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Marlene H. Dortch
Secretary
Federal Communications Commission
445 12th Street, SW
Washington, DC 20554

Re: **Verizon Telephone Companies Petition for Reconsideration, "In The Matter of Stale or Moot Docketed Proceedings," CC Docket Nos. 93-193, 94-65, and 94-157**

Dear Ms. Dortch:

This letter explains why the Commission's accounting rules could not be interpreted to have required carriers to remove the costs of other postretirement employee benefits ("OPEBs") from the regulated rate base prior to the Commission's 1997 adoption of the "RAO 20" rule, which required the carriers to deduct OPEB liabilities from the rate base. The reason for this is that OPEB costs were not included in the rate base prior to 1997 and, therefore, there was nothing to be removed. The Commission's rules have always been very explicit both about what was <u>included</u> in the rate base and what was <u>deducted</u> from the rate base. Prior to the rule change in 1997, accrued OPEB liabilities were <u>neither</u> included in the rate base <u>nor</u> deducted from the rate base.

OPEB costs are primarily liabilities, representing a form of deferred compensation that employees earn during their working years and that the company must pay to them after they retire. ***See*** *Responsible Accounting Officer Letter 20, Uniform Accounting Treatment for Postretirement Benefits Other Than Pensions In Part 32*, 11 FCC Rcd 2957, ¶ 5 (1996) ("*RAO*

20 Rescission Order"). When the Financial Accounting Standards Board adopted SFAS-106, it required companies to account for OPEB costs on an accrual basis during the years that the benefits are earned by recording a liability for the benefit amounts owed to employees. OPEB costs are treated as assets only to the extent that a company has prepaid its OPEB costs. ***See*** id., ¶ 7. This limited exception to the treatment of OPEB costs as liabilities is not relevant here, however, because none of the Verizon companies had any prepaid OPEB costs. ***See*** Verizon Reply Comments, at 15 (filed Apr. 22, 2003).

The regulated rate base consists of "included items" listed in section 65.820 and "deducted items" listed in section 65.830. ***See*** 47 C.F.R. §§ 65.820, 65.830. The "included items" are made up of assets, not liabilities. The assets include telecommunications plant in accounts 2001, 2002, 2003, and 2005; materials and supplies in account 1220.1; other noncurrent assets in account 1410[1] and deferred maintenance and retirements in account 1438; and cash working capital. By definition, none of these assets can include liabilities, such as accrued OPEB liabilities. In addition, while not relevant here, prior to 1997, the rules also did not include prepaid OPEB costs as assets in the rate base. ***See*** id., ¶ 25 (1996).

Liabilities affect the rate base only to the extent that the Commission has decided that certain types of liabilities that have been found to be zero-cost sources of funds should be deducted from the rate base. For instance, the deferred tax account represents liabilities for taxes that are incurred now, but that do not need to be paid until some point in the future. The Commission treats a carrier's deferred taxes as a type of interest-free capital, because the carrier has the use of these funds without paying interest until the taxes are due. The Commission therefore requires the carrier to deduct these amounts from the rate base because the carrier does not need to earn a rate of return on these amounts from the ratepayer. Prior to 1997, the liabilities that the Commission found should be deducted from the rate base included the interstate portion of deferred taxes in accounts 4100 and 4340; the interstate portion of customer deposits in account 4040; the interstate portion of unfunded accrued pension costs in account 4310; and the interstate portion of other deferred credits in account 4360. None of these items included OPEB liabilities. ***See*** id.

When the Bureau issued RAO 20, it instructed the carriers for the first time to classify prepaid OPEB costs as assets in account 1410 and to classify unfunded OPEB costs as liabilities in account 4310. ***See*** *RAO Letter 20, Re: Uniform Accounting for Postretirement Benefits Other Than Pensions In Part 32*, 7 FCC Rcd 2872 (1992). The Bureau also instructed the carriers (again, for the first time) to include prepaid OPEB costs in account 1410 in the rate base and to deduct the unfunded OPEB liabilities in account 4310 from the rate base.

When the Commission reversed the Bureau's RAO 20 letter in the *RAO 20 Rescission Order*, the Verizon companies, except for NYNEX, reversed the deduction of OPEB liabilities

[1] "Other noncurrent assets" include items such as the cost of the company's investments in equities and other securities issued by affiliated companies. ***See*** 47 C.F.R. § 32.1410.

from the rate base. ***See*** *1996 Access Tariff Filings*, 11 FCC Rcd 7564, ¶ 7 (1996). None of the Verizon companies had to change anything with regard to prepaid OPEB benefits in Account 1410, because, as noted above, they never prepaid any OPEB benefits.

For these reasons, the Commission cannot find that OPEB liabilities were among the assets that comprised the "included items" for the rate base either before or after reversal of RAO 20. The only thing that was "included" in the rate base with regard to OPEB costs under the RAO 20 letter, and later when the Commission adopted the RAO 20 rule with regard to OPEB costs, were prepaid OPEB costs in Account 1410. When the Commission reversed RAO 20, this had no effect on the rate base for the Verizon companies, since they had never included any prepaid OPEB costs in the rate base.

If the Commission were to try to take OPEB liabilities out of the "included items" listed in section 65.820, which does not include liabilities of any sort, much less OPEB liabilities, it would make the same mistake that the Bureau made in trying to include OPEB liabilities in the list of "deducted items" in section 65.830. The rules are very explicit about what is included and about what is excluded, and the Commission cannot change this list without a rulemaking proceeding (and then, only prospectively). In the *RAO 20 Rescission Order*, the Commission recognized that "[s]ections 65.820 and 65.830 of our rules define explicitly those items to be included in, or excluded from, the interstate rate base" and that "[t]he Bureau cannot properly address any additional exclusions in an RAO Letter." *RAO 20 Rescission Order*, ¶ 25. In response to MCI's petition for reconsideration of that order, where MCI argued that the Commission had the ability to address the rate base treatment of OPEB through analogy to the treatment of pension costs in section 65.830, the Commission made it clear that the Commission itself could not amend the clear and unambiguous terms of Part 65 through an "interpretation." ***See*** *Responsible Accounting Officer Letter 20, Uniform Accounting for Postretirement Benefits Other Than Pensions In Part 32*, 12 FCC Rcd 2321, ¶ 28 (1997) ("Giving rate base recognition to OPEB in Part 65 would constitute a rule change for which proper notice and comment must be given"). For the same reasons, the Commission cannot "interpret" Part 65 to find that OPEB liabilities were ever part of the "included items" in the rate base.

Sincerely,

Joseph D. Bell

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