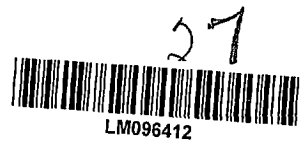


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UNITED STATES GENERAL ACCOUNTING OFFICE  
WASHINGTON, D.C. 20548



LOGISTICS AND COMMUNICATIONS  
DIVISION

B-133201

APR 5 1973

The Honorable Elliot L. Richardson  
The Secretary of Defense

Attention: Assistant Secretary of Defense  
(Telecommunications)

Dear Mr. Secretary:

In August 1972 we submitted our draft report "Government Should Seek Compensation for Use of its Facilities in Providing Telephone Service" to certain Government agencies and private industry interests for comment. We have received comments from your office; the Office of Telecommunications Policy (OTP), Executive Office of the President; the Federal Communications Commission (FCC); the General Services Administration (GSA); the American Telephone and Telegraph Company; and the United States Independent Telephone Association.

This is to advise you and the other respondents that we are deferring further consideration of this question pending evaluation and decision on a related matter which is presently undergoing test and evaluation within the Department of Defense (DOD)--the outcome of which could affect any conclusions or course of action indicated in our draft report. The related matter involves the possible extended use by DOD of the Federal Telecommunications System (FTS), operated by GSA, in lieu of commercial long-distance telephone calls.

BACKGROUND

DOD provides telephone service by means of Government-owned systems within and in the immediate vicinity of about 160 military installations and also provides interconnection with systems of commercial telephone companies. We made a review to determine whether the Government is compensated in any manner when DOD facilities and services are used to complete incoming or outgoing long-distance telephone calls.

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Various regulatory organizations control telephone services and related activities. FCC controls interstate and foreign communications, such as telephone and telegraph, transmitted by wire and radio. The Communications Act of 1934, as amended (47 U.S.C. 151), gives FCC jurisdiction over charges, practices, classifications, and regulations for interstate and foreign communications and empowers FCC to determine whether they are just and reasonable. The various State regulatory organizations have jurisdiction over intrastate communications.

The Government pays the standard tariff (schedule of charges) to the telephone companies for long-distance telephone service, although Government-provided facilities-- including telephones, cables, poles, and switchboards--are used in making the calls. Such tariffs generally are established on a station-to-station basis, i.e., the message toll service charge covers the use of all facilities between originating telephone and the receiving telephone.

Forty military installations queried were not compensated for the use of their telephone facilities or services in completing toll calls charged to telephones used for official Government business. We calculated, in detail, the potential compensation involved at six of these installations.

#### TELEPHONE COMPANIES SHARE REVENUES

Telephone companies share revenues when intercompany facilities are used in providing long-distance telephone services, such as toll calls (discussed below), wide area telephone service, private-line service, teletypewriter exchange service, and telegraph service.

Two basic revenue-sharing methods are used to distribute toll-call revenues among independent telephone companies and between independent telephone companies and Bell System affiliated companies. One method is based on cost and traffic separation studies. Toll-call revenues are distributed between companies on the basis of costs incurred to provide the services.

The other method (hereinafter referred to as the average-revenue-per-message method) applies a series of accepted formulas to distribute toll-call revenues between any two connecting companies. Essentially, the distribution is based on the number of long-distance telephone calls that originate in, end in, or traverse the facilities of a company and the total revenue from those calls. A settlement amount is computed as compensation to such connecting company for the toll calls handled on its facilities.

Revenues from toll calls are also distributed among Bell System affiliated companies for calls completed within the Bell System.

FACILITIES AND SERVICES PROVIDED BY GOVERNMENT-OWNED  
AND INDEPENDENT TELEPHONE COMPANY SYSTEMS

Generally, the Government-owned telephone systems consist of the installation's central office equipment, including switchboard and switching equipment; telephone cables and poles; and telephone instruments. The Government provides the electrical power which sustains voice transmission within the installation boundaries, local operator assistance, and complete maintenance and servicing of the system.

Government-owned telephone systems interface with the commercial telephone network, providing users with complete local and long-distance telephone service. The interface is a physical connection between the Government's and telephone company's cables. Thus long-distance calls placed by users originate from and pass over Government-owned equipment to the interface point and then on to the telephone company's system. This procedure would be reversed for incoming long-distance calls.

Similarly, an independent telephone company owns, operates, and maintains the equipment, including the central office switching equipment, telephone instruments, and cables necessary to provide its customers local and long-distance telephone services. The independent company also

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provides operator assistance and the electrical power that sustains the system's voice channels.

Long-distance calls placed to locations outside the independent company's geographical area travel through the independent company's system. The reverse would be true for incoming telephone calls from the Bell System or another independent company system.

Some telephone companies account for toll calls originating in or traversing their network in order to bill their customers and to compute a connecting telephone company's share of revenues, and some rely on other companies to provide this service. The Government does not compute or accumulate toll charges for calls made. However, in our computation of the potential compensation to the Government below, we used formulas applicable where other companies perform this service.

INDICATION OF POTENTIAL COMPENSATION  
TO GOVERNMENT

We do not say that the costs incurred by DOD installations in completing interstate and intrastate toll calls are completely comparable with such costs incurred by independent telephone companies. For example, DOD is not a common carrier and does not carry toll calls over its installations' lines except outgoing calls originating at the installation or incoming calls terminating at the installation, while some telephone companies carry calls which neither originate nor terminate with such company nor its customers. However, as stated on page 3, the average-revenue-per-message method formulas do not distinguish between originating, terminating, or traversing calls; and the distribution is based, essentially, on the number of calls and the total revenue of such calls. To illustrate the potential magnitude of compensation to the Government for use of its facilities and services in completing toll calls, we estimated the amount attributable

to telephones used for official business,<sup>1</sup> using the average-revenue-per-message method. This method applies to calls that are timed, for which charges are computed by a company other than the one which is to receive the computed share of revenue. This amounted to \$26,544 monthly, or \$318,528 annually, for six military installations.

Although other methods might be used to assess the value of Government services and facilities employed, we used the average-revenue-per-message method because (1) small, independent telephone companies preferred it as simpler and less costly to apply than actual cost and traffic study methods and (2) it appeared that the Government-owned telephone systems resemble small, independent telephone companies.

We reviewed only 6 of about 160 military installations with Government-owned telephone systems. We did not consider toll calls involving the Government's unofficial customers and other long-distance telephone services provided at some military installations, such as wide area telephone service and private-line service. We believe, however, that such services may be subject to the same considerations as the official toll calls. In view of these limitations, we believe that the potential economic consequences to the Government are substantial.

#### AGENCY AND INDUSTRY COMMENTS

The respondents listed in the first paragraph of this report, in general, expressed the opinion that it would be inequitable for the general public to pay higher rates because the Government elected to provide its own facilities. They stated, and we recognize, that any compensation to the Government would ultimately be reflected in increased tariffs because the basis for existing tariffs does not include the operating and investment costs of Government-owned facilities.

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<sup>1</sup>As distinguished from unofficial telephones, such as class B telephones in family housing units.

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FCC's Carterfone decision in June 1968 found discriminatory a telephone company regulation broadly prohibiting the use of interconnecting devices not furnished by the company. As a result, many private individuals and companies are installing their own in-house instruments and other telephone facilities. Some respondents expressed concern that compensation accorded the Government would have to be extended in similar circumstances to other non-Government entities.

Although OTP did not take exception to the principle of compensation to the Government on equity grounds, it stated that the implications of such a concept are too complex to see clearly at this time. It expressed the view that its effect on the growth and structure of the telecommunications industry and the impact on the public at large far outweigh any short-term gains to DOD.

#### CONCLUSION

The Government, in effect, provides the terminal distribution system for long-distance telephone calls at the 160 installations. The Government-provided facilities--being used without compensation--are not, therefore, included in the telephone company's rate base for establishing tariffs or charges. The Government, however, pays the same tariffs for long-distance services as other customers using telephone company facilities and services, the cost of which is included in the company's rate base for establishing such tariffs.

#### IMPACT OF RELATED PROJECT

DOD, with GSA's cooperation, is testing and evaluating the possible use of FTS in lieu of commercial long-distance telephone services, as the result of an earlier GAO review. (See our report, "Economies Available Through Increased Use of the Federal Telecommunications System by Military Installations" (B-146864, Aug. 24, 1972).) If, as a result of this study, DOD should use FTS instead of commercial telephone services, the question regarding compensation for use of Government-owned telephone facilities for long-distance toll calls would no longer be pertinent. Therefore, we are

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deferring further consideration of this question until testing and evaluation of the concept is completed.

We are sending copies of this report to the House and Senate Committees on Appropriations; the House and Senate Committees on Government Operations; the House Committee on Interstate and Foreign Commerce; the Senate Committee on Commerce; the House Committee on Armed Services and its Special Subcommittee on Defense Communications; the Senate Committee on Armed Services and its Preparedness Investigating Subcommittee; the Subcommittee on Priorities and Economy in Government of the Joint Economic Committee; and the respondents to the draft report, previously identified. We are sending copies also to the Secretaries of the Army, Navy, and Air Force and to the Director, Defense Communications Agency for their information.

Sincerely yours,

  
J. K. Fasick  
Director