PUBLIC UTILITIES COMMISSION
505 VAN NESS AVENUE
SAN FRANCISCO, CA 94102-3298

June 3, 2010

TO PARTIES OF RECORD IN CASE 08-08-008, DECISION10-06-001
MAILED JUNE 3, 2010.

On April 29, 2010, a Presiding Officer's Decision in this proceeding was mailed to all parties. Public Utilities Code Section 1701.2 and Rule 15.5(a) of the Commission's Rules of Practice and Procedures provide that the Presiding Officer's Decision becomes the decision of the Commission 30 days after its mailing unless an appeal to the Commission or a request for review has been filed.

No timely appeals to the Commission or requests for review have been filed. Therefore, the Presiding Officer's Decision is now the decision of the Commission.

The decision number is shown above.

/s/ JANET A. ECONOME for
Karen V. Clopton, Chief
Administrative Law Judge

KVC:jt2

Attachment

Decision 10-06-001 June 2, 2010

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Utility Consumers' Action Network (UCAN), Complainant, vs. MPower Communications Corp. dba TelePacific Communications fka MPower Communications aka TelePacific Holding Corp and related entities collectively "TelePacific," U5859C, Defendant.	Case 08-08-008 (Filed August 12, 2008)

Art Neill, Attorney, Utility Consumer's Action Network, for Complainant.
John L. Clark, Attorney at GOODIN, MACBRIDE, SQUERI, DAY & LAMPREY, LLP., for Defendant.

DECISION GRANTING COMPLAINT AND FINDING TELEPHONE CHARGES UNREASONABLE UNDER SECTION 451 OF THE PUBLIC UTILITIES CODE

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DECISION GRANTING COMPLAINT AND FINDING TELEPHONE CHARGES UNREASONABLE UNDER SECTION 451 OF THE PUBLIC UTILITIES CODE

In this decision, we resolve the complaint filed by the Utility Consumers' Action Network on behalf of the Edelweiss Flower Salon and its owners. Utility Consumers' Action Network alleges that defendant MPower Communications Corp.[1] acted wrongfully in billing Edelweiss Flower Salon in 2006 for telephone calls to foreign countries that were placed over Edelweiss Flower Salon's telephone lines, apparently as a result of computer hacking. Utility Consumers' Action Network alleges that Mpower's actions in billing Edelweiss Flower Salon on account of these calls – which Edelweiss Flower Salon denies were authorized – violated Sections 451, 2890, and 2896 of the Public Utilities Code.

As set forth below, we agree with Utility Consumers' Action Network that Mpower's actions violated Section 451, which requires that the rates charged and the service rules promulgated by public utilities must be just and reasonable. However, we reject the contention of Utility Consumers' Action Network that Mpower's actions constituted "cramming" in violation of Section 2890. In addition, although the information that Mpower presented to prospective customers was not a model of clarity, we also reject the contention of Utility Consumers' Action Network that the information furnished by Mpower to Edelweiss Flower Salon did not meet the requirements of Section 2896, which

[1] According to the answer, the defendant's correct corporate name (and the name to which its Commission identification number is assigned) is Mpower Communications Corp. The answer was filed on behalf of Mpower Communications Corp. and its corporate parent, U.S. TelePacific Holdings Corp., which was named as a d/b/a in the caption of the complaint. In the discussion in this decision, we refer to the defendant simply as "Mpower."

requires telephone corporations to furnish their customers with enough information so that the customers can make informed service choices.

Our decision today rests largely upon three factors: (1) the limited warning about toll fraud that Mpower gave to its new customers in 2005, which failed to mention the risks of modem hacking; (2) the measures that Edelweiss Flower Salon took in 2005-6 to secure its computer and telephone facilities, which were reasonable under the circumstances; and (3) the particular language of the parties' service agreement, which – as interpreted by Mpower – unfairly gives the company the unilateral right to determine whether the measures taken by a customer to secure the customer's telephone and computer systems are adequate. In view of the peculiar facts of this case, we are *not* deciding today the more general question of whether a telephone corporation regulated by this Commission is *ever* precluded from shifting liability for novel forms of toll fraud onto business customers.

1. Introduction

The complaint in this case was filed in August 2008. It alleged that Mpower Communications Corp. (Mpower) imposed unauthorized direct dialing charges on customers, failed to provide notice that international calls could be placed on the customers' accounts, and issued bills reflecting unpublished rates that were significantly higher than defendant's published rates. According to the complaint, these alleged acts constituted violations of Sections 451, 2890, and 2896 of the Public Utilities Code.

As explained below, the conduct at issue arises out of international calls that were placed from a telephone line used for facsimile (fax) service by the Edelweiss Flower Salon (Edelweiss), a flower shop located in San Diego, California. Originally a partnership, Edelweiss is now owned solely by

Natalja Stepanova. In 2005, Edelweiss's owners contracted with Mpower for a business telephone package that included, among other things, a DSL internet access line, a DSL modem and three so-called POTS lines.[2]

According to the complaint, Edelweiss's troubles with Mpower began in September 2006, when Ms. Stepanova received a bill for the fax line totaling $1,043.13 (before taxes, fees and surcharges), most of which was attributable to 17 allegedly unauthorized international calls made to expensive satellite facilities. An even larger bill for the fax line was issued by Mpower for October 2006. It totaled $2,180.01 and, once again, reflected charges for another group of international calls made to expensive satellite facilities, calls that Ms. Stepanova insisted were unauthorized.

Ms. Stepanova declined to pay the bills, insisted to Mpower that the international calls were unauthorized and the result of fraud, and requested that the charges for the disputed calls be removed from her bill. When the charges were not removed, Ms. Stepanova hired an attorney. The attorney thought he had reached an understanding with Mpower that if Edelweiss paid the undisputed amounts relating to the fax line, Edelweiss's telephone service would not be cut off pending completion of Mpower's investigation into the alleged fraud. However, this was apparently not Mpower's understanding, and on November 28, 2006, after Ms. Stepanova refused to pay the full amount of the bills, the service on all of her lines was disconnected. On December 20, 2006, Mpower also billed Ms. Stepanova approximately $1,350 in early termination fees as a result of her decision to cancel her service agreement with Mpower. On

[2] "POTS" stands for Plain Old Telephone Service.

January 30, 2007, Ms. Stepanova filed an informal complaint with the Commission's Consumer Affairs Branch (CAB).

In its answer, Mpower alleged that although it cannot be determined with certainty, it appears that the international calls Ms. Stepanova claims were unauthorized took place as a result of someone's hacking into the DSL modem that was connected to the computer connected to Edelweiss's fax line. Mpower also alleged that its June 2005 contract with Edelweiss specifically required the customer to secure its equipment against such unauthorized access, but that Edelweiss apparently failed to do so. Mpower also contended that the disputed calls were billed at $14.67 per minute, the lawful rate set forth on its website for Global Mobile Satellite System (GMSS) calls.[3]

2. Procedural Background

A prehearing conference (PHC) took place in this proceeding on December 3, 2008. During the discussion at the PHC, the parties agreed that as a result of informal discovery between them, there appeared to be little dispute as to the relevant facts in this case. Accordingly, Utility Consumers' Action Network (UCAN) suggested that hearings were unnecessary, and that the case should be submitted on the basis of a stipulated set of facts, followed by briefing. Mpower agreed and noted that even if some factual issues remained, they were not likely to be numerous, so they could probably be resolved through cross-motions for summary judgment supported by declarations. (PHC Transcript at 4-6.) The assigned Administrative Law Judge (ALJ) stated that he

[3] According to page 2 of the answer, publication of Mpower's GMSS rates on the company's website satisfies the applicable rules of the Federal Communications Commission (FCC).

was amenable to this approach, although he would reserve final judgment until he had read the proposed stipulation of facts and briefs.

At the conclusion of the PHC, it was agreed that the parties would submit the proposed joint stipulation of facts (or a statement that they had been unable to agree on one) on January 14, 2009.[4] It was also agreed that concurrent opening briefs would be filed on January 28, 2009, and concurrent reply briefs on February 11, 2009. (*Id.* at 23-24.)

The parties adhered to this schedule, and a scoping memo was issued on April 8, 2009.[5] After summarizing the procedural history of the case, the Scoping Memo concluded that a hearing was not necessary, because "the parties have submitted a detailed stipulation of facts and opening and reply briefs. Taken together, the stipulation and briefs are sufficient to resolve the factual issues, if any, presented by this case." (Scoping Memo at 6.)

On July 30, 2009, we issued Decision (D.) 09-07-042, which – pursuant to Pub. Util. Code § 1701.2(d) – extended the deadline for resolving this adjudicatory proceeding until February 12, 2010. On February 4, 2010, we issued D.10-02-006, which further extended the deadline for resolving this proceeding until November 19, 2010.

3. Summary of the Joint Stipulation

As noted above, the parties submitted their Joint Stipulation of Facts in mid-January 2009. Although the sections of this decision that discuss the parties'

[4] Due to computer problems, the Joint Stipulation of Facts was actually submitted the next day, on January 15, 2009.

[5] *Scoping Memo and Ruling of Assigned Commissioner and Administrative Law Judge*, issued April 8, 2009 (Scoping Memo).

contentions quote particular provisions of the Joint Stipulation at length, we summarize its key provisions below in order to give an overview of the issues. The Joint Stipulation can be accessed on the Commission's website at http://docs.cpuc.ca.gov/efile/STP/96277.pdf.

The service agreement between Mpower and Edelweiss's original owner was signed in June 2005. It stated that Mpower was to provide Edelweiss with one DSL access line and a DSL modem, as well as three POTS lines, one of which was eventually used for a fax machine. (Joint Stipulation ¶ 1.) Shortly after the service agreement was signed, Mpower also sent Edelweiss a "welcome kit," which contained information Mpower provided to new customers. The Edelweiss welcome kit contained the following warning about toll fraud:

> Please be aware that there is a new fraud trend involving international long distance. If you use your own voicemail and/or PBX[6] system and it has a paging feature, it may be susceptible to hackers. These hackers are redirecting voicemail pages to fraudulent telephone numbers in various foreign countries. If you do not take steps to safeguard your voicemail and/or PBX systems from this potential threat, you may be held responsible for fraudulent long distance calls. We encourage you to contact your supplier immediately to protect your business. (*Id.* ¶ 1, Exh. B.)

In early September 2006, Mpower sent Edelweiss a bill that included charges for 17 international calls made through GlobalStar satellite facilities from the flower shop's fax line. The calls were billed at $14.67 per minute and totaled $1,043.13 (before taxes, fees and surcharges). (*Id.* ¶ 5.) On September 11, 2006, Ms. Stepanova contacted Mpower, disputed the charges, and requested a credit for the amount of the calls. On the same date, Mpower personnel checked

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6 "PBX" stands for private branch exchange.

Edelweiss's call records, which showed that the disputed calls had been directly dialed over the flower shop's fax line. (*Id.* ¶¶ 7, 9.)

Ms. Stepanova called Mpower again on September 20, 2006 to inquire how much of a credit she would receive on the disputed calls. She was told that pursuant to a new policy, she would not be receiving any credit for the allegedly fraudulent calls. She was also asked to fax a written complaint about the billing dispute to Mpower, which she did later that day. (*Id.* ¶ 11.) On September 29, 2006, Ms. Stepanova was again advised by phone that she would not receive a credit for the disputed calls, and that her service would be disconnected if she did not pay the bill promptly. (*Id.* ¶ 12.)

On or about October 1, 2006, Ms. Stepanova received another bill for the Edelweiss fax line that included charges for 11 more international calls placed through GlobalStar satellite facilities. The satellite calls were charged at $14.67 per minute and totaled $2,180.01 (before taxes, fees and surcharges). On October 9, 2006, Ms. Stepanova faxed another written complaint to Mpower, which disputed the charges on the October bill as well as those that had appeared on the September bill. (*Id.* ¶¶ 13, 15.)

The next day, October 10, Mpower began a review of the Edelweiss account. Later that day, Ms. Stepanova telephoned Mpower about the disputed charges and asked to be connected with a supervisor. She was told the account review would take some time and was placed on hold, but she apparently hung up before Mpower's staff could get back to her. (*Id.* ¶ 16.)

Within the next week, Ms. Stepanova hired an attorney. On October 17, the attorney spoke with Elaine Calloway in Mpower's fraud department about the billing dispute, and also sent a letter reiterating that no one at Edelweiss had

made the disputed calls. The attorney also enclosed a check for the undisputed amounts due. (*Id.* ¶ 17.)

On October 20, 2006, shortly after receiving the attorney's letter, Mpower's fraud department began an investigation of the alleged fraud. The Joint Stipulation states the following about the fraud investigation:

> The fraud department's review indicated that if the calls were not completed by persons located at [Edelweiss's] premises, then it was likely that the calls were made through a fraudulent scheme. In the following months, the fraud department noted that six other Mpower customers had made similar complaints to Mpower regarding allegedly unauthorized charges for calls completed to GlobalStar satellite telephone numbers. In addition, during conference calls with other carrier representatives who participated with Mpower in an informal industry security task force, Mpower learned that customers of other carriers had been similarly affected by an alleged fraudulent scheme to complete calls to GlobalStar numbers . . . (*Id.* ¶ 19.)

Mpower also contacted GlobalStar, which stated that its call detail records did not match those on which Mpower had based its bills to Edelweiss. Nonetheless, after this contact, Mpower received no further complaints from customers about fraudulent calls placed to GlobalStar numbers. (*Id.* ¶ 20.)

The Joint Stipulation states the following about Ms. Stepanova's claims that the disputed calls were not made from her premises, and the evidence Mpower has unearthed on that issue:

> The Customer has not identified the root cause of the allegedly fraudulent calls; however, Ms. Stepanova has asserted that none of the Customer's authorized employees made the disputed satellite calls and that several of the calls were made outside of normal business hours and on days when the Customer's shop was closed. Further, none of the phone numbers listed for the disputed charges on the September 1 and October 1, 2006 bills had ever previously been called by the Customer or Edelweiss Flowers, and

> Ms. Stepanova asserts that neither she nor other persons having authorized access to the Customer's service during the period in question had knowledge of these phone numbers prior to their appearance on the Customer's phone bill. (*Id.* ¶ 21.)

The Joint Stipulation also offers the following explanation of how Mpower thinks the alleged fraud may have occurred:

> Based on its investigation, Mpower believes that if the calls billed to the Customer were not made by persons located at the Customer's premises, it is most likely that they were completed through "modem hacking" (i.e., manipulating a telephone customer's modem connection to complete calls). The exact nature of any modem hacking that may have occurred in the Customer's case, as well as in the six other affected customers' cases, is unknown. One reported method involves the use of a high speed internet connection by an outside third party to access a computer and dial out calls through a POTS line that is connected to the computer, through a fax modem or dial-up Internet modem. Based on the equipment in use at the Customer's premises at the time the satellite calls for which Mpower billed the disputed charges, it is likely that this would have been the method used to make any fraudulent calls . . . (*Id.* ¶ 22.)

The Joint Stipulation also acknowledges that after pursuing Ms. Stepanova to pay the disputed charges, Mpower suspended her service for nonpayment on November 28, 2006. (*Id.* ¶¶ 18, 23, 24.) Two days later, Ms. Stepanova requested that her agreement be terminated because she did not want to continue paying for service that had been suspended. (*Id.* ¶ 25.) On December 20, 2006, Mpower billed Ms. Stepanova for $1,349.58 in early termination fees as a result of her decision to cancel her service agreement with Mpower. (*Id.* ¶ 28.)

Mpower continued to pursue Ms. Stepanova for payment after her service agreement was terminated, and even after she had filed an informal complaint with the CAB on January 30, 2007. On February 27, 2007, the Law Office of Scott & Associates sent Edelweiss a letter on behalf of Mpower demanding $5,132.88 in

payment on the past due accounts, and noting that if payment was not made, "legal action may be initiated." (*Id.* ¶ 30; Exh. K.) The Joint Stipulation does not indicate whether Ms. Stepanova paid the amount demanded in response to this letter.

4. Are UCAN's Claims Pre-empted by Federal Law?

A. Mpower's Arguments

To defeat UCAN's claims that violations of Pub. Util. Code §§ 451, 2890 and 2896 have occurred here, Mpower relies on the provisions of its Master Service Agreement with Edelweiss, as well as on the warning that was included in the "welcome kit" Mpower furnished to Edelweiss in 2005.

As to the Master Service Agreement, Mpower points out that item 5 of the Installation Policy and Procedures included in this agreement (a copy of which is attached to the Joint Stipulation as Exhibit A) provides that the "Customer acknowledges that it is the Customer's responsibility to adequately secure its computer network, circuits, and customer premises equipment from unauthorized access by 3rd parties." Mpower argues that Edelweiss failed to secure its equipment adequately, and that it is therefore reasonable to hold Edelweiss liable for the allegedly unauthorized calls placed through its facilities.[7]

Mpower also relies on the warning to secure equipment that appeared in the welcome kit that Mpower furnished to its new customers. As noted above, that warning urged new customers to "please be aware that there is a new fraud trend involving international long distance. If you use your own voicemail and/or PBX system and it has a paging feature, it may be susceptible to hackers.

These hackers are redirecting voicemail pages to fraudulent telephone numbers in various foreign countries." The warning also stated that if the customer did not take steps to protect itself from this fraud, "you may be held responsible for fraudulent long distance calls."

In its briefs, Mpower argues that item 5 in the service agreement and the welcome kit warning demonstrate not only that UCAN's claims under the Public Utilities Code are without merit, but also that these claims are preempted by federal law. Specifically, Mpower argues that this case is controlled by the decision of the FCC in *Directel v. AT&T Corp.*, 11 FCC Rcd 7554 (1996), as well as a predecessor FCC decision, *Chartways Technologies, Inc. v. AT&T Communications*, 8 FCC Rcd 5601 (1993). Mpower characterizes these decisions as follows:

> Mpower's billing and collecting such charges from the customer clearly conformed to long-standing FCC policy in cases involving toll fraud carried out by unknown persons through unauthorized remote access to the outbound calling capabilities of customers' networks and equipment. In *Directel v. AT&T* (1996) 11 FCC Rcd 7554 . . . , which involved PBX hacking . . . the FCC directly addressed tariff provisions that placed the cost burden on the customer for fraudulent calls. The complainant in that case contended that such provisions were unjust and unreasonable in violation of 47 U.S.C. § 201(b). The FCC disagreed. Citing *Chartways*, supra, as controlling, the FCC concluded, "In the absence of evidence that the customer lacked the ability to control calling through its PBX or that AT&T was in a position to restrict access to and egress from the PBX, or had otherwise acted in negligent manner with regard to the calls," such provisions properly place liability on the customer. (*Directel* at ¶¶ 17-19, 20.) (Mpower Opening Brief at 12-13; citation omitted.)

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[7] Later in this decision, we will consider at length UCAN's argument that item 5 of the Installation Policy and Procedures is unconscionable under California law.

In view of what it considers the clear federal policy expressed in *Directel*, Mpower argues that UCAN's state law claims are preempted by federal law:

> In light of the FCC's having adopted [the] explicit policy [set forth in *Directel*] pursuant to its authority over rates, terms, and conditions of interstate and international telecommunications services, state "cramming" laws or regulations are preempted to the extent that they would force Mpower to bear the burden of toll fraud under the circumstances of this case. "Under the obstruction strand of conflict preemption, an aberrant or hostile state rule is preempted to the extent it actually interferes with the 'methods by which the federal statute was designed to reach [its] goal.' (*Ting v. AT&T* (9th Cir. 2003) 319 F.3d 1126, 1137, quoting *International Paper Co. v. Ouelette* (1987) 479 U.S. 481, 494 . . .) Clearly, holding Mpower responsible for any toll fraud suffered by the customer cannot be reconciled with the FCC's opposite determination in *Directel* that carriers may hold customers responsible for toll fraud. (*Id.* at 15.)

B. UCAN's Arguments

In its briefs, UCAN argues that the *Directel* and *Chartways* cases are distinguishable and do not establish a policy of federal preemption under the facts to which the parties have stipulated. UCAN argues that toll fraud perpetrated through a PBX system – the type of fraud at issue in *Chartways* and *Directel* – has long been a well-known risk, whereas the modem hacking that apparently took place here is much more sophisticated technologically:

> [R]ather than simply exploiting a well-known weakness of a simple telephone line switching system by simply dialing a phone number, the details of alleged modem hacking events are complicated and still largely unknown. The known schemes involve, by way of IP communications sent into the customer's premises by Mpower, (1) circumventing and exploiting the DSL modem supplied to the customer by Mpower, (2) somehow manipulating the customer's computer software to access attached hardware, (3) manipulating the attached hardware to make calls using the customers' service. The modem hacking Mpower suggests is highly complicated, highly technical fraud. In contrast, PBX hacking involves none of [the]

> types of circumvention and manipulation involved in modem hacking." (UCAN Reply Brief p. 20.)

UCAN also points out that the fraud warning given to Edelweiss when it first became an Mpower customer was concerned solely with PBX and voice-mail service; it did not warn the new customer about the possibility of toll fraud perpetrated through modem hacking. UCAN emphasizes that the 2005 warning quoted above tells customers only that if they have their "own voicemail and/or PBX system and it has a paging feature, it may be susceptible to hackers," who can "redirect[] voicemail pages to fraudulent telephone numbers in various foreign countries."

UCAN argues that this warning was insufficient to alert Edelweiss to the kind of fraud that occurred in this case, in which the modem that Mpower had supplied to Edelweiss was apparently hacked so that international calls to GlobalStar phone numbers could be placed on Edelweiss's fax line.

C. Discussion

In analyzing whether Edelweiss's state law claims are preempted by federal law, we think it is useful to begin by reviewing the parties' stipulation as to how the telephone package that Edelweiss had purchased from Mpower was configured. On this question, the Joint Stipulation states:

> During the period from August 1, 2006 through August 31, 2006, a Brother MFC 7220 combined printer, scanner, and fax machine ("fax machine") was connected at the Customer's [*i.e.*, Edelweiss's] premises to one of the POTS lines provided by Mpower. This POTS line was identified by telephone number 858-751-0376 (the "fax line"). The fax machine was also connected at the Customer's premises to the DSL Internet access line. Ms. Stepanova asserts that Windows Firewall and another antivirus program, which Ms. Stepanova believes was Norton Antivirus, was installed on the computer. The Customer asserts that none of the Customer's lines was connected to a PBX and that the customer did not have

> voicemail; Mpower has no basis for a belief to the contrary. (Joint Stipulation, ¶ 4.)

Based on these facts and the cases discussed below, we do not believe that the FCC decisions cited by Mpower establish the sweeping federal policy that Mpower claims. On the contrary, the FCC's brief decision in *Directel* – the principal federal case on which Mpower relies – emphasized that the dispute there was being decided on the pleadings, since the complainant had submitted no declarations, affidavits, or other evidence concerning the measures it had taken to secure its PBX systems against unauthorized use. On this question, the FCC said:

> With regard to its alternative claim of unreasonableness under Section 201(b) of the [Communications] Act, Directel has presented no facts to support a finding that the subject tariff provisions are unlawful within the meaning of Section 201(b). Directel's own admission that toll-fraud occurrences at both the Westerville and Cincinnati PBXs ceased promptly after its PBX vendors took certain unspecified preventive measures belies any claim by Directel that it lacked the ability to control access to and egress from the PBXs and that such control was the responsibility of AT&T. Further, Directel has provided no information that would indicate whether, and if so, to what extent, it discussed PBX security measures with its PBX vendors or whether measures were put in place to restrict access to the PBX facilities at the time of their installations. Moreover, as was the case in *Chartways*, Directel has failed to cite any authority or provide any persuasive argument to support a finding that AT&T had any affirmative duty to warn Directel about toll-fraud risks, nor has it alleged specific facts that might indicate that AT&T acted unreasonably in its communications with Directel at the time the fraudulent calls occurred. (11 FCC Rcd at 7562-63; footnote omitted.)

We also agree with UCAN that the warning to new customers that appeared in Mpower's welcome kit dealt solely with toll fraud perpetrated through PBX and voice-mail service. As noted above, the warning told

customers that "if you use your own voicemail and/or PBX system and it has a paging feature, it may be susceptible to hackers." The warning also emphasized that "if you do not take steps to safeguard your voicemail and/or PBX systems from this potential threat, you may be held responsible for fraudulent long distance calls." (Joint Stipulation, Exh. B.) Modem hacking is not mentioned in the welcome kit warning.[8]

Although UCAN has not cited any authority to support its claim that hacking a computer modem is substantially more complicated than hacking a PBX, a review of applicable literature we have located lends considerable support to this assertion. First, it is clear that warnings about the risk of toll fraud perpetrated through PBXs and voice mail systems have been around since the mid-1990s. For example, a short 1998 article entitled *[ISN] Toll Fraud: The Crime of the 90's* warned readers that there were several ways a PBX could be compromised, including "crack[ing] the authorization codes for the remote access feature, . . . [which] allows a caller to dial into the system, enter an authorization code and get an outbound line." Another vulnerability of PBX

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[8] The parties' stipulation states that once a customer complains to Mpower about fraud, the customer is provided with a copy of Mpower's then-current "fraud guideline," which "instructs the customer to work with the customer's vendors to identify the root causes of the alleged fraud." (Joint Stipulation, ¶ 35.) The Joint Stipulation also notes that while the fraud guideline Mpower provided to Ms. Stepanova is no longer available, it did not mention modem hacking (although the current guideline on Mpower's website does). (*Id.*; Exh. O.)

For purposes of our analysis here, the contents of the fraud guideline are irrelevant. The Joint Stipulation notes that the guideline was not provided to Ms. Stepanova until October 30, 2006, more than six weeks after she had first complained about the allegedly unauthorized calls. In determining whether the security measures that Ms. Stepanova took were reasonable, we must look to the nature of the fraud warning she was given in the 2005 warning kit; *i.e.,* before the cat was out of the bag.

systems, the article said, was the remote access port, which "allows a remote user, including the PBX vendor, to access the system for maintenance. The maintenance ports have standard user IDs. The standard IDs are well known to the hacker community."[9]

In recent years, modems have become ubiquitous in the public switched telephone network. However, as a recent treatise on information security notes, modems can be hacked through software programs known as "war dialers." The treatise defines war dialing as follows:

> *War dialing* is the action of dialing a given list or range of phone numbers and recording those that answer with handshake tones – a predetermined signal used to establish connections between two terminal devices (and so might be entry points to computer or telecommunications systems). It can detect modem, fax or private branch exchanges (PBXs) tones and log each one separately for nefarious purposes. **III HANDBOOK OF INFORMATION SECURITY** (H. Bidgoli, ed., John Wiley & Sons, 2006), (emphasis in original) at 31 (hereinafter *Security Handbook*).

As noted above, Mpower does not dispute UCAN's assertion that two security systems, Windows Firewall and an antivirus program, had been installed on Edelweiss's computer in 2006. (Joint Stipulation, ¶ 4.) However, the *Security Handbook* points out that while such measures can provide helpful security for home office and other small systems,[10] even apparently well-designed firewalls can be vulnerable to hacking:

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[9] The 1998 article can be found at http://lists.jammed.com/ISN/1998/11/0087.html.

[10] The *Security Handbook* notes that in small office and home office systems, "often digital subscriber line (DSL) or cable modems include firewall functionality because of their 'always on' connection status." III *Security Handbook* at 511.

> [T]o ensure security, firewalls are [often] added to protect the internal network. However, this is not absolutely safe. If the firewall is not carefully configured, it may provide a false sense of security and permit outsiders to hack internal systems. An inadequately configured firewall can make internal hosts visible to the outside world, may pass traffic from untrusted hosts and ports that are supposed to be blocked, and may provide an incorrect proxy server that lets malicious traffic into the internal network. Insiders can invoke malicious software to leak information or import malicious codes. Administrators and users may install tools on systems so that they can work remotely and conveniently. These tools may become backdoors for outside intruders." (*Id.* at 80.)[11]

Even though the security measures that Edelweiss installed were not effective against the hacking that apparently took place in this case, this does not mean that Edelweiss would automatically be liable under federal law for the satellite calls that the hacking made possible. In a line of decisions dating back to the mid-1990s, the FCC and the federal courts have recognized that business

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[11] According to the *Security Handbook*, it has been estimated that 80% of successful network attacks either penetrate or avoid firewall security. In order to be effective, a properly-configured firewall must typically be used with intrusion detection/prevention systems, vulnerability assessment technology, and antivirus technology in order to achieve a complete perimeter security solution. (*Id.* at 502-03.)

One reason that firewalls can be penetrated or avoided with relative ease is that there are apparently no uniform standards for them:

> Another difficulty with firewalls is that there are no standards for firewall types, configuration, or interoperability. As a result, users must often be aware of how firewalls work to use them, and owners must be aware of these issues to evaluate potential firewall technology purchases. Many different devices can all be called firewalls, but that does not imply that these devices provide identical or even similar functionality. (*Id.* at 506.)

As the discussion in the text makes clear, we think it is expecting too much of a small business customer to be aware of these limitations. To most laymen and small business operators, a commercial firewall product seems like good computer security.

customers should not be held liable for unauthorized calls where the customer has used reasonable measures to protect its system against hacking, even if these measures prove to be unsuccessful.

The first of these decisions was *United Artists Payphone Corp. v. New York Telephone Company*, 8 FCC Rcd 5563 (1993). In that case, United Artists (UA) contended that New York Telephone Company (NYT) and AT&T had acted unlawfully in attempting to collect charges for unauthorized interstate and international calls that were either originated or accepted at UA's payphones. Among other arguments, UA contended that it was not a customer of AT&T under the applicable federal tariff, because (1) UA had not presubscribed its payphones to AT&T, and (2) UA had taken affirmative steps to control unauthorized operator-assisted and direct-dialed calls to and from its payphones. AT&T, while conceding that UA had not presubscribed its payphones, argued that UA should be deemed to have "constructively ordered" AT&T service because the security measures that UA put in place were ineffective.

The FCC agreed that the question of whether UA had implemented adequate security measures was crucial to resolution of the constructive ordering issue. The FCC described UA's security precautions as follows:

> The record shows that UA implemented a number of measures designed to control potentially fraudulent operator-assisted or direct-dialed calling. First, when ordering public access lines from NYT, UA told NYT that the payphone lines in question were to have no primary interexchange carrier . . . Further, if operator-assisted interexchange calls did originate or terminate at UA payphones, the originating line and billed number screening services that UA ordered from NYT for all of its payphone lines were intended to inform operator service providers of any billing restrictions on those lines. UA also ordered NYT's 10XXX Restrict service, which was

> intended to block both operator-assisted and direct-dialed 10XXX sequences . . . In addition to the network-based fraud control services it ordered, UA programmed its payphones to block operator-assisted and direct-dialed calling outside of the local area. Beyond all of these preventative steps, UA monitored calling from its phones and regularly reported any apparently fraudulent calling to NYT and AT&T. (8 FCC Rcd at 5566; footnotes omitted.)

The FCC then held that because these preventive measures were reasonable under the circumstances, UA could not be considered a constructive customer of AT&T:

> Based on the record before us, we find that UA took reasonable steps to secure its payphones against fraudulent calling and that it therefore did not constructively order the services used to make the calls at issue. Because UA did not intentionally or constructively order services from AT&T, UA was not AT&T's customer and cannot be held liable for the disputed charges. (*Id.*; footnote omitted.)

In recent years, the federal district courts have shown considerable skepticism toward claims of constructive ordering, in part because of the growing sophistication of hackers. For example, in *AT&T Corp. v. Midwest Paralegal Services, Inc.*, 2007 U.S. Dist. LEXIS 33546, a U.S. District Court in Wisconsin rejected AT&T's argument that a paralegal firm had constructively ordered service from AT&T when the firm's PBX system was hacked and over $10,000 worth of unauthorized calls were made to the Philippines. The court noted that each extension on the paralegal firm's PBX system was encrypted with a four-digit code that the caller was required to enter in order to access the extension's voice-mail. After reviewing prior authority (including *United Artists Payphone*), the court concluded that this security measure was sufficient to defeat AT&T's motion for summary judgment based on the constructive ordering theory:

> AT&T asserts that Midwest Paralegal, similar to the defendants in *Community Health Group*, [12] failed to adequately institute affirmative safeguarding measures to protect its telephone system from fraud and abuse. However, the circumstances in *Community Health Group* substantially differ from those in this case. In *Community Health Group*, the defendants failed to present any evidence 'showing that they acted in any way to control the

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12 As indicated by the reference in *Midwest Paralegal* to *AT&T Corp. v. Community Health Group*, 931 F.Supp. 719 (S.D. Calif. 1993), some cases have held that businesses victimized by toll fraud should be considered constructive customers of AT&T where the businesses failed to implement reasonable measures to prevent unauthorized use of their telephone systems. In *Community Health Group*, the district court concluded that the defendant should be liable for unauthorized calls made from its PBX system, because even though the defendant claimed it had "relied on the anti-fraud expertise" of Centrex Equipment Associates and Pacific Bell to implement security measures, the health group had "provide[d] no explanation of how it relied on Centrex and PacBell, and no evidence that Centrex or PacBell had represented to [defendant] that they would institute any anti-fraud measures" until after the unauthorized calls had been discovered. In addition, the court noted that defendant had presented no other evidence of "affirmative safeguarding measures" that, under *United Artists Payphone*, "the FCC has recognized as a valid defense to a 'constructive ordering' allegation." (931 F.Supp. at 723.)

Similarly, in *American Telephone and Telegraph Co. v. Jiffy Lube International, Inc.*, 813 F. Supp. 1164 (D. Md. 1993), the court rejected the argument that Jiffy Lube should not be liable for unauthorized calls made by hacking its PBX system. Jiffy Lube's security was weak; the court noted that in order to use the PBX's remote access feature, one needed only to know the relevant 800 number. Once remote access had been obtained, the only additional step necessary to make international calls was to enter an access code, which was the word "LUBE". The court noted Jiffy Lube's admission that both the 800 number and the access code had been posted on a computer bulletin board for hackers. (*Id.* at 1165.)

In denying Jiffy Lube's motion for summary judgment motion and granting AT&T's, the district court noted that "Jiffy Lube ignores the fact that it created the vehicle and mechanism by which those long distance calls became possible," and also rejected the argument that "in terms of modern technology and knowledge of the same," AT&T was better equipped than its customers to "offer protection against 'computer hackers'." (*Id.* at 1167-68.)

> unauthorized charging of AT&T [long distance] calls to their system before the fraud occurred.' [931 F. Supp. at 723.] Here, Midwest Paralegal submits evidence demonstrating that, at the time the unauthorized calls occurred, its telephone system required a caller to enter a four-digit access code before the caller could access Midwest Paralegal's network remotely . . . In addition, Midwest Paralegal submits the affidavit of Gierl, the technician who installed and services Midwest Paralegal's telephone system. Suggesting that Midwest Paralegal took reasonable steps to secure its telephone system, Gierl stated that the call-in feature on Midwest Paralegal's telephone system was a standard feature in voice mail systems in business settings, and that based on his training and experience, the manner in which the unauthorized caller gained access to Midwest Paralegal's telephone system required an extremely high level of sophistication and knowledge in the telecommunications field. (2007 U.S. Dist. LEXIS 33546 at *20-*21.)

In *AT&T Corp. v. The Ridge Company*, 2008 U.S. Dist. LEXIS 48319, a U.S. District Court in Indiana reached a similar conclusion. In the Indiana case, hackers had gained access to the Ridge Company's telephone system through its voicemail feature, and over $27,000 of unauthorized calls were placed to countries in Africa and the Middle East over AT&T lines. AT&T argued that as a result of the hacking, Ridge should be deemed to have constructively ordered service from it. Ridge argued that it should not be considered a constructive AT&T customer because of the security measures it had implemented, which included assigning a four-digit pass code to each individual voice mail account, a pass code that had to be changed every 30 days to gain access to the account. In granting Ridge's motion for summary judgment and denying AT&T's, the court said:

> AT&T's submissions never quite articulate why [Ridge's] precautions against unauthorized access fell short of reasonable. AT&T notes that stronger precautions were taken after the unauthorized use (six-digit pass codes were instituted), but

> subsequent remedial measures don't prove that earlier measures were unreasonable. *See* WIGMORE, EVIDENCE § 283, at 175 (Chadbourn rev. 1979). (2008 U.S. Dist. LEXIS 48319 at *8.)

When read together, *United Artists Payphone*, *Midwest Paralegal*, and *AT&T v. Ridge Company* suggest to us that it is very unlikely Edelweiss would be held liable under federal law for the long-distance calls at issue in this case. As noted above, Mpower does not dispute Edelweiss's assertion that both Windows Firewall and an antiviral program were installed on Edelweiss's computer in 2006. Further, even though the *Security Handbook* indicates that experts knew in 2006 that such measures do not provide complete security against hacking, it is unreasonable to expect small business customers like Ms. Stepanova and Edelweiss to have been familiar with these limitations.

Thus, based on the facts to which the parties have stipulated, we think UCAN has demonstrated that in 2006, Edelweiss took reasonable measures under the circumstances to secure its computer and telephone systems. In view of these measures and the cases described above, we conclude that (1) it is unlikely Edelweiss would be held liable under federal law for the unauthorized calls that occurred here, and (2) UCAN's state law claims against Mpower are not preempted by federal law.

5. Did MPower's Attempts to Bill and Collect from Edelweiss for Unauthorized International Calls Violate Pub. Util. Code § 2890?

As noted above, one of UCAN's principal contentions here is that Mpower's insistence on billing for the disputed international calls violates subsections (a) and (e) of Pub. Util. Code § 2890, which is popularly known as the "anti-cramming" statute. Subsection (a) of § 2890 provides that "a telephone bill may only contain charges for products or services, the purchase of which the

subscriber has authorized." Subsection (e) of § 2890 speaks to a carrier's obligations after a customer disputes a charge:

> If any entity responsible for generating a charge on a telephone bill receives a complaint from a subscriber that the subscriber did not authorize the purchase of the product or service associated with that charge, the entity, not later than 30 days from the date on which the complaint is received, shall verify the subscriber's authorization of that charge or undertake to resolve the billing dispute to the subscriber's satisfaction.

In its papers here, UCAN contends that Mpower violated § 2890 by billing Edelweiss for the unauthorized long-distance calls even after Edelweiss insisted the calls had not been made from its premises.

A. UCAN's Contentions

UCAN's argument that Mpower has violated § 2890 rests on several foundations. First, although UCAN concedes that § 2890 (d)(2)(D) provides that "evidence that a call was [direct] dialed is prima facie evidence of authorization," UCAN argues that two factors serve to overcome that presumption in this case. The first factor is that, as the Joint Stipulation indicates, Mpower acknowledges it received similar complaints about unauthorized satellite calls from six other customers, and that through its participation in an industry task force, it learned these calls were most likely the result of hacking. (UCAN Opening Brief at 13.) The second factor is that Ms. Stepanova vigorously denies the calls were made from her shop, a denial supported by the facts that (a) the disputed numbers had never appeared on her bills before, and (b) the calls were made outside of normal business hours. (*Id.* at 15-16.)[13] Based on these factors, UCAN argues that the

[13] Although UCAN asserts that the disputed calls were made outside of normal business hours, the Joint Stipulation acknowledges only that the calls were made to

Footnote continued on next page

presumption in § 2890 (d)(2)(D) has been rebutted, and that the burden therefore shifts to Mpower to prove that the disputed calls were authorized.

The second foundation for UCAN's cramming argument is Commission precedent, especially D.02-10-059, our decision concerning an investigation into the billing practices of Qwest Communications Corporation (Qwest) and one of its subsidiaries. In that investigation, Qwest challenged a report prepared by Pacific Bell and relied on by our Consumer Services Division (CSD) to establish the number of cramming complaints lodged against Qwest and its subsidiary during the relevant time period. In rejecting Qwest's argument that only a handful of crams had been proven, we said:

> Qwest believes that when the customer denies making the call, or has a complaint regarding a calling card billing, these are not crams but rather billing disputes. However, § 2890 provides that a customer may only be billed for authorized charges for products and services. If a customer denies making the call, this is a complaint for an unauthorized charge. (D.02-10-059 at 35.)

B. MPower's Contentions

Mpower argues that the term "authorize" is ambiguous as it is used in § 2890, and that since the statute can be read to support either UCAN's or Mpower's interpretation, the Commission should construe the statute in a way that avoids conflict with federal law:

> In this case, Mpower and the complaining customer were parties to an agreement that specifically included Mpower's provision of international long distance service as one of the services to be furnished to the customer. In Mpower's view, Mpower was thus authorized by the customer to provide such service. UCAN, on the

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numbers that had never appeared on Edelweiss's or Ms. Stepanova's bills before. (Joint Stipulation, ¶ 21.)

> other hand, will undoubtedly contend that, notwithstanding the agreement that the service to be provided . . . included international toll service[,] and that customer is responsible for protecting the customer's computer network . . . and other . . . equipment from unauthorized access by third parties, the customer did not authorize (within the meaning of § 2890) the specific international calls that were placed over the customer's lines[,] or Mpower's billing the customer therefor . . .
>
> There is nothing in the language of § 2890 that resolves this readily apparent ambiguity . . . except that [UCAN's] construction would cause the statute to run afoul of the Supremacy Clause of the United States Constitution to the extent that the statute conflicts with the FCC's adopted policy regarding assignment of responsibility for toll fraud. Thus, given the choice between these two constructions, Mpower submits that the construction that avoids preemption is the appropriate one . . . (Mpower Opening Brief, pp. 18-19.)

Mpower also argues that what UCAN is really advocating here is a requirement the carrier verify that each individual call is authorized, and that such a requirement would be unworkable:

> The hurdle that UCAN must, but cannot, overcome is the fact that the affected customer did authorize Mpower to provide international calling, which is the service for which the disputed charges were assessed. Further, there is no evidence that Mpower failed to follow any applicable verification requirements . . .
>
> To hold, as UCAN contends, that separate authorization and verification is required for each individual call that is made from a customer's premises would be unworkable. To sustain any billed charge, a carrier would have to establish and impose some sort of per-call verification process, which obviously would be extremely burdensome on both the carrier and any customer desiring to make a long distance call. Otherwise, as UCAN argues, a customer could avoid any charges simply by denying that the customer made the call and denying that permission was given to the customer's . . . employee[] or any other person to make the call . . . (Mpower Reply Brief at 9-10.)

C. Discussion

Although we think both parties have taken extreme positions on the cramming issue, we believe that on balance, the facts to which they have stipulated demonstrate that Mpower did meet the minimum obligations that § 2890 imposes on it. However, we also think the record shows that Mpower was very slow to conduct an adequate investigation into Ms. Stepanova's complaints that the international calls at issue were unauthorized. Once Mpower did conduct such an investigation, it became apparent that similar complaints from other customers, as well as Edelweiss's calling history, lent considerable credence to Ms. Stepanova's allegations of fraud. Under these circumstances, Mpower should have reevaluated its decision not to give Ms. Stepanova a credit for the disputed calls.

Before examining the evidence concerning the disputed calls, it is appropriate to address Mpower's federal preemption argument. As noted in the summary of its position above, Mpower asserts that to accept UCAN's interpretation of § 2890 would "conflict[] with the FCC's adopted policy regarding assignment of responsibility for toll fraud." (Mpower Opening Brief at 19.) However, as we have demonstrated in Section IV.C. of this decision, the policies toward toll fraud that the FCC and the federal courts have articulated in their decisions are not what Mpower claims. Contrary to Mpower's assertions, we believe that federal cases dating back to the mid-1990s have recognized that where, as here, a small business customer has used reasonable measures to protect its telephone system against hacking, the customer should not be held liable for unauthorized calls, even if the anti-hacking measures prove to be unsuccessful. Thus, the federal decisions do not serve to preempt anti-cramming statutes such as § 2890.

We begin our analysis under § 2890 with the question of authorization. Although it is not conspicuously stated on the Service Order Form included in the service agreement that Edelweiss signed, the Service Order Form does indicate, as Mpower notes in its opening brief, that Mpower was to be Edelweiss's "New Carrier (PIC)" for international calling. The Service Order Form also states that "LD Rates are domestic rates, except for Alaska and Hawaii; International rates vary by country and are identified on the Mpower website." (Joint Stipulation, Exh. A; Mpower Opening Brief at 4.)[14] Thus, the underlying service agreement between Mpower and Edelweiss does provide that the former is to be the latter's carrier for any international calls, and states how the rates for such calls can be determined.[15]

In addition to this written authorization, the Joint Stipulation states that on September 11, 2006 – the first date on which Ms. Stepanova contacted Mpower to complain about unauthorized charges on her September bill – Mpower verified from its call records that the disputed calls had been direct-dialed from Edelweiss's fax line. (Joint Stipulation, ¶ 9.)

However, the general authorization to provide international service that Edelweiss's owners signed is not sufficient to defeat UCAN's claim of a § 2890 violation. As UCAN points out on pages 12-13 of its opening brief, D.02-10-059 rejected the argument that authorization to provide a particular type of service

[14] It took considerable effort on our part to decipher this language in the Service Order Form included in the Joint Stipulation, since the copy provided was nearly illegible.

[15] Although the Joint Stipulation is silent on the subject, we assume that at the time the service contract was signed, there was also some oral discussion between Mpower's sales agent and Edelweiss's personnel that made clear international calling was included within the telecommunications package Edelweiss was purchasing.

means that a customer cannot challenge the validity of an individual call. In response to such an argument from Qwest, the Commission stated:

> According to Qwest, CSD has not met its burden of proof because § 2890(e)(D) provides, with regard to direct dialed telecommunications services, evidence that a call was dialed is prima facie evidence of authorization. *However, here, we have a complaint from the subscriber rebutting that presumption.* Moreover, this same statute provides that in the case of a dispute, there is a rebuttable presumption that an unverified charge for a product or service was not authorized by the subscriber and that the subscriber was not responsible for that charge. (D.02-10-059, p. 35, n. 35; emphasis added.)

UCAN notes that § 2890 makes rebuttable the presumption that direct-dialed calls are authorized, and argues that it has presented sufficient evidence to overcome that presumption here. As noted above, the Joint Stipulation states that Mpower received similar complaints about unauthorized international calls from at least six other customers, and learned through its participation in the "informal industry security task force" that other carriers' customers had also been victims of this fraud. (Joint Stipulation ¶ 19.) Further, once Mpower commenced a substantive investigation into the Edelweiss matter, it was able to determine from its call detail recordings that none of the numbers relating to the disputed charges had ever been called previously either by Edelweiss or Ms. Stepanova. (*Id.* ¶ 21.) UCAN argues that on the basis of these facts, the burden should shift to Mpower to show that the calls were authorized, that Mpower cannot do so, and thus that a violation of § 2890 has occurred.

Although UCAN's argument has considerable appeal, we decline to adopt it because the facts on which UCAN is relying apparently came to light only *after* Mpower's fraud department commenced a special investigation into Ms. Stepanova's allegations. According to the Joint Stipulation, this special fraud

investigation began on October 20, 2006, three days after Ms. Stepanova's attorney had sent a letter to Mpower (1) reiterating that no one at Edelweiss had made the disputed calls, and (2) enclosing a check for undisputed charges. Thus, the fraud investigation began about five and one-half weeks after Ms. Stepanova had first contacted Mpower to protest the unauthorized charges on her September bill.

As noted above in Section 3, the Joint Stipulation refers to one other brief investigation Mpower undertook. On October 10, 2006, the day after Ms. Stepanova had faxed a second complaint to Mpower about the charges for unauthorized calls, "Mpower's staff began a review of the Customer's account at 11:25 a.m." (*Id.* ¶ 16.) Less than 20 minutes later,

> Ms. Stepanova called Mpower to inquire about the disputed charges and asked to be connected to a supervisor. Ms. Stepanova was advised by the customer service representative that time was needed to review the account and was placed on hold, but the connection was inexplicably interrupted before Mpower could respond to her inquiry. (*Id.*)

The Joint Stipulation does not state what, if anything, Mpower did on October 10 to complete the account review its staff had begun.[16]

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[16] It should be noted that while Ms. Stepanova was sending complaints to Mpower and having her attorney contact the company about the disputed calls, Mpower was energetic in pursuing payment of the full amounts it had billed her. The Joint Stipulation states that Ms. Stepanova was advised on September 20, 2006 that no credit would be given due to Mpower's new policy of not giving credits in connection with fraudulent calls. (*Id.* ¶¶ 8, 10.) On September 29, Mpower phoned Ms. Stepanova again to tell her no adjustment would be made to her bill, and that her service would be disconnected unless she paid the full amount due. (*Id.* ¶ 12.) On October 19, an Mpower collections representative called Ms. Stepanova to pursue payment of the current and past-due balances on her account. (*Id.* ¶ 18.) On October 30, 2006, Mpower

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As noted above, a thorough review of Ms. Stepanova's complaints did not begin until October 20, 2006, three days after Ms. Stepanova's attorney sent Mpower the letter described above. Paragraph 19 of the Joint Stipulation describes the progress of that investigation, which was conducted by Mpower's fraud department, as follows:

> The fraud department's review indicated that if the calls were not completed by persons located at the Customer's premises, then it was likely that the calls were made through a fraudulent scheme. In the *following months*, the fraud department noted that six other Mpower customers had made similar complaints to Mpower regarding allegedly unauthorized charges for calls completed to GlobalStar satellite telephone numbers. In addition, during conference calls with other carrier representatives who participated with Mpower in an informal industry security task force, Mpower learned that customers of other carriers had been similarly affected by an alleged fraudulent scheme to complete calls to GlobalStar numbers. No minutes of the discussions with the security task force were kept and Mpower has no documents regarding the discussions that took place. (Emphasis supplied.)

We draw several conclusions from this chronology of the various examinations Mpower undertook of the Edelweiss matter. First, even under a strict reading of D.02-10-059, we think that Mpower met its minimum obligations under § 2890(e). On September 11, 2006, the day Ms. Stepanova first complained about her September bill, Mpower checked its call records, which showed that the calls in dispute had been direct-dialed on Edelweiss's fax line. Twenty-nine days later, when Ms. Stepanova called after faxing a second complaint about unauthorized charges, Mpower began a review of Edelweiss's account, but the

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phoned Ms. Stepanova again to tell her that she would not be given a credit in connection with the disputed calls on her September bill. (*Id.* ¶ 23.)

review was apparently cut short when Ms. Stepanova tired of being placed on hold and hung up. Although these steps were minimal and they leave unanswered questions, we cannot say that they were insufficient to meet the requirement of § 2890(e) that Mpower, "not later than 30 days from the date on which the complaint is received, shall verify the subscriber's authorization of [the disputed] charge or undertake to resolve the billing dispute to the subscriber's satisfaction."

However, it is also clear to us that Mpower did not make any serious effort to investigate Ms. Stepanova's concerns until five and one-half weeks after her initial complaint, and a few days after it had received the letter from her attorney. Over the next several months, Mpower learned enough from the fraud investigation to indicate that Ms. Stepanova was not exaggerating when she referred to "stolen call charges" and "stolen identity charges" on her bills. (Joint Stipulation, Exh. E.) First, although dates are not given, the fraud department learned that at least six other Mpower customers had made complaints similar to Ms. Stepanova's, all relating to international calls made over GlobalStar satellite facilities. Even though GlobalStar denied that its records showed such calls being made, the complaints about unauthorized calls ceased after GlobalStar was contacted. (*Id.* ¶ 20.)

Mpower also learned from its participation in the informal industry security task force that other carriers' customers had also been victims of the same scheme; *i.e.*, hacking the customers' computer and telecommunications systems to make international calls over GlobalStar satellite facilities. However, Mpower chose not to share this information, either with Ms. Stepanova, with the

six other customers who had complained to Mpower,[17] or with the Commission's CAB after Ms. Stepanova filed an informal complaint with the CAB. (*Id.* ¶ 34.) By proceeding in this manner, Mpower was behaving like a company that knew it had information adverse to its position and did not want this information to come to light.

The Joint Stipulation also does not explain why Mpower did not perform prompt records checks that would have helped to determine whether or not Ms. Stepanova was being candid in her complaints about her bills. For example, although the Joint Stipulation states that "none of the phone numbers listed for the disputed charges on the September 1 and October 1, 2006 bills had ever previously been called by the Customer or Edelweiss Flowers," we are not told when the record check leading to this conclusion was undertaken. (*Id.* ¶ 21.)

To summarize, even though we conclude that Mpower's conduct here met the minimum requirements of § 2890, that conduct was nothing to be proud of. As the Legislature stated in 1998 when it enacted SB 378, the bill that became § 2890, the purpose of the measure was to "reduce the inclusion of unauthorized charges on a subscriber's telephone bill by encouraging the verification of telephone charges, and providing an effective way to resolve disputes." If § 2890

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[17] On the issue of complaints from other Mpower customers, paragraph 38 of the Joint Stipulation makes clear that not all the customers were treated equally:

> The other six customers who Mpower believes may have been victims of the fraudulent calling scheme that may have affected the Customer [*i.e.*, Edelweiss] were initially pursued for payment. The total dollar amount of related usage charges, including those billed to the Customer, was $5,331.93. One of the other six customers who complained of the charges was given a credit at the discretion of Mpower in order to settle the matter after the Customer began taking action that Mpower believed would unduly disrupt its relationships with other existing and future customers.

is to have real meaning, it surely contemplates more of an investigation after a customer disputes a charge than a quick records check, or a perfunctory verification that a disputed call was direct-dialed. As the chronology above demonstrates, by delaying its substantive review of Edelweiss's account until after it had received a letter from Ms. Stepanova's attorney, Mpower was less than conscientious in seeking to resolve her billing dispute.

6. Does Item 5 of the Installation Policy and Procedures in MPower's Master Service Agreement Violate Public Utilities Code Section 451?

As noted above, UCAN's final major contention is that Mpower's insistence on being paid for the international long distance calls in dispute here violates Section 451 of the Public Utilities Code, which requires that "all rules made by a public utility affecting or pertaining to its charges or service to the public shall be just and reasonable." Section 451 also provides:

> All charges demanded or received by any public utility, or by any two or more public utilities, for any product or commodity furnished or to be furnished or any service rendered or to be rendered shall be just and reasonable. Every unjust or unreasonable charge demanded or received for such product or commodity or service is unlawful.

One of the Commission's most recent discussions of the scope of § 451 is found in D.04-09-062, the decision resulting from the Commission's investigation into marketing practices of Cingular Wireless. One of the issues in that case was whether § 451 was violated by Cingular's practices of (1) failing to disclose to customers its coverage problems during the period from 2000 to 2002, and (2) not granting customers a grace period within which they could cancel their service contracts without incurring a substantial Early Termination Fee (ETF). In ruling that these practices violated § 451, the Commission said:

> [Cingular's] policy required customers to pay an ETF if they wished to cancel their contracts before the expiration of the typically one- or two-year contract terms that Cingular offered. That policy was unjust, and therefore unreasonable, because customers were unable to determine whether they would be able to use Cingular's wireless service in the ways they desired until they attempted to make or receive calls – and no customer could do this without first signing a contract for service.
>
> Cingular concedes that its ETF policy was designed to avoid churn. Thus, in pursuit of market share, Cingular's prior official policy effectively trapped customers into contracts for service regardless of whether it could provide the coverage or capacity these customers sought. This is the crux of Cingular's violation of § 451. We focus upon the conditions under which Cingular imposed the ETF, resulting in an unjust rule and constituting unreasonable service. (D.04-09-062 at 50-51; footnote omitted.)[18]

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[18] In *Pacific Bell Wireless, LLC v. Public Utilities Commission*, 140 Cal. App. 4th 718 (2006), the Court of Appeal affirmed the Commission's determinations in D.04-09-062, as well the subsequent decision issued in response to Cingular's application for rehearing, D.04-12-058. In doing so, the Court of Appeal rejected Cingular's argument that § 451 violates due process because it fails to give adequate notice of the conduct the statute prohibits. On this question, the Court of Appeal said:

> Cingular contends it was denied due process because it was punished for actions it could not have known were unjust and unreasonable. Cingular argues the statutes and the Commission order it is charged with violating are so broad that Cingular could not anticipate that its actions were unjust and unreasonable. In analyzing Cingular 's argument, we must focus on its conduct of charging and permitting its agents to charge an ETF with no grace period; failing to disclose known, significant network problems; and providing misleading and inaccurate information regarding its coverage and service to its customers. We conclude that given this conduct, Cingular could be charged with knowledge that its actions were unjust and unreasonable under the relevant statutes and the Commission order.
>
> To accept Cingular's argument would require us to conclude that it is just and reasonable for a wireless provider to charge its customers an ETF to cancel a wireless service contract immediately after activation of the wireless

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As Commissioner Brown pointed out in his concurrence in D.04-09-062, the standards used for assessing the adequacy of the customer service agreement in that case are essentially the same standards used by the California courts to determine whether contracts are unconscionable under Civil Code § 1670.5.[19] On this question, Commissioner Brown stated:

> Standard form contracts presented to the customer in "take it or leave it" fashion are called contracts of adhesion. The law knows that they are not real contracts in the sense that there is a meeting of the minds of the parties. Commercial necessity and efficiency require that such "take it or leave it" contracts be accepted as if there were a real agreement.
>
> The law is uncomfortable with the fiction that a contract of adhesion is a real agreement. As a consequence, it requires that such contracts be fair, or at least not unconscionable. Unconscionable means "not guided by conscience," or "excessive, unreasonable" or "unscrupulous." (Concurring Opn. of Comr. Brown at 1; emphasis in original.)

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telephone, when the customer has been misled as to the coverage area and level of service, and when the wireless provider admits that the best way for the customer to determine whether the service is adequate for his or her needs is to try out the phone for a period of time. This conclusion would be unreasonable. (140 Cal.App. 4th at 739-40.)

[19] Civil Code § 1670.5 provides in full:

(a) If the Court finds as a matter of law the contract or any clause of the contract to have been unconscionable at the time it was made the court may refuse to enforce the contract, or it may enforce the remainder of the contract without the unconscionable clause, or it may so limit the application of any unconscionable clause as to avoid any unconscionable result.

(b) When it is claimed or appears to the court that the contract or any clause thereof may be unconscionable the parties shall be afforded a reasonable opportunity to present evidence as to its commercial setting, purpose, and effect to aid the court in making the determination.

Although the facts in this case are different from those in the Cingular Wireless case, we think that Mpower's actions in imposing liability on Edelweiss for the unauthorized calls made from numbers assigned to the flower shop also violated § 451. As demonstrated in the summary of the Joint Stipulation above, Edelweiss took steps in 2006 to protect its fax, computer, and phone system by installing a Windows firewall and an antivirus program, despite the fact that Mpower's 2005 "welcome kit" did not warn new customers about the dangers of hacking. Moreover, Mpower has admitted that it does not know exactly how the satellite calls at issue were placed, except that they presumably involved clever hacking of the modem attached to Edelweiss's DSL line, a modem Mpower had supplied.[20] The parties surmise in the Joint Stipulation that through this hacking, access was gained to one of the flower shop's POTS lines, from which the unauthorized calls were made.

Under the circumstance of this case, the provision in the Master Service Agreement on which Mpower is relying – item 5 of the Installation Policy and Procedures -- is unjust and unreasonable because, under Mpower's interpretation of the provision,[21] the company may reserve to itself the sole

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[20] As noted above, Mpower acknowledges on page 14 of its Opening Brief that it supplied the DSL modem that Edelweiss used.

[21] It should be noted that in its briefs here, UCAN takes the position that whether a customer has "adequately secured" its "computer network, circuits, and customer premise equipment from unauthorized access by 3d parties," as required by item 5, should be decided on the basis of what a reasonable customer would do to implement this requirement. (UCAN Opening Brief at 5; UCAN Reply Brief at 22.) UCAN points out that such a standard would be consistent with G.O. 168, Part 4.A. of which states that in interpreting the Commission's rules regarding cramming complaints, "the standard to be applied . . . is that of a reasonable consumer."

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power to decide whether the measures taken by a customer to secure its telephone and computer network and equipment are adequate. It is clear from ¶ 41 of the Joint Stipulation that no matter how thorough the customer's security measures might seem to an outside observer,[22] if they are successfully breached, then in Mpower's judgment, that is the end of the matter:

> Mpower does not claim to have knowledge of what the affected customers, including [Edelweiss], did or did not do to protect against modem hacking or other unauthorized access to their inside wiring or other customers premises equipment. *However, Mpower's position is that if the disputed calls were made through modem hacking or other unauthorized access* to their inside wiring or other customer premises equipment, *then the customers, by definition, did not take sufficient steps to prevent or "adequately secure" the customers' equipment from being hacked.* (Emphasis supplied.)

We agree with UCAN that as drafted, item 5 can be read as incorporating a reasonable customer standard. However, as the discussion in the text makes clear, that is not Mpower's interpretation of the provision. Accordingly, we have analyzed item 5 under the law of unconscionability as applied in California, rather than treating item 5 as ambiguous and applying the well-established rule that an ambiguity in a contract provision should be construed against the party who drafted the provision. See, e.g., *Taylor v. J.B. Hill Co.*, 31 Cal.2d 373, 374 (1948); *Victoria v. Superior Court*, 40 Cal. 3d 734, 745 (1985); Civ. Code § 1654 ("In cases of uncertainty . . . the language of a contract should be interpreted most strongly against the party who caused the uncertainty to exist.")

[22] As demonstrated by the discussion of hacking set forth in Section IV.C. of this decision, many reasonable persons would assume that the firewall and anti-viral program Edelweiss had installed on its computer system by 2006 were sufficient security. Moreover, when Mpower became aware that other customers were also victims of the satellite call scheme to which Edelweiss fell prey, Mpower had to participate in an "informal industry security task force" – a fact it did not disclose to Edelweiss during the parties' 2006 negotiations – to learn what the method for placing the unauthorized calls had most likely been. In view of these circumstances, it would be difficult to conclude that from a reasonable customer's perspective, Edelweiss did not take adequate steps to safeguard its "computer network, circuits, and customer premise equipment" from unauthorized access by third parties.

Contrary to Mpower's uncompromising position, it is clear from cases decided under California law that when a provision in a preprinted, standard form contract like the service agreement here gives the party who prepared the contract (and who has greater bargaining power) such unilateral rights as the option to disclaim all warranties about whether specialized goods being sold are adequate for a customer's needs, or the right to decide in which forum a dispute between an employer and employee will be litigated, that provision will be considered so one-sided as to be unconscionable. Because item 5 as interpreted by Mpower is similarly one-sided, it is also unconscionable.

In *Armendariz v. Foundation Health Psychcare Services, Inc.*, 24 Cal.4th 83 (2000), the California Supreme Court pointed out that unconscionability has two aspects under California law:

> As explained in *A & M Produce Co.* [*v. FMC Corp.*,] 135 Cal. App. 3d 473, "unconscionability has both a 'procedural' and a 'substantive' element," the former focusing on "'oppression'" or "'surprise'" due to unequal bargaining power, the latter on "'overly harsh'" or "'one-sided'" results. (*Id.* at 486-487.) "The prevailing view is that [procedural and substantive unconscionability] must both be present in order for a court to exercise its discretion to refuse to enforce a contract or clause under the doctrine of unconscionability." (*Stirlen v. Supercuts, Inc., supra*, 51 Cal. App. 4th [1519, 1533].) But they need not be present in the same degree. "Essentially a sliding scale is invoked which disregards the regularity of the procedural process of the contract formation, that creates the terms, in proportion to the greater harshness or unreasonableness of the substantive terms themselves." (15 Williston on Contracts (3d ed. 1972) § 1763A at 226-227; see also *A & M Produce Co., supra*, 135 Cal. App. 3d at 487.) In other words, the more substantively oppressive the contract term, the less evidence of procedural unconscionability is required to come to the conclusion that the term is unenforceable, and vice versa. (24 Cal.4th at 114.)

A&M Produce Co. v. FMC Corp., 135 Cal.App.3d 473 (1982), one of the cases cited in *Armendariz*, involved a clause in a form contract that was just as one-sided as item 5 in the customer service agreement here. In *A&M Produce*, the issue was whether form contract provisions that disclaimed all warranties and excluded consequential damages were unconscionable. The seller was a large corporation that produced specialized agricultural machinery and had sold a system for processing harvested tomatoes to a farmer. When the system failed to work in accordance with the representations of the FMC sales staff, the farmer suffered a total loss of his crop and sued. On appeal from a jury verdict in the farmer's favor, FMC argued that the verdict should be overturned because of the contract provisions disclaiming all warranties and relieving FMC of liability for consequential damages. Even though the farmer, Abatti, acknowledged he had not read the preprinted form contract, the Court of Appeal upheld the jury's verdict in his favor:

> Even if we ignore any suggestion of unfair surprise, there is ample evidence of unequal bargaining power here and a lack of any real negotiation over the terms of the contract. Although it was conceded that A & M was a large-scale farming enterprise by Imperial Valley standards . . . and that Abatti was farming some 8,000 acres in 1974, FMC Corporation is in an entirely different category. The 1974 gross sales of the Agriculture Machinery Division alone amounted to $40 million. More importantly, the terms on the FMC form contract were standard. FMC salesmen were not authorized to negotiate any of the terms appearing on the reverse side of the preprinted contract. Although FMC contends that in some special instances, individual contracts are negotiated, A & M was never made aware of that option. The sum total of these circumstances leads to the conclusion that this contract was a "bargain" only in the most general sense of the word . . .
>
> Although the procedural aspects of unconscionability are present in this case, we suspect the substantive unconscionability of the

> disclaimer and exclusion provisions contributed equally to the trial court's ultimate conclusion. As to the disclaimer of warranties, the facts of this case support the trial court's conclusion that such disclaimer was commercially unreasonable. The warranty allegedly breached by FMC went to the basic performance characteristics of the product. In attempting to disclaim this and all other warranties, FMC was in essence guarantying nothing about what the product would do. Since a product's performance forms the fundamental basis for a sales contract, it is patently unreasonable to assume that a buyer would purchase a standardized mass-produced product from an industry seller without any enforceable performance standards. From a social perspective, risk of loss is most appropriately borne by the party best able to prevent its occurrence . . . Rarely would the buyer be in a better position than the manufacturer-seller to evaluate the performance characteristics of a machine.
>
> In this case, moreover, the evidence establishes that A & M had no previous experience with weight-sizing machines and was forced to rely on the expertise of FMC in recommending the necessary equipment. FMC was abundantly aware of this fact. A seller's attempt, through the use of a disclaimer, to prevent the buyer from reasonably relying on [the seller's] representations calls into question the commercial reasonableness of the agreement and may well be substantively unconscionable. The trial court's conclusion to that effect is amply supported by the record before us.
> (135 Cal.App.3d at 491-92; citations and footnote omitted.)

In the same vein, an *en banc* panel of the Ninth Circuit recently found the arbitration provisions in a franchise agreement to be unconscionable. In *Nagrampa v. MailCoups, Inc.*, 469 F.3d 1257 (9th Cir. 2006), the arbitration clause required the franchisee, Nagrampa, to submit all of her claims to arbitration, but allowed the franchisor, MailCoups, to "to obtain any provisional remedy 'including, without limitation, injunctive relief from any court of competent jurisdiction, *as may be necessary in MailCoup's sole subjective judgment* to protect its Service Marks and proprietary information'." (469 F.3d at 1286; emphasis supplied.) In holding this provision unconscionable, the *en banc* panel said:

> This language, read plainly, means that MailCoups could go to court to obtain "any provisional remedy," even if it related to a claim for breach of contract, as long as the claim also implicated MailCoup's Service Marks or proprietary information. Moreover, it is far more likely that Nagrampa – and not MailCoups – would assert claims related to the invalidity or unenforceability of the non-negotiable contract written by MailCoups. *Thus, this provision is clearly one-sided, effectively giving MailCoups the right to choose a judicial forum and eliminate such a forum for Nagrampa.* California courts consistently have found such arbitration provisions unconscionable." (*Id.* at 1286-87; emphasis supplied.)[23]

Based on the foregoing cases, we believe that if item 5 of the Installation Policy and Procedures in the Mpower service agreement were to come before a California court, the court would hold item 5 to be unconscionable (and unenforceable) because of the unilateral power it confers on Mpower to decide whether the measures taken by a customer to safeguard its "computer network, circuits and customer premise equipment" are adequate. Item 5 meets the tests for procedural unconscionability under California law because (1) it was set forth in small type in a printed form that Edelweiss's owners probably had little

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[23] Another Ninth Circuit panel reached a similar conclusion in *Davis v. O'Melveny & Myers*, 485 F.3d 1066 (9th Cir. 2007). In that case, the issue was the validity of an arbitration provision that required the employees of a large law firm to submit all of their disputes with the employer to arbitration, but allowed the law firm to seek relief from a court for "claims by the Firm for injunctive and/or equitable relief for violations of the attorney-client privilege or work product doctrine or the disclosure of other confidential information." Although acknowledging that California law "allows an employer to preserve a judicial remedy for itself if justified based upon a 'legitimate commercial need' or 'business reality'," (485 F.3d at 1080), the Ninth Circuit concluded that the law firm's clause did not come within this exception because "its plain language would allow O'Melveny to go to court to obtain any 'equitable relief' for the disclosure of any 'confidential information'." (*Id.* at 1081.) Because of this over-breadth, the Court concluded that the clause was "one-sided and thus unconscionable." (*Id.*)

opportunity to read, and (2) even if item 5 was, in fact, read, there is no evidence that Edelweiss's owners were given a choice whether to accept it. Item 5 also meets the tests for substantive unconscionability, because it lets Mpower be the sole judge of whether a customer's telephone and computer security measures are "adequate," no matter what an impartial outside observer might think.

However, Mpower argues, even if item 5 could be considered one-sided, it should nonetheless be enforced and does not violate any provision of the Public Utilities Code because Edelweiss had a choice of other service providers, "and UCAN has not presented any evidence that the customer could not have obtained different terms of service elsewhere." (Mpower Reply Brief at 4.)

The short answer to this contention is that it is now well-established under California law that the alleged existence of marketplace alternatives is not a defense to a finding of unconscionability. In *Shroyer v. New Cingular Wireless Services, Inc.*, 498 F.3d 976 (9th Cir. 2007), the Ninth Circuit rejected such an argument by Cingular Wireless when it sought to obtain dismissal of a class action brought by a dissatisfied Cingular customer. The district court had granted Cingular's motion to compel arbitration and dismiss the class action, based on a provision in the customer service agreement that (1) required arbitration of all service disputes, and (2) precluded individual customers from bringing claims against Cingular on behalf of a class. In reversing the district court, holding the arbitration clause unconscionable, and remanding the class action to the district court for further consideration, the Ninth Circuit said:

> [C]ontrary to Cingular's contention, a contract may be procedurally unconscionable under California law when the party with substantially greater bargaining power "presents a 'take-it-or-leave-it' contract to a customer – even if the customer has a meaningful choice as to service providers." [*Douglas v. United States Dist. Court*,] 495 F.3d 1062, 1068 [9th Cir. 2007] . . . (holding in a case involving a

> class action waiver in a contract for long distance telephone services that the district court erred when it concluded that the waiver was not procedurally unconscionable on the basis of the availability of "meaningful alternative choices for telephone service" . . .; see also *Ting [v. AT&T,]* 319 F.3d [1126] at 1148; *Discover Bank*, 36 Cal.4th at 160. (498 F.3d at 985-86; citations omitted.)

Based on the caselaw discussed above, we conclude that item 5 of the Installation Policy and Procedures in Mpower's Master Service Agreement would be considered unconscionable under California law. Because item 5 is unconscionable, we also conclude, pursuant to our decision in the Cingular Wireless case (D.04-09-062), that the provision as Mpower interprets it also constitutes a denial of just and reasonable service under Pub. Util. Code § 451.

As noted in the Joint Stipulation, Mpower suspended Edelweiss's service on November 28, 2006 for non-payment of the charges that had been billed. On November 30, Ms. Stepanova informed Mpower that she wished to terminate her service agreement, inasmuch as she was unwilling to pay for service that had been suspended because of the dispute over the calls to GlobalStar facilities. As a result of this decision, Mpower billed Edelweiss for an ETF of $1,349.58 on December 20, 2006.

Under the circumstances of this case, we believe that Mpower's imposition of an ETF on Ms. Stepanova was unfair and unreasonable under Pub. Util. Code § 451. At the time the ETF was imposed, the investigation by Mpower's fraud department had already been underway for two months. Thus, at the time the charge was imposed, Mpower was either aware or should have been aware that (1) none of the GlobalStar numbers in dispute had ever previously been called from Edelweiss, (2) six other customers had made similar complaints to Mpower about unauthorized calls, and (3) other carriers' customers had also been victims of the type of fraud about which Ms. Stepanova had complained. In view of

these circumstances, Mpower should have given Ms. Stepanova a credit for the disputed calls, as it did for one of the six other Mpower customers who had made similar complaints. Instead, Mpower suspended Ms. Stepanova's service, and then added insult to injury by imposing an ETF after Ms. Stepanova understandably informed Mpower that she wished to terminate the service agreement. As we ruled in D.04-09-062, such conduct is not consistent with the requirements of § 451.[24]

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[24] In its complaint in this proceeding, UCAN originally argued that Mpower's conduct also violated Pub. Util. Code § 2896(a), which requires telephone corporations to provide their customers with "sufficient information upon which to make informed choices among telecommunications services and providers," including information concerning the provider's "service options, pricing, and terms and conditions of service." ¶ 78 of the complaint asserted that Mpower had violated § 2896(a) by failing to inform Ms. Stepanova that international long distance calling was included in her service agreement, and that the rate for some international calls was $14.67 per minute.

In its briefs, UCAN now makes a more generalized argument, maintaining that Mpower's conduct in this case amounted to a failure to provide adequate service quality under § 2896(c). (UCAN Opening Brief at 23; UCAN Reply Brief at 15, 28.) The only authority UCAN appears to cite in support of its position is the Cingular Wireless decision, D.04-09-062.

We decline to find a violation of § 2896 here. As noted in Section V.C. of this decision, although its language might have been clearer, the Service Order Form that Ms. Stepanova's predecessor signed indicated that Mpower was to be Edelweiss' new international carrier, and expressly stated that "LD Rates are domestic rates, except for Alaska and Hawaii; International rates vary by country and are identified on the Mpower website." (Joint Stipulation, Exh. A.) In view of these statements, there is no basis for finding a violation of § 2896(a).

We also do not think that D.04-09-062 supports the conclusion that Mpower's conduct – although it violated § 451 – constitutes a violation of § 2896(c) as well. It is evident from reading Section 6.1.2. of the Cingular Wireless decision that the violation found there was of § 2896(a), owing to "the deficiencies in Cingular's disclosures to customers, given known network problems in 2002 in conjunction with the continuing ETF policy." (D.04-09-062 at 59.) In fact, D.04-09-062 expressly noted that there was no need to

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In closing, we wish to emphasize what we are and are not deciding today with respect to item 5 of the Installation Policy and Procedures in Mpower's Master Service Agreement. We hold that as interpreted by Mpower, this provision -- which was included in a preprinted, form agreement prepared by Mpower, and which Edelweiss, a small business customer, had no apparent opportunity to bargain over or reject – violates the unconscionability standard included within Pub. Util. Code § 451. We are not holding, however, that § 451 is violated where a provision shifting liability for fraudulent toll calls, whatever the cause, is included in a contract between a carrier and a sophisticated business customer, and the contract has been the subject of meaningful negotiations between the parties with an opportunity to accept or reject specific terms. We leave the question of what applicability, if any, § 451 may have in that situation to a case where such facts are squarely presented to us.

Assignment of Proceeding

Timothy Alan Simon is the assigned Commissioner and A. Kirk McKenzie is the assigned ALJ and presiding officer in this proceeding.

Findings of Fact

1. The complaint in this case was filed on August 12, 2008, and defendant submitted its answer on September 22, 2008.

2. A PHC was held on December 3, 2008, at which complainant and defendant agreed that it appeared feasible to decide the case on the basis of a joint stipulation of facts.

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address Cingular's alleged failure to establish service standards under § 2896(c), "since neither CPSD nor UCAN pursued this charge at hearing or in the briefs." (*Id.* at 55.)

3. At the PHC, the assigned ALJ stated that, subject to reviewing the proposed stipulation and briefs, he was amenable to the approach suggested by the parties.

4. Pursuant to the agreement reached at the PHC, a Joint Stipulation of facts was filed by complainant and defendant on January 15, 2009. The Joint Stipulation can be found on the Commission's website at http://docs.cpuc.ca.gov/efile/STP/96277.pdf.

5. The parties submitted concurrent opening briefs on January 28, 2009, and concurrent reply briefs on February 11, 2009.

6. On April 8, 2009, the assigned Commissioner and the assigned ALJ issued a Scoping Memo, which set forth the issues and concluded that a hearing was not necessary because, taken together, the Joint Stipulation and the parties' briefs were sufficient to resolve any factual issues presented by the case.

7. On July 30, 2009, the Commission issued D.09-07-042, which extended the statutory deadline for deciding this case until February 12, 2010.

8. On February 4, 2010, the Commission issued D.10-02-006, which extended the statutory deadline for deciding this case until November 19, 2010.

9. On June 23, 2005, Olga Kormuskina, on behalf of Edelweiss, entered into a Master Service Agreement with defendant pursuant to which the latter agreed to furnish various telecommunications services to Edelweiss, including a DSL Internet access line, a DSL modem, and three POTS lines. The Master Service Agreement is attached to the Joint Stipulation as Exhibit A.

10. Shortly after the parties entered into the Master Service Agreement, Mpower sent Edelweiss a "welcome kit" for new customers, which included the notice attached to the Joint Stipulation as Exhibit B. This notice is entitled "Consumer Alert re: Fraud Resulting in International Long Distance Charges."

11. In May 2006, Edelweiss was incorporated and Natalja Stepanova became its sole owner, operating Edelweiss as a single proprietorship. At the same time, Ms. Stepanova and Mpower entered into an assignment and assumption agreement, pursuant to which Ms. Stepanova assumed Edelweiss's obligations under the June 23, 2005 Master Service Agreement with Mpower.

12. On or about September 1, 2006, Mpower sent Edelweiss a bill for services that included international long distance charges to satellite facilities of $1,043.13 (before taxes, fees and surcharges) on the POTS line connected to Edelweiss's fax machine. The relevant portions of this bill are attached to the Joint Stipulation as Exhibit C. The international long distance charges were billed at a rate of $14.67 per minute.

13. On September 11, 2006, Ms. Stepanova telephoned Mpower and stated that neither she nor anyone else authorized to make calls at Edelweiss had incurred the aforesaid international long distance charges. She requested a credit for the calls, as well as a block on international calling for her account.

14. On September 11, 2006, after Ms. Stepanova's complaint, Mpower staff checked the calling records for Edelweiss's account, which indicated that the disputed calls had been direct-dialed over Edelweiss's fax line.

15. On September 20, 2006, when Ms. Stepanova telephoned Mpower again, she was informed that she would not be given a credit for the disputed calls pursuant to a new Mpower policy regarding fraudulent calls. She was also asked to fax a written statement to Mpower concerning the disputed calls, which she did later the same day.

16. On September 29, 2006, Mpower telephoned Ms. Stepanova to reiterate that she would not be given a credit in connection with the disputed calls, and that if she failed to pay the full charges due, her service would be disconnected.

17. On or about October 1, 2006, Mpower sent Edelweiss a bill for services that included additional international long distance charges to satellite facilities of $2,180.01 (before taxes, fees and surcharges) on the POTS line connected to Edelweiss's fax machine. The relevant portions of this bill are attached to the Joint Stipulation as Exhibit F. As with the bill rendered on or about September 1, 2006, the additional international long distance charges were billed at a rate of $14.67 per minute.

18. Although the bills referred to in Findings of Fact (FOF) 12 and 17 stated that the international long distance calls were to Iridium satellite facilities, these calls were in fact made to GlobalStar satellite facilities, as shown on Mpower's call detail records. The $14.67 per minute rate at which the calls were charged was the rate shown on Mpower's website for calls to GlobalStar satellite facilities.

19. On October 9, 2006, Ms. Stepanova faxed a second written complaint to Mpower, which reiterated her dispute regarding the international long distance charges on the September bill and also denied that she had authorized the calls resulting in the international long distance charges on the October bill.

20. On October 10, 2006, following receipt of the second written complaint, Mpower staff began a review of the Edelweiss account. While the review was being conducted, Ms. Stepanova telephoned to inquire about the disputed charges and asked to speak to a supervisor. She was told the review would take some time and was placed on hold, but apparently hung up before the Mpower staff could respond to her inquiry.

21. The Joint Stipulation is silent on the question of whether Mpower's staff continued its review of the Edelweiss account on October 10, 2006 after the call from Ms. Stepanova was interrupted.

22. On October 17, 2006, an attorney hired by Ms. Stepanova sent Mpower a letter summarizing her position in the billing dispute and enclosing a check for charges that were not disputed.

23. On October 20, 2006, Mpower's fraud department began a review of the long distance fraud that Ms. Stepanova alleged had been perpetrated upon her. This review lasted for several months.

24. At some point during the fraud department's review, the department learned that six other Mpower customers had also complained to Mpower about allegedly unauthorized international calls to satellite numbers that had appeared on their bills. One of these customers was given a credit for the disputed calls; Mpower continued to pursue the other customers for payment.

25. At some point during the fraud department's review, Mpower learned through its participation in an informal industry security task force that customers of other carriers had also been victims of a scheme like that alleged by Ms. Stepanova that involved unauthorized calls to GlobalStar satellite facilities.

26. Mpower did not disclose what it had learned through its participation in the informal industry security task force to Ms. Stepanova or to the six other Mpower customers who had complained about unauthorized international long distance charges. Mpower also did not disclose this information to the CAB after Ms. Stepanova filed an informal complaint about her billing dispute with the CAB in January 2007.

27. Although GlobalStar denied that its call detail records showed calls being made to its satellite facilities by Mpower customers, Mpower received no further complaints about such unauthorized calls after it contacted GlobalStar.

28. Based on its investigation, Mpower acknowledges in ¶ 22 of the Joint Stipulation that if the disputed calls were not made from Edelweiss's premises, it

is most likely they were completed through some form of modem hacking. One form of modem hacking involves the use of a high-speed internet connection by an outside party to access a computer and then dial out calls through a POTS line that is connected to the computer, either through a fax modem or a dial-up internet modem.

29. Based on the equipment configuration at Edelweiss during the relevant period as described in ¶ 4 of the Joint Stipulation, the form of modem hacking described in the preceding Finding of Fact (FOF) was feasible.

30. The consumer fraud notice that Mpower included in the welcome kit sent to Edelweiss in 2005 warned only about the danger of unauthorized international long distance calls placed through the hacking of PBXs and voice-mail systems. The notice did not mention modem hacking, or suggest in any way that special precautions might be necessary to prevent unauthorized international long distance calls placed through modem hacking.

31. In ¶ 21 of the Joint Stipulation, Mpower acknowledges that none of the phone numbers listed for the disputed calls on the September and October 2006 bills had ever previously been called from Edelweiss, either before or after Ms. Stepanova began to operate it as a sole proprietorship.

32. In ¶ 4 of the Joint Stipulation, Mpower acknowledges that it has no basis for disputing Ms. Stepanova's assertions that (a) Windows Firewall and an antivirus program (most likely Norton's) had been installed on the computer connected to Edelweiss's fax line, (b) none of Edelweiss's POTS lines were connected to a PBX, and (c) Edelweiss did not have voicemail.

33. A recent treatise on information security states that it is widely but incorrectly believed that off-the-shelf firewall products offer good computer security. In order to be effective, properly-configured firewalls must typically be

used with intrusion detection and prevention systems, vulnerability assessment technology, and antivirus technology.

34. In 2006 the average, reasonable small business customer like Ms. Stepanova was not aware of the limitations of off-the-shelf firewall products described in the preceding FOF.

35. In view of the limited warning about toll fraud contained in the welcome kit that Edelweiss received in 2005, plus the understanding that a reasonable small business customer would have had in 2006 about what constitutes adequate information security, the security measures undertaken by Edelweiss in 2005-06, as described in FOF 32, were reasonable.

36. The FCC has held that where a business customer fails to offer evidence that it has used reasonable measures to prevent unauthorized long-distance calls from being placed through the PBX or voice-mail capabilities of its phone system, the customer may be held liable for such calls.

37. The FCC has held that where a business customer has used reasonable measures to secure its telephone system against fraudulent long distance and international calling, the customer should not be deemed to have constructively ordered long-distance or international service if the security measures prove unsuccessful.

38. Several federal district courts have held that where a business customer has used reasonable measures to prevent unauthorized long-distance or international calls from being placed through hacking of the PBX or voice-mail capabilities of the customer's telephone system, the customer should not be deemed to have constructively ordered long-distance or international service if the security measures prove unsuccessful.

39. Based on the decisions described in FOFs 36 and 37, the FCC has not preempted the applicability of state anti-cramming statutes such as Pub. Util. Code § 2890 to factual situations like the one here.

40. Based on the facts set forth in Joint Stipulation, it is highly unlikely that the international long distance calls in dispute here were authorized by Ms. Stepanova or placed from Edelweiss's premises.

41. Based on the decisions described in FOFs 37 and 38, the facts set forth in the Joint Stipulation, and the preceding FOF, it is unlikely that under federal law, Edelweiss or Ms. Stepanova would be held liable for the international long distance calls at issue in this case.

42. Mpower did not undertake a meaningful review of Ms. Stepanova's allegations that Edelweiss was the victim of a fraudulent calling scheme until the Mpower fraud department began its investigation on October 20, 2006, more than five weeks after Ms. Stepanova had first complained about the disputed calls, and shortly after Mpower had received a letter from her attorney.

43. Mpower interprets item 5 of the Installation Policy and Procedures included in the Master Service Agreement with Edelweiss to give Mpower the sole authority to decide whether the measures taken by a customer to secure its computer network, circuits, and customer premises equipment are adequate.

44. According to ¶ 41 of the Joint Stipulation, Mpower's position in this case is that if the disputed calls were made through modem hacking or other unauthorized access to Edelweiss's inside wiring or customer premises equipment, then by definition, Edelweiss did not take sufficient steps to secure its equipment adequately, no matter what an objective outside observer might think.

45. Decisions under California law have found contract provisions like item 5 of the Installation Policy and Procedures in the Master Service Agreement between Mpower and Edelweiss to be so one-sided and commercially unreasonable as to be unconscionable.

46. During the course of its investigation into Ms. Stepanova's complaints, Mpower did not give equal treatment to the six other customers who had complained to Mpower about unauthorized calls being placed on their lines to GlobalStar facilities.

47. Ms. Stepanova's decision on November 30, 2006 to request termination of her service agreement with Mpower was made because the latter had suspended Edelweiss's service for non-payment, despite the facts that (1) there was a dispute about whether the calls to GlobalStar facilities had been authorized, a dispute Mpower was actively investigating, and (2) Edelweiss had tendered payment for the calls made on its lines as to which there was no dispute.

Conclusions of Law

1. The records check that Mpower performed on September 11, 2006 to verify that the disputed calls had been direct-dialed from Edelweiss's fax line, together with the review that Mpower began of Edelweiss's account on October 11, 2006, were sufficient to meet the minimum requirements imposed on Mpower by Pub. Util. Code § 2890(e).

2. Item 5 of the Installation Policy and Procedures in the Master Service Agreement between Mpower and Edelweiss can be interpreted, in determining whether a customer has adequately secured its computer network, circuits, and customer premises equipment from unauthorized access by third parties, as incorporating the standard of what a reasonable customer would do to meet these obligations.

3. In view of Mpower's position that if an unauthorized third party was able to place international calls over a customer's equipment through modem hacking or other improper means, then by definition, this establishes that the customer did not adequately secure its computer network, circuits, and other customer premises equipment, it is appropriate to evaluate item 5 of the Installation Policy and Procedures in the Mpower service agreement under the law of unconscionability in California.

4. If it were before a court, item 5 of the Installation Policy and Procedures in the Master Service Agreement between Mpower and Edelweiss would likely be considered unconscionable and unenforceable under California law.

5. Because it would be considered unconscionable under California law, item 5 of the Installation Policy and Procedures in the Mpower service agreement also constitutes an unjust rule resulting in unreasonable service under Pub. Util. Code § 451.

6. Mpower's imposition of an ETF on Edelweiss on December 20, 2006, at a time when Mpower knew or should have known that (a) there was merit in Ms. Stepanova's allegations that the calls in dispute had been placed fraudulently, and (b) Ms. Stepanova had decided to cancel her service agreement because of the suspension of service imposed on account of her refusal to pay for the disputed calls, constituted an unfair practice resulting in unreasonable service under Pub. Util. Code § 451.

7. Mpower did not violate Pub. Util. Code § 2896(a) by failing to provide a fuller statement in its Master Service Agreement that under the agreement, Mpower would also be furnishing international calling service to Edelweiss.

O R D E R

IT IS ORDERED that:

1. To the extent that defendant Mpower Communications Corp. has collected payment from Natalja Stepanova or Edelweiss Flower Salon, Inc. for calls to GlobalStar satellite facilities that appeared on the bills for services that Mpower Communications Corp. presented to Edelweiss Flower Salon, Inc. on or about September 1, 2006 and October 1, 2006, Mpower Communications Corp. shall refund the amounts representing payment for such calls to Natalja Stepanova or Edelweiss Flower Salon, Inc., as appropriate, within 30 days after issuance of this order.

2. To the extent that Mpower Communications Corp. has collected from Natalja Stepanova or Edelweiss Flower Salon, Inc. the early termination fees of $1,349.58 that Mpower Communications Corp. imposed on Edelweiss Flower Salon, Inc. on December 20, 2006, Mpower Communications Corp. shall refund such fees to Natalja Stepanova or Edelweiss Flower Salon, Inc., as appropriate, within 30 days after issuance of this order.

3. To the extent that Mpower Communications Corp. has not collected payment from Natalja Stepanova or Edelweiss Flower Salon, Inc. for the calls described in Ordering Paragraph 1 or the early termination fees described in Ordering Paragraph 2, Mpower Communications Corp. and its employees, attorneys and agents shall immediately cease all efforts to obtain payment for such calls and fees, and any debt owing from Natalja Stepanova and/or Edelweiss Flower Salon, Inc. to Mpower Communications Corp. on account of such calls and fees shall be considered extinguished.

4. Neither Mpower Communications Corp., its employees, attorneys, or agents, nor any of them, shall make any adverse report concerning Natalja Stepanova or Edelweiss Flower Salon, Inc. to any credit agency on account of the amounts Mpower Communications Corp. contends it is owed in connection with the calls described in Ordering Paragraph 1 or the early termination fees described in Ordering Paragraph 2.

This order is effective today.

Dated June 3, 2010, at San Francisco, California.