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**Before the**
**FEDERAL COMMUNICATIONS COMMISSION**
**Washington, D.C. 20554**

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

## REPLY COMMENTS OF BELLSOUTH CORPORATION

## I. INTRODUCTION AND SUMMARY

BellSouth Corporation, on behalf of itself and its subsidiaries ("BellSouth"), hereby submits the following Reply Comments to the Comments filed on December 21, 2000 as requested by the *Notice of Proposed Rulemaking* ("*Notice*")[1] released by the Commission on October 18, 2000.

There has been a lot of discussion but very little action in the area of deregulation regarding accounting and ARMIS requirements. This is now the Commission's second biennial review of the matter as required by Section 11 of the Telecommunications Act of 1996 ("1996 Act").[2] In conjunction with these reviews, the Common Carrier Bureau ("Bureau") has asked for and received numerous proposals and suggestions of rules that could be modified or repealed in light of the current regulatory pricing structure in place for most incumbent local exchange

[1] *In the Matter of 2000 Biennial Regulatory Review -- Comprehensive Review of the Accounting Requirements and ARMIS Reporting Requirements for Incumbent Local Exchange Carriers: Phase 2 and 3*, CC Docket No. 00-199, *Notice of Proposed Rulemaking*, FCC 00-364, released October 18, 2000.

[2] *See* 47 U.S.C. § 161.

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carriers ("ILEC") and increasing competition in the local exchange and exchange access markets. Even with Congress' edict to modify or repeal regulation that is no longer in the public interest and with the proposals made by various entities, including BellSouth, to reduce unnecessary regulation, the Commission has offered only negligible regulatory relief to ILECs.[3]

The time has come for the Commission to do more than merely offer nominal modifications to the existing rules and institute meaningful changes in the current accounting and ARMIS requirements. The facts supporting such change are overwhelming. First, and most importantly, the reason most of the current rules were implemented -- to regulate rate-of-return carriers -- has gone away. Large ILECs are under a price cap with no sharing regulatory plan. Thus, subscriber rates are no longer directly tied to ILECs' accounting costs; the link between costs and rates has been broken. This alone should be sufficient for reducing a significant portion of the rules, however, this fact seems to be overlooked when the regulatory reduction orders are written. Second, competition has come to the local exchange and exchange access market. Once again, when the current rules were implemented, there was little competition in the exchange access market, which was exclusive to the business market, and no local exchange competition. Now competition exists in both local exchange and exchange access in both business and residential markets. This is evidenced by the numerous interconnection agreements ILECs have entered with competitive local exchange carriers ("CLEC") and the granting of applications by the Commission to Bell Operating Companies ("BOC") to provide long distance service in the BOC's in-region states.[4] Moreover, the Commission has given price cap ILECs

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[3] The most significant regulatory reduction has been for small and mid-sized LECs.

[4] For example, BellSouth has entered over 300 interconnection agreements with CLECs within BellSouth's region. Additionally, SBC has received authority to provide long distance

the opportunity to obtain pricing flexibility for both special and switched access services once the ILECs achieve certain designated criteria.[5] Meeting these criteria evidence the existence of well formed market mechanisms. Third, price cap ILECs and interexchange companies ("IXC") have entered into the CALLS agreement, which was approved by the Commission, to reduce access rates. Finally, pricing mechanisms for such things as unbundled network elements ("UNE") and universal service support are all based primarily on forward-looking costs and not on embedded accounting costs. Thus, even though many of the commenters repeat the banal argument that the Commission needs to continue many of the rustic accounting and reporting requirements at issue in the *Notice* in order to fulfil the Commission's other regulatory requirements, such argument simply clings to the vestiges of regulation for regulation's sake.

Accordingly, given the above facts and the requirements of Section 11, the Commission should adopt the proposals made by the United States Telecom Association ("USTA") in its June 6, 2000 *ex parte* and in USTA's comments filed in this proceeding. As BellSouth stated in its comments, these proposals are the result of a painstaking analysis performed by USTA's members, including BellSouth, to determine regulations that no longer serve any meaningful purpose and should therefore be eliminated. BellSouth fully supports the positions of USTA and has worked closely with USTA and its members in preparing responses for the reply comments filed by USTA. Therefore, BellSouth supports the reply comments of USTA and provides the following specific comments.

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service in Texas, Kansas, and Oklahoma. Verizon has received authority to provide long distance service in New York.

[5] BellSouth has received pricing flexibility for special access and dedicated transport services in up to 39 Metropolitan Statistical Areas ("MSA").

## II. ACCOUNTING REQUIREMENTS

BellSouth believes that the Commission should have as its ultimate goal to allow all ILECs to move to generally accepted accounting principles ("GAAP") for regulatory accounting and reporting purposes. As BellSouth stated in its comments a significant step toward GAAP would be to allow ILECs to adopt a Class B account structure. Of course, GAAP does not require any specific account structure. GAAP allows companies the flexibility to set up the account structure that the company feels is necessary to effectively operate its business and provide adequate disclosures to financial regulatory agencies such as the Securities and Exchange Commission ("SEC"). Indeed, even if BellSouth was allowed to set up its own set of accounts it would still capture and record the information that it needs to effectively operate the business. This information would in all likelihood very much resemble the information that BellSouth currently captures and records today. BellSouth contends that the Commission could request whatever information it may need for its oversight duties and that BellSouth would be able to provide such information pursuant to the information that BellSouth captures and maintains for its internal needs.

Nothing in any of the comments provide adequate reasons for requiring ILECs to use the Class A account structure. Most of the arguments focused on the need to maintain Class A accounts for UNE pricing issues, universal service support, and cost allocation. None of these are valid, however. As USTA discusses in detail in its reply comments, UNE pricing and universal service support are based on forward-looking costs and not on historical cost data.[6]

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[6] The United States Supreme Court has recently accepted Writ of Certiorari in *Iowa Utilities Board* in which one of the issues addresses whether historical costs should be used for pricing network elements instead of using only long run incremental costs. *Iowa Utilities Board, et al., v. FCC*, 219 F.3d 744 (8th Cir. 2000), *cert. granted sub nom., Verizon Communications,*

Class A accounts are not needed to make these calculations. Moreover, under Class B, ILECs would be able to continue to directly assign costs that were previously directly assigned and would continue to maintain sufficient detail necessary to allocate common costs. Thus, Class A accounts are not needed for Part 64 cost allocation.

The Class B account structure would allow ILECs more flexibility[7] in how they capture and report information necessary for management to operate the business than is currently allowed under a Class A structure. Moving to Class B would permit the Commission to see that all of the information that it may need from carriers will continue to be maintained and will be retrievable under this more flexible and less burdensome set of accounts and corresponding rules. BellSouth is confident that this experience will ready the Commission for allowing ILECs to move completely to GAAP for establishing their accounting and reporting structures.

In addition to adopting Class B accounts, the Commission should also immediately adopt USTA's proposals regarding affiliate transactions. Under price cap regulation, where an ILEC cannot manipulate subscriber rates by increasing its costs through inflated transactions with affiliates, the affiliate transaction rules are beyond understanding.[8] They are extremely

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*Inc. v. FCC*, 69 U.S.L.W. 3269 (U.S. Jan. 22, 2001) (No. 00-511). While there is no way of predicting how the Court will rule, even if it found that historical costs should be used for such calculations, however, the Class A account structure would not be needed. UNE and universal service cost studies would be highly scrutinized independent of the accounting requirements; and the information that could best support the cost studies could well have a different cost categorization. This is especially true considering that Class A accounts were designed long before UNE and universal services costs studies and therefore were not established for that purpose.

[7] The flexibility that the Class B account structure provides is not merely the reduction in the number of accounts but also the reduction in the rules associated with each of the accounts. Indeed, maintaining the actual chart of accounts provided by Part 32, both Class A and Class B, is not the burdensome part of the rules. It is requirements that the rules prescribe for each account that make Part 32 so burdensome.

[8] Indeed, the *Joint Cost Order* specifically stated that "[t]ransactions between communications common carriers and their nonregulated affiliates have always been subject to

burdensome and add unnecessary costs that the ILECs' competitors do not have to endure. Moreover, they greatly hinder the way ILECs have to do business. For example, before a transaction can take place between the ILEC and an affiliate, analysis must be performed to make sure that the affiliate has the proper accounting structure in place to capture fully distributed costs. Additionally, unless the service has sales to third parties that exceed 50%[9] or the amount of the service does not exceed the $500,000 threshold, a fair market valuation must be performed for the service. The fair market valuation is extremely burdensome and costly. In some cases the transaction with the affiliate is abandoned, even though it would create efficiencies for the company, because of the complexities and costs of complying with the affiliate transaction rules. Once again, BellSouth urges the Commission to move to GAAP for all accounting and reporting purposes, but in the mean time BellSouth supports USTA's proposals for streamlining the current affiliate transaction rules.

## III. ARMIS REPORTING

Section 11 of the 1996 Act could not be more clear: the Commission must (1) review all regulations issued under the 1934 Telecommunications Act, as amended by the 1996 Act; (2) determine if any such regulation is no longer necessary in the public interest as the result of

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scrutiny in *rate cases*. This is due to the possibility that, in a non-arm's-length transaction, an affiliate may charge an excessively high price to the carrier. *Since such prices become part of the costs and rate base of the carrier*, they can lead to unreasonably high rates." *In the Matter of Separation of costs of regulated telephone service from costs of nonregulated activities, Amendment of Part 31, the Uniform System of Accounts for Class A and Class B Telephone Companies to provide for nonregulated activities and to provide for transactions between telephone companies and their affiliates*, CC Docket No. 86-111, *Report and Order*, 2 FCC Rcd 1298, 1301 (1987) ("*Joint Cost Order*") (emphasis added). This reasoning is clearly removed under price regulation.

[9] BellSouth fully supports USTA's proposal to lower the sales percentage to 25%, or in the alternative to adopt the states' proposal to allow sales to third parties and non-ILEC affiliates to meet the 50% threshold.

meaningful competition; and (3) modify or repeal any regulation the Commission determines is no longer in the public interest. ARMIS reports 43-01 through 43-04 and 43-07 and 43-08 are all reports that are outdated, no longer in the public interest and therefore should be eliminated. Some commenters stated that there is no meaningful competition and the Commission therefore should not eliminate or streamline these reports.[10] This is simply untrue. As BellSouth stated previously, it has entered into more than 300 interconnection contracts with CLECs. Additionally, the Commission has approved two BOC's applications to provide long distance in four states. The Commission has also approved BellSouth's petition for pricing flexibility for special access and dedicated transport services in up to 39 of its MSAs. Accordingly, competition is alive and well in the local and exchange access markets.[11] Given this competition, the Commission should follow the requirements of Section 11 and repeal the rules requiring the filing of these ARMIS reports.

Other commenters not only want the current ARMIS reports to continue but urge the Commission to add sections increasing the amount of information that must be reported, specifically in the broadband market.[12] The Commission must reject these requests for two reasons. First, ILECs do not have a dominant position in the broadband market. In fact, broadband deployment is much greater over cable than it is over phone lines. In addition,

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10 *See, e.g.*, AT&T at 1 and NARUC at 4.

11 The Commission has specifically stated that it does not limit its Section 11 reviews "to whether meaningful economic competition alone justified changes, but instead looked for any justification to modify or eliminate a rule which would serve the public interest. [The Commission's] biennial reviews, thus, go beyond the minimal statutory requirements of examining our rules pertaining to telecommunications service providers or broadcast ownership that are no longer necessary as a result of meaningful economic competition." Thus, even if meaningful economic competition did not exist, other changes, e.g., price cap regulation, justify eliminating the ARMIS reporting and other accounting requirements.

12 NARUC at 6, Florida PSC at 11-2, and Wisconsin PSC at 18.

multiple CLECs provide broadband service over phone lines. Thus, it is completely unreasonable to require large ILECs, in a nascent market, to report competitive information but not require ILECs' competitors to report the same information. Second, as BellSouth stated in its comments, it is axiomatic that Congress did not intend for the Commission to increase regulation pursuant to a Section 11 biennial review. Accordingly, even if the requests were valid, which they are not, this is clearly not the forum for such requests.

Finally, some states indicate that the Commission should continue the reporting requirements for state informational needs such as to monitor and investigate ILEC activities. This reason is also invalid for continuing the ARMIS reporting. If the Commission needs information for an enforcement proceeding or has other bona fide needs for information, it can authorize data requests from that particular carrier. This is much more efficient than burdening an entire group of carriers with reporting requirements in the event that information may be needed in the future. These efficiencies will benefit the Commission staff as well as the ILECs.

## IV. CONCLUSION

The Commission has ample reasons to eliminate much of the accounting and ARMIS regulation that now exists for ILECs. As the comments have shown, these regulations are no longer necessary in an industry where not only are these ILECs regulated by price cap regulation,

they also face strong competition in practically all of their lines of business. The Commission should therefore follow Section 11 of the 1996 Act and modify or repeal many of these rules by adopting the proposals made by USTA.

Respectfully submitted,

**BELLSOUTH CORPORATION**

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Date: January 30, 2001

## CERTIFICATE OF SERVICE

I do hereby certify that I have this 30th day of January 2001 served the following parties to this action with a copy of the foregoing **REPLY COMMENTS OF BELLSOUTH CORPORATION** by electronic filing, or by placing a copy of same in the United States Mail, addressed to the parties listed on the attached service list.

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