

M e m o r a n d u m

Date: April 16, 2008

To: The Commission
(Meeting of April 24, 2008)

From: Pamela Loomis, Deputy Director
Office of Governmental Affairs (OGA) — Sacramento

Subject: **SB 1389 (Padilla) – Telephone corporations: acquisitions
As Amended: March 24, 2008**

**LEGISLATIVE SUBCOMMITTEE RECOMMENDATION: OPPOSE UNLESS
AMENDED**

SUMMARY OF BILL:

SB 1389 would provide that for California telephone corporations that are not subject to rate-of -return regulation:

- no California Public Utilities Commission (CPUC) authorization is needed for that public utility, or its affiliates, to acquire any part of the capital stock of another California public utility; and
- in cases where a corporation or person is seeking CPUC authorization to merge or acquire such California telephone corporation not subject to ROR regulation, the acquiring corporation/person would not have to prove, and the CPUC would not have to find, that the proposed transaction (1) provides short-term and long-term economic benefit to ratepayers; (2) allocates at least 50% of these economic benefits to ratepayers; (3) will not adversely affect competition; and (4) is in the public interest. Currently these requirements apply when any of the utilities that are parties to the proposed transaction has gross annual California revenues exceeding \$500 Million.

These exemptions would not apply to a telephone corporation that is also an electric or gas corporation.

SUMMARY OF SUPPORTING ARGUMENTS FOR RECOMMENDATION:

- When the CPUC deliberates as to whether a merger or acquisition involving a large telephone utility in California is in the public interest, the CPUC should be able to consider all the critical aspects of such a merger or acquisition. It is especially important for the CPUC to ensure that such a transaction does not adversely affect competition and that it leaves the California utility economically viable and able to provide quality service.
- If the Legislature repeals the requirement that the CPUC find that a merger or acquisition of, or by, a large California telephone utility meets the criteria listed in Sec. 854 (b) and (c), a strong argument could be made that the Legislature intended to prohibit the CPUC from even considering any such criteria in its deliberations. Such an outcome could be detrimental to the public interest itself.
- The CPUC should be given the discretion to decide, based on the facts of the specific Sec. 854 transaction, what percentage, if any, of the economic benefit of the merger/acquisition should be allocated to ratepayers. The current 50% requirement may not be appropriate for every telephone utility merger/acquisition given the changing regulatory landscape in the telecommunications market.

SUMMARY OF SUGGESTED AMENDMENTS:

The bill should be amended to permit the CPUC, at its discretion, to not apply any or all of the criteria of Sec. 854 (b) and (c) to a transaction otherwise subject to this section. For any proposed transaction subject to Sec. 854 (b) and (c), the CPUC should be permitted to waive the requirement of Sec. 854 (c) that the acquiring company prove that the transaction meets any of the criteria or all of the criteria.

In the alternative, the bill should be amended 1) to delete Sec. 854 (c) requiring the acquiring corporation to prove by a preponderance of the evidence that each of the requirements of Sec. 854 (b) and (c) are met; and (2) to permit, but not require, the CPUC to be able to consider all of the criteria of Sec.854 (b) and (c) before authorizing the merger or acquisition involving the large telephone utilities.

Additionally, the bill should be amended to delete the requirement in Sec. 854 (b)(2) that ratepayers must receive not less than 50 percent of the economic benefits of the merger/acquisition, thus giving the CPUC the discretion to determine for each Sec. 854 transaction what percentage of the benefit ratepayers will receive.

DIVISION ANALYSIS (Communications Division):

- SB 1389 would lessen the CPUC's oversight of, and authority over, mergers and acquisitions involving California telephone corporations except for those telephone

corporations subject to rate-of-return regulation and telephone corporations that are also electric or gas corporations (Edison, and a few others).

- PU Code Section 852 prohibits any public utility, including affiliates thereof, from purchasing any of the stock of any other California public utility without CPUC authorization. SB 1389 would exempt Surewest, Frontier (Citizens), AT&T, Verizon and all competitive telecommunications carriers from this prohibition. The only California telephone corporations that would still be required to get CPUC authorization under Sec. 852 to purchase the stock of another California public utility would be the 17 rural ILECs who are still subject to rate-of-return regulation (and any telephone utility that is also a gas or electric corporation).
- Also, SB 1389 would prevent the CPUC from ensuring that mergers and acquisitions involving large telephone corporations do not adversely affect competition and from requiring that ratepayers receive at least 50% of the economic benefit of such acquisition. The bill could hinder the ability of the CPUC to decide if the acquisition was in the public interest.
- PU Code Section 854 prohibits any corporation or person, including out-of-state entities, from merging with, or acquiring, any California public utility without CPUC authorization. SB 1389 would not change this requirement.
- However SB 1389 would delete the requirements of PU Code subsection 854 (b) and (c) as they apply to acquisitions by large entities and acquisitions of large non-ROR California telephone corporations.
- PU Code subsection 854 (b) applies to proposed mergers and acquisitions of a California public utility where any utility that is a party to the proposed transaction has gross annual California revenues over \$500,000,000 (AT&T and Verizon). Currently, in order for the CPUC to approve such a proposed merger/acquisition, subsection 854 (b) requires the CPUC to find that the merger/acquisition 1) provides short-term and long-term economic benefit to ratepayers; 2) allocates at least 50% of these economic benefits to ratepayers; and (3) will not adversely affect competition. Plus the CPUC must also find that the transaction is in the public interest using the eight criteria set out in Subsection 854 (c). The party seeking acquisition or control over the California public utility must prove by a preponderance of evidence that these requirements are met.
- Subsection 854 (c) applies to proposed mergers and acquisitions of a California public utility where any entity that is a party to the proposed transaction has gross annual California revenues over \$500,000,000. In order for the CPUC to approve such a proposed merger/acquisition, subsection 854 (c) requires that the CPUC find that the proposed transaction is in the public interest using the eight criteria listed in subsection 854 (c).

- The eight criteria of 854 (c) are:
 - 1) Maintain or improve the financial condition of the resulting public utility doing business in the state.
 - 2) Maintain or improve the quality of service to public utility ratepayers in the state.
 - 3) Maintain or improve the quality of management of the resulting public utility doing business in the state.
 - 4) Be fair and reasonable to affected public utility employees, including both union and nonunion employees.
 - 5) Be fair and reasonable to the majority of all affected public utility shareholders.
 - 6) Be beneficial on an overall basis to state and local economies, and to the communities in the area served by the resulting public utility.
 - 7) Preserve the jurisdiction of the commission and the capacity of the commission to effectively regulate and audit public utility operations in the state.
 - 8) Provide mitigation measures to prevent significant adverse consequences which may result.

- The fact that California does not regulate the rates of competitive carriers and has deregulated most rates for large ILECs lessens the need of the Commission to be intimately involved in many of their financial transactions.

- Current Sec. 853 (b) permits the CPUC to exempt, by rule or order, any public utility or class of public utility from the requirements of these statutes if it finds that applications of these statutes is not necessary to the public interest. Plus Sec. 852 permits the CPUC to exempt from Sec. 852 requirements any categories of stock acquisitions which it determines will not be harmful to the public interest.

PROGRAM BACKGROUND:

- The CPUC has been applying the Sec. 853 (b) exemption where appropriate. For instance in the most recent merger approvals the CPUC concluded that the carriers did not have to pass through merger savings to ratepayers because the mergers involved holding companies and not the telephone carriers.

FEDERAL INFORMATION:

- Sections 214 and 310 of the federal Communications Act of 1934, as amended, require wireline carriers seeking to transfer direct or indirect control over certain authorizations and licenses to obtain prior approval from the Federal Communications Commission (FCC). Under Section 214, FCC approval is needed for the acquisition of any new interstate facilities and for all discontinuance of service. The FCC will grant such approval only if it finds that the transfers are in the public interest. (Sec. 310 applies to acquisitions by foreign corporations, and has

strict requirements for national security reasons.) FCC regulations governing merger reviews pertaining to wireline carriers can be found in [47 CFR§ 63.03](#) and [47 CFR§ 63.04](#).

- Federal antitrust laws require Department of Justice and Federal Trade Commission approval of any merger of large corporations. (See Section 7A of the Clayton Act, 15 U.S.C. 18a, as added by the Hart-Scott-Rodino Antitrust Improvements Act of 1976, Pub. L. 94-435, 90 Stat. 1390.)

LEGISLATIVE HISTORY:

The criteria in Sec. 854 (b) and (c) were added in 1989 by the State Legislature (Stats.1989, Ch. 390). At that time, Southern California Edison was attempting to purchase San Diego Gas & Electric, and several other utility-related mergers were being contemplated. The Senate Committee on Energy, Utilities & Communications (SEUC) and the Assembly Committee on Utilities and Commerce (U&C) held a joint hearing titled "Utility Merger Mania: Benefits and Risks to Ratepayers and Shareholders" (October 24, 1988). Then-CPUC President Mitch Wilk testified at the hearing. When he was asked by committee members what criteria the CPUC might use in reviewing a merger, he ran through a list of criteria. Those criteria were subsequently put into proposed legislation by members of the Legislature.

FISCAL IMPACT:

None.

STATUS:

SB 1389 passed the Senate Committee on Energy, Utilities and Communications on April 15, 2008 with a 5-3 vote, and will be heard by the Senate Appropriations Committee next.

SUPPORT/OPPOSITION:

SUPPORT:

Verizon - Sponsor

Asian Business Association	Long Beach Area Chamber of Commerce
Black Business Association	Long Beach Black Chamber of Commerce
Brotherhood Crusade	Moreno Valley Black Chamber of Commerce
California Black Chamber of Commerce	National Association for the Advancement of Colored People #1034
California Association for Local Economic Development	National Black Business Council
California Small Business Association	Sacramento Asian Pacific Chamber of Commerce

Century 21 Excellence Organization	San Diego Urban Economic Corporations
Community Union, Inc.	Self-Help for the Elderly
Congress of California Seniors	Sisters at the Well, Inc.
Contractors License Network, Inc.	South Bay Latino Chamber of Commerce
Greater Los Angeles African	Southern Christian Leadership Conference of Greater Los Angeles
American Chamber of Commerce	TELACU/Millennium
Hispanic Chamber of commerce of Silicon Valley	United Cambodian Community
Hispanic Outreach Taskforce	United States Hispanic Chamber of Commerce
Integrity Mortgage Solutions, Inc.	

OPPOSITION:

California Public Utilities Commission (CPUC) Subcommittee (Recommendation)	Division of Ratepayer Advocates
Consumer Action	Geoffrey F. Brown (former CPUC Commissioner)
Consumer Federation of California	Latino Issues Forum
Consumer Watchdog	The Utility Reform Network

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BILL LANGUAGE:

BILL NUMBER: SB 1389 AMENDED
BILL TEXT

AMENDED IN SENATE MARCH 24, 2008

INTRODUCED BY Senator Padilla

FEBRUARY 21, 2008

~~An act to amend Section 2893 of the Public Utilities Code, relating to telecommunications. An act to amend Section 853 of the Public Utilities Code, relating to public utilities.~~

LEGISLATIVE COUNSEL'S DIGEST

SB 1389, as amended, Padilla. ~~Telephone call identification service.~~ Public utilities: telephone corporations: acquisitions.

Existing law prohibits any public utility from purchasing or acquiring any part of the capital stock of another public utility without authorization from the Public Utilities Commission. Existing law prohibits any person or corporation from merging, acquiring, or controlling, directly or indirectly, any public utility without authorization from the commission. Existing law also requires the commission to consider certain criteria, and to make certain findings, before authorizing the merger, acquisition, or control of an electric, gas, or telephone utility having revenues in excess of a specified amount.

This bill would exempt telephone corporations that are not regulated under a rate-of-return regulatory structure from these criteria and finding requirements. The bill would also exempt telephone corporations that are not regulated under a rate-of-return regulatory structure from the prohibition against a public utility purchasing or acquiring stock of another public utility without authorization from the commission. "Rate-of-return regulatory structure" would be defined for these purposes as a system under which the rates and charges of the telephone corporation are limited by a maximum permissible price that may be charged for a specific service.

~~Existing law, with specified exceptions, requires the commission to require any call identification service offered by a telephone corporation, or by any other person or corporation that makes use of the facilities of a telephone corporation, to allow the caller, at no charge, to withhold, on an individual basis, the display of the caller's telephone number from the telephone instrument of the individual receiving the call, but prohibits a caller from withholding the display of the caller's business telephone number when that number is being used for telemarketing purposes. Existing law requires that a telephone corporation notify its subscribers that their calls may be identified to a called party either: (1) 30 or~~

~~more days before the telephone corporation commences to participate in the offering of a call identification service, or (2) by March 1, 1990, if the telephone corporation is participating in a call identification service prior to January 1, 1990.~~

~~This bill would delete the requirement that a telephone corporation that is participating in a call identification service prior to January 1, 1990, notify subscribers by March 1, 1990, that their calls may be identified to a called party.~~

Vote: majority. Appropriation: no. Fiscal committee: ~~no~~
yes . State-mandated local program: no.

THE PEOPLE OF THE STATE OF CALIFORNIA DO ENACT AS FOLLOWS:

SECTION 1. Section 853 of the Public Utilities Code is amended to read:

853. (a) This article does not apply to any person or corporation ~~which transacts no~~ that does not transact

business subject to regulation under this part, except performing services or delivering commodities for or to public utilities or municipal corporations or other public agencies primarily for resale or use in serving the public or any portion thereof, but shall apply to any public utility, and any subsidiary or affiliate of, or corporation holding a controlling interest in, a public utility, if the commission finds, in a proceeding to which the public utility is , or may become a party, that the application of this article is required by the public interest.

(b) The commission may from time to time by order or rule, and subject to those terms and conditions as may be prescribed therein, exempt any public utility or class of public utility from this article if it finds that the application thereof , with respect to the public utility or class of public utility , is not necessary in the public interest. The commission may establish rules or impose requirements deemed necessary to protect the interest of the customers or subscribers of the public utility or class of public utility exempted under this subdivision. These rules or requirements may include, but are not limited to, notification of a proposed sale or transfer of assets or stock and provision for refunds or credits to customers or subscribers.

(c) The provisions of Sections 851 and 854 that prohibit any assignment, acquisition, or change of control without advance authorization from the commission, do not apply to the transfer of the ownership interest in a water utility, with 10,000 or fewer service connections, from a decedent to a member of the decedent's family in the manner provided in Section 240 of the Probate Code or by a will, trust, or other instrument.

(d) *Section 852 and subdivisions (b) and (c) of Section 854 do not apply to a telephone corporation that is not regulated under a rate-of-return regulatory structure. This subdivision does not exempt a telephone corporation that is also an electrical corporation or a gas corporation, unless the commission determines that the telephone corporation is exempt pursuant to subdivision (b) of this section. As used in this subdivision, "rate-of-return regulatory structure" has the same meaning as in Section 829.*

~~(d)~~

(e) It is the intent of the Legislature that

transactions with monetary values that materially impact a public utility's rate base should not qualify for expedited advice letter treatment pursuant to this article. It is the further intent of the Legislature that the commission maintain all of its oversight and review responsibilities subject to the California Environmental Quality Act, and that public utility transactions that jurisdictionally trigger a review under the act should not qualify for expedited advice letter treatment pursuant to this article.

~~SECTION 1. Section 2893 of the Public Utilities Code is amended to read:~~

~~2893. (a) The commission shall, by rule or order, require that every telephone call identification service offered in this state by a telephone corporation, or by any other person or corporation that makes use of the facilities of a telephone corporation, shall allow a caller to withhold display of the caller's telephone number, on an individual basis, from the telephone instrument of the individual receiving the telephone call placed by the caller. However a caller shall not be allowed to withhold the display of the caller's business telephone number when that number is being used for telemarketing purposes.~~

~~(b) There shall be no charge to the caller who requests that his or her telephone number be withheld from the recipient of any call placed by the caller.~~

~~(c) The commission shall direct every telephone corporation to notify its subscribers that their calls may be identified to a called party 30 or more days before the telephone corporation commences to participate in the offering of a call identification service.~~

~~(d) This section does not apply to any of the following:~~

~~(1) An identification service which is used within the same limited system, including, but not limited to, a Centrex or private branch exchange (PBX) system, as the recipient telephone.~~

~~(2) An identification service which is used on a public agency's emergency telephone line or on the line which receives the primary emergency telephone number (911).~~

~~(3) Any identification service provided in connection with legally sanctioned call tracing or tapping procedures.~~

~~(4) Any identification service provided in connection with any "800" or "900" access code telephone service until the telephone corporation develops the technical capability to comply with subdivision (a), as determined by the commission.~~

~~(e) Until the market for local telephone service is competitive, a telephone corporation shall not charge any subscriber for having an unlisted or unpublished telephone number. However, nothing in this subdivision shall be interpreted by the commission to reduce the revenues of telephone corporations. Any actions of the commission pursuant to this subdivision shall be implemented on a competitively neutral basis. This charge shall not be eliminated prior to the effective date upon which offsetting rates are implemented by the commission.~~