

State of Florida



Public Service Commission

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-M-E-M-O-R-A-N-D-U-M-

DATE: MAY 12, 2003

TO: DIRECTOR, DIVISION OF THE COMMISSION CLERK &
ADMINISTRATIVE SERVICES (BAYÓ)

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(WATTS) ^{WJ} ^{for DW} ^{WJ for RB}
OFFICE OF THE GENERAL COUNSEL (BANKS, DODSON) ^{LP} ^{PAC} ^{FRB}

RE: DOCKET NO. 020119-TP - PETITION FOR EXPEDITED REVIEW AND
CANCELLATION OF BELLSOUTH TELECOMMUNICATIONS INC'S KEY
CUSTOMER PROMOTIONAL TARIFFS AND FOR INVESTIGATION OF
BELLSOUTH PROMOTIONAL PRICING AND MARKETING PRACTICES, BY
FLORIDA DIGITAL NETWORK, INC.

DOCKET NO. 020578-TP - PETITION FOR EXPEDITED REVIEW AND
CANCELLATION OF BELLSOUTH TELECOMMUNICATIONS INC'S KEY
CUSTOMER PROMOTIONAL TARIFFS BY FLORIDA COMPETITIVE
CARRIERS ASSOCIATION

DOCKET NO. 021252-TP - PETITION FOR EXPEDITED REVIEW AND
CANCELLATION OR SUSPENSION OF BELLSOUTH TELECOMMUNICATIONS
INC'S KEY CUSTOMER TARIFFS FILED 12/16/02, BY FLORIDA
DIGITAL NETWORK

AGENDA: MAY 20, 2003 - REGULAR AGENDA - PARTICIPATION IS LIMITED
TO COMMISSIONERS AND STAFF. POST-HEARING DECISIONS.

CRITICAL DATES: NONE

SPECIAL INSTRUCTIONS: NONE

FILE NAME AND LOCATION: S:\PSC\GCL\WP\020119.RCM

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CASE BACKGROUND

On January 15, 2002, BellSouth Telecommunications, Inc. (BellSouth) filed its 2002 Key Customer promotional tariff, Tariff No. T-020035, which became effective on January 31, 2002, and expired on June 25, 2002 (the January filing). On February 14, 2002, Florida Digital Network, Inc. (FDN) filed a Petition for Expedited Review and Cancellation of BellSouth Telecommunications, Inc.'s Key Customer Promotional Tariffs and For An Investigation of BellSouth Telecommunications, Inc.'s Promotional Pricing and Marketing Practices (FDN Petition). FDN's Petition triggered the establishment of Docket No. 020119-TP.

On June 11, 2002, BellSouth filed a second promotional tariff, Tariff No. T-020595, which became effective on June 26, 2002 and expired on December 31, 2002 (the June filing). As evident by the respective effective dates, the June filing replaced the expired program of the same name, the January filing.

On June 25, 2002, the Florida Competitive Carriers Association (FCCA) filed a Petition to Intervene, and a separate filing requesting an Expedited Review and Cancellation Of BellSouth's Key Customer Promotional Tariffs (FCCA's Petition). The FCCA's Petition triggered the establishment of Docket No. 020578-TP.

By Order No. PSC-02-1237-FOF-TP, issued September 9, 2002, Docket Nos. 020119-TP and 020578-TP were consolidated for purposes of hearing.

On August 29, 2002, an issue identification meeting was held for Docket Nos. 020119-TP and 020578-TP. All of the issues were agreed upon by the parties, with the exception of FCCA's Proposed Issue 3F. The Prehearing Officer directed parties to file briefs on whether Proposed Issue 3F should be included as an issue; a subsequent ruling by the Prehearing Officer disallowed the issue entirely.

On December 16, 2002, BellSouth filed Tariff No. 021241 to extend the effective date of the June filing (the extension tariff). The extension tariff became effective on December 31, 2002, and expires on July 1, 2003.

On December 20, 2002, FDN filed a Petition requesting an Expedited Review and Cancellation Of BellSouth's Key Customer

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Tariff filed on December 16, 2002. FDN's Petition triggered the establishment of Docket No. 021252-TP, though it was consolidated with Docket Nos. 020119-TP and 020578-TP for hearing purposes.

Throughout the course of this proceeding, individual Alternative Local Exchange Companies (ALECs), as well as the Florida Competitive Carriers Association, were granted intervention. At various times thereafter, these parties withdrew from these dockets; FDN remained as the sole ALEC participant.

The administrative hearing for the consolidated dockets of this proceeding was held on February 19-20, 2003.

This is staff's post-hearing recommendation addressing the allegations raised by FDN in all dockets of this proceeding. Staff notes, however, that the arrangement of the issues has been adjusted for ease of understanding. Additionally, the arguments, analysis, and recommendations are presented in a consolidated format for purposes of efficiency, where necessary, to address interrelated points. A table of contents is included to summarize the staff's order of presentation and the grouping of issues.

The Commission is vested with jurisdiction in this matter pursuant to Sections 364.01, 365.051, 364.08, and 364.285, Florida Statutes.

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EXECUTIVE SUMMARY

This is staff's post-hearing recommendation addressing the allegations raised by FDN in objection to specific BellSouth promotional tariff filings. Collectively, the dockets in this proceeding pertain to three tariff filings:

<u>Tariff and (Docket Number)</u>	<u>Effective Date</u>	<u>Expiration Date</u>
T-020035 (020119-TP)	January 31, 2002	June 25, 2002
T-020595 (020578-TP)	June 26, 2002	December 31, 2002
T-021241 (021252-TP)	December 31, 2002	July 1, 2003

These BellSouth promotional tariffs offer incentives to business customers that meet certain criteria and reside in select wire centers ("hot wire centers"). The main criterion to qualify for the incentives is having total monthly billed revenue between \$75.00-\$3,000.00. Customers that participate in these promotions receive various percentage discounts that range from 10-25% off of their bill, depending upon the tariff and the term commitment. The BellSouth tariffs also waive connection fees and also offer line hunting at no charge.

In its pleadings, FDN alleges that the BellSouth promotional tariffs addressed in this proceeding:

- are "unfair, anticompetitive, or discriminatory," and thus, non-compliant with specific Florida Statutes;
- have oppressive contract terms and conditions;
- unlawfully target, and then "lock up" specific customers.

Additionally, FDN alleges that BellSouth's marketing practices are suspect as well, and should be evaluated.

The issues considered in this proceeding and presented in this document respond to those allegations, and to a limited degree, evaluate the marketing practices associated with BellSouth promotional tariffs. Staff notes, however, that the chronological arrangement of the issues has been adjusted for ease of

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understanding. In addition, the arguments, analysis, and recommendations are presented in a consolidated format for purposes of efficiency, and where necessary, to address interrelated points. A table of contents is included to summarize the staff's order of presentation and the grouping of issues.

Staff's recommends that:

- The Florida Statutes provide sufficient guidance to evaluate promotional tariff filings, including the BellSouth promotional tariffs addressed in this proceeding;
- The BellSouth promotional tariffs addressed in this proceeding comply with the Florida Statutes. These tariffs are available for resale;
- No additional marketing restrictions are necessary for BellSouth beyond the voluntary measures in place system-wide. Federal regulations address the sharing of information between wholesale and retail entities.

DISCUSSION OF ISSUES

ISSUE A: What is the Commission's jurisdiction in this matter?

RECOMMENDATION: Pursuant to Chapter 364, Florida Statutes, the Commission has authority to regulate telecommunications companies. As such, the Commission has jurisdiction to review the promotional tariff filings which are at issue under its regulatory authority.
(BANKS)

POSITION OF THE PARTIES

FDN: The Commission has jurisdiction to determine whether BellSouth's promotions and discounts comport with Chapter 364, Florida Statutes.

BELLSOUTH: The Commission has jurisdiction to review tariff filings for compliance with Florida law.

STAFF ANALYSIS:

There is no dispute between the parties that the Commission has authority to review promotional tariff offerings, which are at issue here. FDN indicates that the Commission has authority to determine whether BellSouth's promotional tariffs comport with Chapter 364, Florida Statutes. (BR at 6) BellSouth states that the Commission has jurisdiction to review tariff filings for compliance with Florida Law. (BR at 10) Chapter 364, Florida Statutes, grants the Commission exclusive authority in regulating telecommunications companies. Specifically, Section 364.01(2), Florida Statutes, provides that:

It is the legislative intent to give exclusive jurisdiction in all matters set forth in this chapter to the Florida Public Service Commission in regulating telecommunications companies. . . .

The central issue in this case is whether BellSouth's promotional tariffs are anticompetitive and discriminatory as defined under Chapter 364, Florida Statutes. Pursuant to Chapter 364, Florida Statutes, the Commission has authority to regulate

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telecommunications companies regarding all matters set forth in Chapter 364, Florida Statutes, including matters which may be anticompetitive or discriminatory in nature. As such, the Commission has jurisdiction to review the promotional tariff filings which are at issue here under its regulatory authority.

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ISSUE 1: How should Section 364.01, Florida Statutes, be interpreted in evaluating a BellSouth promotional tariff for compliance with Chapter 364, Florida Statutes?

RECOMMENDATION: Section 364.01, Florida Statutes, provides the Commission with the authority to promote competition. As such, staff believes that Section 364.01, Florida Statutes, should be interpreted as giving the Commission authority to promote competition by preventing any conduct or practice which contravenes the goal of Section 364.01, Florida Statutes, to promote competition. (BANKS)

POSITION OF THE PARTIES

FDN: Section 364.01 should be interpreted as an expression of the Legislature's overriding intent to promote and preserve sustainable competition for the benefit of all telecommunications customers over the long term, not just to benefit some over the short term to the detriment of the larger goal.

BELLSOUTH: Section 364.01 gives guidance to the Commission as to how to exercise its existing jurisdiction. This guidance focuses on promoting competition, which is what BellSouth's promotions have done. BellSouth has been offering promotions for years, during which time ALECs have gained over 33% of the business lines within BellSouth's territory.

STAFF ANALYSIS:

FDN

In its brief, FDN states that Section 364.01, Florida Statutes, provides the Legislature's intent for interpreting and enforcing the provisions of Chapter 364, Florida Statutes. (BR at 7). FDN asserts that the expression of intent cannot be divorced from the facts of this or any case, for a proposed interpretation of a section of Chapter 364, Florida Statutes, cannot be used to justify results counter to the overriding intent of the Legislature. FDN claims that no one could logically conclude that Section 364.01, Florida Statutes, should sanction conduct that resulted in competition forestalled, a monopoly's dominance preserved, and customers being treated unfairly. FDN concludes that the totality of the facts in this case point out that BellSouth's conduct is

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antithetical to the Legislature's purpose. As such, FDN believes that facilities-based carriers that require real and steady growth to sustain their ability to compete have been stalled as a result of BellSouth's conduct. FDN asserts that without viable competitors, there simply will be no competition for the benefit of anyone. (BR at 8) FDN rejects BellSouth's effort to have the Commission focus on the temporary benefit of its offerings to some customers, while discriminating against other customers. Therefore, FDN asserts that the Commission's evaluation of this case must be tempered with Section 364.01, Florida Statutes, in mind, and indicates that no part of Section 364.01, Florida Statutes, favors stagnating competitors by allowing BellSouth's anticompetitive and discriminatory promotional tariff offerings.

BellSouth

In its brief, BellSouth states that Section 364.01, Florida Statutes, gives guidance to the Commission as to how to exercise its existing jurisdiction. BellSouth asserts that this guidance focuses on promoting competition, which is what BellSouth believes it has done. (BR at 10) BellSouth asserts that Chapter 364, Florida Statutes, requires the Commission to promote competition in several ways:

Section 364.01(4)(b):

Encourage competition through flexible regulatory treatment among providers of telecommunications services in order to ensure the availability of the widest possible range of consumer choice. . .

Section 364.01(4)(e):

Encourage all providers of telecommunications services to introduce new or experimental telecommunications services free of unnecessary regulatory restraints.

Section 364.01(4)(f):

Eliminate any rules and/or regulations which will delay or impair the transition to competition.

Section 364.01(4)(g):

Ensure that all providers of telecommunications services are treated fairly by preventing anticompetitive behavior and eliminating unnecessary regulatory restraint.

(BR at 11.)

BellSouth claims that the consideration in this issue should be whether BellSouth's promotional tariffs create an environment that would prohibit competition or not allow ALECs to adequately compete in the local market. BellSouth agrees with FDN that the Legislature's overriding intent is to promote competition. However, BellSouth asserts that FDN's solutions, to limit BellSouth's tariffs, would have a negative impact on telecommunications customers that would be denied benefits of such promotions. Further, BellSouth claims that ALECs freely compete in Florida with the current BellSouth Key Customer tariffs in place. (BR 12)

Analysis

It is evident that the parties agree that Section 364.01, Florida Statutes, gives the Commission the authority to promote competition. However, the parties differ in the degree and manner in which the Commission should promote competition. FDN states that no one could logically conclude that BellSouth's promotional offerings are in compliance with Section 364.01, Florida Statutes, asserting that they are anticompetitive and discriminatory. FDN claims that BellSouth's promotional tariffs are antithetical to the intent of Section 364.01, Florida Statutes. BellSouth states that Section 364.01, Florida Statutes, gives guidance as to how to exercise its existing jurisdiction. Further, BellSouth asserts that Section 364.01, Florida Statutes, provides several ways in which the Commission is authorized to promote competition.

Staff agrees with the parties that Section 364.01, Florida Statutes, gives the Commission general authority to promote competition. Staff believes that the interpretation of Section 364.01, Florida Statutes, should be guided by the Legislature's intent in the section. As stated previously, the Florida Legislature has given the Commission exclusive authority in regulating telecommunications companies. Staff believes that this

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authority provides the Commission with authority to regulate BellSouth's promotional tariffs at issue. As such, staff believes that Section 364.01, Florida Statutes, should be interpreted as giving the Commission authority to promote competition by preventing any conduct or practice which contravenes the goal of Section 364.01, Florida Statutes, to promote competition.

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ISSUE 3D: What criteria, if any, should be established to determine whether geographic targeting in a BellSouth promotional tariff is unfair, anticompetitive or discriminatory?

(i): Pursuant to Section 364.051(5)(a)(2), Florida Statutes, how should "meeting offerings by any competitive provider" be interpreted?

(ii): Pursuant to Section 364.051(5)(a)(2), Florida Statutes, how should "specific geographic market" be interpreted?

(iii): Pursuant to Sections 364.051(5)(a)(2), and 364.08, Florida Statutes, how should "similarly situated" or "substantially similar" be interpreted?

RECOMMENDATIONS:

3D: Staff recommends that no criteria should be established, other than that included in Section 364.051(5)(a)(2) Florida Statutes, to determine whether geographic targeting in a BellSouth promotional tariff is unfair, anti-competitive or discriminatory. (CASEY)

3D (i): Staff recommends that the phrase "meeting offerings by any competitive provider" implies that BellSouth should have the ability to respond to offerings made by competitors in BellSouth wire centers. (CASEY)

3D (ii): Staff recommends that for purposes of this docket, the phrase "specific geographic market" can mean a wire center, a subset of a wire center, a grouping of wire centers, or it could mean something else depending on how competitors elect to compete. (CASEY)

3D (iii): Staff recommends that for purposes of this docket, "similarly situated" or "substantially similar" should be interpreted as customers facing similar competitive alternatives in a "specific geographic market" as defined in Issue 3D ii. (CASEY)

POSITION OF THE PARTIES

FDN:

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Issue 3D: The Commission must consider, at a minimum, BellSouth's dominant market power and position relative to that of individual ALECs, the level and availability of the BellSouth discounts, the duration of the discounts, UNE costs, the level and effect of the termination liability, and the impacts on customers, competition and competitors over time.

(i): Any permitted discounts should be narrowly tailored to meet specific competitor offerings. BellSouth has the ultimate burden of proof on this question, and BellSouth has failed to meet that burden relative to its discounts generally or to SLA, CLUB and moves specifically.

(ii): The Commission should not permit BellSouth to apply discounts to different locations of the same business entity or to customers who have moved to a new location unless BellSouth can show that it is meeting a competitor's offering for those locations.

(iii): Undue discrimination has historically hinged on cost differences inherent in serving customers - cost differences not present here. BellSouth's position must be rejected since BellSouth has not shown that customers not receiving discounts are not harmed by the discount offerings.

BELLSOUTH:

Issue 3D: Section 364.051(5)(a)(2), permits geographic targeting; no additional criteria should be established.

(i): This language means that, where competition exists, BellSouth can adjust its prices to compete.

(ii): This language depends on what the competition is doing. It can mean a different wire center, a subset of a wire center, a grouping of wire centers, or something else.

(iii): How this language should be interpreted depends on the specific circumstances. The heightened competition in BellSouth's Key Customer "hot" wire centers means customers served out of those wire centers are not "similarity situated" or "substantially similar" to other customers.

STAFF ANALYSIS: Staff's analyses will be broken down by Issue 3D, 3D(i), 3D(ii), and 3D(iii) followed by a conclusion paragraph.

- **Issue 3D**

This issue addresses the question of what criteria, if any, should be established to determine whether geographic targeting in a BellSouth promotional tariff is unfair, anti-competitive or discriminatory.

A. FDN Argument (Issue 3D)

FDN witness Gallagher addresses this issue in his direct testimony by pointing out BellSouth's market share, stating:

First, I think the Commission cannot lose sight of the dominant market power that BellSouth currently has in Florida. In other words, the Commission cannot ignore the fact that BellSouth still effectively enjoys monopoly status in its incumbent territory. Though the exact percentage of ALEC market share in BellSouth territory was the subject of significant debate in BellSouth's 271 case (Docket No. 960786-TP) and the Commission did not make any specific findings as to ALEC market share, I do not believe anyone can seriously dispute that BellSouth is by far the dominant provider for voice services in its incumbent territory and has commanding market share. Nor do I think it can be disputed that BellSouth has substantial market power by virtue of its market share and its position in the market. As a general proposition, the Commission should never permit a dominant market provider like BellSouth to use its market power to dictate market products or prices to the detriment of competitors and consumers, particularly when competition is still in a vulnerable infancy, as is the case here in Florida. (TR 37)

B. BellSouth Argument (Issue 3D)

BellSouth witness Ruscilli addresses the issue of establishing criteria for geographic targeting by stating:

Section 364.051(5)(a)(2) of the Florida Statutes makes clear that a local exchange telecommunications company such as BellSouth is not precluded from meeting offerings by any competitive provider of the same, or functionally equivalent, nonbasic services in a specific geographic market or to a specific customer by deaveraging the price of any nonbasic service, packaging nonbasic services together or with basic services, using volume discounts and term discounts, and offering individual contracts. (TR 184-185)

Witness Ruscilli later in his direct testimony, continues and addresses the question of whether additional criteria should be established by stating:

. . . it is not necessary to establish any such criteria. The BellSouth January Key Customer offering is neither unfair, anti-competitive nor discriminatory. This offering is a competitive response to offerings made by competitive providers. Making this offering available in the wire centers where BellSouth has lost, and is continuing to lose, a significant share of business to competition comports with the "specific geographic market" requirement in Section 364.051(5)(a)(2) of the Florida Statutes. Furthermore, the customers to whom BellSouth made this offer available are "similarly situated" in that they have numerous competitive alternatives. (TR 190)

In its brief, BellSouth states that the Commission has already reviewed the language in the Florida Statutes, and determined by its first Order in this docket (which was protested) that the statutory language does not prevent BellSouth from targeting specific geographic markets and offering volume and term discounts. (BellSouth BR 31)

C. Analysis (Issue 3D)

Section 364.051(5)(a)(2), Florida Statutes, provides, in part, that:

. . . Nothing contained in this section shall prevent the local exchange telecommunications company from meeting offerings by any competitive provider of the same, or functionally equivalent, nonbasic services in a specific geographic market or to a specific customer by deaveraging the price of any nonbasic service, packaging nonbasic services together or with basic services, using volume discounts and term discounts, and offering individual contracts. However, the local exchange telecommunications company shall not engage in any anti-competitive act or practice, nor unreasonably discriminate among similarly situated customers.

Staff believes that the above section of the Florida Statutes allows BellSouth to meet competitor's offerings in a specific market or to a specific customer as long as it does not engage in any anti-competitive act or practice, or unreasonably discriminate among similarly situated customers.

D. Conclusion (Issue 3D)

Staff believes that no additional criteria should be established to evaluate whether geographic targeting in a BellSouth promotional tariff is unfair, anti-competitive or discriminatory. Other than the limitation set forth in the last sentence of Section 364.051(5)(a)(2), Florida Statutes, the statute does not provide any restrictions on geographic targeting. Therefore, staff recommends that no criteria should be established, other than that included in Section 364.051(5)(a)(2), Florida Statutes, to determine whether geographic targeting in a BellSouth promotional tariff is unfair, anti-competitive or discriminatory.

• **Issue 3D(i)**

This issue addresses the phrase "meeting offerings by any competitive provider" contained in Section 364.051(5)(a)(2), Florida Statutes.

A. FDN Argument (Issue 3D(i))

FDN does not address the interpretation of the phrase "meeting offerings" in its direct or rebuttal testimony. However, in its brief FDN did provide its opinion of what "meeting offerings" should entail by stating:

First, the ILECs permission is limited to "meeting" competitor offerings for the same or equivalent nonbasic service. The statute does not say that the ILEC is permitted to "beat" competitor offerings, but to "meet" them, which, in the ordinary sense would mean to "match" those offerings. The competitor offerings the ILEC meets must be for the same or equivalent nonbasic service; hence, if a competitor could not provide a service in a market or to a customer, there is no offering the ILEC is permitted to meet. Next, the ILEC offerings are permitted to meet the offering of any competitive provider in a specific geographic market or to a specific customer. So, if a competitor makes an offering in one specific market or to one specific customer but not in or to another, the ILEC is permitted only to meet the offering in the market or to the customer, which the competitor does. (FDN BR 30)

FDN believes that BellSouth has not met its burden of proving its 2002 Key Customer programs comply with Section 364.051(5)(a)(2), Florida Statutes, because BellSouth's witnesses could not state which competitor offerings were being met in which "hot" wire centers. (FDN BR 30)

B. BellSouth Argument (Issue 3D(i))

BellSouth witness Ruscilli provided an interpretation of the term "meeting offerings" in his direct testimony, stating:

The phrase "meeting offerings by any competitive provider" should be interpreted to mean that, where competition exists, BellSouth is allowed to adjust its prices in order to compete effectively. (TR 186)

BellSouth witness Taylor addresses the phrase "meeting offerings" in his direct testimony, wherein he states:

From an economic perspective, the reference to "meeting offerings by any competitive provider" should be interpreted as the ability of the regulated local exchange carrier (here, BellSouth) to respond to the offering of any substitute service by any competitor operating within the same market and competing for the same set of customers. A substitute need not be an identical service, in terms of either its price or non-price characteristics. Rather, all that matters is that if a customer for a specific BellSouth service is likely to be lured away by a competitor offering a "functionally equivalent" substitute, such as by the offer of a more favorable price or other terms and conditions, then regardless of any of the other rules that may apply, BellSouth should have the ability with that market to attempt to retain or win back that customer by suitably altering or redesigning the terms and conditions under which it offers its own service. Doing so precludes BellSouth neither from repackaging or redesigning the service itself nor from offering the original service at a different price or under contract. (TR 475)

C. Analysis (Issue 3D (i))

Staff believes that the phrase "meeting offerings by any competitive provider" implies that BellSouth should have the ability to respond to offerings made by competitors in BellSouth wire centers. Restricting BellSouth from meeting offerings would limit the choices of the consumer in the marketplace. Staff does not agree with FDN that "meeting competitive offerings" should be interpreted as not allowing BellSouth to "beat" competitor offerings. A BellSouth response to a competitor's offering may not necessarily "beat" the offering by dollars, but may "beat" the competitor's offering through perceived value. Staff believes the Commission should not limit market creativity by either BellSouth, or an ALEC.

D. Conclusion (Issue 3D(i))

Staff agrees with BellSouth witness Taylor that a BellSouth competitive offering need not be an identical service, in terms of either its price or non-price characteristics. (TR 475) BellSouth could introduce a bundle of services which may be more attractive than offerings of competitors and be priced higher or lower than a competitor's offering. Therefore, staff recommends that the phrase "meeting offerings by any competitive provider" implies that BellSouth should have the ability to respond to offerings made by competitors in any of its wire centers.

• **Issue 3D(ii)**

This issue addresses the phrase "specific geographic market" contained in Section 364.051(5)(a)(2), Florida Statutes.

A. FDN Argument (Issue 3D(ii))

FDN agrees with BellSouth's definition of "specific geographic market" which was contained in BellSouth's prehearing statement. In its post hearing brief, it states:

FDN does not take issue with the definition of "specific market" BellSouth suggested in its Prehearing Statement, only with how BellSouth has erroneously and unlawfully applied that definition. (FDN BR 32)

B. BellSouth Argument (Issue 3D(ii))

As mentioned above, FDN does not take issue with BellSouth's definition of "specific geographic market" which was contained in BellSouth's pre-hearing statement:

The meaning of the phrase "specific geographic market" is dependent on what the competition is doing. It can mean a wire center, a subset of a wire center, a grouping of wire centers, or it could mean something else depending on how competitors elect to compete. (PH Statement 10-11)

In its brief, BellSouth included essentially the same language:

This language depends on what the competition is doing. It can mean a different wire center, a subset of a wire center, a grouping of wire centers, or something else. (BellSouth BR 31)

C. Analysis (Issue 3D (ii))

FDN agrees with BellSouth's definition of "specific geographic market" which was contained in BellSouth's prehearing statement. Since both parties agree, staff has no objection to using this definition for purposes of this docket.

D. Conclusion (Issue 3D(ii))

Both parties in this case agree to the definition of "specific geographic market." Therefore, for purposes of this docket, staff recommends that the phrase "specific geographic market" can mean a wire center, a subset of a wire center, a grouping of wire centers, or it could mean something else depending on how competitors elect to compete.

• Issue 3D(iii)

This issue addresses the interpretation of the phrase "similarly situated" contained in Section 364.051(5)(a)(2), Florida Statutes.

A. FDN Argument (Issue 3D (iii))

FDN does not address the interpretation of the phrase "similarly situated" or "substantially similar" in its direct or rebuttal testimony. In its brief, FDN included a position on this issue which was more of an argument regarding discrimination among similarly situated customers than an interpretation of the phrase "similarly situated" or "substantially similar."

The question of undue or unreasonable discrimination has historically hinged on cost differences inherent in serving customers in the same class or different classes. When BellSouth retail rates were set prior to the advent of price cap regulation, the Commission

established rate structure and rate classifications/groupings based on cost differences so as to avoid discrimination among similarly situated customers. Here, BellSouth has not alleged that any cost differences among customers arise by virtue of a competitor's presence in a hot wire center. Rather, in reliance on "the competitive necessity doctrine," BellSouth alleges that discriminatory pricing to meet competitor offerings is reasonable and permissible in certain circumstances. However, as FDN has argued in Issue No. 2 above, BellSouth has not fulfilled all of the criteria of the competitive necessity doctrine because BellSouth has not shown that the customers discriminated against have benefitted from the discrimination through rates lower than what they would have been otherwise. (FDN BR 33)

B. BellSouth Argument (Issue 3D(iii))

BellSouth witness Taylor provided an interpretation of the term "similarly situated" in his direct testimony:

From an economic standpoint, the proper interpretation should be that "similarly situated" or "substantially similar" customers are those whose objective circumstances with respect to a specific service are similar. For example, customers with similar willingness to pay (or price elasticity of demand) for a service, or facing similar competitive alternatives in the same geographic market, could be considered similarly situated. Differential pricing (i.e., price discrimination in the economic sense) should not be permitted for similarly-situated or substantially similar customers. In the context of BellSouth's Key Customer promotional offering, similarly situated customers are those for whom BellSouth faces competition from rivals offering substitute services. Those customers are, however, not similarly situated to BellSouth's other customers who do not have the same competitive options. (TR 476)

C. Analysis (Issue 3D (iii))

Many of the parties' arguments on this issue include testimony as to whether BellSouth customers who are similarly situated are discriminated against. The question of discrimination of similarly situated customers is addressed in Issue 3D(iv). Therefore, staff will limit its analysis and recommendation here to the interpretation of the phrase "similarly situated."

In a 1994 complaint (Raymond DiSalvo against BellSouth Telecommunications, Inc. d/b/a Southern Bell Telephone and Telegraph Company.), the Commission stated that the term similarly situated means "similar treatment in similar circumstances." Specifically, by Order No. PSC-95-1153-FOF-TL, issued September 18, 1995, in Docket No. 941261-TL, the Commission stated:

The statute requires that all subscribers who are similarly situated be afforded the same treatment. To do otherwise would constitute an "undue or unreasonable prejudice." The statute generally requires similar treatment in similar circumstances. (Order No. PSC-95-1153-FOF-TL, p.3)

Staff believes that BellSouth customers in different wire centers face different levels of competition. The large metropolitan areas in BellSouth's territory have wire centers where vigorous competition is present. Some rural areas in BellSouth territory have very little or no competition. It is apparent that competitive carriers aim their marketing efforts at the large metropolitan areas where business customers are most prevalent.

D. Conclusion (Issue 3D(iii))

Staff agrees with BellSouth witness Taylor that "similarly situated customers are those for whom BellSouth faces competition from rivals offering substitute services." (TR 476) Staff believes that BellSouth customers in wire centers with little or no competition would not be similarly situated to BellSouth customers in "hot" wire centers where competition is vigorous. The same competitive circumstances would not apply.

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Staff believes that the Commission's interpretation of similarly situated in Order No. PSC-95-1153-FOF-TL should also apply to this case. Therefore, staff recommends that for purposes of this docket, "similarly situated" or "substantially similar" should be interpreted as customers facing similar competitive alternatives in a "specific geographic market" as defined in Issue 3D (ii).

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ISSUE 3D (iv): Is the BellSouth Key Customer tariff filing (Tariff Number T-020035) unfair, anticompetitive, or discriminatory under the criteria, if any, established pursuant to this issue?

ISSUE 3D (v): Is the BellSouth Key Customer tariff filing (Tariff Number T-020595 or a subsequent tariff filing that extends the expiration date thereof) unfair, anticompetitive, or discriminatory under the criteria, if any, established pursuant to this issue?

RECOMMENDATIONS:

3D(iv) AND 3D(v): No. Based on Section 364.051(5)(a)(2), Florida Statutes, staff recommends that the BellSouth January and June Key Customer tariff filings are not unfair, anti-competitive, or discriminatory pursuant to this issue. (CASEY)

POSITION OF THE PARTIES

FDN:

Issue 3D(iv) and 3D(v): Yes. Any BellSouth discounts should be offered to all BellSouth customers. At a minimum, BellSouth customers discriminated against must not be harmed by the discrimination. The record in this case establishes that customers discriminated against have been harmed.

BELLSOUTH:

Issue 3D(iv) and 3D(v): No.

STAFF ANALYSIS: Issues 3D(iv) and 3D(v) address whether the January and June Key Customer offerings are unfair, anti-competitive, or discriminatory based upon the criteria established, if any, in Issue 3D. Since the positions of both parties are the same for each of the issues, staff is presenting one analysis covering both issues for efficiency purposes.

A. FDN Argument (Issue 3D(iv) and 3D(v))

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FDN believes that discounts offered to BellSouth customers in "hot" wire centers should be offered to all BellSouth customers, not just those in certain wire centers. FDN witness Gallagher states:

In my opinion, because BellSouth has not made its discounts available to all customers in the business class, the discounts are, if not discriminatory, at least anti-competitive in the manner in which they are set up and marketed. If BellSouth wants to offer steep discounts and free hunting to customers, it should offer those discounts and free hunting to every customer in the business class in Florida, not just to those customers who are or may be ALEC customers. (TR 46)

Witness Gallagher alleges that BellSouth's geographic targeting of the Key Customer offering discriminates against other customers of BellSouth without justification:

. . . for BellSouth to justify treating customers in the same class disparately for reasons other than cost differences (such as the Key Customer promotions do), the Commission should require BellSouth to show that the customers not receiving the promotions benefit from the discrimination. I do not believe that BellSouth has yet made such a showing, because instead of getting rate decreases, BellSouth customers not eligible for BellSouth's promotions have felt the full brunt of rate increases. Those customers have not benefitted from BellSouth's promotions or from competition. (TR 68)

Witness Gallagher asserts that BellSouth is discriminating against customers who are not in "hot" wire centers:

. . . To approve BellSouth's arguments, the Commission must ignore equity and tell BellSouth customers not receiving promotional rates that not only do they not qualify for lower rates through no fault of their own, but they will have to pay higher rates. Inevitably, those customers will believe that they are financing the customers receiving the lower promotional rates. (TR 69)

Witness Gallagher proposes that BellSouth initiate across-the-board rate decreases for all BellSouth customers. He believes that with an across-the-board decrease, all BellSouth's customers would benefit from competition. Witness Gallagher believes as competition develops, the Commission should protect the interests of all of BellSouth's customers, not just a few of them, and require any BellSouth rate reductions to apply across-the-board. (TR 69-70)

B. BellSouth Argument (Issue 3D(iv) and 3D(v))

Regarding FDN's claim that BellSouth should make discounts available to all customers in the business class instead of just those customers in "hot" wire centers, BellSouth witness Pitofsky counters that there is no legitimate policy reason to adopt such a suggestion in a competitive market:

BellSouth's rivals do not operate under such restrictions. On the contrary, they can and do target specific classes of customers in specific geographic areas where they believe BellSouth may be vulnerable. It would be unwise to adopt a rule that if a provider (even if that provider were a monopolist) discounts to some customers it must discount to all. Under such a regulatory structure, it likely would be uneconomic for sellers that face competition only for some customers to reduce prices to all customers. Rivals would, of course, be aware of such a regulatory restriction, and would not find it necessary to compete as vigorously to obtain customers. The result of such a requirement would be that consumers would be deprived of the low prices and enhanced service that results from competition on the merits.

A rejection of Mr. Gallagher's suggestion also is consistent with current antitrust thinking. If one were to ignore the competitive nature of the Florida hot wire markets and assume that BellSouth were a monopolist, some have concluded in the past that such a party could not offer low prices in areas where it met considerable competition and at the same time keep its prices high where competition was weak or nonexistent, but that does not reflect current thinking. Indeed, there have been

many factual circumstances where exactly the opposite result has now been obtained, as was the result when Telex Corporation complained about IBM raising prices on part of its line, but lowering prices on other items where competition was more intense. These are ordinary business practices today, and are well accepted as ordinary business practices typical of those used in a competitive market. (TR 413-414)

C. Analysis (Issue 3D(iv) and 3D(v))

Issue 3(D) addresses geographic targeting of BellSouth's January and June Key customer offerings. The January and June Key customer offerings have only minor changes regarding geographic targeting. Wire center eligibility for the January Key customer offering was based on line loss reports by wire center, along with the input of BellSouth Competitive Assessment Managers.

When the June Key Customer offering was being planned in April or May of 2002, BellSouth ranked each wire center in its nine-state region using a model that includes the level of competitive activity as a key factor. Florida wire centers that were ranked among the top 30% of BellSouth's region-wide wire centers throughout BellSouth's region were designated as "hot" under the June Key Customer offering. In addition, any wire centers that were designated as "hot" under the January Key Customer offering and that had not yet been 30% penetrated by contracts were also designated as "hot" under the June Key Customer offering. (EXH 1, p. 275)

Staff believes that the differences noted between the January and June Key customer offerings do not constitute a change in the determination of whether these tariffs are unfair, anti-competitive, or discriminatory regarding geographic targeting. Staff believes that BellSouth customers that are not in "hot" wire centers are not being discriminated against those customers eligible for the Key Customer offering. Section 364.051(5)(b)(2), Florida Statutes, states that local exchange companies cannot unreasonably discriminate among similarly situated customers. Staff believes that customers in non-"hot" wire centers are not "similarly situated" to customers in "hot" wire centers where customers are

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exposed to more competition; therefore they are not being discriminated against.

Staff agrees with BellSouth witness Pitofsky that it would be unwise to adopt a rule requiring that if a provider discounts to some customers it must discount to all. That type of action may produce results which would harm rather than help competition. As brought out through questioning of witness Pitofsky at hearing, if the Commission adopted a policy of requiring discounts to be applied to all wire centers, it may have the effect of perpetuating one dominant carrier in the wire centers where the offerings are not now available. If competitors cannot come in when the dominate provider is charging higher prices, they probably are not going to come in and compete in those wire centers at a lower price. (TR 444)

D. Conclusion (Issue 3D(iv) and 3D(v))

Staff believes that BellSouth should be allowed to target wire centers where it believes competitive activity is high, and not be required to offer promotional discounts in all its wire centers. Section 364.051(5)(a)(2), Florida Statutes, provides that a LEC shall not "unreasonably discriminate among similarly situated customers." Staff believes that customers in "hot" wire centers where competition exists are not similarly situated with customers in other BellSouth wire centers where competition is limited or non-existent. Accordingly, BellSouth customers in non-"hot" wire centers are not being discriminated against because the Key Customer offering is not available to them. Therefore, based on Section 364.051(5)(a)(2), Florida Statutes, staff recommends that the BellSouth January and June Key Customer tariff filings are not unfair, anti-competitive, or discriminatory pursuant to this issue.

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ISSUE 2: What criteria, if any, should be established to determine whether the pricing of a BellSouth promotional tariff offering is unfair, anticompetitive, or discriminatory?

(i): Pursuant to the cost standard identified in Sections 364.051(5) and 364.3381, Florida Statutes.

(ii): Pursuant to any other provisions of Chapter 364, Florida Statutes.

(iii): How should the appropriate criteria identified in Issues 2(i) and 2(ii) be applied to a tariff under which varying customer configurations are possible?

(iv): Is the BellSouth Key Customer tariff filing (Tariff Number T-020035) unfair, anticompetitive, or discriminatory under the criteria, if any, established pursuant to Issues 2(i), 2(ii) and 2(iii)?

(v): Is the BellSouth Key Customer tariff filing (Tariff Number T-020595 or a subsequent tariff filing that extends the expiration date thereof) unfair, anticompetitive, or discriminatory under the criteria, if any, established pursuant to Issues 2(i), 2(ii) and 2(iii)?

RECOMMENDATIONS:

2(i) & (ii): The existing criteria set forth in the Florida Statutes are sufficient to determine whether the pricing of a promotional tariff offering is appropriate.

2(iii): The existing criteria set forth in the Florida Statutes should be applied uniformly to a tariff under which varying customer configurations are possible.

2(iv) & (v): No. Based upon the evidence in the record of this proceeding, the BellSouth Key Customer tariff filings (Tariff Number T-020035, Tariff Number T-020595 or a subsequent tariff filing that extends the expiration date thereof) are not unfair, anticompetitive, or discriminatory. The existing criteria set forth in the

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Florida Statutes are sufficient to determine whether the pricing of a promotional tariff offering is appropriate.
(BARRETT)

POSITIONS OF THE PARTIES

FDN:

Issue 2: The Commission must consider, at a minimum, BellSouth's dominant market power and position relative to that of individual ALECs, the level and availability of the BellSouth discounts, the duration of the discounts, UNE costs, and the impacts on customers, competition and competitors over time.

(i): Neither Section 364.051(5) nor 364.3381 should be interpreted so as to sanction discounts of the nature that BellSouth has offered.

(ii): See FDN's position on the above and subsequent issues, including Issue No. 3D. BellSouth's geographic targeting of customers for discounts is discriminatory, as well as unfair and anticompetitive, since all BellSouth customers do not receive or benefit from BellSouth's discounts.

(iii): See FDN's position to 2(i) and 2(ii).

(iv) & (v): Yes. Any BellSouth discounts should be offered to all BellSouth customers. At a minimum, BellSouth customers discriminated against must not be harmed by the discrimination. The record in this case establishes that customers discriminated against have been harmed.

BELLSOUTH:

Issue 2: The criteria set forth in the Florida Statutes are sufficient.

(i): Section 364.3381 does not apply to regulated companies like BellSouth thus no criteria other than

contained in Section 364.051(5) is necessary. Key customer complies with Section 364.051(5). Notwithstanding that Section 364.3381 does not apply to BellSouth, Key customer complies also with Section 364.3381.

(ii): No other criteria is necessary or appropriate.

(iii): Key Customer clearly complies with the criteria set forth in the Florida Statutes when: (a) after applying the deepest discounts, the rates cover the relevant costs of each service; or (b) BellSouth is meeting competitive offerings.

(iv) & (v): No.

STAFF ANALYSIS: This issue evaluates whether specific criteria should be established to determine whether the pricing of a BellSouth promotional tariff offering is unfair, anticompetitive, or discriminatory. The sub-parts to this issue explore various considerations in general, and then in terms of the specific BellSouth tariffs addressed in this proceeding.

For the purposes of efficiency, staff notes that the arguments, analysis, and recommendations presented herein encompass all sub-parts of Issue 2. The analysis herein begins with an overall review of the arguments presented, followed by a limited analysis of the sub-parts, and then a conclusion.

A. FDN Argument² (Issues 2, 2(i), 2(ii), 2(iii), 2(iv), and 2(v))

FDN believes a central theme in this proceeding and in this issue is BellSouth's high market share. Although BellSouth presented data about the overall statewide market share of ALECs in Florida in Exhibit 8 (the 2002 FPSC publication on the status of competition), FDN believes that BellSouth still effectively enjoys monopoly status in its incumbent territory. The FDN witness asserts that this "effective monopoly status" translates into "substantial market power by virtue of its market share and position in the

²FDN's argument in testimony blended the sub-parts of this issue.

market." (Gallagher TR 37) Because it has such a commanding market share, the witness asserts that BellSouth can raise rates in areas where it does not face competition, and that the revenue from this source would more than make up for the discounts offered under the Key Customer tariff promotions. (Gallagher TR 90; FDN BR 10) The maximum discount authorized in the January Key Customer tariff filing was twenty-five percent (25%), and the maximum discount in the subsequent filings, including the tariff currently in effect, is twenty percent (20%), though FDN asserts that the impact of free hunting pushes the "true" discount to near forty percent (40%).

Witness Gallagher contends that the Commission should not permit BellSouth, as the dominant market provider in its service territory, to use its market power to dictate products or prices to the detriment of competitors and consumers, particularly when Florida's competitive market is still in a "vulnerable infancy." (Gallagher TR 37-38) In its consideration of this issue, the witness believes that the Commission should evaluate the following factors:

- 1) the size of BellSouth's tariffed discounts;
- 2) the availability of BellSouth's tariffed discounts;
- 3) the manner in which the discounts are offered;
- 4) how BellSouth has structured the eligibility of the offers; and
- 5) how BellSouth has marketed its promotional offers.

(Gallagher TR 42, 46)

According to FDN witness Gallagher, public interest considerations should obligate the Commission to protect ALECs, including FDN, from the anticompetitive conduct of a provider with BellSouth's market power. (TR 42) FDN believes that the ALECs have more to lose in this case than BellSouth. (FDN BR 14) FDN witness Gallagher analogizes this case to the scenario when AT&T was a dominant provider of interexchange services, and regulatory restraints were implemented to allow competitors an opportunity to gain a foothold in that market. As competition took hold and AT&T became less dominant in the market, AT&T was granted greater pricing flexibility. (Gallagher TR 38)

FDN witness Gallagher believes the Commission should focus on the "dominant market power that BellSouth currently has in Florida,"

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in deciding whether to adopt or establish specific criteria to determine whether the pricing of a BellSouth promotional tariff offering is unfair, anticompetitive, or discriminatory. (TR 37)

The witness believes that two related aspects of this case are critical in the Commission's overall consideration of the issues in this proceeding. They are:

- 1) The "geographic" aspects of this case; and
- 2) The effective discount levels (up to 40% off with hunting) that BellSouth offers with the tariffs at issue in this proceeding.

(Gallagher TR 38, 62)

Regarding the geographic aspects of this matter, the witness states that in offering the Key Customer tariffs to targeted "hot wire centers," BellSouth is "leveraging the geographic weakness in FDN's and other network topologies by lowering prices only in the 'islands' of competition, while raising or maintaining monopoly type rates elsewhere." (Gallagher TR 38) Witness Gallagher asserts that discounts should be uniformly extended to all business customers, both from a tariffing and marketing standpoint. (TR 46)

The witness asserts that BellSouth uses disparate marketing in "offering" the Key Customer tariff, contending that it preys upon those business customers that may be in the process of shopping for the services of an alternative provider. (TR 46) Though witness Gallagher concedes that the Key Customer tariffs are "theoretically available" to all eligible customers within a given geographic area, he believes that BellSouth intensifies its efforts when it is responding to a competitive overture. (TR 136)

FDN contends that BellSouth's tariffed discount offerings should be universally available across the entire business class. According to witness Gallagher, because BellSouth has categorized selected wire centers as "hot" wire centers,

. . . a customer in the business class not served by a hot wire center pays a higher rate for both basic and nonbasic

services than the same customer in the same business class that is served by a hot wire center. (TR 47)

The witness infers that in doing so, BellSouth is unlawfully discriminating among otherwise similarly situated customers. Witness Gallagher states that it would be "inherently unfair and anticompetitive were BellSouth to use higher prices from captive customers to cover the cost of lower prices to customers subject to competition." (TR 42) The witness believes this pricing discrepancy between wire centers is discriminatory, anticompetitive, or both. (Gallagher TR 47)

Regarding the effective discount levels that BellSouth offers with the tariffs at issue in this proceeding, FDN witness Gallagher states that the concessions of free hunting and the non-recurring charge waiver drive the effective discount to a level that grossly exceeds the maximum discount level authorized in the tariff, citing a figure of forty percent (40%). Additionally, he sponsors a spreadsheet exhibit (previously identified as MPG-1) that directly compares the per-line wholesale and retail rates for identical services in five (5) hypothetical locations. (TR 40, 42-43; EXH 6, 1-11). Witness Gallagher explains the exhibit:

FDN selected . . . a hypothetical customer with three (3) business lines and hunting on all three (3) lines - fairly typical for a small business. The exhibit compares the retail prices under a standard Bell tariff arrangement, a BellSouth Key Customer deal (the current June 2002 tariff), and a standard FDN offering. (TR 43)

He states that BellSouth's Key Customer scenario undercuts the FDN standard offering in each location, and that resale is the only means by which FDN may be able to beat the BellSouth Key Customer price (excluding consideration for any early termination or other liabilities). The witness contends, however, that "resale is not a viable option and does not justify BellSouth's practices" (Gallagher TR 43)

The five (5) sample customer locations are Miami, West Palm Beach, Port St. Lucie, Orlando, and Tamarac; these cities represent various BellSouth rate groups and UNE zones. The following table,

Table 2-1, presents the data for one of the sample customer locations.

ALLAPATTAH - MIAMFLAL (RG12) - ZONE 1						
Sample Configuration	<u>RETAIL</u>			<u>WHOLESALE</u>		
	<u>BellSouth Tariff- Customer</u>	<u>FDN Tariff- Customer³</u>	<u>BellSouth Key Customer⁴</u>	<u>FDN Resale- Standard</u>	<u>FDN Resale-Key Customer⁵</u>	<u>FDN UNE-P⁶</u>
Business Lines x 3	\$110.85	\$ 88.68	\$ 88.68	\$ 92.22	\$ 73.77	\$ 56.13
Hunting Feature x 3	\$ 30.00	\$ 22.50	-0-	\$ 24.96	-0-	\$ 6.51
SUM (Total Monthly Recurring Charges)	\$140.85	\$111.18	\$ 88.68	\$117.17	\$ 73.77	\$ 62.64
SUM (Total Monthly Recurring Charges/ = Per Line Amt.)	\$ 46.95	\$ 37.06	\$ 29.56	\$ 39.06	\$ 24.59	\$ 20.88
Total Non-Recurring Charge	\$ 80.00	\$150.00	-0-	-0-	-0-	-0-

TABLE 2-1: Summary of pages 2-3 from Exhibit 6

Witness Gallagher concludes his discussion of this data by expressing that "ALECs simply cannot beat discounts like this without placing their futures in peril." (TR 43)

In terms of specific actions, witness Gallagher recommends that restrictions be implemented for BellSouth in its franchised areas of Florida until such time that ALECs have achieved "meaningful" market

³Customer signs a 36 month commitment with FDN.

⁴Customer signs a 36 month commitment with BellSouth.

⁵Customer signs a 36 month commitment, FDN pays termination liability to BellSouth.

⁶SL-1 loop. Assumes 380 minutes of outbound local calls on the BellSouth network and 190 minutes of outbound local calls via multiple networks. ADUF/ODUF/CABS charges are not being calculated.

share in these areas. (TR 48) FDN's recommended restrictions are two-fold:

- 1) BellSouth should be barred from offering direct or indirect discounts of more than ten percent (10%) off total billed basic and nonbasic telecommunications services, including hunting and all features.
- 2) Any and all such discounts should be offered to all members of a customer class.

(Gallagher TR 48) The witness believes these restrictions are necessary to shift the concentration of market power away from the incumbent, BellSouth. The threshold level that would signal a market power shift is forty percent (40%) ALEC market share, according to witness Gallagher. (TR 48) Witness Gallagher asserts that the restrictions FDN recommends "should at least diminish the anticompetitive effects of BellSouth's promotional discounts." (TR 48)

As referenced earlier, FDN's argument in its testimony blended the sub-parts of this issue. Under cross examination by BellSouth's counsel, FDN witness Gallagher affirmed that FDN had "no position" on sub-issue (iii), although more assertions specifically addressing the sub-parts were included in the FDN briefs. Therein, FDN contends that BellSouth's reliance on statutory language in Section 364.051(5), Florida Statutes, is misapplied. FDN stresses that BellSouth's cost study was based upon its analysis of *incremental* costs, and not the *direct* costs which Section 364.051(5)(c), Florida Statutes, requires. For this reason, FDN believes BellSouth has failed to support its tariff filings, and this Commission should "strike down" the Key Customer tariffs of this proceeding. Finally, FDN contends that its argument on geographic targeting should be considered in conjunction with the sub-parts to this issue. (FDN BR 15-17)

B. BellSouth Argument (Issue 2 and all sub-parts)⁷

⁷BellSouth's argument in testimony was presented by sub-part; staff has grouped this argument accordingly.

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Staff notes that BellSouth addresses these issues by sub-part, though certain argument encompasses all of the sub-parts.

From a public policy standpoint, witness Ruscilli believes that promotions in general are a natural outgrowth of the market development contemplated by the Telecom Act of 1996, and encouraged by this Commission. (TR 156) At a threshold level, he believes the Key Customer tariff filings at issue in this proceeding comply fully with the Florida Statutes, and are in no way unfair, anticompetitive, or discriminatory. (Ruscilli TR 198) BellSouth witness Pitofsky believes the "discount programs made available to customers in Florida by BellSouth are proconsumer and procompetitive." (TR 408) BellSouth's witness Garcia states that "to compete in the marketplace, BellSouth must respond to . . . [ALEC] offerings by, among other things, offering lower prices for its services." (TR 331) Witness Taylor expresses that

the Florida Statutes provide all the protections necessary against unfair pricing (and, in particular, anti-competitive promotional tariff offerings), and the Commission should apply the tests contained therein to resolve the issues in dispute in this proceeding. (TR 461)

• **Issue 2**

BellSouth witness Taylor states that from an economic standpoint, the fairness of a price is judged by considering if the subject price is fair to competitors, and fair to consumers. (TR 459) A price is fair to competitors as long as it is not anti-competitive, and a price is fair to consumers if it does not discriminate among customers that are similarly situated, he explains. (Taylor TR 459) Witness Taylor asserts that "if BellSouth's promotional offerings are priced in accordance with these two principles, then they will be fair to both competitors and customers." (TR 460) The witness contends that the fairness argument is closely related to the individual circumstances:

While price differentiation (or, in economic parlance, "price discrimination") can occur even in workably competitive markets . . . , the minimum requirement there

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is that customers being charged different prices must be in different circumstances . . .

. . .

For BellSouth's Key Customer plan, similarly situated consumers are those for whom BellSouth faces competition from rivals offering substitute services. Those customers, however, are not similarly situated to BellSouth's other customers who don't have the same set of competitive options. (Taylor TR 459, 513)

- **Issue 2(i)**

This sub-part addresses what criteria should be established to determine whether the pricing of a BellSouth promotional tariff offering is unfair, anticompetitive, or discriminatory pursuant to the cost standards in two specific Sections of the Florida Statutes, Sections 364.051(5) and 364.3381.

Witness Taylor examines each referenced Florida Statute individually. He asserts that in sub-parts (b) and (c) of Section 364.051(5), Florida Statutes, the cost standards that pertain to the pricing of nonbasic services are presented. (Taylor TR 460) Regarding sub-parts (b) and (c) of Section 364.051(5), Florida Statutes, the witness testifies:

Section 364.051(5)(b), Florida Statutes, states the following cost standard for preventing cross-subsidy:

The cost standard for determining cross-subsidization is whether the total revenue from a nonbasic service is less than the total long-run incremental cost of the service. Total long-run incremental cost means service-specific volume and nonvolume-sensitive costs.⁶

⁶ This measure of cost is also frequently called total service long run incremental cost ("TSLRIC").

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Section 364.051(5)(c), Florida Statutes, lays out a cost standard that (implicitly) address[es] both predatory pricing and a price squeeze:

The price charged to a consumer for a nonbasic service shall cover the direct costs of providing the service and shall, to the extent a cost is not included in the direct cost, include as an imputed cost the price charged by the company to competitors for any monopoly component used by a competitor in the provision of its same or functionally equivalent service.

According to witness Taylor, Section 364.3381(1)-(2), Florida Statutes, contains the same cost standards as in Section 364.051(5) for the prevention of cross-subsidy, while also providing that the Commission shall have:

'continuing oversight jurisdiction over cross-subsidization, predatory pricing, or other similar anti-competitive behavior . . . ,' [though] it is my understanding that Section 364.3381 applies to local exchange telecommunications carriers that do not operate under price regulation, while Section 364.051(5) applies specifically to BellSouth and other local exchange carriers operating under the price regulation statute. (Taylor TR 460-461)

Witness Taylor acknowledges that Section 364.3381, Florida Statutes, makes reference to the term "predatory pricing," yet the statute sets out no specific protection against it. (TR 461) Section 364.051(5)(c), Florida Statutes, however, sets out the economic protection against predatory pricing and a price squeeze, but does not name these as forms of anti-competitive pricing. The witness continues:

From an economic standpoint, the price floor that protects against predatory pricing generally is long run incremental cost ("LRIC") . . . , [and] the economic price floor that protects against a price squeeze augments the floor for predatory pricing by adding the contribution

(price less incremental cost) the competitor must pay for the incumbent's essential facilities. (Taylor TR 461-462)

An essential facility, the witness explains, is a "facility that competitors are unable to practically or reasonably duplicate," and a price squeeze occurs when the firm that controls the essential facility sets the price of that item so high that it becomes an unbearable cost to the competitor. (Taylor TR 462) However, he believes that Section 364.051(5)(c), Florida Statutes, seeks to prevent such an occurrence by requiring BellSouth to impute the price of that essential facility into its cost to supply the nonbasic service.⁵

According to witness Taylor, the imputation price floor that provides this protection against a price squeeze is needed only if the supply for the "essential facility" comes from a single source. (TR 463) This level of protection is no longer necessary when competitive alternatives for "essential facilities" exist. Because the "essential facility" itself can be procured from other sources, it ceases to be a "monopoly" component, and in that event, "the price floors needed to prevent other forms of anti-competitive pricing alone suffice." (Taylor TR 463)

Section 364.051(5)(b), Florida Statutes, also references cross-subsidies. The witness explains that cross-subsidies occur based upon an accounting practice that shifts costs from a competitive to a noncompetitive services, though witness Taylor testifies that, "there are several reasons why cross-subsidization of non-basic services is not a serious real-world concern in Florida." (TR 464) He states:

First, regulatory concern with universal service has created prices which, if they embody a subsidy at all, are much more likely to entail a subsidy flow from nonbasic to basic services, rather than the other way around. Second, a complete accounting separation of non-competitive and

⁵From an economic perspective, the imputation price floor should be the sum of the direct incremental cost of the nonbasic service and the contribution margin (i.e., price less incremental cost) that BellSouth could earn from the nonbasic service. When BellSouth's cost to provide the essential facility to its competitors is the same as the cost to provide it to itself, this condition can be shown to be equivalent to that in Section 364.051(5)(c) of the Florida Statutes. (Taylor TR 463)

competitive services makes it difficult for the firm to shift costs in the manner described. Third, most forms of price regulation (like the one that applies to BellSouth under Section 364.051, of the Florida Statutes) automatically prevent cross-subsidization by (1) separating prices from accounting costs and (2) assigning non-basic and basic services to separate baskets and applying different pricing rules. As a result, service prices within each basket are governed solely by pricing rules specific to that basket, and cannot be influenced by costs or prices in other baskets. (Taylor TR 464-465)

Because BellSouth no longer is subject to the traditional cost-of-service standards, cross-subsidization should not be a paramount concern for this Commission, according to witness Taylor. (TR 464) In conclusion, BellSouth believes the criteria set forth in the Florida Statutes are sufficient to determine whether the pricing of a promotional tariff offering is appropriate. (BellSouth BR 12)

- **Issue 2(ii)**

This sub-part addresses what criteria should be established to determine whether the pricing of a BellSouth promotional tariff offering is unfair, anticompetitive, or discriminatory pursuant to any other provisions of Section 364, Florida Statutes.

BellSouth witness Taylor believes that the criteria and statutes under review in sub-part (i) of this issue "are reasonably consistent with the economic tests for anticompetitive pricing in the forms of predatory pricing, cross-subsidization, and a price squeeze." (TR 465) The witness does not specifically enumerate any other criteria specifically applicable to this sub-issue. BellSouth asserts that there is no predatory pricing concern as long as the price for a service is above the appropriate measure of cost, total service long-run incremental cost ("TSLRIC"). (BellSouth BR 15)

- **Issue 2(iii)**

This sub-part addresses how the above-referenced criteria in sub-parts (i) and (ii) of this issue should be applied to a tariff under which varying customer configurations are possible.

Witness Taylor contends that "varying customer configurations" come about when customers are allowed to purchase services in different combinations, with each unique service priced differently in those combinations than they would be on a stand-alone basis. (TR 472) He states there is no economic justification for applying the competitive fairness tests to each such configuration, explaining that fairness in the aggregate is achieved

. . . as long as the [configured] service . . . is priced appropriately, no competitor in the market is placed at a competitive disadvantage. Firms do not generally offer identical packages of services, let alone compete in any product market consisting of a single package. (Taylor TR 472)

- **Issue 2 (iv)**

This sub-part asks whether the January tariff filing is unfair, anticompetitive, or discriminatory pursuant to the above-referenced criteria in sub-parts (i), (ii), and (iii) of this issue.

As mentioned previously, BellSouth believes the Key Customer tariff filings at issue in this proceeding, including the January filing, comply fully with the Florida Statutes, and are in no way unfair, anticompetitive, or discriminatory. (Ruscilli TR 198) Witness Ruscilli contends that the January filing is an "appropriate competitive response brought about by the high level of local service competition that exists in Florida." (TR 158) The witness relies upon two main sources of data to support this assertion:

(1) the information he presents in Hearing Exhibit 12, which was previously identified as Exhibit JAR-1¹⁰ attached to his direct testimony; and

¹⁰ Exhibit JAR-1 is the Affidavit of Elizabeth A. Stockdale, a document that was filed with the FCC in WC Docket No. 02-307. The affidavit was filed in support of BellSouth's application to obtain interLATA long distance authority in Florida and Tennessee. BellSouth witness Ruscilli adopts this information as his own.

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(2) the data contained in the Commission's own 2002 Annual Report on Competition¹¹ (2002 Comp Report), Hearing Exhibit 8.

Citing Hearing Exhibit 12, the witness states:

- ▶ over 105 ALECs were serving approximately 1.3 M access lines, which is 17.7 per-cent (17.7%) of the total access lines in the BellSouth service area.
- ▶ at least 51 of the ALEC providers in Florida are facilities-based providers.
- ▶ BellSouth has over 350 approved Interconnection, Collocation, and/or Resale agreements with ALECs in Florida.
- ▶ BellSouth has completed 1,371 collocation requests for ALECs in 130 of BellSouth's 201 Florida wire centers.
- ▶ From these 130 wire centers, ALECs' collocation arrangements enable facilities-based ALECs to address approximately ninety two percent (92%) of BellSouth's total access lines.

The witness continues by citing the findings contained in Hearing Exhibit 8:

- ▶ Competitors in Florida have obtained a thirteen percent (13%) market share, up from eight percent (8%) in 2001.
- ▶ ALECs have made impressive gains in the business market, increasing their share of business access lines to twenty six percent (26%), up from last year's share of sixteen percent (16%). (This represents an increase of sixty two and one-half percent 62.5%).

(Ruscilli TR 158-159)

¹¹Titled "Telecommunications Markets in Florida, Annual Report on Competition as of June 30, 2002," the publication is prepared annually to satisfy the statutory requirements set forth in Sections 364.386 and 364.161(4), Florida Statutes.

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Based on this data, witness Ruscilli asserts that the substantial growth in the business sector has occurred in the wire centers named in the January Key Customer tariff filing; furthermore, the growth has occurred during periods of time in which BellSouth promotions similar to the Key Customer offerings have been in effect. (TR 160) This fact alone dispels any notion that the January Key Customer filing is somehow anticompetitive, according to witness Ruscilli. (TR 160) The cumulative data presented in Hearing Exhibit 8 clearly shows:

(1) Competition has grown significantly despite BellSouth's promotional offerings; and

(2) BellSouth chose the wire centers for the January tariff filing to correspond with locations where ALECs were aggressively winning business lines.

(Ruscilli TR 161)

BellSouth witnesses' Bigelow and Shell's testimony focused on the cost/price analysis that went into evaluating BellSouth's January tariff offering. Witness Shell states:

. . . [T]he January Key Customer offering . . . provided a maximum discount of 25% off the standard tariffed rates for Key-eligible services. BellSouth first evaluated the 1FB business service line ("1FB") to ensure that it would be above-cost in all rate groups when discounted at the maximum level. No features or other services were included in this test. The subscriber line charge ("SLC") was added to the discounted tariff rate . . . The costs used for this test were the statewide average Unbundled Network Elements ("UNE") rates¹² for the loop-port combination plus usage . . . These rates were based on Total Element Long Run Incremental Cost ("TELRIC") methodology and used as a surrogate for the 1FB cost. While the appropriate cost standard is TSLRIC, the statewide average UNE rates were used as a conservative

¹²The rates used were ordered by this Commission in Order No. PSC-01-2051-POF-TP, issued in Docket No. 990649-TP on October 18, 2001.

approach. Given that TELRIC typically results in higher costs than TSLRIC for business service lines, this test proved that the discounted 1FB is above TSLRIC in all rate groups.

. . .

Next, BellSouth identified the rate elements or USOCs producing 99.9% of the revenue from retail customers matching the guidelines described in the testimony of BellSouth witness Steven Bigelow. The maximum discount for the January Key customer offering of 25% was applied to the prices of these individual rate elements. The discounted prices were then compared to the costs of the rate elements . . . (Shell TR 359-360)

Witness Bigelow states that in designing the price/cost study for Florida, a total of over 800 rate elements were identified up-front for possible inclusion, but that BellSouth records indicated that 99.9% of the revenue was generated from only 208 of these elements. (TR 390) Thus, BellSouth made the decision to limit the scope of this study in this manner. The witness explains that a similar analysis was conducted to support the Key Customer offering that preceded the January filing,¹³ and states that the differences between the June of 2001 promotion and the January promotion were minor. (Bigelow TR 388-389)

Witness Bigelow states that after the initial testing of all elements, certain individual rate elements failed the margin test; thereafter, the failing rate elements were re-analyzed:

the first step was to identify whether the element was a stand-alone service or whether it was a component of a larger service. If it was a component of a larger service, the data for the failed element and all related rate elements were sent to a tariff subject matter expert for evaluation . . . [The subject matter expert] developed a system configuration representative of the target

¹³The witness refers to a tariff that became effective June 26, 2001. (Bigelow TR 388) Hearing exhibit 11, a composite of pre-2002 BellSouth promotional tariff offerings, does not contain this tariff.

market. This system configuration was then evaluated to determine if it passed the margin test. (Bigelow TR 391)

Several system configurations were presented by witness Shell, along with the margin analysis in (proprietary) Hearing Exhibit 25 (f/k/n Exhibit WBS-2 attached to his direct testimony).

In summary, BellSouth does not believe any aspect of its January tariff filing is unfair, anticompetitive, or discriminatory. Witness Garcia states that BellSouth faces its "most fierce" competition in the wire centers named in the January and June Key Customer tariff offerings. (TR 327) Witness Ruscilli believes that promotional offerings (like the January tariff filing) that provide lower prices "serve as concrete evidence from all competitors, ILECs and ALECs alike, that competition is taking hold in the market . . . [and] the public in general will benefit." (TR 198)

- **Issue 2(v)**

This sub-part asks whether the June tariff filing or a subsequent tariff filing that extends the effective date thereof is unfair, anticompetitive, or discriminatory pursuant to the above-referenced criteria in sub-parts (i), (ii), and (iii) of this issue.

As mentioned previously, BellSouth believes the Key Customer tariff filings of this proceeding, including the June and its subsequent tariff, comply fully with the Florida Statutes, and are in no way unfair, anticompetitive, or discriminatory. (Ruscilli TR 198) BellSouth contends that the lower maximum discount offered in the June filing - twenty percent (20%) verses twenty-five (25%) in the preceding tariff - is sufficient justification to demonstrate that its tariff offers rates that are at or above TSLRIC. (Shell TR 361) For that reason, the bulk of BellSouth's argument presented above in Issue 2(iv) is adopted here.

C. Analysis (Issue 2 and all sub-parts)

As noted previously, this issue evaluates whether specific criteria should be established to determine if the pricing of a BellSouth promotional tariff offering is unfair, anticompetitive, or discriminatory. The sub-parts to this issue explore various

considerations in general, and then in relation to the specific BellSouth tariffs addressed in this proceeding. For the purposes of efficiency, staff's analysis encompasses all sub-parts of Issue 2.

At the outset, staff would note that the terms "unfair, anticompetitive, or discriminatory" are rooted in the Florida Statutes. The terms "fair" (or like words derived from the word "fair") and "anticompetitive" are mentioned numerous times throughout, beginning in Section 364.01, Florida Statutes:

364.01 Powers of commission, legislative intent.--¹⁴

. . . .

(4) The commission shall exercise its exclusive jurisdiction in order to:

. . . .

(g) Ensure that all providers of telecommunications services are treated fairly, by preventing anticompetitive behavior and eliminating unnecessary regulatory restraint.

The term "discriminate" (or like words that are derived from the word "discriminate") appears in Section 364.051, Florida Statutes:

364.051 Price regulation.--¹⁵

. . . .

(5) (a) NONBASIC SERVICES.--Price regulation of nonbasic services shall consist of the following:

. . . .

¹⁴History.--ss. 1-4, ch. 6186, 1911; ss. 1-6, ch. 6187, 1911; s. 1, ch. 6525, 1913; RGS 4393; CGL 6357; s. 1, ch. 63-279; s. 1, ch. 65-52; s. 1, ch. 67-541; s. 3, ch. 76-168; s. 1, ch. 77-457; ss. 1, 32, ch. 80-36; s. 2, ch. 81-318; s. 25, ch. 83-218; ss. 6, 7, ch. 89-163; ss. 1, 46, 49, ch. 90-244; s. 4, ch. 91-429; s. 9, ch. 95-403.

¹⁵History.--s. 9, ch. 95-403; s. 8, ch. 98-277; s. 3, ch. 2000-334.

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However, the local exchange telecommunications company shall not engage in any anticompetitive act or practice, nor unreasonably discriminate among similarly situated customers. (emphasis added)

Staff's broad task in evaluating Issue 2 and its sub-parts is to evaluate the matters at hand for compliance with the Florida Statutes.

BellSouth witness Ruscilli states that the true meaning of the word *discrimination* is important to this Commission's consideration. He asserts:

The term *discrimination* merely denotes the offering of different services to different customers under different rates, terms, and conditions . . . [He stresses that] BellSouth is only prohibited from "unreasonably discriminat[ing]" among similarly situated customers. (TR 211-212)

The witness asserts that the Key Customer offerings at issue in this proceeding do not rise to that level because (1) the tariffs are offered to all similarly situated customers, and (2) the tariffs are available for resale to competitors. (Ruscilli TR 211-212)

Staff notes that FDN repeatedly argues that BellSouth's tariffed discount offerings should be universally available across the entire business class. Otherwise, the business class becomes divided between the "haves" and the "have nots," according to FDN witness Gallagher. (TR 12) The FDN witness claims that the result of not offering the Key Customer tariff universally means that

. . . a customer in the business class not served by a hot wire center pays a higher rate for both basic and nonbasic services than the same customer in the same business class that is served by a hot wire center. (Gallagher TR 47)

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FDN believes BellSouth's immense market power enables it to act in an anticompetitive manner whereby BellSouth can raise rates in areas where it does not face competition, the "non-hot wire centers," and that the revenue from this source would more than make up for the discounts offered under the Key Customer tariff promotions. (Gallagher TR 90) The witness believes that the Commission should be especially mindful of:

- 1) The "geographic" aspects of this case; and
- 2) The effective discount levels (up to 40% off with hunting) that BellSouth offers with the subject tariffs of this proceeding.

(Gallagher TR 38, 62) FDN believes the Commission should protect ALECs, including FDN, from the anticompetitive conduct of a provider with BellSouth's market power. (TR 42) Florida's competitive market, according to the FDN witness, is still in a "vulnerable infancy," which justifies his assertion that the Commission should monitor:

- 1) the size of the BellSouth's tariffed discounts;
- 2) the availability of BellSouth's tariffed discounts;
- 3) the manner in which the discounts are offered;
- 4) how BellSouth has structured the eligibility of the offers; and
- 5) how BellSouth has marketed its promotional offers.

(Gallagher TR 37-38, 42, 46)

FDN recommends that tariff restrictions be implemented for BellSouth in its franchised areas of Florida until such time that ALECs have achieved "meaningful" market share in these areas. FDN's recommended restrictions are:

- 1) BellSouth should be barred from offering direct or indirect discounts of more than ten percent (10%) off total billed basic

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and nonbasic telecommunications services, including hunting and all features.

- 2) Any and all such discounts should be offered to all members of a customer class.

(Gallagher TR 48)

Staff, however, does not agree with FDN that the enumerated restrictions are necessary, or appropriate. Rather, staff tends to agree with BellSouth witness Pitofsky, who believes the "discount programs made available to customers in Florida by BellSouth are proconsumer and procompetitive." (TR 408)

FDN and BellSouth both cite to the evidence presented in Exhibit 8 (the 2002 Comp Report), a publication of this Commission that documents the growth in the competitive telecommunications industry in Florida. Therein, Commission research is summarized that reflects (among other things) that:

- In 2002, competitors have obtained a thirteen percent (13%) overall market share, up from an eight percent (8%) figure in 2001.
- ALECs have made impressive gains in the business market,¹⁶ increasing their share to twenty-six percent (26%) of business access lines; last year's figure was sixteen percent (16%).

(EXH 8, p.3)

¹⁶Staff notes that the Key Customer tariffs of this proceeding are specifically designed for the business market.

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Staff notes, as BellSouth does, that this growth has occurred while the Key Customer tariff promotions were (are) in effect. BellSouth's witness Garcia states:

. . . Key Customer offers are a direct result of the competition that has been and continues to take place in Florida in the small business market. And even with the Key Customer [tariffs] in place, other carriers have offered and continue to offer customers lower rates and have experienced line growth. (TR 344)

Staff believes and the evidence suggests that the Petitioner in this case, FDN, has participated in this expansion.

Sub-issue 2(i) asks whether any criteria should be established to determine if the pricing of a BellSouth promotional tariff offering is unfair, anticompetitive, or discriminatory pursuant to the cost standards in Sections 364.051(5) and 364.3381, Florida Statutes. Staff believes the relevant parts of Section 364.051(5), Florida Statutes, are (b) and (c), as noted:

364.051 Price regulation.--

. . .

(5) NONBASIC SERVICES.--Price regulation of nonbasic services shall consist of the following:

. . .

(b) . . . The cost standard for determining cross-subsidization is whether the total revenue from a nonbasic service is less than the total long-run incremental cost of the service . . .

(c) The price charged to a consumer for a nonbasic service shall cover the direct costs of providing the service and shall, to the extent a cost is not included in the direct cost, include as an imputed cost the price charged by

the company to competitors for any monopoly component used by a competitor in the provision of its same or functionally equivalent service.

This sub-issue also references Section 364.3381, Florida Statutes, and staff believes the only relevant portion of this Section that addresses a cost standard is a small portion of Section 364.3381(2), Florida Statutes, which follows:

364.3381 Cross-subsidization.--¹⁷

. . .

(2) . . . The cost standard for determining cross-subsidization is whether the total revenue from a nonbasic service is less than the total long-run incremental cost of the service. Total long-run incremental cost means service-specific volume and nonvolume sensitive costs.

Of these three referenced Sections, staff notes that Sections 364.051(5)(b) and 364.3381(2), Florida Statutes, focus on cross-subsidization; staff believes that Section 364.051(5)(c), Florida Statutes, is most crucial since it is unlikely that non-basic service is being cross-subsidized. Though prohibited by statute, staff does not believe that the Petitioner makes a specific allegation that cross-subsidization is occurring, or evident. Moreover, staff agrees with BellSouth witness Taylor that universal service concerns have likely created a subsidy flow from nonbasic services to basic services, not the reverse.

Section 364.051(5)(c), Florida Statutes, examines direct costs, and staff believes an examination of direct cost is needed to make a determination of whether the post-discounted rates offered in a Key Customer contract remain "compensatory" for BellSouth. If a determination revealed that the such rates were "non-compensatory," such a finding would sway staff to conclude that the tariff offering is unfair, anticompetitive, or discriminatory.

¹⁷History---ss. 38, 49, ch. 90-244; s. 4, ch. 91-429; s. 26, ch. 95-403.

As presented earlier, the January tariff offered a larger maximum discount for the end use subscriber than the June (or the subsequent extension tariff) filing. All other things being equal, staff believes a lesser discount (e.g., the June or subsequent tariff) would yield a higher margin than a contract with a higher maximum discount (such as the January filing). Therefore, staff concludes that if a contract signed under the January tariff is "compensatory" at a twenty-five percent (25%) discount, an identically configured contract signed under a June or subsequent tariff filing would be "compensatory" at a twenty percent (20%) discount. BellSouth's witness Shell essentially states this as well, relying on the extensive analysis BellSouth performed in support of the January filing. (TR 361)

Via discovery, staff obtained and evaluated a selection of actual contracts that were signed under the January tariff offering. (Item 3 of composite Hearing Exhibit 4) These contracts identified the quantities and services of each customer. Staff also obtained the results of the BellSouth cost study to which witnesses Shell and Bigelow refer.^{1E} (Item 1 of composite Hearing Exhibit 4) The proprietary cost study listed by name and USOC the cost/price information and margin information for each of the 208 services that BellSouth analyzed. Witness Shell describes the contents of this spreadsheet in his direct testimony. (TR 364) Staff used this data as a starting point to fully evaluate the contracts within its possession. With this cost/price information, staff conducted its own analysis of the actual contracts it had obtained via discovery; our intent was to evaluate conclusively whether the post-discount contracts were in compliance with Section 364.051(5)(c), Florida Statutes (i.e., staff sought to determine if any post-discount contracts were being offered by BellSouth below their direct cost).

Because Section 364.051(5)(c), Florida Statutes, begins with the phrase: "The price charged to a consumer for a nonbasic service . . ." (emphasis added by staff), various possible interpretations emerge in determining what constitutes a "nonbasic service." Staff

^{1E}Staff obtained this cost study on March 27, 2002; BellSouth witness Shell attached the identical study (f/k/a Exhibit WBS-2) to his direct testimony on October 23, 2002.

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believes the margin analysis to satisfy the above-referenced statute can be done by evaluating either a "component," a "service" (which could be made up of one or more components), or a "contract" (which could be the made up of one or more services). Staff believes an argument could be made that "a nonbasic service" could be any of these, though, for the purposes of a margin analysis, staff believes an aggregate perspective (i.e., the "contract" interpretation) is warranted.

Staff believes the aggregate perspective, in fact, is bolstered by the Petitioner's argument; FDN does not assert that particular BellSouth *services* are non-compliant, but rather that BellSouth's post-discount *contracts* are. Although BellSouth analyzed individual USOCs that account for over ninety-nine percent (99.9%) of the revenue limits for the targeted customers¹⁹, staff believes the aggregate, or "per-contract," interpretation is the most appropriate to evaluate compliance with Section 364.051(5)(c), Florida Statutes, since the collective margins of all services within an individual contract (positive or negative) are a logical indicator of whether a post-discount contract is compliant, or not.

Based on staff's analysis, we did not find that any post-discount contracts were being offered below the direct cost. Staff notes that the contracts were provided while the January filing was in effect, and contain the highest maximum discount of the three Key Customer tariff offerings of this proceeding. Staff therefore concludes that the January contracts it reviewed are "compensatory;" furthermore, all things being equal, any similar contract (from the June or the subsequent Key Customer tariff) would be "compensatory" as well, since the maximum discount level is lower, yielding a higher net margin compared to the January filing.

D. Conclusion (Issue 2 and all sub-parts)

Staff believes that the existing criteria set forth in the Florida Statutes are sufficient to determine whether the pricing of a promotional tariff offering is appropriate. Furthermore, based

¹⁹BellSouth studied customer billed revenue limits which ranged from \$100/month (minimum) to \$3,000/month (maximum). (Bigelow TR 388)

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upon the evidence in the record of this proceeding, staff believes the Key Customer tariff offerings of this proceeding are not unfair, anticompetitive, or discriminatory.

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ISSUE 3A: What criteria, if any, should be established to determine whether the termination liability terms and conditions of a BellSouth promotional tariff offering are unfair, anticompetitive, or discriminatory?

(i): Is the BellSouth Key Customer tariff filing (Tariff Number T-020035) unfair, anticompetitive, or discriminatory under the criteria, if any, established pursuant to this issue?

(ii): Is the BellSouth Key Customer tariff filing (Tariff Number T-020595 or a subsequent tariff filing that extends the expiration date thereof) unfair, anticompetitive, or discriminatory under the criteria, if any, established pursuant to this issue?

RECOMMENDATIONS:

3A: Staff does not believe any specific criteria should be established outside of the existing guidance from the Florida Statutes to determine whether the termination liability terms and conditions of a BellSouth promotional tariff are unfair, anticompetitive, or discriminatory.

3A(i) & 3A(ii): The Key Customer tariff filings at issue in this proceeding are not unfair, anticompetitive, or discriminatory pursuant to the Florida Statutes.

Staff recommends, however, that BellSouth should revise the applicable portion of its current Key Customer tariff, Tariff No. T-021241, to clearly disclose that the termination liability does not apply in a "split-service" scenario. The corresponding revision should be made to the standard contract used to enroll subscribers as well. Additionally, on a going-forward basis, all future BellSouth promotional tariffs that are based on total billed revenue should clearly disclose that the

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termination liability does not apply in a "split-service"
scenario. (BARRETT)

POSITIONS OF THE PARTIES

FDN:

Issue 3A: The Commission must consider, at a minimum, BellSouth's dominant market power and position relative to that of individual ALECs, the level and availability of the BellSouth discounts, the duration of the discounts, UNE costs, the level and effect of the termination liability, and the impacts on customers, competition and competitors over time.

(i) & (ii): Yes. BellSouth's early termination liability should not exceed BellSouth's retail line installation rates. Alternatively, the Commission may order the parties to have reciprocal termination liability not to exceed retail installation rates.

BELLSOUTH:

Issue 3A: Existing Florida law addressing liquidated damages, along with competitive market forces, is sufficient to ensure that termination liability terms and conditions are fair, competitive, and nondiscriminatory.

(i) & (ii): No.

STAFF ANALYSIS: This issue evaluates whether specific criteria should be established to determine whether the termination liability terms and conditions of a BellSouth promotional tariff offering are unfair, anticompetitive, or discriminatory. The sub-parts to this issue explore the specific termination liability terms and

conditions of the Key Customer tariff filings at issue in this proceeding.

For purposes of efficiency, staff notes that the arguments, analysis, and recommendations for this issue encompass all of Issue 3A, including the sub-parts. Staff points out, however, that FDN does not separate out the sub-parts in its argument to the extent that BellSouth does. Additionally, FDN discusses this issue in combination with the "contract duration" series of issues, which are addressed in a subsequent section of this recommendation. Staff's analysis begins with an overall review of the arguments presented, followed by a (limited) sub-part analysis, and then our conclusion.

A. FDN Argument (Issues 3A, 3A(i), and 3A(ii))²⁰

FDN witness Gallagher states that it is important to note that FDN does not argue that termination liabilities are not appropriate, but instead objects on the basis that the termination liabilities of the Key Customer tariffs at issue in this proceeding are anticompetitive. (TR 70) The witness believes the points raised previously should factor into the consideration of criteria for evaluating termination liability provisions and contract durations.²¹ The witness claims that "this is not an issue of creating disparate rules for ILECs versus ALECs," contending that "this is an issue of a firm with dominant market power locking up customers in specific geographic areas over an extended duration and what impact that has on competition." (Gallagher TR 70) The FDN witness asserts that the Key Customer tariffs that preceded these (e.g., the pre-2002 tariff offerings contained in EXH 11) likely contained "a fairly small termination liability, if at all," which contrasts with the Key Customer tariffs of the instant proceeding. (Gallagher TR 130) Though he readily acknowledges that FDN contracts also contain termination liabilities, witness Gallagher claims that

²⁰FDN's argument in testimony blended the sub-parts of this issue.

²¹Termination liability and contract duration provisions are addressed separately by staff. This issue and its sub-parts address termination liability provisions. Issue 3B and its sub-parts address contract duration provisions.

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it is simply not reasonable to suggest that the impact in the competitive market place of an ALEC and BellSouth having similar termination liability provisions is the same . . . (TR 70)

Under cross-examination, however, the witness concedes that, according to the data contained in the Commission's 2002 Comp Report, the ALEC sector overall serves over thirty-three percent (33%) of the business market within BellSouth's franchised area. (TR 93; EXH 8, p. 22) Nonetheless, witness Gallagher believes that the information in the Commission's 2002 Comp Report on market share is "dated," and possibly "overstated." (TR 94)

In evaluating this issue, the witness believes the Commission should be mindful of market share, price/cost, and class-wide eligibility. (Gallagher TR 48; FDN BR 19) Witness Gallagher asserts

while the termination liability provisions such as those in BellSouth's Key Customer tariffs (T-020035 and T-020595) may be acceptable for a company without dominant market power, when a company has BellSouth's monopolistic market power, such termination liability provisions represent an unacceptable anticompetitive practice. (TR 49)

Regarding the termination liability provision of the January tariff filing, Tariff Number T-020035, the witness states that the "penalty consists of the aggregate [of all] rebates the customer has received from BellSouth." (Gallagher TR 49) In practice, this means that the dollar amount of a termination liability penalty would increase through the life of a contract; a termination early in a contract would result in a lesser penalty than a termination at a later period. Either way, the witness believes that ALECs are disadvantaged:

. . . [W]hether early or late in the Key Customer contract term, once a customer is lured away from an ALEC back to BellSouth, the customer has a substantial financial

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disincentive from leaving BellSouth again . . .
(Gallagher TR 49-50)

Regarding the termination liability provision of the June tariff filing, Tariff Number T-020595, the witness states that a customer leaving one of these contracts would pay a flat fee per month remaining in the contract. This termination liability structure would mean that the dollar amount of a termination liability penalty would be highest early in the contract term, and would decrease through the life of a contract, according to witness Gallagher. (TR 49)

In speaking to both tariffs, FDN witness Gallagher testifies that a customer that signed a Key Customer contract would receive the specific discount of that tariff, plus BellSouth would waive any applicable line connection charges. If the customer terminated the Key Customer contract early, the customer would be responsible for repaying the waived line connection charges, in addition to the tariff-specific termination liability fee. (Gallagher TR 49) Witness Gallagher states that the level (i.e., the dollar amount) of the termination liability affects whether customers will even consider migrating to an alternative provider. (TR 125) The witness asserts that BellSouth's "termination provisions 'lock up' customers in the coffers of the dominant provider and deter customers from freely migrating even if they find a better provider." (TR 49) FDN contends that BellSouth's termination charges are substantial, and as such, its customers are "migration-deterred" by BellSouth's contract termination language. (FDN BR 20)

In the throes of competition, witness Gallagher believes that ALECs have much more to lose should a customer leave them than if that same customer left BellSouth. He believes that an ALEC that lost a customer to either BellSouth Key Customer program would have unrecovered costs. (TR 48-49) As a result, "ALECs cannot realistically attempt to regain customers lost to a BellSouth Key Customer program," according to the witness, since spending additional monies in this regard would not be a cost-effective endeavor. (Gallagher TR 50) He contends:

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ALEC market entrants are new businesses with significant capital and customer acquisition costs and a few customers over which to spread those costs. These companies [ALECs] cannot and do not compete on the same or equal footing with the century-old monopoly that is BellSouth. (Gallagher TR 65)

"ALECs cannot beat the Key Customer rates and remain viable," he claims. (Gallagher TR 50, 123)

While being cross-examined, witness Gallagher learned of what is referred to as a "split-service" arrangement. (TR 85, 125) Split service is a term used to describe an arrangement where a customer receives telecommunications services from more than one provider. The witness testified that he was unaware that a customer under a Key Customer contract could, in fact, opt for a competitor's offer and move a portion of his lines to FDN, and not face a termination liability for the lines that moved. (Gallagher TR 84-85) The witness was asked to read from two Key Customer tariffs to discern whether the termination liability language mentioned the "split-service" arrangement; the witness asserts that the tariffs did not. (Gallagher TR 126-127) FDN states in its brief that even though "split-service" from BellSouth is permissible, it is not desirable for customers seeking a single source for their telecommunications needs. Furthermore, FDN asserts that "split-service" is "not a cure for the anticompetitive effects" of the termination liability provisions in BellSouth's Key Customer tariffs. (FDN BR 24)

In proposing a resolution to this issue, FDN provides two solutions, though its alternative solution was only presented in its post-hearing brief. FDN's principal solution involves a specific restriction to be applicable for all BellSouth promotions. Witness Gallagher asserts:

To remove the anticompetitive obstacles posed by the sorts of termination liability provisions in BellSouth's Key Customer programs, I recommend that where a customer leaves a BellSouth promotion early to port to a carrier

serving the customer through UNEs, the customer's termination liability should not exceed BellSouth's retail line installation rates. Aside from the competitive concerns, this also recognizes the benefits that BellSouth would receive on the wholesale side from the nonrecurring and recurring charges paid by the new carrier. (Gallagher TR 51)

FDN's alternative solution is a "fair and reasonable compromise" that features a reciprocal offer of equal-in-practice termination liability language between BellSouth and FDN. (FDN BR 23) Should the Commission decide that equal treatment for BellSouth and FDN is warranted, and not approve their principal recommendation, FDN commits that it too will limit its termination liability to retail line installation rates. As a facilities-based competitor, FDN believes that either of its proposed solutions would facilitate its short-term survival. (FDN BR 23)

As noted previously, FDN does not separate out the argument for sub-parts (i) and (ii).

B. BellSouth Argument (Issue 3A and all sub-parts)²²

Staff notes that BellSouth addresses these issues by sub-part, though certain argument encompasses all of the sub-parts.

• **Issue 3A**

BellSouth witness Ruscilli asserts that termination liability terms and conditions are "common" in the local telecommunications market for promotional and non-promotional offerings. (TR 172-173) The witness offers an exhibit (f/k/a JAR-2) that contains examples of ALEC promotional offerings, and certain of these contain termination liability clauses. (EXH 12; 150-161) He contends that

²²BellSouth's argument in testimony was presented by sub-part; staff has grouped this argument accordingly.

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these promotional offerings represent the kind of competitive offers that BellSouth has to compete against on a daily basis in order to do business in Florida.
(Ruscilli TR 167)

The witness states that ALECs offer various termination liabilities that range from full buy-out provisions to calculations that consider the discount received, or months remaining on a contract. (Ruscilli TR 166, 172-173) He describes the language contained in a filed tariff from FDN, which states that a customer's termination liability for cancellation shall be equal to:

- (A) all unpaid non-recurring charges reasonably expended by Company to establish service to a Customer, *plus*;
- (B) any disconnection, early cancellation or termination charges reasonably incurred and paid to third parties by Company on behalf of Customer; *plus*
- (C) all recurring charges specified in the applicable Service Order for the balance of the then current term discounted at the prime rate announced in the Wall Street Journal on the third business day following the date of cancellation;
- (D) minus a reasonable allowance for costs avoided by the Company as a direct result of Customer's cancellation.

(Ruscilli TR 172)

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Regarding this (FDN) example, witness Ruscilli contends that other ALECs in Florida offer "identical or substantially similar" termination liabilities. He asserts:

Most of the [ALEC] promotional offerings contain provisions that obligate customers who terminate the contract early to repay any credits received. Some termination liability provisions also require customers to pay the value of the monthly recurring charges remaining in the term contract. (Ruscilli TR 166)

BellSouth believes that customers in general are accustomed to termination liability clauses and recognize that they are making a tradeoff in accepting the clauses in exchange for lower rates for a commitment period. (TR 173)

FDN believes the Commission must consider, at a minimum, BellSouth's dominant market power and position relative to that of individual ALECs. The Commission should also evaluate the level and availability of the BellSouth discounts, the duration of the discounts, UNE costs, the level and effect of the termination liability, and the impacts on customers, competition and competitors over time.

Overall, BellSouth believes that existing Florida law addressing liquidated damages, along with competitive market forces, are sufficient to ensure that termination liability terms and conditions are not unfair, anticompetitive, or discriminatory. (Ruscilli TR 171) The imposition of any sort of a limitation on BellSouth is "unreasonable," according to witness Ruscilli. (TR 218)

- **Issue 3A(i)**

Sub-part (i) of Issue 3A asks whether the January Key Customer tariff (Tariff Number T-020035) is unfair, anticompetitive, or discriminatory under the criteria, if any, established in the main issue, Issue 3A.

BellSouth witness Casey testifies on the specific termination liability language that applies to the January Key customer tariff. (TR 290) He asserts that paragraph five of the Key Customer enrollment form (or contract) clearly sets forth the termination liability customers would incur if they discontinued their service with BellSouth under this tariff.²³ The witness explains:

If a customer terminates its January Key Customer contract before the contract expires, the contract provides that the customer must pay an amount equal to: the discounts the customer has received under its January Key Customer contract up to the date of termination; and a \$100.00 [fixed] charge. (Casey TR 292)

Witness Casey explains that by repaying the discounts received up to the date of termination, the customer breaking the contract returns to BellSouth the benefits that BellSouth would not have provided to the customer had it not entered into a Key Customer contract. (TR 293) Regarding the \$100.00 fixed charge, he asserts:

. . . [This] charge represents administrative and acquisition costs BellSouth incurs . . . The \$100.00 charge also includes a component for sales incentives that are paid to the different sales organizations . . . , costs which BellSouth would not have incurred had the customer not entered into the contract that it ultimately breached. (Casey TR 293)

The witness believes that at the inception of a contract period, BellSouth cannot ascertain the damages it would suffer were a contract not fulfilled. (Casey TR 290) He explains that a person under contract can add (or delete) discount-eligible services throughout the life of that contract, and the prices, quantities, and margins of the added or deleted services define the actual discount over the life of a contract term. Witness Ruscilli affirms

²³The January and June Key Customer tariffs contain different termination liability language clauses. A blank enrollment contract for each tariff is attached to the direct testimony of BellSouth witness John P. Casey. (See composite Hearing Exhibit 19)

this as well, stating that the amount of a Key Customer tariff discount is derived based on a percentage of the tariffed rates of the Key-eligible services, as opposed to being a fixed amount. (TR 285) He explains that a Key Customer contract does not "freeze the rate" at a particular level. (TR 285) In summary, BellSouth does not believe the termination liability provisions in the January Key Customer offering are unfair, anticompetitive, or discriminatory.

- **Issue 3A(ii)**

Sub-part (ii) of Issue 3A asks whether the June Key Customer tariff (Tariff Number T-020595), or a subsequent tariff filing that extends the expiration date thereof, is unfair, anticompetitive, or discriminatory under the criteria, if any, established in the main issue, Issue 3A. Staff notes, however, that the June BellSouth Key Customer tariff filing (Tariff Number T-020595) expired on December 30, 2002. As represented in the Case Background, BellSouth filed Tariff No. T-021241 on December 16, 2002, to extend the effective date of the June filing (the extension tariff). The extension tariff became effective on December 31, 2002, and expires on July 1, 2003.

As noted in the previous sub-part issue, the January and June Key Customer tariff filings contain different termination liability language. Witness Casey states the older termination liability language (i.e., the January tariff) was "backward looking" while the June structure is "forward-looking." (TR 300) The witness asserts that the change was implemented so that BellSouth could "address the margin BellSouth expected to realize over the remaining term of the contract." (TR 294) In practice, the January tariff filing reimbursed BellSouth for the benefits extended up to the point of breach, but made no accommodation for a "lost" margin for the period of time remaining on the contract, according to the witness. (TR 294-295) Witness Casey explains that the June termination liability language includes this "lost" margin concept:

If a customer terminates its June Key Customer contract prior to the expiration date, the contract provides that

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the customer must pay an amount equal to all rewards it has received as a result of any line connection charges that were waived pursuant to the contract. In addition, the customer pays a designated amount for each month remaining on the term of the contract.

Customers [with] billing between \$75.00 and \$149.99 [per month] at the time they enter into a June Key Customer contract are charged \$25.00 for each month remaining in the term of their contract if they terminate the contract early.

Customers [with] billing between \$150.00 and \$3,000.00 [per month] at the time they enter into a June Key Customer contract are charged \$40.00 for each month remaining in the term of their contract if they terminate the contract early. (Casey TR 294-295)

The witness explains that BellSouth developed the multipliers (the \$25.00 or \$40.00 per-month amounts) to represent a "conservative estimate of the margin that BellSouth would have received had the customer honored the contract it signed." (Casey TR 295) BellSouth analyzed the average margins that would be associated with the minimum quantity of Flat Rate Business Lines ("1FBs") for eligible customers.²⁴ The "1FB" was viewed as a common denominator for these small business customers. In doing the calculations, BellSouth determined that \$150.00 per-month in total billed revenue (TBR) became a dividing point, and the two tiers were established: the first tier for TBR between \$75.00 and \$149.99, and the second tier for TBR of \$150.00 up to \$3,000.00. (Casey TR 296-297) He further explains:

BellSouth . . . calculated how many "1FBs" a customer would have to purchase at the statewide average price to meet the \$75.00 . . . [or] \$150.00 per month spending

²⁴The June Key Customer tariff filing was offered to business customers with monthly total billed revenue (TBR) between \$75.00 and \$3,000.00.

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levels . . . , and the \$25.00 and \$40.00 per month termination charges . . . represent the statewide average margin associated with those numbers of "1FBs." (Casey TR 296-297)

In addition, the requirement that the customer reimburse the line connection charges waived at signing puts BellSouth in a position it would have otherwise been in had no contract been signed, according to witness Casey. (TR 295) The witness believes this termination liability structure is reasonable because at the inception of a contract, BellSouth cannot predict (1) the sum of benefits the customer will receive over the life of the contract; and (2) the damages it would incur if the contract is ultimately breached. (Casey TR 300)

BellSouth believes the termination liability provisions in the June Key Customer offering are neither unfair, anticompetitive, or discriminatory. (BellSouth BR 26) The June Key Customer termination liability language is appropriate because foregone profit from a breach is not readily ascertainable at the time such a contract is executed.

C. Analysis (Issue 3A and all sub-parts)

The broad topic under review in this issue is termination liabilities; the sub-parts to this issue explore the specific termination liability terms and conditions of the Key Customer tariff filings at issue in this proceeding. In all of the issues, the Commission is tasked with deciding whether any criteria should be established to determine whether the termination liability terms and conditions of a BellSouth promotional tariff offering are unfair, anticompetitive, or discriminatory. Because the words "unfair, anticompetitive, or discriminatory" are rooted in the Florida Statutes, the true evaluation of the issues herein must focus on compliance with the Florida Statutes.

FDN approaches these issues as an extension of its arguments about market share and the alleged anticompetitive intent of a

dominant provider. (Gallagher TR 70) In its argument for Issue 2, FDN broached the topics of market share, price/cost, and class-wide eligibility, and witness Gallagher believes these considerations should be given some weight in this issue as well. (Gallagher TR 48) Although FDN presents an alternative solution in its brief, staff's analysis focuses on FDN's principal recommendation. (FDN BR 23)

FDN witness Gallagher infers that termination liabilities have an impact in the marketplace, and discounts the notion that BellSouth and ALECs should have the same termination liabilities in the marketplace. (TR 70) He does not specifically object to the termination liability provisions of BellSouth's Key Customer tariffs at issue in this proceeding (T-020035, T-020595, and T-021252), yet FDN specifically recommends that the Commission impose a restriction on BellSouth to limit any applicable termination liability such that the dollar amount would not exceed BellSouth's retail line installation rates. (Gallagher TR 51)

BellSouth takes the position that the respective termination liability clauses in its Key Customer tariff filings are in compliance with the applicable Florida Statutes. BellSouth devotes the bulk of its argument explaining that:

- 1) Termination liability clauses are common in all sorts of contracts, and are appropriate for its promotional tariffs;
- 2) Competitors offer contracts with disparate termination liability clauses - some even require "full buy-outs." BellSouth's Key Customer termination liability clauses are far less onerous than some ALEC termination liability clauses.
- 3) BellSouth Key Customer contracts include the applicable termination liability language; customers are aware of, and accept this as a

trade-off for receiving the applicable discounts.

- 4) The termination liability clauses in its Key Customer tariff offerings are lawful in every respect.

- 5) The Commission should not consider any restrictions, limitations, or additional criteria for BellSouth with respect to its termination liability clauses. Such considerations are not warranted, or reasonable.

As such, BellSouth believes that the Commission need not develop any additional criteria with respect to termination liability clauses.

Staff believes the discussion regarding "split-service" is very relevant to the issues under consideration herein. Under cross-examination, witness Gallagher testified that he was unaware that a BellSouth customer under a Key Customer contract could, in fact, move a portion of his lines to a competitor, and not face a termination liability for the lines that moved. (Gallagher TR 84-85) Staff's cross-examination of BellSouth witness Casey confirmed this from BellSouth's perspective. (TR 302-303) FDN witness Gallagher read aloud the termination liability clauses from the January and June Key Customer contracts to discern whether anything therein indicated that "no termination liability applies for split-service," and the witness found no such declaration. (Gallagher TR 126-127)

Under cross-examination from staff, witness Casey was asked a series of questions regarding when BellSouth would apply its termination liability. Specifically, the witness was asked if a breach had occurred if a customer's TBR fell below the minimum threshold for participation in the June Key Customer promotion. (TR 302-303) Staff framed the questions to describe a "split-service" scenario. Using a hypothetical five (5) line customer that signed a Key Customer contract with BellSouth, the witness was asked what would happen if that customer accepted an offer from a competitor

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for four (4) of those lines while still under the term of its Key Customer contract.²⁵ In summary fashion, the answers to those questions revealed the following:

- The Key Customer contract only obligates the customer to maintain *some level of local service* with BellSouth for the agreed-upon term. The Key Customer contract does not obligate the customer to maintain *all local service* with BellSouth for the agreed-upon term;
- The Key Customer discounts would only apply to TBR that equaled or surpassed the minimum threshold. No Key Customer discounts would be applied if TBR is below the minimum threshold;
- A breach of contract would occur if the customer left BellSouth altogether. Such a breach would trigger the termination liability for a Key Customer contract. However, during the term of a Key Customer contract, no breach will occur as long as some level of local service is maintained with BellSouth.

(Casey TR 301-303)

Staff believes these revelations about the applicability of termination liabilities are significant in that BellSouth's Key Customer tariffs and enrollment forms at issue in this proceeding do not disclose the information about "split-service." To demonstrate this, FDN's witness testifies about an actual sales call in which FDN had to "walk away" from a customer in Miami that wanted service from FDN. FDN witness Gallagher states that "there was no way we could get the customer out of that particular [BellSouth] deal." (TR 74) Since the witness does not offer any specific information, staff could not determine whether the customer was under a January, June, or some other offer from BellSouth.

²⁵Staff made the assumption that a five (5) line customer would exceed the minimum threshold TBR for participation in the Key Customer promotion, but that the TBR from a single line customer would not.

In staff's view, "split-service" essentially undermines FDN's argument since customers are not truly "locked up" as FDN alleges. Staff believes FDN's claims of anti-competitive intent are addressed since a BellSouth Key customer is not impeded from entertaining a competitive offer - though the customer must accept that a "split-service" arrangement will be necessary for the remainder of the term commitment with BellSouth. Staff believes a "split-service" arrangement could have been workable in the Miami example described above, if FDN would have had the knowledge that was disclosed by BellSouth witness Casey in the above-referenced cross-examination. Staff is less concerned about whether or not the Miami customer was under a Key Customer contract or not; the more significant concern for staff is whether competitors and customers are aware of the specific applicability of BellSouth's termination liability clauses. Staff can only speculate on how many other potential deals were scratched based on this non-disclosure from BellSouth; the record contains no other information in this regard.

Staff believes the scope of this issue (which covers all of the Key Customer tariffs addressed in this proceeding) incorporates "split-service." Based on the tariff and enrollment contract language from all of the Key Customer tariffs at issue in this proceeding, staff - and apparently FDN - had incorrectly assumed that termination liabilities would apply if any local service lines under a Key Customer contract were ported out (i.e., served by a competitor). BellSouth's witness Casey in no way limits his assertions on "split-service" to one particular tariff or the other; staff believes if that was the case, the witness would have clearly made that distinction, and he did not. Moreover, such a conclusion follows from witness Casey's testimony that discount-eligible services may be added or deleted over the life of a January Key Customer contract, and that BellSouth cannot predict the total benefits the customer will receive over the life of a June (or subsequent) Key Customer contract. (TR 285, 300) Staff believes the "split-service" frame of reference does, therefore, apply to all of the Key Customer tariffs at issue in this proceeding. This option significantly mitigates the practical effect of a termination liability, regardless of how structured.

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D. Conclusion (Issue 3A and all sub-parts)

Staff does not believe that any particular aspect of BellSouth's Key Customer termination liability clauses is contrary to the Florida Statutes. With "split-service," consumers can evaluate competitive offers for a portion of their service if they so choose, and the impact of any termination liability charge becomes a moot issue. Staff does not believe any specific criteria should be established outside of the existing guidance from the Florida Statutes to determine whether the termination liability terms and conditions of a BellSouth promotional tariff are unfair, anticompetitive, or discriminatory.

Staff does recommend, however, that the following actions should be implemented following the Commission's decision on this matter:

- BellSouth should revise the applicable portion of its current Key Customer tariff, Tariff No. T-021241, to clearly disclose that the termination liability does not apply in a "split-service" scenario. In addition, the corresponding revision should be made to the standard contract used to enroll subscribers.

- All future BellSouth promotional tariffs that are based on total billed revenue should clearly disclose that the termination liability does not apply in a "split-service" scenario.

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ISSUE 3B: What criteria, if any, should be established to determine whether the duration (term of individual contracts, length and succession of promotions) of a BellSouth promotional tariff offering is unfair, anticompetitive, or discriminatory?

(i): Is the BellSouth Key Customer tariff filing (Tariff Number T-020035) unfair, anticompetitive, or discriminatory under the criteria, if any, established pursuant to this issue?

(ii): Is the BellSouth Key Customer tariff filing (Tariff Number T-020595 or a subsequent tariff filing that extends the expiration date thereof) unfair, anticompetitive, or discriminatory under the criteria, if any, established pursuant to this issue?

RECOMMENDATIONS:

3B: Staff recommends that no criteria should be established, other than that included in Section 364.051(5)(a)(2) Florida Statutes, to determine whether the duration (term of individual contracts, length and succession of promotions) of a BellSouth promotional tariff offering is unfair, anti-competitive, or discriminatory. (CASEY)

3B(i) & (ii): No. Based on Section 364.051(5)(a)(2), Florida Statutes, staff recommends that the BellSouth Key Customer tariff filings are not unfair, anti-competitive, or discriminatory regarding the term, length and succession of the promotional offerings. (CASEY)

POSITION OF THE PARTIES

FDN:

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Issue 3B: The Commission must consider, at a minimum, BellSouth's dominant market power and position relative to that of individual ALECs, the level and availability of the BellSouth discounts, the duration of the discounts, UNE costs, the level and effect of the termination liability, and the impacts on customers, competition and competitors over time.

(i)&(ii): Yes. The Commission must limit the duration of promotional tariffs, eligibility and contracts to protect against reversing competitive trends and to ameliorate the gap between customers discriminated for and against. FDN recommends a maximum of 120-day tariff duration [sign-up window], and a maximum of one-year discount eligibility, with at least a one year off discount period per customer.

BELLSOUTH:

Issue 3B: No new criteria should be established. The duration of a promotion depends on the offering and the market.

(i)&(ii): No. The offering is available for resale, and is a competitive response to other offerings.

STAFF ANALYSIS: Since the parties' arguments and recommendations are identical for issues 3B(i) and 3B(ii), staff's analyses will first address Issue 3B, then 3B(i) and 3B(ii) together for administrative efficiency, followed by a conclusion paragraph.

Issue 3B examines the question as to what criteria, if any, should be established to determine whether the duration of a BellSouth promotional tariff offering is unfair, anti-competitive, or discriminatory. Issues 3B(i) and 3B(ii) explore whether the Key customer offering is unfair, anti-competitive, or discriminatory regarding the term, length and succession of the promotional offerings under the criteria, if any, established in Issue 3B.

- Issue 3B

- A. FDN Argument (Issue 3B)

FDN Witness Gallagher begins this issue by pointing out BellSouth's market share in Florida, stating that BellSouth still enjoys monopoly status in its incumbent territory. (TR 37) FDN believes that BellSouth's improper use of market power to regain retail market share has caused facilities-based competition in Florida to stall before sustainability is attained and has harmed the customers BellSouth has discriminated against. (FDN BR 26) FDN believes that with the Key Customer tariffs in place for six months at a time, and with programs being rolled over again and again, it will not be long before facilities-based competition has slow or no growth. (FDN BR 26) Witness Gallagher states:

As a general proposition, the Commission should never permit a dominant market provider like BellSouth to use its market power to dictate market products or prices to the detriment of competitors and consumers, particularly when competition is still in a vulnerable infancy, as is the case here in Florida. (TR 37)

- B. BellSouth Argument (Issue 3B)

BellSouth witness Ruscilli believes that it is not necessary to establish any new criteria to determine whether the duration of BellSouth's promotional offerings is unfair, anti-competitive, or discriminatory. He believes that there is not a "one-size fits all" answer to this issue, and that the timeframe for a promotional offering depends on the offering itself, and the market to which it is proffered. (TR 179) Witness Ruscilli continues by stating:

In a competitive market, which clearly exists in Florida, the duration of promotions is dictated by market forces and by customers - not by ALECs. (TR 217-218)

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BellSouth believes that its testimony and exhibits demonstrate the amount of competition in Florida, and that the Commission should refrain from adopting any unwarranted restrictions on the duration of promotions. (BellSouth BR 27) It opines that the competitive marketplace should be the place that dictates the optimum promotion duration. (BellSouth BR 27) BellSouth also believes that because BellSouth has the statutory authority to meet competitive offers, the Commission should not limit the length of time that BellSouth makes competitive offers available because any such limitation would harm competition. (BellSouth BR 27)

C. Analysis (Issue 3B)

Section 364.051(5)(a)(2), Florida Statutes, provides, in part, that:

. . . Nothing contained in this section shall prevent the local exchange telecommunications company from meeting offerings by any competitive provider of the same, or functionally equivalent, nonbasic services in a specific geographic market or to a specific customer by deaveraging the price of any nonbasic service, packaging nonbasic services together or with basic services, using volume discounts and term discounts, and offering individual contracts. However, the local exchange telecommunications company shall not engage in any anti-competitive act or practice, nor unreasonably discriminate among similarly situated customers.

The above section of the Florida Statutes allows BellSouth to offer volume and term discounts through individual contracts. However, it does not place any limits on the duration of those contracts. Pursuant to this section, the local exchange company is allowed to meet competitive offerings as long as it doesn't engage in any anti-competitive act or practice, or unreasonably discriminate among similarly situated customers.

Staff believes that no additional criteria should be established for determining whether the duration of a BellSouth promotional tariff offering is unfair, anti-competitive, or discriminatory. Requiring a fixed length of time for a Key Customer offering would limit BellSouth's marketing and ability to compete. Staff opines that BellSouth needs the flexibility to respond to competitive offerings in the marketplace. If competitors are offering two - three - four - or five - year contracts, BellSouth should be allowed the flexibility to meet those offerings as provided in the above statute.

D. Conclusion (Issue 3B)

Staff believes that no additional criteria, other than that included in Section 364.051(5)(a)(2), Florida Statutes, should be established to determine whether the duration of a BellSouth promotional tariff offering is unfair, anti-competitive, or discriminatory.

• Issues 3B(i) & 3B(ii)

A. FDN Argument (Issues 3B(i) & 3B(ii))

FDN believes the Commission should impose three limitations on the duration of a BellSouth promotional tariff: First, the tariff offering to customers should be no longer than 120 days [sign-up window]; second, the length of the contract should be no longer than one year; and third, once the contract has expired, there should be a waiting period of one year before the customer can participate in another BellSouth promotional tariff offering. (TR 120)

FDN also believes that the Commission should issue an order or rule whereby until such time as BellSouth no longer has market power and ALECs have achieved meaningful market share in BellSouth territory, BellSouth should be barred from offering direct or indirect discounts of more than 10% off total billed basic and nonbasic telecommunications services, including hunting and all

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features. (TR 15) Witness Gallagher expounds on his discount limitation recommendation to include durations of contracts by stating:

My general view of program or contract duration issues is similar in that if a BellSouth promotion meets the market-focused recommendation I made above, for instance, no more than a 10% discount, the program discounts could be available until BellSouth is no longer dominant. However, BellSouth's practice of rolling over recent promotional programs and the prospect of its rolling over related customer contracts compounds the detrimental effects on competition that the promotions cause in the first place. (TR 17)

Witness Gallagher asserts that BellSouth's market power cripples smaller competitors who are just starting out in the business through unreasonable discounts. He believes that the damage is not just that the competitor loses a customer today, but that the cumulative effect of those losses results in future harm because BellSouth is locking up customers for the long term, during the infancy of the competitors, and deterring those customers from migrating in the future. (TR 66) The witness goes on to state:

If the Commission is not going to outright stop BellSouth from offering promotional prices in limited geographic areas, the Commission surely must recognize the potential for these BellSouth promotions to stifle competition over time and the need for the Commission to reserve the power or have mechanisms in place to "put on the brakes" and stop negative competitive impacts before it is too late to reverse those impacts. This is precisely why the Commission must place a meaningful limit on the duration of any tariffed promotions and on any agreement or eligibility terms, as well as addressing termination liability. (TR 67)

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When questioned as to whether FDN has contracts with its business customers, witness Gallagher replied:

It is not valid to compare the contract terms of an ALEC to the contract terms of BellSouth for purposes of this case. BellSouth is the dominant-monopoly provider in its legacy ILEC territory in Florida. BellSouth has 90% plus market share, and it is BellSouth's conduct that is the issue in this case.

FDN has agreements with customers ranging from month-to-month arrangements to 3-year terms. Generally, FDN's standard incentive for the customer to accept a longer term is a larger discount. FDN has one rate for month-to-month and one-year agreements and increasing discounts for longer terms. Basically, there is an additional 2% discount for a two-year term and an additional 5% discount for a three-year term. (EXH 5, pp. 10-11)

Under cross-examination by BellSouth, witness Gallagher stated that customers can receive a 30% discount off BellSouth's prices if they sign a three-year contract with FDN, but most FDN customers don't sign a contract with a three-year term. (TR 77)

B. BellSouth Argument (Issues 3B(i) & 3B(ii))

BellSouth witness Taylor believes that BellSouth needs to be free to meet competitive offerings, and in order to accomplish this, it must have the same flexibility as its competitors to choose the frequency and duration of its promotions. (TR 506) He opines that the more flexibility BellSouth has to propose promotional tariffs, the more vigorous competition will be in Florida and the better off Florida consumers will be. (TR 505)

BellSouth witness Pitofsky believes that FDN's contention that BellSouth's 18-month and 36-month discount offers are comparable to exclusive dealing arrangements which inappropriately fence out

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BellSouth's competitors for the duration of the contract, "are exceptionally wide of the mark." He explains that the Key Customer discounts are not exclusive since the customer is free to contract with BellSouth competitors as long as the customer maintains some service with BellSouth, even if he is not meeting the minimum revenue requirement for the discount. (TR 415) Witness Pitofsky continues by stating:

. . . the Key Customer programs at issue here do not require that a customer deal only with BellSouth. But even if they did, the duration of those programs, eighteen months and thirty-six months, are not so long as to inhibit competition. With respect to duration, there is no lack of authority that exclusive dealing contracts terminable in less than a year are presumptively lawful. Contracts of longer length might be reviewed under a rule of reason but are not likely to be successfully challenged, especially in circumstances like those that pertain here - where competitors are offering discount programs of even longer duration, up to five years in some instances.

BellSouth witness Taylor believes that long-term contracts can be beneficial to both contracting parties and consumers in general. (TR 501) He points out that long-term contracts serve several important functions:

- 1) They can reduce the business risk to BellSouth so that an otherwise unprofitable sunk investment in facilities or in a customer relationship might become profitable.
- 2) They can reduce the business risk of BellSouth's customers, so that investment in facilities or relationships that the customer may make in order to use BellSouth's services might become profitable.
- 3) The general public benefits from such contracts because they: (i) promote continuity between the contracting parties, (ii) reduce

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transaction costs, and (iii) provide the parties an opportunity to reduce risk and manage their budgets more effectively.

4) The ability to offer similar contracts as competitors permits BellSouth to obtain some retail contribution from those customers who otherwise would choose a competitor's service and supply no contribution to BellSouth. (TR 501-502)

Witness Ruscilli believes that the Commission should not place any restrictions on BellSouth's ability to offer successive promotional offerings. (TR 179) He states:

When the term of the promotional contract expires, the customer is free to evaluate all of the competitive alternatives that are available at that time and decide which one of those competitive alternatives to accept. If the customer believes that the successive promotion is better than any other offering, then the customer should not be deprived of the ability to sign a new contract for a successive promotion. Restricting the introduction of successive promotional offerings would deprive customers of an additional choice for lower prices. Furthermore, restricting successive promotional offerings would hinder BellSouth's ability to compete with the competitive offerings being introduced by ALECs. (TR 179)

BellSouth witness Taylor believes it is not unusual or anti-competitive to run successive promotional campaigns in unregulated or competitive markets, even if those campaigns run consecutively and produce, in effect, one long and continuous campaign. (TR 473) Witness Taylor states that:

If BellSouth chooses to reduce prices for a service over a long period in order to run successive promotional campaigns, it is a market calculation that BellSouth must live by. As long as its prices are not anti-competitive and/or discriminatory in the process, BellSouth should not be denied the opportunity to make that market calculation.

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Moreover, consumers stand to benefit from the lower price of the promotional offering. (TR 473)

He also believes that if the Commission imposes a waiting or cooling-off period after the expiration of a promotional tariff as FDN wants, customers would be denied the benefit of the lower promotional prices for the duration of those periods, and competitors would be less compelled to compete on the basis of their efficiency and powers of innovation relative to those of BellSouth. (TR 474) He further states:

. . . mandatory cooling-off periods imposed asymmetrically on BellSouth could leave its competitors with significant competitive advantages. This would be especially so when the length and timing of the cooling-off periods are known, or can be anticipated, in advance. Regulatory restraints on BellSouth in the absence of evidence of anti-competitive or discriminatory behavior could only confer artificial competitive advantages upon BellSouth's unregulated rivals, reducing social welfare in the process. (TR 474)

BellSouth witness Ruscilli believes that while the Commission could, under certain circumstances, impose different regulatory oversight on an ILEC's promotional offerings than it imposes on ALEC's promotional offerings, it cannot do so in an arbitrary, capricious, or discriminatory manner. (TR 170) BellSouth witness Ruscilli refers to the "Fresh Look" proceeding (FPSC Docket No. 980253-TX), which was a rulemaking proceeding in which the Commission issued a rule that basically allowed a customer under a term agreement with an ILEC to leave the contract to go to an ALEC without paying termination charges, hence the name "Fresh Look." The rule only applied to ILECs, not ALECs. (TR 170) Witness Ruscilli further explained in his testimony:

The rule was challenged, and the Division of Administrative Hearings ("DOAHs") issued a final order on July 13, 2000 that overturned the Commission's previous

ruling. Paragraph 114 of the DOAH's order states, "[t]here was no demonstration that the ILECs' long-term contracts present any greater, or even different, obstacles to competing carriers trying to win a customer subject to such an agreement, than would an ALEC's long-term contract. Therefore, the fact that the rules capture contracts of ILECs, and not contracts of ALECs, renders the rules discriminatory, arbitrary, and capricious." (TR 170-171)

Paragraph 114 of the DOAH Order concludes by stating, "Indeed, the discriminatory component may, contrary to the Commission's intended goal, produce less, rather than more, competition." Witness Ruscilli believes the same is true in this instant proceeding - creating a rule or establishing criteria that place restrictions only on an ILEC's promotions, and not on an ALEC's promotions, will only impede competition in Florida. (TR 171)

C. Analysis (Issues 3B(i) & 3B(ii))

As mentioned above, FDN believes that the Commission should impose three limitations on the duration of a BellSouth promotional tariff. The following is staff's analysis of each of the proposed limitations.

1) The tariff offering to customers should be no longer than 120 days.

FDN witness Gallagher believes that the sign-up window for the discounts should be no greater than 120 days, contending that this would mitigate anti-competitive impacts of the promotional offerings. (TR 51,120)

BellSouth witness Taylor believes that BellSouth needs to be free to meet competitive offerings, and in order to accomplish this, it must have the same flexibility as competitors to choose the frequency and duration of its promotions. (TR 506) He believes that

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the more flexibility BellSouth has to propose promotional tariffs, the more vigorous competition will be in Florida and the better off Florida consumers will be. (TR 505)

BellSouth is presently using a six-month sign-up window to offer its Key Customer programs. FDN would like to see that window reduced to 120 days.

Staff agrees with BellSouth witness Taylor that BellSouth should have the same flexibility as competitors do to choose the frequency of its promotions. Staff believes that limiting BellSouth to offering its promotional tariffs for 120 days would not only limit customer choice, but restrict BellSouth's right to meet competitive offerings outlined in Section 364.051, Florida Statutes. Therefore, staff is not recommending a restriction of 120 days for BellSouth to offer these promotions to consumers.

2) The length of the contract should be no longer than one year.

FDN recommends that BellSouth be limited to a one year contract duration for its promotions. (TR 67) Witness Gallagher explains his reasoning by stating:

Aside from serving as a means for the Commission to cushion any problems that develop in the competitive marketplace as a result of the promotions, this would also restore some measure of equity to the situation of so many customers not receiving promotional prices because BellSouth has not offered across-the-board decreases. (TR 67-68)

BellSouth witness Ruscilli believes that the duration of promotions should be dictated by market forces and by customers - not by ALECs. (TR 217) BellSouth witness Pitofsky believes there is no reason to regulate the duration of BellSouth's promotions in response to competition. (TR 416) He goes on to state:

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. . . the duration of those programs, eighteen months and thirty-six months, are not so long as to inhibit competition. With respect to duration, there is no lack of authority that exclusive dealing contracts terminable in less than a year are presumptively lawful. Contracts of longer length might be reviewed under a rule of reason but are not likely to be successfully challenged, especially in circumstances like those that pertain here - where competitors are offering discount programs of even longer duration, up to five years in some instances. (TR 416-417)

Staff believes a Florida Supreme Court decision (In the matter of The Florida Bar, 349 So. 2d 630 Fla. 1977) regarding the right to contract and the concept of an impairment of contract cited in DOAH's final Order (Case Nos. 99-5368RP, and 99-5369RP) in the "Fresh Look" case is also pertinent to this docket. The decision states, in part:

The right to make contracts of any kind, so long as no fraud or deception is practiced and the contracts are legal in all respects is an element of civil liberty possessed by all persons who are sui juris. . . . It is both a liberty and property right and is within the protection of the guaranties against the taking of liberty or property without due process of law. . . . It follows, therefore, that neither the federal nor state governments may impose any arbitrary or unreasonable restraint on the freedom of contract. . . . That freedom, however, is not an absolute, but a qualified right and is therefore, subject to a reasonable restraint in the interest of the public welfare. . . . Freedom of contract is the federal rule; restraint is the exception, and when it is exercised to place limitation upon the right to contract, the power, when exercised, must not be arbitrary or unreasonable, and it can be justified only by exceptional circumstances. (Internal citations omitted). (DOAH 99-5368RP ¶85-88)

Staff believes that the Commission should not impose restrictions on the duration of BellSouth promotional contracts.

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The record shows that both BellSouth and ALECs enter into long-term promotional contracts with clients. Staff agrees with BellSouth witness Taylor that long-term contracts, by themselves, do not reduce the competitive rivalry in a market; they just add an option that many customers value, volume and term commitments in exchange for lower prices. (TR 504) BellSouth witness Ruscilli puts it simply. The longer the term of the contract, the greater discount you receive. (TR 282) Staff believes that placing a maximum one-year term on the duration of BellSouth promotional contracts will reduce consumer choice and may produce less, rather than more, competition in the State of Florida.

3) Once the contract has expired, there should be a waiting period of one year before the customer can participate in another BellSouth tariff offering.

FDN witness Gallagher believes that once a BellSouth promotional contract expires, there should be a waiting period of one year before BellSouth could offer another promotional contract to that customer. He believes that this would cushion any problems that develop in the competitive marketplace as a result of the promotions, and restore some measure of equity. (TR 67-68)

BellSouth witness Ruscilli believes that BellSouth should not be restricted from offering successive promotional offerings. He believes that when the term of the promotional contract expires, the customer is free to evaluate all of the competitive alternatives that are available at that time and decide which one of those competitive alternatives to accept, and that restricting successive promotional offerings would hinder BellSouth's ability to compete with the competitive offerings being introduced by ALECs. (TR 179)

BellSouth witness Taylor believes that it is not unusual or anti-competitive to run successive promotional campaigns which may produce one long and continuous promotion. Witness Taylor believes that if cooling-off periods are mandated, customers would be denied the benefit of competition, and this could leave BellSouth's competitors with significant competitive advantages. (TR 473-474)

Staff agrees with BellSouth witness Ruscilli that the customer should be free to evaluate all of the competitive alternatives that are available at the time a promotional contract expires, and should have the opportunity to decide which one of those competitive alternatives meets his needs. Staff believes that imposing a waiting period of one year before the customer can participate in another BellSouth tariff offering will reduce consumer choice and may produce less, rather than more, competition in the State of Florida, and would impede BellSouth's ability to contract without identifying any pervasive social policy basis for the impediment.

The January and June Key customer offerings have only minor changes regarding the duration of the promotions. The January Key Customer offering includes the option of an 18- or 36-month term length, and the June Key Customer offering includes the option of a 24- or 36-month term length. (Ruscilli TR 180) Staff believes that the differences between the January and June Key customer offerings are minor and do not affect its opinion as to whether these tariffs are unfair, anti-competitive, or discriminatory regarding duration of contracts.

Based on the above analysis, staff believes that the January and June BellSouth Key Customer tariff filings are not unfair, anti-competitive, or discriminatory regarding the term, length, and succession of the promotional offering. Staff believes that these offerings are responses to the competition being experienced in the State of Florida.

D. Conclusion (Issues 3B(i) & 3B(ii))

Based on Section 364.051(5)(a)(2), Florida Statutes, and the above analysis, staff recommends that the January and June BellSouth Key Customer tariff filings are not unfair, anti-competitive, or discriminatory regarding the term, length and succession of the promotional offering.

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ISSUE 3C: What criteria, if any, should be established to determine whether the billing conditions or restrictions of a BellSouth promotional tariff offering are unfair, anticompetitive, or discriminatory?

(i): Is the BellSouth Key Customer tariff filing (Tariff Number T-020035) unfair, anticompetitive, or discriminatory under the criteria, if any, established pursuant to this issue?

(ii): Is the BellSouth Key Customer tariff filing (Tariff Number T-020595 or a subsequent tariff filing that extends the expiration date thereof) unfair, anticompetitive, or discriminatory under the criteria, if any, established pursuant to this issue?

RECOMMENDATIONS:

3C: Staff does not believe any specific criteria should be established outside of the existing guidance from the Florida Statutes to determine whether the billing conditions or restrictions of a BellSouth promotional tariff offering are unfair, anticompetitive, or discriminatory.

3C(i) & 3C(ii): No. (BARRETT)

POSITIONS OF THE PARTIES

FDN:

Issue 3C: The Commission must consider, at a minimum, BellSouth's dominant market power and position relative to that of individual ALECs, the level and availability of the BellSouth discounts, the duration of the discounts, UNE costs, the level and effect of the

termination liability, and the impacts on customers, competition and competitors over time.

(i) & (ii): Yes. Any BellSouth discounts should be offered to all BellSouth customers. At a minimum, BellSouth customers discriminated against must not be harmed by the discrimination. The record in this case establishes that customers discriminated against have been harmed.

BELLSOUTH:

Issue 3C: No new criteria should be established. BellSouth has offered various promotions for years, and these promotions have not inhibited the ALEC's ability to compete for and win approximately one-third of the small business access lines that are being served in BellSouth's territory.

(i) & (ii): No.

STAFF ANALYSIS: This issue evaluates whether specific criteria should be established to determine whether the billing conditions or restrictions of a BellSouth promotional tariff offering are unfair, anticompetitive, or discriminatory. The sub-parts to this issue explore the specific billing conditions of the Key Customer tariff filings at issue in this proceeding. Staff points out that two acronyms are used throughout this issue, Customized Large User Bill ("CLUB") and secondary location address ("SLA"); these acronyms are explained in the argument proffered by BellSouth.

For the purposes of efficiency, staff notes that the arguments, analysis, and recommendations presented for this issue encompass all of Issue 3C, including the sub-parts. The analysis herein begins with an overall review of the arguments presented, followed by a (limited) sub-part analysis, and then a conclusion.

A. FDN Argument (Issue 3C and all sub-parts)

FDN witness Gallagher offers only a very limited amount of testimony about billing conditions, though aspects of his argument for Issue 3D and its sub-parts cover this topic. Overall, the tone of his limited testimony is that the statute provides specific guidance for BellSouth about geographic targeting, and billing practices should not contravene this. The witness states

the Commission should not permit the BellSouth [Key Customer] discount to apply to different locations of the same business entity regardless of geography (such as areas outside "Hot Wire Center" locations) unless competitors can also make the same multi-location offer.
(Gallagher TR 53)

In his opinion, this "runs afoul of . . . [the] basic principles of fairness." (TR 53)

As he did in his argument for Issue 2 and elsewhere, the witness believes BellSouth should offer its Key Customer tariff discounts and free hunting to every customer in the business class in Florida, not just to those customers who are in "Hot Wire Centers." (TR 46, 48) The discrimination issue is largely the result of the geographic targeting, according to witness Gallagher. He believes that the possibility of a billing condition creating a disparity of some kind would be eliminated if BellSouth's discounts were not selectively targeted. (Gallagher TR 46, 48) In its brief, FDN states that BellSouth "sidesteps the statute" with its "customer friendly" billing provisions that may benefit a subscriber while not being offered in response to a specific competitive offering. (FDN BR 31-32)

B. BellSouth Argument (Issue 3C and all sub-parts)

BellSouth witness Ruscilli asserts that the billing-related features of the Key Customer tariffs are not unfair,

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anticompetitive, or discriminatory, but rather, are "customer friendly" provisions. (TR 183) Citing staff's August 8, 2002 Memorandum,²⁶ the witness asserts, "the Commission's Staff raised concerns with the Customized Large User Bill ('CLUB'), secondary location address ('SLA') and 'move' provisions" (Ruscilli TR 181-182) The "CLUB" and the "SLA" provisions are included in all of the Key Customer tariffs at issue in this proceeding, while the "move" provision is included in the June and extension filings only. (See EXH 20²⁷) BellSouth witness Garcia contends that these provisions (CLUB, SLA, and the "move" provisions) were included in the June Key Customer offering as a result of requests from and discussions with BellSouth customers. (TR 327)

BellSouth witness Ruscilli briefly describes the three billing concerns staff raised:

CLUB Billing

Witness Ruscilli explains that CLUB billing is an optional service whereby customers with multiple locations can receive one bill for all locations. (TR 278) The witness asserts:

Specific language is included [in the tariff] . . . to allow subscribers with multi-locations that have a CLUB arrangement to have all locations participate in the promotion as long as one location is in an eligible ["hot"] wire center and one location meets the revenue requirement . . .

²⁶On August 8, 2002 staff filed a recommendation in Docket No. 020578-TP that evaluated the June Key Customer tariff. Among other things, that recommendation detailed concerns about billing conditions. The resultant Order, Order No. PSC-02-1237-FOF-TP, issued on September 9, 2002, consolidated Docket No. 020578-TP with Docket No. 020119-TP. A subsequent consolidation of Docket No. 021252-TP applied to the Key Customer extension tariff as well, (Tariff No. T-021241). The consolidations of the above-mentioned dockets promoted administrative efficiency.

²⁷The billing conditions and restrictions are in the respective tariffs. Copies of the January and June BellSouth tariff filings are a part of composite Hearing Exhibit 20. The copies were attached to the direct testimony of BellSouth witness Carlos Garcia (f/k/a CG-1 and CG-2).

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Since BellSouth's billing systems are not able to treat the various accounts on that CLUB bill differently, all of the accounts either get the [discount] benefits of the Key Customer offering, or none of the accounts get the benefits . . . (Ruscilli TR 182)

In answering concerns about extending the benefits of the Key Customer promotion to wire centers not designated in the tariff, witness Ruscilli states that "it's really kind of moot," since the majority of the BellSouth wire centers in Florida are Key Customer wire centers. (Ruscilli TR 255, 283) Thus, the witness downplays the significance of the "hot" versus "non-hot" wire center debate, which was staff's greatest concern.

Witness Ruscilli concludes by stating "without the inclusion of this [CLUB billing] provision, customers would be forced to choose between the conveniences of the CLUB billing arrangement and the benefits of the Key Customer offering." (TR 182)

SLAs

Witness Ruscilli asserts that Secondary Location Addresses ("SLAs") are used when it is necessary for a particular location or building to be served by a different wire center than the other locations or buildings. (TR 182) The witness states that subscribers with SLAs can participate in the Key Customer program "as long as it [the SLA] is billed under the same account and at least one location is located in an eligible wire center." (Ruscilli TR 182-183) Witness Ruscilli offers a real-world example:

[The need for SLAs] . . . could occur, for example, when a customer has a campus consisting of two or more buildings, one of which is served out of a different wire center than the other buildings. (TR 182)

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As with the CLUB option, the witness asserts that few customers have SLAs which are outside of the listed wire centers for the Key Customer tariffs at issue in this proceeding. (Ruscilli TR 255)

The "move" provision

Witness Ruscilli believes the "move" provision is a "reasonable and customer friendly provision that should not be altered." (TR 183) He states that the "move" provision allows a customer to move to another location that is not served by a designated "hot" wire center and continue to receive the Key Customer benefits at that new location throughout the unexpired term of the customer's contract. (Ruscilli TR 182-183)

Collectively, BellSouth witness Ruscilli believes these provisions are reasonable and do not violate any Florida Statute. (TR 183-184) Because these provisions are included as a restriction in the tariff, there is no ambiguity as to how these situations are handled, according to witness Ruscilli. (TR 284) As such, the BellSouth witness does not believe that any specific criteria should be developed with respect to BellSouth's billing conditions. (Ruscilli TR 184)

C. Analysis (Issue 3C and all sub-parts)

As noted above, staff critically reviewed the billing restrictions and conditions of the Key Customer tariffs at issue in this proceeding, dating all the way back to the filing of the first tariff, the January Key Customer filing. With respect to this issue, staff's principal concern was (and is) to evaluate whether any billing condition or restriction contained in the tariffs would in some way violate a Florida Statute (e.g., be "unfair, anticompetitive, or discriminatory"). Staff and FDN agree that "discrimination" should be the primary concern when evaluating the BellSouth billing conditions of the Key Customer tariffs at issue in this proceeding; staff notes, however, that we approach our analysis from different angles.

FDN witness Gallagher believes the discrimination issue is largely the result of the geographic targeting,²⁶ and that the "way BellSouth has structured its [Key Customer] promotions is discriminatory, anticompetitive, or both." (TR 52) Although the witness does not use the terms "CLUB billing or SLAs," staff believes his testimony describes these billing conditions. The witness believes that in order for a BellSouth promotional offering to meet the requirements of the Florida Statutes, the "permitted discounts must be narrowly designed to meet competitors' offerings in specific geographies." (Gallagher TR 53) Otherwise, BellSouth could possibly be in violation of Section 364.051(5)(a), Florida Statutes, which states, in part:

364.051 Price regulation.--

. . . .

(5)(a) NONBASIC SERVICES.--Price regulation of nonbasic services shall consist of the following:

. . . .

However, the local exchange telecommunications company shall not engage in any anticompetitive act or practice, nor unreasonably discriminate among similarly situated customers.

. . . .

In staff's view, a narrow interpretation would restrict, or at least limit, BellSouth in offering the Key Customer discounts to customer locations that are outside of the listed "hot" wire centers. Witness Gallagher states that "the Commission should not permit BellSouth . . . to apply [Key Customer discounts] to different locations of the same business entity regardless of geography . . . unless competitors can also make the same multi-location offer." (Gallagher TR 53) Staff observes, however, that the witness does not offer evidence that BellSouth or something else impedes FDN from making a similar multi-location offer.

²⁶Staff notes that "geographic targeting" was previously addressed in Issue 3-D.

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Staff is concerned that, in practice, BellSouth's CLUB billing, SLA arrangements, and the "move" provisions could extend the Key Customer discounts to customers with one or more locations outside of the listed "hot" wire centers. Staff points out that each Key Customer tariff listed specific wire centers (i.e., the "hot" wire centers) for which the program applied. Staff's concern is that in extending these benefits beyond the listed wire centers, BellSouth could be "discriminating" against like, yet ineligible, businesses in the "non-hot wire centers." Staff notes, however, that in Section 364.051(5)(a), Florida Statutes, the word "discriminate" is preceded by an important adjective, and that is "unreasonably." Thus, staff believes it must go beyond considering whether BellSouth's CLUB billing, SLA arrangements, and the "move" provisions merely "discriminate," but rather whether such provisions "unreasonably discriminate."

Though BellSouth admits that its CLUB billing, SLA arrangements, and the "move" provisions may extend the benefits outside of the "hot" wire centers, witness Ruscilli maintains that these provisions are reasonable and "customer friendly" provisions. (TR 183) The witness believes that BellSouth's disclosure of these provisions in its tariff prevents any statutory or tariff violation. Furthermore, witness Ruscilli states that the frequency of CLUB billing, SLA arrangements, and the "move" provisions being invoked is rather low. (TR 283) FDN makes no specific case to challenge these assertions, or that such provisions "unreasonably discriminate" against competitors. Without specific evidence to the contrary, staff has no reason to disagree with these assertions, particularly in light of witness Ruscilli's testimony that the majority of the BellSouth wire centers in Florida are Key Customer wire centers. (TR 283) Additionally, staff would note that FDN did not specifically demonstrate how it was impaired in making a multi-location offer similar to BellSouth's CLUB billing arrangement.

As such, staff rejects FDN's (narrow) interpretation that the discrimination resulting from BellSouth's billing practices meets the threshold of being "unreasonably discriminatory," in violation of Section 364.051(5)(a), Florida Statutes. Staff does not believe the "discrimination" at issue here rises to the level of being "unreasonable."

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In short, staff believes that in order for the Commission to consider establishing criteria to evaluate how the billing conditions or restrictions of a BellSouth promotional tariff offering are unfair, anticompetitive, or discriminatory, the burden would be on the Petitioner to demonstrate that such is necessary. Though FDN witness Gallagher argues extensively about geographic targeting and other allegations of discrimination, he provides little argument that is specific to BellSouth's billing conditions and restrictions.

D. Conclusion (Issue 3C and all sub-parts)

Staff recommends that additional criteria are not warranted or necessary. The BellSouth Key Customer tariff filings at issue in this proceeding meet the criteria of the Florida Statutes.

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ISSUE 3E: What criteria, if any, should be established to determine whether any other terms or conditions of a BellSouth promotional tariff offering are unfair, anticompetitive, or discriminatory?

(i): Is the BellSouth Key Customer tariff filing (Tariff Number T-020035) unfair, anticompetitive, or discriminatory under the criteria, if any, established pursuant to this issue?

(ii): Is the BellSouth Key Customer tariff filing (Tariff Number T-020595 or a subsequent tariff filing that extends the expiration date thereof) unfair, anticompetitive, or discriminatory under the criteria, if any, established pursuant to this issue?

RECOMMENDATIONS

3E: No other criteria should be established to determine whether any other terms or conditions of a BellSouth promotional tariff offering are unfair, anticompetitive, or discriminatory.

3(i) & 3E(ii): No other criteria were established in Issue 3E to determine whether the BellSouth Key Customer tariff filings at issue in this proceeding are unfair, anticompetitive, or discriminatory. (GARCIA, BARRETT)

POSITIONS OF THE PARTIES

FDN:

3E: The Commission must consider, at a minimum, BellSouth's dominant market power and position relative to that of individual ALECs, the level and availability of the BellSouth discounts, the duration of the discounts, UNE costs, the level and effect of the

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termination liability, and the impacts on customers, competition and competitors over time.

(i) & (ii): Yes. Any BellSouth discounts should be offered to all BellSouth customers. At a minimum, BellSouth customers discriminated against must not be harmed by the discrimination. The record in this case establishes that customers discriminated against have been harmed.

BELLSOUTH:

3E: It is not necessary to establish any new criteria.

(i) & (ii): No.

STAFF ANALYSIS: This issue was structured to be a "catch-all" issue - an issue where a party could present argument that may not fit under the other issues of this proceeding. Issue 3E and its sub-parts evaluate whether specific criteria should be established to determine whether any other terms or conditions of a BellSouth promotional tariff offering are unfair, anticompetitive, or discriminatory. In similar fashion to the other issues of this recommendation, the sub-parts to this issue relate specifically to the Key Customer tariff filings addressed in this proceeding.

For the purposes of efficiency, staff notes that the recommendations and analysis presented for this issue encompass both of the sub-parts of Issue 3E. Neither FDN or BellSouth offer an argument of substance for this issue.

FDN and BellSouth (Issue 3E and its sub-parts)

FDN's witness Gallagher does not present any unique evidence for consideration in Issue 3E or its sub-parts. Rather, the witness

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points to the existing argument throughout the record of this proceeding. In its brief, FDN states that

the Commission must be ever mindful of the interplay of other matters with its decision in cases like this . . . [and must] be able to promptly adjudicate such offerings to be anticompetitive if the Commission is to preserve a free and fair marketplace.

(FDN BR 34)

As in his arguments for the preceding issues, BellSouth witness Ruscilli advocates that no additional criteria are necessary to address any other terms and conditions. (TR 190) BellSouth believes the Key Customer tariffs at issue in this proceeding are lawful under the existing Florida Statutes. In its brief, BellSouth states that "the Key Customer tariffs benefit end user customers and the Commission should reject implementing new criteria." (BellSouth BR 33)

Analysis & Conclusion (Issue 3E and its sub-parts)

Neither FDN nor BellSouth present unique evidence for consideration in Issue 3E or its sub-parts. Staff does not believe any criteria should be established pursuant to Issue 3E and its sub-parts. As such, there are no other criteria against which to evaluate whether the terms of a BellSouth promotional tariff offering are unfair, anticompetitive, or discriminatory.

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ISSUE 4A: Under what terms and conditions should BellSouth promotional tariff offerings be made available for ALEC resale?

(i): Does the BellSouth Key Customer tariff filing (Tariff Number T-020035) meet the resale terms and conditions established pursuant to this issue?

(ii): Does the BellSouth Key Customer tariff filing (Tariff Number T-020595 or a subsequent tariff filing that extends the expiration date thereof) meet the resale terms and conditions established pursuant to this issue?

RECOMMENDATIONS:

4A: BellSouth's promotional tariff offerings should be and are made available for ALEC resale in accordance with the terms and conditions required by state and federal law. The law provides that incumbent LECs offer for resale at wholesale rates any telecommunications service that the carrier provides at retail to noncarrier subscribers. Also, promotions of more than 90 days must be available for resale at the promotional rate minus the wholesale discount. Further, the incumbent LECs must not prohibit or impose unreasonable or discriminatory conditions or limitations on the resale of such telecommunications service.

4A(i) & 4A(ii): The BellSouth Key Customer tariff filings at issue in this proceeding meets the resale terms and conditions established in Issue 4A. (GILCHRIST)

POSITIONS OF THE PARTIES

FDN:

4A: Resale terms and conditions must be fair and reasonable. BellSouth's are not because it bills ALECs without automatically applying the discounts and because ALECs should not be responsible for

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the full termination liability in the event the customer departs ALEC service, particularly when the customer ports back to BellSouth.

(i) & (ii): No.

BELLSOUTH:

4A: Retail promotions offered for 90 days or less are not discounted while promotions of more than 90 days are available for resale at the promotional rate minus the wholesale discount.

(i) & (ii): Yes. The tariff is available for resale.

STAFF ANALYSIS: This issue evaluates whether ALEC resale of BellSouth promotional tariff offerings should be subject to specific terms and conditions. The sub-parts to this issue explore the specific termination liability terms and conditions of the Key Customer tariff filings at issue in this proceeding.

For purposes of efficiency, staff notes that the argument and analysis presented for this issue encompass both of the sub-parts of Issue 4A. The analysis herein begins with an overall review of the arguments presented, followed by a (limited) sub-part analysis, and then a conclusion.

A. FDN Argument on Issue 4A and all sub-parts

FDN witness Gallagher believes that the resale terms and conditions should be consistent with the FCC's established rules and regulations. (TR 53) In addition, FDN notes that one of the FCC's requirements is that the terms and conditions for resale be reasonable; witness Gallagher believes the Key Customer offerings at issue in this proceeding are deficient in this regard. (TR 53)

According to FDN witness Gallagher, BellSouth indicated that, at present, the bills it will send to ALECs reselling existing Key Customer promotions will not reflect the Key Customer discounts;

rather, the ALECs will have to calculate those discounts on their own and then apply to BellSouth for credits. (TR 54) The witness argues that he does not think that a system of mandatory and recurring credit requests is a reasonable way of billing a customer, and such a scheme would be unduly burdensome on the ALECs. (TR 54) FDN witness Gallagher asserts that BellSouth apparently did not anticipate ALECs reselling these promotions; otherwise BellSouth would already have the systems in place to properly bill ALECs for reselling these promotions. (TR 54)

FDN witness Gallagher contends that in another discovery response BellSouth indicated that if a customer to whom an ALEC resells a BellSouth promotion leaves the ALEC service before the end of the promotion's contract term, BellSouth will charge the ALEC (not the end user) the entire termination liability. (TR 54) If the termination liability is unfair, anticompetitive or discriminatory to begin with, FDN witness Gallagher believes it would be even more so when resold and the ALEC was responsible for those charges. (TR 54) Moreover, FDN argues in its brief that making the ALEC responsible to BellSouth for the termination liability when the resold ALEC customer departs pre-term only to return to BellSouth would be an inappropriate windfall for BellSouth. (BR 36)

B. BellSouth Argument for Issue 4A and all sub-parts

BellSouth witness Ruscilli believes that the Act and this Commission's rules govern its requirements for the resale of promotional offerings, consistent with the Commission's Order in Docket Nos. 960833-TP, 960846-TP, and 960916-TP. (TR 193) He argues that BellSouth is in compliance with the Commission's Orders, and according to the terms of the interconnection agreements entered into between BellSouth and Florida ALECs, all long-term promotions, including the January and June Key Customers offerings, are available for resale at the wholesale discount. (TR 194) Further, BellSouth witness Ruscilli argues that the FCC clearly recognizes that incumbents like BellSouth may offer either short-term or long-term promotions, and that short-term promotions are not subject to the resale discount requirements of the Act. (TR 193)

BellSouth argues in its brief that although FDN has acknowledged that the Key Customer offerings are at issue in this proceeding are available for resale, FDN has chosen not to avail itself of this

opportunity. (BR 34) Thus, BellSouth argues in its brief that FDN's complaint concerning the requirement that ALECs calculate Key Customer discounts and subsequently apply for credits, as well as its complaint about termination liability associated with resale, should be summarily dismissed. (BR 34) Further, in its brief, BellSouth argues that unless and until FDN actually takes advantage of the resale opportunity, FDN has no basis to lodge complaints about terms and conditions with which it has no personal experience. (BR 34)

Regarding the sub-part issues, BellSouth believes the Key Customer offerings are available for resale consistent with the resale obligations of the Act, FCC rules and Commission orders. (Ruscilli TR 193, 194)

C. Analysis of Issue 4A and all sub-parts

As noted previously, for efficiency, the argument and staff's analysis for Issues 4A and its sub-parts are presented in a combined format.

Staff believes that BellSouth's promotional tariff offerings should be made available for ALEC resale in accordance with the terms and conditions required by federal law. Section 251(c)(4), the resale provision in the Telecommunications Act of 1996, provides:

Resale-The duty-

(A) to offer for resale at wholesale rates any telecommunications service that the carrier provides at retail to subscribers who are not telecommunications carriers; and

(B) not to prohibit, and not to impose unreasonable or discriminatory conditions or limitations on, the resale of such telecommunications service, except that a State commission may, consistent with regulations prescribed by the Commission under this section, prohibit a reseller that obtains at wholesale rates a telecommunications service that

is available at retail only to a category of subscribers from offering such service to a different category of subscribers.

Federal Communications Commission (FCC) Order FCC 96-325 reads in part:

948. Section 251(c)(4) provides that incumbent LECs must offer for resale at wholesale rates "any telecommunications service" that the carrier provides at retail to noncarrier subscribers. This language makes no exception for promotional or discounted offering, including contract and other customer-specific offering. We therefore conclude that no basis exists for creating a general exemption from the wholesale requirement for all promotional or discount service offerings made by incumbent LECs. . . .

. . . .

950. . . . [W]e believe that promotions of up to 90 days, when subjected to the conditions outlined below, will have significantly lower anticompetitive potential, especially as compared to the potential procompetitive marketing uses of such promotions. We therefore establish a presumption that promotional prices offered for a period of 90 days or less need not be offered at a discount to resellers. Promotional offerings greater than 90 days in duration must be offered for resale at wholesale rates pursuant to section 251(c)(4)(A). To preclude the potential for abuse of promotional discounts, any benefit of the promotion must be realized within the time period of the promotion, e.g., no benefit can be realized more than ninety days after the promotional offering is taken by the customer if the promotional offering was for ninety days. In addition, an incumbent LEC may not use promotional offering to evade the wholesale obligation, for

example by consecutively offering a series of 90-day promotions.

Staff believes that BellSouth's long-term promotional tariff offerings are required to be made available for ALEC resale in accordance with the terms and conditions required by state and federal law. Based on the evidence presented in the record, staff believes the BellSouth Key Customer tariff offerings at issue in this proceeding are made available for resale in accordance with state and federal requirements.

D. Conclusion (Issue 4A and all sub-parts)

BellSouth's promotional tariff offerings should be, and, are made available for ALEC resale in accordance with the terms and conditions required by state and federal law. Pursuant to law, incumbent LECs must offer for resale at wholesale rates any telecommunications service that the carrier provides at retail to noncarrier subscribers. Also, promotions of more than 90 days must be available for resale at the promotional rate minus the wholesale discount. Further, the incumbent LECs must not prohibit or impose unreasonable or discriminatory conditions or limitations on the resale of such telecommunications service. According to the evidence in the record, staff believes BellSouth has met the terms and conditions required by state and federal law.

ISSUE 4B: What is the competitive impact, if any, of the resale of BellSouth promotional tariff offerings?

RECOMMENDATION: Resale of BellSouth's promotional tariff offerings provides ALECs with another means of competing with BellSouth and is not detrimental to the development of viable competition.
(GILCHRIST/SIMMONS)

POSITION OF THE PARTIES

FDN: The resale of BellSouth's promotional discounts is completely at odds with this Commission's and the FCC's announced goals of promoting facilities-based competition. Resale of promotions leads to the erosion/abandonment of facilities-based infrastructure. Moreover, resale is an unfinanciable, non-viable business option.

BELLSOUTH: The fact that the January and June Key Customer offerings are available for resale has a favorable impact on competition. Among other things, it eliminates the possibility of an anti-competitive price squeeze.

STAFF ANALYSIS: This issue evaluates the competitive impact, if any, of the resale of BellSouth promotional tariff offerings. Staff observes that this is somewhat of a "policy" issue, whereas prior issues were more oriented to evaluating the specific Key Customer tariffs of this proceeding.

A. FDN Argument

FDN witness Gallagher asserts that as long as the Commission permits BellSouth to continue providing discounts like the Key Customer programs, ALECs have a choice of becoming nonviable by trying to beat BellSouth's promotional prices or becoming nonviable by reselling those discounts. (TR 55) Witness Gallagher contends that the resale "option" is not a vehicle for ALECs to mitigate the effects of BellSouth's anticompetitive practices; rather, like the promotions themselves, it is a plan for disassembling facilities-based competition." (TR 55)

According to witness Gallagher, any opportunity ALECs have to resell BellSouth promotional prices is an empty consolation. (TR 55) Witness Gallagher contends that resale does not serve to avoid the harm ALECs suffer from BellSouth promotions, nor does it remedy BellSouth's conduct. (TR 55) Further, witness Gallagher asserts the resale business has been for sometime now widely considered a non-viable, unfinanciable venture, and many ALECs like FDN do not generally resell services because of inadequate margins; margins that do not change when reselling a promotion. (TR 55) According to witness Gallagher, even BellSouth admits that no Florida ALEC has resold a BellSouth Key Customer contract; witness Gallagher questions why this is the case if resale terms and conditions are reasonable and resale is a viable competitive option. (TR 55)

B. BellSouth Argument

BellSouth witness Garcia argues that competition has steadily continued throughout the time that BellSouth has offered the Key Customer promotions. (TR 343) He notes that FDN announced in October 2002 that it had achieved 100,000 lines in just 3.5 years of being in business, which includes a time period during which the Key Customer contracts were available. (TR 343) Also, witness Garcia notes that the number of calls that BellSouth received in the call centers asking about competitive offers did not decline at all during the time the Key Customer promotion was being offered. (TR 343-344)

BellSouth witness Garcia asserts that BellSouth's Key Customer offerings are a direct result of the competition that has been, and continues to, take place in Florida in the small business market. (TR 344) Even with the Key Customer Program in place, other carriers have offered, and continue to offer, customers lower rates and have experienced line growth. (Garcia TR 344) Further, BellSouth witness Massey asserts that in the areas in which competitors choose to compete, the competitors are gaining significant numbers of small business access lines, and are far from being "eliminated." (TR 395) Further, witness Massey contends that from January 2000 to September 2002, the percentage of small business lines that are served by BellSouth has fallen from an overstated estimate of 90.0 percent at the end of 1999 to an overstated estimate of 71.5 percent in September 2002. (TR 395) According to witness Massey, BellSouth's market share is declining 0.3 to 0.4 percentage points every month, which equates to

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roughly 3.6 to 4.8 percentage points annually. (TR 396) Thus, witness Massey argues that these figures clearly demonstrate that customers are able to migrate freely. (TR 396)

In offering its discounts, BellSouth witness Pitofsky indicates that BellSouth is responding to significant marketplace competition. (TR 409) Witness Pifofsky notes that in the Telecommunications Market in Florida/Annual Report on Competition, as of June 30, 2002 (Draft 2002 Report), this Commission noted that "ALECs have made impressive gains in the business market, increasing their share to 26 percent, up from last year's share of 16 percent. (EXH 8) Further, the 2002 Draft Report also notes that "ALECs show the heaviest presence in BellSouth's territory," where they have 33.16 percent of business lines. (Exh 8) According to witness Pitofsky, these "impressive gains" during the period when BellSouth was offering the Key Customer offerings are indicative of a vigorously, and increasingly, competitive market. (TR 410) He argues that FDN saw the number of access lines it was serving in hot wire centers increase significantly from 2001 to 2002, despite the fact that FDN raised its tariffed rates during that same time period. (TR 410) Furthermore, witness Pitofsky notes that the 2002 Draft Report shows that there are 122 ALECs currently providing service in Florida. (EXH 8)

BellSouth witness Taylor argues that the Commission should recognize that the resale provision of the Federal Telecommunications Act of 1996, as implemented by the FCC and this Commission, creates a situation in which BellSouth's competitors are not disadvantaged by BellSouth's control of any "essential facilities" or "monopoly services" as those terms are contemplated in Florida statutes. (TR 487) According to witness Taylor, the resale price the competitor pays BellSouth for any service (including any monopoly component of that service) will always be less than the price BellSouth charges its retail customers for the same service (including any monopoly component thereof). (TR 487)

In its brief BellSouth argues that because the Key Customer offering is available for resale, any ALEC that is at least as efficient as BellSouth in marketing and sales will be able to compete using the resale opportunity. Further, BellSouth argues in its brief that utilizing resale to serve some customers does not mean that FDN has to forego its pursuit of serving customers using its own

facilities. Instead, according to BellSouth, FDN can (as other carriers choose to) utilize more than one mode of serving customers. (BellSouth BR at 34-35)

C. Analysis

Staff notes the argument offered by FDN that the competitive impact of reselling BellSouth promotional tariff offerings is negative. FDN witness Gallagher argues that the resale of promotions leads to the erosion/abandonment of facilities-based infrastructure and that resale is an unfinanciable, non-viable business option. (TR 55) FDN witness Gallagher also points out that no Florida ALEC has resold to an end user with a BellSouth Key Customer Contract. (TR 55)

On the one hand, witness Gallagher seems to suggest that resale will have the undesirable result of undermining facilities-based competition, while on the other hand, he admits that resale is not particularly attractive. Quite simply, staff cannot reconcile FDN's arguments. Since BellSouth's promotional tariff offerings are available for resale, staff does not believe ALECs are adversely affected. Rather, staff agrees with, and is persuaded by, BellSouth's argument that utilizing resale to serve some customers does not mean that FDN has to change its overall strategy of serving customers using its own facilities. Staff believes the resale price the competitor pays BellSouth for any service will always be less than the price BellSouth charges its retail customers for the same service, and as such, competitors suffer no disadvantage.

D. Conclusion

There is no dispute that the BellSouth promotional tariff offerings at issue in this proceeding are available for resale to competitors. Reselling BellSouth's promotional tariff offerings provides ALECs with another means of competing with BellSouth and is not detrimental to the development of viable competition.

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ISSUE 5A: In the context of marketing promotional tariffs, what waiting period or other restrictions, if any, should be applicable to BellSouth?

RECOMMENDATION: In the context of marketing promotional tariffs, staff recommends that the Commission acknowledge BellSouth's voluntary 10-day waiting period after a customer leaves BellSouth for an ALEC before any type of winback activity is implemented. Staff also recommends that the Commission affirm its finding contained in Order No. PSC-02-0875-PAA-TP, prohibiting BellSouth from including any marketing information in its final bill sent to customers who have switched providers.
(CASEY)

POSITION OF THE PARTIES

FDN: BellSouth should not be permitted to market promotions for 30 days after a customer leaves ALEC service. Marketing discounts should be by effective similar means, materials and methods for all eligible customers. Marketing should also be restricted in the wake of an ALEC market exit.

BELLSOUTH: No waiting periods or other restrictions should be placed on BellSouth's ability to market its promotional offerings.

STAFF ANALYSIS: This issue addresses whether any waiting period or other restrictions should be placed on BellSouth in the context of marketing promotional tariffs. The concept of "win-back" can be divided into two distinct types of marketing: marketing intended either to (1) regain a customer, or (2) retain a customer. Regaining a customer applies to the marketing situations where a customer has already switched to and is receiving service from another provider. Retention marketing, by contrast, refers to a carrier's attempts to persuade a customer to remain with that carrier before the customer's service is switched to another provider.

A. FDN Argument

FDN would like the Commission to initiate a 30-day waiting period after a customer leaves BellSouth for an ALEC before BellSouth is allowed to market any winback promotions. FDN would also like the Commission to apply this 30-day waiting period to customers of an ALEC that is leaving the market. In its brief, FDN states:

In order for the ALEC and its customer to have sufficient time to adjust to the transition to ALEC service, the Commission should bar BellSouth from initiating winback contacts with the customer for 30 days after the customer leaves BellSouth service. Any shorter period would be insufficient for the ALEC and the customer to settle into service after curing any problems encountered during the complex provisioning process and to make any necessary adjustments. (FDN BR 37)

FDN would also like this 30-day waiting period to apply in the case where an ALEC is going out of business and a customer needs to find a new carrier. It would like BellSouth to be restricted from making Key Customer offerings to these customers for a period of 30 days. FDN witness Gallagher states:

. . . I note that where an ALEC is voluntarily or involuntarily exiting a market, BellSouth should not be able to take advantage of its unique position as the underlying carrier to offer discounts to customers facing disconnection before the customers could have enough opportunity to fully evaluate other carrier options. A customer of a departing ALEC may be "under the gun" of disconnection or may be placed in the service of BellSouth by default as of a date certain if the customer does not select another carrier. The customer may be notified of such by BellSouth or by the departing carrier. In cases where BellSouth notifies the customers of a disconnection date or where BellSouth is listed as the default carrier on a notice, BellSouth has an inherent marketing advantage because the customers will likely turn to BellSouth for assistance. In cases where the exiting carrier notifies the customer of its departure and

BellSouth is not a default carrier, BellSouth still has an inherent marketing advantage in that it already has subscriber information for all customers in an area that disconnected from BellSouth and can target market its discounts that way. ALECs who wish to compete for the business of the customers of the departing ALEC do not have either of these advantages. Therefore, if the Commission permits BellSouth to continue to offer Key Customer type discounts, the Commission should level the competitive playing field by directing BellSouth not to offer such discounts to customers of a departing ALEC until 30 days after the date that those customers are subject to disconnection or rolling over to BellSouth as a default carrier. This should permit the customers to evaluate offerings of other ALECs interested in their business. (TR 59-60)

FDN also believes that BellSouth should market discounts by effectively similar means, materials and methods for all eligible customers. It believes that BellSouth does not market its discounts to all eligible customers in the same way. In his direct testimony, FDN witness Gallagher states:

. . . nothing FDN has seen from BellSouth's discovery responses or elsewhere convinces FDN that BellSouth uses the same means, methods and materials to offer the Key Customer program to ALL eligible customers. Instead, BellSouth focuses its marketing efforts on ALEC eligible customers, not on BellSouth's own eligible customers. If BellSouth has a lower tariffed rate available, BellSouth should be required to truly "offer" the lower rate to anyone eligible, not just to those who have already shopped around. (TR 47)

In its brief, FDN contends that:

BellSouth should also be required to properly inform eligible customers of discounts. If BellSouth's discount programs were structured such that only ALEC customers were eligible, those programs would not pass muster. BellSouth should not be permitted to do indirectly what it cannot do directly, and

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therefore, BellSouth should offer discounts to all eligible customers using effectively similar means, materials and methods. (FDN BR 37-38)

B. BellSouth Argument

BellSouth has voluntarily initiated a region-wide 10-day waiting period after a customer leaves BellSouth for an ALEC before any type of winback activity is implemented. (Ruscilli TR 194) BellSouth believes that no other restrictions are necessary. (Ruscilli TR 194) BellSouth witness Ruscilli, in his direct testimony, states:

BellSouth's position is there is no basis for any additional restrictions on BellSouth's ability to engage in marketing its promotional offerings. As the Commission acknowledged in its June 28, 2002 order in Docket No. 020119-TP, BellSouth has established a region-wide, 10-day waiting period, whereby BellSouth will not initiate any win-back activities to regain a customer. (See FPSC Order No. PSC-02-0875-PAA-TP at page 21). In this same order, the Commission precluded BellSouth from including any marketing information in its final bill sent to customers who have switched providers. (7d. at page 22). Any additional restrictions would unnecessarily restrict customer choice. (TR 194)

Witness Ruscilli further addresses restrictions on the Key Customer offerings by stating:

If additional restrictions are placed upon BellSouth's ability to offer promotions, Florida consumers will suffer. Without the pressure of BellSouth's promotional offerings, ALECs will be insulated from competition by BellSouth at the cost of depriving Florida consumers of the benefits of the vibrant competition that exists in the local exchange market in Florida. (TR 170)

Witness Ruscilli again addresses marketing restrictions in his rebuttal testimony, stating:

As discussed in my direct testimony, BellSouth has established a region-wide, 10-day waiting period during which BellSouth will not initiate any win back activities to regain a customer. Further, BellSouth has procedures and safeguards to limit disclosure and the use of CPNI and wholesale information in a manner consistent with the requirements of the FCC rules, section 222 of the Act, and any applicable state or local requirement. The placement of additional restrictions upon BellSouth is neither appropriate nor necessary. (TR 219)

Regarding FDN's allegation that BellSouth's Key Customer offerings are not marketed by similar means, materials and methods BellSouth witness Garcia, in his rebuttal testimony, states:

. . . the January and June Key Customer offers are available to all types of customers - whether the customers are new or returning customers, or existing customers - and BellSouth takes reasonable steps to inform all types of customers of these offerings. BellSouth pro-actively sent direct mail to thousands of potentially eligible customers - both former and existing BellSouth customers - to notify them of these offerings. Thus, contrary to Mr. Gallagher's assertions, BellSouth in fact "alerted" customers of these offerings and did not restrict the offerings to former BellSouth customers only, although it would certainly be reasonable for BellSouth to target future marketing efforts to former customers. (TR 331-332)

C. Analysis

Staff believes a win-back promotion such as the Key Customer offering is not, in and of itself, detrimental. In fact, win-back promotions can be very beneficial to Florida consumers by giving them a choice of providers with varied services at competitive prices.

The Federal Communications Commission addressed win-back promotions in its Order FCC 99-223, released September 3, 1999, in which it stated:

Win-back facilitates direct competition on price and other terms, for example, by encouraging carriers to "out bid" each other for a customer's business, enabling the customer to select the carrier that best suits the customer's needs. (§ 68)

Some commenters argue that ILECs should be restricted from engaging in win-back campaigns, as a matter of policy, because of the ILECs' unique historic position as regulated monopolies. Several commenters are concerned that the vast stores of CPNI gathered by ILECs will chill potential local entrants and thwart competition in the local exchange. We believe that such action by an ILEC is a significant concern during the time subsequent to the customer's placement of an order to change carriers and prior to the change actually taking place. Therefore, we have addressed that situation at Part V.C.3, *infra*. However, once a customer is no longer obtaining service from the ILEC, the ILEC must compete with the new service provider to obtain the customer's business. We believe that such competition is in the best interest of the customer and see no reason to prohibit ILECs from taking part in this practice. (§ 69)

Because win-back campaigns can promote competition and result in lower prices to consumers, we will not condemn such practices absent a showing that they are truly predatory. (§ 70)

Staff notes that BellSouth has voluntarily initiated a 10-day waiting period after a customer leaves BellSouth for an ALEC before any type of winback activity is implemented. FDN is recommending a 30-day waiting period after a customer leaves BellSouth before BellSouth is allowed to initiate any winback activity. During cross-examination of FDN witness Gallagher at hearing, staff asked the FDN witness to explain why FDN needed an additional 20 days prior to BellSouth initiating any winback activity. Witness Gallagher replied:

. . . ten days isn't really enough to get to know the customer. There could be some post-cut over hiccup that happened; the customer might still be blaming us for that, whether it was our fault or not. It's just, just a time to

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get to know the customer and try to establish some goodwill.
That's really all that is. (TR 121)

In staff's initial recommendation in this proceeding, we recommended a 30-day waiting period. Our primary concern was that there were potential double billing issues which could occur. However, at the June 18, 2002 agenda conference, FDN witness Gallagher stated that this was not a problem. BellSouth responded to staff's concern on double billing in its brief, noting:

Mr. Gallagher explained "with FDN, the way we do our [billing for] facilities-based [services], we don't have a problem with double billing." (FDN BR 35-36)

Staff disagrees with FDN witness Gallagher that a 10-day waiting period is not enough. (TR 121) Staff believes that since FDN has no double billing issues, the Commission should acknowledge BellSouth's voluntary 10-day waiting period before BellSouth can initiate any winback activity. Staff also believes that the Commission should affirm its finding contained in Order No. PSC-02-0875-PAA-TP, issued June 28, 2002, prohibiting BellSouth from including any marketing information in its final bill sent to customers who have switched providers. That finding by the Commission was not protested.

FDN would also like to have BellSouth initiate a 30-day waiting period on BellSouth when an ALEC exits a market, where BellSouth could not offer discounts to those customers until 30 days after the date that those customers are subject to disconnection or rolling over to BellSouth as a default carrier. During cross-examination by staff at hearing, when asked about FDN's proposal, FDN witness Gallagher explained:

. . . that stems directly from the Network Plus issue where Network Plus was going out of business and they sent their customers a notice that was somewhat scary for the customers that said, you will be out of phone service in a certain number of weeks, you know. And so these people pick up the phone and call BellSouth and were just enrolled in mass in the Key Customer, we believe.

When a customer provider is exiting the market -- I don't think it would -- I think that, that there should be some sort of cooling off period so that -- the monopoly is going to get most of the people when a customer is exiting. Everybody is going to run for the exits and they're going to run for BellSouth. (TR 117)

Staff believes that no waiting period should be established on BellSouth marketing when an ALEC is exiting the market and the exiting ALEC customer is seeking a provider. We believe the consumer is at a critical point when he learns his telephone provider is exiting the market and he needs to find another provider. He should be allowed to examine all options available to him to determine the best possible choice and to ensure a smooth, seamless transition to his new provider. Staff believes that limiting his choices would not be appropriate.

FDN believes that BellSouth's marketing of the Key Customer offerings is focused on ALEC customers, not all eligible customers such as existing BellSouth customers, and that BellSouth does not use similar means, materials and methods of marketing for all eligible customers. BellSouth witness Garcia stated that BellSouth takes reasonable steps to inform all types of customers of these offerings, sending direct mail to thousands of potentially eligible customers - both former and existing BellSouth customers - to notify them of these offerings. (TR 331)

After a review of BellSouth marketing ads for the Key Customer offerings, and a review of exhibits showing direct mail information, staff believes that BellSouth has shown that the Key Customer program is offered to both new and existing BellSouth customers, and no restrictions on the means, materials, and methods of marketing are necessary at this time. (EXH 3, p.66)

In its brief, BellSouth suggests that the Commission may want to initiate a generic proceeding to consider marketing practices in the entire industry, similar to a proceeding underway at the Georgia Public Service Commission (GPSC). BellSouth stated:

To the extent the Commission is interested in examining restrictions at all, the proper course would be to initiate

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a generic proceeding to consider marketing practices in the entire industry with any waiting periods applicable to all carriers. (See e.g., Docket No. 14232-U; Code of Conduct for Winback Activities) (On March 24, 2003 the Georgia Public Service Commission adopted a seven-day waiting period restricting winback activities; the waiting period applies equally to all carriers and does not apply to inbound customer calls). (BellSouth BR 36)

The GPSC ordered that the industry come up with a proposed marketing code of conduct, which includes winback activities. The ILECs, ALECs, and other interested parties worked together on the code of conduct, which was adopted by the GPSC on March 18, 2003, and became effective twenty days after adoption. The Florida Telecommunications Competitive Interests Forum also has a marketing code of conduct as a possible item for discussion (Topics MKT-1-Win back, and MKT-2-Marketing practices). However, the item has been tabled pending the decisions in this docket. Although staff believes that a marketing code of conduct may be beneficial to all parties, staff is not recommending that this Commission proceed to develop one at this time through this docket.

D. Conclusion

Staff believes that the Commission should acknowledge BellSouth's voluntary 10-day waiting period after a customer leaves BellSouth for an ALEC before any type of winback activity is implemented. Staff also believes that no waiting period should be established on BellSouth marketing when an ALEC is exiting the market and the exiting ALEC customer is seeking a provider. Also, the Commission should affirm its finding contained in Order No. PSC-02-0875-PAA-TP, prohibiting BellSouth from including any marketing information in its final bill sent to customers who have switched providers.

In addition, staff believes that BellSouth has shown that the Key Customer program is offered to both new and existing BellSouth customers, and no restrictions on the means, materials and methods of marketing are necessary at this time. Staff further believes that the Commission, in another forum, may wish to explore the idea of a Florida marketing code of conduct which could be developed by industry consensus and submitted to the Commission for adoption.

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Based on staff's analysis, staff recommends that the Commission acknowledge BellSouth's voluntary 10-day waiting period after a customer leaves BellSouth for an ALEC before any type of winback activity is implemented. Staff also recommends that the Commission affirm its finding contained in Order No. PSC-02-0875-PAA-TP, prohibiting BellSouth from including any marketing information in its final bill sent to customers who have switched providers.

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ISSUE 5B: In the context of marketing promotional tariffs, what restrictions, if any, should be placed on the sharing of information between BellSouth's wholesale and retail divisions?

RECOMMENDATION: In the context of marketing promotional tariffs, staff recommends that the Commission affirm its finding contained in Order No. PSC-02-0875-PAA-TP prohibiting BellSouth's wholesale division from sharing information with its retail division, such as informing the retail division when a customer is switching from BellSouth to an ALEC. (CASEY)

POSITION OF THE PARTIES

FDN: No BellSouth retail employee or agent with access to wholesale information should engage in retention or winback efforts. No retention or winback effort should occur during retail customer contact initiated for account activity predicate to a change in carrier, such as moving or removing xDSL, lifting a freeze, etc.

BELLSOUTH: It is BellSouth's policy to treat all Customer Proprietary Network Information and Wholesale information in a confidential manner, and to limit the disclosure and use of CPNI and Wholesale Information consistent with the requirements of the Act, and applicable FCC and Commission orders. No additional restrictions should be imposed.

STAFF ANALYSIS: This issue addresses the sharing of customer proprietary network information (CPNI) and wholesale information between BellSouth's retail and wholesale divisions. The FCC describes CPNI as the following:

CPNI includes, among other things, to whom, where, and when a customer places a call, as well as the types of service offerings to which the customer subscribes and the extent the service is used. (FCC Order 99-233, ¶ 1)

According to BellSouth witness Ruscilli, wholesale information is information that BellSouth has in its possession because it provides

services to other carriers that provide services to end user customers.
(TR 195)

A. FDN Argument

FDN would like assurance that BellSouth abides by existing CPNI and wholesale information restrictions. In his direct testimony, FDN witness Gallagher states:

. . . no BellSouth retail employee or agent should have any access to wholesale information, such as an ALEC's request for CSR [customer service record] information of submission and status of local service orders ("LSRs"). Further, the Commission should forbid BellSouth from using in-bound customer calls as a vehicle for retention efforts when the customer requests account activity predicate to a carrier change, including the following activities: steps necessary to reconfigure BellSouth's tied xDSL services and (until there is a suitable vehicle for ALECs to address pending service orders) steps for clearing pending service orders or problems with CSRs. (TR 58)

FDN further explains its position in its brief:

To ensure competitive fairness and have the advantages of a bright-line rule, the Commission should bar BellSouth retail personnel with access to wholesale information from engaging in retention efforts. The possibility of improper access and conduct is too great otherwise. Further, notwithstanding whether the retail employee has access to wholesale information, BellSouth retail personnel should not be permitted to engage in retention efforts during customer contact initiated for account activity predicate to a carrier change, such as lifting a freeze and moving or removing DSL service. (FDN BR 39-40)

B. BellSouth Argument

In his direct testimony, BellSouth witness Ruscilli noted that the Commission determined in its June 28, 2002 order in Docket No. 020119-TP, that BellSouth is prohibited from sharing information with its retail division, such as informing the retail division when a customer is switching from BellSouth to an ALEC. He stated that it is the policy of BellSouth to treat all CPNI and wholesale information in a confidential manner. (TR 195) He further explained BellSouth's position, stating:

. . . it is the policy of BellSouth to limit disclosure and the use of CPNI and Wholesale Information in a manner consistent with the requirements of the FCC rules, Section 222 of the Act, and any applicable state or local requirement. All employees of BellSouth who may have access to either CPNI or Wholesale Information receive annual training with respect to the proper use of and access to such information. It is against BellSouth policy for any employee or authorized representative of BellSouth to misuse wholesale information. It is the policy of BellSouth that no BellSouth personnel shall access any BellSouth IT system unless that person has a legitimate and authorized business purpose for such access. Without limitation, this means that BellSouth personnel are prohibited from "system surfing" just to see what information is available. BellSouth's wholesale operations do not provide leads to its retail operations. Any information used by BellSouth's retail operations to develop lists of former customers that are potentially eligible for promotional offerings are obtained from retail information sources - not wholesale sources. (TR 42-43)

FDN stated that it believes that the Commission should impose restrictions on in-bound customer calls to BellSouth, specifically, where a customer calls BellSouth for an activity which may indicate a change in carrier, such as moving or removing DSL, lifting a freeze, etc. (FDN BR 38-39) BellSouth witness Ruscilli notes that if a customer is calling in to lift a local service freeze, BellSouth does not initiate any retention efforts. (TR 264) However, if the customer asks for information or the customer asks about what BellSouth offers are available, retention efforts may be initiated. (TR 264) BellSouth

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responds to FDN's proposal for restrictions on in-bound calls concerning DSL in its brief:

FDN's request to impose restrictions on other inbound calls, specifically calls relating to DSL service, should be rejected. FDN and BellSouth have previously litigated the provision of FastAccess service in another proceeding, and there is no need for additional Commission action here. See Docket No. 010098-TP. In Docket No. 010098-TP the parties reached agreement on many issues, including a provisioning process to implement prior Commission orders relating to FastAccess service. This provisioning process is detailed in the interconnection agreement that was executed by the parties and filed with this Commission on February 5, 2003. Notably, BellSouth and FDN have agreed that during the specific provisioning process relating to FastAccess, which process involves a standalone or second loop, when customer contact takes place "BellSouth will not engage in any winback or retention efforts, and BellSouth will refer the end user to FDN to answer any questions regarding the end user's services." (See Order No. PSC-03-0395-FOF-TP, p. 10-11; Docket No. 010098-TP.) (BellSouth BR 38)

C. Analysis

Retention marketing refers to a carrier's attempts to persuade a customer to remain with that carrier before the customer's service is switched to another provider. Staff believes that not all instances of retention marketing should be restricted, just those in which wholesale information obtained from its wholesale division may be shared with BellSouth's retail division. Staff believes that retention marketing is acceptable if the information regarding the customer potentially leaving BellSouth is obtained through independent retail means. The FCC has also addressed retention marketing in many orders. In FCC Order 99-223, the FCC stated:

Several petitioners ask the Commission to reconsider Section 64.2005(b)(3) to permit use of CPNI for the retention of soon-to-be former customers without customer approval. On the other hand, other petitioners request that the Commission expressly prohibit ILECs from engaging in retention

marketing. These petitioners claim that ILECs are using information derived solely from their status as providing carrier-to-carrier services to their competitors in an anti-competitive manner. Petitioners argue that the use of another carrier's order, including a carrier or customer request to lift a PIC freeze, is clearly and separately forbidden by sections 222(b) and 201(b). (§ 75)

We conclude that section 222 does not allow carriers to use CPNI to retain soon-to-be former customers where the carrier gained notice of a customer's imminent cancellation of service through the provision of carrier-to-carrier service. We conclude that competition is harmed if any carrier uses carrier-to-carrier information, such as switch or PIC orders, to trigger retention marketing campaigns, and consequently prohibit such actions accordingly. Congress expressly protected carrier information in section 222(a) by creating a duty to protect the confidentiality of proprietary information of other carriers, including resellers. Section 222(b) restricts the use of such proprietary information and contains an outright prohibition against the use of such information for a carrier's own marketing efforts. As stated in the *CPNI Order*, Congress' goals of promoting competition and preserving customer privacy are furthered by protecting competitively-sensitive information of other carriers, including resellers and information service providers, from network providers that gain access to such information through their provision of wholesale services. (§ 76)

The FCC made it clear that there is no prohibition against an ILEC initiating retention marketing as long as the information regarding a customer switch is obtained through independent retail means. FCC Order 99-223 states:

We agree with SBC and Ameritech that section 222(b) is not violated if the carrier has independently learned from its retail operations that a customer is switching to another carrier; in that case, the carrier is free to use CPNI to persuade the customer to stay, consistent with the limitations set forth in the preceding section. We thus distinguish between the "wholesale" and the "retail" services

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of a carrier. If the information about a customer switch were to come through independent, retail means, then a carrier would be free to launch a "retention" campaign under the implied consent conferred by section 222(c)(1). (§ 78)

However, the FCC went on to state that:

..[w]here a carrier exploits advance notice of a customer change by virtue of its status as the underlying network-facilities or service provider to market to that customer, it does so in violation of section 222(b). We concede that in the short term this prohibition falls squarely on the shoulders of the BOCs and other ILECs as a practical matter. As competition grows, and the number of facilities-based local exchange providers increases, other entities will be restricted from this practice as well. (§ 77)

The FCC also addressed retention marketing and the use of CPNI and wholesale information recently in FCC Order 03-42, issued March 17, 2003, stating:

We clarify that, to the extent that the retail arm of an executing carrier obtains carrier change information through its normal channels in a form available throughout the retail industry, and after the carrier change has been implemented (such as in disconnect reports), we do not prohibit the use of that information in executing carriers' winback efforts. This is consistent with our finding in the Second Report and Order that an executing carrier may rely on its own information regarding carrier changes in winback marketing efforts, so long as the information is not derived exclusively from its status as an executing carrier. Under these circumstances, the potential for anti-competitive behavior by an executing carrier is curtailed because competitors have access to equivalent information for use in their own marketing and winback operations. (§ 27)

We emphasize that, when engaging in such marketing, an executing carrier may only use information that its retail operations obtain in the normal course of business.

Executing carriers may not at any time in the carrier marketing process rely on specific information they obtained from submitting carriers due solely to their position as executing carriers. We reiterate our finding in the Second Reconsideration Order that carrier change request information transmitted to executing carriers in order to effectuate a carrier change cannot be used for any purpose other than to provide the service requested by the submitting carrier. We will continue to enforce these provisions, and will take appropriate action against those carriers found in violation. In addition, we note that our decision here is not intended to preclude individual State actions in this area that are consistent with our rules. (¶ 28)

D. Conclusion

Staff has examined BellSouth's policies concerning CPNI and use of wholesale information, and is satisfied that BellSouth has the appropriate policies in place. However, staff believes that the Commission should affirm its finding contained in Order No. PSC-02-0875-PAA-TP, issued June 28, 2002, prohibiting BellSouth's wholesale division from sharing information with its retail division, such as informing the retail division when a customer is switching from BellSouth to an ALEC. That finding by the Commission was not protested.

Staff believes that it is unnecessary to impose further restrictions on in-bound calls to BellSouth, addressing instances when a customer calls in to lift a carrier freeze or request to move or remove DSL. Staff believes that the FCC has sufficiently addressed retention marketing when a customer calls in to lift a carrier freeze. Staff also believes that the FDN and BellSouth interconnection agreement sufficiently covers retention marketing in the context of in-bound calls concerning DSL.

Therefore, staff recommends that the Commission affirm its finding contained in Order No. PSC-02-0875-PAA-TP prohibiting BellSouth's wholesale division from sharing information with its retail division, such as informing the retail division when a customer is switching from BellSouth to an ALEC.

ISSUE 6: If the Commission determines that a BellSouth promotional tariff is unlawful, what effect, if any, should this decision have on customers who have already contracted for service under the promotional tariff?

RECOMMENDATION: If the Commission finds that the Key Customer tariffs of this proceeding are lawful in Issues 2, 3 and 4 and its subparts, this decision should have no effect on customers who have already contracted for service under the promotional tariffs. However, if the Commission finds in Issues 2, 3 and 4 and its subparts, that the Key Customer tariffs of this proceeding are unfair, anticompetitive, or discriminatory pursuant to Chapter 364, Florida Statutes, staff believes that the customers who have contracted for service under these offerings should be given 45 days from the date of approval of this recommendation to choose to terminate, or to continue their individual contracts. BellSouth should be ordered to waive the applicable termination liability charges for a customer terminating an individual contract to seek an alternative service plan. In addition, no new customers should be allowed to sign contracts under the current tariff from the date of approval of this recommendation. (DODSON)

POSITION OF THE PARTIES:

FDN: If the promotional tariffs in this case are deemed unlawful, FDN does not object to a Commission determination prospective in effect.

BELLSOUTH: BellSouth's promotions comply with Florida law and the Commission's rules as they existed at the time BellSouth filed the offerings. If the Commission finds that these offerings do not comply with criteria established here (and it should not), customers with contracts should be allowed to continue the contract.

STAFF ANALYSIS: FDN and BellSouth only offer minimal argument specific to this issue. Staff will present this limited argument, and then offer its analysis, followed by a conclusion.

FDN states that the harm to them and their customers prospectively is that BellSouth's termination liability will "very soon have a devastating effect on facilities-based competition." (FDN BR 22)

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Witness Gallagher also states that if the BellSouth promotions continue, more people will be locked into contracts, and that will stagnate ALEC growth. (TR 67)

BellSouth states that it offered and continues to offer, the Key Customer Promotional tariffs in a manner consistent with Florida law (TR 196). BellSouth further states that this Commission allowed the then-current Key Customer tariff to remain in effect pending the hearing in this case, and also allowed BellSouth's December 2002 Key Customer promotional tariff to become effective. (See Order Nos. PSC-02-1248-FOF-TP and PSC-03-0148-PAA-TP). Because this Commission allowed those tariffs to remain effective and available to customers, BellSouth contends that any changes to promotional tariffs should apply on a prospective basis and all current customers receiving the benefits of the expired Key Customer tariff should be permitted to continue to enjoy the benefits for which they bargained. (TR 196)

Staff Analysis

The Florida Supreme Court has held on numerous occasions that when a statute is held to be unconstitutional, and taxes have been imposed and paid in reliance that the statute was valid, the declaration of unconstitutionality should apply on a prospective basis. In coming to this conclusion, the Court weighed the equity of the hardship imposed by retroactive application of the refund against the slight benefits to individual taxpayers. See, Gulesian v. Dade County School Board, 281 So.2d 325 (Fla. 1973); Martinez v. Scanlan, 582 So.2d 1167 (Fla. 1991). Staff feels an analogy can be made in this docket since the argument is one of equity.

Staff notes that neither party appears to request retroactive application. The difference in their positions on this issue centers around when the contracts should be terminated. FDN appears to suggest that the customer contracts should be terminated as of the date the Commission order goes into effect. BellSouth indicates that while no further contracts should be added, the existing contracts should be allowed to run their course.

In staff's view, the harm to the customers must be weighed against the harm to FDN. To deem the contracts void from their inception would

require the customers to be backbilled for an undetermined amount. If the Commission declares the Key Customer promotions unlawful, staff proposes that the most equitable approach would be to give the customers the choice of terminating, or continuing their individual contracts. Staff suggests that BellSouth send a letter to each contracting customer notifying him that he may terminate the contract within 45 days from the date of approval of this recommendation. Staff believes the customers, if they so choose, should get the benefit of the bargain into which they freely entered. Staff believes that the harm of backbilling to the contracting customers is greater, and if the Commission declares the Key Customer promotions unlawful, FDN's concerns will be handled by waiving the applicable termination liability charges for a customer terminating an individual contract to seek an alternative service plan.

Conclusion

The effect on customers who have already contracted for services under the BellSouth Key Customer tariffs of this proceeding will be conditioned on the Commission's action in prior issues of this recommendation. If the Commission finds in Issues 2, 3 and 4 and its subparts, that the tariffs are lawful, this decision should have no effect on customers who have already contracted for service under the promotional tariffs.

However, if the Commission finds in Issues 2, 3 and 4 and its subparts, that the Key Customer tariffs in this proceeding are unfair, anticompetitive, or discriminatory pursuant to Chapter 364, Florida Statutes, staff believes that the customers who have contracted for service under these offerings should be given 45 days to choose to terminate or to continue their individual contracts. BellSouth should be ordered to waive the applicable termination liability charges for a customer terminating an individual contract to seek an alternative service plan. In addition, no new customers should be allowed to sign contracts under the current tariff from the date of approval of this recommendation.

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ISSUE 7: Should these dockets be closed?

RECOMMENDATION: If the Commission finds that the Key Customer tariffs of this proceeding are lawful and BellSouth has completed the tariff and contract modifications to the current Key Customer tariff that were recommended Issue 3A, these dockets should be closed. However, if the Commission finds in Issues 2, 3, or 4 and the subparts, that the Key Customer tariffs of this proceeding are unfair, anticompetitive, or discriminatory pursuant to Chapter 364, Florida Statutes, these dockets should remain open pending the disposition of further proceedings.
(BANKS, DODSON)

STAFF ANALYSIS: If the Commission finds that the Key Customer tariffs of this proceeding are lawful and BellSouth has completed the tariff and contract modifications to the current Key Customer tariff that were recommended Issue 3A, these dockets should be closed. However, if the Commission finds in Issues 2, 3, and 4 and the subparts, that the Key Customer tariffs of this proceeding are unfair, anticompetitive, or discriminatory pursuant to Chapter 364, Florida Statutes, these dockets should remain open pending the disposition of further proceedings.