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**IMMEDIATE FUNDING AND PARTNERS:
TAKE A BLOW TORCH TO THE FCC'S ACCOUNTING FREEZE**

The IRREGULATORS have until April 12th, 2019 to appeal a recent FCC decision that tries to bury one of the largest accounting scandals in American history. It is critical that the FCC be required to admit to the issues and then deal with the ramifications. The FCC has allowed the telecoms to engage in accounting shenanigans, and this impacts every current FCC proceeding, pricing at the state level for basic service and, ultimately all communications services in America. It determines who gets high-speed broadband, has led in part to the Digital Divide, controls what price we pay, and has been a major driver for the lack of serious competition for local transmission facilities and services.

We found a 'structural flaw' in every FCC decision. Appealing this case provides a way to attack virtually every current and past FCC proceeding that has given the store away to the telecoms, from Net Neutrality to copper retirement and 5G.

This case could also open up many state decisions, especially those created with the help of ALEC, the American Legislative Exchange Council, which has created model legislation – written by AT&T and Verizon, then handed to their politician members to push through. We note that the FCC's 5G regulations are based on an ALEC bill.

The FCC's cost accounting rules were "frozen" to mimic the year 2000. The rules now assign the majority of all expenses to "intrastate" and basically force state commissions to raise basic rates, even though a huge portion of these expenses are related to activity that has little or nothing to do with basic residential landline service. The FCC has purposefully refused to audit or investigate how their rules impacted basic local rates, or drove federal decisions in other cases. They have never even admitted the harm to consumers and competition. The IRREGULATORS filed in this bizarre proceeding and exposed the whole charade. But the FCC once again refused to acknowledge the problem and extended the 'freeze' for 6 more years in December, 2018.

We have standing to take this appeal and the expertise in the legal, regulatory, and financial analysis areas. Our approach and data could make this case stick and if it does it will blow up the FCC's entire collection of decisions and current proceedings using the structural flaw.

At the same time, we believe that this proceeding, combined with what we have uncovered, could be used to help cities and states take back the infrastructure that they paid for, including solving the Digital Divide and a new path for bringing back competition.

Over the last decade, New Networks Institute and IRREGULATORS have made some startling discoveries. We have focused on Verizon NY, the only state telecommunications

utility we know of that publishes a full annual report. Moreover, in July 2018 there was settlement of Verizon NY with the NY Public Service Commission. Estimated at \$300-500 million, and based in part on our work, Verizon NY is required to upgrade 32,000 lines to fiber optics and maintain the existing copper networks that are not upgraded. And in 2012, we helped Stow Creek and Greenwich NJ get upgraded to fiber.

The History of Broadband in America was Rewritten.

AT&T originally controlled most of the incumbent state telecommunications utilities. In 1984, AT&T was 'broken up' because it had abused its monopoly controls over America's landline infrastructure. Ma Bell was divided into 7 regional local exchange companies. AT&T's "long distance" operations were spun out into a separate company. The original 7 local monopolies have collapsed into a mere 3, and they are even bigger than before. After a series of mergers where the Baby Bells married their siblings (a act against nature), Southwestern Bell had bought up Pacific Telesis (CA), SNET (a non-bell, which controlled CT), Ameritech (5 mid-west states), then took over AT&T and renamed itself again, and bought Bellsouth, (southern states) and now controls many wireless licenses. Bell Atlantic merged with NYNEX to control the East Coast, then renamed itself Verizon when it merged with the old GTE (a previous non-Bell independent), and also took over MCI and also controls many wireless companies. US West, renamed itself Qwest and was purchased by CenturyLink (another independent that mostly operated in rural areas), and that company also owns several other companies that used to compete with the 3 monopolies.

These were all copper-based networks. They got perks from utility status, but they also had to service their entire territory. They still get the perks, but the duty to serve is going away. They received major tax breaks and were allowed to raise basic local rates. These companies were all supposed to use the breaks and increased revenues to make major investments in local fiber networks to provide residential broadband and serve schools, libraries and hospitals. The fiber was supposed to be part of the local utility and regulated as such. But it was all a lie. The fiber to the home upgrades never really happened, and most of the fiber that was placed now serves the telecom's other, unregulated activities. Basic local ratepayers paid for this fiber pig, but all they got was an empty poke.

Manipulation of the Accounting Rules

The FCC under Powell, with now-AT&T, Verizon and CenturyLink, realized there were many reasons to remove the states' power and so in 2001, the FCC 'froze' the cost accounting rules to reflect the year 2000. In 2001, Local Service was 65% of the state utility revenues and it paid 65% of the expenses.

AT&T et al. figured out that freezing the accounting would make 'Local Service' look unprofitable and the freeze would move the majority of all expenses into Local Service, the classification for the basic, copper-based, phone service.

The companies started moving services using these wires to the unregulated categories, either “information services” or wireless. Even though most of the costs were assigned to intrastate the wires were called interstate “special access” (now Business Data Services, but is also known as “backhaul”). These “interstate” services use the construction budgets of the intrastate utilities and, even worse, paid what they had in the year 2000. As revenues increased, the percentage of expenses remained “frozen.” Interstate services paid a fraction of the expenses, from “marketing” to “corporate operations”.

To recap: There still are state telecommunications utilities, but are in the process of being dismantled. It was and still are mainly copper wires, but was supposed to be replaced with fiber optics starting the in 1990’s. By 2001, the companies decided to make the utilities look unprofitable, and had the FCC ‘freeze’ the rules to the year 2000. At the same time, the companies started using the copper utility wires and the fiber they placed using local revenues to service “interstate” and “information” services. The basic local customers of the state-based utilities had to pay the majority of the expenses even though they never used the wires and never got much of the promised fiber to the home.

Forbearance of the Rules

By 2007, the companies all filed for “forbearance” of the rules, i.e., the rules would stay in place but they would not be “enforced.” The FCC agreed, but left a caveat that they would have to sign letters of compliance, that they were not having Local Service cross-subsidize the other lines of business. The FCC also erased the requirements to file financials and business information with the FCC. The FCC stopped publishing the Statistics of Common Carriers, which started in 1939.

Where We Are

In 2017, FCC Chairman Ajit Pai started “weed whacking.” He sought to remove whatever remaining accounting rules that were still in place. He did so to prevent anyone from following the money. During the last 2+ years the FCC has created over 25 interlocking proceedings that will ultimately dismantle the state utility operations and hand over the wires to the major telecoms. Ratepayers funded the networks, but they are getting flushed. Pai wants to give it all to the companies for their own use, mostly for the incumbent-owned wireless companies, none of which are price-regulated at the state or federal level. 5G – the latest “savior” – is merely the latest bait-and-switch.

What We Uncovered using the Verizon NY Annual Reports and the Investigation

Everything you heard from the FCC or the telecoms has been manipulated. We have created a “Walk Through” and a “How to read the Verizon NY Annual Reports Picture Book” to simplify the findings.

In 2017, Verizon New York had \$5 billion in revenues; Local Service was \$1.1 billion, while “Access Fees” (the backhaul for wireless that is called “special access”) was \$2.5 billion. The rest is “nonregulated”, which includes FiOS video, as well as VoIP

The Local Service losses are artificial.

- Local Service (basic phone lines) was charged \$1.2 billion in construction and maintenance, even though only an estimated \$100 million was spent on the copper lines. Local Service was overcharged over \$1.1 billion in construction. This \$1.1 billion was related to servicing unregulated wireless service, and even though the costs were assigned to intrastate the services and revenues were called interstate.
- Local Service was charged \$1.8 billion in Corporate Operations, 62% of the total. This is the executive pay, corporate jets and lawyers, and should not have been charged to basic local service, which does not even advertise anymore. Note: the 60%+ charged to Local Service was caused by the FCC’s cost accounting rules.
- These 2 expense items, with the other items, like Marketing, made Local Service unprofitable and it lost \$2.9 billion. Verizon New York claimed losses of \$2.6 billion and a ‘tax benefit’ of \$948 million.

On Prices;

- Local Service went up 95% since 2006 due to rate increases intended to fund fiber to the home that never happened, and then claimed losses. Ancillary services, like nonlisted numbers or inside wire maintenance, had increases of 50-525%.
- Local Service, based on actual expenses, should have been in steep decline; instead customers were “harvested”.

On Subsidiaries and Cross-Subsidies

- Verizon Wireless only paid \$104 million for use of the Verizon New York infrastructure and there were Zero payments for the construction expenses. From 2010-2012, we estimate that Verizon Wireless should have paid \$2.8 billion to Verizon NY, the state utility.
- Access Services paid ½ of what Local Service paid for construction and maintenance and the other services – making it profitable with a 50+ EBITDA, as were all of the ‘interstate’ services.

Note: This is only part of the story. There is an estimated \$7-10 billion in extra revenues, mainly from Verizon Wireless, Verizon Online and Verizon Business in New York State.

And more importantly, due to the FCC’s cost accounting rules, which are federal, the ugliness of Verizon NY’s financials are almost identical in every state, as far as we can tell.

Access Line Manipulation

The FCC, the phone companies and their paid pundits claim that there were major access line losses. This has been accepted as “common wisdom.” But these numbers have been manipulated as well.

Verizon NY had 1.9 million POTS lines at the end of 2017, down from 2.1 million in 2016. But, this accounting is based on just Local Service with \$1.1 billion in revenue. This means that Verizon NY, with \$5 billion in revenues, has Zero lines for \$4 billion. The access lines are still largely there, they have just been disappeared into accounting oblivion.

Nationwide, this is happening in every state, in varying degrees, based on the last data published by the FCC in 2007. The Verizon NY’s own financials, etc. given to the NY PSC is the only state we know of that requires the data.

Impacts

Whether intentional or not, making the wired networks and Local Service unprofitable had many benefits to Verizon et al. Remember, this started 19 year ago and they ALL had to be part of this plan.

- Billions in tax savings per state—Verizon NY has averaged over \$2 billion annually in losses since 2009.
- Making Local Service unprofitable got the companies rate increases and other tax perks. Every phone line was overcharged \$2,760.00 in New York since 2006
- Claiming rural areas were unprofitable to build out got the companies multiple financial tax perks. AT&T et al. all claimed that they didn’t have to upgrade the rural areas, even though they are state utilities.
- Help to the telcos. Making the networks appear unprofitable helped to eliminate union jobs, get regulatory favors and the illusion was used to shift public opinion

Structural Flaw and Flawed FCC Decisions.

The FCC has used the manipulated data to claim that even more give-aways are necessary to drive “investments” that were already promised but never delivered. You see this in the latest Net Neutrality decision claiming that “utility” treatment harmed investment in broadband, special access and 5G. It has been used to justify cutting off the copper networks, even though this infrastructure is still used and could be used even more. The FCC says the lack of investment led to the Digital Divide when in fact it was the rules changes and the telecoms’ own greed and broken promises that created the problem. Every one of these decisions are wrong and based on fake data. They quit requiring the real data that should have been available and used.

The most disturbing part of this is the 75%-25% rule that requires 75% of construction be paid for by intrastate basic local users even though little to none of the construction

relates to basic service and the funds have been diverted and manipulated by the FCC's cost accounting rules.

Our filing included a complete report detailing the failure of the FCC to supply an accounting of all access lines. As we noted, Verizon NY had \$5 billion in revenues, and Local Service was \$1.1 billion but there was Zero access lines supplied for the \$4 billion in "interstate" revenues.

Not one FCC decision has included the 'intra-state', state-based utilities –on any topic. In 1998, New Networks Institute filed with the FCC detailing that their "advanced network" reports that examine the timely and reasonable fashion of broadband was pure hokum. One-half of the US was supposed to have been upgraded to fiber optics – used to provide broadband to the home – by 2000. But it never happened even though ratepayers supplied the funds. We filed 22 times about this and included three separate books detailing the state-based broadband commitments that were never included in any year.

The FCC's Decisions to 'Extend the Freeze' is Flawed

- The FCC has no data to continue the Freeze, and should have started investigations.
- The FCC refuses to consider intrastate data, other financials, the broken broadband commitments, massive local increases that fund other lines of business.
- The FCC never audited or examined the harms caused by the Freeze distortions.
- The FCC claims that the 'freeze' does not apply to 'price caps' carriers—i.e., AT&T et al., but Appendix 1 of the decision has new language that extends the freeze for price cap carriers for 6 more years.
- The FCC was required to examine the change to 'interstate' revenues on an annual basis and never checked for 19 years.
- The FCC's Brendan Carr was Verizon's attorney in the 2007 forbearance petition and now is working on the same issues.
- The FCC ignored our multiple filings in this and the related cost allocation rules. It has removed Part 32, Part 36 and other parts of the accounting rules with no investigation of our claims or any checking of the harms to intrastate customers.
- The FCC claims no one is using these rules, yet they were part of the Verizon New York 2017 settlement and are part of the Verizon New York Annual reports. – We call these Zombie rules.
- The FCC's 19 years of negligence has led to a pattern of harms that should have been dealt with long ago. But the FCC does not want to fix the rules; it prefers to keep the distortions in place so its evil plan can be carried out to the end.
- The Verizon New York annual report shows how the rules created massive financial cross-subsidies, artificial losses that were used for artificial rate increases and tax benefits. By making Local Service appear unprofitable, Verizon 'harvested' the wireline customers and force-marched customers onto unregulated wireless.

- The price of Local Service had continuous increases, violating Section 201 of the Telecom Act, as the cost accounting rules were applied by the state.
- Forbearance Petitions we all based on violations of Section 254(k) and potential perjury. Starting in 2007, AT&T, Verizon and Centurylink all filed “compliance letters” attesting they had not cross-subsidized unregulated services with revenues obtained from regulated networks. But the fact is the claimed “losses” were fake; billions of dollars of construction were used to fund and support wireless but were charged to local phone customers.
- The FCC has made no effort to figure out how many states are still applying these accounting rules in 2018.
- The FCC made no effort to include the public as none filed, except for the telcos, their associations and related astroturf organization wonks.
- The FCC’s Pai admitted in an interview with Re/Code, 2017 that neither he nor any of his staff ever examined any of the accounting rules.
- The FCC never put out any information about the rules and continually claimed they needed weed-whacking.
- We will ask the court to require the FCC to start immediate proceedings to examine every FCC decision that relied on these accounting failures and all proceedings that failed to include the ‘intrastate’ financials, including all construction budgets, or the manipulation of the access lines.

Chevron Deference can’t be used when the agency of record doesn’t have any data—and we do.

In an interview with Ajit Pai, the Chairman claims that his staff “pretty much never” examined the rules being removed:¹

“Re/Code: “In the early days, you had said that you wanted to take a weed-whacker to remove the rules that are holding back investment. What did you mean by that?”

“Pai: “What I had in mind were some of the regulations that we’ve had on the books for a while that stand in the way of investment in networks. Our Part 32 accounting rules—exceedingly boring, I recognize—but just the fact that companies have to maintain two different sets of books, literally one for their business and one for the FCC’s purposes, and the FCC hadn’t relied on any of that paperwork in years. **I asked our staff, ‘When was the last time you looked at these reports?’ They said, ‘Pretty much never.’** We wanted to relieve some of those.” (Emphasis added.)

We have been filing and writing reports specifically about the Freeze and the FCC cost accounting rules since 2014. We created 2 separate report series since 2015 to document

¹ <https://www.recode.net/2017/5/5/15560150/transcript-fcc-chairman-ajit-pai-net-neutrality-merger-recode-decode>

the freeze and harms including “The Hartman Memorandum”, (written with Paul Hartman, former FCC Asst Chief of the Pricing Policy division). And these have been filed in over 50 separate FCC proceedings.

PREVIOUS REPORTS: FIXING TELECOM REPORTS: 2015-2017

- [Report 1: Executive Summary: Verizon’s Manipulated Financial Accounting & the FCC’s Big “Freeze”](#)
- [Report 2: Full Data Report](#)
- [Report 3: SPECIAL REPORT](#) How Municipalities and the States can Fund Fiber Optic Wireline and Wireless Broadband Networks.
- [REPORT 4: Data Report](#) Verizon’s Wireline Networks Diverted Capex for Wireless Instead of Wiring Municipalities, and Charged Local Phone Customers.
- [Report 5: The Hartman Memorandum](#) proves that the FCC’s own cost allocation rules created massive financial cross subsidies.
- [Report 6: The History & Rules of Setting Phone Rates in America](#)
- Report 7: [SUMMARY REPORT](#): Verizon Massachusetts & Boston: Investigate the Wireless-Wireline Bait-n-Switch, January 17th, 2017
- Report 8: [Full Report](#): Verizon NY 2016 Annual Report Analyzed, June 2017.

Digital Divide by Design, Series 2018-

- [FILING: Comments filed in “The Big Freeze”](#) Docket 80-286 and FCC 18-99 -FURTHER NOTICE OF PROPOSED RULEMAKING
- REPORT 1: Did AT&T, Verizon, CenturyLink & the FCC Intentionally Create the Digital Divide? [FILED WITH COMMENTS](#):
- REPORT 2: Verizon New York 2017 Annual Report: An Analysis of Cross-Subsidies and Customer Overcharging [FILED AS REPLY COMMENTS](#)
- DESCRIPTION: This report, based on the Annual Report. shows that there is a utility and that it is hemorrhaging money because of the FCC.
- **REPORT 3:** Bell Access Line Accounting Manipulation 1984-2018 Verizon, AT&T, CenturyLink, and their association, USTelecom, with the help of the FCC, have manipulated the basic accounting of access lines, and have removed or hidden 80% of all lines, including all Business Data Services, (special access) DSL, competitor lines, FiOS, U-Verse, all of the wires to the cell sites or WiFi hot spots, alarm circuits. [FILED AS COMMENTS](#):

In short, the FCC has manipulated its data-reporting and accounting rules as part of a massive and long-running conspiracy to return us to the old monopoly days, but without the public interest regulation that came with monopoly. Basic ratepayers paid for fiber broadband and were supposed to competition. We got nothing but the finger. The courts must intervene. Help us make this final effort to restore sanity and fairness.

Who We Are: <http://irregulators.org/who-we-are/>