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March 5, 2008

VIA E-MAIL **EX PARTE**

Ms. Marlene H. Dortch
Secretary
Federal Communications Commission
Room TW-325
445 12th Street, S.W.
Washington D.C. 20554

Re: WC Dkt. Nos. 05-342, 07-21

Dear Ms. Dortch:

On March 4, 2008, the undersigned, representing Time Warner Telecom Inc., Cbeyond, Inc., and One Communications Corp., Jim Blaszak on behalf of Ad Hoc Telecommunications Users Committee, Aryeh Friedman of British Telecom, Anna Gomez of Sprint Nextel Corporation, and Karen Reidy of CompTel, met separately with Scott Bergmann, Senior Legal Advisor to Commissioner Adelstein, and John Hunter, Special Counsel to Commissioner McDowell.

The parties discussed the petitions for forbearance filed in the above referenced dockets. The attached presentations formed the basis of the discussions.

Please let us know if you have any questions or concerns in connection with this filing.

Pursuant to Section 1.1206(b) of the Commission's rules, 47 C.F.R. § 1.1206(b), a copy of this notice is being filed electronically in the above-referenced dockets.

Respectfully submitted,

/s/

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Enclosures

cc: Scott Bergmann
John Hunter

AT&T Petitions for
Forbearance from Cost Allocation and Accounting Rules
(WC Docket Nos. 05-342, 07-21)

- Similar petitions from Qwest and Verizon, yet they are all slightly different and, if granted, would result in separate cost allocation, accounting and ARMIS requirements for each of the RBOCs.
- Seek to eliminate the data and/or the reporting of the data needed by regulatory authorities and parties affected by RBOC pricing.
- Seek to eliminate non-structural safeguards prescribed less than six months ago in the *272 Sunset* Order
    - The safeguards are based on the belief that AT&T retains exclusionary market power over local bottleneck facilities.
    - The FCC held that AT&T and other RBOCs must continue to comply with accounting and cost allocation rules, affiliate transaction rules and file ARMIS reports because of their continued market power over local bottleneck facilities.
        - "AT&T, Verizon, and Qwest remain subject to a number of legal obligations that are an important component of the regulatory framework that we find appropriate for the BOCs and their independent incumbent LEC affiliates. In particular…the Commission's accounting and cost allocation rules and related reporting requirements…" *272 Sunset Order*, paragraph 90.
        - The FCC concluded these requirements "adequately address…concerns regarding the incentives and ability of the BOCs and BOC independent incumbent LEC affiliates to use their pricing of access services, including special access services, to impede competition in the provision of in-region, long distance services." *272 Sunset Order*, paragraph 105.
- No evidence that market conditions have changed since the *272 Sunset Order* or the *Verizon Six MSA* order (December 2007)
    - There is no basis for reversal of the *272 Sunset Order* finding that safeguards are necessary because AT&T has provided in this proceeding no analysis of market conditions and no evidence to demonstrate that it has lost its exclusionary market power. The FCC has denied forbearance petitions with "scant evidence in the record regarding the requested relief." *Verizon Six MSA* order, paragraph 45.
    - Special access rates of return prove lack of effective competition.
- Commission previously has found that originating and terminating switched access service markets suffer from "market failure." (Buyers of switched access cannot use market forces to influence pricing.) *Access Reform,* Seventh Report and Order, 16 FCC Rcd 9923, 9935 (2001)
- If AT&T's Petition were granted, or were deemed granted on April 24, 2008, there would be no way to detect anticompetitive pricing or price gouging.
    - Merger conditions prevent some special access price increases for a limited time, but the data that have revealed existing price gouging and that could disclose future profit margins would not be available.
    - Earnings from interstate *switched* access would also be undetectable from available data. Market forces will not prevent price gouging.

- On the Federal level, price cap regulation does not eliminate the need for Commission mandated cost allocations.
    - Data are needed to assess: claims for exogenous cost and indices adjustments, whether price caps prescriptions are properly specified, *i.e.*, whether they are producing a competitive result.
        - In the CALLS proceeding, the FCC targeted price reductions toward the baskets with the highest levels of rates of return. The effect was to reset the price cap index for those baskets at levels that were closer to the costs attributed to the services in the basket. This could only have been achieved by relying on the cost and revenue information ILECs maintain pursuant to the Part 69 rules and related ARMIS reports.
            - *CALLS Order* n. 376 ("Based on 1999 ARMIS data, Commission staff calculated approximate rates of return of 85 percent for the traffic sensitive basket, 20 percent for the trunking basket, and 15 percent for the common-line basket.").
        - The proponents of the Missoula plan relied heavily on ARMIS and cost allocation data in determining the impact of changes to the switched access regime.
        - The FCC is currently relying on ARMIS data in its review of special access prices
    - Elimination of the sharing requirement under price caps does not equate to Commission approval of price gouging.
    - In 2001, the Commission retained cost reporting requirements, and in 2004 convened a Federal-State Joint Conference on Accounting issues to review the requirements that AT&T seeks to eliminate.
    - Grant of AT&T's' petition would violate section 254(k) of the Act.
    - Non-RLEC USF subsidies.
    - Smith v. Illinois mandates that as long as there remain two jurisdictions, Part 36 or similar Separations method remains necessary. Both the Bureau in its recent biennial report and the states in their recent Glide Path II paper agree that Part 36 rules remain necessary.
- Elimination of cost and revenue allocations would allow unfettered cross-subsidizations.
    - In its opposition to the Missoula Plan, Verizon recognized that cross-subsidization disadvantages competitors and hurts consumers.
- Digital networks do not preclude rational cost allocations. Neither analog nor digital carrier networks are single use/service networks.
- States have argued that they continue to use ARMIS and accounting data in numerous ways:
    - to recalibrate their price cap plans periodically to ensure that carriers are not overearning.
        - ARMIS data is particularly important because states can compare earnings across carriers or across states in a uniform manner.
    - to calculate USF support and TELRIC rates.
    - to calculate exogenous adjustments to price caps
    - to determine whether special access rates are just and reasonable.
    - to set intrastate access rates.
    - to monitor and protect against cross subsidization.
    - to oversee transactions between affiliates.

States Rely on the Accounting Rules and ARMIS Data For Numerous Regulatory Functions
(WC Docket Nos. 07-21, 05-342)

1. **ARMIS and Accounting Data Is Used To Reevaluate State Price Cap Plans and The Impact of Rate Reform of Switched and Special Access**

   a. "[R]ates are not completely divorced from costs until the potential for adjustments based on earnings levels [is] also eliminated." Wisconsin Public Service Commission Comments, 80-286, at 5 (Aug. 17, 2006).

   b. Vermont and Nebraska have indicated that even under price caps, "separations rules can still affect [switched access rates]" through the calculation of exogenous adjustments. Vermont Public Service Board, Vermont Department of Public Service, and Nebraska Public Service Commission Comments, 80-286, at 7 (Aug. 22, 2006).

   c. "Under price cap regulation the Commission and states should periodically assess if rates are reasonable, just and nondiscriminatory, such assessments would require cost information...TOPC opposes elimination of Part 36 and Part 64 rules without adequate replacements to protect consumers." Texas Office of Public Utility Counsel Comments, 07-21, at 2-3.

   d. "UTC Staff also used ARMIS Report 43-08 data to develop estimates of the intrastate effects of the so-called 'Missoula Plan' for intercarrier compensation reform on Washington carriers." Washington Utilities and Transportation Commission Comments, 07-273, at 8-9.

   e. "Some States use separations results to set wholesale rates, such as intrastate toll access rates and reciprocal compensation rates." State Members of the Federal-State Joint Board on Separations Comments, 07-21, at 11.

   f. "[ARMIS reporting requirements] have traditionally supported a variety of regulatory uses at the state and federal level. The NYPSC has used this information in several prior proceedings that included setting rates for special access[.]" State of New York Department of Public Service Comments, 07-273, at 1-2.

2. **States Rely on ARMIS Data *in lieu* of State-Specific Reports, Enabling Benchmarking of RBOC Price and Non-Price Behavior**

   a. "[I]n 2006..., the CPUC curtailed oversight of the retail telecommunications service offerings of the four major California ILECs[.] The CPUC expressed its intent to rely on the ARMIS reports as part of its monitoring program to ensure that the competitive market is functioning well[.]" Additionally,"the CPUC eliminated California- specific monitoring reports required under its previous regulatory framework" because it could rely on ARMIS. California Public

Utilities Commission and the People of the State of California Comments, 07-204, at 3-4.

b. "CPUC used ARMIS data in its 2001 complaint proceeding against AT&T (formerly SBC) and concluded that AT&T violated California Public Utilities Code § 451 [regarding service quality]" In the NRUF proceeding, the "CPUC relied, in part, on ARMIS service quality measures to evaluate AT&T and Verizon, Inc's service quality performance." California Public Utilities Commission and the People of the State of California Comments, 07-273, at 6-7.

c. "The ability to perform state-by-state comparisons of these allocations [in ARMIS Report 42-03] was a critical audit and analysis tool for UTC Staff during Verizon's most recent rate case and will remain invaluable for any future Verizon ratemaking proceeding." Washington Utilities and Transportation Commission Comments, 07-273, at 7.

d. "[T]he monitoring of Qwest's current regulatory scheme in Colorado depends upon the continued availability of ARMIS data. Because the COPUC requires the data found in the reports, if the reports are no longer available it may have to resort to the audit process to get the data – a time-consuming and costly process for both Qwest and the COPUC." Colorado Public Utilities Commission Comments, 07-204, at 4.

3. **ARMIS and Accounting Data Are Necessary To Set UNE Rates and USF Requirements**

a. The Texas commission asserted that affiliate transaction rules in Part 36 are necessary in setting UNE rates and state USF requirements. *See* Texas Office of Public Utility Counsel Comments, 00-199, at 3 (May 7, 2002).

b. Part 64 rules are used by states to calculate UNE rates. *See* Public Utilities Commission of Ohio Reply Comments, 00-199, at 7 (May 9, 2002).

c. "The data in [ARMIS 43-03] report are used by the COPUC as inputs into the HAI incremental cost model, which is used, in turn, to calculate Qwest's funding from the CHCSM. The HAI inputs are updated annually. The HAI Model outputs are also used in the development and computation of Total Element Long Run Incremental Cost (TELRIC), the basis for pricing unbundled elements.....The ARMIS reports are the only source of this necessary data." Colorado Public Utilities Commission Comments, 07-204, at 7.

4. **ARMIS and Accounting Requirements are Necessary to Prevent Cost Misallocation and Cross-Subsidy**

a. "AT&T in Ohio has an affiliate offering service both outside and within its traditional service territory. Absent the applicability of Section 32.27 to the largest ILEC in the state, the Ohio Commission's ability to oversee transactions

and limit cross-subsidization for AT&T Ohio will be at best severely hindered." Public Utilities Commission of Ohio Reply Comments, 07-21, at 5.

b. "In Verizon's 2004 Washington general rate case, ARMIS [43-04] data were used in testimony and decision on the merits of the company's separations and interstate and intrastate allocations...The elimination of this data for a major Washington carrier such as Verizon would hamper the UTC's ability to participate meaningfully in any future proceedings involving separations reform." Washington Utilities and Transportation Commission Comments, 07-273, at 7.

c. "Affiliate Transaction, Property Record and Rate-of- Return reporting...are helpful in determining whether Verizon is cross-subsidizing its unregulated activities with its regulated offerings to the detriment of its New York customers. Verizon, for example, is currently offering video in many downstate markets in New York and these rules are useful to monitor Verizon's activities in this highly competitive market and ensure that its legacy network is not overlooked." New York Department of Public Service Comments, 07-273, at 2.

5. **<u>The States Argue Uniformly That Any Changes Should be Made Through a Federal-State Joint Board</u>**

a. "The Separations Joint Board is currently considering the same separations reform issues that are raised by this forbearance petition.... The Joint Board should be allowed to continue its current efforts and not be effectively preempted by piecemeal forbearance decisions that would overthrow existing separations procedures in approximately half of the country." State Members of the Federal-State Joint Board on Separations Comments, 07-21, at 5-6.

6. **<u>The Development of Competition Does Not Obviate the Need For Reporting Requirements</u>**

a. "Even if competition were as well-developed as Qwest claims, the ARMIS reports would be used extensively by the COPUC – and other state commissions – for a variety of functions, including market monitoring, competition assessment, regulatory reform, and administration of universal service subsidy mechanisms. Therefore, the COPUC believes that the level of competition – whatever the truth of the matter may be – is neither a necessary nor a sufficient basis for eliminating the ARMIS reports at issue." Colorado Public Utilities Commission Comments, 07-204, at 9.