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BEFORE THE ARIZONA CORPORATION COMMISSION

WILLIAM A. MUNDELL
Chairman
JIM IRVIN
Commissioner
MARC SPITZER
Commissioner

Arizona Corporation Commission
DOCKETED
MAR 29 2002
DOCKETED BY

IN THE MATTER OF DISSEMINATION OF INDIVIDUAL CUSTOMER PROPRIETARY NETWORK INFORMATION BY TELECOMMUNICATIONS CARRIERS.	DOCKET NO. RT-00000J-02-0066

QWEST CORPORATION'S NOTICE OF FILING CPNI COMMENTS

Qwest Corporation ("Qwest") hereby respectfully submits the attached comments in response to Ernest G. Johnson's Memorandum of February 15, 2002, soliciting comments from interested parties on the Arizona Corporation Commission's investigation into CPNI. Qwest takes very seriously its obligations with respect to customer information, as well as the concerns of the Commission and Qwest customers with respect to that information. Qwest welcomes the opportunity for further discussion of these issues with the Commission and all interested parties. In addition to these attached comments, Qwest also incorporates by reference its previous letters to the Commission and the Attorney General on CPNI[1] and comments made at the Open

[1] The following letters have been sent by Qwest to the Commission or to the Attorney General, of which the Commissioners received copies: 1) Letter dated January 14, 2002 from James A. Smith to Attorney General Janet Napolitano; 2) Letter dated January 14, 2002 to Chairman Mundell, and Commissioners Irvin and Spitzer from Teresa Wahlert; and 3) Letter dated February 6, 2002 to Chairman Mundell from Teresa Wahlert.

Meetings held on this issue.[2] Qwest also requests through its undersigned counsel to be placed on the formal service list for this proceeding.

Respectfully submitted this 29th day of March, 2002.

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ORIGINAL and 10 copies of the foregoing hand-delivered for filing this 29th day of March, 2002 to:

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_____

[2] Open meetings on this issue were held on January 16, 2002 and January 28, 2002.

Qwest's Response to Staff's Questions on February 15, 2002

Qwest respectfully submits these comments in response to the questions posed by Staff on February 15, 2002 concerning customer information issues. Qwest takes very seriously its obligations with respect to CPNI as well as the concerns of this Commission and Qwest's customers with respect to that information. Even before there existed federal legislation in this area, Qwest's tradition was to treat this information confidentially and to protect it from unauthorized uses. Qwest welcomes the opportunity to meet with the Commission and other interested parties and to discuss these issues further at the Commission's convenience.

1. The following questions relate to the adoption of an Opt-In policy for use of CPNI as opposed to an Opt-Out policy:

a. Does your company currently share CPNI with other affiliated entities?

Yes, as permitted under federal law. Qwest may share CPNI with affiliated entities[1] as permitted by 47 U.S.C. § 222(d), which allows carriers to use CPNI without additional customer approval for the initiation, rendering, billing and collection for service; the protection of property; or the provision of inbound telemarketing, referral, or administrative services with customer approval for the duration of the call. CPNI may also be used without additional customer approval when required by law. *Id.* at § 222(c)(1). Moreover, under the Federal Communications Commission (FCC) CPNI rules, CPNI may be shared among affiliates under a "total service" approach. 47 C.F.R. §§ 64.2001, *et seq*. Under this approach, a carrier offering telecommunications services may use CPNI associated with its provision of services to offer its customers telecommunications services in the same category, and to offer related products and services such as customer premises equipment (CPE) and information services. 47 C.F.R. § 64.2005. Carriers may also use CPNI to provide "services necessary to, or used in, the provision of . . . telecommunications service, including the publication of directories." *See* 47 U.S.C. § 222(c)(1)(B). Additionally, if a customer purchases services from more than one of Qwest's business units or companies, those businesses may share between or among themselves the CPNI generated from that customer's purchases to offer additional services in either service category. In such instances, customer approval is inferred based on the customer's purchasing behavior from each service category.

[1] 47 C.F.R. § 64.2003(a) defines an "affiliate" as "an entity that directly or indirectly owns or controls, is owned or controlled by, or is under common ownership or control with, another entity." Some examples of Qwest affiliates that meet this definition are Dex, Qwest Wireless, etc.

Does your company use an opt-in or opt-out policy for CPNI sharing?

Qwest has used both. With respect to uses of CPNI, beyond those described above in 1.a., Qwest used both opt-in and opt-out notifications for CPNI use under prior federal Open Network Architecture ("ONA") rules (*see* discussion below in response to Question 1(b)) and at least one time since the passage of the Telecommunications Act of 1996 ("Act" or "1996 Act"). More recently, Qwest adopted an opt-out process, which Qwest has suspended pending a ruling by the FCC in its CPNI docket.

When did you implement this policy?

Qwest used an opt-out policy for businesses with less than 20 lines under the FCC's previous (no longer existing) ONA CPNI rules. This practice was in effect from the time the ONA CPNI rules were adopted through the promulgation of new rules by the FCC in 1997 under 47 U.S.C. § 222. Since the passage of § 222 and the FCC's new CPNI rules, Qwest used an opt-in notification once (from around August of 1998 to April 1999) and an opt-out notification once (December, 2001).

Please provide a copy of the notice that your company sent to its Arizona customers.

Attached is a copy of the Qwest's (then U S WEST) opt-in notice, which was included on the back of customer bills from August 1998 to April 1999. (Attachment 1) Also attached is a copy of the December, 2001 opt-out bill insert. (Attachment 2)

If you have used an opt-out policy, please provide any data you may have regarding the percentage of customers which opted out and identify the costs associated with administering an opt-out policy.

Qwest data is provided in Confidential **Attachment 3.** Associated costs identified with CPNI in Arizona are greater than approximately $800,000, and consist primarily of costs associated with service representatives' processing labor and time, bill inserts, voice response development, and system changes.

b. Prior to the Tenth Circuit Decision which vacated portions of the FCC rules, did your company share CPNI with other affiliated entities?

Yes, CPNI was shared as permitted under the FCC's ONA CPNI rules prior to its adoption of new CPNI rules under § 222. Those ONA rules allowed the use of CPNI across Qwest's business operations to sell enhanced services and CPE. After the enactment of §222 and the FCC's post-§222 rules (which the FCC held displaced its prior ONA CPNI rules), Qwest shared CPNI with affiliates as described above in response to Question 1.a.

Prior to the enactment of § 222, Qwest (then U S West) as a Bell Operating Company ("BOC"), was bound by the FCC's previous ONA CPNI rules. Those rules required that: (1) affirmative

customer approval ("opt-in") be secured before using the CPNI of large businesses (defined as customers with 20 lines or above) in the sale of enhanced services or CPE; and (2) an opt-out approval mechanism be used with respect to business customers with less than 20 lines for CPNI use in the same context. The FCC's rules allowed CPNI of residential customers to be used without any expression of approval beyond that assumed from the carrier-customer relationship. The FCC found that most mass-market customers would not be concerned by the use of CPNI by carriers in the context of communicating with customers about enhanced services or CPE. The FCC's rules at the time contained separate requirements with respect to sharing CPNI with cellular affiliate. Such sharing was restricted and conditioned on non-discrimination obligations (*i.e.*, if sharing occurred with the affiliate, CPNI sharing had to be available to other requesting entities). *See* 47 C.F.R. § 22.903(f).

Did your company use an opt-in policy as required by the FCC rules?

Yes. Under the no-longer effective ONA CPNI rules, Qwest used an opt-in policy for customers with more than 20 lines. After the passage of § 222 and the FCC's rules, Qwest also used an opt-in CPNI approval process briefly during the 1998-99 timeframe. Based on a prior CPNI affirmative approval trial (addressed in Attachment 4). Qwest neither anticipated nor received a high volume of responses. (At Attachment 5, Qwest also provides a set of slides associated with a follow-up conversation with the FCC regarding the significance of the reported numbers of individuals consenting to the use of their CPNI and those opposing such use.)

Please provide any data you may have regarding the percentage of customers opting in and the costs associated with administering an opt-in policy.

Qwest's experiences with "opt in" are limited to its ONA CPNI experience, its trial, and its limited 1998-99 attempts to secure affirmative approvals. Information about the ONA opt-in approvals and the opt-in approval solicitation during 1998-99 is confidential information at Attachment 6. As demonstrated by Attachments 4 and 5, costs associated with attempts to secure affirmative approvals are beyond any rational cost/benefit analyses and would be impossible for a business to recoup. Each attempt simply continues to escalate the "cost per consent obtained." As an absolute matter, it is impossible – regardless of the actual cost – to spend enough to secure affirmative approvals from a large base of customers. *See Paul H. Rubin and Thomas M. Lenard*, Privacy and the Commercial Use of Information, Boston: The Progress & Freedom Foundation and Kluwer Academic Press, 2002, at 72 (referencing testimony submitted to the Federal Trade Commission by a witness to the effect that when a default approval mechanism was opt-in, 85 percent of consumers chose not to provide personally-identifiable information. In contrast, 95 percent chose to allow use of such information when the default was opt-out. The authors conclude that requiring opt-in would dramatically reduce the amount of information available to the commercial sector and would impose substantial costs on consumers).

Qwest hereby submits for inclusion in the record a recent report entitled "The Hidden Costs of Privacy: The Potential Economic Impact of 'Opt-In' Data Privacy Laws in California," by Peter A. Johnson and Robin Varghese, January 2002 as Attachment 7. Although this report was confined to only certain businesses and a single state, it is indicative of the kinds of cost burdens (particularly those associated with search costs and service inefficiencies) that would be realized by businesses in other contexts should an opt-in requirement for use of customer information be imposed.

See also Fred H. Cate, *Principles of Internet Privacy*, 32 Conn. L. Rev. 877, 883 (2000) ("information on the characteristics of consumers . . . has enabled producers and marketers to fine tune production schedules to the ever greater demands of our consuming public for diversity and individuality of products and services [and is] essential to the functioning of an advanced information based economy such as ours," quoting from Federal Reserve Board Chairman Alan Greenspan).

c. Please identify any competitive concerns associated with the use of an opt-out versus an opt-in policy. If there are competitive concerns associated with an opt-out policy, please identify them with specificity and describe how any adverse competitive impacts would actually occur.

Qwest can identify three competitive concerns. First, as set forth above, restrictions on the free flow of information hinder the ability of carriers to compete through formulating and targeting offers to particular consumers. Indeed,

> The courts have consistently recognized that capitalizing on informational efficiencies such as those permitted by . . . vertical integration . . . is not the sort of conduct that harms competition. . . . It is manifestly pro-competitive and beneficial to consumers to allow a multi-product firm . . . maximum freedom in offering its competitive services to all of its customers.[2]

Second, to the extent restrictive regulations are applied to some carriers but not others, the carriers subject to the restrictions will be placed at a competitive disadvantage relative to the carriers who are not subject to the restrictions.[3] Third, because customers may choose their

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[2] Brief of FCC at 49, in *SBC Communications Inc. v. FCC*, 56 F.3d 1484 (D.C. Cir. 1995) (*SBC v. FCC*) (Nos. 94-1637, 94-1639) (*citing Catlin v. Washington Energy Co.*, 791 F.2d 1343 (9th Cir. 1986), which the FCC described as a case involving "a natural gas distribution monopolist [that] used its residential gas customer list to target advertising of its new 'vent damper' products") Attachment 8; *see also, SBC v. FCC*, 56 F.3d at 1495.

[3] AT&T has argued that "public benefits and legitimate efficiencies" result from this use of sharing CPNI among affiliates, including the ability "to offer . . . customers the ability to engage in 'one-stop shopping' for their telecommunications needs." *See* AT&T's and McCaw's Opposition to Petition for Reconsideration, at 2, File No. ENF-93-44, Attachment 9. AT&T/McCaw characterized arguments by carriers (including some BOCs other than Qwest)

carriers based in part on competing carriers' CPNI policies, processes and procedures, competition between carriers may be affected by the choices these customers make with respect to opt-in, or opt-out or other CPNI issues.

d. Is the "implied consent" assumed by an opt-out policy consistent with the language of Section 222 of the Federal Act?

Yes. As the statute itself provides, and as the FCC has held customer approval to use CPNI for certain purposes is either presumed by § 222 (*e.g.*, subsection (c)) or dispensed with altogether (*e.g.*, subsection (d)). An opt-out CPNI approval mechanism actually goes one step further in providing notice of a carrier's anticipated CPNI sharing practices and extending to individuals the ability to reject the proposals. In such circumstance, a failure to act in opposition to the projected uses may be deemed to confer consent, and as confirmed by the Tenth Circuit, is the only constitutional means by which the government may mandate the obtaining of consent. *See U S WEST, Inc. v. FCC,* 182 F. 3d 1224 (10th Cir. 1999) (*"U S WEST")*. The failure to act most likely reflects either a general position of comfort or one of unconcern. It might also represent inertia born out of the fact that the proposal is simply not important to the person reviewing it. *See* Attachment 10 (letter of Kathryn Marie Krause to FCC dated December 2, 1996 concerning the role and scope of implied consent). But in all events, "implied consent" is sufficient customer approval under § 222, as such consent

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who sought to ban such sharing as "naked protectionist pleas to prevent competition for the business of their existing customers." AT&T asserted that arguments seeking to ban its CPNI sharing were "astonishing claims that [carriers] should be immunized from competition that benefits consumers." *Id.* at 6. AT&T continued:

> [C]ourts have uniformly held that it is pro-competitive and beneficial for consumers for multi-product firms to offer each of their competitive products to each of their customers – and restrictions on the ability of integrated firms to do so are anticompetitive.

The FCC agreed with AT&T, as did the D.C. Circuit Court of Appeals. The Court of Appeals characterized the argument opposing CPNI sharing as follows:

> [The argument is] not that the Commission's decision -- here, its refusal to impose the [ban on CPNI sharing] -- will hurt competition or otherwise adversely affect the public interest, but instead that it will hurt [the opponent of the FCC's position] by increasing the sting of competition it will face from the . . . company [using the CPNI]. We agree with the Commission . . . that AT&T/McCaw's ability to market its services directly to the customers of other carriers [using CPNI] . . . should lead to lower prices and improved service offerings.

SBC v. FCC, 56 F.3d 1484, 1494-95.

> inheres where a person's behavior manifests acquiescence or a comparable voluntary diminution of his or her otherwise protected rights. . . [I]mplied consent is not constructive consent [but, rather] "consent in fact" which is inferred "from surrounding circumstances["] . . . [I]mplied consent -- or the absence of it -- may be deduced from "the circumstances prevailing" in a given situation.

Griggs-Ryan v. Smith, 904 F.2d 112, 116-17 (1st Cir. 1990) (citations omitted).

Implied consent through opt-out notifications is utilized in other federal statutory structures where the information being shared or disclosed is more sensitive than CPNI. For example, opt-out communications are utilized under the *Gramm-Leach-Bliley* (*GLB*) law. They are used with respect to sharing of viewing category information under the Video Privacy Act. 18 U.S.C. § 2710(b)(2)(d). And limited customer information about cable subscribers can be made available to others if an opportunity to opt-out is extended. *See* Qwest Opening Brief at FCC, Attachment 11, pointing out the similarity of structure and language between the Cable Privacy Act and § 222(c).

Please identify any harms associated with "implied consent" for release of individually identifiable CPNI collected by telecommunications carriers.

There are no material harms associated with allowing CPNI sharing among affiliated entities under an implied consent approval regime. There is little, if any, **demonstrable** harm associated with disclosure of CPNI to third parties under the circumstances that typically attend its disclosure (*e.g.*, contractor or agency relationships, joint marketing agreements, sales of portions of businesses, appropriate contractual restrictions, etc.)

e. Do you agree with the Tenth Circuit's finding that communications between telecommunications carriers and their affiliates, divisions and employees constitute "commercial speech" for First Amendment purposes?

Yes. *See* Qwest's Reply Brief in the Tenth Circuit case:

> [T]he [FCC's opt-in] CPNI rules have a prohibitive effect on CPNI-related communications within a telecommunications carrier, and within the carrier's corporate family: employees in different divisions, affiliates, and personnel within the same carrier will not be able to engage in related speech about certain customers because prior affirmative consents will, in the vast majority of cases, be difficult or impossible to obtain. For example, Mary Sue in the landline division is prohibited from talking to Linda May in the wireless division about customer John Jones and his possible interest in receiving information.

Attachment 12, Reply Brief at 4. The fact that sharing of CPNI may occur through an electronic communication rather than through an employee's mouth is of no legal consequence. The

communication is protected speech.[4] A ban on such communication, resulting from an individual's failure to affirmatively approve it, obviously impacts such speech. *See also* Solveig Singleton, cited by U S West in its Opening Brief to the Tenth Circuit, Attachment 11. ("The view that information such as the purchaser's name, address, and buying habits should not be recorded and transferred without his consent conflicts with the general rule that facts and ideas, including our names and addresses, remain free for all to collect and exchange. Attempts to restrict the transfer of information thus run headlong into our rights to free speech.")

f. Does a consumer's privacy interest in CPNI rise to a level such that there is a substantial state interest in its protection?

As the Tenth Circuit Court of Appeals stated, "[t]he breadth of the concept of privacy requires [courts] to pay particular attention to attempts by the government to assert privacy as a substantial state interest." *U S WEST,* 182 F. 3d at 1234.

Privacy interests must always be balanced against other interests, including free speech rights, because privacy protection "imposes real costs on society." *Id.* at 1235, n. 7, *citing* to Fred H. Cate, Privacy in the Information Age 19-30 (1997). Among these costs are the "withholding of relevant true information" and the

> interfer[ence] with the collection, organization, and storage of information which can assist businesses in making rapid, informed decisions and efficiently marketing their products or services. In this sense, privacy [protection] may lead to reduced productivity and higher prices for . . . products or services.

Id.

The Tenth Circuit identified a substantial state interest in protecting people from the disclosure of sensitive and potentially embarrassing personal information.

Early in its opinion, the court stated that "Given the sensitive nature of some CPNI, such as when, where, and to whom a customer places calls," Congress afforded CPNI the highest level of privacy protection under § 222." *U S WEST,* 182 F. 3d at 1229, n. 1. The court was comparing § 222(c) with other subsections of § 222, such as the provisions dealing with aggregated

[4] *See also United Reporting Company v. Los Angles Police Dept.*, 146 F.3d 1133 (9th Cir. 1998), *rev'd sub nom Los Angeles Police Dept. v. United Reporting Company*, 528 U.S. 32 (1999). The Ninth Circuit decision reflects questions about whether speech not directly incorporated into commercial solicitations is commercial speech or some higher form of speech. 146 F.3d at 1136-37. However, the Court proceeded to analyze the case under a commercial speech standard. While the Ninth Circuit found that there was a substantial government interest in withholding the names and addresses of arrestees from commercial solicitors, it also held that the challenged statute failed to advance that government interest in a direct and material manner (*id.* at 1139-40). The Supreme Court reversed the Ninth circuit on the grounds that the government, as the entity in possession of the arrestee information, could determine to whom and under what circumstances the information should be disclosed. It did not address the matter of government interference with speech between private entities based on information lawfully in the possession of one of those entities.

information. The Court was commenting on the fact that, in the former case, customer "approval" was necessary before a carrier could use CPNI; whereas with respect to aggregate information, no such "high[ ] level of privacy protection" was provided for in the statute. Nor was such protection required in the case of subscriber list information (SLI), as the Court observed. By describing this legislative framework, the Tenth Circuit was not validating a substantial state interest in protecting people from disclosure of such information, particularly not if the disclosure were pursuant to customer approval. Qwest also respectfully directs the Commission's attention to the following statement of the Tenth Circuit Court:

> In the context of a speech restriction imposed to protect privacy by keeping certain information confidential, the government must show that the dissemination of the information desired to be kept private would inflict specific and significant harm on individuals, such as undue embarrassment or ridicule, intimidation or harassment or misappropriation of sensitive personal information for the purposes of assuming another's identity.

U S WEST, 182 F. 3d at 1235.

Assuming that protecting sensitive information were a substantial government interest, the government regulation will fail nonetheless to sustain scrutiny unless it materially and directly advances that interest. The Tenth Circuit found that an opt-in CPNI approval regime failed this requirement because "[w]hile protecting against disclosure of sensitive and potentially embarrassing personal information may be important in the abstract, [it had] no indication of how it may occur in reality with respect to CPNI." *U S WEST,* 182 F. 3d at 1237.

Please identify any other substantial state interests involved?

In its decision invalidating the FCC's opt-in requirement, the Tenth Circuit rejected the FCC's suggestion at oral argument that there existed a government interest in protecting people from telemarketing that could appropriately be accomplished through restrictive CPNI rules.

Even if protecting persons from "privacy invasions" associated with marketing contacts amounted to a "substantial" state interest, the government has already provided a remedy to alleviate any privacy harm associated with the telemarketing activity. Federal law requires the establishment and maintenance of Do Not Call Lists. *See* 47 U.S.C. § 227 and 47 C.F.R. § 64.1200. Qwest's Arizona tariffs further provide that Qwest make available to its a residential customers a "no solicitation" listing at an approved monthly rate. *See* Qwest's Exchange and Network Services Price Cap Tariff, Section 5.7.1.K. Under this tariff, customers may choose to have a symbol displayed in the white pages directory, which alerts callers that the listed customer does not wish to received telephone calls or mail designed for solicitation purposes. *Id.*

g. Does the Fact that the Arizona constitutional right to privacy has been interpreted more broadly than the Federal Constitution support the adoption of an opt-in policy in Arizona?

No. As a preliminary matter, the Arizona constitutional right to privacy has only "been interpreted more broadly than the Federal Constitution" in the context of search and seizure cases. More fundamentally, Arizona courts have consistently found that this constitutional provision applies only to intrusions by the *government* or where there is state action. The right may not be asserted as against or between private parties. *See Hart v. Seven Resorts, Inc.,* 190 Ariz. 272, 947 P.2d 846 (App. 1997). Finally, state laws, whether in the form of a statute or state constitution are preempted by the FCC's regulations in this area. As the FCC stated in a portion of its CPNI Order (at ¶ 20), that was not challenged on appeal:

> State rules that likely would be vulnerable to preemption would include . . . state regulations that sought to impose more limitations on carriers' [CPNI] use. This is so because . . . state rules that sought to impose more restrictive regulations would seem to conflict with Congress' goal to promote competition through the use or dissemination of CPNI or other customer information . . . [T]he balance would seemingly be upset and such state regulation thus could negate the Commission's lawful authority over interstate communication and stand as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress.

h. Is an opt-out policy sufficient to protect the substantial state interests involved in protecting people from the disclosure of sensitive and potentially embarrassing personal information?

Qwest believes that an opt-out policy is sufficient to address any consumer privacy interests involving customer information. This is particularly true in light of the fact that **additional** judicial and regulatory mechanisms are available to protect individuals from any actual carrier misuse of CPNI.

First, Arizona recognizes various independent causes of action for interference with privacy, as set forth in the Restatement of Torts and Prosser. *See Godbehere v. Phoenix Newspapers, Inc.,* 162 Ariz. 335, 783 P.2d 781 (1989). Under Section 652D of the Restatement Second, a cause of action exists for giving unreasonable publicity to another's private life. This remedy allows private parties to protect their own interests through access to the courts. Second, unlike many businesses, customers believing carriers have engaged in unreasonable practices may utilize easy and extensive complaint and alternative dispute resolution processes through both formal and informal methods at the Commission. *See* A.R.S. §§ 40-241 through -250; and A.A.C. R14-2-510, R14-3-101 through -112.

Finally, not only is an opt-out CPNI approval regime consonant with the First Amendment (as less restrictive than an opt-in model), but it is supported by additional less restrictive

"mechanisms" that also act to promote the protection of individuals' privacy interests. Rather than stopping the flow of information (*i.e.,* CPNI transfers), Do Not Call lists control the downstream marketing communications by curbing such speech to those specific persons who decline to receive it.

i. How would an opt-in policy alleviate concerns identified with the release of individually identifiable CPNI?

Qwest respectfully submits that an opt-in requirement is unnecessary as a policy matter and prohibited by the First Amendment as a legal matter.

Is an opt-in policy sufficiently narrowly tailored to overcome any First Amendment concerns or should the Commission consider a more flexible opt-in policy?

Even with respect to specific types of information (e.g., call detail) or specific speech contexts (e.g., sharing with unaffiliated third parties), the government may not restrict speech more than is necessary to accomplish a legitimate governmental objective. An opt-in policy fails to meet this requirement, because the interest in privacy can be protected through an opt-out policy. (Of course, a business on its own initiative is always free to curtail its own conduct by not sharing certain types of information or not sharing information in certain contexts. Qwest has done precisely that for years, operating in a fashion that protects the confidentiality of information about its customers and refusing to provide CPNI to unaffiliated parties for their own marketing uses.)

j. Does your company disclose CPNI to any non-affiliated companies? Under what circumstances would you release CPNI to a non-affiliated company?

Yes, in limited circumstances and with appropriate protections for the confidentiality of the information. *See* Attachment 13.[5] Qwest has also filed comments with the FCC stating that there are situations in which sharing CPNI with an unaffiliated entity would be appropriate (e.g., a sale of part of Qwest's business; a jointly marketed product or opportunity).

k. Please comment on Arizona Revised Statutes Section 40-202(C)(5) and the importance of it with regard to any rules that the Commission adopts.

The statute authorizes the ACC to adopt rules that would provide that notwithstanding any other law, customer information, account information and related proprietary information are

[5] Attachment 13 is Qwest's response to the Arizona Attorney General (February 7, 2002, page 1). Qwest there advises that it "does not and will not disclose CPNI to telemarketers or other third parties for their own independent use. Qwest does hire marketing firms to sell Qwest products and services when it makes sound business sense to contract the function out . . . Qwest's use of CPNI in these instances (through its agents) comports with applicable law regarding the use of CPNI."

confidential unless specifically waived by the customer in writing." A.R.S. § 40-202. The application and interpretation of the statute are, like any other statutes, subject to the Arizona and Federal Constitutions, and federal laws and rules.

I. Would an opt-in policy result in additional benefits to consumers relative to an opt-out policy? Explain in detail why or why not.

Most consumers are "pragmatists," weighing the benefits to them from the fair use of information with the use itself.[6] For the most part, these consumers are inclined to allow information use, especially within the relationship that gave rise to the information.

Attached to this filing for inclusion in the record is a survey conducted by Dr. Alan Westin, *Public Attitudes Toward Local Telephone Company Use of CPNI*: Report of a National Opinion Survey Conducted November 14-17, 1996, by Opinion Research Corporation, Princeton, N.J. and Prof. Alan F. Westin, Columbia University, sponsored by Pacific Telesis Group. (Attachment 14, Westin Survey.) (Dr. Westin's credentials are outlined as an attachment to the Survey documents as "Privacy Activities of Professor Alan F. Westin, Columbia University." Notable among his achievements is his long-standing tenure in the area of privacy and information policy as witnessed by his award winning book, Privacy and Freedom in 1967.) The survey provides demonstrable evidence that:

- Despite a generalized concern over privacy issues, a large majority of the public believes it is acceptable for businesses, and in particular local telephone companies, to communicate with their own customers to offer them additional services,[7] especially if those not wishing such communications are provided with an opt-out opportunity.[8]

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[6] *See* Letter from Privacy & Legislative Associates (Dr. Alan Westin and Robert Belair) to the FCC, dated January 23, 1997, at 2, note 2 ("Privacy & Legislative Associates Letter"), Attachment 15. The population can be fairly characterized as comprised of "privacy unconcerned" (about 16%), "privacy fundamentalists" (about 24%) and "privacy pragmatists" (approximately 60%). "Privacy pragmatists" generally tend to favor the benefits extended to them by the free flow of information, but are swift to react when they think that information policies or uses are unfair. *See also* "Hidden Costs" at 7 note 1, referencing Michael Turner and Robin Varghese, Understanding the Privacy Debate. New York: ISEC 2001 and stating that "Turner and Varghese suggest there may be a large discrepancy between those who have privacy concerns based on 'fundamental' principles and those who are concerned about privacy for pragmatic reasons. Among the latter, a significant portion of privacy pragmatists may include those who express a desire to control access to personal data but are not willing to invest the time or energy to ensure compliance."

[7] *Westin Survey,* Question 7 (businesses generally), Question 9 (local telephone companies); Analysis at Item 7.

[8] *Id.,* Question 8 (businesses generally), Question 12 (local telephone companies); Analysis at Item 8.

- In particular, a large public majority believes that it is acceptable for local telephone companies to communicate with their customers using CPNI data.[9] "Majorities in favor of local telephone company use of customer information for marketing were registered for all the demographic subgroups that make up the general public: young, middle-aged, and older persons; lowest to highest incomes; black, white, and Hispanic; male and female; lowest to highest education; conservative, moderate, and liberal political philosophy; urban, suburban, and rural community dwellers; and by Northeast, North Central, South, and West regions."[10] The availability of an opt-out procedure brings initial approvals of local telephone company use of CPNI from the two-out-of-three respondent level up to the 80% range of public approval.[11]

- Individuals understand "notice and opt-out" procedures, and many have used them in one context or another.[12]

- Hispanics, African-Americans, women, young adults (18-24 years of age), persons who have used an opt-out previously, and persons who order many additional telephone services, all have an higher-than-average level of interest in receiving information about new services from telecommunications carriers.[13]

Since the universe of "privacy constituents" contains a large segment of consumers with pragmatic approaches to privacy issues and protections it is a burden on consumers to drive privacy and information policy to the demands of those most concerned, ignoring the vast majority of the population who have little concerns when information is used fairly and along expected or anticipated lines. This is true with respect to CPNI use, as well, since it is reasonable to assume that those most concerned with privacy are those most vigilant to protect their own personal privacy.

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[9] *Id.*, Questions 10-11.
[10] *Id.*, Analysis at Item 10, p. 9.
[11] *Id.*, Questions 11-12; Analysis at Items 8-10, pp. 8-10.
[12] *Id.*, Question 5 (familiarity with notice-and-opt-out), Question 6 (actual use of notice-and-opt-out); Analysis at 9-10 ("The CPNI survey found the respondents who have used opt outs in other business settings are willing to change their position from initial disapproval to positive views of customer-records-based communications by local telephone companies when" follow-up questions are asked).
[13] *Id.*, Questions 9-11; Analysis at 9.

m. Is the CPNI data collected by telecommunications companies different from the personal data collected by companies in other industries (e.g., banks)?

As Qwest stated in its Opening Brief to the Tenth Circuit:

> To telecommunications carriers, including local exchange, long distance, and wireless carriers, CPNI is comparable to the information that credit card companies, grocery stores, mail-order catalogs, banks, Internet service providers, and many other firms maintain about their customers' purchasing and usage characteristics, as part of their routine business operations.

Attachment 11 at page 3. Among those types of information, CPNI is less sensitive than much of it. *See* Attachment 15, Privacy & Legislative Associates Letter at 2-8. The letter states:

> CPNI is not as sensitive as other personally identifiable information such as medical record information, financial and credit record information, insurance information, employment performance information and other categories of personal information which provide insight into an individual's performance or condition or provide information regarding sensitive personal relationships.

Id. at 3. It continues:

> In calculating the sensitivity of categories of personal information, it is important and customary to evaluate the relational interest in which the information is created and used, including the extent to which there is an existing relationship between the individual about whom information is collected and the information collector; the degree of trust between the individual about whom information is collected and the information collector; and the extent to which there is an expectation that the information will be kept confidential.

Id. at 6. The letter concludes that the relationship between carrier and customer does not rise to the level of as critical "privacy sensitivity" as does, for example, the relationship between doctor and patient. *Id.* at 18.

If so, do those differences provide support for an opt-in policy as opposed to an opt-out policy? Explain in detail why or why not.

Given that financial data is more sensitive than CPNI and such data can be shared pursuant to an opt-out regime, CPNI sharing and releases should not be burdened by a more onerous approval process. For example, under the *GLB,* a financial institution generally may not disclose non-public personal information to non-affiliated entities about its customers and/or consumers (two different categories of constituents), unless it has provided notice and, as appropriate, extended an opportunity to opt-out. Although financial institutions are required to provide notice in order to share nonpublic personal information with companies with whom they have joint marketing

agreements, they are not required to extend an opt-out option provided that the use of such nonpublic personal information by the joint marketing partner is confined by contract to the joint marketing activity.

n. Would an opt-in policy result in any additional costs to telecommunications providers relative to an opt-out policy? Explain in detail what the source of the additional costs would be, if any.

Yes. An opt-in policy would result in insurmountable (and unwarranted) costs for carriers seeking affirmative CPNI approvals. *See* response to Question 1.b, *supra*. It is clear that due to inertia no amount of expense would be enough to secure affirmative approvals in sufficient numbers to allow a carrier to make practical or effective use of information to formulate and market offers designed to meet customers' individual needs.

Additionally, the information presented in this filing regarding expenses associated with an opt-out regime may be understated because they represent an educated but not in-depth analysis of such costs.

o. What is the difference in customer response likely to be if an opt-in policy is used instead of an opt-out policy? Explain in detail the basis for your answer, citing any studies that support it.

Essentially an opt-in CPNI approval policy means that CPNI approvals will not be secured from a large enough number of customers for a carrier to be able to use CPNI in its commercial marketing efforts. An opt-out approval mechanism does not create that kind of barrier to speech. *See* response to Question 1.a and 1.b *supra*.

p. Would an opt-in policy create any logistical or administrative problems for telecommunications companies relative to an opt-out policy? Explain in detail the basis for your answer.

See response to Question 1 *supra*.

2. The following questions relate to the content and format of the notice telecommunications companies provide to their customers regarding CPNI:

a. Do the issues regarding such notice change substantially if an opt-in policy is used instead of an opt-out policy? Please explain in detail.

Qwest agrees that opt-out notices should be clear and conspicuous The FCC rules include requirements for opt-out notices that are sufficient. 47 C.F.R. § 64.2007(f).

b. Should notice be provided in multiple languages? If so, what languages should the notice be provided in?

It is in the interest of carriers to consider the demographic make-up of a carrier's customer base in determining the languages associated with the communication any CPNI notice. For example, Qwest provided its December 2001 opt-out notice in both English and Spanish.

c. Should rules be adopted to regulate the form that such notice should take, e.g. should the notice be required to be on a separate page, should a specific font size be required, etc.? If so, what should the requirements of such a rule be? Please explain and support your answer in detail.

No. The Commission should not adopt rules concerning the form of the CPNI opt-out notice. Carriers should be free to craft notices as they deem appropriate for their customer base. The federal rule outlining elements that are required for a CPNI notification have sufficient safeguards to protect consumers. *See* response to Question 2.a.

d. Should rules be adopted to regulate the content of such notice? If so what should be required? Please explain and support your answer in detail.

No. The Commission should not adopt rules regarding the content of CPNI opt-out Notices. The government is not free to dictate the contents of a carrier's communications with its customers. Any governmental insinuation regarding the text of the communication must pass constitutional muster as outlined in U S WEST. That standard is stringent. Qwest does not believe the ACC could meet such burden.

e. Should rules be adopted that standardize the title and labeling of such notice? If so what should be required? Please explain and support your answer in detail.

No. *See* response to Question 2.d, above.

f. Is the CPNI data collected by telecommunications companies different from the personal data collected by companies in other industries (e.g., banks)? If so, do those differences provide support for imposing different noticing requirements for telecommunications companies than those faced by companies in other industries? Explain in detail why or why not.

CPNI is less sensitive than much of the information collected by other industries. *See* response to Question 1.m, above. Even information associated with retail purchasing can prove embarrassing if the person associated with the information was engaging in activity that deviated from the "norm."

3. The following questions relate to how often telecommunications companies should be required to provide notice of CPNI issues:

a. For existing customers how often should telecommunications companies send notice of their CPNI policies if an opt-in system is used? If an opt-out system is used? Please explain your answer in detail.

Notices should be sent out only once to a carrier's existing customer base and once to persons who subsequently become new customers. Valuable resources are consumed in sending out periodic notices (not the least of which is paper). So long as a CPNI notice can be secured by an individual upon request after the initial CPNI notice has been sent out, and so long as a customers have easy access to the Company's policies on use of information, customer privacy concerns are adequately addressed.

b. For new customers when should telecommunications companies send notice of their CPNI policies if an opt-in system is used? If an opt-out system is used? Please explain your answer in detail.

CPNI notices would most likely become a part of carrier's welcome packages (providing service and customer care information) to new customers. If, a customer signs up for services on-line, there may be an on-line CPNI notice for such customers.

c. For customers that are terminating service with a given company is any notice of CPNI policies necessary if an opt-in system is used? If an opt-out system is used? If so, explain in detail what is necessary and why it is necessary.

So long as carriers advise their existing customers about how the carrier might use CPNI if or when a customer that terminates service with the carrier (for example, including information in the CPNI notice about using CPNI for winback purposes or including the information in the carrier's database for product design or development activities in the future), no further notice to customers is necessary. *And see* response to Question 4.a., *below*.

4. The following questions relate to the responsibilities telecommunications companies should have for CPNI data of former customers:

a. If a customer terminates service with a given company should the company be obliged to destroy that customers CPNI data? Explain in detail why or why not.

CPNI should be handled according to a carrier's record keeping, archiving and destruction systems that are crafted to handle all kinds of data, including confidential data. No "special" rules should be set up for CPNI. Carriers should be permitted to use CPNI to design and market offers to remaining or prospective customers, including customers who at the time of such use do not subscribe to the carrier's services.

b. If a customer terminates service with a given company should the company be permitted to use that customers CPNI data to market to that customer? That is, should companies be permitted to use CPNI data in win-back efforts? Explain in detail why or why not.

Yes, CPNI can be used in win-back efforts with former customers. Carriers may market services from categories out of which these ex-customers originally purchased before they terminated such service. The FCC's rules expressly permit such use. 47 C.F.R. § 64.2005(b)(1) and the Commission is not authorized to reach a contrary conclusion.

c. If a customer terminates service with a given company should the company be permitted to use that customers CPNI data for any purpose? Explain in detail what should and should not be allowed and why?

A carrier should still be permitted to use CPNI associated with its former customers for aggregating, modeling, prediction, etc. -- all activities associated with database marketing activities. *See* responses to Questions 3.c and 4.a. Additionally, CPNI should also remain available to the carrier for § 222(d) purposes and other purposes by law.

5. The following questions relate to the verification telecommunications companies provide to their customers that have opted - in or opted - out:

a. If an opt-out system is used, should companies be required to provide notice to their customers that they have successfully opted-out? Should companies be required to provide notice to their customers that they have not chosen to opt-out? Explain in detail why or why not.

Carriers should not be required to verify or confirm customer CPNI approval decisions. Although carriers might volunteer to do such confirmations (as Qwest did earlier this year), the government should not impose such verifications, particularly in the absence of any meaningful cost/benefit analysis.

As a preliminary matter, Qwest believes that the costs of verification would not be trivial and would lack any overall "public interest" benefit. The "harm" to an individual if CPNI is "accidentally" or "inappropriately" used is that the person may be approached via a marketing contact. The "cost" associated with verifying/noticing thousands of individuals to prevent this limited, personal "harm" is unwarranted. Conversely, the Commission should only require carriers to verify/confirm customer choices if an individual agrees to bear the cost of the verification or notification.

b. If an opt-in system is used, should companies be required to provide notice to their customers that they have successfully opted-in? Should companies be required to (or allowed to) provide notice to their customers that they have not chosen to opt-in? Explain in detail why or why not.

No. *See* response to Question 5.a, above.

c. For either an opt-in or opt-out system, should rules be adopted to govern the form of verification notices? If so, what should be required? For example, should verification be required to be in writing or telephonic verification acceptable? Explain and justify your answers in detail.

Qwest does not support a verification requirement. *See* response to Question 5.a. Should verification nevertheless be mandated, carriers should be permitted to chose the method. For any particular customer, this may be through e-mail, telephone verification, or written communication. Qwest used all these methods with respect to the verification efforts it voluntarily undertook with respect to actions taken regarding the December 2001 bill insert.

d. For either an opt-in or opt-out system, should rules be adopted to govern the content of verification notices? If so, what should be required? Explain and justify your answers in detail.

No. *See* response to Question 5(c).

6. What obligations should telecommunications companies have regarding CPNI data for customers who have opted-out (or not opted-in)?

CPNI safeguards are already in place. Under the FCC's safeguard rules, 47 C.F.R. § 64.2009, carriers have obligations with respect to training their employees on how CPNI can/cannot be used. This would also require training on what a customer did/did not choose with respect to CPNI. Carriers are also required to have supervisory overview of employees' activities with respect to CPNI, including marketing campaigns, and officers are expected to make certifications regarding CPNI rule compliance. These safeguards are quite sufficient to safeguard CPNI data whether a customer has expressed approval for CPNI use through either an opt-out or an opt-in method.

7. The following questions relate to the sharing of CPNI data with affiliates or non-affiliates:

a. Should there be restrictions placed on the entities that telecommunications companies can share CPNI data with?

No. As a general matter, there should be no restrictions on CPNI access, use, and disclosure beyond those found in § 222, and rules similar to those enacted by the FCC.

For example, should companies be permitted to sell CPNI data to outside entities or should the sharing of CPNI data be limited to affiliates?

Certainly, sharing CPNI with affiliates should be permitted with customer approval, unencumbered by any additional government interference. Even with respect to unaffiliated entities, to the extent the carrier discloses CPNI in situations that are not extraordinary (such as when it provides CPNI to agents or contractors with appropriate contractual provisions on protection of data and restrictions on use) or where carriers can demonstrate their actions fall within a § 222(d) exception, are required by law, or are supported by customer approval, disclosure should not be prohibited.

Does 47 U.S.C. Section 222 permit CPNI sharing with non-affiliates under any circumstances? Provide detailed justification for your answer.

See response to Question 7(a) above. 47 U.S.C. § 222(d) includes certain exceptions that Qwest believes would support limited CPNI disclosure to non-affiliated entities. Such disclosure would also be permitted if required by law or if supported by customer approval. *Id.* at 222(c).

b. If telecommunications companies profit from the sale of CPNI data should there be a requirement that they share those profits with the customers who have opted-in or not opted-out? For example, should such customers receive discounts?

No. In terms of traditional notions of "ownership," CPNI belongs to the carrier, not to the customer.[14] The fact that CPNI pertains to the purchasing characteristics of customers does not give those customers a property interest in the information. Personal data like telephone numbers, addresses, social security numbers, and medical history -- let alone records of purchases and economic transactions -- are almost always owned by someone else: the Post Office, the government, a bank, or a physician or hospital. A surveillance camera outside a bank or department store may capture the image of persons entering or leaving the establishment without their permission. The resulting footage belongs to the bank or the store, not to the customers, even though their images are depicted in it. In the same way,

> [a] data processor exercises property rights in his data because of his investment in collecting and aggregating them with other useful data. It is the often substantial investment that is necessary to make data accessible and useful, as well as the data's content, that the law protects.

Fred H. Cate, Privacy in the Information Age 74 (1997).

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[14] If a third party were to break into a carrier's computers and steal CPNI, it would be the carrier (and not individual subscribers) who would have a cause of action for theft or conversion.

c. Should there be any restrictions on how CPNI data is used by affiliates of telecommunications companies? If so, what are they and how could such requirements be enforced? Justify your answer in detail.

Qwest respectfully refers the ACC to its responses above.

d. Should there be any restrictions on how CPNI data is used by non-affiliates of telecommunications companies? If so, what are they and how could such requirements be enforced? Justify your answer in detail.

Under federal law, carriers are prohibited from making CPNI available to unaffiliated third parties for their own independent use, absent a written request from a customer under § 222(c)(2) or customer approval. No additional government restrictions are necessary regarding how CPNI is used by non-affiliates of carriers for the same reasons as outlined throughout these comments.

8. Besides an all-inclusive opt-out or opt-in policy, is there merit to a partial opt-in policy? That is, is there merit to requiring an opt-in policy for some categories of customers but allowing an opt-out policy for other categories? Explain in detail why.

The market, rather than the government, should decide which approval process should be used for CPNI.

TAB 1

Qwest's Comments Re: CPNI
March 29, 2002

ATTACHMENT 1

Scripting on the bill envelope:

Important news about your telephone account information.

At U S WEST customer privacy has always been a priority and we want to assure you that your telephone account information, such as calling and billing records, the number of lines and features you have and how you use them, is protected. We use this information to provide your service, as well as to introduce new products and services that are tailored to your needs.

Recent changes in government regulations require that we obtain your approval to use your telephone account information within U S WEST for certain purposes. With your approval, we will use this information only within the U S WEST companies, such as our wireless, long distance, telephone equipment, and voice mail divisions. We will not share this information outside of U S WEST without your authorization.

Your approval will remain in effect unless you decide to change it, which may be done at anytime by just calling us. The choice you make will not affect the quality of your service and will have no impact on the products and services to which you currently subscribe.

If you haven't give your approval, please call us at 1-800-CALLUSW (1-800-225-5879).

TAB 3

ATTACHMENT 3

CONFIDENTIAL AND PROPRIETARY
(REDACTED VERSION)

9-119
TAB 4

U S WEST, Inc.
Suite 700
1020 Nineteenth Street, NW
Washington, DC 20036
202 429-3134
FAX 202 296-5157

Elridge A. Stafford
Executive Director-
Federal Regulatory

DOCKET FILE COPY DUPLICATE

EXPARTE OR LATE FILED

KF CC 96-115 CKB

Notified to: Troy Bennage

EX PARTE

USWEST

RECEIVED

SEP 11 1997

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

September 11, 1997

Mr. William F. Caton
Acting Secretary
Federal Communications Commission
1919 M Street, NW, Room 222, SC-1170
Washington, DC 20554

RE: CC Docket No. 96-115; CC Docket No. 96-149;
WT Docket No. 96-162

Dear Mr. Caton:

Today, Kathryn Krause and the undersigned, representing U S WEST, met with Dorothy Attwood, Lisa Choi, Raelynn Tibayan-Remy, Tonya Rutherford and Jeannie Su of the Policy and Program Planning Division, Common Carrier Bureau, to discuss the attached documents. These documents were previously filed with the Commission, respectively, on September 9, 1997 and September 10, 1997.

In accordance with Commission Rule 1.1206(a)(2), an original and one copy of this letter and the attachments are being filed with you for inclusion in the public record for these proceedings.

Acknowledgment and date of receipt of this submission are requested. A copy of this transmittal letter is provided for this purpose.

Please call if you have any questions.

Sincerely,

Elridge Stafford

Attachments

cc: Ms. Dorothy Attwood
Ms. Lisa Choi
Ms. Tonya Rutherford
Ms. Jeannie Su
Ms. Raelynn Tibayan-Remy

SEP 22 1997

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303 672-2859
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KKRAUSE@USWEST.COM

Kathryn Marie Krause
Senior Attorney

KK
LB
CC 96-115
CKS
9-9-97

September 9, 1997

Mr. William F. Caton
Acting Secretary
Federal Communications Commission
Room 222, SC-1170
1919 M Street, N.W.
Washington, DC 20554

RE: Ex Parte -- Customer Approval For Internal Access, Use and Disclosure of Customer Proprietary Network Information ("CPNI"), CC Docket No. 96-115; Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, as amended, CC Docket No. 96-149; and Amendment of the Commission's Rules to Establish Competitive Service Safeguards for Local Exchange Carrier Provision of Commercial Mobile Radio Services, WT Docket No. 96-162.

Dear Mr. Caton:

Pursuant to Commission rule 47 C.F.R. § 1.1206(b)(1) attached are an original and six copies of a written ex parte presentation which was submitted to Ms. Dorothy T. Attwood, Senior Attorney, Common Carrier Bureau, Policy and Program Planning Division on September 9, 1997. Please associate this presentation with the above-referenced proceedings.

Acknowledgment of this submission is requested. A copy of this letter and the ex parte presentation is provided for this purpose. Please date stamp this copy and return it to the messenger who has been instructed to wait for it.

Please call if you have any questions.

Sincerely,

Kathryn Marie Krause
(RJ)

Attachment

SEP 11 1997

U S WEST, Inc.
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Denver, Colorado 80202
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KKRAUSE@USWEST.COM

Kathryn Marie Krause
Senior Attorney

USWEST

Ex Parte

September 9, 1997

Dorothy T. Attwood, Esq., Senior Attorney
Common Carrier Bureau
Policy and Program Planning Division
Federal Communications Commission
1919 M Street, N.W., Room 533
Washington, D.C. 20554

RE: Customer Approval For Internal Access, Use and Disclosure of Customer Proprietary Network Information ("CPNI"), CC Docket No. 96-115; Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, as amended, CC Docket No. 96-149; and Amendment of the Commission's Rules to Establish Competitive Service Safeguards for Local Exchange Carrier Provision of Commercial Mobile Radio Services, WT Docket No. 96-162.

Dear Ms. Attwood:

Reason for *Ex Parte* Filing and Statement of Position

The purpose of this communication is to reiterate U S WEST's objection to the enactment of any rule under Section 222 of the Telecommunications Act of 1996 ("1996 Act" or "Act") that would engraft on that legislative provision an affirmative customer consent requirement as a condition precedent to U S WEST's internal access, use or disclosure of its business information for lawful business purposes. Such a rule would be contrary to the best and most credible current record evidence; would represent an unreasonable interpretation of the existing statutory language and the legislative history associated with Section 222; would represent a departure from past Federal Communications Commission ("FCC" or "Commission") positions with respect to the public and competitive benefits associated with information sharing; would be contrary to commonplace commercial and industry practice and to customer expectations; and would impact U S WEST's business in a manner that violates both its property and free speech

rights. There is simply no sound reason to define the statutory term "approval" beyond the common business context, wherein such "approval" is generally presumed based on existing business-customer relationships.

Below, U S WEST describes an affirmative consent CPNI trial which it conducted at the end of 1996 and the beginning of 1997. The purpose of the trial was to ascertain U S WEST's likelihood of success in securing affirmative customer consent – either written or oral – to access, use or disclose CPNI. As U S WEST has a lawful right to use its business information internally, it wanted to discover just how seriously an affirmative consent rule promulgated by the Commission might disrupt its rights.

The results of U S WEST's trial demonstrate that affirmative consents cannot be secured in any meaningful numbers. Therefore, were an affirmative consent requirement imposed on U S WEST before it could access, use or disclose CPNI internally, U S WEST personnel would essentially be cut off from access and use of U S WEST's own internal business information to run and grow its business. This would constitute not only an unlawful suppression of speech under the First Amendment,[1] but a *per se* appropriation of U S WEST's property, both in the absence of any Congressional grant of authority to the Commission to undertake such extraordinary and constitutionally significant actions.[2]

In various filings with the Commission, U S WEST has made no secret of its proprietary rights to its internal commercial business information, including its internal business records, even where those records reference or relate to individual customers.[3] U S WEST owns its commercial business information which is incorporated in its business records generated in the normal course of business. Those records include individually-identifiable information that relates to its customers. However, its customers do not "own" the information contained in

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[1] Ex Parte letter of Laurence H. Tribe, dated June 2, 1997 at 2-3 ("Tribe Letter"). See Comments of U S WEST, Inc., CC Docket No. 96-115, filed Mar. 17, 1997 at 2.

[2] There are a number of legal problems that attend a taking of U S WEST's property in the context of Section 222. First and foremost is the absence of any specific or clear legislative language that such a taking was contemplated by Congress. Bell Atlantic Telephone Companies v. FCC, 24 F.3d 1441, 1446 (D.C. Cir. 1994). Second, even if authorized as a general matter, there would be a serious question as to the public purpose sought to be achieved if individuals were granted a sort of black-ball authority with respect to proprietary commercial business information that pertained to them. And, even if the "purpose" were found legally permissible, a mechanism to compensate companies for the loss of their property which would result from the fact that affirmative consents from customers cannot be secured in any meaningful numbers would need to be crafted.

[3] Comments of USWC, CC Docket Nos. 90-623 and 92-256, filed Apr. 11, 1994 at 26, 28 n.54; Reply Comments of USWC, CC Docket No. 90-623, filed Apr. 8, 1991 at 73-75; Comments of USWC, CC Docket No. 90-623, filed Mar. 8, 1991 at 64 n.220.

U S WEST's business records any more than a customer of a department store "owns" the information kept in that store's commercial records.[4]

While U S WEST might be able to minimize the impact of losing access to records that relate specifically to individuals by aggregating CPNI,[5] the consequences associated with such aggregation are undesirable. First, the ability to target an individual for a particular offering is compromised significantly. Second, the statute requires mandatory sharing of aggregate CPNI, which U S WEST believes raises serious equal protection problems.[6] Neither the statutory language nor the record evidence suggests that U S WEST should be confined to the use of only aggregate business information in operating its commercial enterprise, particularly when there are negative consequences associated with the use of such information.

The evidence of record, offered primarily through focus group evidence and statistically valid public opinion survey evidence, demonstrates that individual consumers do not object to a business' ownership interest or use of commercial information in the normal course of business. And, there is clearly nothing in Section 222 that suggests that Congress meant to displace this commercial business interest or expropriate the property of telecommunications carriers in the absence of affirmative customer consent granting companies access and use of their business information.[7]

The Commission could lawfully interfere with U S WEST's constitutional rights only upon express Congressional authority and in support of a significant governmental interest in correcting some clear public harm. The existing record fails to demonstrate either. Absent such demonstration, any regulatory mandate that failed to give proper protection to U S WEST's commercial proprietary interests in its business information at an individually identifiable level would be unlawful.

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[4] Indeed, while it is clear that Congress meant to endow customers with certain control over information that relates to them which is in the hands of carriers, a telecommunications carrier does not "receive or obtain" (the language in Section 222) from its customers the information in its business records. Rather, customers ask for services and that information results in the telecommunications carrier generating a record that indicates, through telecommunications codes, the services to be provided (as well as any underlying necessary services). A reasonable interpretation of Section 222 could obviate any challenge to the applicability of the provision to internal business records.

[5] Section 222(c)(3), (f)(2).

[6] U S WEST's Opening Comments, CC Docket No. 96-115, filed June 11, 1996 at 20-21.

[7] Appendix B to this correspondence summarizes U S WEST's statutory interpretation and legislative history analysis associated with Section 222, for the Commission's easy perusal in this context.

The Commission has an obligation to construe Section 222 in a manner that upholds its constitutionality,[8] not that subjects it to constitutional challenge. Particularly in the absence of any Congressional suggestion that, in enacting Section 222, material and significant access barriers to the use of internal commercial information was contemplated, and in light of the general acceptance of individuals to the internal use of commercial information, the Commission must not impose an affirmative customer consent requirement on U S WEST's internal use of its commercial business information.

Internal Business Information Is Key To Strategic Planning And Growth As Well As Speech

Attached to this filing as Attachment A is a copy of an article from a recent issue of Telephony magazine that makes clear the importance to a business of internal business information, including individually identifiable information.[9] To the extent that the importance of such information in product design, planning and development has not been clear from prior submissions, U S WEST offers this article, which describes generally accepted business practice, as an addition to the record.

The commercial business information in U S WEST's possession, like that of other businesses, is "a key strategic tool"[10] that is calculated to foster the growth and development of U S WEST's commercial operations.[11] U S WEST's commercial information has spawned investment in internal information technologies that allow for better internal communication, integration of information (across both business units and product offerings), and decision-making[12] through information technologies associated with data warehousing,[13] data mining,[14]

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[8] See Edward J. Debartolo Corp. v. Florida Gulf Coast Building & Constr. Trades Council, 485 U.S. 568, 575 (1988).

[9] "The Cost of Entry," by Joan Engebretson, Telephony, August 11, 1997, at 18, attached hereto as Appendix A.

[10] Id.

[11] Id. (a Bell Atlantic executive is quoted as crediting data warehousing, in part, for the overall growth and development of the company).

[12] The Telephony article points out that the technology associated with data warehousing "is aimed at improving a company's decision-making capabilities." Id. and Table 1.

[13] Id. at 18, et seq. (describing different types and architectures associated with data warehousing).

[14] The article discusses data mining, where computer technology "uses statistical techniques such as decision trees and neural scoring to locate patterns in . . . data that users might not have thought to look for." Id. at 22. A cited example of data mining involves a Bell Operating Company that determined that high calling rates were occurring between a certain time frame and, from this knowledge, specifically marketed two different services to the customer households from which such calling generated. Later, the article mentions that U S WEST practices data mining and modeling. "The marketing intelligence group began by developing a model to predict transition – the likelihood that a customer will change carriers or increase or decrease spending with the company. The next project

potential text mining,[15] and the use of intelligent agents.[16] The information and the supporting technologies promote not just internal product design and development, but also customer targeting[17] and future communications with individuals – not necessarily with individuals to whom the business information relates specifically and not in a strictly marketing and sales context.[18]

The Telephony article points out that "[t]he advantage for corporate marketing [is] an integrated view of the company. 'The thrust behind integration is to better create multiproduct offers and target to the right segments.'"[19] Overall, the information in the possession of a business, and the technology that allows for manipulation of that information, is "especially valuable for marketing executives because a wealth of information can be obtained about a company's existing or potential customers, including those customers most likely to switch to a different carrier and the best prospects for new services."[20]

In a commercial enterprise such as U S WEST, "marketing executives" range from mid-level managers to the president of the company. All are interested in consumer buying trends and the ability to match certain consumers, or types of consumers, with the right product/service mix. In this context, one can hardly dispute the strategic nature of a company's commercial information, particularly as that information is manipulated by computer and information technology. Indeed, the successful utilization of both the commercial information itself and the supporting technologies drives U S WEST's network investment. In essence, U S WEST's commercial information, as well as the systems that support the use and manipulation of that information, are critical to the company's successful operation, educated decision making and future growth.

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will be to predict the next product a customer is likely to acquire, which will be followed by a campaign management project." Id. at 23.

[15] Id. at 24 (describing text mining as the taking, as input, "customer service records and other sources that are not easily quantified.").

[16] Id. (describing such agents as those that take information and format it so that vital information is automatically delivered to key company decision makers).

[17] Id. at 18 (a Bell Atlantic executive is quoted as crediting the targeting of customers as a growth and development action). See also a cited example of targeting that does not absolutely require the support of information technology such as data warehousing, but that can benefit from such technology, i.e., finding out how many people in a certain ZIP code pay their bills promptly and have Caller ID. Id. at 22.

[18] Id. at 24 (noting that a GTE executive is interested in looking "at groups of customers that behave similarly and link[ing] them to primary market research to better understand *how to communicate* with different behavioral groups.") (emphasis added).

[19] Id. at 20 (quoting, in part, a BellSouth executive).

[20] Id. at 18 (the quotation is referencing data warehousing specifically, but the concept is applicable equally to other information technologies).

Evidence of Record

The record in this proceeding is replete with evidence that runs counter to the imposition of a customer affirmative consent requirement before internal commercial business information can be used to run the business or communicate with individuals. For example, the record contains statistical evidence that, as a general matter, customers of local exchange carriers trust those carriers with respect to the information in their possession[21] and have no objection to the internal use of business record information (uses which might range from strategic decision making to product design and development).[22] The evidence also demonstrates that any marginal concerns about the use of such information can be overcome easily by notification of intended uses with opportunities afforded to opt out of particular uses.[23] That same record evidence demonstrates that a substantial part of the mass market of consumers is interested in receiving information about the products and services that are developed by local telephone companies through the use of internal commercial business information,[24] with some consumer populations being more interested than the average consumer.[25]

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[21] Survey, Question 2. (When making reference to the January, 1997, Pacific Telesis submission, "Public Attitudes Toward Local Telephone Company Use of CPNI, Report of a National Opinion Survey Conducted November 14-17, 1996," U S WEST makes reference to either the "Survey," which is actually Appendix E of the Report and reflects the actual questions asked the individuals polled, or refers to the "Analysis," by which it refers to the material included in Nos. 1-12.) As U S WEST has pointed out, this high trust level has been demonstrated in customer surveys since 1979. Reply Comments of U S WEST, filed Mar. 27, 1997 at 19 and n.76; U S WEST's Opening Comments, CC Docket No. 96-115, filed June 11, 1996 at 17 n.42, referencing 1991 USWC Comments, CC Docket No. 90-623, filed Mar. 8, 1991 at 65-66 (citing to various surveys and reports wherein customers expressed opinions that such companies did not over-collect information and were highly likely to maintain confidentiality).

[22] Survey, Questions 11-12. As U S WEST has advised, internal focus group work supports this Survey finding. U S WEST's Opening Comments, CC Docket No. 96-115, filed June 11, 1996 at 17 n.42, citing 1994 USWC Comments, CC Docket Nos. 90-623 and 92-256, filed Apr. 11, 1994 at 10-12 (advising of focus group research where participants indicated that they were well aware of the importance to a business of individually identifiable information and were quite comfortable with uses that they agreed to either directly or by implied consent).

[23] Survey, Questions 11-12. The Survey also demonstrates that individuals familiar with such opt-out notifications are aware of their content. Survey, Questions 5-6. Based on the fact that such individuals also demonstrate a higher-than-average interest in receiving information about products and services (Analysis at 5, 9), a clear implication arises that – by not opting out – many individuals are intentionally expressing their interest in receiving information from the entity sending out the notice. Reply Comments of U S WEST, CC Docket No. 96-115, filed Mar. 27, 1997 at 17-18.

[24] Survey, Questions 9-10.

[25] The Survey demonstrated that, for example, for the population at large, there is an interest in "receiving informational communications from businesses they patronize" (an approval rating of 88%) with certain customer segments (e.g., individuals from 18-34 years of age, African Americans, Hispanics) demonstrating an even greater interest (92%). Survey Questions 7, 9; Analysis at 5, 9. More specifically, with respect to communications from local telephone companies, 64% generally indicated an interest in communications about products and services,

All told, the existing record establishes that consumers have little to no concern about a company's internal use of its business information, and by a substantial majority do not even object to that information being used in a manner that specifically identifies individuals and operates to craft targeted communications.[26] While customers are concerned about information leaving U S WEST, they are not concerned about U S WEST's internal use of that information.[27]

The record also clearly demonstrates that the Commission has, over the last almost-20 years, been a champion of information sharing[28] and – only recently – clearly articulated the benefits to both competition and the public interest inherent in such sharing.[29] Indeed, the Commission's pro-information positions have been sufficiently persuasive to win judicial endorsement in more than one Circuit.[30]

The record further demonstrates that interference with U S WEST's right to internally access, use and disclose its commercial information to craft service offerings and frame relevant speech around those offerings would constitute a violation of U S WEST's First Amendment rights.[31] Regulatory destruction of the value of U S WEST's proprietary information would also constitute a compensable taking of U S WEST's property.[32]

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with certain customer segments expressing an even higher interest (69 to 79%). (The latter customer segments included those mentioned above with the ages changing to 18-24 and women joining the segmentation.)

[26] U S WEST is aware that certain commentors, such as the Consumer Federation of America ("CFA"), as well as non-consumer representatives, have filed positions supporting affirmative customer consent. The Commission must, however, weigh this evidence against the statistically valid factual evidence in the record that suggests strongly that advocates supporting affirmative customer consents are either uneducated as to the facts or biased in support of a particular end result, regardless of the facts.

[27] Compare Comments of Cincinnati Bell Telephone Company, CC Docket No. 96-115, filed June 11, 1996 at 2-3; USWC Comments, CC Docket No. 90-623, filed Mar. 8, 1991 at 64-68.

[28] The Commission's Computer II, Open Network Architecture and Computer III proceedings all evidence a pro-information-sharing position, with CPNI associated with individuals in the mass market restricted only upon affirmative denial of access and use. And see Commission's Ninth Circuit Brief in People of the State of California, et al. v. FCC, Nos. 92-70083, et al. (9th Cir., filed July 14, 1993) at 72, 96-97. And see note 29, infra.

[29] Commission's Final Brief in SBC v. FCC, Nos. 94-1637 and 94-1639 (D.C. Cir.) at 47, 49-50.

[30] People of State of Cal. v. FCC, 39 F.3d 919, 931 (9th Cir. 1994), cert. denied, 115 S. Ct. 1427 (1995); SBC Communications Inc., et al. v. FCC, 56 F.3d 1484, 1494-95 (1995) (noting that the Commission's decision to allow the sharing of CPNI furthered the public interest because the increased service offerings likely to result from the use of such information would be expected to lower prices and potentially grow the market overall).

[31] Tribe Letter at 5-10. Those who argue that a company such as U S WEST can speak in the absence of any known information about its customers, such as through general advertisements or "blindly" without regard to the specific characteristics of the customers spoken to, miss the point. U S WEST cannot be confined to speaking in such a blind and general way. It cannot be deprived of the ability to speak knowledgeably and with an educated voice to its own customers. For example, U S WEST has information in its possession that would allow for targeted

In light of the totality of record evidence, any regulatory requirement that individual customers must affirmatively consent to U S WEST's internal use of its commercial business records for the ongoing operation of its business and in formulating communications with those individuals or other similarly situated or like individuals simply because certain records reference or relate to individuals would be not only arbitrary and capricious but unconstitutional, as well.

Affirmative Customer Consent Cannot Be Secured Regarding CPNI

It has been stated by numerous entities that affirmative customer consent cannot be secured from mass market customers.[33] U S WEST recently conducted a trial which confirms the obvious correctness of such assertions. Affirmative consent cannot be secured, whether through written or oral means, in any meaningful numbers, with one exception. And, even with respect to the exception, there are variables that render its use problematic within the context of tying use of internal records to affirmative customer consent.

Before discussing the trial itself, it is important to note how the Commission's current Computer II/ONA/Computer III CPNI rules affect U S WEST's business and the use of its commercial information. Because of the limited number of individuals that have requested restriction of record information that pertains to them, there is no significant impact on U S WEST's business from removing the use of those records from U S WEST's business operations. Only .06% of U S WEST's residential customers have requested restrictions; 3.6% of small business customers[34] and 33% of large business customers (which percentage includes customers who are also competitors and would therefore be expected to restrict CPNI) have

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communication with its customers (see note 17, supra). There is no reason why U S WEST's communication with its receptive customers should not be educated by those facts, as well as the trending, information correlations and product intelligence associated with the information. Nor can U S WEST be put in a position where a general/blind communication model creates confusion between itself and its customer or impedes the normal and expected flow of communication within an existing business relationship.

[32] Ruckelshaus v. Monsanto, 104 S. Ct. 2862 (1984); Lucas v. South Carolina Coastal Council, 505 U.S. 1003 (1992).

[33] Compare Comments of GTE Service Corporation, CC Docket No. 96-115, filed June 11, 1996 at 6 n.9, wherein GTE estimated that "no more than 27 percent of residential customers are likely to provide a written response to the company's request, and the response rate of residential customers might be as low as five percent." GTE also states that its expectations for a response from its small business customers "would not exceed five percent." Id. Comments of Sprint Corporation, CC Docket No. 96-115, filed Mar. 17, 1997 at 2-3 (Sprint describes its recent experience requesting written authorization and notes that very few customers responded).

[34] While some small business customers have more than 20 lines, and thus must affirmatively approve U S WEST's CPNI use, most have fewer than 20 lines. The CPNI communication provided to them is in the nature of an opt-out notification. The numbers of restrictions are in line with what one would expect for such a communication.

restricted U S WEST's record information referencing them.[35] Moreover, the restrictions are limited to the use of U S WEST's commercial information with respect to certain types of conduct (i.e., marketing and sales) in conjunction with limited types of services (i.e., enhanced services and customer premises equipment ("CPE")), that – while complementary to U S WEST's business – do not represent the core business.

An affirmative consent requirement as an implementation of the language in Section 222 would substantially and materially increase the number of records that are "closed" to U S WEST. Essentially, for all practical purposes, such a consent process would deprive U S WEST of access and use of its property in the conduct of its core commercial operations.

The Trial

In the last quarter of 1996 and the first quarter of 1997, U S WEST undertook a number of approaches to securing affirmative customer consent regarding CPNI. With the exception of inbound calling, U S WEST was unable to secure consent in any meaningful numbers. And, as discussed more fully below, while inbound calling produced fairly high levels of affirmative consents, it is not a model that can be employed across the totality of U S WEST's customer base.

The facts associated with the granting or denying of affirmative consent are known to U S WEST. The reasons for the granting/denying are derived from feedback from internal company service representatives (inbound calls) as well as vendor responses (outbound calls). The reasons were not quantitatively tracked.

Inbound Calling Affirmative Consents

From a total of 54,000 calls in to U S WEST's business offices, U S WEST service representatives were advised they should use their judgment in discussing CPNI and attempting to secure affirmative consents. Thus, permission was not asked on each call, and there undoubtedly were "customer friendly" pre-screenings going on with respect to the calls based on the rapport between the service representative and the caller. Such pre-screening conduct would be expected to result in a higher level of consents than if each caller were polled.

U S WEST secured 72% customer consents with the cost per transaction being $0.56, and the cost per positive response being $0.77.

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[35] With respect to customers who are not also competitors, the existence of "Account Representatives" who can often discern information necessary for marketing and sales activities without access to the specific record further reduces the internal business impact of these restrictions.

While the pre-selection opportunities might have increased the affirmative consents received, the percentage of consents received with respect to inbound calls, as opposed to outbound calls (discussed below), demonstrates the extent to which "engagement" of the caller is critical to securing affirmative consent to the access and use of CPNI. Furthermore, U S WEST receives inbound calls from only about 15% of its customers in any given year; and some of those customers are repeat callers. If U S WEST were relegated to using its internal business information only coextensively with the customer consents it received, an inbound oral consent process would be totally unsatisfactory to obtain the breadth of consents necessary for a successful business operation. Obviously, no business can successfully conduct business, let alone compete, by closing off access to 85% of its commercial business records.[36]

Outbound Calling

Approximately 1,250 customers were involved in the sampling, which included both residential and small business customers chosen at random, as well as customers previously identified as high value.[37] Five hundred seventy-eight (578) residential customers were contacted, with the remainder being small business customers. An average of four point eight (4.8) dialing attempts were made in order to reach a live respondent having authority to grant the necessary customer consent. The cost per contact was $5.89; the cost per positive response was $20.66.

From the overall sampling, on average 29% affirmatively consented to CPNI access and usage, with about an equal portion rejecting same. The most specific information available to U S WEST has to do with the calls to the residential market. Where contact was made, the party called was immediately advised that the call was not a telemarketing call. Despite this disclaimer, U S WEST experienced 221 "hang-ups."[38] Of those individuals remaining on the line to hear the substance of the message, 163 consented to CPNI access and use and 190 refused.

Two hundred seven (207) placed calls to residential subscribers were recorded as "unworkables" (representing no answer, wrong number or a language barrier).[39] **Thus, with**

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[36] This paragraph assumes that U S WEST would secure affirmative consents from all 15% of the inbound calls, leaving 85% of the records unassociated with consent. In fact, based on its trial results, U S WEST knows it would not secure consents on all inbound calls, thus rendering the records unassociated with consent greater than 85%.

[37] A sample size of 1,000 customers represents quite a large sample in terms of margin of error and a fairly standard sample size. For example, the CARAVAN telephone survey done in conjunction with Dr. Westin and the Pacific Telesis Survey used 1,000 adults. With respect to U S WEST's trial, the margin of error was less than 2%, which is similar to that reported by CARAVAN in its survey sampling.

[38] Four additional individuals asked to be put on a "Do-Not-Call" list.

[39] Apparently, in any telecommunications survey or calling campaign, the number of "no contacts" (or "unworkables") is usually very high in relation to the number of contacted individuals, and it is not uncommon for

respect to the residential market, the number of unworkables plus hang-ups represented a larger figure than the number of individuals with whom a full communication actually occurred.

Direct Mail

The direct mail aspect of the trial involved both customers chosen at random and targeted customers. The mailing was done *via* first class mail to 15,200 individuals (half residential customers and half small business customers), separate from any U S WEST billing and specifically requested an affirmative response. Some respondents were asked to mail back a form, while others were asked to call an 800 number. The mailings ranged from those which offered no incentive, to those which offered a $1.00 incentive to respond (prepaid calling card included in the mailing), to those that offered a $5.00 incentive upon receipt of response (prepaid calling card).

Response rates were low, regardless of the specific notification approach and the response media used. Positive responses ranged from 6% to 11% for residential customers to from 5% to 9% for small business customers. The $1.00 incentive did not result in response rates different from the no-incentive mailing. The $5.00 incentive affected segments differently, depressing response among business customers but having negligible effects among residential consumers. Calculated on the basis of per positive response, the cost of the direct mail approach was $29.32 per customer **plus** the incentive involved, if any.[40]

Significantly, from the perspective of a notification and opt-out model versus an affirmative consent model, of those individuals that called the 800 number (3%), only 1% called to provide affirmative consent. The other 2% called to "opt out" of the access and use of CPNI.[41]

Extrapolations of Costs Per Positive Consents

It is clear that securing affirmative consents is costly to a business. Overall, the cost per affirmative response can be expected to fall within a two-digit per response range (i.e., $20.66 for outbound calling to $29.32 for direct mail (plus possible additional costs associated with

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this category to contain numbers larger than those for other categories. The fact that "hang-ups" represented an even larger category than no answers was somewhat surprising to U S WEST and suggests that individuals are increasingly reluctant to be engaged by parties calling their homes, whether the call is to market a product or to transmit a non-marketing message.

[40] With a $1.00 incentive, the cost increased to $30.32; with a $5.00 incentive, the cost increased to $34.32.

[41] This 2% figure is less than the 3.6% figure now realized by small business customers who have actually received a notification, but above the .06% of the residential customers who have received no formal CPNI notification.

incentives). Assuming affirmative responses of 30% (which are quite high[42] and yet would still mean that access to 70% of U S WEST's internal records would be cut off), 50% and 70%,[43] the table below demonstrates the ranges of costs associated with securing affirmative consents from 14 million customers (the 14 million being used as an estimate of the entire customer base as represented by access line counts).

		Affirmative Response Percentages		
Cost Per Affirmative Response	**Type of Contact**	**30%**	**50%**	**70%**
$ 20.66	**Outbound calling**	**$ 86,772,000**	**$ 144,620,000**	**$ 202,468,000**
$ 29.32	**Direct mail - no incentive**	**$ 123,144,000**	**$ 205,240,000**	**$ 287,336,000**
$ 30.32	**Direct mail - $1.00 incentive**	**$ 127,344,000**	**$ 212,240,000**	**$ 297,136,000**
$ 34.32	**Direct mail - $5.00 incentive**	**$ 144,144,000**	**$ 240,240,000**	**$ 336,336,000**

The costs are indisputably very significant. In light of the fact that U S WEST's affirmative consent trial failed to produce <u>any</u> affirmative consent rate above 29%, the costs identified above are estimates. These estimates reflect <u>lower</u> costs than would be expected to be incurred; to reach an affirmative response level in the 30 to 70% range would require the incurrence of greater costs than are reflected in the cost per affirmative response reflected above. This is because there would be a need for repeated calls to households and repeated mailings. And, even after having expended such costs, under an affirmative consent model, U S WEST would still be deprived access to between 30 and 70% of its internal corporate records. Were such costs imposed by a regulatory authority, it seems clear that any rational business would become more particular about the customers from whom it seeks consent and how that information is used.[44]

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[42] It bears repeating that U S WEST achieved greater than a 30% consent rate <u>only</u> with respect to inbound calling, the figures of which are not represented on the chart because of the inherent lack of suitability for such a model to secure consents across the customer base. Of the other consent approaches, U S WEST came <u>close</u> to securing 30% consents only with respect to outbound calling.

[43] These figures are provided only to indicate the magnitude of the potential costs involved. U S WEST does not believe it could secure such consent levels through any consent model short of inbound calling.

[44] <u>Compare</u> <u>Denver Area Educational Telecommunications Consortium, Inc., et al., v FCC</u>, 116 S. Ct. 2374, 2391 (1996) (rejecting an "opt-in" approach to information access in part due to the added costs and burdens that such requirements would impose on a cable system operator). It seems fairly basic that a company would direct its

U S WEST's Affirmative Customer Consent Trials Support Existing Record Evidence That Such Consents Would Be Impossible To Secure; That The Vast Majority of Consumers Lack Serious Interest Or Concern About Internal CPNI Use; And That Those That Affirmatively Object To Such Use Do So Primarily To Avoid Future Marketing Contacts

General Observations

If one begins with the direct mail response and moves through the outbound calling to the inbound calling trials, a number of conclusions can be drawn. The direct mail trial confirms that only a very few customers will take affirmative action to respond to such a mailing, even when an incentive is involved. The lack of customer response also suggests that the substance of the communication is not something that is of burning criticality to a majority of the readers. That is, U S WEST customers are not particularly concerned about the issue of CPNI access and use in the abstract.

When the issue of CPNI is raised "in the face" of the customer, responses are very much affected by the manner in which the communication is initiated, i.e., a positive response when the customer initiates the action that results in the communication and the communication is relevant and timely to the consumer; no response or an unfavorable response when the customer's solitude is intruded upon. And, even these latter unfavorable responses were tremendously influenced by the individual's desire "not to be marketed to." Few individuals expressed any opinion on the internal use of CPNI for normal business purposes (such as product planning, design or development), and those that did expressed a concern that such product work might come back to them in the form of a marketing contact if they did not deny consent to access or use their CPNI. In essence, those customers that refused to allow U S WEST to access or use the CPNI relating to them utilized a hammer to kill a flea because that was the context in which they were being asked to respond.

Oral Communications

With respect to the oral communications, it is clear that individuals provided affirmative consent with respect to inbound calling to a substantially greater degree than in an outbound calling environment. However, given the fact that there was a certain "pre-screening" that was done by the service representatives on the inbound calling, it is reasonable to assume that – without such pre-screening – refusals to grant affirmative consent would have been higher.

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efforts to expending costs where access to the record would provide the greatest return. This conduct might well result in certain individuals being offered fewer choices and fewer communications.

The oral consent aspect of the trial demonstrates a number of other things, as well, all consistent with the existing record.

First, individual engagement is critical to a communication about CPNI, especially when there are potential legal consequences associated with the communication (i.e., a refusal of consent renders the information out of bounds with respect to access, use and disclosure).[45] As U S WEST has advised, residential telecommunications customers do not have telecommunications purchases uppermost in their minds.[46] Combining this information with the knowledge that privacy repeatedly shows up on public opinion surveys as a second-tier issue, strongly suggests that attempts to discuss "privacy issues" in a vacuum or where the individual is not currently engaged results in many customers responding reactively and negatively because they fail to see the benefits associated with information use and know only that they do not want the information used to contact them.

Second, the CPNI affirmative consent communication being conveyed does not lend itself to easy oral articulation or explanation between a company employee and a customer. The message can be confusing and cannot really do justice to the benefits associated with the use of the information in the amount of time that is reasonable to expect an individual to remain on the line. Furthermore, the communication might suggest that there is something inappropriate about the use of the information.[47] And, in any given communication where an individual is given *carte blanche* authority to restrict a business' access and use of its commercial information without regard to the consequences to the business, an individual's desire to "control information" about them – fueled by the ongoing press coverage over the loss of control of personal information – could well cause the individual to assert such control.

Third, to the extent that a business must secure affirmative consent before it is entitled to access, use or disclose its business information internally, the fact that "no answers" and "hang-ups" occur is a critical variable to the success of any consent campaign. While a public polling survey is not negatively affected when called individuals either do not answer or hang-up (because they can simply increase the pool called to get to the necessary statistically valid

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[45] U S WEST has previously advised the Commission of the problem of "notices" in the absence of customer engagement. Comments of USWC, CC Docket No. 90-623, filed Mar. 8, 1991 at 95-96. As is obvious from the CPNI affirmative consent trial results, the significance of "engagement" is clear from the customer consent levels U S WEST received when customers initiated calls to U S WEST as opposed to those consents secured from an outbound telemarketing campaign. An individual's lack of engagement is something manageable where the *status quo* is permitted to continue unless and until they are engaged. It is quite another thing when the individual's lack of engagement results in a change in the *status quo*, or – in this instance – the restriction of use of U S WEST's internal commercial records.

[46] U S WEST Opening Comments, CC Docket No. 96-115, filed June 11, 1996 at 2 and n.3 (referencing USWC's 1991 Comments, CC Docket No. 90-623 at 82 and Appendix B at 6-7).

[47] See, e.g., Comments of Pacific Telesis Group, CC Docket No. 96-115, filed June 11, 1996 at 9.

numbers), a requirement that affirmative consent must be gotten before a specific type of information can be accessed or used renders the large class of "no answers/hang-ups" a barrier to use of internal commercial information.[48]

Fourth, it is clear that a substantial number of individuals are interested in decreasing the amount of marketing information they receive from commercial enterprises. It is clear that U S WEST's communication with its customers on a matter of legal significance was "tainted" by what is clearly a more general "telemarketing aversion." U S WEST has described this aversion to the Commission in filings in this proceeding.[49] It is also consistent with Commission observations about the "nuisance" nature of such calls from the perspective of certain individuals.[50] The significance of this aversion to the trial experience, however, is that individuals restrict (or refuse to consent to) the use of CPNI not because they are concerned about routine business or commercial uses of CPNI or even of the use of such information for communications with willing recipients of information, but because they, themselves, do not want to be marketed to in the future.[51] The irony of the customer response associated with the telemarketing aversion is that the greater the sharing and use of internal information, the better able a business is to match a customer with a potentially desired product (i.e., targeting), reducing the levels of shot-gun calling and telemarketing that occurs.

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[48] Even if one were to argue that this category of callers was likely to have split about 50-50 on the issue of affirmative consent in an outbound calling environment, there would still be the other problems associated with this method of securing consent.

[49] As U S WEST has advised the Commission on prior occasions, the CPNI notice that U S WEST sends out to its business customers routinely resulted in large numbers of requests for CPNI restrictions from our small business customers. When further inquiry was made of them, it appeared that these customers believed that their restriction of CPNI would result in their being taken off marketing lists – a consequence that was never communicated to them as being a possibility and one that was, in fact, incorrect. As a result of this phenomenon, U S WEST changed its CPNI notice to include a disclaimer that CPNI restrictions would not result in the entity requesting the restriction being put on "do not market" lists. To accommodate this latter set of customer interests, U S WEST provided a separate number for individuals to call. Similarly, when U S WEST sent out the Billing Name and Address ("BNA") notices required by the Commission, the overwhelming majority of calls received by U S WEST to restrict BNA were to ensure that the individual was not on marketing lists. Again, when it was explained to the individual that restriction of BNA had nothing to do with marketing lists, individuals changed their initial position (i.e., restriction) in the vast majority of the cases. See U S WEST's Opening Comments, CC Docket No. 96-115, filed June 11, 1996 at 18, n.47; Comments of USWC, CC Docket Nos. 90-623 and 92-256, filed Apr. 11, 1994 at 23-24 n.46.

[50] In the Matter of Policies and Rules Concerning Local Exchange Carrier Validation and Billing Information for Joint Use Calling Cards, Petitions for Reconsideration of US West Communications, Inc., Third Order on Reconsideration, 11 FCC Rcd. 6835, 6849 ¶ 23 (1996).

[51] Indeed, on more than one occasion, the example of what they did not want was to be called by U S WEST similarly to the way they were called by interexchange carriers.

Fifth, the combination of the telemarketing aversion discussed above and a company's need to secure affirmative consent produces a less-than-desirable context for communication and has the potential to adversely affect the goodwill between the company and the customer. While a business might be willing to take the risk that an existing customer might consider a telemarketing call an intrusion,[52] the desire to maintain a solid relationship generally and the existence of internal "Do-Not-Call Lists" allows for a call that the customer wishes had not been made or desires not to have repeated to be accommodated in a commercially professional manner.[53] However, a call that a customer considers to be an intrusion is predictably unlikely to result in the individual affirmatively consenting to the use of CPNI because it is precisely the conduct that those customers "restricting their CPNI" want to avoid.[54] This situation will only be exacerbated to the extent that any individual customer is supported by more than one carrier and receives multiple CPNI affirmative consent calls.

Sixth, securing oral affirmative consents would be labor intensive and expensive. The number of customers is a material factor that must be considered in addressing the matter of affirmative **oral** consents. U S WEST has between 10 and 11 million **residential** billed telephone numbers ("BTN").[55] While about 15% of that base could be expected to call in during the course of the year, an additional oral consent initiative would have to be conducted on an outbound basis to reach the remaining customer base.

When outbound calling contact with a household is made, there is an added burden of making sure that the person being communicated with is the customer of record with the

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[52] Indeed, customers who had previously asked to be put on U S WEST's "Do-Not-Disturb List," established not only as a part of good business practice but to conform to the FCC's TCPA rules (47 C.F.R. § 64.1200(e)(2)(vi)), would certainly be aggravated by a telephone call from the company and might not be willing to engage in enough conversation to establish the substantive (i.e., non-marketing) nature of the proposed communication.

[53] Undoubtedly, this is the reason the Commission previously found that marketing calls by businesses to individuals where there is an existing business relationship raise few privacy concerns; and, whatever concerns there are can be addressed professionally through the maintenance of "Do-Not-Call lists." In the Matter of Rules and Regulations Implementing the Telephone Consumer Protection Act of 1991, Report and Order, 7 FCC Rcd. 8752, 8770 ¶ 34 (1992). Despite the fact that there is clearly a hard core "no telemarketing" constituency in the United States, it has yet to become the constitutional, legislative or regulatory policy in this country that commercial communications do not occur unless invited. It remains the position that commercial communications occur unless asked not to occur.

[54] In this respect the "CPNI consent" call is similar to a company calling an individual to ask that individual whether they want to be on a "Please-Call list" or a "Do-Not-Call list." No commercial transaction is being engaged in. The call is an attempt to categorize individuals prior to the engagement in desired speech. Such an approach seems at odds with First Amendment values which favor the free flow of information absent a request to be relieved of that information flow or communication.

[55] The number of actual customers may vary somewhat from this figure. To the extent that a single customer has multiple BTNs (multiple lines into the home billed to a single responsible party), the number of customers will be less than the number of BTNs. However, to the extent that multiple lines into a home are billed to different responsible parties, there may be about the same number of customers as BTNs.

requisite authority to provide the appropriate consent.[56] Often the customer of record is simply not able to be reached easily or at all. Additionally, to the extent that a household has more than one BTN, the existence of multiple BTNs might result in more than one request for consent being made to the same individual (where the BTNs are not cross-referenced on the Customer Service Records) or there may need to be multiple calls made to the same residence requesting consent from different individuals in the household. This is obviously a fact situation ripe for customer irritation and annoyance – states of being that could well adversely affect the granting of consent in the first instance.

An Affirmative Consent Mandate Would Be Contrary To The Public Interest And Would Materially Impact Those Customers Who Want Quality Products And Communications About Them

Affirmative consent requirements are barriers to commercial conduct and speech. They operate to depress spontaneity and are barriers to "easy to do business with" commercial transactions.

From a constitutional and policy perspective, a **written** consent requirement is an obvious barrier to commerce and communication. Congress has never imposed such a requirement on any company with respect to internal use of commercial information.[57] From a policy perspective, in an age of converging computer technology and information technology, the notion of requiring written documents from millions of individuals in order to do business is anachronistic. Most commercial transactions between business enterprises and individuals do not involve written documentation. And, most particularly, the telecommunications industry has a tradition of engaging in transactions telephonically, totally eschewing "written documentation" commercial practices. A requirement that customer consent be secured in writing would be a giant step backward in a commercial environment that is becoming increasingly paperless and, in that regard, becoming more and more like the traditional telecommunications industry.

Affirmative oral consents are also barriers to commerce and speech, not only with customers currently served by U S WEST business, but with future customers, as well. The CPNI in U S WEST's possession educates the company on future product development and design that might be offered to individuals that want their CPNI used or who are not currently

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[56] Compare In the Matter of Implementation of the Subscriber Carrier Selection Changes Provisions of the Telecommunications Act of 1996, Policies and Rules Concerning Unauthorized Changes of Consumers' Long Distance Carriers, CC Docket No. 94-129, Further Notice of Proposed Rule Making and Memorandum Opinion and Order on Reconsideration, FCC 97-248, rel. July 15, 1997, n.44 (noting that the telephone subscriber is the only authorized entity to effectuate a PIC change).

[57] Other than the FCC's CI III/ONA CPNI rules, no business in the United States is subject to a rule that they secure affirmative customer approval before they can use their own business information.

U S WEST customers. The record evidence in this proceeding demonstrates that substantial numbers of individuals are interested in communicating with existing suppliers.[58] And, CPNI use would be consistent with the Commission's prior acknowledgment that internal CPNI use permits carriers "to engage in . . . joint planning and response to customer needs, that many customers apparently desire" and that – barring artificial regulatory requirements – carriers can "efficiently provide."[59] A carrier's inability to secure an existing customer's affirmative consent to access or use CPNI should not compromise that lawful business initiative with respect to existing and future customers.

By way of example, U S WEST has previously advised the Commission that in 1996 it conducted a statistically valid survey that demonstrated that 70% of the customers surveyed supported certain types of cable/telephony offerings, with the interest rating rising to 83% within certain customer segments.[60] Those customers that indicated interest in such combined offerings might not actually know or appreciate, however, that the way in which such integrated offerings are brought to market is through the use of internal business intelligence (captured in business records) that allows for educated business decisions based on trending of purchase patterns, either by product or geographically. If those same customers were asked whether they consented to the use of individually identifiable information about them to craft such integrated offerings and to communicate with them about it, a substantial number might say "no." Does that fact mean that the remaining customers – still interested in the cable/telephony offering – should be deprived of the best offering based on the best internal business information? It certainly does not.

Conclusion

All told, U S WEST's affirmative consent trial confirms the advocacy of U S WEST and others before the Commission. As a general matter, affirmative consents would be expensive to attempt to secure and not largely forthcoming. The trial also confirms prior Commission conclusions on the "privacy" concerns that individuals have within an existing business relationship (very little, as demonstrated by the response to the direct mail piece); and demonstrates that there is an abiding (and perhaps increasing) number of individuals that do not want to be contacted telephonically, even when there exists an ongoing business relationship. The latter situation, however, should not be one that operates to deprive a business of internal use

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[58] See note 25, supra.

[59] BOC CPE Relief Order, 6 FCC Rcd. 143, 148 n.86 (1987). Furthermore, the Commission has observed that "[t]o the extent that the BOCs use CPNI to identify certain customers whose telecommunications needs are not being met effectively and to market an appropriate package of enhanced and basic services to customers, customers would be benefited." Phase II Recon. Order, 3 FCC Rcd. 1150, 1162-63 ¶ 97 (1988).

[60] U S WEST Opening Comments, CC Docket No. 96-115, filed June 11, 1996 at 6.

of its business information for lawful business activities that will inure to the benefit of those that do want to communicate with the business in question.

While one could take the U S WEST trial and attempt to argue that the results demonstrate that U S WEST customers do not want CPNI being used "across buckets" or for product design, development or future marketing, it would be a mistake to draw such a conclusion. Indeed, the response to the written communication strongly suggests just the contrary. It suggests – consistent with advocacy on the record – that customers will not respond at all, affirmatively or negatively, to a company's communication about CPNI. Given the existing statistical information on customers' general acceptance of CPNI uses and customers' basic trust of their local telecommunications carrier, the clear implication from the lack of response communicated to U S WEST is that customers do not care about such internal use (any more than customers care about the internal use of cable subscriber viewing information, another type of internal business record about which customers receive communications).[61] It would be an arbitrary and capricious action to conclude that customer silence and inaction represents an intentional denial to U S WEST to access or use CPNI within the corporate enterprise.

While U S WEST understands that Congress, through its adoption of Section 222, sought to repose in individuals certain rights associated with information that relates to those customers which is in the possession of carriers, the protection of customers' interests in confidentiality does not require consumers to be polled by businesses with whom they have a relationship with respect to whether or not the business can use the record information internally. Nor should consumer interests suffer the predictable degradation of quality services and marketing efforts that would result overall should affirmative customer consents be required before a business can internally use its commercial information.

We appreciate your kind consideration of the facts and arguments contained in this document.

Sincerely,

Kathryn Marie Krause

Kathryn Marie Krause (RH)

[61] 47 U.S.C. § 551.

APPENDIX A

The cost of entry

Do telcos need a data warehouse to play in today's market?

JOAN ENGEBRETSON, Features Editor

Periodically, when a new technology generates good results for one or two local or long-distance carriers, suddenly, at telcos nationwide, management's question becomes not "Why should we do this?" but "Why aren't we doing this?"

A few years ago, this happened with residential broadband; more recently, data warehousing has become hot. Whatever the technology, there are certain similarities in the implementation process. Trials are quickly launched, and the professional conference industry thrives. After gaining some experience with the new technology, carriers—upon seeing clear benefits—will sometimes assimilate it into their operations. Other times, the carriers are disappointed with the results, dropping a new technology en masse, in much the same way they initially embraced it.

Data warehousing, by and large, is still in the honeymoon period. By integrating information from multiple legacy operational systems and making that information easier to access and analyze, the technology is aimed at improving a company's decision-making capabilities (Table 1). This can be especially valuable for marketing executives because a wealth of information can be obtained about a company's existing or potential customers, including those customers most likely to switch to a different carrier and the best prospects for new services.

How will data warehousing fare in the long term? Although a misguided implementation can jeopardize results, the technology has generated some significant success stories—and in an increasingly competitive environment, carriers are generally viewing it as a key strategic tool.

Warehouse blueprints

Although "everyone's doing it" may serve as a justification for data warehousing today, its early adopters often were seeking to solve very specific strategic problems.

"We didn't set out to build a data warehouse. We set out to build a relationship marketing system," says Chip Grim, director of mass markets sales and marketing systems development for MCI. "We dealt with phone numbers, not individuals. Marketing wanted to get more specific about individual needs."

MCI started the process of building its warehouse in late 1993, says Grim. Using massively parallel processing, the system now has 120 nodes and contains 7.5 terabytes of information, including 2.5 terabytes of raw data. "We do things to protect and mirror our data," he says, explaining the size differential.

Contained in the database are records on households nationwide, not just MCI customers. By obtaining more information about the prospects for its services, the company has improved the efficiency of its customer acquisition methods.

"Our revenue per customer has gone up, and our zero usage sales [customers who sign up for a service they do not use] has gone down," says Grim.

Bell Atlantic was also an early player in data warehousing. Hoping to improve stagnant revenues, the carrier started building its data warehouse in 1993, says Bob Ingalls, vice president of consumer marketing. "We believe the revenue growth we've seen over the last couple of years is somewhat a function of this growth and development," says Ingalls. "We've gotten smarter in targeting our customers. We're also benefiting from customer growth."

Carriers have learned many valuable lessons in building their data warehouses—lessons about system architecture, about the planning process and about the data

continued on page 20

TABLE 1

FACTORS DRIVING DATA WAREHOUSING DEMAND

	All carriers	Large LEC	Small LEC	IXC	Cellular carrier	Cable TV
Creating customer profiles to assess product churn or bypass	2.7	2.8	2.8	2.3	2.7	3.0
Identifying ways to optimize products and services	2.6	2.5	2.8	2.8	2.3	3.0
Boosting speed to market for new services/products	2.5	2.3	2.5	2.5	2.3	3.0
Delivering decision support reports faster to end users	2.5	2.5	2.0	2.5	2.7	3.0
Providing better customer service	2.5	2.8	2.3	2.5	2.7	3.0
Producing direct marketing lead lists for campaigns	2.3	2.5	2.3	1.8	2.0	3.0
Finding network infrastructure investment opportunities	1.8	1.3	1.5	2.3	1.3	2.0
Reducing backlog of decision support	1.8	1.5	1.5	1.5	1.7	2.5
Replacing legacy data warehouse systems custom coding	1.4	1.2	1.3	1.3	1.7	1.5

Rating

3 Critical 2 Important, but not critical 1 Not important, or of minor importance

Source: Technology Research Unlimited

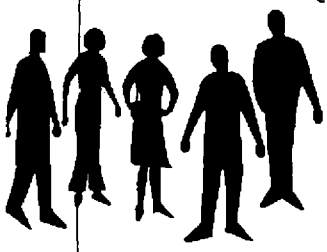
itself (see sidebar on page 23).

Initially, it was common for telcos to have separate data warehouses for different departments, and those warehouses were sometimes capable of providing different answers to the same question, depending on how data was summarized and how often it was updated.

BellSouth is one carrier that initially established several separate initiatives. Robert Bennett, senior director of customer information, says this resulted from a lack of standards among data warehousing vendors. And because few information technology personnel were experienced in data warehousing, they were encouraged to use any vendor's solution with which they were comfortable.

BellSouth and other carriers now are adopting a different approach in which a large central data warehouse feeds several smaller warehouses, known as data marts (Figure 1). Data marts typically support a few hundred users, providing consistent data companywide, while allowing departments to tailor summaries and interfaces.

"Our vision is to build one corporate warehouse at corporate marketing and have data marts feed individual lines of business," says Bennett.



The advantage for corporate marketing will be an integrated view of the company. "The thrust behind integration is to better create multiproduct offers and target to the right segments," says Bennett.

Currently, companies must obtain a release from customers to use customer proprietary network information—such as billing revenue and product usage—from multiple lines of business such as cellular and wireline, says Bennett. The company plans to launch a program to obtain those releases. With such information, and by using the integrated data warehouse design, the company will be in a better position to determine a customer's overall value across multiple lines of business, which will further help in target marketing.

Data marts solved a different problem for U S West. Initially, too many people had the ability to conduct queries against the central data warehouse, which created congestion at peak hours, says Gloria Farler, executive director of market intelligence and decision support. By establishing data marts, the company has significantly improved response time for users.

MCI also relies heavily on data marts fed from a central data warehouse. Often, data marts are implemented for 90 days to support a particular campaign, says Grim. For example, information about affluent customers with personal computers might be loaded into a data mart to support a promotion to sell Internet access.

"If the warehouse goes down, the business can still function," says Grim. "And if one mart goes down, the others are still OK."

MCI is one of several carriers that are using an operational data store. The operational data store, which offers high-performance processing, receives near real-time feeds from the operational systems and may, in turn, feed the data warehouse. Answers to queries generated against the operational data store are more timely than those generated against the data warehouse (Figure 2). Unlike the data warehouse, however, the operational data store does not contain historical information.

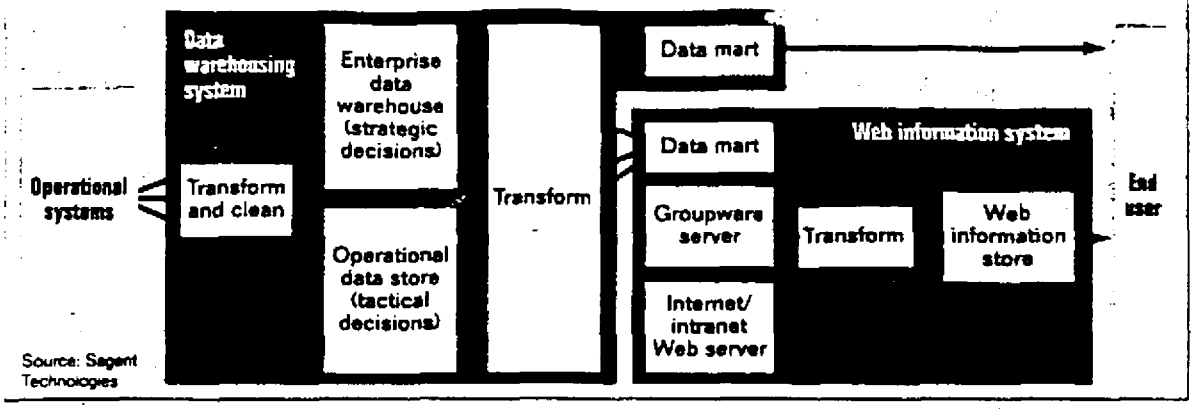
MCI uses its operational data store to provide the most current information to employees who have direct customer contact. Before an MCI telemarketer makes a call to a lead pulled from a campaign management mart, that lead is compared with the operational data store to include any changes that may have occurred since the data left the warehouse.

The danger of any approach that involves a centralized data warehouse for an entire organization is that participants can spend too much time in the planning phase. Complicating matters is the fact that users have difficulty defining their needs until they have some experience using a system.

The ideal methodology for building a data warehouse is different from the waterfall approach typically used

continued on page 22

FIGURE 1
A CORPORATE INFORMATION SYSTEM



Source: Sagent Technologies

by information systems designers, says Mike Blackmon, manager of wholesale services test and design for WorldCom. Blackmon is currently in the process of delivering the first phase of WorldCom's data warehouse.

"It's important to throw as much as you can at users and let them start building requirements on the fly, then work on performance and optimization issues on the second and third iteration," he says.

Close coordination between information systems and marketing personnel is crucial to an effective implementation. Participants will know they have achieved success when the number of users, the complexity of the analysis and the amount of data all increase, says Ben Barnes, general manager of global business intelligence for IBM.

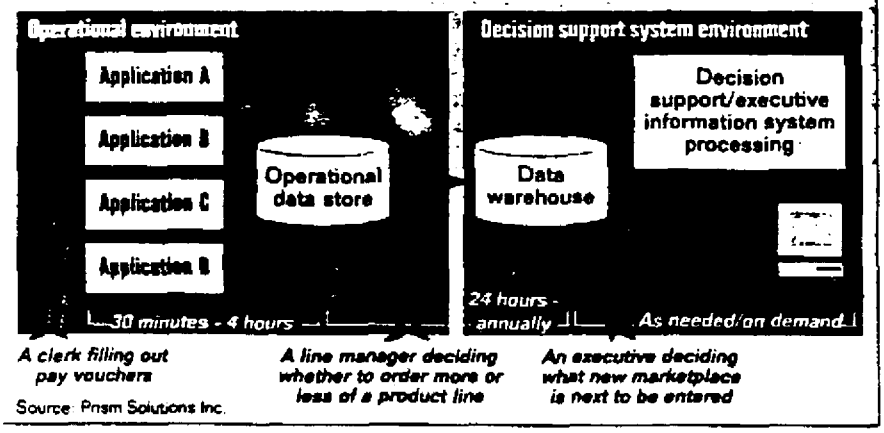
Not surprisingly, some companies have had to expand the size of their data warehouses. Bell Atlantic initially planned for a 125 Gbyte warehouse but now has passed a terabyte, says Bruce Radloff, director of market development systems. "As [internal] customers started using the data, they had more things they wanted to do with it," says Radloff.

Data warehouses lend themselves to unplanned growth, says Barnes.

"Decision support systems are by nature ad hoc," he adds. "There is no finite plan as with a billing system."

Database management systems are available from Oracle, Sybase, Informix and others. Companies offering data marts include Informatica, Sagent and Information Builders. IBM claims to offer a completely integrated solution.

FIGURE 2
DATA WAREHOUSE/OPERATIONAL DATA STORE UPDATES



Source: Prism Solutions Inc.

The miner leagues

Some types of analysis for which a data warehouse is used—such as finding out how many people in a certain ZIP code who pay their bills promptly have caller ID—do not require a warehouse. The alternative, however, typically requires much more work on the part of a company's information technology personnel. This, in turn, reduces the timeliness with which the analysis can be obtained.

Data warehousing enables marketing and other nontechnical staff to conduct their own queries on-line. WorldCom's Blackmon describes this capability, known as on-line analytical processing (OLAP), as "giving users the ability to create their own reports on the fly." OLAP tools are offered by MicroStrategy, Acxiom, Applix, Cognos and others.

The next step in data analysis, which some carriers already have taken, is data mining. Unlike OLAP, which requires users to make decisions about which criteria to analyze and to structure their own queries, data mining uses statistical techniques such as decision trees and neural scoring to locate patterns in the data that users might not have thought to look for.

Barnes cites the example of a Bell regional holding company that discovered, through data mining, that certain customers had very high rates of local calls between 3 and 5:30 p.m. By supplementing this data with household-level demographic information, the carrier realized that many of these homes had teenage children.

Using the demographic data, the carrier divided the group in two. The more affluent households received an offer to purchase a second telephone line, while the less affluent group was targeted with call waiting.

Carriers that use data mining generally keep it in the hands of a small group of specialists who often feed the results to the marketing department as prospect lists, ranked in order of probability of exhibiting a certain behavior, such as purchasing a certain service. Although some data mining tools may be as easy to use as OLAP tools, not everyone can interpret the results.

EDS has been reminded of this in marketing a system it has developed that uses neural clustering to create customer profiles. "The only command issued is 'form yourself,'" says Jed Zaitz, EDS' management consultant. "But to understand what you've got demands a level of knowledge beyond what [many users] have."

U S West is one carrier that has a group of employees focused on mining and modeling.

"We're not only looking at characteristics, but behavior over time," says U S Wests Farler, adding that to build a good predictive model requires at least a year's worth of data. The market intelligence group began by developing a model to predict transition—the likelihood that a customer will change carriers or increase or decrease spending with the company. The next project will be to predict the next product a customer is likely to acquire, which will be followed by a campaign management project.

Some carriers turn to outside consulting firms for customer and prospect profiling and database modeling. Competitive local exchange carrier ICG Communications used consultants to develop a model to predict the number of lines a company would use, says Jay LaPointe, director of marketing services. Components of the model included standard industry classification codes, number of employees and whether a location was a sales branch. ICG has used this information to determine where to focus marketing and sales and where to build out its networks, says LaPointe.

Data mining also lends itself to churn management (see sidebar on page 24).

Data sources

In addition to data from billing and other legacy systems, some carriers—including Bell Atlantic, Ameritech and GTE—have loaded research from customer surveys into their warehouses. Some carriers are also beginning to focus on call detail records and other usage information.

"We've done a lot of thinking about what is a product," says Carter Forringer, GTE's director of marketing information management. A company might use call patterns to generate an idea for a product aimed at someone who makes lots of very short phone calls, says Forringer.

Although many carriers are focusing on marketing applications, particularly programs to increase customer contact, an alternative strategy is to focus on employing usage information to manage the network more efficiently and to become the least-cost producer, says David Holcombe, master consultant for Lander Consulting.

"Usage data allows you to see what products and services are used to what extent in what areas," says Holcombe, who consults with carriers on their warehouses. "If you're considering enhancing a switch, you want the most information possible."

Ameritech is beginning to base its infrastructure decisions on usage data contained in its data warehouse, says James Kinzel, chief architect for marketing decision support for the carrier. Another payoff occurred re-

continued on page 24

The transformers

Before you can "slice and dice"—as marketers like to describe their on-line analytical processing capabilities—you have to "cleanse." Carriers generally agree that the most significant task in building a data warehouse involves the data itself—specifically, moving it from numerous legacy systems into the new system and ensuring that the data is consistent.

Extraction, transformation, cleansing and loading represents about 70% of the effort involved in building a data warehouse, says John Ladley, program director of applications delivery and strategic services for Meta Group.

Typically, system designers create a data transformation layer to convert information from billing, provisioning and other systems into a consistent format and then feed it into the data warehouse. Designers also must create records (known as metadata) of how information fields are generated. Data about multiple cell phones assigned to the same household, for example, might be combined into a single account record. Users need easy access to this explanatory material.

Ensuring that individual customer records have the correct information in each field is another concern. Ann Marlow, business analyst and technology architect for Ameritech Cellular and Paging, says most legacy systems lack free-form data entry fields to capture remarks pertaining to a customer's account. Users who needed to capture facts about a particular situation or customer interaction entered in the data that they recognized was important "just about anywhere it would fit," says Marlow. As a result, a database field like "customer address" may not always contain mailing address data about a customer.

Solving problems like these involves creating thousands of business rules, which reside in the transformation layer. A business rule, for example, might recognize multiple misspellings of Albuquerque, converting them all to a common format.

Ameritech Cellular was able to reduce the complexity of its data cleansing effort by using a customized version of a product from Trillium Software that includes many standard business rules, says Marlow. Data transformation and cleansing software is also available from several other companies, including Prism Technologies, Group One, Apertus and Smart Corp.—JE

cently when usage information enabled the carrier to defend itself against a multimillion-dollar lawsuit from AT&T. The interexchange carrier claimed Ameritech had overcharged for three-way calls. In the past, the local carrier would have had no means of challenging the IXC's claims, but usage data indicated that those claims were inflated.

To support their modeling and on-line analytical capabilities, many carriers also have loaded demographic data—often at the household level—into their warehouses. Users, however, say internal information has much more predictive value.

"We haven't found much relationship to demographic variables," says Farler. "For example, there is no relationship between income and anything."

Christine Wright, vice president of database services for Matrixx Marketing, agrees that demographic information is of little value in segmenting customers, but she says it is useful in developing telemarketing scripts targeting different types of customers.

BellSouth's Bennett says demographic data has been more useful in the business market than for residential applications. Vendor-supplied data might reveal, for example, that purchase decisions for a chain of restaurants are made at corporate headquarters.

GTE has used demographics to corroborate information learned from internal analysis, says Forringer. The carrier built a database of small office/home office users based on information contained in its own systems, then verified the results by comparing them with data from an outside supplier.

What new developments will occur in data warehousing moving forward?

Forringer lists several areas he wants to analyze. One area would look at groups of customers that behave similarly and link them to primary market research to better understand how to communicate with different behavioral groups. Another area would study how segments differ in response to different types of communication and measure the market response to GTE's and competitors' actions. U S West's Farler says she'd like to keep closer tabs on the responses to campaigns, including those who made inquiries but did not purchase a service.

An area that is beginning to get attention is text mining. Like data mining, this would involve looking for patterns in information—but the input would be customer service records and other sources that are not easily quantified. A prerequisite for text mining will be to develop standard terminology for customer service representatives to use in describing their interactions with callers.

W.H. Inmon, author of "Building the Data Warehouse," the book many credit with helping to create the data warehousing boom, says companies that have built data warehouses will turn their attention next to managing those warehouses. Inmon has founded Pine Cone Systems to provide tools that will enable users to apportion data warehousing costs to various departments within an organization.

There also may be an opportunity for intelligent agents that would automatically deliver vital information to key executives without requiring the executives to generate an inquiry, says David Newman, senior manager for KPMG's data warehousing practice.

Clearly, data warehousing is becoming entrenched in carriers' business operations. Bell Atlantic's Ingalls describes the technology as "table stakes" for playing in the new competitive market. "If you look at our competitors now, AT&T, MCI and Sprint have been at this game for some time," he says. "Using data warehousing and data mining is how they've operated. This will be one of the assets we'll have to develop. Data warehousing will be critical to being successful."

Churn control

Several firms are offering wireless carriers data analysis models that they have developed to help prevent churn. Mercury Cellular in Seattle, Charter [illegible] and GTE Wireless Ventures are using a system [illegible] by GTE BSI to help predict which customers are likely to switch wireless service providers, according to Mike O'Brien, GTE BSI's product manager for Churn Manager.

The Churn Manager system collects data from [illegible] customer service and billing systems and activation systems. Results are presented to customer service representatives through a graphical user interface. Which indicates the probability that a particular customer will churn, how valuable that customer is, and the customer's credit class. For customers likely to churn, the system can suggest an action, such as an alternative rate plan, which the carrier can customize.

The system also can be used to create lists of customers to call for specific campaigns. A carrier wishing to convert callers from analog to digital service might target a customer with high revenue and feature usage who carries an old phone.

Cincinnati Bell Information Systems and fellow Cincinnati Bell subsidiary Matrixx Marketing have teamed to offer another churn management system.

A customer likely to churn in three months is different from one who'll churn after one year, says Christine Wright, vice president of database services for Matrixx Marketing. Those in the first group primarily drop out for financial reasons, while the second group is more rate plan-oriented.

Using information from billing systems, the CBIS/Matrixx product segments customers into four groups, including those who are primarily price-driven, hassle-free or service-oriented, says Wright. The final group evaluates all criteria equally.

There are two components of price that drive churn, according to Wright—the number of free minutes and the peak price per minute. Matrixx works with customers to pilot and test offers to address these concerns.

Churn management software is also available from Lightbridge and Coral Systems.—JE

APPENDIX B

Section 222(c), entitled "Confidentiality of Customer Proprietary Network Information," allows carriers to access, use or disclose CPNI with respect to the provision of a telecommunications service from which such information is derived or services necessary or used in the provision of such telecommunications service. No customer approval is required to use information for these purposes. Beyond Section 222(c)(1)(A) and (B) purposes, customer approval (or operation of law) is necessary.

As is obvious from the statutory language, the statute does not specify the type of "approval" necessary to allow for broad CPNI use or the means required to be utilized to obtain such approval. It is clear, under standard rules of statutory construction, that a written consent requirement should not be read into the provisions of Section 222(c)(1), in light of the express mention of a writing in Section 222(c)(2).[1] The absence of such an expression in (c)(1) is a patent indication of Congress' intent not to impose such a requirement with respect to that statutory provision.[2]

As to affirmative consents in general, an expanded view of the legislative history of Section 222 patently demonstrates that such an approach was also rejected. Furthermore, as pointed out by U S WEST in earlier filings, an expanded legislative history of Section 222(c) demonstrates that it was the last in a number of iterations of House Bills initiated by Representative Markey over a period of legislative sessions. The two bills addressing CPNI that immediately preceded the language in H.R. 1555 were H.R. 3432 and H.R. 3626. H.R. 3432 pertained only to LECs and required "affirmative request[s]" to use CPNI broadly. H.R. 3626 changed the scope of the statutory provision to all common carriers and changed the standard for broad use to "approval." Clearly, the deletion of the word "affirmative" in the bill immediately preceding the language chosen for inclusion in H.R. 1555 is significant. It demonstrates a clear Congressional intent that the approval requirements of Section 222(c)(1) have a different aspect than the carrier obligation outlined in Section 222(c)(2) and that an affirmative consent requirement was rejected with respect to CPNI access and use for a statutory standard that allows for a more benign implementation.

It is obvious that Congress mandated nothing "affirmative" by way of customer approval in Section 222. Thus, Congress could certainly not have meant to erect a material and substantial barrier to a business' use of its internal information in a manner that verges on infringing on two fundamental constitutional rights, i.e., property rights and speech rights. A Commission conclusion to the contrary would be unlawful.

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[1] The latter section requires a carrier to provide CPNI to any entity designated by the customer in writing. In this regard, the requirement is a codification of the Commission's existing CPNI rules.

[2] A sound rule of statutory construction holds that an express statutory requirement in one place, contrasted with statutory silence elsewhere, shows an intent to confine the requirement to the specified instance. See Field v. Mans, 116 S. Ct. 437, 442 (1995). See also Gozlon-Peretz v. United States, 498 U.S. 395, 404 (1991); American Civil Liberties Union v. Reno, 929 F. Supp 824, 850 (E.D.PA. 1996).

TAB 5

EX PARTE OR LATE FILED 12/16/97

U S WEST, Inc.
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202 429-3134
FAX 202 296-5157

Elridge A. Stafford
Executive Director-
Federal Regulatory

USWEST

EX PARTE

RECEIVED
DEC 16 1997
FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

December 16, 1997

Ms. Magalie Roman Salas
Secretary
Federal Communications Commission
1919 M Street, NW, Room 222, SC-1170
Washington, DC 20554

RE: Customer Proprietary Network Information, CC Docket No. 96-115

Dear Ms. Salas:

Representatives of U S WEST met today via telephone with Dorothy Attwood, Tonya Rutherford, Daniel Shiman, and Lisa Choi of the Policy and Program Planning Division. U S WEST was represented by Kathryn Krause, B. J. Deering, Ivy Stevens, Debra Adams and the undersigned. The attached material was used as the basis for discussion during this call.

In accordance with Section 1.1206(a)(2) of the Commission's Rules, the original and one copy of this letter, with attachment, are being filed with your office for inclusion in the public record for the above-mentioned proceeding. Acknowledgment of date of receipt of this transmittal is requested. A duplicate of this letter is provided for this purpose.

Please contact me if you have any questions.

Sincerely,

Elridge A. Stafford

Attachment

cc: Ms. Dorothy Attwood
Ms. Lisa Choi
Ms. Tonya Rutherford
Mr. Daniel Shiman

JAN 12 1998

USWEST

Customer Response to CPNI Solicitation-- Trial Findings

CC Docket No. 96-115

U S WEST
B.J. Deering, Market Intelligence and Decision Support
Ivy Stevens, Markets Regulatory Strategy
Kathy Krause, Senior Attorney
Elridge Stafford, Federal Regulatory
Debra Adams, Markets Regulatory

USWEST®

Engagement With The Customer Is The Most Important Underpinning For Affirmative Response

- Affirmative responses were highest when the direct impact on the customer's immediate interest was apparent and the customer was engaged in discussion of telecommunications services, e.g., on inbound calls, when the value of being able to reference the record is obvious.
  - Inbound calling approach produced fairly high levels of affirmative consents (72%).
    - Compare Ameritech trial - 91% affirmative approval (Ameritech Ex Parte, CC Docket 96-115, October 6, 1997).
- Inbound approach reaches only 15% of U S WEST customer base. Achieving the same level of engagement with the other 85% of the customer base is improbable, if not impossible:
  - Company-initiated contact encountered disengagement.
  - When customers were requested to take initiative, they did not.
  - A fairly wide range of incentives did not create interest in the topic.
  - Flat response across options and customer types and segments.
    - Atypical of marketing promotions and indicative of lack of engagement.

USWEST

U S WEST Trial Confirms Other Findings On Privacy And Internal Use Of CPNI

- Internal use of CPNI raises minimal, if any, privacy concerns
  - The public's concern about personal privacy is increasing -- 89% in 1996 -- an 8.5% rise within one year. (Westin survey questions #14, 15)
  - Despite the fact they are concerned about personal privacy, they consider it acceptable for telephone companies to look at and use their records (64%). (Survey question #11)
  - The acceptable rating for the telephone company's use of its customer information increases to around 80% once the customer has an opportunity for opt-out. (Survey question #12)
  - These findings are not surprising, given the high level of trust the public has in the telephone company. (Survey question #2, 2c)

Reference: Public Attitudes Toward Local Telephone Company Use of CPNI, Opinion Research Corporation and Prof. Alan F. Westin, November 14-17, 1996.

Conclusion

- Engagement with the customer is the most important underpinning of affirmative response.
- Disengagement occurs when both the message and medium are out of context and deemed intrusive.
- An opt-out approach for CPNI approval is appropriate, given the public's trust of the telephone company and the public's acceptance for telephone companies to look at and use their records.
- Customers do not have a privacy concern when a carrier's use of its customer records supports the relationship.

TAB6

ATTACHMENT 6

CONFIDENTIAL AND PROPRIETARY
(REDACTED VERSION)

TAB 7

THE HIDDEN COSTS OF PRIVACY:

THE POTENTIAL ECONOMIC IMPACT OF 'OPT-IN' DATA PRIVACY LAWS IN CALIFORNIA

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Embargoed for media release until 10 AM (PT) January 24, 2002

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The report contained herein was funded by The Direct Marketing Association (The DMA), the Information Services Executive Council (ISEC) and the California Chamber of Commerce. The views and findings are solely those of the authors and are not to be construed as representing the views of Columbia University, The DMA, ISEC, or the California Chamber of Commerce.

EXECUTIVE SUMMARY

"Opt-in" restrictions on third-party data sharing would likely cost California consumers, employees, and taxpayers several billion dollars. In addition, such restrictions would cost California charities $1.57 billion in revenue lost to programs.

These costs reflect ONLY the sectors of the California surveyed in this study: financial services, charitable organizations, and non-store retailing. Needless to say, a study of the full spectrum of California's diverse and heavily data-dependent modern economy would likely yield significantly larger figures.

The costs imposed by this most restrictive "opt-in" type of privacy law would take the form of higher interest rates for credit cards and mortgages, lost efficiencies in non-store retailing, lost donations to charitable organizations, and higher premiums for personal insurance policy-holders.

In addition, the California tax base would likely be reduced by $2.1 billion within several years, as mortgage interest payments under a restrictive information regime would be several billion dollars higher than they would be under a less restrictive one. Employment in the construction industry alone would be reduced by thousands of jobs as new home sales were lost.

This study calibrates lost efficiencies for a very limited number of selected sectors of the California economy if financial service companies, direct marketers and charitable organizations were prohibited by new state legislation from using non-sensitive third-party commercial data to conduct their business or charitable work as efficiently as they now do.

Under an "opt-in" data privacy law, such third-party data sharing would not be available to help them efficiently find customers or donors, tailor services and goods to customers' needs, and reduce the cost of goods and services (and especially credit) they offer to consumers.

Using existing sectoral studies of the impact of restrictions on third party data sharing at the national level, we estimated the costs of these restrictions for only a small segment of the total affected California economy. The methodology employed makes a number of conservative cost assumptions. For these reasons, the costs we report may well understate, possibly by a considerable margin, the total hidden costs of an opt-in privacy regime to the state of California.

The major cost areas of an opt-in data privacy regime for the sectors we studied are as follows:

FINANCIAL SERVICES

- **Inefficiencies Incurred by Financial Service Consumers**. Financial services companies rely on personal data to identify the needs of potential customers, target customers and pool offers, as well as other methods of matching customer needs and supplier services. For example, customers save time through pooled offers and pre-filled applications. They also receive lower priced offers. Personal data also reduces consumer exposure to 'noise' from unwanted offers. Further, restrictions on the use of third party data in California would result in higher search expenditures for companies and lost time and savings for customers.

  - California customers of the 90 largest financial services firms alone would incur an annual increase in search costs of approximately $1.02 billion, assuming firms fully pass these on.

  - California households can be expected to aggregately spend an additional 25.4 million hours to acquire the same goods and services from 90 of the largest financial services companies.

- **Shifts from Inability to Fine Tune Risk and Securitize Debt via Personal Information.** Restrictions on the use of personal information of California residents by financial service companies would create upward pressures on interest rates. Mortgages and credit cards would have to assume higher risk levels due to an inability to accurately assess risk. Opt-in data restrictions also create barriers to entry, making it harder for small and medium sized financial service companies to compete with the larger ones. Over time, with a progressive monopolization of the sector and the loss of competitive pressures, prices can be expected to rise even further. While the specific level of increase in interest rates caused by restrictions on personal information cannot be predicted, even modest increases entail substantial costs.

  - *Mortgages*: A possible 1% increase in the baseline of average 1995 mortgage interest rates would have led to approximately 1,850 fewer homes sold as nearly 85,000 renter and homeowner families would find median priced homes in their neighborhoods unaffordable in that year. $332.6 million in home sale revenue would have been lost along with as many as 1,700 jobs in the residential construction sector. New homebuyers for the year would have paid $110 million ($1,760 per household) more in interest payments in 1995.

  - Tax revenues are impacted by higher interest rates. Higher rates would remove $2.1 billion dollars from taxable revenue over 5 years from new home owning households, assuming 1999 mortgage

levels. At a 4% tax rate, this translates into $80 million dollars in lost tax revenue to state coffers for the same time period.

- *Credit Cards*: A 1% increase in the annual interest rate on credit cards of California residents would result in an additional $927 million in interest payments.

- **Compliance Costs**: Financial service companies will face a one-time expenditure on expertise and equipment in order to update their systems to comply with new data restriction requirements. Assuming that 10% of banks and bank-like firms in California operate on-line and will have to update their systems to comply, the sector can be expected to incur costs of more than $154 million for the e-commerce dimension of their businesses alone.

CHARITABLE ORGANIZATIONS

- **Search costs**: As much as $1.57 billion would be lost from charitable program expenditures in the state. Original research conducted in conjunction with this study shows the loss of valuable information from third-parties, especially financial third-party sources, would have a substantial negative impact on charitable fundraising in California. Specifically, the loss of access to third-party information would result in an additional $933 million in expenditures for fundraising and a loss of an estimated $638 million in donations.

DIRECT MARKETING AND E-COMMERCE

- **Search costs**: In so far as the pool of information 'dries up', the direct marketing sector can be expected to spend more on advertising. It is estimated that direct marketers will have to spend, depending on size and segment, $189 million - $594 million in the aggregate in additional advertising to reach the same consumers.

- **Compliance costs**: To the extent that e-tailers extend credit, they will be subject to the same regulations as other financial service firms. Like these financial service companies, they will be obligated to update their systems. For such firms, restrictions on third-party data transfer can be expected to result in compliance costs of $103 million, even if only 1% of the estimated 65,000 on-line retailers are impacted.

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1.0 INTRODUCTION

This study offers what its authors believe to be the most up-to-date and rigorous analysis of the potential costs of a restrictive (opt-in) privacy regime for the California economy. Consulting the Executive Summary and Appendix C at the end of this study most easily identifies these costs.

Our methodology is discussed in detail in the methodological appendix. Briefly, however, our approach has been to adopt the best available cost algorithms and the most conservative behavioral and statistical assumptions from among those used by previously published and frequently cited studies to calculate privacy costs at the national level. We then applied these algorithms and assumptions to the best available California economic data to calculate the costs for those sectors of the California economy covered by this study.

While our study cannot speak to the potential costs in every area of California's economic life, the sectors we have studied represent an important if not comprehensive range of activities. Given the conservative assumptions we make, we further believe our report may significantly understate the actual costs of a fully implemented restrictive privacy regime for the entire California economy. By adopting this conservative approach, we hope that the reader may gain a useful and valid insight into the economic side of the privacy ledger.

To understand the implications of California's pending legislative proposals, a brief word about the nature of privacy regulation is in order. There are essentially three choices legislators can apply at three stages in the information "stream." These regulatory choices are 1) notice only; 2) "opt-out"; and 3) "opt-in" or affirmative consent. The three stages at which these choices may be imposed on firms and consumers are a) data-gathering from consumers; b) data-sharing with affiliates; and c) data-sharing with third parties or unaffiliated firms.

Of the three regulatory choices, "opt-in" or affirmative consent is the most restrictive, as it requires the consumer, from whom the information is originally gathered, to take additional steps to authorize the further use of the data above and beyond his/her primary interaction with the firm. As some studies have suggested, many consumers may not take this step.[1] This may not necessarily be because they oppose the sale of their data; it may be because they wish to maximize the efficiency of their purchasing-time--they simply can't be bothered, in other words.

[1] Michael Turner and Robin Varghese, Understanding the Privacy Debate. New York: ISEC, 2001. Turner and Varghese suggest there may be a large discrepancy between those who have privacy concerns based on "fundamental" principles and those who are concerned about privacy for pragmatic reasons. Among the latter, a significant portion of privacy pragmatists may include those who express a desire to control access to personal data but are not willing to invest the time or energy to ensure compliance.

It is a prevalent and powerful misperception that the privacy debate pertains only or even primarily "on-line," that is, to e-commerce. To make this assumption is to mistake the changed nature of the modern economy and the now pervasive nature of information flows.

Perhaps the greatest contribution of California's technological prowess and commercial savvy over the last decade has been to enable the application of digital technology to the full range of economic activity around the world. Not only has digital technology created the new field of on-line "e-commerce," but it has also allowed information to be applied systematically "off-line" as well. In short, digital technology enables information to be gathered, stored, and shared in new ways, vastly increased quantities, and analyzed with ever-greater sophistication. The current economic revolution has been not simply a product of information technology but a product of new, innovative and efficient uses of information.

But while this explosion of information gathering and its application has facilitated economic efficiency and human connectedness, citizens, consumers, firms and legislators have also become aware of potential drawbacks to the digital revolution, and nowhere more so than in California. As with the technology itself, California may be leading the way in shaping governmental regulation of this issue.

Privacy has emerged as an issue for policy debate in California for two reasons. First, there is a worry that the aggregation of individually identifiable data will violate the privacy of individuals by revealing life styles and actions that individuals wish to keep private. Second, there is a fear of fraud or identity theft that brings a risk of economic loss to the individual or the threat of personal harm.

At the most general level, the private-sector collection of data occurs as individuals engage in the routine business of purchasing clothing, filling in credit-card applications, or making their annual gift to their favorite charity. Now the records of these myriad transactions accumulate with greater efficiency due to advances in digital technology. This digital technology has created new opportunities to better serve customers through sharing of this data by affiliates and the exchange of this data with third parties.

It is primarily this latter, third party phenomenon, though often poorly understood, that has fostered a perception of risk (such as identity theft or other forms of fraud,) or harm (such as "on-line stalking" or "surveillance", etc.). However, it must be borne in mind that data sharing with recognized affiliates and commercial third parties is a very different issue from questions of fraud, "stalking", and other already illegal activities which all interested parties strongly oppose, but which often confuses the terms of public debate. For example, the already illegal activity of stalking typically involves individuals already known personally to the victim, not "third-party" strangers.

Nevertheless, these perceptions have led regulators around the world to begin implementing a range of privacy laws that establish the terms by which consumer information may be collected and shared.[2] In Europe, the European Union passed a Privacy Directive in 1995. In the United States, recent federal legislation has included the Children's On-line Privacy Protection Act (COPPA, effective April, 2000); the Health Insurance Portability and Accountability Act of 1996 (HIPAA), and the Gramm-Leach-Bliley Act (GLB), also commonly referred to as the Financial Services Modernization Act.

Federal legislation thus represents the second, more immediate reason for privacy becoming an issue of legislative concern in California, if not in every state capitol. The Gramm-Leach-Bliley Act, for example, recognizes that many of the financial services it regulates are regulated jointly or primarily at the state level--as with insurance.

Thus, state legislators and regulators must decide what they wish to do about privacy, and how restrictive they wish to be. The Gramm-Leach-Bliley Act, to stick with our example, establishes a floor of "notice" (the least restrictive option) for data sharing with affiliates and "opt-out" (the moderately restrictive option) for data-sharing with unaffiliated third-parties. States such as California are thus enabled to make data protection more restrictive than at the federal level, such as by employing the most restrictive (opt-in) approach for third parties, for example.

Whether states SHOULD do so is an open question. The authors of this study do not argue for any particular view. On the contrary, we believe that this is a decision that should be made by the citizens and elected officials of California in the full light of the best available facts. Among such facts are those we present in this study. We believe legislators owe it to their voters that any proposed privacy restrictions should take into consideration the likely costs and lost efficiency that results from such additional regulation. As will be explained in more detail below, such lost efficiencies and economies can impose hidden but very real and burdensome costs on California consumers, employees, charities and taxpayers.

[2] Turner and Varghese, op. cit.

2.0 THE FINANCIAL SERVICES SECTOR

Changes in access to consumer data by third parties (and affiliates) can be seen as impacting the finance sector in several crucial ways. These include additional costs to the search for and targeting of customers through higher advertising costs; losses from the inability to assess and fine tune risk in the extension of credit (resulting in higher interest rates); more expensive monitoring of data management and protection; greater losses from fraud as a result of a greater inability to detect malfeasance; higher prices resulting from new barriers to entry posed by larger costs of gathering information[3], and less access to credit for consumers.[4] Of these, the following three have been measured to varying extents:

- Restrictions on information sharing raise the **search costs** to companies. The cost of advertising (mail and telephone solicitations) and transacting (call centers needed to process transactions) increase as a result of the loss of pooled resources and capacity to target products to customers who are more likely to demand them. For customers, these translate into higher prices to the extent that costs are passed on. Furthermore, customers also bear non-financial costs in the form of search times and exposure to 'noise' or unwanted solicitations.

- A ban on third party information sharing reduces the ability of financial firms to **assess and fine tune the risk** involved in extending credit to customers, as well as securitizing debt and thereby increasing the pool of credit available. As evidenced in societies with restrictive data transfer regimes, interest rates climb to compensate for an inability to clearly identify risk.

- Finally, restrictions on data sharing bring costs in the form of **compliance** procedures, requiring new monitoring systems, especially for firms that conduct on-line business.

2.1 Search costs

Ernst and Young's study of the estimated savings in terms of money and time from sharing information with affiliate and third parties under the direction of Cynthia Glassman provides a basis for an evaluation of possible costs of

[3] For example, the seven largest banks in France, the Western European country with the most restrictive data transfer regime, account for 96% of all banking assets. Western Europe as a whole has one-tenth the number of US financial service institutions even though it has nearly 50% more households.

[4] According to Walter Kitchenman's "US Credit Reporting: Perceived Benefits Outweigh Privacy Concerns" (The Tower Group, 1999), European consumers have access to one-third less credit as a share of GDP.

restrictions on data transfer.[5] Their survey of members of the Financial Services Roundtable, whose revenues comprise more than 25% of the sector's total earnings, suggests that data sharing with affiliates and third parties yield savings of $195 per customer household and 4 hours per annum. We use their study as a preliminary base for estimating the costs of restrictions on information sharing.

For the 90 members of the FSR alone, a switch to restrictions on transfers to third parties in California translates[6] into $1 billion in lost savings and over 25 million hours per year for consumer households in the state. The size of lost savings to consumers rises to nearly $2 billion and approximately 40 million hours if restrictions were extended to affiliates as well. These do not take into account impacts on the entire financial sector.[7]

The dynamic of freer information flows yielding lower search costs can be seen in various sub-segments of the industry. The automobile, property, and life insurance segments, as with most segments of the insurance industry, heavily rely on third party data for marketing. Another characteristic shared by the various segments of the insurance industry is the role of field agents. Namely, the insurance industry is an agent driven business, in which individual agents in the field are responsible for the bulk of the firm's marketing efforts.

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[5] See Ernst & Young LLP, under the direction of Cynthia Glassman, "Customer Benefits from Current Information Sharing by Financial Services Companies" for a description of the various sources of savings. Conducted for the Financial Services Roundtable. (Ernst & Young, December 2000).

[6] FSR members are representative of the sector as they represent the largest companies in the sector, accounting for approximately 26% of all revenue in the finance, insurance and real estate sector for 2000. Source: FSR, *Annual Report,* 2001, www.fsround.org and Bureau of Economic Analysis, Department of Commerce, www.bea.doc.gov. The members of the FSR are disproportionately commercial banks and insurance companies. The 50 largest firms in the finance and insurance sector accounted for 38.8% of all revenue in 1997; the 50 largest commercial banks account for 60.7% of all commercial banking revenue; the 50 largest insurance firms account for 60.9% of the subsector's revenue; also of note is the fact that the 4 largest credit card issuing companies account for 53.8%. (Bureau of the Census, 2000) Assuming that revenue is proportional to customer base, in terms of accounts receivable, consumer as opposed to business accounts receivable amounted to 28.5% of total receivable accounts, excluding real estate. (www.federalreserve.gov, Federal Reserve, 2001) FSR customer households as a share of total households in California were estimated as the same as for the country as a whole or 9.9 million of the 11.5 million California households.

[7] A straight translation from FSR members to the entire financial sector would of course yield a substantially larger figure. If we assume that the average savings of $195 per customer household extends to all firms in the finance sector, the total costs of restrictions on third party transfers would be approximately $4 billion, requiring approximately $495 million in additional advertising to compensate. The limitations of doing so stems from the fact that the efficiency of data use in all likelihood declines with the size of the financial institution, thus savings may not translate into an average of $195 per customer household. As the size of the enterprise declines, the saving of information sharing is expected to decline if there are economies of scale in information gathering. To the extent that this is the case the ability of smaller financial institutions to share information with larger ones offsets their cost of information gathering disproportionately and reduced barriers to entry.

Marketing: In the past, field agents relied on a variety of data sources for prospect marketing, most of which was either publicly available data (the white pages), public record data (driver's license and motor vehicle data) or self-reported (inbound calls). The days of cold-calling households to pitch pre-packaged product offerings, however, are on the decline. Today, field agents for automobile insurers are reaching out to prospective policyholders through multiple media using sophisticated database marketing techniques.

Prospect marketing and lead generation now occurs through the field agents with the assistance of the home office and outside information service providers, such as Acxiom, Equifax, and Trans Union. In short, the process works as follows:

On a contractual basis, the home office provides an information service provider with data on its policyholders (knows as the firm's house file). The information service provider, in turn, engages in list hygiene (updates contact information) and appends the data in the house file with additional third party data. The appended data is then analyzed in order to identify common attributes among the entire group and subgroups of policyholders: e.g., among new policyholders, policyholders for more than 10 years, premier package policyholders. These leads can also be open-ended, allowing agents to select individuals according to criteria they establish based on personal experience and local knowledge.

Joint Marketing and CRM: One of the benefits policyholders enjoy is the effort made by the policy provider to anticipate and serve their needs. Communicating with customers in order to understand them and identify their needs is a practice commonly referred to as "customer relationship management," or "CRM." Sometimes the insurer may not be able to directly satisfy all the needs of its customers, but may be able to do so through joint marketing arrangements.

For example, a new policyholder receives inserts in his/her monthly statement for a discount on a passive alarm system or a defensive driving course offered locally usually by third parties that would substantially decrease the policyholder's monthly premium payments. A more restrictive data regime that includes affiliate sharing, then, would further impede cross-marketing and deny a policyholder the benefits from economies of scope captured by most insurance companies. In other words, rather than one stop shopping and seamless service, a consumer will be forced to contact service providers separately.

Market Reach: Ordinarily, individuals who are employed or who have substantial personal wealth have access to corporate or private insurance advisors who are able to provide expert counsel and ensure that their insurance needs are fully met. The vast segment of the American population comprised of temporary or seasonal workers (such as migrant labor), or who are living in economically disadvantaged circumstances are disproportionately reliant upon directly marketed insurance policy offers – either through the mail or telephone. The

identification of individuals in this population segment with unmet insurance needs, as well as accurate contact information and data for assessing risk for underwriting purposes are made possible through the use of third party information. An opt-in restriction, then, would not only reduce the percentage of policyholders in this cohort, but would also likely increase the average premium payments necessary to secure coverage.

Michael Staten and Fred Cate's case study of MBNA's provision of credit cards offers a basis for examining the impact of rising search costs for the credit card market.[8] While the use of a single company makes difficult the extension of findings to the entire sector, it should be noted that MBNA services 15% of all outstanding US MasterCard and Visa balances and also that the eight largest credit card issuing firms account for approximately 75% of all revenue in the sector. Staten and Cate found that a blanket opt-in requirement would raise the direct mailing costs of booking a new account by 22%.[9] This cost increase is equivalent to an 8% decline in revenue. Assuming a similar cost structure for the 8 largest credit card providers, which account for approximately 75% of the sectors revenues, the loss in revenue of a California opt-in would amount to approximately $27 million per year.

2.2 Risk Assessment: Insurance, Home Mortgages and Credit Cards

An additional source of costs to consumers and the economy has resulted at various times and places from the fact that credit information is less mobile, making risk assessment less accurate. Consumers generally have a harder time acquiring credit for any given interest rate in societies in which data does not move easily. The ability to use demographic information, credit bureau data and existing data about customers from third parties and affiliates has enabled companies to identify and target low-risk consumers. This practice has contributed to the fall in consumer interest rates, as two studies found for the mortgage market and for credit cards.[10] In some ways, it is in the effect on

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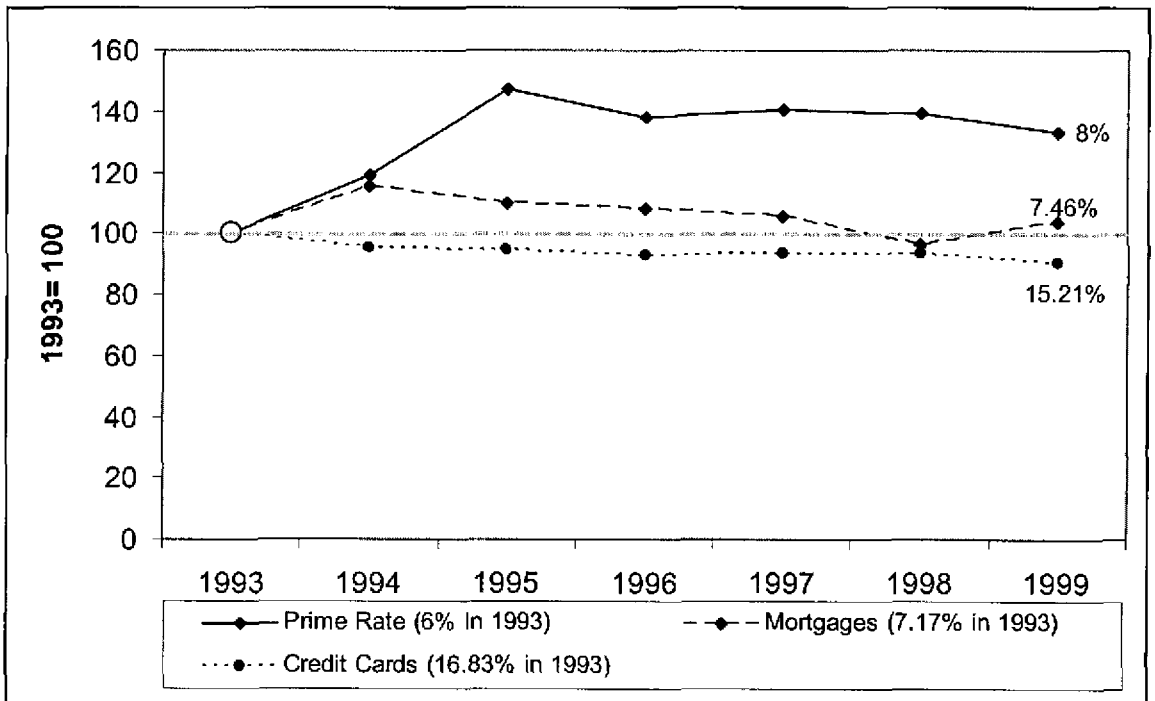
[8] Fred Cate and Michael Staten, "The Impact of Opt-In Rules on Retail Credit Markets: A Case Study of MBNA." Forthcoming, February, 2002. To be available at: www.understandingprivacy.org

[9] The opt-in requirement for affiliates assumes that the MBNA would require consent to utilize credit information about those prospects who also held another MBNA account save for information concerning the customers handling of the MBNA account. That is, the estimates assumed that MBNA could not use information from credit reports and the customers standing with other creditors that it *already* possessed in the context of another MBNA account for the purposes of tailoring a new one.

[10] Walter Kitchenman, "US Credit Reporting: Perceived Benefits Outweigh Privacy Concerns." (The Tower Group, 1999) ; Fred Cate and Michael Staten, "The Impact of Opt-In Rules on Retail Credit Markets: A Case Study of MBNA"; John Baron and Michael Staten, "The Value of Comprehensive Credit Reporting: Lessons from the US Experience." Staten and Baron, following Stiglitz and Weiss (1981) on lending markets without information sharing, offer a reason why interest rates fall (rise) when data is mobile (restricted). "When lenders can't distinguish good borrowers from bad borrowers all borrowers are charged an average interest rate that reflects

interest rates that restrictions on data transfer most sharply impact corporate revenues and consumer prices. The following figure shows the decline in the interest rate on credit cards and 30-year conventional mortgages relative to the prime rate. We believe that risk fine-tuning has been one reason for this decline.

FIGURE 1: EVOLUTION OF PRIME, MORTGAGE AND CREDIT CARD INTEREST RATES, 1993-99



Source: Board of Governors Federal Reserve System, *Annual Statistical Digest*
Bureau of the Census, *Statistical Abstract of the US, 2000*

Mobile consumer data has yielded lower interest rates through two avenues, risk fine-tuning and securitization of debt, both of which depend on the use of consumer information to assess risk. Lenders are able to use past credit history and personalized data to extend lower interest rates to less risky consumers. The ability to identify risk levels also enables financial markets to securitize debt by risk levels, as Fannie Mae does. The purchase of consumer debt by investors in secondary markets channels additional monies into lending institutions expanding the amount of credit available for consumers. The liquidity in the system has contributed to lower mortgage interest rates.

2.2.1 The Case of Insurance Premiums

their pooled experience. But, this rate is higher than good borrowers warrant and causes some good borrowers to drop out of the market, thereby shrinking the customer base and further raising the average rate charged to good customers." (p. 5.) Also see Joseph Stiglitz and Andrew Weiss, "Credit Rationing in Markets with Imperfect Information." *American Economic Review.* 71: 393-410 (1981)

Without a doubt, one of the industries likely to be most affected by an "opt-in" restriction on the use of third party data for commercial purposes is insurance. Firms in the different segments of the insurance industry are heavily dependent upon access to rich sources of third party data for marketing purposes, for risk assessment, for underwriting, and claims verification and fraud prevention.

An opt-in data restriction will increase the marketing and administrative costs of insurance companies in every one of its segments. In addition, the spread of premium payments may converge, all other things being equal, as the ability of insurers to differentiate lower risk from higher risk candidates is reduced. This phenomenon was discussed in the context of credit cards, where the reward for good behavior (a history of meeting credit obligations) would be reduced in order to cover the additional costs from bad loans made to higher risk candidates who default, though the insurance sector contains its own peculiar dynamics that may exert counter pressures.[11] This pattern is an example of the distortions that result from the lack of efficient distribution of information.

Gauging the impact of an opt-in data restriction on the broad insurance industry is a difficult task. This is largely due to the fact that the data needs of each individual segment are relatively unique. For instance, age data that is important to life insurers to assess an applicant's risk to evaluate her likelihood of purchasing a policy and to determine the appropriate policy and premium level, is relatively unimportant to property insurers, who are more concerned with other factors.

When determining the appropriate premium for a coverage policy requested by an applicant, an insurer will use third party data to both ensure that the individual is who he/she is claiming to be (most common when the transaction is conducted online) and to verify the validity of the information provided on the application.

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[11] In the absence of third part data restrictions, it is possible that lower risk policyholders are likely to pay more while a greater number of higher risk policyholders will pay less, on average, pay less. With that said, it is important to note that the way economic agents cope with a lack of information or information asymmetries can vary from industry to industry. This is clear from the various treatments of asymmetric information by Joseph Stiglitz and his collaborator. In their path breaking work, Rothschild and Stiglitz argue that when confronted with different types of individuals -- high-risk and low-risk -- which insurance providers could not differentiate, there exist equilibrium solutions in which the choices offered screen insurance buyers through self-selection. For example, insurance providers can offer two separate insurance contracts: one with partial-coverage and small deductibles and another with full-coverage and high deductibles. Low risk individuals would rationally choose the former whereas high-risk individuals would opt for the latter. The contracts would mitigate against adverse selection and the deductibles control for moral hazard. The salient point here is that the effects of limited information on an industry is peculiar to its structure, products, etc., and thus increases in insurance premiums do not follow or do not follow in the same way that increases in credit interest rates do. Cf. M. Rothschild and J. Stiglitz. "Equilibrium in Competitive Insurance Markets: An Essay on the Economics of Imperfect Information" *Quarterly Journal of Economics.* 95:629-649 (1976)

For example, it is frequently necessary to confirm that an applicant does not have undisclosed drivers living in their household. An applicant with a 15 year old son who is ineligible to drive at the time of application, but who will begin driving shortly thereafter, would be treated very differently than an individual without any teenage children.

In addition, automobile insurers routinely use public record data such as traffic reports and driver's license information from the state department of motor vehicles, as well as claims reports from companies such as DATEK to verify information on an application and assess an applicant's overall risk. In many jurisdictions, individuals with a history or pattern of traffic violations and accidents will usually be required to pay higher premiums than those who have a spotless driving history. Access to third party data is also important for identifying potential fraudulent claims, such as where the same individual submits multiple claims for the same injury to different companies. Third party data may also be important for identifying other patterns of claiming behavior that may indicate higher risks which, if undetected, will result in lower risk drivers being required to subsidize higher risk drivers.

Here, it is important to emphasize that data use for marketing purposes is not used for underwriting and vice versa. In fact, information service providers physically separate their databases used for marketing services from those used for decision products (*e.g.* credit reports, individual reference services, etc.). Furthermore, as defined under the permissible purpose clause of the Fair Credit Reporting Act (FCRA), credit reports can only be used expressly for underwriting, unless a consumer provides written consent, in which case it may also be used for claims analysis and other related purposes.

The value of using credit reports for underwriting cannot be overstated, as the use of credit reporting data is pervasive among automobile insurers. Insurers have found a strong positive correlation between a high credit score and a low loss ratio (the loss pay-out by insurers divided by the premium paid by the policy holder, a.k.a. "loss potential"). In all likelihood, individuals who pays their bills and are able to hold a job over time to provide for their needs will tend to be responsible with respect to driving and the upkeep and maintenance of an automobile or a home. In short, a track record of responsibility in one area is a powerful indicator of responsible behavior in other areas.

Currently, in California, as a result of state law and recent directions from the state's Insurance Commissioner, credit scores can no longer be used by insurers for the purposes of risk assessment and underwriting, forcing insurers to revert to less accurate methods of assessing risk. Insurers may use an individual's credit report, but not their credit score for insurance scoring. This method is more subjective and time consuming than the use of the highly predictive credit score. Given this, there is good reason to believe that consumers will eventually be confronted with higher premium prices, as the overall industry loss ratio

increases as a result of the issuing of policies to high risk candidates at relatively low premiums.

2.2.2 The Case of Mortgages

Assessment of the impact of data restrictions on third party transfers in California must consider the resulting inability to fine-tune risk and securitizing debt by risk level in a secondary debt market. The effect of these on mortgage interest rates are perhaps the most significant, as mortgages account for $4.48 trillion of the $6.46 trillion in household outstanding debt in 1999.[12] In 1999, $411 billion was borrowed in the US for home mortgages in comparison to total household borrowing of $542.9 billion.[13]

- A hypothetical 1% increase in the mortgage rate for 1999 California home buyers from 7% to 8% amounts to approximately an additional $418 million per annum on all outstanding 30 year conventional, fixed-rate mortgages. A 2% increase, or roughly the difference one study found to obtain in Western European societies with strong restrictions on third party information sharing, amounts to an additional $836 million in interest payments per year.

- These increases also imply a loss in tax revenue since interest payments are deducted from taxable income. Assuming the same demand for housing, by the fifth year (2004), more than $2.1 billion, at the same 1% higher rate and more than $4.2 billion, at 2% higher rate, that would otherwise have likely been subject to taxation, becomes exempt from taxable revenue (a loss of more than $170 million.[14])

The costs of course extend beyond higher finance charges as the impact on home ownership rates must be taken into consideration. We use as the basis here the results of a study by a Tower Group study under the direction of Walter Kitchenman, which compared liquidity effects of the relatively liberal US data transfer regimes with the more restrictive ones found in Western Europe and found that mortgages in the US tend to be systematically as much as 200 basis points lower than in Western European states.[15] He offers three reasons for higher rates grounded in data transfer. The inability to fine tune risk results in higher interest rates. One mechanism for pushing rates higher is the fact that some consumers (low-risk ones in this case) subsidize higher risk ones. As

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[12] Federal Reserve, *Flow of Funds Accounts of the United States*. p. 8 (Washington DC: Board of Governors of the Federal Reserve System, June 9, 2000)

[13] Federal Reserve, *Flow of Funds Accounts of the United States*. p. 7.

[14] Assuming an average income tax rate of 4.1% We assumed an average rate of 4.1% on taxable income, based on California's 2000 Income Tax table, using average household gross income and assuming an even distribution between single/married filing separately, married filing jointly, and Head of Household..

[15] Walter Kitchenman, "US Credit Reporting: Perceived Benefits Outweigh Privacy Concerns." (The Tower Group, 1999), p. 7.

many find the costs high relative to their risk levels and thus the value conferred, they will exit from the market, driving the average higher. Fine-tuning risk helps to create a tiered market and thereby reduces the cross-subsidy lower-risk consumers provide to higher risk ones. The ability to clearly identify risk also enables the development of a market in securitized debt, increasing the supply of credit in the market and thereby lowering interest rates. Finally, the difficulty of identifying consumer's preferences creates a barrier to entry and encourages anticompetitive outcomes, as the larger institutions can utilize their information bases in monopolistic fashion.

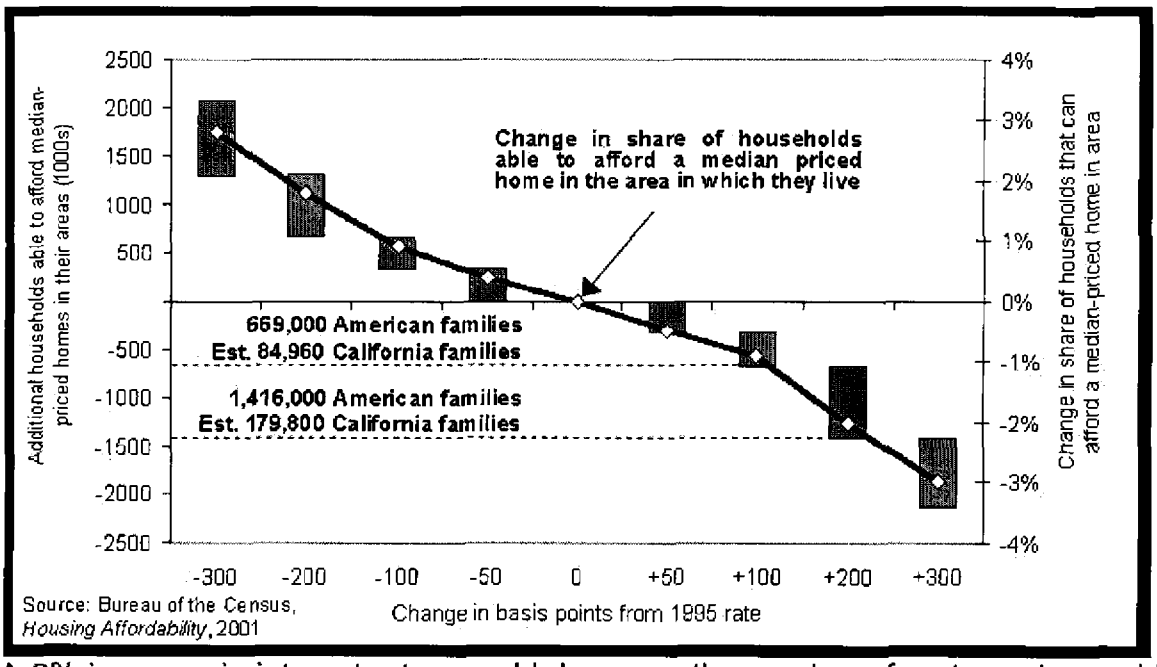
The US Census 1995 housing affordability study permits an assessment of the costs of higher interest rates on home ownership.[16] This provides a basis for assessing further impacts on home construction, employment and tax revenue (in so much as mortgage interest payments are deducted from taxable income) through estimations on what these would have been had the interest rate been higher.[17] It should be noted that there were 667,000 homes sold in the US in 1995; by 2000, that figure rose by more than one-third to 877,000.[18] The following figure shows the impact of interest rate increases on home ownership affordability of median priced homes for Americans in the areas in which they live.

[16] The last comprehensive US Census study was for 1995. We use it here instead of other possible sources for the reliability of the data. At the 1995 interest rate of 8.67% on a 30 year mortgage, only 6.7% of the 21,425,000 US renter households were able afford a median-priced home in the area in which they live. A 2% increase in the interest rate decreases that figure to 6.1%.

[17] Of course had the interest rate been higher as a result in large measure of poor debt securitization, the general impact on economic activity would in all likelihood make the costs listed below actually greater. Here we examine the sold housing market.

[18] Source: Bureau of the Census (2000).

FIGURE 2: HOUSING AFFORDABILITY AND MORTGAGE INTEREST RATES, 1995



Source: Bureau of the Census, *Housing Affordability*, 2001

A 2% increase in interest rates would decrease the number of renters who could afford to own homes where they now live by 119,000. When we recall that 667,000 homes were sold in the United States in 1995, this figure is significant, in so much as first time home ownership accounts for a substantial share of home sales.[19] The impact on home ownership, while wholly negative, cannot be precisely estimated as it is unclear how many families would willingly move to poorer neighborhoods, a move which would have its own costs in the form of poorer social services. But we can make some estimates based on very conservative assumptions.

For the purposes of this study, we make the following assumptions. California home purchases are proportionate to its share of total American households and weighted by its home ownership rate as a share the overall US rate. These imply that California accounts for 9.6% of all US home sales.[20] We assume that the drop in homes demanded is proportionate to those priced out of home ownership as a share of those owners who can afford a home plus that share of renters who can afford a home. That is, of all homes sold, approximately 40% were purchased by first-time home buyers (or renters). 8.9% of renters who could afford a home at the current rate would be priced out of homeownership by a 2% increase in the interest rate. We assume that 8.9% of homes sold to first-time homer buyers would not be sold a result. We similarly assume that a 2% interest

[19] Bureau of the Census, 2000.The principal hurdle faced by would-be homeowners appears to be the cost of down payments. See Howard Savage, "Who can afford to buy a house in 1995?" (Washington, DC: Bureau of the Census, August 1999), available at www.census.gov for definitions and methodology.

[20] See Howard Savage, "Who can afford to buy a house in 1995?"

rate increase would price out of the housing market 4% of current homeowners who can afford a median priced home in their neighborhood, and we assume that 4% of these homes would not be sold.[21]

- An increase of 1% on the interest rate of 30-year mortgages, from 8.67% to 9.67% (with 5% down) would result in[22]
  - Approximately 1,850 fewer homes sold as fewer families would be able to afford median priced homes in their neighborhoods
  - $322.6 million in lost home sales
  - Nearly 1,700 jobs lost in the residential construction sector[23]
  - An additional $1,760 per year for each new home buyer in interest payments or nearly $110 million per annum for 1995 home buyers[24]
  - Had an opt-in system been put in place in 1995, larger exempt income that does not benefit the earner would also yield tax revenue losses of $28 million for 2000 assuming the same interest rate and sale price.

- An increase of 2% in the mortgage interest rate from 8.67% to 10.67% would through its impact on California renters alone result in approximately
  - Approximately 3,830 fewer families able to afford median priced homes in their neighborhoods and thus fewer homes sold
  - $665.8 million in lost home sales
  - Nearly 2,100 jobs lost in the residential construction sector
  - An additional $3,520 per year for each new home buyer in interest payments or nearly $214 million per annum for 1995 home buyers
  - Had an opt-in system been put in place in 1995, larger exempt income that does not benefit the earner would also yield tax revenue losses of $56.8 million for 2000 assuming the same interest rate and sale price.

On the one hand, we have not taken into consideration the fact that many may purchase homes in cheaper neighborhoods. But on the whole, such a move would have to take into account hard to quantify costs such as poorer social services and schools.

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[21] Assumed a home sale price averaged to the 1995 US average home selling price of $173,800.

[22] The US Census Housing Affordability study assumes an 8.67% interest rate.

[23] We have made the assumption that the ratio of labor hours to output remains constant. Far more likely is the fact that given falling sales, jobs would be cut in greater proportion in order to maintain profit margins. Employment losses as a result of lost real estate loan revenue in the banking sector can be expected to be very small, less than 0.004% of the US banking sector, all else being equal. See Ben Craig, "The Long-Run Demand for Labor in the Banking Industry." *Federal Reserve Bank of Cleveland* . p. 27 for the regression coefficients for labor demand in the sector. www.clev.frb.org/research/review97/bencraig.pdf.

[24] On a $173,800 home with a 5% down payment and a 30-year mortgage, compounded quarterly.

The impact would be felt not only by new home buyers but also perhaps by those with adjustable rate mortgages (ARMs), some of whom may be priced out of homes in their neighborhoods. Adjustable mortgages account for approximately 20.1% of all outstanding mortgages and mortgage backed securities as of June 2001.[25] ARMs would rise if information restrictions limit the effective securitization of debt, reducing the overall supply of credit in the system. The lower levels of credit as a share of GDP in Europe can be tied to the institutional hurdles -- including privacy restrictions -- that limit the development of a secondary debt market. Assuming that California accounts for 9.5% of these outstanding mortgages, valued at $3.69 trillion, a 1% increase in the mortgage rate for California mortgages would result in an additional $738 million in interest payments and a 2% increase would result in an additional $1.48 billion. Because the impact of information restrictions on ARMs would operate through the its impact on liquidity, any precise prediction of its magnitude is extremely difficult; in all likelihood, the increase in existing ARM rates would remain well below the increase in fixed mortgage rates. Yet, given the size of this market, even a small increase comprises significant costs for consumers.

The impact is permanent in the sense that while interest rates may move up and down but they will most likely be higher than they would have been under a less restrictive (opt-out) regime. The increase in mortgage interest rates is not transitory and represents an increase in the price of home mortgages for any given level, for any given moment.

2.2.3 The Case of Credit Cards

As with home mortgages, the transfer of consumer information from credit bureaus and other third parties has helped to reduce the interest rate on consumer retail debt in the past decade. Cate and Staten's case study of MBNA provides a basis to assess the impact of opt-in rules.

Credit card debt accounts for approximately 10% of outstanding consumer loans, or $554 billion in outstanding receivables on credit cards. Outstanding credit card debt for California households amounted to approximately 14% of the total or approximately $79 billion.[26] The figure below illustrates more clearly how credit card interest rates have fallen and, more importantly, the distribution of interest rates further suggests that issuers are able to fine tune interest rates, offering significantly lower rates for less risky customers than to more risky ones

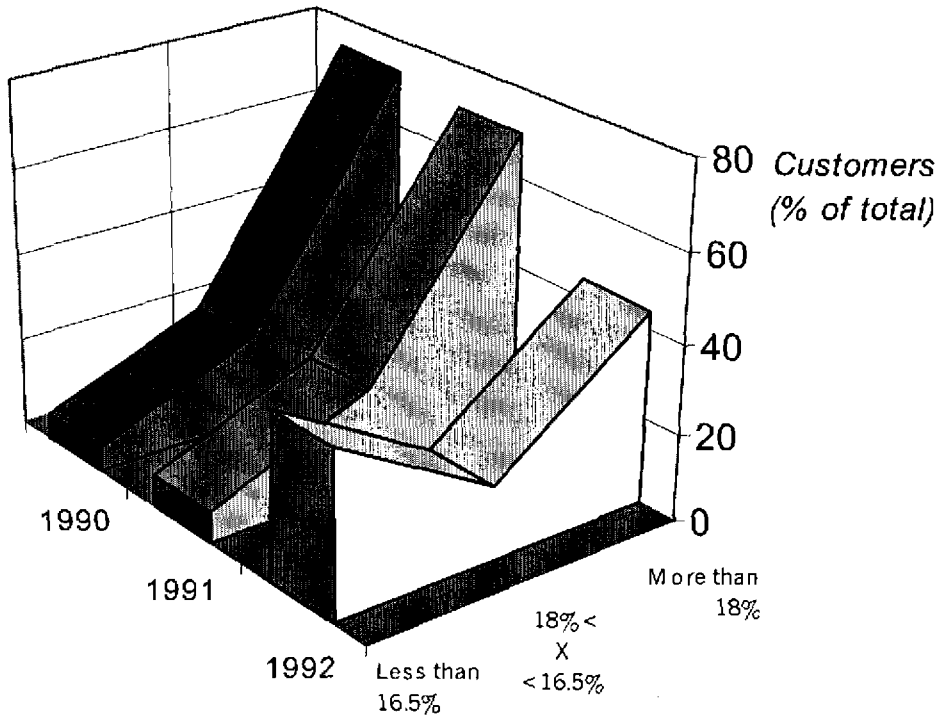
[25] SRM Research Corp. We assume an interest rate of 5.67%. ARMs account for 38.12% of residential mortgage loans owned by the nation's banks, thrifts, and credit unions and 5.4% of Fannie Mae and Freddie Mac outstanding mortgage backed securities. Of course, part of the claim here is that it is the ability to carefully assess risk that permits mortgages to be securitized and thereby remain relatively low.

[26] Source: CardTrak.com, drawn from BankCard Barometer and CardData Online.

as a result of being able to identify them. The initial year, 1991, witnessed the introduction of tiered-pricing based on greater risk fine-tuning.[27]

[27] For a comprehensive description of the evolution and a comparison with more restrictive information transfer regimes, see John Baron and Michael Staten, "*The Value of Comprehensive* Credit Reporting: Lessons from the US Experience."

FIGURE 3: DISTRIBUTION OF BANK CARD INTEREST RATES, 1990-92



Source: *CardTrak*, cited in Cate and Staten, September 21, 2001

Credit card interest rates changes fell consistently as the prime rate continued to climb. An opt-in regime for California may encourage a return to higher rates in three possible ways. Firstly, the increased costs of acquiring new customers (see above) would be passed on. This cost is likely to be small as this cost will most likely be passed onto all American credit card users. Secondly, the inability to target customers creates new barriers to entry, resulting is declining competition. This cost is also likely to be spread across American credit card holders. Thirdly, the inability to fine tune credit and assess risk results in an averaging of interest rates that drives good (low-risk) customers away, raising the average risk level of remaining credit card customers and thereby the interest rate. This is less likely to be spread across all US credit card consumers.

The exact cost is difficult to estimate. But the very rise of the large credit card suppliers was in large measure a product of risk fine-tuning, with the result that a significant share of cards issued are done so with interest rates tiered by risk. That is, a considerable share of the credit card market operates through a tiered system. The loss of access to personal information and the ability to identify potential clients positively and not merely negatively (i.e., defaults, bankruptcies) may well result in a return to higher interest rates.

A rise in credit card interest rates for California consumers entails considerable costs. A 50 basis points increase in the interest rate on California outstanding credit card receivables costs consumers approximately an additional $460 million; a 100 basis points increase similarly results in approximately $920 million in additional costs.[28]

2.3 Compliance Costs

While a study that examines full compliance costs has yet to be done, Robert Hahn's study of the impact of the costs of data restriction for online commercial activity is illustrative. Given that the largest financial firms have significant online business, the additional costs Hahn identifies apply. He estimated an average compliance cost of $190,000 per company, which we adjusted downward to $158,000.[29] These costs stemmed from consultants and new software to protect data. This cost would apply to all businesses that have substantial transactions with consumers and would not be weighted by consumer business as a share of total business.

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[28] Differences in fact are not quite fact are not quite linear due to compounding. Total payment = Principal*$(1 + r/m)^{mt}$, where r is the interest rate, m is the compound periods (here 365, i.e., compounded daily) and t is the period (=1). But the differences between an arithmetic increase and the non-linear estimation remain relatively small. While the impact of rising prices in the form of rising interest rates on credit demanded is hard to predict precisely, a 10% decline in consumer retail credit demanded in California can be expected to lead to a decline in national bank employment of between approximately 0.08% and 0.12% or between approximately 1,300 and 2,000 workers across the US, again all else being equal, and assuming that a labor demand function similar to that of banks holds for credit card providers and California credit card balances are held in equal proportion by providers across the US. Ben Craig, "The Long-Run Demand for Labor in Banking." p. 27, and Bureau of Labor Statistics, www.stat.bls.gov. Given the concentration of finance sector employment in Los Angeles and San Francisco, approximately 10% of all jobs in the finance sector, these areas can be expected to be disproportionately hit. Daniel Immergluck, "Cities and Finance Jobs: The Effects of Financial Services Restructuring on the Location of Employment." Brookings Institute Discussion Paper. November 1999. p. 3.

[29] Hahn (Washington DC: AEI/Brookings Joint Center for Regulatory Studies, 2001)) found an average cost of $190,000, but the average may be skewed upward by the presence of one heavy outlier. Removing outliers (responses more than 2 standard deviation from the mean) reduced the cost -- outliers were found only above the mean -- to $158,000. Costs can be expected to be between $66 million and $242 million, assuming [29]that they fall within one standard deviation of the restricted sample mean. Robert Hahn, "An Assessment of the Costs of Proposed Online Privacy Legislation." Properly, the costs would be incurred by all firms that substantially transact online with California consumers. The number of firms is in all likelihood significantly larger than assumed here. One survey by the Office of the Comptroller of Currency found that 46.2% of FDIC- FDIC-insured commercial banks had no plans to offer Internet services in 2001 or beyond. That is, 53.8% of FDIC-insured commercial banks did or had plans to offer Internet banking. See Office of the Comptroller of Currency, *Economics Working Papers*. (Washington, DC: Congressional Information Service, September 2001) p. 43. If we assume that this share holds for California commercial banks and credit intermediation firms, the compliance cost would rise to approximately $1 billion.

Assuming that only 10% of the approximately 9800 credit intermediation firms in California[30], or large firms are required to comply, the compliance costs of opt-in would exceed $154 million.

Unlike search costs and increased prices from a loss of ability to fine tune risk, these costs are one-time. Yet, we have used very restrictive assumptions here, and in all likelihood the number of firms that would be required to update systems to comply would be considerably larger.

[30] Nationally, firms with more than 10 establishments account for 13% of all firms in the sector but nearly 75% of all revenue and79% of all establishments. Even excluding those firms with more than 100 establishments, this set of firms average more than $138 million per firm. We assume a similar distribution for credit intermediation in California; 10% errs on the side of conservatism, Bureau of Census, *Establishment and Firm Size: Finance and Insurance, 1997 Census. (Washington, DC: Bureau of the Census, 2000) p. 40, Table 2.*

3.0 CHARITABLE GIVING IN CALIFORNIA: OVERVIEW

It is estimated that an opt-in data restriction on the commercial use of third party data would reduce statewide donations to California-based charitable organizations by $1.57 billion. Given the unique characteristics of giving in California, there is good reason to believe that California-based nonprofit organizations would suffer more than similar out of state organizations. This section analyzes charitable giving in California during the late 1990s (the most recent dates for which data are available).

Results from a recent groundbreaking study on patterns of charitable giving and volunteering in California, the nation's largest state with more than 35 million residents and 25 million adults (over 18 years of age), rank Californians significantly above the national average both in terms of how many people give to charities, and how generous they are.[31] The following table offers some of the results of a survey of charitable giving conducted by the Institute for Nonprofit Organization Management at the University of San Francisco.

Table 1: Dimensions of Giving, California and U.S.

	Contributing Households				All Households		
	California			*U.S.*	*California*		*U.S.*
Categories of Giving	**%**	**Median**	**Mean**	**Mean**	**Median**	**Mean**	**Mean**
Total giving	91.7	$628	$1,866	na	$538	$1,712	Na
Total giving as % of income		1.9	4.5	na	.8	3.0	Na
Giving to individuals	57.4	$200	$1,006	na	$20	$577	Na
Giving to individuals as % of income		.5	2.4	na	>.1	1.0	Na
Giving to charitable organizations	89.9	$375	$1,247	$1,017	$300	$1,121	$696
Giving to charit. orgs. As % of income		1.2	3.0	2.2	.5	2.2	1.7
Income	71.7	$37,000	$49,198	$46,637	$35,000	$47,685	$41,484

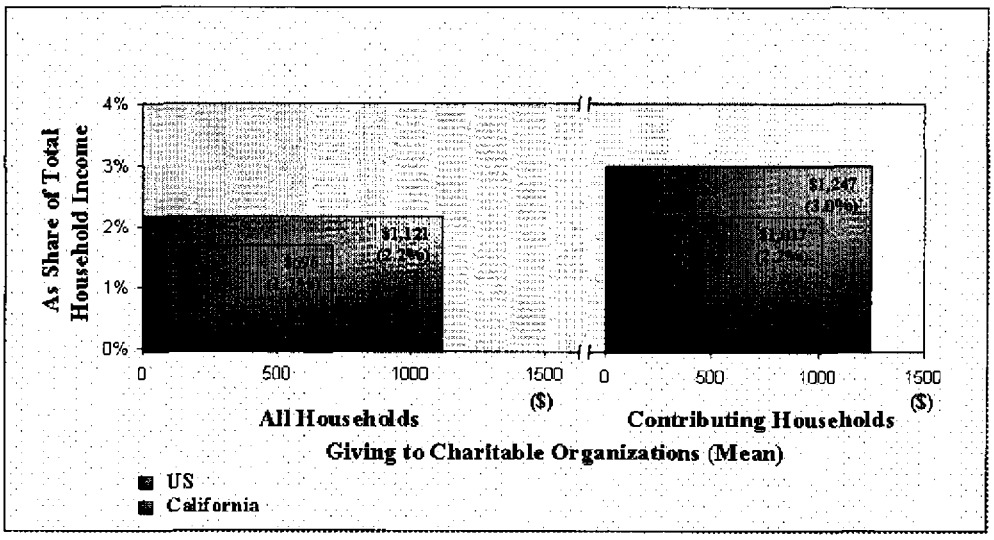
Source: "Giving and Volunteering in California" by Institute For Nonprofit Organization Management

90 percent of respondents to the survey conducted by Institute for Nonprofit Organization Management at the University of San Francisco reported having given to a charitable organization "during the past 12 months." This is 29 percent above the national average.[32] Respondents to the survey also demonstrated a

[31] O'Neill, Michael and William L. Roberts. "Giving and Volunteering in California," Institute for Nonprofit Organization Management, College of Professional Studies as the University of San Francisco. May, 2000.
[32] *Ibid.* p. 3.

much greater level of generosity with respect to both formal giving (person to institution) and informal giving (person to person). Indeed, as **Figure 5** shows, the percentage of household income contributed to charitable organizations is 36 percent higher for Californians than for the rest of the nation.[33]

FIGURE 4: US AND CALIFORNIA CHARITABLE GIVING IN $ AND AS A SHARE OF HOUSEHOLD INCOME



Total giving to operating charitable organizations in California during 1999 amounted to $16.68 billion.[34] This figure represents 12 percent of the national total. There were 25,538 operating charitable organizations based in California that reported in 1999 (filed an IRS Form 990). These included health and human services charities, as well as those oriented toward the arts, community development, the environment, social science research, science and technology, arts, culture, education, animal-related, civil rights and social advocacy among others.

[33] *Ibid.* p. 3. Reported levels of giving and volunteering in California are higher than those reported in other nationally-oriented surveys. One of the most plausible reasons for this may be that Californians are more effectively solicited by nonprofits. The ability of nonprofits to solicit from Californians is, of course, contingent upon their access to rich data bases and information services made possible by the unfettered flow of personal identifying information. A data restriction akin to an "opt-in" would, as this study has found, reduce the efficiency of nonprofits in soliciting funds and result in much lower statewide numbers for giving and volunteering in California.

[34] The National Center for Charitable Statistics identified 25,538 operating public charities that reported in 1999 (filed IRS Form 990). Organizations not required to report include religious congregations and organizations with less than $25,000 in gross receipts. For an explanation on state specific data, see http://nccs.urban.org/guide.htm

3.1 The Impact of Data Restrictions

This study focuses only on the restriction of the commercial use of third party data, and leaves un-addressed similar restrictions on affiliate sharing and the use of internal data.[35] In order to understand how human service charitable organizations would likely be impacted by an "opt-in" requirement, a brief discussion on how charitable organizations use third party data is necessary.

3.1.1 Use of Third Party Data by Charitable Organizations

In general, charitable organizations solicit donations in three ways: (1) person-to-person solicitations; (2) direct mail campaigns; and (3) via telephone solicitations. Each of these three methods is heavily dependent upon access to a robust pool of third party data. The process by which third party data is used by charities to solicit donations for each of the three techniques is briefly summarized below.

a. Person-to-Person (CA- $6.38 billion for operating charities)

This is a three-stage process involving prospect identification and research, prospect cultivation, and the delivery of the solicitation.

➢ *Identification and Research:* Charitable organizations use a variety of different methods – alumni rating sessions, information about acquaintances provided by board members, etc. – to identify individuals with a willingness and capacity to give. For those individuals judged to have the potential to make significant contributions, charities gather external information to further determine the capability of these individuals to give.[36]

➢ *Prospect cultivation:* At this stage, nonprofits seek to ensure that a prospect understands the mission of the charity. This may involve personal visits, invitations to dinner, or direct telephone calls. During this process, charities are also trying to determine how much should be asked for. Conventional fundraising wisdom is that prospective donors will give more if asked for a concrete amount. It is widely held that donors almost never give more than they are asked to give, and that asking them for a "stretch" gift often produces one. On the other hand,

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[35] "**Internal data**" refers to personal identifying information collected by an organization during the course of its interaction with a consumer or donor. This information typically includes name, address, phone number, amount of transaction or donation, credit card number and other data necessary to execute the transaction. Collectively, this information is referred to as an organization's "house file." "**External data**" refers to personal identifying information and other data about consumers that is collected and compiled from a variety of sources including public record data, self-reported data from surveys or product registration cards, or modeled information.

[36] Such information could include property records and assessments; filings with the Securities and Exchange Commission; Census Bureau information; and trade journal articles.

asking for too much almost always results in a rejection or a donation that is less than would have been the case had a more appropriate amount been requested. Thus, information pertaining to a donor's capability and willingness to contribute is critical in determining "the ask."

➢ *Solicitation:* Requests are made to individuals identified and an amount is determined based on the use of third party data and information provided by the prospect during the course of the cultivation process.

b. Direct Mail Fundraising (CA - $3.17 billion for operating charities)

Many charitable organizations rely upon direct mail as their primary method for raising funds. This type of fundraising is very effective in collecting a large sum of money in modest amounts, a necessity for most human service charitable organizations that must raise money in increments of $10 or $15 dollars. While more expensive than person-to-person solicitations, mature direct mail campaigns often raise a dollar of revenue for every 30 cents spent on fundraising.[37] External data is used in a number of ways in acquiring new donors and re-soliciting existing ones. Below is a brief description of how charitable organizations use external data to acquire new donors and re-solicit existing donors.

➢ *Acquiring New Donors:* Many charities acquire new donors by sending direct mail solicitations to prospects. They do this to raise revenues for existing and new programs, but also to compensate for past donors who have stopped contributing. House lists of active donors experience attrition or turn over and, without replacement, would eventually decay to a very small number of donors. Over time, nonprofits would "go out of business" if they could not attract new donors.[38]

Charitable organizations typically use two types of external information to prospect. First, they obtain mailing lists of individuals who are likely to give to the organization. For example, lists of high-income individuals and individuals who have recently made donations almost always yield higher response rates than random prospect mailings. Second, charitable organizations purchase

[37] This amount is over the donation life cycle. Initially, prospect mailing yields only about 70 cents for each dollar invested. However, once a prospect is converted to an actual donor, the response rate from the house file of donors is substantially higher than that from prospect mailing – which typically ranges from 0.5 percent to 2.5 percent. The additional contributions, then, after the conversion has occurred, more than outweigh the initial cost of prospecting. See, Turner, Michael A. and Larry Buc. "The Impact of Data Restrictions on Nonprofit Fundraising." January, 2002. A joint study conducted by The Direct Marketing Association's Information Services Executive Council (ISEC) and the Nonprofit Federation.

[38] *Ibid.* P. 16. The attrition rate for most nonprofits ranges between 20 percent and 40 percent per annum.

demographic information about their prospects and send mailings only to the demographic groups that are most likely to contribute. This secondary screening can increase the donations generated by a prospect mailing by a factor of two.[39]

➢ *Donor Re-Solicitation:* Contacting existing donors – names on the organization's house file – represents the primary source of funds for nonprofits as these individuals are more likely to donate in the future than is the average prospect. However, even with the company's house file, it is too expensive to contact the entire list because some donors may not be interested in donating. Many of the larger, national charities use sophisticated predictive modeling to target their mailings. This, of course, relies crucially on access to third party data. Mailings to existing donors typically result in response rates between 6 percent and 12 percent, with a dollar raised for every 25 cents spent.[40]

c. Telephone Fundraising (CA - $4.61 billion for operating charities)

Typically, the larger national charitable organizations call prior supporters – both active and lapsed donors – and to ask for donations to support their mission. Because they may not have a visible presence in a particular community, these organizations have found it extremely difficult to acquire new donors by making cold calls. Smaller nonprofit charities, on the other hand, with a clear mission and a visible presence in the region or locality in which they are based have traditionally enjoyed more success acquiring new donors by making cold calls to members of the communities in which they operate. It is noteworthy that even cold calls involve the use of third party data as lists of potential donors from within a community are purchased from or compiled by third parties.

➢ *Neighbor-to-Neighbor Campaigns:* A second less known form of cold call solicitations frequently used by larger, nationally known charitable organizations is a "neighbor-to-neighbor" (N2N) campaign. Such campaigns are referred to in the non-profit community parlance of the industry as "active" campaigns. In short, a large national charitable organization will call a prospective donor – Ms. Jane Doe, for example -- and ask her to go door-to-door and/or write letters to her friends that she feels would be interested in either contributing to the organization or providing additional leads for further prospecting efforts. Again, as with the cold calls for straight charitable appeals discussed above, the N2N campaigns also make use of third party data, although much more so.

N2N campaigns utilize complex data models designed to identify those individuals most likely to participate in an active campaign. Experian does the

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[39] *Ibid.* P. 17.

[40] Warwick, Mal. *Raising Money by Mail.* P. 16. Some direct mail fundraisers have achieved response rates in excess of 20 percent on some mailings to existing donors. See Turner and Buc. Pp. 18-19.

modeling for one major national charitable organization interviewed by ISEC for their study. While somewhat unorthodox, there is ample evidence that N2N campaigns are an extremely effective method for acquiring new donors. Indeed, a major national human services charitable organization interviewed by ISEC indicated that, of the $40 million in total donations received during 2000, approximately $8 million or 20 percent was raised through neighbor-to-neighbor campaigns.[41] Among others, N2N campaigns are employed by Easter Seals, March of Dimes, the American Heart Association, the American Lung Association, and the American Cancer Society.

3.2 Third Party "Opt-in" and Charitable Fundraising

Given the pervasive use of third party data by charities for soliciting donations through every communications media during each stage of the fundraising process, it is easy to understand how a data restriction akin to an "opt-in" requirement would seriously disrupt the time-honored business model currently employed by charities across the nation.

This report analyzes restrictions that we expect would result from third-party sharing "opt-in" legislation. As previously mentioned, this opt-in scheme would result in a practical ban on the use of external information. If prospective legislation considers a more restrictive opt-in scheme for internal and external data, then fundamental business practices would change.[42]

3.2.1 Analysis of Opt-In for External Data – Person-to-Person Fundraising

As outlined above, external prospect identification and research, cultivation, and solicitation are the steps in the person-to-person solicitation process. Charitable organizations use external information from the first step through the last step. External information helps identify prospective donors with the willingness and capacity to give, helps reveal interests, and helps determine the amount to ask for. Person-to-person fundraising would continue even if external information became unavailable, but efficiency would be reduced significantly.

Fundraisers would have a more difficult time determining how much they should ask for and would be less able to prioritize their donor cultivation efforts. Some nonprofits would respond by maintaining their current efforts without the use of external data, others by increasing their fundraising staff. Hence, some

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[41] Turner and Buc. "The Impact of Data Restrictions on Nonprofit Fundraising," January, 2002. P. 20.

[42] While analyzing this considerable change is beyond the scope of this report, certainly the impacts of a more restrictive regime would be more extensive than under the less restrictive regime presented below. For example, if legislation significantly impacted the ability of organizations to use internally generated information on existing donors, nonprofits would have to eternally prospect, a certainly losing proposition.

nonprofits would maintain their fundraising costs (and therefore lose revenue) while others would increase their costs in an attempt to keep revenue constant.

The lack of external information would affect a nonprofit's ability to determine how much to ask for and, therefore, the resulting donations. Less information would cause inefficient decisions as well as inefficient requests. Inefficient requests are those requests where donors would have given more had they been asked to stretch and those requests where the donors gave smaller amounts because they were asked for too much.

Based on results from a recent ISEC/Nonprofit Federation survey of health and human service charitable organizations, an opt-in style regime is expected to reduce the efficiency of person-to-person fundraising by 10 percent to 30 percent. Using the conservative estimate of 10 percent, an opt-in data restriction would translate to a loss of $638 million in donations annually from California.

3.2.2 Analysis of Opt-In for External Data – Direct Mail Campaigns

If charitable organizations cannot use external data to identify prospects who are likely to give, then the only way to prospect would be to send untargeted mailings to a random list of prospects. Untargeted, random mailings would achieve much lower response rates than the targeted prospect mailings currently being sent by most nonprofits. Hence, to receive the same amount of donations from prospects, charitable organizations would need to significantly increase their mailings to prospects and, therefore, their fundraising cost to achieve a specified revenue goal. This is the scenario we analyze below.[43]

To estimate the increase in fundraising costs that would be required to keep fundraising revenue constant under a third-party sharing opt-in scheme, we utilize the analysis of campaign data from fifteen nonprofit organizations that raise significant funds through direct mail.[44] As **Table 5** shows, we expect that these nonprofits would need to increase their fundraising costs from 41 cents per dollar raised to at least 53 cents per dollar of revenue, significantly reducing the amount of revenue that these organizations can spend on services for their communities.

Furthermore, these information restrictions would increase the proportion of revenue that nonprofits would need to spend on fundraising to well above recommended thresholds. The Better Business Bureau's Philanthropic Advisory Service recommends that prospective donors give only to charities whose fund-

[43] It is worth noting, however, that increasing mailing size is not the only possible way that a nonprofit could respond to restrictions on the use of external information. Another potential scenario would be for nonprofit organizations to keep fundraising costs constant. In this scenario, organizations' donor bases would erode over time, eventually forcing them out of operation or at least into a smaller operation.

[44] Turner and Buc. "The Impact of Data Restrictions on Nonprofit Fundraising."

raising costs amount to no more than 35 percent of the total collected. An opt-in restriction, then, would push most charities well over the threshold of acceptable fundraising expenditures.

Table 2. Impact of Restriction on Use of External Information on Fundraising Costs

Type of Mailing	Cost as a Percentage of Revenue (Current Use of Information)	Cost as a Percentage of Revenue (No Ext. Information)
Prospect Mailing	17%	29%
House List Mailing	24	24
Total Mailing	41	53

Specifically, these fifteen organizations currently spend about 17 cents of every dollar they raise sending mailings to prospective donors. Furthermore, losing the predictive power provided by external information would ***cause their response rate to drop by 43 percent***. To gain the same number of new donors with this lower response rate, these organizations would need to increase their prospect mailings by 76 percent. Assuming constant returns to scale, this would ***increase their fundraising cost by 12 percent of total revenue, or $380 million***.

3.2.3 Analysis of Opt-In for External Data – Telephone Solicitations

Given the likely substitution between direct mail and telephone fundraising efforts, the precise quantification of the impact of an "opt-in" type data restriction upon the effectiveness of fundraising via the telephone is virtually impossible. There is, however, sufficient anecdotal evidence from those charitable organizations interviewed and surveyed that use the telephone to raise funds to make reasonable claims about the direction and magnitude of the likely costs associated with an "opt-in" third party data restriction.

Any attempt to assess the impact of such a restriction must be tied to the specific data sets that would disappear as a result of a third party data restriction. Assuming that such a restriction included core marketing data, including name, address, gender, previous names or aliases, age, phone number, and e-mail address – such as would be the case in California were a restrictive opt-in regime to become law – the impact on the ability of human service charities to use the telephone to acquire new donors would be immediate and significant. Indeed, the executive director of one national human services charitable organization stated, "We have never been able to make a straight charitable appeal for (the) acquisition (of new donors) ... the neighbor-to-neighbor model drives all the new blood through our organization."[45]

Foreclosing access to core marketing data for commercial purposes weakens the ability of major national charitable organizations to efficiently engage in cold call active process (neighbor-to-neighbor) marketing, as the model that drives this type of campaign loses data sets vital to its functioning. If we assume that, as with direct mail, response rates decrease by 43 percent as a result of less data and less accurate data, then the typical charitable organization would have to increase its marketing expenditure by 76 percent to raise the same amount of donations – resulting in a transfer of resources away from programs toward administrative costs – or, donations would decline by a similar magnitude. This increase equals 12 percent of total revenue.

In the example cited above, the national charitable organization that raised 20 percent of its total donations through neighbor-to-neighbor campaigns ($8 million of $40 million) would only be able to raise 13 percent of its total annual donations ($4.6 million of $36.6 million) through active giving campaigns with a constant marketing expenditure – a decline of $3.4 million or 43 percent of the amount raised through N2N campaigns.

In California, if we assume conservatively that a typical charitable organization receives approximately two-thirds or 66 percent of its total donations from past or extant donors over their lifetime, and one-third or 33 percent from newly acquired donors, then a 43 percent decrease in telephone solicitations to prospects results

[45] Interview with major health and medical human service charitable organization president. 6 December, 2001.

in a ***loss of approximately $650 million in donations each year***. If charitable organizations engaged in active process donor acquisition programs increase their marketing expenditures by 76 percent (i.e., 12 percent of total revenue) to offset the decline in response rates, this would still result in a ***transfer of over $550 million annually from charitable programs to administrative costs***. Under either scenario, an "opt-in" third-party data restriction that limits the use of core marketing data for commercial purposes – including fundraising for charitable organizations – would result in greater costs, lower expenditure or both. Unfortunately, the segment of society that would be forced to bear the heaviest costs – the recipients of services from charitable organizations – are precisely those that are least able to do so.

3.2.4 Additional Impacts of Opt-In for External Data

An opt-in third-party data restriction would have at least two additional negative externalities on charitable organizations. First, charitable organizations would lose revenues earned from the rental of their appended and unappended house file list. Revenues earned from the rental of house file lists typically go directly into the general fund for charitable programs.

To illustrate this point, in the case of the $40 million national charity referenced above, $1.7 million in revenues are derived annually from the sale of appended and unappended lists. This money directly covers program costs. Under an opt-in regime, assuming a 15 percent opt-in rate, the charitable organization would lose 85 percent of the earnings from list rentals, resulting in an additional reduction of $1.5 million for their programs and services. In California, assuming that the average charitable organization accounts for 2 percent of its annual revenues through the sale or rental of lists, then an opt-in data restriction would result in ***a loss of program funds in the range of $132 million annually.*** Even if we reduce the average earnings from list sales and rentals by 50 percent, from 2 percent of total annual revenue to 1 percent, this still results in an annual decline in charitable contributions of ***$66 million***.

A second negative consequence resulting from an opt-in third party data restriction, although less quantifiable, is no less serious. Should the availability of accurate core marketing data diminish – and in this case, particularly data about an individual's age – then charitable organizations that operate bequest, legacy, and planned giving programs will be severely hampered. Often times, charitable organizations with a focus on a particular medical condition – cancer, Parkinson's, or Alzheimer's, for instance – are more oriented toward a mature or elderly donor base. One such organization indicated that the average age of a donor on their house file list was 66 years old.[46] This particular organization selects candidates for its planned giving programs based on a number of criteria,

[46] Interview with national medical/health care human services charitable organization. 6 December, 2001.

including highest previous contribution, total lifetime contribution, whether or not the individual has made multiple contributions, and their age.

Age is an important identifier for planned giving programs, as those who are more advanced in their age are more apt to participate. Given the focus on this elderly cohort, accurate age information is critical. Charitable organizations do not want to solicit donations from deceased individuals, as families of the deceased are likely to be highly sensitive to such inadvertent mistakes. These errors, no matter how innocent, will result in extreme negativities that will alienate individuals who otherwise may have made a contribution.

3.2.5 Calculating the Total Cost of Data Restrictions to CA Charities

The above analyses suggest that a third-party sharing opt-in scheme would increase direct mail campaign costs by 12 percent of total direct mail campaign revenue and could potentially decrease person-to-person contributions by 10 percent. Table 7, Decrease in Disposable Funds, presents the net effect of increased costs and decreased revenues for the nonprofit industry. To raise a constant amount of revenue with lower response rates, direct mail costs increase by $380 million. Assuming a similar impact on telephone solicitations, these telephone solicitation costs would increase by another $553 million. Person-to-person revenues could also drop due to inefficient information by $638 million.

Table 3. Decrease in Disposable Funds

	Direct Mail	Telephone	Person-to-Person	Total
Fundraising Revenue	$3.17 billion	$4.61 billion	$6.38 billion	$14.16 billion[a]
Increase in Fundraising Cost	12%	12%	10%	N/A
Decrease in Revenue	$380 million	$553 million	$638 million	$1.57 billion

[a] Of the $16.68 billion given in California during 1999, $14.16 billion is from person-to-person, direct mail, and telephone campaigns and $2.52 billion is from newspaper, magazine, television, radio, and other campaigns.
N/A = not applicable.

Of the $14.16 billion raised in 1999 from direct mail, telephone solicitation, and person-to-person solicitations, charitable organizations could have as much as $1.57 billion less to spend on their missions. Instead of researching cures for diseases, caring for children, feeding the homeless, nurturing the environment, and providing the many considerable services of charitable organizations, an additional $933 million must go towards fundraising and as much as $638 million is not captured.

3.3 Conclusion for California Charities

The $1.57 billion projected loss to California-based charities is a conservative estimate. It does not include the estimated $132 million in lost

revenues from list rentals and sales, nor does it consider the possibility that donations may decline as potential contributors consider the administrative costs of charities too high to be ethical. Taken together, the cost of a third party data restriction could run well in excess of $1.7 billion each year.

Exempting nonprofits from third party opt-in laws is not a workable solution. Information service providers derive less than 10 percent of their marketing services revenues from sales to nonprofits. Thus, if a law precluded the sale of third party information to the for-profit world, then none will be available for either charities or law enforcement entities.

4.0 DIRECT MARKETING AND NON-STORE RETAILING

The consideration of retailing, like the consideration of non-profit fund raising, is included in this study in order to assess of the costs of generic types of legislation aimed at restricting third party-use of commercial data, through "opt-in" provisions. Many retailers, whether because they extend credit, use credit information, or rely on other kinds of commercial data shared or obtained through third-party sources of any kind will be affected by such a law. For instance, the transfer of consumer demographic and preference data by any credit extender would become prohibited under a privacy regime that prohibits the transfer of information to third parties. In this instance, direct marketers would lose access to one of the most reliable sources of personal information, financial service institutions; information shared by consumers with their banks, insurance firms and credit card companies tend to be far more reliable and current than information shared with other types of businesses. Therefore an examination of the impact of opt-in requirements on this sector should be undertaken.[47]

While risk fine-tuning does not play any significant role in the costs of opt-in for direct marketing retailers, both search costs and the implementation costs of compliance with restrictions of third party data transfer must be considered. The sector is substantial, accounting for 13.2% of all California's $113 billion retail trade sector, registering approximately $14.9 billion in sales revenue in 1999.[48] Direct marketers utilize personal information to target customers most likely to buy their products and services, reducing unwanted solicitations to those less likely to demand the offers. Accurately predicting the likelihood of response based on demographic information saves on advertising and other search costs.

No general study on the impact of data restrictions on the entire subsector exists. An examination of restrictions on data transfer for apparel catalog and Internet retailers provides a basis for analysis.[49] The study of 26 catalog and Internet apparel retailers found that opt-in restrictions on outside or third party data would increase search costs by 3.5 to 11 percent. While the sample set was relatively small, it contained a representative sample of catalogers and Internet apparel retailers by revenue and market reach. The total revenue for the respondents accounted for approximately 20% of industry revenue. Furthermore, the estimates of the survey were conservative for the following reasons. (i) The model did not include the use of cooperative data, a wide spread practice among

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[47] GLB has been interpreted in this fashion.

[48] Source: Wharton Economic Forecasting Associates; Bureau of Economic Analysis, Department of Commerce. *California: 1997 Economic Census, Retail Trade.* (Washington, DC: Bureau of the Census, 2001) This figure is the GAF number that represents those retail formats where the bulk of consumer good shopping occurs. These formats include general merchandise, department, apparel, furniture, and miscellaneous shopping goods stores. It does not include automobile sales or restaurants. The $113 billion in direct marketing represents 14.5% of the total $782 billion in revenue.

[49] Michael Turner, "The Impact of Data Restrictions on Consumer Distance Shopping." (New York: DMA, March 2001)

apparel catalog retailers. Including the lift to response rates from the use of cooperative data would have amplified the cost of restricting the use of third party data even further and thereby increased the costs of recovering lost revenue. (ii) Very large firms and small firms will be most impacted because they are unaffected by additional discounts in bulk printing and shipping. Consequently, a larger share of goods, accounted for by sales from the larger catalog and Internet retailers, will face marketing cost increases greater than the 7% median figure we use in this study. (iii) Given the high cost structure that small catalog retailers confront, an increase of costs in the magnitude of 7% or more will likely result in exit from the market, eliminating competition and thereby a source of downward price pressure. This anticompetitive effect can be expected to persist as the higher barriers to entry stemming from the new cost structure will serve to discourage new competitors.

In 2001, California non-store retailers spent approximately $1.185 billion in advertising.[50] Assuming that the cost increase of approximately 7% (3.5 to 11 percent) holds across the sector, and assuming that companies seek to preserve total revenue rather than profit margins, opt-in requirements would have increased advertising costs by nearly $189-594 million with a mean of $378 million had companies been unable to gather information from third parties.[51] .

The full impact is harder to measure as many of the smaller companies would have found the costs prohibitive, reducing competition. While companies can be expected to bear much of this cost, a rise in cost and fall in supply will be felt disproportionately by disadvantaged rural and inner city consumers, that is, those who do not live near brick and mortar stores or who have no comparable alternative. For instance, recent studies by Price, Waterhouse and Cooper and the Boston Consulting Group[52] found that economically disadvantaged inner city shoppers overwhelming receive lower quality goods at inflated prices from traditional, store retailers, which is why one study found inner city African

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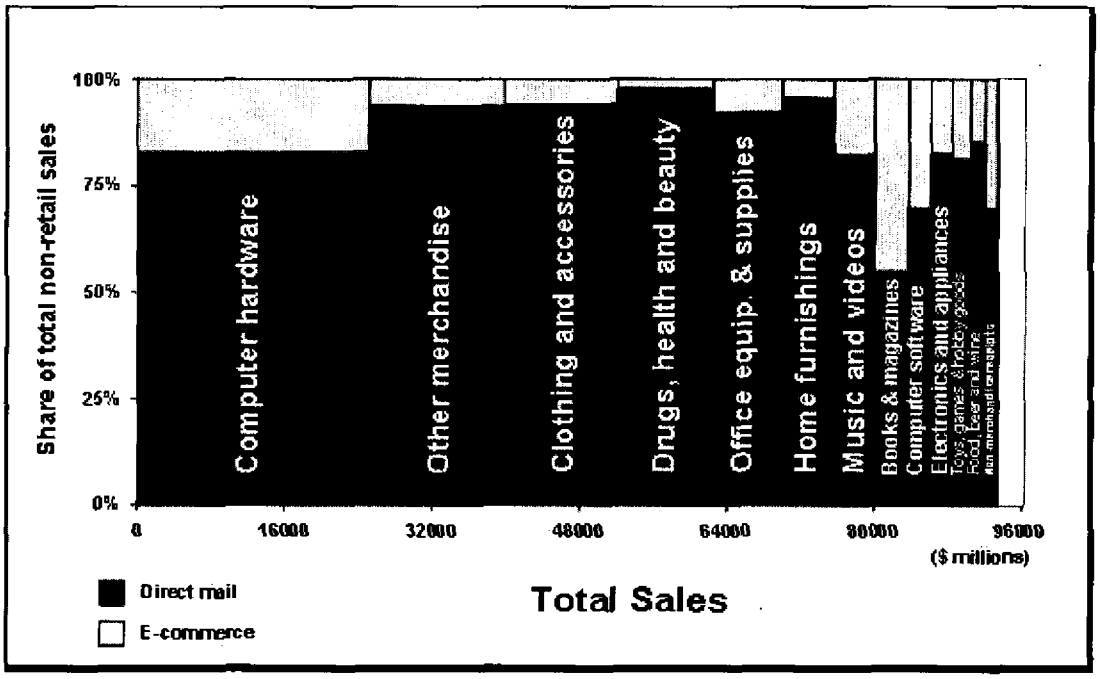
[50] Respondents to the ISEC distance shopping survey reported that they on average spent 22% of net sales revenue on marketing (printing, postage, creative, administration, etc.). $1.185 billion would therefore represent 22% of 5.4 billion in net sales revenues for non-store retailers in California. Given this, a third-party data restriction would increase total costs to firms in the range of $189 million - $594 million. This represents the *projected cost increase* multiplied by net sales revenue. See Turner, The Impact of Data Restrictions on Consumer Distance Shopping, Appendix F.

[51] The survey of apparel nonstore retailers revealed an expected cost increase of 3.5% and 11%. Extrapolating to the wider direct marketing sector, the associated range of expected cost is $41 to $130 million. We have used the average because there are good reasons to believe that the average understates costs. It does so because of (ii), namely, the market segment is comprised of small and large firms, which unlike medium sized firms, will not reap any significant discounts as a result of scale economies in, e.g., printing and mailing. Large firms already exploit scale economies whereas smaller ones are unlikely to expand search by a sufficient factor to do so.

[52] The Boston Consulting Group in partnership with The Initiative for a Competitive Inner City, *The Business Case for Pursuing Retail Opportunities in the Inner City.* June 1998; PricewaterhouseCoopers in partnership with The Initiative for a Competitive Inner City, *The Inner City Shopper: A Strategic Perspective.* January 1999. www.icic.org/research/pubs_and_studies.html

American women use catalogs as primary means for purchasing their apparel at a rate 75% above the national average.

FIGURE 5: E-COMMERCE AND TOTAL SALES FOR MAIL ORDER & DIRECT MAIL RETAILERS BY INDUSTRY, US, 1999



4.1 E-Commerce and Internet Retailers

By 1999, e-commerce came to account for more than 8% of the US $138 billion dollars in non-store retail trade. The following chart illustrates e-commerce as a share of total mail order and e-commerce retail sales by merchandise line.[53] If we assume the same proportions hold for California, e-commerce accounts for $1.26 billion in retail sales in 1999 for pure play firms alone.

We raise e-commerce here because the subsector has made significant inroads quickly into the structure of commerce in the US, and it will continue to do so.[54] The chart understates e-commerce revenue as it is confined to firms in non-store

[53] Home fuel, e.g., comprises a considerable share of non-store retail sales, comprising $17 billion of the $123 billion for 1997. It is, along with smaller sectors, excluded from mail order and e-commerce. Bureau of the Census, *Merchandise Line Sales: Retail Trade, 1997.* (Washington, DC: Bureau of the Census, 2001) p. 151. Source: Bureau of the Census, "E-Commerce Multi Sector Survey 1999." www.census.gov

[54] Michael Exstein and Dohyun Cha, "Effects of E-Commerce and Globalization on the Retail Industry." Credit Suisse First Boston, Equity Research, March 9, 2000 report that US e-commerce retail sales are expected to double in 2 years (2004) and worldwide e-commerce sales are expected to quadruple. Of course, this study predates the collapse of Internet stock prices.

retailing. It does not cover firms which operate in an array of media as well as brick and mortar. To illustrate, while there were 9,139 firms categorized as mail order and e-commerce retailers in 1997, the vast majority of which must be assumed to be mail order firms if revenue is any indication, there were 7,513 websites with secure web servers for e-commerce.[55] By 2000, there were 65,565 websites with secure web servers for e-commerce. At least those that extend credit can be expected to have to update their systems to comply with opt-in requirements for financial services.

The costs of compliance for the protection of on-line data from third party access and transfer are particular and have been estimated, as noted, to be approximately $158,000 per firm. If we conservatively estimate that these costs must be born only by large e-commerce firms that extend credit, perhaps 1% of the 65,565 websites with secure servers[56], compliance costs would exceed $103 million.[57] (Given the size of the variance in costs reported by the sample, this figure is rough; if we assume that costs lie somewhere within one standard deviation of the average, total costs may range between $44 million and $162 million for this 1% of firms.) Again, this cost, stemming from compliance software and expert labor, is a one-time expenditure for these firms and is unlikely to impact significantly on their regular operating expenditure.

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[55] Council of Economic Advisers, *Economic Report of the President*. (Washington, DC: Congressional Information Service, Inc., 2001) p. 201

[56] Retailers which would be subject to opt-in provisions for financial services are those that extend their own line of credit , e.g., Macy's, Banana Republic. While figures for the share of firms offering their own credit cards are not available, retail credit card issuers held 25.7% of outstanding credit card debt in 1994. "Holding Their Own." *Card Fax*. August 19, 1995. p. 1. This figure may have fallen considerably since 1994 and with the rise of credit card issuers such as MBNA and Capital One, which have, as argued above, helped to lower interest rates considerably. According to Card Source One figures, the 15 largest retail credit extenders account for 16% of credit card debt and thus suggests otherwise. www.cardsourceone.com/cardsource/2002/demo/credit_card_issuers/retail_cards/by_outstanding s. The estimate of 1% of the 65,565 on-line retailers does not appear to be excessive. There were more than 49,000 firms in retailing that earned $10 million or more in 1997. Bureau of the Census, *Establishment and Firm Size: Retail Trade, 1997*. (Washington, DC: Bureau of Census, 2001) p. 7. Both of these figures suggest that 1% is a conservative estimate. See Robert Hahn, "An Assessment of the Costs of Proposed Online Privacy Research" for the derivation of compliance costs. He assumes that there are 94,000 firms.

[57] If we further assume that only firms in California will need to comply and that the number of California firms that face these compliance costs is proportional to California firms as a share of all American firms, the costs of compliance would be $11.85 million. This assumption may be heavily restrictive as California accounts for far too large a market for businesses to write-off. The figure above is therefore more likely to be the total cost of compliance.

5.0 CONCLUSION

This study shows the significant but often hidden costs of an "opt-in" (i.e., most restrictive) privacy regime in California. By sampling a narrow but economically significant range of economic activities--financial services (including insurance, credit cards, and home mortgages), charitable giving, and direct marketing, the study concludes that the aggregate costs of this most severe data regime could run, by our conservative estimates, into several billions of dollars. (See Appendix C.)

The range of hidden costs, as we show in Appendix C, is extensive. They include adjustment costs for virtually all sectors. Even if adjustment costs were to be borne entirely by the affected firms, a still greater cost would be borne by consumers in the form of reduced access to credit for the least credit-worthy customers, and increased price of credit (i.e., higher interest rates) for all borrowers. Housing will likely become less accessible for first-time home-buyers (renters) and premiums and risk-categories are likely to be less finely tuned in the insurance industry, making the proper allocation of risk more costly to firms, and by extension, those seeking insurance. Direct marketers will have to bear extensive search costs, and non-profit organizations will find it more difficult to identify and solicit their most generous donors. Finally, as Appendix C summarizes, costs have been identified in the areas of lost employment and lost tax base, as well.

Whether such costs should be imposed on the California economy is for its citizens and elected representatives to decide. This study aims simply to fill a perceived information gap in that decision-making process.

In doing so, however, this study bases itself on how third-party data--sharing is actually used in the modern economy. Many objections to third-party data sharing arise from misunderstandings of how businesses gather and share data to better serve customers. For example, data sharing with third-party affiliates does not INCREASE undesirable solicitations (customers addresses are already publicly available) but rather DECREASE them. Third-party data sharing allows marketers to refine their searches for new customers by soliciting only those who are MOST likely to be receptive to such solicitations, and EXCLUDE those who would be unwilling or unable to respond.

Nor should the data privacy issue as discussed here bear the burden of extraneous legal issues, such as fraud. All responsible parties to the privacy debate recognize that fraudulent activities such as "identity theft" or more personal crimes, such as "Internet stalking" are reprehensible. Public policy should ensure that risks of harm and fraud in any sound "on-line" or "off-line" environment are reduced as far as economically feasible. Privacy regulations, such as those contemplated in some California bills, it must be understood, gain some of their media attention because of these separate "harm" and "fraud"

issues, even though third-party data privacy laws for commercial purposes are not calibrated to address these concerns.

Finally, like the Internet itself, data flows in modern commerce are a seamless web. The nature of third-party data sharing is to create a common "pool" of information that all participants can draw upon. By this analogy, it is not possible to exempt one set of parties (such as charities) to the information pool while imposing restrictions on others. If restrictive policies are applied to commercial data sharing there will not be a deep and wide "pool" of data for the exempted parties such as charitable organizations to draw upon. Exempting even the most socially popular elements of the modern digital economy does little to slake their thirst for information. In other words, it is not possible to say that the leak in the privacy pool can be plugged at one "end"; restrictions creating drains at the other (for-profit) "end" may leave the pool depleted for ALL who need its benefits.

APPENDIX A: METHODOLOGY

To achieve methodological consistency with other published analyses of restrictive privacy regimes studies, this study estimates costs upon the postulated passage of a generic "opt-in" privacy regime. We assume such a regime would restrict access to all non-personally identifying commercial information for the State of California. This generic model has been widely deployed by privacy researchers through-out the United States, and to some extent, internationally. It allows broad comparative analyses not only between types of bills within the same jurisdiction, but types of bills between different jurisdictions (or indeed, different levels of jurisdictions, such as Federal vs. State-level.)

Therefore, this study does not attempt to calculate the costs of any specific legislative proposal (such as e.g., Senator Speier's SB 773, or Senator Peace's bill, or any one of the other privacy bills that have been drafted at one time or another.) The calculation of costs associated with any particular bill is not possible, given the minutiae of many of the provisions in such bills, and the near-certainty that the specific provisions and/or effects of such bills would be altered not only in conference but in the devising and implementing of the specific regulations attendant thereon.

The authors recognize that much of the current debate around data privacy laws is driven by proposals to restrict access to financial data. However, the emphasis of this study on the financial services industry is not premised on the desire of any proposed bill to foreclose access to this type of data in particular. Instead, the extensive reporting of costs for this sector of the California economy is to be explained by the presence of several important and oft-cited studies of this sector at the national, and indeed, international level, and the unfortunate paucity of such studies for other sectors of the economy. [58]

It is a frequent point of methodological and policy confusion, then, that the type of data (financial vs. broad commercial data, e.g.) is to some degree independent of the sector which generates or uses it. Thus, financial data is not confined to the financial services industry, nor is that industry exempt from relying upon non-financial data.

Costs of opt-in were estimated on the basis of the findings of a number of the above-mentioned studies on the impact of data restrictions on selected sectors (see Appendix B). The use of existing studies, while limited by selectiveness,

[58]The insurance industry is perhaps the most notable exception to this rule: it is a significant sector of the financial services industry, but perhaps owing to its regulatory 'locus' at the state level, and certainly, the complexity and diversity of its product range, no systematic studies of the likely costs of privacy laws on the various components of the insurance industry have yet been conducted. This omission, we believe, should be addressed, as the insurance industry is perhaps the most data-dependent sector of the entire economy.

scope and differing methodologies, provides for estimations in the basis of search cost increase, compliance costs, and credit price impact. The differences in methods and scope serve to address different dimensions of the questions, as the impact of restrictions on transfers to third parties varies by sector.

The findings of these studies were adjusted to meet California parameters, where California specific information on costs was unavailable. The parameters are offered and explicated in the body of the study. Parameters were derived firstly on the basis of the share of California households as a share of US households. Where applicable, the ratio of spending on products (credit, homes, etc.) in California to that of the overall US economy serves as a further weight. Secondly, parameters were derived by examining the California share of the market for each sector.

The prior availability of previously published national studies for individual economic sectors thus has the further consequence of limiting our study's estimates to only a small (albeit significant, and, we suspect, not unrepresentative) segment of the overall California economy. If comparable national studies had been available for the full range of economic activity found in California (a scarcely imaginable possibility) it is conceivable our study would have found costs far higher than those we do report. Though such a conclusion would seem to follow as a matter of logic, absent such empirical studies, this can only be speculation.

These estimates are in turn dependent on the methodologies applied for each of the core studies. Three studies -- Turner and Buc's study of charitable organizations, Ernst & Young's study of the Financial Services Roundtable and Turner's study of non-store apparel retailers -- are based on surveys of companies or organizations in the sectors. The findings of the Ernst & Young are not extended to the entire financial services sector. Turner and Buc's study is used to extrapolate for the non-profit sector in California. Turner's apparel study's findings of the level of advertising cost increases as a result of restrictions on third party data transfer are extended widely to the entire direct marketing retail sector.

Robert Hahn's study surveys consultants to estimate the cost of making on-line systems and servers compliant with restrictions on third party data transfer. Costs in his survey result from the need for new systems that tracks and records the provision and transfer of data to third parties, informs third parties of changes in privacy preferences received from clients/consumers and enables consumers to be notified about information stored about them. The summary statistics he provides are skewed by the presence of a heavy outlier, which was more that 3 standard deviations (higher) from the mean. Excluding the outlier reduced average costs from $190,000 to $158,000. We use this figure for compliance calculations. Ranges defined as one standard deviation from the mean are also provided. Given the high variance, we felt one standard deviation to be

reasonable. This compliance costs is selectively extended to segments of credit intermediation firms and e-commerce businesses; the extensions are conservative in scope and their justifications are provided in the main body.

Two studies, Kitchenman (2000) and Staten and Barron (2000) utilize cross-national comparisons in order to establish a correlation between higher interest rates and greater restrictions on data transfer. As no measure of changes in interest rates is provided for changes in the (unmeasured) degree of restrictiveness, we have offered a range of possible costs as a result of interest rate changes.

The Cate and Staten study examines a large player in the credit card sector, MBNA. This case study is used to extrapolate the increased advertising costs for the 8 largest credit card companies on the assumption that they possess similar cost structures.

How the parameters of costs incurred by the FSR and the impact of higher mortgage rates on home ownership and tax revenue must be elaborated.

Search Costs: Financial sector search costs estimates were based on the survey of 90 large financial services companies conducted by Ernst & Young under the direction of Cynthia Glassman. The companies, members of the Financial Service Roundtable (FSR) had a combined revenue of $504 billion in FY2000, or approximately 25% of the sectors revenues. Commercial banking is heavily represented in the membership of the FSR, while the insurance and securities subsectors are underrepresented. Only outliers that reported savings far larger than those reported by most respondents were replaced with the median so that errors would tend towards underestimation of costs. California FSR customer households were estimated to be proportionate to FSR customer households as a share of total US households.

Fred Cate and Michael Staten's study of MBNA provides a basis for estimating search costs for credit card suppliers. Their costs were weighted by California households as a share of US households and by the share of credit card provision accounted for by the 8 largest issuers on the assumption that similar costs extended to those firms with similar market size and power. We made no assumption about the cost structure of smaller firms given that it cannot be assumed that they operate in similar segments.

Costs from Loss of Risk Fine-tuning, Estimation of Losses from Higher Mortgages: Higher interest rates on mortgages, credit cards and other forms of consumer credit was found by Walter Kitchenman's study of credit provision and John Barron and Michael Staten's study of credit reporting. Both use comparisons of US data transfer regime with those of other societies, Kitchenman's with Europe and Cate and Staten's with Australia and Latin

America, to demonstrate higher prices for credit. The mechanisms are explicated in the body of the text above.

Estimations of the impact of an increase in mortgage interest rates are based on the Bureau of the Census Housing Affordability Study 1995. The study provides estimates of the number of renters and home-owners that would be priced out of (come to afford) median price homes in the areas in which they live by and increase (decrease) in the interest rate of fixed-rate 30 year mortgage. Given the reliability of the data, we make counterfactual estimates of housing demand, construction and interest rate payments for a hypothetical 1% increase in the mortgage interest rate in 1995.

The number of renters and homeowners priced out of the national housing market was weighted by the California share of home ownership in the US. California households as a share of US households was weighted by the ratio of California home ownership rates to US home ownership rates to obtain this figure. For both classes of home buyers we assumed that the propensity to purchase a new home was distributed evenly across the spectrum of those who could afford a home; e.g., if at the 1995 interest rate 6.7% of all renters could afford a median priced home in their area and if a 1% increase in the interest rate reduces that level to 6.4% we estimated housing demand among first time home buyers to fall by 0.3/6.7 or 4.5%. Estimates are provided for a 1% and a 2% increase in the interest rate. We use a 1% increase as a base figure. For employment loss, we assume that the loss in housing construction is proportionate to new homes as a share of home sold weighted level of single unit residential housing construction. We conservatively assumed that output per worker to be that of the 1995 level, not taking into consideration the possibility that employment may be disproportionately cut, as in recessions, to defend profit margins. For tax revenue losses, we assumed an average rate of 4.1% on taxable income, based on California's 2000 Income Tax table, using average household gross income and assuming an even distribution between single/married filing separately, married filing jointly, and Head of Household.

APPENDIX B: SOURCE STUDIES

John Baron and Michael Staten, "The Value of Comprehensive Credit Reporting: Lessons from the US Experience." available at: www.understandingprivacy.org

Fred Cate and Michael Staten, "The Impact of Opt-In Rules on Retail Credit Markets: A Case Study of MBNA." Forthcoming, February, 2002. To be available at: www.understandingprivacy.org

Cynthia Glassman, "Customer Benefits from Current Information Sharing by Financial Services Companies." Conducted for the Financial Services Roundtable. (Ernst & Young, December, 2000)

Robert Hahn, "An Assessment of the Costs of Proposed Online Privacy Legislation." (Washington DC: AEI/Brookings Joint Center for Regulatory Studies, 2001)

Walter Kitchenman, "US Credit Reporting: Perceived Benefits Outweigh Privacy Concerns." (The Tower Group, 1999)

Michael Turner, "The Impact of Data Restrictions on Consumer Distance Shopping." (New York: DMA, 2000)

Turner, Michael A. and Larry Buc. "The Impact of Data Restrictions on Nonprofit Fundraising." January, 2002. A joint study conducted by The Direct Marketing Association's Information Services Executive Council (ISEC) and the Nonprofit Federation.

APPENDIX C: OVERVIEW OF COSTS

($millions)	Search Costs	Lost Revenue	Employment (Workers unemployed)	Additional Interest Payments	Implementation Cost	Other
Financial Services	$1,047*				$154◊	
Mortgages†		$322.6†	1,700†	$418‡		• 1,850 [3,830] families priced out of median-prices homes in their area† • Tax loss equivalent to 4.1% of the additional interest payment for all mortgages post-opt-in†
Credit Cards				$927.5		
Charitable Organizations		$1,571¤				
Retail (Direct Marketing)	$378					
Retail (Direct Marketing)	$189 - $584					
E-Commerce					$103	

* For the 90 members of the FSR and for 8 largest credit card companies.
◊ See text for basis. Costs can be expected to fall between $66 million and $254 million for 10% of credit intermediation firms.
† Assuming a 1% increase in the 1995 base rate, revenue, employment and other costs are calculated for a hypothetical 1% in 1995. Increase in interest payments are for 1999 and 2000.
‡ For a 1% increase in the interest rate of new mortgages in 1999.
¤ Monies lost for direct charitable use.

TAB 8

BRIEF FOR APPELLEE

ORAL ARGUMENT SCHEDULED
FEBRUARY 16, 1995

IN THE
UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

RECEIVED
APR 27 1995
CLERK, U.S. COURT OF APPEALS

NOS. 94-1637, 94-1639

SOUTHWESTERN BELL CORPORATION, ET AL.,

APPELLANTS

v.

FEDERAL COMMUNICATIONS COMMISSION,

APPELLEE

ORIGINAL

ON APPEAL FROM AN ORDER OF THE
FEDERAL COMMUNICATIONS COMMISSION

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4148 12/
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14

CERTIFICATE AS TO PARTIES, RULINGS AND RELATED CASES

(A) Parties and Amici:

According to the Commission's records, the parties who appeared in the proceeding before the Commission leading to the order on appeal are as follows:

Bell Atlantic Companies
NYNEX Corporation
Pacific Bell
BellSouth Corporation, BellSouth Telecommunications, Inc., BellSouth Enterprises, Inc. (BellSouth)
Southwestern Bell Corporation
Ad Hoc IXCs
Cellular Marketing, Inc., Lawrence Communications Company, Car Telephones, Inc., and Key Cellular, Inc. (collectively the "HCTC Agents")
National Cellular Resellers Association
Allnet Communications Services, Inc.
Ameritech
People of the State of California and the Public Utilities Commission of the State of California
Comsat Mobile Corporation
Kenneth Robinson
AMSC Subsidiary Corporation
AT&T and McCaw Cellular Communications, Inc.
US West, Inc.
Vanguard Cellular Systems, Inc.
National Association of the Black Owned Broadcasters
Maxcell Telecom Plus, Inc.
TPI Enterprises, Inc.
MCI Telecommunications Corporation
Mobile Communications

The parties and intervenors appearing before the Court are as follows:

Southwestern Bell Corporation
BellSouth Corporation, BellSouth Telecommunications, Inc., and BellSouth Cellular Corporation
AT&T
Bell Atlantic Companies
Federal Communications Commission

(B) Ruling under Appeal:

Craig O. McCaw, 9 FCC Rcd 5836 (1994) (J.A. 1347).

(C) Related Cases:

The Commission's decision to approve transfer of McCaw's radio licenses to AT&T has not been considered by this Court or any other court. The merger is the subject of other litigation:

United States v. Western Electric Co., No. 94-5252 (D.C. Cir., filed September 13, 1994), on appeal by BellSouth Corporation from a District Court decision granting a waiver of the 1982 AT&T divestiture decree to allow AT&T's acquisiton of certain McCaw cellular properties. Oral argument was held on November 16, 1994.

United States v. AT&T Corp., Civ. Action No. 94-01555 (HHG) (D.D.C., filed July 15, 1994), a complaint filed by the Justice Department alleging that the AT&T/MCCaw merger would violate Section 7 of the Clayton Act, 15 U.S.C. § 18. A Stipulation and proposed Final Judgment allowing the merger to proceed with conditions were filed concurrently with the Complaint.

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GLOSSARY

BOC:	Bell Operating Company
CPNI:	Customer Proprietary Network Information
HSR:	Hart, Scott, Rodino Antitrust Improvements Act, 15 U.S.C. § 18
MFJ:	Modified Final Judgment
MSA:	Metropolitan Service Area
RSA:	Rural Service Area
SBC:	Southwestern Bell Corporation

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* *Cases and other authorities principally relied upon are marked with asterisks.*

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ARGUMENT SCHEDULED
MAY 16, 1995

In the
UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

Case No. 94-1637
(and consolidated Case No. 94-1639)

SOUTHWESTERN BELL CORPORATION, et al.,

Appellants

v.

FEDERAL COMMUNICATIONS COMMISSION,

Appellee

BRIEF FOR APPELLEE

ON APPEAL FROM AN ORDER
OF THE FEDERAL COMMUNICATIONS COMMISSION

STATEMENT OF ISSUES

On September 19, 1994, AT&T Corp. and McCaw Cellular Communications, Inc. consummated a $17.2 billion merger, which required a series of regulatory actions by the Federal Communications Commission and other regulators. Those actions included approval by the Commission of applications to transfer to AT&T indirect control of some 400 radio licenses and other FCC authorizations that McCaw held. In the order on appeal in this case, the Commission concluded that the grant of those transfer of control applications, subject to certain conditions, would serve the public interest, convenience and necessity. In re Applications of Craig O. McCaw and American Telephone and Tele-

graph Company for Consent to the Transfer of Control of McCaw Cellular Communications, Inc. and its Subsidiaries, 9 FCC Rcd 5836 (1994) ("Order") (J.A. 1347).

Two Bell regional holding companies ("BOCs") that compete against McCaw's cellular services -- SBC Communications Inc. (formerly, Southwestern Bell Corporation, and hereafter referred to as "SBC") and BellSouth Corporation, BellSouth Telecommunications, Inc. and BellSouth Cellular Corp. (collectively, "BellSouth") -- ask the Court to vacate and remand the FCC's Order. The issues for review are:

1. Whether the FCC acted arbitrarily and capriciously in determining that the transfer of certain licenses from McCaw to AT&T, as conditioned, would serve the public interest by, among other things, promoting competition, innovation, and consumer choice, and would have no countervailing anticompetitive effects.

2. Whether the FCC acted arbitrarily and capriciously in declining to impose upon AT&T and McCaw additional conditions proposed by appellants relating to AT&T's use of its customer information, the treatment of proprietary information of AT&T's equipment customers, conversion of McCaw's systems to equal access, and the bundling of cellular and interexchange service.

3. Whether the FCC abused its discretion by (a) resolving the applications on the basis of a written record rather than holding trial-type hearings, (b) declining to order the production of millions of pages of documents that AT&T and McCaw had provided to the Justice Department in a Hart-Scott-Rodino proceeding concerning the same merger, or (c) declining to waive

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the terms of an applicable protective order to permit SBC to use the documents it had reviewed in this proceeding in separate litigation involving AT&T.

STATUTES AND REGULATIONS

Relevant statutes and regulations are attached to the appellants' opening briefs.

JURISDICTION

This Court has jurisdiction pursuant to 47 U.S.C. § 402(b).

COUNTERSTATEMENT OF THE CASE

This is an appeal of a decision by the FCC under Section 310(d) of the Communications Act, 47 U.S.C. § 310(d), finding that the transfer of certain radio licenses and other authorizations from McCaw to AT&T would serve the public interest. These license transfers were necessary in order to effectuate the merger of AT&T and McCaw.

The FCC decision was one of several governmental approvals that were necessary in order for the merger to proceed. The FCC decision was issued after (1) AT&T and McCaw sought and received approval from numerous state regulatory commissions with jurisdiction over aspects of the transaction, and (2) the Justice Department conducted an independent review of the merger under the Hart-Scott-Rodino Antitrust Improvements Act, 15 U.S.C. § 18,

and likewise determined that the merger, as conditioned by a proposed consent decree, would promote competition.

In this appeal, BellSouth and SBC -- each of whom competes with the McCaw cellular companies in a number of markets -- challenge the Commission's decision. In order to place their claims and the Order in the proper context, it is helpful to review (1) the manner in which cellular and other wireless services are provided today, (2) the AT&T-McCaw merger and the FCC proceedings on the license transfer applications, (3) the other governmental approvals of the merger, (4) the FCC Order under review, and (5) the procedures the Commission followed in considering the transfers.

1. **Cellular radio and other wireless services.** Cellular radio is one of a number of wireless services and products that use radio waves to allow mobile customers to place and receive telephone calls and other messages without being physically wired into the local "landline" telephone network. Cellular service is fully interconnected with the wireline networks of both local exchange and interexchange (long distance) carriers. Cellular subscribers thus can both place calls to and receive calls from wireline subscribers throughout the country and beyond. See Proposed Final Judgment and Competitive Impact Statement; United States v. AT&T Corp. and McCaw Cellular Communications, Inc., D.D.C. No. 94-01555 (HHG) (filed August 5, 1994), 59 Fed. Reg. 44158, 44167 (August 26, 1994) (J.A. 1268, 1277)(hereafter

referred to as "Proposed Final Judgment" or "Competitive Impact Statement," as appropriate).

Although competitive alternatives to cellular service are being developed,[1] cellular service today generally is offered by two licensees in each community. The FCC has granted licenses to two carriers in each of hundreds of metropolitan statistical areas ("MSAs") and rural service areas ("RSAs"), the local boundaries established to define the scope of the licenses. For each such area, the FCC has granted a "B" Block license that was set aside for the Bell Operating Company (BOC) or other wireline carrier with the local exchange monopoly in that area, and an "A" Block license to a carrier, such as McCaw, that does not control the local landline exchange.[2]

Customers can use their cellular telephones to make "local" calls within a calling area as well as interexchange, or long distance, calls to other calling areas. Today, however, the manner in which cellular customers obtain interexchange service differs depending on whether the cellular service is provided by

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[1] For example, the FCC recently has begun auctioning off licenses for "personal communication services" or "PCS," which can offer the same capabilities as cellular service while using different bands of radio spectrum. See generally Adams Telecom, Inc. v. FCC, 38 F.3d 576 (D.C. Cir. 1994). Other companies provide such capabilities by using other frequencies to offer what is known as "wide area specialized mobile radio."

[2] See Cellular Communications Systems, 86 FCC 2d 469, 487-93 (1981), modified, 89 FCC 2d 58, further modified, 90 FCC 2d 571 (1982), petitions for review dismissed, United States v. FCC, No. 82-1526 (D.C. Cir. 1984); Competitive Impact Statement, 59 Fed. Reg. at 44167 (J.A. 1277).

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a BOC cellular carrier such as BellSouth or SBC, or by a non-BOC carrier such as McCaw. The BOCs are prohibited by the consent decree that broke up the former Bell System (the Modification of Final Judgment, or "MFJ") from offering interexchange service, and are required to provide each customer with "equal access" to the interexchange carrier of that customer's choice, such as AT&T, MCI or Sprint.[3] BOC cellular customers thus pick an interexchange carrier in the same way that they choose one for their wireline telephones at home, and the BOCs route both cellular-originated and landline-originated interexchange calls to the interexchange carriers the customers have selected. AT&T and other interexchange carriers provide the same service, at the same rates and from the same tariffs, to cellular customers as to landline customers. See Order, 9 FCC Rcd at 5847 (para. 14) (J.A. 1358).

In contrast, McCaw and other non-BOC carriers are not bound by the MFJ. They are not barred from providing interexchange service or required to provide equal access. McCaw, for example, is the exclusive provider of all services used by its customers, long distance as well as local. It has provided long distance service to its own customers by obtaining bulk service at wholesale rates from AT&T and reselling it to McCaw customers. The service it purchases from AT&T is the same bulk interexchange

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[3] See United States v. AT&T, 552 F. Supp. 131 (D.D.C. 1982), aff'd, Maryland v. United States, 460 U.S. 1001 (1983).

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service, at the same rates and from the same tariffs, as the service that is purchased by large corporate customers of interexchange services and by other carriers that resell such services for landline-originated calling. See Order, 9 FCC Rcd at 5856 (para. 30), 5879-82 (paras. 74, 77) (J.A. 1367, 1390-93).

In the past, BellSouth and SBC have contended that the ability of non-BOC systems to provide interexchange service and the freedom of such systems from equal access requirements have put the BOCs at a competitive disadvantage. In particular, these companies have contended that these differences have allowed those systems both to establish larger local cellular calling areas and to offer wide area calling plans that "bundle" local and interexchange service at a discount by providing all calls between points in a wide area at a single per minute rate that is lower than the total rate at which local cellular and interexchange service are sold separately. See, e.g., Equal Access and Interconnection Obligations Pertaining to Commercial Mobile Radio Services, Notice of Proposed Rulemaking, 9 FCC Rcd 5408, 5419-20, 5437-38 (1994) ("Equal Access NPRM").

The FCC now is considering whether it should impose equal access obligations on non-BOC cellular systems, and has proposed such a rule and sought comment in a pending rulemaking. Equal Access NPRM, 9 FCC Rcd at 5423-29. At the same time, BellSouth and SBC are seeking to have those MFJ obligations and restrictions lifted from themselves. They have filed motions in the

antitrust court that oversees the MFJ, seeking "generic wireless relief" -- i.e., freedom to provide interexchange service to their cellular customers and to cease providing equal access in connection with their cellular services.[4] They also have moved separately to vacate the MFJ in its entirety.[5] Those motions are pending. Under the terms of the MFJ, the BOCs must be granted interexchange relief -- even if such relief is opposed by another party to the decree -- if the Court finds that "there is no substantial possibility that [a BOC] could use its monopoly power to impede competition in the market it seeks to enter." See United States v. Western Electric Co., 969 F.2d 1231, 1240-41 (D.C. Cir. 1992).

2. **The AT&T-McCaw merger and the applications for approval of license transfers.** McCaw is the nation's largest cellular carrier, operating systems in just under 30 percent of the top 200 MSAs. Order, 9 FCC Rcd at 5840 (para. 3) (J.A. 1351). Each of its systems competes with a "B" Block system owned by a BOC or by another local telephone monopoly. AT&T is the largest provider of interexchange service and also is a manufacturer of network

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[4] See Motion of BellSouth Corporation for Generic Wireless Relief, United States v. Western Electric Co., No. 82-0192 (D.D.C.) (filed April 15, 1994); Motion of Southwestern Bell Corporation for Removal of Cellular and Other Wireless Services from the Decree, United States v. Western Electric Co., No. 82-0192 (D.D.C.) (filed June 20, 1994).

[5] See Motion of Bell Atlantic Corporation, BellSouth Corporation, NYNEX Corporation, and Southwestern Bell Corporation to Vacate the Decree, United States v. Western Electric Co., No. 82-0192 (D.D.C.) (filed July 6, 1994).

equipment, including cellular network equipment. Order, 9 FCC Rcd at 5840 (para. 2) (J.A. 1351). In August of 1993, AT&T and McCaw filed applications with the FCC under Section 310 of the Act seeking approval of the license transfers necessary to effectuate their proposed merger.

In those joint applications and subsequent pleadings, McCaw asserted that it had sought an alliance with AT&T after determining that it needed to be substantially strengthened in order to compete effectively in the existing and emerging wireless services market. McCaw stated that it had faced inherent disadvantages in competing as a start-up company with the well-known and well-financed cellular businesses of the BOCs. These disadvantages, McCaw asserted, had been exacerbated by the FCC's cellular licensing rules, which had allocated B Block licenses to the BOCs (and other local exchange carriers) in the areas in which they provided wireline exchange service, and thus had given the B Block licensees a de facto headstart over their A Block rivals. McCaw stated that, in contrast, it had had to engage in costly transactions to acquire licenses in adjacent MSAs and RSAs, and had been able to commence service only after its competitors had initially signed up the customers with the greatest demand for the service. The result, according to McCaw, was that it had had to borrow heavily and was more than $5 billion in debt at the

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time of its agreement with AT&T.[6] McCaw contended that the agreement with AT&T was necessary to enable it to obtain the financing required to remain an effective competitor to the BOCs, and that AT&T's technological and other expertise would enhance its services. By this time, every other significant "A" block carrier had sold itself to a BOC.

BellSouth and SBC, among others, opposed the AT&T/McCaw applications, arguing that the license transfers should be approved, if at all, subject to stringent conditions.[7] A major focus of the appellants' petitions was the claim the merger would exacerbate the MFJ-related disadvantages that BellSouth and SBC claimed to suffer. Although labelling the MFJ "an obsolete obstacle to competition,"[8] BellSouth and SBC argued that the FCC should impose essentially the same conditions upon AT&T/McCaw. See BellSouth Pet., pp. iv, 5 (J.A. 82, 87); SBC Pet., pp. iv, 7 (J.A. 302, 307). BellSouth also argued that the Commission should condition its approval of the license transfers on AT&T's agreeing to cease opposing BellSouth's efforts to vacate the MFJ

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[6] See AT&T's and McCaw's Opposition to Petitions to Deny and Rely to Comments, pp. 31-35 (December 2, 1993) (J.A. 478-82) ("AT&T Opp."); id., Affidavit of James L. Barksdale (Attachment B) (J.A. 615).

[7] See BellSouth Petition to Impose Conditional Grant to Create a Competitive Market, or Deny as Filed (J.A. 77) ("BellSouth Pet."); Petition of Southwestern Bell Corporation to Impose Conditions or, in the Alternative, to Deny (November 1, 1993) (J.A. 295) ("SBC Pet.").

[8] BellSouth Pet., p. iii (J.A. 81).

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in Court or in Congress. BellSouth Pet., pp. iii-iv, 48-49 (J.A. 81-82, 130-31).

The appellants also raised other issues that they now press on appeal. BellSouth argued that the merger would enable AT&T to provide "end to end" service, and urged the Commission to impose a condition prohibiting AT&T/McCaw from providing service that competes with local exchange service. BellSouth Pet., pp. 29-34, 52 (J.A. 111-16, 134). SBC complained (1) that the merger would have anticompetitive horizontal effects because AT&T and McCaw were significant competitors in an alleged "wireless long distance market," SBC Pet., pp. 16-33 (J.A. 318-35); and (2) that the Commission should impose additional conditions to prohibit AT&T from using information about its interexchange and equipment customers to market cellular services, id., pp. 80-81 (J.A. 382-83).

AT&T and McCaw opposed these petitions. They argued that the BOCs were improperly seeking to use the license transfer proceeding to mount a collateral attack on the MFJ, and that there was no basis for imposing MFJ-type restrictions on parties that did not control a bottleneck monopoly. AT&T Opp., pp. 125-45 (J.A. 572-92). AT&T disputed that cellular service was likely to become a genuine substitute for wireline local exchange service in the near term, but argued that such a development, if it did occur, would be a public interest benefit. Id., pp. 119-25 (J.A. 566-72). With respect to SBC's horizontal concerns, AT&T and McCaw argued that there was no separate "wireless long

distance market," that McCaw's role as a provider of long distance service was too trivial to raise horizontal concerns, and that their commitment to convert McCaw's systems to "equal access" meant that the merger would enhance, not lessen, interexchange competition. AT&T Opp., pp. 49-60 (J.A. 496-507). Finally, AT&T stated that the Commission's existing regulations on AT&T's use of customer information for marketing purposes, which permit such use where the customer does not object, were sufficient to protect any legitimate public interests. Id., pp. 81-84 (J.A. 528-31). AT&T contended that existing safeguards likewise would be sufficient to prevent any misuse of the information it obtained in its role as an equipment manufacturer. Id., pp. 111-12 (J.A. 559-60).

In the course of its review of the AT&T/McCaw applications, the Commission staff determined that its investigation would profit from the review of some of the millions of pages of documents and interrogatory responses that AT&T and McCaw had provided to the Justice Department in connection with a parallel investigation under the Hart-Scott-Rodino Act ("HSR"). The staff therefore ordered AT&T and McCaw to produce approximately 44 boxes of HSR materials, and to make those materials available to any parties that would adhere to a protective order forbidding further dissemination. See Order, 9 FCC Rcd at 5842-43 (para. 6) (J.A. 1353-54); Protective Order, 9 FCC Rcd 2613 (1994) (J.A. 1171). After those documents were produced, the parties were allowed to submit additional comments.

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3. Other governmental approvals of the merger. While the FCC's investigation was proceeding, AT&T and McCaw received other approvals that were necessary to the closing of the merger. All state regulatory commissions with jurisdiction over portions of the transaction approved the merger and rejected claims similar to those advanced here.[9] The MFJ Court granted a waiver of a provision of the MFJ that otherwise would have barred the acquisition.[10] And the Justice Department completed its Hart-Scott-Rodino investigation and concluded that the merger, as conditioned by a proposed consent decree, would bring the "benefits of competition to millions of subscribers of cellular service" by leading to "lower prices" and "better service." DOJ Release (July 15, 1994).

To implement its conditional approval of the merger, the Department filed a complaint in district court to enjoin the merger, and accompanied its complaint with the proposed consent decree that it had negotiated with AT&T. Proposed Final Judgment, 59 Fed. Reg. 44158 (J.A. 1268). The proposed consent decree includes several terms that relate to issues in this

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[9] See, e.g., In the Matter of the Joint Application of the American Telephone and Telegraph Company, Ridge Merger Corp. and McCaw Cellular Communications, Inc., California Public Utilities Commission, Application 93-08-035 (April 6, 1994) (J.A. 1113, 1158) (finding that the merger will produce "benefits to ratepayers" and "adds a new competitive element in an industry of burgeoning competition").

[10] See Order, United States v. Western Electric Co., No. 82-0192 (D.D.C. Aug. 25, 1994), aff'd, D.C. Circuit No. 94-5252 (Feb. 17, 1995).

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appeal. Among other provisions, the proposed decree (1) requires all McCaw cellular systems to provide equal access under provisions modeled after those that are applicable to the BOCs under the MFJ, (2) prohibits the "bundling" of local and interexchange service at discount rates by requiring AT&T and McCaw to state separately the prices for each service and to make each available at those stated prices without regard to whether the customer purchases the other, and (3) establishes detailed provisions to prevent the misuse of competitive information obtained by AT&T in the course of providing equipment to unaffiliated cellular carriers.[11] The proposed decree is subject to review under the Tunney Act, 15 U.S.C. § 16(e), and AT&T and McCaw have stipulated that they will be bound by its terms pending its consideration by the district court. 59 Fed. Reg. at 44159 (J.A. 1269). The proposed decree is before the judge who oversees the MFJ.

4. **The Order under review.** At the conclusion of its investigation, the FCC determined that the license transfers, subject to appropriate conditions, would serve the public interest, and it therefore granted the applications. The Commission identified three relevant markets -- interexchange services in the United States, local cellular service in each MSA or RSA in which McCaw offers service, and the manufacture of cellular network equipment

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[11] See Proposed Final Judgment, §§ II(B), IV(F), V(A), 59 Fed. Reg. at 44162-64 (J.A. 1272-74).

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in North America -- and found that the license transfers under the conditions established by the Order would have no anticompetitive or other adverse effects in those markets. Order, 9 FCC Rcd at 5844-71 (paras. 9-56) (J.A. 1355-82).

To the contrary, the FCC found that the transfers would promote competition and further the public interest by enhancing consumer choice, creating greater price and service competition for cellular services, and spurring innovation. Order, 9 FCC Rcd at 5871-73 (paras. 57-61) (J.A. 1382-84). It found that the transfers would further promote the public interest by strengthening the largest non-BOC cellular carrier and thereby increasing the potential development of alternatives to the existing landline local exchange services that "the BOCs traditionally have provided on a monopoly basis." 9 FCC Rcd at 5872-73 (paras. 58, 60) (J.A. 1383-84).

The FCC imposed several conditions on AT&T and McCaw in approving their applications -- to prevent discrimination by AT&T in the provision of equipment, 9 FCC Rcd at 5892-93 (paras. 97-100) (J.A. 1403-04); to require AT&T to honor its interexchange customers' requests with respect to the use of information about them, 9 FCC Rcd at 5885-86 (para. 83) (J.A. 1396-97); and to prevent the possibility of predatory pricing of bundled offerings, 9 FCC Rcd at 5881-82 (paras. 77-78) (J.A. 1392-93).

The FCC rejected the additional claims that BellSouth and SBC now advance on appeal. It thus rejected the claim that the merger would adversely affect competition by eliminating a

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significant interexchange competitor of AT&T's, finding that McCaw's present and future interexchange capacities were de minimis in light of the numerous other carriers capable of providing the same service. Order, 9 FCC Rcd at 5856-57 (para. 30) (J.A. 1367-68). It declined to prohibit AT&T from using its interexchange customer lists to market cellular services as long as the customer does not object, finding that such activities are pro-competitive. 9 FCC Rcd at 5885-86 (para. 83) (J.A. 1396-97). And it declined to order additional restrictions to protect against misuse by AT&T of the proprietary information of its equipment customers, because it concluded that the existing legal safeguards and economic incentives would be sufficient to protect legitimate interests in confidentiality. 9 FCC Rcd at 5898 (paras. 112-113) (J.A. 1409).

5. **Procedural Issues**. The Commission considered the license transfer applications on the basis of an abundant record. Following a full pleading cycle on the applications, the Commission's Common Carrier Bureau asked AT&T and McCaw also to make available for staff inspection approximately 44 boxes of confidential or proprietary documents and information, which the applicants previously had provided to the Justice Department in the course of the Hart-Scott-Rodino pre-merger review process. Order, 9 FCC Rcd at 5842-43 (para. 6) (J.A. 1353-54). The Commission directed that these documents also be made available to counsel for all parties to the license transfer proceedings upon the execution of protective agreements providing, among

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other things, that the documents and information would be used only in connection with the pending administrative proceeding and any subsequent judicial proceedings related to the license transfers. See Protective Order, 9 FCC Rcd at 2616 (para. 11) (J.A. 1174). The staff permitted the parties to supplement their prior comments in the administrative proceeding on the basis of their inspection of the Hart-Scott-Rodino materials. A number of parties, including BellSouth, SBC, and the Ad Hoc IXCs, did so. Order, 9 FCC Rcd at 5842-43 (para. 6) (J.A. 1353-54).

In the course of the proceedings, opponents of the license transfers raised a number of procedural objections. First, they argued that the Commission should have required AT&T and McCaw to make all -- or significantly more -- of their HSR documents available for inspection. Apart from the scope of the HSR document production, several parties also insisted that the proceeding had generated factual issues requiring a trial-type hearing under 47 U.S.C. § 309(e). Finally, SBC, among others, asked the Commission to waive the protective order insofar as it operates to prevent it from presenting some of the HSR documents and associated information to the MFJ court in connection with separate judicial proceedings in that court.

The Commission denied these procedural claims. With respect to the requests for inspection of additional HSR documents, the Commission noted, as a general matter, that it had broad discretion in determining what information was needed in licensing proceedings. Order, 9 FCC Rcd at 5921 (para. 157) (J.A. 1432)

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(citing 47 U.S.C. §§ 154(j), 308(b), 309(a)). As pertinent here, the FCC concluded that the Bureau had "reasonably identified" the documents that would be most useful in carrying out its public interest mandate, and that opponents had not shown how the relevance of approximately 1,200 boxes of HSR documents filed with the Justice Department outweighed the burden of such an extensive production. Order, 9 FCC Rcd at 5921-22 (para. 158) (J.A. 1432-33).

Moreover, the Commission found no substantial and material question of fact that would require a full trial-type hearing. In this regard, the agency noted that most of the disputes in the record did not involve material factual issues, but rather concerned the "inferences and conclusions to be drawn from the facts, namely, the competitive impacts of the merger." Order, 9 FCC Rcd at 5927-28 (para. 173) (J.A. 1438-39). Such disputes, the Commission stressed, did not require evidentiary hearings under prevailing precedent. Id.

Finally, the Commission denied the BOCs' request for waiver of the protective order. The Commission found that, absent the use limitations contained in the protective order, AT&T and McCaw "certainly would have opposed release to McCaw's competitors of their confidential HSR submission to the DOJ." Order, 9 FCC Rcd at 5925 (para. 167) (J.A. 1436). That would have substantially delayed disclosure and complicated the transfer proceeding. Id. In light of the importance of the protective order's use restrictions -- as well as the fact that the MFJ court itself has the

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power to compel the production of such documents if they are needed -- the Commission found that the BOCs had not justified a waiver. 9 FCC Rcd at 5925 (paras. 167, 168) (J.A. 1436).

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After the Order issued, BellSouth sought a stay from this Court. The Court denied the stay request, holding that BellSouth had failed to demonstrate either a likelihood of success on the merits or the prospect of irreparable harm. Order, D.C. Circuit No. 94-1639, filed October 18, 1994.

INTRODUCTION AND SUMMARY OF ARGUMENT

The license transfer applications approved by the Commission in this case pursuant to the public interest standard of Section 309(a) are pro-competitive and pro-consumer, and the Order approving them is not arbitrary and capricious. The Commission's analysis of competitive and other effects was factual, realistic, and consistent with applicable statutory standards. The conditions that the Commission attached to its approval addressed all realistic concerns about competitive (and other) abuses. The procedures the Commission followed were appropriate to the task.

1. The Commission reasonably determined that grant of the transfer application subject to certain conditions would serve the public interest. The agency applied the correct statutory standard -- the public interest -- and considered the competitive effects of the transfers as a component of the public interest.

The Commission correctly found that the transaction would promote competition by creating a "strengthened competitor" in wireless services, widening the range of choices available to consumers, and bringing about greater price competition, innovation and responsiveness to customers. The Commission also found that, with appropriate conditions and continuing scrutiny, the transaction would not have adverse effects on competition in either long distance service or local cellular services.

2. The Commission reasonably declined to impose restrictive conditions on the transaction that were designed to create a parity between the AT&T/McCaw operation and operations of the BOCs under restrictions set forth in the Modified Final Judgment. The Commission concluded that, whatever the justification might be for continuing to apply those restrictions to the BOCs, there was no justification for extending them automatically to carriers that lacked bottleneck local exchange facilities. The Commission acted within its broad discretion in deferring final resolution of the equal access issue to an ongoing rulemaking, in which it will consider whether to require equal access for all cellular carriers. In allowing the merged cellular company to use AT&T's customer proprietary network information (unless customers object) and in relying on existing safeguards to control AT&T's use of BOC information obtained in supplying equipment to the BOCs, the Commission properly exercised its broad discretion to avoid restrictive regulation where market and other forces are adequate to avoid overreaching.

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3. The Commission followed procedures that were appropriate to its task. It was not required to hold trial-type hearings where no substantial and material questions of fact were raised. The oppositions to the application primarily raised ultimate, conclusionary arguments on which hearings would not be useful. The Commission properly declined to require the production of voluminous files of material that had been presented to and considered by the Justice Department in its antitrust review of the AT&T/McCaw merger. The agency required the production of those parts of that record that its staff believed would be useful, and allowed the parties to see and comment on those materials. Its decision that additional production would not be useful is entitled to deference. Finally, the Commission properly refused to waive the protective order under which those documents had been produced to allow SBC to use those documents in support of other litigation. The Commission had obtained production of those documents without great resistance primarily because the parties had relied upon the protective order restricting their use to the license transfer proceeding. The Commission's decision to enforce the protective order in the absence of a strong showing in support of waiver is reasonably designed to protect the integrity of the agency's confidentiality procedures.

ARGUMENT

I. THE FCC MADE A REASONED DETERMINATION THAT THE AT&T-MCCAW LICENSE TRANSFERS, AS CONDITIONED, WOULD PROMOTE THE PUBLIC INTEREST.

The FCC determined that the license transfers satisfied the statutory requirement that they serve the public interest. Such public interest determinations are "entitled to substantial judicial deference." FCC v. WNCN Listeners Guild, 450 U.S. 593, 596 (1981); see also United States v. FCC, 652 F.2d 72, 88 (D.C. Cir. 1980) (en banc). Judicial review "is limited to determining whether the FCC's action resulted from consideration of the relevant factors and whether the agency has succumbed to a clear error of judgment." GTE Service Corp. v. FCC, 782 F.2d 263, 268 (D.C. Cir. 1986). Under this standard of review, the BOCs bear a "substantial burden" in asking this Court to set that action aside. Id.

SBC and BellSouth cannot bear that burden. Their arguments that the license transfers would be anticompetitive or otherwise would disserve the public interest were considered by the FCC and properly rejected. Indeed, contrary to BellSouth's contentions, the Commission conducted precisely the type of broad public interest analysis the Communications Act requires. It concluded that the license transfers, as conditioned, would promote the public interest by strengthening price and service competition with the BOCs' cellular affiliates, accelerating technological and other market developments, and broadening the choices avail-

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able to consumers. And it rejected BellSouth's and SBC's arguments that the merger would have anticompetitive consequences either in its vertical or horizontal features. As shown below, the BOCs have identified no infirmity in those findings and conclusions.

A. The FCC Applied The Proper Standard.

BellSouth contends that the FCC applied the wrong standard in reviewing the AT&T and McCaw applications. It claims (BellSouth Brief at 13-14) that the FCC failed to conduct a broad "public interest" inquiry focused on the "special considerations" of the industry, and instead improperly confined its analysis to a "strict . . . antitrust review." Paradoxically, BellSouth also contends (BellSouth Brief at 6, 10 n.4) that it was arbitrary for the FCC to decline to exercise its authority to determine whether the merger violated Section 7 of the Clayton Act. See 15 U.S.C. § 21(a).

These claims are inexplicable. Under Section 309(a), the Commission must determine whether the "public interest, convenience and necessity will be served" by the proposed license transfers. "'Competitive considerations'" are a significant "'element'" of that standard. See United States v. FCC, 652 F.2d at 82-83 (quoting Northern Natural Gas Co. v. FPC, 399 F.2d 953, 961 (D.C. Cir. 1968)). This Court therefore has "insisted" that agencies "consider antitrust policy as an important part of their public interest calculus." 652 F.2d at 88. At the same time,

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the Commission also must consider any separate public interest factors that bear on its determination. Id.

In this case, the Commission did precisely that. It first explained that its examination under the public interest standard includes evaluating the "effect of the transfer on competition." Order, 9 FCC Rcd at 5844 (para. 9) (J.A. 1355). The Commission therefore assessed the merger under "antitrust principles" for each relevant market. 9 FCC Rcd at 5844-73 (paras. 9-61) (J.A. 1355-84). Then, after determining that the "competitive component" of the public interest standard would be satisfied by approval of the merger subject to certain conditions (9 FCC Rcd at 5849-50 (para. 20) (J.A. 1360-61)), the Commission considered a broad range of other, independent public interest issues specific to the industry. These issues included the effects of the merger on technical innovation, interconnection agreements, international competitiveness, investment in infrastructure, customer privacy, and the FCC's policies on rate structure, billing and collection, affiliate transactions, and cross-ownership. Order, 9 FCC Rcd at 5871-5920 (paras. 57-154) (J.A. 1382-1431). BellSouth can claim inadequacy only by ignoring major substantive parts of the Order.

BellSouth's suggestion that the FCC was obligated to exercise its authority under the Clayton Act in considering these transfers is likewise insubstantial. This Court has held specifically that the FCC is not required to exercise its Clayton Act authority in licensing proceedings that involve merger or

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joint operations by several substantial parties. United States v. FCC, 652 F.2d at 81-88. Here, there was no cause to do so for at least two reasons. First, the FCC found that the transfers would enhance, not lessen, competition. See Order, 9 FCC Rcd at 5844-73 (paras. 9-61) (J.A. 1355-84). Second, the Justice Department, the federal government's principal antitrust enforcement agency, already had conducted an exhaustive Clayton Act review and had determined that, subject to the conditions in its proposed consent decree, the merger would be pro-competitive. 9 FCC Rcd at 5843, 5844 (paras. 7, 9, & n.25) (J.A. 1354, 1355).

B. The FCC Reasonably Determined That The Vertical Effects of The License Transfers Would Promote Competition And The Public Interest.

The Commission concluded that the AT&T/McCaw license transfers would promote the public interest in several substantial respects. It found, inter alia, that the transfers would create a "strengthened competitor" providing wireless services, broaden the range of choices available to consumers, and bring about greater price competition, innovation, and customer responsiveness by McCaw, its competitors, and future entrants. See Order, 9 FCC Rcd at 5871-73 (para. 57, 60) (J.A. 1382-83). The Commission further found that the transfers would help preserve the independence of the largest non-wireline cellular carrier from the BOCs and other wireline carriers. As a result, the transfers would improve the fairness and quality of interconnection with landline exchange facilities while fostering

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the potential for bypass of those monopoly facilities and the possibility of future local exchange competition. 9 FCC Rcd at 5872-73 (paras. 58, 60) (J.A. 1383-84).

BellSouth and SBC do not directly challenge any of these findings. BellSouth nonetheless asserts that the license transfers are contrary to the public interest because -- in light of MFJ restrictions on comparable BOC activities -- the transfers will allow AT&T to offer "the only facilities-based national and local end-to-end service in the country since divestiture." BellSouth Brief at 2-3. BellSouth argued below that the merger therefore should not be permitted to proceed unless AT&T ceases its opposition to BellSouth's efforts to have the MFJ vacated or until the MFJ is in fact vacated.

As a preliminary matter, BellSouth's description of the effect of the merger is inaccurate. Integrated carriers providing both local cellular service and cellular-originated interexchange calling existed well before this merger and would have continued to exist regardless of the Commission's action on these license transfer applications. Many, if not all, non-BOC cellular carriers, including McCaw prior to the merger, offered both local and interexchange services. See Order, 9 FCC Rcd at 5856-57, 5879-80 (paras. 30, 74) (J.A. 1367-68, 1390-91). Indeed, because non-BOC cellular carriers generally have not offered their customers equal access to interexchange carriers, their customers have relied almost exclusively upon those

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carriers for cellular-originated interexchange calling. See Equal Access NPRM, 9 FCC Rcd at 5415-16.[12]

Nor is AT&T the only "facilities-based" carrier permitted to provide both long distance and local wireless service. AT&T's interexchange competitors likewise may purchase wireless carriers, participate with other firms in seeking to obtain licenses to provide wireless personal communications service (PCS), and engage in the sale of wireless services through other means -- as some have sought to do.[13]

Further, despite BellSouth's reference to a supposed provision of "national and local end-to-end service," McCaw has not offered cellular service to customers throughout the nation and will not do so as a result of the merger. McCaw is a licensee in only 30 percent of the 200 largest MSAs in which service is provided. Order, 9 FCC Rcd at 5840-41 (para. 3) (J.A. 1351-52). A customer whose home or business is located in an MSA that McCaw

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[12] Thus, the principal respect in which BellSouth had claimed to be disadvantaged in competing against McCaw had been that McCaw, unlike BellSouth, had been capable of bundling local and interexchange service and pricing the bundle at a flat rate. See Order, 9 FCC Rcd at 5859-60 (para. 33) (J.A. 1370-71). To the extent that this capability had operated as a disadvantage to BellSouth, the merger has eliminated it. McCaw was able to bundle such services before the merger, but that type of offering now is prohibited to McCaw as a result of AT&T's and McCaw's agreement to comply with the conditions contained in the Justice Department's proposed consent decree.

[13] See, e.g., "PCS License Auction Gets Going Today; Big Players Dominate What's Expected To Be The Biggest FCC Wireless Permit Sale Yet," Los Angeles Times, December 5, 1994 (consortium of Sprint Corp. and three of the largest cable television companies bidding on more than two dozen PCS licenses).

does not serve cannot subscribe to McCaw, but instead must choose one of the two licensed carriers in that customer's MSA (or a reseller that provides service in the area) -- as BellSouth's expert acknowledged below.[14]

BellSouth is thus wrong in now asserting that the geographic market for cellular service is national rather than local. BellSouth Brief at 11.[15] A market is local "where the purchasers cannot, as a practical matter, turn to suppliers outside their own areas." Standard Oil v. United States, 337 U.S. 293, 299 n.5 (1949). BellSouth's claim of a "national" cellular market relies on the irrelevant fact that McCaw and other cellular carriers have entered into "roaming" and "handoff" agreements with cellular carriers in other MSAs so that McCaw's customers can use their cellular phones when they travel outside their home MSAs. But, although McCaw and other cellular carriers can thereby provide their customers with nationwide coverage, each customer remains limited in its choice of carriers to the two licensed cellular carriers, plus whatever resellers also provide service, within the customer's area.[16] As a consequence of regulation,

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[14] See BellSouth Petition, Ex. III (Affidavit of Richard Rozek), p. 15 (J.A. 214)(cellular market is "local in nature" because consumers "select from among the cellular providers serving the area around either their home or work").

[15] SBC agrees that the cellular market is local. See SBC Brief at 18 n.1.

[16] BellSouth's error in confusing the scope of cellular service with the scope of the cellular market is akin to characterizing the retail sale of new automobiles as a national market

therefore, the "'area of effective competition'" is necessarily local. See Hecht v. Pro-Football, Inc., 570 F.2d 982, 988 (D.C. Cir. 1977) (quoting Tampa Elec. Co. v. Nashville Coal Co., 365 U.S. 321, 328 (1961)).

In any event, although BellSouth claims that the "integrated provision of nationwide end-to-end cellular and interexchange service" is the "relevant market" in which to examine these applications (BellSouth Brief at 11), it presented no evidence below showing that such a market currently exists under any accepted method of market definition. Cf. BellSouth Reply Comments, p. 4 (criticizing "static-market" approach that "focus[es] on the present-day cellular market alone") (J.A. 826). Instead, it asserted that such a "market" might develop in the future as a result of the merger, and that it would be unfair if the MFJ were to bar BellSouth from participating in it.

The FCC properly rejected this claim. As an initial matter, if this merger in fact would create a new market, that would hardly render the license transfers anticompetitive. See United States v. FCC, 652 F.2d at 99 ("[i]t would be anomalous to hold that [a firm] could be guilty of lessening competition in a submarket which it will create") (emphasis in original). BellSouth's argument, however, was that the combination instead would have adverse consequences in current markets in which BellSouth

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simply because, although purchasers choose only from among retail outlets located in their own general areas, they can drive the automobiles they buy across the country.

provides service or wishes to do so. Specifically, BellSouth argued that the license transfers would have anticompetitive effects because (1) they purportedly would enable AT&T to bypass the BOCs' monopoly access facilities and "compete[] with local exchange service" (BellSouth Brief at 27; see Order, 9 FCC Rcd at 5851 (para. 23) (J.A. 1362)); and (2) BellSouth and other BOCs would continue to be barred under the MFJ from providing interexchange service and therefore would not be permitted to provide all the same services that McCaw has provided and would continue to provide (BellSouth Brief at 3; see Order, 9 FCC Rcd at 5858-59 (para. 32) (J.A. 1369-70)). These claims are groundless.

First, although the FCC could not determine with any certainty whether or when cellular service will become competitive with landline local exchange monopolies (as it is not today), the potential for such competition is a benefit of the license transfers, not a reason to disapprove them. See Order, 9 FCC Rcd at 5872-73 (paras. 58, 60) (J.A. 1383-84). BellSouth thus confuses its own desire to retain a monopoly with the public interest. The Commission has a well-established policy that local exchange competition is in the public interest and should be promoted.[17]

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[17] See, e.g., Expanded Interconnection with Local Telephone Company Facilities, Memorandum Opinion and Order, 9 FCC Rcd 5154 (1994), Third Report and Order, 9 FCC Rcd 2718 (1994), Report and Order and Notice of Proposed Rulemaking, 7 FCC Rcd 7369 (1992), recon., 8 FCC Rcd 127 (1992), further recon., 8 FCC Rcd 7341 (1993), vacated in part and remanded, Bell Atlantic Telephone Cos. v. FCC, 24 F.3d 1441 (D.C. Cir. 1994).

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Indeed, the FCC's focus in reviewing previous cellular mergers has been to ensure that they would not inhibit competition between cellular and landline carriers.[18]

The related suggestion by intervenor Ad Hoc IXCs that the license transfers would "recreate the same end-to-end nationwide network that the MFJ dismantled" (Intervenors' Brief at 10) is therefore frivolous. The defining characteristic of the former Bell System was its control of "bottleneck" local exchange monopolies, which gave it the ability and incentive to act anticompetitively in adjacent markets. See United States v. Western Electric Co., 900 F.2d 283, 289 (D.C. Cir. 1990). Those bottlenecks now are controlled by the BOCs and other local exchange carriers, not by AT&T. So if the license transfers do result in genuine local exchange competition, that will contribute to dismantling the bottleneck. See Order, 9 FCC Rcd at 5862-63 (para. 39) (J.A. 1373-74)(merger does not raise the dangers of the former Bell System because interexchange service and local cellular service today are substantially more competitive than the interexchange and landline local exchange services of the pre-divestiture Bell System).[19]

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[18] See, e.g., Application of James F. Rill, 60 Radio Reg. 2d (P&F) 583, 594-97 (1986); Metromedia Company, 1 FCC Rcd 1227, 1231-32 (1986).

[19] Ignoring the Court's express admonition, see Order, Southwestern Bell Corp. v. FCC, No. 94-1637 (Dec. 19, 1994) (citing Illinois Bell Tel. Co. v. FCC, 911 F.2d 776, 786 (D.C. Cir. 1990)), the Ad Hoc IXCs also seek to raise a new issue in their Intervenors' Brief that neither BellSouth nor SBC has raised.

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Second, the FCC properly rejected BellSouth's effort to use this license transfer proceeding collaterally to attack the MFJ. Because McCaw and other non-BOC cellular carriers had provided integrated long distance and local calling services before the merger, and would continue to do so even if the merger were blocked, BellSouth's claimed competitive "imbalance" had nothing to do with this proceeding. Indeed, the only effect of the merger with respect to the asserted imbalance has been to mitigate it, as a result of AT&T's and McCaw's agreement to comply with the Justice Department's proposed Consent Decree. That agreement means that McCaw, like the BOCs, now must allow its cellular customers to have equal access to competing interexchange carriers, and no longer may offer the type of flat rate discount "bundling" of which BellSouth previously had complained. BellSouth's claim that the MFJ-like conditions it had proposed were necessary to create "parity" were thus groundless.

Moreover, the Commission noted that the Communications Act does not permit the FCC to subordinate the public interest in increased competition to the goal of "equalizing competition among competitors." See Order, 9 FCC Rcd at 5858 (para. 32 & n.80)

They claim that the FCC acted arbitrarily in refusing to deny the applications on the basis of allegations that AT&T has engaged in unrelated anticompetitive conduct towards resellers. Intervenors' Brief at 3-4, 6-12, 14 n.5. That claim is meritless in any event. The FCC reasonably concluded that those allegations, which are the subject of separate complaint proceedings, are most appropriately dealt with in those proceedings, where the FCC has fully effective remedial powers if any violations of law should be proved. Order, 9 FCC Rcd at 5919-20 (para. 154) (J.A. 1430-31).

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(J.A. 1369)(citing Hawaiian Telephone Co. v. FCC, 498 F.2d 771, 776 (D.C. Cir. 1974)). That holding is directly applicable here, for BellSouth was asking the FCC to block the substantial public benefits the merger would achieve in order to impose on AT&T and McCaw the same MFJ-type restrictions BellSouth deemed "anticompetitive" when applied to itself. 9 FCC Rcd at 5856-57 (para. 30) (J.A. 1367-68). If the MFJ is anticompetitive or hobbles the BOCs in serving customers, the solution is to change the MFJ -- not to impose its restrictions on obligations on the rest of the industry and deny consumers the benefits they otherwise would receive from the BOCs' competitors. There was no justifiable reason for the Commission to limit AT&T-McCaw to the "lowest common denominator" of the MFJ when allowing less restrained competition would serve the public interest.

Even more fundamentally, AT&T and the BOCs are not similarly situated, and it would be perverse to treat them identically. Order 9 FCC Rcd at 5858 (para. 32) (J.A. 1369). The MFJ restrictions -- like the Commission's "structural separation" requirements of which BellSouth also complains (BellSouth Brief at 13) -- addressed "the existence of a long-entrenched exchange service bottleneck encompassing virtually every home and business in the BOCs' territories." 9 FCC Rcd at 5858-59 (para. 32) (J.A. 1369-70). Because AT&T divested these bottleneck monopolies, it is not subject to those restrictions. See United States v. AT&T, 552 F.Supp. at 170-73.

Moreover, although BellSouth asked that the FCC declare the MFJ to be anticompetitive and condition its approval of the license transfers on AT&T's agreement not to oppose BellSouth's litigation and lobbying efforts,[20] the Commission quite properly declined to do so. Because the MFJ is a judicial decree that was entered to enforce the antitrust laws, the Commission sensibly held that BellSouth's claims were more appropriately addressed in other forums. See Order, 9 FCC Rcd at 5858-59 (para. 32) (J.A. 1369-70).[21]

BellSouth's remaining arguments are insubstantial. Contrary to BellSouth's repeated assertion, the Commission did not apply "contradictory standards" by "rel[ying] on the merger's enhancement of Applicants' competitive position" in assessing its pro-competitive benefits, while ignoring the impact on competitors in assessing possible anticompetitive effects. BellSouth Brief at 6, 8, 10. The Commission found that a strengthened competitor

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[20] BellSouth has lodged with the Court a videotape allegedly showing that the pre-divestiture Bell System made a "promise" in 1982 to support MFJ relief in the future, and claims that the FCC should have required the post-divestiture AT&T to fulfill that "commitment" in exchange for approval of the license transfers. BellSouth Brief at 3, 27, 29-30. This claim was rejected by this Court in a different context in 1992. See United States v. Western Electric Co., 969 F.2d at 1239-40. The Commission properly rejected it as well.

[21] The Commission's decision in 800 MHz Air-Ground Rulemaking, 6 FCC Rcd 4582 (1991) (BellSouth Brief at 15), is thus entirely inapposite. There, the Commission conditioned its approval on the invalidation of contracts that the FCC deemed anticompetitive and that had been negotiated at a time when GTE had a monopoly over the relevant services.

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would benefit the public interest by improving price and service competition, innovation, and customer responsiveness, and rejected BellSouth's contention that it should handicap AT&T and McCaw until BellSouth is relieved of the MFJ restrictions. Order, 9 FCC Rcd at 5871-72 (para. 57), 5858-59 (para. 32) (J.A. 1382-83, 1369-70). In so holding, the FCC applied a single, consistent standard derived from the statutory public interest standard: to "protect 'competition, not competitors.'" United States v. FCC, 652 F.2d at 102 (quoting Brown Shoe Co. v. United States, 370 U.S. 294, 320 (1962)).

Similarly, there was nothing improper in the fact that the Order, in discussing pro-competitive benefits, mentioned markets that were not expressly discussed in assessing claims of possible anticompetitive effects. BellSouth Brief at 6, 8. Although BellSouth does not identify the markets it has in mind, it apparently is referring to the fact that the Commission identified as benefits of the merger the possibility of enhanced competition in the local exchange market and greater international competitiveness. Order, 9 FCC Rcd at 5872-73 (paras. 58-60) J.A. 1383-84). The FCC mentioned the local exchange market only in the context of discussing pro-competitive benefits because, contrary to BellSouth's view, local exchange competition is a positive, not a negative, development. And the Commission likewise discussed international competitiveness only when discussing the benefits

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because there was no serious argument that the license transfers would affect international competitiveness adversely.[22]

Finally, there is no merit to BellSouth's contention that the FCC "ignored" the Hart-Scott-Rodino documents. BellSouth Brief at 16-19. Those submissions contained information on market share and market structure that earlier had been submitted to the Justice Department in response to its interrogatories and document requests. They were reviewed by the FCC staff, along with the many briefs and affidavits submitted by the parties, as part of its investigation. See Order, 9 FCC Rcd at 5842-43 (para. 6) (J.A. 1353-54). Contrary to BellSouth's argument, the Commission had no obligation to cite those particular documents in its Order, particularly given that they had been submitted under seal. 9 FCC Rcd at 5920-21 (para. 155 n.343) (J.A. 1431).

BellSouth claims that the documents revealed that the merger was part of an AT&T "plan" to "dominate" the telecommunications industry and "take advantage" of the MFJ restrictions, and that the Commission erred in not so finding. Most of BellSouth's argument merely attributes to AT&T the types of objectives that are common to profit-maximizing firms generally. More fundamentally, BellSouth misapprehends the nature of the Commission's

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[22] BellSouth did contend that the merger would adversely affect international competitiveness, but the only reason it offered was that the BOCs would continue to be barred by the MFJ from providing long distance service and would be unable to compete fully with AT&T in that market. BellSouth Pet., pp. 42-44 (J.A. 124-26). The FCC addressed and rejected BellSouth's MFJ argument. Order, 9 FCC Rcd at 5858-59 (para. 32) (J.A. 1369-70).

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inquiry. The FCC did not seek the documents in order to conduct an investigation into the subjective intent of AT&T executives, but to assess the objectively likely competitive and other effects of the transaction. Even if BellSouth's interpretations of documents and their individual authors' motivations were correct, they would not bear on the economic and other public interest analysis on which the Commission's Order relied. See, e.g., Brook Group Ltd. v. Brown & Williamson Tobacco Corp., 113 S. Ct. 2578, 2597 (1993); Olympia Equip. Leasing v. Western Union Telegraph Co., 797 F.2d 370, 379 (7th Cir. 1986).

C. The FCC Reasonably Determined That The Horizontal Aspects Of The Merger Were De Minimis And Would Have No Anticompetitive Effects.

Recognizing that vertical mergers rarely harm competition, BellSouth and SBC also went to great lengths to recast the merger of AT&T and McCaw as a "horizontal combination" between two suppliers of interexchange services. But there has been no direct competition between AT&T and McCaw. McCaw provides interexchange service only to its cellular customers. Conversely, AT&T and other interexchange carriers have not offered service to McCaw's customers, because McCaw generally has acted as the exclusive provider of interexchange service to its customers (reselling services it obtains from AT&T). See Order, 9 FCC Rcd at 5874-75 (para. 64) (J.A. 1385-86).

Moreover, the Commission properly determined that "[e]ven if AT&T and McCaw were viewed as [interexchange] competitors," the

merger would not have an adverse impact on interexchange competition. 9 FCC Rcd at 5856-57 (para. 30) (J.A. 1367-68).[23] The Commission found that McCaw's sales comprised only 0.3 percent of the national long distance market. Id.[24] The Commission reasoned that McCaw, one of hundreds of resellers of interexchange service, is a "relatively de minimis presence" in that market and its disappearance could have no cognizable effect on competition. Id. Further, relying upon the competitive analysis of the California Attorney General, the FCC recognized that the very existence of an "active resale market" for interexchange services would foster "arbitrage activities [that] would defeat any attempt by AT&T/McCaw to raise cellular interexchange rates." 9 FCC Rcd at 5846-47 (para. 13) (J.A. 1357-58) (citing Cal. Atty. Gen. Op., p. 13) (J.A. 1211).

On review, SBC does not challenge the Commission's overall economic conclusion. Indeed, SBC does not even attempt to explain how AT&T/McCaw could exercise power over the price cellular customers pay for interexchange service. Instead, SBC asks this Court to set aside one of the FCC's intermediate factual findings -- that the "relevant market" for purposes of assessing AT&T/McCaw's ability to raise prices is the general market for interexchange services, and not, as SBC had urged, the much nar-

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[23] See also Opinion of California Attorney General, p. 27, (Feb. 9, 1994) (J.A. 1225) ("Cal. Atty. Gen. Op.").

[24] See AT&T Opp., p. 44 (J.A. 491) (putting McCaw's share of national interexchange revenues at less 0.1 percent).

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rower submarket consisting only of interexchange services to cellular customers. Order, 9 FCC Rcd at 5845-48 (para. 11-15) (J.A. 1356-59).[25]

SBC bears a substantial burden in seeking to overturn the FCC's factual finding on an issue of market definition. See, e.g., United States v. FCC, 652 F.2d at 99 (courts generally will decline to interfere with the FCC's conclusions on relevant submarkets). See also Kaiser Aluminum & Chemical Corp. v. FTC, 652 F.2d 1324, 1329 (7th Cir. 1981). SBC's argument on appeal falls far short of overcoming that deference, and indeed confuses some very basic concepts of economics.

SBC's attack on the FCC's market definition hinges on its assertion that the Commission should have ignored the critical fact that "there is no significant difference" between the interexchange facilities used to serve cellular customers and those used to serve landline customers. 9 FCC Rcd at 5847 (para. 14) (J.A. 1358). Because of that fact, even a "monopolist" in SBC's narrowly-defined "market" for cellular-originated interexchange calls could not raise prices above competitive levels without evoking an effective competitive response from interexchange carriers that previously provided service only to landline

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[25] It is unclear why SBC presses this argument. The only condition SBC contends its horizontal claim should have led the FCC to impose is a requirement that AT&T and McCaw provide equal access. See SBC Brief at 15. But AT&T and McCaw committed during the course of this proceeding to do precisely that. See Order, 9 FCC Rcd at 5872 (para. 59), 5877-78 (paras. 69-70) (J.A. 1383, 1388-89).

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customers but are fully capable of serving cellular customers as well. A cellular customer faced with such a price increase would not have to switch to landline service; it could keep making cellular calls and simply switch to one of those other interexchange carriers, who would have the incentive and capability to provide interexchange service to cellular customers and undercut the monopolist's price.

SBC nonetheless argues that the FCC's consideration of such "supply" substitution is "at odds" with market definition principles, and that it should have focused on "demand" substitution. SBC Brief at 15. SBC is wrong. Indeed, the very cases on which it relies validate the Commission's approach. See Brown Shoe Co. v. United States, 370 U.S. at 325 n.42 ("[t]he cross-elasticity of production facilities may also be an important factor in defining a product market"); Rothery Storage Van Co. v. Atlas Van Lines, Inc., 792 F.2d 210, 218 (D.C. Cir. 1986) ("Because the ability of consumers to turn to other suppliers restrains a firm from raising prices above the competitive level, the definition of the 'relevant market' rests on a determination of available substitutes.").

This Court made clear in Rothery Storage that consideration of supply substitution is an integral part of market definition:

> The degree to which a similar product will be substituted for the product in question is said to measure the cross-elasticity of demand, while the capability of other production facilities to be converted to produce a substitute product is referred to as cross-elasticity of supply. The higher these cross-elasticities, the more likely it is that similar products or the capacity

> of production facilities now used for other purposes are to be counted in the relevant market.

792 F.2d at 218. This is because a firm's ability to maintain a price increase for a given product can be frustrated either by consumers' shifting to other products, or by competitors' shifting production to the given product. If either response is likely, the given product is not a relevant market.

Antitrust law recognizes this:

> Defining a market or "submarket" on the basis of demand considerations alone is erroneous. The function of defining a market is to determine that grouping of sales that, if controlled by a single firm or a cartel, could charge non-competitive prices. But that is not possible if either demand or supply elasticity is high.

Areeda, Hovenkamp & Solow, IIA Antitrust Law 175 (1995). See also Equifax, Inc. v. F.T.C., 618 F.2d 63, 66 (9th Cir. 1980); Federal Trade Comm'n v. Elders Grain, Inc., 868 F.2d 901, 907 (7th Cir. 1989). Given the ability of other interexchange companies to defeat the profitability of even a hypothetical monopolist's increase in cellular interexchange rates, the Commission reasonably concluded that interexchange services generally constitute a relevant market in the case. Order, 9 FCC Rcd at 5846-48 (para. 11-15) (J.A. 1357-59)

Although SBC cites Section 1 of the Merger Guidelines[26] for the proposition that "[m]arket definition focuses solely on demand substitution factors" (SBC Brief at 16), it ignores the

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[26] Department of Justice/Federal Trade Commission Horizontal Merger Guidelines, 4 Trade Reg. Rep. (CCH) ¶ 13,104 (1992).

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express statement in that section that "[s]upply substitution factors are considered . . . in the identification of firms that participate in the relevant market and the analysis of entry." Merger Guidelines § 1.0. The Merger Guidelines are thus entirely consistent with the Commission's conclusions. The Merger Guidelines, like the judicial precedents, are designed in the first instance to "assess whether the merger would significantly increase concentration and result in a concentrated market, properly defined and measured." Merger Guidelines § 0.2. Under decisions such as Rothery Storage, supply substitution leads to a broader market definition, and concentration is measured by all of the firms active in that broadly defined market.

Under the Merger Guidelines, in contrast, supply substitution generally is accounted for not when defining the market but when measuring concentration -- the more narrowly "defined" market is therefore deemed to include the sales of all firms that currently sell in the relevant market and "uncommitted entrants" that within one year would likely enter the relevant market in response to "a small but significant and nontransitory price increase." Merger Guidelines § 1.32.[27] Under either approach, the result is the same, and market concentration figures

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[27] But see id. § 1.321 n.14 (recognizing the accepted analytical approach of reflecting supply substitution in defining the relevant market and noting that "[i]f production substitution among a group of products is nearly universal among the firms selling one or more of those products . . . the Agency may use an aggregate description of those markets as a matter of convenience").

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account fully for supply substitution. Cf. Town Sound and Custom Tops, Inc., et al. v. Chrysler Motors Corp., 959 F.2d 468, 493 n.13 (3d Cir. 1992) (market definition "always involves the difficult task of line drawing, so that the two-step process of (1) market definition and (2) determination of market power therein is unavoidably somewhat artificial").[28]

SBC faults the Commission for not deferring to the Justice Department, which found a narrow market of cellular-originated interexchange service in its own investigation of the merger. SBC Brief at 14-15. But the Commission was not required to defer to the Department. As noted in the Order, the Commission and the Justice Department have concurrent and equal jurisdiction under the antitrust laws to consider acquisition matters involving communications common carriers.[29] Indeed, the Commission's special role and the expertise it has acquired with regard to communications suggests that its own market definition is the one warranting deference. More particularly with regard to this case, SBC does not explain why the Commission should have

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[28] The Commission thus found that the transfers necessary to effectuate the merger of AT&T and McCaw would present no competitive risks even if the market were defined as narrowly as SBC contends it should be. See Order, 9 FCC Rcd at 5847-48 (para. 15) (J.A. 1358-59).

[29] 9 FCC Rcd at 5844 (para. 9) (J.A. 1355), citing 15 U.S.C. § 21(a). In this case, the Commission chose not to consider the matter as an exercise of its Clayton Act powers because its authority to rule on applications to transfer licenses under the Communications Act was entirely adequate and, in fact, more flexible. Order, 9 FCC Rcd at 5843 (para. 7)(J.A. 1544).

deferred to the Department's finding, which was made without benefit of a public record, responsive pleadings, or the adversary procedures for finding facts that the Commission afforded. The Commission was not arbitrary or capricious in declining to follow the Justice Department's market definition.

Finally, SBC claims that even if the Commission correctly determined that the merger does not threaten existing competition, it failed adequately to account for the possibility that McCaw in the future might become a significant interexchange competitor. SBC Brief at 20-21. The Commission's responsibility is to deal with "probabilities," not "ephemeral possibilities." United States v. FCC, 652 F.2d at 99. And, contrary to the implication in SBC's brief, the Commission found that McCaw would not have had the capability to become a large-scale interexchange provider. Order, 9 FCC Rcd at 5856-57 (para. 30 n.73) (J.A. 1367-77).

II. THE FCC DID NOT ACT ARBITRARILY OR CAPRICIOUSLY IN DECLINING TO IMPOSE ADDITIONAL CONDITIONS.

In approving the license transfers, the FCC imposed several conditions on AT&T/McCaw. These included, inter alia, requirements that cellular and interexchange service be made available on an unbundled basis; that any bundled offerings be subject to pricing regulations to prevent certain forms of cross-subsidization and predatory pricing; that AT&T and McCaw comply with existing regulations governing the use of customer information and

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transactions between affiliates; and that AT&T not discriminate against McCaw's competitors in the provision of network equipment. Order, 9 FCC Rcd at 5928-30 (paras. 175-185) (J.A. 1339-41).

On appeal, SBC and BellSouth contend that the FCC acted arbitrarily in not imposing additional conditions relating to the use of customer information, proprietary BOC information, equal access, and bundling.

A. The FCC Reasonably Declined To Prohibit AT&T From Using Its Interexchange Customer Information To Market Cellular Service When The Customer In Question Has No Objection.

SBC contends that the FCC should have banned completely AT&T's use of its own interexchange customers' proprietary network information ("CPNI") to market other (e.g., cellular) services to those customers.[30] SBC Brief at 24-29. However, applying longstanding CPNI regulatory standards, the Commission allowed AT&T to use such information to market other services

[30] Contrary to SBC's suggestion (SBC Brief at 12, 24, 29), the CPNI at issue here does not involve proprietary information belonging to the BOCs, but rather information (e.g., customer lists) gathered from AT&T's own interexchange customers relating to their use of AT&T services. Moreover, unlike BOC CPNI -- which FCC rules allow the BOCs to use in some contexts to market their other services (see, e.g., Computer III Remand Proceedings, 6 FCC Rcd 7571, 7609-14 (paras. 84-89) (1991), aff'd in pertinent part, California v. FCC, 39 F.3d 919, 930-31 (9th Cir. 1994)) -- AT&T's CPNI does not come from monopoly operations, but is obtained because consumers have voluntarily chosen AT&T as their interexchange carrier from among competitive alternatives.

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unless its customers directed otherwise. Order, 9 FCC Rcd at 5885-86 (para. 83) (J.A. 1396-97). That decision was reasonable.

The CPNI standards that the Commission applied to AT&T/McCaw in this case are the culmination of nearly a decade of regulatory and court proceedings in which SBC and the other BOCs participated (and generally supported the FCC's decisions to allow the use of CPNI in marketing other services). Those regulations are designed to balance considerations of privacy, efficiency and competitive equity.[31] And, as applied to AT&T, those considerations have led to Commission rules that permit AT&T to use its customers' CPNI to market other products and services (e.g., enhanced services and customer premises equipment (CPE)) unless the customers ask that it not be used.[32] Here, as in the enhanced services and CPE contexts, the Commission concluded that the information/marketing advantages created by vertical integration -- including the ability to offer consumers "one-stop shopping" -- were a significant public benefit, which

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[31] See, e.g., Computer III Remand Proceedings, 6 FCC Rcd at 7609; Rules Governing Telephone Companies' Use of Customer Proprietary Network Information, Public Notice, 9 FCC Rcd 1685 (1994).

[32] See Furnishing of Customer Premises Equipment and Enhanced Services by American Telephone & Telegraph Company, 102 FCC 2d 655, 691-94 (1985); Amendment of Section 64.702 of the Commission's Rules and Regulations (Third Computer Inquiry), 104 FCC 2d 958, 1002-04, 1086-92 (1986), recon., 2 FCC Rcd 3035 and 2 FCC Rcd 3072, 3096-97 (1987), recon., 3 FCC Rcd 1150, 1161-65 (1988), further recon., 4 FCC Rcd 5927 (1989), vacated in other part, California v. FCC, 905 F.2d 1217 (9th Cir. 1990).

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would be undermined by the CPNI restrictions SBC urged. Order, 9 FCC Rcd at 5884-86 (paras. 81-83) (J.A. 1395-97).[33]

SBC disputes the connection between one-stop shopping and AT&T's ability to use its CPNI. SBC Brief at 27. The nexus, however, is clear. "One-stop shopping" results from allowing the carrier to employ an integrated marketing and sales force. Denying those who market complementary products access to CPNI, in effect, requires two sales forces within the same company. The Commission explained the connection in rejecting a less intrusive restriction on BOC use of CPNI in the enhanced services context:[34]

> [W]ithout the integrated marketing and sales made possible by our CPNI rules, if a customer called the telephone company to discuss basic network services, such as additional lines or call waiting, and then wanted merely to get information about an enhanced service, such as voice mail, he would have to be

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[33] See also 9 FCC Rcd at 5871-72 (para. 57) (J.A. 1382-83) ("The merger will allow McCaw to use AT&T's strong brand name and its marketing and sales force. Each of the applicants also will have an opportunity to cross-sell or bundle its service with the other's products and services.... As a result, we expect the AT&T/McCaw merger to lead to a broadened range of consumer choices, more price competition, an increased responsiveness to consumer needs and desires on the part of competing carriers and potential entrants, as well as incentives for continued technical and service innovations in the cellular service business."); Cal. Atty. Gen. Op., p.23 (J.A. 1221) ("There is little doubt that synergies between the applicants offer real potential for enhancing McCaw as a competitor in the provision of mobile telephone service.").

[34] The condition at issue in Computer III Remand, unlike the absolute ban SBC urged here for application to AT&T, would have allowed a BOC to share a customer's CPNI with the BOC's enhanced services marketing personnel if the BOC had obtained the customer's approval in advance.

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> transferred to a separate enhanced services representative.... With integrated marketing and sale, the BOC service representative receiving a call can also offer consumers additional choices that may better suit their needs, including combinations of basic and enhanced services.

Computer III Remand Proceedings, 6 FCC Rcd at 7610 (para. 85).[35]

SBC argues that the CPNI standards the Commission applied to AT&T/McCaw were promulgated in contexts that are not applicable here. It claims, for example, that the CPNI standards developed in the enhanced services and CPE contexts were intended to address services marketed to "large, sophisticated businesses that can take care of themselves," whereas many cellular customers are small businesses and individuals. SBC Brief at 28. The relevance of this claim -- assuming it to be correct -- is far from clear. SBC does not explain how its purportedly "smaller" cellular customers could be harmed by access to information about competing services.

SBC also claims that, unlike the enhanced services context, there is no market growth potential associated with allowing AT&T unrestricted use of the CPNI of AT&T's interexchange customers who already are customers of other cellular carriers. Rather, SBC asserts, the Commission has simply given AT&T license to raid SBC's cellular customers. SBC Brief at 29. AT&T presumably can

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[35] SBC's argument that its proposed CPNI restriction would not completely "prevent" one-stop shopping is beside the point. It certainly would "undercut" such marketing, which is why the Commission found the restriction contrary to the public interest. Order, 9 FCC Rcd at 5886 (para. 83) (J.A. 1397).

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lure customers away from SBC's cellular operations only by offering superior service or more attractive terms. Thus, if SBC loses cellular customers, it will be the result of competition on the merits. And to the extent that SBC and other cellular carriers are forced to compete more vigorously, consumers should benefit.

The courts have consistently recognized that capitalizing on informational efficiencies such as those permitted by the vertical integration of AT&T and McCaw is not the sort of conduct that harms competition. In Catlin v. Washington Energy Co., 791 F.2d 1343 (9th Cir. 1986), for example, a natural gas distribution monopolist, WNG, used its residential gas customer list to target advertising of its new "vent damper" products. WNG's vent damper competitors brought an antitrust suit, asserting that "WNG should be barred from permitting its merchandising division to use the list to advertise vent dampers to the detriment of competition in the vent damper market." 791 F.2d at 1345. The Ninth Circuit affirmed the district court's judgment in favor of WNG, noting that the plaintiffs had not "cited authority for the proposition that WNG has a duty to disclose its customer list or to bar its merchandising division from using it." 791 F.2d at 1348.[36] It is manifestly pro-competitive and

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[36] In defending against "competitive equity" challenges to the Commission's Computer III regulations that allow BOCs to use their CPNI to market "enhanced services," the BOCs, relied upon Catlin and "argue[d] that their access to CPNI is no different from an unregulated company's access to its customer records and

beneficial to consumers to allow a multi-product firm such as AT&T maximum freedom in offering its competitive services to all of its customers. See, e.g., Berkey Photo, Inc. v. Eastman Kodak Co., 603 F.2d 263, 273-75 (2d Cir. 1979), cert. denied, 444 U.S. 1093 (1980); Eastern Publishing and Advertising, Inc. v. Chesapeake Publishing and Advertising, Inc., 831 F.2d 488, 493 (4th Cir. 1987) ("the antitrust laws are inapposite here because the only damage is to Eastern as a competitor; there is no alleged injury to competition in the relevant market"), vacated and remanded on other grounds, 492 U.S. 913 (1989).

B. The FCC's Reliance On Existing Safeguards Backed By Competitive Pressures, The Threat Of Legal Sanctions, And Its Continuing Jurisdiction To Check Any Potential Misuse Of Cellular Carriers' Confidential Information Was Not Arbitrary or Capricious.

The affiliation of AT&T's business of manufacturing cellular network equipment and McCaw's business of providing cellular service is a "vertical" affiliation. The courts have held that vertical affiliations generally are pro-competitive and can create beneficial efficiencies that are not the result of market power.[37] The Commission so found with respect to the transfer below.

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should therefore be permitted." Computer III Remand Proceeding, 6 FCC Rcd at 7608.

[37] See, e.g., Tenneco Gas v. FERC, 969 F.2d 1187, 1200 (D.C. Cir. 1992), citing with approval Berkey Photo, Inc. v. Eastman Kodak Co., 603 F.2d at 276.

SBC raised a point before the Commission about the information that AT&T has obtained and AT&T/McCaw will obtain in its capacity as supplier of cellular network equipment to SBC (and other cellular companies). It claimed that, in those situations where SBC competes with McCaw and AT&T is SBC's supplier, AT&T would have an incentive to share such information with McCaw, which could use it to SBC's competitive disadvantage. SBC proposed regulations on the flow of such information within AT&T/McCaw, and it argues here that the Commission was arbitrary and capricious in failing to adopt its proposal. SBC Brief at 30-34.

The Commission declined to imposed the requirement, for good reasons. Order, 9 FCC Rcd at 5898 (paras. 112-113) (J.A. 1409). The Order's reasoning shows the Commission's understanding of competitive marketplace realities and its policy that, where marketplace factors can operate, detailed government regulation of daily business conduct is not required. The Order notes the following facts: (1) AT&T has years of experience with protecting the proprietary information of its equipment customers, and has protected the BOCs' information for years; (2) the BOCs, who account for 75 percent of AT&T's revenues from cellular network equipment sales, have enormous bargaining power over AT&T, and as sophisticated corporations they know (a) how to bargain for confidentiality clauses and (b) how to find other equipment

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suppliers if AT&T will not give them satisfactory protection;[38] and (3) it would be irrational for AT&T to leak BOC information to McCaw because new sales to the BOCs in AT&T's half-a-billion-dollar-a-year network equipment business would vanish overnight if it did so.[39] All these facts about the normal workings of the marketplace make it highly unlikely that AT&T/McCaw would misuse the BOC's proprietary information.

SBC notes that the Order does include a condition protecting the BOCs from abuse in the supply of equipment under existing contracts with AT&T/McCaw. SBC Brief at 32-33. SBC asks why the Order did not also impose a like condition to protect the BOCs' proprietary information supplied to AT&T/McCaw under those same contracts. There is a simple reason why the Commission drew a distinction, and protected the former and not the latter. In the former situation, before the transfer the BOCs had no reason to

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[38] Elsewhere, the Order notes the many other equipment suppliers in competition against AT&T in this country, and the many more in foreign countries who could enter the U.S. market. 9 FCC Rcd at 5868 (para. 51 & n.135) (J.A. 1379).

[39] 9 FCC Rcd at 5870-71 (para. 55) (J.A. 1381-82). See also AT&T-McCaw Opposition at 93-94 (J.A. 540-41). SBC claims that the money AT&T/McCaw might make by leaking the BOCs' information to McCaw for use in the cellular business would be more than it might lose in its equipment business. Such speculation, in the absence of evidence, has been rejected by the courts, and the Commission was right to reject it also. See Order, 9 FCC Rcd at 5869 (para. 52) (J.A. 1380), citing Matsushita Elec. Indus. Co. v. Zenith Radio Corp., 475 U.S. 574, 586-87 (1986) ("if the factual context renders respondents' claim implausible -- if the claim is one that simply makes no economic sense -- respondents must come forward with more persuasive evidence to support their claim than would otherwise be necessary.").

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fear that AT&T would favor McCaw over them in supplying equipment and thus had not accounted for that risk in their contracts. In the case of proprietary information, however, the BOCs have always guarded it against misuse by any outsider, including the pre-transfer AT&T. For example, an affiant on whom SBC relies stated: "All of the [network equipment] contracts contain some protections regarding the use of information obtained by AT&T in its role as vendor . . . . These provisions typically require that such information be used only for the purpose of the contract." Bell Atlantic Petition, Affidavit of Mr. Lynch, ¶ 44 (J.A. 33-34). Accordingly, no additional regulatory protection was needed in the case of proprietary information.

In light of these realities, the Commission can better serve the public interest by making its complaint procedures available to the BOCs for any abuse by AT&T/McCaw, and by not imposing detailed regulatory conditions that would require constant application and revision in a dynamic business. Courts properly defer to regulatory agencies in making such predictions about likely future events in regulated industries.[40] In this as in

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[40] See, e.g., FCC v. WNCN Listeners Guild, 450 U.S. at 596 (affirming FCC decision to rely on market forces to accommodate changing tastes of listeners and noting that "[t]hese predictions are within the institutional competence of the Commission"). Declining to impose burdensome regulations until there is at least some evidence of a problem is eminently reasonable. See, e.g., United States v. FCC, 652 F.2d at 104-05 ("continuing supervision" by FCC may accomplish "the same end" as detailed regulation, where serious anticompetitive effects, if they arise at all, will do so only in the future).

other respects, the Order created only the protections that the future marketplace will likely require. In so doing, the Commission spared the industry (and consumers) the intrusive regulatory protection for which SBC had pleaded.[41]

C. The Remaining Conditions Proposed by BellSouth Were Likewise Unwarranted.

BellSouth also contends that the FCC acted arbitrarily in not imposing two additional conditions. First, BellSouth argues that the FCC should have imposed equal access obligations on AT&T. The Commission expressly addressed the issue of equal access and declined, for the moment and in the Order here under review, to impose it on AT&T/McCaw. The Commission did so because it has not imposed an equal access obligation on any cellular carrier and because there is a pending rulemaking in which the Commission is considering whether to require all cellular carriers (and certain other radio carriers) to provide equal access. Order, 9 FCC Rcd at 5876-78 (paras. 68-70) (J.A. 1387-88). In the meantime, AT&T/McCaw is implementing equal access pursuant to commitments made to Congress and to the Justice Department. The Order noted these commitments and expressly stated the expectation that AT&T/McCaw will honor them. 9 FCC

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[41] The Commission did not forever close the door to parties' raising legitimate CPNI confidentiality concerns. To the contrary, the FCC recognized that any cellular carrier who "could prove that AT&T/McCaw misappropriated CPNI or misused such information entrusted to it ... would have a remedy through the Commission complaint process." Order, 9 FCC Rcd at 5886 (para. 83) (J.A. 1397). See United States v. FCC, 652 F.2d 104-05.

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Rcd at 5877-78 (paras. 69-70) (J.A. 1388-89). The Commission thus decided reasonably to defer the issue to the pending rulemaking.

There is no substance to BellSouth's claim (Brief at 15-16) that the FCC's decision to defer the issue to rulemaking is inconsistent with AT&T v. FCC, 978 F.2d 727 (D.C. Cir. 1992). The Court in that case held that the Commission could not dismiss a complaint alleging that a carrier had acted unlawfully by deferring the legal issues the complaint had raised to a future rulemaking. The Court held that the FCC had a statutory responsibility under 47 U.S.C. §§ 206-208 to adjudicate the complaint under "the law currently applicable." 978 F.2d at 732. Here, there was no claim of past unlawful acts by AT&T, and no filed complaint. Instead, the FCC determined that the license transfers would advance the public interest, deferring to a rulemaking only the policy question of whether additional equal access conditions should be imposed on the industry as a whole. The Commission expressly conditioned the grant on compliance with whatever rules emerged from that rulemaking. Order, 9 FCC Rcd at 5930 (para. 185) (J.A. 1441).

It is well established that regulators, and this Commission specifically, have discretion to proceed either by rulemaking or by adjudication. E.g., Southern Bell Tel. & Tel. Co. v. FCC, 781 F.2d 209, 216 n.8 (D.C. Cir. 1986). This Court repeatedly has affirmed Commission decisions to defer issues that arise in adjudications because they are more appropriate for rulemakings.

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E.g., National Organization for Women v. FCC, 555 F.2d 1002, 1011 (D.C. Cir. 1977). The reasons for this judicial deference are sound and are present in this case: An adjudication now about the desirability of equal access for AT&T/McCaw could, in light of the pending rulemaking, needlessly burden the Commission with duplicative proceedings and could result in piecemeal decisionmaking about an issue of industry-wide and national scope, which is better addressed and resolved in a rulemaking.

BellSouth's brief argument that the FCC should have imposed more stringent restrictions on bundling is both academic and baseless. It is academic because, as with equal access, AT&T has agreed to comply with the Justice Department's proposed restrictions on bundling, and those requirements satisfy all concerns BellSouth has expressed. It is baseless because the FCC found that bundling brings customers the benefits of innovative rate structures and lower prices, and BellSouth has presented no grounds below or here to doubt that conclusion. See Order, 9 FCC Rcd at 5879-82 (paras. 73-78) (J.A. 1390-93). BellSouth's only argument on appeal is that the MFJ prohibits BellSouth from providing bundled offerings, and the FCC reasonably concluded that this provided no basis for denying the public the pro-consumer benefits of the license transfers. 9 FCC Rcd at 5879-80 (para. 74) (J.A. 1390-91).

III. APPELLANTS' PROCEDURAL OBJECTIONS ARE MERITLESS.

Finally, appellants raise three procedural objections to the Order. BellSouth contends that the Commission was obligated (a)

to hold a trial-type hearing, and (b) to order AT&T and McCaw to produce to the FCC staff other documents in addition to the tens of thousands of pages of documents that it did order. SBC contends that the Commission should have waived the requirements of the protective order pursuant to which those documents were produced in order to permit SBC to use those documents in separate litigation involving AT&T.

A. An Evidentiary Hearing Was Not Required.

This Court's cases are clear that "the decision of whether or not hearings are necessary or desirable is a matter in which the Commission's discretion is paramount." Gencom Inc. v. FCC, 832 F.2d 171, 181 (D.C. Cir. 1987) (quoting United States v. FCC, 652 F.2d at 91). "Review of that determination is particularly deferential," in part "because Congress intended to vest in the FCC a large discretion to avoid time consuming hearings whenever possible." Citizens for Jazz on WRVR v. FCC, 775 F.2d 392, 398 (D.C. Cir. 1985) (emphasis added).

In order to be entitled to a hearing under 47 U.S.C. § 309, a party must satisfy two threshold requirements. First, it must file a petition to deny setting forth "specific allegations of fact sufficient to show that ... a grant of the application would be prima facie inconsistent with the public interest." Gencom, 832 F.2d at 180 (citation omitted). Where a party merely alleges "ultimate, conclusionary facts . . . supported by general affidavits," or where its allegations, even if true, would not contravene the elements of the public interest defined by the FCC, it

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is not entitled to a hearing. See California Public Broadcasting Forum v. FCC, 752 F.2d 670, 674, 680-81 (D.C. Cir. 1985) (citation omitted).

Second, "the application, the pleadings filed, or other matters which the Commission may officially notice" must present "a substantial and material question of fact." Gencom, 832 F.2d at 181. In applying that test, the Commission "must consider not only petitioner's evidence, but it must also weigh that evidence against the facts offered in rebuttal." Id. The Commission "may draw factual and legal inference from undisputed evidentiary facts, and it may determine how much weight to accord disputed facts on the record before it." Id. A hearing is required only if "the totality of the evidence arouses a sufficient doubt on the point that further inquiry is called for." Id.

None of BellSouth's claimed "hearing" issues satisfies these standards. Indeed, all of them were either immaterial to the Commission's public interest determination, or represented precisely the sort of "legal and economic conclusions concerning market structure, competitive effect, and public interest" that may be resolved on a written record and "manifestly do not" require a live hearing. United States v. FCC, 652 F.2d at 89-90.

This is plain from BellSouth's list of purported factual disputes. BellSouth Brief at 22. Most of the items on that list involved claims that the Commission found were immaterial to its conclusion that the license transfers were in the public interest, such as those relating to the MFJ, AT&T's precise plans

for implementing equal access, or AT&T's use of AT&T customer lists to market cellular service. The remainder merely involved generalized economic analyses about the competitive effects of the merger, for which live testimony would not have improved upon the written record.

Those deficiencies are fatal to BellSouth's claim that it was entitled to a hearing on various issues of market definition. First, BellSouth's contention that the transaction should have been examined in the context of the purported "market" for the "integrated nationwide provision of interexchange and exchange telecommunications services," which it asserted would be "a non-competitive market after the merger," did not warrant a hearing. BellSouth Brief at 24-25. BellSouth's argument was that any such integration by AT&T and McCaw would be contrary to the public interest because it would promote local exchange competition and because that competition would be unfair in light of the MFJ's prohibition on similar integration by the RBOCs. However, the Commission determined that local exchange competition was a public interest <u>benefit</u>, not a <u>detriment</u>, and that the existence of the MFJ was not a reason to deny consumers the benefits of these license transfers. The "facts" BellSouth asserted, even if accepted, did not make out a <u>prima facie</u> case that the transfers was contrary to the public interest.

Second, BellSouth's claim that the geographical scope of the cellular market was national likewise did not require a hearing. As BellSouth conceded below, this issue was relevant only to its

argument that the Commission should require that the MFJ be vacated before approving the license transfer. BellSouth Reply, p. 36 (J.A. 858). It therefore was immaterial to the FCC's public interest determination.

BellSouth never refuted, or even addressed, the critical fact that cellular carriers are licensed locally and that customers only choose from among those carriers providing service in their local areas. Instead, it contended that because roaming and handoff arrangements make it possible for carriers to offer national coverage, the market itself must be national. This contention presents no "substantial" question for hearing. The scope of service coverage does not alter a consumer's range of alternatives, which can only include cellular companies that operate locally, as the Commission found on an adequate record. That McCaw has discussed and AT&T may in the future offer a nationwide cellular service is not to the contrary.

Third, the FCC properly did not hold a hearing on allegations that the transfers would have anticompetitive horizontal effects. BellSouth Brief at 26. Given the undisputed ease of entry by other interexchange carriers, BellSouth's assertion of a separate cellular interexchange market raised no substantial and material question of disputed fact regarding any alleged anticompetitive effect as a consequence of the transaction.[42] The

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[42] The Commission also made clear that it would continue to monitor the cellular marketplace in general and the combined offerings of the new AT&T/McCaw. Order, 9 FCC Rcd at 5843 (para.

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Commission followed procedures that were appropriate to its task.

B. The FCC Acted Within Its Discretion In Deciding Which Documents To Review.

BellSouth contends that the Commission should have ordered AT&T and McCaw to produce additional documents. As it was, the FCC staff reviewed voluminous comments and affidavits filed by BellSouth, AT&T, and other parties. It then identified 40 document requests and interrogatories from the discovery sought by the Justice Department in the related Hart-Scott-Rodino proceeding that it believed would be helpful to its task here. After ordering AT&T and McCaw to produce its responses to those document requests and interrogatories, the FCC staff reviewed that production, which numbered in the tens of thousands of pages. See Order, 9 FCC Rcd at 5921-22 (paras. 157-158) (J.A. 1432-33).

Although the Commission as a matter of discretion in this case permitted the other parties to review those materials and to file additional comments addressing them, the Communications Act provides no discovery rights to parties that object to license transfer applications. The documents were ordered produced because the FCC staff determined that they could be useful in the agency's determination of whether the transfers would serve the public interest. In ordering their production, the staff stated that its examination of Hart-Scott-Rodino documents would be

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7), 5873 (para. 61) (J.A. 1384). Such a commitment is properly a factor in a decision not to hold a hearing. Cf. United States v. FCC, 652 F.2d at 104-05.

"limited" to the designated information, that it reserved the right to seek additional such information, but that requests by private parties to expand the scope of production "will not be entertained in the absence of extraordinary circumstances and a specific factual showing that good cause exists for delaying the Commission's decision in this matter." Letter from G. Weiss, acting chief of the Common Carrier Bureau's Enforcement Division, to Francine J. Berry, et al. (May 26, 1994) at p.2 (J.A. 1192).

Less than two weeks later, BellSouth requested that AT&T and McCaw be ordered to produce the entirety of the Hart-Scott-Rodino materials that already had been reviewed by the Justice Department -- literally millions of pages of additional documents. The FCC properly rejected BellSouth's request.

The Act grants the FCC broad discretion in determining what information it will review. See 47 U.S.C. §§ 308(a), 309(b). BellSouth claims that additional documents might have been "relevant" to the merger. But the FCC is not obligated to review every document that is arguably "relevant" to an application. This Court held in United States v. FCC that when the Commission fashions procedures concerning a proposed new business venture, it may take account of the fact that lengthy proceedings can be "a potent instrument for delay," will necessarily postpone any benefits from the venture, and may even kill it in the capital markets. 652 F.2d at 91, 95-96. The FCC need only obtain "sufficient information to make an informed decision," and the scope of judicial review of its "information-gathering process"

is "quite narrow." Bilingual Bicultural Coalition v. FCC, 595 F.2d 621, 630-31 (D.C. Cir. 1978).[43]

Here, having obtained access to the documents that appeared most pertinent, and recognizing that the Justice Department -- which had had access to all the documents -- had conditionally approved the merger, the Commission reasonably concluded that further discovery of the Hart-Scott-Rodino documents would serve no useful purpose. Order, 9 FCC Rcd at 5921-22 (paras. 157-158) (J.A. 1432-33). Indeed, there was reason to believe that the delay such additional discovery would create ultimately might deprive the public of the benefits of the transfers.[44]

C. The FCC Properly Declined To Waive The Protective Order Under Which The Documents Had Been Produced.

The Commission's order requiring AT&T and McCaw to produce the Hart-Scott-Rodino documents and permitting the BOCs and other parties to inspect them was accompanied by a stringent protective

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[43] BellSouth notes that the Commission passed over some documents that AT&T also regarded as relevant. BellSouth Brief at 5. But the Commission is not bound by AT&T's view of the need to consider documents, any more than it is bound by BellSouth's view. The Commission need only obtain "sufficient information to make an informed decision." Bilingual Bicultural Coalition v. FCC, 595 F.2d at 631. Cf. Rule 43, Federal Rules of Evidence, which states that proferred evidence, even if it relevant, may be refused if "its probative value is substantially outweighed ... by considerations of undue delay [or] waste of time...."

[44] McCaw had advised the Commission that if, by September 30, 1994, it did not have financing from AT&T, it would have to cancel the merger and pursue other financing. See Opposition of AT&T and McCaw to BellSouth's Emergency Motion for Temporary Stay, Supplemental Affidavit of Wayne M. Perry (J.A. 1460).

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order. Protective Order, 9 FCC Rcd 2613 (J.A. 1171). That protective order explicitly barred the use of these documents in any other proceeding:

> Persons obtaining access to stamped confidential documents under this order shall use the information only for preparation and the conduct of this proceeding and any subsequent judicial proceeding, and shall not use such information for any other purpose, including business, governmental, commercial, or other administrative or judicial proceedings.

9 FCC Rcd at 2616 (J.A. 1174).

Less than a month after being granted access to review the documents under those terms, SBC sought a wholesale waiver. It requested permission to submit to the district court with responsibility for the MFJ its comments on the documents, along with a multi-volume appendix consisting of hundreds of pages from the documents themselves. It claimed that those documents would be useful in that Court's generic wireless proceeding. The Commission denied the request, finding that such disclosure was both unnecessary and contrary to the clear expectations of the parties. The Commission pointed out that the prospect of such disclosure would have interrupted the proceedings before the agency and would inhibit the use of such measures in future proceedings. Order, 9 FCC Rcd at 5925 (paras. 167-168) (J.A. 1436).

Applications of agency confidentiality procedures in a protective order are made pursuant to the agency's broad discretion. See FTC v. Owens-Corning Fiberglass Corp., 626 F.2d 966, 974 (D.C. Cir. 1980); FTC v. Texaco, Inc., 555 F.2d 862, 884 n.62

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(D.C. Cir. 1977) (en banc). Here, the FCC acted well within its discretion in rejecting SBC's request.

SBC did not seek a narrowly targeted waiver of the protective order or ask for an isolated exception. Instead, it sought a comprehensive removal of the central confidentiality provision for all such documents. If the Commission had granted that waiver, the practical effect would have been to convert this license transfer proceeding into an opportunity for parties to conduct non-reciprocal discovery against a party in support of separate litigation. This would have violated not only the letter but also the spirit of the protective order.

Moreover, all of these documents already were in the possession of the Justice Department, which has principal responsibility for government factfinding in MFJ matters and statutory authority to disclose them to the MFJ court if it believes such disclosure to be relevant to any judicial proceeding there. Although the Justice Department has supported the BOCs' motion for generic wireless relief (subject to certain additional conditions), it has not disclosed the documents SBC has identified to the MFJ court.

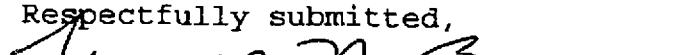
The Commission has a strong interest in maintaining the integrity of its confidentiality procedures. A party can always claim -- as SBC did here -- that submission of documents under seal to a court will not injure another party's legitimate competitive interests. But if that claim were sufficient, any Commission proceeding in which documents are produced would

become an opportunity for non-reciprocal discovery for the benefit of unrelated litigation. The voluminous document production in this proceeding was accomplished expeditiously precisely because the parties were confident that the Commission would enforce the terms and spirit of the protective order and did not feel the need to engage in extensive pre-production litigation. See Order, 9 FCC Rcd at 5925 (para. 167) (J.A. 1436). If the Commission had held (or if this Court holds now) that an opposing party can obtain access to confidential documents on those terms and then make use of the documents in separate litigation simply because it views the documents as "relevant" and promises to submit them under seal, the Commission's ability to implement such procedures in the future may be severely compromised.

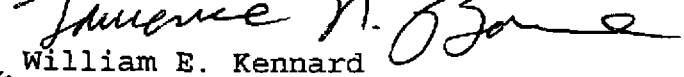
CONCLUSION

For the foregoing reasons, the decision of the FCC should be affirmed.

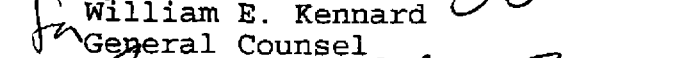
Respectfully submitted,



for William E. Kennard
General Counsel



for Christopher J. Wright
Deputy General Counsel



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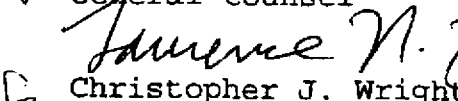
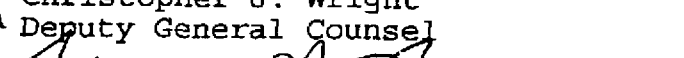
Associate General Counsel



John E. Ingle
Deputy Associate General Counsel



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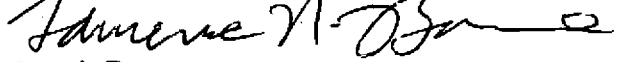

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February 13, 1995

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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

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In the Matter of	)	
American Telephone and Telegraph Company	)	
and	)	File No. ENF-93-44
McCaw Cellular Communications, Inc.	)	DA 93-1119
Applications for Consent to Transfer of Control of Radio Licenses	)	

AT&T'S AND McCAW'S OPPOSITION
TO PETITIONS FOR RECONSIDERATION

AT&T Corp. ("AT&T") and McCaw Cellular Communications, Inc. ("McCaw") hereby oppose the petitions for reconsideration filed by Allnet Communication Services, Inc. ("Allnet Petition") and by NYNEX Corporation and Bell Atlantic Corporation ("NYNEX/Bell Atlantic Petition"). Each petition repeats arguments that the Commission's decision fully considered and correctly rejected.

BACKGROUND

On September 19, 1994, the Commission issued its Memorandum Opinion and Order ("Order") in which it concluded under Section 310(d) of the Communications Act that "the public interest, convenience, and necessity will be served" by the transfer of McCaw's radio licenses to AT&T, subject to specified conditions. Order, ¶ 174. These conditions include a prohibition on AT&T's providing proprietary manufacturing services and products to McCaw on terms more favorable than those afforded to other cellular carriers (id., ¶ 105), the imposition of a price floor on bundles of local cellular and long-distance service (id., ¶ 78), and

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requirement that AT&T/McCaw cellular personnel follow the same Customer Proprietary Network Information ("CPNI") rules that apply to AT&T's marketing of customer premises equipment ("CPE") and enhanced services (id., ¶ 83).

At the same time, the Commission properly rejected the more draconian conditions requested by some parties that would have undercut or eliminated the public benefits and legitimate efficiencies of the AT&T-McCaw merger. For example, the Commission rejected the proposal by several Bell Operating Companies ("BOCs") that AT&T should not be allowed to disclose to McCaw the CPNI of AT&T's long-distance customers. The Commission stated that the prohibition proposed by the BOCs "would undercut one of the benefits of the AT&T/McCaw combination: the ability of AT&T/McCaw to offer its customers the ability to engage in 'one-stop shopping' for their telecommunications needs." Id.

The Commission was similarly "not persuaded by [several] petitioners that [it] should impose equal access requirements as a condition of [its] approval of the proposed merger." Id., ¶ 70. The Commission stated that cellular equal access was a policy matter that would be resolved on a comprehensive basis in a pending cellular rulemaking and need not be determined in this license transfer proceeding. See id. The Commission also noted that AT&T/McCaw had already made commitments to Congress and the Commission to provide equal access as set forth in a proposed settlement agreement with the Justice Department that was already being complied with. See id., ¶¶ 69, 70.

ARGUMENT

The two petitions for reconsideration rehash the same arguments that the Commission rejected in its Order.[1] Each should be denied.

I. NYNEX/BELL ATLANTIC'S ARGUMENT CONCERNING AT&T'S USE OF CUSTOMER INFORMATION IS BOTH IMPROPER AND INCONSISTENT WITH THE COMMISSION'S ESTABLISHED POLICIES.

NYNEX/Bell Atlantic request that the Commission reconsider its Order insofar as it "allow[s] AT&T to provide McCaw with the names, addresses and other . . . CPNI . . . of BOC cellular customers that have chosen AT&T as their presubscribed carrier for cellular long-distance calls, or otherwise permit[s] such CPNI to be used by McCaw or its sales agents to compete for cellular sales." NYNEX/Bell Atlantic Petition, pp. 1-2. NYNEX/Bell Atlantic assert (1) that the Commission's Order allows appropriation of "trade secrets" of BOC cellular carriers (id., p. 6), (2) that it will irreparably harm them if AT&T/McCaw can market cellular services to AT&T long-distance customers who also subscribe to NYNEX/Bell Atlantic cellular services (id., p. 7), and (3) that the Commission erroneously concluded that AT&T interexchange service customers benefit when they are afforded the option of using other AT&T services or products (id., p. 8).

These are the same contentions that the Commission correctly rejected not only in the Order, but also in its prior CPE

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[1] Two appeals have also been filed (one by BellSouth and the other by Southwestern Bell). These have been consolidated, with Southwestern Bell Corp. v. FCC, No. 94-1637 (D.C. Cir.), as the lead docket.

and Enhanced Services decisions.[2] While NYNEX/Bell Atlantic are now making even more naked protectionist pleas to prevent competition for the business of their existing customers, the only new argument petitioners make is an improper and erroneous one.[3]

First, NYNEX/Bell Atlantic's claims all rest on the false premise that the Order allows AT&T/McCaw to use cellular carriers' customer lists and customer usage information, which NYNEX/Bell Atlantic analogize to intellectual property akin to trade secrets or patents. See NYNEX/Bell Atlantic Petition, p. 3. But this is incorrect. AT&T has not obtained and does not have access to the BOCs' lists of cellular customers' names and addresses or to cellular usage information of BOC customers.[4] Rather, the

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[2] See Third Computer Inquiry, 104 F.C.C.2d 958, 1002-04 (1986), recon., 2 FCC Rcd. 3035, 3042 & 2 FCC Rcd. 3072, 3097 (1987), recon., 3 FCC Rcd. 1150, 1161-65 (1988), further recon., 4 FCC Rcd. 5927 (1989), vacated in other part California v. FCC, 905 F.2d 1217 (9th Cir. 1990); Furnishing of CPE and Enhanced Services by AT&T, 102 F.C.C.2d 655, 679-81, 692-94 (1985); see also AT&T's and McCaw's Opposition to Petitions to Deny and Reply to Comments, pp. 81-84 (Dec. 2, 1993).

[3] In particular, petitioners have violated the terms of a court order in stating that "AT&T has agreed not to provide McCaw with cellular customer CPNI pending the outcome of a lawsuit brought by NYNEX and Bell Atlantic" in the Eastern District of New York. NYNEX/Bell Atlantic Petition, p. 2 n.2. The consent order to which NYNEX/Bell Atlantic refer provides that "nothing in this Stipulation and Order shall be admissible or used in any form in any other proceeding." Bell Atlantic v. AT&T, No. CV 94-3682 (ERK), p. 4 (Sept. 14, 1994 E.D.N.Y.) (emphasis added). The statement is also inaccurate, for AT&T/McCaw there agreed to refrain from using CPNI of customers who are also Bell Atlantic and NYNEX customers only through December 31, 1994 -- in exchange for NYNEX's and Bell Atlantic's agreeing to abandon their attempts to obtain a preliminary injunction or other relief against closing of the merger. See id., pp. 1, 4.

[4] In this regard, NYNEX/Bell Atlantic miss the point when they state, correctly, that complete cellular customer lists are not currently turned over to interexchange carriers. See Petition, pp.

information at issue consists of names and addresses of individuals who are AT&T's long-distance customers and their long-distance usage information. AT&T has this information about individuals who are also cellular customers because these individuals (1) have freely presubscribed to AT&T's long-distance service from their cellular (and generally also their landline) phones, or (2) have, in many cases, also obtained cellular CPE, other CPE, the AT&T Universal Card, or other products and services from AT&T.

Further, the Commission has long recognized that it is the customer, not carriers, who should determine whether and to what extent an interexchange customer's CPNI may be used in marketing other products or services to that customer, and NYNEX/Bell Atlantic are wrong in suggesting that the Commission has ever concluded otherwise.[5] Indeed, the Commission's Order merely requires that "AT&T/McCaw cellular services personnel must follow the same CPNI rules that currently apply to AT&T's marketing of CPE and enhanced services." Order, ¶ 83 (emphasis added). Under these rules, "AT&T must, upon the (interexchange) customer's request: (1) make the customer's CPNI available to competing CPE suppliers;

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[4] (...continued)
4-5. Contrary to the misimpression petitioners seek to create, the Order does not contemplate, much less require, such action by BOCs.

[5] NYNEX/Bell Atlantic now claim (Petition, pp. 5-6) that their former tariffs had prohibited each interexchange carrier from marketing other services or products to the cellular customers who presubscribed to the interexchange carrier's services. Although AT&T does not so read the tariffs, the short answer to NYNEX/Bell Atlantic is that these are carrier-initiated tariffs that the Commission never found lawful and that the tariffs would have been contrary to Commission policies and unlawful if they had the meaning now ascribed to them. In any event, because the Commission has ordered cancellation of the tariffs, the [illegible]

and (2) prohibit personnel who are involved in CPE and enhanced services marketing from gaining access to that customer's CPNI." Id.

These rules otherwise allow AT&T to use its customers' CPNI in marketing products or services, for the Commission found that because AT&T's interexchange customers have chosen to obtain products or long-distance service from AT&T in competitive markets, they generally will value the ability to receive information about other AT&T offerings. See p. 4 n.2, supra. In this regard, NYNEX/Bell Atlantic miss the point in noting (Petition, pp. 8-10) that the information about AT&T's long-distance customers would here be used not in marketing long-distance service, but in marketing other products or services to those customers. That was the case in the prior CPE and Enhanced Services orders, and it is receipt of information about other offerings that creates the consumer benefits that the Commission has now found in three separate orders.

Second, there is no substance to the NYNEX/Bell Atlantic claim (Petition, pp. 7-8) that AT&T/McCaw's use of AT&T's CPNI would irreparably harm petitioners' cellular businesses and that the Commission "must therefore prohibit" it. Such protectionist claims have been rejected by the Commission in three separate orders, were recently apparently rejected by the Court of Appeals,[6]

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[6] BellSouth recently sought a stay and other interim relief against this aspect of the Commission's Order pending appeal. The D.C. Circuit rejected this claim and held that BellSouth not only had failed to demonstrate "the requisite irreparable injury" but also had not shown the "likelihood of success on the merits to warrant" this relief. See Southwestern Bell Corp. v. FCC, No. 94-1637, Order, p. 1 (D.C. Cir. Oct. 18, 1994).

and reduce to astonishing claims that NYNEX/Bell Atlantic should be immunized from competition that benefits consumers.

The basic fallacy of petitioners' argument is that they are complaining about legitimate competition on the merits. In this respect, courts have uniformly agreed with the Commission's three prior decisions. Courts hold that it is pro-competitive and beneficial to customers for multi-product firms to offer each of their competitive products to each of their customers -- and restrictions on the ability of integrated firms to do so are anticompetitive. See, e.g., Berkey Photo, Inc. v. Eastman Kodak Co., 603 F.2d 263, 273-75 (2d Cir. 1979).

Conversely, NYNEX/Bell Atlantic are seeking to prevent competition for the business of their existing customers. What they fear is that their customers will find the AT&T/McCaw cellular offering -- and the prospect of "one-stop shopping" -- attractive. However, if customers do, the only legitimate response is for NYNEX/Bell Atlantic to reduce their prices, improve the quality of their services, or otherwise make their offerings more attractive. That is the competition that benefits consumers. By contrast, it harms consumers to prevent AT&T/McCaw from marketing services to existing customers of AT&T's other services or products or to prevent these customers from changing cellular carriers -- which is all NYNEX/Bell Atlantic ultimately seek.[7]

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[7] Contrary to their implication, NYNEX/Bell Atlantic have available, and have used, ample means of assuring that they recover marketing investments made to attract particular customers. NYNEX/Bell Atlantic refer (Petition, p. 7) to the fact that, in addition to general advertising, they often pay sale agents or offer discounted CPE to attract customers. They ignore, however, (continued...)

In this regard, it is noteworthy that Bell Atlantic and NYNEX make the astonishing assertion (Petition, p. 7) that they will otherwise "lose 10 to 25% of their existing customers in the first year" due to the "power of the AT&T/McCaw brand, the offering of packaged cellular and interexchange services, and other marketing advantages enjoyed by AT&T/McCaw." These predictions strain credulity. However, here, too, the complete answer to NYNEX/Bell Atlantic is that they have it in their power to retain their customers by strengthening their own brands, improving their own services, or otherwise making their offerings more attractive. The public interest will be advanced if the Order leads NYNEX and Bell Atlantic to seek to do so.

Third, there is no substance to the claim that AT&T/McCaw should offer "one-stop shopping" or other benefits only to "new" cellular customers and not to "existing" cellular customers. See NYNEX/Bell Atlantic Petition, pp. 8-9. To the extent customers value obtaining cellular as well as interexchange services from AT&T, there is no distinction between "new" and "existing" customers.

Finally, the NYNEX/Bell Atlantic Petition underscores that the prohibition that petitioners seek would have little practical effect other than creating opportunities for "vexatious litigation." Compare Order, ¶ 82. NYNEX/Bell Atlantic have conceded that "most customers that use AT&T for long-distance

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[1] (...continued)
that these cellular carrier "investments" are recouped by requiring term commitments from customers and agents. See Bundling of Cellular CPE and Cellular Service, 7 FCC Rcd. 4028, 4030 (1992)

cellular service also use AT&T for landline long-distance service" (Petition, p. 9), and the reality is that large customers generally (and small customers increasingly) subscribe to a single long-distance service (e.g., SDN, Tariff 12, or a residential or small business plan) for their cellular-originated and landline-originated calls alike. Because no basis has even been suggested for restricting AT&T/McCaw's use of CPNI of landline interexchange customers in marketing their cellular services, NYNEX/Bell Atlantic's proposal could likely lead only to endless disputes about the source of information used by AT&T/McCaw marketing personnel.

II. ALLNET SEEKS CONDITIONS INCONSISTENT WITH THE COMMISSION'S ORDER.

Allnet seeks reconsideration of the Order on a different ground. While Allnet purports to request that the Commission "clarify" certain requirements concerning equal access, unbundling, and structural separation, Allnet effectively concedes (Petition, p. 7) that it is asking that all the provisions of the proposed consent decree in United States v. AT&T and McCaw, No. 94-CV-1555 (D.D.C.), be independently imposed by the Commission as well.

However, these, too, are claims that the Commission considered and rejected. In the prior proceedings, AT&T noted that it had made equal access commitments to Congress, and those commitments (which AT&T reiterated to the Commission) are discussed in the Order (¶¶ 69-70). The provisions in the proposed consent decree also include bundling and other restrictions that go beyond these AT&T commitments and that were insisted upon by the Justice Department. The Commission stated in its Order that it did not

agree with the Department of Justice that each of these restrictions was necessary or appropriate. See Order, ¶¶ 68, 75.

Against this background, there is no basis for the Commission independently to impose the provisions of the proposed decree. Indeed, the Commission would then be imposing conditions that it has found to be inappropriate, but that nonetheless would apply to AT&T-McCaw even if the anti-bundling provisions of the consent decree were not adopted or were hereafter vacated. That would be especially inappropriate because, regardless of what occurs in the District Court, these and other issues would still then be reconsidered by the Commission in the pending CMRS Notice rulemaking, because "AT&T/McCaw cellular companies shall comply with any equal access rules that the Commission may [later] adopt in the CMRS Notice proceeding" (Order, ¶ 185; see also id., ¶ 174), and because AT&T-McCaw will, in all events, comply with the precise equal access commitments that AT&T made to the Commission and Congress, pending any further action by the Commission.

CONCLUSION

For the reasons stated, the petitions for reconsideration should be denied.

Respectfully submitted,

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November 2, 1994

Certificate of Service

I, Thomas P. Van Wazer, hereby certify that on this 2nd day of November, 1994, copies of the foregoing AT&T's and McCaw's Opposition to Petitions for Reconsideration were served by first class mail on the following:

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File No. ..... Initials ..... KS
Proceeding ..... CC 96-115
Assigned To ..... WT Docket

USWEST

December 2, 1996

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96-162

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Re: CC Docket No. 96-115, Customer Proprietary Network Information ("CPNI") and WT Docket No. 96-162, Commercial Mobile Radio Services ("CMRS")

Dear Mr. Kehoe and Ms. Brinkmann:

On November 19, 1996, U S WEST Communications, Inc. ("U S WEST") made an *ex parte* contact with the Wireless Telecommunications Bureau. Much of the content of that contact focused on the particulars of the potential arrangements between telephone carriers and their wireless operations. However, some of the discussion focused on CPNI, particularly the types of products and services that could benefit from internal CPNI use and the role and scope of "implied consent" within the context of internal corporate sharing and use of CPNI. Questions were also raised about the scope of the written consent provision of Section 222(c)(2) of the Telecommunications Act of 1996.[1]

[1] Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (1996) ("1996 Act" or "Act").

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U S WEST wishes to go on record with our response to these issues.

Section 222(c)(2)

With respect to Section 222(c)(2), the observation was made by Staff that the provision did not seem one that prohibited the transfer of CPNI to third parties without written approval, but one that -- rather -- simply imposed an obligation on telecommunications carriers when a certain event occurred to respond with a specific action (i.e., to release information to a person designated by a customer, upon receipt of a written customer request). The Section can certainly be read, as a literal matter, to be circumscribed in the way suggested by the Staff. When read literally, Section 222(c)(2) can be viewed as imposing on all telecommunications carriers an obligation similar to that already imposed on Bell Operating Companies ("BOC") pursuant to the Federal Communications Commission's ("Commission") Open Network Architecture ("ONA") CPNI regime, i.e., the obligation to release commercially valuable customer information when requested to do so in writing by an individual reflected in the records.

However, a broader reading of the Section is possible and generally comports with existing business practices of most local exchange carriers ("LEC"), we believe. Section 222(c)(2) can be read to reflect a Congressional recognition that individuals recognize and appreciate that there is a different relationship between themselves and those businesses with which they have an existing business relationship and those with which they do not. With respect to the former, information access and use should not be encumbered by a "written consent" requirement; with respect to the latter, and the protection of the individual's privacy expectations, a written instrument authorizing the release of information should not be deemed unexpected or unwarranted.[2]

As U S WEST has advised the Commission, focus group research conducted by U S WEST confirmed that individuals did not want information released to third parties without their consent, while they had no concern about U S WEST using the

[2] It is important to note that the written consent requirement is not an absolute requirement, in any event. To the extent that an entity needs CPNI to fulfill a permissible Section 222(d) purpose, the information could be accessed and made available without a customer's written consent. See, e.g., Comments of U S WEST, Inc., WT Docket No. 96-162, GD No. 90-314, filed Oct. 3, 1996 at 25; Reply Comments, WT Docket No. 96-162, filed Oct. 24, 1996 at 10-14. Indeed, it is for this reason that U S WEST is agreeable to accepting carrier representations, short of written instruments, that they are authorized to access information with respect to interconnection, resale and the purchase of unbundled network elements.

same material internally for product design, development and marketing.[3] Survey information submitted by Cincinnati Bell Telephone Company (or "CBT") in CC Docket No. 96-115 makes out a similar case.[4]

U S WEST's internal practices have always been such that an individual's privacy interests are protected when record information about them is released. Indeed, in the White Pages of the telephone directories we advise customers that information about them is "fully protected." Sometimes this protection requires a writing signed by the customer before information is released to a third party. Other times, when requests for information are received orally, the processes involve sending the information only to the address of the customer (regardless of where someone requests the information to be sent), so that the customer knows of the request and the information is calculated to be received by the customer.[5] While Section 222(c)(2) might not mandate a process requiring a writing before information be sent to third parties, internal company practices of many telecommunications carriers -- undoubtedly in place as a matter of institutional practice for years -- have certainly created customer expectations that information about them is not released to third parties, absent some type of customer-initiated transaction and request.[6]

Moving from release of information to third parties to internal use of customer information, questions have arisen about the scope of the products and services that should be permitted to benefit from such use and "implied consent" within an organization and affiliate organizations to make use of CPNI.

Customer Premises Equipment ("CPE") and Enhanced Services

U S WEST reads Section 222(c)(1)(B) as a statutory provision expressly authorizing the realization of overall corporate benefits associated with CPNI access and usage across the corporate family with respect to complementary telecommunications services and non-telecommunications services, including CPE

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[3] See U S WEST's Comments, CC Docket Nos. 90-623 and 92-256, filed Apr. 11, 1994 at 10-12 ("U S WEST April 11, 1994 Comments").

[4] See Comments of Cincinnati Bell Telephone Company, CC Docket No. 96-115, filed June 11, 1996 at 7-8 and Appendix A.

[5] See U S WEST April 11, 1994 Comments at 19-20, where we described this as our standard practice.

[6] Indeed, this may be why telephone companies, traditionally, have been deemed by individuals as institutions likely to safeguard individually identifiable information. See U S WEST's Comments, CC Docket No. 90-623, filed Mar. 8, 1991 at 65-66.

and enhanced services. The literal language of that provision makes clear that services or products "used in" or "necessary to" the provision of telecommunications services *per se* can benefit from the CPNI in the possession of telecommunications carriers, in both the design and marketing operations. The consumer welfare associated with such use is obvious. Not only is one-stop shopping advanced, but products and services that add value to the basic telecommunications service can be developed and offered to customers in a manner that is efficient and effective. Both statutory authorization, as well as implied consent (discussed further below), support the use of CPNI with respect to such offerings.[7]

CPE is clearly "necessary" with respect to and "used in" the provision of virtually all telecommunications services, whether wireline or wireless. To be sure, many types and styles of CPE are available from other than telecommunications carrier sources, but offering the CPE on the service call offers consumers increased efficiencies and facilitates service transactions (i.e., the faster the customer has the CPE, the faster the service can be operational). Furthermore, some types of CPE, such as those which support Caller ID services/functions and wireless services, may be idiosyncratic to the particular service and more difficult to obtain.[8]

Similarly, enhanced services often have a clear and direct connection with telephony services, both supporting and being supported by such services. For example, voice mail services, except in rare cases, are a complementary service to basic telephone service. Other services such as fax store and forward and Internet access services work in conjunction with telephone lines/services purchased by consumers.

Inside wire, a non-telecommunications service, is also a service that meets the clear statutory requirement of Section 222(c)(1)(B). Indeed, the wire has no purpose above or beyond supporting the telephone exchange and toll services.

Specific rules which attempt to "catalog" every service as either "in" or "out" of the Section 222(c)(1)(B) "box" are neither necessary nor desirable from either a

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[7] Even if the statute were not clear in authorizing such use, the Commission's prior findings of implied consent by the mass market to allow for the use of such information with respect to CPE and enhanced services would support such information sharing.

[8] For example, CPE needed by CMRS customers is necessarily quite specialized. The configuration of a given Personal Communications Service ("PCS") provider's handset will depend on: 1) which air interface, i.e., Code Division Multiple Access ("CDMA") or Time Division Multiple Access ("TDMA") or possibly Group Special Mobile ("GSM") the provider has chosen for its primary network; and 2) whether the handset is to operate on a dual-band basis to make use of both PCS and cellular frequencies. Making CPE available at the point of service sale is not only efficient but, in many instances, necessary for the services to be made available in a timely fashion.

market or a public interest perspective. While there might be some regulatory concern over the inability to impose "bright line" rule restrictions with respect to the statutory language (e.g., what is not included in the phrase "necessary" or "used in"?), the Commission should craft rules utilizing, verbatim, the Congressional language. Furthermore, to maximize the public interest associated with commercial communications,[9] one-stop shopping, and the realization of efficient transactions, the Commission should indicate its support for a broad interpretation of the phrases, similar to the approach it took in the Interconnection Proceeding.[10] Such interpretation would advance the public interest.[11]

Implied Consent

U S WEST has consistently taken the position that internal use of CPNI can be implied from the existing business relationship between U S WEST and its customers. Certainly, our focus group research supports such use. The propriety of using such information beyond U S WEST, i.e., with affiliates, is one that must be based on statistical evidence of consumer opinion and logic, as there has not -- to the best of U S WEST's knowledge -- been a specific survey done with respect to information sharing in a telecommunications environment.

Implied consent "inheres where a person's behavior manifests acquiescence or a comparable voluntary diminution of his or her otherwise protected rights. . . . [I]mplied consent is not constructive consent [but, rather] 'consent in fact' which is

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[9] CPNI access and use facilitates educated and meaningful communication, as well as the "dissemination of information as to who is producing and selling what product, for what reason, and at what price. So long as we preserve a predominantly free enterprise economy, the allocation of our resources in large measure will be made through numerous private economic decisions. It is a matter of public interest that those decisions, in the aggregate, be intelligent and well informed. To this end, the free flow of commercial information is indispensable." In the Matter of Unsolicited Telephone Calls, Memorandum Opinion and Order, 77 FCC 2d 1023, 1035-36 ¶ 32 (1980).

[10] In the Matter of Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, Interconnection between Local Exchange Carriers and Commercial Mobile Radio Service Providers, CC Docket Nos. 96-98 and 95-185, First Report and Order, FCC 96-325, rel. Aug. 8, 1996 ¶ 579 ("'Necessary' does not mean 'indispensable' but rather 'used' or 'useful.'").

[11] There is surely no reason to broadly interpret the phrase with respect to carrier-to-carrier relationships but narrowly with respect to carrier-to-customer relationships. To the extent the Commission believes the public interest is advanced by a broad interpretation of the word "necessary" with respect to competitive interactions, it has even more compelling reasons to find a broad interpretation supports the public interest in retail consumer transactions, where consumers are simply trying to get their needs met in the most efficient, quickest way possible.

inferred 'from surrounding circumstances.'" "[I]mplied consent -- or the absence of it -- may be deduced from the 'circumstances prevailing' in a given situation."[12]

U S WEST believes we, as well as other commenting parties, have provided the Commission with ample evidence that individuals expect a business having information about them to use that information in ways that are calculated to produce potential benefits to the individuals about whom the information relates. Furthermore, we believe that common sense and logic support a finding that implied consent to use CPNI exists not only within a specific corporate organization (organizational structures are not matters that many consumers manifest an interest in) but to affiliates, as well. We believe such use is supported by prior findings of the Commission (i.e., the Common Carrier Bureau found that it was not improper for AT&T Corp. ("AT&T") to share CPNI with its credit card operation;[13] and within the context of the Telephone Consumer Protection Act of 1991 interpretations,[14] the Commission found that minimal privacy issues were raised when an individual was contacted by a business with whom the individual had an existing business relationship or one of its affiliates), as well as research (the Louis Harris Survey demonstrating a high level of consumer support for affiliate and information sharing)[15] and, more recently, by Congressional action.[16]

The scope (as opposed to the fact) of such sharing should be guided by common and market sense as opposed to regulatory mandate. Beginning with the proposition that -- particularly in an information market and an information

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[12] Griggs-Ryan v. Smith, 904 F.2d 112, 116 (1st Cir. 1990) (addressing whether implied consent to monitor telephone calls existed).

[13] In the Matter of BankAmerica Corporation, The Chase Manhattan Corporation, Citicorp, and MBNA America Bank, N.A. v. American Telephone & Telegraph Co., AT&T Universal Card Services Corp., and Universal Bank, Memorandum Opinion and Order, 8 FCC Rcd. 8782, 8787 ¶¶ 26-27 (1993).

[14] 47 USC § 227.

[15] Consumers, Credit Reporting, and Fair Credit Reporting Act Issues, 1994, A National Opinion Survey conducted by Louis Harris & Associates and Dr. Alan F. Westin for MasterCard International, Inc., and VISA, U.S.A., Inc. ("Louis Harris Survey").

[16] 142 Cong. Rcd. H. 11746 § 2402(e)(4)(i) excluding from the term "credit report" "information solely as to the transactions or experiences between the consumer and the person making the report" (a past exception), as well as the "communication of that information among persons related by common ownership or affiliated by corporate control." Affiliate sharing with respect to "non-experience" information can occur only after a notice and opt-out process has been put in place. Furthermore, states are preempted from interfering with this authorized affiliate sharing until at least January 1, 2004. See id. § 2419(2) amending Section 624 of the Fair Credit Reporting Act.

economy[17] -- affiliate sharing produces market and consumer benefits,[18] the Commission should allow the market to define the extent and the scope of that sharing, absent an individual's request to not participate. It is impossible for the Commission to articulate, in advance, all the beneficial uses of affiliate sharing. Yet, the Commission can depress market and consumer benefits by trying to do so.[19]

Section 222(c)(1) of the statute should be construed to permit the sharing of CPNI across corporate affiliates with respect to (c)(1)(A) and (B) purposes, without any additional consent requirement beyond the imputation of "implied consent." This is consistent with general customer expectations and business practices. Thus, it is clearly the "least burdensome" consent requirement and it benefits from allowing LECs that are not highly diversified from seeking further "approvals" from their existing customers.

And, while U S WEST believes that an existing customer relationship could support an implied consent to use CPNI beyond (c)(1) purposes,[20] depending on the facts of any particular case, we can also see the reasonableness in notifying consumers of the various activities in which corporate affiliates might be involved, beyond telephony, and the way in which CPNI might be used by them to better serve the individuals about whom the information relates. The combination of the existing business relationship and the open and honest disclosure certainly would

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[17] The 1996 Act clearly acknowledged the convergence of both technology and industries. One aspect of that convergence that might not be immediately apparent, however, is the rebirth of all businesses as "information companies." Certainly, the attachments submitted to U S WEST's Opening Comments in CC Docket No. 96-115 demonstrate that companies are well aware of the value of information in the design, development and marketing of their products, whether they be telecommunications or cable companies. See U S WEST, Inc.'s Opening Comments, CC Docket No. 96-115, filed June 11, 1996 at Appendices A and B. Similar reincarnations are being realized in other market segments, such as banking.

[18] The Louis Harris Survey, for example, indicated clearly that as particular benefits associated with affiliate sharing are articulated, consumer "approval" of the sharing increased.

[19] For example, a conservative approach to affiliate sharing would have, at least potentially, deprived AT&T of its ability to use its CPNI with respect to its credit card venture, and perhaps its wireless operations, as well.

[20] For example, non-telecommunications businesses use their individually identifiable information across their integrated corporate operations. Individuals are sometimes aware of the relationships between various affiliates and sometimes are not. The level of awareness often has to do with the public manifestations of the corporate enterprise. It may be either implicit (similar offerings from a market perspective) or explicit (i.e., dissimilar, but branded offerings). See U S WEST April 11, 1994 Comments at 18 and note 34 (noting that corporate affiliate sharing might be outside an individual's expectations if the relationship between or among the affiliated companies was not well known or understood). Such activity, at least in the past, has not generally been deemed "invasive" of the individual's privacy.

be sufficient to support a finding of "implied consent" or "customer approval." But in no event should general affiliate CPNI sharing, even beyond telecommunications services offerings, be deemed *per se* inappropriate.

To the extent that a business openly and honestly disclosed to its customers the type of affiliates with which information might be disclosed, permission to use information across the panoply of affiliates should be permitted, absent a customer-imposed restriction.[21] Customer "approval" should be deemed once the notification is completed. Absent an individual's request not to have CPNI shared, or a later complaint about a particular use (which could be addressed by not sharing that individual's information in the future), the market benefits potentially associated with affiliate information sharing and use should be permitted to flow through the economy, regardless of whether there are close connections between the affiliated operations.[22]

The market is well poised to address the scope of information sharing and use. Increasingly, the marketing of "privacy" is being realized. For example, the benefits of "privacy" associated with digital wireless communications are being touted in full-page advertisements in newspapers; credit card companies are advising that the privacy of their cardholders is important to them; similar messages are being conveyed by telecommunications companies. Thus, within the context of an existing business relationship, the Commission should first and foremost rely on the relationship to define the scope of use and customer "approval." Businesses which over-assume will pay a market price for their mistakes; but the individual will not suffer material prejudice from the assumption.

Finally, to the extent that the Commission receives a complaint from a consumer on the matter of information sharing and deems the information sharing associated with the complaint as being "unreasonable" under the Communications

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[21] U S WEST currently provides disclosures regarding our CPNI use to all business customers (not just to those with more than 20 lines). With respect to those customers with fewer than 20 lines, the disclosure is framed as a "notice and opt out." Approximately 5% of these customers have restricted their CPNI be used only for basic telecommunications purposes.

[22] For example, a telecommunications company that also owns an appliance store or a pizza operation might deem it appropriate to share information with the affiliate operation (assuming any value could be gained from such sharing). To the extent the potential sharing was clearly disclosed and no objection to the sharing arrangements was received, customers should be deemed to have "approved" the sharing. See U S WEST April 11, 1994 Comments at 18 and note 34 (noting that Sears is generally considered a retail outlet of consumer goods, but that it also engages in car rentals and banking operations (through its then-affiliate Dean Witter) and that customers might not be opposed to this type of sharing if what was occurring was that the customer was being afforded a benefit as a result of the information sharing).

Act based on the facts and circumstances associated with the specific situation, it has ample authority to address the matter within a particular factual context. Particularly in light of the fact that the 1996 Act does not even require a Commission rulemaking regarding Section 222, the Commission should seriously consider a conservative approach to rulemaking in this area, especially where there is an existing business relationship between a company and an individual, relying on market conduct in the first instance to ensure the proper level of privacy protection.

Sincerely,

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TAB 11

ORAL ARGUMENT REQUESTED

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10TH CIRCUIT
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IN THE
UNITED STATES COURT OF APPEALS
FOR THE TENTH CIRCUIT

No. 98-9518

U S WEST, INC.,

Petitioner,

v.

FEDERAL COMMUNICATIONS COMMISSION and
UNITED STATES OF AMERICA,

Respondents,

BELLSOUTH CORPORATION and
SBC COMMUNICATIONS INC., *et al.*,

Intervenors.

On Petition for Review of an Order
of the Federal Communications Commission

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IN THE
UNITED STATES COURT OF APPEALS
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No. 98-9518

U S WEST, INC.,

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v.

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On Petition for Review of an Order
of the Federal Communications Commission

CORPORATE DISCLOSURE STATEMENTS

Pursuant to Rule 26.1 of the Federal Rules of Appellate Procedure, Petitioner U S WEST and Intervenors BellSouth Corporation and SBC Communications Inc. submit the following corporate disclosure statements:

U S WEST, Inc.

On June 12, 1998, the former U S WEST, Inc. (subsequently renamed MediaOne Group, Inc.) consummated a transaction whereby it was separated into two independent companies. The former U S WEST, Inc. had conducted its businesses through two groups, the U S WEST Communications Group ("Communications Group") and the U S WEST Media Group ("Media

Group"). Pursuant to the separation, the former U S WEST, Inc. contributed the businesses of the Communications Group and the domestic directories business of the Media Group ("Dex") to USWC, Inc. (which was subsequently renamed U S WEST, Inc. and is referred to as follows as "U S WEST"). As a result of the separation, U S WEST became an independent company conducting the businesses of the Communications Group, Dex and other subsidiaries. MediaOne Group, Inc. continues as an independent company conducting the businesses of the Media Group other than Dex.

U S WEST is a publicly-held corporation that provides services to the public only through its operating subsidiaries. U S WEST is the parent holding company of U S WEST Communications, Inc., a local exchange carrier that provides local exchange telecommunications, exchange access, wireless, and long distance services pursuant to tariff and contract in 14 western and mid-western states (formerly separately incorporated as The Mountain States Telephone and Telegraph Company, Northwestern Bell Telephone Company, and Pacific Northwest Bell Telephone Company).

The following U S WEST entities have securities in the hands of the public:

U S WEST, Inc.
U S WEST Communications, Inc.
U S WEST Capital Funding, Inc.

U S WEST owns other subsidiaries that market unregulated products and services, none of which has issued debt or stock to the public.

BellSouth Corporation

BellSouth Corporation is a publicly held corporation and has equity securities in the hands of the public. It is principally in the business of providing communications services and products to the general public. BellSouth Corporation's wholly owned subsidiaries have issued debt securities to the public as obligations of BellSouth Telecommunications, Inc., Southern Bell

Telephone and Telegraph Company, South Central Bell Telephone Company, Harbinger Corporation, Tele 2000 S.A., BellSouth Capital Funding Corporation, BellSouth Savings and Security ESOP Trust, and BellSouth Savings and Employee Stock Ownership Trust.

SBC Communications Inc.

SBC Communications Inc. (formerly Southwestern Bell Corporation) is a publicly held corporation with equities and debt in the hands of the general public. The principal directly and indirectly held subsidiaries of SBC Communications Inc. include Pacific Telesis Group; Pacific Bell; Nevada Bell; Southwestern Bell Telephone Company; SBC Wireless, Inc.; Southwestern Bell Yellow Pages, Inc.; Pacific Bell Directory; and SBC International, Inc. The subsidiaries of SBC Communications Inc. are principally engaged in the business of providing communications services and products to the general public.

SBC Communications Inc., Southwestern Bell Telephone Company, and SBC Communications Capital Corporation have publicly held debt. A trust established and funded by Pacific Telesis Group has issued "Trust Originated Preferred Securities" to the public. Pacific Bell, Nevada Bell, and PacTel Capital Resources, subsidiaries of Pacific Telesis Group, have issued debt securities to the public. SBC and Pacific Telesis Group have guaranteed the repayment of certain trust originated preferred securities that have been issued to the public. In addition, certain indirectly held subsidiaries of SBC Wireless, Inc., have small groups of minority shareholders.

No other affiliates of SBC Communications Inc. have outstanding debt or equity securities that are publicly held.

SBC Communications Inc. currently anticipates completing its pending acquisition of Southern New England Telecommunications Corporation ("SNET") later this year.

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August 13, 1998

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STATEMENT OF RELATED CASES

Pursuant to Tenth Circuit Rule 28.2(a), petitioner and intervenors certify that there are no prior or related appeals in this Court.

IN THE
UNITED STATES COURT OF APPEALS
FOR THE TENTH CIRCUIT

No. 98-9518

U S WEST, INC.,

Petitioner,

v.

FEDERAL COMMUNICATIONS COMMISSION and
UNITED STATES OF AMERICA,

Respondents,

BELLSOUTH CORPORATION and
SBC COMMUNICATIONS INC., *et al.*,

Intervenors.

On Petition for Review of an Order
of the Federal Communications Commission

BRIEF FOR PETITIONER AND INTERVENORS

JURISDICTION

This action seeks review of an *Order* of the Federal Communications Commission ("FCC"): *Second Report and Order and Further Notice of Proposed Rulemaking: In the Matter of Implementation of the Telecommunications Act of 1996; Telecommunications Carriers' Use of Customer Proprietary Network Information and Other Customer Information; Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, as Amended,* FCC 98-27, CC Docket Nos. 96-115 and 96-149 ("*CPNI Order*"). The *CPNI Order* was released on February 26, 1998, with a summary published in the Federal Register on April

24, 1998. 63 Fed. Reg. 20326. The *CPNI Order* was also subsequently published in the FCC Record (see attahed hereto). 13 FCC Rcd. 8061 (1998). A timely petition for review was filed on May 18, 1998. This Court has jurisdiction of this petition for review pursuant to 47 U.S.C. § 402(a) and 28 U.S.C. § 2342(1).

STATEMENT OF ISSUES

Whether the *CPNI Order* and accompanying rule amendments are, in whole or in part, arbitrary, capricious, an abuse of discretion, in violation of 47 U.S.C. § 222 and related provisions of the Communications Act as amended, or otherwise not in accordance with law.

Whether the *CPNI Order* and accompanying rule amendments are, in whole or in part, contrary to constitutional right, power, privilege or immunity in that they violate:

- the freedom of speech and press guaranteed by the First Amendment to the United States Constitution; and
- the takings and/or due process clauses of the Fifth Amendment to the United States Constitution.

Whether the *CPNI Order* and accompanying rule amendments are, in whole or in part, arbitrary, capricious and not in accordance with law in that the FCC failed adequately to consider the serious constitutional questions raised by the CPNI rules.

STATUTES AND REGULATIONS

47 U.S.C. § 222 and the Final Rules adopted pursuant to the *CPNI Order* are reprinted in the appendix to this brief.

STATEMENT OF THE CASE

A. Introduction

This case involves the FCC's rules preventing telecommunications carriers from using certain kinds of their business information to speak to their customers unless the carriers first obtain the customers' affirmative consent. For example, the FCC's rules preclude local telephone companies from using business information about their customers to determine

whether a specific customer would be interested in hearing about voicemail services or cellular or other wireless offerings, in the absence of the customer's prior affirmative consent permitting this information to be used for such a purpose.

More specifically, this case concerns FCC regulations implementing the otherwise self-effectuating Section 222 of the Federal Telecommunications Act of 1996, 47 U.S.C. § 222, which addresses Consumer Proprietary Network Information ("CPNI"). CPNI is valuable commercial information that a telecommunications carrier generates or accumulates in the course of doing business with individual members of the public. CPNI includes information about what telecommunications services customers purchase — such as number of lines, how they are used (for example, whether customers have three-way calling, call waiting, Caller I.D., or whether they make use of "star-69" for automatic redialing of the last number called), and information about calling patterns (for example, toll call detail.).[1] To telecommunications carriers, including local exchange, long distance, and wireless carriers, CPNI is comparable to the information that credit card companies, grocery stores, mail-order catalogs, banks, Internet service providers, and many other firms maintain about their customers' purchasing and usage characteristics, as part of their routine business operations.

As with other kinds of individually-identifiable customer information that companies collect and use within their business operations, CPNI allows telecommunications carriers to identify customers, on the basis of their past purchasing habits, who are most likely to be interested in particular new services, and to offer them information about packages of services through communications tailored to their individual needs. Without CPNI, if communications occur at all, they must take the form of blanket, undifferentiated, "broadcast-type" speech to any

[1] Section 222 defines CPNI as "(A) information that relates to the quantity, technical configuration, type, destination, and amount of use of a telecommunications service subscribed to by any customer of a telecommunications carrier, and that is made available to the carrier by the customer solely by virtue of the customer-carrier relationship; and (B) information contained in the bills pertaining to telephone exchange service or telephone toll service received by a customer of a carrier; except that such term does not include subscriber list information." 47 U.S.C. § 222(f)(1).

and all customers, regardless of their individual service interests or needs. CPNI is thus essential for carriers to communicate with their customers effectively and to avoid undue intrusions on those individuals least likely to be interested in the communications.

In sum, this case involves the FCC's interposing itself into the service relationship between telecommunications carriers and their customers and interfering with protected speech and property rights. As will be demonstrated, that intrusion reflects a marked departure from well-settled regulatory policy, frustrates rather than reflects customers' expectations of their relationships with their existing carriers, and is in no way compelled by the statutory language or legislative history of Section 222. For these reasons, this Court should vacate the FCC's rules and remand the case for further consideration.

B. Regulatory History of FCC CPNI Rules

Prior to Congress' enactment of Section 222, the FCC had given extensive consideration to CPNI issues, although it had adopted rules only with regard to certain carriers and certain types of services. Throughout, the FCC had repeatedly rejected prior affirmative consent requirements for carriers in existing customer relationships. The FCC's rules generally permitted carriers to use CPNI to market new and innovative services without any expression of customer approval beyond that implied in the existing carrier-customer relationship. As a general rule, the FCC's rules were designed around periodic customer notifications and opt-out rights.

The FCC's CPNI rules were originally crafted when the Commission was considering whether to require certain carriers (AT&T and later the Bell Operating Companies ("BOCs")) to offer certain non-regulated services — customer premises equipment ("CPE") (such as telephone sets) and "enhanced services" (such as voicemail or Internet access) — through structurally separate subsidiaries.[2] The FCC ultimately decided *not* to require separate subsidiaries for these

[2] *See Second Computer Inquiry, Final Decision*, 77 FCC 2d 384, 481 (1980), *recon.*, 84 FCC 2d 50 (1980), *further recon.*, 88 FCC 2d 512 (1981), *aff'd sub nom. Computer & Communications Indus. Assn. v. FCC*, 693 F.2d 198 (D.C. Cir. 1982), *cert. denied*, 461 U.S. 938 (1983).

non-regulated services,[3] and, in lieu of such separation, it established certain "competitive safeguards." CPNI rules were one of those safeguards.

The FCC's CPNI safeguards were limited to certain offerings by AT&T, the BOCs, and GTE.[4] Other carriers were free to use CPNI in any way they wished. Similarly, even for carriers subject to CPNI rules, services other than CPE, enhanced services, and certain cellular services were unaffected by the FCC's rules. For example, the FCC did not regulate CPNI use for credit card operations.[5]

Further, the FCC crafted its CPNI rules, where applicable, to avoid severe restrictions, such as a prior affirmative consent requirement, on the use of this valuable commercial

---

[3] The Commission established a special rule with respect to cellular services offered by certain carriers, requiring that any carrier required to establish a separate cellular subsidiary was prohibited from providing CPNI to that subsidiary unless the CPNI was provided to others. 47 C.F.R. § 22.903(f).

[4] The BOCs, AT&T, and GTE were required to send annual notices of CPNI rights regarding enhanced services to all of their multi-line (2 or more lines) business customers. *Computer III Phase II Order*, 2 FCC Rcd. 3072, 3096 (1987); *Application of Open Network Architecture and Nondiscrimination Safeguards to GTE Corp.*, 9 FCC Rcd. 4922, 4944-45 (1994). With respect to CPE, the BOCs were required to send annual notices to multi-line business customers, and AT&T was required to provide a one-time notice to its WATS and private line customers. Each notice included a response form that allowed the customer to restrict access to CPNI from the carriers' enhanced services and/or CPE marketing personnel.

In addition, the BOCs and GTE (but not AT&T) were required to obtain prior written authorization from business customers with 20 or more access lines before using CPNI to market enhanced services (but not CPE). *Computer III Remand Order*, 6 FCC Rcd 7571, 7609 (1991), *vacated in part and remanded*, 39 F.3d 919 (9th Cir. 1994). This requirement was adopted only on the basis of extensive record evidence and a showing that the account partner relationship between such customers and their carrier made it relatively easy for the carriers to communicate with the customers and secure the requisite approval. *See Computer III Remand Order*, 6 FCC Rcd. at 7611 ¶ 86; *Communications Satellite Corporation Petition for Declaratory Ruling*, 8 FCC Rcd. 1531, 1535 n.39 (1993). The constitutionality of the Commission's 20-lines rule was never adjudicated. For a more complete history of the FCC's CPNI rules, see the FCC's *Notice of Proposed Rulemaking ("NPRM")* 11 FCC Rcd. 12513, 12516 ¶ 4, 12530 ¶ 40 (1996) and *CPNI Order* at ¶¶ 174-79.

[5] *See In the Matter of BankAmerica Corporation, The Chase Manhattan Corporation, Citicorp, and MBNA America Bank, N.A. v. AT&T Co., Memorandum Opinion and Order*, 8 FCC Rcd. 8782, 8787 ¶¶ 26-27 (1993) ("*Universal Card Order*").

information. The Commission did so, in substantial part, because it recognized that such burdens would themselves have posed a form of "passive" structural separation on the affected carriers.[6] Having rejected operational structural separation on the ground that it hindered the efficient delivery of telecommunications and related services to the public, the FCC did not want to resurrect such separation through severe limitations on the use of CPNI. Such limitations, the FCC recognized, would have hindered one-stop shopping and joint marketing, thus defeating the important federal goals of carrier efficiencies and customer convenience.

In the FCC's *Computer III Remand Order*, 6 FCC Rcd. 7571 (1991), for example, the FCC rejected a prior customer authorization rule for enhanced services, reasoning that a large majority of mass market customers would fail to respond to a request for authorization, and that the resulting restriction on CPNI would be inefficient and anticompetitive:

> **Under a prior authorization rule, a large majority of mass market customers are likely to have their CPNI restricted through inaction**, and in order to serve them the BOCs would have to staff their business offices with network-services-only representatives, and establish separate marketing and sales forces for enhanced services. Thus, a prior authorization rule would **vitiate** a BOC's ability to achieve efficiencies through integrated marketing to smaller customers . . . .

Id. at 7610 n.155 (emphasis added). The Commission preempted state CPNI rules that might require prior authorization, "determining that such state rules would effectively negate federal policies promoting both carrier efficiency and consumer benefits."[7] The Ninth Circuit upheld this preemption, opining that a contrary determination could impede the efficient development of marketing strategies "for small customers."[8] The court added:

> The FCC found that BOC access to CPNI is justified because it allows customers the benefit of one-stop shopping which is important to the development of a mass market in enhanced services. The FCC found that the BOCs are uniquely positioned to reach small customers, and that it would be economically infeasible

[6] *Phase II Recon. Order*, 3 FCC Rcd. at 1173 n. 83.

[7] *NPRM*, 11 FCC Rcd. at 12522 ¶ 16 (describing prior Commission policy).

[8] *California v. FCC*, 39 F.3d 919, 933 (9th Cir. 1994), *cert. denied*, 514 U.S. 1050 (1995).

> to develop a mass market for enhanced services if prior authorization was required for access to CPNI. **If small customers are required to take an affirmative step of authorizing access to their information, they are unlikely to exercise this option and thereby impair the development of the mass market for enhanced services in the small customer market.**[9]

A federal district court in Texas agreed. *See Southwestern Bell Tel. Co. v. Public Util. Comm'n of Texas*, 812 F. Supp. 706, 709, 710 (W.D. Tex. 1993) (upholding FCC's conclusion that "prior authorization rules would require separation of . . . marketing personnel, defeating the goal of integration of all marketing forces" and the goal of "increasing the market for enhanced services").

Subsequently, when AT&T acquired McCaw's cellular operations in 1995, the FCC refused to bar AT&T from sharing its long-distance service CPNI with its new cellular affiliate, finding that neither customer privacy nor competitive equity warranted such a prohibition. The FCC cited "consumer choice and efficiency" as the basis for its ruling, reasoning that any customers with contrary desires could opt out.[10] The FCC vigorously defended this view on appeal,[11] and the D.C. Circuit upheld the Commission's determination that allowing

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[9] *Id.* at 931 (emphasis added).

[10] *In re Applications of McCaw and AT&T Co.*, 10 FCC Rcd. 11786, 11794 (1995). "[W]e expect that permitting AT&T to disclose the information at issue to its cellular affiliates will increase competition for cellular customers as those affiliates, BOC cellular affiliates, and other providers seek to improve service and/or lower prices to attract and retain customers." *Id.* at 11792. *See also AT&T/McCaw Proceedings, Order*, 9 FCC Rcd. 5836, 5886 ¶ 83 (1994) (prohibiting the sharing of CPNI between AT&T and McCaw "would undercut one of the benefits of the . . . combination: the ability . . . to offer its customers the ability to engage in 'one-stop shopping' for their telecommunications needs").

[11] On appeal, the FCC explained that "courts have consistently recognized that capitalizing on informational efficiencies . . . is not the sort of conduct that harms competition," and that it "is manifestly pro-competitive and beneficial to consumers to allow a multi-product firm . . . maximum freedom in offering its competitive services to all of its customers" by utilizing CPNI. Brief for Appellee FCC in *Southwestern Bell Corp. v. FCC*, Nos. 94-1637, 94-1639, at 49 (D.C. Cir. filed Feb. 13, 1995). The FCC explained that CPNI restrictions would undermine AT&T's ability to offer "one-stop shopping" by bundling long-distance and cellular service together — "a significant public benefit." *Id.* at 46. "'One-stop shopping' results from allowing the carrier to employ an integrated marketing and sales force. Denying those who market complementary products access to CPNI, in effect, requires two sales forces within the same company." *Id.* at

AT&T/McCaw to use AT&T's long-distance CPNI to solicit the cellular customers of competing providers would "lead to lower prices and improved service offerings." *SBC Communications Inc. v. FCC*, 56 F.3d 1484, 1495 (D.C. Cir. 1995).

Hence, the FCC has concluded time and time again that a prior affirmative consent requirement to use CPNI was:

- unnecessary to protect competition; [12]
- at odds with efficient carrier operations;[13]
- at odds with joint marketing;[14]
- at odds with customers' desires for one-stop shopping;[15] and

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47. The FCC rejected the argument that CPNI protections were needed for "small businesses and individuals," explaining that the objectors had failed to explain how "'smaller' cellular customers could be harmed by access to information about competing services." *Id.* at 48.

[12] *Phase II Order*, 2 FCC Rcd. 3072, 3094 (1987); *Phase II Further Reconsideration Order*, 4 FCC Rcd 5927, 5929 (1989), *vacated on other grounds*, 905 F.2d 1217 (9th Cir. 1990).

[13] *See AT&T CPE Relief Order*, 102 FCC 2d 655, 678-79 ¶ 39 (1985) and *BOC CPE Relief Order*, 2 FCC Rcd. 143, 147 ¶ 29 (structural separation results in higher prices to consumers and a reduction in the quality and variety of service offerings due to an inhibition of research, development and innovation) (1987); *Phase I Order*, 104 FCC 2d at 1088 ¶ 258 (restrictions on use of customer information "impose a burden on all contacts between carriers and their customers, . . .substantially increase the difficulties attendant with providing customers a single point of contact, and prove extremely expensive to implement).

[14] *Computer III*, 3 FCC Rcd. 1150, 1162 ¶ 97 (1988) (to the extent carriers "use CPNI to identify certain customers whose needs are not being met effectively and to market an appropriate package of . . . services to such customers, customers would be benefited."); *BOC CPE Relief Order*, 2 FCC Rcd at 167 n.86 (internal CPNI use permits carriers to "engage . . . in joint planning and response to customer needs, that many customer apparently desire"); *Universal Card Order*, 8 FCC Rcd. 8782, 8786-88 ¶ 27 (1993) ("joint marketing . . . necessarily involves sharing of some customer network information").

[15] *See e.g., AT&T CPE Relief Order*, 102 FCC 2d at 692-93 ¶ 64 (noting that to deprive AT&T of CPNI use with respect to CPE sales would deprive it of the ability to offer one-stop shopping and would eliminate one of the fundamental consumer benefits associated with integration and access to such information); *BOC CPE Relief Order*, 2 FCC Rcd. 143, 147-48 ¶¶ 29, 31 (1987) (structural separation – and being cut off from CPNI – "prevent the BOCs from satisfactorily serving customers that desire integrated telecommunications systems solutions and designs. . . . [A] broad spectrum of communications users desire vendors that can be single sources for telecommunications products."); *Phase I NPRM*, 50 Fed. Reg. 33581, 33592 n. 58 (1985)

• unnecessary to protect consumer privacy.[16]

Indeed, even outside the CPNI context, the FCC has typically understood the utter impracticality of requiring affirmative customer consents and therefore has permitted notice-and-opt-out options.[17]

C. The 1996 Telecommunications Act

Against the background of the lengthy CPNI regulatory history, Congress adopted Section 222 in the 1996 Telecommunications Act. That Section applied CPNI rules to all carriers, rather than merely to AT&T, the BOCs, and GTE, as had been the FCC's previous approach. It also granted telecommunications carriers the right to use CPNI in their "provision of (A) the telecommunications service from which such information is derived, or (B) services necessary to, or used in, the provision of such telecommunications service." 47 U.S.C. § 222(c)(1). In order for a telecommunications carrier to use CPNI for broader purposes, the use must be "required by law or with the approval of the customer" or must meet the exceptions

("subscribers desire [ ] 'one stop shopping.'"); *1994 Public Notice*, 9 FCC Rcd. 1685 (1994) (FCC concluded that a prior authorization rule would, as a practical matter, deny to all but the largest business customers the benefits of one-stop shopping).

[16] *Computer III Phase II Recon. Order*, 3 FCC Rcd. 1150, 1163 ¶ 98 (1988) ("we anticipate that most of the BOCs network service customers . . . would not object to having their CPNI made available to the BOCs to increase the competitive offerings made to such customers"); *Phase II Order*, 2 FCC Rcd. 3072, 3094 ¶ 152 (1987) (prior authorization unnecessary to protect customer interests).

[17] For example, in the *BNA Second Recon. Order*, 8 FCC Rcd 8798, 8810 (1993), the Commission reversed a prior decision that required affirmative written authorization from customers with unlisted or unpublished numbers before local telephone companies were permitted to provide the customer's billing name and address ("BNA") information to unaffiliated telecommunications service providers. The FCC noted the "burden[some]" nature of requiring customers to "return[ ] authorization form[s]," *id.* at ¶ 68, and permitted carriers, once notification was made, "to presume that unlisted and nonpublished end users consent to disclosure and use of their BNA if they do not make [an] affirmative request" that such information not be disclosed. *Id.*

stated in Section 222(d).[18] Other than these changes, Congress made no finding that the FCC's prior approach to CPNI was inadequate or contrary to the public interest.

Most importantly for purposes of this appeal, there is no indication in Section 222(c)(1) that Congress intended the word "approval" to require before-the-fact, affirmative customer consent. Indeed, Section 222(c)(1) stands in stark contrast to Section 222(c)(2), which requires telecommunications carriers to provide CPNI in their possession to any entity designated by the customer, "upon *affirmative* written request by the customer." (emphasis added). Notably, Section 222(c)(1) does not contain the word "affirmative," nor does it contain the term "express."

Section 222 was adopted in the context of sweeping telecommunications industry reforms designed to foster competition in all telecommunications markets. Properly read in accordance with well-established customer expectations, it grants carriers in existing customer relationships broad authority to use CPNI. Customers have the power to exercise choice and control by requesting any carrier to refrain from using certain information and to constrain the potential dissemination of customer information to parties unaffiliated with the carrier absent affirmative customer consent. In this manner, Congress itself struck the appropriate balance between (i) privacy interests and (ii) competitive efficiencies and carrier rights.

D. The FCC's *NPRM*

The FCC soon sought to revise the congressional balance. As a self-effectuating statutory provision, Section 222 required no independent FCC rulemaking.[19] However, in February of 1996, several local telephone company associations advised the FCC that their members — who unlike the BOCs, AT&T, and GTE had never been subject to CPNI rules — were unclear about their obligations under Section 222 and requested the Commission to provide "guidance"

[18] These exceptions include the initiating, rendering and billing of service; fraud prevention; and the provision of inbound telemarketing, referral or administrative services on an inbound call if the customer approves of the use of CPNI during the call.

[19] The FCC has acknowledged that Section 222 is self-executing. *See Computer III Remand Proceedings: Rules Governing Telephone Carriers' Use of Customer Proprietary Network Information*, 11 FCC Rcd. 16617, 16619 (1996).

regarding such obligations. *CPNI Order* at ¶ 6 & n. 15. Subsequently, NYNEX, a BOC, filed a petition for a declaratory ruling regarding the proper interpretation of a single aspect of Section 222 — the scope of the phrase "telecommunications service" in subsection (c). The FCC responded by initiating a broad-based rulemaking regarding the meaning of virtually the entirety of the Section. *NPRM*, 11 FCC Rcd. 12513.

In the *NPRM*, the FCC read Section 222 as revolutionizing CPNI rules for telecommunications carriers. Under the guise of its interpretive and implementing authority, the FCC created a unique regulatory regime not comparable to the rules under which every other business in the United States operates — including companies that might compete with telecommunications carriers, such as cable operators.[20] Despite the long-standing absence of a prior authorization rule with respect to the use of CPNI (with the limited exception of marketing enhanced services to businesses having more than twenty lines), the FCC in the *NPRM* repeatedly referred to "prior"[21] customer "authorization"[22] as potentially being mandated by Section 222(c)(1), even though the words "prior" or "authorization" are never used in that subsection.

The Commission also set out its tentative conclusions regarding the meaning of the term "telecommunications service" as used in Section 222. It concluded that the term should be construed to reflect three separate "traditional service distinctions":[23] local exchange (including local long-distance or short-haul toll), interexchange (also including short-haul toll) and Commercial Mobile Radio Service ("CMRS" or "wireless").[24] The significance of the categories was that, barring appropriate customer "approval," carriers would be limited in their ability to

[20] Cable operators are free to use subscriber information internally and are obligated to secure affirmative consent only when releasing the information to unaffiliated third parties. 47 U.S.C. § 551.

[21] *NPRM* at 12523-26 ¶¶ 20, 23, 26 (prior authorization), 21 (prior approval).

[22] *Id.*

[23] *Id.* at 12523-24 ¶ 22.

[24] *Id.* at 12525 ¶ 24 and n. 60.

use CPNI derived from one service category to communicate to customers about services not in that category.

E. The Comments and Evidence Filed With the FCC

The *NPRM* raised the spectre that the FCC was proposing to disrupt seriously the carrier-customer relationship. Commentors[25] urged the Commission to reconsider its tentative views with respect to both the appropriate scope of the term "telecommunications service" and the construction of the word "approval." Various commentors argued that the word "approval" was capable of various constructions and urged the Commission to adopt a construction of the word consonant with reasonable customer expectations and commercial practices. They noted that "approval" could be construed in a variety of ways, ranging from tacit or implied approval stemming from an existing business relationship, to a notice-and-opt-out approval process in the context of an existing business relationship, to oral or written express consents. Essentially, commentors maintained that carriers should be able to determine what type of "approval" mechanism was appropriate under the self-effectuating Section 222. Certain commentors (petitioner and intervenors, for example) argued that the only "approval" mechanism that should be *prohibited* was the use of a notice-and-opt-out approval mechanism with respect to the disclosure of CPNI to unaffiliated third parties having no relationship with the customer.

1. Consumer Survey Evidence

Pacific Telesis (now a part of SBC Communications Inc.) provided the Commission with a statistically-valid public opinion survey on the use of CPNI by local telephone companies.[26] The survey was conducted under the leadership of Dr. Alan Westin,

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[25] As part of the Designated Appendix to be submitted to the Court are included relevant filings and submissions of Petitioner, Intervenors (including Pacific Bell), as well as other carriers or associations pressing the salient points addressed in this "Statement of the Case," including Bell Atlantic, GTE, USTA, and AT&T.

[26] *Public Attitudes Toward Local Telephone Company Use of CPNI*: Report of a National Opinion Survey Conducted November 14-17, 1996, by Opinion Research Corporation, Princeton, N.J. and Prof. Alan F. Westin, Columbia University, Sponsored by Pacific Telesis Group ("Westin Survey").

Professor of Public Law and Government at Columbia University and one of the world's foremost authorities on information policy and privacy. The study concluded that:

1. The public has a great deal of confidence in telephone companies (particularly local companies) and trusts them to use the personal information they collect about customers in a responsible way and to protect its confidentiality.[27]

2. Despite a generalized concern over privacy issues, large majorities of the public believe it is acceptable for businesses, and in particular local telephone companies, to communicate with their own customers to offer them additional services,[28] especially if those not wishing such communications are provided with an opt-out opportunity.[29]

3. In particular, a large public majority believes that it is acceptable for local telephone companies to communicate with their customers using CPNI data.[30] The availability of an opt out procedure brings initial approvals of local telephone company use of CPNI from the two-out-of-three respondent level up to the 80% range of public approval.[31]

4. Individuals understand "notice and opt out" procedures, and many have used them in one context or another.[32]

5. Hispanics, African-Americans, women, young adults (18-24 years of age), persons who have used an opt-out previously, and persons who order

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[27] Westin Survey, Questions 2C, 3; Analysis at Item 5, pp. 5-7 ("the finding that 77% of the American public have medium to high trust in local telephone companies gives strong support to the idea that a voluntary program of notice and opt outs in local company use of customer information for offering additional telephone services would be regarded with confidence and approval by more than three out of four Americans").

[28] *Id.* Questions 7 (businesses generally), 9 (local telephone companies); Analysis at Item 7.

[29] *Id.* Questions 8 (businesses generally), 12 (local telephone companies); Analysis at Item 8.

[30] *Id.* Questions 10-11.

[31] *Id.* Questions 11-12; Analysis at Items 8-10, pp. 8-10.

[32] *Id.* Question 5 (familiarity with notice-and-opt-out), 6 (actual use of notice-and-opt-out); Analysis at 9-10 ("The CPNI survey found the respondents who have used opt outs in other business settings are willing to change their position from initial disapproval to positive views of customer-records-based communications by local telephone companies when" follow-up questions are asked).

> many additional telephone services, all have an higher-than-average level of interest in receiving information about new services from telecommunications carriers.[33]

The Westin Survey confirmed other consumer survey evidence submitted into the record regarding customer expectations and CPNI use within the carrier-customer relationship. For example, Cincinnati Bell Telephone ("CBT") informed the Commission of a survey it conducted which demonstrated that customers were quite comfortable with carriers' using CPNI internally but believed that affirmative customer consent should be secured before CPNI could be disclosed to unaffiliated entities.[34] Like the Westin study, the CBT survey demonstrated that the "vast majority of customers surveyed (81.5%) want[ed] to be kept aware of the services" offered by their local carrier[35] and those same customers expected their carrier to use CPNI to tailor the communication.[36]

Additionally, U S WEST advised the FCC of a survey it had conducted which demonstrated that telephone customers were very interested in receiving information about packaged cable/telephone offerings.[37] Bell Atlantic cited to survey evidence demonstrating that 85.9% of respondents wanted to deal with a single carrier for all of their companies telecommunications needs[38] and noted another study documenting customer interest in one-stop shopping.[39]

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[33] *Id.* Questions 9-11; Analysis at 9.

[34] CBT Comments, CC Docket No. 96-115, filed June 11, 1996 ("CBT Comments") at 9 and n.12. The FCC cited the CBT survey in the *CPNI Order* at nn. 224 and 230.

[35] CBT Comments at 8 and n.10 and Aragon Consulting Group Attachment A.

[36] *Id.* Aragon Question USE:INFO.

[37] U S WEST Opening Comments, CC Docket No. 96-115, filed June 11, 1996 at 6.

[38] Bell Atlantic Comments, CC Docket No. 96-115, filed June 11, 1996 at 6 (citing to a 1994 NFIB Foundation business survey, "Who Will Connect Small Businesses to the Information Superhighway?", at 22 (Dec. 1994)).

[39] *Id.* at 7 (citing to 1996 IDC/LINK consumer survey, Telecommunications Brand Equity Study at 1 (1996). *See also* Bell Atlantic Reply, CC Docket No. 96-115, filed June 26, 1996 at 4 and n.11 (citing to another recent poll showing that large numbers of consumers and businesses

Furthermore, certain filing parties provided the FCC with public opinion survey evidence demonstrating that customers were comfortable with carriers sharing individually-identifiable information internally within the same corporate enterprise.[40]

2. **U S WEST Affirmative Consent Trial**

U S WEST undertook a statistically valid trial at the end of the 1996 and the beginning of 1997 seeking to test the feasibility of securing written and oral affirmative customer consents. The trial involved (i) letters to customers, some accompanied by incentives (ranging from $1 to $5 prepaid phone cards) asking that affirmative approval be provided either in writing or through calling a toll-free number; (ii) outbound calls to customers attempting to secure oral approvals; and (iii) requests for approval through the ordinary course of customer inbound calls to U S WEST business offices.

The results of the U S WEST survey were filed with the FCC in September of 1997 and showed the devastating effect that an affirmative customer consent requirement would have on a carrier's ability to use CPNI internally as well the barrier to communication that such a consent requirement would impose. For example, the outbound **mail** campaign produced affirmative consents in the range of 6-11%. The offering of incentives appeared to have no material impact on the frequency with which consents were provided. The cost per affirmative response was $29.32, plus whatever incentive was offered ($1 to $5 phone cards), for a maximum total of

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would defect from their current provider if they could not realize one-stop shopping, citing to Contra Cost Times, June 19, 1996 and attaching copy of article to filing).

[40] *See* Letter from Todd Silbergeld, Director, Federal Regulatory, SBC Communications Inc. to William F. Caton, Acting Secretary of the FCC, dated Oct. 20, 1997, attaching a copy of Study No. 934016, "Consumers and Credit Reporting 1994," Conducted for MasterCard International Incorporated and Visa U.S.A. Inc., Louis Harris and Associates, Inc. *See also* Letter from Gina Harrison, Director, Federal Regulatory Relations, Pacific Telesis, to William F. Caton, Acting Secretary of the FCC, dated Jan. 24, 1997, attaching a letter from Privacy & Legislative Associates, to A. Richard Metzger, Jr., Deputy Chief, Common Carrier Bureau (signed by Dr. Alan Westin and Robert R. Belair), dated Jan. 23, 1997 ("Privacy & Legislative Associates Letter"), which at Part IV, pp. 16-18 and n. 28 discusses this survey; Bell Atlantic Reply Comments (June 26, 1996) at 4-5 (mentioning that it had provided a copy of this report to FCC in 1994 and provided it again as an attachment to its Reply Comments).

$34.32. The outbound **calling** campaign produced consents in the range of 29%, with refusals in about the same amount. The cost per affirmative response was $20.66.

The largest percentage of affirmative consents were secured through the inbound calling channels in those circumstances where the customer had initiated the communication and was engaged in discussions about telecommunications.[41] Yet this approval venue is quite limited. U S WEST pointed out that it hears from at most about 15% of its customer base (between 10 and 13 million customers and access lines) in any given year, and some contacts are with the same customers. It could well take a decade or more to secure affirmative consents through this mechanism.

U S WEST also demonstrated the significance of the combined "no answer/hang up" response to its CPNI affirmative consent initiative. On average, 4.8 dialing attempts (at a cost of $5.89 per attempt) were necessary to reach a live respondent having authority to grant the necessary consent. In the outbound calling trial, U S WEST could not even establish communication with one-third of the customers that it attempted to contact. U S WEST explained that such difficulty might not necessarily be a problem in a general public opinion survey or telemarketing environment (where it is not uncommon to encounter large numbers of no answers or hang ups), because in those situations the lack of contact can be "corrected" — if larger numbers are desired — simply by increasing the size of the sample. But this solution could not be used in a CPNI affirmative consent regime. Both a "no answer" and a "hang up" count as a "no" with respect to CPNI consent.

Furthermore, U S WEST expressed its view that not only the customer "hang ups" but also some of the refusals to grant affirmative consent to use CPNI were as much the result of aversion to telemarketing as they were a considered response to the CPNI request based on its own merits. The initial call could itself have been deemed an intrusion on privacy, resulting in either a hang-up or a denial of consent.

[41] U S WEST *Ex Parte, dated Sep. 11, 1997* at 9-10. *See also CPNI Order* at nn.390, 403 (noting this phenomena and that it had been repeated by other carriers).

With respect to the issue of customer "privacy" (the ostensible focus of Section 222), U S WEST also advised that the FCC's approach would only *increase* the volume of blanket telemarketing to subscribers because it would prevent carriers from targeting individual customers based on their likely subjects of interest. Marketing would therefore become less individualized and more intrusive in nature.

U S WEST also explained to the Commission that the low volume of responses to the requests for affirmative consents probably represented a lack of customer interest in the subject matter and a perception that the information being conveyed was not important. This explanation was supported by the about-even numbers of "yes" and "no" responses encountered across customer segments in both direct mail and oral outbound solicitations, without regard to the consumption profiles of telecommunications customers (*i.e.*, whether highly active telecommunications use or very little use). If the matter being communicated had been of interest to customers or considered important, it would be expected that highly active users would have responded differently than low-users.

U S WEST noted that previous FCC CPNI rules had rendered very few customer records unavailable to it.[42] However, as shown by the survey results, an affirmative consent requirement would prevent U S WEST from using the vast majority of its customer records to communicate with its subscribers. Furthermore, given the cost per affirmative response of up to $34.32 for outbound mail and of $20.66 for outbound calling, and given U S WEST's service population of over 11 million customers, U S WEST estimated that it would cost hundreds of millions of dollars to attempt to secure affirmative CPNI consents from its customer base. And even that immense expenditure would not assure contact with each individual, much less assure that the customer would have an interest in or consider the CPNI affirmative consent request on its merits.

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[42] U S WEST reported that, previously, only .06% of residential customers, 3.6% of small business and 33% of large business customers (a customer category that included competitors) had requested that CPNI be restricted.

3. Constitutional Analyses

U S WEST submitted a detailed First Amendment analysis by Professor Laurence Tribe (now counsel for petitioner and intervenors in this proceeding) of the First Amendment implications of an affirmative consent requirement.[43] Based on both judicial precedent and the evidence included in the then-existing record, Professor Tribe concluded that, given the clear First Amendment attributes of CPNI, Section 222 — which contains no affirmative consent requirement on its face — should not be construed to require a carrier to obtain prior affirmative customer consent before CPNI could be broadly used. Instead, Professor Tribe asserted that the Act should be interpreted as permitting an "opt-out" approval mechanism, whereby a carrier, after full and fair notice to customers, would be permitted to use CPNI across different service categories and among its affiliates, so long as customers did not object. The FCC dismissed Professor Tribe's analysis in a single footnote and two paragraphs of its *CPNI Order*. *CPNI Order* at n. 164 and ¶¶ 106-107.

In addition, various parties argued that the Commission's approach would impermissibly intrude on carriers' property rights. They noted that CPNI constitutes intellectual property belonging to carriers.[44] They urged the Commission to avoid rules that would raise constitutional questions under the Fifth Amendment.

4. Expert Views of Other Agencies

During the course of the proceedings, the FCC was advised of an analysis by the Privacy Working Group of the Clinton Administration's National Information Infrastructure Task Force

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[43] Letter from Kathryn Marie Krause, Senior Attorney for U S WEST to Mr. William F. Caton, Acting Secretary of the FCC, dated June 2, 1997 (cover letter and summary of Professor Tribe's conclusions) ("U S WEST Cover Letter"), attaching letter from Laurence H. Tribe to Messrs. A. Richard Metzger and John Nakahata and Ms. Attwood, dated June 2, 1997 ("Tribe Original Analysis"); letter from Laurence H. Tribe to Messrs. A. Richard Metzger and John Nakahata and Ms. Attwood, dated Sept. 10, 1997 (responding to MCI letter) ("Tribe Response").

[44] *See, e.g.*, Comments of USTA, CC Docket No. 96-115, filed June 11, 1996 at 8; Comments of GTE, CC Docket No. 96-115, filed June 11, 1996 at 13.

(NIITF),[45] as well as a prior study by the National Telecommunications and Information Administration (NTIA) of the Department of Commerce.[46] Both organizations concluded that an opt-out method of customer approval was generally appropriate with respect to the commercial use of individually-identifiable information.

The NTIA Privacy Report explained that CPNI was not sensitive information, in contrast to personal information relating to health care, political persuasion, sexual matters and orientation, and personal finances, for example. NTIA Privacy Report at 20, 23, 25 n.98. The NTIA concluded that a notice-and-opt-out approach to CPNI was entirely consistent with individual privacy. It also acknowledged the procompetitive advantages associated with easy access and use of information like CPNI: "[T]he free flow of information – even personal information – promotes a dynamic economic marketplace, which produces substantial benefits for consumers and society as a whole." NTIA Privacy Report at 24, 25.

The conclusion of the NTIA Privacy Report was reinforced by a filing from the NTIA itself in the CPNI proceeding,[47] as well as by a separate filing by Dr. Westin.[48] Dr. Westin confirmed that an opt-out approval procedure for CPNI was appropriate.[49]

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[45] *See* "Privacy and the National Information Infrastructure: Principles for Providing and Using Personal Information, A Report of the Privacy Working Group" (Oct. 1995) ("Privacy Working Group Report").

[46] *See* U.S. Department of Commerce, NTIA, "Privacy and the NII: Safeguarding Telecommunications-Related Personal Information," (Oct., 1995) ("NTIA Privacy Report"). The FCC cited to this Report in its *CPNI Order* at ¶ 22 n.96. This report was referenced by various parties including U S WEST (at 16); BellSouth at 9, 14-17; SBC at 8-9, Pacific at 7-8 and Attachment A (containing a copy of the report).

[47] Reply Comments of NTIA, filed Mar. 27, 1997 at 25-27 (arguing that an opt-out process represented an appropriate process for securing customers' approvals, particularly in light of the existing business relationship).

[48] *See* Pacific Telesis, Ex Parte, CC Docket No. 96-115, dated Jan. 24, 1997 attaching the Privacy & Legislative Associates Letter at 4 (discussing both the Privacy Working Group Report and the NTIA Privacy Report, identifying as "sensitive" information (based on 1994 survey data) health and medical information, banking and credit information, insurance information).

[49] Privacy & Legislative Associates Letter at 9.

The carrier submissions to the FCC also included a copy of a recent Federal Trade Commission ("FTC") Report to Congress involving certain types of "locator" services. That report, which involved information far more sensitive than CPNI, generally endorsed the self-regulatory guidelines promulgated by the industry participants. Those guidelines included an "opt out" provision with respect to use of personally-identifiable information.[50]

F. FCC's CPNI Order

The *CPNI Order* is a 261-paragraph order purporting to implement a six-paragraph self-effectuating statutory provision. That the FCC managed to derive such a lengthy and detailed order from a statute otherwise hailed as "deregulatory,"[51] demonstrates how far the Commission strayed from Congress' intent. The FCC rejected the expert views of other agencies;[52] rejected authoritative evidence demonstrating the propriety of a notice-and-opt-out approval model; rejected the proposed statutory construction of petitioner and intervenors; and rejected the constitutional analyses submitted to the Commission.

Instead, the FCC adopted a series of rules forbidding carriers from using CPNI without prior affirmative customer consent to market and speak to both existing and future customers they believe would be receptive to new services. Under the FCC's so-called "total service approach," a carrier providing only local service to a particular customer would not be able to use CPNI, without prior affirmative customer consent, to speak to the customer regarding cellular or

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[50] Letter from Ben G. Almond, Executive Director-Federal Regulatory, BellSouth, to Ms. Magalie R. Salas, Secretary, Federal Communications Commission, dated Dec. 18, 1997 (reflecting the submission to the FCC of the FTC document, "Individual Reference Services: A Report to Congress," dated Dec. 17, 1997 and noting that the report "highlighted the use of an Opt-Out process to permit consumers access to their own non-public information").

[51] Joint Statement of Committee of Conference, S. Conf. Rep. No. 230, 104th Cong., 2d Sess. 113 (1996).

[52] *CPNI Order* at ¶ 94 and n.348 (specifically rejecting the Privacy & Legislative Associates submission) and n.353 (rejecting NTIA argument).

long-distance service. A carrier providing only long-distance service would be similarly constrained with respect to local or wireless services not currently provided to its customer.[53]

The result of the *CPNI Order* is that carriers who have an *existing relationship with customers* may not use CPNI associated with a customer's existing purchasing behaviors or service usage to determine that the customer would likely be interested in information about another service offering, *unless* the carrier has had a *prior* communication with the customer and has secured an affirmative consent to use the information in such manner. In short, the FCC forbade telecommunications carriers from using CPNI to speak unless they had secured prior affirmative consent from each of their millions of customers.

The FCC's rules create three unsatisfactory alternatives: (1) carriers can undertake the difficult and expensive task of seeking to secure prior affirmative consent from each of their customers; (2) carriers can stay mum and await a customer's spontaneous and affirmative inquiry of a carrier about "What's new?;" or (3) carriers can engage in a kind of "broadcast" speech to all customers, regardless of their individual purchasing characteristics and interests. Under each alternative, the *CPNI Order* bars individualized and customized speech.

The Commission reached this burdensome and impractical result by construing the term "approval" in Section 222(c)(1) to require prior affirmative consent from customers and by ruling out any other way of ascertaining customer approval — such as a notice-and-opt-out approval process. The FCC's rule is in no way commanded by the language of Section 222 or consistent with the deregulatory thrust of the 1996 Act. It is unprecedented with respect to commercial operations and speech in the United States. And it raises serious constitutional questions under both the First and Fifth Amendments.

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[53] The FCC applied a variation on this theme to a carrier's use of aggregate customer information. It held that if aggregated information was used to develop a profile of a customer most likely to be interested in a product or service that an individual customer meeting that profile could not be approached regarding an "out of service relationship" service *unless* that customer had provided prior affirmative consent for his/her CPNI to be "used" with respect to such contact. *See CPNI Order* at ¶ 149.

SUMMARY OF ARGUMENT

I. CPNI is an essential element of speech between carriers and their customers. Further, the internal sharing and use of CPNI within carriers is itself constitutionally protected speech. The *CPNI Order* violates the First Amendment by requiring that carriers secure prior affirmative consents from customers before using individually-identifiable customer information to speak with their customers on an individualized basis about services beyond the "categories" of telecommunications services to which they currently subscribe. In addition, the *CPNI Order* restricts the ability of carriers to share and use CPNI internally — to have different divisions, affiliates, and personnel within the same carrier communicate information to each other (*i.e.*, to speak to each other), absent a prior affirmative consent from the customer.

The FCC did not engage in a serious First Amendment analysis regarding the adverse speech impacts of its CPNI rules. Instead, it pretended there was no First Amendment issue on the facile theory that carriers remain free to speak to subscribers so long as they do not use CPNI to do so. But the First Amendment is concerned with "practic[al]" realities. *Linmark Associates, Inc. v. Willingboro*, 431 U.S. 85, 93 (1977). It is undisputed that requests for affirmative consent have extremely low response rates. The practical effect of the FCC's *CPNI Order* will be to choke off meaningful, individualized speech that depends on CPNI. It is sophistry for the Commission to say that carriers theoretically remain free to speak, while it simultaneously withdraws the essential ingredient for educated communication. Indeed, by declining to examine the First Amendment issues associated with its Order in a serious fashion, the FCC failed at the most fundamental level to engage in reasoned decision making.

II. The *CPNI Order* also raises grave questions under the Fifth Amendment's Takings Clause. The Takings Clause protects stored proprietary data. *Ruckelshaus v. Monsanto Co.*, 467 U.S. 986, 1001 (1984). CPNI is valuable intellectual property that belongs to *carriers*, not to *customers*. Yet the FCC quite cavalierly divested carriers of their property interest in CPNI. It deemed CPNI to be the customers' property and imposed a prior affirmative consent requirement that will have a devastating impact on carriers' ability to use CPNI for productive (indeed,

constitutionally protected) purposes. The Government may not, "by ipse dixit," decree that a private person no longer owns his property. "This is the very kind of thing that the Taking Clause of the Fifth Amendment was meant to prevent." *Webb's Fabulous Pharmacies, Inc. v. Beckwith*, 449 U.S. 155, 164 (1980). The FCC's analysis of the takings issues was the antithesis of reasoned decision making.

III. The *CPNI Order* is an unnecessarily severe construction of Section 222. It gratuitously raises constitutional issues where longstanding principles call for avoidance of such questions. The term "approval" in Section 222(c)(1) does not, as a matter of statutory interpretation, mandate the adoption of a prior affirmative consent requirement. Instead, the Commission could have allowed carriers to utilize a broad range of approval mechanisms, including affirmative consents if desired but also permitting notice and opt out processes where there is an existing service relationship between carrier and customer. Such approach, clearly narrower and less burdensome than that adopted by the FCC, would have fully protected customer privacy interests while avoiding constitutional questions.

For all of the above reasons, the *CPNI Order* and the accompanying rule amendments implementing the FCC's prior affirmative consent requirement for CPNI must be vacated.

ARGUMENT

STANDARD OF REVIEW

This Court has explained that it "review[s] agency action *de novo* to determine whether it was 'arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law.'" *City of Albuquerque v. Browner*, 97 F.3d 415, 424 (10th Cir. 1996), *cert. denied*, 118 S. Ct. 410 (1997); *see also Hill v. NTSB*, 886 F.2d 1275, 1278 (10th Cir. 1989) (agency's "interpretation of constitutional or statutory provisions" is "reviewed *de novo*").

A. THE *ORDER* FAILS TO GIVE PROPER WEIGHT TO THE FIRST AMENDMENT INTERESTS IMPLICATED BY THE CPNI RULES

1. CPNI Is Information Whose Communication Is Subject to First Amendment Protection

CPNI is information whose communication is entitled to First Amendment protection. The creation, assembly, compilation, and/or communication of information lie at the core of what the First Amendment protects. *See Hurley v. Irish-American Gay, Lesbian and Bisexual Group of Boston*, 515 U.S. 557, 570 (1995); *Turner Broadcasting System, Inc. v. FCC*, 512 U.S. 622, 636-37 (1994).

It is fundamental that the First Amendment protects the right to use information to communicate with others. CPNI is valuable commercial information and an essential ingredient for communication between carriers and their millions of customers regarding not just the current service relationship but also regarding new and innovative services that customers may desire or find useful. In this respect, CPNI is to carriers what wire service reports are to newspapers — *i.e.*, the raw source material from which information and communications are crafted. In the case of CPNI, the information is communicated from one speaker to another within the carrier (*i.e.*, from one division or affiliate to another), and also forms the source of protected expression to customers.

The Supreme Court has applied the First Amendment to regulations falling on *physical* objects and substances (let alone bits or clusters of information) that are essential ingredients in expression, such as the newsprint and ink that were the subject of the tax invalidated by the Supreme Court in *Minneapolis Star v. Minnesota Comm'r of Revenue*, 460 U.S. 575, 581 (1983), and the newsracks regulated by the laws struck down in *Cincinnati v. Discovery Network, Inc.*, 507 U.S. 410, 426-29 (1993), and *Lakewood v. Plain Dealer Publishing Co.*, 486 U.S. 750, 757 (1988).

Furthermore, the First Amendment protects not only a speaker's right to solicit customers, *Edenfield v. Fane*, 507 U.S. 761, 765-66 (1993), but also the audience's right to *receive* information. *Lamont v. Postmaster General*, 381 U.S. 301 (1965). With respect to both dimensions of the right to free speech, CPNI is information that is central to meaningful communication and well-informed customer decisions. It is precisely the kind of information that the Supreme Court has described as being the lifeblood of a free enterprise economy:

> So long as we preserve a predominantly free enterprise economy, the allocation of our resources in large measure will be made through numerous private economic decisions. It is a matter of public interest that those decisions, in the aggregate, be intelligent and well informed. To this end, the free flow of commercial information is indispensable.

Virginia State Board of Pharmacy v. Virginia Citizens Consumer Council, Inc., 425 U.S. 748, 765 (1976) ("*Virginia Pharmacy*"). *See also Rubin v. Coors Brewing Co.*, 514 U.S. 476, 481-82 (1995). Indeed, in other proceedings the FCC has frequently cited to *Virginia Pharmacy*, recognizing that "[t]he proper allocation of resources in our free enterprise system requires that consumer decisions be intelligent and well informed," *In the Matter of Billed Party Preference for InterLATA 0+ Calls*, 13 FCC Rcd. 6122 ¶ 18 (1998), and that the "dissemination of information as to who is producing and selling what product, for what reason, and at what price" is critical information for consumers. *In the Matter of Unsolicited Telephone Calls, Memorandum Opinion and Order*, 77 FCC 2d 1023, 1035-36 ¶ 32 (1980). Nowhere in the *CPNI Order* did the FCC so much as pay even lip service to these cardinal principles.

2. A Prior Consent Requirement for CPNI Is an Unconstitutional Burden on Speech

The *CPNI Order* unquestionably burdens speech. It prohibits carriers from using CPNI to market services outside the existing service relationship unless prior affirmative consent by customers is first obtained. For example, "a carrier whose customer subscribes to service that includes a combination of local and CMRS would be able to use CPNI derived from this entire service to market to that customer all related offerings, *but not to market long distance service to*

that customer, because the customer's service excludes any long distance component." *CPNI Order* at ¶ 30 (italics added). Thus, carriers are forbidden from using CPNI without prior affirmative customer consent to discuss with customers various categories of services that the customer may need or desire. If prior affirmative consent cannot be obtained, the *CPNI Order* bans the use of CPNI to tailor the communication.

In addition to the barrier the *CPNI Order* imposes on carrier-customer communications, it also restricts the right of common corporate affiliates and divisions, and of personnel within the same carrier, to share CPNI — to communicate information to each other.[54] These restrictions are imposed despite otherwise express congressional authority permitting local carriers to engage in joint marketing — to market as a single package local phone service together with other services that might be offered or managed through a separate affiliate or division, such as long distance and wireless services. *See* 47 U.S.C. § 601(d) (granting carriers joint marketing authority "[n]otwithstanding . . . any . . . Commission regulation"); 47 U.S.C. § 272(g)(3) (excluding joint marketing activities from certain identified non-discrimination obligations). By preventing carriers' separate divisions or affiliates from communicating CPNI to each other, even where Congress has explicitly granted the right for those divisions or affiliates to engage in joint marketing, the *CPNI Order* operates as a classic restriction on speech.

Accordingly, scholars have warned that "[r]egulations intended to protect privacy by outlawing or restricting the transfer of consumer information would violate rights of free speech." Solveig Singleton, *Privacy as Censorship: A Skeptical View of Proposals to Regulate Privacy in the Private Sector* at 3 (Cato Institute Policy Analysis No. 295, Jan. 22, 1998). "From light conversation, to journalism, to consumer credit reporting, we rely on being able to

[54] The FCC's CPNI rules provide: "If a telecommunications carrier provides different categories of service, but a customer does not subscribe to more than one offering by the carrier, the carrier is not permitted to share CPNI among the carrier's affiliated entities." 47 C.F.R. § 64.2005(a)(2). The rules also forbid a carrier from "disclos[ing] or permit[ting] access to CPNI" with regard to the provision of services "that are within a category of service to which the customer does not already subscribe to from that carrier, unless the carrier has customer approval to do so." *Id.* at § 64.2005(b).

freely communicate details of one another's lives. Proposals to forbid businesses to communicate with one another about real events fly in the face of that tradition." *Id.* at 1. *See also* Fred H. Cate, PRIVACY IN THE INFORMATION AGE 55 (Brookings 1997) (the First Amendment "fundamentally blocks the power of the government to restrict expression, even in order to protect the privacy of other individuals. . . . [The First Amendment] restrains the power of the government to control expression or to facilitate its control by private parties in an effort to protect privacy.").

In a variety of contexts, the Supreme Court has recognized that imposing a prior affirmative consent requirement in the context of otherwise protected communications is an unconstitutional burden on speech. For example, in *Martin v. Struthers*, 319 U.S. 141 (1943), the Court invalidated a city ordinance that forbade door-to-door solicitation unless the residents of the household had affirmatively requested the solicitor to approach. The Court opined that "[w]hether such visiting shall be permitted has in general been deemed to depend upon the will of the individual master of each household, and not upon the determination of the community. In the instant case, the City of Struthers, Ohio, has attempted to make this decision for all its inhabitants." *Id.* at 141. Here, the FCC has attempted to make the decision for all telecommunications customers in the entire United States.

Similarly, in *Lamont v. Postmaster General*, 381 U.S. 301 (1965), the Court invalidated a requirement that the recipients of Communist literature notify the Post Office in advance that they wish to receive it. Most recently, in *Denver Area Educational Telecommunications Consortium, Inc. v. FCC*, 116 S. Ct. 2374 (1996), the Supreme Court struck down an affirmative opt-in rule for "patently offensive" cable programming. The Court opined that "[t]hese requirements have obvious restrictive effects" (*id.* at 2391), even apart from the reluctance of customers to order offensive material for viewing. *Id.* The Court predicted that "[f]urther, the added costs and burdens that these requirements impose upon a cable system operator may encourage that operator to ban programming that the operator would otherwise permit to run[.]" *Id.*

The *CPNI Order* is similarly unconstitutional because it impermissibly burdens speech. It imposes onerous prior affirmative consent requirements on information sought to be communicated internally, within a carrier, in support of protected speech with customers. The CPNI rules violate the rights of both speakers and listeners.

3. The Commission's First Amendment Analysis Was Flawed

The FCC did not engage in a conscientious First Amendment analysis. Instead, it tried to sweep the First Amendment issues under the rug. The FCC's theory was that, under its rules, "[c]arriers remain free to communicate with present or potential customers about the full range of services that they offer, and [its interpretation of] section 222 therefore does not prevent a carrier from engaging in protected speech with customers regarding its business or products." *CPNI Order* at ¶ 106. According to the Commission, no speech was burdened, let alone prohibited.

This reasoning is sophistry. First, the Commission completely overlooked the ban on a carrier's internal or corporate use of CPNI — on CPNI-related communications between various divisions and personnel within the same carrier. That ban on speech is in no way alleviated by allowing carriers the option of non-CPNI-related communications with customers.

Second, the Commission's argument flies in the face of the Supreme Court's teaching that the First Amendment is concerned with "practic[al]" realities. *Linmark Associates, Inc. v. Willingboro*, 431 U.S. 85, 93 (1977). Without the use of CPNI, carriers cannot engage in customized or individualized speech with their customers. The FCC's approach relegates carriers to types of "broadcast" speech, when communication with their customers as individuals is much more meaningful, informative, and effective. The "broadcast speech" option cannot save the *CPNI Order* from its clear constitutional infirmities. As the Supreme Court has explained in striking down a ban on paid petition circulators, the fact that a regulation "leaves open 'more burdensome' avenues of communication, does not relieve its burden on first Amendment expression. The First Amendment protects [the speakers'] right not only to advocate their cause but also to select what they believe to be the most effective means for doing so." *Meyer v.*

Grant, 486 U.S. 414, 424 (1988). Similarly, in *Shapero v. Kentucky Bar Ass'n*, 486 U.S. 466 (1988), the Supreme Court struck down a state rule banning targeted solicitation letters by attorneys to potential clients known to have specific legal problems (in that case, persons facing foreclosure actions). The Court held that "the First Amendment does not permit a ban on certain speech merely because it is more efficient; the State may not constitutionally ban a particular letter on the theory that to mail it only to those whom it would most interest is somehow inherently objectionable." *Id.* at 473-74.

Thus, a law prohibiting newspapers from using wire service reports could not be saved by arguing that newspapers remained free to publish stories using other kinds of source materials. In *Edenfield v. Fane*, 507 U.S. 761, 770-71 (1993), the Court invalidated a ban on in-person solicitation by CPAs (*i.e.*, a type of individualized and targeted speech), even though the regulation allowed accountants to solicit by mail or advertisement (*i.e.*, a type of broadcast speech). In *Rubin v. Coors Brewing Co.*, 514 U.S. 476, 488 (1995), the Court struck down a federal statute that prohibited the disclosure of alcohol content on beer labels (targeted speech), even though the statute permitted such disclosure in advertisements (broadcast speech). And, in a situation resembling the converse of the FCC's *CPNI Order*, it was no answer to the newsrack ban invalidated in *Cincinnati v. Discovery Network, Inc.*, 507 U.S. 410 (1993) (a type of "broadcast" ban), that commercial leaflets might be distributed by hand (a type of individualized speech).[55]

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[55] *See also City of Ladue v. Gilleo*, 512 U.S. 43, 57 & n.16 (1994) (prohibition on residential signs invalid, even though it did not prevent homeowners from "taking out a newspaper advertisement, handing out leaflets on the street, or standing in front of one's house with a handheld sign," or even from displaying flags with written messages); *International Society for Krishna Consciousness v. Lee*, 505 U.S. 672, 708-09 (1992) (Kennedy, J., concurring in the judgment) ("the Port Authority's regulation allows no practical means for advocates and organizations to sell literature within its airports"); *id.* at 715 (Souter, J., concurring in the judgment in relevant part) ("A distribution of preaddressed envelopes is unlikely to be much of an alternative.").

Here, the practical burden on speech is no less severe than those restrictions struck down by the Supreme Court. The FCC did not deny that its interpretation of Section 222 might "constrain carriers' ability to more easily 'target' certain customers for marketing." *CPNI Order*, at ¶ 106. The Commission recognized the importance of CPNI, agreeing that "the use of CPNI may facilitate the marketing of telecommunications services to which a customer does not subscribe." *Id.* at ¶ 104. Indeed, in the FCC's own words, "as competition grows and the number of firms competing for consumer attention increases, CPNI becomes a powerful resource for identifying potential customers and tailoring marketing strategies to maximize customer response." *Id.* at ¶ 22.

The FCC also acknowledged that "the form of approval has bearing on carriers' use of CPNI as a marketing tool" for new services. *Id.* at ¶ 86. The Commission did not, and could not, dispute that requests for affirmative consent have extremely low response rates. In fact, the FCC itself pointed to the U S WEST trial to show that U S WEST's outbound mail campaign produced affirmative consents in the range of 6-11% and that only about 29 percent of customers give their consent when "cold called" by a carrier. *Id.* at ¶ 111.

Thus, the FCC acknowledged that its *Order* "might make incumbent carriers' marketing efforts less effective and potentially more expensive" (*id.* at ¶ 66) and cited comments indicating that "restricting intra-firm use of CPNI makes product development and marketing more costly and less efficient, thereby raising prices and reducing the quality and variety of service." *Id.* at n.244. Indeed, "[d]evelopments in Europe, where regulations strictly limit the transfer of personal information, suggest that a mandatory opt-in regime would nearly wipe out direct marketing." *Supra at 26,* Solveig Singleton, *Privacy as Censorship*, at 12-13.

Moreover, even the obligation to *seek* prior affirmative consents (even if they could be obtained) itself imposes severe burdens on carriers. Making repeated unsolicited calls and other communications to subscribers to seek consent risks losing customer goodwill. Indeed, the FCC acknowledged that "[c]arriers that make frequent outbound calls to obtain oral approval . . . do so at the risk of losing their customer base." *CPNI Order* at ¶ 113. For carriers like U S WEST,

BellSouth and SBC, which collectively have over 91 million access lines and wireless subscribers, such a campaign would also be extremely labor-intensive, expensive, and lengthy. Speech would be suppressed for a significant amount of time, and the carriers would undoubtedly refrain from speech in situations where they otherwise would seek to communicate. In fact, U S WEST's study documented that the *CPNI Order* would prevent it from using the vast majority of its customer records to communicate with its subscribers and would impose enormous costs on U S WEST — running into the hundreds of millions of dollars — through attempts to secure customer affirmative CPNI consents, if the consents could be obtained at all.

Hence, the Commission's assertion that its *CPNI Order* does not burden speech is fanciful. In fact, it burdens speech so greatly as to make CPNI-supported expression utterly impracticable.

4. The *CPNI Order* Cannot Not Survive First Amendment Scrutiny

The Commission asserted that, even if expression is burdened, its prior affirmative consent requirement amounted at most to a restriction on commercial speech that passes muster under intermediate First Amendment scrutiny because "the government asserts a substantial interest in support of the regulation, the regulation advances that interest, and the regulation is narrowly drawn." *CPNI Order* at ¶ 106. This conclusory claim does not suffice.

Under even intermediate First Amendment scrutiny,[56] a restriction on speech must be invalidated unless the Government **bears its burden** of demonstrating that the law "directly

[56] Commercial speech is defined as speech which proposes a commercial transaction. *See Virginia State Board. of Pharmacy*, 425 U.S. at 762. CPNI communications within a carrier itself — such as internal communications between different personnel or divisions within the same carrier — do not merely propose commercial transactions. Rather, they convey raw, factual information stemming directly from the service relationship. Such communications are thus entitled to full and undiluted First Amendment protection, rather than merely the intermediate scrutiny triggered by restrictions on commercial speech. However, because the *CPNI Order* cannot survive even intermediate scrutiny, *a fortiori* it could not pass muster under full First Amendment scrutiny.

advances" a "substantial interest" and "is no more extensive than necessary." *44 Liquormart, Inc. v. Rhode Island*, 116 S. Ct. 1495, 1509 (1996) (plurality opinion). In recent years, the Supreme Court has repeatedly struck down restrictions on commercial speech under this standard. *See Liquormart*, 116 S. Ct. at 1509-10; *id.* at 1521 (O'Connor, J., concurring); *Rubin v. Coors Brewing Co.*, 514 U.S. 476, 487-90 (1995); *Ibanez v. Florida Dept. of Business & Professional Reg.*, 512 U.S. 136, 142-44 (1994); *City of Cincinnati v. Discovery Network, Inc.*, 507 U.S. 410, 416-17 (1993); *Edenfield v. Fane*, 507 U.S. 761, 767-68 (1993); *see also Revo v. Disciplinary Bd. of the Supreme Court of the State of New Mexico*, 106 F.3d 929, 935-36 (10th Cir.), *cert. denied*, 117 S. Ct. 2515 (1997).

The *CPNI Order* should similarly be invalidated, because the Government cannot meet its burden here.

a. The FCC Cannot Demonstrate the Existence of a Substantial Governmental Interest

The Supreme Court has instructed that "a governmental body seeking to sustain a restriction on commercial speech must demonstrate that the harms it recites are real and that its restriction will in fact alleviate them to a material degree." *Edenfeld v. Fane*, 507 U.S. 761, 770-71 (1993). That burden "is not satisfied by mere speculation or conjecture," *id.* at 770, or by "anecdotal evidence and educated guesses." *Rubin v. Coors Brewing*, 514 U.S. at 490.

In this case, the FCC did not even articulate with any precision the privacy interest sought to be advanced. Nor did it deny that its *CPNI Order* will actually result in more invasions of customer privacy and solitude. If carriers cannot identify and communicate with individual customers based on their likely interest in receiving information about specific new services, they will be forced (in those instances where they do not remain silent) to use blanketed "broadcast-type" telemarketing speech fashioned for an "all customer" audience — the very sort of solicitations that the FCC itself has branded a nuisance. *See CPNI Order* at ¶ 113 (unsolicited telemarketing can be a nuisance); *BNA Third Order on Reconsideration*, 11 FCC Rcd. 6835,

6848-49 ¶ 23 (1996) ("unsolicited marketing contacts are in fact a nuisance, and we may take notice of this fact").

Even if the FCC could articulate a privacy interest in this case, it would be unduly speculative. The Commission itself has repeatedly and extensively documented, over many years, that an affirmative consent requirement is not needed to protect either customer privacy or competitive equity, and that there are many benefits to consumers from permitting CPNI to be used by carriers without prior affirmative consent. *See* pp. 7-8, *supra.* Without exception, reviewing courts have upheld the Commission's determinations. Further, the record demonstrates that use of service relationship or account information to discuss services, including "out of category" services, is consistent with customer expectations and that customers trust carriers to protect their privacy. *See* pp. 7-8, 12-15, *supra.* In fact, carriers with existing customer relationships have every incentive to cultivate customer goodwill and honor their customers' wishes. Moreover, expert agencies well versed in privacy issues have concluded that a prior affirmative consent requirement for individually-identifiable information such as CPNI is unnecessary and unwise. *See* pp. 18-19, *supra.*

Even in the *CPNI Order*, the FCC acknowledged that customer approval "can be *inferred* in the context of an existing customer-carrier relationship" in some circumstances. *CPNI Order* at ¶ 23 (emphasis in original). Thus, the FCC agreed "that Congress recognized . . . that customers expect carriers with which they maintain an established relationship will use information derived through the course of that relationship to improve the customer's existing service" (*CPNI Order* at ¶ 54); that there are no significant privacy concerns with respect to the sharing of CPNI within an integrated firm (*CPNI Order* at n. 203); and that "customers expect their carriers to offer related offerings within the total service to which they subscribe." *Id.* at n. 372; *see also* n. 206. Inexplicably, however, the FCC insisted that customer marketing expectations did not "extend to all of a carrier's available service offerings." *Id.* at n.372. The

Commission could cite no evidence to support this hair-splitting assertion. And its micro-managing cannot be squared with the central "deregulatory"[57] thrust of the 1996 Act.

The FCC's defense of the *CPNI Order* thus rests on the kind of impermissible speculation that cannot suffice under intermediate scrutiny. In *Turner Broadcasting*, a plurality of the Court explained that, even when Congress makes "unusually detailed" factual findings that "are recited in the text of the Act itself," 512 U.S. at 632, 646, in a First Amendment case a reviewing court is obligated to exercise "independent judgment" to ensure that the Government has "demonstrate[d] that the recited harms are real, not merely conjectural, and that the regulation will in fact alleviate these harms in a direct and material way." *Id.* at 665, 666. The cable must-carry rules were adopted by Congress along with extensive factual findings made in the text of the statute itself. In addition, the Court noted that the factual development on remand had yielded "a record of tens of thousands of pages" of evidence. *Turner Broadcasting System, Inc. v. FCC*, 117 S. Ct. 1174, 1185 (1997) (*Turner II*) (internal quotation omitted). The Court stressed that there was a "substantial basis to support Congress' conclusion that a real threat justified enactment of the must-carry provisions." 117 S. Ct. at 1190. The Court pointed to "specific support" for Congress' conclusion (*id.*): "substantive evidence" and "contemporaneous stud[ies]" regarding market structure and market power exercised by cable operators (*id.* at 1192-93); and "[e]mpirical research in the record before Congress" (*id.* at 1195).

In contrast, here the FCC cannot show any articulated or detailed congressional findings to support its position. Based on its position in the *CPNI Order*, the FCC will no doubt argue here that Congress, in adopting Section 222, essentially rejected the rationale underlying the Commission's prior CPNI regulations. But if the FCC's newly prescribed CPNI rules had truly been intended by Congress, one would expect — given their unprecedented nature — some discussion of the significance of a prior affirmative consent requirement in the legislative history

[57] Joint Statement of Committee of Conference, S. Conf. Rep. No. 230, 104th Cong., 2d Sess. 113 (1996).

of Section 222. But no such discussion exists. The absence of such legislative history is equivalent to "the dog that did not bark." *Chisom v. Roemer*, 501 U.S. 380, 396 n.23 (1991) (citing A. Conan Doyle, *Silver Blaze*, in THE COMPLETE SHERLOCK HOLMES 335 (1927)).

And even if there had been some type of congressional expression of dissent with the FCC's previous regulatory approach, Congress may not by fiat override First Amendment rights simply by declaring existing administrative schemes inadequate. That much is clear from the Supreme Court's decision in *Sable Communications of California, Inc. v. FCC*, 492 U.S. 115 (1989), which invalidated a federal "dial-a-porn" statute and rejected Congress' unsupported assertion that the FCC's previous rules were inadequate to protect minors. The Court held that, "[b]eyond the fact that whatever deference is due legislative findings would not foreclose our independent judgment of the facts bearing on an issue of constitutional law, our answer is that the congressional record contains no legislative findings that would justify us in concluding that there is no constitutionally acceptable less restrictive means, short of a total ban, to achieve the Government's interest in protecting minors." *Id.* at 129. The Court noted that "[the legislative] record contains no evidence as to how effective or ineffective the FCC's most recent regulations were or might prove to be," but only "conclusory statements" regarding the FCC's rules. *Id.* at 129-30. Here the legislative record does not contain even such "conclusory statements."

The FCC cannot establish the existence of a substantial governmental interest in this case.

b. The CPNI Rules Are Not Narrowly Tailored to Any Substantial Governmental Interest

Even if the Government could assert a substantial interest here, the *CPNI Order* would not be a narrowly tailored means of advancing it. A notice-and-opt-out rule, which enables a customer to request that CPNI pertaining to him not be used to contact him, gives the customer ample means to protect his privacy without trenching on speech. The FCC, along with other expert agencies, has previously documented in detail the wisdom of such a "do not disturb" policy, which is the constitutionally required solution. *See Martin*, 319 U.S. at 148. The notice-

and-opt-out approach is a familiar device in Fed. R. Civ. P. 23 class actions and other situations even when grievous personal injury, huge financial stakes, or other issues of great moment are at stake. It is certainly an obvious and simple alternative in the case of telephone company CPNI.

The proven availability of a notice-and-opt-out rule in this context demonstrates that the stringent approach taken in the *CPNI Order* is not narrowly tailored to the asserted interest. *44 Liquormart, Inc. v. Rhode Island*, 116 S. Ct. 1495, 1510 (1996) ("It is perfectly obvious that alternative forms of regulation that would not involve any restriction on speech would be more likely to achieve the [Government's] goal[.]"); *Rubin v. Coors Brewing*, 514 U.S. at 490 ("We agree that the availability of these options, all of which could advance the Government's asserted interest in a manner less intrusive to respondent's First Amendment rights, indicates that [the statute] is more extensive than necessary."); *City of Cincinnati v. Discovery Network, Inc.*, 507 U.S. 410, 417 & n.13 (1993) (considering possible alternatives to restriction on speech); *Central Hudson Gas & Elec. Corp. v. Public Serv. Comm'n*, 447 U.S. 557, 566, 570 (1980) (government must make showing "that a more limited restriction" on speech "would not serve adequately the [governmental] interests").

The *CPNI Order* and the accompanying rule amendments are not narrowly tailored to any substantial governmental interest and are therefore invalid.

B. THE *ORDER* FAILS TO GIVE PROPER WEIGHT TO THE FIFTH AMENDMENT PROPERTY INTERESTS IMPLICATED BY THE CPNI RULES

The *CPNI Order* also raises grave constitutional issues under the Takings Clause of the Fifth Amendment. The Commission stripped carriers of their property interest in CPNI altogether by declaring that "to the extent CPNI is property . . . it is better understood as belonging to the customer, not the carrier." *CPNI Order* at ¶ 43.

The FCC implemented this pronouncement by imposing a prior affirmative consent requirement for carrier use of CPNI outside existing service categories. As already noted, such customer veto power on carriers' ability to use CPNI for productive (indeed, constitutionally

protected) purposes will have a devastating effect. In short, the *CPNI Order* denies carriers the ability to use their valuable property in order to promote the supposed social policies favored by the Commission.

Fifth Amendment analysis must begin with the Supreme Court's decision in *Ruckelshaus v. Monsanto Co.*, 467 U.S. 986, 1001 (1984), which held that the Takings Clause protects stored data and that the government's use of private proprietary research data constituted a compensable taking. Similarly, an appropriation of a carrier's proprietary commercial business information pertaining to its transactions with its customers amounts to a taking. As one scholar has concluded in the context of customer information, "[a] legislative, regulatory, or even judicial determination that denies processors the right to use their data could very likely constitute a taking and require compensation. . . . [F]or the billions of data files currently processed and used by U.S. individuals and institutions, a dramatic alteration on user rights makes a compelling case for the existence of a taking." Cate, PRIVACY IN THE INFORMATION AGE, *supra*, at 74.

The FCC's decree that CPNI belongs to customers, not carriers, does not avoid the takings principle. Rather, it *underscores* the constitutional violation. The Government may not divest a private person of his property "by ipse dixit. . . . This is the very kind of thing that the Taking Clause of the Fifth Amendment was meant to prevent." *Webb's Fabulous Pharmacies, Inc. v. Beckwith*, 449 U.S. 155, 164 (1980). The FCC "may not sidestep the Takings Clause by disavowing traditional property interests[.]" *Phillips v. Washington Legal Foundation*, 118 S. Ct. 1925, 1931 (1998). In *Phillips*, the Supreme Court held that interest earned on client funds in IOLTA accounts is "private property" of the client, notwithstanding a state's attempt to deem the interest to be public property. In the same way, the FCC may not decree that carriers no longer own their customer information. *See also Preseault v. ICC*, 494 U.S. 1, 20 (1990) (O'Connor, J., joined by Scalia and Kennedy, JJ., concurring) (opining that federal agency could not override state-law entitlements by deeming reversionary interests preempted under federal law).

In this case, it is clear that CPNI belongs to a carrier, not to the customer. The telephone company, not its customers, owns its property. "The relation between the company and its

customers is not that of partners, agent and principal, or trustee and beneficiary." *Board of Pub. Util. Comm'rs v. New York Tel. Co.*, 271 U.S. 23, 31 (1926). "Customers pay for service, not for the property used to render it....By paying bills for service, they do not acquire any interest, legal or equitable, in the property used for their convenience or in the funds of the company." *Id.; see also Pacific Gas & Electric Co. v. Public Utilities Comm'n*, 475 U.S. 1, 22 n.1 (1986) (Marshall, J., concurring in the judgment); *Simpson v. Shepard*, 230 U.S. 352, 454 (1913) (a utility's "property is held in private ownership").

CPNI is a record of the subscription for service which is provided and delivered over the *carrier's* network. CPNI is gathered, organized, maintained, and stored by carriers, not by customers. If a third party were to break into a carrier's computers and steal CPNI, it would be the carrier (and not individual subscribers) who would have a cause of action for conversion. The Commission did not deny that CPNI is "commercially valuable to carriers." *CPNI Order* at ¶ 2. The Commission itself explained that carriers "view CPNI as an important asset of their business" and "hope to use CPNI as an integral part of their future marketing plans." *Id.* at ¶ 22.

For the carriers who have spent billions of dollars accumulating CPNI on the settled understanding that they owned it, the FCC's proclamation that the property now belongs to customers upsets investment-backed expectations that the Takings Clause protects. *Monsanto*, 467 U.S. at 1005; *Kaiser Aetna v. United States*, 444 U.S. 164, 175 (1979). Indeed, the Supreme Court recently warned that "statutes should not be construed in a manner that would impair existing property rights," because doing so "can deprive citizens of legitimate expectations and upset settled transactions." *Eastern Enterprises v. Apfel*, 118 S. Ct. 2131, 2151 (1998) (plurality opinion) (internal quotation omitted). In *Eastern Enterprises*, the Court held that a federal coal miner health benefit statute could not be applied retroactively, with a plurality finding the law an impermissible taking, rather than an appropriate regulatory initiative, because of "the economic impact of the regulation, the extent to which the regulation interferes with investment-backed

expectations, and the character of the governmental action." *Id.* at 2146 (internal citation omitted).[58]

That CPNI pertains to the purchasing characteristics of customers does not give them a property interest in it. Even personal data like telephone numbers, addresses, social security numbers, and medical history — let alone records of purchases and economic transactions — are almost always owned by someone else: the Post Office, the government, a bank, or a physician or hospital.[59] A surveillance camera outside a bank or department store may capture the image of persons entering or leaving the establishment without their permission. The resulting footage belongs to the bank or the store, not to the customers, even though their images are depicted in it. 17 U.S.C. §§ 101-06. In the same way, "[a] data processor exercises property rights in his data because of his investment in collecting and aggregating them with other useful data. It is the often substantial investment that is necessary to make data accessible and useful, as well as the data's content, that the law protects." Cate, PRIVACY IN THE INFORMATION AGE, *supra*, at 74. As one noted scholar has observed, "the expand[ing] protection for commercial information reflects a growing awareness that the legal system's recognition of the property status of such information promotes socially useful behavior" and therefore encourages reliance by data processors. Arthur R. Miller, *Confidentiality, Protective Orders, and Public Access to the Courts*, 105 HARV. L. REV. 427, 469 (1991).

To hold that customers rather than carriers own CPNI would have revolutionary implications for a panoply of service companies, such as credit card companies, mail order catalogs, direct marketing companies, and other databases housing comparable consumer

[58] Justice Kennedy, concurring in the judgment and dissenting in part, would have applied the same factors as a matter of substantive due process.

[59] The Supreme Court has held that individuals have no reasonable expectation of privacy in the telephone numbers dialed from their phones, *see Smith v. Maryland*, 442 U.S. 735 (1979), or even with respect to checks and deposit slips used in banking. *United States v. Miller*, 425 U.S. 435, 443 (1976); *see also California Bankers Ass'n v. Schultz*, 416 U.S. 21, 69-70, 73-76 (1974) (upholding numerous banking transaction recordkeeping and reporting requirements).

information. The assets these companies have developed through the investments of billions of dollars would be wiped out. And if personal information is property of the customer, then the implication is that the "owner" must give permission for every use or collection of the information (personal address books and Rolodex files, for example), not just commercial uses. The consequences of the FCC's pronouncement are as staggering as they are unanalyzed by the Commission.

The Commission tried to defend its CPNI restrictions by maintaining that its *Order* "does not deny all economically beneficial use of property." *CPNI Order* at ¶ 43 (internal quotation). But the *Order does* destroy the value of that portion of the CPNI as to which consumer consents cannot be obtained. It may no longer be used for communications between corporate affiliates and divisions, or for communications with customers for new services outside the existing service relationship. Further, the Supreme Court has repeatedly rejected the FCC's argument that a regulation that does not take every last stick in a bundle of property rights cannot be a taking. In *Hodel v. Irving*, 481 U.S. 704 (1987), for example, the Court struck down a federal statute restricting the ability of Native Americans to pass certain undivided fractional interest in land to their heirs by intestacy or devise, even though they retained full beneficial use of the property during their lifetimes as well as the right to convey it inter vivos. The Court explained that "[t]he fact that it may be possible for the owners of these interests to effectively control disposition upon death through complex inter vivos transactions such as revocable trusts is simply not an adequate substitute for the rights taken, given the nature of the property." *Id.* at 716. In *Babbitt v. Youpee*, 117 S. Ct. 727 (1997), the Court reaffirmed this holding and invalidated an amended version of the same statute. The Court rejected the Government's contention that the statute satisfied the Constitution's demand because it did not diminish the owner's right to use or enjoy property during his lifetime, and did not affect the right to transfer property at death through non-probate means. The Court opined that "[t]hese arguments did not persuade us in *Irving* and they are no more persuasive today." *Id.* at 733.

The FCC's argument was also rejected in *Ruckelshaus,* where the Court specifically noted that the data submitted with a pesticide application has a variety of uses to the producer. *See* 467 U.S. at 1012 ("That the data retain usefulness for Monsanto even after they are disclosed — for example, as bases from which to develop new products or refine old products, as marketing and advertising tools, or as information necessary to obtain registration in foreign countries — is irrelevant to the determination of the economic impact of the EPA action on Monsanto's property right.").

Here, the *CPNI Order's* severe burden on carriers' ability to use CPNI to market new categories of services raises such serious Fifth Amendment questions that it should be invalidated.

C. THE *ORDER* IS A GRATUITOUSLY SEVERE CONSTRUCTION OF SECTION 222

In light of the serious constitutional questions presented by the FCC's interpretation of Section 222, the FCC was bound to construe the statute to avoid those constitutional questions. "[W]here an otherwise acceptable construction of a statute would raise serious constitutional problems, the Court will construe the statute to avoid such problems." *Edward J. DeBartolo Corp. v. Florida Gulf Coast Building & Constr. Trades Council*, 485 U.S. 568, 575 (1988).[60]

When, as here, an administrative interpretation raises such constitutional concerns, the agency's construction of the statute is not entitled to deference. *Edward J. DeBartolo Corp.*, 485 U.S. 568 at 574-577; *Bill Johnson's Restaurants, Inc. v. NLRB*, 461 U.S. 731, 742-743 (1983). In particular, the deference ordinarily afforded administrative action under *Chevron, U.S.A., Inc. v. NRDC, Inc.*, 467 U.S. 837 (1984), is wholly inapplicable here. *See Bell Atlantic Corp. v. FCC*, 24 F.3d 1441, 1445 (D.C. Cir. 1994).

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[60] *See also United States v. X-Citement Video, Inc.*, 513 U.S. 64, 78 (1994) (construing statute in light of First Amendment question "to eliminate those doubts so long as such a reading is not plainly contrary to the intent of Congress"); *see also NLRB v. Catholic Bishop of Chicago*, 440 U.S. 490, 506-507 (1979); *Machinists v. Street,* 367 U.S. 740, 749-750 (1961); *Crowell v. Benson*, 285 U.S. 22, 62 (1932).

Further, an agency's failure "to give adequate consideration" to constitutional objections to agency action is "the very paradigm of arbitrary and capricious administrative action." *Meredith Corp. v. FCC*, 809 F.2d 863, 865, 874 (D.C. Cir. 1987).

The need for clear congressional authorization is especially urgent where administrative action raises takings issues, for "[w]hen there is no authorization by an act of Congress or the Constitution for the Executive to take private property, an effective taking by the Executive is unlawful because it usurps Congress's constitutionally granted powers of lawmaking and appropriation." *Ramirez de Arellano v. Weinberger*, 745 F.2d 1500, 1510 (D.C. Cir. 1984) (*en banc*), *vacated on other grounds*, 471 U.S. 1113 (1985); *see also United States v. Security Indus. Bank*, 459 U.S. 70, 78, 82 (1982) (rejecting construction of statute that would raise taking questions); *Western Union Tel. Co. v. Pennsylvania R.R.*, 195 U.S. 540, 569 (1904) (statutes are not read to delegate power to take property unless they do so "in express terms or by necessary implication"). Thus, in *Bell Atlantic Corp. v. FCC*, 24 F.3d 1441 (D.C. Cir. 1994), the Court of Appeals invalidated certain FCC rules in order to avoid a takings issue. The court held that Congress had not clearly granted the FCC the authority to take private property for public use and that the Commission was therefore forbidden from adopting regulations that "directly implicate[d] the Just Compensation Clause of the Fifth Amendment." *Id.* at 1445.

The same analysis is dispositive here, for the Commission's *CPNI Order* flouts all of these principles of restraint. The *Order* raises serious constitutional questions. Yet nowhere is there clear statutory language compelling the FCC's interpretation of Section 222 — much less an unmistakably plain congressional intent to impose such stringent CPNI rules. Indeed, the Commission itself confessed that the word "approval" was "ambiguous" (*CPNI Order* at ¶ 87), and that the statutory issues were sufficiently unclear that a "clarification of section 222" was necessary. *CPNI Order* at ¶ 14. The FCC acknowledged that, "while section 222(c)(1) requires customer approval for carrier use of CPNI outside the scope of sections 222(c)(1)(A) and (B), it does not expressly state the form of this approval." *CPNI Order* ¶ 91; *see also id.* at ¶ 86 ("section 222(c)(1) does not specific what kind of approval is required"). Indeed, the words

"prior," "express," or "affirmative" do not appear in Section 222(c)(1). By contrast, Section 222(c)(2) refers to an "affirmative" request. "When Congress uses explicit language in one part of a statute . . . and then uses different language in another part of the same statute, a strong inference arises that the two provisions do not mean the same thing." *Persinger v. Islamic Republic of Iran*, 729 F.2d 835, 843 (D.C. Cir. 1984).

There were numerous reasons that the Commission could and should have interpreted "approval" to include authorization pursuant to a notice-and-opt-out arrangement (for use of CPNI by carriers with existing relationships with the customers in question) rather than requiring only prior affirmative customer consent in order to avoid the constitutional issues raised by the *Order*:

• "Approval" can easily and reasonably be inferred in the context of an existing customer-carrier relationship. That is why the Commission adopted a "total service" approach that would permit a carrier providing both local and cellular service to a customer to use for marketing and speech purposes the CPNI from either service, *without seeking prior consent*:

> [T]he language of section 222(c)(1)(A) and (B) reflects Congress' judgment that customer approval for carriers to use, disclose, and permit access to CPNI can be *inferred* in the context of an existing customer-carrier relationship. This is so because the customer is aware that its carrier has access to CPNI, and, through subscription to the carrier's service, has implicitly approved the carrier's use of CPNI within the existing relationship.

CPNI Order at ¶ 23 (emphasis in original). In the same way, approval can be inferred across service categories in the context of an existing customer-carrier relationship, especially when the customer is given an opt-out opportunity.

• Section 222(c)(1) uses the term "approval." The word "approve" "in its strictest etymological construction, is an after-the-fact ratification." *AT&T Communications of the Southwest, Inc. v. Southwestern Bell Telephone Company*, No. A 96-CA-397 SS, at 9-10 (W.D.Tex. 1996). In fact, the FCC itself cited a dictionary definition of "approve" as meaning

"ratify." *CPNI Order* ¶ 91 n.336. A notice-and-opt-out process is therefore a permissible way of ascertaining customer "approval."

• The FCC construed Section 222(c)(1) in a manner compelled by neither the language of the statute nor its legislative history, and in a manner at odds with the Commission's own long-standing position that requiring prior CPNI authorizations from customers was impracticable and unnecessary, and would result in substantial denials of consents due to customer inertia and confusion. There is no indication that Congress in the 1996 Act sought to depart so dramatically from this longstanding regulatory practice.

• Indeed, in light of the significant differences between Section 222 and earlier legislative proposals, it is plain that Congress specifically did *not* mandate affirmative consents from customers. Section 222 was based on S. 652 and H.R. 1555, which, in turn, emerged from a series of House bills proposed by Rep. Edward Markey. H.R. 3432, for example, would have required an "affirmative request" from the customer before a local exchange carrier could use CPNI beyond certain specified purposes. H.R. 3626, the next legislative proposal, expanded the scope of the proposal to all carriers. It also *removed* the word "affirmative" and substituted the word "approval." The legislative history thus suggests that Congress meant *not* to require "affirmative" customer consent in Section 222(c)(1).

• Furthermore, Congress itself acknowledged that customers want "one-stop shopping."[61] Moreover, to facilitate the integrated marketplace of the future, Congress explicitly granted telecommunications carriers joint marketing authority with respect to long distance,[62] electronic publishing,[63] and wireless services.[64] Joint marketing necessarily entails speech about different

[61] *See* Senate Report on S.652 (Report No. 104-230) at 22-23 ("the ability to bundle telecommunications, information, and cable services into a single package to create 'one-stop-shopping' will be a significant competitive marketing tool" such that BOCs and their affiliates should be permitted to jointly market services).

[62] 47 U.S.C. § 272.

[63] 47 U.S.C. § 274.

[64] 47 U.S.C. § 601.

products and services, and the formulation of any such speech requires CPNI. As the FCC has acknowledged, "joint marketing . . . necessarily involves sharing of some customer network information." *Universal Card Order*, 8 FCC Rcd. at 8787 ¶ 27. There is nothing in Section 222 to suggest that Congress meant to erect an insurmountable barrier to communications about those services it allowed to be jointly marketed.

• The *CPNI Order* is utterly unprecedented. In situations ranging from credit cards to mail order catalogs to grocery purchases, companies are generally free to do whatever they wish with respect to individually-identifiable information generated in the course of the commercial relationship. Where regulations do exist (typically involving more sensitive information than is at issue in this case), they fall far short of the stringent rules adopted by the FCC here. For example, cable operators are allowed to use subscriber information for their own business purposes and are required to obtain written or electronic consent (*i.e.*, affirmative approval), *only* to share subscriber information with unaffiliated third persons. 47 U.S.C. § 551(c)(1). Under the 1996 Consumer Credit Reporting Reform Act, credit reporting agencies may furnish consumer credit information for marketing credit or insurance opportunities to consumers, so long as the agency establishes a toll-free number so that consumers can call and opt out by having their names removed from lists for direct marketing purposes. 15 U.S.C. § 1681b(c)(5). The Uniform Health Care Information Act, adopted by the National Conference of Commissioners on Uniform State Laws, *see* 9 U.L.A. 475 (1988 & Supp. 1992), creates an opt-out scheme for certain disclosures of medical information *Id.* at §§ 2-103, 2-104. The Driver's Privacy Protection Act of 1994 requires states to allow drivers to opt out of having personal motor vehicle information released. 18 U.S.C. § 2721(b)(11)-(12). Numerous states have adopted opt-out statutes for release of other public records information.[65] Even the Video Privacy Protection Act of 1988, adopted in response to the disclosure of the list of videos rented by Supreme Court nominees,

[65] Privacy & Legislative Associates Letter at 14.

allows disclosure of data about customer viewing habits for marketing purposes if the consumer has been given an opportunity to opt out. 18 U.S.C. § 2710(b)(2)(D).

In short, the universal legal baseline is that customers are not viewed as having the kind of privacy or property interests in commercial proprietary information that would grant them a legally enforceable right to veto transmission of the information to third parties, much less presumptively to deny the use of that information by the entity that created it. It is untenable to suppose, as did the FCC, that Congress would have intended so casually to depart from this baseline without comment beyond the choice of the word "approval."

• In issuing the *CPNI Order*, the Commission substituted its own (clearly revisionist) notions of "customer expectations" for solid record — including expert —evidence,[66] departed from long-standing Commission precedent, and disregarded the recommendations of agencies far more expert in the matter of customer privacy than the Commission. The FCC imposed its prior affirmative consent requirement in disregard of statistically valid public opinion survey evidence in the record documenting that customers trust their existing telecommunications carriers, expect CPNI to be used to market products and services of all types with them, and are even more comfortable with this use of CPNI when it is accompanied by a notice and opt out procedure. Although the Commission sought to dismiss this empirical evidence, the criticisms it offered were off-base[67] and flew in the face of the FCC's **own directive** to carriers regarding the

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[66] *Compare In the Matter of Petition to Promulgate a Rule Restricting the Advertising of Over-the-Counter Drugs on Television*, 62 FCC 2d 465, 468 n.11 (1976) (noting the FCC's lack of "claim to expertise in the field of behavioral research" and observing that "research focusing on emotionally and politically charged issues" "should best be left to independent organizations which are expert in such matters and have no direct responsibility for . . . regulation").

[67] The Commission claimed that one of the questions in the Westin study "refers to the examination of records by customer service representatives as 'normal' and implies that the representative will be looking only at the services the customer has before offering new services" and not more sensitive information "such as destination-related information." *CPNI Order* at ¶ 62. But the question carried no such implication. It stated: "[W]hen you call your local telephone company to discuss your services, the customer service representative that you speak with normally looks up your billing and account service record." *Id.* at n. 227 (quoting the question). The description of what a service representative "normally" does is accurate (*i.e.*,

importance of market survey evidence in fashioning arguments and crafting educated regulatory decisions.[68]

The Commission made no attempt to construe Section 222 in a manner that would avoid the constitutional questions under the First and Fifth Amendments. It devoted a **total of six paragraphs** (out of an *Order* containing 261 paragraphs) addressing the constitutional issues raised by petitioners.[69] By itself, this approach was an abuse of discretion and warrants vacating the *CPNI Order*.

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looks up the service record and, if appropriate, the billing record), and the reference to "billing information" clearly implies call-detail information, contrary to the Commission's assumption.

[68] *See In the Matter of Implementation of the Subscriber Carrier Selection Changes Provisions of the Telecommunications Act of 1996; Policies and Rules Concerning Unauthorized Changes of Consumers' Long Distance Carriers*, CC Docket No. 94-129, *Further Notice of Proposed Rulemaking and Memorandum Opinion and Order on Reconsideration*, 12 FCC Rcd. 10674, at ¶ 49 (1997)(chastising AT&T and other commentors for failure to "cite to any relevant market research supporting their claims of consumer indifference or opposition" to proposed regulatory requirement); *In the Matter of The Revision of Programming and Commercialization Polices, Ascertainment Requirements, and Program Log Requirements for Commercial Television Stations*, MM Docket No. 83-670, 98 FCC 2d 1076, ¶ 64 (1984) (noting approvingly the "empirical data" previously outlined by the FCC in its Notice of Proposed Rulemaking).

[69] The total might be increased by two paragraphs if one counts the paragraphs in which the FCC paraphrased the position of the commenters.

CONCLUSION

The petition for review should be granted; the *CPNI Order* and accompanying rule amendments to 47 C.F.R. §§ 64.2005 and 64.2007 should be vacated; and the matter should be remanded to the FCC for further consideration.

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STATEMENT REGARDING ORAL ARGUMENT

Petitioner and Intervenors request oral argument. This case presents free speech and takings questions with national significance, as well as important questions of statutory interpretation that are of first impression. Petitioner and Intervenors believe the Court would find oral argument helpful in reaching its decision.

TAB 12

ORAL ARGUMENT REQUESTED

U.S. COURT OF APPEALS
10th CIRCUIT
98 OCT 15 PM 4:43

IN THE
UNITED STATES COURT OF APPEALS
FOR THE TENTH CIRCUIT

No. 98-9518

U S WEST, INC.,

Petitioner,

v.

FEDERAL COMMUNICATIONS COMMISSION and
UNITED STATES OF AMERICA,

Respondents,

BELLSOUTH CORPORATION and
SBC COMMUNICATIONS INC., *et al.*,

Intervenors.

On Petition for Review of an Order
of the Federal Communications Commission

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REPLY BRIEF FOR PETITIONER AND INTERVENORS
INTRODUCTION AND SUMMARY OF ARGUMENT

The opening brief of petitioner and intervenors (collectively, "petitioners") demonstrated that the FCC's construction of Section 222, which addresses customer proprietary network information ("CPNI"), is unreasonable and arbitrary in several fundamental respects: it contradicts Congress' intent in enacting Section 222; represents a sudden and unwarranted departure from prior Commission policy; and is utterly unprecedented among federal laws. In light of the serious constitutional issues raised by the FCC's interpretation of Section 222, the FCC was bound to construe the statute to avoid those constitutional questions. *E.g., Edward J. DeBartolo Corp. v. Florida Gulf Coast Building & Constr. Trades Council*, 485 U.S. 568, 575 (1988). Indeed, the FCC's very efforts to brush off these grave constitutional issues warrants vacating the CPNI rules, because that failure "to give adequate consideration" to constitutional objections to agency action is "the very paradigm of arbitrary and capricious administrative action." *Meredith Corp. v. FCC*, 809 F.2d 863, 865, 874 (D.C. Cir. 1987).

The FCC and its supporting intervenors (collectively, "respondents") mischaracterize the nature of CPNI and distort what is at issue in this case. CPNI is generated, gathered, organized, maintained, and stored by *carriers* in the course of providing services to subscribers. After a customer requests particular services, the *carrier* generates a record of the services. Respondents further confuse the issues of (i) CPNI in the hands of a carrier that has an existing relationship with a customer with (ii) third-party disclosure of CPNI to unrelated, unaffiliated entities that do not have any existing relationship with the customer. Respondents' privacy argument focuses on third-party disclosure and is therefore irrelevant here.

Respondents also claim that CPNI "belongs to" customers. That, too, is erroneous. Although consumers undoubtedly have certain expectations regarding carriers' use of CPNI –

which the record demonstrates petitioners have always respected – CPNI is owned by carriers. Respondents' contrary view is a radical one that, were this Court to embrace it, would turn well-settled property law on its head and would profoundly upset the property rights of mail-order catalogs, credit card companies, and practically any other firm that, as part of its routine business operations, maintains individually identifiable customer information.

Finally, respondents misstate the applicable First and Fifth Amendment principles. They insist that the CPNI rules do not by their express terms dictate what carriers can and cannot say. However, they ignore the direct choking impact of the FCC's rules on intra-corporate communications and also ignore the Supreme Court's repeated teaching that the First Amendment is concerned with the *practical effect* of a regulation on speech. Here, the practical effect of the FCC's rules on carrier-customer communication is devastating.

With respect to the Fifth Amendment, respondents' argument hinges on the mistaken premise that carriers have no reasonable, investment-backed expectation in owning or using CPNI. The CPNI rules should be vacated.

ARGUMENT
STANDARD OF REVIEW

Respondents plead for deference under *Chevron, U.S.A., Inc. v. NRDC, Inc.*, 467 U.S. 837 (1984). Yet the constitutional questions raised by the *CPNI Order* render such deference wholly inapplicable. *See Edward J. DeBartolo Corp.*, 485 U.S. at 574-77; *Bell Atlantic Corp. v. FCC*, 24 F.3d 1441, 1445 (D.C. Cir. 1994). This Court "review[s] agency action *de novo* to determine whether it was 'arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law.'" *City of Albuquerque v. Browner*, 97 F.3d 415, 424 (10th Cir. 1996), *cert. denied*, 118 S. Ct. 410 (1997).

A. THE *ORDER* RAISES GRAVE QUESTIONS UNDER THE FIRST AMENDMENT THAT THE FCC WAS REQUIRED TO AVOID.

1. **The Communication Of CPNI Is Speech.**

Respondents do not deny that CPNI is information, or that the creation, assembly, compilation, and/or communication of information lie at the core of what the First Amendment protects. The strained efforts of CPI to compare CPNI to "postage stamps, sheets of paper," or even a day-care center (CPI Br. at 6) are beside the point. The propriety of the CPNI rules must be judged solely according to the justifications put forward by the FCC, *see SEC v. Chenery Corp.*, 332 U.S. 194, 196 (1947); *see also Edenfield v. Fane*, 507 U.S. 761, 768 (1993), which never relied on such reasoning in the *CPNI Order*. Further, CPI's argument is frivolous on its own terms. CPNI is communicated from one speaker to another within a carrier (*i.e.*, from one employee to another), and also forms the basis for protected expression to customers. If anything, CPNI is far more integral to expression than many of the activities that the Supreme Court has held to be protected under the First Amendment. *E.g., Barnes v. Glen Theatre, Inc.*, 501 U.S. 560, 565-66 (1991) (plurality opinion) (nude dancing); *Clark v. Community for Creative Non-Violence*, 468 U.S. 288, 293 (1984) (assuming *arguendo* that sleeping in park is protected expression). Moreover, CPI's analogy proves the very opposite of what CPI appears to believe, for the Supreme Court has consistently applied the First Amendment to regulations falling wholly on *physical objects* like "sheets of paper" when they are essential ingredients in expression. *See Minneapolis Star v. Minnesota Comm'r of Revenue*, 460 U.S. 575, 581 (1983). A regulation purporting to govern only the cold type of a printing press can violate the First Amendment as effectively as a classic prior restraint.

2. **The CPNI Rules Abridge Speech.**

Respondents' primary position is that the *CPNI Order* does not have a constitutionally cognizable impact on speech because the rules "do not prohibit any carrier from soliciting

business from any customer." FCC Br. 26. Yet respondents concede, as the record in this case proves, that "[t]he carriers are almost certainly correct in their expectation that many customers will not give them advance approval" and that "customers would not give affirmative approval for use of their CPNI in a high percentage of cases – regardless of the level of confidence that might have built up over the years of the carrier-customer relationship." FCC Br. 19. Respondents admit (in classic understatement) that "Section 222 might have *some* effect on internal communications within a company." FCC Br. 26 (emphasis added); see also MCI Br. 3. In fact, the FCC has long recognized that "[u]nder a prior authorization rule, a large majority of mass market customers are likely to have their CPNI restricted through inaction . . . . Thus, a prior authorization rule would *vitiate* a BOC's ability to achieve efficiencies through integrated marketing to smaller customers." *Computer III Remand Order*, 6 FCC Rcd. 7571, 7610 n.155 (1991) (emphasis added).

a. <u>Burdens On Intra-Carrier Speech.</u>

The burden on speech cannot be dismissed as "an economic effect." FCC Br. 26. First, the CPNI rules have a prohibitive effect on CPNI-related communications within a telecommunications carrier, and within the carrier's corporate family: employees in different divisions, affiliates, and personnel within the same carrier will not be able to engage in related speech about certain customers because prior affirmative consents will, in the vast majority of cases, be difficult or impossible to obtain. For example, Mary Sue in the landline division is prohibited from talking to Linda May in the wireless division about customer John Jones and his possible interest in receiving information. This impact is precisely the "ban[] on the use of particular types or channels of communication" that respondents admit the First Amendment forbids. MCI Br. 4.

The FCC suggests that "restrictions on internal business communications do not present a substantial . . . First Amendment question," in light of the history of separate subsidiary requirements that have gone unchallenged in the courts. FCC Br. 27. But few, if any, of the FCC's structural separation rules have prevented different members of a corporate family from communicating with each other. Such rules generally require separation of ownership and control, but they neither compel nor induce silence. When separate subsidiary requirements have burdened speech and have been challenged, they have been struck down, as in *FEC v. Massachusetts Citizens for Life, Inc.*, 479 U.S. 238 (1986), where the Court held unconstitutional a federal statute requiring corporations to make political expenditures only through special segregated funds, as applied to a nonprofit advocacy group. *See id.* at 252-53 (plurality opinion); *id.* at 266 (O'Connor, J., concurring in part and in the judgment).

Moreover, under prior Commission policy, petitioners were authorized to offer customer premises equipment ("CPE"), and enhanced services in some cases, on an integrated basis, without structural separation. Opening Br. 4-10. The previous notice and opt-out options employed by the Commission did not appreciably infringe on the right of carriers to use CPNI for expressive purposes, *id.* at 17 n.42, and thus did not run afoul of First (or Fifth) Amendment rights. The FCC also overlooks new joint marketing opportunities reflected in the Act's separate subsidiary requirements, 47 U.S.C. §§ 272(g) (long distance), 274(c)(2) (electronic publishing), Pub. L. 104-104, § 601(d), 110 Stat. 143 (wireless) which opportunities were barred by pre-Act rules. 47 C.F.R. § 64.702(c)(1).

b. <u>Burdens On Carrier-Customer Speech.</u>

In addition to their effect on speech within a carrier's business, the CPNI rules have a devastating practical impact on carriers' communications with their customers. If prior affirmative consent cannot be obtained, carriers will be forbidden from using CPNI to discuss

with customers information about categories of services and products that the customers may need or desire. The CPNI rules thus prevent individualized or customized speech. This is exactly the kind of limitation on the "mode of carriers' speech" that respondents properly concede is within the First Amendment's ambit. MCI Br. 4. A carrier's ability to resort to "broadcast" speech to all customers on a blunderbuss basis is not an adequate substitute, for "[t]he First Amendment protects [the speakers'] right not only to advocate their cause but also to select what they believe to be the most effective means for so doing." *Meyer v. Grant*, 486 U.S. 414, 424 (1988). Thus, in *Shapero v. Kentucky Bar Ass'n*, 486 U.S. 466 (1988), the Supreme Court recognized an attorney's First Amendment right to send targeted solicitation letters to potential clients by name. *See also Edenfield v. Fane*, 507 U.S. 761, 770-71 (1993) (CPA's right to engage in in-person solicitation); *Rubin v. Coors Brewing Co.*, 514 U.S. 476, 488 (1995) (right to disclose alcohol content on beer labels (targeted speech)).

In *Revo v. Disciplinary Bd. of the Supreme Court of the State of New Mexico*, 106 F.3d 929, 935-36 (10th Cir.), *cert. denied*, 117 S. Ct. 2515 (1997), this Court invalidated a state bar rule prohibiting attorney direct mail advertisements to personal injury victims and family members of wrongful death victims, unless the recipient of the solicitation was a relative of the attorney sending the letter or had a prior personal, business or professional relationship with that attorney. That rule was *less* restrictive than the CPNI rules, which interfere even with established, ongoing carrier-customer relationships.

Respondents apparently concede that, if the CPNI rules explicitly barred carriers from engaging in individualized and customized speech, then the First Amendment would be implicated. They take the view that, short of such an express ban, the practical impact of the CPNI rules is not constitutionally cognizable. The Supreme Court squarely rejected that argument in *Riley v. National Federation of the Blind, Inc.*, 487 U.S. 781 (1988), holding that a

financial regulation of professional fundraisers could not be defended as a "merely economic" regulation having "only an indirect effect on protected speech." *Id.* at 789 n.5. The Court therefore struck down a rule limiting a professional fundraiser to a "reasonable" fee, even though by its terms the law did not ban any speech at all. *See also Secretary of State of Maryland v. Joseph H. Munson Co.*, 467 U.S. 947, 959-61 (1984); *Schaumburg v. Citizens for a Better Environment*, 444 U.S. 620, 632-36 (1980). The Court has frequently invalidated other laws that do not by their terms prohibit speech, but simply regulate activities having a connection to expression. *E.g., United States v. NTEU*, 513 U.S. 454, 469 (1995) (striking down a ban on honoraria); *Simon & Schuster, Inc. v. Members of New York State Crime Victims Bd.*, 502 U.S. 105 (1991) (invalidating law preventing criminals from profiting from publishing deals).

In none of these cases did the Supreme Court require an explicit ban on speech before striking down the laws in question. Rather, the Court has always looked to the law's practical effect. For example, respondents put great emphasis on *Martin v. Struthers*, 319 U.S. 141 (1943). CPI Br. 7; MCI Br. 4. But the ordinance invalidated in *Martin* did not expressly prohibit door to door solicitation. Rather, the ordinance made it unlawful "for any person distributing handbills, circulars, or other advertisements to ring the door bell, sound the door knocker, or otherwise summon the inmate or inmates of any residence to the door . . . ." 319 U.S. at 142. The solicitor was free to distribute handbills; he or she simply could not ring or knock. In *Meyer v. Grant*, 486 U.S. 414, 424 (1988), the Court struck down a ban on the payment of petition circulators, not a rule restricting what they could say. In *NAACP v. Claiborne Hardware Co.*, 458 U.S. 886, 912 (1982), the Court held that even generally applicable tort laws (which did not target speech at all) were unconstitutional as applied to an expressive boycott because of the "incidental effect on First Amendment freedoms." Respondents' argument is thus completely without merit because it ignores the practical effect of the CPNI rules.

c. The CPNI Rules Are Invalid Even If Petitioners' Expression Is Treated As Commercial Speech.

Respondents contend that "[m]arketing is generally considered 'commercial' speech." MCI Br. 5 n.4, apparently seeking to trivialize the carrier-customer speech burdened by the CPNI rules.[1] However, the Supreme Court has held that a restriction on commercial speech is invalid unless the government shows that it "directly and materially advances a substantial state interest in a manner no more extensive than necessary to serve that interest." *Ibanez v. Florida Dept. of Business & Professional Reg.*, 512 U.S. 136, 142, 143-44 (1994); *see also Revo*, 106 F.3d at 932 ("Protected commercial speech may also be regulated, but only if the government can show that (1) it has a substantial state interest in regulating the speech, (2) the regulation directly and materially advances that interest, and (3) the regulation is no more extensive than necessary to serve the interest.").

Respondents' assertion that this is a deferential, toothless standard is belied by the fact that, under this test, the Court has repeatedly struck down restrictions on commercial speech. *See 44 Liquormart, Inc. v. Rhode Island*, 116 S. Ct. 1495, 1509-10 (1996) (plurality opinion); *id.* at 1521 (O'Connor, J., concurring); *Rubin v. Coors Brewing Co.*, 514 U.S. 476, 487-90 (1995); *Ibanez*, 512 U.S. at 142-44 (1994); *City of Cincinnati v. Discovery Network, Inc.*, 507 U.S. 410, 416-17 (1993); *Edenfield v. Fane*, 507 U.S. at 767-68; *see also Revo*, 106 F.3d at 935-36.

Indeed, the only Supreme Court decision in recent years to uphold a restriction on commercial speech was *Florida Bar v. Went for It, Inc.*, 515 U.S. 618 (1995), a 5-4 ruling which

[1] Intra-carrier speech does not fall within "the core notion of commercial speech -- speech which does no more than propose a commercial transaction," *City of Cincinnati v. Discovery Network, Inc.*, 510 U.S. 407, 422 (1993) (citations omitted), and thus is entitled to full First Amendment protection. Many kinds of fully protected speech, including books providing financial advice, could be said to be "related solely to the economic interests" of the speaker and the listener. CPI Br. 9 n.5. That standard is not the appropriate test here.

upheld a state bar rule prohibiting lawyers from using targeted direct mail to solicit personal injury clients within 30 days of an accident. Unlike this case, *Florida Bar* involved a rule that was supported by extensive evidence and empirical studies. *Id.* at 626-27. Even so, the Court specifically agreed that a claim that the ban was too broad "would have force" but for the absence of "obvious less-burdensome alternatives to Florida's short temporal ban." *Id.* at 633. In concluding that the thirty-day ban was constitutional, the Court said "the palliative devised by the Bar to address these harms is narrow both in scope and in duration." *Id.* at 635. In *Revo*, this Court distinguished *Florida Bar* as a decision of limited application. *See Revo,* 106 F.3d at 935. By contrast, the CPNI rules are broad, not narrow, and perpetual, not temporary; they demonstrably burden far more speech than necessary in light of the proven, obvious and less burdensome opt-out alternative. See Part A-4(b), *infra*.

3. The CPNI Rules Are Not Narrowly Tailored To Any Important Governmental Interest In "Fair Competition."

Respondents contend that the CPNI rules serve the interests of "fair competition," which they accuse petitioners of overlooking. That is untrue. As discussed in detail in petitioners' opening brief (at 7 & n.11, 8 & n.12), the FCC has closely examined this question over the past decade and has repeatedly concluded that a prior affirmative consent rule is *not* needed to protect competition. In fact, the FCC found that such a rule would be *anti*-competitive and would injure consumers. If there was no competitive harm in CPE and enhanced services markets during the period when LECs held exclusive local franchises, it would be passing strange to suppose that there was more risk now that the 1996 Act has eliminated those franchises and has created local competition pursuant to 47 U.S.C. §§ 251-53. Mere speculation that the CPNI rules would serve a competitive purpose is inadequate. As this Court has opined, "we have an obligation to make an independent examination of the whole record in order to make sure that the speech regulation

does not constitute a forbidden intrusion on the field of free expression." *Revo*, 106 F.3d at 932. "The [Government's] burden 'is not satisfied by mere speculation and conjecture; rather, a governmental body seeking to sustain a restriction on commercial speech must demonstrate that the harms it recites are real and that its restriction will in fact alleviate them to a material degree.'" *Id.* at 933-34 (citation omitted).

Moreover, there is nothing in the 1996 Act to suggest that Congress took a different view from the FCC's pre-Act policy. Although, in discussing Section 222, Congress referred to "competitive . . . interests," S. Conf. Rep. No. 104-230, 104th Cong., 2d Sess. 205 (1996), Congress itself addressed that concern by applying Section 222 to *all* carriers, rather than only to AT&T, the BOCs, and GTE, as had been the FCC's prior policy. Congress itself struck the competitive balance, without otherwise altering the FCC's pre-Act opt-out approach.

Confidential customer information is widely used in other markets (*see* Part A-5, *infra*), even those involving regulated utilities, without any affirmative consent requirements, and without raising any concerns of unfair competition. *See Catlin v. Washington Energy Company*, 791 F.2d 1343 (9th Cir. 1986) (antitrust laws permitted utility to disclose customer list to its merchandising division to sell "vent damper" products, while withholding it from its competitors in the "vent damper" market). The FCC has undertaken no reasoned analysis to justify or even explain its evident conclusion that a different approach is compelled here

4. The CPNI Rules Are Not Narrowly Tailored To Any Important Governmental Interest In "Customer Privacy."

a. Respondents' Argument Rests On A Mischaracterization Of The Nature Of CPNI.

Respondents contend that CPNI relates to "private matters that citizens ordinarily would not be required to disclose to anyone" and involves "private data that customers ordinarily would not surrender to a telephone company or anyone else." FCC Br. 22, 31. However, a carrier

possesses this commercial information *not* because the customer "discloses" it (FCC Br. 22), but because the information represents the company's own record of its transaction with the customer, by means of its providing services to the customer. For example, respondents contend that it is somehow improper for a telephone carrier to know "how much the customer spends on telephone service," FCC Br. 3; but that claim illustrates the illogic of respondents' view. For information as to "how much the customer spends" is another way of expressing the carrier's *revenue*. Surely the carrier is perfectly entitled to record and use such data – indeed, it could hardly function otherwise. *See* Thomas E. McManus, Telephone Transaction-Generated Information: Rights and Restrictions 50 (Harvard Program on Information Resources Policy, May 1990) ("Generally, people and organizations have a right to make records of transactions to which they are a party, and they have control over those records. In a sense, when two parties enter into a contract, each party owns the records he or she keeps in the ordinary course of business.").[2]

A telecommunications carrier does not *receive* or *obtain* from its customers the information contained in its business records of the services provided to customers. Rather, after a customer requests particular telecommunications services, the carrier generates a record of the services actually provided. CPNI represents the *carrier's* record of the subscription for services provided and delivered over its own network. The information is generated, gathered, organized,

[2] Telephone users do not have an expectation of privacy in the numbers they dial, because they "typically know that they must convey numerical information to the phone company; that the phone company has facilities for recording this information; and that the phone company does in fact record this information for a variety of legitimate business purposes." *Smith v. Maryland*, 442 U.S. 735, 743 (1979). Nothing in Section 222 suggests that Congress took a different view.

maintained, and stored by carriers; in no sense is it "provided by" customers, any more than are the sales records maintained by a mail-order catalog to track its inventory and prior transactions.[3]

Respondents are thus incorrect when they refer to the question presented in this case as one of CPNI "disclosure." FCC Br. 10, 22, 31; MCI Br. 7; CPI Br. 12, 15 ("dissemination"). "Disclosure" is generally understood to involve the release of CPNI to an unrelated third party (which has no existing relationship with the customer), not a carrier's own use of the CPNI that the carrier itself has generated.[4] Congress has drawn that distinction in statutes like 47 U.S.C. § 227(a)(3), which *exempts* from the term "telephone solicitation" those calls "to any person with whom the caller has an established business relationship."

In short, all that respondents have shown is that the government has an interest in preventing a carrier like U S WEST from disclosing the information to an unrelated third party such as MCI. But this case involves the quite different question of U S WEST's rights to use its own information itself.[5]

b. <u>The CPNI Rules Fail The Narrow Tailoring Requirement.</u>

Even if there were a material privacy interest in the internal use of CPNI, the FCC's rules would not be narrowly tailored to protecting it. In *Revo*, this Court held that a restriction on

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[3] CPI suggests that, if the information is neither made available to the carrier by the customer, nor received or obtained from the customer, "then the information is not CPNI and its use is not in any way limited by the *CPNI Order*." CPI Br. 16. U S WEST has raised this issue with the FCC. *See Ex Parte* Submission from Kathryn Marie Krause to Dorothy T. Attwood, in CC Docket 96-115 (September 9, 1997), at 2 n.4. A reasonable interpretation of Section 222 could well obviate any challenge to the application of the provision to internal business records.

[4] *See* Pacific Telesis Reply Comments, CC Docket 96-115, filed June 26, 1996, p. 9, n.19 (Section 222(c)(2) "makes plain that the section applies only to 'disclosure' to *third parties*, contrary to the assertion of some, as one cannot 'disclose' information to oneself.").

[5] Respondents' reliance on *Lanphere & Urbaniak v. Norton*, 21 F.3d 1508 (10th Cir. 1994), which involved a claimed third-party right of access to arrest records maintained by the government (not the right of a speaker to use information it has generated itself in order to communicate), is wholly misplaced.

attorney solicitation was not narrowly tailored to the government's asserted interest because "[t]here are several less-burdensome alternatives available to the Board -- alternatives which the Board has not shown would be insufficient to materially address its concerns." *Revo*, 106 F.3d at 935. "While it is true that the 'least restrictive means test has no role in the commercial speech context,' 'the existence of numerous and obvious less-burdensome alternatives to the restriction on commercial speech . . . is certainly a relevant consideration in determining whether the "fit" between ends and means is reasonable.'" *Id.* (internal quotations omitted). Just as the rule in *Revo* was unconstitutional because "[t]he Board ha[d] not shown why subjecting personal injury direct mail letters to a screening process would not protect against misleading potential clients," *id.*, here the CPNI rules are invalid because the FCC has not shown why a notice and opt-out method cannot accommodate any legitimate interests customers may have in the information generated by a telecommunications service provider.

Notice and opt-out is the time-tested and proven regulatory method in the CPNI field and other information-use venues. Over the course of more than a decade, the FCC repeatedly studied this approach and found that it adequately protected consumers. The FCC documented that a prior affirmative consent rule was unnecessary to protect competition or customer privacy and was at odds with efficient carrier operations and with customers' desires for one-stop shopping. Nothing in the 1996 Act suggests that Congress intended the Commission to depart from this aspect of its prior policy. Indeed, notice and opt out procedures are a common way of accommodating consumer interests, particularly in commercial contexts where the supplier and customer have an established business relationship.[6] Fed. R. Civ. P. 23(c)(2) uses notice and opt

[6] *See* 47 C.F.R. § 64.1509 (pay-per-call rules under 47 U.S.C. § 208, which require carriers to give subscribers notice of their rights to block pay per call services, with a lack of response resulting in no block); 47 C.F.R. § 64.1600-1603 (caller ID rules requiring carriers to deliver

out even where there is no prior relationship among class members and grievous personal injury or substantial monetary loss may be at stake.

Furthermore, the FCC has never denied that its CPNI rules will result in *additional* violations of customer privacy and solitude – "the right to be let alone."[7] If carriers are "dumbed down" so that they cannot identify and communicate with individual customers based on their likely interest in receiving information about specific new services, carriers will be forced (in those instances where they do not remain silent) to use blanketed "broadcast-type" telemarketing speech fashioned for an "all customer" audience. Hence, the net effect of the CPNI rules may well be to increase intrusions and decrease privacy.

c. **The CPNI Rules Rest On Impermissible Speculation.**

At bottom, the FCC's defense of the *CPNI Order* rests on its unsupported view that "[o]bviously" (FCC Br. 29) there must be some customers who would not bother to respond to an opt-out notice, but who nonetheless feel so strongly about their "privacy" that the FCC is entitled to burden carriers' speech (and increase the number of intrusions on *all* customers) in order to protect this imagined set of subscribers. The notion that government must intervene to protect customers who it believes are incapable of responding to an opt-out notice sent to them by first-class mail reflects the kind of paternalistic attitude that the Supreme Court has repeatedly

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calling party number unless caller has opted out by dialing *67 and requiring carriers to provide notice to customers); 16 C.F.R. § 425.1 ("negative option plans," such as those used by book and record clubs); 16 C.F.R. § 435.1 (FTC requirement that, if mail or telephone order merchandise is delayed, the seller must give notice of shipping delay and permit buyer to cancel or opt out); 12 C.F.R. § 226.9 (Federal Reserve Regulation Z, which requires credit card provider to give notice of changes in terms and annual renewal fees, with card holder having option to "opt-out" of further use of the card).

[7] *Olmstead v. United States*, 277 U.S. 438, 478 (1928) (Brandeis, J., dissenting). The FCC itself has treated unwanted solicitations as an invasion of privacy. *See BNA Third Order on Reconsideration*, 11 FCC Rcd. 6835, 6848-49 ¶ 23 (1996); *In the Matter of Rules and*

rejected as a justification for restrictions on commercial speech. *44 Liquormart*, 116 S. Ct. at 1507 (principal opinion); *Edenfield v. Fane*, 507 U.S. at 767; *Virginia State Bd. of Pharmacy v. Virginia Citizens Consumer Council, Inc.*, 425 U.S. 748, 769 (1976).

The FCC's argument is based on nothing but "mere speculation or conjecture," *Edenfeld v. Fane*, 507 U.S. at 770, and "anecdotal evidence and educated guesses." *Rubin v. Coors Brewing*, 514 U.S. at 490. *See also Revo*, 106 F.3d at 933-34. The FCC has adduced no empirical evidence to support its supposition. In fact, as noted in petitioners' opening brief (at 4-9), the FCC has repeatedly concluded that customer privacy interests do *not* necessitate a prior affirmative consent requirement in the context of existing carrier-customer relationships: "a solicitation to someone with whom a prior business relationship exists does not adversely affect subscriber privacy interests. Moreover, such a solicitation can be deemed invited or permitted by a subscriber in light of the business relationship."[8] The evidence in the record confirms this conclusion. Petitioners' Opening Brief at 12-15, 18-20.

5. <u>The CPNI Rules Are Unprecedented.</u>

Regulations Implementing the Telephone Consumer Protection Act of 1991, Report and Order, 7 FCC Rcd. 8752, 8753 (1992).

[8] *In the Matter of Rules and Regulations Implementing the Telephone Consumer Protection Act of 1991, Report and Order*, 7 FCC Rcd. 8752, 8770 ¶ 34 (1992); *see also In the Matters of Amendment to Sections 64.702 of the Commission's Rules and Regulations (Third Computer Inquiry), Memorandum Opinion and Order on Reconsideration*, 3 FCC Rcd. 1150, 1163 ¶ 98 (1988) ("most of the BOC network service customers . . . would not object to having their CPNI made available to the BOCs to increase their competitive offerings made to such customers."); *In the Matter of the Telephone Consumer Protection Act of 1991, Notice of Proposed Rulemaking*, 7 FCC Rcd. 2736, 2738 ¶¶ 13-14 (1992) ("If a party has chosen to do business with a particular caller, a contact by that caller to offer additional products or services is not as intrusive as a call from a business with whom the called party has no relationship. . . . The Commission tentatively concludes that the privacy rights the [Telephone Consumer Protection Act] intends to protect are not adversely affected when the called party has or had a voluntary business relationship with the caller.").

Respondents claim that accepting petitioners' constitutional objection would necessarily call into question a host of other statutes regulating commercial information. The opposite is true. The CPNI rules are utterly unlike any other federal statute or regulation. and upholding them would create a dangerous precedent for government interference in a company's relationship with its customers and its ability to engage in intra-corporate speech.

In a futile attempt to find *any* precedent for the CPNI rules, the FCC cites the example of "negative option solicitations." FCC Br. 19 n.51. Yet that example proves the opposite of what the FCC claims. The Federal Trade Commission has reaffirmed its rule permitting such arrangements in ongoing business relationships,[9] stressing that the system "continues to be of value to consumers and firms, and is functioning well in the marketplace at minimal cost." 63 Fed. Reg. at 44555. The FTC twice referred to the very example of encyclopedia sales cited by the FCC. *See id.* at 44559 (specifically referring to "the monthly shipment of volumes of an encyclopedia or a book series"); 44557 n.8. The FTC found that clear and conspicuous disclosure in notice and opt-out forms, as well as the ability to cancel (or change one's mind), were sufficient to establish the fairness of an opt-out model. *Id.* at 44558. Petitioners have long complied with these conditions.

MCI cites a series of statutes which simply confirm that the *CPNI Order* is badly out of step with legislative approaches in other contexts. MCI Br. 7 n.6. MCI's examples involve third-party disclosures, not use of the information by the company collecting it. Further, the statutes generally *allow* third-party disclosure, sometimes using an opt-out process. For instance, the Fair Debt Collection Practices Act of 1977 *permits* debt collectors to disclose a debtor's financial

[9] *See Trade Regulation Rule Regarding Use of Negative Option Plans by Sellers in Commerce*, 63 Fed. Reg. 44555, 44556 (Aug. 20, 1998) ("A negative option allows a seller to interpret the

situation to credit reporting agencies. 15 U.S.C. § 1692c(b). Under the 1996 Consumer Credit Reporting Reform Act, credit reports *may* be distributed for a "legitimate business need" in connection with a "business transaction that is initiated by the consumer" or "to review an account to determine whether the consumer continues to meet the terms of the account." 15 U.S.C. § 1681b(a)(3)(F). Credit reporting agencies *may* furnish consumer credit information for marketing credit or insurance opportunities to consumers, so long as the agency establishes a toll-free number so that consumers can call and opt-out by having their names removed from lists for direct marketing purposes. 15 U.S.C. § 1681b(c)(5).

The Electronic Funds Transfer Act of 1978, 15 U.S.C. §§ 1693-1693r, establishes mandatory guidelines for the relationship between consumers and financial institutions in connection with electronic funds transactions, but does *not* restrict the use or disclosure to third parties of information about consumer transactions. Nor does it restrict the gathering of personal information or limit the duration of storage of transaction records. The Electronic Communications Privacy Act, 18 U.S.C. § 2703, establishes procedures for law enforcement access to certain electronic records, but *permits* "a provider of electronic communication service or remote computing service [to] disclose a record or other information pertaining to a subscriber to or customer of such service . . . to any person other than a government entity." § 2703(c). The Cable Communications Policy Act leaves cable operators *free* to use subscriber information internally and obliges them to secure affirmative consent only when releasing the information to unaffiliated third parties. 47 U.S.C. § 551. MCI's assertion that the Cable Act "creates an 'opt-

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failure of a consumer to reject goods or services as the acceptance of a sales offer, when, under traditional contract law, an affirmative response accepting the offer would be necessary.").

in' scheme much like that set out in the CPNI Order" (MCI Br. 7 n.6) is simply wrong.[10] The FAA regulations cited by MCI, 14 C.F.R. § 243.9 (MCI Br. 7 n.6), govern only passenger manifest information that airlines are required to collect by FAA rules (*e.g.*, for notifying next of kin in the event of aviation disasters). The regulations do not restrict airlines' ability to use or disclose frequent flier records or other information obtained by airlines in the usual course of business.[11]

The fact remains that there is *no federal statute anywhere* in the U.S. Code that remotely resembles the *CPNI Order*. The FCC failed to appreciate the unique nature of its rules. Surely, Congress would have spoken more clearly in Section 222 if it had meant to authorize such a radical departure from prior legislative approaches and commercial practices.

B. THE *ORDER* RAISES GRAVE QUESTIONS UNDER THE FIFTH AMENDMENT.

1. A Carrier Is Not A Mere "Custodian" Of CPNI.

[10] The statute provides that "a cable operator shall not disclose personally identifiable information concerning any subscriber without the prior written or electronic consent of the subscriber concerned and shall take such actions as are necessary to prevent unauthorized access to such information by *a person other than the subscriber or cable operator*." 47 U.S.C. § 551(c)(1) (emphasis added). The statute specifically permits a cable operator to disclose subscriber information when "necessary to render, or *conduct a legitimate business activity* related to, a cable service or other service provided by the cable operator to the subscriber." 47 U.S.C. § 551(c)(2)(A) (emphasis added).

[11] MCI also cites a variety of state statutes regulating disclosures of nonpublic customer information by banks with respect to the marketing of insurance products. MCI Br. 7 n.6. Some of the statutes restrict only the disclosure of information to third parties and do not prohibit the use of the information by the bank itself. *E.g.*, N.J. Stat. Ann. § 17:16K-3; Conn. Gen. Stat. § 38a-775(d). Other statutes impose a limited restriction with respect to insurance products, an area where states have found such rules necessary to prevent deceptive marketing practices. The rules do not affect the ability of banks to use the nonpublic information at issue for any other business purpose, and the rationale behind them is inapplicable here. In short, *none* of the statutes is remotely comparable to the CPNI rules, and *none* of them supports respondents' argument.

The FCC contends, without citation, that a telephone company holds CPNI merely as a "custodian" for its customers, "for the limited purposes of performing its services as a telephone company." FCC Br. 23. But no respondent cites, let alone addresses, the Supreme Court's holding that even a public utility (let alone a local telephone company, which by federal law cannot hold a local franchise and is subject to competition, 47 U.S.C. §§ 251-253) does not stand in a fiduciary relationship with its customers. "The relation between the company and its customers is not that of partners, agent and principal, or trustee and beneficiary." *Board of Pub. Util. Comm'rs v. New York Tel. Co.*, 271 U.S. 23, 31 (1926). "Customers pay for service, not for the property used to render it. . . . By paying bills for service, they do not acquire any interest, legal or equitable, in the property used for the convenience or in the funds of the company." *Id.* *See also Simpson v. U S WEST Communications*, 957 F. Supp. 201, 206 (D. Or. 1997) ("as a matter of law, . . . a telephone company is not in a 'fiduciary relationship' with its customers").[12]

Furthermore, confidential customer information, including records of customer purchasing habits, has long been deemed protected commercial property. *See, e.g., DeVries v. Starr*, 393 F.2d 9, 13 (10th Cir. 1968) (confidential customer list is a trade secret); Restatement (Third) of Unfair Competition § 42, comments (e) and (f) (1995) (business information such as customer lists are protected property); Melvin F. Jager, Trade Secrets Law § 3.03[2][c], at 3-45 (1998) ("customer identities and related information can be a company's most valuable asset"); Edward C. Wilde & Gary A. Nye, *The Customer List as Trade Secret*, 2 Intellec. Prop. Law 135, 139 (1994) ("personal information concerning customers constitutes protected confidential

[12] The Supreme Court rejected a much more modest position than that advanced by the FCC here, in holding that the "extra space" (up to one ounce for first-class mailing) in public utility billing inserts could not be appropriated by a state public utility commission and used to force a utility to distribute the messages of a pro-consumer group. *Pacific Gas & Electric Co. v. Public*

information").[13] Indeed, cases from virtually every state confirm the property interest in confidential customer information.[14]

Utilities Comm'n, 475 U.S. 1, 17-18 (1986) (plurality opinion). *See also id.* 22 n.1 (Marshall, J., concurring in the judgment).

[13] *See, e.g., Sigma Chemical Company v. Harris*, 794 F.2d 371, 374 (8th Cir. 1986) (company records of customer purchasing habits were protected trade secrets); *Zoecon Indus. v. The American Stockman Tag Co.*, 713 F.2d 1174, 1179-80 (5th Cir. 1983) (memorandum containing the names, addresses, and purchasing characteristics of a business's customers is a trade secret under Texas law); *Hollingsworth Solderless Terminal Co. v. Turley*, 622 F.2d 1324, 1331 (9th Cir. 1980) (Kennedy, J.) (salesman's experience with plaintiff's customers, their buying habits, purchasing history, and other special considerations raised issue of fact as to whether knowledge of salesman constituted protectable trade secret); *W.R. Grace & Co. v. Hargadine*, 392 F.2d 9, 16 (6th Cir. 1968) ("customer books and customer service information materials . . . clearly belonged to" the manufacturer that compiled them); *All West Pet Supply Co. v. Hill's Pet Prods. Div.*, 840 F. Supp. 1433, 1438 (D. Kan. 1993) (customer purchasing patterns, sales volumes, and payment histories could qualify as trade secrets).

[14] *Tyler v. Eufaulo Tribune Pub. Co.*, 500 So.2d 1005 (Ala. 1986); *Amex Distrib. Co. v. Mascari*, 724 P.2d 596, 602 (Ct. App. Ariz. 1986); *Allen v. Johar, Inc.*, 823 S.W.2d 824, 827 (1992); *Reid v. Massachusetts Co.*, 318 P.2d 54, 60 (Cal. App. 1957); *R&D Bus. Sys. v. Xerox Corp.*, 152 F.R.D. 195, 197 (D. Colo. 1993); *Holiday Food Co. v. Munroe*, 426 A.2d 814 (Conn. 1982); *Delmarva Drilling Co. v. American Well Sys., Inc.*, No. 8221, 1988 WL 7396 (Del. Ch. Jan. 28, 1988); *Unistar Corp. v. Child*, 415 So.2d 733, 734 (Fla. App. 1982); *Avnet, Inc. v. Wyle Labs, Inc.*, 437 S.E.2d 302 (Ga. 1993); *Stampede Tool Warehouse, Inc. v. May*, 651 N.E. 209, 214 (Ill. App.), *review denied*, 657 N.E.2d 639 (1995); *Ackerman v. Kimball Int'l*, 652 N.E.2d 507, 509 (Ind. 1995); *Basic Chems., Inc. v. Benson*, 251 N.W.2d 220, 228 (Iowa 1977); *Koch Eng'g Co. v. Falconer*, 610 P.2d 1094, 1104 (Kan. 1980); *Wright Chem. Corp. v. Johnson*, 563 F. Supp. 501 (M.D. La. 1983); *Space Aero Prods. Co. v. R.E. Darling Co.*, 208 A.2d 74 (Md.), *cert. denied*, 382 U.S. 843 (1965); *Jet Spray Cooler, Inc. v. Crampton*, 282 N.E.2d 921, 926 (Mass. 1972); *Chem Trend, Inc. v. McCarthy*, 780 F. Supp. 458 (E.D. Mich. 1991); *Surgidev Corp. v. Eye Tech, Inc.*, 828 F.2d 452, 455-46 (8th Cir. 1987) (Minn. Law); *National Rejectors, Inc. v. Trieman*, 409 S.W.2d 1, 18-19 (Mo. 1966); *Cudahy Co. v. American Labs., Inc.*, 313 F. Supp. 1339, 1343-44 (D. Neb. 1970); *Home Gas Corp. v. Strafford Fuels, Inc.*, 534 A.2d 390 (N.H. 1987); *Mailman, Ross, Toyes & Shapiro v. Edelson*, 444 A.2d 75, 78 (N.J. Ch. Div. 1982); *Salter v. Jameson*, 736 P.2d 989, 991 (N.M. App. 1987); *McLaughlin, Piven, Vogel, Inc. v. W.F. Nolan & Co.*, 498 N.Y.S.2d 146 (2d Dept. 1986); *Drouillard v. Keister Williams Newspaper Serv.*, 423 N.E.2d 324, 327 (N.C. App. 1992); *Advanced Bus. Tels., Inc. v. Professional Data Processing, Inc.*, 359 N.W.2d 365, 367-68 (N.D. 1984); *Consumer Direct, Inc. v. Limbach*, 580 N.E.2d 1073, 1075 (Ohio 1991); *Morgan's Home Equip. Corp. v. Martucci*, 136 A.2d 838, 842 (Pa. 1957); *Paramount Office Supply v. MacIsaac, Inc.*, 524 A.2d 1099, 1011 (R.I. 1987); *1stAm. Sys., Inc. v. Rezatto*, 311 N.W.2d 51, 58-59 (S.D. 1981); *One Stop Deli, Inc. v. Franco's, Inc.*, 1993 U.S. Dist. Lexis 17295 (W.D. Va. 1993); *B.C. Ziegler & Co. v. Ehren*, 414 N.W.2d 48, 50 (Wis. App. 1987); *Ridley v. Krout*, 180 P.2d 124, 131 (Wyo. 1947).

The FCC's contrary view, if permitted to stand, would work a revolution not only in the telecommunications industry, but in many other sectors of American commerce, including credit card companies, grocery stores, mail-order catalogs, banks, Internet service providers, and other companies that maintain individually identifiable customer information as a valued part of their routine business operations. *See* Brief of Amicus Information Industry Association. It is settled law that such information belongs to the companies that generate, compile, and maintain it, and it is nothing short of astonishing for respondents to suggest otherwise.

Hence, petitioners have plainly established a reasonable, investment-backed expectation in their ability to use CPNI for productive purposes. In *Ruckelshaus v. Monsanto Co.*, 467 U.S. 986 (1984), the Court held that state law creates a property right in trade secrets for purposes of the Fifth Amendment. *Id.* at 1003-04. The Court opined that, if the federal government could "'pre-empt' state property law in the manner advocated by EPA, then the Taking Clause has lost all vitality." *Id.* at 1012. *See also Preseault v. ICC*, 494 U.S. 1, 22-23 (1990) (O'Connor, J., joined by Scalia and Kennedy, JJ., concurring) (federal regulatory program works a taking if it upsets state-law property rights).[15]

2. <u>The Commission's Prior Practice Refutes Its Argument.</u>

The FCC contends that its assertion that CPNI belongs to customers rather than carriers is nothing new. But none of the respondents denies that the *CPNI Order* reflects a radical departure from prior Commission policy. The most the Commission can muster to justify its turnaround is an offhand reference in the *AT&T CPE Relief Order*, 102 F.C.C.2d 655 (1985).

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[15] Respondents argue that *Ruckelshaus* is inapplicable because there is no comparable federal statute here guaranteeing the right to use CPNI. But state law supplies the relevant property right. *See Phillips v. Washington Legal Foundation*, 118 S. Ct. 1925, 1930 (1998). And here no pre-existing federal program comparable to the pre-1978 pesticide program in *Ruckelshaus* calls into question petitioners' property interest.

However, that Order undermines rather than supports the FCC's position. Despite its reference to ownership, the Order permitted AT&T to use CPNI for all legitimate business purposes. In the *AT&T CPE Relief Order*, the Commission *allowed* data collected in AT&T's telephone operations to be shared with personnel in a different AT&T division, which sold CPE (such as telephones) to consumers. The only constraint imposed by the Commission was a notice and opt out requirement - the very regulatory option that the FCC has rejected in this context and that petitioners are willing to accept.

Far from restricting AT&T's use of the commercial information, the FCC explained that "AT&T's CPE sales personnel will . . . have a legitimate need for access to customer proprietary information dealing with network services. *Id.* at 693. The FCC rejected the arguments of AT&T's competitors that they were entitled to access to information on the same terms and conditions: "given that AT&T's CPE sales personnel will have access to all customer proprietary information under this plan, providing equivalent access to all CPE vendors would require AT&T to make all its large customers' information public. Since this information belongs to the customers, and many may not want it to be made public, this approach is also unacceptable." *Id.*

Thus, the FCC considered the customers' interest in the information only in the context of rejecting an obligation that would have required AT&T to disclose its commercial information to unaffiliated third parties. The FCC saw no privacy or customer ownership issues in AT&T's own use of the data – even use by a different division of AT&T. The *AT&T CPE Order* thus strongly supports petitioners' position here.

3. <u>The Rules Raise Serious Takings Issues.</u>

Respondents contend that this is merely a case where the government has affected the value of property by regulation. Respondents implicitly concede that a regulation is invalid if, in the words of Justice Holmes, it "goes too far." *Pennsylvania Coal Co. v. Mahon*, 260 U.S. 393,

415 (1922). But respondents insist that whether a taking has occurred depends on "the character of the [government's] action and its purported economic impact." MCI Br. 15. There are two flaws in respondents' argument.

First, the CPNI rules do not simply prevent carriers from using CPNI. They also purport to transfer ownership of it to customers, in whom the rules vest the power of prior affirmative consent. Respondents' do not deny that "a law that takes property from A. and gives it to B.," *Eastern Enterprises v. Apfel*, 118 S. Ct. 2131, 2146 (1998) (plurality opinion) (citation omitted), is a classic form of taking, regardless of the economic impact on the owner A. *See* MCI Br. 17 (laws which "transfer ownership interest to . . . third parties").

Second, respondents are wrong to argue that "this *Court* must weigh the 'public and private interests' affected by the *CPNI Order*." CPI Br. 25 (emphasis added). The *FCC*, not this Court in the first instance, has the responsibility of examining the economic effect of the CPNI rules, their impact on petitioners' investment-backed expectations, and the remainder of the factors cited by respondents. The FCC has the obligation to engage in a reasoned analysis of the takings issue. It has the duty to construe Section 222 to avoid a takings question. It is forbidden from adopting regulations that "directly implicate[] the Just Compensation Clause of the Fifth Amendment." *Bell Atlantic Corp. v. FCC*, 24 F.3d 1441, 1445 (D.C. Cir. 1994). The FCC discharged none of those duties here. Instead, the Commission – no doubt heavily influenced by its faulty theory that carriers have no ownership interest at all in CPNI -- brushed off petitioners' takings claim with the blithe assertion that, under the CPNI rules, carriers would still be able to use CPNI for certain limited purposes. *Order* ¶ 43. Even the cases on which respondents rely most heavily warn that "Resolution of each case . . . ultimately calls as much for the exercise of

judgment as for the application of logic." *Andrus v. Allard*, 444 U.S. 51, 65 (1979). Here, the FCC has exercised no such judgment, and the rules should be vacated on that basis.[16]

C. THE *ORDER* REFLECTS AN IMPERMISSIBLE CONSTRUCTION OF SECTION 222.

In light of the serious constitutional issues raised by the CPNI rules, they must be vacated. Even apart from those constitutional concerns, however, the CPNI rules cannot stand. The FCC construed Section 222(c)(1) in a manner at odds with congressional intent and with the Commission's own long-standing position that requiring prior CPNI authorizations from customers was impracticable, unnecessary, and counterproductive. There is no indication that Congress in the 1996 Act sought to depart so dramatically from this longstanding regulatory practice, or to authorize the FCC to create a special rule for telecommunications carriers utterly unprecedented in American industry. Petitioners' opening brief demonstrated, without rebuttal, that, in light of the significant differences between Section 222 and earlier legislative proposals, Congress plainly did *not* mandate affirmative consents from customers. Opening Br. 44.

"Even under the deference mandated by *Chevron*, 'legislative regulations are [not] given controlling weight [if] they are arbitrary, capricious, or manifestly contrary to the statute.'" *Southern Ute Indian Tribe v. Amoco Prod. Co.*, 119 F.3d 816, 835 (10th Cir. 1997) (alterations in original), *aff'd en banc on other grounds*, 1998 WL 404549 (10th Cir. July 20, 1998). "No deference is warranted if the interpretation is inconsistent with the legislative intent reflected in the language and structure of the statute or if there are other compelling indications that it is

[16] The FCC contends that petitioners have no significant "unrecovered investment in the data" because "[m]ost of the relevant costs . . . in all likelihood would have been expensed for ratemaking purposes." FCC Br. 34. But the value of CPNI to carriers is not represented simply by the administrative costs of collecting it. The FCC has recognized that "CPNI becomes a powerful resource for identifying potential customers and tailoring marketing strategies to

wrong." *Mountain Side Mobile Estates Partnership v. Secretary of Housing & Urban Dev.*, 56 F.3d 1243, 1248 (10th Cir. 1995) (citation omitted). The FCC's *CPNI Order* fails this test.

CONCLUSION

The petition for review should be granted; the *CPNI Order* and accompanying rule amendments to 47 C.F.R. §§ 64.2005 and 64.2007 should be vacated; and the matter should be remanded to the FCC for further consideration.

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October 15, 1998

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maximize customer response." *Order* at ¶ 22. *See also Phillips*, 118 S. Ct. at 1933 (possession and control of property are valuable rights regardless of economically realizable value).

IN THE
UNITED STATES COURT OF APPEALS
FOR THE TENTH CIRCUIT

No. 98-9518

U S WEST, INC.,

Petitioner,

v.

FEDERAL COMMUNICATIONS COMMISSION and
UNITED STATES OF AMERICA,

Respondents,

BELLSOUTH CORPORATION. and
SBC COMMUNICATIONS INC., *et al.*,

Intervenors.

CERTIFICATE OF SERVICE

I, Kathryn Marie Krause, on this 15th day of October, 1998, do hereby certify that two copies of the foregoing **REPLY BRIEF FOR PETITIONER AND INTERVENORS** were caused to be served, via first-class United States mail, postage prepaid, upon each of the following persons:

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Washington, DC 20530

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Federal Communications Commission
Room 614
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Washington, DC 20554

John E. Ingle
Carl D. Lawson
Federal Communications Commission
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Kathryn Marie Krause

Kathryn Marie Krause

TAB 13

Vice President - Legal Affairs
and Senior Associate General Counsel

1801 California Street, Suite 3800
Denver, Colorado 80202

303 672 2777
303 675 0764 fax

ride the light
Qwest

February 7, 2002

VIA HAND DELIVERY

Paul A. Bullis, Esq.
State of Arizona
Office of the Attorney General
1275 West Washington
Phoenix, AZ 85007-2926

Dear Mr. Bullis:

This is in response to Attorney General Napolitano's letter dated January 18, 2002, to James A. Smith, Executive Vice President - Consumer Markets, requesting information regarding Qwest's sharing of customer proprietary network information ("CPNI"). We understand and share your commitment to protecting the privacy interests of our customers. Qwest is working hard to improve customer service and earn customer confidence, and we take your concerns and those of our customers very seriously.

Your letter asks whether Qwest shares CPNI with third parties for commercial purposes, *i.e.*, telemarketers[1] and companies such as Microsoft with which Qwest has a co-marketing arrangement. As an initial matter, we wish to be clear that Qwest does not and will not disclose CPNI to telemarketers or other third parties for their own independent use. Qwest does hire marketing firms to sell Qwest products and services when it makes sound business sense to contract the function out. As requested, we are enclosing copies of our contracts with these firms.[2] Qwest's use of CPNI in these instances (through its agents) comports with applicable law regarding the use of CPNI.

As you can see, Qwest's contracts with these marketing firms require that customer information be kept confidential. We understand from your letter that you have practical concerns as to whether such confidentiality will, in fact, be maintained. In this regard, please be advised that Qwest does more than merely rely on the confidentiality provisions of these contracts to protect CPNI. The employees of these firms are provided with the same CPNI training as that received by Qwest employees, including some live training, supplemented with handbooks, manuals and scripts, and a web based information source that explains the proper handling of CPNI. Moreover, there have been no reported abuses or problems regarding the improper use of CPNI by Qwest agents.

---

[1] As you know, some of our activities are handled by contractors as well as employees. We understand your inquiry to be directed to the use of CPNI in connection with sales activities, so where contractors engage in sales activities, we have included those contracts. If the contractors engage in no sales activity, but might have access to some CPNI (specifically, in connection with customer surveys, billing and collections, and the administrative handling of direct mailings), we have not enclosed those contracts. In addition, Qwest has established relationships with a number of agents who sell Qwest products and services strictly to businesses, not residential customers. These agents sign a form contract with Qwest, a copy of which is enclosed. In order to ensure the proper handling of the sales and service to these businesses, the agents receive permission from the customer to access its account information, including CPNI, which the agents specifically agree to protect. A copy of the form of authorization is also enclosed.

[2] For your convenience, we are also enclosing a list containing the names of each vendor for which we are producing contracts. As I mentioned in our phone conversation yesterday, in a few instances we have redacted certain pricing information and service standards from these contracts. To the extent it is possible, we also ask that all documents we have produced be kept confidential, and to this end, we have so marked the documents.

You also expressed interest in our co-marketing arrangement with Microsoft whereby customers can purchase a package from Microsoft that includes Microsoft's ISP service powered by a Qwest DSL line.[3] Under this arrangement, if a customer calls Qwest to order the service, the following information is gathered and forwarded to Microsoft: name, address, telephone number, type of connection (*i.e.*, DSL speed), and ISP plan purchased (*i.e.*, Microsoft Basic Plan). In addition, Qwest provides Microsoft with a due date for commencement of service. Without this information from the customer, Microsoft would be unable to set up and bill for the service ordered by its customer.

Additionally, sometimes customers order retail DSL service directly from Qwest for use with other ISPs such as Earthlink or America Online. In such cases, Qwest gathers and forwards the same information to the customer's chosen ISP as that sent to Microsoft. Again, without this information, the chosen ISP could not set up the service the customer has ordered.

Finally, as you know, Qwest has withdrawn its plans to share CPNI among different divisions in the company, and will defer its decision on when and how it might do so until after the FCC has an opportunity to issue new CPNI rules. We sincerely hope that Qwest's withdrawal of its previously announced plans, along with the other information provided with this letter, allays your concerns. Qwest remains committed to protecting the privacy interests of its customers and ensuring the responsible use of CPNI in accordance with applicable law.

Should you have questions or concerns regarding the information provided with this letter, or any further questions about Qwest's policies, please do not hesitate to contact me.

Sincerely,

John J. Hopkins

Enclosures

[3] Microsoft purchases the DSL service for its customers from Qwest pursuant to a federal tariff.

CONTRACTS PRODUCED BY QWEST WITH LETTER TO ARIZONA ATTORNEY GENERAL'S OFFICE DATED FEBRUARY 7, 2002

1. Aegis Communications Group, Inc.
2. APAC Customer Services, Inc. (contract has been redacted at the supplier's request)
3. Affinitas Corporation
4. Bi-Lingual Soluciones
5. Center Partners
6. Convergys Corporation
7. Dakotah Direct II, L.L.C.
8. Direct Marketing Services
9. Focus Communications
10. Kipany Productions, Ltd.
11. LTD Direct Marketing
12. Markafon De Mexico SA
13. Phase 2 Solutions, Inc.
14. Prism Marketing Group
15. Risk Management Alternatives, Inc.
16. Sutherland Group, Ltd.
17. Synergy Solutions
18. Telac (Access Worldwide)
19. Telelink Systems, Inc.
20. Teleperformance USA
21. Telespectrum Worldwide, Inc.
22. Teletech Customer Care Management (Colorado), Inc. (contract has been redacted at the supplier's request)
23. Transcom USA
24. Tele-Servicing Innovations (TSI)
25. West Telemarketing Corporation (contract has been redacted at the supplier's request)
26. Sample Qwest Sales Agent Agreement and Letter of Agency (redacted)

TAB 14

1-16-97

Gina Harrison
Director
Federal Regulatory Relations

1275 Pennsylvania Avenue N.W., Suite 400
Washington, D.C. 20004
(202) 383-6423

PACIFIC TELESIS.
Group-Washington

KK ORIGINAL COPY (DISREGARD ... ED)
Initials .....
CC 96-115
Assigned To Wykenga

January 16, 1997

EX PARTE

William F. Caton
Acting Secretary
Federal Communications Commission
Mail Stop 1170
1919 M Street, N.W., Room 222
Washington, D.C. 20554

Dear Mr. Caton:

Re: CPNI, CC Docket No. 96-115

Today, Alan Westin, Professor of Law and Public Government, Columbia University, Rex Mitchell, Vice President, Regulatory, Pacific Bell, Michael Yourshaw of Wiley, Rein & Fielding, Peter Filon, intern, Columbus School of Law, Catholic University, and I met with Regina Keeney, Bureau Chief, A. Richard Metzger, Jr., Deputy Chief, Laurence Atlas, Associate Chief, Paul Gallant, Assistant to the Chief, Common Carrier Bureau; and William Kehoe III, Dorothy T. Atwood and Gayle Teicher, all the Common Carrier Bureau, to discuss issues summarized in Attachment A. Copies of "Public Attitudes Toward Local Telephone Company Use of CPNI", included as Attachment B, were also distributed. Please include these materials in the above-referenced docket. We are submitting two copies of this notice, in accordance with Section 1.206(a)(1) of the Commission's rules.

Please stamp and return the provided copy to confirm your receipt. Please contact me should you have any questions.

Sincerely yours,

Attachments

cc: L. Atlas
D. Atwood
P. Gallant
R. Keeney
B. Kehoe
A.R. Metzger
G. Teicher

JAN 27 1997

CPNI Ex Parte (CC Docket No. 96-115)

- Public attitudes
- Notice and opt-out in other industries
- Competition vs. privacy
- Joint marketing

Pacific Telesis Group

January 16, 1997

Public Attitudes Toward Local Telephone Company Use of CPNI

- Pacific Telesis Group sponsored a national opinion survey by Opinion Research Corporation and Prof. Alan F. Westin, Columbia University
  - The public is concerned about maintaining personal privacy
  - The public also wants their telephone company to communicate with them about new services

The Public Overwhelmingly Wants Business Communications from Their Telephone Company

- 88% of the public says it is acceptable for their telephone company to "communicate with them from time to time about new products, or special discounts they are offering to customers"
- Providing an opt out procedure raises acceptance of such business communications to 93%

Consumers Trust Their Local Telephone Company with CPNI

- Local telephone companies received a 78% High and Medium trust level regarding their use and protection of consumers' confidential information
  - This is the same high group as hospitals, banks, and employers
  - They were slightly ahead of long distance telephone companies
  - This was much higher trust than was given to insurance companies and cable television companies
- Less than 10% of the public say their local telephone company has ever released their personal telephone information improperly

Most Consumers Want To Learn from Their Local Telephone Company About New Services

- 64% say they want to hear about services such as "voice mail, long distance calling plans, cellular telephone services, and expanded cable television or home interactive video services"
  - Even higher percentages of Hispanics, African-Americans, women, and young adults
- 64% also say it's acceptable for the local telephone company to use its CPNI to target such offers
  - With notice and opt out, this acceptance level rises to 80%
- 69% say it's OK for a service representative to look up CPNI during an inbound call to offer new services

Carrier Use of Its CPNI Does Not Fit the "Sensitive Information/Opt-In" Model

- Carrier use of CPNI does not raise the risks of embarrassment, humiliation, or stigma
- The relationship between carrier and customer does not critically depend on the confidentiality of CPNI
- CPNI is not used, and has little potential to be used, to make decisions affecting an individual's access to employment, insurance, licenses, or other entitlements or benefits

Use of personal information which is not highly sensitive is customarily used and disclosed pursuant to an opt-out procedure

- Prescreening provisions of the Fair Credit Reporting Act (as amended by the Consumer Credit Reporting Reform Act of 1996)
- Medical directory information under the Uniform Health Care Information Act
- Driver's license information under the Driver's Privacy Protection Act
- State statutes in areas of telecommunications, financial services, direct marketing, health and medical records

There Is High Public Support for Companies Sharing Customer Information With Their Affiliates for Related Marketing

- Almost two out of three consumers support "subsidiaries" getting customer information "to make offers of services or products" (1994 Harris survey)
- This is widely adopted by legislation and regulation in areas such as credit reporting and medical records

Competition vs. Privacy

- Section 222's provisions deal separately with competition and privacy
  - Section 222 already makes ample provision for enhancing competition and protecting privacy
  - The Commission does not need to create additional privacy or competitive provisions or alter those that already exist

Competition

- Prohibition on use of another carrier's CPNI for marketing (§222(b))
- Mandatory disclosure on affirmative written request (§222(c)(2))
- Nondiscriminatory access to aggregate information used by a LEC for any purpose other than providing services from which the aggregate information is derived (§222(c)(3))
- Mandatory provision of subscriber list information by LECs on an unbundled, nondiscriminatory basis (§222(e))

Privacy

- Duty to protect proprietary information of carriers and all customers(§222(a))
- Limits on use of another carrier's CPNI(§222(b))
- Duty to protect CPNI of all customers(§222(c)(1))
- Approval required to use, disclose, or permit access to CPNI(§222(c)(1))
- Affirmative written request required for release of CPNI to third parties (§222(c)(2))

The Commission Should Not Treat Section 222(c)(1) as a Competitive Provision

- Section 222(c)(1) is a privacy provision
  - It deals with how a carrier may use CPNI internally
  - It allows carriers to obtain approval to use CPNI internally by a notice and opt out process
- The Act does not require a carrier that obtains approval for internal use of CPNI by a notice and opt out process to obtain such approval on behalf of other carriers
  - Congress clearly intended for a carrier to communicate with its own customers in seeking approval
  - Congress did not intend for one carrier to be forced to act on behalf of another carrier

Aggregate Customer Information

- The Commission should not create additional telecommunications service "buckets"
  - The three buckets the Commission proposes (local service, long distance service, and CMRS) adequately comport with Section 222(c)(1)
  - Increasing the number of buckets may inadvertently hamper LECs' ability to use aggregate customer information for product planning, research and development, and other efforts

LECs Use Aggregate Customer Information To Develop New Products

- LECs generally use aggregate customer information from multiple products when developing new products
  - Examples: product volumes, customer locations
- This innovation is beneficial to consumers, and is at the heart of the 1996 Act
  - Squelching this innovation will harm consumers

If the Commission Were To Increase the Number of Buckets, LECs Would Be Less Able To Serve Customers

- LECs could not
  - use aggregate customer information from a broad array of services to develop new products and services
  - use aggregate customer information for routine business purposes
    - Measuring productivity
    - Forecasting
    - Tracking revenues and expenses
- This result is antithetical to the intent of the 1996 Act

Special Restrictions in Section 222(c)(3) Apply to LEC Use of Aggregate Customer Information Without Consent

- LECs may use such information for the telecommunications service from which it was derived, or services necessary to or used in the provision of such services
- LECs may use aggregate customer information for other purposes, but it must then make the information available to others
- These restrictions are adequate to ensure appropriate use of aggregate customer information

A BOC May Seek Customer Approval To Use CPNI for Joint Marketing Without Making Solicitations for Other Carriers

- This is necessary for a BOC to engage in permissible joint marketing activities, including targeting customers, responding to inquires, processing orders, and performing sales functions
- Section 272(g)(3) exempts requests to use CPNI in support of joint marketing efforts with a BOC's interLATA affiliate from the nondiscrimination requirement of section 272(c)(1)
  - A BOC may solicit approval to use CPNI for its own joint marketing of the affiliate's services or to share CPNI with the affiliate pursuant to a joint marketing agreement
- Requiring a BOC to solicit approvals for other carriers would violate the First Amendment

A BOC May Provide CPNI to Its InterLATA Affiliate in Support of Joint Marketing Without Providing It to Others

- The provision of CPNI is a necessary part of sharing the resources of the two companies for successful joint marketing
- Customer approval is required
- This joint marketing function is covered by section 272(g)(3)
- A requirement to make CPNI available to others would violate the prohibition against disclosure in section 222(c)(1)
- The BOC will provide CPNI to other companies who have obtained the requisite customer approval under section 222(c)(2)

Summary

- Customers are overwhelmingly comfortable with their telecommunications providers using CPNI to tell them about new services, especially if given the ability to opt out
- Legislation and industry practice in banking, credit, health care, and direct marketing provide ample precedent for the notice and opt-out practice
- The Commission cannot increase the number of proposed "buckets" without harming LECs' ability to use aggregate CPNI to develop new products and services
- Both sections 222 and 272 allow the BOC and its interLATA affiliate to use CPNI for joint marketing with adequate customer approval, without providing it to others

Attachment B

PUBLIC ATTITUDES TOWARD LOCAL TELEPHONE COMPANY USE OF CPNI

REPORT OF A
NATIONAL OPINION SURVEY
CONDUCTED NOVEMBER 14-17, 1996

BY
OPINION RESEARCH CORPORATION,
PRINCETON, N.J.

AND

PROF. ALAN F. WESTIN,
COLUMBIA UNIVERSITY

SPONSORED BY
PACIFIC TELESIS GROUP

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E. Questions and Tabulated Responses

Executive Summary

A representative national survey on issues relating to local telephone company use of CPNI information was conducted in November of 1996 by Opinion Research Corporation of Princeton, New Jersey and Dr. Alan F. Westin, Professor of Public Law and Government, Columbia University, sponsored by Pacific Telesis Group.

The major findings of the survey relevant to the FCC's CC Docket No. 96-115 Rule Making are:

• Public concerns over threats to privacy and the desire for better control over the uses made by companies of customer information are very high, and still rising.

• At the same time, large majorities of the public believe it is acceptable for businesses to communicate to their own customers to offer them additional services and benefits, and especially if an opt out procedure is provided.

• This is specifically true of local telephone companies communicating with their customers through use of CPNI data.

• The public has strong confidence in local telephone companies to use the personal information they collect about customers in a responsible way, and to protect its confidentiality.

• Less than 10% of the public believe their local telephone company has ever released their information in an improper way.

• The availability of an opt out procedure brings initial approvals of local telephone company use of CPNI data from the two out of three respondent level up to the 80% range of public approval.

Introduction

Pacific Telesis Group commissioned Opinion Research Corporation of Princeton, New Jersey (ORC) and Dr. Alan F. Westin, Professor of Public Law & Government at Columbia University, to develop, conduct, and report the results of a national survey of public opinion about the use of customer proprietary network information (CPNI) by telecommunications carriers. We will refer to this as the "CPNI Survey."

Pacific Telesis believes the CPNI Survey's findings represent a fresh and highly valuable contribution to the Federal Communications Commission's CC Docket No. 96-115 Rule Making.

Dr. Westin is widely considered the nation's leading expert on information privacy, and is publisher of *Privacy & American Business*, the well-known national report on business-privacy issues. He has been the academic advisor to 22 national surveys on privacy since 1978, 15 of these with Louis Harris and Associates and 7 with Opinion Research Corporation. (A Privacy Vita for Dr. Westin is included as Appendix A).

Opinion Research Corporation has been, for over 50 years, a leading U.S. and international survey research firm, with a long roster of business, government, and non-profit clients. (A description of ORC appears in Appendix B) ORC conducts a weekly omnibus telephone survey ("CARAVAN")of a national probability sample of 1,000 adults 18 years of age and older, living in private households in the United States. (A description of the weekly CARAVAN survey is included as Appendix C)

The questions relating to CPNI were placed on the weekly ORC CARAVAN survey for November 14-17, 1996. (A full description of the methodology used and demographic make-up of the sample of 1,011 adults responding to our questions will be found in Appendix D) A copy of the entire CARAVAN question set relating to CPNI, with the tabulations obtained, has been attached as Appendix E.

This report to the FCC has been written by Dr. Westin. It was reviewed for accuracy and completeness of data presentation by Opinion Research Corporation and approved by ORC for public release.

1. Public Concerns About Threats to Privacy Are Very High and Still Rising

The CPNI survey asked four questions about privacy attitudes, to probe levels of concern and define the environment within which the FCC's CPNI Rule Making is unfolding. (We put these four questions at the end of the survey, to avoid any influence on the specific CPNI issues that might be exerted by presenting respondents at the outset with privacy-oriented questions.)

Our basic, long-term trend question (developed by Dr. Westin and used in national privacy surveys since 1978) asks respondents: "How concerned are you about threats to your personal privacy in America today." The choices given are: "very concerned, somewhat concerned, not very concerned, or not concerned at all."

When first asked in 1978, in the aftermath of Watergate, the response was 68% concerned -- 33% "very concerned" and 31% "somewhat concerned". When asked in mid-1995, after issues of consumer, employee, and citizen privacy in the increasingly computerized government and business environment had been widely discussed in the mass media in the 1990's, 82% of the public said they were concerned -- 47% saying "very concerned" and 35% "somewhat concerned."[1]

In the CPNI Survey, far from receding, concern about privacy continued to climb. Eighty-nine per cent of the public in November of 1996 -- almost nine out of ten Americans -- now say they are concerned about privacy threats. And, 55.5% now say they are "very concerned" with 33.1% "somewhat concerned."

An 8.5% rise in "very concerned" sentiment within one year indicates clearly that public apprehension about privacy threats has not "crested"; rather, it is still rising significantly in the late 1990's.

2. Public Concern is Also Very High Over Uses of Consumer Information by Businesses

A set of three additional privacy-trend questions on the CPNI survey asked respondents whether they agreed or disagreed with a number of statements about privacy. The answers to these questions were not only useful in themselves, compared to replies on these questions recorded in earlier years, but also to create a High, Medium, and Low concern About Privacy Index. This was used to see how respondents with certain attitudes -- such as interest in hearing about new telephone services or having exercised an opt out -- divided along lines of intensity of privacy concern.

---

[1] Figures for this question between 1978 and1995 appear in *The Equifax-Harris Mid-Decade Consumer Privacy Survey, 1995*, conducted by Louis Harris & Associates and Dr. Alan F. Westin.

(As we will see, majorities of respondents scoring either High and Medium in their concern about uses of consumer information accept an opt out procedure for the local telephone company communicating to them about additional services.)

The questions that made up our index were as follows:

• 83% of the public agrees that ***"consumers have lost all control over how personal information about them is circulated and used by companies."***

This is up from 80% agreeing to that statement in 1995.[2]

• 72% of the public agree that ***"If privacy is to be preserved, the use of computers must be sharply restricted in the future."*** This is up from 67% stating such agreement when the question was last asked, in 1994.[3]

• 52% of the public disagree that ***"Your rights to privacy as a consumer are adequately protected today by law or business practice."*** [No exactly worded previous question is available for trend-line use.]

These concerned responses of the American public about business uses of consumer information, the uses of advanced information technologies to process consumer and citizen data, and weaknesses in existing law and business practices all justify the FCC's current attention to assuring that telephone service providers meet the public's legitimate expectations of privacy in the use of their customer information for marketing purposes.

The balance of the CPNI Survey was devoted to exploring just what those public expectations are, and what policies the public would like to see used in the handling of customer information.

3. At the Same Time, Very Large Public Majorities Favor Businesses Being Able to Inform Their Customers About New Services

As many previous consumer privacy surveys have documented, the public's concern about how consumer personal information is used by businesses does NOT mean that the American public wants to stop receiving communications about products and services from the businesses they are already patronizing.

To test this outlook in late 1996, the CPNI survey asked respondents the following:

When you are a customer of a business -- such as a bank, a department store, an insurance company, or a local telephone service -- do you consider it acceptable for this business to communicate with you from time

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[2] Ibid.

[3] *The Equifax-Harris consumer Privacy Survey, 1994.*

to time about new products or services, or special discounts they are offering to their customers they think may be of interest or benefit to you?

Almost nine out of ten members of the public -- 88% -- said receiving such informational communications from businesses they patronize would be acceptable to them.

Such communications were approved even more strongly than the public at large by the following groups:

18-24 year olds	93%
25-34 year olds	92
African-Americans	93
Hispanics	91
Persons who order many additional telephone services	94
People who are aware of and have used an opt out from any business	92

4. Offering an Opt Out Procedure Raises Public Acceptance of Such Business Communications to Customers to 93%

Twelve per cent of respondents (117) had said such business communications were either not very acceptable to them or not acceptable at all. These respondents were then asked a further question:

Would it become acceptable to you if this company offered you the opportunity to "opt out" or decline to receive information about new products or services or special discounts, and contacted only those customers who did NOT "opt out"?

Forty-two percent of these 117 respondents said yes. When these 49 persons are added to the 88% that found business communications to existing customers acceptable, a total of 93% of the American public finds such marketing acceptable.

5. Local Telephone Companies Are Among the Business Organizations Most Trusted by the Public to Use Customer Information Responsibly and Protect Its Confidentiality

Past consumer privacy surveys have documented that public confidence in the voluntary privacy and fair information practices policies of business organizations is highly correlated with the overall level of trust that the public has in how a particular industry handles the personal consumer information it collect and uses. When trust in an industry is very low, based on public perceptions (and dominant media treatment) of an industry's

failure to treat consumer information in ways the public considers responsible, the public will favor legal duties and regulatory enforcement, rather than the public's usual preference for voluntary policies and market-based dynamics.

With this well-documented trend in mind, the CPNI Survey asked respondents to indicate their level of trust in twelve types of industries, with the following question:

I will read you a short list of organizations which collect and use information about consumers. On a scale of 1 to 10, HOW MUCH DO YOU TRUST THEM to collect and use information about people like you in a responsible way and protecting its confidentiality. Answering "1" means you do not trust them at all and "10" means you have complete trust in them.

Our analysis combined answers of 10, 9, and 8 into a "High Trust" rating; 7, 6, 5, and 4 into a "Medium Trust" rating; and 3, 2, and 1 into a "Low Trust" rating. Following the procedure used in past consumer privacy surveys, we ranked the 12 industries in terms of a combined High and Medium Trust rating, producing the following pattern:

Public trust that organizations collecting information about consumers use such information in a "responsible way" and "protecting its confidentiality"

Type of Organization	High and Medium Trust
Hospitals	79%
Banks	78
Employers	78
Local telephone companies	76
Long distance telephone companies	72
Health insurance companies	66
Cable television companies	66
Credit card companies	64
Life insurance companies	64
Credit bureaus	48
Private investigators	43
Companies that sell to consumers at their homes, by direct mail	40

The twelve industries fall into three clearly-differentiated segments, in public estimation. The five types of organizations receiving more than seven out of ten Americans' medium to high trust -- hospitals, banks, employers, local telephone companies, and long distance telephone companies -- represent industries whose promises of proper handling of consumer information enjoy very broad public confidence.

The four industries in the middle segment -- health insurance companies, cable television firms, credit card companies, and life insurance companies -- enjoy a two-out-of-three Americans' trust rating, a quite creditable standing in an era marked by general distrust of government and many sectors of business and non-profit organizational life.

Finally, direct marketers, credit bureaus, and private marketers were given a medium to high trust rating by less than a majority of the public.

For the purposes of the FCC's CPNI Inquiry, the finding that 77% of the American public have medium to high trust in local telephone companies gives strong support to the idea that a voluntary program of notice and opt outs in local telephone company use of customer information for offering additional telephone services would be regarded with confidence and approval by more than three out of four Americans.

6. Less than 10% of the Public Say Their Local Telephone company Has Ever Released Their Personal Telephone Information Improperly

Another indication of the level of confidence that the public presently has in local telephone companies was explored by the CPNI survey with the following question:

Have you ever had the company you use for local telephone service release the personal information they had about you in a way you thought was not proper?

Only 9% of the public said that this had ever happened to them. Eighty-two per cent said it had never happened, and 9% didn't know or didn't answer. By contrast, 25% of the American public said in 1993 that they believed an organization that had their medical information -- such as a doctor, hospital, clinic, or health insurance company -- had released their medical information in a way the respondent thought was improper.[4]

7. Large Majorities Say They Would be Interested in Learning From Their Local Telephone Company About New Telephone Services

Turning specifically to telephone services, the CPNI Survey posed this question:

Many new consumer services are being developed by local telephone companies today. These include voice mail, long distance calling plans, cellular telephone service, expanded cable television or home interactive

[4] *The Harris-Equifax Health Information Privacy Survey, 1993.*

video services. How interested would you be in having your local telephone company inform you about such new services from time to time?

Almost two-thirds of the public -- 64% -- said they would be interested in being so informed of new services by their local telephone company.

8. Large Majorities Also Say it is Acceptable for Their Local Telephone Company to Look Up Their Records and Offer Them Additional Services, and Offering an Opt Out Increases This Majority to 82%

Turning to how the local telephone company selects customers to receive offers of additional services and benefits, the CPNI Survey asked this question:

Your local telephone company may also look at its customer records to see which of its current customers it thinks would be most interested in or benefit from hearing about new services. Do you consider it acceptable for your local telephone company to look over customer records for this purpose?

Again, almost two out of three members of the public -- 64% -- say this procedure would be acceptable to them. When the 36% who said it was NOT acceptable were asked whether providing an opt out procedure would make this record-based communication process acceptable, 45% said it would.

Combining those initially favorable with those becoming favorable if an opt out is provided produces a majority of 80% for this customer-record-based local telephone company communication process.

9. Similar Majorities Accept Checking Customer Records and Offering New Services During Service Calls

Looking at another common use of customer account records by local telephone companies, the CPNI Survey asked:

When you call your local telephone company to discuss your services, the customer service representative that you speak with normally looks up your billing and account service record. As a result of talking with you and seeing the services you already have, the representative may also want to offer you new services. On that call, do you consider it acceptable for the representative to offer you new services?

More than two-thirds of the public -- 69% -- say that such customer-account-based communication to them from a customer service representative would be acceptable.

(Since local telephone companies say their customer service representatives ask the person they are talking with whether it is all right to tell them about new services, an oral "opt out" is built into this process.)

10. Positive Views Toward Local Telephone Company Use of Customer Information Are Held by Majorities of All Demographic Groups

The questions we have reported were not close calls of the 51-49% variety; rather, as noted, they drew approving majorities in the 64-88% ranges. It is not surprising therefore, but important to note, that majorities in favor of local telephone company use of customer information for the marketing procedures presented were registered for all the demographic sub-groups that make up the general public – young, middle-aged, and older persons; lowest to highest incomes; black, white, and Hispanic; male and female; lowest to highest education; conservative, moderate, and liberal political philosophy; urban, suburban, and rural community dwellers; and by Northeast, North Central, South, and West regions.

In terms of the FCC's mission to protect and promote "the public interest," this overall pattern of general-public and demographic-group majorities represents an important input to the FCC's CPNI Proceeding.

At the same time, it is important to note that many groups that the FCC is often especially concerned to protect, and to see well served in telephone services, were even more positive toward customer-information-based service offering than the public as a whole. For example, we saw in Section 5 that 64% of the overall public say they would be interested in having the local telephone company inform them about new telephone services.

However, among the groups that scored well above the public's 64% in their interest in receiving such information were:

Hispanics	79%
African-Americans	72
Women	69
18-24 year olds	76
Persons who have used an opt out	72
Persons who order many additional telephone services	83

It seems particularly useful to note that higher interest in receiving local telephone company communications on new services was registered by almost three out of four persons (72%) who have exercised an opt out from third-party marketing use of their name and address.

Analysis of the people who have used opt outs indicates that they are at the highest levels of privacy concern (as reflected in the privacy questions on the CPNI Survey, #14 and 15 A, B, and C) The CPNI survey found the respondents who have used opt outs in

other business setting are willing to change their position from initial disapproval to positive views of customer-records-based communications by local telephone companies when our follow-up questions asked whether providing an opt out would make such practices acceptable.

11. The Public Divides About Equally Between Offering an Opt Out in the Monthly Bill and Sending a Separate Mailing

To explore how the public would like local telephone companies to notify them about opt out choices and procedures, the CPNI Survey asked:

If your local telephone company provides you with an opportunity to "opt out" or decline to have your customer information used in this way, would you prefer receiving such a notice and "opt out" opportunity in your monthly telephone bill or in a separate mailing to you?

The public was almost evenly divided on this matter -- 51% preferred a separate mailing; 46% chose the monthly bill; and 4% gave no opinion.

Summing Up

In terms of the FCC's CPNI Rule Making, the November, 1996 ORC survey data show that:

- Large majorities of the American public believe it is all right for their local telephone company to communicate with them to offer additional services, whether by looking up their records to identify those likely to be interested in or benefit from such services or during calls from customers being handled by customer service representatives.
- When respondents who do not initially find such customer-record-based communications acceptable are told that an opt out procedure would be available, almost half of these say that this would make the communication to them acceptable.
- Adding those for whom the opt out makes the communication acceptable to those who originally approved of the communication provides favorable majorities at the 80% level.
- This very high approval for CPNI use by local telephone companies parallels the survey's findings as to initial approval and then opt out procedures for businesses in general communicating with their customers to offer additional services.

APPENDICES

Privacy Activities of Professor Alan F. Westin, Columbia University

General

Alan F. Westin is Professor of Public Law and Government at Columbia University, where he has taught for the past 37 years. Born in 1929, he earned his BA. from the University of Florida; his LL.B. from Harvard Law School; and his Ph.D. in political science from Harvard University. He is a member of the District of Columbia Bar, the author or editor of 26 books, and has been listed for the past three decades in Who's Who in the United States.

Privacy Activities

For four decades, Professor Westin has specialized in studying, writing, and consulting about the impacts of information technology on individuals, organizations, and society.

1. Writing and Speaking

Dr. Westin's award-winning 1967 book, Privacy and Freedom, is considered the leading work in this field. Other books he has written about privacy include: Databanks in a Free Society (1972), with Michael Baker, for the National Academy of Sciences, and two monographs for the U.S. National Bureau of Standards on Computers, Health Records, and Citizen Rights (1976) and Computers, Personnel Administration, and Citizen Rights (1979). He is currently completing a new book for the Columbia University Press on "The American Public and Privacy: New Roles and Rules for the Computer Age."

In addition to publishing in law reviews and scholarly journals, his articles on privacy issues have appeared in the New York Times, Wall Street Journal, Fortune, Business Week, the Los Angeles Times, Newsday, and many industry, trade, and technical publications.

He has discussed privacy issues often on such television programs as the Today Show, CBS Morning Show, the McNeil-Lehrer Show, and many others. In the past three decades, he has spoken about privacy issues at the national conventions of more than two hundred business, professional, and governmental associations.

2. Governmental Work

In the governmental arena, he was consultant to Senator Sam Ervin Jr. in drafting the Federal Privacy Act of 1974; a Presidential appointee (by Richard M. Nixon) to the National Wiretapping Commission (1973-76); Senior Consultant to the U.S. Privacy Protection Commission (1975-77); Privacy Consultant to the New York State Identification and Intelligence System, and Project SEARCH; and a member of Privacy Task Forces for the U.S. Department of Commerce, General Services Administration, Social Security Administration, and other federal agencies.

He has been chair or a member of more than 20 panels of the U.S. Office of Technology Assessment on privacy issues over the past two decades. Dr. Westin has testified frequently since the late 1960's before dozens of Congressional and state legislative committees on privacy issues involving credit, employment, medical and health records, banking, insurance, law enforcement, telecommunications, credit cards, and other issues.

During the 1970's, he was Vice Chairman of the New Jersey State Commission on Individual Liberty and Privacy, which held extensive hearings on privacy issues in banking, insurance, public records, health records, and other sectors, and sponsored several privacy bills that were enacted by the New Jersey legislature.

3. Public Opinion and Survey Work

Over the past 18 years, he has been the academic advisor to Louis Harris & Associates for fifteen national public and leadership opinion surveys of privacy conducted in the United States and Canada.

These have included national surveys on "The Dimensions of Privacy" (for Sentry Insurance, 1979); "Consumers in the Information Age" (for Equifax, 1990, and consumer privacy suerveys in 1991, 1992, 1994, 1995, and 1996); "Consumers and Privacy in the Information Age" (for Equifax Canada, 1993); "Health Information Privacy Survey, 1993" (for Equifax Inc.); "Workplace Privacy Issues," for the Educational Film Center, 1993; "Credit and the Consumer, 1994" (for VISA and MasterCard); and "Interactive Services, Consumers, and Privacy" (sponsored by Bell Atlantic, U.S. West, and Citicorp Technology Resources), 1994

He has also designed and supervised seven proprietary or public surveys on privacy issues for business firms and industry associations in collaboration with Opinion Research Corporation of Princeton, N.J. A recently-released public survey done with ORC was on "Public Attitudes Toward Finger Imaging as an Identification Technique" (for National Registry, Inc.), 1996.

4. Private-Sector Consulting, Training, and Advocacy Work

In the private sector, Dr. Westin has been a consultant on privacy over the past 25 years to several dozen corporations. In the early 1970's, he developed IBM's employee privacy guidelines, which served as a model for hundreds of other companies in the late 1970's and 1980's. He has been the principal consultant for new privacy codes by such companies as American Express, Equifax, and Security Pacific National Bank. Among the other firms for which he has been a privacy consultant for consumer and customer privacy issues are Citicorp, Prudential, Aetna Life & Casualty, Nabisco, A.T. & T., and many more.

Dr. Westin has personally conducted privacy-issues briefings for CEO's, senior management, and Boards of Directors in over 100 corporations.

5. Privacy & Legislative Associates

In 1993, Dr. Westin joined with Robert R. Belair, a leading Washington attorney specializing in privacy and freedom of information law, to found **Privacy & Legislative Associates** (P&LA), a consulting firm in Washington that specializes in privacy work. P&LA clients include Glaxo Wellcome, Smith Kline Beecham, HealthPoint, Bell Atlantic, Pacific Telesis, Chrysler Corporation, Health Data Exchange (a Shared Medical Systems company), EMX, National Registry, Inc., Image Data, VISA U.S.A., Harris Corporation, and Science Applications International Corporation (SAIC).

P&LA works with clients to develop innovative privacy policies and procedures; make presentations to senior executives; conduct privacy training programs for staff and operating managers; support preparation of public relations and marketing materials presenting privacy policies and practices; conduct proprietary surveys on the public's perceptions of client products and services, and client privacy policies under consideration; provide representation of clients on

pending legislation in Congress and the states, and before federal and state regulatory agencies. and present proposed client privacy policies for advance (and confidential) reactions by key consumer, employee, and privacy groups and experts; and provide crisis-management support for clients experiencing major public challenges.

P&LA also offers a monthly, customized monitoring report service for clients on an industry-by-industry basis, covering emerging legislative and regulatory trends, advocacy-group positions, litigation trends and judicial-decision analysis; analysis of published surveys and opinion trends; and media-trend round-ups. These reports cover trends for firms in the credit card, telecommunications, health care, pharmaceutical, information services, and biometric identification industries.

6. *Privacy & American Business*

Also in 1993, Dr. Westin founded (with Robert Belair) a new bi-monthly report and information service called ***Privacy and American Business***. (P&AB) P & A B covers consumer, health, communications, and employment privacy, as well as multi-national and international arenas, and is the first "privacy-sensitive but business-friendly" publication in this field. It is supported by continuing grants from 25 leading companies and industry associations, including American Express, Citicorp, Equifax, Bell Atlantic, Pacific Bell, U.S. West, VISA, MasterCard, Microsoft, the National Commission on Confidentiality of Health Records, Direct Marketing Association, State Farm Insurance, MCI, A.T. & T., Metromail, TransUnion, First USA, First Data Corporation, Prudential Insurance, Experian (formerly TRW), and other firms.

P&AB organizes and conducts an annual Fall national conference on "Managing The Privacy Revolution," in Washington, D.C. The Third Annual conference, held in October, 1996, explored the 1995-96 developments on business-privacy issues, privacy issues in cyberspace, and the increasing globalization of privacy issues for bhusiness (including U.S. multi-national companies' relationship to the European Union's recently enacted Data Protection Directive).

P&AB also manages the Corporate Privacy Leadership Program, a cooperative, peer-group forum sharing policies and techniques among pro-active companies and industry associations in financial services, telecommunications, insurance, health-information processing, human resources, information services, online systems, and other sectors.

7. Privacy and Health Information

Since the mid-1960's, Professor Westin has maintained a continuing special interest in medical confidentiality and health-information-systems privacy issues.

A comprehensive field study of computerization trends and health information was led by Dr. Westin for the U.S. National Bureau of Standards between 1974-76, and produced Westin's report on Computers, Health Records, and Citizen Rights (1976). The Privacy Code this report recommended was sent by NBS to every hospital in the U.S., and served as a model for hundreds of hospital and health institutions. The NBS Report remains to this day the leading empirical study of how computer use is affecting the three main zones of health information use -- direct care, payment and quality-assurance, and social uses of medical data.

Between 1978 and the early 1980's, he served as Research Director of the National Commission on Confidentiality of Health Records, a national association composed of the major health-care provider, payer, and quality-care associations in the United States. During this period, he spoke frequently on privacy and health information issues at national conventions or special meetings of the American Medical Association, Health Insurance Association, American

Medical Records Association, American Orthopsychiatric Association, American Psychiatric Association, and many other health-professional groups.

In the past 2-3 years, he has been a featured speaker at the U.S. Department of Health and Human Services Privacy Task Force Conference on Medical Records and Privacy (February, 1993); a reviewer of reports on privacy for the National Institute of Medicine (on emerging regional health data systems), the Journal of the American Medical Association, and for the U.S. Office of Technology Assessment (on privacy and the computerized medical record).

Dr. Westin was the privacy advisor to a 1994 Public Television Special Documentary on "Privacy and Health in the American Workplace." Dr. Westin drafted a national corporate-employee and human resources executives survey conducted by Louis Harris and Associates for use on this program, covering employee health and privacy issues in depth.

In 1993, he served as the academic advisor for a national public and leaders Harris survey on "Health Information Privacy." Results from this survey were released at a national conference in Washington, D.C. in November, 1993, at which Dr. Westin spoke, co-sponsored by the U.S. Office of Consumer Affairs, the American Health Information Management Association, and Equifax Inc.

Also in 1993-95, Dr. Westin served as Principal Investigator on a 15-month project on privacy issues in the uses of genetic testing and genetic-test applications, funded by the U.S. Department of Energy for the Human Genome Project and its ELSI Program (Ethical, Legal and Social Issues).

In his consulting work, Dr. Westin has recently drafted privacy codes for the Health Data Exchange of Shared Medical Systems; EMX, a new health information service; Equifax's Health Information Sector; and HealthPoint.

8. Overseas and Multinational Activities

For three decades, Professor Westin has been a keynote speaker at leading business, government, and technology conferences on privacy and data protection in the United Kingdom, Western Europe, Scandinavia, Japan, and Hong Kong. In 1985, for example, NTT of Japan brought Dr. Westin to Tokyo as the Privacy Keynote Speaker at the NTT International Conference on Technology and Society in the Information Age, and Dr. Westin lectured on U.S., European, and Japanese approaches to privacy protection at several Japanese universities and technology institutes.

In 1996, he has spoken at business and government sponsored privacy conferences in Victoria and Ottowa, Canada; London; and Berlin.

Opinion Research Corporation, headquartered in Princeton, New Jersey, was founded in 1938 to apply public opinion polling techniques to business issues. ORC has been a public company since October 1993 (NASDAQ-ORCI).

ORC specializes in the global business-to-business market and addresses for its clients such strategic issues as market definition, corporate equity assessment and customer retention tracking research. ORC's concentration is in the automotive, financial services, health care, information technology/telecommunications, media & leisure and retail trade industries.

In addition, the firm offers a number of proprietary and shared-cost research products. These include BrandPerceptions℠ and CORPerceptions℠, global equity studies conducted among consumers and executives, LeaseBASE℠, the first needs and behavior-based study of the automobile leasing market, and NetTrack℠, a nationally projectable panel of Internet and online services users available to companies for ad hoc research and product testing.

ORC opened ORC-Asia in 1995 to ensure the standardization of its research across the Pacific Rim. The Company also established ORC-International, a network comprising Affiliate Companies in 23 countries across Latin America, Asia, Europe and the Middle East. Through ORC-International, multinational clients benefit from national expertise regarding the domestic business environment and the appropriate means of national/cultural data collection in each geography. ORC's development of a Global Standard for data collection and analysis ensures that market intelligence is delivered within a consistent architecture that provides cleaner comparisons between diverse markets.

ORC has two central telephone interviewing centers, in Tucson and London, each having 100+ CATI-equipped interviewing stations. All European telephone interviewing is conducted through the London center, which is staffed with native language interviewers. Interviewing is regularly conducted in the Pacific Rim, Europe and the Americas by ORC-International Affiliates. A full complement of data processing, analytic and modeling capabilities are also provided.

Key clients include AT&T, Bell Atlantic, Dean Witter, EDS, General Electric, General Motors, ITT Sheraton, Moody's and PNC Bank.

Offices are located in Princeton, NJ, Chicago, IL, Detroit, MI, Toledo, OH, Tucson, AZ, Washington, DC, Hong Kong and London, England.

Michael R. Cooper is Chairman and CEO. John F. Short is Vice Chairman and CFO.

Selected Clients

Advanced Care Products
AETNA Life & Casualty
AGF
AIG
Airco Distributor Gases
Alexander Consulting Group
AlliedSignal
ALC Communications
American Medical Association
American Airlines
Arthur Andersen & Co.
Angotti, Thomas, Hedge
AT&T

BankAmerica
Barclays Life
Bell Atlantic
BellSouth
Bellcore
Beltone Electronics
Beneficial Management
Bissell
Blue Cross of California
BMW of North America
Boatmen's Bancshares
Boeing Commercial Airplane Group
Bordon
Bozell
Braun
British Gas
Brodeur & Partners
Brown and Powers
Buick Motors
Business Week
Burson-Marsteller

Cable & Wireless
Cadillac Motor Car
Campbell Soup
Campbell Mithun Esty
Carter Wallace
CBS Broadcast Group
The Chase Manhattan Bank
Chemical Bank
Chevrolet Motor
Chiat/Day Advertising
Chrysler
Chrysler Financial
Church & Dwight
Citibank
Clydesdale Bank
CNBC
Coca-Cola
Comcast
Commercial Union
Connaught Laboratories
Coopers & Lybrand
Cramer Krasselt
CSX

Data General
Dataplan
DDB Needham Worldwide
Dean Witter, Discover & Co.
Dorf & Stanton Communications
Dow Chemical
DuPont

Eagle Star
Earle Palmer Brown & Spiro
Eastman Kodak
Edelman Public Relations Worldwide
EDS
ElectroCom Automation, L.P.
Exxon

Fingerhut Companies
First Union Bank
First National Bank of Chicago
Food Marketing Institute
Ford of Europe
Fortune
Friends Provident
Frigidaire

GE
Gellman Public Relations
Gem Star Development
General Accident Insurance
General Motors
Glaxo
GM Credit Card Division
Grey Advertising
GTE
Guardian Royal Exchange

Hagar Sharp
Hal Riney Partners
Harley-Davidson
Harvard University Graduate School of Education
Hershey Foods
Heublein
Hewlett-Packard
Hexcel
Hoechst-Roussel Pharmaceuticals
Hoffman-LaRoche
Hoover
Horan & Associates
Hughes Aircraft

IBM
ICI
IGD
Industry Week
InfoWorld
Inside Edition
Intracorp
ITT Sheraton

J. Walter Thompson
Johnson & Johnson
Johnson & Johnson Vistakon Canada

Selected Clients

Johnson & Johnson
Vistakon Products
Joy Technologies

Kellogg
Ketchum Public Relations
Key Corporation
Kidder, Peabody & Company
Kiwi Brands
KPMG Peat Marwick

Land-O-Lakes
Lederle Laboratories Division
Thomas J. Lipton
Arthur D. Little
Lockheed
LTV
Lukens

Makovsky & Company
Marketing Corporation of America
Marks & Spencer
Marriott Hotels Resorts and Suites
Mars Confectionery
Maryland Public Television
Mastercard International
Mazda Motor
McCann Erickson
MCI Communications
Medtronic
Meldrum and Fewsmith
Merrill Lynch & Co.
Minnesota Star Tribune
Mona, Meyer, McGrath and Gavin
Money Access Service
Moody's Investors Service
Motion Picture Association of America
MTV Networks
Mullen Advertising

NationsBank
New Jersey Cable Television Association
New York Stock Exchange
Nickelodeon
Norwich Union
NYNEX

Ogilvy, Adams & Rinehart
Oldsmobile
Owens-Corning Fiberglas

Padilla Speer, Beardsley
Partners & Shevack
Philips Consumer Electronics
Phillips Petroleum
Pirelli Cable
PNC Bank
Pontiac Motor
Porter Novelli
Portland Holidays
Prudential Securities
Public Communications

The Reader's Digest Association
Revlon Consumer Products
Rhone-Poulenc Rorer
Roche Vitamins & Fine Chemicals
RochesterTelephone
Rockwell International
Rolm
Ruder-Finn
Ryder Truck Rental

Saab Cars
Saatchi & Saatchi
Saturn
Schaeffer & Associates
Schenkein/Sherman Public Relations
SCM Chemicals
Scott Aviation

Scottish Provident
The Signature Group
SmithKline Beecham
Solar Turbines
Southern New England Telecommunications
Steelcase
Summit Marketing Communications

TBWA
Tedel
Temerlin McClain
Timex
Turner Broadcasting Systems

United States Postal Service
Universal Card Services
U.S. Bank
U S WEST
USA Network

Valley National Bank
VISA U.S.A.
Vision Interfaith Satellite Network

The Wall Street Journal
Walt Disney
Warner Home Video
Warner Lambert
Weber Group
Wells Fargo Bank
The Wharton School of the University of Pennsylvania
Whitehall Laboratories
Woolworth
Wrangler

Xerox

Yorkshire Bank

CARAVAN® INTRODUCTION

CARAVAN is a telephone survey conducted among a national probability sample of 1000 adults 18 years of age and older, living in private households in the continental United States.

Interviewing for CARAVAN® is completed 50 weeks per year, Thursday through Sunday. All data collection efforts take place under the direction of ORC Information Services. ORC's Central Telephone Facility is located in South Plainfield, New Jersey. The core of our telephone center is the interviewers. All ORC interviewers complete an intensive training and test period. Additionally, they attend follow-up training classes that cover advanced screening techniques, in-depth probing and the art of refusal avoidance. Interviewers are continuously supervised, monitored and reviewed in order to maintain the highest quality interviewing standards.

All CARAVAN interviews are conducted using Opinion Research Corporation's computer assisted telephone interviewing (CATI) system. The system is state-of-the-art and offers several distinct advantages such as: full-screen control which allows multi-question screens, fully-programmable help and objection screens to aid interviewing, an extremely flexible telephone number management system and powerful data checking facilities. CATI ensures that interviews are conducted in the most efficient manner and allows interviewers easy response recording. This interviewing method also allows for the most accurate form of data entry by guiding the interviewer through the programmed question flow and by providing on-screen interviewer instructions.

The most advanced probability sampling techniques are employed in the selection of households for telephone interviewing. Opinion Research Corporation utilizes an unrestricted random sampling procedure that controls the amount of serial bias found in systematic sampling to generate its random-digit-dial sample. The sample is fully replicated and stratified by region. Only one interview is conducted per household. All sample numbers selected are subject to up to four attempts to complete an interview.

Completed interviews are weighted by four variables: age, sex, geographic region, and race, to ensure reliable and accurate representation of the total population, 18 years of age and older. The raw data are weighted by a custom designed program which automatically develops a weighting factor for each respondent. Each respondent is assigned a single weight derived from the relationship between the actual proportion of the population with its specific combination of age, sex, geographic characteristics and race and the proportion in our CARAVAN sample that week. Tabular results show both weighted and unweighted bases.

The use of replicable sampling, standardized interviewing procedures and representative weighting provides that all CARAVAN studies are parallel to one another. Thus, CARAVAN usage is appropriate both for point-in-time analysis as well as tracking and trend comparisons.

CARAVAN Telephone Sampling Methodology

Opinion Research Corporation's national probability telephone sample is an efficient form of random-digit-dialing. The sample is designed to be a simple random sample of telephone households. Unlike published directories, ORC's national probability telephone sample includes both unlisted numbers and numbers issued after publication of the directories. The following procedure is used to create the sample:

- Opinion Research Corporation has an annual license for GENESYS, a custom RDD sample generation system developed by Marketing Systems Groups.

- The methodology for generating random digit dialing (RDD) telephone samples in the GENESYS system provides for a single stage, EPSEM (Equal Probability of Selection Method) sample of residential telephone numbers. It is updated twice a year.

- When a national probability sample is needed, a random selection is made from approximately 40,000 exchanges in two million working banks.

- Each telephone number is transferred to a separate call record. The record shows the computer-generated telephone number to be called, as well as the county, state, MSA (if applicable), band and time zone into which the telephone number falls. Our computerized interviewing system (CATI) uses this information to keep track of regional quotas. The CATI interviewing program also keeps track of the disposition categories for each call attempt.

INTRODUCTION

This report presents the findings of a telephone survey conducted among a national probability sample of 1011 adults comprising 504 men and 507 women 18 years of age and older, living in private households in the continental United States.

Interviewing for this CARAVAN® Survey was completed during the period November 14-17, 1996. All data collection efforts took place at Opinion Research Corporation's Central Telephone Facility in Tucson, Arizona. The core of our telephone center is the interviewers. All Opinion Research Corporation's interviewers complete an intensive training and test period. Additionally, they attend follow-up training classes that cover advanced screening techniques, in-depth probing and the art of refusal avoidance. Interviewers are continuously supervised, monitored and reviewed in order to maintain the highest quality interviewing standards.

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The use of replicable sampling, standardized interviewing procedures and representative weighting provides that all CARAVAN studies are parallel to one another. Thus, CARAVAN usage is appropriate both for point-in-time analysis as well as tracking and trend comparisons.

Included in the Technical Information which follows are tables of sampling tolerances of survey results, and a copy of the question series as it appeared in the survey questionnaire.

As required by the Code of Standards of the Council of American Survey Research Organizations, we will maintain the anonymity of our respondents. No information will be released that in any way will reveal the identity of a respondent. Our authorization is required for any publication of the research findings or their implications.

Opinion Research Corporation's CARAVAN is a syndicated, shared-cost data collection vehicle. Opinion Research Corporation has exercised its best efforts in the preparation of this information. In any event, Opinion Research Corporation assumes no responsibility for any use which is made of this information or any decisions based upon it.

CARAVAN Telephone Sampling Methodology

Opinion Research Corporation's national probability telephone sample is an efficient form of random-digit-dialing. The sample is designed to be a simple random sample of telephone households. Unlike published directories, Opinion Research Corporation's national probability telephone sample includes both unlisted numbers and numbers issued after publication of the directories. The following procedure was used to create the sample:

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- When a national probability sample is needed, a random selection is made from approximately 40,000 exchanges in two million working banks.

- Each telephone number is transferred to a separate call record. The record shows the computer-generated telephone number to be called, as well as the county, state, MSA (if applicable), band and time zone into which the telephone number falls. Our computerized interviewing system (CATI) uses this information to keep track of regional quotas. The CATI interviewing program also keeps track of the disposition categories for each call attempt.

Reliability Of Survey Percentages

Results of any sample are subject to sampling variation. The magnitude of the variation is measurable and is affected by the number of interviews and the level of the percentages expressing the results.

The table below shows the possible sample variation that applies to percentage results reported from Opinion Research Corporation's CARAVAN sample. The chances are 95 in 100 that a CARAVAN survey result does not vary, plus or minus, by more than the indicated number of percentage points from the result that would be obtained if interviews had been conducted with all persons in the universe represented by the sample.

Size of Sample on Which Survey Results Is Based	Approximate Sampling Tolerances Applicable to Percentages At or Near These Levels				
	10% or 90%	20% or 80%	30% or 70%	40% or 60%	50%
1,000 interviews	2%	2%	3%	3%	3%
500 interviews	3%	4%	4%	4%	4%
250 interviews	4%	5%	6%	6%	6%
100 interviews	6%	8%	9%	10%	10%

Additional Sampling Tolerances for Samples of 1,000 Interviews

9% or 91%	8% or 92%	7% or 93%	6% or 94%	5% or 95%
2%	2%	2%	1%	1%

4% or 96%	3% or 97%	2% or 98%	1% or 99%
1%	1%	1%	.2%

Sampling Tolerances When Comparing Two Samples

Tolerances are also involved in the comparison of results from independent parts of any one Opinion Research Corporation's CARAVAN sample and in the comparison of results between two independent CARAVAN samples. A difference, in other words, must be of at least a certain number of percentage points to be considered statistically significant. The table below is a guide to the sampling tolerances in percentage points applicable to such comparisons, based on a 95% confidence level.

Size of Samples Compared	Differences Required for Significance At or Near These Percentage Levels				
	10% or 90%	20% or 80%	30% or 70%	40% or 60%	50%
1,000 and 1,000	3%	4%	4%	4%	4%
1,000 and 500	3%	4%	5%	5%	5%
1,000 and 250	4%	6%	6%	7%	7%
1,000 and 100	6%	8%	9%	10%	10%
500 and 500	4%	5%	6%	6%	6%
500 and 250	5%	6%	7%	7%	8%
500 and 100	6%	9%	10%	11%	11%
250 and 250	5%	7%	8%	9%	9%
250 and 100	7%	9%	11%	11%	12%
100 and 100	8%	11%	13%	14%	14%

Telephone Customer Information Uses And Privacy

A National Public Opinion Survey Conducted by OPINION RESEARCH CORPORATION and Dr. Alan F. Westin, November, 1996*

---

1. Does your household currently have any of the following telephone services? (RECORD AS MANY AS APPLY).

Any listed service asked about	68%
Voice mail	12%
Caller ID	19%
Call waiting	48%
Call forwarding	12%
Cellular phone service	25%
Internet access	17%
Personal 800 number service	6%
DON'T KNOW; NONE OF THESE	32%

2. I will read you a short list of organizations which collect and use information about consumers. On a scale of 1 to 10, HOW MUCH DO YOU TRUST THEM to collect and use information about people like you in a responsible way and protecting its confidentiality. Answering "1" means you do not trust them at all and "10" means you have complete trust in them.

2 A

Health insurance companies

Do not trust them at all	18%
	6%
	7%
	6%
	23%
	9%
	9%
	9%
	3%
Have complete trust in them	7%
DON'T KNOW	3%

---

* Sponsored by Pacific Telesis

2 B

Life insurance companies

Do not trust them at all	19%
	7%
	7%
	6%
	21%
	8%
	10%
	8%
	3%
Have complete trust in them	8%
DON'T KNOW	3%

2 C

Local telephone companies, like Pacific Bell, Southwestern Bell, Bell Atlantic and Bell South

Do not trust them at all	10%
	4%
	5%
	5%
	26%
	8%
	10%
	13%
	5%
Have complete trust in them	10%
DON'T KNOW	4%

2 D

Long distance telephone companies, like AT&T, MCI, and Sprint

Do not trust them at all	15%
	6%

_____	6%
_____	7%
_____	22%
_____	8%
_____	10%
_____	11%
_____	3%
Have complete trust in them_____	11%
DON'T KNOW_____	2%

2 E

Employers

Do not trust them at all_____	10%
_____	3%
_____	4%
_____	5%
_____	19%
_____	7%
_____	13%
_____	14%
_____	7%
Have complete trust in them_____	13%
DON'T KNOW_____	4%

2 F

Credit bureaus, like Equifax, TRW, or TransUnion

Do not trust them at all_____	26%
_____	7%
_____	9%
_____	4%
_____	18%
_____	6%
_____	7%
_____	6%
_____	1%

Have complete trust in them	4%
DON'T KNOW	11%

2 G

Companies that sell to consumers at homes by direct mail

Do not trust them at all	36%
	12%
	10%
	6%
	18%
	4%
	4%
	4%
	1%
Have complete trust in them	3%
DON'T KNOW	2%

2 H

Hospitals

Do not trust them at all	10%
	4%
	5%
	6%
	19%
	7%
	12%
	15%
	8%
Have complete trust in them	13%
DON'T KNOW	2%

2 I

Credit card companies like Visa, MasterCard, or American Express

Do not trust them at all	19%

	7%
	7%
	6%
	18%
	8%
	8%
	12%
	4%
Have complete trust in them	8%
DON'T KNOW	3%

2 J

Banks offering consumer checking and savings accounts

Do not trust them at all	11%
	4%
	6%
	5%
	19%
	8%
	12%
	14%
	7%
Have complete trust in them	13%
DON'T KNOW	1%

2 K

Cable television companies

Do not trust them at all	15%
	6%
	7%
	6%
	26%
	6%
	9%

_____	8%
_____	4%
Have complete trust in them_____	7%
DON'T KNOW_____	6%

2 L

Private investigators

Do not trust them at all_____	28%
_____	7%
_____	7%
_____	5%
_____	18%
_____	4%
_____	5%
_____	5%
_____	2%
Have complete trust in them_____	4%
DON'T KNOW_____	15%

3 Have you ever had the company you use for local telephone service release the personal information they had about you in a way you thought was not proper?

YES_____	9%
NO_____	82%
DON'T KNOW_____	9%

4 In the past year, have you or a member of your household bought something from a mailing such as a catalog or brochure that was sent to your residence or workplace, or not?

YES_____	72%
NO_____	27%
DON'T KNOW_____	1%

5 Have you ever received a notice from a business you used, such as a credit card company, catalog firm, publication, or non-profit organization giving you the opportunity to "opt out" or decline having them give your name and address to other organizations that wanted to send you offers by mail for related products or services?

YES_____	41%
NO_____	57%

DON'T KNOW	1%

6. Have you ever checked such an "opt out" yourself, and declined to have such use made of your name and address? (412)

YES	62%
NO	37%
DON'T KNOW	1%

7. When you are a customer of a business--such as a bank, a department store, an insurance company, or a local telephone service--do you consider it acceptable for this business to communicate with you from time to time about new products or services, or special discounts they are offering to their customers that they think may be of interest or benefit to you? Is this... (READ LIST)

Acceptable (very plus somewhat)	88%
Very acceptable	36%
Somewhat acceptable	52%
Not very acceptable	5%
Not at all acceptable	6%
DON'T KNOW	1%

8. Would it become acceptable to you if this company offered you the opportunity to "opt out" or decline to receive information about new products or services, or special discounts and contacted those customers who did NOT "opt out." Would providing such notice and "opt out" make this ...? (READ LIST) (117)

Acceptable (very plus somewhat)	42%
Very acceptable	21%
Somewhat acceptable	21%
Not very acceptable	18%
Not at all acceptable	36%
DON'T KNOW	3%

9. Many new consumer services are being developed by local telephone companies today. These include voice mail, long distance calling plans, cellular telephone service, expanded cable television or home interactive video services. How interested would you be in having your local telephone company inform you about such new services from time to time? Would you say you are... (READ LIST)

Interested (very plus somewhat)	64%
Very interested	16%
Somewhat interested	48%
Not very interested	19%

Not at all interested	17%
DON'T KNOW	0%

10 When you call your local telephone company to discuss your services, the customer service representative that you speak with normally looks up your billing and account service record. As a result of talking with you and seeing the services you already have, the representative may also want to offer you new services. On that call, do you consider it acceptable for the representative to offer you new services? Would that be...(READ LIST)

Acceptable (very plus somewhat)	69%
Very acceptable	20%
Somewhat acceptable	48%
Not very acceptable	16%
Not at all acceptable	15%
DON'T KNOW	1%

11 Your local telephone company may also look at its customer records to see which of its current customers it thinks would be most interested in, or benefit from hearing about new services. Do you consider it acceptable for your local telephone company to look over customer records for this purpose? Would that be... (READ LIST)

Acceptable (very plus somewhat)	64%
Very acceptable	15%
Somewhat acceptable	48%
Not very acceptable	19%
Not at all acceptable	17%
DON'T KNOW	1%

12 Would it become acceptable to you if your local telephone company offered you the opportunity to "opt out" or decline to have your customer information used to describe new services to you, and them communicated such new services to customers who did not choose to "opt out"? Would that become..(READ LIST) (358)

Acceptable (very plus somewhat)	45%
Very acceptable	19%
Somewhat acceptable	25%
Not very acceptable	19%
Not at all acceptable	35%
DON'T KNOW	1%

13 If your local telephone company provides you with an opportunity to "opt out" or decline to have your customer information used in this way, would you prefer receiving such a notice and "opt out" opportunity in your monthly telephone bill or in a separate mailing to you?

Monthly bill	46%

Separate mailing	51%
DON'T KNOW	4%

14 How concerned are you about threats to your personal privacy in America today -- are you very concerned, somewhat concerned, not very concerned, or not concerned at all?

Concerned (very plus somewhat)	89%
Very concerned	55%
Somewhat concerned	13%
Not very concerned	8%
Not concerned at all	3%
Don't know	0%

15. Do you agree or disagree with each of the following statements? Please tell me if you agree strongly, agree somewhat, disagree somewhat, or disagree strongly with each statement.

15A

Consumers have lost all control over HOW personal information about them is circulated and used by companies

Agree (strongly plus somewhat)	82%
Agree strongly	50%
Agree somewhat	32%
Disagree somewhat	12%
Disagree strongly	5%
DON'T KNOW	1%

15 B

Your rights to privacy as a consumer are adequately protected today by law or business practice

Agree (strongly plus somewhat)	47%
Agree strongly	14%
Agree somewhat	33%
Disagree somewhat	26%
Disagree strongly	26%
DON'T KNOW	1%

15 C

If privacy is to be preserved, the use of computers must be sharply restricted in the future

Agree (strongly plus somewhat)	72%
Agree strongly	47%
Agree somewhat	25%
Disagree somewhat	14%
Disagree strongly	13%
DON'T KNOW	1%

TAB 15

1.24.97

Gina Harrison
Director
Federal Regulatory Relations

1275 Pennsylvania Avenue, N.W. Suite 400
Washington, D.C. 20004
(202) 383-6423

PACIFIC TELESIS
Group-Washington

ORIGINAL COPY (DISCARDED)
File No. CC
Proceeding CC96-115
Assigned To Lori Berger

January 24, 1997

EX PARTE

William F. Caton
Acting Secretary
Federal Communications Commission
Mail Stop 1170
1919 M Street, N.W., Room 222
Washington, D.C. 20554

Dear Mr. Caton:

Re: CPNI, CC Docket No. 96-115

A copy of the attached analysis of privacy issues, and accompanying summary of points, by Privacy & Legislative Associates was sent to the individuals listed below. Please include this material in the above-referenced docket. We are submitting two copies of this notice, in accordance with Section 1.206(a)(1) of the Commission's rules.

Please stamp and return the provided copy to confirm your receipt. Please contact me should you have any questions.

Sincerely yours,

Attachment

cc: L. Atlas
D. Atwood
P. Gallant
R. Keeney
B. Kehoe
A.R. Metzger
G. Teicher

JAN 29 1997

PRIVACY & LEGISLATIVE ASSOCIATES
1150 CONNECTICUT AVE., N.W., SUITE 700
WASHINGTON, D. C. 20036
202-296-2862

January 23, 1997

A. Richard Metzger, Jr.
Deputy Chief, Common Carrier Bureau
Federal Communications Commission
1919 M Street, N.W.
Room 500
Washington, D.C. 20554

Re: Telecommunications Carriers' Use of Customer Proprietary Network Information, FCC Docket No. 96-115

Dear Mr. Metzger:

Privacy & Legislative Associates, Inc. has authored this analysis of privacy issues relevant in the above-referenced docket.[1] We submit this analysis on behalf of the Pacific Telesis Group.

I. SUMMARY

This submission makes the following three points.

- Customer Proprietary Network Information ("CPNI") contains personal information and is appropriately the subject of privacy concern. The use of CPNI, however, does not pose the same privacy risks as does the use of certain other categories of personal information, such as medical and financial record information. For the reasons discussed below, CPNI is not as "sensitive" as medical or financial or certain other categories of personal information.

- Because CPNI is not as "sensitive" as many other kinds of personal information, it is appropriate that the use and disclosure of CPNI be subject to opt-out rules, as opposed to affirmative consent rules -- opt-in rules -- customarily applied to medical and financial records.

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[1] See Appendix A for a description of Privacy & Legislative Associates, Inc.

- The sharing of personal information among affiliated corporations (related by common ownership or control) is customarily permitted, subject to customer notice and opt-out, where the personal information at issue is not highly sensitive.

II. SENSITIVITY OF CPNI

An opt-out process -- customer notice of intended information disclosures and/or uses and an opportunity for the customer to indicate the customer's disapproval of the proposed disclosure and/or use -- is a legitimate, customary and appropriate process when the information at issue is relatively non-sensitive and the disclosure and use at issue do not affect an individual's eligibility for or access to benefits or entitlements.

While no exact formula measures the level of sensitivity of personal information, the following three factors customarily are used to classify or rank the sensitivity of personal information:

- The subject matter to which the information pertains;
- The relationship between the individual about whom the information is collected and the collector of the information ("relational interest"); and
- The actual and potential use of the information.[2]

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[2] Moreover, sensitivity varies substantially depending upon the individual about whom information is collected. Analyses conducted by Dr. Alan F. Westin of Columbia University and Privacy & Legislative Associates, and based upon surveys conducted by Louis Harris and Associates and commissioned by Equifax, indicate that the public divides into three categories of privacy sensitivity. Approximately 16 percent of the public are "privacy unconcerned" and, for them, there is very little in the way of personal information which they deem to be "sensitive." Another approximately 24 percent of the public can be classified as "privacy fundamentalists" and, for them, almost any personal information is deemed to be quite sensitive. The majority of the American public, approximately 60 percent, can be usefully categorized as "privacy pragmatists." For them, the sensitivity of personal information will vary, depending upon the factors discussed in this submission, as will their tolerance for the disclosure and use of this information. The 1996 Equifax-Harris Consumer Privacy Survey, at 13-14 (1996).

CPNI, as defined in the Telecommunications Act of 1996, consists of:

(A) information that relates to the quantity, technical configuration, type, destination, and amount of use of a telecommunications service subscribed to by any customer of a telecommunications carrier, and that is made available to the carrier by the customer solely by virtue of the carrier-customer relationship; and

(B) information contained in the bills pertaining to telephone exchange service or telephone toll service received by a customer of a carrier; except that such term does not include subscriber list information.[3]

As such, CPNI is personally identifiable information and its collection, use and disclosure can raise privacy issues. On the other hand, however, CPNI is not as sensitive as other personally identifiable information such as medical record information, financial and credit record information, insurance information, employment performance information and other categories of personal information which provide insight into an individual's performance or condition or provide information regarding sensitive personal relationships.

[3] The Telecommunications Act of 1996, Sec. 702, Pub. L. No. 104-104, 110 Stat. 148 (codified at 47 U.S.C. § 222).

A. Subject Matter

The Privacy Working Group of the Clinton Administration's National Information Infrastructure Task Force has addressed the issue of sensitivity of personally identifiable information in its "Principles for Providing and Using Personal Information."[4] The explanatory commentary to those principles emphasizes that not all personal information is of equal sensitivity. The commentary calls for a "nuanced" approach to crafting privacy protections which take into account a "host of factors," including specifically, the subject matter of the information. Similarly, the National Telecommunications and Information Administration's Report on Privacy and the NII: Safeguarding Telecommunications-Related Personal Information distinguishes among categories of personal information and concludes that information pertaining to health care, political persuasion, sexual matters and orientation, personal finances and Social Security Numbers are "sensitive" information.[5]

Public opinion surveys make clear that the public evaluates the privacy threat posed by personal information by weighing a variety of factors including, in particular, the subject matter of the information. A 1994 survey conducted by Louis Harris and Associates and commissioned by Equifax with Alan Westin as academic advisor, rated the following four types of personal information as most sensitive: (1) health and medical; (2) banking and credit card; (3) insurance; and (4) credit reports. All of these types of personal information share a common element: they reveal information about health or financial status and, when disclosed

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[4] "Privacy and the National Information Infrastructure: Principles for Providing and Using Personal Information, A Report of the Privacy Working Group," (October, 1995) [hereafter, "Report of the Privacy Working Group"].

[5] U.S. Department of Commerce, National Telecommunications and Information Administration, "Privacy and the NII: Safeguarding Telecommunications-Related Personal Information," (October 1995), at 25 n.98.

without authorization, this kind of personal information customarily has the capacity to embarrass and stigmatize the individual about whom the information is collected.[6]

Health and medical record information, for example, is widely viewed as extraordinarily sensitive.

> Medical records often contain intimate personal information. If disclosed to others, this information could cause embarrassment and humiliation.... Disclosure of medical information could also damage family relationships, reputation and self-esteem.[7]

CPNI, by contrast, does not contain intimate personal information and, if disclosed to others, poses far less of a risk than health and medical information of resulting in embarrassment, humiliation or stigma. For example, the unauthorized disclosure of medical record information, containing such intimate details as a history of physical or mental illness or a genetic predisposition to a certain disease, can result in humiliation and embarrassment. Similarly, the unauthorized disclosure of financial record information, such as depository records or credit history, can embarrass and stigmatize. The unauthorized disclosure of CPNI, by contrast, does not present nearly the same threat. For example, information about the number of telephones in a residence or whether the customer subscribes to call waiting is highly unlikely to embarrass, humiliate or stigmatize the customer.

B. Relational Interest

Most personal information is not "created" wholly by the individual who is the subject of the information. Instead, personal information customarily arises out of transactions or events which occur in a relationship. In some of these relationships, such as a doctor-patient

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[6] See, Bloustein, "Privacy as an Aspect of Human Dignity," Philosophical Dimensions of Privacy, Shoeman F., Editor (1984) at 176.

[7] "Privacy Rights in Medical Records," 13 Ford. Urban L.J. 165 (1985).

relationship, a lawyer-client relationship or a banker-depositor relationship, creating and sharing personal information is crucial to establishing a bond of trust which, in turn, is critical to the success of the relationship. In other words, the express or implied promise of privacy and confidentiality attaching to the relationship is viewed as a prerequisite for the success of the relationship.

In calculating the sensitivity of categories of personal information, it is important and customary to evaluate the relational interest in which the information is created and used, including the extent to which there is an existing relationship between the individual about whom information is collected and the information collector; the degree of trust between the individual about whom information is collected and the information collector; and the extent to which there is an expectation that the information will be kept confidential.

Confidentiality in the relationship between a telecommunications carrier and a customer (apart from the content of telephone or telecommunications messages) is not as important as confidentiality is in certain other relationships, such as the doctor-patient relationship. In the doctor-patient relationship, if a patient fears that the doctor will divulge the patient's sensitive medical information, the patient will not repose trust and confidence in the doctor and thus, the patient is less likely to fully and candidly share wide-ranging and intimate personal information.[8] In the relationship between a customer and a telecommunications carrier, by contrast, it is not imperative or even appropriate that the customer share wide-ranging and intimate personal information. Simply stated, privacy and confidentiality safeguards are not as critical to the success of the telecommunications carrier-customer relationship as they are to the doctor-patient relationship.

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[8] "Confidentiality encourages the unfettered exchange of information between the patient or client and the professional. Such uninhibited discourse is essential to effective treatment or therapy. Under this view of confidentiality, the immunity arising from non-public disclosure of health care information protects the integrity of the relationship by promoting trust between the patient or client and the professional." Turkington, "Legal Protection for the Confidentiality of Health Care Information in Pennsylvania: Patient and Client Access," 32 Vill. L. Rev. 259, 268 (April, 1987).

This view is reflected in the results of a 1993 Louis Harris survey conducted for *Privacy & American Business*. The survey asked the public, "how important is it that businesses have strong privacy policies?" The following categories of services (and relationships) were seen as requiring very strong privacy policies: banks - 72 percent of the public said that strong privacy policies are "very important"; health insurance companies and hospitals and clinics - 71 percent provided this answer; credit card companies - 67 percent provided this answer; life insurance companies - 66 percent provided this answer; and stock brokers and investment firms - 56 percent provided this answer. By contrast, only 53 percent of the American public said that it was "very important" that long distance telephone companies adopt strong privacy policies. This finding is consistent with the view that the American public does not think that the relationship between consumers and telephone companies is the kind of fiduciary relationship that requires or warrants privacy policies in the same way that the relationship with health or financial service providers does.

C. The Purpose for Which CPNI Can Be Used

The third element that is customarily considered in a sensitivity calculation is the extent to which personal information is being used, or could be used, to make significant decisions affecting an individual's access to benefits or entitlements. CPNI is used only to provide telecommunications services to a customer or to market such services to an existing or potential customer. Medical record information, by contrast, can, and does, influence decisions about treatment; about entitlement to health care payment; and about employment decisions, licensing decisions, and numerous other decisions that have a significant impact upon an individual.[9] Similarly, financial and credit report information can, and does, routinely influence decisions

[9] See, for example, "Health and Medical Records" in Trubow, Privacy Law and Practice, Matthew Bender and Co. (1991) at 7-3 through 7-5.

about access to credit (and thus, access to goods and services), access to insurance and, in some cases, access to employment and licensing.[10]

On the other hand, CPNI is not used to allocate scarce resources or benefits. Indeed, it is difficult even to envision how CPNI could be used to make a significant decision affecting an individual. Instead, CPNI is used to make service decisions regarding a consumer's existing telecommunications services and to apprise consumers of new or enhanced telecommunications products and services. These are not decisions that have a significant or adverse impact upon consumers.

Applying the three criteria customarily used in a sensitivity analysis -- the subject matter of the information; its impact on the relationship in which it was created; and its potential for use in making decisions affecting benefits and entitlements -- it is clear that CPNI is not sensitive personal information in the way that medical or financial record information is sensitive. This does not mean that there is no privacy interest in CPNI or that privacy safeguards should not be attached to CPNI. It does mean, however, that these privacy safeguards should be proportionate to CPNI's privacy sensitivity and risk. A sensitivity analysis of CPNI, therefore, suggests that an opt-out approach -- and not an opt-in approach -- is the preferred and attractive option.

III. OPT-OUT IS CUSTOMARY AND APPROPRIATE

Under an "opt-in" approach, an information holder cannot disclose personally identifiable information unless the individual affirmatively consents to the disclosure. Under an "opt-out" approach, an information holder may disclose personally identifiable information

[10] "For many Americans their credit standing is a significant asset. Their credit reporting file affects their access to home mortgages, car loans and other forms of consumer credit, residential tenancies, employment and even insurance." National Consumer Law Center, Fair Credit Reporting Act, Third Edition (1994) at 29.

unless the individual, after receiving a notice describing the proposed disclosure(s), notifies the holder that the individual does not consent to the disclosure.

An opt-out approach is the customary and appropriate method for obtaining an individual's approval for the use and disclosure of personal information pertaining to the individual when the subject matter of the information is personal, but not highly sensitive; when the information has not been developed in a fiduciary relationship; and when the information is not used, intended to be used or capable of being used to make significant decisions about the individual. For all of these reasons, it is appropriate that the use and disclosure of CPNI be subject to an opt-out procedure.

The notion that an individual should have notice of the collection, maintenance, use and disclosure of his personal information by a recordkeeper and an opportunity, in some manner, to approve the use or disclosure is relatively recent. In 1973, the Advisory Committee on Automated Personal Data Systems ("Advisory Committee"), appointed by the Secretary of Health, Education, and Welfare, proposed the first-ever comprehensive information privacy principles for computerized recordkeeping of personal information.[11] The Advisory Committee made five recommendations which have come to be referred to as the "Code of Fair Information Practices." The Advisory Committee's report emphasized that these fair information practice principles should be made applicable only to "administrative personal data systems," i.e., systems using personal information to make decisions affecting an individual's access to benefits or entitlements.[12] When personal information is used for other purposes,

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[11] See, Report of the Secretary's Advisory Committee on Automated Personal Data Systems, U.S. Department of Health, Education and Welfare (1973), in Records, Computers and the Rights of Citizens, MIT Press (1973).

[12] Id. at 53.

such as to sell products or services to an individual, the Secretary's Advisory Committee recognized that an opt-out approach would be a practicable and appropriate form of consent.[13]

The Privacy Protection Study Commission's 1977 report also endorsed an opt-out approach for personal information which will not be used to make decisions affecting an individual's access to benefits or entitlements. In discussing the appropriate fair information practice approach to mailing lists and other databases used for marketing purposes, the Privacy Commission stated, "The negative check-off in some form is nonetheless the most convenient method for the individual to use, and is not without benefit to the organization that offers it."[14]

Almost 20 years later, in October of 1995, the Privacy Working Group's Report reached the very same conclusion. In the commentary to the Privacy Working Group's "fairness principle" (which reads, "Information users should not use personal information in ways that

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[13] Id. at 71-73. The Advisory Committee enunciated the following principles:

- There must be no personal data record-keeping systems whose very existence is secret.
- There must be a way for an individual to find out what information about him is in a record and how it is used.
- There must be a way for an individual to prevent information about him obtained for one purpose from being used or made available for other purposes without his consent.
- There must be a way for an individual to correct or amend a record of identifiable information about him.
- Any organization creating, maintaining, using, or disseminating records of identifiable personal data must assure the reliability of the data for their intended use and must take reasonable precautions to prevent misuse of the data. Id. at 53-64.

[14] Report of the Privacy Protection Study Commission, Personal Privacy in an Information Society, p.144 (1977).

are incompatible with the individual's understanding of how it will be used, unless there is a compelling public interest for such use"), the report emphasizes that an information user seeking to use personal information in an incompatible manner must first notify the individual and, "obtain his or her explicit or implicit consent." The commentary goes on to discuss the appropriateness of opt-out versus opt-in, depending upon the use involved.

> The nature of the incompatible use will determine whether such consent should be explicit or implicit. In some cases, the consequences to an individual may be so significant that the prospective data user should proceed only after the individual has specifically opted into the use by explicitly agreeing. In other cases, a notice offering the individual the ability to opt out of the use within a certain specified time may be adequate.[15]

A. Examples of Opt-Outs in Connection with Other Types of Personally Identifiable Information

1. Fair Credit Reporting Act, as Amended by the Consumer Credit Reporting Reform Act of 1996

Numerous statutes and regulations provide for an opt-out, even when the personal information at issue is arguably more sensitive than CPNI.

For example, the prescreening provisions of the Consumer Credit Reporting Reform Act of 1996 contain opt-out authorization.[16] Consumer reporting agencies may provide consumer reports for credit and insurance prescreening purposes (marketing offers of credit or insurance), provided that the following opt-out options are offered:

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[15] Report of the Privacy Working Group, supra note 4, at 8.

[16] The Consumer Credit Reporting Reform Act of 1996 was enacted as part of the Omnibus Consolidated Appropriations Act of 1997, Pub. L. No. 104-208.

- Written Notification: A signed notice of opt-out election form is distributed by the consumer reporting agency; or

- A Consumer Reporting Agency Notification System: A toll-free telephone number system; and an annual notification in a publication of general circulation that consumer reports may be used in this manner and the address and toll-free telephone number for consumers to use to select the opt-out option.[17]

CPNI (like consumer credit information when used for prescreening purposes) is used for marketing purposes, i.e., to acquaint consumers with the opportunity for new or enhanced telecommunications services. On the other hand, credit reporting information, in terms of its subject matter, is almost certainly more sensitive than CPNI information. Accordingly, the fact that the Congress in 1996 felt comfortable prescribing an opt-out procedure for this kind of use of credit reporting information provides support for applying an opt-out procedure to the use of CPNI.

2. Medical Directory Information

The Uniform Health Care Information Act ("Uniform Act"), adopted by the National Conference of Commissioners on Uniform State Laws and now enacted in several states, requires an opt-in for disclosures of health care information that is to be used for purposes of making decisions regarding benefits or entitlements but requires only an opt-out when the health care information at issue is less sensitive and where the information is unlikely to be used for purposes of determining benefits or entitlements. For example, Section 2-104(b)(1) of the Uniform Act provides that, "a health care provider may disclose health care information about a patient without the patient's authorization if the disclosure is directory information, unless the patient has instructed the health care provider not to make the disclosure."[18]

[17] Consumer Credit Reporting Reform Act § 2404(a)(2) (to be codified at 15 U.S.C. § 1681b(e)).

[18] "Directory information" is defined as "information disclosing the presence and the general health condition of a particular patient who is an in-patient in a health-care

Furthermore, the Uniform Act provides that, where the disclosure of personally identifiable health care information is to immediate family members or to any other individual with whom the patient is known to have a close personal relationship, or is to any health care provider who has previously provided health care to the patient, the disclosure can be made unless the patient has "opted-out" by "instruct[ing] the health care provider not to make the disclosure."[19]

3. Driver's Privacy Protection Act

In 1994, the Congress enacted the Driver's Privacy Protection Act in order to restrict the disclosure of personal information collected by state motor vehicle departments.[20] Under the Driver's Privacy Protection Act, state motor vehicle departments are permitted to disclose "personal information" (i.e., photograph, Social Security Number, driver identification number, name, address (excluding zip code), telephone number, and medical and disability information but not driving history), for certain categories of uses (i.e., government uses, motor vehicle safety uses); and for any other use, provided that the department has developed a system by which individuals are given adequate notification and an opportunity to opt-out.[21]

The Driver's Privacy Protection Act uses the opt-out approach, even though the information at issue is arguably more sensitive than CPNI, and even though the information can certainly be used for determining eligibility for benefits or entitlements. The factors that encouraged the Congress to rely on an opt-out included the history of motor vehicle

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facility or who is currently receiving emergency health care in a health-care facility." § 1-102(2).

[19] Section 2-104(a)(3) and (5).

[20] Driver's Privacy Protection Act of 1994, Pub. L. No. 103-322, 18 U.S.C.A. § 2721 - § 2725.

[21] Prior to the enactment of the Driver's Privacy Protection Act, the following seven states had enacted legislation permitting the disclosure of information held by motor vehicle departments subject to an opt-out: Delaware, Illinois, Maryland, New York, Oregon, Utah and Wisconsin.

information as public record information and the convenience of the opt-out for motor vehicle departments and the consumer.

4. State Opt-Out Statutes

In the last two years, numerous states have enacted information privacy legislation with opt-out provisions. Customarily, states have selected opt-out strategies for relatively non-sensitive types of personal information, such as "public records," or in circumstances where information is not being used to determine eligibility for benefits or entitlements.[22]

5. Direct Marketing

The Direct Marketing Association ("DMA"), the national trade association for the direct marketing industry, encourages the direct marketing industry to adhere to the DMA's Fair Information Practice Guidelines ("Guidelines").[23] The DMA's fourth Guideline provides that, "An individual should have the ability to limit the disclosure of information about her or him that was obtained for one purpose from being disclosed for other unrelated purposes."[24] The

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[22] Vermont adopted legislation permitting telecommunications customers to opt-out of a database permitting the display of the customer's name in the state's enhanced emergency 911 system. Connecticut and Massachusetts both added opt-out provisions to privacy legislation relating to financial services information (Connecticut H. 6667, signed into law on June 6, 1995, and Massachusetts S. 79, signed into law on September 7, 1995). Alaska, Delaware, Iowa, Minnesota, New Hampshire, Tennessee and West Virginia have all enacted legislation in the last two years implementing the Driver's Privacy Protection Act and including opt-out provisions. Maine enacted direct marketing legislation with an opt-out provision (H. 100/LD 135, signed into law on June 27, 1995). Washington state enacted health and medical record legislation which includes an opt-out provision for certain "non-sensitive" types of medical record information (H. 1589, signed into law May 8, 1995).

[23] Direct Marketing Association, Inc., Fair Information Practices Manual, Chapter 2, p. 1.

[24] Id. at Ch. 2, p. 2.

system which the DMA supports for limiting such disclosures is to provide individuals with notice regarding the uses of customer lists and an opportunity to opt-out.[25]

Under the DMA's Mail Preference Service ("MPS") and Telephone Preference Service ("TPS"), consumers may contact the DMA and request that their names be removed from the mailing lists of marketing companies which participate in the MPS.[26] Businesses subscribing to the MPS are notified periodically of the names of consumers who have exercised their opt-out option.[27]

B. Model Notices and Opt-Out Language

Providing an effective notice at regular intervals and a convenient opportunity and method for consumers to communicate an opt-out is critical to the development of a meaningful opt-out system.

Literally thousands of companies have adopted notice and opt-out policies to apply to the disclosure of personal information -- particularly where the information does not involve highly sensitive categories of personal information and where the information is not being used or disclosed for purposes of making decisions regarding benefits or entitlements. We have collected a group of the best examples of opt-out notices in Appendix B.

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[25] Id. at Ch. 2, pp. 2, 4.

[26] Id. at Ch. 2, pp. 7-8.

[27] Id. at Ch. 2, p. 11.

These notices share several common features:

- The opt-out notices describe the uses and disclosures in sufficient detail to be meaningful to the consumer and specifically identify information which is not disclosed and, therefore, not subject to the opt-out. Notices also concentrate on uses or disclosures that might not be anticipated by the consumer or do not seem to be compatible with the relationship or the purpose for which the consumer's information was first collected.

- The notices are relatively brief and, in general, do not exceed one page.

- The notices are in "plain English." The Federal Trade Commission and various consumer groups have done studies which establish the importance of expressing consumer notices in very simple, easy to understand language.

- The notices contain numerous headings and other visual cues.

- The notices explain how the opt-out works; how much time elapses between the time the opt-out designation is signed and returned to the recordkeeper and the time the opt-out goes into effect; the period of time for which the opt-out is effective and whether the opt-out must be renewed; and whether, and the extent to which, the opt-out applies to any new information about the consumer obtained by the third party recordkeeper after the date of the submission of the opt-out.

- Opt-out designations and notices which incorporate these kinds of characteristics have proven to be practicable and successful for third party recordkeepers and meaningful and effective for consumers.

IV. AFFILIATE SHARING

In recent years, the Congress and state legislatures have applied more flexible privacy rules when personal information is shared among corporate affiliates than when it is shared with third parties. This is especially apt to occur when the personal information at issue is not highly sensitive and/or the corporate affiliate is expected to use the information for a purpose compatible with the purpose for which the information was first collected or for a purpose, such as marketing, that does not involve a decision about access to entitlements or benefits. CPNI meets all of these criteria. The personal information comprising CPNI is not highly sensitive and a telecommunications carrier's affiliates will use CPNI for marketing purposes

-- not to make decisions about access to benefits or entitlements.

Public opinion research makes clear that the American public feels comfortable receiving marketing offers from corporate affiliates. A 1994 survey by Louis Harris and Associates conducted for MasterCard International and Visa U.S.A., with Alan Westin as academic consultant, found that 63 percent of the public feel that it is acceptable for "subsidiaries of the same corporate family" to share customer information "to make offers of services or products."[28]

A variety of factors account for the public's comfort level with marketing offers from affiliated companies. The consumer, of course, already has a relationship with the company and has, therefore, already reposed a degree of trust in the company. Furthermore, consumers have expectations that companies share information among employees, contractors and agents in order to accomplish the mission for which the consumer's personal information was first collected. Where the sharing also includes another use which does not have a significant impact upon the consumer, such as a marketing use, it is apparent that disclosure and use by other corporate family members comes within the ambit of consumer expectations.

There are numerous examples of permissible sharing of personal information among affiliated parties. Under the Fair Credit Reporting Act, as amended, for example. reports pertaining to transactions or experiences of a consumer with a company which are then shared with an affiliate of that company ("persons affiliated by common ownership or common

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[28] "Consumers and Credit Reporting 1994 Conducted for MasterCard International, Inc. and Visa U.S.A. Inc.," Louis Harris and Associates, Inc., pp. 11-12. More specifically, 71 percent of the public said that it was acceptable to offer a credit card to customers who have a mortgage with one of the credit card issuer's subsidiaries; 77 percent found it acceptable to offer a credit card to customers who have a checking account with the issuer's subsidiary; 70 percent found it acceptable to offer insurance to customers who have a loan with the insurance organization's subsidiary; and 71 percent said that it was acceptable to offer mutual funds to customers who have a checking account or loan with one of the subsidiaries. Id.

corporate control") do not fall within the definition of "credit report" and are, therefore, not subject to the Fair Credit Reporting Act.[29] Similarly, all other communications between a company and its affiliates are not considered "credit reports" as long as the consumer is provided with a notice that the information may be communicated between the company and its affiliates and the consumer has an opportunity to "direct that such information not be communicated among such persons."[30]

As another example, numerous health and medical record privacy bills and statutes permit the sharing of health information with agents and contractors, as well as other health care providers who have previously provided care to the patient (the NCCUSL Uniform Law includes this kind of provision) on the theory that these are affiliated persons who not only have a need for access to the information but, perhaps more importantly, present less of a privacy threat with respect to the use of the information.

Even various information privilege laws recognize the concept of affiliated parties. Under both the lawyer-client and the doctor-patient privileges, for example, disclosures to affiliated parties sharing a common interest do not necessarily forfeit the privilege.[31] The courts and the common law have come to recognize that these disclosures are often necessary and useful to effectuate the purpose for which the privilege exists and are not inimicable to confidentiality and the prohibitions against third party disclosure on which all information privileges rest.

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[29] Consumer Credit Reporting Reform Act, § 2402(e), § 2419(2). See, § 2411(e) ("Duties of Person Taking Certain Actions Based on Information Provided by Affiliate") (amending 15 U.S.C. § 1681m(c)). See, also, Andrew Taylor, Bank Regulations Eased, Congressional Quarterly, Dec. 7, 1996, at 3358.

[30] Consumer Credit Reporting Reform Act, § 2402(e).

[31] See, United States v. McPartlin, 545 F.2d 1321, 1335-37 (7th Cir.), cert. denied, 444 U.S. 833 (1979).

V. CONCLUSION

We appreciate this opportunity, on behalf of the Pacific Telesis Group, to present information regarding the "sensitivity" of CPNI; the appropriateness of an opt-out procedure for CPNI; and the relative absence of a privacy threat when CPNI is disclosed among affiliated parties.

Respectfully submitted,

Alan F. Westin by RRB

Robert R. Belair

Privacy & Legislative Associates, Inc.
1150 Connecticut Avenue, N.W., Suite 700
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(202) 296-2862

On behalf of Pacific Telesis Group

APPENDIX A

Privacy & Legislative Associates, formed in 1993, specializes exclusively in privacy matters. The two founders and principals, Alan F. Westin and Robert R. Belair, have a combined 70 years of experience as lawyers and political scientists in the privacy arena.

Dr. Westin is widely regarded as the nation's leading privacy expert, having written dozens of books and monographs on the subject including *Privacy and Freedom* and *Databanks in a Free Society*, two seminal works in the field. He has also pioneered in public opinion and survey research on privacy and has served as privacy advisor to many of the nation's largest and best known corporations.

Robert Belair is a Washington lawyer specializing in privacy matters. Mr. Belair has served as an attorney at the Federal Trade Commission, handling, among other things, Fair Credit Reporting Act matters and as Deputy Counsel of the White House Committee on the Right of Privacy. Mr. Belair has served as General Counsel of the National Commission on the Confidentiality of Health Records and as a privacy lawyer and consultant for numerous government agencies and commissions including the National Science Foundation, the National Paperwork Commission and the National Academy of Sciences.

APPENDIX B

MODEL NOTICES AND OPT-OUT LANGUAGE

Many companies that collect information about customers, particularly companies collecting non-sensitive personal information, have developed and currently implement methods by which they notify customers of the companies' policies regarding the disclosure of personal information and customers' options to opt-out of such disclosures. The most effective notices and opt-out provisions provide adequate notice regarding possible uses or disclosures of the information and the opt-out option and are clear, concise and written in "plain English." The following are examples of notice and opt-out provisions that meet these criteria.

AMERICAN EXPRESS[1]

An Important Notice Concerning Cardmember Privacy, Mailing, and Telemarketing Options

At American Express, we want you to understand all that the Card affords you, including the offers you receive through the mail and by telephone.

These offers come directly from us, from our affiliates, from establishments that accept the Card, or from other well-established companies. Each offer is carefully developed to ensure that it meets our standards. Additionally, we try to make sure that these offers reach only those Cardmembers most likely to take advantage of them.

To do this, we develop lists for use by us and our affiliates based on information you provided on your initial application and in surveys, information derived from how you use the Card that may indicate purchasing preferences and lifestyle, as well as information available from external sources including consumer reports.

We may also use that information, along with non-credit information from external sources, to develop lists which are used by the companies with whom we work.

These lists are developed under strict conditions designed to safeguard the privacy of Cardmember information.

Notice to New Cardmembers: Your name and address will be suppressed from marketing mailing lists used by non-American Express companies for four weeks after you have been accepted for Cardmembership to give you an opportunity to elect not to receive marketing mailings in accordance with this notice.

Many Cardmembers tell us they appreciate these offers, as well as information on Cardmember benefits. However, if you no longer wish to receive these offers and information about benefits, please select one or more of the following options:

- o Please exclude me from American Express mailings, including new benefits and American Express Merchandise Services catalogs.
- o Please exclude me from mailings by other companies, including offers in cooperation with American Express provided by establishments that accept the Card.
- o Please exclude me from lists used for telemarketing.

If you have previously informed us of your preferences, you do not need to complete this form unless you have new accounts to add, or wish to change your selections.

Please enter all of your American Express and Optima® Card account numbers for which you would like the options to apply.

- o Check here if you also wish these selections to apply to Additional Cardmembers on your account(s).

Please note:

- 8 to 10 weeks are generally required for your request to become effective.
- So that you receive important information about the Card, we may continue to enclose notices in your monthly account statement, and on a very limited basis, we may send you other notices from American Express.

[1] Handbook of Company Privacy Codes (Vol. 3, 1996) (compiled by ***Privacy & American Business***), 13-14.

HARRON CABLEVISION[2]

SUBSCRIBER PRIVACY NOTICE

Section 631 of the Cable Communications Policy Act of 1984, as amended by the Cable Television Consumer Protection and Competition Act of 1992 ("Cable Act") requires us to inform you of the following information annually:

1. So that we may continue to provide reliable, high quality service to you, we keep regular business records that contain your name, address, and other personally identifiable information. Such records include billing, payment and deposit records, records indicating the number of television sets you have connected to cable, and the service options you have chosen. We use this information to make sure that you are being properly billed for the service you receive. We also use this information to sell, maintain, disconnect, and reconnect services, for service calls, customer surveys, bill collections, in-house telemarketing, our own tax and accounting records, statistics, demographic studies, and the detection and prosecution of theft of services. We take reasonable precautions to prevent unauthorized access to this information.

2. We consider information we keep to be confidential. We may collect personally identifiable information from you and may disclose it to a third party if (a) you consent in advance in writing or electronically; (b) disclosure is necessary to render cable service and other services we provide to you and related business activities; or (c) disclosure is required under court order, and you are notified of such order. Disclosure "necessary to render cable services" includes release of personally identifiable information to employees, contractors, and other agents of the company to install, market, provide and audit cable service; to collection agencies if necessary to collect past due bills; to program suppliers (or their agents) to send program guides and for auditing purposes; to our attorneys and accountants if required for the proper functioning of our business; to third party billing systems to prepare and send your bills; and to our attorneys and law enforcement agencies if necessary for the detection and prosecution of theft of services.

3. Unless you object, from time to time, we may also disclose your name and address for cable-related mailing lists and other purposes. This information may also be used for surveys and various marketing mailings. We will not disclose the extent of your viewing or use of a particular service or the nature of any transaction you may make over the cable system, but we may disclose that you are among those who subscribe to a particular service. If you wish to remove your name from such lists or limit the use of your name at any time, please contact us in writing. Your written notification should NOT be sent with your payment, it should be mailed to your local Harron Cable TV office. The local office address appears on the top left corner of your bill.

Please note, however, Harron does <u>not</u> release the names and addresses of its customers to any third party <u>except</u> as it relates to providing legitimate cable-related services to our customers.

4. We may also electronically test the system from time to time to determine whether you are being properly billed for the cable services you are receiving.

5. We will maintain information about you for as long as we provide service to you, and for a longer time if necessary for related business activities. Ordinarily, for tax reasons, we would keep records for six (6) years. When information is no longer necessary for our purposes, we will destroy the information unless there is a legitimate request or order to inspect the information still outstanding.

6. You have the right to inspect our records that contain information about you, correct any error in our information, and enforce your rights under federal law. Included among your federal rights is the right to participate in a proceeding in which the government seeks to obtain your personally identifiable information from the company. If you wish to inspect the records at our system office pertaining to you or review your statutory rights, please contact us to set up an appointment during regular business hours.

7. Federal law limits our collection and disclosure of personally identifiable information, except as described above. An aggrieved party may bring a private action to enforce his/her federal rights, including recovery of statutory damages and costs.

8. If you have previously notified us, in writing, to remove your name from any mailing list, it is NOT necessary to notify us again.

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[2] <u>Handbook of Company Privacy Codes</u> (Vol. 2, 1995) (compiled by ***Privacy & American Business***), 10.

PRIVACY RIGHTS[3]

IMPORTANT SUBSCRIBER PRIVACY NOTICE

Cable television subscribers are entitled to certain privacy rights under the Cable Communications Policy Act of 1984. The act restricts the ways in which we may collect, retain and disclose personally identifiable subscriber information, and requires us to inform you of your rights and remedies.

We maintain records containing your name, address, telephone number, and information concerning service packages and equipment, and service complaints and repairs. Our records also contain information on billing and payment including (for new subscribers after 9-1-91) credit information as well as credit card information for pay-per-view events. We use this information to provide the services you order and for billing, tax, accounting, marketing and research functions.

We will not disclose personally identifiable subscriber information to any third party without a subscriber's prior consent, except when disclosure is necessary to provide our services or to conduct our business. We may provide information to outside contractors and engineers to perform installation, maintenance, or repair functions; to computer services and accountants for billing, collection, and financial purposes; to program suppliers for audit purposes; and to distributors to provide program guides. In addition, law enforcement authorities may obtain personally identifiable subscriber information from our records upon court order. You must be afforded the opportunity to appear in court and contest the government's claim. We're required to notify you if a court order is entered requiring us to make disclosure.

We are sometimes requested by outside parties such as charities, independent contractors that conduct advertising and program research, and direct order retailers to supply them with subscribers' names, addresses and services subscribed to. If you don't want to have this information disclosed to these entities, complete the form below and return it to us. Under no circumstances will we provide any information which discloses to them the extent to which you view or use any of our services or the nature of transactions you make through our cable system.

Personally identifiable information about you will be collected and retained for so long as you remain a subscriber to our system. Thereafter, we will retain such information only for so long as is necessary to complete billing and accounting functions and as otherwise required by law.

No personally identifiable subscriber information will be disclosed to third parties after a subscriber ceases to be a subscriber.

You have the right to examine all personally identifiable information about you which we are maintaining at any time during our normal business hours at our offices at 14650 Old Lee Road, Chantilly, Virginia. You may bring to our attention any errors which you believe to exist in such information.

Cable subscribers whose privacy rights are violated under the act may, in addition to any other remedies, bring a civil suit in federal court. The court may award actual or liquidated damages, punitive damages, attorney's fees and litigation costs incurred by the subscriber.

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SUBSCRIBER PRIVACY - REPLY FORM

If you don't want to have your name and address disclosed to the organizations described in the enclosed Subscriber Privacy Notice, complete this form and return it to:

Media General Cable
Attn: Communications Department
14650 Old Lee Road, Chantilly, VA 22021

Signature: _____

Print Your Name: _____

Address: _____

Account Number: _____ Date: _____

~~Personal Identification Numbers (PIN codes) are available upon request to ensure privacy regarding your cable service account.~~

For information please call 378-8422.

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[3] Handbook of Company Privacy Codes (1994) (compiled by ***Privacy & American Business***), 9.

TELECOMMUNICATIONS ACT OF 1996
CUSTOMER PROPRIETARY NETWORK INFORMATION
FCC DOCKET 96-115

SUMMARY OF POINTS MADE IN THE PRIVACY & LEGISLATIVE ASSOCIATES CPNI SUBMISSION

January 23, 1997

THREE FACTORS CUSTOMARILY ARE USED TO CLASSIFY THE SENSITIVITY OF PERSONAL INFORMATION.

The following three factors are customarily used to classify the sensitivity of personal information:

- The subject matter to which the information pertains;
- The relationship between the individual about whom the information is collected and the collector of the information ("relational interest"); and
- The actual and potential use of the information.

CPNI IS NOT A CATEGORY OF HIGHLY SENSITIVE PERSONAL INFORMATION.

- A "sensitivity analysis" of CPNI indicates that CPNI is not sensitive personal information.
- The unauthorized disclosure or use of CPNI is less likely to result in embarrassment, humiliation or stigma than is the unauthorized disclosure or use of medical or financial information.
- CPNI is not used, and has little potential for being used, to make decisions affecting an individual's access to employment, insurance, licenses or other entitlements or benefits.
- Personal information which is not in a highly sensitive category is customarily used and disclosed pursuant to an opt-out procedure.

MEMBERS OF THE PUBLIC CONSIDER THE SUBJECT MATTER OF THE INFORMATION WHEN EVALUATING THE THREAT POSED BY INFORMATION.

- In a 1994 survey conducted by Louis Harris and Associates and commissioned by Equifax with Alan Westin as academic advisor, the public ranked the following four types of personal information as most sensitive:
  - Health and medical information;
  - Banking and credit card information;
  - Insurance information; and
  - Credit reports.

OPT-OUT PROCEDURES ARE WIDELY USED TODAY TO OBTAIN CUSTOMER AUTHORIZATION FOR THE USE AND DISCLOSURE OF NON-SENSITIVE PERSONAL INFORMATION.

- Numerous privacy studies and commissions have endorsed the use of an opt-out procedure for non-sensitive personal information, particularly where it is used for marketing-only purposes.
- Numerous statutes provide for an opt-out:
  - The prescreening provisions of the Fair Credit Reporting Act (as amended by the Consumer Credit Reporting Reform Act of 1996);
  - The Uniform Health Care Information Act medical directory information provisions;
  - The Driver's Privacy Protection Act;
  - A variety of state statutes in the areas of telecommunications, financial services, Driver's Privacy Protection Act implementation, direct marketing, and health and medical record legislation (for "non-sensitive" types of medical record information); and
- The Direct Marketing Association's "Fair Information Practice Guidelines" include an opt-out.

DISCLOSURE OF PERSONAL INFORMATION WITHIN A CORPORATE FAMILY IS CUSTOMARILY ACCOMPLISHED PURSUANT TO FLEXIBLE PRIVACY STANDARDS, INCLUDING AN OPT-OUT PROCEDURE.

- Consumers have already established a relationship of trust with the corporation and public opinion surveys show that consumers are more comfortable with an affiliate obtaining their personal information than with an unrelated third party obtaining the information.

- An opt-out procedure is especially appropriate for affiliate sharing when the personal information is not highly sensitive and is being used for marketing and customer service-only purposes, as is the case with CPNI.