

**Before the
Federal Communications Commission
Washington, D.C. 20554**

In the Matter of)
)
Jurisdictional Separations)
and Referral to the Federal-) CC Docket No. 80-286
State Joint Board)

COMMENTS OF THE IRREGULATORS

And Re:

- *Federal-State Joint Board on Universal Service, CC Docket No. 96-45 and 97-21;*
- *Special Access for Price Cap Local Exchange Carriers, WC Docket. No.05-25;*
- *AT&T Corporation Petition/or Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates/or Interstate Special Access Services, RM-10593;*
- *Connect America Fund, WC Docket No. 10-90;*
- *AT&T Petition to Launch a Proceeding Concerning the TDM-to-IP Transition, GN Docket No. 12-353;*
- *Technology Transitions, GN Docket No. 13-5;*
- *Inquiry Concerning the Deployment of Advanced Telecommunications Capability to All Americans in a Reasonable and Timely Fashion, and Possible Steps to Accelerate Such Deployment Pursuant to Section 706 of the Telecom Act of 1996, as Amended by the Broadband Data Improvement Act, GN Docket No. 15-191;*
- *Policies and Rules Governing the Retirement of Copper Loops by Incumbent Local Exchange Carriers, RM-11358;*

And Re:

- *Investigation of Certain Price Cap Local Exchange Carrier Business Data Services Tariff Pricing Plans, WC Dkt. No. 15-247;*
- *Protecting and Promoting the Open Internet, GN Docket No. 14-28;*
- *City of Wilson, North Carolina Petition for Preemption of North Carolina General Statute Sections 160A-340 et seq., WC Docket No. 14-115;*
- *The Electric Power Board of Chattanooga, Tennessee Petition for Preemption of a Portion of Tennessee Code Annotated Section 7-52-601, WC Docket No 14-116;*
- *Petition of Granite Telecommunications, LLC for Declaratory Ruling Regarding the Separation, Combination, and Commingling of Section 271 Unbundled Network Elements, WC Docket No. 15-114;*
- *Lifeline and Link Up Reform and Modernization, WC Docket No. 11-42;*
- *Telecommunications Carriers Eligible for Universal Service Support, WC Docket No. 09-197;*

- *Amendments to Part 4 of the Commission's Rules Concerning Disruptions to Communications*, PS Docket No. 15-80 and ET Docket No. 04-35;
- *Implementation of Section 224 of the Act, WC Docket No. 07-245 and National Broadband Plan for Our Future*, GN Docket No. 09-51;

And Re:

- *Computer III Further Remand Proceedings: Bell Operating Company Provision of Enhanced Services; 1998 Biennial Regulatory Review – Review of Computer III and ONA Safeguards and Requirements*, CC Docket Nos. 95-20, 98-10;
- *2000 Biennial Regulatory Review Separate Affiliate Requirements of Section 64.1903 of the Commission's Rules*, CC Docket No. 00-175;
- *Notice of Inquiry Concerning a Review of the Equal Access and Nondiscrimination Petition of BellSouth Telecommunications, Inc. for Forbearance Under 47 U.S.C. § 160 from Enforcement of Certain of the Commission's Cost Assignment Rules*, WC Docket No. 05-342;
- *Petition of AT&T Inc. for Forbearance Under 47 U.S.C. § 160 (Petition of Qwest Corporation for Forbearance from Enforcement of the Commission's ARMIS and 492A Reporting Requirements Under 47 U.S.C. § 160 (Petition of Verizon for Forbearance, 47 U.S.C. § 160 (Service Quality, Customer Satisfaction, Infrastructure and Operating Data Gathering*, WC Docket No. 08-190;
- *Petition of United States Telecom Association for Waiver from Application of the Equal Access Scripting Requirement*, WC Docket No. 08-225;
- *Petition of Cincinnati Bell Telephone Company LLC for Waiver from Application of the Equal Access Scripting Requirement*, WC Docket No. 09-206;
- *Review of Wireline Competition Bureau Data Practices*, WC Docket No. 10-132;
- *Petition of US Telecom for Forbearance Under 47 U.S.C. § 160 (Certain Legacy Telecommunications Regulations*, WC Docket No. 12-61;

Dear Ms. Dortch:

The IRREGULATORS hereby submits, for inclusion in each of the above-captioned dockets, the attached documents:

Bruce Kushnick
Paul Hartman
Tom Allibone
Fred Goldstein
Kenneth Levy, Esq
David Bergmann, Esq
W. Scott McCollough
Chuck Sherwood
Dana Spiegel
Joe Plotkin

April 17th, 2017

IRREGULATOR Team

In April 2017, a new group called the “IRREGULATORS” was formed¹. The core of the IRREGULATORS is an independent consortium of retired and semi-retired telecom experts, analysts, policy wonks, forensic auditors, and lawyers who are former senior staffers from the FCC, state advocate and Attorneys General Office experts and lawyers, as well as former telco staff and consultants. Members of the group have been working together, in different configurations, since 1999.

Some of the following documents and comments were submitted by New Networks Institute. Established in 1992, NNI has been a consortium of independent communications-focused experts, analysts, auditors and lawyers over the last 5 years.²

16 Years of Extensions

The FCC has requested yet another extension in Docket 80-186,³ this time for 18 months, to examine the cost allocation rules that are applied to revenues and expenses of AT&T, Verizon and Centurylink’s state utilities, which they control.⁴

At the same time, at a meeting scheduled for April 20th, 2017, the FCC is steam-rolling and is doing a hatchet job on a series of upcoming proposals that will be discussed. From Broadband Data Services, (BDS), to the shutting off the copper networks, or the IP Transition, the FCC plans are to gut all customer protections, block competition, and harm all businesses that rely on these data services, among other harms.

How can the agency, then, attempt to shut down and delay examination of the accounting rules that are directly tied to these other items?

Our Conclusions

- The FCC must audit the financial accounting books of the incumbent state utilities immediately and stop all proceedings until it actually does the proper analysis of Business Data Services, (formerly called “Special Access” services), revenues and profits, as well as the treatment of the copper utility networks, or the financial impacts of the IP Transition.

¹ <http://irregulators.org/> For more information and a brief bio of the signatories

² See: <http://newnetworks.com/>

³ <https://www.federalregister.gov/documents/2017/04/03/2017-06532/jurisdictional-separations-and-referral-to-the-federal-state-joint-board>

⁴ NOTE: The state utilities include all of the copper and fiber optic wires that are part of the “PSTN”, the Public Switched Telephone Networks, and include all of the wires for “Special Access” (non-switched) and all of the copper wires being shut off, or ‘transitioned’. This fact is never even mentioned in any of the FCC’s proposed new regulations.

- We object to the extension on the grounds that it is being done as a cover-up so that actual financial data is excluded from the FCC rulemaking process.
- The FCC has been negligent in examining the harms that its Big Freeze has caused for over a decade, and it is clear it will continue to do so by allowing this extension to go forward.
- We call for an investigation into the FCC's processes by the Inspector General's Office as it is clear that there was no mention of our letter, the reports or other related filings that detailed the harms of the FCC's Big Freeze.⁵
- **On December 16th, 2015 New Networks Institute Filed a Letter and Two Reports in the Aforementioned Dockets at the FCC, as well as this proceeding CC Docket 80-286.**

NNI previous filed these reports:

- **Report 1: Verizon's Manipulated Financial Accounting & the FCC's "Big Freeze"**
- **Report 2: Data Report on Verizon New York's Financial Accounting**

We wrote:

"Summary:

"The reports detail Verizon New York's ongoing cross-subsidization⁶ of its lesser-regulated subsidiaries' use of its wireline, mostly POTS, Plain Old Telephone Service, copper-based network, (sometimes referred to as the 'PSTN', 'Public Switched Telephone Networks'). The reports show how this abuse of Verizon's (ILEC)⁷ telephone customers was abetted by the FCC's freeze of jurisdictional separations factors, beginning in 2001, where the FCC 'froze' the calculations of expenses, from network costs to corporate operations and advertising, to be based on the year 2000.⁸

⁵ <https://www.fcc.gov/inspector-general>

⁶ There is much confusion in, and over-use of, the term "subsidy" in telecommunications discussions, even by the FCC. See Faulhaber, G., "Cross Subsidization: Pricing in Public Enterprises," American Economic Review, Vol. 65, No. 5 (Dec. 1975), at 966-977; see also 2002 update, <http://assets.wharton.upenn.edu/~faulhabe/cross%20subsidy%20analysis.pdf>. "Cross-subsidy," as used here, includes the unfair allocation of network (joint and common) costs, as alleged for Verizon in a 2014 NNI paper, "It's All Interconnected" (<http://newnetworks.com/wp-content/uploads/PublicNN3.pdf>).

⁷ ILEC, Incumbent local exchange company, is the term used to connote the state-based utility phone companies, who control the critical, wired communications infrastructure.

⁸ **NOTE:** We focus on Verizon New York because New York State has maintained a requirement that the incumbent telecommunications utilities, in this case Verizon New York, supply an extensive financial annual report based on the Uniform System of Accounts (USOA). This financial accounting information is identical to the data that had been collected by the FCC as part of the "**Automated Reporting Management Information System (ARMIS)**" data, provided in the FCC's *Statistics of Common Carriers* ("SOCC").

“This Freeze has allowed Verizon and others to create a manipulated, financial fiction—that the local service communications networks are unprofitable. In fact, our findings reveal that Verizon’s affiliate transactions a) charge local service a disproportionate amount of every expense; b) do not allocate a fair share of common costs to the subsidiaries, affiliates and their other lines of business; c) many of the affiliates’ products and services are not paying tariff or market-based prices to Verizon New York, thus artificially and improperly lowering regulated revenues; with the result that d) these affiliate transactions lead to local service (and the ratepayers) ‘funding’ these non-core lines of business with the result that Verizon New York improperly and inaccurately “reports” massive financial losses in New York State.

“These and other regulatory and accounting manipulations allowed Verizon New York to claim that all fiber optic deployments are being done as part of the “Title II”, common carrier, incumbent utility operations; and that the fiber deployment is an enhancement to the existing, telecommunications service network. Verizon’s FiOS services use Title II, common carriage, fiber optic wires, as do the services used by wireless carriers that go to the cell towers. But neither FiOS nor Verizon Wireless operations actually pay Verizon New York prices equal to those paid by unaffiliated carriers and providers for the same services. The affiliates get a discount funded by basic service ratepayers that is not available to competitors. These massive affiliate transaction-based cross-subsidies between regulated and lesser-regulated activities unfairly burden Verizon New York ratepayers and competitively harm those who seek to compete with FiOS and Verizon Wireless.

“These machinations also demonstrate that Verizon has been able to ‘vertically integrate’ its products and services at the expense of all other competitors. And this is at the expense of all customers, because Verizon has inflated all prices to end users and competitors, but most of all local phone service. In New York, Verizon was able to get multiple rate increases for basic service – 84% – starting in 2006, based on the claim of artificial ‘losses’ that were not actually or fairly attributable to actual expenses or investment incurred in offering the mostly copper-based basic service to ratepayers.”

- **What is the FCC Hiding? Massive Financial Cross Subsidies and Data Manipulation Were Caused by the FCC’s Own Accounting Rules –“The Big Freeze”.**

Another report, “**Verizon Massachusetts & Boston: Investigate the Wireless-Wireline Bait-n-Switch**” published in January 2017, found identical financial cross subsidies and harms caused by the FCC’s Big Freeze.⁹

EXAMPLE: This financial excerpt is taken directly from the Verizon Massachusetts financial accounting for the year 2014. It shows that Local Service has paid the majority of all expenses and cross-subsidized all of the other lines of business, including construction budgets.

Verizon MA Financial Report Excerpt, Local Service Expenses, 2014

2014	Local Service Expenses	% of Total	Overcharged
Network Costs (Plant)	\$296,502,378	43%	(\$134,802,513)
Customer Service	\$165,106,720	68%	(\$108,159,547)
Corporate Operations	\$557,934,103	60%	(\$341,196,688)
Marketing	\$61,149,078	53%	(\$33,883,136)
Total Overcharge (specific items)			(\$618,041,884)
Expenses	\$1,080,692,279		
Local Service Revenues	\$476,909,000	23%	
Local Service Losses	\$603,783,279		
Total Verizon MA Losses	\$(814,449,000)		

- **Paid 60% of All “Corporate Operations” Expense** — At \$558 million, this is \$81 million—119%— more than the revenues. Corporate Operations includes lawyers, lobbying, executive pay, and even the corporate jets - all aimed at pushing Verizon’s agenda nationwide.
- **Paid 53% of All “Marketing”**— When is the last time you saw a Verizon advertisement for basic phone service?
- **Paid 43% of All “Network (Plant)” Costs** — even though the company stopped upgrading most of the copper-based Local Service networks.
- **Verizon Local Service Expenses Were Over \$1 Billion in Just 2014** — yet it is all a manipulated financial accounting scheme. Local Service shows claimed losses (of just these specific major expenses) of \$604 million on \$1.1 billion in expenses
- **Verizon Massachusetts Showed Overall Losses of \$814 Million for 2014** — Because of all of the manipulation of accounting, Verizon MA, overall, has been

⁹ <http://newnetworks.com/verizonmareport/>

showing losses in most years. In fact, Verizon MA paid no income taxes and had multiple tax benefits from these losses.

In short, Verizon Massachusetts' financials shows that Local Service was overcharged over \$600 million dollars in just 2014. There should be no marketing costs and little or no network costs, as most of the copper wires are not being upgraded or maintained. And charging Local Service excessive Corporate Operations expenses would not have been allowed if there was oversight by the state regulators.

- **How did this Happen? The FCC's Big Freeze — 16 Years of Regulatory Neglect**

This is happening in every state and the impacts are caused by the FCC's "freeze" on accounting rules that were set in the year 2001. While there are multiple questionable acts, at the core, the fact is that the losses of Verizon MA were created, in large part, by the FCC, which sets the rules about the incumbent phone companies' accounting.

Simply put:

In 2001, the FCC "froze" the calculations of expenses that are used in every state based on the year 2000 — and this freeze has continued through the year 2017. And now the FCC, instead of auditing the financial books and investigating the cross-subsidies, (which we have been filing about for the last 5+ years) wants to punt for another one and a half years.

- **Verizon New York's Corporate Operations Expense Charges to Local Service Via the FCC's Big Freeze**

Returning to the Verizon New York financials in our previous report, the Freeze can best be seen by this detail of Corporate Operations expense of Verizon New York, the state utility, from 2003-2014

Corporate Operations expense is a massive garbage pail fund of corporate expenses (mostly the parent holding company) from executive pay and the corporate jets to the lawyers and lobbyists defending Verizon's position.¹⁰

¹⁰ http://www.huffingtonpost.com/bruce-kushnick/did-rate-increases-on-ver_b_8029032.html

Verizon NY Local Service Revenues and Corporate Operations Expense, 2003-2014

	Expenses	Revenues
2003	65.00%	65.30%
2009	60.70%	49.00%
2010	60.80%	44.10%
2011	60.80%	39.40%
2012	60.70%	34.90%
2014	60.40%	27.60%

Sources: Verizon NY, New Networks Institute

In 2003, then, expense allocations were based on revenues, but the “FREEZE” froze the percentage of expenses for the year 2001. However, this also meant that the other lines of business paid a fraction of what they should have been paying.

From 2003 through 2014, Verizon NY, the state utility, had Local Service pay about 60% of all Corporate Operations expenses, even though the revenue of Local Service went from 65% to 27.6%. By 2014 this caused Local Service to pay 119% of revenues, causing losses.

- **The Big Freeze Impacts on Special Access: A Mockery of the Principles of a Utility and Public Obligations.**

Corporate Operations expense is only one area where the Big Freeze slapped the local phone customers in the financial face. Specific parts of the state networks have been deemed “interstate” and profitable, such as “Special Access”, as they aren’t paying their fair share of the expenses, while the local networks have been allowed to deteriorate. And this is not simple conjecture but based on publicly available data, such as Verizon NY’s financial reports or the current ongoing investigation of Verizon New York by the NY State Public Service Commission.

Also interstate special access (private line) costs as a result of NYNEX’s interpretation of the separations freeze were not updated annually despite the clear language in § 36.3(a)

“Direct assignment of private line service costs between jurisdictions shall be updated annually. Other direct assignment of investment, expenses, revenues or taxes between jurisdictions shall be updated annually.”

Despite the exponential growth in interstate special access services and therefore interstate special access revenues there was not the expected increase in interstate special access costs per the rules. Instead the interstate private line (special access) cost categorization % was not updated per the rules. This effectively had the majority of interstate private line (special access) costs remain in the intrastate jurisdiction ala 2000.

- **Verizon New York’s 2015 Annual Report Shows the Big Freeze Financial Manipulation of the Construction Expenses, Making Special Access Extremely Profitable.**

As mentioned, Local Service revenues are mostly from the copper-based “POTS”, “Plain Old Telephone Service”, lines. Verizon has stated it is no longer upgrading and maintaining these lines, the retail copper lines.

Then how can Local Service be paying the majority of network expenses? And how can Special Access services have a 66% EBITDA, (Earnings Before Interest, Taxes, Depreciation and Amortization), for mostly copper-based services while the same exact wires have massive losses?

According to Verizon NY’s 2015 annual report, Local Service brought in \$1.3 billion and had an EBITDA of -132%. This is in contrast to Special Access fees, which were \$2.5 billion in revenue and had an EBITDA of 66%. (Special Access was \$2 billion and represents 80%+ of the total.)

Verizon New York Local Service and Access Revenues and Expenses, 2015

Operating Revenues	Local Service	Access Service
(Special Access)		\$2,008,589,749
Total Operating Revenues	\$1,314,760,587	\$2,508,453,620
Operating Expenses		
Plant Specific & Non-Specific	\$1,470,969,520	\$716,168,027
Subtotal	\$1,731,367,648	\$ 843,549,033
EBITDA	-132%	66%

Sources: Verizon New York 2015, New Networks Institute

One would say that ‘Local Service’ was losing money until one examines the network costs (“Plant Specific and Non-Plant Specific”) and notices that Local Service paid \$1.47 billion, which is in contrast to Special Access services only paying \$716 million, literally half of what Local Service paid. i.e., Local Service paid 117% of its revenue while Special Access paid 29% of its revenue.

These financial analyses are based entirely on Verizon’s financial annual reports and the findings directly impact not just the big freeze but every upcoming FCC decision.

Because of the FCC’s negligence in examining the Big Freeze:

- Special Access of Verizon has obscene profits, and is not paying its fair share of the expenses.

- Local phone customers have been overcharged thousands of dollars to pay for the expenses of Special Access and Verizon's other services.
 - If Local Service customers are paying the capital expenditures, then the all of the FCC and phone companies special access models, not to mention all of the paid 'experts' are wrong as none of them bothered to use actual available financial information.
 - Verizon NY's financial Annual Reports are public and available, so there is no excuse to create meaningless mathematical models. However, it appears that virtually all of the phone companies and their paid analysts fall into the same trap. These financial excerpts from the actual incumbent phone companies, shows that Verizon's special access services are NOT paying what a mathematical model claims; i.e., the construction expenses in the model are not being paid by the incumbent's actual service, but are paid, in large part, by local phone customers.
-
- **The Hartman Memorandum Rips Apart the FCC's Proposed New Regulations Pertaining to The IP Transition, Shutting Off the Copper Networks and Special Access**

In November 2016, we created two new reports which are direct hits to the FCC's Big Freeze harms, including a history to educate the public and the FCC as it appears that the agency has never examined the details of their own rules for over a decade+.

We filed these reports with a cover letter, with the FCC on November 3rd, 2016 in:

- Re: Business Data Services in an Internet Protocol Environment, WC Docket No. 16-143; Special Access Rates for Price Cap Local Exchange Carriers, WC Docket No. 05-25 and RM-10593
- **The Hartman Memorandum.**¹¹
- **The History & Rules of Setting Phone Rates in America —The FCC's 'Big Freeze' & Cross Subsidies** — which supplies a history of the FCC and state rules discussed herein.¹²

We wrote:

“Declaration

“The FCC has not examined the massive cross subsidies created by the FCC's own malformed and distorted cost allocation rules.

¹¹ <http://newnetworks.com/hartmanmemorandum/>

¹² <http://newnetworks.com/hartmanhistory/>

“This includes the fundamental cross subsidy—that 75% of most network costs are paid by the local services (intrastate) while only 25% are paid by ‘interstate’ services, such as special access, recently renamed ‘Business Data Services’. Worse, another set of rules created in 2001, requires the allocation of expenses to represent the year 2000—16 years ago, which has little to do with the connected, digital world of 2016.¹³

“‘Special access’ are not special services but a fabricated regulatory classification that takes a wire from the state utility and claims it is no longer an ‘intrastate’ service (which are services within the state controlled by the state commission), but are ‘interstate’ services, which are for business data and broadband, and they are controlled by the FCC; same exact wire, however.

“The FCC claims that it can determine pricing that will be just and reasonable.

Two Items Stand Out:

- **“75%-25% Rule** — 75% of all message loop costs are allocated to the intrastate jurisdiction and 25% of all message loop costs are allocated to the interstate jurisdiction. Because message loop costs are the largest portion of the network, the intrastate jurisdiction is allocated the majority of overall network costs. Because local service is the largest portion of the intrastate jurisdiction and the desire of regulators to mirror interstate access rates, most of the intrastate network expenses are paid by the Local Service phone networks. This rule was created in 1984 and has not been adjusted or replaced for 32 years.
- **“Cost Allocation Rules” Were Set Based on the Year 2000** — In 2001, the FCC created a series of rules pertaining to the allocation of expenses to match the year 2000—16 years ago. In 2001, Local Service was about 65% of revenues and it paid 65% of costs. In 2015, Verizon New York's Local Service revenues were 25% but it still paid 61.2% of all corporate operations expense. Access services, which had

¹³ We note that there are a host of caveats as different rules and calculations applied to different parts of the regulated networks. On top of this, the big freeze was applied to other expense areas, such as corporate operations or marketing. Moreover, the cross subsidies created by the rules allowed the affiliate subsidiaries to have different beneficial financial arrangements where they pay fractions of the market prices charged to competitors for use of the network or paid a fraction of the actual construction expenses used by Verizon Wireless for fiber optic build outs to the cell sites.

47% of revenues only paid 28.6% of the corporate operations expenses.¹⁴

And the FCC's Big Freeze caused a myriad of problems which the FCC has never investigated.

- **This Distortion of the Accounting has had Multiple, Direct and Harmful Impacts on All Services** — Special access had a 66% “Earnings Before Interest Taxes Depreciation and Amortization”, (EBITDA) -- because it paid only a fraction of expenses while Local Service paid the majority. In fact, all of the 'interstate' broadband networks, including the wires to the cell sites for Verizon Wireless or even FiOS TV, all paid fractions of the expenses and thus have very high profit margins.
- **Direct Harms to All Wired Services** — Unfortunately, interstate special access cannot be examined without looking at all of the other lines of business, from local service to the implications of massive cross subsidies that were designed and helped to create harmful public policies. At the same time, these expenses made the local phone networks artificially unprofitable, which as been used as an excuse to 'shut off the copper' or force customers onto 'more profitable' wireless services. This has also been an excuse for not building out FiOS broadband to many areas throughout the East Coast.
- **The FCC's Proposed Rules Do Not Address Cross Subsidies** — The proposal does not fix the excessive profit margins nor examine that the FCC's rule making doesn't include the fact that local phone customers have been overcharged, having paid the excess profits. Moreover, the agency has never addressed the fact that these wires are part of the state utility as they are classified as Title II, and that the expenses paid are mostly 'intrastate' where the FCC does not have jurisdiction.
- **The FCC's Plan Also Includes a Host of Proposed Actions that Will Cause Multiple Harms** — For example, the FCC plans do not require the incumbents to share any new build-out of fiber optic special access services with high speeds with competitors, even though the majority of the expenses were paid for by local service under the FCC's own rules, or rate increases agreed to by the state commissions.
- **Harm to Broadband and Internet Competition** — Much of the incumbent's retail business is in Internet access now, including DSL and FiOS and they are classified as interstate. In fact, anything that carries Internet is interstate. Thus, all of the growth areas, including

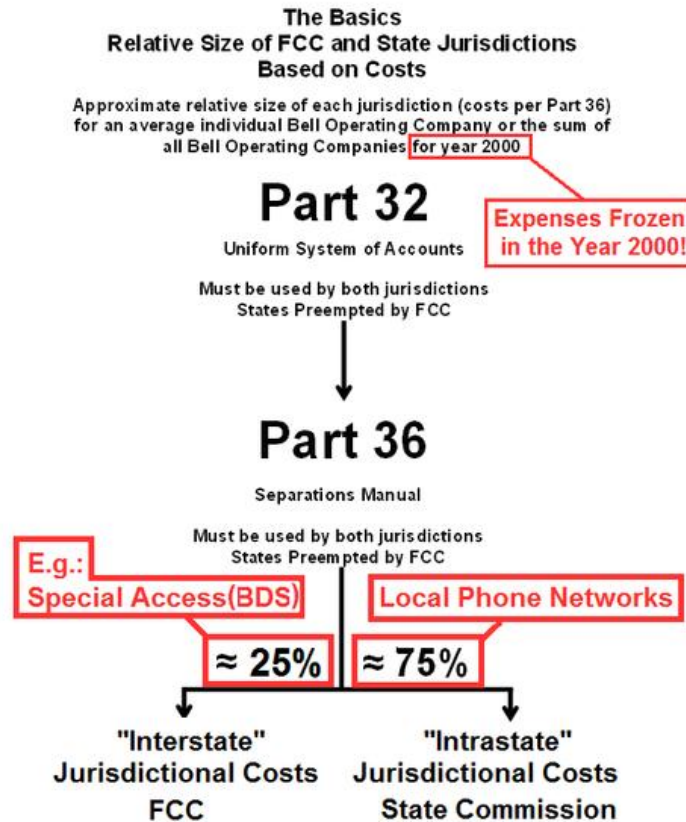
¹⁴ This Memorandum only focuses on Local Service and Access Services, and does not go into detail about the other revenue and expense areas for “Nonregulated”, “Black Hole” revenues, or revenues and expenses for affiliate companies, from Verizon Online to Verizon Wireless.

competitive ones, are in the interstate basket, which is not paying its fair share. This also makes it easier for the ILECs to undercut "broadband" competition.

- **Harms to Users and Municipalities** — As we discuss, Consumer Federation of America found over \$75 billion in special access customer overcharging in just the last five years. Moreover, these financial distortions diverted monies to the affiliate companies, such as Verizon Wireless, that should have gone to upgrade and maintain communities' network infrastructure for broadband and internet services.
- **The Cost Allocation Regulations have been Erased But Are Still in Use** — There are those who, as a knee-jerk reaction, will say that the rules have been 'forebeared' – i.e., while the rules are still on the books they are no longer required. Unfortunately, the Verizon New York annual reports and matching reports from Massachusetts prove that the rules are still in use. But it also exposes that the price caps did not work¹⁵
- **The Primary Data**—Verizon New York has been required to file detailed annual reports through 2015. But we have obtained other financial data from other Verizon states, as well as corporate financial transcripts, state filings, FCC filings, and even press releases covering all Verizon states. We also used FCC ARMIS data through 2007 to show that the same financial rules have been and continue to be applied in all AT&T and CenturyLink states.

The Hartman Memorandum proves that the FCC can never create just and reasonable pricing for Broadband Data Services because the FCC's own cost allocation rules created massive financial cross subsidies between and among the state-based wired utilities, and the companies' other lines of business, such as special access, or the wireless service.

¹⁵ Price caps allow for the company to keep the price of a service at a fixed rate, or incrementally increase based on some factor, like inflation, while the company's profits are not examined. This document proves that price caps failed to keep basic prices 'just and reasonable' as special access has excessive profits. Moreover, without serious accountability or enforcement, price caps are just another means for the company to make more profits, without fulfilling the commitments that got the company this financial largesse.



How it Works: (See the Report for full detail.)

In order to make sure that the different lines of business paid their fair share to use the networks, a system was created so that both state and federal regulators were on the same page:

- **Uniform System of Accounts (USOA) (also called “Part 32”)** was created. It itemized the tens of thousands of expenses, revenues, taxes, and put them into a database/catalog with hundreds of separate categories.
- **Separations Manual (Part 36)** was created to be able to allocate these expenses to the different lines of business.

Local ‘POTS’ or plain old telephone service would be listed in specific revenue categories using the USOA and the expenses would be charged based on the Separations Manual. Originally, the expenses were based mostly on revenues (with caveats).

And in one of the first acts to erase all obligations, in 2017 the FCC has erased the Part 32 obligations, claiming it is just too burdensome for companies to deal with.

- **75-25% Rule Allocates Costs to Local Service vs “Interstate”**

And as mentioned, previously, but worth repeating, around 1984 the Separations Joint Board recommended and the FCC ruled that the ‘interstate’ portion would only pay 25% of expenses for a majority of the network costs (message loop) —Intrastate would pay 75% of these expenses associated with such loop investments as Cable and Wire Facilities.

This means that on top of the failed cost allocations, a second whammy is in place: Local phone service (the majority of “Intrastate”, would pay the majority of the capital expenditures.

This rule was created in 1984 and has not been adjusted or replaced for 32 years despite the increase of fiber in the loop, which was NOT placed to benefit the local service customer but rather to benefit advanced services. Per the cost causer philosophy of the FCC, local service customers should only be paying incremental costs for fiber in the loop

- **Timeline: 16 Years of Extensions with Even the Same Wording**

We collected for the reader this embarrassing timeline of 16 years of extensions. This takes the term “kicking the bucket’ to a whole new level of government cover-up.

This same phrase has appeared in some form since 2000— **“until comprehensive reform could be achieved”**.

Time Line:

- **2000:** “On July 21, 2000, the Joint Board issued its 2000 Separations Recommended Decision, recommending that, **until comprehensive reform could be achieved**, the Commission should freeze the expenses.
- **2001:** “The Commission ordered that the freeze would be in effect for a five-year period beginning July 1, 2001, or until the Commission completed **comprehensive separations reform, whichever came first**.
- **2006:** “On May 16, 2006, in the “2006 Separations Freeze Extension and Further Notice”, the Commission extended the freeze for three years or **until comprehensive reform could be completed**, whichever came first. The Commission concluded that extending the freeze would provide stability to LECs pending further Commission action to reform the... rules, and that **more time was needed to study comprehensive reform**. The freeze was subsequently extended by one year in 2009, 2010, and 2011 and by two years in 2012.”
- **2010:** “March 30, 2010, the State Members of the Joint Board released a proposal for interim and comprehensive separations reform... On September 24, 2010, the Joint Board held a meeting with consumer groups, industry representatives, and state regulators to **discuss interim and comprehensive reform...**“

- **2011:** “In addition, in 2011, the Commission comprehensively reformed the universal service and intercarrier compensation systems and proposed additional reforms. The Joint Board is considering the impact of the reforms proposed by the USF/ICC Transformation Order and any subsequent changes on its analysis of the various approaches to separations reform.”
- **2014-2017:** “On March 27, 2014, the Commission sought comment on extending the freeze once more. We extend through June 30, 2017.... We conclude that extending the freeze will provide stability to carriers that must comply with the Commission’s jurisdictional separations rules **while the Joint Board continues its analysis of the jurisdictional separations process.**“

Conclusion, Repeated.

- The FCC must audit the financial accounting books of the incumbent state utilities immediately and stop all proceedings until it actually does the proper analysis of Business Data Services, (formerly called “Special Access” services), revenues and profits, as well as the treatment of the copper utility networks, or the financial impacts of the IP Transition.
- We object to the extension on the grounds that it is being done as a cover-up so that actual financial data is excluded from the FCC rulemaking process.
- The FCC has been negligent in examining the harms that its Big Freeze has caused for over a decade, and it is clear it will continue to do so by allowing this extension to go forward.
- We call for an investigation into the FCC’s processes by the Inspector General’s Office as it is clear that there was no mention of our letter, the reports or other related filings that detailed the harms of the FCC’s big freeze.¹⁶

Documents Submitted

We have submitted these documents as part of this record.

- The Hartman Memorandum
- <http://newnetworks.com/hartmanmemorandum/>
- The History & Rules of Setting Phone Rates in America —The FCC’s ‘Big Freeze’ & Cross Subsidies
- <http://newnetworks.com/hartmanhistory/>
- Letter to the FCC pertaining to the Hartman Memorandum
- <http://newnetworks.com/fccletterhartman/>
- Cover letter in 31 separate FCC proceedings
- <http://newnetworks.com/fcccoverletter/>
- Report 1: Executive Summary: Verizon’s Manipulated Financial Accounting & the FCC’s “Big Freeze”

¹⁶ <https://www.fcc.gov/inspector-general>

- <http://newnetworks.com/report1executivesummary/>
- Report 2: Full Data Report
- <http://newnetworks.com/report2data/>
- Verizon Massachusetts & Boston: Investigate the Wireless-Wireline Bait-n-Switch
- <http://newnetworks.com/verizonmareport/>
- Joint filings with Consumer Federation of America
- <http://newnetworks.com/nnicfacomments/>

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