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BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

RULEMAKING: In re Generic Competitive Services Under 66 Pa.C.S.A. §§ 3005(b) and 3005(g)(2)	)))	**Docket No. L-00990141**

COMMENTS OF STATE SENATOR ALLEN G. KUKOVICH

I. Introduction.

Pursuant to the Secretary Letter of January 3, 2001, these comments are submitted in order to convey my support for a comprehensive Code of Conduct that effectively ensures the development of local phone service competition and prevents anti-competitive conduct by incumbent telecommunication providers.[1] On September 30, 1999, this Commission entered a final order and decision comprehensively resolving several important public policy issues related to the development of local phone service competition. Otherwise known as the *Global Order*, the Commission's Order included a detailed code-of-conduct intended to govern the relationship between Verizon's (as an incumbent local exchange carrier) wholesale business operations and its competitive retail affiliates.[2]

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[1] Joint Petition of Nextlink et al., P-00991648 et sew., Opinion and Order (September 30, 1999) (hereinafter referred to as "*Global Order*").

[2] The Code of Conduct applicable to Verizon is attached as Appendix C to the *Global Order*. The Commission ordered Verizon to structurally separate its retail and wholesale operations, and to implement and adhere to the Code of Conduct based on its finding that "the evidence presented by competitors to Bell Atlantic in this proceeding and in earlier proceedings incorporated into this docket have presented numerous examples where Bell Atlantic has abused its market power by providing competitors with less than comparable access to its network or engaged in other discriminatory conduct that prevented Bell Atlantic customers from switching to competitors." *Global Order* at 228.

Pursuant to the *Global Order,* on November 30, 1999, the Commission initiated a proposed rule-making proceeding in an effort to establish an industry-wide Code of Conduct consistent with the one adopted in the *Global Order.* However, as a result of Bell Atlantic's appeal of the *Global Order* to Commonwealth Court, the Commission stayed the period for the submission of comments in this proceeding. *See,* Secretarial Letter (April 26, 2000) PUC Dkt. L-00990141. On October 25, 2000, Commonwealth Court unanimously upheld the Commission's *Global Order* – specifically concluding that the provisions of the proposed Code of Conduct were "supported by the law and the record, and they do not contravene First Amendment constraints." *Bell Atlantic - Pennsylvania, Inc. v. Pennsylvania Public Utility Commission,* 763 A.2d 440, 470 (Pa. Cmwlth. 2001). Thereafter, the PUC reinitiated this proceeding and requested parties to file Comments to the November 30, 1999 Proposed Rulemaking Order.

I support the Commission's efforts to develop an even playing field for local phone service competition, but I am concerned that the Code of Conduct set forth in the proposed rulemaking will not accomplish that objective. The proposed rulemaking set forth, inexplicably, deviates from the interim Code of Conduct and proposed substantially less restrictive provisions.[3] As the PUC explained in its *Global Order*:

> If BA-PA's position prevailed, that is, only a code of conduct that is agreeable to the company can be implemented by this Commission, it would be akin to allowing the fox to guard the hen house. We are aware of no authority that would allow the monopolist to have the final say over what rules it will have to follow to prevent market abuses against its would-be-competitors." *Global Order* at 236.

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[3] The Commission's proposed rulemaking order's inclusion of several provisions initially advocated by Bell Atlantic is contrary to its prior rejection in the *Global Order.*

The proposed Code of Conduct does not establish a sufficient barrier against anit-competitive conduct in several respects. Two provisions in particular substantially diminish the effectiveness of the Code, as follows:

(1) The provision precluding the incumbent from providing itself or its affiliate with preferences or advantages in the provision of goods or services; and,

(2) The provision which requires the incumbent to make market information available to all competitors, including its own retail affiliate or division, at the same time and in the same manner.[4]

Through the submission of these comments, I urge the PUC to ensure that the Code of Conduct as originally proposed and outlined in the *Global Order* remains the adopted policy of the Commission. The same terms and conditions in the *Global Order* Code of Conduct must be implemented, on a permanent basis, in order to ensure the development of local phone service competition and the prevention of anti-competitive behavior. In order to accomplish its stated goal to adopt a Code which will "prevent discrimination, cross subsidies, and other market power abuses by ILECs in their local exchange markets and (is) therefore in the public interest,"[5] the Commission should restore the omitted provisions from its originally adopted Code of Conduct.

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[4] This Commission has recently underscored the importance of these provisions as part of its on going efforts to deregulate the competitive market for the supply of natural gas. See Binding Interim Standards of Conduct Pursuant to 66 Pa C.S.A. § 2209(a), PUC Dkt. M-00991249F0004 (November 18, 1999).

[5] Proposed Rulemaking Order, 30 Pa.B. at 542.

II Comments.

A. AN EFFECTIVE CODE OF CONDUCT APPLICABLE TO INCUMBENT MONOPOLIES IS CRITICAL TO THE DEVELOPMENT OF COMPETITION

The transition of public utility markets from a model based on a monopoly to a model based on competition presents a particularly challenging task for state and federal regulators alike. This is because, although competition is being introduced at the retail level, the incumbent maintains its role as dominant wholesale supplier to all new entrants and, at the time, competes with the new entrants on the retail side.[6] Unless the relationship between the incumbent wholesale and retail lines of business is strictly controlled by regulators, including the Commission, the incumbent will leverage the relationship between its two lines of businesses in order to maintain a dominant and insurmountable position in the retail marketplace.

As the Commission concisely described the problem pertaining to Bell:

> The functional/structural separation issue arises because of BA-PA's dual role as both supplier and competitor to other local exchange carriers who must rely on BA-PA for the ordering provisioning, maintenance, and operation of network elements that BA-PA's competitors need to provide their own local services to customers. If the potential conflict of interest created by the new role is not adequately addressed, an unlevel playing field will be created, which will severely hamper the development of a new, vibrant and effective competitive telecommunications markets in Pennsylvania. *Global Order* at 216.

A Code of Conduct governing the relationship between the ILEC's wholesale and retail business units is an essential element of the regulatory requirements and restrictions by which this

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[6] To make matters worse, at the time of the introduction of competition, the incumbent's retail line of business inherits a dominant position in the retail market as well.

potential conflict of interest must be addressed.[7] Without an adequate Code, as the Commission has acknowledged, market abuses by ILECs will undoubtedly become prevalent.[8]

Clearly, the Commission "got it right" when, after reviewing a mountain of evidence, it designed a Code of Conduct for Bell which, if strictly enforced, will prevent market abuses by incumbents and will provide an adequate safeguard for the development of competition. However, the proposed Code falls short of that mark and should be modified to return its substantive content to the Code adopted by the Commission in its *Global Order*.

B. THE CODE OF CONDUCT REQUIRES MODIFICATIONS TO RETURN IT TO THE EFFECTIVE CODE REQUIRED TO PRECLUDE ILEC MARKET ABUSES.

As explained above, two provisions of the proposed Code of Conduct included in the Commission's Proposed Rulemaking Order have, without explanation, been weakened in one case or completely omitted in another case, as compared to the appropriate Code of Conduct adopted in the *Global Order*. These deficiencies should be corrected in order to assure an effective Code of Conduct which, if strictly enforced, will preclude ILEC market abuses. Furthermore, the

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[7] In the Global proceedings, both Bell and GTE acknowledged that it is important to the development of competition that incumbent utilities do not provide unfair advantages to their affiliated interests and that preventing such anti-competitive behavior before it happens is preferable to reacting after the problem has already occurred. Tr. pp. 113, 1178.

[8] Proposed Rulemaking Order, 30 Pa. B. at 542. As the Commission acknowledged, the purpose of the Code of Conduct is to address the "entities with market power that [which market power] may be abused without adequate competitive safeguards in place" and that applying such a Code to new entrants who do not have the market power to engage in this type of anti-competitive behavior is inappropriate. 30 Pa. B. at 542-543. Of course, the Commission was correct and any suggestion by an ILEC that the Code should be applied to CLECs defies economic reality and should be summarily rejected.

provisions should be modified to clarify the application of the Code of Conduct to smaller ILECs and the inclusion of a potential structural separation requirement for GTE.

1. Section 63.143(2) Should Be Modified To Prelude All Preferences and Disadvantages.

In its *Global Order*, based upon the huge evidentiary record in that proceeding, the Commission included provision no. 1 in its Code of Conduct which reads as follows:

> 1. No incumbent local exchange company shall give its competitive local exchange affiliate or division preferential treatment in the provision of goods and services.

The provision properly bars all preferential treatment by the ILEC regardless of the given function it is performing at any given time.

Unfortunately, and for completely unexplained reasons, when the Commission issued its Proposed Rulemaking Order, it included a similar, but substantially different provision under §63.143(2) which provides as follows:

> 2. An ILEC may not give itself (or any of its affiliates, divisions or operating units) or any CLEC any preference or advantage over any other CLEC in the ordering, provisioning or repair of any services that it is obligated to provide CLECs under any applicable Federal or State law.

The new, proposed provision weakens the *Global Order* provision by permitting an ILEC to give preference or advantage to itself as long as it is not engaged in the ordering, provisioning or repair functions or as long as it is providing a service which is not absolutely mandatory under applicable law. So, for example, the proposed rule would allow an ILEC to design its functions in a way that would create opportunities for providing itself preferential treatment.[9] Furthermore, the

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[9] The proposed Code provides no guidance as to how an ILEC determines what function employees are engaged it at any given time, thus leaving it up to the ILEC's discretion to design its functions any way it sees fit.

ILEC could provide itself preferences and advantages by providing itself services, like for example UNE-P to a customer with over $80,000 in total billed revenue, which it may not be legally required to provide to CLECs. These types of preferences and advantages are completely inappropriate in a competitive environment and certainly should not be blessed by the Commission.

It is noteworthy that in establishing a Code of Conduct applicable to the natural gas industry, the Commission emphatically rejected a similar limitation on the provision precluding preferences and advantages. In its Tentative Order adopted August 26, 1999, the Commission proposed the following provision to be included in its Natural Gas Code:[10]

> (11) Natural Gas distribution companies shall not give its affiliated natural gas suppliers preference over a non-affiliated natural gas supplier in the provision of goods and services, including processing requests for information, complaints and responses to service interruptions. Natural gas distribution companies shall provide comparable treatment without regard to a customer's chosen natural gas supplier.

The provision proposed by the Commission properly barred all preferences in the provision of all goods and services and merely identified certain service functions where it apparently believed preferences might be particularly prevalent.

Comments submitted to the Commission by the Pennsylvania Gas Association and Columbia Gas of Pennsylvania, Inc. requested the Commission to place restrictions on the provision to preclude preferences only for "Commission regulated" services. In its Final Order, after finding that "To ensure that a competitive natural gas supply market is established in the Commonwealth, the Standards of Conduct must ensure that natural gas distribution companies do

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[10] Tentative Order Re: Proposed Interim Binding Standards of Conduct Pursuant to 66 Pa. C.S. §2209, M-00991249F0004.

not provide their affiliated natural gas supplier with any preferential treatment." The Commission stated as follows in rejecting the PGA and Columbia comments and maintaining the proposed provision.

> Specifically, PGA and Columbia question those standards which place limitations on a natural gas distribution companies' provision of "goods and services" or "all other services" to its affiliated natural gas supplier. PGA asserts that these limitations extend beyond the Commission's existing policy statement and if real literally would restrict a natural gas distribution company from providing its affiliated natural gas supplier with legal or accounting services. To correct the perceived problem, PGA and Columbia required that these standards be clarified by insertion of the words "Commission regulated" prior to services.
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> The Commission is cognizant that the Standards of Conduct differ from the existing policy statement. Contrary to the arguments from some of the commenters, however, the introduction of competition to the natural gas supply service in Pennsylvania warrants such changes. Moreover, the requirement that natural gas distribution companies not provide [any] preferential treatment to their affiliated natural gas supplier is consistent with the Act's requirements prohibiting cross-subsidization and the requirement that natural gas distribution companies and natural gas suppliers maintain separate books. 66 Pa. C.S. §2209(c)(3) and (4).

November 18, 1999 Final Order at 6-7.

The comparable provision in the Code of Conduct governing electric generation suppliers and electric distribution company to an electric generation supplier, including but not limited to, its affiliates or divisions. The regulation, 52 Pa. §54.122, provides as follows:

> (1) An electric distribution company may not give an electric generation supplier, including without limitation, its affiliate or division, any preference or advantage over any other electric generation supplier in processing a request by a distribution company customer for retail generation supply service.

Despite its adherence to a comparable approach in both energy industries and in the *Global Order*, the Commission has now proposed a more lenient provision to govern preferences and advantages in the telecommunications industry.[11] The Commission's concerns with cross-subsidization and equal treatment are just as critical in the telecommunications industry as they are in the natural gas industry. The Commission should not permit incumbent preferences or advantages in the telecommunications industry, either, and should restore the language of the original Code of Conduct in the *Global Order*.

2. Section 63.143 Improperly Omits A Provision Requiring Equal Disclosure of ILEC Marketing Information To All Competitors.

The Code of Conduct ordered by the Commission in its *Global Order* includes a critical provision which provides as follows:

> The incumbent local exchange company shall simultaneously make available to any competitor any market information not in the public domain that is supplied to any competitive local exchange affiliate or division.

The provision recognizes that because CLECs rely on the ILEC as a wholesale provider, the wholesale affiliate or division of the ILEC will be in a unique position to collect marketing or commercially valuable information pertaining to the competitive market. The provision assures that competitive parity is maintained by requiring the ILEC to either refrain from disclosing such information to any retail competitor, including its affiliate or division, or provide the information to all retail competitors at the same time. The competitive advantage provided if only one retail competitor has access to such valuable information is obvious and should not be permitted.

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[11] The restrictions proposed by PGA/Columbia did not limit the functions for which preferences and advantages were precluded and did not limit the service to those that were legally mandated, only to those that were Commission regulated.

Nevertheless, without any explanation, the Commission completely omitted this important provision from Annex A to its Proposed Rulemaking Order. It is critical for the Commission to correct this omission in its final rulemaking order, otherwise, one retail competitor, the ILEC affiliate or division, will be provided a crucial advantage in the marketplace which others cannot match.

Inclusion of such a provision has precedent in other utility group codes of conduct. For example, the Natural Gas Code of Conduct includes a provision which states that "A natural gas distribution company should not provide information received from non-affiliated customers or natural gas suppliers to its affiliated natural gas suppliers." This provision is based on the Natural Gas deregulation statute, 66 Pa. C.S. §2209(c)(2), which bars the disclosure or preferential sharing of any confidential information. The Comparable *Global Order* Code of Conduct provision prohibits the sharing of any non-public information, which by definition is confidential information.

Since, generally speaking, marketing or other commercially valuable information would be collected by an incumbent through information received (and aggregated or otherwise analyzed) from non-affiliated customers or other retail competition, the provision seeks to generally prohibit the dissemination of commercially valuable information to the incumbent's retail affiliate or division. Furthermore, a similar provision was enacted in the final rules for the electric industry code of conduct. The Code of Conduct that governs electric generation suppliers and distribution companies, 52 Pa. Code §54.122, proscribes as follows:

(2) Subject to any customer privacy or confidentiality constraints, an electric distribution company may not give an electric generation supplier, including without limitation its affiliate or division, any preference or advantage in the dissemination or disclosure of customer information and any dissemination or disclosure shall occur at the same time and in an equal and nondiscriminatory manner. "Customer information" means all information pertaining to retail electric customer identity and current and future retail electric customer usage patterns, including appliance usage patterns, service requirements or service facilities.

The term "customer information" as used in the electric regulation squares with the use of the term "market information that is not in the public domain" that is used in the *Global Order* Code of Conduct provision. "Customer information" may actually be broader than "market information that is not in the public domain" but in any event is certainly consistent with the language of the *Global Order* Code of Conduct. Inclusion of such provision in the Commission's telecommunication's code of conduct is just as important as for other industry groups. The Commission should modify its proposed regulations to include Provision no. 3 adopted in Appendix C to its *Global Order*.

3. The Commission Should Clarify The Application Of The Code To Smaller ILECs.

The Commission's proposed regulation is ambiguous as to its application to ILECs with less than 250,000 access lines. Section 63.143(1) provides that ILECs with more than 250,000 access lines must functionally separate their wholesale and retail operating units. Accordingly, it was presumably the Commission's intent that ILECs with less than 250,000 access lines would not be required to functionally separate.

However, at the same time, the plain language of the regulation applies the Code of Conduct provisions contained in subsections (2) through (10) of Section 63.143 to all ILECs, regardless of their size. While this is an appropriate result, from a practical perspective it would seem to be virtually impossible for a smaller ILEC to comply with subsections (2) through (10) without functionally separating.[12]

The regulation should be clarified to eliminate this ambiguity by requiring ILECs with less than 250,000 access lines to functionally separate to the extent necessary to comply with subsections (2) through (10). Such a modification reaches a fair balance by only requiring a more limited functional separation for smaller ILECs with more limited resources.

However, it is essential that all ILECs of all sizes remain subject to the Code of Conduct. The General Assembly never intended for any ILEC to be isolated from competition (or to be able to engage in unfair competition). All of Pennsylvania's citizens, regardless of whether they reside in an urban or rural areas and regardless of their incumbent service provider, deserve and must be provided the far-reaching benefits provided by a competitive marketplace. Obviously, this issue is of particular concern to members of the General Assembly who represent constituents who reside within the service territories of smaller ILECs. The modifications outlined above will move forward a pro-competitive agenda in these areas without placing undue burden on the smaller ILECs.

4. The Regulation Should Be Modified To Establish Procedures For Structural Separation Of GTE.

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[12] For example, subsection (2) places restrictions pertaining to customer proprietary information on the "ILEC's wholesale operating unit." and subsection (7) establishes restrictions on the ILEC's provision of goods and services to any affiliate, division or operating unit.

Section 63.143(1) establishes procedures for Commission consideration of whether an ILEC should be subjected to a structural separation requirement. As proposed, the regulation only establishes procedures to address the structural separation of ILECs with over 1,000,000 access lines — by definition limiting the provision's applicability to Verizon.

There is no justification for not making these procedures available to address the potential structural separation of GTE. GTE Corp., the parent of GTE North, through its operating companies, is the largest ILEC in the Nation. The fact that this huge corporation only operates approximately 800,000 access lines in Pennsylvania does not diminish the Company's extensive ability to leverage its market power to impede competition in its service territory. The only reason that the Commission did not find the same market abuses for GTE as it did for Verizon in its *Global Order*, is that GTE has somehow completely avoided opening its local markets to any competition.

In the Global Proceedings, extensive evidence was introduced that argued stridently in support of imposition of a structural separation requirement for GTE. While the Commission did not adopt such an approach for now, there is no justification for not including procedures applicable to Commission review of whether GTE should be subject to a structural separation requirement in the future.

Simply because Verizon has chosen for GTE North and the former Bell Atlantic-PA operations to remain separate in Pennsylvania, is no reason to exempt the former GTE North operations from the structural separation requirements. Considering that the merged company has multiplied its market power for both operating companies, such a result shall be precluded at all costs.

Accordingly, the regulation should be modified to adopt a threshold of 600,000 access lines for procedures relating to further safeguards, including structural separation. Such a modification will provide some assurance that GTE's markets will be opened to competition in the foreseeable future.

C. THE PUC SHOULD REJECT ALL ILEC ATTEMPTS TO PURSUE BACKSLIDING ON THE PROPOSED CODE

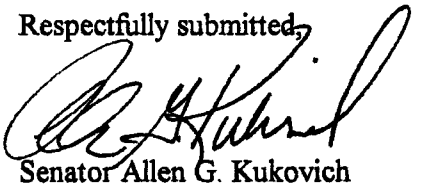
Undoubtedly, the ILECs will submit comments to the Commission complaining that the proposed Code puts them at a competitive disadvantage and will make various proposals to the Commission to modify, delete or add provisions in an attempt to weaken the Code. As it did in the Global Proceedings, the Commission should reject these comments and recognize them for what they are — self-serving attempts to maintain their ability to leverage their dual roles as wholesale supplier and retail competitor.

In particular, the Commission should be acutely aware of attempts by Bell and other ILECs to modify the regulation to fundamentally change how the ILEC separates its business units. In the Global Proceedings, Bell proposed a Code of Conduct which would have actually hurt rather than helped competition. For example, the Bell Code of Conduct proposed in the Global Proceedings does not govern the interaction between business units or affiliates, it merely places certain superficial requirements on its employees regardless of their responsibilities. The structure of Bell's code does nothing more than attempt to evade a meaningful separation of its operations.

Most notably, Bell's proposed *Global* code does separate out a group of employees to deal with CLECs but, amazingly, this is not the same group which provides service to Bell's retail arm. Accordingly, to the extent there is any separation in Bell's code, it separates and formalizes a structure which, by its very nature, is unequal and anti-competitive by meshing together its own wholesale and retail arms and establishing a separate organization to deal with CLECs.[13]

Fortunately, the Commission rejected this approach, which formalizes rather than eliminates preferences and advantages, in both its *Global Order* and its Proposed Rulemaking Order. It is critical that the Commission continue to resist any ILEC attempts to pursue such an approach in finalizing these regulations.

Respectfully submitted,



Senator Allen G. Kukovich

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[13] Not only does Bell's Global code separate out an organization to deal with CLECs, it requires the organization to have a separate direct line of management. At the same time, the Bell code claims that the meshed together wholesale and retail arm of Bell's business will not provide any preference to itself as compared to what the separate organization provides to unaffiliated CLECs. The obvious question is how Bell would even know whether preferences were being provided given the completely separate treatment provided CLECs as compared to Bell's retail arm.