

Decision **DRAFT DECISION OF ALJ DUDA** (Mailed 9/9/2003)

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of 360networks (USA) inc., (U-6028-C) for authorization to transfer control of public utility operations in California.

Application 02-10-022
(Filed October 18, 2002)

**OPINION GRANTING INDIRECT TRANSFER OF CONTROL
AND FINING APPLICANT FOR VIOLATION OF SECTION 854(a)
OF THE PUBLIC UTILITIES CODE**

1. Summary

360networks (USA) inc. (Applicant) requests approval to transfer control of its public utility business in California in connection with reorganization of its parent company, 360networks inc. (360networks), pursuant to orders of Canadian and United States bankruptcy courts.

This decision grants Application (A.) 02-10-022 to the extent it requests prospective authority under Pub. Util. Code § 854¹ for the indirect transfer of control. This decision denies the application to the extent it requests retroactive authority for the transfer. Finally, this decision requires Applicant to pay a fine of \$ 2,500 for its failure to obtain Commission authorization for this transfer of control prior to consummating the transaction as required by § 854(a).

¹ All statutory references are to the Pub. Util. Code unless otherwise indicated.

2. Background

Applicant is a Nevada Corporation authorized to do business in California. Applicant holds a certificate of public convenience and necessity (CPCN), issued by the Commission, to provide interexchange telecommunications services in California.² Applicant is a wholly owned subsidiary of 360networks holdings (USA) inc. (US Holdings). US Holdings is a subsidiary of 360networks Corporation (360 Corp.), and 360 Corp. is a wholly owned subsidiary of 360networks, a Canadian Corporation.

In June 2001, 360networks and certain of its subsidiaries commenced bankruptcy proceedings in The Supreme Court of British Columbia, Canada and in the United States Bankruptcy Court, Southern District of New York. On October 1, 2002, the U.S. Bankruptcy Court approved the First Amended Joint Plan of Reorganization and Consolidated Plan of Compromise or Arrangement (collectively referred to as the “Plans”) filed by Applicant and 360 Corp.³

On October 18, 2002, Applicant filed A.02-10-022 for authority under §854 for indirect transfer of its public utility business according to the Plans approved by the U.S. Bankruptcy Court. The application states that Plans will be effectuated by October 31, 2002 and requests Commission approval of the transfer by October 24, 2002, or six days after the application was filed. The

² See D.98-07-057 which granted a CPCN to Applicant’s predecessor, Pacific Fiber Link L.L.C.

³ See Exhibit A of A.02-10-022 containing the order of the U.S. Bankruptcy Court approving the Plans.

application further requests retroactive, or “nunc pro tunc”⁴ approval of the application should the Commission not act before the Plans are effectuated.

On February 20, 2003, Applicant explained in a letter to the Administrative Law Judge that the Plans were implemented on November 12, 2002. On September 5, 2003, Applicant filed a motion to supplement the record to provide a copy of its financial statements and a copy of the Plans, as required by Rule 36 of the Commission’s Rules of Practice and Procedure.

3. Requested Authority

Applicant requests approval to implement the transfer of control contained in the Plans approved by the U.S. Bankruptcy Court. Pursuant to the Plans, 360networks no longer owns or controls 360 Corp., and 360 Corp. has become the new parent company of the reorganized 360networks group of companies, including Applicant. 360 Corp issued and allotted shares of its treasury stock to the company’s new shareholders such that the company’s Senior Lenders received 80.5% of the outstanding shares,⁵ unsecured U.S. and Canadian creditors received 12%, and certain employees and outside directors received 7.5%.

As a result of the Plans, the entity that previously held 20% or more of the shares of 360networks, Ledcor Holdings Inc., no longer indirectly controls Applicant. Instead, 360 Corp. has become Applicant’s ultimate parent rather

⁴ The phrase “nunc pro tunc,” meaning “now for then,” refers to those acts which are allowed to be done at a later time “with the same effect as if regularly done.” (Blacks Law Dictionary (4th Revised ed. (1968), p. 1218)).

⁵ The Senior Lenders consist of approximately 60 unaffiliated institutions and none will hold a majority interest of the outstanding shares.

than 360 networks and shares of 360 Corp. have been distributed to creditors, employees, and outside directors.

Applicant states that the change in indirect control of applicant's parent, 360 Corp., will serve the public interest and promote competition. According to Applicant, the change will improve the financial strength of the operating entity providing service in California. In addition, the change will be transparent to customers because Applicant's public utility operations will continue unabated with the same management and under the same name.

There were no protests or responses to the application.

4. Discussion

A. Whether to Approve the Application

In this application, Applicant requests authority under § 854 to transfer indirect control of its public utility business through implementation of the Plans ordered by the U.S. Bankruptcy Court. Section 854(a) states, in relevant part, as follows:

No person or corporation...shall merge, acquire, or control...any public utility organized and doing business in this state without first securing authorization to do so from the commission...Any merger, acquisition, or control without that prior authorization shall be void and of no effect.

The Commission has broad discretion to determine if it is in the public interest to authorize a transaction pursuant to § 854(a).⁶ The primary standard used by the Commission to determine if a transaction should be authorized

⁶ D.95-10-045, 1995 Cal. PUC LEXIS 901, *18-19; and D.91-05-026, 40 CPUC2d 159, 171.

under § 854(a) is whether the transaction will adversely affect the public interest.⁷ The Commission may also consider if the transaction will serve the public interest.⁸ Where necessary and appropriate, the Commission may attach conditions to a transaction in order to protect and promote the public interest.⁹

For the following reasons, we conclude that it is reasonable to grant A.02-10-022 to the extent the application requests prospective authority under § 854(a) for the transfer of control of Applicant's parent company, 360 Corp. First, there will be no change to terms or conditions of service for Applicant's customers as a result of the transaction. Thus, Applicant's customers, and the public will not be harmed by the transfer of control. Second, Applicant's California operations will continue under the same management. Third, the public may benefit from the transfer of control to the extent the transaction improves the financial strength of Applicant's parent company and enhances Applicant's ability to compete through lower rates and/or new or improved services. Fourth, there is no opposition to this application. For these reasons, we see no reason to withhold authority for the indirect transfer of control before us here.

⁷ D.00-06-079, p. 13; D.00-06-057, p. 7; D.00-05-047, p. 11 and Conclusion of Law (COL) 2; D.00-05-023, p. 18; D.99-03-019, p. 14; D.98-08-068, p. 22; D.98-05-022, p. 17; D.97-07-060, 73 CPUC2d 601, 609; D.70829, 65 CPUC 637, 637; and D.65634, 61 CPUC 160, 161.

⁸ D.00-06-005, 2000 Cal. PUC LEXIS 281, *4; D.99-04-066, p.5; D.99-02-036, p. 9; D.97-06-066, 72 CPUC2d 851, 861; D.95-10-045, 62 CPUC2d 160, 167; D.94-01-041, 53 CPUC2d 116, 119; D.93-04-019, 48 CPUC2d 601, 603; D.86-03-090, 1986 Cal. PUC LEXIS 198 *28 and COL 3; and D.8491, 19 CRC 199, 200.

⁹ D.95-10-045, 62 CPUC2d 160, 167-68; D.94-01-041, 53 CPUC2d 116, 119; D.90-07-030, 1990 Cal. PUC LEXIS 612 *5; D.89-07-016, 32 CPUC2d 233, 242; D.86-03-090, 1986 Cal. PUC LEXIS 198 *84-85 and COL 16; and D.3320, 10 CRC 56, 63.

We deny A.02-10-022 to the extent it requests retroactive authority under § 854(a) for the transfer of control. The purpose of § 854(a) is to enable the Commission to review a proposed acquisition, *before it takes place*, in order to take such action as the public interest may require.¹⁰ Granting this application on a retroactive basis would thwart the purpose of § 854(a). Since we do not grant retroactive authority, the transfer of control is void under § 854(a) for the period of time prior to the effective date of this decision. The Applicant is at risk for any adverse consequences that may result from its parent company having implemented the transfer of control without Commission authority.

**B. Whether to Penalize the Applicants for
Their Failure to Comply with Pub. Util. Code § 854(a)**

Applicants failed to comply with § 854(a) by effectuating the transfer of control without Commission authorization. Violations of § 854(a) are subject to monetary penalties under § 2107 which states as follows:

Any public utility which violates or fails to comply with any provision of the Constitution of this state or of this part, or which fails or neglects to comply with any part or provision of any order, decision, decree, rule, direction, demand, or requirement of the commission, in a case in which a penalty has not otherwise been provided, is subject to a penalty of not less than five hundred dollars (\$500), nor more than twenty thousand dollars (\$20,000) for each offense.

For the following reasons, we conclude that the Applicant should be fined for its failure to comply with § 854(a). First, any violation of § 854(a),

¹⁰ D.99-02-061, 1999 Cal. PUC LEXIS 56 *12; D.98-07-015, 1998 Cal. PUC LEXIS 526 *7; D.98-02-005, 1998 Cal. PUC LEXIS 320 *8; D.97-12-086, 1997 Cal. PUC LEXIS 1168 *8; and San Jose Water Co. (1916) 10 CRC 56, 63.

regardless of the circumstances, is a serious offense that should be subject to fines. Second, the imposition of a fine will help to deter future violations of § 854(a) by the Applicants and others.

To determine the size of the fine, we shall rely on the criteria adopted by the Commission in D.98-12-075. We address these criteria below.

Criterion 1: Severity of the Offense

In D.98-12-075, the Commission held that the size of a fine should be proportionate to the severity of the offense. To determine the severity of the offense, the Commission stated that it would consider the following factors:¹¹

Physical harm: The most severe violations are those that cause physical harm to people or property, with violations that threatened such harm closely following.

Economic harm: The severity of a violation increases with (i) the level of costs imposed upon the victims of the violation, and (ii) the unlawful benefits gained by the public utility. Generally, the greater of these two amounts will be used in setting the fine. The fact that economic harm may be hard to quantify does not diminish the severity of the offense or the need for sanctions.

Harm to the Regulatory Process: A high level of severity will be accorded to violations of statutory or Commission directives, including violations of reporting or compliance requirements.

The number and scope of the violations: A single violation is less severe than multiple offenses. A widespread violation that affects a large number of consumers is a more severe offense than one that is limited in scope.

¹¹ 1998 Cal. PUC LEXIS 1016, *71 - *73.

Applicant's violation of § 854(a) was not an especially egregious offense. The violation did not cause any physical or economic harm to others. In addition, there is no evidence that Applicant significantly benefited from its unlawful conduct or that its actions affected any consumers. The only factor that indicates the violation should be considered a serious offense is our general policy of according a high level of severity to any violation of the Pub. Util. Code. However, this factor must be weighed against the other factors indicating that Applicant's failure to comply with § 854(a) was not an egregious offense.

Criterion 2: Conduct of the Utility

In D.98-12-075, the Commission held that the size of a fine should reflect the conduct of the utility. When assessing the conduct of the utility, the Commission stated that it would consider the following factors:¹²

The Utility's Action to Prevent a Violation: Utilities are expected to take reasonable steps to ensure compliance with applicable laws and regulations. The utility's past record of compliance may be considered in assessing any penalty.

The Utility's Actions to Detect a Violation: Utilities are expected to diligently monitor their activities. Deliberate, as opposed to inadvertent wrongdoing, will be considered an aggravating factor. The level and extent of management's involvement in, or tolerance of, the offense will be considered in determining the amount of any penalty.

The Utility's Actions to Disclose and Rectify a Violation: Utilities are expected to promptly bring a violation to the Commission's attention. What constitutes "prompt" will depend on circumstances. Steps taken by a utility to

¹² 1998 Cal. PUC LEXIS 1016, *73 - *75.

promptly and cooperatively report and correct violations may be considered in assessing any penalty.

Applicant did not take reasonable steps to comply with §854(a) because the application was not timely. The application was filed only days before the order of the U.S. Bankruptcy Court took effect and did not allow the Commission reasonable time to review the transaction before it took effect. Although Applicant and its parent company were required to comply with the order of the Bankruptcy Court and implement the Plans, Applicant initially gave the Commission only six days to process this application before the scheduled date for the Plans to take effect. Even though implementation of the Plans was ultimately delayed until November 12, 2002, Applicant's timing would not have allowed for the customary 30-day comment period on applications or for any comments on a draft order before the transfer of control took effect. Applicant states that it could not file earlier because the Bankruptcy Court did not issue its order until October 1, 2002 and because of the underlying complexity of the transaction.

We find that Applicant could have given the Commission earlier notice by filing the application with the proposed Plans while awaiting the final order of the Bankruptcy Court. This would have allowed the Commission to consider the proposed plan and review any changes to it on an expedited basis following action by the Bankruptcy Court. Although Applicant filed in advance of the transfer of control, its timing was not reasonable. Nevertheless, Applicant did disclose its violation and its error in judgment in not filing earlier is not an especially egregious offense. This suggests a smaller fine is appropriate.

Criterion 3: Financial Resources of the Utility

In D.98-12-075, the Commission held that the size of a fine should reflect the financial resources of the utility. When assessing the financial

resources of the utility, the Commission stated that it would consider the following factors:¹³

Need for Deterrence: Fines should be set at a level that deters future violations. Effective deterrence requires that the Commission recognize the financial resources of the utility in setting a fine.

Constitutional limitations on excessive fines: The Commission will adjust the size of fines to achieve the objective of deterrence, without becoming excessive, based on each utility's financial resources.

Applicant provided the most recent unaudited financial statements of its parent company, 360 Corp. which indicate the parent company has current assets of approximately \$100 million dollars, and operating revenues of over \$75 million for the first seven months of 2003. (*See* September 5, 2003 Motion to Supplement Record, Appendix A.) The financial statements also indicate that 360 Corp. has incurred a net loss for the same reporting period. (*Id.*) From this information, we conclude that Applicant, or its parent company, has the financial resources to pay a fine in the range normally applied by the Commission for violations of Section 854(a). We will weigh this information accordingly when setting the amount of the fine.

Other than the above information, Applicant requested confidential treatment of its financial statements because they are unaudited and have not yet been reviewed and made public. Because the financial statements have not yet been made public, we will grant the request for confidentiality.

¹³ 1998 Cal. PUC LEXIS 1016, *75 - *76.

Criterion 4: Totality of the Circumstances

In D.98-12-075, the Commission held that a fine should be tailored to the unique facts of each case. When assessing the unique facts of each case, the Commission stated that it would consider the following factors:¹⁴

The degree of wrongdoing: The Commission will review facts that tend to mitigate the degree of wrongdoing as well as facts that exacerbate the wrongdoing.

The public interest: In all cases, the harm will be evaluated from the perspective of the public interest.

The facts of this case indicate that the degree of wrongdoing was not egregious. Applicant was required to implement the order of the U.S. Bankruptcy Court, but should have exercised better judgment and filed its proposed reorganization plan earlier to allow the Commission adequate time to review the Plans before they took effect. No one was harmed by Applicant's failure to comply with § 854(a) and Applicant does not appear to have materially benefited from its unlawful conduct. These facts indicate that the public interest was not significantly harmed by Applicant's violation of § 854(a). In setting the fine, we will consider the relatively small harm to the public interest from this violation.

Criterion 5: The Role of Precedent

In D.98-12-075, the Commission held that any decision which imposes a fine should (1) address previous decisions that involve reasonably comparable factual circumstances, and (2) explain any substantial differences in outcome.¹⁵

¹⁴ 1998 Cal. PUC LEXIS 1016, *76.

¹⁵ 1998 Cal. PUC LEXIS 1016, *77.

In D.00-09-035, we held that our precedent of meting our lenient treatment to those who violate § 854(a) had failed to deter additional violations; and we indicated that henceforth we would impose fines in order to deter future violations of § 854(a). In both D.00-12-053 and D.03-05-033, the Commission fined telecommunications carriers \$5,000 for failure to obtain advance approval under §854(a) for transfers of control. The facts of this case are somewhat unique in that this case involves implementation of an order of the U.S. Bankruptcy Court and Applicant's failure to make a timely application to the Commission. Therefore, we will impose a smaller fine in this case.

Conclusion: Setting the Fine

We conclude based on the facts of this case that the Applicant should be fined \$2,500 for violating § 854(a). The fine we impose today is meant to deter future violations of § 854(a) by the Applicant and other parties. We emphasize that the size of the fine we impose today is tailored to the unique facts and circumstances before us in this proceeding. We may impose larger or smaller fines in other proceedings if the facts so warrant.

A review of Applicant's compliance with Commission reporting requirements reveals that Applicant has been delinquent in filing Public Program Surcharge Transmittal Reports. Applicant should correct this deficiency by submitting these Surcharge Transmittal Reports and paying any applicable surcharges it owes. Carriers are required to file these reports every six months, even if the surcharge collection is zero.

5. Category and Need for Hearing

In Resolution ALJ 176-3099, dated November 7, 2002, the Commission preliminarily categorized this proceeding as ratesetting, and preliminarily

determined that hearings were not necessary. Based on the record, we affirm that this is a ratesetting proceeding, and that hearings are not necessary.

6. Comments on Draft Decision

The Commission mailed the draft decision of the Administrative Law Judge (ALJ) in this matter to the parties in accordance with § 311(g)(2) and Rule 77.7 of the Rules of Practice and Procedure. Applicants agreed to a shortened seven-day comment period as allowed by Rule 77.7(g). There were no comments on the draft decision.

7. Assignment of Proceeding

Geoffrey F. Brown is the Assigned Commissioner and Dorothy Duda is the Administrative Law Judge in this proceeding.

Findings of Fact

1. Applicant is a Nevada corporation authorized to provide interexchange telecommunications services within California.
2. Applicant is a wholly owned subsidiary of 360 Corp.
3. On October 18, 2002, Applicant filed A.02-10-022 for authority to transfer control of its public utility business in California pursuant to reorganization plans ordered by the U.S. Bankruptcy Court.
4. The transfer of control was completed on November 12, 2002, prior to the Commission acting on this application.
5. Under the plans for reorganization, 360 Corp. became Applicant's ultimate parent company and shares of 360 Corp. were distributed to creditors, employees, and outside directors.
6. Pub. Util. Code § 854(a) requires Commission authorization to transfer control of a public utility. Any transfer of control without Commission authorization is void under the statute.

7. There will be will be no changes to Applicant's terms or conditions of service or its management as a result of the transfer of control.

8. There were no protests to A.02-10-022.

9. Pub. Util. Code § 2107 provides the Commission with authority to impose a penalty of between \$500 and \$20,000 for violations of the Pub. Util. Code.

10. In D.98-12-075, the Commission adopted the following criteria for determining the amount of a fine: (i) the severity of the offense, (ii) the conduct of the utility, (iii) the financial resources of the utility, (iv) the totality of the circumstances, and (v) the role of precedent.

11. Applicant's failure to comply with § 854(a) did not harm others and did not significantly benefit Applicant.

12. Applicant has adequate financial resources to pay a fine for its violation.

13. Applicant has not filed the required Public Program Surcharge Transmittal Reports with the Commission.

Conclusions of Law

1. This is a ratesetting proceeding and no hearing is necessary.

2. A.02-10-022 should be approved on a prospective basis because it is not adverse to the public interest.

3. Applicant violated § 854(a) by transferring indirect control of its public utility operations without Commission authorization.

4. Pursuant to §2107, Applicant should be fined for violating § 854(a). The amount of the fine should be based on the criteria set forth in D.98-12-075.

5. Applicants' violation of § 854(a) was not particularly an egregious offense.

6. The public interest was not significantly harmed by Applicant's violation of § 854(a).

7. The application of the criteria in D.98-12-075 to the facts of this case indicates that Applicant should pay a fine of \$2,500 for violating § 854(a).

8. It is necessary to fine Applicant for violating § 854(a) in order to deter future violations of § 854(a).

9. Applicant's request for confidential treatment of the financial information contained in its September 5, 2003 supplemental filing should be granted for two years.

10. The following order should be effective immediately.

O R D E R

IT IS ORDERED that:

1. Application (A.) 02-10-022 for authority under Pub. Util. Code § 854 for 360networks (USA) inc. (Applicant) to transfer control of its public utility business is granted to the extent it requests authority effective as of the date of this order. A.02-10-022 is denied to the extent that it requests retroactive authority for the transfer of control.

2. Applicant shall notify the Director of the Commission's Telecommunications Division in writing of the transfer of control, as authorized herein, within 10 days of this order. A true copy of the instrument(s) of transfer shall be attached to the notification.

3. Applicant shall pay a fine in the amount of \$2,500 for violating Pub. Util. Code § 854(a). Applicant shall pay the fine within 20 days from the effective date of this order by tendering to the Fiscal Office of the California Public Utilities Commission a check in the amount of \$2,500 made payable to the State of California General Fund.

4. Applicant's motion to supplement the record is granted.

5. Applicant's request to file its financial information under seal is granted for two years from the effective date of this decision. During that period the information shall not be made accessible or disclosed to anyone other than the Commission staff except on the further order or ruling of the Commission, the Assigned Commissioner, the Assigned Administrative Law Judge (ALJ), or the ALJ then designated as Law and Motion Judge.

6. If the Applicant believes that further protection of the information kept under seal is needed, it may file a motion stating the justification for further withholding of the information from public inspection, or for such other relief as needed.

7. Within 30 days of this order, Applicant shall file its delinquent Public Program Surcharge Transmittal Reports with the Director of the Telecommunications Division and pay any applicable surcharges that it owes based on those reports.

8. A.02-10-022 is closed.

This order is effective today.

Dated _____, at San Francisco, California.