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December 4, 2002

Marlene Dortch
Secretary
Federal Communications Commission
445 12th Street, NW
Washington, DC 20554

Re: *Consolidated Application for Authority to Provide In-Region, InterLATA Services in Colorado, Idaho, Iowa, Nebraska, North Dakota, Montana, Utah, Washington, and Wyoming*, WC Docket No. 02-134

Dear Ms. Dortch:

This letter responds to the November 22, 2002 *ex parte* letter filed by KPMG LLP in the above-captioned proceeding. The purpose of the KPMG letter was to inform the Commission that a previous submission by KPMG to the Commission concerning Qwest's compliance with section 272(b)(2) and 272 (c)(2) of the Communications Act is withdrawn and can no "longer be relied upon." This astonishing development confirms beyond doubt that Qwest's application must be denied, because Qwest has not, and could not, meet its obligation under 47 U.S.C. § 271(d)(3)(B) to demonstrate its compliance with the critically important accounting safeguards of section 272.

Specifically, in the prior Qwest 271 proceedings, Qwest argued that, despite the fact that neither Qwest Corp. ("QC"), Qwest's Bell Operating Company, nor Qwest Communications Corp. ("QCC"), Qwest's section 272 affiliate, could certify compliance with generally accepted accounting principles ("GAAP"), QC and QCC were nonetheless accounting for transactions with each other in conformity with GAAP. To support this contention, Qwest submitted a September 4, 2002 letter from KPMG. In that statement, KMPG purported to "review" Qwest's representation regarding its ongoing accounting investigation. According to Qwest, it had as of August 19, 2002, identified 42 potential accounting violations, and the only one that pertained to a BOC-272 affiliate transaction had been resolved. Based on its "review," KPMG attested that "nothing came to our conclusion that caused us to believe that management's assertions" were incorrect. AT&T demonstrated in the prior proceedings that KPMG's "review" opinion was entitled to no weight because it did nothing more than accept Qwest's representations about potential restatement items and did not independently examine the underlying transactions between QC and the 272 affiliate in order to ensure that those transactions were being properly recorded by QC

In the current proceeding, Qwest nonetheless incorporated the KPMG statement by reference and again argued that QC is accounting for transactions with the 272 affiliate (now Qwest Long Distance Corporation ("QLDC")) in conformity with GAAP, despite QC's ongoing inability to certify its books. By way of its November 22 letter, however, KPMG has acknowledged that its prior conclusions must be retracted and should be accorded no weight in this proceeding. KPMG provides no explanation why it has withdrawn its prior statement, other than to state cryptically that "in these instances" a "review-level service" was inappropriate. The Commission must therefore assume that KPMG has subsequently discovered information that caused it to reverse its prior conclusions about the propriety of QC's accounting for transactions with the 272 affiliate. But whatever the reason for KPMG's action, there is now plainly no basis for any reasoned Commission finding that Qwest has demonstrated compliance with the section 272 accounting safeguards.

As a result of KPMG's retraction, the only "evidence" offered by Qwest to show its compliance with section 272(c)(2) is the bare assertion of its own employee, Ms. Schwartz, that "[t]he accounting policies and practices that give rise to QC's inability to certify its financial statements have been revised such that instances of material noncompliance with GAAP are not continuing and further do not affect GAAP compliance for transactions between QC and QLDC."[1] But in the absence of any factual support, her *ipsi dixit* simply cannot be credited. Qwest has provided no evidence of any independent examination of Qwest's accounting policies, practices and internal controls to support that bare assertion. Moreover, in both the Qwest I and Qwest II proceedings, Ms. Schwartz opined that QC "follows Generally Accepted Accounting Principles,"[2] – a statement that Qwest never retracted even after it was clear that it was not true.[3] In all events, as Professor Holder has explained, it is well established in the accounting profession that mere management representations are patently inadequate support for any reasoned finding of GAAP compliance. Qwest proffers no expert testimony to rebut Professor

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[1] Qwest III, Schwartz Reply Dec. ¶ 7.

[2] *See* Qwest I, Schwartz Dec. ¶ 48; Qwest II, Schwartz Dec. ¶ 47.

[3] *Compare* Qwest I & II, *Ex Parte* Letter from Peter A. Rohrbach to Marlene Dortch (August 27, 2002) (attaching revised Brunsting and Schwartz Declarations that continued to state unqualifiedly that QCC and QC "follow[] Generally Accepted Accounting Principles") *with* Qwest I & II, *Ex Parte* Letter from Oren Shaffer to Marlene Dortch, at 1 (August 20, 2002) ("QCII's internal investigations have now identified, with respect to the QC and QCC financial statements, (1) accounting transactions for QCC that did not comply with the requirements of GAAP, and (2) certain potential adjustments to the financial statements of QC that may be necessary to comply with GAAP.")

Holder, and it is now clear that the Commission can expect no rebuttal from KPMG, the accounting firm that is actually conducting the investigation of Qwest's concededly flawed accounting policies and concededly inadequate internal controls.[4]

Thus, in light of the evidence of record, only one conclusion could withstand appellate review – that Qwest does not satisfy section 272(c)(2). As Professor Holder has testified, Qwest's filings with the SEC establish that: i) Qwest's accounting policies themselves are under investigation; ii) Qwest has a history of pervasive and systemic non-compliance with GAAP; and iii) Qwest's internal investigation is ongoing and the full extent of Qwest's problems is still not known. Indeed, since it filed its latest section 271 application, Qwest has been forced to acknowledge that its accounting problems go well beyond mere capacity swaps, that it has begun investigating "routine" transactions, that its review of its internal accounting controls is incomplete, and that the new controls have not been adequately reviewed and tested by KPMG.[5] Given these undisputed facts, there can be no grounds for crediting the mere assertion that QC is now complying with GAAP with regard to transactions with Qwest's 272 affiliate.[6] To the contrary, as Professor Holder concludes, "before there can be any reasonable assurance that QLDC and QC will be able to produce financial information that complies with GAAP in the immediate future, Qwest should finish its investigation, establish and test the functioning of adequate controls, and provide sufficient evidence of GAAP-compliance that goes beyond mere representations."[7]

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[4] *See* Qwest III, *Ex Parte* Letter from C. Frederick Beckner III to Marlene Dortch (Nov. 7, 2002) (attaching Declaration of William Holder ("Holder *Ex Parte* Dec.")).

[5] *See generally* Qwest November 14, 2002 8-K. In this regard, Qwest has acknowledged that effective internal controls are a pre-condition to finding compliance with section 272. Qwest III Reply at 14 ("The relevant question is whether a Section 272 affiliate has implemented internal control mechanisms reasonably designed to prevent, as well as detect and correct, any noncompliance with section 272.").

[6] *See* Holder *Ex Parte* Dec. ¶¶ 21-27.

[7] *Id.* ¶ 22. In addition, as AT&T has explained in its prior filings on this issue, Qwest cannot satisfy section 272 without proffering hard evidence that QCC – the entity which Qwest concedes will eventually become its 272 affiliate – complies with the section 272 accounting requirements.

Sincerely

C. Frederick Beckner III