

PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

**Communications Division
Carrier Oversight & Programs**

**RESOLUTION T-17344
October 6, 2011**

RESOLUTION

RESOLUTION T-17344. Disposition of Protest of Straitshot RC, LLC for U.S. TelePacific (U-5721-C) Advice Letter No. 314, Filed May 6, 2011.

SUMMARY

This Resolution suspends the Written Disposition of the Communications Division regarding U.S. TelePacific Advice Letter 314, and directs the parties to the proposed acquisition of IXC Holdings, Inc. by TelePacific's subsidiary, TelePacific Managed Services to file an application seeking Commission approval of the proposed acquisition of assets

BACKGROUND

U.S. TelePacific (TelePacific) filed Tier III Advice Letter (AL) 314 on May 6, 2011, pursuant to General Order (G.O.) 96-B, Decisions (D.) 04-10-038, D.97-06-096, and D.94-05-051, to notify the Commission of its proposed acquisition of the assets, including the customer base, Certificate of Public Convenience and Necessity ("CPCN") of IXC Holdings, Inc. (U-6647-C) ("IXCH, Inc.") by TelePacific's wholly-owned subsidiary, TelePacific Managed Services ("TMS").

On May 27, 2011, Straitshot RC LLC and Straitshot Communications, Inc. (collectively, "Straitshot"), submitted a timely protest to AL 314. The protest was filed pursuant to G.O. 96-B General Rule 7.4.2. (3), alleging that TelePacific failed to disclose in Advice Letter 314 pending litigation in the United States District Court for the Western District of Washington in Washington State (hereafter referred to as the Washington District Court). According to Straitshot, the alleged failure to reveal the pending litigation represents a material error or omission in the Advice Letter. Straitshot alleges a series of unlawful schemes agreed to and perpetuated by IXCH, Telekenex, Inc. (Telekenex), IXCH/Telekenex officers and controlling owners Brandon Chaney and Anthony Zabit, and other individual defendants (collectively, the "IXCH/Telekenex defendants") for the purposes of the following: 1) stealing Straitshot's trade secrets and confidential

customer information, 2) making a series of misrepresentations to Straitshot's customers, and 3) using the stolen trade secrets and confidential customer information to destroy Straitshot's business and coerce its customers into long-term contracts that favored IXCH/Telekenex. Straitshot is seeking damages in the amount of \$17.5 million, which is the alleged value of the Straitshot enterprise destroyed by IXCH/Telekenex.

The original litigation was between Straitshot and Telekenex until Straitshot discovered that in August 2010, the assets of Telekenex had been moved to another corporate entity, IXCH, which is owned by, and under the control of Brandon Chaney and Anthony Zabit. Pursuant to a request from Straitshot, on December 8, 2010, the Washington District Court allowed Straitshot to add IXCH as a party to the litigation. Telekenex had notified the Commission of this transfer in Advice Letter 71, dated June 3, 2010. Straitshot maintains that through this transfer of assets, the Telekenex defendants Brandon Chaney and Anthony Zabit attempted to leave the liabilities of Telekenex, including the \$17.5M lawsuit, in the essentially insolvent company, Telekenex.

Straitshot maintains that granting the proposed transfer of assets from IXCH, Inc. to TelePacific would have the following effects: 1) potentially eliminate Straitshot's ability to collect a judgment should it prevail in the afore-mentioned litigation, and 2) be unjust and unreasonable.

Straitshot further maintains that TelePacific's failure to disclose in AL 314 the pending litigation in Washington state constitutes an error and omission under G.O. 96-B §7.4.2(3) and is grounds for protest.

Straitshot requests that the Commission both 1) not permit AL 314 to become effective, and 2) disapprove the Proposed Transfer, or in the alternative approve the Proposed Transfer only the express condition that TelePacific assume full financial responsibility for paying Straitshot any and all judgments and other relief awarded to Straitshot in the Litigation between Straitshot and IXCH in Washington State. In addition, Straitshot asks that, at the very least before granting permission or approval in response to AL 314 and the Proposed Transfer, the Commission should fully investigate and conduct an evidentiary hearing regarding the IXCH/Telekenex Defendants' failure to disclose the Litigation to the Commission, their misrepresentations to consumers, and the unjust and unreasonable effects that the Proposed Transfer could cause.

On June 3, 2011, TelePacific responded to Straitshot's protest recommending that the Commission disregard the protest because it does not raise issues that the Commission can or should address. Specifically, TelePacific maintains that Telekenex is not a party to the transaction. The Commission approved the transfer of Telekenex assets to IXCH over a year ago, TelePacific notes, and Telekenex is no longer a certificated utility under the Commission's jurisdiction. TelePacific also offers the following arguments:

- 1) the courts in Washington state provide the appropriate venue for Straitshot to resolve its complaints against Telekenex;
- 2) the addition of IXCH to the Washington State litigation does not adversely affect the public interest in carrying out the proposed transfer;
- 3) approving the transaction will be of benefit to Straitshot because IXCH will receive compensation from the transaction which may put Straitshot in a better position to collect any judgment awarded by the Washington Court;
- 4) omitting reference to the Washington District Court litigation was not a deviation from the Commission's rules with respect to providing information relevant to TelePacific's acquiring IXCH's assets and customers because D.04-10-038 does not provide clear guidance on the scope of litigation to be disclosed; and
- 5) allegations about complaints filed against the IXCH/Telekenex defendants are without merit. To the best of TelePacific's knowledge, the companies referenced in the Straitshot's response to AL 314 are cases concerning Telekenex, Inc. and were filed prior to IXCH acquiring the assets and customers of Telekenex. As such, TelePacific asserts, the Commission's rules do not require TelePacific and TMS to disclose such actions.

On July 15, 2011, pursuant to G.O. 96-B §7.6.1, the Communications Division (CD) issued a Written Disposition of the protest of Straitshot informing Straitshot of the approval of AL 314 and that AL 314 was deemed effective pursuant to Decision (D.) 04-10-038, Appendix A, Paragraph 1 and 2.

On July 22, 2011, Straitshot made a timely request for Commission review of the July 15, 2011 CD Written Disposition of its protest pursuant to G.O. 96-B General Rule 7.7.1. Straitshot alleged that CD's disposition of AL 314 is "unlawful and erroneous," and "will harm consumers and the public interest." Straitshot maintains that the Written Disposition deprived them of due process because the disposition did not state the basis for rejecting the protest, and that it does not discuss or evaluate the substance of the protest. Straitshot argues that the Commission should review and reverse CD's disposition of AL 314. Straitshot maintains that the IXCH/Telekenex Defendants, including 122 Telekenex employees and one of the principal owners, Brandon Chaney, intend to continue their involvement if the transfer goes forward. Straitshot further alleges that the continued involvement by IXCH/Telekenex Defendants will perpetuate IXCH's improper practices, such as fraud against Straitshot and other customers.

On July 29, 2011, TelePacific responded to Straitshot's request for Commission review of the CD Written Disposition of AL 314. TelePacific countered that a) D.04-10-038 governs the type of acquisition and/or transfer transaction before the Commission, and G.O. 96-B rules to the contrary are inapplicable, b) CD correctly approved the AL, based on the framework in D.04-10-038, governing acquisitions, and c) Straitshot's request was improper because D.04-10-038 does not provide for a Resolution Request. TelePacific claims that G.O. 96 – B General Rule 7.7.1 does not apply to Advice Letter 314, but if it were to apply, the Commission can, and should, grant an exception to the rule pursuant to G.O. 96-B General Rule 1.3.

DISCUSSION

Under the Advice Letter process adopted in G.O. 96-B, an Advice Letter is subject to disposition by the reviewing Industry Division whenever such disposition would be a “ministerial” act even through the subject matter is technically complex, so long as a technically-qualified person could determine objectively whether the proposed action has been authorized by the statutes or Commission orders cited in the advice letter. Whenever such determination requires more than ministerial action, the disposition of the advice letter on the merits will be by Commission resolution, as provided in General Rule 7.6.2.¹

CD reevaluated the proposed transaction using the criteria adopted for transfers and acquisitions for Nondominant Interexchange Carriers (NDIECs) and Competitive Local Exchange Carriers (CLECs) in D.04-10-038. Decision 04-10-038 expands the scope of the advice letter process to allow CLECs to use ALs to seek prospective authority to transfer control or assets of non-controversial transactions subject to Public Utilities Code §§ 851 through 854, and in Appendix A, sets forth specific criteria that the requesting party must meet. Appendix A condition 1.a (3) requires that the Advice Letter “identify any decided or pending legal complaints against the involved entities, in California or other states.”²

IXCH is a certificated CLEC in California, and acquired Telekenex in August 2010. IXCH is currently doing business in California under the dba Telekenex. We understand that on December 8, 2010, IXCH was added as a defendant to Straitshot's suit against Telekenex before the Washington District Court. Accordingly, IXCH is a party to the Washington State litigation and is one of the entities involved in the transfer of assets. For these reasons, TelePacific should have disclosed in AL 314 the pending litigation in Washington State against IXCH and Telekenex.

¹ G.O. 96-B § 7.6.1

² D.04-10-038, App. A.

TelePacific contends that omitting reference to the Washington State litigation was not a deviation from the Commission's rules with respect to providing information relevant to TelePacific acquiring IXCH's assets and customers because D.04-10-038 does not provide clear guidance on the scope of litigation to be disclosed. We find TelePacific's contention unpersuasive. The Washington State litigation alleged bad behavior by one of the parties to the proposed transaction, and one of the principals in the selling entity will remain a principal in the continuing entity. More specifically, the litigation alleges that a predecessor to IXHC, while controlled by two principals, one of whom will be a principal in the acquiring entity in the currently proposed transaction, engaged in unlawful behavior to steal customers from Straitshot. Notwithstanding silence in D.04-10-038 regarding the specific type of litigation that must be reported, it should be readily apparent that this Commission would be interested in the particular litigation ongoing in the Washington District Court. Accordingly, CD now believes that TelePacific should have disclosed the existence of the Washington State litigation to the Commission, and that this omission is material.

Furthermore, CD now believes that the matter is not appropriate for the Advice Letter process. The issues Straitshot has raised and which arise from the omitted litigation (impact on Straitshot's ability to collect on any judgment it might obtain, and alleged bad behavior by one of the principals) demonstrate that disposition of AL 314 would be more than a ministerial matter. Under GO 96-B, General Rule 7.6.1, Industry Division Staff is only authorized to dispose of an advice letter where that disposition would be a "ministerial" act.

For these reasons, the Commission concludes that CD's July 15, 2011 written disposition of AL 314 in response to Straitshot's request for Commission review should be reversed.

In its response to Straitshot's request for Commission review, TelePacific argues that the provisions of General Rule 7.7.1 of G.O. 96-B "Review of Industry Division Disposition" do not apply to this Advice Letter. We come to the contrary conclusion. The Commission adopted G.O. 96-B on January 25, 2007. General Rule 1.1 of G.O. 96-B "Structure; Purpose; Applicability" provides in pertinent part:

The General Rules govern advice letters and information-only filings submitted to the Commission by public utilities that are gas, electrical, telephone, water, sewer system, pipeline, or heat corporations, as defined in the Public Utilities Code. . . . The provisions of this General Order govern only those informal matters submitted for filing on or after July 1, 2007.

This section of the General Order does not state any exception for advice letters filed under previously approved decisions, such as D. 04-10-038, which the Commission approved in October of 2004. Nor, is it appropriate to imply an exception here. As shown by the facts described above, construing D.04-10-038 to restrict a protestant's right to request Commission review of a Staff disposition would produce the following results: (i) allowing Staff to make a decision more than ministerial in nature (i.e. dispose of a protest raising issues that can only the Commission can decide); and (ii) allow an advice letter requesting approval of an acquisition of assets to be approved without any substantive review, even though the proposed acquisition poses important questions that the Commission should be consider and decide. Accordingly, we conclude that the more recent provisions of G.O. 96-B, including General Rule 7.7.1 "Review of Industry Division Disposition" apply to this advice letter, and that no exception to this rule should be found appropriate in this instance.

General Rule 7.7.1 provides, in pertinent part:

a person filing a protest . . . may request Commission review of an Industry Division disposition. . . . The request for Commission review shall be filed with the reviewing Industry Division within 10 days after the issuance of the disposition, shall be served on the utility, all persons filing protests or responses, and any third party whose name and interest in the relief sought appear on the face of the advice letter, and shall set forth specifically the grounds on which the requester considers the disposition to be unlawful or erroneous. Upon filing of a timely request for Commission review, the Industry Division will prepare and place on the Commission's meeting agenda a proposed resolution, and will serve it on the requester and all others on whom the request was served.

Straitshot timely filed a request for Commission review. Thus, CD properly prepared this draft resolution for our consideration, which, under General Rule 7.7.1, preserves our opportunity to review CD's written disposition, and to reverse that disposition where, as here, such a reversal is appropriate.

Having determined that we must reverse Staff's written disposition of AL 314, we consider what steps should be taken next. Appendix A to D.04-10-038 provides that, [i]f the Commission believes that the matter warrants more comprehensive review, the Commission may suspend the advice letter and direct the parties to file an application." For the reasons detailed above, this matter does require more comprehensive review than is available under the advice letter process, and, therefore, we will suspend the

advice letter, and we direct the parties to the proposed transaction to file an application seeking Commission approval of the proposed acquisition of assets.

COMMENTS

Public Utilities Code section 311(g)(1) requires that a draft resolution be served on all parties, and be subject to a public review and comment period of 30 days or more, prior to a vote of the Commission on the resolution. A draft of today's resolution was distributed for comment to the utilities and other interested parties.

FINDINGS

1. IXCH is a party to the Washington State litigation as well as one of the entities involved in the transfer of assets.
2. TelePacific should have disclosed in AL 314 the Washington State litigation, and the failure to identify this information in the advice letter was a material omission.
3. The Advice Letter process provides a simplified review of the types of utility requests that are expected to be non-controversial, that do not raise important policy questions, and do not require evidentiary hearings that may be considered only in a formal proceeding.
4. G.O. 96-B General Rule 7.7.1 does apply to Advice Letter 314.
5. G.O. 96-B General Rule 1.1 does not set forth any exception for advice letters filed under previously approved decisions, such as D.04-10-038, and it is not appropriate to find an exception here.
6. TelePacific's Advice Letter 314 contains complexities requiring disposition of more than a ministerial nature by an Industry Division.
7. Straitshot timely filed a request for review of the Communications Division's Written Disposition regarding TelePacific's Advice Letter 314 which denied Straitshot's protest and approved TelePacific's acquisition of IXCH

8. The Communications Division's Written Disposition regarding TelePacific's Advice Letter 314 should be reversed.
9. Pursuant to D.04-10-038 Appendix A.2, the Commission should suspend TelePacific's Advice Letter 314 and direct the parties to the proposed transaction to file an application seeking Commission approval of the proposed acquisition of assets.

THEREFORE, IT IS ORDERED that:

1. The Written Disposition of the Communications Division regarding TelePacific Advice Letter 314 is suspended and the parties to the proposed transaction are directed to file an application seeking Commission approval of the proposed acquisition of assets.

This resolution is effective today.

I certify that the foregoing resolution was duly introduced, passed, and adopted at a conference of the Public Utilities Commission of the State of California held on October 6, 2011, the following Commissioners voting favorably thereon:

PAUL CLANON
Executive Director