically monitor the quantity of, and the concentration of pollutants in storm water discharges from the areas and locations designated in the Chattanooga Storm Water Management Plan.
(Ord. No. 9942, § 1, 8-31-93)

**Sec. 31-331. Detection of illicit connections and improper disposal.**

(a) The Manager shall take appropriate steps to detect and eliminate illicit connections to the Chattanooga Storm Water System, including the adoption of a program to screen illicit discharges and identify their source or sources.

(b) The Manager shall take appropriate steps to detect and eliminate improper discharges, including programs to screen for improper disposal and programs to provide for public education, public information, and other appropriate activities to facilitate the proper management and disposal of used oil, toxic materials and household hazardous waste.
(Ord. No. 9942, § 1, 8-31-93)

**Sec. 31-332. Inspections.**

(a) The Manager or his designee, bearing proper credentials and identification, may enter and inspect all properties for regular periodic inspections, investigations, monitoring, observation, measurement, enforcement, sampling and testing, to effectuate the provisions of this article and the storm water management program. The Manager or his designee shall duly notify the owner of said property or the representative on site and the inspection shall be conducted at reasonable times.

(b) Upon refusal by any property owner to permit an inspector to enter or continue an inspection, the inspector shall terminate the inspection or confine the inspection to areas concerning which no objection is raised. The inspector shall immediately report the refusal and the grounds to the Manager. The Manager may seek appropriate compulsory process.

(c) In the event the Manager or his designee reasonably believes that discharges from the property into the Chattanooga Storm Water System may cause an imminent and substantial threat to human health or the environment, the inspection may take place at any time and without notice to the owner of the property or a representative on site. The inspector shall present proper credentials upon reasonable request by the owner or representative.

(d) At any time during the conduct of an inspection or at such other times as the Manager or his designee may request information from an owner or representative, the owner or representative may identify areas of its facility or establishment, material or processes which contains or which might reveal a trade secret. If the Manager or his designee has no clear and convincing reason to question such identification, the inspection report shall note that trade secret information has been omitted. To the extent practicable, the Manager shall protect all information which is designated as a trade secret by the owner or their representative.
(Ord. No. 9942, § 1, 8-31-93)

**Secs. 31-333 -- 31-339. Reserved.**

## DIVISION 6. ENFORCEMENT AND ABATEMENT

### Sec. 31-340. Unauthorized discharge a public nuisance.

Discharge of storm water in any manner in violation of this article or of any condition of a permit issued pursuant to this article or a stormwater discharge permit issued by the State of Tennessee is hereby declared a public nuisance and shall be corrected or abated.
(Ord. No. 9942, § 1, 8-31-93)

### Sec. 31-341. Illicit discharge and illegal dumping.

The following direct or indirect discharges into "Community Waters" or "Waters of the State" are prohibited and shall be unlawful:

(1) Sewage dumping or dumping of sewage sludge;

(2) Chlorinated swimming pool discharge;

(3) Discharge of any polluted household wastewater, such as but not limited to laundry washwater and dishwater, except to a sanitary sewer or septic system;

(4) Leaking sanitary sewers and connections, which shall have remained uncorrected for seven days or more;

(5) Leaking water lines shall have remained uncorrected for seven days or more;

(6) Commercial, industrial or public vehicle wash discharge;

(7) Garbage or sanitary waste disposal;

(8) No dead animals or animal fecal waste shall be directly discharged or discarded into the "Community Waters"

(9) No non-storm water discharges shall be discharged into the "Community Waters", except pursuant to a permit issued by the State of Tennessee or the City of Chattanooga;

(10) No dredged or spoil material shall be directly or indirectly discharged or discarded into "Community Waters;"

(11) No solid waste shall be directly or indirectly discharged or discarded into "Community Waters;"

(12) No chemical waste shall be directly or indirectly discharged or discarded into "Community Waters;"

(13) No wrecked or discarded vehicles or equipment shall be discharged or discarded into "Community Waters."

(Ord. No. 9942, § 1, 8-31-93)

**Sec. 31-342. Prohibition of pollutant discharge not covered by the NPDES Program.**

(a) A permit is a license to conduct an activity which is regulated by the Clean Water Act, the Water Pollution Control Act (T.C.A. § 69-3-101, et seq) or this article.

(b) Every person who is or who is planning to carry out any of the activities requiring a permit, shall obtain such a permit prior to carrying out such activities.

(c) It shall be unlawful for any person to carry out any of the following activities, except in accordance with the conditions of a valid permit:

(1) The alteration of the physical, chemical, radiological, biological, or bacteriological properties of any waters of the state or community waters;

(2) The construction, installation, modification, or operation of any treatments works or part thereof, or any extension or addition thereto;

(3) The increase in volume or strength of any wastes in excess of permissive discharges specified under any exiting permit;

(4) The development of a natural resource or the construction, installation, or operation of any establishment or any extension or modification thereof or addition thereto; the operation of which will or is likely to cause an increase in the discharge of wastes into the waters of the waters of the state or would otherwise alter the physical, chemical, radiological, biological or bacteriological properties of any waters of the state in any manner not already lawfully authorized;

(5) The construction or use of any new outlet for the discharge of any wastes into the waters of the state;

(6) The discharge of sewage, industrial wastes or other wastes into waters, or a location from which it is likely that the discharged substance will move into waters;

(7) The discharge of sewage, industrial wastes, or other wastes into a well or a location that is likely that the discharged substance will move into a well, or the underground placement of fluids and other substances which do or may affect the waters of the state.

(Ord. No. 9942, § 1, 8-31-93)

**Sec. 31-343. Accidental discharges.**

(a) In the event of any discharge or a hazardous substance in amounts which could cause a threat to public drinking supplies, a "significant spill", or any other discharge which could constitute a threat to human health or the environment, the owner or operator of the facility shall give notice to the Manager of Storm Water Management Section and the field office of Tennessee Department of Environment and Conservation as soon as practicable, but in no event later than the close of business on the day following the accidental discharge or the discharger

becomes aware of the circumstances. If an emergency response by governmental agencies is needed, the owner or operator should also call 911 immediately to report the discharge. A written report must be provided within five days of the time the discharger becomes aware of the circumstances, unless this requirement is waived by the Manager for good cause shown on a case-by-case basis, containing the following particulars: 1) a description of the discharge, 2) the exact dates and times of discharge, and 3) steps being taken to eliminate and prevent recurrence of the discharge.

(b) The discharger shall take all reasonable steps to minimize any adverse impact to the "Community Waters" or the "Waters of Tennessee," including such accelerated or additional monitoring as necessary to determine the nature and impact of the discharge. It shall not be a defense for the discharger in an enforcement action that it would have been necessary to halt or reduce the business or activity of the facility in order to maintain water quality and minimize any adverse impact that the discharge may cause.

(c) It shall be unlawful for any person to fail to comply with the provisions of this section.
(Ord. No. 9942, § 1, 8-31-93)

**Sec. 31-344. Administrative enforcement remedies.**

(a) *Notification of Violation*. Whenever the Manager finds that any permittee or any person discharging storm water has violated or is violating this article, or a Storm Water permit or order issued hereunder, the Manager or his agent may serve upon said user written notice of the violation. Within 10 days of the receipt date of this notice, an explanation of the violation and a plan for the satisfactory correction and prevention thereof, to include specific required actions, shall be submitted to the Manager. Submission of this plan in no way relieves the discharger of liability for any violations occurring before or after receipt of the notice of violation.

(b) *Consent Orders*. The Manager is hereby empowered to enter into consent orders, assurances of voluntary compliance, or other similar documents establishing an agreement with the person responsible for the noncompliance. Such orders will include specific action to be taken by the industrial user to correct the noncompliance within a time period also specified by the order. Consent orders shall have the same force and effect as administrative orders issued pursuant to paragraph (d) below.

(c) *Show Cause Hearing*. The Manager may order any person who causes or contributes to violation of this article or Storm Water permit or order issued hereunder, to show

cause why a proposed enforcement action should not be taken. Notice shall be served on the person specifying the time and place for the meeting, the proposed enforcement action and the reasons for such action, and a request that the violator show cause why this proposed enforcement action should not be taken. The notice of the meeting shall be served personally or by registered or certified mail (return receipt requested) at least 10 days prior to the hearing. Such notice may be served on any principal executive, general partner or corporate officer.

(d) *Compliance Order*. When the Manager finds that any person has violated or continues to violate this article or a permit or order issued thereunder, he may issue an order to the violator directing that, following a specified time period, adequate structures, devices, be installed or procedures implemented and properly operated. Orders may also contain such other requirements as might be reasonably necessary and appropriate to address the noncompliance, including the construction of appropriate structures, installation of devices, self-monitoring, and management practices.

(e) *Cease and Desist Orders*. When the Manager finds that any person has violated or continues to violate this article or any permit or order issued hereunder, the Manager may issue an order to cease and desist all such violations and direct those persons in noncompliance to:

(1) Comply forthwith; or

(2) Take such appropriate remedial or preventive action as may be needed to properly address a continuing or threatened violation, including halting operations and terminating the discharge.

(Ord. No. 9942, § 1, 8-31-93)

**Sec. 31-345. Unlawful acts, misdemeanor.**

It shall be unlawful for any person to:

(a) violate any provision of this article;

(b) violate the provisions of any permit issued pursuant to this article;

(c) fail or refuse to comply with any lawful notice to abate issued by the Manager, which has not been timely appealed to Storm Water Regulations Board, within the time specified by such notice; or

(d) violate any lawful order of the Storm Water Regulations Board within the time allowed by such order shall be guilty of a misdemeanor; and each day of such violation or failure or refusal to comply shall be deemed a separate offense and punishable accordingly. Any person found to be in violation of the provisions of this article shall be punished by a fine of not less than twenty-five dollars ($25.00) nor more than five hundred dollars ($500.00) for each offense. (Ord. No. 9942, § 1, 8-31-93)

**Sec. 31-346. Civil penalty.**

(a)(1) Any person who does any of the following acts or omissions shall be subject to a civil penalty of up to five thousand dollars ($5,000) per day for each day during which the act or omission continues or occurs:

(i) Who fails to obtain any permit required;

(ii) Violates the terms or conditions of a permit issued pursuant to a pretreatment program;

(iii) Violates a final determination or order of the Storm Water Regulations Board; or

(iv) Violates any provisions of this article.

(2) Any civil penalty shall be assessed in the following manner:

(i) The Manager may issue an assessment against any person or permittee responsible for the violation;

(ii) Any person against whom an assessment has been issued may secure a review of such assessment by filing with the Manager a written petition setting forth the grounds and reasons for his objections and asking for a hearing in the matter involved before the Storm Water Regulations Board and if a petition for review of the assessment is not filed within thirty (30) days after the date the assessment is served, the violator shall be deemed to have consented to the assessment and it shall become final;

(iii) Whenever any assessment has become final because of a person's failure to appeal the Manager's assessment, the Manager may apply to the appropriate court for a judgment and seek execution of such judgment

and the court, in such proceedings, shall treat a failure to appeal such assessment as a confession of judgment in the amount of the assessment;

(iv) In assessing the civil penalty the Manager may consider the following factors:

a) Whether the civil penalty imposed will be a substantial economic deterrent to the illegal activity;

b) Damages to the city, including compensation for the damage or destruction of public storm water facilities, and also including any penalties, costs and attorneys' fees incurred by the city as the result of the illegal activity, as well as the expenses involved in enforcing this article and the costs involved in rectifying any damages;

c) Cause of the discharge or violation;

d) The severity of the discharge and its effect upon public storm water facilities and upon the quality and quantity of the receiving waters;

e) Effectiveness of action taken by the violator to cease the violation;

f) The technical and economic reasonableness of reducing or eliminating the discharge; and

g) The economic benefit gained by the violator.

(3) The Storm Water Regulations Board may establish by regulation a schedule of the amount of civil penalty which can be assessed by the Manager for certain specific violations or categories of violations.

(b) Any civil penalty assessed to a violator pursuant to this section may be in addition to any civil penalty assessed by the Commissioner of Environment and Conservation for violations of T.C.A. §69-3-115; however, the sum of penalties imposed by this section and by §69-3-115 shall not exceed ten thousand dollars ($10,000) per day for each day during which the act or omission continues or occurs.

(Ord. No. 9942, § 1, 8-31-93)

**Sec. 31-347. Judicial proceedings and relief.**

(a) The Manager may initiate proceedings in any court of competent jurisdiction against any person who has or is about to:

(1) violate the provisions of this article;

(2) violate the provisions of any permit issued pursuant to this article;

(3) fail or refuse to comply with any lawful order issued by the Manager, which has not been timely appealed to the Storm Water Regulations Board, within the time allowed by this article;

(4) violates any lawful order of the Storm Water Regulations Board within the time allowed by such order.

(b) Any person who shall commit any act or fail to perform any act declared unlawful under this article shall be guilty of a misdemeanor, and each day of such violation or failure shall be deemed a separate offense and punishable accordingly.

(c) The Manager with consent of the Mayor may also initiate civil proceedings in any court of competent jurisdiction seeking monetary damages for any damages caused to publicly owned storm water facilities by any person, and to seek injunctive or other equitable relief to enforce compliance with the provisions of this article or to enforce compliance with any lawful orders of the Manager or the Storm Water Regulations Board.
(Ord. No. 9942, § 1, 8-31-93)

**Sec. 31-348. Disposition of damage payments and penalties; special fund.**

All damages collected under the provisions of sections 31-346 and civil penalties collected under section 31-347, following adjustment for the expenses incurred in making such collections, shall be allocated and appropriated to the storm water system for the administration of its program.
(Ord. No. 9942, § 1, 8-31-93)

**Sec. 31-349. Reserved.**

## DIVISION 7. FEES

### Sec. 31-350. Levied.

For the purpose of operating the storm water program of the City and the payment of the costs and expenses appurtenant, incident or necessary thereto for the construction, extension, enlargement, or acquisition of necessary storm water facilities or flood control improvement, including replacement thereof, and for the operation and maintenance thereof, there hereby is imposed a storm water user's fee upon the owner of property now served directly or indirectly by the city's storm sewer system at the rates set forth in this division.
(Ord. No. 9942, § 1, 8-31-93)

### Sec. 31-351. Property owners to pay charges.

The owner of each lot or parcel which directly or indirectly uses the storm water system maintained by the City shall pay the storm water fees and charges as provided in this division. The owner of record as determined by the records of the Assessor of Property for Hamilton County as of October 1 shall be liable for payment of the storm water fees for that calendar year; providing nothing herein shall preclude the proration of fees between property owners.
(Ord. No. 9942, § 1, 8-31-93; Ord. No. 10670, § 1, 2-24-98)

### Sec. 31-352. Charges to be based upon area and intensity development factors.

The charges for each lot or parcel shall be based upon the size of the lot or parcel and the category of land use as shown on the records of the Assessor of Property of Hamilton County and intensity development factors. The intensity development factor is based upon the relative degree of runoff of storm water anticipated from various uses of the land and proportions the cost based upon the estimated proportionate contribution to the total storm water runoff from all user classes, based upon such factors as impervious areas, the water quality of the user class runoff, storm water runoff and the volume or rate of runoff per user class. For ease of administration of the charges, single unit or two unit residential development shall be divided into categories, those with 10,000 square feet or less of land and those with greater than 10,000 square feet of land. The square footage for each parcel and the category of development shall be based upon the records maintained by the Assessor of Property of Hamilton County as the same may be changed from time to time; provided, that should an error in those records be brought to the attention of the City it shall seek to have the records corrected and shall adjust any erroneous charges made in reliance thereon.
(Ord. No. 9942, § 1, 8-31-93)

**Sec. 31-353. Billing procedure.**

(a) The storm water charges shall become effective at the rates hereinafter imposed, shall be billed annually by the City Treasurer at the same time that the city's real property taxes are mailed, and shall be due and payable at the same time as property taxes, October 1 of each year.

(b) The storm water charge shall be designated as a separate item on the property tax bill.

(c) The storm water charge shall be paid in person or by mail at the City Treasurer's Office and shall become delinquent as of the next February 1 following the billing. Any unpaid storm water charge shall bear interest at the legal rate if it remains unpaid after March 1.

(d) Pursuant to section 13, Public Chapter Number 257, T.C.A. §68-221-1112, each bill that shall contain storm water charges shall contain the following statement in bold-faced type:

"**THIS TAX HAS BEEN MANDATED BY CONGRESS**"

(Ord. No. 9942, § 1, 8-31-93)

**Sec. 31-354. Schedule of charges.**

(a) The annual storm water charge, fee, or tax shall be based upon the land area, the category of land use, and the intensity development factor as shown in the following table:

| Land Use Group | IDF | Annual Cost |
|---|---|---|
| Residential with 2 or less units and located on a lot of 10,000 square feet or less | 0.25 | $24.00 |
| Residential with 2 or less units and located on a lot of greater than 10,000 square feet | N/A | $36.00 |
| Multi-family residential with 3 or more units | 0.60 | $0.00576 times the lot area in square feet |

| | | |
|---|---|---|
| Industrial | 0.75 | $0.0072 times the lot area in square feet |
| Commercial | 0.85 | $0.00816 times the lot area in square feet |
| Institutional | 0.50 | $0.0048 times the lot area in square feet |
| Transportation, Communication and Utility | 0.70 | $0.00672 times the lot area in square feet |
| Recreational | 0.05 | $0.00048 times the lot area in square feet |
| Roadway | 0.00 | $0.0000 times the lot area in square feet |
| Agricultural | 0.04 | $0.000384 times the lot area in square feet |
| Vacant | 0.02 | $0.000192 times the lot area in square feet |
| Water | 0.00 | $0.00000 times the lot area in square feet |
| Forest | 0.00 | $0.00000 times the lot area in square feet |

(b) Provided, however, that where the charge calculated pursuant to sub-paragraph (a) shall be less than five dollars ($5.00), then no bill shall be issued.
(Ord. No. 9942, § 1, 8-31-93; Ord. No. 10111, § 4, 9-20-94)

**Sec. 31-355. Correction of erroneous billing.**

(a) Any owner or duly authorized agent may contest the accuracy of the charges imposed pursuant to this article by lodging with the Manager of the Storm Water Management Section a notice of protest. The Manager shall develop and maintain appropriate forms for the lodging of such protest, but any written protest shall be sufficient providing that it sets forth with

particularity the nature of any errors allegedly committed in the computation of such bill. Such a protest may be filed without payment of the storm water fee on or before the first December 31 following the billing, but thereafter the protest must be accompanied by payment of the bill and which shall be considered as payment under protest.

(b) The Manager shall duly consider all notices of protest as soon as practicable, and when he or she shall agree with all or any portion of the protest shall adjust the billing in accordance with such factors as are in this article. The Manager shall refund any erroneous billing for the year involved in the protest and when the conditions in the previous years also warrant an agreement, the Manager shall adjust the previous two (2) years' fees for a total of three (3) years of adjustment of erroneous fees.

(c) If the Manager disapproves the protest in whole or in part, he or she shall notify the owner or duly authorized agent as soon as practicable. In no event shall there be more than a ninety (90) day delay in resolving any protest. In the event more than ninety (90) days elapses following the filing of the protest without a decision having been rendered by the Manager, the protest shall be deemed to have been denied.

(d) If the owner disagrees with the administrative ruling of the Manager concerning a protest which was timely filed, the owner may within thirty (30) days following the date of the decision of the Manager appeal the bill and the Manager's administrative determination to the Storm Water Regulations Board by filing a notice of appeal to said board in care of the Administrator of the Department of Public Works, City Hall, Chattanooga, Tennessee, 37402, with a copy of said notice provided to the Manager. The Manager shall develop and maintain forms appropriate for filing the notice of appeal, but no particular form for such an appeal shall be required providing that the appeal sets forth with particularity the nature of the owner's complaint.

(e) If a notice of appeal to the Storm Water Regulations Board is timely filed, the board shall schedule a time and place within which to consider the appeal. The hearing on such appeals shall be informal, but the owner and Manager will each be given the opportunity to present documentary evidence in support of their position and will be given the opportunity to address the board. The board shall receive such evidence relating to the matter as may be necessary to resolve the dispute, and shall render such determinations and issue such orders as the law and facts of the case may require.
(Ord. No. 9942, § 1, 8-31-93; Ord. No. 10670, § 2, 2-24-98)

**Sec. 31-356. Adjustment for users constructing storm water retention and control facilities.**

(a) Upon application by any user adequately supported by documentation to show that the user has constructed facilities to retain and control the quantity of storm water runoff and the nature and extent of any such retention and control quantified by adequate data, the user shall be entitled to an adjustment of their storm water user fee as provided in this section.

(b) The storm water user's fee shall be reduced by twenty-five percent (25%) for users who shall have constructed and properly maintained storm water detention facilities which are adequate in design and operation for a ten (10) year storm event and discharging at the pre-development rate into the storm water system or to other waters.

(c) The storm water user's fee of commercial, industrial, institutional and multi-family residential users of the storm water system which shall have constructed and properly maintained storm water treatment facilities which are adequate in design and operation to treat or remove oil and other pollutants shall be reduced by twenty-five percent (25%) providing that the user can demonstrate that the facility removes at least eighty percent (80%) of the pollutant load which would otherwise go into the receiving storm water facility or other waters.

(d) In the event the owner shall design and construct a storm water detention or treatment facility larger or technologically more advanced than necessary for present or anticipated future development of the owner's site which is used to remediate an existing water quantity or quality problem either upstream or downstream of the owner's facility, the owner may receive an additional twenty-five percent (25%) reduction in the owner's storm water fee.

(e) The reductions authorized under sections b, c and d above shall be cumulative, providing that the total reduction in storm water users fee shall not exceed seventy-five percent of the fee as it would be calculated without reduction for the construction and operation of storm water retention and treatment facilities.

(f) The user shall make application to the Manager of the Storm Water Section for reductions in the storm water fee pursuant to this section. Each application shall be accompanied by plans or drawing of the storm water facility, and any claim of a reduction in the rate of reduction of storm water runoff or the quality thereof shall be supported by adequate data to demonstrate the accuracy of the claims. The Manager shall not be bound to accept such plans or data, but may make such independent investigation thereof as he or she may deem necessary to determine the accuracy of the claimed reductions.

(g) To the extent that the Manager is satisfied that the reductions applied for are warranted by the circumstances, he shall reduce the bill as provided herein. If the fee shall have been paid, a refund shall be authorized to the extent warranted by the reductions.

(h) The Manager shall act upon any application for a reduction in fees within ninety (90) days of the receipt thereof. In the event he shall not have acted upon same within this time, then the application shall be deemed to have been denied.

(i) The user may appeal the denial by the Manager of any claimed reduction in the quantity or quality of the storm water runoff to the Storm Water Regulations Board by filing a written notice of appeal in care of the Administrator of Public Works within thirty (30) days following the action of the Manager. No particular form for a notice of appeal shall be required and any written notice setting forth with reasonable particularity the grounds for the appeal shall be acceptable, but the Manager shall develop and maintain a form for such purposes. A copy of the notice of appeal shall be filed with the Manager. Unless the Storm Water Regulations Board shall consent to an enlargement of the administrative record, the appeal shall be decided upon the plans and data submitted by the applicant in support of the claimed reduction and any information relating thereto generated by the Administrator in review of the application. The board shall schedule a meeting to consider the appeal and both the applicant and the Manager shall be allowed to make a written and oral argument before the board in support of their respective positions.
(Ord. No. 9942, § 1, 8-31-93)

**Sec. 31-357. Elderly low-income or disabled homeowner exemption from fees.**

Those persons who have qualified as an elderly low-income homeowner pursuant to T.C.A. § 67-5-702 or who have qualified as a disabled homeowner pursuant to T.C.A. § 67-5-704 shall be exempt from payment of fees on that property which they use as their residence.
(Ord. No. 10111, § 1, 9-20-94)

**Secs. 31-358 -- 31-359. Reserved.**

DIVISION 8. STORM WATER REGULATIONS BOARD

**Sec. 31-360. Established.**

There is hereby established a Board of nine (9) members to be known as the "Storm Water Regulations Board."
(Ord. No. 9942, § 1, 8-31-93; Ord. No. 11496, §1, 12-02-03)

**Sec. 31-361. Composition; terms; filling vacancies.**

(a) The nine (9) members of the Board shall initially be appointed by the Mayor for staggered terms of one (1) to three (3) years, subject to the approval of the City Council, with terms, after the initial appointments being for three (3) years. Members shall not serve more than two (2) consecutive three (3) year terms. The Mayor shall appoint members with the following qualifications: environmental engineer or environmental scientist or educator; a representative of an industrial or commercial establishment that is regulated by this Article; two (2) representatives of neighborhood groups; a representative of the development community; a representative of an environmental interest or environmental organization; and a representative of the contractor community. The remaining two (2) members shall not have any particular qualifications, but to the extent practical, shall be selected to maintain diversity on the Board. All members shall serve at the pleasure of the Mayor and the City Council. In the event of a vacancy, the Mayor shall appoint a member to fill the unexpired term, subject to approval by the City Council. The Mayor shall select the Chairman, subject to approval by the City Council
(Ord. No. 9942, § 1, 8-31-93; Ord. No. 10111, § 5, 9-20-94; Ord. No. 11496, §2, 12-02-03)

(b) The Board shall select its own Vice-Chairman and Secretary. All officers other than the Chairman shall serve for terms of one (1) year. (Ord. No. 11496, §2, 12-02-03)

(c) If any member of the Board misses two (2) regular meetings during a calendar year without an adequate justification, they shall be notified by the Chairman they are being placed on probation. They must attend the next two (2) regularly scheduled meetings to be released from probation. If they shall fail to satisfactorily complete a probation or if they are placed on probation for a second time during a term of office, the Chairman of the Storm Water Regulations Board shall request the Mayor to dismiss the Board member and to appoint a new member approved by the City Council. If the Chairman of the Storm Water Regulations Board shall be absent from two (2) regular meetings in one (1) year without an adequate justification, the Vice-Chairman shall request the Mayor to dismiss the Chairman of the Storm Water Regulations Board and select a new Chairman to perform the duties. (Ord. No. 11496, §2, 12-02-03)

**Sec. 31-362. General duties of the board.**

In addition to any other duty or responsibility otherwise conferred upon the board by this chapter, the board shall have the duty and power as follows:

(a) To recommend from time to time to the city council that it amend or modify the provisions of this article;

(b) To hold hearings upon appeals from orders or actions of the Manager as may be provided under any provision of this chapter;

(c) To hold hearings relating to the suspension, revocation, or modification of a storm water discharge permit and issue appropriate orders relating thereto;

(d) To hold hearings relating to an appeal from a user concerning the accuracy of any fees imposed upon the user by this article;

(e) To hold such other hearings as may be required in the administration of this chapter and to make such determinations and issue such orders as may be necessary to effectuate the purposes of this article;

(f) To request assistance from any officer, agent, or employee of the city or the Chattanooga-Hamilton County Regional Planning Commission and to obtain such information or other assistance as the board might need;

(g) The board acting through its chairman shall have the power to issue subpoenas requiring attendance and testimony of witnesses and the production of documentary evidence relevant to any matter properly heard by the board; and

(h) The chairman, vice chairman or chairman pro tem shall be authorized to administer oaths to those persons giving testimony before the board.
(Ord. No. 9942, § 1, 8-31-93)

i) To prepare, with the assistance of the storm water management staff, a storm water program mission, goals, and objectives for a five (5) year time frame to plan for the existing NPDES permit and to plan for at least one (1) year subsequent to the anticipated renewal of a permit. The goals and objectives shall be reviewed on an annual basis and with the assistance of the staff an annual report shall be prepared in a timely manner for consideration in the annual capital budget submissions by the storm water staff. (Ord. No. 11496, §3, 12-02-03)

(j) The Board shall consider the proposed capital budget submission and recommend to the Mayor and Council any suggestion to change those priorities. (Ord. No. 11496, §3, 12-02-03)

(k) To review at least on a bi-annual basis the storm water rates and to recommend to the Mayor and City Council any changes to make them fairer and to insure that they adequately fund the storm water program. (Ord. No. 11496, §3, 12-02-03)

(l) To review and provide constructive comments to the storm water management staff relative to the development and implementation of a level of storm water service acceptable to the rate payers. (Ord. No. 11496, §3, 12-02-03)

(m) To respond to citizen complaints and petitions and to recommend an appropriate remedial action when appropriate. (Ord. No. 11496, §3, 12-02-03)

(n) To provide a report to the Mayor and City Council on an annual basis addressing such matters as programmatic direction, project review, and effectiveness of the storm water program. (Ord. No. 11496, §3, 12-02-03)

**Sec. 31-363. Variances.**

(a) The board may grant a variance from the requirements of this article providing to do so would not result in the violation of any state or federal law or regulation and if exceptional circumstances applicable to the site exist such that strict adherence to the provisions of this article will result in unnecessary hardship and will not result in a condition contrary to the intent of the ordinance.

(b) A written petition for a variance shall be required and shall state the specific variance sought and the reasons, with supporting data, why a variance should be granted. The request shall include all information necessary to evaluate the proposed variance. The petition shall be filed with the Manager.

(c) The Manager shall conduct a review of the request for a variance within ten (10) working days after receipt and may either support the petition or may object to the petition. The manager may elect to receive advice of the City Attorney or designee prior to rendering a decision and may defer to the advice of the City Attorney on legal issues. If the Manager objects to the variance, he shall state the reasons therefore. (Ord. No. 11496, §4, 12-02-03)

(d) Once the Manager's review is complete or the ten (10) days for review have expired, the petition shall be subject to board action at the next regularly scheduled meeting or at a special meeting called in the discretion of the chair.
(Ord. No. 9942, § 1, 8-31-93)

**Sec. 31-364. Meetings; quorum.**

(a) The board shall hold regular quarterly meetings and such special meetings as the board may find necessary. (Ord. No. 11496, §5, 12-02-03)

(b) Five (5) members of the board shall constitute a quorum, but a lesser number may adjourn a meeting from day to day. Any substantive action of the board shall require five (5) votes, but a majority of the quorum may decide any procedural matter.
(Ord. No. 9942, § 1, 8-31-93; (Ord. No. 11496, §5, 12-02-03)

**Sec. 31-365. Hearing procedure; judicial review.**

(a) *When to be held*. The storm water regulations board shall schedule an adjudicatory hearing to resolve disputed questions of fact and law whenever provided by any provision of this article.

(b) *Record of hearing*. At any such hearing, all testimony presented shall be under oath or upon solemn affirmation in lieu of oath. The board shall make a record of such hearing, but the same need not be a verbatim record. Any party coming before the board shall have the right to have such hearing recorded stenographically, but in such event the record need not be transcribed unless any party seeks judicial review of the order or action of the board by common law writ of certiorari, and in such event the parties seeking such judicial review shall pay for the transcription and provide the board with the original of the transcript so that it may be certified to the court.

(c) *Subpoenas*. The chairman may issue subpoenas requiring attendance and testimony of witnesses or the production of evidence, or both. A request for issuance of a subpoena shall be made by lodging with the chairman at least ten (10) days prior to the scheduled hearing date a written request for a subpoena setting forth the name and address of the party to be subpoenaed and identifying any evidence to be produced. Upon endorsement of a subpoena by the chairman, the same shall be delivered to the chief of police for service by any police officer of the city, if the witness resides within the city. If the witness does not reside in the city, the chairman shall issue a written request that the witness attend the hearing.

(d) *Depositions*. Upon agreement of all parties, the testimony of any person may be taken by deposition or written interrogatories. Unless otherwise agreed, the deposition shall be taken in a manner consistent with Rules 26 through 33 of the Tennessee Rules of Civil Procedure, with the chairman to rule on such matters as would require a ruling by the court under such rules.

(e) *Hearing procedure*. The party at such hearing bearing the affirmative burden of proof shall first call his witnesses, to be followed by witnesses called by other parties, to be followed by any witnesses which the board may desire to call. Rebuttal witnesses shall be called in the same order. The chairman shall rule on any evidentiary questions arising during such hearing and shall make such other rulings as may be necessary or advisable to facilitate an orderly hearing subject to approval of the board. The board, the Manager, or his representative, and all parties shall have the right to examine any witness. The board shall not be bound by or limited to rules of evidence applicable to legal proceedings.

(f) *Appeal to board of manager's order*. Any person aggrieved by any order or determination of the Manager may appeal said order or determination to the board and have such order or determination reviewed by the board under the provisions of this section. A written notice of appeal shall be filed with the Manager and with the chairman, and such notice shall set forth with particularity the action or inaction the Manager complained of and the relief sought by the person filing said appeal. A special meeting of the board may be called by the chairman upon the filing of such appeal, and the board may in its discretion suspend the operation of the order or determination of the Manager appeals from until such time as the board has acted upon the appeal.

(g) *Absence of chairman*. The vice-chairman or the chairman pro tem shall possess all the authority delegated to the chairman by this section when acting in his absence or in his stead.

(h) *Review of board's decision*. Any person aggrieved by any final order of determination of the board hereunder shall have judicial review by common law writ of certiorari.

(Ord. No. 9942, § 1, 8-31-93)

Permit #_____

Report Date:_____

# CITY OF CHATTANOOGA
# INTERCEPTOR SEWER SYSTEM
# INDUSTRIAL pH SELF-MONITORING REPORT FORM

COMPANY NAME: _____
DISCHARGE POINT: _____
REPORTING PERIOD: FROM:_____ TO: _____ (DATES)
METER CHECKED BY: _____ (NAME)
FREQUENCY OF CALIBRATION:_____
pH RANGE ALLOWED BY PERMIT FROM: _____TO: _____(pH STANDARD UNITS)

If pH did not violate the allowable range for the reporting period then check here: ☐
and sign certification. If violations did occur, then list below and sign certification.

## pH VIOLATIONS REPORT

| DATE | HIGHEST OR LOWEST EXTENT (STANDARD UNITS) | TOTAL DAILY DURATION (MINUTES) | CAUSE AND CORRECTIVE ACTION |
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Continue on back of this page if needed. All monitoring records must be retained on facility site for at least three years. All monitoring must conform to standards in 40 CFR Part 136.

## CERTIFICATION

I certify under penalty of law that this document and all attachments were prepared under my direction or supervision in accordance with a system designed to assure that qualified personnel properly gather and evaluate the information submitted. Based on my inquiry of the person or persons who manage the system, or those persons directly responsible for gathering the information, the information submitted is, to the best of my knowledge and belief, true, accurate, and complete. I am aware that there are significant penalties for submitting false information, including the possibility of fine and imprisonment for knowing violations.

Signature:_____Title: _____ Date:_____

**(Must be signed by a "responsible corporate officer, partner or duly authorized representative" as provided in Code Section 31-53 (h) (11). A copy of authorization must be on file with the Superintendent if signature authority has been delegated.)**

Permit #_____
Report Date:_____

# CITY OF CHATTANOOGA
# INTERCEPTOR SEWER SYSTEM
# INDUSTRIAL WASTE DISCHARGE SELF-MONITORING REPORT FORM

COMPANY NAME:_____
DISCHARGE POINT: _____
(DESCRIBE LOCATION IF DIFFERENT FROM MONITORING STATION USED BY CITY PERSONNEL)
SAMPLE DATE: _____ FLOW PROPORTIONAL COMPOSITE: _____ OR GRAB: _____
SAMPLE TIME: FROM: _____
TO: _____ SAMPLING PERIOD FLOW _____(MILLION GALLONS)
COLLECTED BY: _____

(ALL ITEMS MUST BE COMPLETED OR THIS REPORT WILL NOT BE CREDITED FOR COMPLIANCE.)

Production Rate _____ (If required by Permit)

| CHECK HERE IF PERMIT LIMIT IS VIOLATED | POLLUTANT | PERMIT LIMIT mg/l | ACTUAL DISCHARGE mg/l | DATE ANALYZED | ANALYZED BY | METHOD* |
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_____ = TOTAL NUMBER OF PERMIT LIMITS VIOLATED DURING THIS DISCHARGE EVENT.
(INDICATE ZERO IF NO VIOLATIONS WERE DETECTED.)

Use continuation sheet for longer reports. Insert pollutant name from permit, as appropriate. Some pollutants listed above may not be required to be monitored - check permit. Surcharge monitoring should be reported on the appropriate form. Records must be retained on facility site at least three years. (Section 31-53 k)

*Method must conform with EPA Regulations 40 CFR Part 136.

Form - TOXICS DMR

Permit #_____
Report Date:_____

# INDUSTRIAL WASTE DISCHARGE SELF-MONITORING REPORT FORM

## Page 2 - REPORT CONTINUATION AND CERTIFICATION

| VIOLATION | POLLUTANT | PERMIT LIMIT mg/l | ACTUAL DISCHARGE mg/l | DATE ANALYZED | ANALYZED BY | METHOD* |
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_____ = TOTAL NUMBER OF VIOLATIONS

## CERTIFICATION

| | Yes | No |
|---|---|---|
| Have any slugs occurred since the last report?<br>If so, give date of report to the treatment plant: _____<br>(Section 31-53 (h) (6) | ☐ | ☐ |
| Has any substantial change occurred in volume or waste character (including reportable hazardous wastes - Section 31-53 (h) (8)?<br>If so, identify change: _____<br>(Section 31-53 (h) (9) | ☐ | ☐ |
| Has all sampling and monitoring conducted in addition to permit been reported?<br>If not, then why not? _____<br>Section 31-53 (h) (13) | ☐ | ☐ |
| Has any sampling been needed to comply with the requirement for follow-up sampling within 30 days after violations?<br>f so, give date of sampling: _____<br>(Section 31-53 (h) (12) | ☐ | ☐ |

I certify under penalty of law that this document and all attachments were prepared under my direction or supervision in accordance with a system designed to assure that qualified personnel properly gather and evaluate the information submitted. Based on my inquiry of the person or persons who manage the system, or those persons directly responsible for gathering the information, the information submitted is, to the best of my knowledge and belief, true, accurate, and complete. I am aware that there were significant penalties for submitting false information, including the possibility of fine and imprisonment for knowing violations.

Signature: _____ Title: _____ Date: _____
(Must be signed by a "responsible corporate officer, partner or duly authorized representative" as provided in Code Section 31-53 (h) (11). A copy of the authorization must be on file with the Superintendent if signature authority has been delegated.)

Permit #_____
Report Date:_____

# CITY OF CHATTANOOGA
# INTERCEPTOR SEWER SYSTEM
# INDUSTRIAL SURCHARGE SELF-MONITORING REPORT FORM

COMPANY NAME:_____
DISCHARGE POINT: _____
REPORTING PERIOD: FROM:_____ TO: _____ (DATE)
NUMBER OF OPERATING DAYS IN REPORTING PERIOD: _____
NUMBER OF SAMPLES REQUIRED BY PERMIT TO BE COLLECTED THIS PERIOD: _____
NUMBER OF SAMPLES ACTUALLY COLLECTED: _____
REASON FOR DEFICIENCY IF SAMPLING LESS THAN REQUIRED: _____

| DATE COLLECTED | FLOW (mgd) | BOD (mg/l) | TSS (mg/l) | COLLECTED BY | ANALYZED BY |
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Permit #_____
Report Date:_____

# INDUSTRIAL SURCHARGE SELF-MONITORING REPORT FORM

## PAGE 2 - REPORT CONTINUATION AND CERTIFICATION

| DATE COLLECTED | FLOW (mgd) | BOD (mg/l) | TSS (mg/l) | COLLECTED BY | ANALYZED BY |
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**ALL MONITORING RECORDS MUST BE RETAINED AT THE SITE OF THE PERMITTED FACILITY FOR AT LEAST THREE YEARS. (SECTION 31-53 k). THE FINAL SURCHARGE BILL WILL BE CALCULATED USING ALL AVAILABLE, VERIFIED MONITORING INFORMATION, INCLUDING MONITORING CONDUCTED BY CITY PERSONNEL. (SECTION 31-41 e). ALL MONITORING AND ANALYSIS MUST CONFORM TO STANDARDS IN 40 CFR PART 136.**

## CERTIFICATION

**I certify under penalty of law that this document and all attachments were prepared under my direction or supervision in accordance with a system designed to assure that qualified personnel properly gather and evaluate the information submitted. Based on my inquiry of the person or persons who manage the system, or those persons directly responsible for gathering the information, the information submitted is, to the best of my knowledge and belief, true, accurate, and complete. I am aware that there were significant penalties for submitting false information, including the possibility of fine and imprisonment for knowing violations.**

**Signature: _____ Title: _____ Date: _____**
**(Must be signed by a "responsible corporate officer, partner or duly authorized representative" as provided in Code Section 31-53 (h) (11). A copy of the authorization must be on file with the Superintendent if signature authority has been deligated.)**

# PERMIT APPLICATION*

## CITY OF CHATTANOOGA, TENNESSEE - INTERCEPTOR SEWER SYSTEM

Applicant's Name_____

(Firm Name)

Address_____

Telephone No. _____

Contact _____
(Person to be contacted concerning this permit application)

## PRINCIPAL ACTIVITY CONDUCTED BY THE PERMIT APPLICANT

_____

_____

_____

_____

_____

Standard Industrial Classification (SIC Code) _____

Hours of Operation _____

Number of Days Per Week _____

Number of Employees _____

**I CERTIFY THAT ALL STATEMENTS MADE IN THIS APPLICATION ARE TRUE TO THE BEST OF MY KNOWLEDGE.**

DATE _____ SIGNED _____

TITLE _____

***A separate application must be completed for each point where industrial wastes enter the Chattanooga Sewer System.**

All information, samples, measurements, and analyses must be made by the permit applicant or a consultant retained by the applicant at his expense. The City of Chattanooga will not be responsible for sampling or analysis of wastewater for the purpose of completing this permit. The Industrial Waste Program Staff at 757-5026 will be available to explain this application and answer questions pertaining to the program.

## I. WASTEWATER VOLUME

**AVERAGE WATER USAGE**
**(Past 12-months)**

**(Indicate if information is from water bills)**

Municipal Water Supply _____gal/day

Wells _____gal/day

Other Sources _____gal/day

Total _____gal/day

**WASTEWATER VOLUME TO**

**CHATTANOOGA SEWER SYSTEM (indicate how measured)**

Flow Rate (Peak day) _____gal/day

Flow Rate (minimum day) _____gal/day

Flow Rate (30 minute peak) _____gal/day

Normal Time of Day of Peak Flow _____

Duration of Total Discharge _____ hours/day

Normal Time of Day of Total Discharge _____

Seasonal variation: _____

_____

_____

_____

_____

**TO OTHER RECEIVING STREAMS (storm sewers or surface drainage, describe)**

Peak Flow Rate _____gal/day

Minimum Flow Rate _____gal/day

## II. WASTEWATER PARAMETERS

These analyses shall be run on twenty-four (24) hour composite flow proportional samples. Alternate methods may be used only if EPA approved and acceptable to the City of Chattanooga.

| PARAMETER | METHOD* | AVERAGE CONCENTRATION MG/L | |
|---|---|---|---|
| Antimony (Sb) | 204.2 | _____ | mg/l |
| Arsenic (As) | 206.2 | _____ | mg/l |
| Cadmium (Cd) | 213.1,213.2 | _____ | mg/l |
| Chromium (Cr) | 218.1,218.2 | _____ | mg/l |
| Hexavalent Chromium (Cr6) | 218.4 | _____ | mg/l |
| Cpper (Cu) | 220.1,220.2 | _____ | mg/l |
| Cyanide (CN) (Grab only) | 335.2,335.3 | _____ | mg/l |
| Iron (Fe) | 236.1,236.2 | _____ | mg/l |
| Lead (Pb) | 239.1,239.2 | _____ | mg/l |
| Manganese (Mn) | 243.1,243.2 | _____ | mg/l |
| Mercury (Hg) | 245.1,245.2 | _____ | mg/l |
| Nickel (Ni) | 249.1,249.2 | _____ | mg/l |
| Phenols (Grab only) | 420.1,420.2 | _____ | mg/l |
| Phosphorus (PO4-P) | 365.1,365.2, 365.3,365.4 | _____ | mg/l |
| Selenium (Se) | 270.2,270.3 | _____ | mg/l |
| Silver (Ag) | 272.1,272.2 | _____ | mg/l |
| Zinc (Zn) | 289.1,289.2 | _____ | mg/l |
| Biochemical Oxygen Demand (5 day) | 405.1 | _____ | mg/l |
| Chemical Oxygen Demand | 410.1,410.2, 410.4 | _____ | mg/l |
| Total Suspended Solids (TSS) | 160.2 | _____ | mg/l |
| Total Kjehldahl Nitrogen (TKN) | 351.1,351.2, | _____ | mg/l |
| | 351.3,351.4 | _____ | mg/l |
| Ammonia Nitrogen (NH3-N) | 350.1,350.2 | _____ | mg/l |
| | 350.3 | _____ | mg/l |
| Oil & Grease (Total) (Grab only) | 413.1 | _____ | mg/l |
| Methylene Blue Active Substances (MBAS) | 425.1 | _____ | mg/l |
| Total Dissolved Solids (TDS), 103-105 C | 2540C** | _____ | mg/l |
| Volatiles | 624 | _____ | mg/l |
| Semi-Volatiles | 625 | _____ | mg/l |
| Temperature | 170.1 | AVG _____ | C |
| | | MAX _____ | C |
| pH | 150.1,150.2 | MAX _____ | pH |
| | | MIN _____ | pH |
| Color | | _____ | *** |

Sampled by _____ Date _____

Analyzed by _____ Date _____

*Methods for Chemical Analysis of Water and Wastes, EPA-600/4-79-020, Rev. 3/83
**Standard Methods for the Examination of Water and Wastewater, 18th edition, 1992
***Verbally describe i.e. Dark Brown, Light Blue, Straw, Clear, Turbid, etc.

**All sampling and analysis must be in accordance with 40 CFR 136.**

## III. PROCESS DESCRIPTION

A. Describe manufacturing process(es) which generate wastewater.
Estimate the quantity of product and wastewater.

B. Describe other water uses in process(es) which do not generate wastewater.
(i.e. water sold as product, indirect cooling waters, etc.). Estimate the
quantity per operating day.
Indicate any seasonal variations.

C. Is the process a continuous process or batch process? _____
If batch, describe in detail.

Number batches per day _____/day
Volume of wastewater per batch _____/batch
Frequency of batch discharges _____

D. List of raw materials used in manufacturing process, including hazardous or toxic substances on premises which could be spilled into sewer system. Any EPA priority pollutant on the attached list with this application should be listed here.

_____ _____

_____ _____

_____ _____

(use extra sheets if necessary)

## IV. SANITARY WASTEWATER

1. Is this separate from industrial wastewater? yes _____ no _____
2. How many fixtures on premises? _____
3. Volume of water utilized for sanitary purposes: _____ gal/day

## V. DESCRIPTION OF SEWERS AND TIE-INS TO CITY SYSTEM

A. Are sanitary and industrial sewers separated? yes _____ no _____

B. Are any roof drains or storm water catch basins connected to the process or sanitary sewers? yes _____ no _____

If so, how many? _____

C. Furnish drawings or sketches showing locations, sizes and elevations of sewers, both process and sanitary and storm sewers, (if applicable) with respect to major buildings and City streets.

D. Are any flow measuring devices (i.e. weir, flume, meters) presently installed in outfall sewers? yes _____ no _____

If yes, please describe and show location on drawings and sketches requested in item V. (c).

## VI. PRETREATMENT FACILITIES

A. Is any type of pretreatment (including grease or grit traps) provided for process wastewaters? yes _____ no _____

B. If yes, please describe in detail.

_____

_____

C. Please furnish simplified flow diagram noting unit process(es) if applicable.

D. Do you monitor your wastewater? yes _____ no _____

If yes, describe monitoring program to include frequency of samplings, parameters monitored, past history on monitoring.

(use extra sheet if necessary)

E. If solids, sludge or grit is collected from grease or grit traps or generated by pretreatment (or process) how are they disposed of? Describe.

_____

_____

_____

_____

_____

_____

_____

Volume of solids produced

MAX _____ $yd^3$ /day
AVG _____ $yd^3$ /day
MIN _____ $yd^3$ /day

Weight of solids produced

MAX _____ lbs /day
AVG _____ lbs /day
MIN _____ lbs /day

F. Are any hazardous wastes as defined by EPA and 40 CFR Parts 260 and 261 generated, stored, handled, or disposed of at this location?

yes _____
no _____

## Appendix B — List of 126 Priority Pollutants

| | |
|---|---|
| 001 | Acenapthene |
| 002 | Acrolein |
| 003 | Acrylonitrile |
| 004 | Benzene |
| 005 | Benzidine |
| 006 | Carbon tetrachloride (tetrachloromethane) |
| 007 | Chlorobenzene |
| 008 | 1,2,4-trichlorobenzene |
| 009 | Hexachlorobenzene |
| 010 | 1,2-dichloroethane |
| 011 | 1,1,1-trichloreothane |
| 012 | Hexachloroethane |
| 013 | 1,1-dichloroethane |
| 014 | 1,1,2-trichloroethane |
| 015 | 1,1,2,2-tetrachloroethane |
| 016 | Chloroethane |
| 017 | Bis (2-chloroethyl) ether |
| 018 | 2-chloroethyl vinyl ether (mixed) |
| 019 | 2-chloronaphthalene |
| 020 | 2,4,6-trichlorophenol |
| 021 | Parachlorometa cresol |
| 022 | Chloroform (trichloromethane) |
| 023 | 2-chlorophenol |
| 024 | 1,2-dichlorobenzene |
| 025 | 1,3-dichlorobenzene |
| 026 | 1,4-dichlorobenzene |
| 027 | 3,3-dichlorobenzidine |
| 028 | 1,1-dichloroethylene |
| 029 | 1,2-trans-dichloroethylene |
| 030 | 2,4-dichlorophenol |
| 031 | 1,2-dichloropropane |
| 032 | 1,2-dichloropropylene(1,3-dichloropropene) |
| 033 | 2,4-dimethylphenol |
| 034 | 2,4-dinitrotoluene |
| 035 | 2,6-dinitrotoluene |
| 036 | 1,2-diphenylhydrazine |
| 037 | Ethylbenzene |
| 038 | Fluoranthene |
| 039 | 4-chlorophenyl phenyl ether |
| 040 | 4-bromophenyl phenyl ether |
| 041 | Bis(2-chloroisopropyl) ether |
| 042 | Bis(2-chloroethoxy) methane |
| 043 | Methylene chloride (dichloromethane) |
| 044 | Methyl chloride (dichloromethane) |
| 045 | Methyl bromide (bromomethane) |
| 046 | Bromoform (tribromomethane) |
| 047 | Dichlorobromomethane |
| 048 | Chlorodibromomethane |
| 049 | Hexachlorobutadiene |
| 050 | Hexachloromyclopentadiene |
| 051 | Isophorone |
| 052 | Naphthalene |
| 053 | Nitrobenzene |
| 054 | 2-nitrophenol |
| 055 | 4-nitrophenol |
| 056 | 2,4-dinitrophenol |
| 057 | 4,6-dinitro-o-cresol |
| 058 | N-nitrosodimethylamine |
| 059 | N-nitrosodiphenylamine |
| 060 | N-nitrosodi-n-propylamin |
| 061 | Pentachlorophenol |
| 062 | Phenol |
| 063 | Bis(2-ethylhexyl) phthalate |
| 064 | Butyl benzyl phthalate |
| 065 | Di-N-Butyl Phthalate |
| 066 | Di-n-octyl phthalate |
| 067 | Diethyl Phthalate |
| 068 | Dimethyl phthalate |
| 069 | 1,2-benzanthracene (benzo(a) anthracene |
| 070 | Benzo(a)pyrene (3,4-benzo-pyrene) |
| 071 | 3,4-Benzofluoranthene (benzo(b) fluoranthene) |
| 072 | 11,12-benzofluoranthene (benzo(b) fluoranthene) |
| 073 | Chrysene |
| 074 | Acenaphthylene |
| 075 | Anthracene |
| 076 | 1,12-benzoperylene (benzo(ghi) perylene) |
| 077 | Fluorene |
| 078 | Phenanthrene |
| 079 | 1,2,5,6-dibenzanthracene (dibenzo(,h) anthracene) |
| 080 | Indeno(,1,2,3-cd)pyrene(2,3-o-pheynylene pyrene) |
| 081 | Pyrene |
| 082 | Tetrachloroethylene |
| 083 | Toluene |
| 084 | Trichloroethylene |
| 085 | Vinyl chloride (chloroethylene) |
| 086 | Aldrin |
| 087 | Dieldrin |
| 088 | Chlordane (technical mixture and metabolites) |
| 089 | 4,4-DDT |
| 090 | 4,4-DDE (p,p-DDX) |
| 091 | 4,4-DDD (p,p-TDE) |
| 092 | Alpha-endosulfan |
| 093 | Beta-endosulfan |
| 094 | Endosulfan sulfate |
| 095 | Endrin |
| 096 | Endrin aldehyde |
| 097 | Heptachlor |
| 098 | Heptachlor epoxide (BHC-hexachlorocyclohexane) |
| 099 | Alpha-BHC |
| 100 | Beta-BHC |
| 101 | Gamma-BHC(lindane) |
| 102 | Delta-BHC (PCB-polychlorinated biphenyls) |
| 103 | PCB-1242 (Arochlor 1242) |
| 104 | PCB-1254 (Arochlor 1254) |
| 105 | PCB-1221 (Arochlor 1221) |
| 106 | PCB-1232 (Arochlor 1232) |
| 107 | PCB-1248 (Arochlor 1248) |
| 108 | PCB-1260 (Arochlor 1260) |
| 109 | PCB-1016 (Arochlor 1016) |
| 110 | Toxaphene |
| 111 | Antimony |
| 112 | Arsenic |
| 113 | Asbestos |
| 114 | Beryllium |
| 115 | Cadmium |
| 116 | Chromium |
| 117 | Copper |
| 118 | Cyanide, Total |
| 119 | Lead |
| 120 | Mercury |
| 121 | Nickel |
| 122 | Selenium |
| 123 | Silver |
| 124 | Thallium |
| 125 | Zinc |
| 126 | 2,3,7,8-tetrachloro-dibenzo-p-dioxin (TCDD) |

# SURCHARGE RATES

## JULY 1, 2007 - JUNE 30, 2008

BIOCHEMICAL OXYGEN DEMAND (BOD) - $0.094

TOTAL SUSPENDED SOLIDS (TSS) - $0.067