**Before the**
**FEDERAL COMMUNICATIONS COMMISSION**
**Washington, D.C. 20554**

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| In the Matter of | ) | |
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| Petition of Verizon For Forbearance Under 47 U.S.C. § 160(c) From Enforcement of Certain of the Commission's Recordkeeping and Reporting Requirements | ) | WC Docket No. 07-273 |

# REPLY COMMENTS OF VERIZON


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## REPLY COMMENTS OF VERIZON[1]

## I. INTRODUCTION AND SUMMARY.

The Commission should forbear from application of the recordkeeping and reporting requirements that are the subject of Verizon's Petition for Forbearance. Verizon's Petition is narrow and asks for relief only from limited regulatory requirements that serve no legitimate purpose in a competitive market and are not necessary to ensure just, reasonable, and nondiscriminatory rates or to protect consumers. It is in the public interest for the Commission to forbear from these requirements, which are obsolete relics of a bygone regulatory era.

The modern communications marketplace looks nothing like the competitive landscape existing when the Commission put in place the recordkeeping and reporting requirements addressed in Verizon's Petition. Indeed, even in the short time since Verizon's Petition was filed competition, particularly intermodal competition, continues to expand and thrive. In conjunction with the Commission's transition to price cap regulation long ago, the competitive market eliminates any legitimate federal need to continue the recordkeeping and reporting requirements

[1] The Verizon companies participating in this filing ("Verizon") are the regulated, wholly owned subsidiaries of Verizon Communications Inc.

that are the subject of Verizon's Petition. Facing that reality, those few parties that oppose Verizon's Petition ignore or dismiss out of hand the rise of competitive choices for consumers. Rather, opposing commenters suggest generally that the Commission's ARMIS reports, affiliate transaction rules, rate-of-return reporting, and property records requirements should be retained for reasons other than legitimate federal objectives. These commenters miss the mark in several respects.

The existence of other proceedings or future proceedings that may also address the issues raised in Verizon's Petition has no bearing on the merits of Verizon's request for forbearance relief. The Commission is required by Section 10 to grant forbearance if the recordkeeping and reporting requirements are no longer necessary, which they are not, whether or not the same issues might also be addressed in a different proceeding. Further, the Commission cannot maintain the recordkeeping and reporting requirements to satisfy largely undefined state uses of this information. The Commission must grant Verizon's forbearance request unless it identifies a present federal need for the recordkeeping and reporting requirements. There is no such need.

In addition, reference to certain of the recordkeeping and reporting requirements by the Commission in unrelated proceedings, particularly the Commission's recent Section 272 sunset proceeding, does not preclude relief. The Commission's discussion of recordkeeping and reporting requirements in that proceeding presumed the status quo with these requirements. The Commission did not say in that proceeding nor at any other time that these requirements must continue in perpetuity. Further, Verizon's obligation to comply with last year's *Non-Dominant Order* would be unchanged by forbearance relief granted through the instant petition. These attempts to obfuscate the issues notwithstanding, the recordkeeping and reporting requirements

addressed in Verizon's Petition have outlived their usefulness and now unfairly constrain a few among many competitors to the detriment of consumers.

Those few commenters that do attempt to identify a continuing federal need for the recordkeeping and reporting requirements are strained to do so, and ultimately their attempts fall flat. In particular, the Commission has long acknowledged that the ARMIS reports were not designed to last forever. After more than 16 years of price cap regulation and an explosion in competition, it is past time to eliminate ARMIS. Likewise, the Commission's affiliate transaction rules, remaining rate-of-return reporting rules, and continuing property records rules applicable to price cap carriers have no connection to just, reasonable, and nondiscriminatory rates under current price cap regulation. Rather, these rules today serve only to divert resources away from innovative services consumers want. In addition, myriad other accounting safeguards applicable to all public companies, including GAAP, the Sarbanes-Oxley Act, and the Foreign Corrupt Practices Act, are more than adequate to protect consumers just as these controls do in virtually all other markets. The Commission should grant Verizon's Petition.

## II. COMPETITION CONTINUES TO EXPAND AND THRIVE.

Even in the short time since Verizon filed its petition, competition in the communications marketplace continues to expand and thrive. For example, as of December 31, 2007, Comcast had approximately 4.4 million voice telephone customers, and it added over 2.5 million VoIP customers in 2007 as compared to 1.6 million in 2006 – an increase of 61 percent. Comcast currently markets VoIP service to 42 million homes, which represents 86 percent of its cable footprint.[2] Likewise, Time Warner Cable had more than 2.9 million voice telephone customers

[2] Press Release, *Comcast Reports 2007 Results and Provides Outlook for 2008* (Feb. 14, 2008) (available at http://www.cmcsk.com/phoenix.zhtml?c=118591&p=irol-newsArticle&ID=1108172&highlight=).

at the end of 2007, which represents a 12 percent penetration of service-ready homes passed, and it added 285,000 VoIP customers during the fourth quarter of 2007, marking its largest quarterly gain ever.[3] As of December 31, 2007, Cox had approximately 2.4 million telephone subscribers, which represented an approximately 18 percent increase in subscribership.[4] Just last month, Charter announced that it had surpassed one million telephone customers, and Charter expects its VoIP service to reach approximately 10 million homes passed by the end of 2008.[5]

Indeed, customers have a great many competitive choices today. By the end of this year cable companies are, combined, expected to serve more than 19 million lines.[6] In addition, approximately 16 percent of all households are projected to be wireless-only by the end of 2008, and the number of wireless-only households is expected to increase steadily over the next few

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[3] Press Release, *Time Warner Cable Reports 2007 Full Year and Fourth-Quarter Results* (Feb. 6, 2008) (available at http://files.shareholder.com/downloads/TWC/176374502x0x166410/9f2f505d-77bb-4a96-8d26-4029c5ecee0c/q407earningsrelease.pdf).

[4] News Release, *Cox Celebrates 7th Consecutive Year Adding More Than One Million New Revenue Generating Units* (available at http://phx.corporate-ir.net/phoenix.zhtml?c=76341&p=irol-newsArticle&t=Regular&id=1107954&).

[5] Press Release, *Charter Communications Surpasses One Million Telephone Customers* (Feb. 28, 2008) (available at http://phx.corporate-ir.net/phoenix.zhtml?c=112298&p=irol-newsArticle&ID=1112918&highlight= ); Press Release, *Charter Reports Third-Quarter Financial and Operating Results* (Nov. 7, 2007) (available at http://phx.corporate-ir.net/phoenix.zhtml?c=112298&p=irol-newsArticle&ID=1074737&highlight=).

[6] Craig Moffett, *et al.*, Bernstein Research, *VoIP: The End of the Beginning*, at Ex. 8 (Apr. 3, 2007).

years, reaching 32 percent in 2012.[7] Further, independent VoIP providers also have been successful in gaining customers.[8]

## III. THE EXISTANCE OF OTHER PROCEEDINGS THAT MAY ALSO ADDRESS ISSUES RAISED IN VERIZON'S PETITION IS NOT GROUNDS TO DENY FORBEARANCE.

Several commenters argue that Verizon's Petition should be denied because the recordkeeping and reporting requirements at issue: (1) are properly the subject of an industry-wide rulemaking; (2) should be considered in the first instance by a federal-state joint board; or (3) are under review in other Commission proceedings.[9] Such arguments are without merit; Verizon's ability to obtain regulatory relief in another proceeding or forum is not a lawful basis to deny forbearance.

Section 10 forbearance was designed precisely for circumstances such as those presented in this petition – where antiquated regulatory requirements are no longer necessary to ensure

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[7] S. Flannery, et al., Morgan Stanley, Cutting the Cord: Wireless Substitution Is Accelerating at 3, Exhibit 2 (Sept. 27, 2007).

[8] For example, Vonage, the largest independent VoIP provider, serves approximately 2.6 million customers, having experienced a nearly 16% increase in customers in 2007 as compared to 2006. *See* Vonage Holdings Corp. Reports Fourth Quarter and Full Year 2007 Results (Feb. 13, 2008) (available at http://files.shareholder.com/downloads/VAGE/155194909x0x169924/f977b368-188d-4cf2-b840-0d416e39f957/VG_News_2008_2_13_Financial.pdf). Skype, a subsidiary of eBay, allows customers to make free Skype-to-Skype voice and video calls and send instant messages using its software; as of January 2008, Skype software has been downloaded more than half a billion times and over 246 million people have registered to use Skype's service. Press Release, Skype to Support Internet Voice and Video Calls on Intel-based Mobile Internet Devices (Jan. 7, 2008) (available at http://about.skype.com/2008/01/).

[9] Comments of Sprint Nextel, WC Docket No. 07-273, at 3-10 (Feb. 1, 2008) ("Sprint Nextel Comments"); Comments of New York State Department of Public Service, WC Docket No. 07-273, at 2-3 (Feb. 1, 2008) ("New York PSC Comments"); Comments of Washington Utilities and Transportation Commission, WC Docket No. 07-273, at 15 (Feb. 1, 2008) ("Washington PSC Comments"); Comments of Public Service Commission of Wisconsin, WC Docket No. 07-273, at 1-3 (Jan. 31, 2008) ("Wisconsin PSC Comments").

reasonable rates or to protect consumers. 47 U.S.C. § 160(a). Indeed, elimination of the outdated and unnecessary recordkeeping and reporting requirements that are the subject of Verizon's Petition is required to ensure that the pro-competitive, deregulatory goals of the Telecommunications Act of 1996 ("1996 Act") are realized.[10] That the futility of continuing certain regulatory requirements might also be an appropriate topic in another forum does not obviate the Commission's obligation to evaluate those requirements in the context of Verizon's Petition. If regulations are no longer necessary, which those addressed in Verizon's Petition are not, the Commission's forbearance authority is mandatory. 47 U.S.C. § 160(a) ("the Commission *shall forbear* from applying any regulation. . .") (emphasis added). And, importantly, unlike a generic rulemaking, Section 10 forbearance includes a time limit to make sure that unnecessary regulations do not burden competition. *Id.*

The D.C. Circuit specifically rejected the Commission's view that it could deny forbearance relief merely because such relief might be obtained in a different proceeding.[11] In *AT&T Corp. v. FCC*, the Court held that the Commission could not deny US WEST's petition seeking forbearance from certain regulatory requirements merely because the same relief was

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[10] *See, e.g.*, *AT&T v. FCC*, 452 F3d 830, 832 (D.C. Cir. 2006) ("Critical to Congress's deregulation strategy, the [1996] Act added section 10 to the Communications Act of 1934"); *2000 Biennial Regulatory Review*, Notice of Proposed Rulemaking, 15 FCC Rcd 20008, 20008 ¶ 1 (2000) ("The major purpose of the 1996 Act is to establish 'a pro-competitive, deregulatory national policy framework' designed to make available to all Americans advanced telecommunications and information technologies and services 'by opening all telecommunications markets to competition.' Congress empowered the Commission with an important tool to realize this goal in Section 10 of the Act.") (citations omitted).

[11] *AT&T Corp. v. FCC,* 236 F.3d 729, 737-38 (D.C. Cir. 2001).

available under the Commission's *Pricing Flexibility Order.*[12] The Court reasoned that the availability of alternative relief was "beside the point" because "Congress has established § 10 as a viable and independent means of seeking forbearance[,]" and thus, "[t]he Commission has no authority to sweep it away by mere reference to another, very different, regulatory mechanism." *AT&T Corp. v. FCC*, 236 F.3d at 738. The D.C. Circuit's reasoning applies equally here.

Commenters' arguments to refer the issues raised in Verizon's Petition to a joint board are equally unavailing. The Commission is not required to defer to a federal-state joint board. The only federal-state joint board required by 47 U.S.C. § 410(c) is the Jurisdictional Separations Federal-State Joint Board, and Verizon's Petition does not seek forbearance from the Commission's separations rules in Part 36. The Federal-State Joint Board on Universal Service is also mandated by the 1996 Act, but the universal service joint board is an equally ill-suited home for these issues because Verizon's Petition is unrelated to universal service. 47 U.S.C. § 254(a)(1). Regardless, Congress directed the full Commission, not a federal-state joint board, to decide forbearance requests. Nothing in Section 10 permits the Commission to withhold or delay ruling on a forbearance petition by referral to a joint board. Such an approach is antithetical to the Commission's 15-month deadline to rule on forbearance requests in 47 U.S.C. § 160(c).

## IV. STATES' DESIRE TO MAINTAIN THE RECORDKEEPING AND REPORTING REQUIREMENTS IS NOT GROUNDS TO DENY FORBEARANCE.

Various commenters insist that the Commission must maintain the recordkeeping and reporting requirements that are the subject of Verizon's Petition in order for state public service

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[12] *Id.*; *see also Access Charge Reform; Price Cap Performance Review for Local Exchange Carriers*, Fifth Report and Order and Further Notice of Proposed Rulemaking, 14 FCC Rcd 14221, 14224 ¶ 2 (1999) ("*Pricing Flexibility Order*").

commissions to meet their state regulatory responsibilities.[13] Foremost, Verizon already operates under price cap regulation or deregulation in the vast majority of states, and the clear state trend is toward price caps and ultimately deregulation. The recordkeeping and reporting requirements addressed in Verizon's Petition are just as meaningless in price cap and deregulated states as they are on the federal level. And Verizon does not ask the Commission to eliminate all cost assignment regulations. Verizon's Petition is limited to those recordkeeping and reporting requirements that truly serve no useful purpose in today's competitive environment and does not include, for example, the regulated and nonregulated transactions recorded in Part 32 accounts or the regulated and nonregulated cost allocations resulting from Part 64. Moreover, a state interest, absent a corresponding federal need, is simply not lawful grounds to deny Verizon's Petition.

The D.C. Circuit construed the term "necessary" as used in the forbearance context in Section 10 "as referring to the existence of a *strong connection* between what [the Commission] has done by way of regulation and what [the Commission] *permissibly sought to achieve* with the disputed regulation."[14] Because the Commission has authority to regulate only interstate and

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[13] *See, e.g.,* Comments of the People of the State of California and the California Public Utilities Commission, WC Docket No. 07-273, at 3 (Feb. 1, 2008) ("California Comments") (asserting that "[w]ithout access to this information, California, and likely other states, will have difficulty meeting their oversight obligations"); New York PSC Comments at 2 (arguing that "ARMIS data continues to be an essential tool in evaluating competition and Verizon's intrastate rates and practices as well as other regulatory functions"); Washington PSC Comments at 2 (opposing Verizon's Petition because "it relies extensively on many of these reports in carrying out its responsibility to monitor, report on, and act upon matters within its state statutory authority"); Michigan Public Service Commission, WC Docket No. 07-273, at 6 (Feb. 1, 2008) ("Michigan PSC Comments"); Opposition of Comptel, WC Docket No. 07-273, at 8 (Feb. 1, 2008) ("Comptel Comments").

[14] *Cellular Telecomms. & Internet Ass'n v. FCC,* 330 F.3d 502, 512 (D.C. Cir. 2003) (emphasis added).

foreign communications and is prohibited from regulating intrastate service, 47 U.S.C. §§ 151, 152(b), a regulatory requirement that is the subject of a forbearance petition is only "necessary" for purposes of Section 10 if it serves a federal need. If a regulatory obligation does not achieve a "permissible" federal objective, as would be the case for a regulatory requirement designed to meet the needs of the states, the "strong connection" required to make the obligation "necessary" is lacking.

The Commission has acknowledged its lack of authority to maintain regulatory obligations that do not serve a federal purpose. In its *Phase Two Order* addressing accounting simplification, the Commission concluded that "if we cannot identify a federal need for a regulation, we are not justified in maintaining such a requirement at the federal level."[15] The Commission's *Phase Two Order* conclusion is fatal to those commenters seeking to deny Verizon's Petition based on a purported state need for continued recordkeeping and reporting obligations.

## V. THE COMMISSION'S *NON-DOMINANT ORDER* DOES NOT PRECLUDE GRANTING RELIEF.

There is no merit to the argument advanced by several commenters that the Commission's *Non-Dominant Order*[16] precludes granting Verizon's request for forbearance.[17]

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[15] *2000 Biennial Regulatory Review -- Comprehensive Review of the Accounting Requirements and ARMIS Reporting Requirements for Incumbent Local Exchange Carriers: Phase 2 Amendments to the Uniform System of Accounts for Interconnection Jurisdictional Separations Reform and Referral to the Federal-State Joint Board Local Competition and Broadband Reporting*, Report and Order and Further Notice of Proposed Rulemaking, 16 FCC Rcd 19911, 19985 ¶ 207 (2001) ("*Phase Two Order*").

[16] *Section 272(f)(1) Sunset of the BOC Separate Affiliate and Related Requirements,* Report and Order and Memorandum Opinion and Order, 22 FCC Rcd 16440 (2007) ("*Non-Dominant Order*").

This argument is based on a mischaracterization of Verizon's Petition and a misunderstanding of the *Non-Dominant Order*.

Foremost, Verizon seeks very limited relief from those recordkeeping and reporting obligations that truly serve no legitimate purpose in today's competitive market. Verizon's Petition does not seek forbearance from the rules requiring: (1) Part 32 recording of investment and expense into regulated and nonregulated accounts; (2) filing of a cost allocation manual or the regulated and nonregulated cost allocations resulting from Part 64; or (3) adherence to the jurisdictional separations process. AdHoc Comments at 3; Sprint Nextel Comments at 12. In the *Non-Dominant Order*, the Commission concluded that adherence to these rules, particularly the continued treatment of the costs and revenues from the direct provision of in-region, long distance services as nonregulated for accounting purposes, would protect "against improper cost shifting." *Non-Dominant Order* ¶ 94. Granting Verizon's Petition would have no impact on these protections.[18]

Second, there is nothing "logically incompatible" with the consumer safeguards put in place by the Commission's *Non-Dominant Order* and the relief Verizon seeks in its petition, nor

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[17] *See* Sprint Nextel Comments at 10-13; Comptel Comments at 2-4; Opposition of AdHoc Telecommunications Users Committee, WC Docket No. 07-273, at 2-5 (Feb. 1, 2008) ("AdHoc Comments"); Comments of Time Warner Telecom, Cbeyond, and One Communications, WC Docket No. 07-273, at 4-7 (Feb. 1, 2008) ("Time Warner Comments").

[18] Likewise, granting Verizon's Petition would have no impact on the *Computer III* non-structural safeguards that the Commission decided to retain in *Petitions of the Verizon Telephone Companies for Forbearance Pursuant to 47 U.S.C. § 160(c) in the Boston, New York, Philadelphia, Pittsburgh, Providence, and Virginia Beach Metropolitan Statistical Areas,* WC Docket No. 06-172, FCC 07-212 (rel. Dec. 5, 2007), *appeal pending*, *Verizon v. FCC*, Docket No. 08-1012 (D.C. Cir. filed Jan. 14, 2008). *See* AdHoc Comments at 5. The *Computer III* non-structural safeguards to which the Commission was referring in that order were the existing basic and enhanced service categories and comparably efficient interconnection (CEI) and open network architecture (ONA) requirements, *id.* ¶ 4, none of which is the subject of Verizon's Petition.

would granting Verizon's Petition "circumvent" those safeguards. AdHoc Comments at 2-3; Sprint Nextel Comments at 12. The essence of the safeguards adopted in the *Non-Dominant Order* are the imputation and transparency requirements. *Non-Dominant Order* ¶ 95. Even if granted forbearance relief, Verizon would continue to be required to record the charges for any access services provided to its in-region, long distance operations in account 32.5280, and these imputed amounts would be included in the biennial audit of Verizon's cost allocation manual. Time Warner's complaint that these imputation amounts must also then still be reflected in a particular ARMIS report elevates form over substance. Time Warner Comments at 5-6.

## VI. IT IS PAST TIME TO ELIMINATE ARMIS REPORTING.

More than six years ago the Commission concluded that the right question was not *whether* the ARMIS reports should be eliminated – "but rather *when*." *Phase Two Order* ¶ 206 (emphasis added). Since the *Phase Two Order*, the remaining Bell Operating Companies ("BOCs") – AT&T, Qwest, and Verizon – have lost approximately 25 percent of their switched access lines,[19] and, as discussed above, competition in the communications marketplace has exploded.

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[19] *Compare* SBC, *Investor Briefing* at 16 (Jan. 28, 2003) (http://www.att.com/Investor/Financial/Earning_Info/docs/4Q_02_IB_FINAL.pdf) (57,083,000 total switched access lines) and BellSouth Press Release, *BellSouth Reports Fourth Quarter Earnings* (Jan. 23, 2003) (http://bellsouth.mediaroom.com/index.php?s=press_releases&item=2093) (24,600,000 total access lines; *with* AT&T Inc., *Investor Briefing: 4th Quarter 2007* at 23 (Jan. 24, 2008) (http://www.att.com/Investor/Financial/Earning_Info/docs/4Q_07_IB_FINAL.pdf) (61,582,000 total switched access lines); *Compare* Verizon, *Investor Quarterly 4Q 2002* at 13 (Jan. 29, 2003) (http://investor.verizon.com/financial/quarterly/vz/4Q2002/4Q02Bulletin.pdf?adfds) (57,974,000 total switched access lines) with Verizon, *Investor Quarterly Q4 2007* at 17 (Jan. 28, 2008) (http://investor.verizon.com/financial/quarterly/vz/4Q2007/4Q07Bulletin.pdf) (41,441,000 total switched access lines); *Compare* Qwest Press Release, *Qwest Communications Reports Fourth Quarter and Full-Year 2002 Unaudited Results* and *Fourth Quarter Financials*, Attachment E (Feb. 19, 2003) (http://phx.corporate-ir.net/phoenix.zhtml?c=119535&p=irol-reportsOther) (17,006,000 total access lines) *with* Qwest Press Release, *Qwest Reports Fourth Quarter And*

Attempting to manufacture a legitimate present need for the ARMIS reports, opposing commenters largely ignore the reasons the Commission established the reports in the first place. Most ARMIS reports were designed for a rate-of-return regulatory regime, and the Commission has long expected to eliminate the reports. Commenters that suggest the reports have perpetual relevance in a competitive market under a price cap regime are wrong.

There are generally three varieties of ARMIS reports – financial reports, service quality reports, and infrastructure reports. The Commission adopted the original ARMIS financial reports more than 20 years ago to "facilitate the timely and efficient analysis of revenue requirements and rates of return ...."[20] Other ARMIS financial reports were adopted because "forecasts of relative use were identified ... as key elements in the accurate allocation of costs on a cost causal basis because many costs are incurred in anticipation of future demand rather than in response to the current level and pattern of demand for service." *ARMIS Order* ¶ 45.

The ARMIS financial reports primarily contain cost data that relates only to rate-of-return regulation. Even after moving to price cap regulation in the 1990s, the Commission only preserved the ARMIS financial reports to monitor the transition to price caps.[21] The Commission also added the ARMIS service quality and infrastructure reports to: (1) respond to concerns about the transition to price cap regulation; (2) accumulate data to facilitate the

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*Full Year 2007 Results –Continued Growth In Net Income And Free Cash Flow*, Attachment D (Feb. 12, 2008) (http://phx.corporate-ir.net/phoenix.zhtml?c=119535&p=irol-reportsAnnual) (12,789,000 total switched access lines).

[20] *Automated Reporting Requirements for Certain Class A and Tier 1 Telephone Companies (Parts 31, 43, 67, and 69 of the FCC's Rules)*, Report and Order, 2 FCC Rcd 5770, 5770 ¶ 1 (1987) ("*ARMIS Order*").

[21] *Policy and Rules Concerning Rates for Dominant Carriers*, Order on Reconsideration, 6 FCC Rcd 2637, 2730 ¶ 198 (1991) ("*Carrier Rate Order*").

Commission's review of the price cap regime; and (3) out of "an abundance of caution." *Carrier Rate Order* ¶ 179.

Under price cap regulation, now itself more than 16 years old, the cost information in the ARMIS financial reports is irrelevant. Price caps are cost agnostic. And in today's environment, even if the Commission were to make adjustments to its price cap regime, those changes must foremost be driven by the competitive landscape and not a regressive analysis of carrier costs as some commenters suggest. *See, e.g.*, Sprint Comments at 15-18. In that connection, commenters generally do not dispute – nor could they – that the original purpose of the ARMIS financial reports has vanished.

Moreover, the vibrant competition of the last several years has also washed away any remaining justification for even the ARMIS service quality and infrastructure reports. As discussed above, with a host of competitive choices today, customers seeking voice service increasingly are purchasing service from non-ILEC providers, including cable companies, wireless carriers, and independent VoIP providers. Contrary to the claims of opposing commenters, in such an environment it is a choice among competitors that ensures just and reasonable rates, protects consumers and drives innovation, not arcane regulatory reporting requirements applicable to only a few among many competitors.[22]

Indeed, even if the ARMIS reporting process added material value in a competitive market, which it does not, any potential value is lost in the application of the reporting requirements themselves. The requirements apply only to a small subset of ILECs, and in some cases only to AT&T, Verizon, and Qwest. Competitive LECs, cable companies, wireless

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[22] *See, e.g.*, Sprint Comments at 23; Joint Comments and Opposition of the New Jersey Division of Rate Counsel and the National Association of State Utility Consumer Advocates ("NASUCA Comments") at 28-29.

carriers, and independent VoIP providers are not subject to *any* ARMIS reporting requirements. Neither consumers, the Commission, state commissions, nor even ILEC competitors could possibly make informed choices by analyzing narrow categories of data from only a limited number of providers.

Several commenters simply waive their hands at fundamental changes in the market over the last several years. AdHoc, for example, argues that intermodal competition is "simply irrelevant to the level of competition for special and switched services." AdHoc Comments at 16. Likewise, NASUCA argues that because ILECs retain a substantial share of the market for end user switched access lines, the ARMIS reports must be retained. NASUCA Comments at 19-20. Such arguments miss the point entirely.

Only by artificially defining a narrow market do opposing commenters attempt to justify continued regulation, and even with that definition their justification falls flat. As the huge line losses suffered by Verizon and other ILECs prove, even traditional basic phone service can be delivered through a variety of technologies. Still, opposing commenters dismiss intermodal competition and customer choice incentives by blindly concluding that while available, intermodal alternatives cannot be considered alternatives to traditional wireline service. Ad Hoc Comments at 15-16; NASUCA Comments at 17. This view is misguided and simply wrong.

Several opposing commenters also support retaining the ARMIS reports because of the claim that ARMIS financial data is needed to pursue new special access regulation in other, unrelated proceedings. *See, e.g.,* Sprint Comments at 19; Time Warner Comments at 5. As Verizon and other carriers have repeatedly explained, these segment-specific ARMIS data are *not* accurate reflections of a carrier's actual returns, but rather are artifacts of the Commission's rules for allocating network investment among services. The need to allocate shared and

common costs in the ARMIS financial reports means that this process will inevitably yield arbitrary results. The Commission has been clear on this point: The accounting rates of return reported in ARMIS do "not serve a ratemaking purpose."[23]

ARMIS reports themselves do not even provide rates of return – they merely provide cost and revenue data that some parties have used to try to calculate returns. ARMIS data suffer from shortcomings that make them unreliable both for analyzing returns in any given year, and for comparing annual returns over time.[24] The ARMIS accounting categories for special access do not track the economic costs for these services, but are driven instead by artificial regulatory considerations such as jurisdictional separations and divisions between regulated and nonregulated services. Taylor Supp. Decl. ¶ 44. Relatedly, the ARMIS cost categories were subject to a separations freeze in June 2001 that distorts any attempt to use these data to approximate special access rates of return.[25] The freeze was implemented "to provide stability and simplification for the separations process pending comprehensive reform." *Separations Freeze Order* ¶ 10. Having determined that it made no sense to make carriers endure the "regulatory burden" of recalibrating their cost allocations "during the transition from a regulated monopoly to a deregulated, competitive environment in the local telecommunications marketplace," *id.* ¶ 13, it would be arbitrary and capricious for the Commission to rely on those frozen categories as a proxy for the costs of providing special access that carriers incur today.

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[23] *Carrier Rate Order* ¶ 199.

[24] *See* Comments of Verizon, *Special Access Rates for Price Cap Local Exchange Carriers*, WC Docket No. 05-25 & RM-10593, at 43 (Aug. 8, 2007) *citing* Attachment A, Supplemental Declaration of Dr. William E. Taylor on Behalf of Verizon ("Taylor Supp. Decl.") (April 8, 2007).

[25] *See Jurisdictional Separations and Referral to the Federal-State Joint Board*, Report and Order, 16 FCC Rcd 11382 (2001) ("*Separations Freeze Order*").

ARMIS is simply not a useful tool in the special access context, either for measuring absolute special access rates of return in a given year or for assessing trends in such returns from year to year. Taylor Supp. Decl. ¶ 44.

Commenters also offer other various unsupported theories in an attempt to ensure Verizon remains saddled with the outdated and unnecessary ARMIS reporting requirements. None of these miscellaneous arguments has merit. For example, AdHoc suggests that ARMIS reports are necessary for the "average variable cost showing" that a price cap carrier must make when its tariff filings include rate changes below the pricing bands established by the Commission. AdHoc Comments at 7. First, the lower service band indices that AdHoc references were eliminated in 1996, and the low-end adjustment mechanism was eliminated in 1999.[26] Second, the Commission's rules do not mandate the use of ARMIS reporting in this context and/or for this application. ARMIS reporting is based on incurred booked costs and does not reflect variable and/or forward-looking costs. Nor are ARMIS reports necessary for establishing exogenous cost changes under 47 C.F.R. § 61.45(d). *See* AdHoc Comments at 7-8; Sprint Nextel Comments at 16-17. The exogenous adjustments listed in Section 61.45(d) present no obstacle to granting forbearance because (1) none of these exogenous adjustments requires use of or relies upon ARMIS reporting; and (2) Verizon will continue to allocate investment and

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[26] *See Access Charge Reform; Price Cap Performance Review for Local Exchange Carriers; Transport Rate Structure and Pricing; Usage of the Public Switched Network by Information Service and Internet Access Providers*, Notice of Proposed Rulemaking, Third Report and Order, and Notice of Inquiry, 11 FCC Rcd 21354, 21485-86, 21487-88 ¶¶ 301, 305 (1996); *Access Charge Reform; Price Cap Performance Review for Local Exchange Carriers; Interexchange Carrier Purchases of Switched Access Services Offered by Competitive Local Exchange Carriers; Petition of U S West Communications, Inc. for Forbearance from Regulation as a Dominant Carrier in the Phoenix, Arizona MSA*, Fifth Report and Order and Further Notice of Proposed Rulemaking, 14 FCC Rcd 14221, 14235, 14253 ¶¶ 25, n.56, 162 (1999) (eliminating the low-end adjustment mechanism for price cap LECs that elect to exercise either Phase I or Phase II pricing flexibility).

expense accounts consistent with Part 32 and Section 64.901, and thus the information necessary to evaluate any exogenous adjustments will remain available.

At bottom, the current ARMIS reporting process was designed as a temporary check to ensure that price cap regulation functioned properly. Whatever the value of the ARMIS reports had at the start of the price cap regime, they are inappropriate now under the current regulatory regime in today's competitive market. The Commission should no longer burden only a few among many providers with cumbersome and unnecessary ARMIS requirements. It is past time to eliminate the ARMIS reports.

## VII. THE COMMISSION SHOULD FORBEAR FROM CONTINUED APPLICATION OF ITS AFFILIATE TRANSACTION RULES.

In its Petition, Verizon demonstrated that the affiliate transaction rules involve a complex and time-consuming exercise that is unnecessary to ensure Verizon's rates are just, reasonable, and nondiscriminatory or to protect consumers. First, the process of documenting, tracking, and recording transactions in accordance with the Commission's affiliate transaction rules does not ensure that Verizon's rates are just, reasonable, and nondiscriminatory because, under price cap regulation, the costs that Verizon records on its books as a result of these rules have no bearing on interstate rates. Ratepayers are also protected in this regulatory environment by the maximum caps on prices that Verizon may not exceed. Second, this process does not protect consumers because, as a publicly held company, Verizon already is required to maintain accurate records to ensure that the provision of services or the purchase, transfer, and retirement or disposition of assets are made in accordance with Verizon policies and are properly valued in the Company's financial records. Verizon's Petition also demonstrated that continued application of the affiliate transaction rules is not in the public interest because, when applicable, they can constrain Verizon in the marketplace to the detriment of customers by adding to the complexity of

introducing innovative offerings – a complexity that the vast majority of Verizon's competitors do not face.

Few commenters address the affiliate transaction rules, and none make any serious attempt to justify continued application of these rules. For example, the Michigan PSC disclaimed any need for the Commission's affiliate transaction rules. Michigan PSC Comments at 5. Likewise, the Wisconsin PSC expressed only a lack of clarity concerning the "impact" that forbearance from the affiliate transaction rules would have on its legislative mandate to oversee transactions between Wisconsin utilities and their affiliates (even assuming this impact were relevant to the Commission's forbearance analysis, which, as explained above, is not the case). Wisconsin PSC Comments at 4. The New York PSC insists that the affiliate transaction rules are "helpful" in identifying cross-subsidies, New York PSC Comments at 2, although it does not explain how the rules are useful in this regard. Furthermore, the standard is not whether regulatory requirements are "helpful" but whether they are "necessary" to serve a federal purpose – an issue the New York PSC does not address.

NASUCA expresses "doubt that affiliate transaction reporting prevents Verizon from introducing new products," pointing to Verizon's rollout of its FiOS services. NASUCA Comments at 26. In the competitive market in which it operates, Verizon has no choice but to innovate. Verizon's efforts, however, can be frustrated by the affiliate transaction rules when they apply. In its petition, Verizon provided specific examples of fair market value studies Verizon was required to complete under the affiliate transaction rules, which are only part of the complicated and burdensome maze of regulation for valuing and pricing certain transactions imposed by these rules, that can constrain provisioning of new services customers want. No

rational commercial entity would conduct its business in this manner, and neither NASUCA nor any other commenter contends otherwise.

NASUCA argues that the "marginal cost" of complying with the Commission's affiliate transaction rules (as well as the other recordkeeping and reporting requirements that are the subject of Verizon's Petition) is minimal if the information is reported elsewhere. NASUCA Comments at 35-36. This argument misses the mark because it overlooks the excruciating and unnecessary level of detail and complexity required by the Commission's affiliate transaction rules. Where the affiliate transaction process applies Verizon must: (1) identify each affiliate that would be transferring or providing goods or services in connection with a new good or service; (2) determine whether a tariff or interconnection agreement exists for each such good or service and, if so, record the price from that tariff or agreement; (3) for those goods and services for which no tariff or interconnection agreement exists, determine whether the 25 percent threshold has been satisfied on an asset-by-asset basis and service-by-service basis in order to record the value of the product or service at the prevailing market price; (4) calculate the fair market value of the product or service when neither a tariff nor interconnection agreement exists and in the absence of a prevailing market price; (5) calculate net book costs or fully distributed costs; and (6) compare the estimated fair market value of the product or service to its net book cost or fully distributed cost, depending upon whether a product or service is involved and the total aggregate annual value of the asset or service used.

Requiring Verizon to engage in such an exercise is pointless, particularly given the myriad other financial safeguards to which Verizon is subject as a publicly held company, including GAAP, the Sarbanes-Oxley Act, and the Foreign Corrupt Practices Act, which require that Verizon maintain detailed records accurately and fairly reflecting transactions and

dispositions of Verizon's assets. These safeguards provide more than adequate inducement for Verizon to properly record transactions with its affiliated entities.[27]

## VIII. THE COMMISSION SHOULD FORBEAR FROM CONTINUED APPLICATION OF ITS RATE-OF-RETURN REPORTING RULES.

The Commission also should forbear from applying its rate-of-return reporting rules – the rules set forth in Part 69, Subparts D and E as well as the rate-of-return monitoring report, as required by Part 65, Subpart E. First adopted more than 25 years ago, the rules in Subparts D and E were designed for developing access charges for rate-of-return carriers.[28] Under today's price cap regime, these rate-of-return reporting rules have no effect on Verizon's rates and are not necessary to ensure that Verizon's rates are otherwise just, reasonable, and nondiscriminatory or to protect consumers. Report 492A, the rate-of-return monitoring report, similarly has no bearing on Verizon's price-cap regulated rates or the protection of consumers. Forbearance from these rules is also consistent with the public interest because the rules serve no valid regulatory purpose and apply only to a limited number of competitors.

Few commenters address the rate-of-return reporting rules, even in passing. Time Warner's argument that forbearance from these rules would "prevent" the Commission from "being able to measure Verizon's rate of return for its different access elements ..." is nonsensical. Time Warner Comments at 3 n.6. First, there is no need for the Commission to

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[27] AdHoc argues that GAAP, the Sarbanes-Oxley Act, and the Foreign Corrupt Practices Act are irrelevant because "[o]nly the FCC's rules require the tracking and allocation of costs between services and between non-competitive (regulated) and competitive (unregulated) services." AdHoc Comments at 14-15. This argument is a red herring, since, as discussed above, Verizon's Petition does not seek forbearance from the Commission's cost allocation rules.

[28] *Access Charge Reform; Price Cap Performance Review for Local Exchange Carriers; Transport Rate Structure and Pricing; Usage of the Public Switched Network by Information Service and Internet Access Providers*, Notice of Proposed Rulemaking, Third Report and Order, and Notice of Inquiry, 11 FCC Rcd 21354, 21380 ¶ 52 (1996).

"measure" Verizon's rate of return because the price cap regime regulates prices, not earnings.[29] Second, as explained above, these reports are *not* accurate reflections of a carrier's actual returns, but rather are artifacts of the Commission's rules for allocating network investment among services.

Equally misguided is Sprint Nextel's argument that report 492A (and ARMIS financial reports) would "assist the Commission" if it determines that price caps need "to be reinitialized." Sprint Nextel Comments at 16. The Commission has made no determination to reinitialize price caps. Indeed, doing so would run counter to the Commission's expectation that competition will dictate just and reasonable prices, not a new federal regulatory regime.[30] Requiring Verizon to collect and report data in perpetuity under rate-of-return reporting rules in the unlikely and hypothetical event that the Commission decides to reinitialize price caps at some point in the future (and decides to do so based upon antiquated reporting rules versus more relevant data) is a solution looking for a problem. Denial of forbearance for this reason would be arbitrary and capricious and would run afoul of the deregulatory purpose of the 1996 Act. *See AT&T, Inc. v. FCC,* 452 F.3d at 836.

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[29] *Policy and Rules Concerning Rates for Dominant Carriers,* Second Report and Order, 5 FCC Rcd 6786, 6789 ¶ 22 (1990).

[30] *See Access Charge Reform; Price Cap Performance Review for Local Exchange Carriers; Low-Volume Long Distance Users; Federal-State Joint Board On Universal Service*, Sixth Report and Order in CC Docket Nos. 96-262 and 94-1, Report and Order in CC Docket No. 99-249, Eleventh Report and Order in CC Docket No. 96-45, 15 FCC Rcd 12962, 12969 ¶ 16 (2000) ("*CALLS Order*") ("... price caps act as a transitional regulatory scheme until the advent of actual competition makes price cap regulation unnecessary"), *aff'd in part, rev'd in part, and remanded in part, Texas Office of Public Utility Counsel v. FCC,* 265 F.3d 313 (5th Cir. 2001); *Petition for Waiver of Pricing Flexibility Rules for Fast Packet Services,* Memorandum Opinion and Order, 20 FCC Rcd 16840, 16848 ¶ 14 (2005) (price cap regulation "was designed to replicate some of the efficiency incentives present in competitive markets and to act as a transitional regulatory mechanism en route to full competition").

## IX. THE COMMISSION SHOULD FORBEAR FROM CONTINUED APPLICATION OF ITS PROPERTY RECORD RULES.

Verizon also has made the requisite showing for forbearance from the Commission's property record rules. The property records that Verizon must maintain under these rules are completely unnecessary to ensure Verizon's rates are just, reasonable and nondiscriminatory. These rules were developed under rate-of-return regulation and serve no valid purpose under price cap regulation. Verizon's interstate rates are unaffected by underlying accounting costs or the property records the Commission's rules require that Verizon continue to maintain. Nor are the Commission's property record rules necessary to protect consumers in today's competitive marketplace. Other accounting safeguards and controls such as GAAP that apply to all publicly traded companies adequately protect consumers in virtually all other markets and are more than sufficient here. As is the case with the other recordkeeping and reporting requirements that are the subject of Verizon's Petition, forbearance from the Commission's property record rules also is in the public interest because the rules serve no valid regulatory purpose and distort competition by imposing costs on a small subset of competitors.

Few commenters address the property records issue, although one commenter does acknowledge that "a reduction in the current standards related to continuing property records may be appropriate." Michigan PSC Comments at 6. More than a "reduction" is necessary, particularly when the Commission concluded that it should have eliminated its property record rules three years ago. *Phase Two Order* ¶ 212. No commenter attempts to reconcile the Commission's conclusion to eliminate its property record rules with demands for continued compliance with those rules.

There is no merit to NASUCA's claim that "regulators' access to detailed property records is essential to ensure that costs are not being erroneously assigned and allocated to non-

competitive services." NASUCA Comments at 31. The Commission's property record rules specify in detail the information that an incumbent LEC must maintain for all plant accounts, including detailed descriptions of the property, location information, date of placement into service, and original cost data and supporting records. *See, e.g.*, 47 C.F.R. § 32.2000(f). The Commission's property record rules do not address, and having nothing to do with, the allocation of costs between regulated and nonregulated services.

In addition, the Michigan PSC's concern that forbearance from the property record rules will somehow make Verizon's infrastructure more vulnerable to damage is misplaced. Michigan PSC Comments at 6. As a matter of sound business practice, Verizon maintains sufficient records to safeguard and protect its network infrastructure. Moreover, Verizon's required compliance with GAAP, the Sarbanes-Oxley Act, and other accounting safeguards and controls already protects assets from physical loss and ensures that asset purchases, transfers, and retirements or dispositions are made in accordance with management's authorization and are properly valued in the company's financial records.

## X. CONCLUSION.

For the foregoing reasons, the Commission should grant Verizon's Petition for Forbearance.

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