DT 02-076

VERIZON NEW HAMPSHIRE

Special Contract with Genuity Solutions, Inc.

Order Approving Special Contract

O R D E R   N O. 23,995

June 21, 2002

Pursuant to RSA 378:18-b, on April 22, 2002, Verizon New Hampshire (Verizon-NH)filed a petition for approval of a special contract (Contract) to provide Digipath Digital Services (DDS), Digital Signal Level 3 (DS3), and IntelliLight Broadband Transport (IBT) data transport services to Genuity Solutions, Inc. (Genuity). In support of its petition, Verizon-NH submitted the Contract, a cost analysis, and billing details of the service offerings. Some of the supporting documents submitted are subject to confidential treatment pursuant to RSA 378:43. By Secretarial Letter dated May 13, 2002, the New Hampshire Public Utilities Commission (Commission) extended the length of time for review of the filing by 30 days, making the effective date of the special contract June 21, 2002. *See* RSA 378:18-b, II.

The services offered in the Contract are currently available from a Verizon-New England interstate tariff. FCC Tariff 11, Sections 31.7.9, 31.7.12, and 31.26.5. The terms and conditions in the Contract permit Genuity to purchase DDS and DS3 at discounted rates that are lower than those in the interstate tariff.

Genuity is an Internet Service Provider (ISP). According to the Contract, Genuity is an Enhanced Services Provider eligible to purchase intrastate services under the Contract and applicable state jurisdictional tariffs instead of interstate access services under applicable FCC rules. Contract at Section 11.

Genuity began as a subsidiary of Bechtel Enterprises, and was purchased by a subsidiary of GTE Corporation in late 1997.http://www.genuity.com/announcements/news/press_release_1997 1113-01.xml. When Bell Atlantic and GTE Corp. merged in 2000 to form Verizon Communications, Inc. (Verizon), Genuity was spun off via an initial public offering, as a condition of FCC approval of the merger. http://investor.verizon.com/shareowner/faqs.html, at 7. Verizon retained a 8.2% voting equity interest in Genuity, and the right to purchase the remaining shares upon receipt of authority to enter the interstate interLATA markets under Section 271 of the Telecommunications Act of 1996 (Tact). *Id.*, at 7-8.

Genuity has entered into agreements with Verizon "whereby Genuity will become the preferred provider of internet protocol (IP) backbone and access services" for Verizon. http://www.genuity.com/announcements/news/press_release_20020531-01.xml. In addition, Verizon and Genuity have a contract for Verizon to provide referrals to Genuity's "Black Rocket Voice," an enterprise voice-over-internet service. *Id.* Verizon has also extended credit to Genuity, and Genuity has "the ability to borrow ... $1.7 billion from Verizon and a consortium of banks." *Id.* Genuity has reported its expanded relationship with Verizon as a positive indicator for investors, in its report of First Quarter 2002 financial results. http://www.genuity.com/announcements/news/press release 20020502-02.xml. In pursuit of these stronger ties, Genuity developed a Verizon Awards Program, "to promote mind-share among Verizon sales teams that sell Genuity services." Verizon customer account managers, technology solutions, and regional sales managers had an opportunity to be rewarded for selling Genuity services in 2001. http://genuity.com/dmail/vzawards/form.htm.

COMMISSION ANALYSIS

The general standard for examining special contracts under RSA 378:18 is a two part test: (1) whether sufficient evidence of special circumstances exist; and (2) whether the special contract is just and in the public interest. *Bell Atlantic-New Hampshire (Special Contract Cost Standard Order)*, 84 NH PUC 646, 651 (1999). Public interest considerations include, among other things, both lost contribution and the impact of special contracts on the development of competition. *Id*. To measure the impact of a special contract, as well as to prevent unnecessary loss of contribution, we examine special contracts against the proper price floor and require a showing of sufficient competition. *Id.* at 651-652. In the *Special Contract Cost Standard Order*, we identified the pricing methodology by which the proper price floor is determined for analyzing special contracts under RSA 378:18 and 378:18-b. RSA 378:18-b permits

> all special contracts for incumbent local exchange carriers providing telephone services...[to] become effective 30 days after filing, provided the rates are set not less than: (1) the incremental cost of the relevant service; or (2) where the telephone utilities competitors must purchase access from the telephone utility to offer a competing service, the price of the lowest cost form of access that competitors could purchase to compete for customers with comparable volumes of usage, plus the incremental cost for related overhead.

Accordingly, pursuant to 378:18-b and the *Special Contract Cost Standard Order*, the Contract shall not go into effect unless the cost imputation requirements are met.

Staff has reviewed the filing and reports that the Contract meets the cost imputation requirements, as specified in the *Special Contract Cost Standard Order* and required under RSA 378:18-b. Staff also reports that special circumstances exist justifying the request for a special contract pursuant to RSA 378:18. The special contract will permit Verizon-NH to respond to competitive pressures, as shown by the evidence presented of actual competition for providing the same services to Genuity.

Nonetheless, in addition to the question of meeting the statutory tests for special contracts, the instant case raises an additional question regarding contracts between affiliates, because Verizon owns just under 10% of the total voting equity in Genuity, and has a right of "contingent conversion" to increase its equity holding up to 95% at any time. By letter dated June 11, 2002, Verizon asserts that Genuity is not currently its affiliate as defined under section 153(1) of the Communications Act of 1934, in that Verizon holds less than a 10% ownership interest and does not control Genuity. Under State law, however, the definition of affiliate is not so limited. An affiliate of a New Hampshire utility includes "[A]ny person with whom a public utility has a management or service contract...not including contracts for personal services with persons not otherwise affiliated." RSA 366:1,II(c). By that definition, we find that Genuity is an affiliate of Verizon. Verizon has a service contract with Genuity to sell Genuity products. Verizon also has indirect control and ownership of Genuity, through its minority interest coupled with the power to obtain a supermajority of shares upon completion of Verizon's efforts to obtain Section 271 permission, and its role as financier of Genuity. RSA 366:1, II(d). That Verizon and Genuity are operating as affiliates is indicated by the preferential relationship Genuity has with Verizon in terms of internet backbone services and voice-over-IP services.

We believe that the public interest standard of RSA 378:18 requires that we take into consideration Verizon's affiliate relationship with Genuity. In so doing, we note that the Contract would provide Genuity with access to services that its competitors must purchase at higher rates through an FCC tariff. We believe that this situation is potentially discriminatory and may adversely affect competition in the New Hampshire ISP market. On the other hand, however, we note that revenues paid by Genuity and other ISPs under the FCC tariff are currently interstate revenues and therefore do not contribute to Verizon-NH's bottom line. Although the revenue generated by the contract with Genuity will benefit Verizon-NH and its New Hampshire customers, that fact alone is not dispositive of whether the contract is in the public interest. Applying the price floor test that we have previously established for special contracts, we find that the discounted prices meet that test. We also find that the special contract would increase the availability of advanced telecommunications service in New Hampshire. And while all of these factors weigh in favor of a positive conclusion about whether the Contract is in the public interest, we cannot make such a finding in light of the potential adverse effect that this particular contract might have on Genuity's competitors.

Accordingly, to address our above-stated concerns, we find that the public interest requires that we grant our approval of the special contract on the following condition: within 14 days of the date of this Order, Verizon-NH must state its intent to file with this Commission an intrastate tariff of general applicability which incorporates the terms and conditions of the Contract within 90 days. We believe that this conditional approval is just and reasonable in that it is fair to Verizon, Genuity and those ISPs who compete with Genuity. It is also consistent with legislative directives that rates charged by utilities should not unduly favor one customer in a particular category over another. *See* RSA 378:11-a I (to ensure fairness, electricity retention rate may be offered to competitors of customers even if the competitors do not qualify for the rate), *see also* RSA 366 (governing affiliate transactions).

Based upon the foregoing, it is hereby

ORDERED, that Verizon's petition for approval of the special contract with Genuity is hereby CONDITIONALLY APPROVED; and it is

FURTHER ORDERED, that Verizon shall notify the Commission, within 14 days, of its intent to file the special contract as a tariff making the DDS, DS3, and IBT services available throughout New Hampshire upon the same terms and conditions.

By order of the Public Utilities Commission of New Hampshire this twenty-first day of June, 2002.

Thomas B. Getz	Susan S. Geiger	Nancy Brockway
Chairman	Commissioner	Commissioner

Attested by:

Debra A. Howland
Executive Director & Secretary