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

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In the Matter of)
)
Comprehensive Review of the)
Accounting Requirements)
And ARMIS Reporting Requirements for)
Incumbent Local Exchange Carriers: Phase 1)
)

CC Docket No. 99-253

COMMENTS OF BELLSOUTH CORPORATION

BELLSOUTH CORPORATION

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COMMENTS OF BELLSOUTH CORPORATION

BellSouth Corporation, for itself and its affiliated companies (collectively “BellSouth”), submits the following comments in response to the *Notice of Proposed Rulemaking* released in the above-captioned proceeding.¹

I. Introduction and Summary

BellSouth is pleased and supportive of the conclusions reached by the Commission in this Phase I of its comprehensive accounting review. BellSouth believes that most of the proposed changes will result in a legitimate reduction of unnecessary work. Moreover, the changes are consistent with the mandates prescribed to the Commission by Congress as set forth in the Telecommunications Act of 1996 (“1996 Act”).

BellSouth, however, expresses this support with cautious optimism. Although the *Notice* proposes to reduce or eliminate several outdated rules, their replacement, in some cases, may be as bad as the existing rule. For example, BellSouth supports the tentative conclusion to eliminate the expense matrix and in its place allow the Commission to make specific request of expense

¹ *In the Matter of Comprehensive Review of the Accounting Requirements And ARMIS Reporting Requirements for Incumbent Local Exchange Carriers: Phase 1*, CC Docket No. 99-253, *Notice of Proposed Rulemaking*, FCC 99-174, released July 14, 1999 (“*Notice*”).

information that it may need. Such requests, however, must not be so overly broad as to be equal to or more burdensome than preparing the entire matrix.

Moreover, BellSouth supports the proposal to require an attestation audit instead of the current requirement of a financial statement audit of cost allocation information. BellSouth again stresses concern that an attestation audit may become as taxing as a financial statement audit if the Commission's staff continues to request information of both the carrier and the independent auditor that exceeds the bounds of the attestation audit.

BellSouth also supports the elimination of the 15-day prefiling period for cost pool changes, but is apprehensive about this change not going far enough to protect large carriers from competitive harm. BellSouth advocates an annual filing only of the cost allocation manual.

Finally, BellSouth supports the remaining proposed revisions of the rules. Although, it believes more can be done to reduce this type of regulation, it commends the Commission on these first steps.

II. BellSouth Supports the Conclusions Set Forth in the *Notice Regarding Accounting Rules*

The opening section of the *Notice* proposes changes to various accounting rules that have been plaguing incumbent local exchange carriers ("LECs") since the implementation of price cap regulation. Indeed, BellSouth commends the Commission for finally acknowledging that such rules are completely unnecessary outside of a rate of return regulation environment. BellSouth is optimistic that the Commission will continue this view and work toward eliminating even more useless rules in Phase II of its review.

A. The Commission Should Eliminate the Expense Matrix

BellSouth agrees with the Commission's conclusion that the expense matrix required by section 32.5999(f) should be eliminated.² While reporting the total expense amount per account is necessary,³ a separate aggregation of the expenses into salary and wages, benefits, rents, and other expenses is unnecessary to any informed reader of the financial data including management. Preparation of the information provided in the matrix, as well as the reporting process, is burdensome for the modest benefit that the matrix provides. Its elimination will not be noticed by anyone except, perhaps, by those who have the responsibility of segregating the expenses into such sub-categories.

The *Notice* indicates that elimination of the matrix may affect certain activities performed by the Commission. In particular, the *Notice* seeks comment on how elimination of the matrix may affect price cap performance/productivity factor calculations, jurisdictional separations process, universal service support, and service quality studies. Although limited information in the expense matrix is used for some of the above calculations, continued preparation of the matrix is not needed to satisfy the Commission's narrow need. Carriers can provide information to the Commission on an as needed basis to easily fulfill such a need. The Commission must, of course, evaluate and request only the information that it truly needs and avoid any temptation to be over broad with its request, or specific request will become as burdensome as preparing the entire matrix. Precise request for specific information will meet the needs of the Commission and limit the reporting burden currently placed on carriers.

² *Notice* ¶ 8.

³ Reporting of the total expense for a required account is necessary. What is not necessary is the number of accounts that BellSouth is required to maintain. As demonstrated in BellSouth's comments in *In the Matter of 1998 Biennial Regulatory Review – Review of*

B. The Commission Should Require An Attestation Engagement Instead of a Financial Statement Audit for Part 64

The *Notice* proposes to change the annual Joint Cost audit for large incumbent LECs to an attestation audit instead of an annual financial audit. An attestation engagement by independent auditors was, of course, the original requirement established by the Commission in its *Cost Separations Order*.⁴ BellSouth agrees that to the extent any independent review of cost allocation data is needed for a price cap regulated company, an attestation engagement by an independent auditor is more than sufficient to provide comfort to the Commission that the cost allocation process is working properly. Indeed, BellSouth's cost allocation manual ("CAM") is reviewed annually by the Accounting Safeguard Division ("ASD") of the Common Carrier Bureau for compliance with the Commission's accounting safeguards. Accordingly, an attestation engagement covering a carrier's compliance with the CAM will provide the ASD with the independent auditor's assistance and professional opinion sought by the genesis of this Rule. Moreover, returning to the original form of the audit prescribed by the Commission in Part 64.904 would reduce the unnecessary burden and expense of this engagement.

BellSouth feels, however, that one issue of clarification must be made. The Commission states in the *Notice* that "[a]n attestation requires that the auditor provide assurance that specific management assertions are fairly stated. An attestation generally provides less assurance and is governed by less stringent standards of testing, reporting, and expression of opinion than the

Accounting and Cost Allocation Requirements, et. al., CC Docket No. 98-81, all carriers, regardless of size, should be allowed to use the Class B set of accounts.

⁴ See *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 nonregulated activities and to provide for transactions between telephone companies and their affiliates*, CC Docket 86-111, *Report and Order*, 2 FCC Rcd 1298 (1987) ("*Cost Separations Order*"). The Commission changed the original attestation requirement to a financial statement audit in 1991. See *In the Matter of Computer III Remand*

financial audits required by section 64.904 for large ILECs.”⁵ The characterization of an attestation engagement as providing “less assurance” and thus implying that it will entail less work does not fairly represent an attestation engagement on two fronts.

First, both a financial statement engagement and an attestation engagement result in an opinion being expressed by the independent auditor after extensive testing of data. The contrast of the two, as related to Part 64, is that a financial statement engagement tests and opines on the numbers presented on a specific financial statement, while an attestation engagement results in an opinion upon management’s written assertion regarding compliance with its cost allocation procedures. Consequently, in addition to the ASD having reviewed the CAM for compliance, the return to the original form of the Part 64 attestation engagement provides the Commission with an independent auditor’s professional opinion of BellSouth’s compliance with the CAM.

Second, in 1991 when the Commission changed the form of the audit from an attestation to a financial statement engagement, the administrative burden and cost of the annual engagement for Tier I Carriers approximately doubled. The lion's share of this work, however, was not the result of simply changing the form of the engagement from an attestation to a financial statement audit, but in the extensive requests for additional summaries, specified audit work-paper formats, and other additional detailed requests which the ASD has treated as requirements under the Commission’s rules. The additional detail is not and has never been necessary for the independent auditors to express their professional opinion as required in Part 64. Hence, for there to be savings in administrative burden and cost, as sought by this proceeding, the change in engagement form must be accompanied by the cessation of such

Proceedings: Bell Operating Company Safeguards and Tier 1 Local Exchange Company Safeguards, CC Docket No. 90-263, 6 FCC Rcd 7571, 7581-83, ¶¶ 21-24 (1991).

⁵ Notice ¶ 11.

extraneous requirements. Part 64.904(a) states “[t]he audit shall be conducted in accordance with generally accepted auditing standards, except as otherwise directed by the Chief, Common Carrier Bureau.” To facilitate safeguards against future unnecessary administrative burdens in this area, the authority relating to exceptions should remain with the Common Carrier Bureau and should not be delegated to the ASD. If the ASD continues to prescribe unnecessary requests of the incumbent LECs and the independent auditors, the attestation engagement could be as taxing as a financial statement audit.

The *Notice* seeks further comment on the possible change to an Agreed Upon Procedure Engagement as will be used for the Section 272 biennial audit. BellSouth opposes using this form of independent auditor engagement. One of the purposes of this proceeding is to seek “reform measures that can be implemented without delay.”⁶ The general standard procedures for the biennial audits, required pursuant to Section 272 of the 1996 Act, took two years to design and resulted in a 49-page template. A similar effort should be expected for an Agreed Upon Procedure Engagement under Part 64. Accordingly, such a lengthy development process clearly would be contra to the Commission’s intent of swift implementation of reform measures in this proceeding and should therefore be avoided.

C. A *De Minimis* Exception for Affiliate Transactions is Long Overdue

The *Notice* proposes to establish a *de minimis* exception from the Affiliate Transactions Rule requiring the comparison of estimated fair market value (“EFMV”) and fully distributed cost (“FDC”). BellSouth supports such an exception. With three reporting years now falling under the rules promulgated in the *Accounting Safeguards Order*,⁷ experience has shown that

⁶ *Notice* ¶ 2.

⁷ *In the Matter of Accounting Safeguards under the Telecommunications Act of 1996*, CC Docket 96-150, *Report and Order*, 12 FCC Rcd 2993 (1996) (“*Accounting Safeguards Order*”).

obtaining EFMV for services that are not readily available on the commercial market can be costly.⁸

The cost of obtaining EFMV is an unnecessary burden placed upon Tier I Carriers where there is little or no impact upon the ratepayer. As it has explained on numerous occasions to the Commission, BellSouth's rates are no longer subject to rate of return regulation but are governed by price cap regulation. Thus, the cost of a service that is recorded on the regulated company's books pursuant to a transaction with an affiliate does not directly impact the rates that BellSouth charges its customers.⁹ Accordingly, for BellSouth *de minimis* transactions represent administrative services shared between affiliates to take advantage of economies of scope and scale. Billing for these services between affiliates is a matter of cost reimbursement, not profit generation. These *de minimis* services should not be subject to the additional cost of obtaining and maintaining dual documentation which can negate the economies of shared administrative services. Carriers should be allowed to record *de minimis* services at FDC.

⁸ See, e.g., The Theodore Barry & Associates study which projected an average annual cost of \$45,000 per EFMV study for knowledge based transactions that are not readily available on the commercial market. Appendix A p. 8, to BellSouth Comments filed on August 26, 1996 in the *Accounting Safeguard Order* proceeding. BellSouth has incurred this amount and more to produce the EFMV documentation required by the new rules for a single transaction.

⁹ Indeed, in addition to the elimination of the documentation of both EFMV and FDC for services not priced at tariff or meeting the Commission's 50% rule, the Commission should consider the elimination of this asymmetrical rule in its entirety for carriers under price cap regulation with no sharing. In the *Notice for Proposed Rulemaking* in CC Docket 93-251, released on October 23, 1993, the Commission stated "Since the adoption of the affiliate transactions rules, we have adopted a price cap system for AT&T that imposes no sharing obligations. This system greatly reduces the incentives that AT&T may have to shift costs between its nonregulated operations and its carrier operations. Since AT&T's price caps are unrelated to AT&T's current costs, attempts by AT&T to manipulate the costs it records for affiliate transactions will not increase AT&T's rates." (¶ 101). The Commission further states the affiliate rules are needed for the Commission to determine LEC's sharing obligations. (¶ 103). Using its own arguments against imposing the affiliate transactions rules upon AT&T as a guide, the Commission should remove the imposition of affiliate transaction rules from LECs under price cap regulation with no sharing. At a minimum the Commission should remove the unnecessary and extremely anti-competitive asymmetrical rules.

The *Notice* also seeks comment on the application of a *de minimis* standard for affiliates arising from Sections 260 and 271–276 of the 1996 Act. As a prerequisite, the following points of application should be recognized about each of these sections. First, section 260, which relates to telemessaging, section 275, which relates to alarm monitoring, and section 276, which relates to payphones, do not require the formation of separate affiliates. In the event that an incumbent LEC chose to place such services in a separate “nonregulated” affiliate, however, as BellSouth has done with its payphone service, the *de minimis* standard should apply. Second, affiliates created under sections 271 and 272, which relate to the provisioning of interLATA services, are subject to section 272 safeguards. Section 272 requires the provision of services, from the Bell operating company (“BOC”) to the section 272 affiliate, on a nondiscriminatory basis with the exception of joint marketing. Part 32.27(d) states “in the case of transactions for assets and services subject section 272, a BOC may record such transactions at prevailing price regardless of whether the 50 percent threshold has been satisfied.” Consequently, the transactions covered under Section 272 and Part 32.27(d) are not subject to the asymmetrical rules discussed above and extension of a *de minimis* standard to affiliates under these safeguards is not necessary. Third, the separate affiliate requirements pursuant to section 274, which relates to electronic publishing, are time limited based on the sunset provision of section 274(g)(2) of the 1996 Act.¹⁰ The extension of the *de minimis* exception would be appropriate for any transactions with a section 274 affiliate only prior to the sunset provisions taking effect. Otherwise, the 274 affiliate will revert to a “normal” affiliate and benefit from any exception

¹⁰ Section 274(g)(2) states “[t]he provisions of this section shall not apply to conduct occurring after 4 years after the date of enactment of the Telecommunication Act of 1996.” The 1996 Act was enacted on February 8, 1996. Thus, the sunset provision will eliminate the separate affiliate requirement on February 8, 2000, approximately six months from the date on this filing.

extended to other “normal” affiliates. Finally, transactions under section 273, which relate to a manufacturing affiliate, should fall under exceptions provided to other affiliates.

D. The Commission Should Eliminate the 15-Day Pre-filing for Cost Pool Changes

BellSouth supports the Commission’s tentative conclusion that the 15-day pre-filing requirement for cost pool changes should be eliminated. Cost pool changes are frequently triggered by the introduction of new competitive products or services. The current 15-day pre-filing provides competitors with sensitive data in advance of implementation of the services, thereby putting the Tier I Carriers at a competitive disadvantage. Merely eliminating the 15-day pre-filing requirement, however, will not sufficiently eliminate this anti-competitive disclosure. If cost pools are necessary for a new nonregulated service, these cost pools are necessary not only at commercial deployment, but also during the technical and market trial phase of service development. Even though the proposed change would eliminate the pre-filing requirement, the CAM, a public document, would still have to be filed contemporaneous with the implementation of the cost pool change, i.e., during technical or market trial phase prior to commercial roll out. Filing a public CAM revision contemporaneous with the cost pool change continues to provide competitors (interexchange carriers (“IXC”), competitive LECs (“CLECs”), Internet service providers (“ISP”), etc.) enough advanced notice to “scoop” their competition, the incumbent LECs.

Such competitive gains, and attempts at gains, are very real. For example, BellSouth cites just two occasions in which a competitor obtained advanced notice and sought further information based on this notice. In 1991, MCI sought detailed information on equal

access/network reconfiguration (“EA/NR”).¹¹ In 1994 MCI sought detailed information on video dial tone (“VDT”).¹² In both instances, MCI used the cost pool changes, or lack thereof, as a means for requesting competitive information on internal costs and quantities on specific elements. In each instance, the Commission found BellSouth’s CAM revisions to be compliant and did not require BellSouth to publish sensitive information in advance of deployment. Neither the Commission nor BellSouth, however, should be placed in the position of handling these competitively motivated requests.

Accordingly, subjecting incumbent LECs’ new services to public disclosure during technical and marketing trials provides competitors an unfair competitive advantage. The Tier 1 Carriers covered by these rules are not provided advanced information on their competitors. Hence, the publication of such information on the public record is anti-competitive and unnecessary. While the Commission will continue to require the filing of revisions to cost pools, the public filings should be limited to an annual basis as allowed by the 1996 Act. While annual filings may still cause the advance publication of nonregulated services’ information during a trial stage, such premature disclosure would occur less frequently and be more manageable.

The 1996 Act allows CAM revisions to be made annually. Filing these revisions on a more frequent basis puts the Tier I Carriers at a profound competitive disadvantage. Therefore, the Commission should not only eliminate the 15-day prefiling period, but also move to an annual filing of CAM revisions.

¹¹ See *In the Matter of Cost Allocation Manuals of The Ameritech Operating Companies, Bell Atlantic Telephone Companies, BellSouth Corporation, Central Telephone Company, NYNEX Telephone Companies, Rochester Telephone Corporation, Southwestern Bell Telephone Company, Southern New England Telephone Company and US West*, AAD 91-53.

¹² See *In the Matter of BellSouth Telecommunications, Inc.*, AAD 94-22.

E. Revision of Accounts

The *Notice* proposes to revise the requirements of various accounts that are a part of the Uniform System of Accounts (“USOA”). First, the *Notice* tentatively concludes to eliminate the 30-day notification period subsequent to the establishment of temporary or experimental accounts as required in section 32.13(a)(3). Second, the *Notice* proposes to eliminate the requirement that the Commission review journal entries detailing extraordinary items, contingent liabilities, and material prior period adjustments prior to the entries being recorded in the company financial records. Third, the *Notice* tentatively concludes that the requirement that costs recorded in account 32.2002, which remain in the account for over two years, may continue to remain in account 32.2002 instead of being required to be transferred to account 32.2006.¹³ Finally, similar to immediately preceding item, the *Notice* proposes to end the requirement that cost recorded in account 32.2003, which relate to construction projects that have been suspended for six months or more, be reclassified to account 32.2006.

BellSouth supports all of these proposals. Indeed, BellSouth commends the Commission for eliminating such useless forms of regulation that do nothing other than detract resources from entities such as BellSouth, and the Commission who must review such rules, when these resources can hardly afford to be squandered.

III. ARMIS Reporting

The *Notice* also proposed several changes to reduce ARMIS reporting requirements. BellSouth supports these proposed changes and believes that each of these changes will result in a benefit for future ARMIS reporting. To truly maximize the benefit of some of the proposed

¹³ Carriers would still be required to exclude the cost of such property and the associated depreciation reserve from the ratebase.

revisions to accounts discussed in II.E., above, specifically revisions to section 32.2002 and 32.2003, however, the Commission should also change the reporting requirements for ARMIS reports 43-01, 43-03, and 43-04. Price regulation eliminates any need for large LECs to maintain cost records of this detail. Such records play no role in setting rates and therefore are not needed by the Commission for any oversight capacities to protect consumers. Their continued production is a waste of resources. Accordingly, BellSouth recommends that the Commission expand the section 32.2002 and 32.2003 simplification changes for ARMIS reporting.

In addition, BellSouth requests the Commission to reconsider BellSouth's prior proposed changes to ARMIS reports 43-01, 03, 04, and 495 A&B in its Phase I review.¹⁴ That proposal sought the consolidation of all information reported in 43-01, 03, and 04 into one report and the elimination of Forms 495 A&B. Any additional information beyond that presented in BellSouth's proposal could be maintained by the carrier and provided to the Commission on a requested basis. BellSouth contends that under the current regulatory paradigm the Commission's efforts would be better utilized in areas other than monitoring accounting costs. Such monitoring could be performed effectively by the information reported in the revised ARMIS reports proposed by BellSouth.

IV. BellSouth Eagerly Anticipates Phase II of the Commission's Review

As demonstrated in the above comments, BellSouth supports the proposals set forth in the Notice and commends the Commission on its honest efforts to reduce needless regulation. And, while the proposals are a good first step, BellSouth fully believes that much more can be done. Consequently, BellSouth is looking forward to working with the Commission on Phase II of its

¹⁴ See BellSouth *ex parte* presentation filed on June 4, 1999 in CC Docket Nos. 98-64, 98-177, 96-150, 98-74, and 98-117 and *In the Matter of 1998 Biennial Regulatory Review-Review of*

review. BellSouth feels that the Commission's efforts will be much more effective and productive if it engages the thoughts and insights of the incumbent LECs prior to this stage of its review. Under such conditions, BellSouth anticipates a meaningful and fruitful Phase II review.¹⁵

V. Conclusion

BellSouth believes that the proposals set forth in the *Notice* will reduce its regulatory administrative burden and complement the reporting process. Therefore, based on the forgoing,

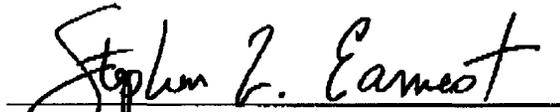
ARMIS Reporting Requirements, CC Docket No. 98-117 BellSouth's Comments, filed on August 20, 1998.

¹⁵ BellSouth made a few suggestions for additional changes to the proposals in Phase I. BellSouth contends that these suggestions are related to the current proposals and hopes the Commission will consider these in addition to its original tentative conclusions. In no event, however, does BellSouth intend these few suggestions to be a list or even a partial list of its suggested changes for Phase II of the review.

BellSouth supports, subject to certain caveats, the proposals recommended by the Commission in the *Notice*.

Respectfully submitted,

BELLSOUTH CORPORATION
By its Attorneys

A handwritten signature in cursive script that reads "Stephen L. Earnest". The signature is written in black ink and is positioned above a horizontal line.

~~M. Robert Sutherland~~
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Date: August 23, 1999

CERTIFICATE OF SERVICE

I do hereby certify that I have this 23rd day of August, 1999, served the following parties to this action with a copy of the foregoing *COMMENTS OF BELLSOUTH CORPORATION*, reference CC Docket No. 99-253, by hand delivery or by placing a true and correct copy of the same by Federal Express, addressed to the parties listed below.

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