2. The Remedies Offered For Consideration Are Unwarranted And Should Not Be Adopted As Conditions To Approval

Based upon its erroneous view of the wholesale marketplace, Staff proposes a number of remedies for Commission consideration. Because the underlying premise for these remedies – *i.e.*, that wholesale quality will be negatively affected by the merger – is wrong, the proposed remedies should be rejected out of hand. None has any merit in any event.

a. MCI's Service Quality Should Not Be Reported Separately In Carrier-to-Carrier Reporting

Staff notes that "[t]he C2C Guidelines measure performance against an established absolute standard or against parity with performance that Verizon provides to its own retail customers. Whether MCI products will continue to be reported separately or reported in Verizon's retail parity data will impact measurement against remaining CLEC performance data."[177] In light of this, Staff asks whether "MCI's service quality performance [should] be reported separately in carrier-to-carrier reporting."[178]

MCI's data should not be reported separately. After the transaction is completed, all of MCI's regulated subsidiaries will become Verizon affiliates, and to the extent MCI continues to provide services as a separate subsidiary MCI data should not be included in the monthly reports provided pursuant to the Carrier-to-Carrier Guidelines. The metrics in the Guidelines are intended to measure the wholesale services that Verizon provides to its CLEC customers, not the services that Verizon provides to any of its affiliates.

Furthermore, contrary to Staff's contention, MCI's service quality is not reported separately in the monthly C2C reports submitted to the Commission. Rather, MCI's data is part

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[177] White Paper at 55 n.126.

[178] *Id.* at 56.

of the CLEC aggregate data included in the monthly reports. Once the transaction is completed MCI's data will no longer be included with the CLEC aggregate data pursuant to the Guidelines.[179]

In addition, after MCI's data are excluded from the CLEC aggregate, they should not be included, as Staff suggests, with the Verizon retail data that is used to determine parity of service to the CLECs. The level of service that Verizon provides its retail customers and that is currently captured in C2C metrics will continue to provide the Commission with sufficient information on Verizon's wholesale service quality. If, and when, the MCI operations are fully integrated with Verizon's operations, the Commission can review the efficacy of measuring the MCI operations as part of the retail compare groups. As the Commission knows, Verizon and MCI have not done any integration planning and it is therefore, impossible at this time to project how difficult it would be to capture and report MCI performance in the C2C retail compare groups.[180]

b. It Would Be Inappropriate To Require Reporting Of Service Quality Provided Under Commercial Agreements

Staff asks whether "service quality performance [should] be reported to Staff for wholesale products and services purchased by a carrier through commercial agreements."[181] First, this issue is not unique to this transaction and, in fact, is being addressed by the Carrier Working Group (the "CWG") in Case 97-C-0139. The parties' positions in that proceeding will

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[179] *See* C2C Guidelines at 13. (Verizon affiliate reporting is always excluded from the CLEC aggregate for all metrics.)

[180] *See id.* at 14 (Retail Analog Compare Table).

[181] White Paper at 56.

be presented to the Commission at its October session.[182] There is no need or reason to address this industry-wide issue in the context of this bilateral transaction.

Second, any such reporting requirements would be inappropriate since, as discussed, the Commission lacks authority over commercial agreements negotiated outside the Section 252 process. It would also be contrary to the intent of the Commission, which has attempted to foster the development of business-to-business relationships among Verizon and its CLEC customers, and which has encouraged parties to move from reliance on regulation to reliance on commercial agreements.[183] Since all of the agreements are negotiated at arms-length in a commercial setting, the terms and conditions included in them are kept confidential by agreement of the parties. Requiring Verizon to report the services purchased under these agreements would unduly interfere with the process in that it would discourage parties from striking commercial deals that would ultimately have to be disclosed to others who were not parties to either the negotiations or the agreements that emerged from them. Nor could such a requirement be squared with either the Commission's goal of increasing reliance on commercial agreements. Any perceived service issues can and should be resolved through discussions between Verizon and its wholesale customers.

Finally, the service quality that Verizon provides to CLECs under the commercial agreements for the Wholesale Advantage services that replace UNE-P will be captured in the retail metrics (not the C2C metrics) along with Verizon's performance to its resale and retail customers, as it is today. In this way, the Commission (as well as Verizon's customers) will be

[182] In addition, no CLEC in the PAP Annual Review has requested that the Wholesale Advantage lines provided pursuant to commercial agreements be included in any metrics under the PAP.

[183] *See, e.g.*, Letter from William M. Flynn, New York PSC Chairman, to Michael K. Powell, FCC Chairman (Mar. 14, 2004).

able to detect declines in performance, make further inquiry concerning the cause of the declines and take steps to address them.

c. It Would Be Inappropriate To Expand The List Of Collaboratively Developed Wholesale Special Services And High-Cap Metrics

Staff asks if "future commercial and interconnection negotiation processes and resultant agreements [would] benefit from an expanded list of collaboratively developed wholesale special service and high cap metrics to draw from."[184] In fact, future negotiation processes will be impeded by the development of wholesale and high-cap metrics, and enforcement of adequate and nondiscriminatory service performance will not be affected by the transaction. The Commission has no authority to interfere with that process and any attempt to do so would violate federal law prohibiting the states from regulating commercial agreements negotiated outside of Section 252. It would also be contrary to the Commission's expressed intention to remain outside the commercial agreement process. The Commission should not use this transaction as its basis for injecting itself into the process since the transaction will not affect the process in any way.

Interconnection agreements ("ICAs") and commercial agreements are negotiated at arms-length between Verizon and other parties. ICAs are used for services that Verizon is obligated to provide. The ICAs themselves are publicly available documents, and CLECs who have unfettered access to the ICAs can either adopt an existing ICA or negotiate a new one. To facilitate the process, Verizon provides a template ICA as the basis for negotiation. Any attempt by the Commission to add to or supplement that template with a list of wholesale special service

[184] White Paper at 56.

and high-cap metrics would interfere with this process, which has worked well to date and which will not be disrupted by the transaction.

In contrast, commercial agreements are for services that Verizon is not obligated to provide. The terms of these agreements generally are kept confidential between the parties. If the Commission wants to foster the use of these commercial agreements, it should not attempt to develop through some collaborative process an expanded list of metrics for wholesale special services and high-cap loops. Service quality issues between Verizon and its wholesale customers who obtain services from commercial agreements are effectively managed on a business-to-business basis now and they should continue to be managed that way after the transaction is completed. A Commission-mandated template of metrics would unlawfully and unnecessarily interfere with this process.

Additionally, adequate metrics have already been developed in the Special Services Guidelines applicable to special access services and the C2C metrics applicable to unbundled high-cap loops. An expanded list of metrics is not needed since parties can refer to these measures to detect any service quality issues and to pursue them with Verizon. That MCI may have done so in the past, but will no longer do so after the transaction, is no reason to conclude that the metrics will become insufficient once the transaction is completed. Other carriers have the capacity and resources to pursue service-related issues with Verizon (as their active participation in this proceeding makes quite clear). The existing metrics need not be expanded merely because the number of providers that have relied on them is being reduced.

Staff also questions "[h]ow . . . adequate and nondiscriminatory service performance [will] be enforced" after the transaction.[185] It expresses a concern that the transaction might

[185] *Id.*

somehow disrupt continued enforcement of adequate and nondiscriminatory wholesale service performance. That concern is misplaced and provides no reason to adopt new or expanded wholesale service quality metrics. Contrary to Staff's suggestion, the transaction will in no way reduce Verizon's "incentive . . . to address deficiencies in wholesale service quality, specifically for smaller carriers, and in particular carriers now obtaining services through commercial agreements."[186] Intrastate wholesale services provided under state tariff will remain subject to Commission oversight. To the extent interstate services are regulated by the FCC, that agency (and only that agency) can enforce any service quality requirements that might exist at the federal level. This provides more than adequate incentive to maintain high quality service and to address any deficiencies that might arise in the future.

It is simply not true that "[l]osing MCI as a major wholesale competitor for the provision of T-1 circuits may have an effect on the quality of high capacity services provided to retail customers."[187] As discussed, numerous providers are competing to serve customers with the high-capacity services they demand. Even after the transaction, competition for these customers will remain intense and will itself compel Verizon to provide high quality special access service. Imposing even more special access service quality obligations on Verizon than are currently included in the Special Services Guidelines is neither necessary nor appropriate. Special access is a competitive market, and Verizon would simply be ceding that market to its competitors if it could not provide first-rate service.

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[186] *Id.* at 55.

[187] *Id.*

d. There Is No Need To Adopt a Process To Ensure The Integrity Of The Reporting System

Staff asks whether "the Commission need[s] to implement a process to ensure the integrity of the reporting systems for transport and special services."[188] This proposal should be rejected. There is absolutely no evidence that there are any problems with the current reporting systems for transport or special services and there is no reason to believe that the transaction will in any way impair the integrity of reporting. The notion that Verizon and SBC will engage in "collusion" is baseless to begin with and should not be seized upon as a reason to speculate that reporting performance metrics will be tainted after the Verizon/MCI and SBC/AT&T transactions are completed.[189] To the extent that any plausible allegations of mis-reporting are made after the transactions, the Commission has a panoply of regulatory tools at its disposal that it can use to investigate any such allegations. The Commission need not and should not take any action at this time.

IV. THE TRANSACTION DOES NOT RAISE ANY CONSUMER ISSUES THAT REQUIRE COMMISSION ACTION

A. Verizon And MCI Will Take All Necessary And Appropriate Steps To Ensure That Consumers Receive Adequate Notification Of And Information Concerning The Transaction

Staff "tentatively concludes that MCI's residential and small business customers should be properly notified regarding 1) the proposed merger and 2) any potential changes post-merger that will affect telephone service plans or rates."[190] It believes that Petitioners should discuss notification with Staff prior to issuance. Staff seeks "comments on customer notification procedures" and concludes that "no other remedies are warranted." Petitioners agree that

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[188] *Id.* at 56.

[189] *See, e.g., id.* at 34.

[190] *Id.* at 58.

customers (whether residential or business customers) should be advised of the merger and any changes in service plans or rates and will provide such notice when and as appropriate.

At this early stage of the transaction, however, it is premature to advise customers of the transaction. As noted in the Joint Petition, the Agreement does not call for any changes in the rates or terms of service of any New York regulated subsidiary of either Verizon or MCI. As also noted in the Joint Petition, MCI's New York subsidiaries will remain separate from Verizon's New York subsidiary after the transaction is completed. Inasmuch as Petitioners have not begun any post-transaction planning, there are no "post-merger changes" about which to notify customers at this time. Petitioners will develop a communications plan designed to provide customers with adequate notice of any changes that will affect their relationship with the post-transaction company should any changes be made. As in the past, Petitioners will be sure to keep Staff informed of its customer notification activities and will endeavor to address any Staff concerns in that area should any such concerns arise.

B. The Transaction Presents No Financial Issues Or Risks That Require Commission Action

Staff analyzes the transaction's effect on Verizon's New York intrastate return on equity ("ROE") and on Verizon's financial position generally. It seeks comments on a number of tentative conclusions and suggested remedies that are ostensibly designed to "insulate" customers from any possible adverse financial effects from the transaction. Petitioners address these tentative conclusions and remedies in the following sections.

1. Staff Properly Concluded That A Rate Case Is Not Necessary To Consider Synergies

Staff purported to analyze the transaction's effects on Verizon's New York intrastate ROE and tentatively concluded:

> The merger begins to noticeably improve net income in 2007 but it is not until 2009 that the improvement reaches a level where it might have a material impact on Verizon's New York intrastate ROE. As indicated above, Verizon's current New York intrastate ROE is below what it would be in a traditional rate proceeding. Thus, there appears to be no basis, at this time, for the Commission to institute a rate proceeding or require Verizon to pass along the savings to customers as PULP suggests.[191]

Staff seeks comment on this tentative conclusion.

Verizon agrees that it would be inappropriate to commence a rate proceeding to analyze the synergies expected from the transaction and, in particular, to require Verizon to pass them along to customers. Putting aside whether Staff's calculation of the merger's effect on Verizon's New York intrastate ROE is accurate, it is beyond dispute that Verizon is currently *not* earning anything in New York like the kind of "authorized rate of return" that emerged from the lengthy and hotly contested rate cases of the past. It is also true that most of the synergies expected from the transaction are not expected to inure to the benefit of Verizon's operating telephone companies. And any savings that the New York operating company might achieve from the transaction are hardly likely to create an "over earning" situation now or in the future.

Indeed, the rate case concepts of "guaranteed rate of return" and "over earning" are anachronistic in these times in which Verizon is struggling to keep up with competitors that are using new technologies to provide competitively-priced services and that are steadily luring customers away from the public switched telephone network. As Staff is well aware, Verizon must remain competitive with the many cable companies, wireless providers, Internet and broadband services providers and VoIP providers operating throughout the state, all of whom are offering New York residential and business customers of all sizes a wide array of services,

[191] *Id.* at 63.

including voice and data services, using their existing platforms. Under the circumstances, Verizon needs to use any savings that it might gain as a result of the merger to invest in new services and to maintain competitive prices. Market forces will require the merged company to share the benefits of the transaction with customers, and it would be unnecessary and counterproductive for the Commission to interfere with this process and with the merged company's its efforts to remain a viable provider of competitively-priced communications services.

2. The Transaction Will Not Impair Verizon's Ability To Attract Capital And, While A Downgrade Is Not Anticipated, There Would Be No Significant Effect On Cost Of Capital If One Were To Occur

Staff seeks comment on its tentative conclusions that:

> [t]he acquisition of MCI is not expected to impair Verizon's ability to attract the capital necessary to upgrade Verizon's wireline infrastructure in New York. However, Verizon's securities could be downgraded, resulting in higher capital costs for Verizon's New York regulated operations.

These tentative conclusions are technically accurate but present no reason for concern and no basis for taking any action concerning the transaction. It should first be noted that Verizon's operating telephone companies do not go directly to the market to secure debt but borrow instead from their parent company, Verizon Communications Inc. Staff concluded that "[w]ith a market capitalization of approximately $100 billion, it is not expected that the acquisition of MCI will impair Verizon's ability to attract the capital necessary to upgrade Verizon's wireline infrastructure in New York."[192] In fact, Verizon studied whether the transaction would impair the parent company's ability to attract capital and determined that it will not. While certain debt ratings agencies have placed

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[192] *Id.* at 65.

the parent company on credit watch to monitor the transaction's effects on its credit-worthiness, no transaction-related downgrade has occurred to date and none is expected. Yet even if one were to occur, Verizon's analysis indicates that the effect of such a downgrade on Verizon's cost of capital would be insignificant.

3. The Acquisition Is A Reasonable Response To Industry Dynamics

Staff seeks comment on its conclusion that '[f]rom a financial perspective, the acquisition appears to be a reasonable competitive response and strategy to growing intermodal competition."[193] Petitioners agree with that conclusion and the industry developments discussed above explain why Verizon's decision to acquire MCI makes good business and economic sense. The transaction responds to the continuing evolution of the industry as driven by customer demand and by changing technology. The industry is rapidly restructuring to deal with the reality of intermodal competition and convergence. As a recent report starkly observed, traditional landline carriers face major challenges: "The underlying business model for landline telephony has formally ceased to exist and the stock markets no longer have faith in this sector."[194] Moody's recently cut the debt ratings on certain divisions of Verizon Communications, including New York, stating that "inroads made by rivals will cause the division's operating performance to deteriorate faster than anticipated."[195] The competitive need for firms to offer products and services that respond to telecommunications convergence is

[193] *Id.* at 69.

[194] PR Leap, Probe Group Releases First Schnee-Tumollilo Report: The End Of The Landline Business, Can Service Providers Adapt? (Apr. 21, 2004).

[195] http://www.newyorkbusiness.com/news/cms?id=10732&print=1.

further supported by Gartner Research, which found that "operators that fail to recognize this need [for unified services] will struggle to stay relevant in the market."[196]

For its part, Verizon is responding to the changing competitive landscape by accelerating its expansion into broadband and wireless services. The planned transaction with MCI will facilitate Verizon's ability to complete those plans. MCI's facilities and customer base will complement Verizon's continuing transformation into a premier wireless and broadband provider. The combination of Verizon's fiber deployment with MCI's IP backbone and IP applications will enable the development of an advanced broadband platform, one that is capable of delivering next-generation communication services to a wide range of customers. From the perspective of MCI's existing enterprise customers, the transaction adds a widespread local network and the ability to obtain wireless services and wireline services from a single source. Thus, the combined company will be able to provide one-stop shopping for consumer, small business, and enterprise customers.

The proposed transaction will enable the new firm to meet the challenges of convergence and changing industry dynamics far better than each could on its own. The post-transaction entity will be a stronger competitor that is able to meet customers' new expectations for services and pricing, and to better match the offerings of the cable companies and their suite of advanced services. In short, the post-transaction company will be better positioned to develop and to offer innovative services, providing valuable benefits to customers without harming competition.

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[196] Gartner Media Relations, *Gartner Says Three Major Shifts to Transform Fixed Telecommunications Operator Business in Europe* (Nov. 3, 2004), http://www4.gartner.com/5_about/press_releases/asset_113416_11.jsp, accessed December 6, 2004.

4. The Finance-Related Remedies Offered For Consideration Are Unnecessary Or Inappropriate And Should Not Be Adopted As Conditions To Approval

a. It Would Be Inappropriate To Insulate Customers From Transaction Costs If Doing So Would Violate GAAP

Staff suggests that "Verizon's New York utility customers should be insulated from costs that result from the merger, including the amortization expenses resulting from the write-up of intangible assets recorded as a result of the transaction, and any charges to earnings from the write-off of goodwill recorded by Verizon as a result of the acquisition."[197] In considering this suggestion, it must be noted that Verizon New York is obligated to prepare its financial statements in accordance with Generally Accepted Accounting Principles ("GAAP"). To the extent that GAAP requires cost allocations of the sort at issue here, it would be inappropriate to depart from GAAP and other requirements merely to serve Staff's narrow interest in "insulating" utility customers from costs that Staff personally believes those customers should not have to bear.

b. Consideration Of Additional Equity In Derivation Of Verizon New York's Intrastate ROE

Staff seeks comment on its conclusion that "[n]one of the additional equity resulting from the transaction under the purchase method of accounting should be considered in derivation of Verizon's New York intrastate ROE."[198] Given the way the transaction is structured, GAAP provides that any additional equity that might result from the transaction under the purchase method of accounting will not be considered in derivation of Verizon's New York intrastate ROE. There is no need for concern or action here.

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[197] White Paper at 69.

[198] *Id.*

c. There Is No Need To Take Steps To Ensure That Verizon New York's Intrastate Operations Are Not Impacted As A Result Of MCI Accounting Improprieties

Staff suggests that the "Commission should condition its approval of the transaction on requiring that Verizon take steps to ensure that Verizon's New York intrastate operations are not impacted as a result of any MCI accounting or other improprieties."[199] Verizon records each affiliate's taxes, litigation costs (including settlements and judgments), and liabilities separately. After the transaction is completed, Verizon New York and MCI will remain separate subsidiaries. Accordingly, in the unlikely event that past MCI accounting improprieties give rise to any future financial obligations, Verizon New York should not be impacted by such an occurrence.

V. THE COMMISSION HAS NO AUTHORITY TO DISAPPROVE THE PROPOSED TRANSACTION OR TO IMPOSE CONDITIONS ON IT

Quite apart from the fact that the White Paper provides no factual basis to adopt remedies (or conditions on approval), the Commission should not interfere with the proposed merger because it lacks authority to disapprove or to impose conditions on it. As explained in the Joint Petition, the Agreement and Plan of Merger Between Verizon and MCI (the "Agreement") does not involve any of the transactions covered by Public Service Law ("PSL") §§ 99(2) or 100. Thus, the Commission should refrain from adopting the remedies set forth in the White Paper because such action would constitute an unauthorized exercise of authority in contravention of the PSL.

Staff "concludes that jurisdiction to investigate and approve or deny the proposed transaction of MCI by Verizon is vested in the Commission by the statutory authority conferred

[199] *Id.*

pursuant to [] Sections 99 and 100."[200] That conclusion is fundamentally unsound. It cannot be squared with the plain language of these provisions, or the construction placed on those provisions by seven decades of Commission and judicial decisions. The Commission's recent and abrupt "reconstruction" of these jurisdictional provisions – without any intervening change in their language – cannot support Staff's position.

A. The Plain Text Of §§ 99 And 100 Demonstrates That This Transaction Is Not Subject To Commission Jurisdiction And Fails To Support Staff's Contrary Conclusion

Section 99(2) gives the Commission authority to approve (i) the "assignment, transfer [or] lease" of a "franchise or right to or under any franchise;" (ii) "any contract or agreement made with reference to or affecting any such franchise or right;" (iii) the "transfer or lease" by a "telephone corporation" of its "works or system or any part of such works or system" or any contract "for the operation of its works or system." The Agreement involves none of the transactions contemplated by this section. As a parent company stock transaction, it does not provide for the assignment, transfer or lease of franchises to own or operate telephone lines within New York. Nor was the Agreement "made with reference to or affecting" any such franchises – indeed New York franchises are not even mentioned in the document. MCI, a Delaware holding company, is not a "telephone corporation" within the meaning of PSL § 2(17); it does not "own, operate, or manage any telephone line in New York State." Nor is MCI transferring any works or systems under the Agreement. Rather, the transaction only involves the acquisition of MCI's capital stock by a subsidiary of Verizon, another Delaware holding company.

[200] *Id.* at 12.

Staff asserts that § 99(2) grants the Commission jurisdiction to approve the proposed transaction arguing that "[c]ontrol of the MCI subsidiaries' franchises and assets will pass from MCI to Verizon, a different corporation," and "this transfer of control will affect how the MCI subsidiaries operate as telephone corporations in New York State."[201] Thus, Staff's jurisdictional theory is that the single word "affect" in § 99(2) provides the Commission with jurisdiction over holding company transactions involving the "indirect" transfer of control over a subsidiary. But Staff's effort to shoehorn the transaction into § 99(2) is unavailing. By its explicit terms that section applies only to contracts that "refer to or affect" a "*franchise* to own or operate a telephone line in the state," not to those that "affect how a subsidiary operates" after transfer of ownership of a holding company. A "franchise" is not a "subsidiary" and it is not a telephone corporation" (a term which is defined in PSL § 2(17)). While the PSL does not define "franchise," a franchise is an *asset* belonging to a "telephone corporation," or more specifically, the telephone corporation's right "to own and operate a telephone line in the state."[202] Staff is improperly reading the term "franchise" to mean a "telephone corporation" subsidiary. Yet even if "franchise" meant telephone corporation or, to use Staff's term, a "subsidiary," this transaction does not directly affect the subsidiary telephone corporations. Staff is improperly attempting to impute indirect jurisdiction into the text of the statute.

Staff makes the same error when it concludes that the transaction is subject to Commission approval under PSL § 100. By its very terms, § 100 confers jurisdiction only over transactions involving the "capital stock" of a "telephone corporation organized or existing under or by virtue of the laws of this state." MCI, whose stock is being acquired, is not a "telephone

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[201] *Id.* at 10-11.

[202] Black's Law Dictionary, Revised Eighth Edition, defines "franchise" as "the right conferred by the government to engage in specific business or to exercise corporate powers."

corporation" within the meaning of PSL § 2(17); it does not own operate or manage any telephone line in the state and is not "organized or existing under" New York law. Staff contends that "transfer of control [of MCI stock to Verizon] will affect how the MCI subsidiaries operate as telephone corporations in New York State."[203] But Section 100 does not even employ the term "affect," and it makes no reference to transfers of control of stock that might "affect how [regulated] subsidiaries operate as telephone corporations in New York State." Nor does it suggest that approval is required where a transaction might have such an incidental effect. Nor does Section 100 require approval for the "indirect" transfer of control over a telephone corporation's stock.

Staff's interpretations of both §§ 99(2) and 100 are not supported by the plain language of those provisions or by long standing rules of statutory construction. It is long settled that the "[j]urisdiction of the Public Service Commission cannot be conferred by implication, but must be given by language which admits of no other reasonable construction." *City of New York v. Maltbie*, 274 N.Y 90, 98 (1937) (citing *Siler v. Louisville & Nashville R. R. Co.*, 213 U.S. 175 (1909)).[204] The Legislature has used the term ***"directly or indirectly"*** in the Public Service Law where it intended to confer pass-through or similarly broad jurisdiction over an entity and its affiliates. The absence of the term "indirectly" in §§ 99 and 100 indicates that the Legislature did not confer jurisdiction over indirect transfers of control. If the Legislature intended for the Commission to exercise jurisdiction over holding companies in this context, it could and would

[203] White Paper at 10-11.

[204] *See also New York Telephone Co. v. Public Service Comm'n of State of N.Y.*, 684 N.Y.S.2d 829 (N.Y.Sup. Ct. 1998) ("[Public Service Commission] possesses only those powers expressly delegated to it by the Legislature, or incidental to its expressed powers, together with those required by necessary implication to enable it to fulfill its statutory mandate."); *Brooklyn Union Gas Co. v. Public Service Comm'n*, 478 N.Y.S.2d 78 (N.Y. App. Div. 1984) ("Public service commission has only those powers conferred upon it by the legislature and such other powers as are incidental thereto or necessarily implied therefrom.").

have included the phrase "directly or indirectly" in the text of §§ 99 or 100, just as it did in neighboring provisions.[205] It did not, and Staff's attempt to read the term "indirect" into the statutory language of PSL § 99(2) or § 100 is not permitted under common law and statutory rules of construction.[206]

Staff's sweeping interpretation of §§ 99(2) and 100 is also inconsistent with the explicit grants of authority over holding companies in other provisions of the Public Service Laws. For example, § 110 was added in response to concern over the state's lack of regulatory authority over holding companies that owned public utilities. However, § 110 does not create jurisdiction over transactions *between two holding companies.* For example, PSL § 110(1) grants jurisdiction over the holding companies of regulated "public utility companies" only "to the extent as may be necessary to enable the commission to require the disclosure of the identity in respective interests of every owner of any substantial interest in such voting capital stocks." And PSL § 110(3) requires the filing of "management, construction, engineering, or similar contracts *between public utilities and their affiliates.*" These limited grants of jurisdiction sharply conflict with the broad jurisdictional authority over holding companies that the Staff attempts to conjure out of §§ 99(2) and 100.

Staff's interpretation also conflicts with the legislative history of §§ 99(2) and 100. In the late 1920s, states had significant concerns about their authority over out-of-state companies that held controlling interests in state utilities. At the federal level, the Public Utility Holding

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[205] *See, e.g.*, PSL §§ 92, 106.

[206] Staff's construction violates the longstanding principle of statutory construction "*expressio unius est exclusio alteriu.*" That principle is codified in N.Y. Stat. § 240 (McKinney 2005), which provides "where a law expressly describes a particular act, thing or person to which it shall apply, an irrefutable inference must be drawn that what is omitted or not included was intended to be omitted or excluded." When the legislature intended to refer to "indirect" ownership, it did so expressly. It did not do so in § 99 or § 100, and there is no basis for reading the term into either provision.

Company Act was enacted to give the Securities and Exchange Commission jurisdiction over transactions involving holding companies that held electric and gas utilities.[207] PUHCA did not apply to telephone utilities, however.[208] New York State responded to these and other concerns by creating the 1929 Knight Commission to investigate possible revisions of the PSL.

The Knight Commission explicitly addressed the issues surrounding holding companies in its investigation and legislative recommendations.[209] In legislative hearings, the Knight Commission directly asked two Public Service Commissioners and the Public Service Commission Chief Accountant whether the PSC had jurisdiction under then-current law to approve a merger precisely like the merger of Verizon and MCI involving holding companies that own regulated operating companies. All three explicitly stated that the Commission did ***not*** have jurisdiction over such transactions and cited multiple cases in which the Commission had expressly so held.[210] In particular, one of the testifying Commissioners noted that ***the Commission did not have control over sales of stock from one holding company to another:***

> Q: Do you believe that the provisions of Section 70 and [Section 100, which is the] corresponding section related to telephone and telegraph companies, etc. are applicable to holding companies that seek to acquire control of other holding companies?

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[207] Public Utility Holding Company Act of 1935, 15 U.S.C. §§ 79 *et seq.* (the "PUHCA").

[208] *See id.* § 79(b) (defining "[p]ublic-utility company" as "an electric utility company or a gas utility company").

[209] The Knight Commission's Report concluded that "[h]olding companies and affiliated service agencies have acquired pre-eminent importance in their bearing on the regulation of public utility companies in New York State," estimating that "98.5 per cent of all of the electric power sold in New York State during 1928 was distributed by holding company groups." Knight Commission Report, Vol. 1., at 27. Concerns focused, in particular, on the potential for holding companies to provide a means of circumventing regulatory controls on utility companies. "The domination of operating companies by holding companies may in some instances be so complete that the holding company is actually engaged in public utility operation, in which case it should be subject to regulation as a public utility corporation." *Id.* The Report indicates a particular concern regarding the financial practices of holding companies, because "[t]he interests both of consumers and of investors may be abused by the adoption of unsound financial practices by holding companies. We recognize and desire to emphasize particularly these dangers." *Id.*

[210] *See, e.g.*, *Mohawk Hudson*, Case No. 3192, reversing Initial Order for Mohawk Hudson, Case No. 2649; *Buffalo, Niagara & Eastern Power Corp.*, Case No. 2621; *Central Empire Power Company*, Case No. 5018.

A: No, because these sections apply only to ***operating utilities***.[211]

When asked about a particular transaction that came to the Commission's attention in *Central Empire Power Company*, that same Commissioner replied, "as I remember that case, these small companies were operating companies, where the stock was acquired by a holding company of all of these companies. Then this holding company sold to another holding company, and if that is the situation, ***I don't think that we had any control over the selling of the stock from one holding company to the other***."[212] Further, the Commissioner was asked:

> Q: In the case of a company, a foreign corporation operating in the State, and of course other states, how would you provide . . . for any control over such companies?
>
> A: We have control over the operating company, no matter who owns it, in the first instance, but ***that corporation, I think, could transfer its stock to some other corporation outside the State without our consent***.[213]

Significantly, the Commissioners urged the Legislature to amend the Public Service Law so that the Commission would have authority to approve or disapprove acquisitions of holding companies by holding companies. The Knight Commission issued a Report that included recommendations for amendments to the PSL. While those recommendations led to changes to the PSL that, *inter alia*, expanded Commission authority over out-of-state holding companies,[214] these amendments and expansions ***did not*** result in Commission jurisdiction over stock transactions between holding companies. Specifically, the Legislature did not amend PSL §§ 99 or 100 and did not adopt ***any*** statutory amendments that could justify the Commission's assertion

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[211] Knight Comm'n Pub. Hr'g Tr., Vol. II, at 614 (emphasis added).

[212] *Id.* at 614 (emphasis added).

[213] *Id.* at 615 (emphasis added). *See also id.* at 1552 ("Q. ... Has the Commission any jurisdiction over security issues of holding companies? A. It has not. Q. Or the acquisition of property or securities from holding companies? A. It has only to the limited extent where the operating company would desire to issue securities against the property acquired from the holding corporation. Q. Has it jurisdiction over the acquisition of stockholding companies? A. It has not. Q. Or the reorganization of holding companies? A. It has not.").

[214] *See, e.g.*, PSL § 106 (added in 1933); *id.* § 110 (added in 1930).

of jurisdiction over holding company mergers. It did, however, adopt a new PSL § 110, which, as discussed, gives the Commission jurisdiction over certain contracts between holding companies and regulated entities but which does not confer jurisdiction over transactions between holding companies themselves.[215] That the Legislature expanded the Commission's authority over holding companies in some respects but refused to expand the Commission's authority to approve mergers between holding companies demonstrates the Legislature's clear intention to deny the Commission jurisdiction over mergers such as this one. It also completely defeats Staff's conclusion that §§ 99 and 100 confer jurisdiction over this transaction.

The Commission recognized the limits of its authority over holding company transactions not merely in hearings before the Knight Commission but also in its review of transactions that came before it. Thus, in *Rochester Telephone*, the Commission denied a petition by Rochester Telephone, a regulated New York telephone company, to reorganize by establishing a holding company structure for diversification purposes.[216] In its brief to the Commission in that proceeding, Staff opposed Rochester's petition, noting that the relevant Public Service Law provisions do not confer on the Commission jurisdiction over acquisitions of holding companies and stating that "if the reorganization is permitted, Rotelcom [the new holding company] could acquire a non-utility firm without any regulatory approval."[217] The Commission adopted Staff's recommendation and specifically cited its concern that it might lose regulatory oversight of the utility if it were owned by a holding company over which the Commission had no jurisdiction. When applied to the instant transaction, both Staff's and the Commission's reasoning in

[215] *See* PSL § 110(3); *see also id.* § 106 (requiring Commission approval for any loans from a public utility to a corporation "owning or holding, directly or indirectly, any stock of said public utility").

[216] *See* Case 27015, *Rochester Tel. Corp.*, 18 NY PSC 271 (1978), at 1, 4-5.

[217] *See* Case 27015, Staff's Brief on Exceptions, at 6.

Rochester Telephone means that Verizon, a holding company, "could acquire [MCI,] a non-utility firm[,] without any regulatory approval."[218]

In its 1989 decision in *McCaw/LIN*, the Commission once again acknowledged its lack of jurisdiction over the merger of two holding companies. In concluding that it lacked jurisdiction over AT&T's acquisition of McCaw, a holding company, the Commission observed that a contrary ruling would mean that "every corporate parent of a telephone corporation would become subject to [the Commission's] authority."[219] The Commission did not attempt to assert jurisdiction over that transaction precisely because it recognized that such an attempt would extend the Commission's authority well beyond its statutory limits.

In sum, the plain language of §§ 99(2) and 100, the legislative history that underlies those sections and other sections that address holding companies, as well as the Commission's longstanding recognition of the limits §§ 99(2) and 100 imposed on its authority over holding company transactions inexorably lead to the conclusion that the Commission lacks jurisdiction to review and approve the instant transaction.

B. The Commission's Most Recent Applications Of PSL §§ 99 And 100 Arbitrarily Depart From More Than Seventy Years Of Commission Precedent Recognizing The Commission's Lack Of Authority Under Those Sections

Although Staff attempts to stretch the statutory language of §§ 99(2) and 100 to cover the structure of the Verizon/MCI transaction, Staff primarily relies on the Commission's prior

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[218] Staff claims that *Rochester Telephone* did not address the Commission's jurisdiction over the proposed transaction. According to Staff, the decision merely prohibited Rochester Telephone from reorganizing as a holding company "because of the difficulty of ensuring that customers would not be harmed by improper affiliate transactions." White Paper at 12. Staff's reasoning is specious. It ignores the fact that the very reason the Commission would have had difficulty protecting consumers from "improper affiliate transactions" if it approved a holding company structure is because, as the Commission acknowledged in the decision, it had no jurisdiction over transactions between two non-utility holding companies. *See Rochester Tel. Corp.*, at 3-4 (observing that the Commission "could [not] prevent the holding company from being acquired" by other interests).

[219] Case 89-C-116, Order Granting Petition (Oct. 25, 1989).

assertion of jurisdiction over the Bell Atlantic/NYNEX transaction as support for similar assertion of jurisdiction in this instance. The *Bell Atlantic/NYNEX* decision, however, was based on an erroneous interpretation of the PSL and provides no legal basis for asserting jurisdiction here.

The Commission's exercise of jurisdiction over holding company transactions is a baseless and arbitrary reversal of the decades-old position it articulated in *Rochester Telephone* and *McCaw*. In *AT&T/Ridge Merger Corporation*,[220] the Commission overruled *McCaw* and, without explanation, created a presumption of Commission jurisdiction: "[a]bsent proof that transfer of the stock of a holding company that indirectly has a controlling interest in a New York telephone corporation does not effectively constitute a transfer of an interest in such a telephone corporation, we will assert jurisdiction over the transaction under Section 100." The Commission's unexplained (and inexplicable) departure from *Rochester Telephone* and *McCaw* is arbitrary and capricious and cannot stand for that reason alone.[221] Certainly the Commission's expanded view of its authority over holding companies occurred without any intervening changes in the statutes governing the Commission's jurisdiction. Thus, the *AT&T* decision stands as an improper attempt to re-write the PSL in clear contravention of plain statutory language, legislative history and Commission precedent. That decision and the attempt in the *Bell Atlantic/NYNEX* decision to create jurisdiction over a parent based on jurisdiction over its

[220] Case 93-C-0777, Order Asserting Jurisdiction and Approving Transaction (Dec. 31, 1993).

[221] *See, e.g.*, *New York Tel. Co. v. PSC*, 62 N.Y.2d 57, 61-62, 476 N.Y.S.2d 60, 62 (1984); *MCI Telecommunications Corp. v. PSC*, 108 A.D.2d 289, 298, 488 N.Y.S.2d 840, 847 (3d Dep't), *appeal discontinued and withdrawn*, 66 N.Y.2d 760, 497 N.Y.S.2d 1033 (1985); *New York Tel. Co. v. PSC*, 64 A.D.2d 232, 245-46, 410 N.Y.S.2d 124, 132 (3d Dep't 1978), *leave to appeal denied*, 46 N.Y.2d 710, 414 N.Y.S.2d 1028 (1979).

regulated subsidiary and such efforts to manufacture jurisdiction have been squarely rejected by the New York state courts.[222]

Although the Commission has exercised jurisdiction over several holding company mergers since *McCaw*, it nonetheless approved those mergers and, in doing so, evidently removed any incentive for the petitioner-holding companies to challenge its jurisdictional rulings. In the case of the *Bell Atlantic/NYNEX* transaction, the Commission expressly sought the holding companies' consent to conditions that the Commission sought to impose, thereby implicitly conceding that it could not impose those conditions unless the petitioners relented in their opposition to the Commission's assertion of jurisdiction over the transaction. In nearly all such cases, the Commission has given little or no explanation supporting its jurisdictional argument, other than the blanket statement that it has previously asserted jurisdiction in similar cases. Similarly, in its White Paper, Staff dismisses Verizon's and MCI's jurisdictional challenge with no explanation other than a comparison to the equally flawed *Bell Atlantic/NYNEX* ruling.[223] Indeed, Staff fails to even acknowledge that the current position is both a contradiction of Staff's more reasoned examination of §§ 99(2) and 100 in *Rochester Telephone* and a reversal of over 70 years of Commission and state precedent. The White Paper thus reflects an arbitrary and capricious proposal to once again depart from the clear language of §§ 99(2) and 100 and to take an expansive view of jurisdiction that is fundamentally at odds with well-reasoned and longstanding precedent and legislative history.

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[222] *See N.Y. Tel. Co. v. Pub. Serv. Comm'n of N.Y.*, 258 A.D.2d 234, 236-37 (3d Dep't 1999) (rejecting § 99 jurisdiction over sale of interest in research organization created by telephone local carriers), *reversed on other grounds*, *N.Y. Tel. Co. v. Pub. Serv. Comm'n of N.Y.*, 95 N.Y.2d 40 (2000); *Matter of Brooklyn Union Gas Co. v. Pub. Serv. Comm'n of N.Y.*, 34 A.D.2d 71, 73 (3d Dep't 1970) (rejecting pass-through jurisdiction over a New Jersey affiliate of a New York utility company).

[223] *See* White Paper at 10-11.

Petitioners do not challenge the Commission's jurisdiction over Verizon's and MCI's regulated New York subsidiaries. Indeed, it is precisely because the Commission maintains regulatory oversight of those subsidiaries' rates terms and conditions of service that it need not assert jurisdiction over the parent companies. However, Staff would have the Commission obliterate the legal and factual distinctions between a parent entity and a subsidiary, just as Staff would have the Commission ignore the distinction between "directly" owned and "indirectly" owned. The assertion of jurisdiction over this transaction is, quite simply, contrary to law. The Commission recognized this for decades before abruptly reversing course in *AT&T*. Petitioners respectfully submit that the decades-old position that preceded *AT&T*, grounded in the plain language of the PSL and supported by legislative history is the correct one and should once again be embraced by the Commission.

C. Any Attempt To Impose Conditions On The Commission's Approval Of The Merger Would Violate The Federal Constitution

Even if the Public Service Law could be construed to authorize the Commission to review and approve the transaction, any attempt to attach conditions to such an approval would be inconsistent with the dormant Commerce Clause of United States Constitution. Simply stated, a state cannot impose burdensome conditions on this transaction which serve only to benefit the narrow interests of a single state to the detriment of the Petitioners' right to engage in interstate commerce. Yet that is precisely what Staff urges be done, here, as even Staff admits.[224]

[224] "Staff recognizes that the mergers impact not only New York state telecommunications markets, but national markets as well, and that certain market concerns/considerations may be more appropriately addressed at the federal level (by the FCC or the Department of Justice). However, this paper analyzes the impacts of the mergers on New York State telecommunications markets specifically, and the tentative conclusions and remedies that are put forth in this document are aimed at impacts on New York's consumers." White Paper at 5.