Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of	
Stale or Moot Docketed Proceedings	
1993 Annual Access Tariff Filings Phase I	CC Docket No. 93-193
1994 Annual Access Tariff Filings	CC Docket No. 94-65
AT&T Communications Tariff F.C.C. Nos. 1 and 2, Transmittal Nos. 5460, 5461, 5462, and 5464 Phase II	CC Docket No. 93-193
Bell Atlantic Telephone Companies Tariff FCC No. 1, Transmittal No. 690	CC Docket No. 94-157
NYNEX Telephone Companies Tariff FCC No. 1, Transmittal No. 328	

COMMENTS OF VERIZON

Michael E. Glover
Edward Shakin
Of Counsel

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Joseph DiBella
1515 North Courthouse Road
Suite 500
Arlington, Virginia 22201
(703) 351-3037
joseph.dibella@verizon.com

Attorney for the Verizon
telephone companies

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COMMENTS OF VERIZON[1]

I. Introduction and Summary

The issue here is whether the Commission's rules required Verizon and other carriers to deduct other postretirement employee benefit ("OPEB") liabilities from the interstate regulated rate base for purposes of calculating earnings for years prior to 1997, when the Commission changed the rules only on a going forward basis to deduct such liabilities from the rate base. The

[1] The Verizon telephone companies ("Verizon") are the affiliated local telephone companies of Verizon Communications Inc. These companies are listed in Attachment A. They include the former Bell Atlantic, NYNEX, and GTE local telephone companies in the above-referenced investigations.

Commission itself addressed this issue on two separate occasions, finding both times that the rules prior to 1997 did not allow these liabilities to be deducted. First, it issued an order in 1996 reversing the Common Carrier Bureau's *RAO 20*[2] letter, which had incorrectly instructed the carriers to deduct these liabilities from the rate base. In that order, the Commission found that its rules defined explicitly those items to be deducted from the rate base, and that OPEB liabilities were not among them. Second, it issued an order in 1997 rejecting a petition that sought reinstatement of *RAO 20*, finding that the rules prior to 1997 could not be interpreted as requiring OPEB liabilities to be deducted from the rate base. When Verizon and other carriers filed their 1996 tariffs, they complied with the order rescinding *RAO 20* by recalculating their rates of return for the prior years to correct for the impact of the Bureau's erroneous instructions and to comply with the Commission's rules. There is no need to address this issue a third time – the investigation should be terminated.

II. Background

On May 4, 1992, the Common Carrier Bureau (now the Wireline Competition Bureau) issued *RAO 20*, which interpreted the Commission's accounting rules at that time as requiring the local exchange carriers to deduct accrued OPEB liabilities from their regulated interstate rate base. Section 65.800 *et. seq.* of the Commission's rules defines the interstate rate base used for ratemaking purposes. The rate base includes the interstate portion of the Part 32 accounts listed in Section 65.820, minus the interstate portion of the Part 32 accounts listed in Section 65.830. ***See*** 47.C.F.R. § 65.800. *RAO 20* required the carriers to include OPEB liabilities in the items to

[2] *Responsible Accounting Officer Letter 20, Uniform Accounting For Postretirement Benefits Other Than Pensions In Part 32*, 7 FCC Rcd 2872 (1992) ("*RAO 20*").

be deducted from the rate base in Section 65.830. This reduced the net investment in the local exchange carriers' rate of return calculations and therefore increased the return on investment that they reported in their annual Form 492 reports, resulting in increased sharing obligations for many carriers under price caps.

In 1996, after reviewing objections by Verizon and others, the Commission reversed *RAO 20* insofar as it applied to the rate base treatment of OPEB costs. ***See*** *Responsible Accounting Officer Letter 20, Uniform Accounting For Postretirement Benefits Other Than Pensions In Part 32*, 11 FCC Rcd 2957 (1996) ("*RAO 20 Rescission Order*"). The Commission found that *RAO 20* exceeded the scope of the Bureau's delegated authority to explain and interpret the accounting rules and to resolve accounting errors, stating that;

> Sections 65.820 and 65.830 of our rules define explicitly those items to be included in, or excluded from, the interstate rate base. The Bureau cannot properly address any additional exclusions in an RAO letter, which under Section 32.17 of our rules must be limited to explanation, interpretation, and resolution of accounting matters.[3]

The *RAO 20 Rescission Order* issued in 1996 made it clear that the rules never allowed, much less mandated, a rate base deduction for OPEB liabilities. ***See*** id. Recognizing that OPEB liabilities could only be deducted from the rate base by a rule change, the same order contained a notice of proposed rulemaking to amend Section 65.830(a), which enumerates specific items to be deducted from the rate base, to include accrued OPEB liabilities. ***See*** *RAO 20 Rescission Order*, ¶ 32.

In response to the *RAO 20 Rescission Order* and as required by Section 65.830(a), Verizon and other price cap carriers adjusted their reported earnings for 1993 to 1995 to reverse

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[3] *RAO 20 Rescission Order,* ¶ 25 (footnotes omitted).

the OPEB deductions that had been made under the *RAO 20* letter rescinded by the Commission. This increased Verizon's rate base and reduced its interstate rate of return and its sharing obligation under the price cap rules.

In its 1996 annual access tariff filings, Verizon increased its price cap indexes to reflect the reduced sharing obligations. The Bureau suspended and investigated the tariff filings to determine, *inter alia*, if it was consistent with the Commission's rules to include OPEB liabilities in the rate base. ***See*** *1996 Annual Access Tariff Filings*, 11 FCC Rcd 7564 (1996). Notwithstanding the Commission's express conclusion that the existing rules did not require (or permit) OPEB liabilities to be deducted from the rate base, the Bureau stated that it might be possible to interpret Section 65.830 of the Commission's rules to allow deduction of OPEB liabilities from the rate base through analogy to other similar costs that are specifically deducted. ***See*** id., ¶ 19. The Bureau also consolidated the investigation of the rate base treatment of OPEB liabilities into the pending investigation of other tariff filings involving OPEB costs in CC Docket No. 93-193, which itself had been consolidated with a combined investigation of OPEB issues in CC Docket No. 94-157. ***See*** id., ¶ 110; ***See*** *1993 Annual Access Tariff Filings; 1994 Annual Access Tariff Filings; AT&T Communications, Tariff FCC Nos. 1 and 2, Transmittal Nos. 5460, 5461, 5462, and 5464; Bell Atlantic Telephone Companies, Tariff FCC No. 1, Transmittal No. 690; NYNEX Telephone Companies, Tariff FCC No. 1, Transmittal No. 328*, 10 FCC Rcd 11804, ¶ 38 (1995) ("*Combined OPEB Investigations Order*"). The Bureau stated that it would issue an order designating issues for investigation and establishing a pleading cycle. However, no such order was issued, and no record was developed in this proceeding.

In 1997, the Commission completed the rulemaking proceeding it had initiated in the *RAO 20 Rescission Order*. ***See*** *Responsible Accounting Officer Letter 20, Uniform Accounting For Postretirement Benefits Other Than Pensions In Part 32*, 12 FCC Rcd 2321 (1997) ("*OPEB Rate Base Order*"). The Commission amended Section 65.830(a)(3) to explicitly deduct all long term liabilities in account 4310, including unfunded accrued OPEB liabilities, from the rate base. ***See*** id., ¶ 19. As with all rule changes, this change had only prospective effect. ***See*** id., ¶ 34. In that order, the Commission also rejected MCI's petition to reconsider the *RAO 20 Rescission Order* and to require the carriers to deduct OPEB liabilities from the rate base prior to the effective date of the rule change. MCI had argued that the Commission had broad discretion in interpreting its rules and that a rule change was not needed to deduct OPEB liabilities from the rate base. MCI also had argued that because the rules already deducted pension liabilities from the rate base, and because pensions were similar to OPEBs, the Commission could have applied the pension rule to OPEB for past periods through an interpretation. ***See*** id., ¶ 25. The Commission rejected these arguments, stating that;

> We also are not persuaded by MCI's argument that the Commission can amend Part 65 through an interpretation without providing affected parties with any notice of or chance to comment on the amendment. Giving rate base recognition to OPEB in Part 65 would constitute a rule change for which proper notice and comment must be given.[4]

The 1996 Access Tariff investigation lay dormant for over six years until the Commission issued an order terminating a number of investigations, including the investigation in CC Docket No. 94-157, into which the CC Docket No. 93-193 investigation of several OPEB tariff filings, including the filings reversing the impact of the rescinded *RAO 20* letter, had been consolidated.

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[4] Id., ¶ 28 (footnote omitted).

See *Termination of Stale or Moot Docketed Proceedings*, 17 FCC Rcd 1199 (2002) ("*Termination Order*"). Nine months later, AT&T made an *ex parte* presentation to the Bureau seeking resolution of the issue concerning rate base treatment of OPEB costs prior to the rule change. In response, the Bureau issued an order reinstating the investigation of OPEB costs in CC Docket No. 94-157 and related dockets. ***See*** *Stale or Moot Docketed Proceedings*, Order, Notice, and Erratum, DA 03-488, ¶ 18 (rel. Feb. 25, 2003) ("*OPEB Reinstatement Order*").

III. The Commission's Rules Do Not Permit The Carriers To Deduct OPEB Liabilities From The Rate Base For 1996 Or Prior Years.

It would be unlawful for the Commission to require carriers to deduct OPEB liabilities from the rate base prior to the date that the Commission changed its rules. The Commission's rules only permit carriers to deduct specific listed items from the interstate regulated rate base, and for the period at issue, OPEB liabilities were not among them. The courts have made it clear that the Commission is required to follow its own rules until such time as it alters them through another rulemaking. ***See, e.g.,*** *Southwestern Bell Telephone Company v. FCC*, 28 F.3d 165, 169 (D.C. Cir. 1994) ("[b]oth sides agree that the FCC's statement of its criteria for exogenous cost treatment constituted a rule, not a policy statement. . . . Accordingly, the Commission was bound to follow those statements until such time as it altered them through another rulemaking"). After the Commission rescinded the Bureau's *RAO 20* letter, the carriers were required to restate their rate of return reports and their sharing obligations for the prior years to reverse the OPEB liabilities deduction previously required by the erroneous *RAO 20* letter. Although the Bureau's order investigating the 1996 tariffs stated that it might be possible to interpret Section 65.380 of the Commission's rules to allow exclusion of costs that were not listed in that Section by analogy

to costs that were, such an interpretation would be inconsistent with the rule, and the Commission accordingly ruled out that possibility in the *OPEB Rate Base Order*.

Section 65.830 of the Commission's rules specifically limits the Part 32 investment accounts or portions of those accounts that must be deducted from the interstate rate base. The rate base deductions in the rules that were applicable to the 1996 tariff filings include the interstate portions of the following accounts;

> (1) deferred taxes (Accounts 4100 and 4340);
>
> (2) customer deposits (Account 4040);
>
> (3) unfunded accrued pension costs (Account 4310); and
>
> (4) other deferred credits (Account 4360) to the extent they arise from the provision of regulated telecommunications services. This shall include deferred gains related to sale-leaseback arrangements.[5]

These were the only items that could have been deducted from the rate base at the time of the 1996 tariff filings. The rules did not state a general principle or guideline – an account or a portion of an account either was listed or it was not. For this reason, other Part 32 accounts or sub-accounts could not be deducted from the rate base until the rule was changed. In the *RAO 20 Rescission Order*, the Commission made it clear that, in 1992, when the Bureau issued *RAO 20*, Section 65.830 did not include OPEB liabilities in the list of items to be deducted from the rate base. ***See*** *RAO 20 Rescission Order*, ¶ 32 ("Under our current Part 65 rules, unfunded accrued pension costs recorded in Account 4310 are removed from the rate base, although other items recorded in Account 4310, such as accrued OPEB liabilities, are not removed from the rate base"). As a result of the 1997 rule change discussed above, item number 3 on this list was

[5] 65 Fed. Reg. 9047 (Mar. 3, 1989).

modified on a prospective basis to encompass accrued OPEB liabilities, which are currently deducted from the rate base.[6]

The Commission also made it clear that the Bureau exceeded its delegated authority when it "interpreted" Section 65.830 to require the carriers to deduct OPEB liabilities from the rate base. In *RAO 20* (at p. 2), the Bureau had stated that "[i]t is our opinion that postretirement benefits are similar to pension expenses recorded in Accounts 4310 and 1410 and as such should be given the same rate base treatment. Therefore, the interstate portion of unfunded accrued postretirement benefits recorded in Account 4310 should be deducted from the rate base . . . ." The Commission found that this exceeded the Bureau's delegated authority under Section 32.17 of its rules to explain, interpret, or resolve matters that are not clearly provided for in Part 32, because Section 65.380 defined explicitly those items to be deducted from the rate base and no "interpretation" could expand upon that list to include OPEB liabilities. ***See*** *RAO 20 Rescission Order*, ¶ 25. The only way that OPEB liabilities could be removed from the rate base was through a rule change, after notice in the Federal Register and an opportunity for comment.[7] For this reason, the Commission reversed *RAO 20* and established a notice of proposed rulemaking to amend Part 65 to deduct unfunded accrued OPEB costs from the rate base. ***See*** id., ¶ 32. Consequently, Verizon and the other carriers subject to the Part 32 accounting rules were required to restate their rate of return reports for the prior periods to reverse the deduction of

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[6] ***See*** *OPEB Rate Base Order*, ¶ 18 (unfunded OPEB liabilities liabilities recorded in Account 4310 that are derived from the expenses in Section 65.450(a) will be removed from the rate base).

[7] In contrast, the Commission found that the portion of *RAO 20* instructing the carriers about the accounts in which to record OPEB costs did not require prior notice and comment under the Administrative Procedure Act, because it did not change the accounting rules, but merely interpreted them. ***See*** *RAO 20 Rescission Order,* ¶ 19.

OPEB liabilities from the rate base and to adjust their resulting sharing obligations in the 1996 annual access tariff filings.

In the order investigating Verizon's 1996 tariff filings, the Bureau again raised the issue of whether "it would be possible to interpret our rules to permit a case-by-case evaluation of the correct rate base treatment of costs not explicitly identified in Part 65" and to "determine, for example, that OPEB costs should be accorded a particular rate base treatment based on an analogy to other costs." *1996 Annual Access Tariff Filings*, 11 FCC Rcd 7564, ¶ 19 (1996). In the *OPEB Rate Base Order*, the Commission closed the door for a second time on the "interpretive" approach to expanding the list of accounts deducted from the rate base. In rejecting MCI's request to apply the rule for deduction of OPEB liabilities prior to 1997 "by analogy" to unfunded accrued pension liabilities, the Commission stated unequivocally that the Commission cannot "amend Part 65 through an interpretation without providing affected parties . . . notice of or chance to comment on the amendment. Giving rate base recognition to OPEB in Part 65 would constitute a rule change for which proper notice and comment must be given." *OPEB Rate Base Order*, ¶ 28, ***citing*** the Administrative Procedure Act, 5 U.S.C. § 553. That notice and comment rulemaking was not concluded until February 1997, and the rules did not and could not have any retroactive effect on Verizon's rate of return calculations for the 1993-95 period. ***See, e.g.***, *Bowen v. Georgetown Hospital*, 488 US 204, 208 (1988).

The D.C. Circuit has already rejected an attempt by the Commission to alter the treatment of OPEB costs without a rule change. In *Southwestern Bell Telephone Company v. FCC*, 28 F.3d 165, 169 (D.C. Cir. 1994), the Court held that the Commission was bound by its rules concerning the exogenous treatment of GAAP changes such as SFAS 106 until such time as it

amended the rules through a notice and comment rulemaking proceeding. Specifically, the Court rejected the Commission's attempt to apply a "control" test for exogenous adjustments that included control over the level and timing of OPEB expenses, stating that there was "not a hint of such a control test" in the Commission's prior rules. Id. The Commission subsequently adopted a rule change to deny exogenous treatment to changes in accounting rules that change the timing of when costs are recognized but that do not have an actual economic impact. ***See*** *Price Cap Review for Local Exchange Carriers*, 10 FCC Rcd 8961, ¶¶ 306-09 (1995). The Commission correctly observed that these rule changes would have only prospective effect. ***See*** id., ¶¶ 306-07. Similarly, its 1997 rule changes for the rate base treatment of OPEB liabilities only had prospective effect. Any attempt to "interpret" the prior rules to deduct OPEB liabilities from the rate base would fail judicial review for the same reason as the Commission's attempt to "interpret" its prior rules to create a special class of GAAP changes that would not be treated as exogenous.

IV. The Commission Should Not Investigate Other Issues In The OPEB Tariff Investigations.

In the *OPEB Reinstatement Order*, the Commission invited parties to raise any other issues that they believe remain open in the investigations that were consolidated in CC Docket No. 94-157, including the tariff investigations in CC Docket No. 93-193 and the 1996 OPEB

tariff filings.[8] For several reasons, the Commission should not conduct further evidentiary proceedings and it should terminate this investigation.

First, as Verizon demonstrated in its March 27, 2003, Petition for Reconsideration of the *OPEB Reinstatement Order*, these consolidated investigations were terminated in the *Termination Order*, and the Bureau did not have the authority to "correct" that order long after the period for seeking review has expired. ***See*** *Stale or Moot Docketed Proceedings*, CC Docket Nos. 93-193, 94-65, 94-157, Verizon Petition for Reconsideration (filed Mar. 27, 2003). The Commission simply lacks statutory authority to reestablish these investigations or to order refunds.

Second, it would be highly prejudicial to Verizon if the Commission went forward with a further inquiry into the reasonableness of the OPEB costs in the various tariff filings in 1993, 1994, 1995, and 1996, all of which have been incorporated into this investigation. The OPEB exogenous cost changes involved complex calculations and detailed expert economic studies that were the subject of extensive pleadings and evidentiary submissions by the carriers. The passage of almost ten years since the first OPEB tariff investigation began has prejudiced Verizon's ability to introduce new studies or even to defend its original studies and calculations. Many key personnel and expert witnesses who helped prepare those filings have left the company or have moved to other responsibilities, and their ability to help Verizon reconstruct and defend the basis for the calculations has been impaired. The difficulty that parties face in trying to resolve factual issues after so long a time is one reason why Congress took additional action in the 1996

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[8] ***See*** *OPEB Reinstatement Order*, ¶ 25. The Bureau's order also required commenters to designate the portions of their previous filings that remain relevant. ***See*** id., ¶ 24. In addition to the supporting information in Verizon's 1996 annual access tariff filings, Section A of Bell Atlantic's opposition filed May 13, 1996 in the 1996 Annual Access Tariff proceeding addresses the issue of the rate base treatment of OPEB liabilities.

Telecommunications Act to shorten the deadline for completing tariff investigations to five months from the previous deadline of 12 months, both of which have been far exceeded here. ***See*** 47 U.S.C. § 204(a)(2)(A).

Third, the access charge regime has changed substantially from the time that these investigations were initiated, such that the current charges applicable to interexchange carriers are no longer based on OPEB costs. In addition to the 1995 order requiring the local exchange carriers to remove OPEB exogenous cost changes from their interstate access charges, the Commission ordered a major restructuring of access charges in 1998 that shifted costs out of traffic sensitive access charges paid by interexchange carriers, and it adopted the CALLS order in 2000 that required the local exchange carriers subject to price caps to reach a "target" rate for traffic-sensitive charges. ***See*** *Price Cap Performance Review for Local Exchange Carriers*, 10 FCC Rcd 8961, ¶ 309 (1995) (requiring price cap carriers to remove OPEB costs from their indexes); *Access Charge Reform*, 12 FCC Rcd 15982 (1997) (restructuring access charges); *Access Charge Reform*, 15 FCC Rcd 12962 (2000) (adopting CALLS proposal). The target rate is not based on cost, but on an industry agreement designed, in part, to lower charges to interexchange carriers and, in turn, to facilitate reductions in long distance rates to consumers. ***See*** 15 FCC Rcd 12962, ¶¶ 151, 176. Shifting additional amounts of revenues from the local exchange carriers to the interexchange carriers at this time would distort the market and contradict the Commission's finding that charges paid by interexchange carriers should not be reduced further once the target rates are achieved.

Fourth, the benefits at this point of pursuing these issues are tenuous at best. AT&T, the largest potential recipient of refunds in these investigations, would have to refund most of those

amounts in turn to its own customers from a decade ago, since AT&T incorporated the local exchange carriers' exogenous cost increases for OPEB costs (plus its own OPEB costs) in its own 1993 tariff filings, which are also part of this investigation and subject to suspension and an accounting order. ***See*** *AT&T Communications Tariff FCC Nos. 1 and 2, Transmittal Nos. 5460, 5461, 5462 and 5464*, 8 FCC Rcd 6227 (Com. Car. Bur. 1993). It is unlikely, despite the accounting order, that AT&T could identify the millions of customers from as much as ten years ago that would be entitled to these refunds, many of whom have since migrated to other carriers, including Verizon. Furthermore, the second largest recipient of potential refunds, WorldCom, is currently in bankruptcy, where it seeks to avoid a substantial portion of its debts from the pre-bankruptcy period. The rest of the interexchange carriers, who recovered Verizon's OPEB costs through their own long distance charges in 1993, would also be unjustly enriched if they were to obtain refunds at this late date.

For these reasons, pursuing these issues would be pointless. The Commission should terminate this investigation for a second time.

Conclusion

For the foregoing reasons, the Commission's rules make it clear that OPEB liabilities could not be deducted from the interstate rate base for the years at issue. The Commission should terminate this investigation for a second and final time.

Respectfully submitted,

By: _____
Joseph DiBella

1515 North Court House Road
Suite 500
Arlington, VA 22201-2909
(703) 351-3037
joseph.dibella@verizon.com

Attorney for the Verizon
telephone companies

Of Counsel
Michael E. Glover
Edward Shakin

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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.