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EX PARTE

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

Re: 1993 Annual Access Tariffs, CC Docket No. 93-193; 1994 Annual Access Tariffs, CC Docket No. 94-65

Dear Ms. Dortch:

As Verizon has demonstrated in its comments, the Commission cannot legally apply its "add-back" rule retroactively to tariffs filed prior to the 1995 effective date of the add-back rule change. In *Bell Atlantic Telephone Companies v. FCC*, 79 F.3d 1195, 1207 (D.C. Cir. 1996) the Court found that the enforcement of the rule in the 1995 annual access tariff filings was acceptable because it only affected the 1995 tariffs, even if it calculated a carrier's rate of return for the 1994 base year using add-back. The Court made it clear that the new rules did not apply to earlier tariffs or require refunds of money collected under those tariffs. ***See*** *id.* at 1206.

If the Commission nonetheless concludes that it is legally authorized to order refunds in this context, it should exercise its well-established equitable discretion not to do so. The ordering of refunds in a tariff investigation is not automatic. To the contrary, refunds are "a matter of equity," and the Commission must "balance the interests of both the carrier and the customer in determining the public interest," with "each case . . . examined in light of its own particular circumstances." *American Television Relay,*[1] ¶ 15; *see Public Service Comm'n v. Economic*

[1] Memorandum Opinion and Order, *American Television Relay, Inc., Refunds Resulting from the Findings and Conclusions in Docket 19609*, 67 F.C.C.2d 703 (1978).

Economic Regulatory Admin., 777 F.2d 31, 36 & n.5 (D.C. Cir. 1985); *Las Cruces TV Cable v. FCC*, 645 F.2d 1041, 1047 (D.C. Cir. 1981). As the D.C. Circuit has explained, "once the Commission finds that a carrier has exceeded (as a pure mathematical matter) its prescribed rate of return, it then should consider other relevant factors in determining whether a rate is unreasonable and a refund warranted. *Virgin Islands Tel. Corp. v.* FCC, 989 F.2d 1231, 1239 (D.C. Cir. 1993).[2] Those factors include (1) whether the LECs' projections were reasonable when made, (2) the actual harm suffered by the ratepayer, and (3) any overriding equitable considerations. *Id.* at 1240. Applying a similar standard, the Commission has found it inappropriate to order refunds in a number of proceedings where it found that a carrier had overearned.[3]

Here, the factors set forth in *Virgin Islands* likewise militate against a refund. The first factor (reasonable projections) is directly relevant only in a rate-of-return context, which is not applicable here. Nonetheless, by analogy, the LECs that did not use add-back in 1993 and 1994 acted eminently reasonably, since the Commission did not mandate the use of add-back until 1995.

The second factor (ratepayer harm) likewise counsels against a refund because there is no reason to believe there was any harm to access customers here. Rather, AT&T and other IXCs undoubtedly passed the LECs' access charges through to customers as an element of their long distance rates. *See AT&T Communications Tariff FCC Nos. 1 and 2 Transmittal Nos. 5460, 5461, 5462 and 5464*, 8 FCC Rcd 6227 (1993). While end users may have paid more than they should have for long distance services, there is no mechanism for assuring that they would receive the benefit of any refund now, so any refund (or forward-looking reduction in the PCI) would simply create a windfall for IXCs – many of whom did not even exist in 1993 and 1994.[4] And even if IXCs passed through refunds (or lower access charges) to their customers – and there is no reason to believe they will – the customers that would benefit are not those that suffered harm from alleged overcharges in the early 1990s. Not only has the passage of time changed the composition of the customers that use long-distance services, but those customers now use cell phones, cable telephony, and e-mail as substitutes for wireline long distance service.

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[2] The same principle holds true in the price cap context, since the court was interpreting Section 204 of the Act, which applies to tariff investigations under any regulatory framework.

[3] *See, e.g.*, Memorandum Opinion and Order, *Tariffs Implementing Access Charge Reform*, 13 FCC Rcd 14683 (1998); Memorandum Opinion and Order, *Local Exchange Carrier Access Tariff Rate Levels; Bell Atlantic Telephone Companies Tariff F.C.C. No. 1; GVNW Inc./Management Bourbeuse Telephone Company Tariff F.C.C. No. 1*, 8 FCC Rcd 6202 (1993); Memorandum Opinion and Order, *Investigation of Special Access Tariffs of Local Exchange Carriers*, 5 FCC Rcd 1717 (1990).

[4] Ordering a refund that has the effect of reducing access charges also would go beyond the rate reductions called for in the *CALLS Order* and thereby undo the guarantee of a particular rate level for switched access that was part of the CALLS compromise. *See Access Charge Reform; Price Cap Performance Review for Local Exchange Carriers*, 15 FCC Rcd 12962, ¶ 166 (2000).

The third factor (general equitable considerations) also militates against a refund. As Verizon previously has explained, it reasonably relied on the *Bell Atlantic* court's ruling that the new add-back rules did not require refunds. ***See*** *Bell Atlantic* at 1207 (application of the add-back rule to the 1995 annual access tariffs was not retroactive because it "does not change the past legal consequences of carriers' decisions to choose" the X-factors in previous annual access tariff filings). It is patently unfair to undermine that reliance here – particularly since the lengthy delay in resolving this issue has prejudiced Verizon's ability to defend the tariff filings at issue. In the more than ten years since the Bureau initiated the first of these investigations, key personnel and expert witnesses who helped prepare Verizon's tariff filings have left the company or moved on to other responsibilities, and memories have faded. It is inequitable for the Commission to order refunds when its own delay has compromised a party's ability to defend its decade-old tariff filings and therefore has contributed to an adverse ruling on the tariff's lawfulness.

If the Commission nonetheless determines that (1) it has authority to apply the add-back rule retroactively in the above-referenced 1993 and 1994 tariff investigations, and (2) some form of refund would be equitable, it should require refunds due as a result of any tariff revisions to be developed only on a total company basis.[5] The Commission should not require the carriers to provide refunds for study areas that would have had increased sharing obligations (and lower rates) without offsetting the amounts by which other study areas would have had larger lower formula adjustments (and higher rates). For example, during the period at issue, the former GTE companies had twenty-six interstate tariff entities. ***See*** GTE Reply Comments, CC Docket No. 93-179 at 10 (filed Sep. 1, 1993). In 1991, some of these tariff entities were in the sharing mode and some were in the lower formula adjustment mode. This resulted in adjustments to 1992-1993 revenues (revenue reductions for sharing entities and revenue increases for lower formula adjustment entities). When GTE filed its access tariffs in 1993 and 1994, it did not apply add-back to any of its 1992 and 1993 revenues, regardless of whether the tariff entity was under sharing or lower formula adjustment. In other words, it did not add the revenues in the sharing states or reduce revenues in the lower formula adjustment states. This was consistent with its view that the Commission's price cap rules did not incorporate the add-back mechanism that had been part of the previous rate-of-return enforcement mechanism. GTE pursued a consistent approach in all tariff entities, despite the fact that applying add-back in the lower-formula-adjustment entities would have increased the lower formula adjustment and allowed higher rates.

If GTE were required to provide refunds to reflect the increased sharing obligations produced by add-back, it should be allowed to offset its refunds by the amount of increased lower formula adjustment that it would have obtained through add-back. As explained above, the ordering of refunds in a tariff investigation is not automatic – it is an equitable decision within

[5] The offset calculation, moreover, should aggregate both tariff years (1993 and 1994). GTE should not be required to provide refunds for one year if the higher rates due to addback in the other year would offset some or all of those refunds. Failing to do so could expose the company to financial liability when none should apply, since the IXCs that purchased access in 1993 almost certainly did so in 1994 as well.

the Commission's discretion. ***See, e.g.***, *Las Cruces TV Cable v. FCC*, 645 F.2d at 1047-8. Here, fundamental fairness dictates that a carrier such as GTE, which had different tariff entities for different study areas, should not be treated differently than a carrier with a single tariff entity for multiple study areas. Otherwise, a carrier with multiple tariff entities would be able to protect itself only by adopting the ratemaking methodology that maximized revenues in each study area, regardless of whether the approaches in different study areas were inconsistent. Access customers, who generally obtained GTE services in all study areas, would be unjustly enriched if they were to receive refunds in the sharing areas without offset from the higher rates due to add-back in the lower formula adjustment areas. A carrier such as GTE should not be penalized for adopting a consistent position on add-back across all of its study areas.

The D.C. Circuit's decision in *MCI Telecommunications Corp. v. FCC*, 59 F.3d 1407 (D.C. Cir. 1995) in no way constrains the Commission's ability to exercise its equitable discretion to offset refunds by the amount of an increased lower formula adjustment that the GTE entities, taken as a whole, could have obtained through add-back. The *MCI* case arose in an entirely different context – complaints for refunds based on violations of the Commission's category-specific rate of return prescriptions. In that context, the court explained that the Commission's hands were tied: unlike a Section 204 tariff investigation, where the Commission has permissive authority to determine refund liability, "[i]n the present cases ... the Commission is responding to complaints brought by customers of the LECs under § 206 of the Act, which is phrased in mandatory terms. ... Therefore, the factors that we set out in the *Virgin Islands* case do not apply where, as here, the Commission is adjudicating a damage claim made by a customer pursuant to § 206." *Id.* at 1414. Here, in contrast, the Commission's discretionary authority under § 204 is unconstrained – and, given that the Commission has discretion not to order refunds at all, it must have discretion to determine how much any refunds should be, taking into account the equitable factors discussed above.

In addition, the specific considerations relied on by the D.C. Circuit in invalidating the Commission's "limited offset" policy, which reduced damages for overearnings in one category by a LEC's underearnings in other access categories, do not apply here. The court held that the limited offset policy (1) was inconsistent with FCC precedent that prevented the Commission from using claims by carriers against customers to offset claims by customers against carriers, (2) amounted to an implicit determination that the defendant LEC was entitled to earn more than the amount that it actually earned from the rates it charged, even though there was no such entitlement under rate of return regulation, and (3) discriminated between those IXCs that filed complaints and those that did not. *Id.* at 1417-1420.

The Commission's precedent against using claims by carriers against customers as an offset in determining damages in the § 206 context is irrelevant here because this case arises under § 204, not § 206. There are no claims between carriers and customers in either direction; this is simply a tariff investigation. Nor would an equitable offset here violate rate of return regulation, for the simple reason that this case arises under price cap regulation. Indeed, while the Commission had stated that the authorized rate of return is only a maximum, not a minimum, the opposite holds true for the low-end adjustment. Here, LECs were entitled to earn at least 10.25 percent under price cap regulation; the failure to do so enabled them to claim a low-end adjustment. If LECs are forced to refund in sharing states but not to offset the amount of that reduction based on underearnings in low-end adjustment states, the very premise of the price cap framework would be violated. Finally, there is no discrimination among IXCs here because, once again, this is a tariff investigation, not a complaint case. And, even apart from the different legal context, there is every reason to believe, as noted above, that IXCs would have taken access services throughout GTE's service area, ameliorating any concern that some IXCs would receive more than they should and some less.

Sincerely,

/s/Joseph DiBella

cc: T. Preiss
D. Shetler