



Romney Building, 10th Floor
Lansing, Michigan 48909
Phone: 517/373-6466

PROHIBIT SWITCHING TELEPHONE PROVIDERS WITHOUT CUSTOMER CONSENT

**House Bill 5280 as passed by the Senate
Sponsor: Rep. Agnes Dobronski**

**Senate Bill 837 as passed by the Senate
Sponsor: Sen. Mike Rogers**

**House Committee: Public Utilities
Senate Committee: Technology and Energy
Third Analysis (6-17-98)**

THE APPARENT PROBLEM:

Since the deregulation of the telecommunications industry, the competition for phone customers is intense, and sometimes illegal. For example, there have been reports of long distance carrier switching, unauthorized by the customer. The Federal Communications Commission has reported that unauthorized switching complaints rose to 44,000 in 1997 from 16,000 in 1996, causing the U.S. Congress to introduce bills to set higher penalties and to provide for stronger regulatory measures to protect consumers.

Unauthorized switching of telephone services without permission, known as "slamming" in the telecommunications industry, seems to be occurring at a higher rate in Michigan than in most other states, according to a recent survey by the National Consumers League. That survey ranked Michigan eighth in unlawful carrier switching. Between January and June 1997, Ameritech reported 12,500 complaints, and in September 1997 alone, 5,126 complaints (as reported in the *Detroit Free Press*, 10-21-97).

The National Consumers League (a Washington-based group hired by Ameritech), recently conducted a survey of residents in Detroit, Grand Rapids, Chicago, and Milwaukee, because those cities are reportedly among the hardest hit in the nation. According to the survey, slammers target people with higher incomes, and large phone bills. They sometimes trick customers into authorizing a switch in service by getting them to sign their name on contest entries. Other times they send a promotional mailing with a

card enclosed that must be returned in order to stop a switch in service.

Current Federal Communications Commission (FCC) policies and rules prohibit slamming and require long distance companies to obtain a customer's authorization in order to change his or her long distance service. Consumers who receive higher bills as a result of being slammed are required to pay only the toll charges they would have paid to the original long distance carrier.

Although the unauthorized switching of telephone services without permission from the customer is a federal offense, Michigan law does not outlaw the practice, and thus there is no authority for the Public Service Commission to enforce penalties against companies that engage in it. Without state regulatory authority, renegade companies are free to continue their unlawful practices, and consumers are often unaware of their right (under federal law) to request further information about alternative companies, and the responsibility those companies have to disclose detailed information about their services.

Currently, the Public Service Commission (PSC) records customers' complaints, and tries to get credits for people who have been slammed, since the commission cannot fine slammers. Sometimes the PSC forwards the complaints to the Federal Communications Commission, which does have the jurisdiction to fine. Some argue that "slamming" would decline if the PSC had the authority to penalize companies guilty of unauthorized switching practices,

House Bill 5280 and Senate Bill 837 (6-17-98)

and that such regulatory authority would help to educate consumers about their rights under the law.

THE CONTENT OF THE BILLS:

House Bill 5280 (S-6) and Senate Bill 837 (S-4) would amend the Michigan Telecommunications Act to provide for rulemaking authority and set penalties when telephone companies switch customers' service without the customers' consent. The bills are tied to each other.

House Bill 5280 would amend the Michigan Telecommunications Act (MCL 484.2505) to provide that an end user (the retail subscriber) of a telecommunications services provider could not be switched to another provider without the end user's authorization. Under the bill, the Public Service Commission (PSC) would have to issue orders to ensure that an end user was not switched without the end user's oral authorization, written confirmation, confirmation through an independent third party, or other verification procedures subject to commission approval that confirmed the end user's intent to make a switch and his or her approval of the specific details of the switch. Further, the PSC order would require that all providers comply with the regulations of the Federal Communications Commission on verification procedures for the switching on an end user's telecommunications provider. Under House Bill 5280, "telecommunications provider" would mean a person that provided one or more telecommunications services for compensation; the term would not include a provider of commercial mobile service as defined in the Federal Communications Act.

Senate Bill 837 would amend the Michigan Telecommunications Act (MCL 484.2506) to allow the PSC to conduct a contested case upon the receipt of a complaint filed by a person alleging a violation of the provisions of House Bill 5280, an end user who had been switched to another provider in violation of the bill, or a provider who had been removed as an end user's provider without the end user's authorization, or on the PSC's own motion. Under the bill, if the PSC found that a telecommunications provider had violated an order, the PSC would be required to order remedies and penalties to protect those who had suffered damages as a result of the violation, including but not limited to any of the following:

- 1) Order a person to pay a fine of at least \$10,000 but not more than \$20,000 for a first offense, or at least \$25,000 but not more than \$40,000 for a second or

subsequent offense. If the PSC found that a second or subsequent violation had been made knowingly in violation of the act, the maximum fine would be \$50,000. Each switch made in violation of the act would be a separate offense.

- 2) Order an unauthorized provider to make a refund to the end user.

- 3) Order an unauthorized provider to reimburse an authorized provider.

- 4) Revoke the license of a person licensed under the Michigan Telecommunications Act, if the PSC found a pattern of violations.

- 5) Issue cease and desist orders.

Under Senate Bill 837, a provider would not be liable for a violation of House Bill 5280 if the provider had otherwise fully complied with the bill and showed that the violation was an unintentional and bona fide error notwithstanding the maintenance of procedures reasonably adopted to avoid the error. Examples of a bona fide error would include a clerical, calculation, computer malfunction, programming, or printing error. An error in legal judgment with respect to a person's obligations under the bill would not be considered a bona fide error. The burden of proving that a violation was an unintentional and bona fide error would be on the provider. If the PSC found that a party's complaint or defense was frivolous, the PSC would be required to award the prevailing party costs, including reasonable attorney fees.

FISCAL IMPLICATIONS:

The House Fiscal Agency notes that the new regulatory rule-making provisions of Senate Bill 837 are expected to increase state costs. State revenue may also increase if the commission imposes fines on violators. (6-16-98)

ARGUMENTS:

For:

In May 1998, the U.S. Senate overwhelmingly approved a bill to provide federal regulators and the courts with new powers to determine fault and impose penalties and damages when telephone companies switch the long distance service of customers without their permission. Unless the FCC finds mitigating circumstances, a carrier that fails to follow procedures for showing that it has a consumer's permission is

punishable by a fine of not less than \$40,000 for a first offense and not less than \$15,000 for further offenses. The FCC is also authorized to award damages that amount to three times the cost to the consumer of the unauthorized phone charge. The bill requires that when a telephone customer selects a new telephone exchange service, the carrier selected must notify the consumer in writing within 15 days, and it directs the FCC to set a time period of not more than 120 days for a carrier to resolve a complaint of an unauthorized change of telephone service. The legislation also requires the FCC to make a series of reports to Congress, including notifying lawmakers of the 10 carriers with the highest number of slamming complaints. Similar legislation is pending in the U. S. House of Representatives, as reported by the *New York Times* (5-13-98).

For:

Certain kinds of competitive practices are unacceptable and must be regulated. For example, competition among long distance telephone service companies is out of control and should be regulated when customers find their carriers have been switched without their authorization. According to articles in the *Detroit Free Press* earlier this year, one company that aggressively promotes switching, Long Distance Services, Inc. (LDSI), is located in Michigan (Troy), and it re-sells long distance service across the country. In May 1997, the Alabama Public Service Commission asked the state's attorney general to prosecute LDSI for allegedly defrauding customers and conducting misleading and deceptive marketing campaigns. Alabama had logged 889 complaints against LDSI since the company began reselling long distance service in January 1995. New York suspended LDSI's license to operate, and Georgia, which received more than 500 complaints in 12 months, recently held hearings on the company's tactics. The Michigan Public Service Commission also has received many complaints. Though this practice is illegal under federal law, the PSC has no authority to penalize violators as Michigan statute does not criminalize the practice. This legislation to prevent unauthorized switching, or "slamming," is necessary in order to give Michigan regulators the authority to penalize violators.

For:

Telephone customers have the right to use any long distance carrier they choose and to change carriers whenever they wish, especially because different companies charge different rates. Slamming takes choices away from consumers, often without their

knowledge, and distorts the long distance competitive market by rewarding companies that engage in deceptive practices. Current Michigan law, however, does not contain a prohibition against slamming, and the PSC does not have the authority to penalize carriers that engage in this practice. Currently, the PSC can do little more than record complaints, attempt to get credit for people who have been slammed, and/or forward complaints to the FCC. By requiring the PSC to issue orders ensuring that customers were not switched without their authorization, the bill would empower the commission to conduct contested case hearings to hear customer complaints. The PSC also could make sure that violators paid substantial financial penalties, and that slamming victims received a refund for overcharges or reimbursement for lost revenue. By providing for regulatory authority at the state level, the bill also could help to educate customers about their rights under the law.

Against:

Some people believe that the bill also should provide for the continuation of "PIC" (primary interexchange carrier) protection against slamming. (A PIC is the carrier that a customer chooses to handle its 1+ toll dialing.) This approach allows customers to freeze their telephone service provider until they indicate their intent to change carriers. Although the PSC recently found that Ameritech Michigan's method of enforcing PIC protection was anticompetitive, and in violation of previous PSC orders, evidently PIC protection can be implemented in valid ways that enable customers to change carriers when they desire to do so. Arguably, this tool also is needed to protect customers against slamming.

Against:

The financial penalties set in Senate Bill 837 should correspond to those set in similar federal legislation. Senate Bill 837 proposes a fine for a first offense that is lower than the penalty established by the U.S. Senate in similar legislation. The federal legislation sets the fine at \$40,000 for a first offense, but this legislation would set a first time fine at between \$25,000 and \$40,000. Also, fines for subsequent offenses would be higher than their counterparts in the federal legislation. Ultimately, the fines should be identical.

Against:

The financial penalties in these bills remain excessive. Occasionally carriers make mistakes in their effort to

win new customers from their competitors. Financial penalties should not be assessed for most of these mistakes. Instead, carriers can use third-party verification (which allows the carrier who the customer is leaving to hire an independent contractor who calls the departing customer to "verify" their imminent departure). More extensive use of third-party verification would detect (and thwart) the most egregious competitive practices, and it would not be necessary to impose financial penalties on the carrier.

Response:

These bills have been amended to allow for "bona fide errors" on the part of telecommunication carriers. If the case of bona fide errors--errors that the carrier proves are unintentional--no penalties will be assessed. (A bona fide error would include a clerical, calculation, computer malfunction, programming, or printing error.) As to third-party verification, it is wise to keep in mind that third party verification is a form of peer-review. Peer-review may reverse particular unethical events among carriers if the peer review is uniform and pervasive. However, peer review does not penalize such behavior or prevent it within an institutionalized and systematic regulatory scheme. Eliminating the recruitment practices of aggressively competitive telecommunication carriers will not be accomplished through self- or peer-review. Egregious marketing practices are illegal and unethical, they harass customers, and they are unwanted. One way to punish and prevent such behavior is to assess a stiff fine.

POSITIONS:

Ameritech supports the bills. (6-16-98)

MCI supports the bills. (6-16-98)

Analyst: J. Hunault

■ This analysis was prepared by nonpartisan House staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.