

**STATE OF NEW HAMPSHIRE
PUBLIC UTILITIES COMMISSION**

DT 07-011

VERIZON NEW ENGLAND, ET AL.

Transfer of Assets to FairPoint Communications, Inc.

Order Addressing Broadband Investment with Service Quality Penalties

ORDER NO. 25,360

May 8, 2012

I. FACTUAL AND PROCEDURAL BACKGROUND

In 2007, Verizon New England and affiliated entities (Verizon) filed a joint application for merger with FairPoint Communications, Inc. (FairPoint) whereby Verizon would transfer its assets and franchise in Northern New England, including New Hampshire, to FairPoint. By Order No. 24,823 (February 25, 2008), the Commission approved a settlement agreement that permitted the transfer, subject to certain conditions. Relevant to the instant matter, under that settlement and the subsequent order, FairPoint agreed to abide by certain service quality standards and to self-enforcing penalties should it fail to meet those standards. *Verizon New England, et al.*, Order No. 24,823 (Feb. 25, 2008) at 33, 72. The standards and penalties were modified in a settlement agreement reached in the context of FairPoint's bankruptcy and approved by the Commission. *FairPoint Communications, Inc., et al.*, Order No. 25,129 (July 7, 2010) at 17. In particular, under the new settlement, FairPoint was subject to a service quality penalty of \$6,000,000 for service quality failures in calendar year 2009, but that amount could be reduced based upon improvements in its performance in calendar year 2010. Significantly, the penalty and reporting conditions of the original settlement were, in all other relevant respects, retained following the new settlement.

On January 25, 2012, Staff filed a memorandum and recommendation relative to the service quality penalties. According to Staff's recommendation, following review of FairPoint's calculations and the potential reductions to the amount owed for failures in 2009, it and FairPoint agreed that FairPoint was entitled to a reduction of the 2009 penalties from \$6,000,000 to \$2,400,000. In addition, they agreed that FairPoint had incurred an additional penalty of \$190,418 in calendar year 2010. Accordingly, Staff's memorandum and recommendation specified that it and FairPoint agreed that FairPoint owed \$2,590,418 for service quality failures in 2009 and 2010. Staff recommended that the Commission direct FairPoint to refund the money to customers through a credit of \$0.99 per month beginning in April 1, 2012 and ending upon full payment of the penalty amount.

On January 31, 2012, FairPoint responded to Staff's memorandum and recommendation and requested that the Commission not adopt Staff's recommendation but instead grant FairPoint and Staff a period of time to discuss the possible use of the service quality penalty funds for the expansion of broadband in Northern New Hampshire. FairPoint contended that the credit recommended by Staff would have only minimal economic benefit to the residents of New Hampshire, but that expanding broadband would provide meaningful economic benefits. Under the existing agreements FairPoint is obligated to achieve 95 percent broadband availability statewide, including 75 percent broadband availability in rural areas of the state, by March 31, 2013. FairPoint stated that the service quality penalty funds would be used to deploy broadband beyond those existing commitments. FairPoint further stated that if it and Staff could not reach an agreement on the use of the funds for broadband expansion, the Commission could then act upon Staff's memorandum and recommendation.

On February 6, 2012, the Commission issued Order No. 25,331 adopting Staff's recommendation regarding bill credits. The Commission, however, noted that there may be merit in FairPoint's request to expand broadband. Therefore, the Commission concluded that if FairPoint submitted a broadband expansion plan by March 1, 2012, the Commission would hold a hearing on the plan to determine whether the plan was acceptable. FairPoint submitted a plan on March 1, 2012 in which it noted that, for calendar year 2011, there are additional penalties of \$233,333, bringing the total amount to \$2,823,751. On April 6, 2012, Staff filed a memorandum confirming the 2011 amount and thus the total of \$2,823,751.

At the March 19 hearing, numerous record requests were made of FairPoint, which was given two weeks to respond. One record request resulted from a concern that, should service quality penalties be used to assist the broadband expansion, FairPoint should contribute additional funds in order to ensure that any benefit to FairPoint from the use of these funds be offset and the 'penalty' nature of the funds be maintained. In response to record request 3, Fairpoint stated it would be willing to provide an additional \$500,000, for a total of \$3,323,751 should the plan be approved.

Because the requested information about the broadband expansion plan would not be submitted until after the April 1, 2012 deadline originally set for paying bill credits, the Commission amended Order No. 25,331 by extending the bill credit date to June 1, 2012. Further, the Commission concluded that credits should be paid in a single month at the amount per line necessary to refund the total amount due and that FairPoint was to file an accounting of the refund confirming that the credited amount fully refunded the total penalty.

Despite the above, the Commission also stated that if, upon review of the information responsive to the outstanding record requests, the broadband expansion plan was acceptable, credits would not be paid and the broadband expansion plan could continue to be developed.

II. COMMISSION ANALYSIS

There are portions of New Hampshire in which broadband services are not available, and in prior Commission proceedings regarding Verizon's transfer to FairPoint and FairPoint's emergence from bankruptcy, we addressed the need to expand broadband availability. Order No. 24,823 and Order No. 25,129 established dates by which FairPoint would achieve levels of availability, commitments which continue irrespective of this proceeding. What we have before us is an opportunity to go beyond those levels of availability by supplementing FairPoint's broadband deployment plans with additional funds that arise from service quality penalties. Though we recognize that not all customers who experienced substandard service would receive a benefit from an expanded broadband commitment, on balance we find merit in directing the service quality penalties, as well as the \$500,000 offered by FairPoint in response to a Commission request, to expand the reach of broadband in New Hampshire. Indeed, a recent decision by the Federal Communications Commission (FCC) to incorporate broadband service requirements in Universal Service Fund distributions highlights the growing interdependence of basic telephone and Internet services. *See Connect America Fund et al.*, WC Docket No. 10-90 *et al.*, Report and Order and Further Notice of Proposed Rulemaking, 26 FCC Rcd 17663 (2011). It is critical, however, that funds be targeted to bring about meaningful improvement in telecommunications to some of the unserved parts of the state. To simply refund the penalty amounts to customers would, in our view, grant a relatively small benefit to individual

households, while missing an opportunity to provide significant improvement to areas we consistently hear are in need of modern telecommunications options.

To have confidence that a plan for such an expansion of broadband service would be successful, however, requires more than what FairPoint has provided to date. Having heard testimony on the plan filed on March 1 and reviewed the information submitted in response to our record requests, we cannot approve the plan as filed by FairPoint but will allow further opportunity for the company, with input from the Staff, to develop a plan that meets consumer protection conditions set forth herein. In light of currently pending legislation in the General Court that would restrict the Commission's authority in telecommunications regulation, we sought FairPoint's analysis as to whether the Commission would have the continuing authority to monitor the progress of the proposed expansion and ensure its completion. FairPoint responded that should the legislation be enacted as written, the Commission would have no such authority. FairPoint Response to Record Request 1. FairPoint offered, however, that it would be willing to work with the Commission and the New Hampshire Office of the Attorney General to ensure compliance with an expansion plan and posited that a contract with the State of New Hampshire may be sufficient. We consider enforceability a necessary component to any plan to re-direct customer credits and will require finalized terms regarding the Commission's authority over plan performance as a necessary condition of approval.

Further, at the March 19 hearing, FairPoint stated that using these funds to expand broadband might help it secure funding from the FCC based upon that agency's recent reforms to universal service funding. Transcript of March 19, 2012 Hearing (Tr.) at 27. FairPoint also stated, however, that it had not yet created a financial plan relating to its proposed expansion in

Northern New Hampshire. Tr. at 28. FairPoint also confirmed that it did not know the scope of the proposed project – and could not know it until late in 2012 – as it had not yet completed the engineering needed to reach the 95 percent broadband availability standard required by March 31, 2013. Tr. at 42-44. Given FairPoint’s planning projections, and the interrelationship with the FCC’s universal service funding plan, FairPoint requested that the Commission extend the date by which it would achieve 95 percent broadband availability from March 31, 2013, to December 31, 2013. In exchange for approving the extension, FairPoint stated that it would commit to achieving 92 percent broadband availability by the end of 2012, Tr. at 56, and would combine the remaining 3 percent of its previously existing commitment with the work related to the investment of service quality penalty funds, for a total broadband availability of greater than 95 percent. Both commitments would be completed by the end of 2013.

In light of the unknown financial and engineering requirements for both the existing, and any new broadband commitment, it is not clear what impact, if any, the use of the service quality money would have on FairPoint’s access to or use of funding from the FCC. We also note our understanding that the funding from the FCC to which FairPoint referred relates to a voluntary commitment to expand broadband to unserved areas, and that there is no requirement that FairPoint, or any other carrier, accept the available money. *See Connect America Fund et al.*, at ¶ 138. Thus, absent some assurance that FairPoint would be willing and able to leverage the service quality penalty funds with the available FCC funding, there is further uncertainty about the likelihood of success of FairPoint’s plan.

To the degree the plan has been formulated by FairPoint, it proposes to use the service penalty funds to expand broadband exclusively in Northern New Hampshire. Tr. 45-47. While

there are many unserved areas within the North Country in need of broadband, FairPoint has provided no analysis to justify excluding other unserved areas in the state. Given that the service quality penalty funds have been generated by service quality failures throughout the state, we conclude that any plan to re-direct service quality penalties be based on targeting unserved areas, in the North Country or elsewhere.

Furthermore, despite repeated questioning, FairPoint could provide no estimates of the number of customers that would be served by investment of these funds in broadband deployment. Tr. at 50. FairPoint stated that it would work with Staff over the course of the next year to determine a scope and that if too few customers would be served, the issue of bill credits could be revisited. Tr. at 51. We are not willing to allow another year for development of a plan that may ultimately prove to be so unworkable that bill credits would again be raised as the preferred method of disbursing the penalty money. FairPoint requested that the Commission not order the payment of credits – the penalty payment method it previously agreed to – because it believed it could provide a plan for broadband expansion that would benefit the state as a whole. It appears, however, that FairPoint has undertaken insufficient planning or analysis to determine what benefits would be achieved, and it cannot say with certainty that it can produce a plan that provides any greater benefit than would be obtained through the payment of bill credits. Given the paucity of analysis and information FairPoint has provided, and its continuing admission that bill credits may ultimately be the preferred avenue for dealing with this money, we cannot approve the plan as proposed.

Despite these reservations, we believe that a sound broadband expansion plan, if submitted, would be a better use of the service penalty funds. Accordingly, we provide FairPoint

a final opportunity to demonstrate its commitment to meaningful broadband expansion in New Hampshire with this penalty money. By this order FairPoint is given two options. First, in consultation with Staff, the Office of the Attorney General, and any other necessary agency, FairPoint produce for Commission review and approval on or by May 29, 2012, an escrow arrangement that includes, at a minimum: (1) a binding escrow agreement or other financial instrument, covering the \$2,823,751 in penalties and the additional \$500,000 FairPoint stated it would provide for broadband expansion in response to record request 3, funds being held by an entity unrelated to FairPoint; (2) a binding agreement with the Commission and the State of New Hampshire guaranteeing the enforceability of a broadband deployment plan by a state agency, notwithstanding legislative developments; (3) a commitment to expand broadband in areas of New Hampshire within FairPoint's franchise and unserved by another terrestrial broadband provider, not merely within one county or discrete area; (4) a specific minimum number of broadband connections that will be made above the 95 percent already required and a meaningful penalty for failure to meet that number by December 31, 2013; and (5) a binding commitment that, should FairPoint undertake broadband expansion but subsequently abandon the effort, for whatever reason, the balance then held in escrow be credited to customers. Alternatively, if FairPoint chooses not to meet the Commission's terms, it shall pay bill credits in a single month beginning on June 1, 2012, as previously ordered by the Commission.

If FairPoint establishes an escrow arrangement that meets the above conditions by May 29, 2012, then bill credits shall not be paid on June 1, 2012, and FairPoint, with Staff input, will formulate a proposal for deployment of broadband facilities using the escrowed funds, for submission to the Commission by November 1, 2012.

We conclude that a plan containing, at a minimum, the conditions set forth above, assures a broadband expansion that benefits New Hampshire. We await FairPoint's determination as to whether it will commit to a meaningful plan to use \$3,323,751 to expand broadband or, beginning June 1, 2012, refund to customers the \$2,823,751 it owes as a result of its quality of service failures spanning multiple years.

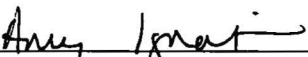
Based upon the foregoing, it is hereby

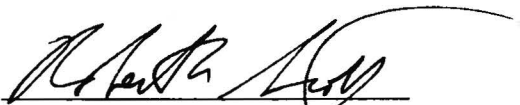
ORDERED, that FairPoint establish an escrow arrangement of \$3,323,751 with, at a minimum, the features outlined above on or by May 29, 2012; or, alternatively, pay bill credits in a single month beginning on June 1, 2012 to repay the \$2,823,751 owed; and it is

FURTHER ORDERED, that should FairPoint elect to establish an escrow, it shall file a proposal for broadband expansion beyond 95 percent as outlined above, by November 1, 2012, for Commission approval, or refund the money in escrow to customers; and it is

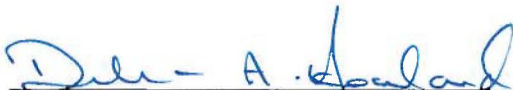
FURTHER ORDERED, that should FairPoint elect to pay bill credits, it shall, after doing so, file an accounting demonstrating that the total amount due has been paid.

By order of the Public Utilities Commission of New Hampshire this eighth day of May, 2012.


Amy L. Ignatius
Chairman


Robert R. Scott
Commissioner

Attested by:


Debra A. Howland
Executive Director

DISSENTING OPINION OF COMMISSIONER HARRINGTON

I respectfully dissent from the decision by the majority of Commissioners in this docket to allow FairPoint to use penalty funds to build out broadband. FairPoint's service quality penalties were developed to incent FairPoint to deliver service to its customers at acceptable service quality levels as well as to compensate customers for FairPoint's failures to meet those levels. In addition, service quality penalties exist to set an example for other regulated utilities. In my opinion, allowing FairPoint to keep the money and use it for unregulated capital investment sends the wrong message about the purpose of performance penalties.

The agreements creating these service quality penalties provided that FairPoint would repay its customers for lapses in the quality of their service. Therefore, this is money that belongs to the injured ratepayers. Allowing FairPoint to retain this money, however, means that FairPoint will be permitted to use money to which it would not otherwise be entitled. Further, it will use this money to expand its offerings of an unregulated service for the benefit of FairPoint's shareholders, and not the people and businesses harmed by the low service quality. I am not aware of any other instance where penalty money belonging to the ratepayers of a regulated company has been returned to that company for the expansion of that company's unregulated business.

Moreover, I am not convinced that spending the money on the proposed broadband build out is, in fact, good for the state as a whole. While it will help those who are able to receive broadband as a result of this project, it will not necessarily aid anyone else in the state. Fairpoint stated that it "believes [its] proposal to be more beneficial to the State of New Hampshire than issuance of bill credits." FairPoint's March 1, 2012 Proposal to Expand Broadband at 4.

FairPoint, however, provides no evidence to support this assertion. I must assume FairPoint is implying that it spending ratepayer money to expand broadband service to selected areas of the state would provide greater benefit than the ratepayers independently spending the money as they see fit. This is an assumption with which I disagree; whatever benefit would be realized by FairPoint expanding its broadband service using ratepayers' money would be surpassed by the ratepayers spending/investing their own money in the marketplace. The burden of proof to use ratepayers' money to expand the non-regulated portion of their business rests on FairPoint and it has not met that burden.

For all of these reasons, I do not support allowing FairPoint to use service quality penalties for additional broadband build out and would instead order an immediate rebate of these penalties to those who paid for sub-standard services, FairPoint's ratepayers.



Michael D. Harrington
Commissioner