**State of Florida** **REVISED 10/09/01**

# Public Service Commission

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

**DATE:** OCTOBER 4, 2001

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

**FROM:** DIVISION OF COMPETITIVE SERVICES (LOGUE, SIMMONS) SAS
DIVISION OF LEGAL SERVICES (FUDGE)

**RE:** DOCKET NO. 010345-TP - PETITION BY AT&T COMMUNICATIONS OF THE SOUTHERN STATES, INC., TCG SOUTH FLORIDA, AND MEDIA ONE FLORIDA TELECOMMUNICATIONS, INC. FOR STRUCTURAL SEPARATION OF BELLSOUTH TELECOMMUNICATIONS, INC. INTO TWO DISTINCT WHOLESALE AND RETAIL CORPORATE SUBSIDIARIES.

**AGENDA:** 10/16/01 - REGULAR AGENDA - MOTION TO DISMISS - PARTIES MAY PARTICIPATE

**CRITICAL DATES:** NONE

**SPECIAL INSTRUCTIONS:** NONE

**FILE NAME AND LOCATION:** S:\PSC\CMP\WP\010345.RCM

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## CASE BACKGROUND

On March 21, 2001, AT&T Communications of the Southern States, Inc., TCG South Florida and MediaOne Florida Telecommunications, Inc. (collectively, "AT&T"), filed a petition requesting that this Commission institute proceedings and enter an order requiring the structural separation of BellSouth Telecommunications, Inc. ("BellSouth") "into two distinct wholesale and retail corporate subsidiaries." Subsequently, on April 10, 2001, BellSouth filed its Motion to Dismiss, or in the Alternative, Motion to Strike AT&T's Petition seeking the Structural Separation of BellSouth. (First Motion to Dismiss) On May 2, 2001, AT&T filed a response opposing BellSouth's Motion to Dismiss.

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On April 10, 2001, the Florida Competitive Carriers Association (FCCA) filed its Request for Commission Investigation Concerning the Use of Structural incentives to Open Local Telecommunications markets in Support of AT&T's Petition to Initiate Proceeding. On April 17, 2001, BellSouth filed its Motion to Dismiss or in the Alternative Motion to Strike FCCA's Request. On May 2, 2001, FCCA filed its Response in Opposition to BellSouth's Motion to Dismiss FCCA's Request.

By Order No. PSC-01-1206-PCO-TP, issued May 30, 2001, the Commission found that a Commission workshop would provide the best forum to determine subsequent courses of action, which would include ruling on the Motions filed in this docket. A Commission Workshop (Workshop) was held on July 30 and 31, 2001, in Tallahassee.

On June 20, 2001, AT&T filed its Motion to Clarify and Amend Petition for Structural Separation. On July 2, 2001, BellSouth filed its Opposition to Motion to Clarify and Amend AT&T's Petition for Structural Separation. By Order No. PSC-01-1615-PCO-TP, issued August 8, 2001, AT&T's Motion to Amend its Petition was granted.

On August 28, 2001, BellSouth filed its Motion to Dismiss, Motion for More Definite Statement, and Motion to Strike Clarified and Amended Petition (Second Motion to Dismiss).

On September 10, 2001, AT&T filed its Response to BellSouth's Second Motion to Dismiss.

The Commission has jurisdiction over this matter pursuant to Section 364.01(4)(g), Florida Statutes.

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**DISCUSSION OF ISSUES**

**ISSUE 1:** Should BellSouth's Motions to Dismiss, or in the alternative Motions to Strike AT&T's Petition~~, filed April 10, 2001,~~ and FCCA's Request be granted?

**RECOMMENDATION:** No, the Motion regarding AT&T's Petition has been rendered moot. Staff's recommendation on BellSouth's Motion regarding FCCA's Request is subsumed in its recommendation in Issue 2 and 4. **(FUDGE)**

**STAFF ANALYSIS:** The arguments raised by BellSouth in its Motion assert that "(1)the Commission lacks subject matter jurisdiction over the relief requested; (2) AT&T fails to state a cause of action upon which relief can be granted; and (3) the Commission is barred by the operation of the Telecommunications Act of 1996 (Act) and other federal law from granting the requested relief." These arguments addressed the sole issue of whether the Commission could order full structural separation as requested by AT&T in its original petition.

By Order No. PSC-01-1615-PCO-TP, issued August 8, 2001, AT&T's Motion to Amend its Petition was granted. AT&T's amended petition clarified that it requests the Commission to consider all relief necessary or appropriate under the circumstances.

Consequently, BellSouth's Motion to Dismiss which was based solely upon the Commission's alleged inability to grant full structural separation, has been rendered moot.

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**ISSUE 2:** Should BellSouth's Motion to Dismiss, filed August 28, 2001, be granted?

**RECOMMENDATION:** No, the Motion should be denied with the understanding that the Commission's authority to order any relief will be made when the appropriate relief, if any, is determined. This analysis is also applicable to BellSouth's Motion to Dismiss FCCA's Request filed April 17, 2001. **(FUDGE)**

**STAFF ANALYSIS:** Under Florida law, the purpose of a motion to dismiss is to raise as a question of law the sufficiency of the facts alleged to state a cause of action. Varnes v. Dawkins, 624 So. 2d 349, 350 (Fla. 1st DCA 1993). In order to sustain a motion to dismiss, the moving party must demonstrate that, accepting all allegations in the petition as facially correct, the petition still fails to state a cause of action for which relief can be granted. In re Application for Amendment of Certificates Nos. 359-W and 290-S to Add Territory in Broward County by South Broward Utility, Inc., 95 FPSC 5:339 (1995); Varnes, 624 So. 2d at 350. When "determining the sufficiency of the complaint, the trial court may not look beyond the four corners of the complaint, consider any affirmative defenses raised by the defendant, nor consider any evidence likely to be produced by either side." Id.

BellSouth's Motion to Dismiss

BellSouth argues that to the extent the Clarified and Amended Petition seeks structural separation as relief, BellSouth moves that the Commission dismiss AT&T's Amended Petition. In support of this Motion, BellSouth incorporates by reference all arguments set forth in its First Motion to Dismiss.[1]

BellSouth argues that no statute expressly nor impliedly grants the Commission the authority to order structural separation. BellSouth states that when AT&T cites to an order of the Pennsylvania Commission in support of structural separation, AT&T fails to point out that the Pennsylvania Commission had the express authority to order structural separation. The same or similar authority does not exist in Florida. Consequently, the Florida

[1]These arguments were also incorporated in BellSouth's Motion to Dismiss FCCA's Request. Consequently, staff believes the conclusion reached herein is equally applicable to that Motion.

Public Service Commission does not have the express authority to order structural separation.

Next, BellSouth states that any implied authority must be derived from fair implication and intendment incident to any express authority. See Atlantic Coast Line R.R. Co. v. State, 74 So. 595, 601 (Fla. 1917); State v. Louisville & N.R. Co., 49 So. 39 (Fla. 1909). Moreover, if there is any reasonable doubt as to whether the Commission does or does not have the authority to order structural separation, BellSouth argues that it must be found that the Commission lacks the power. State v. Mayo, 354 So. 2d 359, 361 (Fla. 1977).

BellSouth also argues that the general authority over telecommunications companies contained within Section 364.01(2), Florida Statutes, does not impliedly authorize the Commission to split up a telephone company. BellSouth argues that if AT&T were correct in its contention that this statute authorizes the Commission to break up BellSouth, then the Commission would also have the less drastic remedy of awarding monetary damages. However, the Florida Supreme Court in Southern Bell Tel. Co. v. Mobile America Corp., 291 So. 2d 199, 202 (Fla. 1974), held that the Commission does not have the authority to award monetary damages, which is a judicial function.

BellSouth also points out that any implied authority must have been within the contemplation of the legislature when it passed the statute. Radio Telephone Communications, Inc. v. Southeastern Telephone Co., 170 So. 2d 577 (Fla. 1965). BellSouth states that Section 364.01(2), Florida Statutes, was enacted prior to the advent of local competition. Therefore, the Legislature could not have contemplated splitting up BellSouth into retail and wholesale entities, because there were no competitors to whom the company could sell its wholesale services.

BellSouth raises the same arguments regarding AT&T's reliance on Section 364.01(4)(c) and (i), Florida Statutes, in that those Sections were enacted prior to the removal of franchises to promote competition in the local telecommunications market.

Next, BellSouth argues that AT&T's interpretation of Section 364.01(2), Florida Statutes, contradicts the principle that Commission regulation cannot conflict with a company's corporate charter. See Southwestern Bell Tel. Co. v. Missouri Public Serv. Comm'n, 262 U.S. 276, 289, 43 S.Ct. 544, 67 L.Ed. 981 (1923); State

v. Western Union Telegraph Co., 118 So. 478, 479-480 (1928). Splitting up BellSouth would take away its fundamental rights to: (1)select a management and organizational structure; (2) be self-governing; and (3) make independent financial decisions for the benefit of its shareholders.

BellSouth also argues that Section 120.80(13)(d), Florida Statutes, neither grants the Commission any new substantive authority nor expands its existing substantive authority. Wither v. Department of Bus. & Prof. Reg., 662 So. 2d 1299, 1301-02 (Fla. DCA 1995). The statute merely addresses the procedures the Commission may employ to exercise its substantive authority.

BellSouth further contends that the language of Section 364.01(3), Florida Statutes, which says, "but nothing in this chapter shall limit the availability to any party of any remedy under state or federal antitrust laws," makes it clear that the legislature did not intend to authorize the Commission to order the antitrust relief that AT&T seeks in its Petition.

Next, BellSouth argues that the language of Sections 364.051 and 364.163, Florida Statutes, clearly indicates that the Legislature envisioned a single "local exchange telecommunications company" providing both retail services under Section 364.051 and wholesale services under Section 364.163, Florida Statutes.

BellSouth states that even if the Commission were authorized to break up BellSouth, the Commission could not order the remedy requested, because doing so would violate the Commerce Clause. Article I, Section 8 of the United States Constitution empowers Congress to "regulate Commerce . . . among the several states . . . ." Armstrong v. City of Tampa, 118 So. 2d 195, 199 (Fla. 1960). This provision has been construed to preclude states from "imposing any undue or unreasonable burden on interstate commerce." Id.

BellSouth argues that each state commission in which BellSouth operates could conceivably order BellSouth to create nine separate forms of corporate organization, which would constitute an impermissible burden on interstate commerce.

Next, BellSouth argues that Section 253(a) provides that "[n]o State or local statute or regulation, or other State or local legal requirement, may prohibit or have the effect of prohibiting the ability of any entity to provide any interstate or intrastate telecommunications service." 47 U.S.C. § 253(a). The company

mentions that splitting BellSouth into two separate entities, while prohibiting the wholesale entity from providing any telecommunications services to any end users, would clearly violate Section 253(a).

Moreover, argues BellSouth, splitting up BellSouth while not requiring the other ILECs or ALECs in Florida to undergo structural separation and the costs associated with that separation, would not be competitively neutral. See 47 U.S.C. § 253(b). While Sections 272(a)(1), (a)(2), and 274 of the Act, impose separate affiliate requirements, none of these requirements apply to the provision of any intraLATA telecommunications service.

BellSouth notes that Congress clearly envisioned one entity providing both wholesale and retail intraLATA services through the same corporate entity when it required incumbents "to offer for resale at wholesale rates any telecommunications service that the carrier provides at retail to subscribers who are not telecommunications carriers." 47 U.S.C. 251(c)(4)(A). If the wholesale entity provides no services to end users, there would be no retail rate for the services provided by the wholesale entity. Presumably the retail entity and other telecommunications service providers would pay TELRIC (Total Element Long Run Incremental Cost) based rates. BellSouth then poses the question: which entity has the resale obligation? BellSouth adds that AT&T's request to require BellSouth to unbundle its entire network from its retail offerings exceeds what the Supreme Court found acceptable in AT&T Corp. v. Iowa Utilities Board, 119 S.Ct. 721, 525 U.S. 366, 142 L.Ed.2d 835.

Finally, BellSouth argues that AT&T's Petition should be stricken because it does not comply with the requirements of Rule 1.110(f) of the Florida Rules of Civil Procedure. This argument is addressed in Issue Three.

AT&T's Response:

AT&T argues that there is no need to address BellSouth's Second Motion to Dismiss, because the Commission has previously ruled on whether AT&T's Clarified Petition is proper. AT&T contends that because the Order granting the Clarified Petition found that "it does not appear that BellSouth will be unduly prejudiced by the amendment," BellSouth's Motion to Dismiss should be denied. AT&T also incorporates all of the arguments set forth in its Memorandum in Opposition to Motion to Dismiss filed on May

2, 2001, as well as the arguments presented at the Commission workshop held July 30 and 31, 2001.

AT&T first notes that the Commission has "broad regulatory powers with regard to the telecommunications industry." GTC, Inc. v. Garcia, 778 So. 2d 923, 929 (Fla. 2001). AT&T contends that the Commission has broad jurisdiction to "protect the public health, safety and welfare by ensuring that basic local telecommunications services are available to all consumers in the state at reasonable and affordable prices." Section 364.01(4)(a), Florida Statutes. AT&T points out that this public welfare jurisdiction has been construed expansively to include the implied authority under Section 364.01(3)(a) to order the transfer of title. See Telecom Communications Co. v. Clark, 695 So. 2d 304 (Fla. 1997).

AT&T contends that when the Legislature amended Chapter 364 in 1995, it expressly considered the encouragement of local competition and explicitly stated the intent to foster Local Exchange Carrier ("LEC") competition in Section 364.01(3). AT&T also cites to other provisions of Chapter 364 which authorize the Commission to eliminate specific forms of anticompetitive conduct.[2] Therefore, under both Chapter 364 and the Act, the Commission may define anticompetitive conduct and fashion an appropriate remedy, according to AT&T. See Otter Tail Power Co. v. United States, 410 U.S. 366 (1973); U.S. v. Terminal Railroad Assoc. of St. Louis, 224 U.S. 383 (1912); MCI Communications v. American Telephone and Telegraph, Inc., 708 F. 2d 1081 (7th Cir.), cert. den., 464 U.S. 891 (1983).

AT&T further alleges that under federal enabling authority conferred on the FCC, similar to the Florida Legislature's grant of authority, the courts have upheld the FCC's implied authority to order structural separation. See e.g., GTE Service Corp. v. Federal Communications Comm'n, 474 F. 2d 724, 729-732 (D.C. Cir. 1973)(holding that order of structural separation was within the FCC's general enabling authority to promote efficient economical

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[2]Section 364.051(5)(a)(2), provides that a LEC "shall not engage in any anticompetitive act or practice, nor unreasonably discriminate among similarly situated customers; Section 364.051(5)(c), prohibits LECs from engaging in below cost or predatory pricing; Section 364.058(1), gives the Commission authority "to *conduct a limited or expedited proceeding to consider and act* upon any matter" within its jurisdiction under the statute; Section 364.01(4)(g), requires the Commission to "[e]nsure that all providers of telecommunications services are treated fairly, by preventing anticompetitive behavior and eliminating unnecessary regulatory restraint."

telephone service.); see also Policy Rules Concerning Rates for Common Carrier Services and Facilities Authorization Therefore, FCC Docket No. 79-252, Fifth Report and Order, 98 FCC 2d 1191 (1984)(noting other instances where the FCC has implemented structural separation without a challenge from affected entities).

AT&T further argues that Section 120.80(13)(d), Florida Statutes, gives the Commission express authority to implement the Act. Order No. PSC-99-0769-FOF-TP, issued April 21, 1999, in Docket No. 981834-TP ("FCCA Proceeding"). In the FCCA proceeding, the Florida Competitive Carriers Association (FCCA) and certain ALECs (including AT&T) requested pro-active and declaratory relief to promote LEC competition. BellSouth filed a motion to dismiss, arguing that the Commission had "no legal authority to implement procedures other than those provided by the Act." In rejecting BellSouth's motion to dismiss, the Commission stated:

> Put simply, processes designed to further open the local competition are entirely consistent with the purposes and procedures of the Act. If the Commission finds that the requested relief is designed to achieve that goal and does not undermine the procedures prescribed by the Act, then the relief is well within the legal authority of the Commission.

Next, AT&T responds to BellSouth's attempt to distinguish Bell Atlantic, by arguing that the FPSC's jurisdiction is at least as broad as that of Pennsylvania's public utility laws, which do not contain the "public welfare" and "anticompetitive behavior" mandates contained within Chapter 364.

AT&T also disagrees with BellSouth's interpretation of Mobile America Corp. that because the Commission cannot award monetary damages, the Commission also lacks subject matter jurisdiction to order structural separation. 291 So. 2d 199. AT&T points out that Mobile America Corp. merely holds that "primary jurisdiction in a tort action does not rest with the PSC and that the PSC does not have authority to award damages for past failure to meet service standards." Id. at 234.

Similarly, AT&T argues that Radio Telephone does not stand for the proposition that any implied authority must have been contemplated by the Legislature when it passed the statute, as BellSouth has argued. 170 So. 2d 577 (Fla. 1965). AT&T states that the court's holding was based upon a finding that Chapter 364

did not apply to the entire radio service communication industry, which was then considered a "new type of communications service[]." Id. at 582.

Next, AT&T argues that Western Union does not prevent the Commission from ordering any remedy that would impede certain rights BellSouth enjoys pursuant to its charter. 118 So. 2d at 478 AT&T states that in Western Union the Florida Supreme Court held that requiring Western Union Telegraph to place a telegraph station in a specific location was not justified by the evidence. Id. "Being creatures of statute, corporations are amenable to all reasonable regulations imposed by statute, both as to their internal operation and as to the rights of those who own them, their stockholders." Florida Telephone Corp. v. State, 111 So. 2d 677, 679 (Fla. 1st DCA 1959).

AT&T states that there are three ways in which state law is preempted by federal law: (1) when Congress explicitly defines the extent to which it intends to preempt state law when enacting federal law; (2) Congress indicates an intent to occupy an entire field of regulation and left no room for States to supplement the federal law; and (3) when compliance with both state and federal law frustrates the objectives of Congress. See Michigan Canners and Freezers Ass'n., Inc. v. Agricultural Marketing and Bargaining Board, 467 U.S. 461, 469 (1984). AT&T argues that the Act expressly preserves state commission authority over local telephone competition and does not occupy the entire field of regulation.[3]

AT&T contends that the proposed remedy is consistent with the Act and its goal of achieving competition in local telephone markets. AT&T states that in Bell Atlantic, the court rejected the arguments structural separation would create an "impermissible barrier to entry," by holding that where "the state agency mandate is that Bell provide retail services through a structurally separate affiliate, albeit operating independently, it cannot be said that Bell as a business organization is being precluded on the

[3]See 47 U.S.C. § 152(b), reserving to the states existing jurisdiction over intrastate communications; 47 U.S.C. § 251(d)(3), stating that the [FCC] shall not preclude the enforcement of any regulation, order, or policy of a State commission . . . ."; 47 U.S.C. § 253, stating that "[n]othing in this section shall affect the ability of a State to impose, on a competitively neutral basis and consistent with section 254, requirements necessary to preserve and advance universal service, protect the public safety and welfare, ensure the continued quality of telecommunications services, and safeguard the rights of consumers."

whole from providing retail services." Id. 763 A. 2d at 463. The court also rejected the argument that structural separation would not be "competitively neutral" when it stated:

> [E]xamination of the [competitively neutral] requirement shows that the wholesale-retail separation is just that - competitively neutral in the practical sense that its intent is to insure neutrality in competition and thereby protect consumers' rights to choice of suppliers without encountering the higher costs which ensue from lack of competition.

Id. 763 A. 2d at 463.

The Bell Atlantic court also rejected the argument that structural separation was limited to equipment manufacturing and certain long-distance and information services and electronic publishing services by stating:

> However, the straightforward terms of those sections only describe those services for which the federal law mandates separate affiliates; in no way do those sections constrain a state regulatory body from requiring separated affiliates for other functions.

Id.

AT&T also argues that structural separation requiring BellSouth to modify its corporate structure is not equivalent to the unbundling of BellSouth's network elements; and thus, BellSouth's reliance on Iowa Utilities Board is misplaced. 119 S.Ct. 721.

AT&T contends that the Commerce Clause is not implicated in this instance, because the proposed action involves regulation over local intrastate telephone competition, over which Congress has preserved the State's authority under the dual federal and state regulatory scheme. Moreover, the Commission's action in this proceeding to promote competition in the local intrastate telephone markets would be in the national interest, and therefore, would not violate the Commerce Clause.

AT&T states that unlike Southern Pacific Co. v. Arizona, 325 U.S. 761 (1945),where the achievement of the national interest was unduly burdened and obstructed by a competing state interest, the

goal of promoting local telephone competition is both a national and state interest. AT&T asserts that BellSouth's Commerce Clause challenge fails because it is too early to determine whether structural separation is "clearly excessive" compared to the benefits of local telephone competition. While BellSouth has stated that structural separation would cause transactional and administrative burdens, AT&T claims BellSouth has failed to show how such burdens are a burden to interstate commerce or obstruct a national interest. Whether BellSouth would have to face varying requirements in different states is a matter for each state's public utility commission to make.

Finally, AT&T states Rule 25-22.036(3)(b), Florida Administrative Code, and not Rule 1.100(f) of the Florida Rules of Civil Procedure, applies to this proceeding. As stated above this issue is fully addressed in Issue Three.

Staff's Analysis

The main thrust of BellSouth's Second Motion to Dismiss is whether the Commission has the authority to order full structural separation.

While the Commission has broad authority to regulate the telecommunications industry, it only has those powers expressly granted by statute or necessarily implied. See Florida Interexchange Carriers Ass'n v. Beard, 624 So. 2d 248, 251 (Fla. 1993); Deltona Corp. v. FPSC, 220 So. 2d 905, 907 (Fla. 1969). Section 364.01, Florida Statutes, states that "the transition from the monopoly provision of local exchange service to the competitive provision thereof will require appropriate regulatory oversight to protect consumers and provide for the development of fair and effective competition . . . ." Moreover, Section 364.01(4)(g), Florida Statutes, requires the Commission to exercise its exclusive jurisdiction to "[e]nsure that all providers of telecommunications services are treated fairly, by preventing anticompetitive behavior and eliminating unnecessary regulatory restraint."

AT&T alleges that BellSouth's anticompetitive actions result from an inherent conflict of interest. Namely, its contradictory roles as both the operator of the local telephone network that virtually all ALECs rely upon, and its role as the principal competitor of those same ALECs in the retail markets. AT&T argues that to remedy this inherent conflict of interest, BellSouth must

be separated into two distinct wholesale and retail subsidiaries.

Assuming, arguendo, that these allegations are true, then the Commission must determine whether it has the authority to order structural separation. While staff agrees that the Commission does not have the express authority to order structural separation, at this time, staff believes that the Commission may have the authority to do so by necessary implication.

"A statutory grant of power or right carries with it by implication everything necessary to carry out the power or right and make it effectual and complete." Deltona Corp., 220 So. 2d at 907.[4] When Chapter 364 was amended in 1995, the legislature found "the competitive provision of telecommunications services, including local exchange telecommunications service," to be in the public interest. § 364.01(3), Fla. Stat. (2000). "Under this new scheme, the Commission is charged with exercising its exclusive jurisdiction in order to encourage and promote competition in telecommunications services." Florida Interexchange Carriers Assoc. v. Clark, 678 So. 2d 1267, 1269 (Fla. 1996).

Clearly, the statutes provide that the Commission must promote competition and prevent anticompetitive behavior. If, in fact, structural separation is the only means to accomplish that mandate, then by necessary implication, the Commission has the authority to order structural separation. See Order No. PSC-99-0769-FOF-TP, issued April 21, 1999, in Docket No. 981834-TP, (finding that if "the requested relief is designed to further local competition and do[es] not undermine the procedures prescribed by the Act, then the relief is well within the legal authority of the Commission.")

However, based on the pleadings, and again, assuming arguendo the truth of the allegations before the Commission, staff is unable to determine: whether structural separation is the only means to eliminate alleged anticompetitive behavior; whether structural separation is necessary to promote competition; and/or whether

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[4]BellSouth has argued that the implied authority must have been in the contemplation of the legislature when it passed the statute. See Radio Telephone Communications, Inc. v. Southeastern Telephone Co., 170 So. 2d 577, 581 (Fla. 1965). However, staff agrees with AT&T that this holding only stands for the proposition that the Commission cannot use its authority over telecommunications to regulate the entire radio service communications industry. Here, the Commission has authority over telecommunications at issue and is being asked to exercise that authority.

structural separation will eliminate alleged anticompetitive behavior in the best interests of the public.

Staff believes and recommends to the Commission that structural separation is a remedy which may very well be within the scope of the Commission's jurisdiction. Whether it is the appropriate remedy is another matter. That determination must follow from careful consideration of an evidentiary record in which allegations and defenses are put to their proof.

Consequently, staff recommends that to determine whether full structural separation would fulfill the legislative mandate to promote competition and therefore confer the authority to do so by necessary implication, an evidentiary hearing must be held. See FPSC v. Bryson, 569 So. 2d 1253, 1255 (Fla. 1990)(holding that so long as the Commission has a colorable claim of jurisdiction, it has the authority to proceed with a determination of whether it indeed has jurisdiction). Only then will staff be able to make an informed recommendation on whether structural separation will promote competition in Florida.

**ISSUE 3:** Should BellSouth's Motion for More Definite Statement and Motion to Strike Clarified and Amended Petition, filed August 28, 2001, be granted?

**RECOMMENDATION:** No, the Motions should be denied. **(FUDGE)**

**STAFF ANALYSIS:**

BellSouth

BellSouth argues that AT&T's request that the Commission "order all relief necessary or appropriate as the facts and circumstances requires" prejudices BellSouth in that it must speculate as to what relief AT&T is seeking. Without this knowledge, BellSouth contends that it is unable to prepare a defense to these unlimited, unspecified claims for relief. Moreover, it is necessary to specify the type of relief requested so that the parties and the Commission can determine whether the Commission has the authority to order the requested relief. Therefore, BellSouth requests that pursuant to Rule 1.140(e), Florida Rules of Civil Procedure, and Rule 28-106.24, Florida Administrative Code, AT&T provide a more definite statement as to the specific type of relief requested.

In addition, BellSouth also requests that the Commission strike the Amended Petition because it does not identify the specific relief requested and therefore, fails to comply with Rule 25-22.036, Florida Administrative Code. Moreover, the Amended Petition does not satisfy the basic pleading requirements, including the requirement that the Petition identify the actions that allegedly constitute a violation of rule, order or statute as set forth in Rule 25-22.036, Florida Administrative Code.

AT&T

AT&T asserts that it has complied with Rule 25-22.036, Florida Administrative Code, and that the Rule does not prohibit a petitioner from seeking general relief in addition to the specific relief requested. AT&T contends that its Petition alleges: BellSouth's failure to provide unbundled network elements in a nondiscriminatory manner, as required by Chapter 364, Florida Statutes, and the Act; the facts constituting BellSouth's anti-competitive behavior; the specific relief requested, structural separation, as well as any other necessary and appropriate relief.

In its Memorandum in Opposition to BellSouth's Motion to Dismiss, AT&T cited to its original petition which alleged that BellSouth violated the Act by engaging in the following practices:

- ALECs using BellSouth's OSS must wait much longer than BellSouth's retail arm to obtain access to BellSouth's network. (Petition at p. 11)

- BellSouth has not devoted sufficient technical and related resources necessary to develop OSS which provide parity to ALECs. (Petition at p. 12)

- BellSouth is unwilling to provide UNEs in the manner requested by ALECs and on the same terms and conditions as BellSouth provisions its own retail services. (Petition at p. 13)

- BellSouth has established retail prices that inure to the detriment of ALECs in Florida. (Petition at p. 14)

- Florida lags behind the national average, in that ALECs have only a 6.1 percent market share in the state. (Petition at p. 15)

Analysis

Staff believes that AT&T has complied with each of the requirements of Rule 25-22.036(3)(b), Florida Administrative Code., which states that

> Each complaint, in addition to the requirements of paragraph (a) above shall also contain:
> 1. The rule, order, or statute that has been violated;
> 2. The actions that constitute the violation;
> 3. The name and address of the person against whom the complaint is lodged;
> 4. The specific relief requested, including any penalty sought.

To the extent that AT&T's general request for relief may require the Commission to determine its authority to grant such relief, staff recommends that be determined concomitantly with the determination on the appropriate relief, if any.

**REVISED 10/09/01**

**ISSUE 4:** Should the Commission proceed to hearing on AT&T's Amended Petition to consider structural separation of BellSouth, as well as other remedies?

**RECOMMENDATION:** Yes, the Commission should set this docket for hearing and continue its investigation of the matters raised in AT&T's Amended Petition and FCCA's Request. **(LOGUE, SIMMONS, FUDGE)**

**STAFF ANALYSIS:**

Workshop Policy Arguments

Most workshop participants recognized that the local telecommunications market is at a crossroads, with competing visions as to the appropriate role of regulation. Most CLECs take the position that attempting to develop local competition by continued reliance on regulatory enforcement is very time consuming, resource intensive, and ineffective. Structural separation is seen as a way of aligning incentives such that BellSouth's wholesale entity would be dealing with all retail entities on an equal footing. According to the CLECs, this would eliminate the inherent conflict of interest with BellSouth being the dominant retail provider and also the dominant supplier upon which its competitors rely.

According to the ILEC representatives, structural separation is premised on the belief that local telecommunications remains essentially a natural monopoly. To the contrary, ILECs perceive local telecommunications as rapidly becoming a natural competitive market. In addition to the one-time and ongoing costs of structural separation, which will be passed on to end users in the form of higher rates, ILECs argue that such a plan would reduce BellSouth's incentive to invest. In addition, ILECs believe that CLECs would also have less incentive to invest, since entrants could rely on the BellSouth wholesale entity and minimize the inherent risks associated with investing. Less investment would translate into less innovation.

To the extent workshop participants suggested specific remedies, staff briefly discusses them below. To the extent workshop participants discussed only support for or against

structural separation, their support is recognized, but not specifically discussed herein.

Among the proposals presented, Mr. Gillan, representing the Florida Competitive Carriers Association (FCCA), suggested that the goal of structurally separating BellSouth is to have arms-length transactions wherein the OSS would be the same so that there is parity by design, not parity by performance measures, and also the same cost basis for the common network. (TR 133) Additionally, however, Mr. Gillan stated that a consequence, per se, of functional separation is that the retail arm would forever be considered an ILEC and would still have the Section 251 obligations associated with being an ILEC. (TR 135) Mr. Gillan further identified a "middle ground" between functional separation and full divestiture. (TR 135) Mr. Gillan suggested that a middle ground could be the issuance of a publicly traded stock for the retail entity, the majority of which would be held by a holding company with BellSouth the majority owner. The stockholders could then trade this stock, thus allowing for market valuation. (TR 135) Mr. Gillan stated that the "advantage of this type of structure is that for the first time here, the managers of that retail arm would have to report back to stockholders different than BellSouth stockholders . . . ." (TR 135-136) Mr. Gillan further stated that this type of approach would promote economic transparency between the affiliates. (TR 136)

Speaking on behalf of AT&T, Mr. Morrissey stated that the challenge, in terms of implementation, "will be to determine whether there is any ILEC separation methodology short of complete wholesale retail business divestiture that will allow demonopolization and competition to occur." (TR 164) Also speaking on behalf of AT&T, Mr. Bradford stated that "structural separation substitutes economic self-interest for regulatory oversight . . . it aligns corporate incentives with public policy goals and with the best interest of the customers . . . ." (TR 199)

Ms. Sheldrew, on behalf of AT&T, intimated that the challenge to regulators is to determine whether and how the incumbent utility is to be allowed to play two roles: (1) allow the single entity to provide both monopoly and competitive services; or (2) preclude a single affiliate from performing both non-competitive and competitive services, but allow activities in separate affiliates, provided there are code of conduct requirements. Another approach is to permit no mixing of non-competitive and competitive services in the same corporate family. (TR 205-207)

While the record at this point is incomplete, staff believes the points presented thus far warrant additional consideration. For example, Ms. Sheldrew stated that the Nevada Commission established in its affiliates code of conduct an arms-length relationship. This relationship limited the use of certain shared services between the competitive and non-competitive affiliates and restricted the use of shared officers and employees. (TR 207-208) Further, the Nevada Commission established transfer pricing rules for the transfer of goods and further prohibited the competitive (i.e., retail) affiliate from having a name that was similar to the non-competitive affiliate and had restrictions on the use of corporate logos and names. (TR 208)

Ms. Sheldrew further stated that the benefits of structural separation are stronger competition in local markets, greater protection to consumers, and improved efficiency in the regulatory process. (TR 209) Mr. Graham, in summing up AT&T's position, stated that "only full and complete structural separation will get to the core problem . . . any alternative remedy is not going to get us to the full and fair open competition that we are all seeking." (TR 214)

Mr. Ball, on behalf of WorldCom, took the position that the greatest benefit would come from a complete divestiture or creation of the same type of environment that a full divestiture would provide. (TR 251) Mr. Ball further believes that ". . . the separation in ownership would require a line of business restriction on the monopoly wholesale company, but it would also change their incentives." The wholesale company would be forced to treat all CLECs, including BellSouth's retail unit, on a more equal footing. (TR 251)

In discussing what would happen if BellSouth were structurally separated, Mr. Kramer, representing IDS Telecom, suggested that BellSouth's retail company would seriously entertain buying services from a company that was fifty percent less expensive than BellSouth. Additionally, Mr. Kramer lamented that BellSouth retail would become the largest consumer of a wide variety of cost-effective services and products offered by other wholesalers in order to stay competitive. (TR 274) Mr. Kramer further stated that it is the marketplace that could force BellSouth wholesale to reduce costs and improve services and introduce new products. (TR 275)

Speaking to the position of the ILEC, Mr. May, of the Progress and Freedom Foundation, believes that there are two competing visions in terms of how to regulate telecom companies: (1) telecom remains a natural monopoly and how does a commission shape future regulations, or (2) telecom is rapidly becoming a natural competitive market. (TR 330) Mr. May further states that the questions facing this Commission are how to assist this transition, and what regulations are needed for the remaining pockets of monopoly. (TR 330) Mr. May states that the proposals to create a structurally separate "LoopCo" assume that the local loop is an essential facility in a monopoly antitrust sense for the indefinite future. (TR 330) In quoting the Pennsylvania Commission (in reference to its findings regarding the structural separation of Verizon, Pennsylvania) Mr. May professes, "The parties have convincingly argued that even with the implementation of structural separation of Verizon's wholesale and retail arms, no less regulatory oversight than that currently prevailing will be required to ensure compliance." (TR 331) Staff believes there could be a significant amount of oversight required by this Commission should the structural separation of BellSouth or others similarly situated, be ordered. It is certainly a factor that deserves additional scrutiny. Finally, Mr. May expresses concern that excessive regulation, in the form of structural separation or some other alternative, will discourage investment by both BellSouth and CLECs. (TR 335,340)

Verizon representative, Ms. Caswell, advised the Commission that the only conclusion to be drawn here is that there is no problem, at least not a problem of the ILEC's making. Ms. Caswell alleged that it is not the ILEC's fault that the capital markets have dried up for some CLECs, many of which did not have realistic business plans. (TR 355) In fact, Ms. Caswell stated that structural separation would precipitate increases in both wholesale and retail rates. (TR 355)

In describing the terms of the settlement reached with the Pennsylvania Commission, Verizon representative Mr. Whelan stated that there was not a structural separation, but instead a functional separation. Additional requirements included a code of conduct, levels of penalties for nonperformance under the state's performance plan, creation of a consumer education fund, a universal service fund that would last a couple of years and temporary UNE rate reductions in the most rural areas of Pennsylvania. And while there are others, Mr. Whelan described only the aforementioned. (TR 373) When asked by a Commissioner how

the functional separation component of the settlement works, Mr. Whelan advised that this component would require that all orders that come in from the CLECs would come in through a separate channel, i.e., the service reps would take the orders that flow directly in those legacy systems, and the legacy systems would then either mechanically, automatically, or with human intervention get the order worked. (TR 374) Mr. Whelan further alluded to the Commission having the means at its disposal to assure parity, which he believes goes a long way to alleviating many of the concerns of the competitors. (TR 377)

A common thread among many presenters was cost. However, very few actually addressed cost specifics regarding the structural separation of BellSouth. It would be safe to assume the lack of discussion on this topic was because very few can provide an accurate estimate of the costs involved with such a breakup. However, Mr. Malone, of the Eastern Management Group, did indicate that whatever the amount of money needed to structurally separate a company into two, the customer will see the majority of the cost passed on to them. (TR 412) Mr. Malone further indicated that he did not believe structural separation would be in the best interest of the ALECs, nor would it be in the best interest of Florida's consumers. (TR 413)

In relating his position on behalf of the ILEC, Mr. Danner, formerly of the California Commission, stated that the parallel between the electricity problems [of California] and the structural separation discussion lies in two general areas. (TR 434)

> The first is the attempt by government to formulate some sort of comprehensive market vision as to where it thinks an industry is going, and then to impose that vision forcefully or forcibly on the industry, and then to have something go wrong. The second parallel lies in the difficulty government then has in trying to adjust or adapt to what has gone wrong and to rescue the situation on a timely basis, or on a basis that won't come at great disruption and cost. (TR 434)

Mr. Wilk, on behalf of the ILECs and also formerly of the California Commission, related that there are five tests he used when viewing controversial issues such as the structural separation issue currently before the Florida Commission. First, is there genuine customer interest and demand in any of this? Secondly, where is the balance of cost and benefits? Are they tangible? Are

they speculative? Thirdly, what are the implications for regulatory policy in terms of complexity and cost . . . for everybody? Fourth, what is the exit strategy? And lastly, does it pass the straight face test? Who really wants it and why do they want it? (TR 458-459) Staff believes that Mr. Wilk's "test" is both thought-provoking and raises issues this Commission should address further.

Workshop Legal Argument

BellSouth

At the workshop BellSouth raised an additional argument, which staff believes does merit some discussion even though it was not contained in either Motion to Dismiss. That argument questions whether a finding that the Commission has the implied power to structurally separate BellSouth would require a finding that the legislature intended to allow the commission to deregulate the newly formed wholesale entity. BellSouth contends that such an intent is unpalatable. Staff notes that it addresses this argument for informational purposes only.

In support of its argument, BellSouth cites to Section 364.02(12), Florida Statutes, which defines "telecommunications company" as "every corporation, partnership, and person . . . offering two-way telecommunications service to the public for hire within this state by the use of a telecommunications facility." This definition expressly excludes "an entity which provides a telecommunications facility exclusively to a certified telecommunications company." § 364.02(12)(a), Florida Statutes. If BellSouth were structurally separated into two distinct retail and wholesale entities, the company contends that the wholesale entity would then cease to provide telecommunications service to the public and would be providing telecommunications facilities exclusively to certificated telecommunications carriers.

Verizon

Like BellSouth, Verizon (a workshop participant) argued that the wholesale company would cease to be regulated by the Commission. In addition, Verizon argues that the retail company, would be regulated as an ALEC, not an ILEC. This would require resolution of carrier of last resort obligations and universal service issues.

Verizon also responded to AT&T's assertion that if the Commission lost state jurisdiction over the wholesale company, then the 1996 Act would confer jurisdiction over the wholesale company. Verizon stated that the Act does not confer to state commissions any independent jurisdiction over companies it cannot regulate under its own state law. Moreover, Verizon contends that even if the Act were read to confer independent state jurisdiction, the "ILEC" obligations of Section 251(c) would not apply to the new wholesale company. Under the Act,

> the term 'incumbent local exchange carrier' means, with respect to an area, the local exchange carrier that -
> (A) on the date of enactment of the Telecommunications Act of 1996, provided telephone exchange service in such area; and
> (B)(i) on such date of enactment, was deemed to be a member of the exchange carrier association pursuant to section 69.601(b) of the Commission's regulations (47 C.F.R. 69.601(b)); or
> (ii) is a person or entity that, on or after such date of enactment, became a successor or assign of a member described in clause (i).
>
> 47 U.S.C. § 251(h)(1)

The new wholesale company did not exist and thus, could not have been providing exchange service when the Act was adopted. Moreover, in a decision regarding the structural separation proposal for Southern New England Telephone Company (SNET), the court held that the divided SNET wholesale entity would not have 251(c) obligations. MCI TeleComms. Corp. v. Southern New Eng. Tel. Co., 275 F. Supp. 2d 326(1998).

Verizon also argues that the wholesale company could not be treated as an ILEC under section 251(h)(2), which allows the FCC to determine, by rule, that a "local exchange carrier" is to be treated as an ILEC if the carrier occupies a market position "comparable to the position occupied by the [ILEC]" and it has "substantially replaced an ILEC." Verizon argues that even if the wholesale company were designated a "local exchange carrier," it would not occupy a comparable position.

Finally, Verizon argues that even if a state commission were to impose structural separation, the FCC would be required to preempt it. Section 253 of the Act requires the Commission to

preempt any state legal requirement that "may . . . prohibit the ability of any entity to provide any . . . telecommunications service." Preventing the wholesale company from providing retail services, as urged by AT&T, would violate section 253 of the Act.

ALECs

The ALECs contend that BellSouth's argument does not apply to the form of structural separation most focused on at the workshop. Under that proposal, the BellSouth wholesale company would continue to serve existing retail customers, while the BellSouth retail company would serve new retail customers. Consequently, as long as BellSouth wholesale is still serving one retail customer, it would continue to be regulated as a "telecommunications company."

Moreover, they contend that BellSouth's argument is premature, because it focuses solely on one particular remedy that might be imposed, when the fundamental question is whether the Commission has the jurisdiction to continue this proceeding. Even if one alternative out of the many presented might ultimately lead to deregulation of BellSouth's wholesale service, they believe that BellSouth's argument provides no basis for finding that the Commission lacks jurisdiction to conduct proceedings on the petition. The ALECs argue that to preclude further proceedings on this matter out of the fear that one of the possible remedies may lead to deregulation of the wholesale company is contrary to the legislative directive to "encourage competition through flexible regulatory treatment." § 364.01(4)(b), Florida Statutes.

Furthermore, the ALECs argue that even if structural separation would deregulate the wholesale entity, the Commission would still have jurisdiction under the Federal Act. See AT&T Corp. v. Iowa Utilities Board, 525 U.S. 366, 199 S.Ct. 721 (1999). They contend that the wholesale entity would still qualify as an ILEC under Section 251(h) of the Act. Consequently, the wholesale entity would have obligations regarding number portability, interconnection, and unbundled access to network elements. See 47 U.S.C. § 251(b).

Staff's Analysis

Staff agrees with the ALECs that it would be premature at this time to determine whether or not any and every wholesale entity resulting from any remedy ultimately implemented in this Docket would be regulated by this Commission. Staff notes, however, that this Commission derives its authority to act in this case from state law; thus, it would appear, based on Section 364.02(12), Florida Statutes, that the Commission's authority to regulate a fully separate wholesale entity that "provides a telecommunications facility exclusively to a certificated telecommunications company" may be limited to some degree. However, simply because there is the possibility that a resulting wholesale entity may be deregulated does not necessarily mean that the Commission would be precluded from ordering structural separation. To the contrary, as stated herein, if the Commission determines that full structural separation of BellSouth is necessary to prevent anticompetitive behavior and encourage competition, it appears that the Commission could take this action, even if it means the resulting wholesale entity could be deregulated.

**CONCLUSION**

Staff believes that the workshop participants have all provided serious points to be considered, both for and against the structural separation of BellSouth. To that end, staff believes that, while the information provided by all participants is very educational and thought-provoking, there is additional information that needs to be obtained, digested and scrutinized. It is clear from the workshop that no one presented a well-conceived plan or remedy. In addition, no one presented a serious benefit/cost analysis. To proceed in this case, considerable discovery will be needed to address these important voids as this evidence will have a significant bearing on the selected remedy, if any. Staff believes that the practical, technical and legal considerations are just as prevalent, or perhaps more so, than initially believed.

Therefore, staff believes that this matter should formally proceed so that evidence may be obtained from all interested persons and parties. Such evidence would include, but not be limited to, alternative approaches to full structural separation, the qualitative and quantitative benefits and costs from a variety of perspectives, the legal impediments to implementing alternatives, and the impacts, if any, on BellSouth's obligations as they relate to the Telecom Act and Florida Statutes.

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Staff notes that this matter need not go to hearing in the near term. Several dockets are currently pending, which may address and mitigate AT&T's concerns, and conceivably even render some issues moot.

Finally, staff wishes to make it clear that if AT&T's and FCCA's allegations stand the test of proof, which at this point we cannot know, structural separation is but one remedy among others available to the Commission. In other words, staff believes that the proof, if any, will determine the need and nature of the remedy.

**ISSUE 5:** Should this docket be closed?

**RECOMMENDATION:** No, based on staff's recommendations in Issues 1, 2, 3, and 4, this docket should remain open. **(FUDGE, LOGUE, SIMMONS)**

**STAFF ANALYSIS:** As stated above, staff believes that further evidentiary proceedings need to be held. Consequently, this docket should remain open to determine the appropriate remedy, if any.