

Before the  
Massachusetts Department of Telecommunications and Energy  
Boston, Massachusetts

**C O M P L A I N T**

**ON THE NEED TO INVESTIGATE BELL ATLANTIC'S FAILED  
DEPLOYMENT OF ADVANCED NETWORKS AND THE IMPACTS ON  
CUSTOMERS**

**AND TO DENY BELL ATLANTIC'S ENTRY INTO THE LONG  
DISTANCE MARKETPLACE AT THIS TIME**

Filed by:  
**Bruce A. Kushnick**  
**NEW NETWORKS INSTITUTE**  
826 Broadway, Suite 900  
New York, New York 10003

and:  
**Peter J. Brennan**  
111 Perkins Street  
Jamaica Plain, Massachusetts 02130

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## STATEMENT OF INTEREST

New Networks Institute ("NNI") was founded in 1992. Its mission is to explore, on a totally independent basis, the impact of the break-up of AT&T and the creation of the Regional Bells Operating Companies ("RBOCs") on telephone subscribers in general and on the deployment of new and advanced telecommunications networks. Since that time, the NNI has conducted extensive research on these topics. Titled "The Future of the Information Age," this seven-year analysis consists of over 1,900 pages in 14 volumes, with over 910 exhibits, two computer databases, and data from more than 2,000 consumer interviews, (conducted independently through Fairfield Research). We have recently updated this research in the form of a new book, , *The Unauthorized Biography of the Baby Bells & Info-Scandal*, published March 1999. NNI's research is independently funded from the sales of the reports books, and databases. No company, lobbying organization, trade association or political party had any input, either editorial or financial.

Peter J. Brennan is the former co-chair of the White House Roundtable for Telephone Information Services, a joint project of the US Office of Consumer Affairs and the Interactive Services Association (now known as the Internet Alliance), a past chair and current director of the Internet Alliance. Brennan is a residential telephone subscriber, property-owner and taxpaying citizen of the Commonwealth.

Our reasons for filing this formal complaint are two-fold: The complainants believe that Bell Atlantic misled Massachusetts consumers and regulators with promises of advanced network deployments for the purpose of removing important pro-consumer regulation. This has led Bell Atlantic to not only garner excess profits from customers, but has also has stifled Massachusetts' ability to compete in the global digital economy, and denied customers new and advanced services. Therefore, we call upon the Department to audit Bell Atlantic's past execution of it promises, to review Bell Atlantic's pricing policies for all basic and enhanced services and, in view of Bell Atlantic's demonstrable bad faith, regulate the company to the full extent of its jurisdiction. Secondly, we offer this complaint in furtherance of our oral testimony in public hearings held by the Department relative to Bell Atlantic's "271" petition, requesting that the DTE deny Bell Atlantic's entrance the long-distance market in Massachusetts.

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## SUMMARY

In 1994, Bell Atlantic (then “NYNEX”) proposed a plan to rewire the Commonwealth of Massachusetts with new fiber optic technology, replacing the older copper wiring. Bell Atlantic represented that, if implemented, residential subscribers would soon have access to up to eight hundred channels of new services, including video-conferencing, movies on-demand and other enhanced cable television and online services. Bell Atlantic proposed that this new fiber optic technology would replace the copper wiring already in place. According to Bell Atlantic, 330,000 residential consumers would have access to the new fiber optic network by 1995, at a cost of \$500 million, and the rest of the Commonwealth would be connected subsequently.

Bell Atlantic proposed that they could only afford to make this considerable investment if the rate-of-return restrictions were relaxed at the state and federal level, in Massachusetts and elsewhere. Traditionally, rate-of-return restrictions capped Bell company profits at 10-12 % annually. Instead, they proposed “alternate regulations” that would allow them to become vastly more profitable, and promised those profits would be used to fund the development of the new services. Bell Atlantic sought regulatory relief from the Massachusetts Department of Public Utilities (now the Department of Telecommunications and Energy). They sought similar relief in every other state in which they were the incumbent local exchange carrier and from the Federal Communications Commission, on the basis of, substantially, the same promises to build a new network and offer new services.

The alternate regulations in Massachusetts went into effect in September 1995 and expire in 2001. In February 1995 the FCC granted Bell Atlantic’s petition to offer “video-dialtone” services. In 1996, Congress passed the Telecommunications Act, based on a record that included various Bell company promises of advanced network deployment, including those made by Bell Atlantic.

As a result of the alternate regulations, we estimate that Bell Atlantic garnered over one billion dollars in increased profit above the rate-of-return in Massachusetts alone. But they never built the new network, or deployed the new services that were the rationale for the regulatory relief. In fact, just months after being granted relief as an incentive to invest in the Massachusetts infrastructure, Bell Atlantic abandoned plans to build and deploy the new network. NYNEX’s 1996 Annual report states: “In February 1996, New England Telephone

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advised the FCC that it relinquished authorization to construct advanced video dialtone network facilities in portions of Massachusetts and Rhode Island.”

The complainants believe that Bell Atlantic misled Massachusetts consumers and regulators for the purpose of removing important pro-consumer regulation. Once regulatory relief was granted they abruptly discontinued plans to deploy important new technologies.

The complainants believe that Bell Atlantic may have taken as much as \$800 million in improper tax deductions in Massachusetts in addition to similar write-offs in other Bell Atlantic states, based on annual reports from New Jersey Bell and Pennsylvania Bell

The complainants believe that in the time since rate-of-return regulation was replaced by alternate regulation, proposed by Bell Atlantic and adopted by the Department, Bell Atlantic profits have been excessive and generated at considerable and unreasonable cost to the telephone subscribers and consumers of the Commonwealth.

The complainants believe that Bell Atlantic’s entry into the long distance market would be an obvious violation of the intent of the Telecommunications Act of 1996 that specifically emphasized advanced network deployment and local competition prior to the incumbent being allowed to compete in the long distance marketplace.

The complainants believe that Bell Atlantic has demonstrated an ongoing pattern of deception and outright misrepresentation in every state in which they are the incumbent local exchange carrier.

The complainants recognize the gravity of the allegations set forth herein and do not make them lightly. We call upon the Department to audit Bell Atlantic’s past execution of its promises, to review Bell Atlantic’s pricing policies for all basic and enhanced services and, in view of Bell Atlantic’s demonstrable bad faith, regulate the company to the full extent of its jurisdiction.

## DISCUSSION

### **1. Bell Atlantic misled Massachusetts consumers and regulators with promises of advanced network deployments for the purpose of removing important pro-consumer regulation.**

In statement after statement, before consumers, advocates, regulators and the press, employees and executives at the top echelon of New England Telephone made repeated and unambiguous representations that NYNEX would spend over \$500 million to build the fiber optic network in Massachusetts, commencing in 1995. On July 15, 1994, New England Telephone Chairman Paul O'Brien announced that NYNEX was "...putting its money behind its beliefs. We recently announced plans to build what is essentially a new....state-of-the-art broadband network.... capable of providing video-on-demand and interactive information services." O'Brien went on to promise that construction would begin late that year, 1994, in eastern Massachusetts.

A few months later, the *Patriot Ledger* quoted NYNEX spokesman Kenneth Horne describing a very specific plan: "In Massachusetts, NYNEX plans to begin the new service in Somerville, Revere and Winthrop, then move to Brookline, Cambridge and neighborhoods in Boston, including Roxbury, Brighton, Beacon Hill and the Back Bay...."

In its testimony before the Department as it considered the alternate regulation plan, NYNEX agreed to "deploy a fiber-based broadband network, with initial deployment to approximately 330,000 access lines, by year-end 1995."

NYNEX made essentially the same promise to the FCC in 1994:

"On July 8, 1994, NYNEX filed two (Section 214) applications for authority to provide video dialtone service in certain areas of Massachusetts and Rhode Island. The application to provide video dialtone service in Massachusetts proposes a system that will pass approximately 334,000 homes and businesses."

[FCC 95-50 Order and Authorization, released 3/6/95]

NYNEX put forward a very specific technological definition of what it would offer if granted relief. As the FCC understood the NYNEX proposal,

"NYNEX proposes to deploy hybrid fiber optic and coaxial (HFC) broadband networks that will provide advanced voice, data, and video services, including interactive video entertainment, multimedia education and health care services. NYNEX's proposed video dialtone systems make available three types of service arrangements: analog broadcast, digital broadcast, and digital interactive service. Video programmers may deliver an 'analog, digital, or other agreed-upon signal' that NYNEX plans to modulate or encode as necessary. The allocation plan provides for the offering of 21 analog channels, all but one of which will be used

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for over-the-air broadcast programming services, and, depending on compression rates, between 400 and 800 digital channels.”

[FCC 95-50 Order and Authorization, released 3/6/95]

NYNEX also spun a very compelling vision of the consumer benefits the new technology would allow:

“[T]he new technology would give Massachusetts residents access to a wide range of information and entertainment services. Among the new types of services envisioned are improved cable television, home banking and shopping, civic and community-based forums and bulletin boards and new forms of interactive entertainment such as movies on demand.

“Ultimately, the broadband network would help Massachusetts education institutions further expand interactive and distance learning opportunities for students of all ages. The health care industry would gain advanced communications capabilities to reduce costs and expand delivery of services, including remote diagnoses and other forms of telemedicine.”

[NYNEX Press Release: 4/14/94]

The rate-of-return doctrine that NYNEX sought so aggressively to replace protected consumers in important ways. It stipulated that as telecommunications became less expensive to provide, consumer prices would fall because telephone company profits would be capped at 11%. Had alternate regulation not been approved, consumers would benefit by economies of scale brought about by an increase in overall use of telecommunications and realize the benefit wrought by a substantial investment in the copper plant, that, as ratepayers, we had underwritten over time. NYNEX, and the other “Baby Bells,” presented an ambitious vision of the future—one that would require substantial investment in new technologies. Rather than lower rates, they proposed to freeze rates for basic services at the 1995 level, and agreed to invest increased profits in the new network and services.

We estimate that between 1994 and 1999, Massachusetts consumers paid over one billion dollars more for basic telecommunication services than we would have if alternate regulation was not established. However, the exact amount requires an investigation and audit. And is doubtful that NYNEX ever intended to build the new network.

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## **2. Once regulatory relief was granted Bell Atlantic abruptly discontinued plans to deploy important new technologies.**

The five-year effort by NYNEX to establish the regime of alternate regulation was mirrored by every other “Baby Bell” throughout the United States. It involved an intensive lobbying campaign, on the federal and state level, before lawmakers, local officials, regulators, consumer advocates and the press.

In early 1996, a few short months after NYNEX successfully prevailed upon the Department to grant their scheme of alternate regulation and just after the FCC granted their request to be able to offer new video-dialtone services, NYNEX abruptly cancelled all plans to deploy the new network. Indeed, NYNEX’s 1996 Annual Report states: “In February 1996, New England Telephone advised the FCC that it relinquished authorization to construct advanced video dialtone network facilities in portions of Massachusetts and Rhode Island.” NYNEX had gotten what it wanted—relief from the rate-of-return doctrine, and was raking in millions of dollars in excess profits paid for by Massachusetts ratepayers. The alternate regulations continue presently and will not expire until 2001.

Today, more than four years later, there are no fiber-optic, full-motion-video-with-eight-hundred-channels services being offered in the region by Bell Atlantic or anyone else. The promises: digital delivery of hundreds of channels, at speeds one hundred times faster than current high-speed internet services, made by NYNEX were broken and they have not, as yet, been held accountable. Currently new products are being offered via ADSL – a service that is deployed over the copper network—the original twisted pair of wires that was to be replaced by fiber to every home.

It would be bad enough to find that NYNEX (now Bell Atlantic) promised its customers and regulators a bright future, enhanced by important new technologies that would vastly improve the ways we educate, edify and entertain ourselves, then simply changed its corporate mind. Because vast new profits were garnered, not by raising prices but by freezing prices at artificially high levels, perhaps Bell Atlantic thought no one notice. State and federal regulators are notoriously over-burdened. But it is even more distressing to find that Bell Atlantic then ceased investing in and, in fact, wrote-off the copper network, upon which Massachusetts subscribers still rely, taking massive tax deductions in the process and making still more incremental profit.

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### 3. **Bell Atlantic may have taken as much as \$800 million in improper tax deductions in Massachusetts.**

In 1995, NYNEX, the holding company (which owned New York Telephone and New England Telephone) took a one-time tax deduction of \$2.9 billion, claiming that new regulations in states, including Massachusetts, allowed it to write-off the copper network that it intended to replace with a new fiber optic one. The amount of the Massachusetts write-off is difficult to document precisely because tax returns are not public documents, but we estimate the total amount in Massachusetts to be \$800 million. This calculation is based on similar deductions in New Jersey and Pennsylvania for the same item, and making adjustments to account for relative size. The New Jersey and Pennsylvania figures were provided in annual reports filed with the Security and Exchange Commission (SEC). We have not found a similar report for Massachusetts specifically, but the deduction was referred to in aggregate form by NYNEX.

Of course the wire was never replaced, making the write-offs premature at best. NYNEX explained the deductions this way:

“In the second quarter of 1995, NYNEX discontinued accounting for the operations of the telephone subsidiaries in accordance with the provisions of Statement No. 71. As a result, NYNEX recorded an extraordinary non-cash charge of \$2.9 billion.

"The operations of the telephone subsidiaries no longer met the criteria for application of Statement No. 71 due to a number of factors including: significant changes in regulation (*achievement of price regulation rather than rate-of-return regulation in New York, Massachusetts and Maine, and ongoing efforts to achieve price regulation in the remaining jurisdictions*); *an intensifying level of competition; and the increasingly rapid pace of technological change*. Under Statement No. 71, NYNEX had accounted for the effects of rate actions by federal and state regulatory commissions by establishing certain regulatory assets and liabilities, including the depreciation of its telephone plant and equipment using asset lives approved by regulators and the deferral of certain costs and obligations based on approvals received from regulators. NYNEX had continually assessed its position and the recoverability of its telecommunications assets with respect to Statement No. 71.

[NYNEX Annual Report 1995, *emphasis added*]

In Massachusetts specifically:

"NYNEX stated that it will require additional increases in its depreciation rates over the next few years of approximately \$100 million. The Company attributes this to the planned expansion of its broadband network in Massachusetts, and the shorter economic lives of its plant resulting from these technological improvements (Exh. NYNEX-9, 16-18).

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[In 1998, New Network Institute filed a \$21 billion dollar complaint with the Criminal Justice Division of the US Internal Revenue Service against NYNEX, Bell Atlantic, and the other Bell Holding companies, in each of the states in which they operated in 1995. The complaint, (refiled with new information in October 1999) highlights how the Bells took substantial one-time deductions of the older copper plant, claiming that they were replacing it with fiber-optics. However, since these networks were never replaced and are still in use, NNI contends that the IRS should investigate the \$21 billion dollars of improper deductions.]

#### **4. Since rate-of-return regulation was replaced by the alternate regulation, Bell Atlantic profits have been excessive and generated at an unreasonable cost to the telephone subscribers and consumers of the Commonwealth.**

Without speculating as to whether the Department would have granted Bell Atlantic a rate increase if they had simply asked for it outright, they managed to achieve the same objective as the cost of providing service to Massachusetts subscribers plummeted while rates to consumers remained frozen.

Though a Massachusetts annual report was unavailable, the filings of both Bell Atlantic, the holding company, and New England Telephone's FCC's make clear the impact of the alternate regulation plans. First, Bell Atlantic's overall profitability is clearly indicated in their second quarter 1999 report. The exhibit below shows that Bell Atlantic's return on equity was 33.4%, a 200% increase over the traditional 11% rate of return. Profit margins of 43% for Telecom Services and over 50% for Directory Services are unconscionable for a supposed regulated monopoly.

#### **Bell Atlantic's Return on Equity and Profit Margins**

(second quarter results for 1999)

Bell Atlantic Return on Equity	33.4%
Bell Atlantic Profit margins for Telecom	42.8%
Bell Atlantic's Profit Margins for Directory Services	52.1%

More specifically, the information provided to the FCC by the companies regarding annual earnings clearly show that the Bell Atlantic, more specifically New England Telephone,

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greatly benefited from the alternate regulation. Dividends paid to Bell Atlantic doubled from \$424 million in 1994 to a whopping \$845 million in 1998. In addition, the Bells vastly increased their deductions based on the depreciation of the copper network garnering nearly \$100 million more by 1998 throughout all of the New England Telephone states, including Massachusetts, Maine, Vermont, New Hampshire, and Rhode Island, all of which operate under some form of alternate regulation. Massachusetts accounts for approximately half of all New England Telephone subscriber lines.

## **Bell Atlantic-New England Telephone Dividends, Depreciation Expenses, 1994 vs.1998**

	<u>1994</u>	<u>1998</u>	<u>Change</u>
Dividends paid to Bell Atlantic	\$424	\$845	Doubled
Depreciation expenses	\$862	\$952	Increased \$100 million

*[Source: Statistics of Common Carriers, FCC: 1994, 1995, 1996, 1997, 1998]*

According to the Massachusetts Alternate Regulation Plan, depreciation expenses were supposed to be related to NYNEX's installation and deployment of the fiber optic network. As previously noted:

"NYNEX stated that it will require additional increases in its depreciation rates over the next few years of approximately \$100 million. The Company attributes this to the planned expansion of its broadband network in Massachusetts, and the shorter economic lives of its plant resulting from these technological improvements."

[Exh. NYNEX-9, at 16-18]

More to the point, the information provided clearly shows that NYNEX never spent the \$500 million, as promised, to deploy the fiber. In fact, while revenues increased 15% from 1994 to 1998, expenses only increased 6 percent and income rose 56%.

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## Bell Atlantic-New England Telephone Revenues, Expenses and Income, 1994-1999

(In \$ billions)	1994	1995	1996	1997	1998	% of change
Total Revenues	\$4.1	\$4.2	\$4.6	\$4.5	\$4.7	15%
Operating Expenses	\$3.3	\$3.3	\$3.3	\$3.4	\$3.5	6%
(In \$ millions)	1994	1995	1996	1997	1998	% of change
Operating Income	\$790	\$905	\$1,299	\$1,096	\$1,230	increased 56%

It is important to note that while revenue rose, and expense stayed the same, there was a continued and accelerated increase in profits, from \$790 million to \$1.23 billion---a 56% increase since 1994. In short, New England Telephone clearly benefited from alternate regulations. Dividends doubled, depreciation rose almost \$100 million, Net Operating Income increased 56%. Meanwhile, expenses, including sales and marketing, customer service operations and expenditures on the network plant, all decreased or increased only marginally.

These statistics also hide another major issue-- Did Bell Atlantic charge customers for the development of video services? According to testimony and comments from the Attorney General in the original alternate regulation case. NYNEX added an additional \$7 million dollars to the cost of customer services for the development of its proposed video service. The Alternate Regulation Order stated: (94-50)

“The Attorney General asserts that NYNEX’s video and broadband research and development ("R&D") activities are intended to allow it to deploy a cable television system at the expense of telephone customers... Therefore, the Attorney General concludes that NYNEX’s cost of service should be reduced by \$6,635,000.”

[Massachusetts Attorney General Reply Brief at 69]

Meanwhile, the New England Cable Television Association (“NECTA”), claimed that the overcharging of customers by added expenses was closer to \$19 million.

“The Company’s test year expenses concerning affiliate transactions are rife with costs relative to video transport, video-on-demand ("VOD"), and broadband applications that should be excluded from cost of service., NECTA maintains that NYNEX's cost of service should be reduced by at least \$18,629,482” [Alternate Regulation Order, 94-50]

Based on this data, we estimate that New England Telephone customers could have paid over \$500 million in excess charges above previous regulated amounts for 1998 alone. This

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statistic is derived primarily from the depreciation increases and the excess dividends paid. Further, taking into account the current growth described in Bell Atlantic's 1999 second quarter report, we estimate that an additional \$500 million in over-charges are likely.

For the five year period, up to and including the current year, we estimate that the subscribers served by New England Telephone will have been over-charged as much as \$1.3 billion. These estimates do not include the more than \$800 million in depreciation taken by NYNEX in Massachusetts in 1995.

In consideration of these questionable tax deductions taken and in light of vast increases in New England Telephone dividends, we estimate that over \$1 billion dollars of additional charges to Massachusetts subscribers warrants investigation. Our findings are based on raw data provided by Bell Atlantic. NNI believes that a through audit of the company might find other questionable practices.

This pattern of Bell company excess suggests that the Department has been unable or unwilling to monitor and regulate the ongoing commercial practices of Bell Atlantic and its corporate predecessor, NYNEX. These excesses take various forms, for example, Bell Atlantic still charges Massachusetts subscribers for Touchtone service, an "option" that costs nothing to make available. Ironically, Bell Atlantic seems to be caught between two worlds, one typified by the most advanced features imaginable, which they have charged us for but can't deliver, and the other, where consumers are charged for the most basic tool of the information age— DTMF signaling, without any compelling rationale.

Furthermore, we believe Bell Atlantic probably never had any serious intention of deploying the new networks, and made the decision not to build the new networks before the Massachusetts alternate regulation plan even went into effect. According to press accounts, Bell Atlantic shifted focus to a wireless technology, supposedly capable of delivering the same advanced cable services to Massachusetts subscribers sooner than the fiber network could be installed:

"In recent weeks, three regional phone companies unwrapped plans to enter the cable-TV market sooner than expected, using simple transmission towers and fishbone-style rooftop receivers. While the technology may be as old as a Jack Benny punch line, the phone companies say it will enable them to offer customers an alternative to cable programming long before their exotic fiber-optic networks are rolled out later in the decade.

"It gives customer choices sooner than what we would otherwise be able to accomplish with fiber," says Jack Hoey, a spokesman in Boston for Nynex Corp., which last month teamed

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up with Bell Atlantic Corp. to invest up to \$100 million in CAI Wireless Systems Inc. of Albany, N.Y....”

...“It will take years before the [fiber-optic] technology becomes widespread, though, and the phone companies have been pushing back their timetables. Just this week, Bell Atlantic asked the federal government to withdraw its application to deliver fiber-coaxial - or so called broadband - services to as many as 3 million homes in Philadelphia, Pittsburgh and nearby centers. It said it wants to reconsider its technology strategy.”

[*Boston Globe*, 4/27/95]

The timing of the *Globe* report is significant. It indicates that in April 1995, a full five months before the alternate regulation plan was approved, Bell Atlantic probably knew they were not going to build the new network. Alternate regulation was approved in September 1995. Three months later, the same Bell Atlantic spokesperson explains that they changed their minds while wiring Somerville:

“Since the work began in Somerville, however, wireless technology has emerged as a faster, more efficient way to get into more homes - at least for video, Hoey said. Nynex plans to begin offering Multichannel Multipoint Distribution Service (MMDS), also known as “wireless cable,” to residential customers by the fourth quarter of 1996.”

[*Boston Herald*, 1/4/96]

Would the department have acceded to Bell Atlantic’s alternate regulation scheme without the promise of the new network? Obviously we have no way of knowing for sure. We recognize that the Massachusetts regulation does not immediately link the Bell Atlantic deployment plan with the alternate regulation, but it is impossible to ignore the fact that for four years in every statement, filing, and press release related to this topic, Bell Atlantic made a verbal commitment to its customers and to regulators that they would deliver on their promise of a new network. There is absolutely no evidence that they made any substantial effort to inform the public when they changed their mind, or the reasoning for the change, and we believe Bell Atlantic had a good faith obligation to inform the public and, certainly the Department. We have not been able to locate documentation that Bell Atlantic did inform the Department, but if they did, we believe the Department had a moral, legal and fiduciary obligation to reconsider the alternate regulation plan. And, by the way, the CAI Wireless technology, the technology that was supposed to bring cable competition to the Commonwealth faster than the fiber-optic Infobahn, never worked as advertised and was also abandoned.

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These findings: the regulatory slight-of-hand; a billion dollars in possible overcharges; runaway profits and unprecedented dividends paid, along with the sheer complexity and pace of change of the telecommunications market point to the unavoidable questions: Where are the regulators and how have they allowed this to continue?

## **5. Bell Atlantic has demonstrated an ongoing pattern of deception and outright misrepresentation in every state in which they are the incumbent local exchange carrier.**

The achievement of “incentive” regulation plans in New England, must also be seen as one component of a major national effort by all the Bell operating companies to deceive American consumers and regulators. Similar plans to build the new network were put forward in almost every state, including every state where NYNEX and Bell Atlantic were the incumbent local carrier. They got away without keeping their promises. This pattern of misrepresentation clearly shows that neither NYNEX nor Bell Atlantic had any intention of rolling out these networks but were instead engaged in a bait and switch operation on a massive and unprecedented scale.

The systematic approach by each of the Bell operating companies to the state utility commissions in their regions and to the FCC in Washington is presented thoroughly in *The Unauthorized Biography of the Baby Bells & Infoscandal* by Bruce A. Kushnick, published by New Networks Institute. According to the regional Bell companies annual reports and press announcements made between 1993 and 1994, by the year 2000, forty-five million households would be wired to the all-digital, 500-800 channel, full-motion video network. Here's some representative excerpts:

"The Pennsylvania Plan requires deployment of a universal broadband network, which must be completed in phases: 20% by 1998. Deployment must be reasonably balanced among urban, suburban and rural areas".

[Pennsylvania Bell Annual Report, 1998]

"In 1993 the company announced its intentions to build a 'broadband', interactive telecommunications network... US West anticipates converting 100,000 access lines to this technology by the end of 1994, and 500,000 access lines annually beginning in 1995."

[US West Annual Report, 1993]

"We're building a video network that will extend to six million customers within six years." [Ameritech Investor Fact Book, March 1994]

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"We're prepared to install between 1.5 and 2 million fiber-optic lines through 1996 to begin building our portion of the Information Superhighway."  
[NYNEX Annual Report, 1993]

So great was Bell Atlantic's hubris that they sought to position themselves, dubiously, as leaders in this multi-billion dollar grand scam:

"First, we announced our intention to lead the country in the deployment of the information highway... We will spend \$11 billion over the next five years to rapidly build full-service networks capable of providing these services within the Bell Atlantic Region....We expect to have 8.7 million households wired by the end of 2000:"  
[Bell Atlantic Annual Report, 1993]

Alas, Bell Atlantic was outdone when Pacific Telesis President Philip Quigley boldly announced still higher numbers:

"In November 1993, Pacific Bell announced a capital investment plan totaling \$16 billion over the next seven years to upgrade core network infrastructure and to begin building California's 'Communications superhighway'. This will be an integrated telecommunications, information and entertainment network providing advanced voice, data and video services. Using a combination of fiber optics and coaxial cable, Pacific Bell expects to provide broadband services to more than 1.5 million homes by the end of 1996, 5 million homes by the end of the decade.  
[Pacific Telesis 1993 Annual Report]

Notwithstanding very aggressive plans put forward by the Bell operating companies none of them came to fruition. In fact, the New Jersey Consumer Advocate issued a scathing critique of Bell Atlantic's "Opportunity New Jersey" plan saying: "...low income and residential customers have paid for fiber-optic wiring every month, but have not yet benefited." The Advocate's report, filed with the New Jersey Board of Regulatory Commissioners on March 27, 1997, stated: "Bell Atlantic-New Jersey (BA-NJ) has over-earned, under-spent and inequitably deployed advanced telecommunications technology to business customers, while largely neglecting schools and libraries, low-income and residential ratepayers and consumers in Urban Enterprise Zones as well as urban and rural areas." [For more details about New Jersey Bell's failed deployment see: <http://www.newnetworks.com/chapter4.html>].

Another harsh critic of Bell Atlantic's performance is Economics and Technology, Inc. a well-respected Massachusetts-based consulting firm. In addition to citing the same problems documented in the New Jersey report, their report, "*Broken Promises: A Review Of Bell*

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*Atlantic's Performance Under Chapter 30 (part 2 b)*" clearly demonstrates the same failure of Bell Atlantic to deliver on its promises happened in Pennsylvania:

"In 1993, the Pennsylvania legislature added Chapter 30 to the Public Utility Code with the specific goal of assuring that all areas of the state will be provided with a modern, state-of-the-art broadband telecommunications infrastructure. Basically, Chapter 30 offered Pennsylvania's incumbent local exchange carriers (ILECs) a quid pro quo: In exchange for a firm commitment to provide broadband service capability throughout its entire network by the year 2015, each participating ILEC would become subject to an alternative form of regulation providing substantially greater pricing and earnings flexibility than the traditional rate of return form of regulation under which the ILECs prices and earnings had been set.

"Having made its commitment and been granted its alternative regulation reward, Pennsylvania's largest local telephone company Bell Atlantic Pennsylvania (BA-PA) has paid more attention to escaping from, rather than fulfilling, the terms of its promised upgrade. This study demonstrates that, despite strong financial performance and earnings growth in Pennsylvania, as well as a generous and flexible regulatory framework, BA-PA has failed to increase investment in the state's telecommunications network and, in fact, has actually extracted capital out of Pennsylvania for use elsewhere. At the same time, BA-PA has been extremely successful in protecting its monopoly from competitive encroachment. Without the discipline of actual, effective competition, the incumbent has been permitted to charge excessive prices and earn excessive profits, while confronting no business incentive to undertake new investment in Pennsylvania. As we approach the end of 1998 a point by which BA-PA is supposed to have broadband available throughout 20% of its rural, urban and suburban areas there is no sign of any broadband service being offered to Pennsylvania's residential customers"

In his book *The Billionaire Shell Game*, published by Doubleday in October 1998, award-winning, former *New York Times* reporter L. J. Davis describes the Bell operating companies bait and switch tactics employed in every state and at the federal level in Washington. Based on independent interviews and a survey of the documentary evidence, Davis came to many of the same conclusions that NNI reached. Further, Davis posits that the tactics were part of the RBOC plans to win approval to enter the long distance markets earlier than they would have otherwise been allowed to.

"Like the other six regional telephone companies that had come into independent existence with the break up of AT&T in 1984, Bell Atlantic had a single great goal in the autumn of 1993. Bell Atlantic and the other six baby bells were determined to enter the lucrative long distance business before the march of science rendered their existing equipment vulnerable, obsolete, or both, but getting there was no simple task. Before Bell Atlantic could offer a long distance service- even within its own part of the country, using its own lines and switches- sixty years of federal law and judicial decisions had to be overthrown, and there was only one certain, reliable, and simple way to do it: persuade Congress to pass bold new legislation that would remake Bell Atlantic's world".

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"Unfortunately, there was no great public outcry for such a new law. There was, in fact, not a peep from the public, whose indifference on the subject of telecommunications law was as large as the public's very considerable ignorance of it, and it was extremely difficult to explain why Bell Atlantic, a company with annual profits of over a billion dollars, felt a compelling need to overturn more than half a century of lawmaking in order to make more money. The easy part had already been done; influential congressman had been provided with large sums of money and more would be forthcoming, but encouraging the legislators to think correct thoughts was only part of the task. It was also essential to provide Congress with a plausible- and, above all, a popular and easily understood-reason for writing the new law. The secret of the trick, Bell Atlantic and other regional television companies had correctly come to believe, was cable television".

"With great fanfare, the telephone companies announced that, if only one small condition was met, they would provide cheap, friendly, and reliable cable television service, using their existing networks. The cable companies would no longer hold the country in the iron grip of monopoly, and the viewing public would soon be happy. All it took was a small change in the existing laws- and, while the legislators were at it, they might as well make a few additional and long-overdue modifications of the statutes in the interest of tidiness and for the benefit of all .To the regional telephone companies, God-long distance service- would be found in the modifications. Television was the cover story".

"The regional telephone companies had never been interested in television, and most of them weren't interested now. The goal had always been the long distance business, and the goal never changed. Once the new telecommunications bill was passed and signed, the telephone companies could run a few inexpensive tests in places like Omaha, El Cerrito and Richardson, Texas. If the tests succeeded, well and good, the telephone companies could make some extra money. If the test failed, no great harm was done; the telephone companies could claim technical difficulties and public indifference and quietly abandon the undertaking. In the meantime, it was important to feign enthusiasm until the law changed..."

The fact that Bell Atlantic was joined in this cynical and blatantly dishonest business practice by the other Bell operating companies certainly should not excuse it (although it puts to rest any notion that, between divestiture in the early 1980's and deregulation in 1996, the RBOCs went their own ways). The plain fact in Massachusetts is that Bell Atlantic abused the trust of regulators who apparently took their representations at face value, notwithstanding the warning of the Attorney General's Office, and garnered millions of dollars in extra profit on the backs of Bay State ratepayers.

***We therefore call upon the Department to audit Bell Atlantic past execution of it promises, to review Bell Atlantic's pricing policies for all basic and enhanced services and, in view of Bell Atlantic's demonstrable bad faith, regulate the company to the full extent of its jurisdiction.***

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**6. Bell Atlantic's entry into the long distance market would be an obvious violation of the intent of the Telecommunications Act of 1996 that specifically requires advanced network deployment and local competition prior to the incumbent being allowed to compete in the long distance marketplace.**

There is little doubt that the Congressional intent of the Telecommunications Act of 1996 was to provide all Americans with access to the most advanced telecommunications network and the most vibrant competitive environment possible. Indeed, in its Preamble, Congress made it clear that a central goal of the Act was "to promote competition and reduce regulation in order to secure lower prices and higher quality services for American Telecommunications consumers and encourage the rapid deployment of new telecommunications technologies."

On the federal level, as in the Commonwealth, NYNEX lobbied since the early 1990's to have restrictions lifted so they could offer new services. On June 21, 1991, NYNEX CEO Ivan Seidenberg testified to of the House Committee on Energy and Commerce stating that "the public switched network is burdened by a number of restrictions which frustrate our ability to deploy new technology as rapidly as possible." Seidenberg also was "concerned" that if new laws weren't forthcoming, then the "ability of the broadband electronic highway to play a critical role in defining our strength as a nation in a global information economy" was at stake.

Two years later, in NYNEX's 1993 Annual Report, CEO Ivan Seidenberg sounded the same theme: "restrictions have been major roadblocks to bringing the Information Age to all Americans... [and if Congress passes the Telecom Act] it would enable phone companies to offer video programming in their own service areas."

NYNEX got what they wanted:

"The Communications reform bill signed into law by President Clinton in February 1996 helps us grow to our full potential and lets us take advantage of new freedoms to provide a range of services that include new communications, information and entertainment choice... (t)he new market freedoms spelled out in the nation legislation complement the state regulatory breakthroughs we've already achieved. With incentive regulation plans approved in New York, Massachusetts and Maine, we've brought the regulation of more than 95% of our telecommunications operations into line with marketplace reality."

(Ivan Seidenberg, NYNEX, Annual Report, 1996)

Siedenberg's marketplace reality is apparently one where consumers get bilked by the millions of dollars and telephone company profits soar. Lawmakers and regulators have been

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unable or unwilling to stem the excessive greed of the Bell operating companies. In the 1996 Act, Congress took a principled stand by establishing conditions that would allow for Bell company participation in the long distance marketplace. We are disturbed by the Department's recent decision to not require reciprocal compensation because it is in direct opposition to the letter and spirit of the Telecom Act's. (Reciprocal Compensation is a payment to the local competitive service when they complete or handle a call, and it is one of the principle conditions of the Telecom Act.) Unless the Department changes its mind it may be illegal, based on federal law, for the Bells to ever enter the long distance business.

Furthermore, meaningful competition in the local telecommunications market simply does not exist in Massachusetts. Though some companies have intimated that they "will soon be offering services," there exists no significant competitive alternative for most residential subscribers today. Obviously the barriers to entry in the local residential market are difficult to overcome. We note that RCN has ceased offering residential service in New York, and therefore, may do the same in Massachusetts. In 1998, both AT&T and MCI testified that under the current regulations, RBOC pricing to competitors leaves too little margin of profit. John D. Windhausen, President of the Association of Local Telecommunications Services, stated in recent congressional testimony that none of the RBOCs have been able to pass the most basic test, that their networks were competitor-friendly, as stipulated in the Act.

Then there are the issues of how the RBOCs treat those competitive local exchange carriers ("CLECs") that have entered the market, and Internet Service Providers ("ISPs"), with whom the RBOCs also compete. NNI is currently conducting a survey of CLECs and ISPs related to service issues. More than 50% of them reported that they were receiving poor customer service including: lines dropping in and out of service; failure of the RBOC to keep scheduled appointments for installation and service calls; the RBOCs' inability to deliver on advertised products such as ISDN and Digital Centrex; and significant billing errors. Global Napps and TelEnergy each testified to similar problems at the recent public hearings held by the Department. Meanwhile, Covad Communications, a CLEC that offers advanced network DSL services, testified to the New York Public Service Commission that Bell Atlantic's service was "dismal to date" and stated that half of all lines weren't being provided on time:

"Bell Atlantic's record, particularly as it concerns broadband services, clearly shows that it has not yet met the standard of parity access set forth in the Telecom Act. Our records show that more than 50% of our loops are not being provided on time, making it clear to us that

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this filing is premature. Expanding access to broadband services is a national priority that should not be overlooked as there is a need for these vital services."

[Covad Testimony, NYS PUC, 8/31/99]

Covad strongly warned regulators that it would be a mistake to let the Bells into long distance before they were have fulfilled their obligations to competitors.

"If approved by state and federal regulators, Bell Atlantic would be able to provide long-distance services before it allows Covad timely access to local loops and software connections to Bell Atlantic's operating support services, which would speed up installations of data service. This approval could also delay adherence to the FCC's recent ruling regarding terms of collocation in central offices."

[Covad Testimony, NYS PUC, 8/31/99]

The network problems that Covad and other CLECs experience exacerbates the problems encountered by the Internet Service Providers who depend on them for connectivity. For example, Joe Plotkin of Bwaynet, an Internet Service Provider dependent on Covad, stated:

"It's a chain reaction--- Covad can't get Bell Atlantic to deliver the basic circuit to the customer, and then it makes us look bad. And it's happening on virtually every other order we place. The New York Public Service Commission should have stepped in and fined Bell Atlantic for its incompetence--- (or more like foul play). But it's turning out that they can't get their act together to fix the problems either. I hear Bell Atlantic wants to get into long distance. What-are they kidding? Make them give customers, including Covad, decent service, and pay us for our lost time and business and then talk. Not now. That's for sure.."

[Plotkin interview, 9/1/99]

Bell Atlantic has chilled competition by failing to provide necessary customer service to new market entrants. Rather than investing in new technologies and managing appropriate customer service, Bell Atlantic has chosen to dedicate attention and resources to their effort to enter the long distance market, where consumers already enjoy competitive choice. Ironically, in order to enter the long distance market Bell Atlantic is once again promising to deliver the same advanced networks subscribers have already paid for, but only if the pesky regulations are removed.

Bell Atlantic CEO Seidenberg's strategy and tactics have changed very little. His August 1999 Keynote Address at *Cyberspace and the American Dream VII Conference*, was described by *Wired* magazine this way:

"The same plodding US government bureaucracy that has two agencies inspecting the quality of frozen pizzas is preventing Internet users from enjoying a future full of video-conferencing, movies on demand, and other nifty high-speed digital benefits.

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"So began the annual Cyberspace and the American Dream VII, as Seidenberg preached the wonders of wireless during his keynote address Monday morning.

"And," he said, "only broadband can unleash the Web's true potential. Video-conferencing and streaming media will become a common reality. Small audio files and video files can be embedded in Web sites," he said, adding that the "real benefits would come in greater access to expert health care and real-time interaction among nations."

[*Wired* 8/23/99, "US Out of Broadband Now"]

According to Seidenberg, once again government regulation is preventing broadband deployment:

"The government is neither equipped nor prepared to introduce broadband to the masses, and "that's particularly bad when moving on Internet time," said Bell Atlantic CEO Ivan Seidenberg.

[*Wired* 8/23/99, "US Out of Broadband Now"]

Like a broken record, Seidenberg once again calls for the wholesale removal of any regulation, including all state regulations, replacing them with a regime modeled after the current wireless regulations:

"According to Seidenberg, wireless is the logical regulation model that would clear the way for the country's telecommunications companies to quickly install and deliver the promising broadband future."

"After all, it was limited government regulation -- *confined strictly to federal and not state legislation* -- that permitted the cellular phone industry to provide more capacity, more competitors, more services, and lower prices to customers."

"If the telcos and Baby Bells were regulated in a similar way, they'd be more inclined to invest in a broadband infrastructure', Seidenberg said.

[*Wired* 8/23/99, "US Out of Broadband Now" *emphasis added*]

***Therefore, we call upon the Department to use any means available to deny Bell Atlantic's entrance into the long-distance marketplace in Massachusetts at this time.***

## IMPACT

It is difficult to over-estimate the negative impact of NYNEX's and Bell Atlantic's behavior we have outlined herein. By failing to keep their commitments to build and make available the new network, and by abusing their position as the uniquely-qualified entity to provide such an infrastructure, Bell Atlantic has held the Commonwealth's digital future hostage in the following ways:

- 1) Massachusetts role in the global economy has been stifled. Had Bell Atlantic provided services as promised, Massachusetts could have been in the forefront of the global digital revolution. The benefits to the Massachusetts economy would have been substantial, the lost opportunity, immeasurable.
- 2) Massachusetts consumers paid for a network that was never delivered. The public trust and confidence in the telecommunications industry and those responsible for its regulation risks severe damage unless the Department steps in now to make Massachusetts consumers whole.
- 3) Massachusetts consumers have been denied the benefits of competition in the cable television market, as they were promised. Cable television rates have not diminished and enhanced services have never been offered.
- 4) Competitive local exchange carriers and Internet Service Providers complain of unfair treatment by Bell Atlantic. Unless the Department can effectively monitor and assure a level playing field for all local carriers, some will go out of business and Massachusetts consumers will be denied the widest array of choices
- 5) Though all Massachusetts subscribers have paid for and not received fiber-optic wiring, the burden has been unevenly born by seniors and low-income subscribers—those with the least ability to pay.
- 6) Some broadband alternatives are being offered by a limited number of providers to select areas of the Commonwealth. Bell Atlantic had made it clear that they would be wiring all communities, including public schools and libraries, without regard to demographics. Their failure to do has widened the digital divide: that gap between the digital have and have-nots.

## CONCLUSION

The clear implications of the data we present herein are that Bell Atlantic and its predecessor NYNEX, willfully made broad misrepresentations to their consumers and to those charged with the responsibility of regulating them. Their motivation for doing so was greed, plain and simple. They have perpetrated a massive fraud against every telephone user in the Commonwealth. This undeniable pattern of willful and outright deception was duplicated in every state in which they do business. We call upon the Department of Telecommunications and Energy to launch an immediate and thorough investigation and to assure that Massachusetts consumers are made whole.

Respectfully submitted,

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Bruce A. Kushnick  
New Networks Institute  
826 Broadway Suite 900  
New York, New York 10003

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Peter J. Brennan  
111 Perkins Street Apt. 282  
Jamaica Plain, Massachusetts 02130

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