Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of 2000 Biennial Regulatory Review – Comprehensive Review of the Accounting Requirements for Incumbent Local Exchange Carriers: Phase 2 and Phase 3	CC Docket No. 00-199

PHASE 2 REPLY COMMENTS OF VERIZON[1]

The Commission's "Phase II" proposals for streamlining its Part 32 accounting rules and the automated reporting and management information system ("ARMIS") reporting requirements do not face up to the reality that these rules have become obsolete as the result of competition and the use of price cap regulation. Section 11 of the Act imposes a duty on the Commission to overcome the bureaucratic inertia that causes a regulation, once adopted, to exist in perpetuity despite the fact that the regulation's original justification has disappeared. The accounting and ARMIS reporting rules are a prime example of this phenomenon. They were adopted to facilitate rate of return regulation, a regime that no longer applies to the carriers that are most heavily burdened by these rules – the large incumbent local exchange carriers. These rules are no longer necessary and must be eliminated. At the very least, the Commission should adopt the less-detailed "Class B" accounts in Phase II of this proceeding for all carriers that are still subject to the Part 32 accounting rules, and it should adopt the streamlining proposals set forth in the comments and reply comments of the United States Telecom Association ("USTA"). The

Commission should reject the proposal of the National Association of Regulatory Utility Commissioners ("NARUC") to expand the scope and complexity of the accounting and reporting rules.

I. The Commission Should Eliminate Its Part 32 Accounting And ARMIS Reporting Rules.

The Commission's adoption of price cap regulation, the CALLS plan for reducing and restructuring access charge, and pricing flexibility have eliminated the need for the incumbent local exchange carriers to maintain a separate Part 32 set of books in addition to the books they maintain under generally accepted accounting principles ("GAAP"). Price cap regulation broke the link between rates and costs and the Commission abandoned earnings sharing years ago. The CALLS plan substantially reduced access charges and, by targeting switched access rates to a specific price, made any effort to forge a theoretical link between regulated costs and price even more remote. Moreover, even the possibility that costs may be used to calculate lower formula adjustments is fading as carriers invoke pricing flexibility, which requires them to waive use of the lower formula adjustment on a holding company basis. The minimal need for cost data in the future can be met more cost-effectively by developing reports and studies using GAAP accounts.

The primary proponents of maintaining, and in fact expanding, the burden of the Commission's accounting and reporting requirements are several state regulatory agencies. ***See, e.g.,*** Florida PSC, 4-6; Maryland PSC, 3-6; NARUC 3-10. However, their arguments to continue (and, in fact, increase) these obligations for new intrastate purposes merely highlight the fact that

[1] The Verizon telephone companies ("Verizon") are the affiliated local telephone companies of Verizon Communications Corp. These companies are listed in Attachment A.

these rules are no longer necessary with regard to their original purpose – to support rate of return regulation. As such, Section 11 of the Act *requires* that these obsolete rules be eliminated.

Some state commissions argue that the Commission's Part 32 accounting system and the ARMIS reports are useful to the states in carrying out their own responsibilities to regulate the rates and terms for state services and to establish state funding mechanisms for universal service. ***See, e.g.***, Wisconsin PSC, 4-7; NARUC, 5. This provides no justification for the Commission to retain a comprehensive and burdensome system of federal bookkeeping and reporting requirements. The state commissions have their own statutory authority to require carriers under their jurisdiction to keep records and report data. The Act does not appoint the Commission as the data collection agent for the states.

These states also argue that the Part 32 accounts are needed to develop rates for unbundled network elements and for the Commission's high-cost universal service model. ***See, e.g***., Maryland PSC, 3-4; Idaho PUC, 3; NASUCA, 5; ***see also*** AT&T, 3-4. However, the Commission's rules require the use of forward-looking costs for these purposes, not the embedded costs that are reflected in Part 32. In the state proceedings to establish rates for unbundled network elements, the parties have used a variety of sources to support proposed cost inputs. Although data from the ARMIS reports have been used for some of the inputs in the Commission's proxy model, such as overhead loading factors, the model does not require inputs from any particular source, and Commission has considered several alternatives for each input. Moreover, the carrier-specific data in the ARMIS reports are not necessary to run the model, which uses nationwide average data as inputs. ***See*** *Federal-State Joint Board on Universal Service*, 10th Report and Order, 14 FCC Rcd 20156 (1999), ¶¶ 30-32, 360-361. There is no schedule, or apparent need, to update the model's cost inputs, and any future revisions can be

based on inflation factors or additional cost studies using GAAP accounts. The Commission cannot justify requiring the industry to spend upwards of $20 million per year to maintain a Part 32 accounting system on an annual basis merely on the possibility that some of the data might be useful in the future to update a few of the proxy model inputs.[2] Moreover, as the state commissions continue to certify competitive local exchange carriers and wireless carriers as eligible for high cost support from the universal service fund, it becomes increasingly irrelevant to base the model's inputs solely on Part 32 accounting costs that are reported only by the incumbent local exchange carriers. GAAP accounting provides a consistent basis for examining the costs of both the incumbents and new entrants in any future updates to the model inputs.

AT&T opposes *any* streamlining of these rules, arguing (at 1-2) that the Commission cannot make a showing under Section 11 that there is "meaningful economic competition" for the incumbent local exchange carriers' services. This argument is based on AT&T's mistaken belief that "meaningful economic competition" equates to non-dominance, and that it should be determined by AT&T's "market share" analysis. There is no question, even taking AT&T's data at face value, that the incumbent local exchange carriers face meaningful economic competition for access lines. AT&T turns a blind eye to the fact that competitive local exchange carriers have established tens of thousands of collocation arrangements in the incumbent local exchange carriers' central offices, that they have established hundreds of thousands of interconnection trunks with the incumbents, that cable and satellite companies provide more broadband services to residential customers than the incumbents, and that AT&T itself competes with the incumbents in both broadband and local telephony. In the Verizon-east territory alone, Verizon has provided over 2 million unbundled loops and over 2 million interconnection trunks to competitors pursuant

[2] ***See*** Ex parte letter of Arthur Andersen, dated July 15, 1998.

to over 1,700 interconnection agreements. Given the growth in competition over the last four years under the Telecommunications Act of 1996, streamlining of the Commission's accounting and reporting rules is long overdue.

II. The Commission Should Not Adopt The State Proposals To Increase The Carriers' Accounting And Reporting Burdens.

Several state commissions support the NARUC proposal to expand the scope of the accounting and reporting rules to include 30 new revenue and cost accounts and sub-accounts in areas such as reciprocal compensation, resale, retail and wholesale services, collocation, and loop and interoffice transport. ***See, e.g***., Florida PSC, 6; Wisconsin PSC, 6-7; NASUCA, 5-6. As Verizon and other commenters demonstrated, this proposal would increase the scope and complexity of the Commission's accounting rules, and it is inconsistent with the functional nature of the Part 32 accounting system because it would require identification of revenues, expenses and investments for specific services. ***See, e.g***., Verizon, 4; USTA, 9-12. It would turn the Part 32 chart of accounts into ongoing special studies to breakdown functional accounts into the new categories. For example, loop and transport breakdowns cannot be accomplished without special studies.[3] This significant increase in the carriers' accounting burden would make a mockery of the deregulatory purpose of biennial review. As the Commission recently observed, "as part of the biennial review process, we do not intend to impose new obligations on parties in lieu of current ones, unless we are persuaded that the former are less burdensome than the latter and are necessary to protect the public interest." *2000 Biennial Regulatory Review*, CC Docket No. 00-

[3] Such a level of detail would also require proprietary treatment, as is normally given by the states in studies performed in pricing unbundled network elements.

175, Report, FCC 00-456 (rel. Jan. 17, 2001), ¶ 19. Even AT&T recognizes that "Section 11 is a purely deregulatory provision," and that it provides no authority to impose new regulations. AT&T, 8. While AT&T would apply that limitation only to the regulation of new entrants, Section 11 makes no distinction between incumbents and new entrants. It requires the Commission to eliminate unnecessary regulations, not to make them more onerous.

III. The Commission Should Adopt "Class B" Accounting For All Carriers And Adopt USTA's Streamlining Proposals.

Assuming that the Commission retains the Part 32 accounting system (which it should not), several commenters agree with Verizon that the Commission should go beyond its proposal to eliminate one-fourth of the "Class A" accounts and allow all carriers, including the large local exchange carriers, to keep their accounts at the "Class B" level of detail. ***See, e.g.***, BellSouth, 4; Qwest, 13; USTA, 4-8. They also agree that the Commission should adopt the other streamlining proposals set forth in USTA's comments. Id.; ***see also*** Cincinnati Bell, 4-7.

Contrary to the arguments of some parties (***see, e.g.***, AT&T, 3; Idaho PUC, 4) the Class A accounts serve no regulatory purpose. There is no schedule for updating the universal service proxy model's cost inputs, and doing so does not require reliance on the local exchange carriers' actual costs. To the extent that the Commission uses the carriers' costs for inputs such as overhead loading factors and expense ratios, these can be developed from Class B accounts and special studies. ***See*** USTA, 7-8. For example, the overhead factors used as inputs to the model today are taken from "subject to separations" data, which are derived from Class B accounts. ***See*** 10th Report and Order, fn. 1161. Although the state commissions argue that they need Class A data for ratemaking and universal service proceedings, they concede that the carriers maintain underlying data more detailed than the Class A accounts. ***See*** Florida, 6; Idaho PUC, 4-5;

Maryland PSC, 4. Carriers will continue to maintain the underlying detail required for business purposes to support GAAP. The Class A account requirement should be eliminated for all carriers.

The Commission also should adopt the USTA proposals to bring Part 32 more in line with GAAP accounting, and to significantly streamline the Part 32 affiliate transaction rules, the Part 64 cost allocation rules, and ARMIS, as further discussed in USTA's reply comments.

IV. Conclusion

For the foregoing reasons, the Commission should eliminate or substantially streamline its Part 32 accounting and ARMIS reporting requirements, and it should reject the NARUC proposal to add new burdens on the carriers.

Respectfully submitted,

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ATTACHMENT A

THE VERIZON TELEPHONE COMPANIES

The Verizon telephone companies are the local exchange carriers affiliated with Verizon Communications Inc. These are:

Contel of the South, Inc. d/b/a Verizon Mid-States
GTE Midwest Incorporated d/b/a Verizon Midwest
GTE Southwest Incorporated d/b/a Verizon Southwest
The Micronesian Telecommunications Corporation
Verizon California Inc.
Verizon Delaware Inc.
Verizon Florida Inc.
Verizon Hawaii Inc.
Verizon Maryland Inc.
Verizon New England Inc.
Verizon New Jersey Inc.
Verizon New York Inc.
Verizon North Inc.
Verizon Northwest Inc.
Verizon Pennsylvania Inc.
Verizon South Inc.
Verizon Virginia Inc.
Verizon Washington, DC Inc.
Verizon West Coast Inc.
Verizon West Virginia Inc.