

Decision 05-02-022 February 10, 2005

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Mpower Communications Corp. (U-5859-C),

Complainant,

vs.

Pacific Bell Telephone Company (U-1001-C),

Defendant.

Case 02-09-045
(Filed September 27, 2002)

John L. Clark, Attorney at Law, for Mpower
Communications Corp., Complainant.

Michael J. Kass, Attorney at Law, for Pacific Bell
Telephone Company, Defendant.

Martin Mattes, Attorney at Law, for California
Payphone Association, Intervenor.

OPINION RESOLVING COMPLAINT

1. Summary

In today's decision, we find Pacific Bell Telephone Company (SBC California) indirectly rebated tariffed charges in violation of Pub. Util. Code § 532.

Specifically, SBC California and complainant Mpower Communications Corp. (Mpower) compete in providing lines to payphone service providers. As relevant to this complaint, SBC California pays to an independent third-party

aggregator of affiliated payphone service providers¹ the compensation owed under federal rules for calls that are made by means other than depositing coins, including calls to its 800 “platform.” SBC California offered a limited-term “Fast Start Program” and paid fixed “compensation” owed to payphone service providers by crediting amounts designated by the aggregator. Mpower asserts these payments are unlawful rebates of tariffed charges owed to SBC California by the payphone service providers, while SBC California states they are lawful compensation under the federal rules.

Section 532 provides that no public utility shall charge other than its tariffed rates. Both direct and indirect rebates are impermissible. Federal law requires carriers to compensate payphone service providers for “non-sent paid” calls, generally 800 “platform” and access code calls. We find one of the four payments at issue, the “new line added” component of the “New Connect Award,” is an indirect rebate, and we order SBC California to terminate its “Fast Start Program.” The payment is identical to the installation charge, was directly paid by SBC California to payphone service providers within a month of verification, and was accounted for as “contra revenue,” a credit to the COPT access line tariffed charge. The evidence is insufficient to find the other payments constitute indirect rebates.

2. Procedural Background

Mpower filed motions for interim injunctive relief (September 27, 2002) and for expedited hearing (October 28, 2002). On November 15, 2002, the assigned Administrative Law Judge (ALJ) denied the motion for expedited

¹ The aggregator in question is G-Five Corporation (G-Five).

hearing and set a prehearing conference (PHC). We held PHCs on November 26, 2002, and on February 19, 2003. Between the PHCs, Mpower and SBC California conducted discovery to determine whether there were disputed factual issues. Mpower stated factual disputes existed, and this matter was set for hearing on April 23 and 24, 2003. By a March 12, 2003 letter, the parties requested an extension of the schedule in order to complete discovery and better prepare for hearing or, alternatively, summary disposition of the issues in this proceeding. Hearings were rescheduled for June 11 and 12, 2003, and were held on June 11, 2003. Opening briefs were filed on July 3, 2003, and reply briefs were filed on August 8, 2003, on which date this matter was submitted.

On August 18, 2003, the parties contacted the ALJ and requested that the Commission delay issuance of the presiding officer's decision (POD) to enable the parties to discuss settlement. Settlement discussions were delayed due to scheduling conflicts and on October 2, 2003, the parties requested in writing extension of this proceeding beyond the one-year statutory timeframe and extension of the timeframe within which the POD must issue. In December 2003, the assigned ALJ requested an update on the settlement negotiations and the parties stated that they had been unable to reach a settlement agreement. On December 18, 2003, the parties confirmed the failure to reach settlement in writing and requested that the POD issue.

3. Parties' Contentions

Two issues remain in this proceeding:

1. Whether SBC California's payments to pay telephone service aggregators when a pay telephone service provider migrates to SBC California's Customer Owned Pay Telephone (COPT) service are unlawful rebates under § 532.
2. Whether SBC California's payments to pay telephone service aggregators are commissions mandated by federal law and Federal Communications Commission (FCC) orders to pay telephone service providers for non-sent paid calls beyond the jurisdiction of this Commission.

Mpower further alleges that SBC California's payments violate our price floor regulations. Mpower requests that the Commission terminate SBC California's alleged rebate arrangements that are the subject of the complaint, order SBC California to rebill COPT customers for the full amount of any alleged rebates received, and fine SBC California. SBC California denies that it has violated § 532 or our price floor rules. SBC California further denies Mpower is entitled to the relief sought in the complaint.

4. Factual Background

The following describes the setting in which the two carriers compete. To fully understand the competitive setting, it is important to bear in mind that a carrier providing lines to a payphone service provider collects money from the latter in connection with certain kinds of services but also pays money to the payphone service provider for certain kinds of calls. Defendant SBC California (an incumbent local exchange carrier) and complainant Mpower (a facilities-based competitive local exchange carrier), compete in providing lines to payphone service providers, who are for this purpose customers of the carriers

providing the lines. SBC California, pursuant to its intrastate tariffs, bills and collects from payphone service providers a non-recurring charge of \$112 to establish a new COPT service line. SBC California also bills and collects from payphone service providers other tariffed charges on a monthly basis, including a service charge of \$14.53 per line.²

The revenue from some of the calls placed at coin phones belonging to payphone service providers goes not to those providers but to the local exchange carrier (or interexchange carrier) which then pays compensation to the providers. Specifically, the FCC requires carriers to compensate payphone service providers for “non-sent paid” calls, which generally are 800 platform and access code calls.³ However, the FCC provides latitude on how the compensation is calculated. The carrier can pay compensation to the payphone service provider at a default rate of \$0.24 per call or at a negotiated higher amount.⁴ SBC California’s June 2001 Compensation Agreement for “O”/”O+” intraLocal Access Transport Areas non-sent paid traffic with G-Five provides volume sensitive monthly compensation per non-sent paid call. (Exhibit C-9, Attachment 1.)

² SBC California derives additional revenue from miscellaneous and access charges.

³ Non-sent paid calls include collect calls, calls billed to a third number, and calls billed to a calling card. They are placed by dialing “O” or “O plus.” SBC California also pays compensation for calls to its “800 platform,” 800-522-2020, on behalf of its platform provider, Sprint Communications Company.

⁴ After submission of this proceeding, the FCC ordered an increase in this compensation to \$.494 per call. (Report and Order, *In the Matter of Request to Update Default Compensation Rate for Dial-Around Calls from Payphones*, WC Docket No.03-225, released August 12, 2004, ¶ 1.)

The record shows that G-Five asked SBC California to waive or credit installation charges to payphone service providers to ensure SBC California could compete with new Unbundled Network Element-P competitive local exchange carriers who were teaming up with established carriers like Verizon to offer better compensation plans. SBC California rejected G-Five's proposal and instead agreed to make payments to G-Five pursuant to an "Additional Compensation" agreement with G-Five. (Exhibit 7.)⁵ Under the "Fast Start Program," offered during 90 days in 2002, the payments to G-Five include the "New Connect Award," a fixed amount plus an amount for a "new line added" payable within 30 days of verification of the new order, another amount payable at the end of the 12-month term of the promotion, and a monthly amount. For lines G-Five retains as SBC California lines, SBC California pays an amount at the beginning of the promotion, an amount at the end of the 12-month term, and a monthly payment.

SBC California can pay "commissions" owed to payphone service providers under the Compensation Agreement either directly to G-Five or, at G-Five's direction and as authorized by the payphone service provider, by crediting amounts designated by G-Five to bills for services provided by SBC California to the payphone service provider or by check. (*Id.*) G-Five could retain a portion of the payments and distribute the remainder to the payphone service providers. These are the payments that Mpower asserts are unlawful rebates in violation of § 532.

⁵ SBC California called a similar "Additional Compensation" agreement an addendum to the agreement for SBC California non-sent paid traffic. (September 27, 2002 Motion for Interim Injunctive Relief, Exhibit A.)

In setting the payments to G-Five under the “Additional Compensation” agreement, SBC California calculated average revenue per non sent-paid call, subtracted the amount paid to G-Five per call in commissions, estimated additional revenue per platform call, and set compensation accordingly. Payphone service providers entered into agreements with G-Five to purchase or continue to purchase SBC California’s line service. SBC California verified the line information G-Five provided and made payments to G-Five or to a designated payphone service provider at G-Five’s direction.

5. Discussion

Resolution of this complaint requires interpretation of the nature of payments between payphone service providers and SBC California under state and federal law. California law precludes a carrier from rebating tariffed charges. Federal law requires carriers to pay compensation to payphone service providers for “non-sent paid” calls. The issue presented here is whether payments made to G-Five under the promotional “Fast Start Program” are rebates or compensation. After weighing the evidence before us, we find the “New Connect Award” is an indirect rebate. Below, we discuss the basis for our determination.

5.1 SBC California Improperly Rebated Tariffed Charges

Under state law, rebates of tariffed charges are unlawful. Section 532 provides that no public utility shall charge other than its tariffed rates. It further provides that no public utility shall refund or remit directly or indirectly any portion of its tariffed rates and charges unless such refund is on file and in effect

at that time.⁶ We address whether the payments are direct or indirect rebates, both of which are prohibited. (*Empire West v. Southern California Gas Co.* (1974) 12 Cal. 3d 805, 809.) SBC California continued to charge its tariffed rates to payphone service providers for non-recurring and monthly charges. Thus, there was no direct rebate of tariffed charges. We next analyze whether the payments were indirect rebates.

To determine whether the payments to G-Five are impermissible rebates or required compensation, we must look at the circumstances surrounding the payments. On the one hand, SBC California made payments designated for G-Five, including two “New Connect Award” payments, directly to payphone service providers at G-Five’s direction. (Exhibit C-8, p. 6.) The “New Connect Award” includes two fixed payments; one of those payments mirrors the tariffed installation charge and there is another upfront payment. Another payment

⁶ Section 532 states in its entirety: “Except as in this article otherwise provided, no public utility shall charge, or receive a different compensation for any product or commodity furnished or to be furnished, or for any service rendered or to be rendered, than the rates, tolls, rentals, and charges applicable thereto as specified in its schedules on file and in effect at the time, nor shall any public utility engaged in furnishing or rendering more than one product, commodity, or service, charge, demand, collect, or receive a different compensation for the collective, combined, or contemporaneous furnishing or rendition of two or more of such products, commodities, or services, than the aggregate of the rates, tolls, rentals, or charges specified in its schedules on file and in effect at the time, applicable to each such product, commodity, or service when separately furnished or rendered, *nor shall any such public utility refund or remit, directly or indirectly, in any manner or by any device, any portion of the rates, tolls, rentals, and charges so specified*, nor extend to any corporation or person any form of contract or agreement or any rule or regulation or any facility or privilege except such as are regularly and uniformly extended to all corporations and persons. The commission may by rule or order establish such exceptions from the operation of this prohibition as it may consider just and reasonable as to each public utility.” (*Emphasis added.*)

comprises almost half of the monthly line charge; the “Additional Compensation” agreement states SBC California will credit that amount monthly. (Exhibit C-7, Attachment 1.) In addition, there is an end-of-term payment. SBC California also temporarily accounted for the payments identical to the installation charge as “contra revenue,” a credit of the COPT access line tariffed charge. Finally, platform call revenues from new lines may not have equaled “commission” payments to payphone providers who switched to SBC California.

On the other hand, the “Fast Start Program” is not a new offering, the payments were characterized as compensation in the agreement with G-Five, G-Five at its discretion could have obtained the payments from SBC California and distributed them to payphone service providers, and G-Five received some portion of the compensation. SBC California’s original compensation agreement with G-Five included a less generous version of the “Fast Start Program,” which contained two lump-sum payments.

Two of the above-referenced circumstances argue in favor of finding that the payments were rebates rather than compensation. First, SBC California directly sent payments to payphone service providers at G-Five’s direction and agreed to credit the monthly payments. Even though SBC California’s agreement was with G-Five, that agreement permitted direct payments, and those payments were made by SBC California to payphone service providers. A connection between the tariffed charge and the alleged rebate is a criterion in determining whether there has been a violation of § 532. The circumstances here establish such a connection. The installation charge is a non-recurring charge due after COPT service is established. The “new line added” payment, the identical amount, was made within 30 days after the new connection was

verified. Retained lines did not receive this payment. However, both new and retained lines received another upfront payment, supporting the connection between the installation charge and the “new line added” component of the “New Connect Award.” SBC California’s denominating the payments “commissions” is insufficient to determine the nature of the payments.

Second, SBC California, at least initially, accounted for one type of payment as a credit (“contra revenues”) to tariffed charges by booking the “New Connect” (installation) expense to the COPT access line non-recurring revenue account at the end of 2002. When SBC California makes refunds of or credits to customers’ payments for regulated service, it must account for them as deductions to the revenue accounts to which the customers’ payments were booked. SBC California initially accounted for the “New Connect” expense as a deduction to the revenue account for a regulated service. SBC California’s actions lend support to a conclusion that the payments were rebates of tariffed charges.

SBC California’s claim that this “contra revenue” treatment was based on an SBC California employee’s mistaken belief the procedure was proper is unpersuasive. SBC California’s internal e-mail communications during the four months prior to the end of 2002 noted the entire “New Connect” (installation) revenues would be moved as “contra revenues.” In addition, SBC California also considered similar “contra revenue” treatment for another payment. One e-mail states that the “monthly line credit” expense would be moved to “contra revenue”; however, that move did not occur.

The two circumstances favoring SBC California’s position are the FCC’s endorsement of fixed compensation and the existence of an earlier “Fast Start

Program.” Use of per call and fixed compensation payments is consistent with FCC directives. The FCC gives broad discretion to carriers in establishing compensation to payphone service providers, including the ability to negotiate the amount and form of compensation. (First Payphone Order, 11 FCCR at 20, 578-79, ¶ 73; Third Report and Order, 14 FCCR 2245, 2597, ¶ 115.) Thus there is no rule precluding SBC California from making fixed compensation payments. Further, SBC California issued a payment for fixed “commissions” under the earlier “Fast Start Program,” but there is no allegation that payment was a rebate of tariffed charges.

On balance, we determine that SBC California indirectly rebated tariffed charges by virtue of its “New Connect Award.” Paying a “commission” payment identical to a tariffed charge directly to the payphone service provider within 30 days after the new line is verified, combined with accounting for part of that payment as a credit against a tariffed charge, belies SBC California’s claim that it was paying compensation pursuant to FCC rules. We determine the “New Connect Award” is an indirect rebate, because it is identical to a tariffed charge and SBC California accounted for it as a credit of a tariffed charge. The evidence is insufficient to find the other payments are indirect rebates.

5.2 Relief

In discussing what relief and/or fines will remedy this violation of our rules and regulations, we consider whether we should terminate SBC California’s indirect rebate of the installation cost, order SBC California to rebill payphone service providers for the installation costs, fine SBC California, or grant such other relief as may be appropriate.

The “Fast Start Program,” offered during 90 days in 2002, contained fixed payments and an indirect rebate of tariffed charges. Fixed compensation

payments violate § 532 when they indirectly rebate a tariffed charge. Thus, we order SBC California to terminate the “Fast Start Program” that is the subject of this complaint. We understand the program is currently terminated, but we further order SBC California not to reinstate it.

SBC California must charge its tariffed rates or seek and receive authority from us for an exception, as provided in the last sentence of § 532. We may by rule or order establish exceptions for a particular utility to the statute’s prohibition against rebates of tariffed charges, if to do so is just and reasonable. *See Cal. Western Railroad & Nav. Co.* (1913) 2 CRC 584; *Re Regulation of Cellular Radiotelephone Utilities*, Decision (D.) 95-04-028, 59 CPUC 2d 192, 199, 201, 212-213, D.97-02-053, 71 CPUC 2d 162, 173.

We decline to order SBC California to rebill payphone service providers for the indirect rebates. We note SBC California’s per-call compensation was significantly lower than other carriers’ compensation. We further acknowledge SBC California may be able to restructure its fixed payments to qualify as compensation under the FCC rules. Thus, ordering SBC California to rebill payphone service providers for the “New Connect Award” might actually produce a windfall for SBC California but not accomplish the desired goal of ensuring that SBC California complies with statutes and Commission orders.

Pursuant to § 2107, we may impose fines for violations of our rules. We examine numerous factors, including severity of the offense, Commission precedent in comparable cases, the conduct of the utility in mitigating the offense, and the financial resources of the utility. (*See* D.03-01-070, 2003 Cal PUC LEXIS 45 *126; D.98-12-075, Appendix B.)

On the one hand, this violation of our rules was of limited duration. SBC California acted to avoid a direct rebate. However, Mpower was harmed.

Indeed, it lost payphone service providers to SBC California as a result of the “Fast Start Program,” although Mpower’s client states it would have moved to SBC California anyway for better service. The generosity of the “Fast Start Program” was at least responsible for the timing of the switch. Still, the violations demonstrated in this complaint are not as severe as violations raised in other complaints for which we ordered fines. (*See* D.03-01-070.) Thus, we determine fines are not warranted for this violation of § 532.

Having found a violation of § 532, we decline to address Mpower’s additional allegation that the “Fast Start Program” violates our price floor rules. Should SBC California seek an exception to § 532’s rebate of tariffed charges prohibition, SBC California should address whether granting such an exception is consistent with our price floor rules.

6. Motion for Protective Order

Mpower filed a motion for a protective order to protect from public disclosure certain portions of the confidential version of its opening brief and its response to SBC California’s appeal, which contain material concerning costs and accounting treatment of certain revenues SBC California asserts is proprietary and confidential. We have admitted into evidence under seal the material Mpower relies on in its brief and have granted requests for confidential treatment in this circumstance. We will issue an appropriate protective order.

7. Assignment of Proceeding

Michael R. Peevey is the Assigned Commissioner and ALJ Janice Grau is the presiding officer in this proceeding.

8. Appeal

The decision of the presiding officer, ALJ Grau, was mailed on November 4, 2004. Pursuant to Rule 8.2 of the Commission's Rules of Practice and Procedure, SBC California filed an appeal of the Presiding Officer's Decision (POD) on December 6, 2004. Mpower filed a response on December 20, 2004. This section addresses the issues raised in the appeal.

We first consider assertions of legal error raised by SBC California. As a threshold matter, SBC California asserts the POD violates the Supremacy Clause of the United States Constitution in finding that the "New Connect Award" is an indirect rebate. We disagree. The Supremacy Clause does not preempt § 532. In establishing rules for mandated compensation for "non-sent paid" calls, the FCC did not preempt state regulation of tariffed charges for COPT service. Further, as noted by Mpower, federal rules similarly prohibit improper rebates of tariffed charges. (*See* 47 U.S.C. § 203(c).) We find the POD properly weighed applicable federal requirements in determining the "New Connect Award" was an indirect rebate.

Next, SBC California asserts the POD erroneously relied on the similarity between the tariffed installation charge and the "New Connect Award" in finding the "New Connect Award" was an indirect rebate. SBC California acknowledges the "new line added" component of the "New Connect Award" and the installation charge were identical, \$112, but states the total payment package, not one component, is relevant. We find SBC California's argument unpersuasive. The total payment package is relevant if it is conclusively established that all components of the package are compensation and not rebates. The POD reached no such conclusion. Insofar as the "Fast Start Program" was a

package offering, it is not necessary to decide whether each payment contained in the package was a rebate. Although Mpower alleged all “Fast Start Program” payments were rebates, the POD did not find enough evidence to support that allegation. The POD properly analyzed whether the three one-time payments and one monthly payment were permissible compensation or improper rebates in reaching its conclusion that the “new line added” payment was an indirect rebate. If one component is an indirect rebate, the package containing that rebate violates § 532. Thus the POD properly ordered that SBC California terminate the “Fast Start Program.”

We next examine SBC California’s allegations of factual error. First, SBC California asserts the POD relied on an incorrect fact—that the “New Connect Award” was directly credited on payphone service providers’ bills. The record evidence indicates SBC California credited per-call compensation on payphone service providers’ bills, at G-Five’s direction. (RT 57:15-19.) The “Additional Compensation” agreement states SBC California will pay the one-time payments and will credit the monthly amount. (Exhibit 7, Attachment 1.) In its appeal, SBC California clarifies that all “Fast Start Program” payments were made by check to payphone service providers. The “new line added” payment was made within 30 days after the new connection was verified. (SBC California’s Appeal, p. 8.) We have clarified the decision in that regard.

SBC California states the POD misunderstands the significance of the “contra revenue” treatment SBC California mistakenly made. That “contra revenue” treatment is handling “New Connect Award” payments as “contra revenue” against the COPT access line revenue account instead of against the non-sent paid revenue accounts. We clarify the decision on that issue.

Finally, SBC states the POD's reliance on the alleged factual errors negates the POD's conclusion that the "new line added" component of the "New Connect Award" is an indirect rebate. We disagree. The POD's balance test weighs numerous factors in reaching its result. The result is independent of the factual clarifications discussed above. Nonetheless, we have modified the POD to incorporate an analysis of the factual clarifications.

Findings of Fact

1. SBC California, pursuant to its intrastate tariffs, bills and collects from payphone service providers a non-recurring charge of \$112 to establish a new COPT service line and a monthly service charge of \$14.53.
2. Under the "Fast Start Program," offered during 90 days in 2002, SBC California pays payphone service providers a fixed amount and a payment per new line added as a "New Connect Award," payable within 30 days of verification of the new order, another amount payable at the end of the 12-month term of the promotion, and a monthly amount. Retained lines receive an upfront fixed amount, a monthly amount, and an amount payable at the end of the promotion.
3. The FCC requires carriers to compensate payphone service providers for "non-sent paid" calls.
4. Pub. Util. Code § 532 provides that no public utility shall charge other than its tariffed rates. It further provides that no public utility shall refund or remit directly or indirectly any portion of its tariffed rates and charges unless such refund is on file and in effect at that time.
5. The "New Connect Award" was the same amount as the installation charge, was directly paid to payphone service providers, and was accounted for as "contra revenue," a credit to the COPT access line tariffed charge.

6. SBC California could restructure a fixed payment comparable to the “New Connect Award” that would be consistent with FCC requirements and would not constitute a rebate.

7. SBC California’s appeal has not shown the POD failed to make required findings or committed legal error. However, the POD has been modified as set forth herein.

Conclusions of Law

1. SBC California violated Pub. Util. Code § 532 by rebating the COPT line installation charge as a “New Connect Award” in the “Fast Start Program.”

2. The “Fast Start Program” should be terminated.

3. Due to the confidential and proprietary nature of certain identified materials received into evidence and contained in the confidential versions of Mpower’s opening belief and of Mpower’s response to SBC California’s appeal, it is reasonable that they remain under seal for two years unless a request made prior to the expiration of that time demonstrates a need for further protection.

4. Proposed modifications to the POD are adopted; otherwise, the appeal lacks merit and is denied.

5. It is reasonable to make this order effective today in order to resolve this complaint without further delay.

O R D E R

IT IS ORDERED that:

1. The complaint of Mpower Communications Corp. (Mpower) is granted as set forth herein and is otherwise denied.

2. Pacific Bell Telephone Company (SBC California) shall terminate the “Fast Start Program” and shall not reinstate it.

3. Mpower's motions for a protective order for the confidential versions of its opening brief and its response to SBC California's appeal are granted. Mpower's confidential opening brief and confidential response to appeal of presiding officer's decision shall remain under seal and not be accessible or disclosed to persons other than Commission staff absent an order of the Commission, the assigned Commissioner or administrative law judge (ALJ) or the law and motion ALJ, for a period of two years. If protection beyond that date is required, Mpower shall file a motion prior to the expiration of that period, explaining why further protection is needed.

4. This proceeding is closed.

This order is effective today.

Dated February 10, 2005, at San Francisco, California.

MICHAEL R. PEEVEY
President
GEOFFREY F. BROWN
SUSAN P. KENNEDY
DIAN M. GRUENEICH
Commissioners