Overview of Accounting Regulation in the United States

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Note: The views expressed in this presentation are those of the author and may not necessarily represent the views of the Federal Communications Commission.

Overview

- Background and History of Accounting Regulation
- Jurisdictional Accounting Separations
- Uniform System of Accounts
- Accounting Regulation
  - 1984-1991
  - Streamlining 1996-2008
- Freeze and Forbearance
- Recent Developments

Accounting Regulation Background

- The FCC is required by statute to prescribe a uniform system of accounts for use by telephone companies.
  - The first accounting system was adopted in 1935 when a rigid institutionalized regulatory environment was expected to continue forever.
- Historically, all incumbents were subject to rate-of-return regulation at the federal and state levels
- In 1986, The FCC adopted the Uniform System of Accounts (USOA) contained in Part 32 of the Commission's Rules.
  - The 1986 USAO was designed to respond to the introduction of competition and an explosion of new products and services to which the existing systems could not respond without massive modification.

Accounting Regulation Background
Federal vs. State

- One regulatory focus is the separation of interstate and intrastate property and expenses

  - Jurisdictional separations is the process of apportioning regulated costs between the interstate and intrastate jurisdictions.

  - The primary purpose of jurisdictional separations is to determine whether a local exchange carrier (LEC)'s cost of providing regulated services are to be recovered through its rates for intrastate services or through its rates for interstate services.

Accounting Regulation Background The Federal-State Joint Board

- The Federal-State Joint Board on Jurisdictional Separation was established by the Commission in June, 1980

  - The Joint Board is made up of FCC Commissioners and FCC staff, and state Commissioners and state staff

  - The Joint Board evaluates and makes recommendations with respect to any amendment of the commission's rules governing the jurisdictional separation of common carrier property and expenses between interstate and intrastate operations.

Uniform System of Accounts - 1986

- The FCC intended that the USAO accommodate generally accepted accounting principals (GAAP) to the extent that regulatory considerations allowed.
  - FCC regulations (Part 32) specifies a chart of accounts and the types of transactions to be maintained in each account, while GAAP allows companies to determine their own system of accounts subject to certain principles.
- The USAO was adopted at a time when regulators were required or inclined to organize telecommunications costs in a manner that allowed a logical mapping of these costs to telecommunications rate structures.
  - The USAO was designed to complement ~~the~~ rate-of-return regulation and the system of tariffed interstate charges that incumbents were required to follow at the time.

Uniform System of Accounts – 1986 (2)

- Goal of USAO: The access rates charged by carriers were directly attributed to the costs of the carriers, and carriers were required to accurately record those costs in the USAO.
- FCC Rules governing the USAO – 1986 thru 1991, rate-of-return
  - Part 32 required carriers to record their assets, expenses and revenues in prescribed accounts
  - Part 64 contained cost assignment rules to apportion the investment, expenses and revenues between regulated and unregulated activities.
  - Part 36 prescribed rules for separating regulated investment, expenses and revenues between the interstate and intrastate jurisdictions.
  - Part 69 specified how rate-of-return carriers were to apportion costs to the interstate jurisdiction among the interexchange service category and the access categories and rate elements

Accounting Regulation 1984 through 1991

- Virtually all interstate access services were subject to rate-of-return regulation~~s~~.
  - Carrier's charges were set to recover the entity's regulated operating expenses and provide the opportunity to earn a prescribed return on the capital the carrier uses to provide regulated services.
- In 1991, the FCC adopted price cap regulation for the largest LECs.
  - Price cap regulation is a form of incentive regulation that relies on price cap indices to limit prices carriers charge for service so that the prices are presumed to be just and reasonable.
  - Price cap regulation eliminates the link between changes in allocated accounting costs and price and provides incentives for carriers to become more efficient so they realize higher returns.

Accounting Regulation
1996 through 2008 Streamlining

- 1997: The FCC clarified that certain cost allocations and filing requirements only applied to incumbent LECs.
- 1999: The FCC streamlined the depreciation requirements for price cap carriers and established a waiver process so these carriers could set their own depreciation rates in accordance with GAAP.
- 2000: The FCC streamlined the reporting of assets and expenses in specified account by eliminating the expense matrix filing, reducing the cost allocation manual audit requirement, relaxing certain affiliate transactions and eliminating reclassification for certain under construction plant expenses.
- 2001: The FCC consolidated certain accounting requirements, relaxed affiliate transaction rules, reduced financial reporting requirements for mid-sized incumbents

Accounting Regulation Freeze and Forbearance

- Beginning in 2001, the FCC froze
  - for price cap carriers, category relationship and allocation factors, and
  - for rate-of-return carriers, froze all allocation factors
    - The FCC concluded that several issues should be addressed in comprehensive reform, and that a freeze would reduce regulatory burdens
- In 2008, the FCC conditionally granted petitions for forbearance of Part 36 jurisdictional separations to AT&T, Bell South, Verizon and Qwest.
- In 2013, forbearance was extended to the remaining price cap LECs.

Accounting Regulation
February 2017

- The Commission completed its review of USOA and issued an Order that minimized burdens on carriers while insuring that the FCC had access to the information it needs to regulate.
  - The FCC found that with its actions in the areas of price cap and universal service reform and the development of intermodal telephone service competition, price cap carriers should no longer be required to comply with regulations that required them to keep two sets of books.
- The FCC streamlined the USOA rules for all carriers, amending 39 rules effective January 2018.
- The FCC will allow price cap carriers to elect to use GAAP for all regulatory accounting purposes so long as they comply with targeted accounting rules.
  - Reduces the burden of keeping two sets of books- one based on GAAP and one based on FCC requirements

Accounting Regulation February 2017 (2)

- Order consolidates Class A and Class B accounts
  - Class A, which requires larger carriers to maintain 138 accounts is eliminated, and all carriers are now under Class B, which formerly applied only to smaller carriers, who had to maintain 80 accounts.

- Order makes permanent forbearance for price cap carriers from the continuing property records requirements, so long as they can demonstrate how they will maintain records to track substantial assets and investments in an accurate and auditable manner

- Order aligns the USOA more closely with GAAP
  - Asset accounting rules
  - Rules relating to allowance for funds used during construction, and
  - Materiality rules

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