

GAO

Report to the Chairman, Permanent
Subcommittee on Investigations,
Committee on Governmental Affairs,
U.S. Senate

April 1998

TELECOMMUNICATIONS

Telephone Slamming and Its Harmful Effects





United States
General Accounting Office
Washington, D.C. 20548

Office of Special Investigations

B-279628

April 21, 1998

The Honorable Susan M. Collins
Chairman, Permanent Subcommittee
on Investigations
Committee on Governmental Affairs
United States Senate

Dear Madam Chairman:

This letter responds to your request of January 6, 1998, and in subsequent discussions, that we assist the Subcommittee by (1) determining which entities or companies engage in telephone slamming violations—the unauthorized switching of a customer from one long-distance provider to another; (2) determining the process by which the providers defraud consumers; and (3) reviewing what the Federal Communications Commission (FCC), state regulatory entities, and the telecommunications industry have done to curtail slamming. In addition, you asked that we present a case study of a long-distance company that repeatedly slammed consumers as a standard business practice.

Telephone customers who are victims of intentional slamming¹ can be harmed in a number of ways ranging from having to pay higher, sometimes exorbitant, long-distance rates to being unable to use the calling cards of their provider of choice. Determining the prevalence of telephone slamming is very difficult because no central repository for slamming complaints exists. But according to the FCC, slamming is a growing problem: The complaints received by the FCC have grown from under 2,000 in 1993 to over 20,000 in 1997. Further, one local telephone exchange company (another general recipient of slamming complaints) reported receiving over 80,000 complaints in the first 9 months of 1997 alone. Indeed, Daniel H. Fletcher, the owner/operator of the companies discussed in our case study (see app. I), apparently slammed over 500,000 consumers, through his companies, in one effort.

Results in Brief

All three types of long-distance providers—facility-based carriers, which have extensive physical equipment; switching resellers, which have one or more switching stations; and switchless resellers, which have no

¹Sometimes, legitimate mistakes are made in transcribing data that result in slamming, but these mistakes are not paramount to the slamming issue and can be easily rectified.

equipment²—have incentives to engage in slamming. However, switchless resellers—having the least to lose and the most to gain—most frequently engage in intentional slamming, according to the FCC, state regulatory agencies, and the telecommunications industry. Intentional slamming is accomplished by deceptive practices. These include falsifying documents that authorize a switch and misleading customers into signing such a document.

The FCC, state regulatory agencies, and the telecommunications industry each rely on the others to be the main forces against intentional slamming. However, with regard to the FCC, its antislamming measures effectively do little to protect consumers from slamming. Although representatives of state regulatory agencies and the industry view a provider's FCC tariff—a schedule of services, rates, and charges—as a key credential, the FCC places no significance on the tariffs that long-distance providers are required to file with it before providing service. Although the FCC in 1996 attempted to regulate tariffs out of existence,³ the D.C. Circuit Court stayed that FCC regulation in 1997 as a result of a lawsuit.⁴ The FCC now accepts tariffs; however, it does not review the tariff information.

Thus, having a tariff on file with the FCC is no guarantee of a long-distance provider's integrity or of FCC's ability to penalize a provider that slams consumers. Indeed, as part of our investigation and using fictitious information, we easily filed a tariff with the FCC and could now, as a switchless reseller, slam consumers with little chance of being caught.

State regulatory measures that could preclude slamming range from none in a few states to extensive in others. Industry's antislamming measures appear to be more market-driven. However, a "PIC freeze"—an action that consumers can take by contacting their local exchange carrier and "freezing" their choice of Primary Interexchange Carriers (PIC), or long-distance providers—effectively reduces the chance of intentional slamming.

²Facility-based carriers, e.g., AT&T (American Telephone and Telegraph), MCI Telecommunications Corporation, and Sprint, have the physical equipment including hard lines and switching stations necessary to take in and forward calls. Switching resellers lease capacity on a facility-based carrier's long-distance lines, resell long-distance services, and have one or more switching stations. Switchless resellers also lease capacity and resell long-distance services but have no equipment and little or no substantive investment in their companies.

³47 C.F.R. section 61.20.

⁴MCI Telecommunications Corp. v. FCC, No. 96-1459.

Daniel H. Fletcher, the company owner/operator discussed in our case study, apparently entered the business of long-distance reselling in 1993. Between then and 1996—by when most industry firms ended dealings with his eight companies, his companies had slammed or attempted to slam hundreds of thousands of consumers, some likely more than once. In that period, according to incomplete industry records, Fletcher companies billed their customers at least \$20 million in long-distance charges and left at least \$3.8 million in unpaid bills to industry firms, including long-distance networks, with which they were doing business. Another long-distance provider obtained a \$10-million judgment⁵ against one Fletcher company.

Background of the Slamming Problem

In July 1997, the FCC estimated that U.S. consumers could choose from over 500 long-distance service providers. Slamming subverts that choice because it changes a consumer's long-distance provider without the consumer's knowledge and consent. It distorts telecommunications markets by enabling companies engaged in misleading practices to increase their customer bases, revenues, and profitability through illegal means. In addition, slammed consumers are often overcharged, according to the FCC and the industry; are unable to use their preferred long-distance service; cannot use calling cards in emergencies or while traveling; and lose premiums (e.g., frequent flyer miles or free minutes of long-distance calls) provided by their properly authorized provider.

Collectively, slamming increases the costs to long-distance providers and other firms involved in this industry. Their increased costs occur when slamming victims refuse to pay the charges of unauthorized service providers or when slammers themselves take the profits and leave unpaid bills, sometimes amounting to millions of dollars.

Determining the prevalence of slamming is extremely difficult. Although the FCC began receiving slamming complaints after the divestiture of AT&T in 1985,⁶ no central repository exists for slamming complaints; and no entity, in our opinion, has made a significant effort to estimate the prevalence of slamming. Contributing to the uncertainty concerning the prevalence of slamming, some consumers, who do not review their

⁵Phone Calls, Inc. v. Atlas Communications, Ltd., No. CIV. A. 96-5734, 1997 U.S. Dist. LEXIS 12321 (E.D. Pa. Aug. 8, 1997).

⁶At that time, facility-based carriers began to compete for presubscription agreements with potential customers as a result of the equal access rules and the procedures imposed on the long-distance telephone industry by the FCC and the courts.

monthly telephone bills closely, are unaware that they have been slammed. Others may be aware that they were slammed but take no corrective action, such as filing a complaint.

Customers can voluntarily change their long-distance company—or Primary Interexchange Carrier (PIC)—by contacting, or submitting an “order” to, the local exchange carrier. Long-distance companies can also legitimately process a PIC change to which the customer has agreed through either a written or verbal authorization.⁷

What Entities Engage in Slamming and Why Do They Do It?

The three types of long-distance providers are facility-based carriers such as AT&T, MCI, and Sprint; switching resellers; and switchless resellers. According to representatives of the FCC, numerous state regulatory agencies, and the industry, those who most frequently engage in intentional slamming are switchless resellers. They have the least to lose by using deceptive or fraudulent practices because they have no substantive investment in the industry. Nevertheless, the economic incentives for slamming are shared by all long-distance providers.

Facility-based carriers have an economic incentive to slam because they have high fixed costs for network equipment and low costs for providing service to additional consumers. Thus, providing service to additional consumers, even without authorization, adds to a carrier’s cash flow with little additional cost. Conversely, those same high fixed costs represent a strong commitment to the long-distance industry and a need to maintain the trust, and business, of their existing customers.

Resellers—switching and switchless—also provide long-distance service to their customers. Switching resellers maintain and operate switching equipment to connect their customers to the networks of facility-based carriers. Switchless resellers, however, have no equipment and generally rely on facility-based carriers and other resellers to service their customers. Resellers make a profit by selling long-distance services to their customers at rates that are higher than the fees the resellers pay to facility-based carriers for handling their customers’ calls. Both switching and switchless resellers have an economic incentive to slam because additional customers increase their profits.

⁷Written authorization is obtained by using a letter of agency (LOA), whose sole purpose is to authorize a local exchange carrier to initiate a PIC change. The LOA must be signed and dated by the subscriber requesting the change. (47 C.F.R. section 64.1150(b)) Verbal authorizations are usually initiated by a telemarketer.

Further, unscrupulous telemarketers, that contract with a long-distance provider, may slam consumers to increase their commissions (e.g., a flat fee for every customer switched).

However, entrepreneurial criminals engaged in slamming operations prefer acting as switchless resellers to generate fast profits and to make criminal prosecution more difficult. They have few, if any, overhead costs and need little, if any, financial investment in their businesses. In addition, the cost of filing the required tariff—or schedule of services, rates, and charges—with the FCC to initiate a business is inexpensive; and an unscrupulous individual can avoid that cost altogether. The unscrupulous reseller can then slam customers, collect payments from them, and run—leaving unpaid bills to the facility-based carrier and other entities, such as billing companies, that assisted the reseller. If the reseller did not submit correct information to the FCC or state regulatory agencies, the likelihood of getting caught and prosecuted is negligible.

The owner/operator of our case-study companies used such tactics. (See app. I.) His eight known switchless reselling companies operated at various times between 1993 and 1996, charged their customers at least \$20 million, and have been fined hundreds of thousands of dollars by state regulatory agencies and the FCC. However, neither the FCC nor we were able to locate him in 1997 or to date in 1998 because he has concealed his whereabouts.

How Is Slamming Accomplished?

Both business and individual consumers must select a PIC to provide their long-distance service through their local exchange carrier. Intentional slamming is thus possible because the legitimate ways a consumer's PIC are changed (see following section) can be manipulated easily and in a fraudulent manner.

Slamming can occur through deceptive marketing practices—whether by facility-based carriers, resellers, or telemarketers acting on their behalf—by which consumers are misled into signing an authorization to switch their PIC. Unscrupulous telemarketers or long-distance providers may also falsify records to make it appear that the consumer agreed verbally or in writing to the switch. It is also possible to slam consumers without ever contacting them, such as by obtaining their telephone numbers from a telephone book and submitting them to the local exchange carrier for changing. As an FCC Commissioner stated before a U.S. Senate subcommittee, “slamming scenarios involve [, among other

methods,] deceptive sweepstakes, misleading forms, forged signatures and telemarketers who do not understand the word no.”⁸

What Have the FCC, State Regulators, and the Industry Done to Curtail Slamming?

Although the FCC, most states, and the telecommunications industry have some antislamming rules and practices in place, each relies on the others to be the main forces in the antislamming battle. Of the antislamming efforts, those by some states are the most extensive. However, we found no effective antislamming effort to keep unscrupulous individuals from becoming a long-distance provider. For example, the FCC does not review information submitted to it in tariff filings that may alert it to unethical applicants. In addition, the FCC lags far behind some individual state regulatory agencies in the amount of fines imposed on companies for slamming.

Antislamming Measures

The FCC

The FCC first adopted antislamming measures in 1985⁹ and has subsequently promulgated regulations to improve its antislamming efforts. For example, in 1992 as a result of an increase in telemarketing, the FCC required long-distance providers to obtain one of four forms of verification concerning change-orders generated by telemarketing.¹⁰ Verification would occur upon

- the customer’s written authorization;
- the customer’s electronic authorization placed from the telephone number for which the PIC was to be changed;
- receipt of the customer’s oral authorization by an independent third party, operating in a location physically separate from the telemarketing representative; or
- the long-distance provider’s mailing of an information package to the customer within 3 business days of the customer’s request for a PIC change.

⁸Statement by Susan Ness, Commissioner of the FCC, before the U.S. Senate, Subcommittee on Communications, Committee on Commerce, Science, and Transportation (Aug. 12, 1997).

⁹In a 1985 policy statement (50 Fed. Reg. 25,982 (June 24, 1985)), the FCC decided that allowing customers to select long-distance carriers via ballot rather than automatically assigning consumers, through default, to only one competitor would benefit the public interest. Providers would then have incentive to provide consumers with helpful information and competitive services, which the consumers could use to make informed choices.

¹⁰47 C.F.R. section 64.1100 (1992).

In 1995, as a result of receiving thousands of slamming complaints, the FCC again revised its regulations. The revision,¹¹ in part, prohibited the potentially deceptive or confusing practice of combining a letter of agency (LOA)¹² with promotional materials sent to consumers.

However, we found nothing in FCC practices that would effectively curtail unscrupulous individuals from entering the telecommunications industry. And no FCC regulation discusses what preventive measures the FCC should take to ensure that long-distance-provider applicants have a satisfactory record of integrity and business ethics. Further, according to FCC's Deputy Director for Enforcement, Common Carrier Bureau, Enforcement Division, the FCC relies largely on state regulatory agencies and the industry's self-regulating measures for antislamming efforts.

According to representatives from state regulatory agencies, facility-based carriers, resellers of long-distance services, and others in the industry, they view an entity's possession of an FCC tariff as a key credential for a long-distance provider. Each long-distance service provider is now required¹³ to file a tariff with the FCC, including information that should allow the FCC to contact the provider about, among other matters, an inordinate number of slamming complaints against it.

However, according to knowledgeable FCC officials, the FCC merely accepts a tariff filing and does not review a filed tariff's information, including that regarding the applicant. Thus, the filing procedure is no deterrent to a determined slammer. Neither does the procedure support the validity that states and the industry place on an entity that has filed an FCC tariff.

For example, we easily filed a tariff with the FCC through deceptive means during our investigation when testing FCC's oversight of the tariff-filing procedure. In short, although we submitted fictitious information for the tariff and did not pay FCC's required \$600 application fee, we received FCC's

¹¹47 C.F.R. section 64.1150.

¹²In 1997, the FCC amended the LOA form and content provision, in part, to add the requirement that every LOA must be translated into the same language as any promotional materials, oral descriptions, or instructions provided with the LOA. (47 C.F.R. section 64.1150 (g) (1997))

¹³Under section 203 of The Telecommunications Act of 1934, each common carrier must file a tariff with the Commission. However, under section 203 (b), the Commission has discretion to modify this requirement. In 1996, the FCC promulgated a regulation (47 C.F.R. section 61.20), under which nondominant long-distance providers (e.g., providers without the power to control prices) were exempted from the requirement to file tariffs. However, the regulation was stayed in 1997 as a result of MCI Telecommunications Corp. v. FCC, No. 96-1459. Therefore, all common carriers must file tariffs at the Commission.

stamp of approval. Thus, with a tariff on file, our fictitious company—PSI Communications—is able to do business and slam consumers as a switchless reseller with little chance of adverse consequences.

Another antislamming measure—the FCC’s Common Carrier Scorecard—publicizes the more flagrant slammers, but it is inaccurate. The FCC prepares the scorecard, which lists the long-distance providers about which the FCC has received numerous slamming complaints, for the telecommunications industry and the public. The scorecard also compares those providers by citing the ratio of the number of complaints per million dollars of company revenue. However, it presents an inaccurate picture because it severely understates the number of complaints per million dollars of revenue for resellers. This occurs because resellers are not required to, and generally do not, report their revenue to the FCC unless that revenue exceeds \$109 million. Therefore, in the absence of actual data and for the sake of comparison, the FCC assumes that those resellers had \$109 million in revenue. This assumption results in unrealistically low complaint-to-revenue ratios for a large number of resellers.

States and Industry

According to representatives of some state regulatory agencies, states rely largely on the FCC and the industry’s self-regulating measures for antislamming efforts. While most state regulatory agencies have some licensing procedures and requirements for an entity to become a long-distance service provider, those procedures/requirements vary from negligible to restrictive. For example, Utah does not regulate long-distance service providers. In contrast, in Georgia, switchless resellers must first file an application with the state public utility commission and provide a copy to the governor’s Office of Consumer Affairs. The commission then reviews the submission, determines whether to issue an interim certificate, and rereviews the interim certificate after 12 months to determine whether to issue a permanent certificate. In addition, switchless resellers must adhere to Georgia commission rules.

The telecommunications industry also attempts to weed out companies involved in slamming. For example, various facility-based carriers have different antislamming measures based on the companies’ marketing philosophies. Such measures include MCI’s emphasis on the use of third party verifications and AT&T’s¹⁴ emphasis on use of written authorizations, or LOAs. In addition, a facility-based carrier may question a reseller’s

¹⁴In March 1998, AT&T publicly announced new steps that it would be taking to curb slamming. Those steps included cessation of the use of outside sales agents to sell AT&T long-distance service at community events, such as fairs, and institution of a toll-free hotline to resolve consumer complaints about slamming.

submission of a large number of telephone numbers at one time. However, we found few activities that resellers were undertaking to curtail slamming. In addition, we found no industry practices that would effectively keep unscrupulous individuals from entering the telecommunications industry. Moreover, according to officials of a reselling company and a billing company, the industry largely relies on the FCC and state regulatory agencies for antislamming measures.

Indeed, the most effective antislamming measure appears to be one that consumers themselves can effect against all but the most resourceful of slammers—a “PIC freeze.” The individual customer can contact the local exchange carrier and request a PIC freeze, in essence freezing the customer’s choice of long-distance providers from change. The customer may lift the freeze by recontacting the local exchange carrier and answering certain identifying questions about the customer’s account.

Punitive Actions Against Slammers

In comparison with some states’ actions, the FCC has taken little punitive action against slammers. During 1997, the FCC obtained consent decrees from nine companies nationwide that paid \$1,245,000 in fines because of slamming. However, in May 1997, the California Public Utilities Commission suspended one firm for 3 years because of slamming, fined it \$2 million, and ordered it to refund another \$2 million to its customers. Further, within the same general time period, other state regulatory commissions took more extensive actions than did the FCC against the same companies. For example,

- In December 1996, the California Public Utilities Commission reached a settlement with another company and its affiliate that were involved in slamming. The settlement suspended the firms from offering long-distance service in California for 40 months and required the firms to offer \$600,000 in refunds to 32,000 customers that had complained about slamming. In comparison, during 1997, the FCC issued a Notice of Apparent Liability to this company for \$200,000 for apparent slamming violations.
- In February 1998, the Florida Public Service Commission voted to require a third firm to show cause, in writing, why it should not be fined \$500,000 for slamming violations. (This firm is also the subject of numerous slamming complaints in New Jersey and Tennessee.) In comparison, during 1997 the FCC issued a Notice of Apparent Liability to this firm amounting to only \$80,000 for apparent slamming violations.

Further, the FCC takes an inordinate amount of time, as acknowledged by FCC officials, to identify companies that slam consumers and to issue orders for corrective actions (i.e., fines, suspensions) or to bar them from doing business altogether. For example, Mr. Fletcher, the owner/operator of the case-study companies, began his large-scale slamming activities in 1995. But it was not until June 1997 that the FCC initiated enforcement action¹⁵ against the eight known Fletcher-controlled companies¹⁶ with an Order to Show Cause and Notice of Opportunity for Hearing. In the order, the FCC indicated that it had substantial evidence that the companies had ignored FCC's PIC-change verification procedures and routinely submitted PIC-change requests that were based on forged or falsified LOAS. The FCC thus directed Mr. Fletcher and his companies to show cause in an evidentiary hearing why the FCC should not require them to cease providing long-distance services without prior FCC consent and why the companies' operating authority should not be revoked. Because Mr. Fletcher waived his right to a hearing when he did not file a "written appearance," stating that he would appear for such a hearing, the FCC could have entered an order detailing its final enforcement action against the Fletcher companies and Mr. Fletcher. However, as of March 1998, the FCC had taken no such action.

Conclusions

Neither the FCC, the states, nor the telecommunications industry have been effective in protecting the consumer from telephone slamming. Because of the lack of FCC diligence, companies can become long-distance service providers without providing accurate background information. Some states have taken significant action to protect consumers from slamming, but others have taken little action or have no antislamming regulations. Further, the industry approach to slamming appears to be largely market-driven rather than consumer-oriented. Given this environment, unscrupulous long-distance providers slam consumers, often with virtual impunity. As a consequence, consumers and the industry itself are becoming increasingly vulnerable as targets for large scale fraud. The most effective action that consumers can take to eliminate the chance of

¹⁵In December 1996, the FCC initiated a Notice of Apparent Liability for Forfeiture against one of Mr. Fletcher's companies, Long Distance Services, Inc. An Order of Forfeiture was entered against the company in May 1997.

¹⁶The eight switchless resellers were CCN, Inc.; Church Discount Group, Inc.; Discount Calling Card, Inc.; Donation Long Distance, Inc.; Long Distance Services, Inc.; Monthly Discounts, Inc.; Monthly Phone Services, Inc.; and Phone Calls, Inc. (PCI). Only two of these, Discount Calling Card and PCI, had filed tariffs with the FCC, according to FCC's June 1997 order.

intentional slamming is to have their local exchange carrier freeze their choice of long-distance providers.

Scope and Methodology

Our investigation took place between January and March 1998. We interviewed representatives of the FCC and long-distance providers, including facility-based carriers and resellers. In addition, we interviewed representatives of billing and data-processing firms servicing long-distance providers. We reviewed available public records on slamming including prior congressional hearings and documents belonging to long-distance providers. These included AT&T documents provided to us pursuant to a subpoena issued by the Permanent Subcommittee on Investigations, Senate Committee on Governmental Affairs. Further, through the National Association of State Regulatory Agencies, we obtained and reviewed information from state entities that regulate long-distance service providers. To determine the extent of FCC's oversight of tariff filings, we filed fictitious documentation with the FCC and did not pay the required filing fee.

As arranged with your office, unless you announce its contents earlier, we plan no further distribution of this report until 30 days from the date of this letter. At that time, we will send copies to interested congressional committees and the Chairman of the Federal Communications Commission. Copies of this report will also be made available to others upon request. If you have any questions about our investigation, please call me at (202) 512-7455 or Assistant Director Ronald Malfi of my staff at (202) 512-7420.

Sincerely yours,



Eljay B. Bowron
Assistant Comptroller General
for Special Investigations

Case Study of Daniel H. Fletcher's Business Ventures as a Long-Distance Provider

This case study is based on our limited investigation of four of Daniel H. Fletcher's eight known business ventures¹⁷ operating as long-distance providers between 1993 and 1996. Through each business, it appears that Mr. Fletcher slammed or attempted to slam many thousands of consumers. As a further indication of the extent of his dealings, industry records, although incomplete, indicate that between 1993 and 1996 two of Mr. Fletcher's companies billed their customers more than \$20 million in long-distance charges.

Mr. Fletcher apparently began reselling long-distance services in 1993. By mid-1996, the industry firms dealing with Mr. Fletcher's companies began to end those dealings because of his customers' slamming complaints and/or his nonpayment for long-distance network usage by his customers. Collectively, these firms claim that Mr. Fletcher's companies owe them \$3.8 million. Another firm has obtained a \$10-million judgment against one Fletcher company.¹⁸

Mr. Fletcher's companies have also come under regulatory scrutiny by several states and the FCC. For example, in 1997 the Florida Public Service Commission cancelled the right of one Fletcher-controlled company—Phone Calls, Inc. (PCI)—to do business in the state and fined it \$860,000 for slamming. New York also took action against PCI in 1997. In May 1997, the FCC ordered another Fletcher company—Long Distance Services, Inc.—to forfeit \$80,000 to the United States “for violating the Commission's rules and orders” when it changed (or caused the change of) the long-distance providers of two customers without authorization and through the use of apparently forged LOAS. The FCC did not refer the \$80,000 forfeiture to the U. S. Department of Justice for collection, according to an FCC official, because the Justice Department had previously failed to take action with similar cases. In addition, in June 1997, the FCC, citing numerous complaints and evidence of forged or falsified LOAS, issued an Order to Show Cause and Notice of Opportunity for Hearing regarding Mr. Fletcher and his eight companies. In that order, the FCC, in effect, directed Mr. Fletcher and his companies to show cause why the FCC should not require them to stop providing long-distance services without prior FCC consent and why the companies' operating authority should not be revoked. However, since Mr. Fletcher did not

¹⁷The eight switchless resellers were CCN, Inc.; Christian Church Network, Inc., doing business as Church Discount Group, Inc.; Discount Calling Card, Inc.; Donation Long Distance, Inc.; Long Distance Services, Inc.; Monthly Discounts, Inc.; Monthly Phone Services, Inc.; and Phone Calls, Inc.

¹⁸Phone Calls, Inc. v. Atlas Communications, Ltd., No. CIV. A. 96-5734, 1997 U.S. Dist. LEXIS 12321 (E.D. Pa. Aug. 8, 1997).

provide the FCC a written appearance, or explanation, the FCC could have entered the order, citing FCC's final enforcement action. However, as of March 1998, the FCC had not done so.

It appears that all eight known Fletcher-controlled companies were out of business by the end of 1996. However, our investigation identified several instances of Mr. Fletcher's continued involvement since then in the telecommunications industry. We have been unable to locate Mr. Fletcher for his response to the allegations because he knowingly used false information to conceal his identity and the location of his companies and residence(s).

Fletcher's Christian Church Network, Inc. and Long Distance Services, Inc. Relationships With Billing Concepts and Sprint (1993-1996)

Business Relationships

Based on an introduction by a Sprint representative, Mr. Fletcher's long-distance reselling business Christian Church Network, Inc. (doing business as Church Discount Group, Inc.) entered into a contract on August 18, 1993, with Billing Concepts¹⁹ and Sprint.²⁰

Under the terms of the contract, Christian Church Network submitted electronic records to Billing Concepts, representing its customers' long-distance calls made over Sprint's network. Billing Concepts (1) advanced 70 percent of the calls' cost (as charged by the Fletcher company) to Sprint²¹ and (2) retained 30 percent in reserve for its administrative costs and potential nonpayment by the Fletcher company's customers. Sprint deducted its network charges and sent the remainder to Christian Church Network.

¹⁹Billing Concepts was doing business as USBI.

²⁰Sprint—then known as US Sprint—had a business arrangement with Billing Concepts under which Sprint would introduce resellers to Billing Concepts.

²¹Billing Concepts charged the Fletcher company interest for the money advanced to Sprint.

Under this arrangement, Billing Concepts sent the electronic records of the customers' long-distance calls to the appropriate local exchange carriers for billing (at Christian Church Network's charged rate) and collection. Within 60 days, the local exchange carriers sent approximately 95 percent of the billings' value to Billing Concepts for the Fletcher company. The local exchange carriers withheld 5 percent for possible nonpayment by the Fletcher company's customers.

On July 22, 1994, Sprint, Billing Concepts, and Mr. Fletcher's Christian Church Network modified their agreement whereby Billing Concepts would advance 70 percent²² of the billings directly to the Fletcher company rather than to Sprint. The Fletcher company was to pay Sprint for its network charges from the advances. Then from November 1994 to July 1995, the company did not receive advances²³ from Billing Concepts and instead paid Sprint from payments received from the local exchange carriers. However, starting in July 1995, the Fletcher company requested and again received 70-percent advances from Billing Concepts.

Sharp Increase in Customer Base and Subsequent Problems

From November 1995 through April 1996, Christian Church Network produced a tenfold increase in the billable customer base. Between January and April 1996, the company also apparently stopped paying Sprint for its customers' network usage, keeping the full 70-percent advance from Billing Concepts as its profit. Further, in July 1996, Mr. Fletcher—representing another of his eight companies, Long Distance Services, Inc.—signed a second contract with Billing Concepts.

Billing Concepts continued advances to Christian Church Network until September 1996. Then, after receiving a large number of slamming complaints from Christian Church Network's customers following the increase in the company's customer base, Billing Concepts terminated all business with both Fletcher companies.

From December 1993 through December 1996,²⁴ the two Fletcher companies submitted over \$12,432,000 in bills for long-distance usage to be forwarded to their customers. When Billing Concepts terminated business with the two Fletcher companies in September 1996 because of

²²The Fletcher company still paid interest to Billing Concepts on the advances.

²³The company did this apparently to avoid the interest charges.

²⁴Under the contracts, Billing Concepts continued the billings for the Fletcher companies' customers for 90 days beyond termination of the contract.

the alleged slamming, it had already advanced the companies more than it would receive from the local exchange carriers. (Those carriers returned less than had been billed because some customers did not pay after learning they had been slammed.) Billing Concepts claims that the two Fletcher companies owe it approximately \$586,000 that it was unable to collect from the local exchange carriers.

In addition, Sprint terminated its business relationship with Christian Church Network and Long Distance Services in September 1996 for nonpayment of outstanding network charges. Sprint claims that the two companies still owe it about \$547,000 for that nonpayment. (Sprint attempted to renegotiate its contract with Mr. Fletcher's Christian Church Network before the termination. Our investigation indicates that Mr. Fletcher instead took his increased customer base to Atlas Communications via another of his eight companies, Phone Calls, Inc. [PCI], and did not pay Sprint. See later discussion regarding PCI and Atlas.)

Fletcher's Long Distance Services, Inc. Relationship With AT&T (1994-1997)

On October 19, 1994, Mr. Fletcher, doing business as Long Distance Services, Inc., signed a contract with AT&T to place his customers on its network. The agreement called for Long Distance Services to purchase a minimum of \$300,000 of long-distance service annually.

AT&T's incomplete records²⁵ indicated that starting in March 1996, the Fletcher company began to dramatically increase the number of new customers to be placed on AT&T's network. During an April 8, 1996, telephone call to AT&T and in an April 9, 1996, letter sent via facsimile, Mr. Fletcher requested that AT&T confirm that (1) AT&T had accepted the new customers that his company had transmitted to AT&T since March 1, 1996, and (2) AT&T had put them on line. According to Mr. Fletcher's letter, his Long Distance Services had requested that more than 540,000 new customers be switched to AT&T. The letter also noted that the company was sending an additional 95,000 customer telephone numbers that day.

In an April 9, 1996, return letter²⁶ to Mr. Fletcher, AT&T questioned his customer base and his customers' letters of agency (LOA) authorizing the

²⁵Although AT&T was subpoenaed to provide us all documentation involving its business dealings with Long Distance Services, it produced limited documentation that provided only sketchy information concerning its approximately 3-year contractual agreement with the Fletcher company. AT&T officials told us that because of poor recordkeeping, they were unable to produce the proper records.

²⁶In the letter, AT&T stated that Mr. Fletcher had submitted about 35,000 new customers in March 1996, a significant contrast with the over 540,000 claimed by Mr. Fletcher in his April 9, 1996, letter.

change of long-distance companies. AT&T requested that Mr. Fletcher forward a sampling of the LOAS, and Mr. Fletcher provided approximately 1,000.

In another letter to Mr. Fletcher, dated April 16, 1996, AT&T provided reasons why it believed the LOAS were in violation of FCC regulations (47 C.F.R. section 64.1150): (1) the LOAS had been combined with a commercial inducement, (2) Mr. Fletcher's LOA form did not clearly indicate that the form was authorizing a change to the customer's Primary Interexchange Carrier (PIC), and (3) it did not identify the carrier to which the subscriber would be switched. On April 25, 1996, AT&T wrote Mr. Fletcher informing him that it had rejected all "orders" (new customers) sent by Long Distance Services, Inc., presumably since March 1, 1996.

Although AT&T recognized a problem with Mr. Fletcher and his business practices during April 1996, it continued service to Long Distance Services, Inc. until November 1, 1997, when it discontinued service for nonpayment for network usage. According to an AT&T representative, Long Distance Services, Inc. still owes AT&T over \$1,652,000.

Fletcher's Discount Calling Card, Inc. Relationship With Integretal (1995-1996)

On January 5, 1995, Mr. Fletcher, doing business as Discount Calling Card, Inc., signed a contract with Integretal, a billing company. Although Integretal officials provided us little information, stating that the information was missing, we did determine the following.

From May 5, 1995, through February 26, 1996, Integretal processed approximately \$8,220,000 in long-distance call billings for Discount Calling Card customers. Under the terms of its agreement, Integretal advanced the Fletcher company 70 percent²⁷ of the billing value of the electronic records of calls submitted by the company. Integretal was contractually entitled to retain 30 percent of the calls' value for processing and potential nonpayment by Discount Calling Card's customers.

Because of billing complaints made by Discount Calling Card's customers,²⁸ Integretal claims that it lost about \$1,144,000 that it was unable to recover from the company. Integretal stopped doing business with Discount Calling Card in November 1996 because of numerous customer complaints.

²⁷Integretal charged the Fletcher company interest on the advances.

²⁸Because of incomplete Integretal records, company officials were unable to determine if these were slamming complaints.

Fletcher's Phone Calls, Inc. Relationships With Atlas Communications, Inc. and Sprint (1996)

Business Relationships

On June 18, 1996, the Fletcher-controlled Phone Calls, Inc. (PCI) and Atlas Communications, Inc. signed a business contract for PCI's customers to be placed on Atlas' network (Sprint). In early July 1996, PCI provided its customer base of 544,000 telephone numbers to Atlas. (Information developed by our investigation suggests that Fletcher companies slammed these customers largely from the customer base they had given to Billing Concepts.) Subsequently, Atlas provided the PCI customer telephone numbers to Sprint for placement on Sprint's network.

However, within the next several weeks, Atlas was able to place only about 200,000 telephone numbers from PCI's customer base on Sprint's network. This occurred, according to Atlas representatives, because (1) the individual consumers had placed a PIC freeze with their local exchange carriers, preventing the change or (2) the telephone numbers were inoperative. Because of this low placement rate, Atlas became concerned that PCI was slamming customers and elected not to honor its contract. Subsequently, on August 19, 1996, PCI filed a lawsuit against Atlas in Pennsylvania,²⁹ attempting to obtain (as per the original contract) the raw record material representing the details of its customers' telephone usage, which would allow PCI to bill its customers. Sprint had supplied this raw record material to Atlas.

Legal Scrutiny

In August 1996, Atlas submitted evidence, in the breach-of-contract suit brought by PCI, indicating that many slamming complaints had been made against PCI. For example, after the first bills, representing PCI customers' calls for July and August 1996, had been sent out, an unusually high percentage (approximately 30 percent) of PCI customers lodged complaints with regulators and government law enforcement agencies—including the FCC, various public utility commissions, and various state attorneys

²⁹Phone Calls, Inc. v. Atlas Communications, Ltd., No. CIV. A. 96-5734, 1997 U.S. Dist. LEXIS 12321 (E.D. Pa. Aug. 8, 1997).

general; Sprint; and numerous local exchange carriers. According to an Atlas representative, Atlas attempted to answer these complaints and reviewed the customers' LOAs authorizing the change of long-distance companies. After the review, Atlas believed that a number of the LOAs were forgeries.

According to the vice president of Atlas Communications, the judge issued a temporary restraining order, preventing PCI from obtaining the raw record material. The judge also agreed to allow Atlas to charge PCI's customers at the existing standard AT&T long-distance rates (as the most prevalent U.S. service) rather than PCI's excessively high rates. Subsequently, Atlas entered into a contract with US Billing to perform billing-clearinghouse services for Atlas regarding PCI's customers. In this instance, Atlas' prompt action prevented PCI from receiving any payments for its customers' long-distance calls.

By February 1998, Atlas was serving less than 20 percent of the original 200,000 PCI customers that had been successfully placed on Sprint's network. This sharp drop in the customer base occurred, according to an Atlas representative, largely because PCI had initially slammed the customers. On the basis of the 1996 suit in Pennsylvania, Atlas obtained a \$10-million judgment against the Fletcher-controlled PCI because, according to the court, PCI

- fraudulently obtained customers to switch their long-distance telephone service to Atlas' network;
- identified customers to Atlas, for Atlas' placement on its network, in states within which PCI was not certificated as a long-distance service provider;
- failed to supply customer service to those customers it had caused Atlas to place on its network; and
- failed to supply customers, Atlas, or regulatory agencies with those customers' LOAs upon request.

Further, in August 1997, the Florida Public Service Commission fined the Fletcher-controlled PCI \$860,000 for slamming, failing to respond to commission inquiries, and misusing its certificate to provide telecommunications service in Florida. This fine was in addition to the commission's March 1997 cancellation of PCI's certificate. According to a statement by the chairman of the commission, PCI accounted for over 400 of the nearly 2,400 slamming complaints received by the commission in 1996. This was the largest number of complaints logged by the commission

Appendix I
Case Study of Daniel H. Fletcher's Business
Ventures as a Long-Distance Provider

against any company in a similar period. New York regulators also revoked PCI's license in mid-1997.

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