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IN THE SUPREME COURT STATE OF FLORIDA

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| FLORIDA CABLE TELEVISION ASSOCIATION, INC., Appellant, v. J. TERRY DEASON, Chairman, THOMAS M. BEARD, SUSAN F. CLARK, LUIS J. LAUREDO, and JULIA L. JOHNSON, Commissioners, as and constituting the FLORIDA PUBLIC SERVICE COMMISSION, an agency of the State of Florida, Appellees. | Case No. 82,281<br>FPSC Docket No. 910757-TP<br>Filed: 11-29-93 |

# ANSWER BRIEF OF APPELLEE SOUTHERN BELL TELEPHONE AND TELEGRAPH COMPANY AS A PARTY OF RECORD IN THE PROCEEDINGS BELOW

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| v. | |
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**ANSWER BRIEF OF APPELLEE**
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## PRELIMINARY STATEMENT

Pursuant to Section 350.128, Florida Statutes (1991), Southern Bell Telephone and Telegraph Company, as a party who entered an appearance of record in the proceedings below before the Florida Public Service Commission, files its Answer Brief. This Brief utilizes the following abbreviations:

Appellant, The Florida Cable Television Association: "FCTA" or "Appellant"

Appellee, Florida Public Service Commission: "Commission"

Appellee, Southern Bell Telephone and Telegraph Company: "Southern Bell"

Local Exchange Company: "LEC"

In addition, Southern Bell will indicate references to the materials listed below as follows:

Transcript of the hearing held March 10-11, 1993: (Tr. at ___).

Record on Appeal: (R. ____).

Southern Bell's Appendix to this Answer Brief: (App. at ___).[1]

Exhibits introduced at the hearing held March 10-11, 1993: (Ex. ____)

Appellant's Initial Brief: (FCTA Brief at ____).

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[1] The index to this Answer Brief contains the Final Order entered by the Commission in this case (Order No. PSC-93-1015-FOF-TP, entered July 12, 1993) and the Commission's Order Establishing Procedure, which was entered in this case on November 16, 1992 (Order No. PSC-92-1323-PCO-TP). Citations in this Brief to each Order will refer to the page of the Appendix at which the particular portion of the Order appears.

## STATEMENT OF THE CASE AND FACTS

In keeping with the requirements of the Florida Rules of Appellate Procedure, Rule 9.210(c), Southern Bell will limit its Statement of the Case and Facts to the specific identification of those portions of Appellant's Statement of the Case and Facts with which Southern Bell disagrees.

Southern Bell does not agree with the manner in which FCTA has summarized the "subject of this appeal" in the first paragraph of FCTA's Statement of the Case and of the Facts. (FCTA Brief at 2) Southern Bell believes that a more appropriately neutral statement of the issue would be as follows: Whether the Commission erred by ruling that the terms "competitive", "effectively competitive", and "subject to effective competition" "have identical meanings when used in Sections 364.338 and 364.3381." (App. at 18)

Southern Bell also disagrees with the second and third paragraphs of Appellant's Statement because these paragraphs constitute argument and are not appropriately included in a Statement of Facts. (FCTA Brief at 2-3)[2]

Southern Bell also disagrees with the approach taken by FCTA of identifying very limited language from the Commission's Final Order (Order No. PSC-93-1015-FOF-TP) and stating that the quoted

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[2] The language to which Southern Bell objects begins with the sentence on page 2 that "[t]his is not an academic exercise in statutory interpretation, but rather a question with significant impact on the future viability of competition in the telecommunications industry in Florida". The objectionable language ends with Appellant's italicized quotation from Section 364.01(3)(e) on the following page.

language constitutes the only "relevant portions of the Commission's decision with respect to the above issues". (FCTA Brief at 6)

## SUMMARY OF ARGUMENT

Appellant argues in its initial brief that the Commission's Order departs from the essential requirements of law because it is contradicted by the record evidence and it ignores the rules of statutory construction. The fundamental problem with Appellant's first point is that it misconstrues totally the inherently legal nature of statutory construction. A statute is not properly interpreted on the basis of testimony or other evidence as to what it should mean, but rather by applying the legal rules of statutory construction to the language of the statute. The Commission made precisely such a legal interpretation. It did not undertake to consider evidence on this point, nor would it have been proper to do so.

Under Florida law, an administrative agency's interpretation of a statute that it is charged to enforce is entitled to great weight and will not be overturned unless it is clearly erroneous. In interpreting such a statute, the agency must apply the normal rules of statutory interpretation. These rules require the agency to give effect to the legislative intent as expressed in the language of the statute and to interpret the statute in a way that will render it reasonable when considered in its totality.

At the conclusion of the proceeding below, the Florida Public Service Commission entered an order in which it held that the terms "competitive", "effectively competitive", and "subject to effective competition", have the same meaning when used in Sections 364.338 and 364.3381, Florida Statutes. This ruling by

the Commission not only constitutes a permissible interpretation of the statute, but is, indeed, the only interpretation that will allow the statute to make sense when read in its entirety and in context. On the other hand, FCTA's interpretation of the statute (i.e., that these three terms have separate and distinct meanings) would render the statute absurd and, thereby, violate a fundamental tenet of statutory construction. Accordingly, the Commission's ruling on this point of law is correct and should be sustained.

FCTA has argued that the Commission's interpretation is in error because it would fail to give effect to the broader legislative intent of Chapter 364 to foster competition. FCTA, however, offers neither legal nor logical support for this proposition. FCTA also argues that the Order would effectively limit the Commission's ability to prevent anti-competitive behavior relating to any service that has not yet been found to be effectively competitive. This contention, however, ignores the language of the Commission's Order and is simply wrong. The Commission's interpretation of Section 364.3381 is also correct, and FCTA has offered no argument to the contrary.

## ARGUMENT

### I. THE STANDARD OF REVIEW AND RULES OF STATUTORY INTERPRETATION

#### A. An agency's interpretation of a statute that it is charged to enforce must be upheld unless it is clearly erroneous.

The standard of review in this case is well settled under Florida law. As this Court stated in PW Ventures, Inc. v. Nichols, 533 So.2d 281, 283 (Fla. 1988),

> ...[W]e note the well established principle that the contemporaneous construction of the statute by the agency charged with its enforcement and interpretation is entitled to great weight ... [citation omitted] .... The Courts will not depart from such a construction unless it is clearly unauthorized or erroneous.

See also, State ex rel. Biscayne Kennel Club v. Board of Business Regulation, 276 So.2d 823, 828 (Fla. 1973) (The "administrative construction of ... [a] ... statute by the agency or body charged with its administration is entitled to great weight and will not be overturned until clearly erroneous").

This standard has been applied by the First District Court of Appeal to mean that "[i]f an agency's interpretation [of its governing statutes] is one of several permissible interpretations, it must be upheld despite the existence of reasonable alternatives." Pershing Industries, Inc. v. Dept. of Banking and Finance, 591 So.2d 991, 993 (Fla. 1st DCA 1991); Dept. of Professional Regulation v. Durrani, 455 So.2d 515 (Fla. 1st DCA 1984). In Pershing, the appellant advanced a statutory interpretation that the appellee, agency (the Department of Banking) admitted was possible. At the same time, the agency

concluded that a different interpretation was more plausible. The reviewing Court stated that "because the Department's interpretation of ... [the statute] ... is not unreasonable or outside the range of permissible interpretations, ... it must be upheld. Pershing at 994.[3]

On the basis of the above-cited authority, it would appear that an administrative agency's interpretation of a statute that it is charged to enforce will be overturned only in relatively unusual circumstances. A rejection of the agency's interpretation is only supportable if that interpretation is so clearly erroneous that it simply cannot be deemed to be within a range of reasonable conclusions as to the meaning of the statute.

### B. A statute must be interpreted in a way that will render it reasonable in the context of the statute as a whole.

In order to determine the meaning of a statute, any tribunal, including an administrative agency, must consider all pertinent legal principles of statutory construction. The most simply applied of these principles is that no interpretation is appropriate when the statute is facially clear and totally lacking in ambiguity. In this instance, the tribunal considering

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[3] Federal courts have similarly deferred to agency interpretations. An "administrative agency's interpretation of its own regulations must be accorded the greatest deference .... If the agency interpretation is merely one of several reasonable alternatives, it must stand even though it may not appear as reasonable as some other". Expedient Services, Inc. v. Weaver, 614 F.2d 56, 57 (5th Cir. 1980) (quoting Allen M. Campbell Co. General Contractors, Inc. v. Lloyd Wood Construction Co., 446 F.2d 261, 265 (5th Cir. 1971)).

the statute does not so much interpret it as simply apply it in the manner that is dictated by its clear language. As this Court stated in Streeter v. Sullivan, 509 So.2d 268, 271 (Fla. 1987):

> The first rule of statutory interpretation is that '[w]hen the language of the statute is clear and unambiguous and conveys a clear and definite meaning, there is no occasion for resorting to the rules of statutory interpretation and construction; the statute must be given its plain and obvious meaning'. A.R. Douglass, Inc. v. McRainey, 102 Fla. 1141, 1144, 137 So. 157, 159 (Fla. 1931).[4]

Thus, when a statute's meaning is so obvious that there is essentially no room for interpretation, the tribunal considering the statute has nothing more to do than simply apply its plain language to reach an obvious result.

In a circumstance, however, in which discerning the meaning of a statute requires some degree of interpretation, the rules become more complex. In this instance, there are a number of principles of statutory interpretation that must be applied to reach a proper result. Although there are myriad cases that set forth these principles, the guidelines they prescribe can be summarized in three broad rules: (1) the interpretation must be consistent with the legislative intent, (2) it must be reasonable

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[4] The same rule was expressed, albeit in somewhat different language, in Citizens v. Public Service Commission, 425 So.2d 534, 541-42 (Fla. 1982) as follows:

> The rule in Florida is that where the language of the statute is so plain and unambiguous as to fix the legislative intent and leave no room for construction, the Court should not depart from the plain language used by the legislature.

(i.e., absurd results are to be avoided), and (3) the statute should be interpreted as a whole so that all parts of the statute are consistent with one another.

When a statute is susceptible to more than one interpretation, the reviewing tribunal must first seek to give effect to the intent of the legislature in creating the statute. As stated in Lowry v. Parole and Probation Commission, 473 So.2d 1248, 1249 (Fla. 1985), "[w]here reasonable differences arise as to the meaning or application of a statute, the legislative intent must be the polestar of judicial construction". At the same time, this Court has repeatedly held that the legislative intent must be determined whenever possible by looking to the way in which it is reflected in the language of the statute:

> In statutory construction, case law clearly requires that legislative intent be determined primarily from the language of the statute. [citations omitted]. The reason for this rule is that the legislature must be assumed to know the meaning of the words and to have expressed its intent by the use of the words found in the statute.

S.R.G. Corp. v. Dept. of Revenue, 365 So.2d 687, 689 (Fla. 1978). "It is a well-established rule of construction that the intent of the legislature as gleaned from the statute is the law". Dept. of Legal Affairs v. Sanford-Orlando Kennel Club, Inc., 434 So.2d 879, 882 (Fla. 1983) (quoting Small v. Sun Oil Co., 222 So.2d 196, 201 (Fla. 1969)). Accordingly, in determining the legislative intent, "the statutory language is the first consideration". St. Petersburg Bank & Trust Co. v. Hamm, 414 So.2d 1071, 1073 (Fla. 1982).

Consistent with this rule, it is only appropriate to attempt to discover the legislative intent by looking outside a statute when the language of the statute itself is not sufficiently clear to reveal this intent. In this uncommon circumstance, the typical source of guidance is the legislative history of the particular statute. See, e.g., Streeter, supra; Florida State Racing Commission v. McLaughlin, 102 So.2d 574 (Fla. 1958);[5]

The second fundamental applicable principle of statutory construction is that the tribunal interpreting the statute is "obligated to avoid constructing [the] particular statute so as to achieve an absurd or unreasonable result". Carawan v. State, 515 So.2d 161, 167 (Fla. 1987). Instead, a statute should be interpreted in a manner that will render it reasonable. This rule is not intended to be an alternative to the rule that the legislative intent should control. Instead, the two rules are entirely consistent and the requirement that a statute be construed so as to be reasonable is, in fact, a corollary to the mandate to give effect to the legislative intent. In other words, it is assumed that an absurd or unreasonable result is contrary to what the legislature intended:

> It is, of course, a well settled principle that courts should avoid interpreting statutes in ways which ascribe to the legislature an intent to create an absurd result. [citations omitted] ... Allied

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[5] In Ison v. Zimmerman, 372 So.2d 431, 433 (Fla. 1979), this Court accepted as extrinsic evidence of the legislative intent the history of the legislation together with "contemporaneous commentary on the drafters intent" that was contained in the reporter and "subsequent legislative action".

> Fidelity Insurance Co. v. State, 415 So.2d 109, 110-11 (Fla. 3rd DCA 1982) ('[A]n axiom of statutory construction [is] that an interpretation of a statute which leads to an unreasonable or ridiculous conclusion or result obviously not designed by the legislative will not be adopted').

Ferre v. State ex rel. Reno, 478 So.2d 1077, 1082 (Fla. 3rd DCA 1985).

Further, the necessity to construe a statute in a way that will render it reasonable pertains despite any contrary result that might be suggested by the literal language of the statute. "It is fundamental that a statute should be given a reasonable interpretation. No literal interpretation should be given which leads to an unreasonable or ridiculous conclusion". Johnson v. Presbyterian Homes of Synod of Florida, Inc., 239 So.2d 256, 263 (Fla. 1970).

The third fundamental applicable tenet of statutory construction is that a statute should be interpreted on the basis of the entire statute, not merely by looking to isolated portions of the statute. As this Court stated in Forsythe v. Longboat Key Beach Erosion Control District, 604 So.2d 452, 455 (Fla. 1992), "[i]t is axiomatic that all parts of a statute must be read together in order to achieve a consistent whole". Further, "every statute must be read as a whole with meaning ascribed to every portion and due regard given to the semantic and contextual interrelationship between its parts". Forsythe, at 455 (quoting Fleischman v. Dept. of Professional Regulation, 441 So.2d 1121,

1123 (Fla. 3rd DCA 1983), review denied, 451 So.2d 847 (Fla. 1984)).

The purpose of this rule also is to observe the legislative intent. The "[l]egislative intent should be gathered from consideration of the statute as a whole rather than from any one part thereof". Florida Jai Alai, Inc. v. Lake Howell Water and Reclamation District, 274 So.2d 522, 524 (Fla. 1973); Escambia County v. Trans Pac, 584 So.2d 603, 605 (Fla. 1st DCA 1991) ("We are required to consider a statute as a whole in determining the legislature's intent").

Taking into consideration all of the above-cited authority allows for a cogent statement of the full range of applicable rules of statutory interpretation. If a statute is so clear that interpretation is unnecessary, then the plain language of the statute will simply be applied. On the other end of the spectrum, if a statute is so ambiguous that the legislative intent cannot be discerned from the language of the statute, it may be interpreted by the use of extrinsic evidence such as the history of the legislation. In the middle ground between these two extremes fall what one would presume to be the vast majority of cases, those that require interpretation, yet include language that is sufficiently clear to allow their meaning to be discovered by applying to this language certain established principles of statutory construction. These principles require that the tribunal reach a reasonable interpretation that takes into consideration the statute as a whole and is consistent with

the legislative intent as expressed in the language of the statute.

Applying these principles described to the instant case requires the conclusion that the Commission's interpretation of Section 364.338, Florida Statute, cannot possibly be viewed as constituting clear error. In point of fact, the Commission's construction of the statute is not only within the range of permissible interpretations, it is the only interpretation that is consistent with the above-described rules of statutory construction.

## II. THE COMMISSION CORRECTLY RULED THAT THE TERMS "COMPETITIVE", "EFFECTIVELY COMPETITIVE" AND "SUBJECT TO EFFECTIVE COMPETITION" HAVE THE SAME MEANING AS USED IN SECTION 364.338, FLORIDA STATUTES.

The Commission originally determined in Order No. PSC-93-0289-FOF-TL, which was issued February 23, 1993 in Docket Nos. 910590-TL and 920255-TL, that "the legislature did not differentiate the meaning of 'competitive', 'effectively competitive', and 'subject to effective competition' as those terms are used in Sections 364.338 and 364.3381 (App. at 15)[6] The same result was, of course, reached in the instant case. Before explaining the basis for this result, the Commission first noted and rejected the contention of FCTA that certain rules of statutory construction required that these terms be viewed in this case as having separate, distinct meanings. Specifically, FCTA argued "(1) that every provision in the statute is there for a purpose; and (2) that every word in the statute must be given its plain and ordinary meaning". (App. at 16)

Although the Commission acknowledged that FCTA had identified viable rules of statutory construction, it rejected the contention that these were the only pertinent rules or that they should control. Instead, the Commission relied expressly upon the "well accepted rule of interpretation that a statute is passed as a whole and not in sections; therefore, each part of the statute must be construed in connection with every part to

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[6] Even though FCTA was a party to the consolidated proceedings that resulted in this Order, it elected not to appeal the Commission's ruling.

produce a harmonious whole. In addition, even apparently plain words may not convey the meaning the drafters intended it to impart; it is only within the full context of the statute that a word can convey an idea". (App. at 16) The Commission also relied upon the rule of statutory construction that a "statute should not be read literally where such a reading would be contrary to its purposes". Id.

Thus, FCTA argued for a narrow and mechanical interpretation of these terms that would fail entirely to place them in the larger context of Section 364.338 and the obvious purpose of the statute. The Commission properly rejected this contention and, instead, ruled that considering the statute in toto, the only conclusion that would render it logical and reasonable is that the terms "competitive", effectively competitive", and "subject to effective competition" are synonymous.[7]

A review of Section 364.338 in its entirety leads to the inescapable conclusion that the Commission's interpretation is correct. Applying the Commission's determination that the three subject terms all mean "effectively competitive" renders the

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[7] The Commission also rejected the contention that if the three similar terms were not intended to have separate and markedly distinct meanings then the legislature would have only used one phase rather than three. The Commission found that "[t]his argument is not persuasive. The argument is more compelling by reversing it: if the legislature had intended 'effective competition' and 'subject to effective competition' to have different meanings, it simply would have defined them separately in Section 364.02." (App. at 16) The Commission's conclusion is not only logical, it is, again, the only interpretation that allows the statute to make sense when viewed as a whole.

statute lucid, practical and easily applied. Applying FCTA's interpretation, however, would render the statute not only unintelligible, but impossible to apply.

By scrutinizing each portion of Section 364.338 and considering how the various parts fit together to form a cohesive whole, one can readily see that if there is a single definition for the three terms, then the statute makes perfect sense. Section 364.338(1) contains an explicit statement of the legislature's intent:

> It is the legislative intent that, where the Commission finds that telecommunication service is effectively competitive, market conditions be allowed to set prices so long as predatory pricing is precluded, monopoly ratepayers be protected from paying excessive rates and charges, and both ratepayers and competitors be protected from regulated telecommunications services subsidizing competitive and telecommunication services.

Thus, when a particular product has reached the point at which market conditions will be effective to set prices, the service will then be deemed effectively competitive and the market will replace the traditional regulation of the service, provided that the above-described conditions are met. Accordingly, subsection (2) provides that a determination as to whether a particular service is effectively competitive shall be made by considering the seven criteria specifically identified in Section 364.338(2)(a) through (g).

Subsection (3)(a) follows logically in its provision that "[i]f the Commission determines, ... that a service provided by a local exchange telecommunications company is ... [effectively competitive] ..., the Commission may ... prescribe different regulatory requirements than are otherwise prescribed for a monopoly service". (Section 364.338(3)(a)1) Alternatively, the Commission may "[r]equire that the competitive service be provided pursuant to a fully separated subsidiary or affiliate". (Section 364.338(3)(a)2)

Under the Commission's interpretation of 364.338, the statute is absolutely clear. It states the legislative intent to allow market conditions to set prices of a service that is found to be competitive, it states the criteria for making this finding, then it states two allowable alternative regulatory treatments for the service. When the statute is viewed as a whole, as it must be under Forsythe and Florida Jai Alai, supra, it is obvious that the Commission's interpretation will accommodate a reasonable result.

On the other hand, the adoption of FCTA's interpretation would render Section 364.338 not only absurd, but totally unintelligible. For example, Section 364.338(1) states that it is the legislative intent that, where "the Commission finds that a telecommunications service is effectively competitive, market conditions be allowed to set prices so long as ... both ratepayers and competitors be protected from regulated communications services subsidizing competitive

telecommunications services." (emphasis added) In FCTA's analysis "effectively competitive" services are different than "competitive" services. Thus, the reference to an "effectively competitive" service in the first clause of the above-quoted sentence and the latter reference to "competitive" services in that same sentence must refer to two different services. Therefore, the statute would mean that if one service is found to be effectively competitive, then market prices should be allowed to set prices for that service as long as doing so would not result in a cross-subsidy to some completely different, separate service, i.e., the one that is competitive.[8]

On the basis of the same type of contextual analysis, the Commission concluded that if FCTA's "claim of separate meanings for the terms were true, the statute would make no sense". (App. at 17) The Commission then commented upon the absurd result of FCTA's argument:

> For example, Section 364.338(3)(a)2 reads, in part, that '[i]f the Commission determines ... that a service ... is subject to effective competition, the Commission may: ... require that the competitive service be provided pursuant to a fully separated subsidiary or

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[8] Likewise, since Section 364.338(3)(a) refers to both a service that is "subject to effective competition" and a "competitive" service, FCTA's analysis would cause the same absurd result a second time. After determining that a service is "subject to effective competition" the Commission would have the option of requiring that some different, unrelated and unidentified "competitive" service be offered through a separate subsidiary. As discussed below, this absurd result was expressly noted in the Commission's Order as a basis to reject FCTA's interpretation.

> affiliate.' (emphasis added). If separate meanings are to given in this sentence, the sentence simply no longer makes logical sense. What competitive services are being discussed? If it cannot be the one referred to as "subject to effective competition", which one is it?

Id. On the basis of the foregoing, it is clear that the only reasonable interpretation of the statute as a whole is the one that was reached by the Commission, that the three terms are synonymous. This interpretation is consistent with the clear expression of legislative intent set forth in 364.338(1), it renders the statute reasonable and logical when the entire statute is read in context, and it avoids the patently absurd result that would necessarily follow from the interpretation urged by Appellant. For these reasons, the Order of the Commission is correct in all respects and must be sustained.

## III. APPELLANT HAS RAISED NO BASIS FOR A FINDING THAT THE ORDER OF THE COMMISSION IS ERRONEOUS.

For the reasons set forth above, the Commission's interpretation of Section 364.338 is, when considered in light of all applicable tenets of statutory construction, irrefutably correct. Appellant, nevertheless, engages in a scattershot effort to find some basis to challenge the Commission's Order. To this end, FCTA reiterates arguments that were made in the proceeding below and properly rejected by the Commission. These include both the novel contention that a word used in a statute is best interpreted by simply looking it up in a dictionary without any reference to the context in which it is used (FCTA Brief at 14), as well as the previously discussed argument that, since there are three terms, they must have three distinct meanings, the lack of separate definitions notwithstanding. (FCTA Brief at 20-22) Appellant also makes what purports to be a contextual analysis in an attempt to render inscrutable the clear purpose of Section 364.338(2) to enumerate the criteria to determine whether a service is competitive. The same illogical argument is applied to Section 364.338(3) to attempt to obscure its clear prescription of alternative treatment for a service that is found to be competitive. (FCTA Brief at 19-22)

The real thrust of Appellant's initial argument, however, is twofold: One, FCTA argues that the Commission's decision is unsupported by substantial, competent evidence. Two, FCTA argues that the Commission's Order violates some broader expression of legislative intent that is contained in other portions of Chapter

364. Neither argument is well taken and both should be summarily rejected.

### A. FCTA'S contention that the Commission's order is not based on substantial competent evidence is misapplied to the legal issue of statutory interpretation.

FCTA argues that the interpretation by the Commission of Section 364.338 is not supported by the "competent, substantial evidence of record" that was introduced in the hearing. (FCTA Brief at 14) The insurmountable problem with this argument is that it fundamentally misapprehends the nature of statutory interpretation and, therefore, advocates the application of a standard of review that is simply inappropriate.

Appellant correctly notes that, in general, orders of an administrative agency are to be upheld if they are supported by any competent, substantial evidence. (FCTA Brief at 11) FCTA, however, appears not to understand that, in all but those rare cases in which reference to extrinsic evidence is required, the interpretation of a statute by an administrative agency is not a matter that turns upon the admission and consideration of evidence. Instead, it is an essentially legal process that involves applying to the language of the statute the principles of statutory construction outlined above.[9] As stated previously, the use of extrinsic evidence to aid in interpreting a statute is only proper when the statute is otherwise so

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[9] See e.g., Dept. of Legal Affairs, supra, at 882 ("...[t]he intent of the legislature as gleaned from the statute is the law).

ambiguous that a facial analysis is simply not possible. Streeter, Florida State Racing Commission, supra.

This clearly was not the situation in the case now under review. In the Order Establishing Procedure (Order No. PSC-92-1323-PCO-TP) entered November 16, 1992, the Commission specifically designated the subject issue as legal in nature. (App. at 34)[10] Thus, the issue was designated as a matter to be addressed by the parties in their briefs through the presentation of legal argument. Consistent with this dictate, the Commission's Order was based solely upon the inherently legal process of statutory interpretation. The Commission did, of course, acknowledge that FCTA presented testimony from a witness as to his view of what these three terms mean. (App. at 15) The basis of the Commission's Order, however, was the legal analysis of the statute at issue, not the weighing of inappropriate "evidence" on this point. Thus, FCTA's argument that the Commission's ruling is contradicted by the evidence presented at the hearing is wholly misplaced.

Moreover, even if the statute had been determined by the Commission to be so ambiguous as to require the admission of extrinsic evidence, the controlling case law cited previously makes it clear that any such evidence is to be considered for the purpose of clarifying the legislative intent. Streeter, supra. Southern Bell is unaware of any Florida case that authorizes the

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[10] "ISSUE 5: Is there a distinction between the terms "effectively competitive", "subject to effective competition", and "competitive" as used Chapter 364? (LEGAL)"

practice of advocating a particular statutory interpretation by presenting the testimony of someone who is, for these purposes, essentially a lay witness as to his impression of what the statute means. Nevertheless, this is essentially what FCTA attempted to do through the testimony of its witness, Mark Cicchetti (Tr. at 26-32)[11] The fact remains, however, that this was not an issue for which the presentation of evidence was authorized by the Prehearing Order, and even if it were, the "evidence" proffered by FCTA was not of a type that could be properly considered on this issue. Therefore, FCTA's argument that the legal interpretation of the Commission is not supported by substantial competent evidence clearly misses the point of the Commission's ruling and the analysis that supports that ruling.

Finally, even if this were an issue upon which evidence could properly be offered by questioning witnesses as to their interpretation of the statute, FCTA's contention that the Commission's ruling is unsupported by substantial, competent evidence still must fail. There is substantial and competent record evidence to support the ruling of the Commission.[12] Specifically, when pressed at the hearing to give his opinion on this point, Southern Bell's witness, Dr. Richard Emmerson stated the following:

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[11] Likewise, FCTA repeatedly demanded on cross examination that witnesses provide their understanding of the "everyday meaning" of the term "competition". (Tr. at 304, 550)

[12] Put differently, there is record evidence that would support the Commission's ruling if it could be properly considered for this purpose.

> My interpretation of the statute is that regulation presumably substitutes for competition, when competition is not performing its job. And to the extent that this Commission determines that competition is an adequate substitute for regulatory oversight, the Commission has the discretion to declare services competitive, and ... [the Legislature] put forth some criteria to be used in making that determination. To me that suggests that they are looking for precisely the same conditions that an economist would look for to say that these services are competitive and should be treated as such.

Further,

> COMMISSIONER CLARK: Dr. Emmerson,.... You said you reviewed Section 364.338 and 364.3381?
>
> DR. EMMERSON: Correct.
>
> COMMISSIONER CLARK: I just want your general impression of the purpose of those sections. .... And the purposes of all those authorizations is, in effect, to allow us to set up a structure to allow competition to work and for us to receive [sic] from regulation the local exchange company, and let competition drive price, costs and keep the service adequate. Do you agree with that?
>
> DR. EMMERSON: I agree completely. And even more specifically, I think that the legislature has said under paragraph 2, Items A through G are specific things the Commission should look at to determine whether competition can do that job ....

(Tr. at 335-336)

Thus, Dr. Emmerson opined that, under the instant statutory scheme, a service will be regulated as a monopoly service until the market for the particular service functions in a way such that an alternate form of regulation is appropriate, i.e., it

becomes competitive. When this occurs and traditional regulation is, therefore, no longer needed, the Commission may order an alternative form of regulation and/or allow competition to set prices.

Thus, even if it were appropriate to interpret Section 364.338 on the basis of opinions expressed by witnesses, the foregoing testimony makes it clear that there was substantial, competent evidence admitted into the record to support the Commission's determination of the meaning of Section 364.338.

**B. <u>The Commission's ruling is not anti-competitive.</u>**

FCTA next argues that the Commission erred by overlooking the legislative intent that underlies all of Chapter 364, "which is to foster telecommunications competition in the public interest". (FCTA Brief at 23) As stated above, Southern Bell believes that the Commission clearly gave effect to the legislative intent of Section 364.338 as that intent is reflected in the language of the statute. In other words, the Commission made an interpretation that is consistent with the express statement of intent contained in Section 364.338(1). The Commission also made a reasonable interpretation of Section 364.338 in light of the statute as a whole, thereby also giving effect to the legislative intent as it is expressed in the language of the statute.

In response to this, Appellant argues that the Commission has somehow failed to "apply the overriding legislative intent behind Chapter 364". (FCTA Brief at 23) To this end, FCTA

argues that "the overriding legislative intent of Chapter 364, Florida Statutes, ... is clearly to encourage telecommunications competition in the public interest". (FCTA Brief at 24) FCTA then argues that its interpretation of Section 364.338 encourages competition while the Commission's interpretation is, in effect, anti-competitive.

As to this first point, while Southern Bell does not agree that fostering competition is the sole "overriding legislative intent" of all of Chapter 364, fostering competition is certainly one of the goals that Section 364.01 mandates the Commission to use its authority to achieve. In fact, Section 364.01(3)(c) provides specifically that the Commission shall exercise its jurisdiction to "encourage cost-effective technological innovation and competition in the telecommunications industry if doing so will benefit the public by making modern and adequate telecommunications services available at reasonable prices". The fallacy of FCTA's argument, however, becomes apparent when it attempts to make the obviously insupportable leap to the conclusion that only its interpretation of Chapter 364 will serve the legislative mandate to promote competition.

In support of its conclusion, FCTA offers nothing more than a circular argument that relies totally upon the presumption that its interpretation of Section 364.338 is correct and the Commission's is incorrect. Specifically, FCTA argues that "... Chapter 364 contains two specific passages stating that the Commission is required to prevent cross-subsidization of

'competitive services'". (FCTA Brief at 28) "Chapter 364 also requires cross-subsidization protection to be maintained if a 'competitive' service is determined to be 'subject to effective competition'...." Id. Thus, Appellant assumes as its starting point the proposition that it is ultimately attempting to prove, that Section 364.338 contemplates more than one type of "competitive" services.

FCTA then argues that, under the Commission's Order, cross-subsidization would be prohibited for what FCTA defines as "effectively competitive" services (i.e., those that have been defined as competitive by the application of Section 364.338), but would be allowed for "competitive" services (those that FCTA considers to be competitive even though they have not been declared as such under Section 364.338). FCTA asserts that this would have an anti-competitive effect. The error of this argument is that, for the reasons set forth above, the Commission found that there are no competitive services except those determined to be such by applying Section 364.338. Thus, FCTA argues that the Commission is impeding competition by failing to protect a classification of competitive service that the Commission has specifically found not to exist. Therefore, unless one accepts as a starting point FCTA's ultimate conclusion that there is more than one type of competitive service contemplated by Section 364.338, FCTA's entire argument on this point collapses.

Finally, FCTA argues that the Commission's interpretation would necessarily mean that, absent a finding that a service is "effectively competitive", there would be no "statutory safeguards against anti-competitive behavior". (FCTA Brief at 29) This contention is flatly wrong.

Section 364.01(d) provides specifically that the Commission shall "[e]nsure that all providers of telecommunications services are treated fairly, by preventing anti-competitive behavior and eliminating unnecessary regulatory restraint". Thus, separate from the dictates of Section 364.01(c), the language of Section 364.338 and the protection from cross-subsidy contained in Section 364.3381, the legislature has also delegated to the Commission in Section 364.01(d) very broad powers to prevent behavior that it determines to be anti-competitive. In the subject Order, the Commission specifically confirmed its intention to exercise these powers as necessary with its statement that "[v]arious provisions of the statutes, including Sections 364.01(3)(d), 364.03 and 364.10 are sufficient to deal with any allegations of anti-competitive behavior". (App. at 15)

FCTA's witness advanced an exhaustive list of practices that he contended are not only anti-competitive but which constitute

impermissible cross-subsidization.[13] The Commission responded to this position as follows:

> ... [FCTA's] witness Cicchetti described these practices as forms of cross-subsidization. However, we have determined herein that these practices are not cross-subsidization, but may be anti-competitive acts, depending on individual circumstances. Without the facts of each case before us, the Commission should not be put in the position of making blanket judgments regarding anti-competitive behavior. Additionally, there is no evidence presented by any witness that any of these possible anti-competitive behaviors are occurring in the State by any LEC.

(App. at 20) Further, even if facts were presented that one of these forms of ostensibly anti-competitive behavior were taking place, this behavior would be addressed not by the rules that apply to prevent cross-subsidy, but rather by the separate rules that apply to prevent anti-competitive behavior in general. Nevertheless, FCTA ignores the clear language of the Commission's Order and inexplicably contends that, under the Commission's interpretation of Section 364.338, there will be no protection from anti-competitive behavior in connection with any service that has not been deemed competitive pursuant to Section 364.338. For the reasons set forth above, this contention is demonstrably false.

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[13] The Order summarized these as follow: (1) predatory pricing by LECs; (2) excessive cost transferred to monopoly ratepayers by the LEC paying excessive rates for some services; (3) discriminatory provision of service to competitors by LECs; (4) discriminatory charges for services to competitors by LECs; (5) inferior services provided to competitors by LECs; and (6) undue preference by LECs for LEC provided services such as marketing CPE with equipment. (App. at 19)

C. **The Commission ruled correctly that the prohibition of cross-subsidization contained in Section 364.3381 applies only to those services found to be competitive under Section 364.338.**

In its brief, FCTA states that it is appealing two points. The second issue is, in the words of FCTA, whether "Section 364.3381, Florida Statutes, only prevents the cross-subsidization of 'effectively competitive' services". (FCTA Brief at 7) At a different point, FCTA states fully the issue:

> Issue No. 6: Does the application of the provisions of Section 364.3381 first require a determination that a service is effectively competitive, pursuant to the provisions of 364.338? If not, what criteria should be used to identify those services subject to the provisions of 364.3381?

(FCTA Brief at 5) The Commission answered this question in the affirmative and found that the prohibition of cross-subsidy contained in Section 364.3381 only applies after a subject is found to be effectively competitive under Section 364.338. Curiously, the initial brief submitted by FCTA contains no argument whatsoever as to the Commission's interpretation of Section 364.3381 even though it has identified this matter as an issue on appeal. Southern Bell takes the silence of FCTA on this point to be an implicit acknowledgement that the resolution of this issue necessarily follows the resolution of the first issue on appeal, i.e., how the three interchangeably used terms for competition are to be defined. The Commission expressly concluded as much.

The Commission first noted in the Order that a number of parties to the proceeding "all agreed that a determination must

first be made that a service is effectively competitive before Section 364.3381 is applicable". (App. at 18) The Commission then stated:

> We agree that this issue is a direct result of the decision reached regarding the terms above. Section 364.338 and 364.3381 are concerned primarily with services that are 'competitive' and 'subject to effective competition'. If these terms are synonymous with the term 'effective competition', as we have determine herein, a plain and ordinary reading of Section 364.3381 tells us that this section deals solely with the determination and treatment of effectively competitive services. Accordingly, we find that the provisions of Section 364.3381 apply only after a determination is made, pursuant to Section 364.338, that the service is effectively competitive.

(App. at 18-19)

In other words, since the cross-subsidy test of Section 364.3381 will apply only to an effectively competitive service, the Commission's ruling that there are no competitive services except those determined to be so by application of the procedure in Section 364.338 necessarily prompts the conclusion that Section 364.3381 only applies after this determination has been made.

Again, FCTA has inexplicably elected not to address this issue in any direct sense, despite identifying it as an issue on appeal. Southern Bell submits that there is, in fact, no basis for a valid challenge to this aspect of the Order. To the contrary, the Commission correctly ruled that the subject terms are used synonymously in Section 346.338. This prompts the conclusion that the only competitive services are those

determined to be so through the application of Section 364.338. Therefore, the only logical interpretation of Section 364.3381 is that it must follow the application of Section 364.338.

## CONCLUSION

On the basis of the foregoing, Southern Bell submits that the Commission correctly interpreted Section 364.338 in the only manner that is supportable in light of the clearly established rules of statutory construction. FCTA has failed totally to sustain any argument to the contrary, just as it has failed to demonstrate clear error in the Commission's Order. For these reasons, Southern Bell requests that the Commission's Order be upheld in all respects.

Respectfully submitted,

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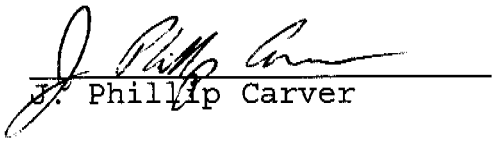

J. Phillip Carver

IN THE SUPREME COURT STATE OF FLORIDA

| | |
|---|---|
| FLORIDA CABLE TELEVISION ASSOCIATION, INC.,<br><br>Appellant,<br><br>v.<br><br>J. TERRY DEASON, Chairman, THOMAS M. BEARD, SUSAN F. CLARK, LUIS J. LAUREDO, and JULIA L. JOHNSON, Commissioners, as and constituting the FLORIDA PUBLIC SERVICE COMMISSION, an agency of the State of Florida,<br><br>Appellees. | Case No. 82,281<br><br>FPSC Docket No. 910757-TP<br><br>Filed: 11-29-93 |

**APPENDIX TO**
**ANSWER BRIEF OF APPELLEE**
**SOUTHERN BELL TELEPHONE AND TELEGRAPH COMPANY**

## INDEX TO APPENDIX

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

| | |
|---|---|
| In Re: Investigation into the regulatory safeguards required to prevent cross-subsidization by telephone companies | ) DOCKET NO. 910757-TP<br>) ORDER NO. PSC-93-1015-FOF-TP<br>) ISSUED: July 12, 1993 |

The following Commissioners participated in the disposition of this matter:

J. TERRY DEASON, Chairman
THOMAS M. BEARD
SUSAN F. CLARK
JULIA L. JOHNSON
LUIS J. LAUREDO

Pursuant to Notice, a public hearing was held on March 10-11, 1993, in Tallahassee, Florida.

APPEARANCES:

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FINAL ORDER

BY THE COMMISSION:

## I. CASE BACKGROUND

By Order No. 24510, issued August 13, 1991, this Commission determined that issues regarding cross-subsidization resulting from the revisions to Chapter 364, Florida Statutes, should not be dealt with in Docket No. 900633-TL, the local exchange company cost of service docket, but instead should be addressed in a separate proceeding. Consequently, this docket was opened to examine matters concerning regulatory safeguards required to prevent cross-subsidization by local exchange companies (LECs). On September 20, 1991, intervening parties submitted briefs addressing the legal requirements of revised Chapter 364. Based on the reaction of the parties at the February 4, 1992 Agenda Conference, the Commission determined that any proposed agency action issued would be protested by the parties. Accordingly, by Order No. 25816, issued February 4, 1992, this docket was set for hearing.

By Order No. 24853, issued July 25, 1991, the Commission acknowledged the intervention of the Office of Public Counsel (OPC) in this docket. In addition, intervention was sought by and granted to the following parties: AT&T of the Southern States, Inc. (ATT-C), BellSouth Telecommunications, Inc. d/b/a Southern Bell Telephone and Telegraph Company (Southern Bell), Central Telephone Company of Florida (Centel), the Florida Ad Hoc Telecommunications User's Committee (Ad Hoc), the Florida Cable Television Association (FCTA), the Florida Interexchange Carriers Association (FIXCA), the Florida Pay Telephone Association (FPTA), GTE Florida Incorporated (GTEFL), MCI Telecommunications Corporation (MCI), United Telephone Company of Florida (United), and US Sprint Communications Telecommunications Company Limited Partnership (Sprint).

Pursuant to Notice, a Prehearing Conference was held on February 26, 1993, establishing the issues to be addressed and the procedure to govern the hearing. The hearing was held on March 10-11, 1993, in Tallahassee.

## II. DEFINITION OF CROSS-SUBSIDIZATION

In order to prevent cross-subsidization, it is initially necessary to define the term. Cross-subsidization is not specifically defined in Chapter 364, but is addressed in Section 364.3381, which is titled "Cross-subsidization." This section provides that:

> (1) The price of a competitive telecommunications service provided by a local exchange telecommunication company shall not be below its cost by use of subsidization from rates paid by customers of monopoly services subject to the jurisdiction of the commission.
>
> (2) A local exchange telecommunications company which offers both monopoly and competitive telecommunications services shall segregate its intrastate investments and expenses in accordance with allocation methodologies as prescribed by the commission to ensure that competitive telecommunications services are not subsidized by monopoly telecommunications services.

Paragraph (1) explicitly prohibits the cross-subsidization of a LEC's competitive services by its monopoly services, while Paragraph (2) requires that a LEC segregate its investments and expenses associated with competitive services from those related to its monopoly services, to guard against cross-subsidization of the former by the latter.

The characterizations of cross-subsidization presented generally fall into two categories. The LECs, including Centel, GTEFL, Southern Bell, and United, assert that the "economic definition" of cross-subsidy is well understood, widely accepted and is the notion that most appropriately conforms with Section 364.3381. However, the FCTA, FPTA, FIXCA, and ATT-C advocate a more expansive definition which they assert is derivative from, and supported by reading Chapter 364 as a whole.

Although the LECs differ somewhat as to the wording of their respective definitions, they all agree that cross-subsidization is an economic concept that fundamentally deals with the relationship between a service's price and its cost. Southern Bell and United maintain that a cross-subsidization occurs when the revenue caused by the provision of a particular segment of the firm's output is exceeded by the incremental cost of producing that segment. Centel

contends that cross-subsidization is the support of a LEC's effectively competitive services whose prices do not cover total incremental costs with revenues from the LEC's monopoly services. GTEFL asserts that cross-subsidization is the pricing of some services above their incremental cost in order to allow other products sold by the firm to be priced below their incremental costs of production. Thus, GTEFL believes that the comparison of price with incremental cost is the appropriate determinant.

FCTA supports a much broader concept maintaining that cross-subsidization occurs when the monopoly provides the following: benefit to its competitive business for which it is not fully compensated by the competitive business; benefit to its competitive business that is not provided to competitors; or, benefit to its competitive business under more favorable terms than provided to competitors. FPTA also proposes the broad definition that cross-subsidization includes any activity on the part of the LEC monopoly involving a competitive service that works to the detriment of the LEC's monopoly ratepayers and impedes competition for end users. FIXCA believes that cross-subsidization occurs when a service fails to recover an appropriate allocation of the LEC's accounting costs. ATT-C also supported the more expansive position that cross-subsidization is a situation in which investments and/or expenses associated with the provision of a competitive service are inappropriately borne by monopoly ratepayers. MCI did not take a position on this issue.

Finally, OPC proposes that cross-subsidization includes the transfer of costs from unregulated operations to regulated operations or the lack of appropriate compensation from competitive operations to the regulated operations.

FCTA's witness Cicchetti stated that the FCTA's primary concern was that if the Commission adopted a cross-subsidy standard based on incremental cost, the LECs could install fiber optic facilities in excess of what would be economically efficient for the provision of local exchange service. Given the acceptance of incremental cost as the benchmark for compensatory pricing, FCTA presumably is concerned that in the future the LECs may offer video services in competition with cable companies, with the bulk of the cost of the necessary facilities being recovered through rates for monopoly services.

Given the above exchange, one of two fundamental concerns of FCTA's, which is shared, in varying degrees, by FPTA, FIXCA, and

ATT-C, can be described as follows. The LECs are multiproduct firms which enjoy economies of scale and scope in the provision of their services. Where economies of scale are present, both the average cost per unit and the incremental cost per unit produced are declining, and the incremental cost per unit--the cost of the next unit or increment produced-- is less than average cost. Simply stated, economies of scope exist where it is less costly for a single firm to produce two goods, than it would be for two single-product firms to produce these two goods separately.

Fiber optics is a transmission technology that affords significant economies of scale because of its nonlinear cost characteristics. Once a fiber route is in place, on a per unit basis the cost of expanding the route's capacity in terms of additional derived channels declines; the major limiting factors are technological limitations and the offered demand. For most transport applications fiber optics is currently the technology of choice. For example, when upgrades are needed, many if not most Florida LECs are installing fiber optics for interoffice transport.

The issue raised here by FCTA is a matter of equity in pricing. Assume that fiber facilities originally were installed to provide local exchange service, but a LEC now proposes to offer a new service, such as video transport, using these same embedded facilities. If this is a service for which competitive alternatives exist, the LEC presumably would set its price, subject to a floor cost, in recognition of the market characteristics. FCTA is concerned that if the price floor for this new service were set relative to its associated incremental cost, the result should be viewed as cross-subsidization.

When dealing with a technology such as fiber optics that can yield economies of scale, the incremental cost of any one service can be quite sensitive to the sequence in which services are offered. As noted in the above example, where fiber optic facilities are installed and local exchange services are offered first, the incremental cost of services subsequently provided using this technology will tend to be lower than the cost of the local exchange service first service provided. Further, by the time that additional services are eventually offered, the bulk of the fixed costs of the fiber optic facilities usually either have been or are being recovered through the rates for existing services, in this case primarily local exchange services.

It appears FCTA believes that the cost of fiber optics is not justified solely for the provisioning of local exchange service, but the LECs nevertheless are installing it and recovering the costs from local exchange ratepayers. No evidence was presented at the hearing as to whether or not this in fact is true. We would note that issues involving whether or not a LEC was installing the most cost-effective technology to provide service are routinely dealt with in rate cases and in depreciation cases. Regardless, we believe that whether such actions are occurring relates to questions of prudence, not cross-subsidization.

Witness Cicchetti also contended that cross-subsidy pertains to various forms of behavior which could be considered instances of anticompetitive behavior. Such behavior would include price discrimination, refusal to deal, above-cost affiliate transactions, among others. The specific forms of anticompetitive behavior enumerated by witness Cicchetti are addressed in Section V, herein. However, witness Cicchetti did acknowledge that anticompetitive behavior can be distinct from cross-subsidization in the economic sense. Moreover, witness Cicchetti agreed that the Commission could fulfill its statutory duties under Chapter 364 by treating anticompetitive matters separately from cross-subsidy concerns.

Upon review, we find that the record in this proceeding does not support the broad characterization of cross-subsidy advocated by FCTA's witness Cicchetti. Witness Cicchetti admitted during cross-examination that his broad definition of cross-subsidization was distinct from the test used by federal antitrust courts, while the economic definition is the standard for antitrust cases. He was unable to cite any works, treatises or court opinions that supported his characterization of cross-subsidy. Witness Cicchetti agreed that the economic definition, based on the relationship between price and cost, has a well-known and widely accepted meaning. Moreover, he was unaware of any articles in journals or in the professional literature which indicate that the economic definition, based on the relationship between price and incremental cost, is inappropriate. We find that the record in this proceeding does support the more narrow view propounded by the LECs. Accordingly, we find it appropriate to adopt the following economic definition of cross-subsidy: Cross-subsidization exists when competitive services are priced below their incremental costs, and the resulting revenue shortfall is recovered through the rates for monopoly services.

III. DETECTION OF CROSS-SUBSIDIZATION

All parties in this proceeding generally agree that it is necessary to examine the revenues and costs associated with competitive services in order to detect cross-subsidization; they differ according to their views on how the costs should be determined or measured. FCTA also maintains that cross-subsidization can be detected by comparing the prices that the monopoly service provider charges when making services available to its own competitive business to what it charges other competitive providers for such service. Again, FCTA appears to be advocating a broader approach to the concept of cross-subsidization.

There is no significant disagreement among the parties regarding the need to examine a service's revenues and costs to detect cross-subsidization. Accordingly, we find that the presence of cross-subsidization can be determined by comparing the revenues generated from a service with the relevant costs of providing the service, or, equivalently, a service's price with its relevant unit cost.

IV. COST STANDARD

Centel, GTEFL, Southern Bell and United all agree that incremental cost is the proper standard against which to determine the presence or absence of cross-subsidization. Southern Bell witness Emmerson noted that the total incremental cost test, which involves comparing a service's total incremental costs to its total revenues generated, is the accepted standard among economists.

FCTA's witness Cicchetti contended that the cost standard for detection of the presence or absence of cross-subsidization must be based on fully distributed cost (FDC). He asserted that Section 364.3381 requires a full allocation of a LEC's costs between competitive and monopoly services that ties back to the books and records of the company. Moreover, witness Cicchetti objected to the use of incremental cost because it fails to share equitably the benefits arising from the firm's economies of scope. FPTA and FIXCA also endorse FDC as the cost standard.

The LEC witnesses argued against the propriety of using FDC as the standard for cross-subsidy because of its inherent flaws. A fundamental problem noted by the LECs is that FDC approaches attempt to do the impossible: to directly attribute joint and

common costs among services. Since by definition joint and common costs are unattributable, the LECs assert that any FDC methodology is inherently arbitrary.

Even witness Cicchetti conceded numerous points relating to the arbitrariness of FDC methods. He admitted that FDC ignores market forces and customer demand, sets an arbitrary price floor, and yields an allocation of overhead costs that does not reflect any causal relationship. Further, witness Cicchetti acknowledged that requiring a competitive service to be priced to cover fully distributed cost may result in the service not being offered, resulting in a lost contribution towards monopoly services.

ATT-C witness Guedel espoused a position somewhat in between that of the LECs and FCTA. He contended that the Commission should establish a price floor for LEC competitive services based on their direct costs; where monopoly services are used to provide the competitive service, the tariffed rates for the monopoly services should be imputed as direct costs of the competitive service. Witness Guedel further testified that as more and more services are subject to competition, it will become necessary to develop a mechanism to allocate overhead costs between monopoly and competitive services, to protect the monopoly ratepayer. However, overhead costs need not be assigned to individual competitive services, or to affect the level of the price floors for individual services.

Southern Bell witness Emmerson took exception to witness Guedel's proposal to allocate overhead costs between competitive and monopoly services. He argued that there is no rational economic basis to perform such an allocation, that it would result in economic inefficiencies, and thus would be plagued with the same problems associated with fully distributed costs.

GTEFL witness Beauvais indicated that witness Guedel's proposal for imputing monopoly inputs into price floors is not generally correct, but rather represents a special case of the economically proper imputation treatment. Witness Beauvais stated that imputing tariffed rates is only appropriate where there are no differences in the cost of the LEC providing the monopoly service to itself as opposed to a competitor, and there are no qualitative or quantitative services in the service being provided. Instead, the appropriate method would impute the LEC's incremental cost of

providing the monopoly service to itself, plus any foregone contribution it would have received from selling it to another party.

Additionally, we note that the incremental cost standard is embodied in the economic definition of cross-subsidy which has been adopted by the federal antitrust courts. In Northeastern Telephone v. AT&T, 651 F.2d 76 (2d Cir. 1981), the court endorsed the economic cost standard. The court also adopted the incremental cost standard, while repudiating the use of fully distributed costs, in MCI v. AT&T, 708 F.2d 1081 (1983):

> MCI argues at considerable length that an FDC methodology is required to prevent AT&T from subsidizing its competitive services with revenues from services in which it retains a monopoly.
>
> . . . .
>
> MCI's argument presumes that customers of monopoly services will have to pay higher prices if AT&T prices below FDC in markets where competition is present. (citation omitted) Such arguments ignore the nature of costs and revenues in a multi-service enterprise. AT&T's unattributable overhead costs do not increase when AT&T offers a new service, nor do they decrease when such a service is discontinued. When a multiproduct firm prices a competitive service above its long-run incremental cost, no cross-subsidy can occur because the additional revenues produced exceed all additional costs associated with the competitive service and provide a contribution to the unallocable common costs otherwise borne by the firm's existing customers.

Id. at p. 1123-24.

Upon consideration, we find that fully distributed cost is not an appropriate cost standard for use in the telecommunications industry, for detecting cross-subsidy or for any other purpose. First, an FDC methodology assigns all of the firm's costs to individual goods and services. Multiproduct firms such as LECs have at least two types of costs, common and family costs, for which it is impossible to arrive at a causal basis for allocating them to individual services. Common costs are general overhead costs, such as the president's salary and the cost to prepare the firm's annual report to stockholders. Family costs are those costs that are occurred to offer a group of services, but for which there

is no rational basis to assign them to individual services. By definition there is no correct way to allocate these costs; any allocation scheme is inherently arbitrary and thereby subject to manipulation by the analyst. Cross-subsidy is a function of a service's price and cost; a service either is being cross-subsidized or it isn't. Since FDC cannot yield a single unique cost standard, it is impossible for it to detect cross-subsidy.

Second, the results of an FDC study are inappropriate for pricing purposes, especially where competitive entry is allowed into a LEC market. Where an FDC methodology is used to establish floor prices for LEC services that are also available from other providers, the result is an artificial price level. The LECs' competitors are not required to recover their common costs from their services based on an FDC allocation scheme; as such, they have greater flexibility than the LEC to set prices for individual services, especially those for which the greatest competition exists. Consequently, the LEC's FDC price floor affords its competitors an arbitrary price ceiling.

Third, based on the evidence presented, it appears that advocates of FDC confuse pricing and costing. They contend that it is necessary to allocate <u>all</u> costs to individual services in order to ensure that the firm's total costs are recovered. We believe this represents a fundamental conceptual confusion. Costing is properly limited to determining and quantifying the identifiable costs associated with producing a given good; whereas, pricing uses cost results in conjunction with demand characteristics and other information to arrive at an optimal means of recovering costs. An FDC study effectively yields prices for individual services, but it disregards all market considerations. By collapsing the two activities, costing and pricing, FDC approaches are intrinsically unable to yield efficient prices.

Based on the record in this proceeding, we conclude that the appropriate cost standard for detecting cross-subsidization is incremental cost. Although we believe that how and when to require imputation is a legitimate fairness issue, we do not believe it is relevant for purposes of detecting cross-subsidy. The incremental cost standard is universally endorsed in the economics literature and is accepted in the federal antitrust courts in the context of predatory pricing and cross-subsidization cases.

Moreover, this Commission has previously endorsed the incremental cost standard. In Order No. 22282, issued in Docket

No. 891181-TL on December 12, 1989, concerning Southern Bell's tariff filing to introduce ESSX Station Message Detail Recording, the Commission stated that new competitive offerings such as ESSX SMDR must feature rates that at least meet the incremental cost associated with the service. This is a means of ensuring that cross-subsidization of competitive offerings does not occur. Similarly, by Order No. 23431, issued September 5, 1990, in Docket No. 900514-TL regarding Southern Bell's proposed CO LAN offering, the Commission concluded that incremental costs are the relevant costs for this decision since they apply to the pricing decision and do not affect costs that are not affected as a result of the decision. Furthermore, since all services with prices set above their incremental cost will not affect other service rates, but will make a contribution to the common and joint costs. Accordingly, we find that incremental cost is the proper cost benchmark against which to determine the presence or absence of cross-subsidization.

## V. BEHAVIORS THAT CONSTITUTE CROSS-SUBSIDIZATION

The parties are clearly divided on this issue. Southern Bell, GTEFL, United, and Centel believe that the only type of behavior which constitutes cross subsidization, as contemplated by Section 364.3381, is pricing some services above incremental costs in order to allow other services sold by the same firm to be priced below incremental costs. They believe that cross-subsidization is distinctly different from other forms of anticompetitive behavior, and as such, advocate a narrow and specific type of behavior. ATT-C supports the concept of a specific type of behavior; however, it also believes that the provisions of Section 364.3381 should be read in conjunction with the other provisions of Chapter 364.

FCTA, FPTA, and OPC assert that behaviors considered to be cross subsidization should be considered in the broad sense. They believe that this Commission should be concerned not only with the relationship between price and cost, but also with any actions which might be considered to be discriminatory or anticompetitive. FCTA witness Cicchetti listed six types of behavior that he contended amount to cross subsidization:

1. Losses incurred from competitive services are financially subsidized through revenues from monopoly services (cross-subsidy).

2. The LEC monopoly pays in excess of current fair market price for products or services received from its subsidiaries or affiliated companies (cross-subsidy).
3. The LEC monopoly receives less than fair market price for products or services provided to its subsidiaries or affiliated companies (cross-subsidy).
4. A LEC competitive service does not bear its share of the costs of providing the service, including a pro rate share of overhead, and those costs are instead covered by revenues received from monopoly services (cross-subsidy).
5. The LEC monopoly provides service to its own competitive activity under rates, terms, or conditions more favorable than those services are provided to other companies offering similar competitive service (anticompetitive behavior).
6. The LEC monopoly provides services to its own competitive services that the monopoly will not provide to other companies (anticompetitive behavior).

We agree that the first case cited by FCTA does amount to cross-subsidy and thus is proscribed by Section 364.3381; however, although the other five cases noted may, in certain instances, be prohibited by the Commission in accord with the statutes, they are not prohibited by Section 364.3381.

The second case cited by witness Cicchetti is where a LEC purchases goods and services from an affiliate at prices in excess of fair market value. We agree that this behavior would be improper if the excess costs were passed on to LEC's ratepayers. If such actions result in ratepayers absorbing excess costs, then Section 364.03(1) affords the Commission the necessary authority to prohibit these actions.

Neither FCTA's third case, concerning a LEC charging less than fair market value for services rendered to an affiliate or subsidiary, or the fifth case, regarding a LEC providing monopoly service to its competitive operation under terms more favorable than those afforded a competitor, pertain to cross-subsidy. Moreover, in certain instances they are not necessarily improper. A differential in a price charged two parties in and of itself does not constitute undue price discrimination. However, where instances of undue discrimination by the LECs are identified, Section 364.10 expressly gives the Commission the authority and responsibility to evaluate these matters. Since the LECs are not

immune from the antitrust laws, adversely affected parties may also have recourse in the courts.

Witness Cicchetti's fourth case, where a LEC-provided competitive service does not bear its appropriate share of the firm's overhead costs, is associated with FCTA's concerns that, absent the Commission mandating a fully distributed cost methodology, LEC competitive services will get a free ride, to the detriment of monopoly ratepayers. We believe that the overheads to which witness Cicchetti referred are the LEC's joint and common costs, which are not reflected in incremental cost studies. The real issue thus is: How should rates for a mixture of competitive and monopoly services be set so as to recover in an equitable manner the LEC's total costs? This is clearly unrelated to cross-subsidization, although it is an extremely important issue to which the Commission devotes considerable efforts. One of this Commission's prime statutory directives is to establish just and reasonable rates.

Finally, witness Cicchetti's sixth example concerns a LEC providing certain services to its competitive operations that it will not provide to alternative providers. Again, we believe that these matters do not relate to cross-subsidization; rather, they tend to be associated with general policy questions regarding what actions the Commission should take to foster competition. Consequently, the appropriate action would depend upon the particular circumstances. In such matters, it is the function of the Commission to balance and resolve matters relating to the availability of monopoly services and inputs. In reaching decisions on such issues, the Commission has been directed by the Legislature to consider various factors, including encouraging competition in the telecommunications industry where it is deemed to be in the public interest.

This Commission is aware of FCTA's concerns regarding the potential for anticompetitive behavior to occur in the Florida telecommunications market, and the Commission will continue to identify such actions and provide appropriate remedies. With the expansion of competition into more sectors of the telephone market, the need for Commission oversight has increased as well.

However, we believe it is improper to interpret the cross-subsidization statute in so broad a sense that, conceivably, almost <u>any</u> business practice that adversely affects a party could be construed as "cross-subsidy." In addition to being improper, such

a broad interpretation is unnecessary. Various provisions of the statutes, including Sections 364.01(3)(d), 364.03, and 364.10, are sufficient to deal with any allegations of anticompetitive behavior.

We believe that cross-subsidization should be understood in terms of the economic definition, as a function of a service's price and cost. This Commission has determined herein that the incremental cost standard is the appropriate benchmark for detecting the presence or absence of cross-subsidy. Consequently, it follows that we believe that Section 364.3381 prohibits only a narrow range of actions: specifically, those instances where a LEC-provided competitive service is priced below its total incremental cost.

## VI. EFFECTIVELY COMPETITIVE SERVICES

By Order No. PSC-93-0289-FOF-TL, issued February 23, 1993, in Docket Nos. 910590-TL and 920255-TL, this Commission determined that the legislature did not differentiate the meaning of "competitive," "effectively competitive," and "subject to effective competition." That Order is, at this time, subject to a Motion for Reconsideration. However, witness Cicchetti filed testimony on behalf of FCTA asserting exactly the same arguments put forth by FPTA in the above referenced dockets.

Centel, GTEFL, Southern Bell, United, and ATT-C assert that the terms "competitive," "subject to effective competition," and "effectively competitive" are used interchangeably in Chapter 364. These terms are not specifically defined in the statute, but a monopoly service is defined as one "for which there is no effective competition, either by fact or by operation of law."

FIXCA, FPTA, and FCTA all argue that the three terms are not synonymous. FPTA and FCTA both argue that the terms had distinct meanings and should be construed as separate terms when reading the statute. FCTA witness Cicchetti testified that the term "competitive" means a service experiencing some form of competition, "subject to effective competition" means having the potential to become effectively competitive, and "effective competition" means a service experiencing true and fair competition between two or more providers.

FCTA and FPTA argue that the LECs' claims are also contrary to the rules of statutory interpretation. FPTA and FCTA cited numerous examples of case law that supported two specific rules: 1) that every provision in a statute is there for a purpose; and 2) that each word in a statute must be given its plain and ordinary meaning. FPTA argues:

> If the Legislature had intended the terms to have the same meaning, it would have left the words "subject to" and "effectively" out of the statute altogether. See, Sumner v. Board of Psychological Examiners, 555 So. 2d 919, 921 (Fla. 1st DCA 1990). (FPTA brief at 15)

This argument is not persuasive. The argument is more compelling, by reversing it: if the Legislature had intended "effective competition" and "subject to effective competition" to have different meanings, it simply would have defined them separately in Section 364.02.

Witness Cicchetti also argued that the plain and ordinary meaning of the term "competitive" according to Webster's dictionary is one relating to a service offered by the LEC and at least one other provider.

We do not dispute the rules of statutory interpretation cited by FPTA and FCTA, but would note that other more compelling rules of statutory interpretation exist as well. For example, it is a well-accepted rule of interpretation that a statute is passed as a whole and not in sections; therefore, each part of the statute must be construed in connection with every other part to produce a harmonious whole. In addition, even apparently plain words may not convey the meaning the drafters intended to impart; it is only within the full context of the statute that a word can convey an idea. When interpreting a statute, it is generally unnecessary to look beyond the language of the statute itself to arrive at its meaning. However, when different readings are urged, the tribunal must look to the reasons for enactment and the purposes to be served by the statute so that it can be construed consistent with such purposes. A statute should not be read literally where such a reading would be contrary to its purposes. These rules of interpretation negate the rules invoked by FPTA.

Also, a statute must be construed so as to make sense as a whole. This rule was cited by Southern Bell in its brief. If the

plain and ordinary meaning of a word or phrase causes the sentence or statute to become illogical or nonsensical, an interpretation that allows the statute to make sense must be used.

Applying the rules of construction stated above, a simple analysis of Sections 364.02 and 364.338 makes it clear that the Legislature did not differentiate the meaning of "competitive," "effectively competitive," and "subject to effective competition." Section 364.02 provides definitions for the terms used in Chapter 364. None of the three terms is defined in this section. However, the term "monopoly service" is defined as "a telecommunications service for which there is no effective competition, either in fact or by operation of law." This, under a plain and ordinary interpretation, provides for only two types of services: monopoly services and effectively competitive services. No provision is made for a service that is potentially competitive.

The term "effectively competitive" is only used once in Section 364.338, and is sandwiched between two uses of the term "competitive" in the same provision. One could extrapolate that the interchangeable use of these two terms in one provision means that they are synonymous.

The term "subject to effective competition" is used three times in Sections 364.338(2) and (3). It is also interlaced with several uses of the term "competitive." For example, "the competitive service" is used several times in Section 364.338(3) to refer back to "a service provided by a local exchange telecommunications company is subject to effective competition ..." It is evident that the meanings of "competitive" and "subject to effective competition" in these provisions are identical.

In addition, we note that if witness Cicchetti's claim of separate meanings for the terms were true, the statute would make no sense. For example, Section 364.338(3)(a)2 reads, in part, that "[i]f the commission determines ... that a service ... is subject to effective competition, the commission may: ... require that the competitive service be provided pursuant to a fully separate subsidiary or affiliate." (emphasis added) If separate meanings are to be given in this sentence, the sentence simply no longer makes logical sense. What competitive service is being discussed? If it cannot be the one referred to as "subject to effective competition," which one is it?

Therefore, even though "effectively competitive" and "subject to effective competition" are used in separate provisions of the statute, they are inextricably interwoven through the repeated use of the term "competitive." This fact, coupled with the clear lack of definitions for any of the three terms in Section 364.02, leads us to conclude that all three terms have identical meanings when used in Sections 364.338 and 364.3381. FCTA has not offered any evidence that would persuade us to change in any way the determination this Commission made in Docket Nos. 910590-TL and 910255-TL.

## VII. DETERMINATION THAT SERVICE IS EFFECTIVELY COMPETITIVE REQUIRED BEFORE PROVISIONS OF SECTION 364.3381 APPLY

ATT-C, Centel, GTEFL, Southern Bell, United and OPC all agreed that a determination must first be made that a service is effectively competitive before Section 364.3381 is applicable. FCTA, FPTA, FIXCA, and MCI all believe that no such determination is necessary. The parties arguments are a direct result of the positions taken on the distinction of the terms "effectively competitive," "subject to effective competition," and "competitive." The LECs and ATT-C maintained that since the three terms are synonymous, the only services mentioned in Section 364.3381 would be effectively competitive ones. Thus, they conclude that a determination that a service is effectively competitive must precede the actions proffered in Section 364.3381. OPC maintains that a determination about the existence of effective competition must precede the actions in Section 364.3381.

FIXCA, FPTA, and FCTA argue that since the terms have different meanings, no such determination need be made. Witness Cicchetti testified that since "competitive" is used in Section 364.3381, F.S. and "competitive" means any service provided by two or more providers, all such services would invoke the requirements of Section 364.3381. MCI agreed with FPTA's position; however it used its "building block" approach as its basis in its brief. MCI maintained that if the Commission properly implemented MCI's building block methodology, cross-subsidization would not occur. However, it presented no witnesses or testimony to substantiate this claim.

We agree that this issue is a direct result of the decision reached regarding the terms above. Sections 364.338 and 364.3381 are concerned primarily with services that are "competitive" and

"subject to effective competition." If these terms are synonymous with the term "effective competition," as we have determined herein, a plain and ordinary reading of Section 364.3381 tells us that this section deals solely with the determination and treatment of effectively competitive services. Accordingly, we find that the provisions of Section 364.3381 apply only after a determination is made, pursuant to Section 364.338, that a service is effectively competitive.

## VIII. OTHER FORMS OF ANTICOMPETITIVE BEHAVIOR

The LECs maintained that existing antitrust laws and Commission policies and complaint processes are adequate provisions for controlling any anticompetitive behavior.

ATT-C, FCTA, FPTA, FIXCA, and OPC all argued that certain forms of anticompetitive behavior should be prohibited. FCTA witness Cicchetti's list was the most exhaustive, and included the issues and items raised by all of the other parties:

1) predatory pricing by LECs;
2) excessive costs transferred to monopoly ratepayers by the LEC paying excessive rates for some services;
3) discriminatory provision of service to competitors by LECs;
4) discriminatory charges for services to competitors by LECs;
5) inferior services provided to competitors by LECs; and
6) undue preference by LECs for LEC-provided services such as marketing CPE with equipment.

Witness Cicchetti's first example, predatory pricing, is cited in Section 364.338(1) as a practice this Commission should not tolerate. The other examples given by witness Cicchetti are certainly areas that this Commission should investigate in detail, but are not necessarily anticompetitive behaviors.

For example, situation 2 may be an anticompetitive act if the regulated LEC pays an excessive cost for an unregulated service from an affiliate. However, it would only be an anticompetitive act if the service were identical to one offered from another entity, yet priced higher.

Situation 3 could be anticompetitive if the LEC used a discriminatory policy in its provision of services to competitors. For example, if a LEC provided certain features and functions to its pay telephone instruments but did not make them available to non-LEC pay telephones, it could be an anticompetitive act. However, there also could be technical limitations, a substitutable product, or public policy considerations that make such a policy desirable.

Situation 4 could also be anticompetitive if a LEC used price discrimination to artificially inflate its competitors' costs by marking up features the competitors needed such as access lines. On the other hand, there could also be justifiable reasons of fairness to other similarly-situated industries, cost differentials, or other public policy goals that make price discrimination a desirable outcome (for example, residence versus business access lines).

The same alternatives could be argued, depending on circumstances, for each of witness Cicchetti's examples with the exception of predatory pricing, which should be avoided whenever encountered. Witness Cicchetti described these practices as forms of cross-subsidization. However, we have determined herein that these practices are not cross-subsidization, but may be anticompetitive acts, depending on individual circumstances. Without the facts of each case before us, the Commission should not be put in the position of making blanket judgments regarding anticompetitive behavior. Additionally, there was no evidence presented by any witness that any of these possible anticompetitive behaviors are occurring in this state by any LEC.

ATT-C's witness Guedel attempted to address this issue by recommending several pricing guidelines for use by LECs. He advocated the imputation of tariffed rates for services when determining price floors, and the unbundling of LEC services consistent with Open Network Architecture guidelines. We agree that witness Guedel's ideas have some merit. However, they are not the focus of this case. Witness Guedel's arguments are aimed at how the Commission should set prices for certain LEC services. But, cross-subsidization concerns whether, given a set of prices, they are compensatory.

We do recognize the potential for anticompetitive behavior given the LECs' position as a monopoly provider of access for many of its competitors. We also acknowledge that the activities

identified by witness Cicchetti could be determined as poor public policy by this Commission. However, there was no evidence presented in this docket that would indicate that any such behavior exists. Additionally, each case should be examined separately to determine if the practice is detrimental to ratepayers, or possibly serves a public policy goal.

Southern Bell's witness Denton argued that the Commission's complaint process is sufficient for controlling these instances. We agree. This Commission has conducted in the past and is currently conducting several investigations, regarding anticompetitive behavior in the pay telephone market, voice mail market, and others. Many of these investigations were a result of complaints filed by customers or competitors of the LECs.

## IX. LEC REQUIREMENTS FOR COMPETITIVE SERVICES

We have defined cross-subsidy and have determined that once a service is found to be effectively competitive it is subject to the provisions of Section 364.3381. In addition, we must decide how to ensure that the requirements of Section 364.3381 are met.

### A. When Services Should Be Tested to Meet Requirements of Section 364.3381

The positions of the various parties regarding this issue derive from their views as to which services are subject to the cross-subsidy restrictions, the proper cost standard to detect cross-subsidization, and whether cross-subsidy should be understood in a narrow or a broad sense.

Southern Bell and Centel contend that once the Commission has determined, pursuant to Section 364.338, that a service is effectively competitive, it should be tested for compliance with Section 364.3381. United and GTEFL assert that the appropriate times to test for compliance are when new services are first offered, and when a significant change in price is made for a service.

ATT-C believes that the Commission should ensure that the prices charged for LEC competitive services exceed an established price floor. Witness Guedel advocated the imputation of tariffed rates for services when determining those price floors, and that the price floors should be adjusted whenever the underlying tariff

rate changes. We do not believe that the issue of whether imputation should be required is relevant to the detection of cross-subsidy. Accordingly, ATT-C's proposed imputation requirement is neither required nor appropriate to implement Section 364.3381.

FCTA witness Cicchetti asserted that cost studies should be filed every four years by the LECS as part of their minimum filing requirements. FPTA believes that the LECs should provide cost support for all LEC competitive services now and whenever a rate change is requested.

A review of the record in this proceeding reveals three instances where cross-subsidy tests may be appropriate: when a service has been found to be effectively competitive; when a new service is being offered; and, when a major change in rates is proposed. Southern Bell witness Emmerson also noted that the Commission's normal complaint process is always available to the Commission or an affected party as a means to require a LEC to establish that a competitive service is not being priced below its incremental cost.

Thus, we hereby approve the following guidelines to ensure that cross-subsidization is not present:

1) Once a service has been found to be effectively competitive pursuant to Section 364.338, it is subject to the cross-subsidization requirements of Section 364.3381 and the LEC must file the required revenue and incremental cost support information.

2) The LECs shall file cost data with new tariff filings sufficient to confirm that the service is covering its incremental costs and thus that the service is not being cross-subsidized.

3) We will not require the LECs to submit information showing the absence of cross-subsidy for all rate changes, as proposed by FPTA, when they file their Modified Minimum Filing Requirements, or for major rate changes. This requirement would prove excessive and could place the LECs at a competitive disadvantage with respect to certain service offerings. Depending upon the form of regulatory oversight afforded the effectively competitive service, requiring the LEC to submit

> incremental cost support in these instances may impede the LEC's ability to react in a timely fashion to the pricing actions of its competitors. As noted by Southern Bell witness Emmerson, the complaint process affords a party the opportunity to ascertain if a service is compensatory, if concerns exist. Moreover, for a major rate change, no party is precluded from requesting the LEC to confirm that its proposed rates are subsidy-free. Consequently, the complaint process provides a sufficient safeguard to require additional cross-subsidy tests as circumstances warrant.

Finally, we note that this Commission will initiate rulemaking proceedings, if necessary, to facilitate implementation of the requirements of Sections 364.338 and 364.3381.

B. Accounting Requirements

FCTA, FIXCA and FPTA believe that accounting requirements are needed. It appears that this view derives from their position that the Commission should mandate a fully distributed allocation methodology that ties back to the books and records of the company, to segregate a LEC's costs between competitive and monopoly services. Such an embedded cost approach presumably would be analogous to the FCC's Cost Allocation Manual (CAM). In that case, accounting guidelines would be required to ensure that allocation procedures were implemented correctly. FCTA witness Cicchetti asserted that, absent the use of fully separate subsidiaries, a fully distributed cost methodology is necessary in order to prevent cross-subsidization of competitive services by monopoly services. Although FCTA contends that use of separate subsidiaries would be the optimal way to prevent cross-subsidization, they did not indicate under what conditions this option would be preferable. However, witness Cicchetti acknowledged that the LECs currently enjoy economies of scope and scale, and admitted that these economies would be lost if the Commission imposed a separate subsidiary requirement. We have determined herein that the fully distributed cost standard is not appropriate for the detection of cross-subsidization; consequently, we conclude that there is no need for accounting requirements to track embedded cost allocations.

The LECs are all opposed to the Commission imposing additional accounting requirements. They contend that cross-subsidization is an economic notion, involving the relationship between a service's

price and its incremental cost; detection and thus prevention of cross-subsidy merely requires performing a Total Incremental Cost (TIC) test for the service. Given the nature of cross-subsidy it is inappropriate to impose ongoing accounting requirements to prevent its occurrence. Further, witness Beauvais asserted that even if the Commission were to impose accounting requirements, the existing accounting systems are inadequate, because they do not and are unable to track the financial performance of individual services. To develop such a service or product oriented system would be a massive undertaking, and unless it was maintained as a dual accounting system, would require coordination with the FCC.

Given that prevention of cross-subsidization is the primary basis for imposing accounting requirements for services subject to Section 364.3381, we do not believe such an action is needed at this time. We have identified certain specific instances where the LECs would be required to demonstrate that their effectively competitive services are not being cross-subsidized by revenues from monopoly services. We find that these requirements will constitute adequate safeguards.

C. Ensuring that Requirements of 364.3381 Are Met Before Offering Services

With the exception of MCI, who took no position, and FIXCA, all non-LEC intervenors contend that the Commission should prohibit LECs from offering services subject to the provisions of Section 364.3381 if the LECs have not provided assurance that the requirements of Section 364.3381 have been met. FCTA witness Cicchetti states that the language in the statute is mandatory and requires that the Commission prohibit the LECs from offering competitive services before the requirements of Section 364.3381 have been met.

FIXCA asserts that the LECs are currently providing services that are subject to the provisions of Section 364.3381, but that instead of having these services withdrawn, the Commission should rapidly initiate investigations for the major LECs to establish allocation methodologies for the major service categories. We would note that FIXCA did not sponsor a witness in this proceeding, and no evidence was introduced at hearing that substantiates the claim that LECs are presently offering effectively competitive services.

The LECs state that the introduction of new services which might be subject to effective competition should not be hindered due to a Section 364.338 proceeding. United witness Poag asserted that the telecommunications marketplace is too dynamic to have any procedures in place which would delay a service offering until an effectively competitive determination was made. He testified that the Commission already has the appropriate means to require cost support for prices and that tariffs can be denied if they do not meet the test. Centel agrees that the marketplace is fast moving, and suggests that services be allowed to go into effect immediately, with a requirement that the LEC demonstrate the absence of cross-subsidies within one year of their introduction. GTEFL witness Beauvais testified that the LEC will only offer those services whose prices are greater than or equal to incremental costs and whose total incremental revenues are greater than or equal to total incremental costs plus causally related fixed or common costs. If a proposed service does not pass these tests, then it will not be offered to the public. Southern Bell witness Denton stated that the provisions of Section 364.3381 do not apply until after a Section 364.338 hearing and a finding of effective competition. After such a finding the Commission must give the LECs sufficient time to be in compliance with the requirements of Section 364.3381.

We believe that all new services should follow the normal course for tariff filings, whether the service has been determined to be effectively competitive or not. The LECs routinely submit incremental cost support with the bulk of their tariff filings, and they should continue this practice. If properly conducted, the LECs' cost support should be sufficient to determine if the proposed service is being cross-subsidized. We believe that prohibiting a LEC from introducing an effectively competitive service until the conclusion of a Section 364.338 proceeding could give an undue advantage to the LEC's competitors. If this restriction were imposed, the LEC's competitors could delay implementation merely by filing a complaint alleging that the new LEC service was subject to effective competition. Further, imposing such a procedural obstacle could subvert the Commission's desire to allow fair and equitable competition where it is in the public interest.

However, we shall not allow the LEC an overabundance of time to bring a service into compliance with Section 364.3381. Absent a specific date certain for compliance, the LEC could do harm to the competitive market by underpricing the service, while using the

Commission's procedures as a means to delay remedying the problem. We thus believe it is appropriate to establish a requirement as to when the LEC must demonstrate that its effectively competitive service is in compliance with Section 364.3381. For a new service offering, this also should give the LEC an added incentive to submit all relevant information when initially filing a tariff, to ensure that the requirements of Section 364.3381 have been met.

Therefore, this Commission will not prohibit LECs from offering services subject to the provisions of Section 364.3381, before ensuring that the requirements of Section 364.3381 have been met. However, once a LEC service is found by this Commission to be effectively competitive and a final order is issued, within 90 days of the order the LEC shall file incremental cost data demonstrating that the service meets the requirements of Section 364.3381. We believe that this is an appropriate requirement, in that it does not restrict the LEC from introducing new services and it provides for a reasonable period for the LEC to bring its effectively competitive service into compliance with the statute.

D. Application of Cross-Subsidization Restrictions

The issue has been raised as to whether or not the language of the statute implies that cross subsidy is acceptable or appropriate in some cases. MCI, Southern Bell and OPC did not take positions on this issue.

The parties who took positions on this issue are in general agreement that the cross-subsidization restrictions only apply to subsidization of competitive services by LEC monopoly services. ATT-C witness Guedel did not believe that it would ever be acceptable for monopoly services to subsidize competitive services. However, he stated that the statute does not specifically address other cases, such as competitive services subsidizing other competitive services. GTEFL's witness Beauvais also asserted that the statute only applies to services that have been determined to be effectively competitive.

United witness Poag maintained that the intent of the statute is not to judge whether a cross-subsidy is appropriate or acceptable, but only to ensure that services determined by the Commission to be effectively competitive are not being subsidized by monopoly services. FCTA's witness Cicchetti stated that the language in Chapter 364 implies that cross-subsidy may be acceptable in instances to allow the Commission's universal service

goals to be met, but that the determination must be done on a case-by-case basis.

We agree with the parties and acknowledge that the statute only prohibits cross-subsidization of LEC effectively competitive services by LEC monopoly services, but is silent as to whether or not cross-subsidization is appropriate or acceptable in any other cases.

E. Further Requirements

Finally, those parties who took a position, stated that no further action by the Commission on this matter is necessary at this time. However, FCTA states that Section 364.338 allows the Commission to exempt a service subject to effective competition from certain statutory requirements and to impose other constraints. In particular, FCTA notes that Section 364.338(3)(a) allows the Commission to require a LEC to offer an effectively competitive in a fully separate subsidiary. Witness Cicchetti asserted that use of a fully separate subsidiary would be a more effective means to guard against economic cross-subsidy and anticompetitive behavior than imposition of accounting safeguards.

We could impose a separate subsidiary requirement for a LEC competitive service, which may prevent cross-subsidization. However, as acknowledged by FCTA witness Cicchetti, requiring a LEC to provide an effectively competitive service in a separate subsidiary could result in the loss of any economies of scale and scope that may exist. We believe that the record in this proceeding is insufficient to conclude under what conditions a fully separate subsidiary may be the most appropriate solution. Accordingly, we find that whether or not it is appropriate to impose a separate subsidiary requirement should be considered on a case-by-case basis in the Section 364.338 proceeding wherein a service is determined to be subject to effective competition. Thus, no further restrictions shall be imposed at this time.

Based on the foregoing, it is

ORDERED by the Florida Public Service Commission that each and every finding set forth herein is approved in every respect. It is further

ORDERED that the term cross-subsidization, as contained in Section 364.3381, Florida Statutes, shall be defined as the pricing

of competitive services below their incremental costs, with the resulting revenue shortfall recovered through the rates for monopoly services. It is further

ORDERED that the appropriate standard for detecting cross-subsidization is whether a service is priced below its total incremental cost. It is further

ORDERED that there is no distinction between the terms "effectively competitive," "subject to effective competition," and "competitive," as used in Sections 364.338 and 364.3381. It is further

ORDERED that the application of the provisions of Section 364.3381, first requires a determination that a service is effectively competitive, pursuant to the provisions of Section 364.338. It is further

ORDERED that the appropriate measures to ensure compliance with Section 364.3381 are set forth in the body of this Order. It is further

ORDERED that this docket shall be closed.

By ORDER of the Florida Public Service Commission this 12th day of July, 1993.

STEVE TRIBBLE, Director
Division of Records and Reporting

( S E A L )

PAK

by: Kay Flynn
Chief, Bureau of Records

NOTICE OF FURTHER PROCEEDINGS OR JUDICIAL REVIEW

The Florida Public Service Commission is required by Section 120.59(4), Florida Statutes, to notify parties of any administrative hearing or judicial review of Commission orders that is available under Sections 120.57 or 120.68, Florida Statutes, as well as the procedures and time limits that apply. This notice should not be construed to mean all requests for an administrative hearing or judicial review will be granted or result in the relief sought.

Any party adversely affected by the Commission's final action in this matter may request: 1) reconsideration of the decision by filing a motion for reconsideration with the Director, Division of Records and Reporting within fifteen (15) days of the issuance of this order in the form prescribed by Rule 25-22.060, Florida Administrative Code; or 2) judicial review by the Florida Supreme Court in the case of an electric, gas or telephone utility or the First District Court of Appeal in the case of a water or sewer utility by filing a notice of appeal with the Director, Division of Records and Reporting and filing a copy of the notice of appeal and the filing fee with the appropriate court. This filing must be completed within thirty (30) days after the issuance of this order, pursuant to Rule 9.110, Florida Rules of Civil Procedure. The notice of appeal must be in the form specified in Rule 9.900 (a), Florida Rules of Appellate Procedure.

FILE COPY

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

| | | |
|---|---|---|
| In re: Investigation into the Regulatory Safeguards Required to Prevent Cross-Subsidization by Telephone Companies | ) DOCKET NO. 910757-TP<br>) ORDER NO. PSC-92-1323-PCO-TP<br>) ISSUED: 11/16/92 |

ORDER ESTABLISHING PROCEDURE

By Order No. 24910, issued August 13, 1991, this Commission determined that issues regarding cross-subsidization should be addressed in a forum separate from the development of the local exchange company cost of service methodology docket. Accordingly, this docket was opened to examine the regulatory safeguards required to prevent cross-subsidization by telephone companies. On September 20, 19981, intervening parties submitted briefs addressing the legal requirements of revised Chapter 364. Based on the reaction of the parties at the February 4, 1992, Agenda Conference, this Commission determined that any proposed agency action issued would be protested by the parties. Accordingly, by Order No. 25816, issued February 4, 1992, we set this docket for hearing.

The scope of this proceeding shall be based upon the issues raised by the parties and Commission staff (staff) up to and during the prehearing conference, unless modified by the Commission. The hearing will be conducted according to the provisions of Chapter 120, Florida Statutes, and the rules of this Commission.

Discovery

a. When discovery requests are served and the respondent intends to object to or ask for clarification of the discovery request, the objection or request for clarification shall be made within ten days of service of the discovery request. This procedure is intended to reduce delay in resolving discovery disputes.

b. The hearing in this docket is set for March 10-12, 1993. Unless authorized by the Prehearing Officer for good cause shown, all discovery shall be completed by March 3, 1993. All interrogatories, requests for admissions, and requests for production of documents shall be numbered sequentially in order to facilitate their identification. The discovery requests will be numbered sequentially within a set and any subsequent discovery requests will continue the sequential numbering system. Unless subsequently modified by the Prehearing Officer, the following shall apply: interrogatories, including all subparts, shall be limited to 300, and requests for production of documents, including all subparts, shall be limited to 150.





c. Any information provided pursuant to a discovery request for which proprietary confidential business information status is requested shall be treated by the Commission and the parties as confidential. The information shall be exempt from Section 119.07(1), Florida Statutes, pending a formal ruling on such request by the Commission, or upon the return of the information to the person providing the information. If no determination of confidentiality has been made and the information has not been made a part of the evidentiary record in the proceeding, it shall be returned expeditiously to the person providing the information. If a determination of confidentiality has been made and the information was not entered into the record of the proceeding, it shall be returned to the person providing the information within the time period set forth in Section 364.183, Florida Statutes.

Diskette Filings

See Rule 25-22.028(1), Florida Administrative Code, for the requirements of filing on diskette for certain utilities.

Prefiled Testimony and Exhibits

Pursuant to Rule 25-22.048, Florida Administrative Code, each party shall prefile, in writing, all testimony that it intends to sponsor. Such testimony shall be typed on 8 1/2 inch x 11 inch transcript-quality paper, double spaced, with 25 numbered lines, on consecutively numbered pages, with left margins sufficient to allow for binding (1.25 inches).

Each exhibit intended to support a witness' prefiled testimony shall be attached to that witness' testimony when filed, identified by his or her initials, and consecutively numbered beginning with 1. All other known exhibits shall be marked for identification at the prehearing conference. After an opportunity for opposing parties to object to introduction of the exhibits and to cross-examine the witness sponsoring them, exhibits may be offered into evidence at the hearing. Exhibits accepted into evidence at the hearing shall be numbered sequentially. The pages of each exhibit shall also be numbered sequentially prior to filing with the Commission.

An original and fifteen copies of all testimony and exhibits shall be prefiled with the Director, Division of Records and Reporting by the close of business, which is 4:45 p.m., on the date due. A copy of all prefiled testimony and exhibits shall be served

by mail or hand delivery to all other parties and staff no later than the date filed with the Commission. Failure of a party to timely prefile exhibits and testimony from any witness in accordance with the foregoing requirements may bar admission of such exhibits and testimony.

Prehearing Statement

Pursuant to Rule 25-22.038(3), Florida Administrative Code, a prehearing statement shall be required of all parties in this docket. Staff will also file a prehearing statement. The original and fifteen copies of each prehearing statement shall be prefiled with the Director of the Division of Records and Reporting by the close of business, which is 4:45 p.m., on the date due. A copy of the prehearing statement shall be served on all other parties and staff no later than the date it is filed with the Commission. Failure of a party to timely file a prehearing statement shall be a waiver of any issue not raised by other parties or by the Commission. In addition, such failure shall preclude the party from presenting testimony in support of its position. Such prehearing statements shall set forth the following information in the sequence listed below.

(a) the name of all known witnesses that may be called by the party, and the subject matter of their testimony;

(b) a description of all known exhibits that may be used by the party, whether they may be identified on a composite basis, and the witness sponsoring each;

(c) a statement of basic position in the proceeding;

(d) a statement of each question of fact the party considers at issue, the party's position on each such issue, and which of the party's witnesses will address the issue;

(e) a statement of each question of law the party considers at issue and the party's position on each such issue;

(f) a statement of each policy question the party considers at issue, the party's position on each such issue, and which of the party's witnesses will address the issue;



(g) a statement of issues that have been stipulated to by the parties;

(h) a statement of all pending motions or other matters the party seeks action upon; and

(i) a statement as to any requirement set forth in this order that cannot be complied with, and the reasons therefore.

Prehearing Conference

A prehearing conference will be held in this docket at the Fletcher Building, 101 East Gaines Street, Tallahassee, Florida. The conditions of Rule 25-22.038(5)(b), Florida Administrative Code, shall be observed. Any party who fails to attend the prehearing conference, unless excused by the Prehearing Officer, will have waived all issues and positions raised in that party's prehearing statement.

Prehearing Procedure: Waiver of Issues

Any issue not raised by a party prior to the issuance of the prehearing order shall be waived by that party, except for good cause shown. A party seeking to raise a new issue after the issuance of the prehearing order shall demonstrate that: it was unable to identify the issue because of the complexity of the matter; discovery or other prehearing procedures were not adequate to fully develop the issue; due diligence was exercised to obtain facts touching on the issue; information obtained subsequent to the issuance of the prehearing order was not previously available to enable the party to identify the issue; and introduction of the issue could not be to the prejudice or surprise of any party. Specific reference shall be made to the information received, and how it enabled the party to identify the issue.

Unless a matter is not at issue for that party, each party shall diligently endeavor in good faith to take a position on each issue prior to issuance of the prehearing order. When a party is unable to take a position on an issue, it shall bring that fact to the attention of the Prehearing Officer. If the Prehearing Officer finds that the party has acted diligently and in good faith to take a position, and further finds that the party's failure to take a position will not prejudice other parties or confuse the

proceeding, the party may maintain "no position at this time" prior to hearing and thereafter identify its position in a post-hearing statement of issues. In the absence of such a finding by the Prehearing Officer, the party shall have waived the entire issue. When an issue and position have been properly identified, any party may adopt that issue and position in its post-hearing statement.

Document Identification

To facilitate the management of documents in this docket, exhibits will be numbered at the Prehearing Conference. Each exhibit submitted shall have the following in the upper right-hand corner: the docket number, the witness's name, the word "Exhibit" followed by a blank line for the exhibit number and the title of the exhibit.

An example of the typical exhibit identification format is as follows:

Docket No. 12345-TL
J. Doe Exhibit No. _____
Cost Studies for Minutes of Use by Time of Day

Tentative Issues

Attached to this order as Appendix "A" is a tentative list of the issues which have been identified in this proceeding. Prefiled testimony and prehearing statements shall address the issues set forth in Appendix "A".

Controlling Dates

The following dates have been established to govern the key ivities of this case.

| | | |
|---|---|---|
| 1) | Direct Testimony and exhibits | December 23, 1992 |
| 2) | Rebuttal Testimony and exhibits | January 21, 1993 |
| 5) | Prehearing Statements | January 21, 1993 |
| 6) | Prehearing Conference | February 26, 1993 |



| | | |
|---|---|---|
| 7) | Hearing | March 10-12, 1993 |
| 8) | Briefs (2 weeks after transcript) | April 23, 1993 |

Use of Confidential Information At Hearing

It is the policy of this Commission that all Commission hearings be open to the public at all times. The Commission also recognizes its obligation pursuant to Section 364.183, Florida Statutes, to protect proprietary confidential business information from disclosure outside the proceeding. Any party wishing to use any proprietary confidential business information, as that term is defined in Section 364.183, Florida Statutes, shall notify the Prehearing Officer and all parties of record by the time of the Prehearing Conference, or if not known at that time, no later than seven (7) days prior to the beginning of the hearing. The notice shall include a procedure to assure that the confidential nature of the information is preserved as required by statute. Failure of any party to comply with the seven day requirement described above shall be grounds to deny the party the opportunity to present evidence which is proprietary confidential business information.

When confidential information is used in the hearing, parties must have copies for the Commissioners, necessary staff, and the Court Reporter, in envelopes clearly marked with the nature of the contents. Any party wishing to examine the confidential material that is not subject to an order granting confidentiality shall be provided a copy in the same fashion as provided to the Commissioners, subject to execution of any appropriate protective agreement with the owner of the material. Counsel and witnesses are cautioned to avoid verbalizing confidential information in such a way that would compromise the confidential information. Therefore, confidential information should be presented by written exhibit when reasonably possible to do so. At the conclusion of that portion of the hearing that involves confidential information, all copies of confidential exhibits shall be returned to the proffering party. If a confidential exhibit has been admitted into evidence, the copy provided to the Court Reporter shall be retained in the Division of Records and Reporting's confidential files.

Post-Hearing Procedures

Pursuant to Rule 25-22.056(3)(a), Florida Administrative Code, each party is required to file a post-hearing statement of issues and positions. Positions in the post-hearing statement shall be summarized in no more that 50 words per issue. If a party's position on an issue in the post-hearing statement differs from what appears in the Prehearing Order, the position will be marked with an asterisk; in the absence of such demarcation, the party's position on that issue will be shown in the staff recommendation as it appears in the Prehearing Order. The rule also provides that any issue or position not included in the post-hearing statement is considered waived. If a party's position has not changed since the prehearing order was issued, the post-hearing statement can simply restate the prehearing position.

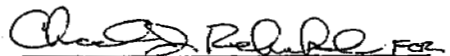
All post-hearing memoranda, including findings of fact, conclusions of law, statement of issues and positions, and briefs, shall be no more than 50 pages combined, and shall be filed simultaneously. Proposed findings of fact and conclusions of law are not required. If proposed findings of fact are submitted, the proposed findings must conform with Rule 25-22.056(2)(a) and (b). In addition, each proposed finding of fact shall be separately and consecutively numbered and shall be followed by a citation to the record, identifying transcript page and line number or exhibit number and page. Proposed findings shall identify the issue to which they relate and shall be grouped by issue, following the order of issues appearing in the Prehearing Order. Any written statement which is not clearly designated as a proposed finding of fact shall be considered to be legal argument rather than a proposed finding of fact. Arguments in briefs must be identified by issue number.

Based upon the foregoing, it is

ORDERED by Commissioner J. Terry Deason, as Prehearing Officer, that the provisions of this Order shall govern this proceeding unless modified by the Commission.



By ORDER of Commissioner J. Terry Deason, as Prehearing Officer, this 16th day of November, 1992.



J. TERRY DEASON, Commissioner
and Prehearing Officer

( S E A L )
PAK

NOTICE OF FURTHER PROCEEDINGS OR JUDICIAL REVIEW

The Florida Public Service Commission is required by Section 120.59(4), Florida Statutes, to notify parties of any administrative hearing or judicial review of Commission orders that is available under Sections 120.57 or 120.68, Florida Statutes, as well as the procedures and time limits that apply. This notice should not be construed to mean all requests for an administrative hearing or judicial review will be granted or result in the relief sought.

Any party adversely affected by this order, which is preliminary, procedural or intermediate in nature, may request: 1) reconsideration within 10 days pursuant to Rule 25-22.038(2), Florida Administrative Code, if issued by a Prehearing Officer; 2) reconsideration within 15 days pursuant to Rule 25-22.060, Florida Administrative Code, if issued by the Commission; or 3) judicial review by the Florida Supreme Court, in the case of an electric, gas or telephone utility, or the First District Court of Appeal, in the case of a water or wastewater utility. A motion for reconsideration shall be filed with the Director, Division of Records and Reporting, in the form prescribed by Rule 25-22.060, Florida Administrative Code. Judicial review of a preliminary, procedural or intermediate ruling or order is available if review of the final action will not provide an adequate remedy. Such review may be requested from the appropriate court, as described above, pursuant to Rule 9.100, Florida Rules of Appellate Procedure.

APPENDIX "A"

PROPOSED ISSUES

1. What is the appropriate definition of cross-subsidization, as contained in Section 364.3381, Florida Statutes?

2. How can the presence or absence of cross-subsidization be detected?

3. Does the detection of the presence or absence of cross-subsidization require a cost standard? If so, what is the appropriate cost standard?

4. As used in Section 364.3381, Cross-subsidization, what specific types of behavior are considered to constitute "cross-subsidization"? Specifically, should cross-subsidy be understood in a narrow sense (a function of the relationship between price and cost) or a broad sense (to include various other forms of anticompetitive behavior)?

5. Is there a distinction between the terms "effectively competitive", "subject to effective competition," and "competitive" as used in Chapter 364? (LEGAL)

6. Does the application of the provisions of 364.3381 first require a determination that a service is effectively competitive, pursuant to the provisions of 364.338? If not, what criteria should be used to identify those services subject to the provisions of 364.3381?

7. Section 364.01(3)(d), indicates that the Commission should prevent anticompetitive behavior in order to ensure that all telecommunications providers are treated fairly. Other than cross-subsidization, which is explicitly identified in the statute, are there identifiable forms of anticompetitive behavior that the Commission should prohibit? If so, what are they, what restrictions are appropriate, and how should any restrictions be implemented?



8. Once the Commission has defined cross-subsidy and the type of services that are subject to the provisions of 364.3381, what actions should the Commission take?

   a) How often and under what circumstances should the Commission require tests of specific services to ensure that the requirements of 364.3381 have been met?

   b) Should the Commission establish accounting requirements for those services subject to the provisions of 364.3381?

   c) Should the Commission prohibit local exchange companies (LECs) from offering services subject to the provisions of 364.3381, without assuring that the requirements of 364.3381 have been met?

   d) Does the language of the statute imply that cross-subsidy is appropriate or acceptable in some cases and unacceptable or inappropriate in others? If so, under what circumstances is it to be judged acceptable or not?

   e) What other actions should be taken?

9. Should the Commission order the LECs to:

   a) identify all services they offer which are also offered by other providers?

   b) identify the nature of the competition for services offered by other providers?